



South African Reserve Bank

## Opinion Piece

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### Globalisation and free trade are not enemies

*By Daniel Mminele and Andreas Dombret*

We are living in times of elevated uncertainty, which could intensify in the period ahead, given the heightened risks to global growth brought about by the current geopolitical environment. We have been witnessing a rise in populism against multilateralism and globalisation. As both the Brexit vote in the UK and the presidential election in the USA made clear, there are increasing concerns with regard to the burden resulting from globalisation and therefore higher support for tighter controls on trade and migration. Some of these fears are founded on the assumption that slow economic growth, increasing unemployment and higher inequality are the consequence of free trade, growing cross-border movement of labour and off-shoring of business operations. The pushback against globalisation and free trade, and the embracing of nationalistic tendencies in an interconnected global world, should be of concern to all of us.

In advanced economies, nothing symbolises the problem more clearly than the impression that good manufacturing jobs have been lost to other countries. However, contrary to the current rhetoric, trade has not been the primary reason for the loss in manufacturing employment. Rather the explanation lies with productivity gains as a result of increased mechanisation and technological progress. It is for this reason that even Germany – where manufacturing has flourished and manufacturing employment is increasing again – has seen a halving of the manufacturing share of employment since 1970.

In fact, greater trade openness has led to the development of Global Value Chains (GVCs) which have allowed countries to participate in stages of the production process in which they have a competitive advantage. Improved competitiveness results in goods being produced at lower cost which ultimately increases the spending power of consumers. This, in turn, facilitates higher demand, promotes trade, wealth, investment, and ultimately, more jobs. Additionally, more trade implies a wider range of goods and services which also means a higher welfare.

Yet world trade growth has slowed from an average of 6.5 per cent between 1986 and 2008, to 3.2 per cent between 2012 and 2015, and is predicted to have expanded by just 1.7 per cent in 2016.

Protectionists believe that trade barriers will bring jobs home, boosting growth and employment. However, given the spread of GVCs, trade restricting measures might result in a significant disruption to production globally with adverse consequences for global demand. And this global economic downturn could dampen domestic production, too. Additionally, barriers to imports will lead to higher consumer prices. In the end, protectionist measures would reduce the purchasing power, especially of the socially weakest in society who are usually not able to protect themselves against higher consumer prices.

None of this means we should overlook the rise in inequality which has coincided with globalisation and the need to improve its governance. Lowering inequality would improve the resilience of economies by making them more robust to shocks. It is also likely to have broader social and political benefits.

Of relevance, is how to ensure that the benefits of globalisation are more fully realised and widely shared. The G20 was created in the wake of the financial crises of the 1990s with the primary objective of finding solutions to the problems confronting an integrated world. Paul Martin, former prime minister of Canada and a founding member of the G20, said in 2001 that globalisation has to work for all. This is the challenge confronting the G20 today, and which is receiving priority attention from Germany's 2017 G20 presidency.

The G20 has updated its growth agenda to include not only "strong, sustainable, and balanced growth", but also inclusive growth. There is recognition that the path to achieve this goal will likely have characteristics tailored to individual countries' needs, while not compromising on the agreed upon principles for macro-economic frameworks that support resilience and sustainability. This implies to strive for sound public finances, to reduce vulnerabilities in the private sector, especially in the financial systems, and to ensure favourable business environment, flexible labour market conditions and efficient social security systems.

What do globalisation and trade mean for Africa? Trade is critically important to enhance growth and development on the continent. This calls for accelerating both intra-African trade as well as embracing partnerships for innovative approaches to securing Africa fairer access and stronger participation in global trade. The 'Compact with Africa' initiative is therefore intended to create better investment conditions, by, for example, improving legal certainty, making taxation more reliable, and reducing investment risks with the help of international guarantees. Furthermore, the G20 will provide political support for specific investment agreements between African countries and international organisations and – if desired – with developed partner countries.

In addition, transfers of money from migrant workers to their home countries are an important source of funds for many countries – not only in Africa. In several countries these remittances account for up to one fifth of GDP and significantly contribute to domestic consumption and investment. The aim is therefore to improve the conditions for frictionless and efficient money transfers without weakening existing rules against money laundering and the financing of terrorism. In this regard, the

decline in correspondent banking services in the region – an unintended consequence of the global regulatory reform undertaken in the wake of the Global financial crisis – warrants attention.

It is for this reason that where appropriate we should be open to revisiting the reform agenda in a prudent manner to ensure it is effective in achieving its stated goals, while preserving hard-won progress achieved over many years of hard work and collaborative engagement.

In short, the future of globalisation and multilateralism will, to a large extent, depend on G20 countries delivering on the commitment made at the G20 Hangzhou Leaders' Summit in 2016, to “... *work to ensure that our economic growth serves the needs of everyone and benefits all countries and all people including in particular women, youth and disadvantaged groups, generating more quality jobs, addressing inequalities and eradicating poverty so that no one is left behind.*”

Let us harness the positive forces of free trade and globalisation, while managing the risks and ensuring greater inclusiveness. Globalisation and free trade are not the enemies, short-termism and expediency are!

- *Mminele is Deputy Governor of the South African Reserve Bank and Dombret, a member of the Executive Board of the Bundesbank and Supervisory Board of the European Central Bank (ECB).*
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