

WHO NEEDS THE NATION STATE?

Dani Rodrik
Arrow Lecture
May 2012

The nation state refuses to wither away

- ⦿ The death of the nation state has long been predicted
- ⦿ But in practice it has proved remarkably resilient, and remains the primary determinant of:
 - the global distribution of income
 - the locus of market-supporting institutions
 - personal attachments and affiliations
- ⦿ The financial crisis has further underscored its centrality
 - crisis response: bailouts, fiscal stimulus, culprits
 - the Eurozone experience
- ⦿ Yet the nation state is held in quite low regard
 - A weak, and perhaps non-existent normative case

Two lines of attack

- ⦿ The economic argument: scope of market
 - national borders impose transaction costs
 - eliminating jurisdictional discontinuities would enhance gains from trade
- ⦿ The ethical argument: moral cosmopolitanism
 - communication revolution renders borders meaningless and enlarges our community
 - national borders become morally irrelevant

Peter Singer: a global ethic

“If the group to which we must justify ourselves is the tribe, or the nation, then our morality is likely to be tribal, or nationalistic. If, however, the revolution in communications has created a global audience, then we might need to justify our behavior to the whole world. This change creates the material basis for a new ethic that will serve the interests of all those who live on this planet in a way that, despite much rhetoric, no previous ethic has done.”

Note how global ethic depends on “global audience” – death of distance

Amartya Sen: multiple identities

- ⦿ Each of us has a plurality of identities: ethnic, religious, national, local, professional, political,...
- ⦿ The importance of any one of these does not come at the expense of others'
- ⦿ “there is something of a tyranny of ideas in seeing the political divisions of states (primarily, national states) as being, in some way, fundamental, and in seeing them not only as practical constraints to be addressed, but as divisions of basic significance in ethics and political philosophy.”

Amartya Sen, Identity and Violence, 2006 and The Idea of Justice, 2009, p. 143.

So who needs the nation state?

- ⦿ Is the nation-state, as a territorially confined political entity, a hindrance to the achievement of desirable economic and social outcomes, in view of the globalization revolution?
- ⦿ In other words, is it just national politicians that need the nation-state?
- ⦿ Or does the nation state remain indispensable to the achievement of those goals?

A clarification on terminology

- ◎ I am less concerned with “nation” and “nationalism” than the “state” as a spatially demarcated entity
 - I define the nation as a consequence of a state, rather than other way around: “What is a nation? A body of associates living under one common law and represented by the same legislature?” (Sieyes, as quoted in Kedourie, 7).
- ◎ Question is not what is a nation, whether each nation should have its state, or how many states there ought to be, but
- ◎ Why should the world be organized into multiple states, rather than a single one
 - “If, on this definition, all the people wanted of the world decided on a common government, they would form one nation. But such an inference, though correct, is merely academic” wrote Kedourie (7). Why so?

