

BOOK REVIEW

The World is Flat: A Brief History of the Twenty-First Century

by Thomas L. Friedman, New York:
Farrar, Straus & Giroux, 2005.

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The world is flat according to Thomas Friedman. He attributes its flatness to ten flatteners, which are, in essence, events, technology and systems (i.e., fall of the Berlin Wall), Windows 3.0, Netscape and work flow software, and forms of collaboration, e.g., outsourcing (taking a specific, limited function done in-house by a company and having another company perform that same function, and then reintegrating it back into the overall operation), offshoring (taking a factory and moving it offshore to another country where costs of production are cheaper). They tend to level the playing field, enabling individuals to collaborate and compete globally. He refers to this as Globalization 3.0, a stage of globalization where individuals, including those who are non-western and non-white, are empowered and constitute the unit of analysis. In previous stages—Globalization 1.0 (1492-1800) and Globalization 2.0 (1800-2000)—the units of analysis were countries and companies, respectively.

Be that as it may, Friedman notes that developing countries must be able to address five basic issues related to what he calls reform retail (as opposed to reform wholesale) which points to how easy or difficult it is to: 1) start a business in terms of local

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rules, regulations, and license fees, 2) hire and fire workers, 3) enforce a contract, 4) get credit, and 5) close a business that goes bankrupt or is failing. In other words, issues that point to flexibility. Here, he cites the significance of Hernando de Soto's earlier work on the informal economy in relation to the need to simplify systems, processes and rules at the micro level, to align them with reform wholesale (which pertains to reforms at the macro level entailing export-oriented, free-market strategies).

Friedman asks: Is David Ricardo still right?

Ricardo is credited with the theory of comparative advantage. According to the theory, a country should focus its production efforts on goods over which it has an advantage compared to other countries. A country has a comparative advantage over another if it can produce a certain commodity with a relatively lower opportunity cost. For instance, a country whose economy is basically agricultural should concentrate on the production of agricultural goods. Because of the built-in advantage, so the theory goes, the economy will become more productive. And if the productive capacity of the economy is increased over time, economic growth would invariably ensue.

Friedman says that Ricardo is still right and gives illustrations to prove his point. He notes that trade barriers ought to be removed and workers in a country participating in free trade must make adjustments. Knowledge and high-skill workers have to adjust horizontally while low-skill workers should adjust vertically, to take advantage of the opportunities (and challenges) posed by a larger, more complex economic pie brought in by combining markets and free trade. In this regard, he emphasizes the importance of public and private investments in human capital to address shifts or changes in the demand for labor—new jobs are being created with more and more specialization.

The prescriptions in the book are straightforward. But let us take a closer look at free trade.

Free Trade

The General Agreement on Tariffs and Trade (GATT) was premised upon the theory of comparative advantage. GATT was also rooted

in the concept of economic globalization. Economic globalization has two components—economic cooperation and trade integration. Economic cooperation usually comes in the form of harmonization of policies among countries, including investment and tariff policies. Trade integration refers to the removal of distortions that arise from trade among economies. Specifically, it entails the lowering of trade barriers between economies.

GATT was established for the purpose of promoting a multilateral trading system based on non-discriminatory trade liberalization and fair rules and discipline between member nations. It was the global institution that sponsored multilateral trade negotiations (like the Uruguay Round) aimed at the progressive lowering of import tariffs, reduction or elimination of non-tariff barriers to trade, and improvements in the rules and disciplines governing multilateral trade. Since its creation in 1947, GATT pushed for the expansion of free trade, competition, minimization of trade disputes, and a stable and predictable trade regime.

The Uruguay Round of GATT provided for three basic key result areas: market access, institutions, and rules and disciplines.

Market access covers agreements on industrial or manufacture tariffs, agricultural tariffs and tariffication, textiles and clothing, and services. The Uruguay Round achieved an average 33% across-the-board reduction in tariffs (or taxes on imports). Moreover, as far as agriculture is concerned, the Philippines bound itself to remove all current quantitative restrictions imposed on imports of agricultural products, and to convert these into tariff equivalents in a process known as tariffication. Likewise, the Round required the phase-out of the quota-based Multi-Fibre Arrangement over a 10-year period beginning 1995. The last area covered by market access is the General Agreement on Trade in Services (GATS) which provides for basic obligations like the Most-Favored Nation treatment (MFN, i.e., non-discrimination), transparency (e.g., publication of domestic laws and regulations), and fair application of domestic laws and regulations affecting the supply of services.

Institutions encompass agreements on dispute settlement, a trade policy review mechanism, global policy coherence, and the formation of the World Trade Organization (WTO) which eventually replaced GATT.

Rules and disciplines pertain to agreed procedures and guidelines on anti-dumping, subsidies and countervailing measures, trade-related intellectual property rights (TRIPS), trade-related investments measures (TRIMS), safeguards, technical barriers to trade, rules of origin, health and sanitary regulations, customs valuation, import licensing, and pre-shipment inspection.

Under GATS, trading may take place under any of the following modes:

Cross-border trade – Supply of service from one country to another in a situation where the buyer and the seller do not meet face to face.

Consumption abroad – Supply of service for a consumer coming from outside the territory. In other words, the foreign buyer goes to the country of the service provider.

