DISCUSSION PAPER

Ceidir *January, 2020*

Beyond the debate in favour or against international economic integration: What can be done to better understand, inform and act on its effects on places and people?

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Abstract:

Recently, politicians in different countries have achieved electoral success by opposing economic globalisation. Social exclusion and disparities in income distribution have triggered a protectionist discourse in both, developing and developed countries. Policy recommendations based on sound economic theories have been put into doubt. By the same token, prestigious economists and economic geographers argue that despite international economics theory clearly acknowledges that free trade causes winners and losers, the expected higher gains have not been effectively used to compensate the losses. This paper presents and grounds two courses of action mutually beneficial. One that could contribute to face the challenges and make the best of the opportunities of economic globalisation; and the other, to better inform policy makers and the general public on the outcomes and benefits of public policies including international economic integration instruments. I illustrate both proposals with examples related to Mexico, a nation known by its increasing degree of economic openness since the last decade of the twentieth century.

Key Words: Globalisation, trade agreements, local economic development, regional disparities, public policy, economic geography.

JEL Classification: *F15, F63, F68, R12*

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Introduction

According to Krugman and Obstfeld (1999), the mission of international economics as a branch of economics is to show the economic advantages of free international trade and analyse and inform on the negative economic impact of protectionist policies.

The results of recent elections in different countries have shown a strong sympathy with political positions that question the benefits of free international flows of goods, services, labour and capital.

Considering the support of the general public to politicians with views against economic globalisation, understood as the international functional integration of economic activity across national territories (Dicken, 2015), it seems that international economics is not fulfilling its mission.

Taking also into account that the debate in favour or against protectionism is not new as it dates back at least from the XVI century (Krugman and Obstfeld, 1999), this paper proposes two complementary activities that could contribute to the international economists efforts. Firstly, I argue that the consideration of a more balanced focus of public policies between the bottom-up and the predominant top-down perspective could help both, overcoming the predicted negative effects of international trade, and making the best of its benefits. Secondly, I propose contemplating intrinsically and explicitly the evaluation of international integration instruments.

Economics, economic geography and economic adjustments in territories

Microeconomic theory explains the mechanisms behind markets' functioning such as the interaction between the basic building blocks of markets, demand and supply, illustrating how the quantity of services or goods traded and the price paid for them are determined. It studies markets considering perfect competition as a benchmark to analyse efficiency and economic agents' gains in comparison with other market conditions such as oligopolies, monopolies and monopolistic competition. In the case of international economics, its foundations are the mainstream microeconomic theories around the functioning of markets, macroeconomics postulates, and the classical fundamental concept of comparative advantage which considers openness to trade as key for reaching economic efficiency and maximum gains (Heather, 2004).

Since the last century, formal international economic integration has taken many specific forms from the General Agreement on Tariffs and Trade (GATT) to the World Trade Organisation (WTO), and from it to bilateral or multilateral agreements or associations with a regionally international competitive focus. That is, economic integration occurs mainly by regional international blocs such as the North American Free Trade Agreement (NAFTA), probably soon, USMCA (United States, Mexico, Canada Agreement); the European Union (EU) and Mercosur in South America.

The benefits for Mexico from participating in NAFTA and other trade agreements since 1994 have been evident in terms of the diversification and growth of its productive and exporting capacity[1]. The following table compares Mexico's economic complexity index with the one of China, a country that experimented an economic transformation since its World Trade Organisation (WTO) membership in 2001, and Cuba and Ukraine which openness to the world economy has been low.[2]

Table 1. Economic Complexity Index

Country	1995 Ranking and index	2016 Ranking and index
Mexico	27 0.676	21 1.11
China	50 0.143	18 1.16
Cuba	79 0.419	89 0.671
Ukraine	48 0.239	47 0.249

Source: Atlas of Economic Complexity rankings: http://atlas.cid.harvard.edu/rankings[3]

Economic complexity measures a country's knowledge as expressed in the goods and services it produces. Economic complexity is calculated based on the diversity of exports a country produces and the number of the countries able to make them. Countries that are able to sustain a diverse range of productive know-how are able to make a wide diversity of goods, including complex products that not many countries can produce.

Table 1 shows that the two countries experimenting increasing openness to international markets between 1995 and 2016, China and Mexico, improved considerably their economic complexity, while Cuba and Ukraine remained in the lowest positions with relatively small improvements.

According to data from the World Integrated Trade Solution platform[4], in 1993, Mexico had a deficit in manufactures and capital goods while in 2017 was the opposite. Between 1990 and 1994, Mexico had a trade deficit with the rest of the North American countries and the world, but since 1995 it has had a surplus with the former. The number of its exports partners were 142 in 1993 while in 2017 were 200. Mexican exports grew 4.3 times while its imports were multiplied by 4.1 along those years. Its index of export market penetration nowadays is higher than 12 while in 1993 was 4.6. Trade as a percentage of its gross domestic product (GDP) was 27.83% in 1993 while in 2017 was around 77%.