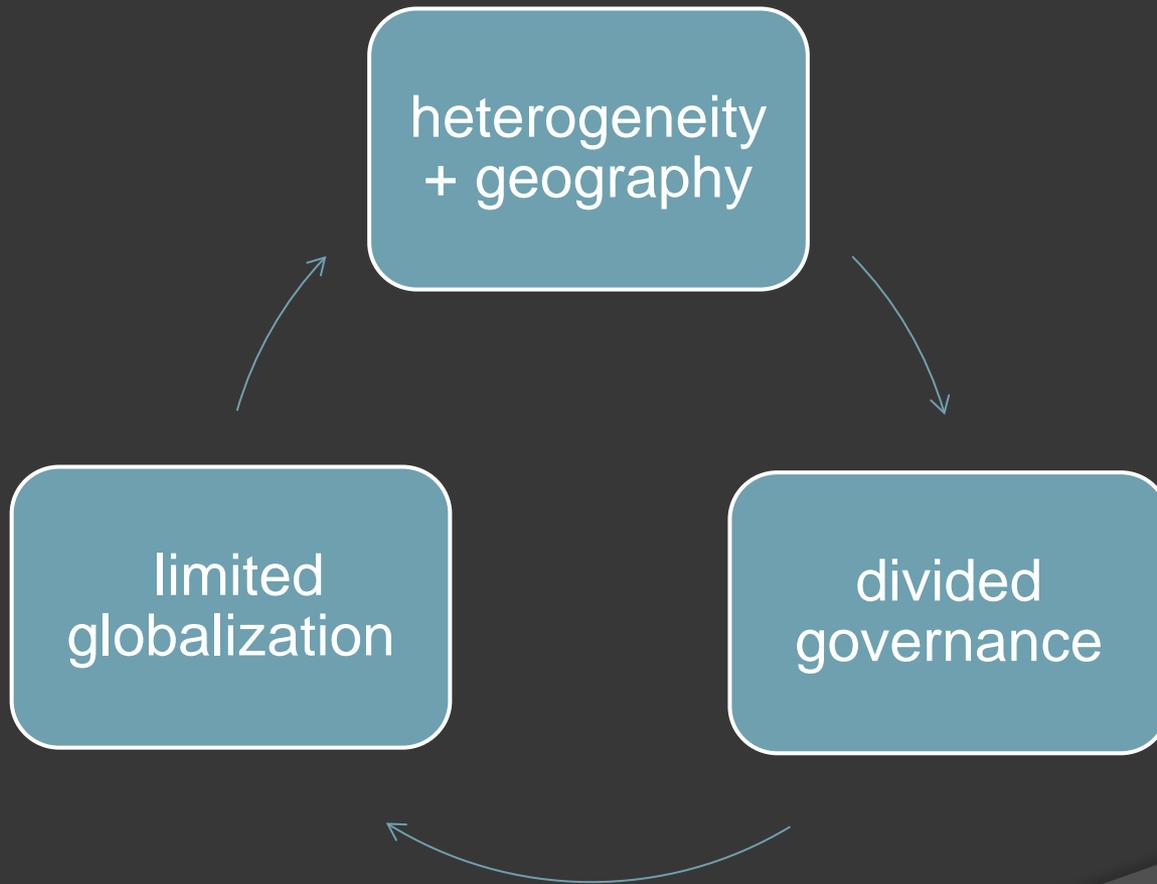
Roadmap

- ⦿ The argument in brief
- ⦿ Is there evidence that attachments and identities are becoming more global?
 - Not really
- ⦿ Is a borderless global market possible?
 - Only with “global governance,” i.e. the creation of governance institutions that match the global scale and scope of markets
- ⦿ Is global governance desirable?
 - Not really, on account of
 - institutional malleability
 - diversity
 - limited convergence
 - value of competition, experimentation

The globalist dynamic



The nation-state dynamic



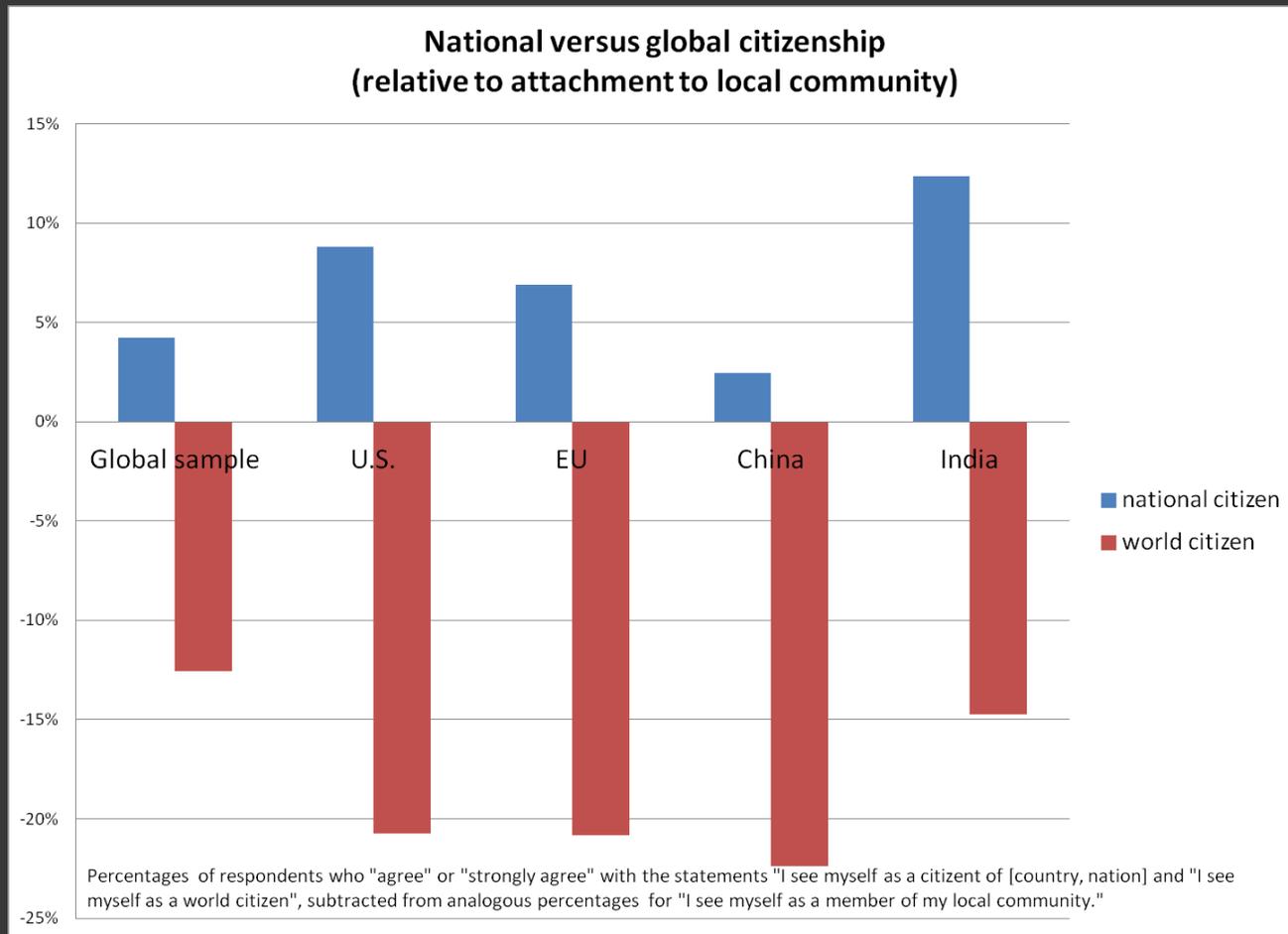
How strong is national identity relative to local and global attachments?

