

Globalization, Populism and the Decline of the West

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Since the 1970s, globalization — the cross-border movements of capital, goods, and people — has expanded significantly. There were immense welfare gains from this growth, especially from trade, in both the developing and developed worlds. These gains were not evenly distributed, either within or across countries. Some economic theories, particularly the Stolper-Samuelson theorem, predict adverse distributional consequences for less skilled labor in rich economies. Other economists argue that globalization speeds up skill-biased technological change, which can explain the reduced demand for lower skilled labor in developed countries and the wage stagnation they have experienced in the past twenty years. Rising inequality and immigration are also associated with globalization and seen as a threat to lower skilled workers in the developed world. If these workers are the median voters in these countries, what does this mean for politics? Will political parties respond by turning against globalization and openness? If the means for compensating losers from globalization no longer work, then do these voters turn toward populism?

This strand of research goes back to Karl Polanyi (1957), who argues in *The Great Transformation* that the growth of the capitalist market, including its opening to the global economy, led to the decline of democracy and the rise of fascism in the inter-war period. He claims that if the market is not regulated and embedded within society, it will disrupt people's lives so much they will turn against democracy and fall prey to extremism. Globalization needs to be politically contained. Dani Rodrik (2011) seems to agree. In *The Globalization Paradox*, he argues that democracy, national sovereignty, and extensive globalization are not compatible and that preserving national diversity and democracy make sacrificing globalization an appealing alternative. Is globalization undermining democracy?

Economists are beginning to research the political consequences of globalization. They generally find strong electoral effects from trade, especially import competition from less developed countries like China. The losses from trade carry significant adjustment costs in terms of job displacement and reduced earnings for individuals (Acemoglu, et al. 2016, Autor, et al. 2016, Autor, Dorn and Hanson 2013, Dauth, Findeisen and Suedekum 2014). These costs and the rising uncertainty associated with globalization create strong demands for assistance from the state, increasing demands for redistribution and compensation for exposed individuals (Cusack, Iversen and Rehm 2006, Margalit 2013, Rehm 2009, Walter 2010). When these demands are not met, voters may become attracted to more extreme candidates and their programs. Autor et al. (2016) and Autor, Dorn and Hanson (2013) show that districts in the United States most affected

by import competition from China tend to remove moderate members of Congress and elect more extreme ones, especially on the right. Colantone and Stanig (2018a) show that increased trade, especially Chinese imports, leads voters in Western Europe to increase support for nationalist and extreme right parties. Colantone and Stanig (2018b) find that support for the “Leave” option in the UK referendum on European Union membership was stronger in areas hit hardest by trade. Dippel, Gold and Heblich (2016) demonstrate that German voters in areas most exposed to this trade, especially imports from China and Eastern Europe, increase their support for extreme right parties.

Since the 1990s, scholars of party politics have observed the rise of extremist parties and especially of populist ones (see Betz 1994, Kitschelt 1996, Kriesi 2010, Mayer 2013, Mudde 2007). Inglehart and Norris (2016) note that populist parties recently entered into government coalitions in 11 Western democracies, grew their average vote share in national and European elections from 5% to 13%, and saw their average seat share rise from 4% to 13%.

One puzzle is why working class voters choose right-wing parties instead of their more “natural” home on the left. For a long time, scholars assumed that voters in an open economy would demand compensation in exchange for openness, and the “embedded liberalism” bargain was embraced by left-wing, Social Democratic parties. Some scholars now question whether compensation is still appealing or effective. What is the alternative to embedded liberalism?

Is the only option economic nationalism with protectionism? This would involve reducing not just trade but also migration and capital flows. The economic nationalist bargain offers broad protectionism to “compensate” workers threatened by globalization. At the same time, if the welfare state is no longer needed to mitigate globalization shocks, the government’s need for tax revenues declines. The promise of lower taxes is combined with protectionism to generate appeal across constituencies. The whole platform is motivated by an ideological appeal to nationalism and nostalgia for “making the country great again.” This is the alternative to embedded liberalism offered by extremist parties.

In my research, I find that globalization increases support for right-wing populist parties and decreases support for left parties. This effect mainly operates through the erosion of manufacturing jobs, since the loss of jobs in this sector and the inability to find jobs of similar pay leads to dissatisfaction with the status quo and openness to populist appeals. More trade and foreign direct investment are also associated with greater anti-internationalism and anti-globalization in political party platforms. Social welfare spending seems less able to mitigate these consequences from globalization.

What is to be done? Should we end globalization and retreat into protectionism? Would this help politics and democracy? There is evidence that trade and FDI promote growth and innovation, so ending both of them would probably make countries worse off overall (e.g., Dollar and Kraay 2004, Frankel and Romer 1999, Grossman and Helpman 1991). The better path is to maintain openness but help those who lose out from it. The welfare state developed, in part, to achieve this, but these policies may no longer work to reduce the pressures associated with globalization and rapid economic change. It may be that unions are so weakened that they can no longer

contain globalization pressures. Left parties are also caught between policies which help labor in the long-run but entail unappealing short-run costs. The welfare state itself may be financially unable to compensate the public for globalization, as open capital markets make it harder for governments to collect taxes.

Rising inequality, financial crises, deflationary pressures, deindustrialization, competition from developing countries, and rapid technological change may be undoing the compromise of embedded liberalism that sustained globalization for decades. Into this breach are coming radical left- and right-wing parties which articulate a populist program that offers workers protection from the vicissitudes of contemporary global capitalism. Such programs provide help in the short-run but also tend to have unsustainable long-run costs (Dornbusch and Edwards 1991, Sachs 1989). Populist leaders combine these policies with strongly nationalist and anti-democratic practices, as evidenced recently in countries like Hungary and Poland. Populist, anti-democratic politics is what Polanyi anticipated would arise when individuals are left to face the market without political or social help. The question is what can be done to stop this trend.

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