Ex-post formal evaluations (i.e. academic research) of the effects of NAFTA in Mexico and the United States have found gains in both countries (Swarnali, 2016) but also income distribution effects as predicted by international economics theory (Rodrik, 2018).

[1] The Atlas of Economic Complexity elaborated and published by the Centre for International Development at Harvard University presents information on Mexico's economic complexity from shortly after the agreement came into force (1995) up to 2016 (http://atlas.cid.harvard.edu - Site accessed on January 10th 2019).

[2] Ukraine is not a member of the European Union and was until 2017 that their Deep and Comprehensive Free Trade Area (DCFTA) agreement with it, signed in 2014, came into full force.

[3] Accessed on January 10th 2019.

[4] Accessed on January 10th 2019 (https://wits.worldbank.org).

Therefore, openness to trade caused economic structural changes implying that economic agents in less competitive productive activities lost with the agreement. That is the same in any other country and any other particular international economic integration instrument. In David Ricardo's conceptualisation, the production of a good without comparative advantage would tend to suffer from integration in favour of more efficiently produced imports of that good.

In other words, international trade can have a strong impact within countries by means of distributional effects between economic sectors or industries as well as between the owners of different factors of production, and even within the same factor of production. An example of the latter is labour depending on the characteristics of the skills needed in the winning economic activities in comparison with the losing ones.

Economic geography studies the location, distribution, and spatial organisation of economic activities across the world. It looks at where economic activities take place, as well as how and why these activities interact among places. Three main factors shape the process of dispersion or agglomeration and connectedness of economic activity in space: the level of trade costs, the monopolistic power of firms as well as external economies or diseconomies. Economic geographers have found that the spatial distribution of economic activity in an open market context has contributed to larger gaps between core and peripheral or lagging behind places (Ascani, Crescenzi and Iammarino, 2012).

On that ground, despite the methodical scientific explanations of international economics academics and their research results that confirm efficiency gains with international trade, doubts about the benefits of economic globalisation prevail as a consequence of the adjustments in markets with negative impact on specific territories between and across countries (Rodríguez-Pose, 2018).

Hanson (1996) explored the effects of falling trade costs between Mexico and the U.S. as a consequence of NAFTA on the location of Mexican manufactures. He found that despite the fact that deeper economic integration has increased market access for Mexican firms, a great deal of local production was relocated in the bordering localities with the United States.

Later, Katz (1999) confirmed that trend, identifying the border Mexican states as well as some in the central and western part of Mexico as the main beneficiaries, increasing the income gap between them and the states located in the south and south-east of the country. Reduced trade and labour costs and proximity to the U.S. markets explain great part of firms location in the border states, while lower trade costs and the presence of external economies are considered the main factors of the concentration of economic activity in some central and western states.

Mexico's car, aerospace, electrical equipment and electric consumer goods industries, which accounted for two-thirds of its exports of manufactures in 2014, are mainly located in its northern border and some central states.[5]

In the case of European Union enlargements, in general, new countries have experienced similar results within their territories in favour of already richer and

[5] Atlas de Complejidad Económica de México (Atlas of Mexico's Economic Complexity): https://datos.gob.mx/complejidad/ (Accessed on January 10th 2019).

more dynamic places, as well as older member countries have benefited more than the new ones, reinforcing polarisation or economic disparity patterns (Ascani, Crescenzi and Iammarino, 2012).

Considering the previous context, what can be done to better respond to the challenges and opportunities of greater economic openness, and to better understand and inform on its outcomes? The following two sections offer two feasible suggestions and the argumentation around them.

Comprehensive public policy based on the bottom-up approach to economic development

Overall, international economics experts and other economists state that the economic benefits or gains of international trade are greater than the losses and, therefore, compensation to losers could happen by means of public policy (Krugman, Obstfeld and Melitz, 2012; Stiglitz, 2015). Nevertheless, Rodrik (2018) argues that U.S. administrations have failed redistributing the gains from trade:

"In principle, U.S. governments could have followed the European model. It could have complemented trade agreements --NAFTA, the WTO, and China's WTO entry-- with much more robust social insurance mechanisms and active labour-market programmes and protections".[6]

However, social protection and other welfare state programmes in Europe have not prevented the mentioned regional disparities in the EU. In addition, Rodrik, himself highlights the distortionary effects of the taxation and transfer mechanisms that could be put in place within a welfare state optic.

A solution can be given by the EU, but this time considering its approach to regional policy. Barca, McCann and Rodríguez-Pose (2012) stress the importance of a change in the EU regional policy intervention towards a place-based instead of a place neutral approach.