Data from World Values Survey

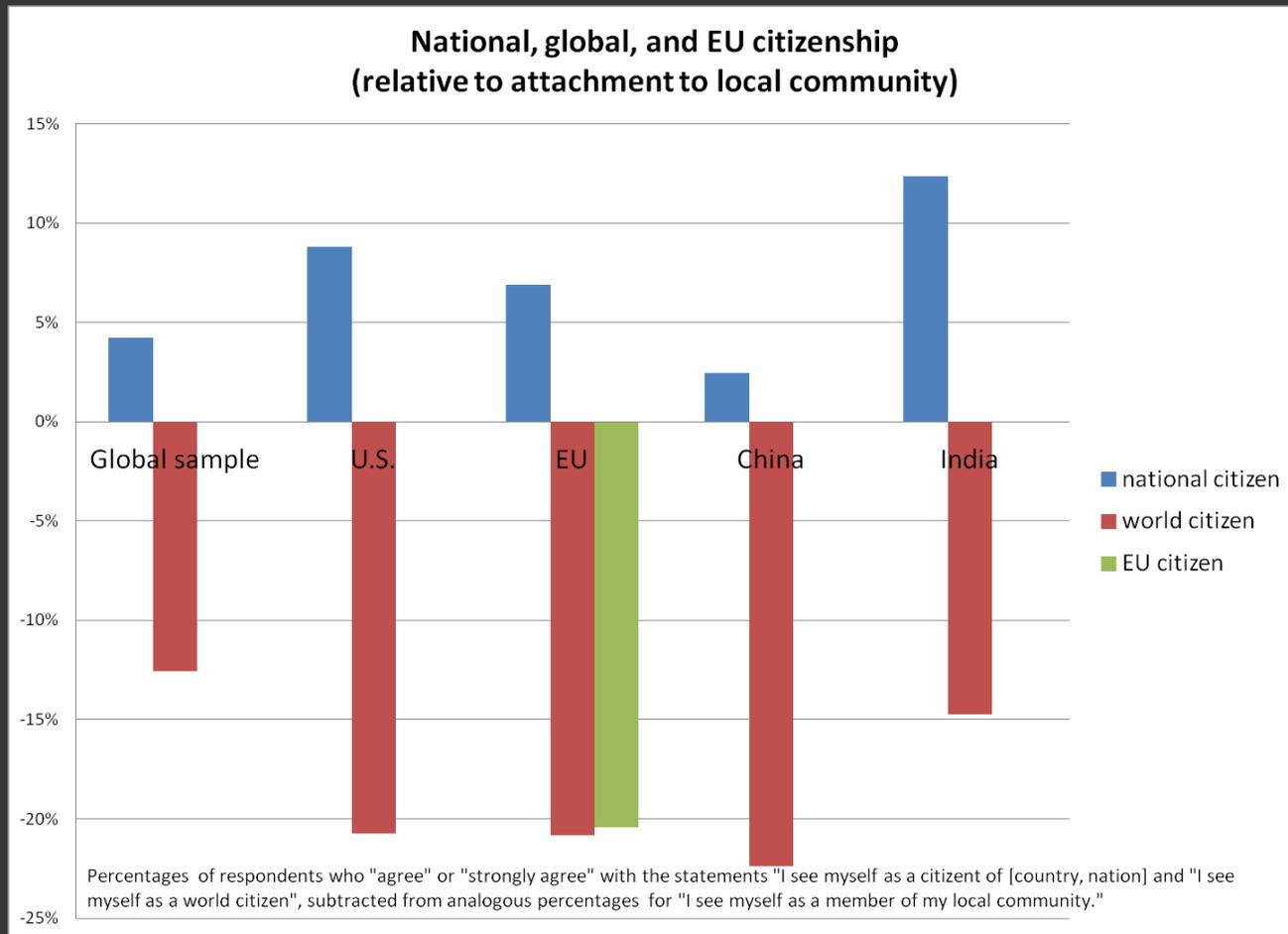
83,000 individuals in 57 countries over 2004-2008

