The Globalization Paradox: A response to Rosa Lastra and Robert Howse

Dani Rodrik*

I am grateful to Professors Rosa Lastra and Robert Howse for their comments on and reactions to my book. Their remarks, even when in disagreement, help crystallize some of the key trade-offs I laid out in the book. Therefore they help advance the debate.

Professor Lastra puts her argument crisply: there should be "more international law and less national law." She considers "hard" international law, emanating from treaties, as inherently legitimate from a democratic standpoint. She says further that the International Monetary Fund (IMF) should be turned into a "global sheriff" to provide international law the missing element of enforcement. This vision is a particular version of the "global governance" solution I discuss in the context of my global trilemma.

If I advocate a regime that places greater emphasis on national sovereignty than Professor Lastra, it is because I differ from her as regards both the normative and efficiency properties of such a solution. First, as Professor Howse notes, international treaties do not automatically qualify for democratic legitimacy, even if the parties are democratic sovereigns. Saying that anything that a democratically elected sovereign does is democratically legitimate would empty democracy of much of its normative content. Democratic "delegation" has its limits domestically, and similar limits should apply internationally. Put differently, a well-functioning democratic polity would place severe limits on the transfer of rule-making and enforcement authority to transnational bodies.

As for efficiency, the globalist solution presumes there is a well-defined set of "ideal" rules that all countries should submit to. In fact, countries may have different preferences (along the financial stability–financial innovation frontier, for example), and therefore different ideal rules. And the location of the efficiency frontier itself is uncertain. Therefore an efficient solution would trade off some transaction costs in finance against the benefits of national diversity and experimentation. The "corner solution" of common rules is in fact sub-optimal.

Professor Howse considers instances where the "negative global or trans-boundary externalities from domestic policies exceed the domestic welfare gains from keeping

* Institute for Advanced Study, Princeton, NJ. Email: drodrik@ias.edu.

those policies in place." Typical examples are the optimum tariff, mercantilist currency policies, and tax regimes that permit money laundering. We call these "beggar-thy-neighbor" policies. I agree with him that international regulation is desirable in such cases, as the gains that accrue domestically come at the expense of (even greater) damage created for other nations.

But what makes these cases special, and in fact rare, is that they generate domestic benefits only if they generate foreign harm. Many other cases of cross-border externalities and spillovers arise as the unintended side effect of domestic policy choices. Europeans would subsidize domestic farmers even if there was no farm trade. If America's financial regulators fell asleep on the job, the intent was not to make the rest of the world pay. In fact, it is the domestic economy first and foremost that suffers from "democratic failure" in these and similar cases. We may call these "beggar-thyself" policies.

I would be much more skeptical about international regulation in such instances. After all, democracies are entitled to their mistakes. The rest of the world has little business telling a country what its policy objectives ought to be, even if those objectives seem to defy economic efficiency or rationality. The fact that cross-border harms are created for some other nations is by itself an inadequate argument for international regulation. After all, when a country reduces its tariffs, some of its competitors are hurt too, but we do not regard this as a reason for regulating unilateral liberalizations.

It seems to me that the democratic failures evinced by "beggar thyself" policies can be fixed only by improving democratic deliberation at home. International rules have at best an indirect effect. By requiring transparency, representativeness, scientific scrutiny, etc. in rule-making, they may enhance the quality of decision-making. But they should not substitute for domestic bodies of deliberation.

The case of fuel subsidies mentioned by Howse is an interesting mix. On the one hand, they are domestically costly policies that would exist even in the absence of any environmental externalities. So, to that extent, they are "beggar-thyself" policies. On the other hand, they greatly aggravate the mother of all "global commons" failures—the absence of a global climate change regime. It seems to me that any international control would have to be justified on the basis of that second failure, rather than the presence of externalities from the subsidy regime per se.