In a place-based intervention, public policy considers the local internal and external context and it is verifiable and subject to the participation and examination of local stakeholders. It also responds to the expectation of the population living in any locality of a country that everyone can benefit from the economic gains of an open economy, as well as have equal access to opportunities and the right to face challenges within a comprehensive development strategy.

In other words, it is not about compensating the losers of international integration instruments but designing and implementing better public policies alongside those instruments. Those policies seek to disentangle and harness the economic potential of lagging behind, poor or peripheral areas (Rodríguez-Pose, 2018). Therefore, it is not about subsidising them but integrating them to viable economic development paths.

In 2015, an article on The Economist called "Of cars and carts"[7] highlighted the lack of public policy around Mexico's participation in the global economy by presenting the case of Audi's construction of a new plant in the municipality of San

[6] Rodrik Dani, 2018 (p. 17).
[7] https://www.economist.com/briefing/2015/09/19/of-cars-and-carts (Accessed on January 12th 2019)

José Chiapa, in the central state of Puebla. While this state had been home of the automotive sector as a leading manufacturer of automobiles and automobile parts for almost two decades, more than half the municipality inhabitants had not finished their secondary education and depended on low scale traditional farming activities.

The lack of a comprehensive and coordinated strategy to make the best of the openness of the Mexican economy has been putting aside of the development path to an important part of the population even in the places where economic growth and increases in productivity have been taking place.

Let us consider now the clothing industry to give another simple illustration of the above. Gradually lowering the tariffs of garments and diverse types of clothes would allow an increasing flow of those products between the countries participating in a trade agreement. Consumers would expect a greater variety of the different kinds of products and lower prices. In some places, there would be potential losers from the agreement. However, some firms might be able to adapt and react.

If we consider Mexico at the beginning of this century when competition in textiles was fierce due to China's and other Asian countries' exports, firms producing clothes in the border with the U.S. could have benefited from external economies that would allow them to compete by means of introducing innovative design and marketing; while smaller firms in Tlaxcala (a Central state) could have achieved economies of scale and, therefore, be able to compete by getting together to satisfy a larger demand. These possibilities can only be identified in more placed-based public policies with the corresponding capacity building, fostering of entrepreneurship and innovation, as well as social capital building actions, among others, as part of a comprehensive and inclusive strategy to economic development.

In this sense, Audretsch (2015), Pike, Rodríguez-Pose and Tomaney (2017), and Palavicini-Corona (2014) propose an emphasis on a regional and local economic development focus of public policy to respond to the challenges and opportunities of economic globalisation.

Accordingly, international integration mechanisms such as NAFTA or USMCA, must be part of a national public policy strategy that considers the diverse characteristics of a country and its territories, and pursues the economic development and well-being in a comprehensive and inclusive way (without omitting the identifiable winners and losers of those mechanisms) in order to achieve national, regional and local goals within a framework of effective coordination with local stakeholders.

The place-based and bottom-up development approach emphasises the collaboration between levels of government as well as the participation of the public, social, private and academic sectors. Local stakeholders lead the development process and strategy which are based on their territories potential. The idea according to Pike, Rodríguez-Pose and Tomaney (2017) is to use the place specific characteristics to provide the conditions to stimulate local economic activities in a context of national and global changing environments.

Evaluation of international integration instruments

Attributing employment creation and economic growth, without further analysis, to international trade and the attraction of foreign direct investment, and giving statistics about how international flows have changed before and after the interventions seem to have been enough for public administrations in favour of the openness to international markets. However, it has not been enough for the critics of economic globalisation.

Academics have been testing the international economics theory with certain degrees of rigour and diverse methodologies finding that it remains valid (Cheong, 2010; Kazumoto, 2007; Stevens et al. 2015). Despite those academic efforts, there are some criticisms as for example, Stiglitz (2015) argues that most analyses are based on testing the effects predicted by the theory with its strong assumptions that do not hold in reality. Swarnali (2016), after finding positive economic gains of international trade, acknowledges several unrealistic assumptions of his innovative methodology (i.e. synthetic control methods) and the need to use novel techniques to study other effects such as labour adjustments and the impact on income inequality.

To complement the methods for ex-post economic assessment of free trade agreements, a rational and transparent way to pursue the benefits and monitor the outcomes of a particular international integration instrument is to set its specific performance and impact measures as well as monitor and inform on its effectiveness in a periodical basis. Encouraging the design of methods for periodically assessing the impact of any policy intervention in parallel to the design of the intervention helps setting, from the very beginning, a path to constantly improve public policy and to opportunely react to possible negative effects based on concrete evidence (Foray, McCann and Ortega-Argilés, 2015; Kubera, 2017; Overman, 2016).

Moreover, if international trade negotiations are conducted considering the comprehensive and deep diagnosis that demands the wider public policy context under the local economic development perspective proposed in the previous section, that evaluation will feed the place-specific public policy processes in operation to face the expected challenges and make the best of the potential opportunities of economic international integration mechanisms.