<http://www.worldvaluessurvey.org/>

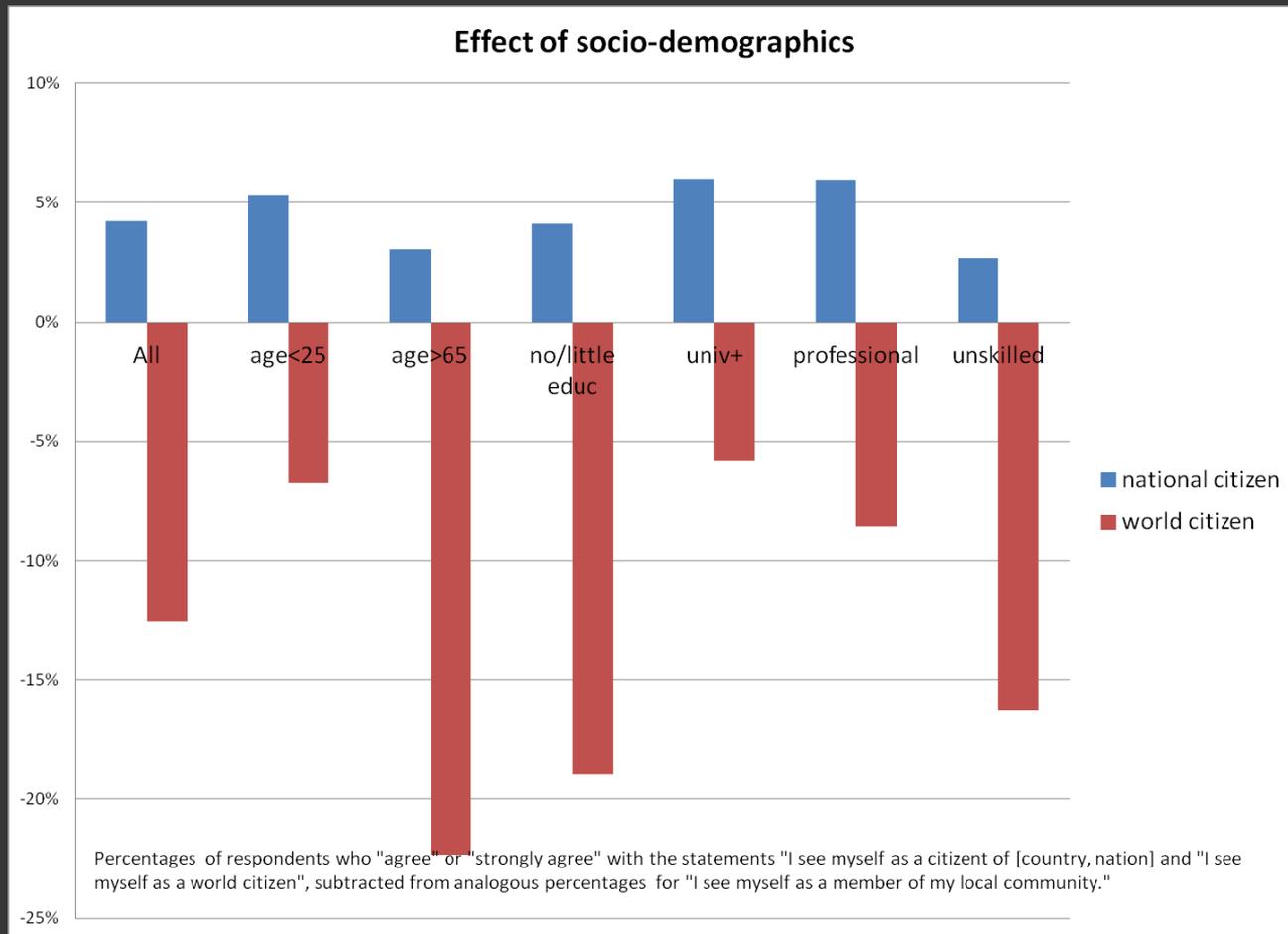
Comparing national and global attachments: survey evidence



