

## LINKING THE BEST AND WORST OF GLOBAL TRENDS<sup>1</sup>

by Roger B. Myerson

<http://home.uchicago.edu/~rmyerson/research/globaltrends.pdf>

In a panel that is asked to focus on a few trends that are truly important for the world today, I want to note a connection between two great developments in recent years. One is among the greatest positive developments in human history: the miracle of declining global poverty rates even as population of the world grows.<sup>2</sup> The other is a disturbing political development which became strikingly clear in the past year: a strong xenophobic discontent in America and other rich nations. We should see a fundamental connection between these two phenomena.

The greatest discovery of modern times has been the amazingly high long-run elasticity of national output with respect to the protection of property rights for citizens at large. Throughout most of history, states and empires kept peace between villages but protected property rights mainly for the benefit of an exclusive ruling class or oligarchy, whose members had responsibility for supporting and maintaining the state. In modern times, however, it was discovered that, when a nation extends reliable protection of property rights to millions of ordinary citizens without special political connections, the result can be to unleash widespread competitive entrepreneurial activity that can increase the national GDP and tax base so much that even members of the ruling elite may be better off without the exclusivity of their privileges.

The benefits of this discovery were at first confined to a small fraction of humanity in Europe and America. I have argued elsewhere that the successful development of the United States depended particularly on the long history of decentralized federal democracy here, going back to colonial times.<sup>3</sup> But over the past 70 years, nations on every continent have gradually learned how to distribute political power and protection of law more broadly, to bring real benefits of modern economic development to more people everywhere.

By any moral standard, this is a good and great development.

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<sup>1</sup> Text prepared for delivery at a session on "Where is the world economy headed?" at the Allied Social Science Associations meeting in Chicago, January 6, 2017.

<sup>2</sup> See for example Xavier Sala-i-Martin, "The world distribution of income: falling poverty and ...convergence, period," *Quarterly Journal of Economics* 121(2):351-397 (2006).

<sup>3</sup> Roger Myerson, "The strength of American federal democracy," World Bank policy research working paper 7512 (2015); also at <http://home.uchicago.edu/~rmyerson/research/amerfed.pdf>

This great global transformation since the early 20th century has vastly increased what we might call the effective global labor supply, that is, the world's supply of people who live in communities where they can be employed by local firms that have competitive access to global markets. In the 70 years since 1947, the population of the world has increased by a factor of about 3. But the fraction of the world's population who live in nations that can produce modern goods competitively for global markets has also increased by almost the same factor, from less than a third of humanity to a large global majority. So over the past 70 years, our planet has become about 8 times richer in globally employable labor, corresponding to an average annual growth rate of about 3%. This enormous growth of the effective global labor supply should be expected to have historic significance on a planetary scale.

Since the time of Malthus 200 years ago, pessimists who predicted diminishing returns in aggregate economic growth have been proven wrong. So by the late 20th century we became accustomed to thinking in terms of growth models with positive steady-state growth rates, even though everybody has always understood the impossibility of any physical quantity growing forever at a positive exponential rate on a planet that has a fixed finite size. But planetary limits may have been easier to ignore because, until recent decades, most benefits of modern economic growth were concentrated in a small fraction of the world. The material requirements for each 1% increase in per-capita consumption become vastly larger when people throughout the whole world are all involved.

The vast increase in the effective global labor supply, which is large relative to every other resource on our planet, must have an adverse effect on the real wages for unskilled workers in the countries where local firms have long had the ability to produce modern goods with globally trusted quality. A decline in real wages could be partially countered by technological change, but Robert Gordon has found that US productivity growth rates peaked during the years 1920-1970.<sup>4</sup> Since then, much of global growth has come from poorer countries catching up with the great technological advances that America achieved previously.

Now a failure to meet expectations of continuing growth of real wages has led to mass discontent in the old developed nations in America and Europe. Many understand that something has changed in the relationship with the poorer nations of the world, but there is broad

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<sup>4</sup> Robert J. Gordon, *The Rise and Fall of American Growth: The U.S. Standard of Living Since the Civil War* (Princeton University Press, 2016).

misunderstanding of how this change could be problematic for people in America. We economists have not adequately communicated the simple fact that aggregate living standards in America cannot be harmed by the availability of cheap imported goods from poor countries. But Americans' comparative advantages and terms of trade can be adversely affected when people in the traditionally poor countries are no longer totally dependent on America and Europe for their supply of modern manufactured goods. Even if America erected trade barriers to block imports from foreign manufacturers, people in the rest of the world could not be compelled to buy American goods that they can now make more cheaply themselves.

But America's new President-elect has promised to restore the past terms of trade which benefitted Americans a generation or two ago. We need to explain that such a promise could never be achieved by any renegotiation of international trade agreements, but only by reversing the political and legal changes in formerly poor countries which have enabled their people to participate in modern technological investment. Surely nobody should want to do that! We need to explain that the changes in trade which stir such discontent in America today are directly connected with global developments which have also generated historically unprecedented increases in aggregate human welfare across the globe.

How might our basic assumptions in economics change to better fit a world where people everywhere can participate in economic advances and investment?

- It may be time to back off from models which suggest that good economic policies can promote infinite unbounded exponential growth in the broad global economy.
- The global scope of modern production implies that limits on the planet's ability to recycle waste products, which we used to consider freely disposable, may now require more active regulation or taxation by governments, to accommodate global ecological constraints.
- Benefits of economic productivity may accrue relatively more to those who have positions of trust and power in global economic networks, less to the marginal product of unskilled labor, and so problems of income inequality may become more acute.
- The whole global development miracle depends on the spread of good government, and trust in these expanding global economic networks can be maintained only with legal protection and regulation from governments and their international agreements. From this perspective, it may be appropriate for governments to tax those who benefit most from the global economy, to fund a safety net for those who benefit least. Indeed, social safety nets have been essential for

modern development since the beginning of the industrial revolution, because efficiency-enhancing economic changes can be politically blocked by people whose existing livelihoods would be destroyed, unless they get some hope of benefiting from the increased productivity.

But the most important point goes beyond economic efficiency to a fundamentally ethical observation. Economists usually try to avoid ethical statements, but let me offer this one which, I think, we can defend by any ethical standards that value all human beings in any reasonably balanced way: **If admitting all of humanity to participate in the benefits of modern economic development implies that we must forfeit hope for further exponential growth in our time, this is a price that we should be morally willing to accept.**

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