The seemingly challenging case for an exhaustive evaluation scheme of international integration instruments under a comprehensive bottom-up local economic development strategy demands to write a full paper. Here, two examples of evaluation mechanisms that could be designed at the start and applied throughout the implementation of a trade agreement, and that could be reported and published periodically to inform the general public would illustrate the proposal.

As mentioned, one of the positive effects attributed to trade agreements are the benefits for consumers, as they could buy a wider basket of final goods and cheaper than before the agreement. If public administrations consider the evaluation since the very beginning, after defining success and the agreement's concrete consumption goals[8], they could design and apply surveys before and after it comes

[8] To encourage public administrations to undertake better assessments of the outcomes of their public policies, the *What Works Centre for Local Economic Growth* in the United Kingdom promotes 8

into force; so that, combined with other sources of data, could inform on the matter and, later, on those goals.

For example, policy makers would be able to obtain information related to the monetary values and contents of consumption baskets (including the origin of the different products in the basket and their weights) for different percentiles of income and regions across a country, as well as information on consumer expectations in relation to the agreement. Then, convert the data in valuable knowledge and diffuse it across the country. A follow-up of the information every year or two years, depending on budget and other considerations, could reveal if the agreement is achieving the established consumption goals and general public expectations. Later, part of the information could be used to identify or not the presence of causation using more sophisticated ex-post methodologies.

Moreover, if the reduction of tariffs on foreign products is implemented little by little, monitoring the results in the way proposed could also reveal information on what works better (the level beyond it no further changes are obtained) to achieve certain goals.

Let us consider again the car industry in Mexico. This has been one of the most benefited industries by the trade agreement with Canada and the United States. Setting short, medium and long run goals for training, employment growth, labour productivity increases, industry-related firms creation, R&D investment growth, research institutes and universities collaboration with the industry, exports growth, among others, would have allowed to follow closely and inform constantly on the performance and results of the agreement in this industry, helping not only to highlight the benefits but also to respond opportunely if the achievement of a goal was being at risk. However, this would have required, as mentioned, a clear strategy on all those matters in terms of both, this particular sector of the economy and the sub-national territories involved.

Evaluation of performance and outcomes must be inherent to any public policy alone and as a part of a comprehensive strategic development plan as the resources of public administrations are scarce, and their mandate is to provide opportunely, effectively and efficiently public services and social protection, as well as to foster the economy and prevent and solve economic, social and environmental problems in the same way (Stiglitz, 2000, 2015).

Summary and final remarks

This is a discussion article that acknowledges both, the vast academic literature supporting the validity of international economics postulates, and the poor results of international economic integration in terms of social inclusion and reducing income gaps between people and regions.

In past years, economic globalisation enthusiasm has been losing momentum as a result of increasing disparities among people and places. Therefore, it seems that international economics academics are losing the debate in favour of international

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steps that civil servants can take to improve their evaluations: start early, define success, what to evaluate?, find a control group, collect data, how long?, "plagiarise", and get everyone on board [https://whatworksgrowth.org/how-to-evaluate/ (Accessed on February 7th 2019)].

trade and the economic benefits of increasing flows of goods, services, labour and capital.

To contribute to their efforts, this paper proposes two complementary activities to take into account, preferably, from the very thought of starting a negotiation or renegotiation of an international economic integration instrument:

1. A comprehensive public policy based on the bottom-up and placed-oriented approach towards economic development.
2. The intrinsic and explicit evaluation of international integration instruments alongside the rest of public policies.

The mentioned increasing disparities among people and places are a reminder of the need and importance of effective public policies to make the best of the benefits of international trade by improving the determinants of a country's competitiveness (Porter, 2008) considering their uncontested interrelation with its sub-national territories (Pike, Rodríguez-Pose and Tomaney, 2017), and seeking to create new opportunities for the losers as well as incorporating the population who have always been excluded. Both proposals are in line to help achieving these goals.

Economic geography can help to identify suitable policies for particular places by looking at the centripetal and centrifugal forces in place, which are caused by a combination of elements such as trade and transaction costs, labour mobility, imperfect competition, and the local availability of inputs and knowledge. Other considerations such as the characteristics of formal and informal institutions, the presence of internal and external networks, entrepreneurial aptitudes and attitudes, smart specialisation ideas and local amenities, are fundamental for the competitiveness of countries and their localities in a context of a globalised economy (Audretsch, Link and Walshok, 2015). Policies taking into account ideas such as acquired comparative advantage and dynamic gains of trade according to places' particularities are also of special pertinence (Meier, 1998; Sandilands 2015).

Finally, knowing what works and what works better to achieve countries' and their territories' economic development goals, and improve the well-being of their citizens, seems to be essential.

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