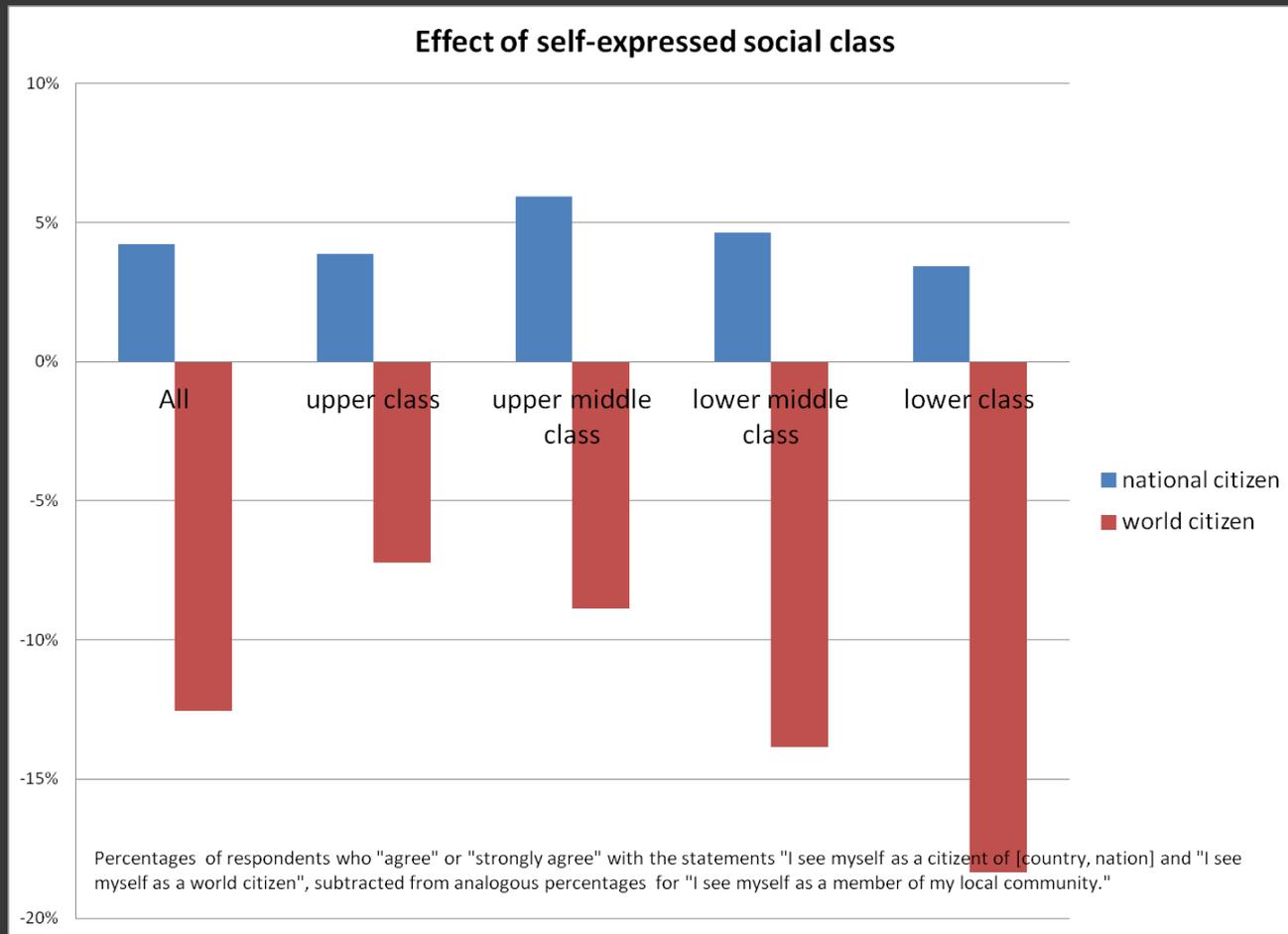
Comparing national and global attachments: the EU



Comparing national and global attachments: effect of socio-demographics



Comparing national and global attachments: effect of social class



Is a truly global market feasible? The futile pursuit of hyper-globalization (1)

- ⦿ Markets are not self-creating, self-regulating, self-stabilizing, self-legitimizing
- ⦿ Therefore they need to be “embedded” in a wide range of non-market institutions
 - Regulatory institutions, redistributive institutions, monetary and fiscal institutions, institutions of conflict management, ...
- ⦿ Those institutions have been largely those of the nation state
 - E.g., national monetary systems/CBs as cornerstones of financial globalization (Agnew 2012, 8-9)
- ⦿ Paradox: nation states have been both obstacle but enabler of globalization

Is a truly global market feasible? The futile pursuit of hyper-globalization (2)

- ⊙ Hyper-globalization requires elimination of transaction costs on international trade and finance, both at and behind the border
 - In practice: financial globalization + World Trade Organization
- ⊙ Emergent forms of global governance remain weak
 - transnational networks of regulators (Slaughter)
 - “private governance” (fair trade, CSR, etc.) (Ruggie, Mayer and Gereffi 2010)
- ⊙ So domestic governance/regulatory mechanisms have been weakened while their global counterparts remain incomplete
 - Which results in economic and political malfunction: inequality, financial crises, democratic legitimacy deficit
 - Europe: the “exception” that tests the rule



Is global governance feasible or desirable?

- ◉ Joshua Cohen and Charles Sable: a new identity created by accountable global administrative processes
- ◉ John Tomasi: the post-territorial state
- ◉ David Held: social democratic cosmopolitanism
- ◉ Anne-Marie Slaughter: global networks of regulators and legislators
- ◉ John Ruggie: A global compact and CSR
- ◉ G-20, Financial Stability Forum, IMF with improved governance, etc.

A substantive argument against visions of global governance

- ⦿ Market-supporting institutions are not unique
- ⦿ Regions/nations/communities differ in their needs and preferences with regard to institutional blueprints
- ⦿ Geography and distance limit the convergence in those needs and preferences
- ⦿ Experimentation and competition among diverse institutional forms is desirable

1. Institutional multiplicity

- ⦿ There is no unique set of market-supporting institutions
- ⦿ Institutional *function* does not map into unique institutional *form*
 - Each desired function (e.g., appropriate incentives) can be provided in a multiple ways
- ⦿ There are “varieties of capitalism”
 - Liberal market economies vs. coordinated market economies
 - East Asian versus American versus European models
- ⦿ Plus, there is no reason to believe that plausible institutional variation is limited by existing range of models (Unger)

Multiplicity of desirable institutional arrangements

OBJECTIVE	UNIVERSAL PRINCIPLES	PLAUSIBLE DIVERSITY IN INSTITUTIONAL ARRANGEMENTS
<p><u>Productive efficiency</u> (static and dynamic)</p>	<p><u>Property rights</u>: Ensure potential and current investors can retain the returns to their investments</p> <p><u>Incentives</u>: Align producer incentives with social costs and benefits.</p> <p><u>Rule of law</u>: Provide a transparent, stable and predictable set of rules.</p>	<p>What type of property rights? Private, public, cooperative?</p> <p>What type of legal regime? Common law? Civil law? Adopt or innovate?</p> <p>What is the right balance between decentralized market competition and public intervention?</p> <p>Which types of financial institutions/corporate governance are most appropriate for mobilizing domestic savings?</p> <p>Is there a role for “industrial policy” to stimulate investment in non-traditional areas?</p>

OBJECTIVE

Macroeconomic and Financial Stability

UNIVERSAL PRINCIPLES

Sound money: Do not generate liquidity beyond the increase in nominal money demand at reasonable inflation.

Fiscal sustainability: Ensure public debt remains “reasonable” and stable in relation to national aggregates.

Prudential regulation: Prevent financial system from taking excessive risk.

PLAUSIBLE DIVERSITY IN INSTITUTIONAL ARRANGEMENTS

How independent should the central bank be?

What is the appropriate exchange-rate regime? (dollarization, currency board, adjustable peg, controlled float, pure float)

Should fiscal policy be rule-bound, and if so what are the appropriate rules?

Size of the public economy.

What is the appropriate regulatory apparatus for the financial system?

What is the appropriate regulatory treatment of capital account transactions?

OBJECTIVE

Distributive justice and poverty alleviation

UNIVERSAL PRINCIPLES

Targeting: Redistributive programs should be targeted as closely as possible to the intended beneficiaries.

Incentive compatibility: Redistributive programs should minimize incentive distortions.

PLAUSIBLE DIVERSITY IN INSTITUTIONAL ARRANGEMENTS

How progressive should the tax system be?

Should pension systems be public or private?

Should grant schemes be conditional?

What are the appropriate points of intervention: educational system? access to health? access to credit? labor markets? tax system?

What is the role of “social funds”?

Redistribution of endowments? (land reform, endowments-at-birth)

Organization of labor markets: decentralized or institutionalized?

Modes of service delivery: NGOs, participatory arrangements., etc.

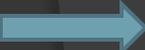
2. Heterogeneity and diversity

- ⦿ There are legitimate differences over the shape that institutions should take
 - Kant: religion and language divide people and prevent a universal monarchy
 - Greater heterogeneity => greater gap between nature of public goods provided and the type preferred (Alesina and Spolaore)
- ⦿ These differences arise from differences in preferences, needs, income levels, and historical trajectories
 - Social preferences: innovation vs stability in financial regulation
 - Low versus rich countries: varieties of market reform
 - Hysteresis: institutional lock-in in social protection

2. Heterogeneity and diversity: caveat

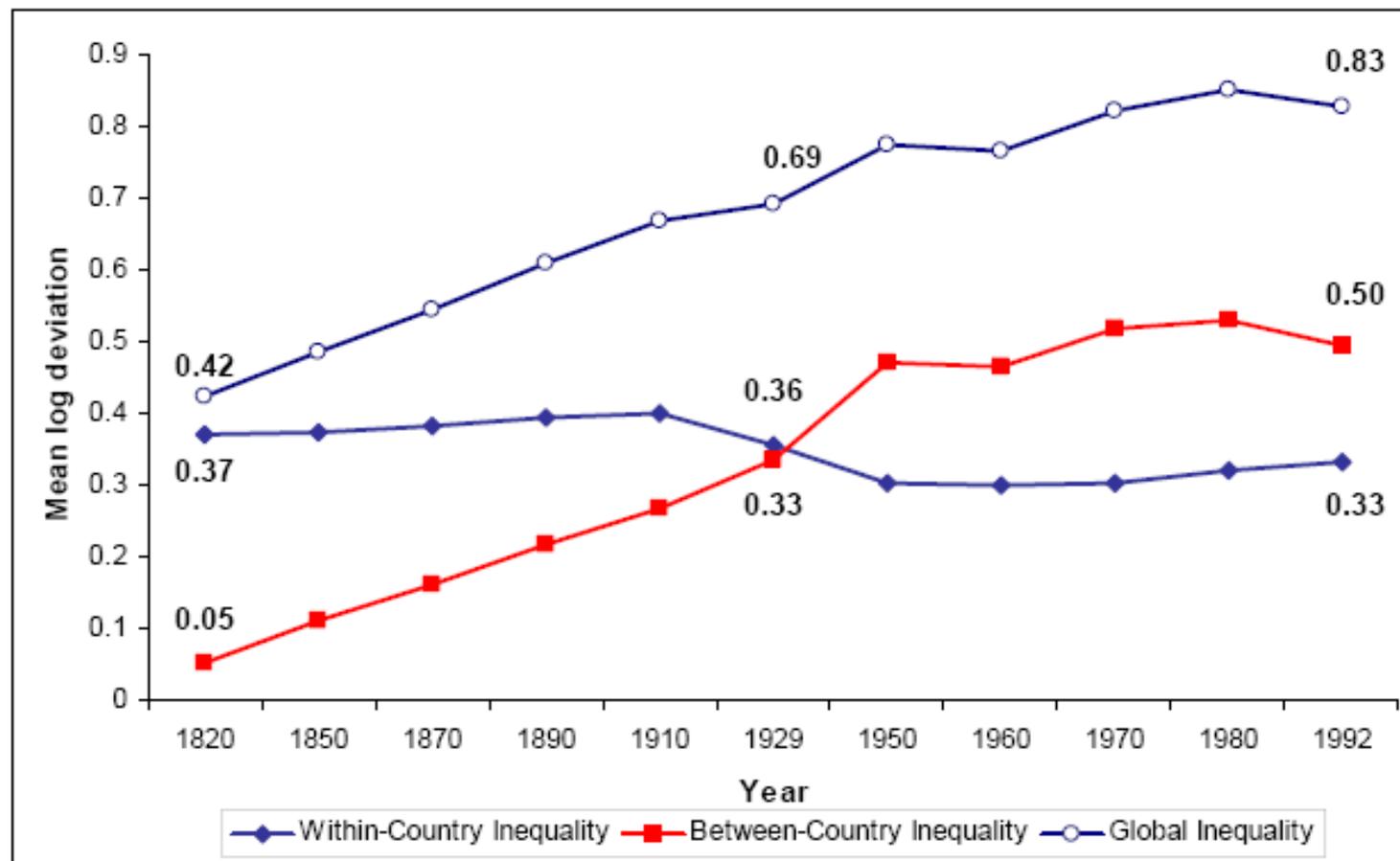
- ◎ But heterogeneity is partially endogenous
 - As theorists of nationalism have stressed from Ernest Renan on, cultural differences are not innate and can be shaped by state policies (education, being the key one)
 - And income levels could converge too

3. Limited convergence

- ◉ We can expect limited convergence in institutional preferences because geography/distance still matters
 - Global distribution of income: within and across countries (slide)
 - Gravity effects in trade, Internet (slide)
 - Impact of high-speed communications on attachments (slide) 
- ◉ An explanation: many exchanges are based on relationships, not anonymous markets
- ◉ Geographic distance protects relationships
 - Leamer (2007): “Geography, whether physical or cultural or informational, limits competition since it creates cost-advantaged relationships between sellers and buyers who are located “close” to one another.”
- ◉ But relationships also create role for geography: once relationship-specific investments are made, geography becomes more important
 - Example of cost advantages of producing iPhone in China because now there is mass of suppliers there (NYT)

Global inequality: countries matter more

Figure 4: Global Inequality and its components, 1820-1992.

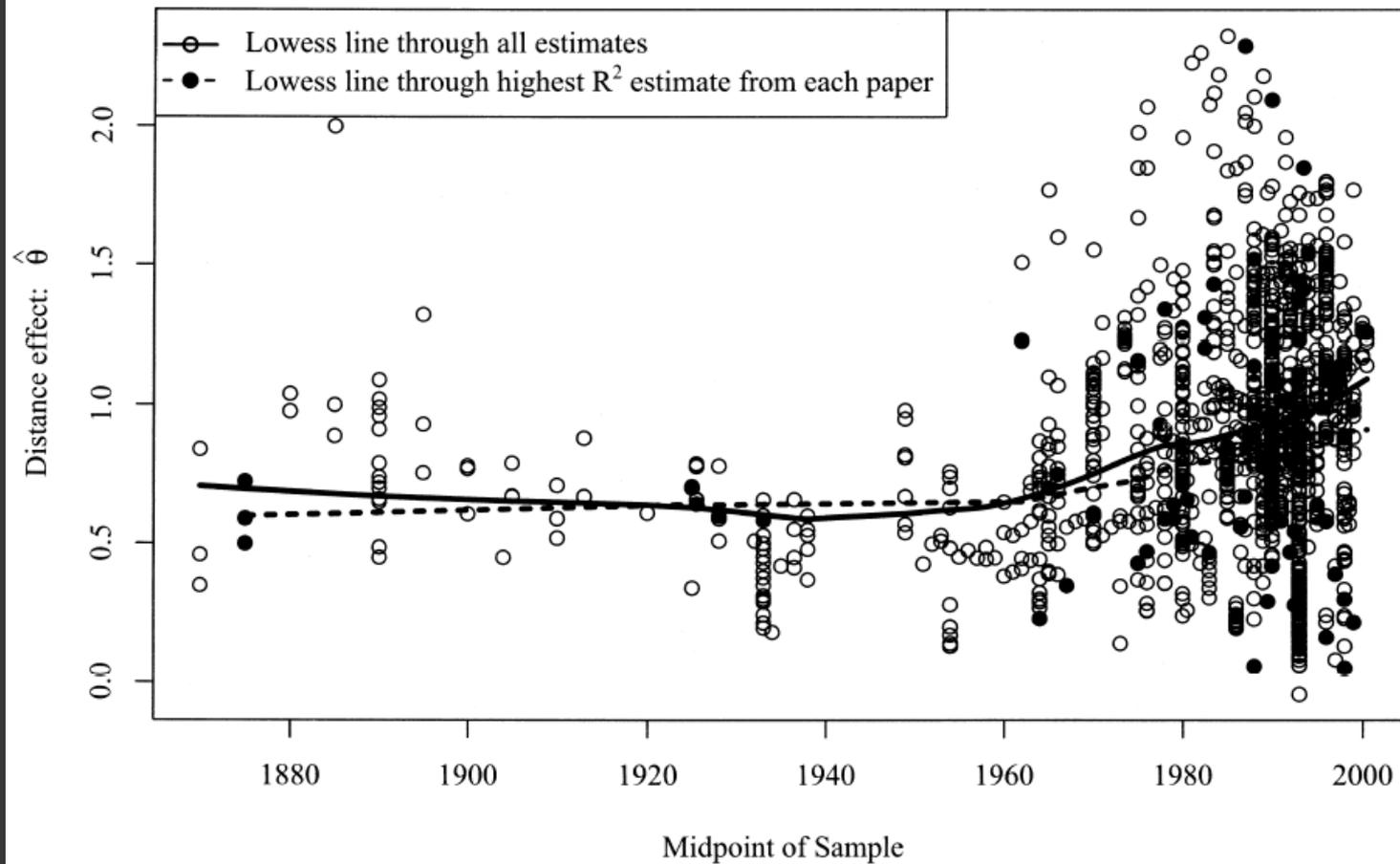


Source: Bourguignon and Morrisson (2002) and World Bank (2005).

Source: Ferreira and Ravallion (2008)

Gravity effects in trade remain strong

FIGURE 3.—THE VARIATION OF $\hat{\theta}$ GRAPHED RELATIVE TO THE MIDPERIOD OF THE DATA SAMPLE



High-speed communications do not attenuate local attachments

- Gravity and the Internet. “Americans are more likely to visit websites from countries that are physically close than from countries that are far, even after controlling for country-level Internet expertise, language, income, immigrant stock, and many other factors. Furthermore, we show that this effect only holds for digital products that depend on taste, such as music, games, and pornography. For these, a 1% increase in physical distance reduces the probability an American will visit the website by 3.25%. For less taste-dependent products, such as software, distance has no statistical effect.” Blum and Goldfarb (2006)
- “Netville” “Compared to non-wired residents, [wired residents] recognized more of their neighbors, talked to them more often, visited them more frequently, made many more local phone calls. They were more likely to organize local events and mobilize the community around common problems. They used their computer network to facilitate a range of social activities, from organizing barbecues to helping local children with their homework. Netville exhibited, as one resident put it, “a closeness that you don’t see in many communities.” What was supposed to have unleashed global engagement and networks had instead strengthened local social ties.” Rodrik (2011), summarizing Hampton (2004).



Technological changes have an ambiguous effect on importance of relationships

- ◉ Decline in transport and communication costs reduce the effect of distance in market relationships, and maybe also enable the creation of relationships across space that crosses national boundaries
- ◉ At the same time, the increase in complexity of production and in product differentiation, along with the shift from mass production to services and new, distributed modes of learning increases the relative importance of spatially circumscribed relationships
 - new economy runs on tacit knowledge, trust, cooperation, which depend on personal contact
 - spatial reach does not equal “social depth” (Morgan 2004)
- ◉ This implies market segmentation is natural, even in the absence of jurisdictional discontinuities

4. Experimentation and competition

- ⦿ Since there is no fixed, ideal shape for institutions, experimentation, learning, and competition are desirable
- ⦿ This argues against convergence, and for letting multiple forms co-exist
- ⦿ But also a nasty side:
 - 19th century notion of war among states as the struggle through which we get progress and self-realization of humanity (Kedourie 47)
 - A Darwinian competition among states
 - Modern-day equivalent of “economic competition”
 - Trade as zero-sum game

What about “race to the bottom”?

- ⦿ In practice, seems to be limited to corporate tax competition
 - high taxes/regulation have compensating benefits
- ⦿ But need to accept principle that nation states have right to protect social arrangements
 - prevent regulatory arbitrage that undermines integrity of domestic institutions

Who needs the (nation) state?

- ⦿ We all do...
- ⦿ Relationships and heterogeneity in local preferences push governance down
- ⦿ Scale/scope benefits of market integration push governance up
- ⦿ This tension lies at the heart of globalization's unaddressed ills
- ⦿ Since corner solution is not optimal...
- ⦿ A divided world polity is the best we can do