Commercial presence – Supply of service by a provider of a member country in the territory of the service consumer through the setting up of a shop, branch, or subsidiary in the said territory.

Movement of service personnel – Service supplier sends personnel to another country to render service.

These modes cover initially any of the following:

- Business services, including professional services
- Communication services, including telecommunication and audio-visual services
- Construction and related engineering services
- Distribution services
- Educational services
- Environmental services
- Financial services, including insurance and banking services
- Health related and social services
- Tourism and travel-related services
- Recreational, cultural, and sporting services
- Transport services, including maritime, waterways, air, and road transport services

All this was ratified by the Philippines, along with other countries, and the ratification was upheld by the Supreme Court in *Tañada v. Angara* (272 SCRA 18, 1997).

However, free trade is not all that simple. There are development administration concerns especially since there has been a movement away from the multilateral framework of WTO. Specifically, developed countries are pushing for regional and bilateral Free Trade Agreements (FTAs) with developing countries.

In a paper written for the United Nations Development Programme (UNDP, 2005), it was noted that developed countries expand or modify the trade agenda beyond WTO through "third-generation agreements" that extend into domestic policies (e.g., sanitary measures, trade facilitation, liberalization of trade in services, investment and competition disciplines, intellectual property rights and government procurement) and shift the rule-making process to the regional and bilateral stages.

For instance, it was noted that the United States has used FTAs as a mechanism for structural adjustment in the textiles and clothing industry by encouraging offshore production and establishing "yarn forward" rules of origin that support the use of US yarn and fabrics in offshore facilities, and as a condition for made-up or clothing products to enjoy duty-free entry. This tends to create a captive market for US yarns and fabrics exporters while increasing the cost of products using these inputs exported by countries benefiting from duty-free entry.

FTAs negotiated by the US also seek to dilute the rights of governments to issue compulsory licenses authorizing companies to produce generic drugs without the patent holder's permission (low-cost generic versions of patented drugs have been of tremendous value to poor countries for decades), by limiting the ground for issuing such licenses to, say, national emergencies, or by requiring conditions such as adherence to anti-competitive laws. They also limit the ability of poor countries that do not have the capacity to produce generic drugs to avail of imports from countries with such capacities.

Another TRIPS-plus trend pursued by the US in FTAs is to request the developing country to agree to the patenting of life forms and plant varieties, and to accede to the International Union for the Protection of New Varieties of Plants (UPOV), which effectively

dilutes the *sui generis* system under Article 27.3 (b) of the TRIPS Agreement. For example, countries like Singapore and Jordan that signed FTAs with the US have been obliged to become UPOV members. The UPOV system does not allow farmers to save, exchange or sell seeds of the varieties it protects, thus subjecting poor farmers to dependence on commercial breeders.

Geographical indications (GI, Articles 22-24 of TRIPS) are permanent and community-owned, and provide one of the mechanisms for protection of some forms of traditional knowledge and culture. Some FTAs insist on a "first to file" trademark approach, which permits firms from developed countries to expropriate traditional knowledge and the interests of communities by registering a trademark for products made, grown or nurtured by traditional communities. From the perspective of developing countries affected, this is an issue of "biopiracy."

The United States is also employing FTAs for coalition building (e.g., FTAs with Middle Eastern countries that cooperate in the regional peace process and FTAs with countries that support the War on Iraq through the "Coalition of the Willing") and coalition busting (e.g., FTAs with former Group of 20 members. US and Europe encountered opposition on agriculture negotiations from G-20, a group of non-subsidizing developing countries during the 5th WTO Ministerial Conference).

Thus, there is a political element in FTAs. The interests of developed countries in FTAs can be non-trade-related: (1) long-term energy security; (2) reward developing countries for supporting global foreign policy (e.g., on drugs and terrorism); and (3) reduce pressures for migration by raising living standards in poorer, neighboring countries.

North-South FTAs tend to be asymmetric. The burden of tariff liberalization in North-South FTAs weighs disproportionately on developing countries. For example, 32% of tariff lines in the United States MFN tariff are duty-free, and 45% at rates of three percent or less (i.e., at a level where it is more profitable to pay the MFN tariff than assume the costs involved in satisfying the rules of origin and related administrative procedures).

There is no convincing evidence that FTAs with developed countries increased investment flows to developing countries. Joseph Stiglitz (2005) has pointed out that bilateral FTAs tend to

create "false hopes and dreams" of increased investment flows from developed countries.

Upon joining an FTA, a country may switch its imports from an efficient producer of certain goods to one that is less efficient because of incentive distortions (most pronounced for highly substitutable goods) created by tariff differentials. Trade diversion may be welfare reducing, while trade creation is almost always welfare-enhancing. South-South FTAs tend to be more trade creating and thus welfare-enhancing. Trade diversion, i.e., the rise in trade among FTA members at the expense of trade between FTA members and non-members, diverts trade from non-members who are least-cost suppliers. This is likely to diminish welfare in member and non-member countries alike. Another view is that an FTA formed among low-income countries is likely to harm the lowest income member due to trade diversion and, unless there is at least one high-income member, convergence to a high-income level is not possible.

Stiglitz (2005) noted that the "spaghetti bowl" of FTAs undermines the market economy. Some have used the term "spaghetti bowl" to portray what appears to be an incoherent, often overlapping and seemingly random maze of FTAs. According to Stiglitz, bilateral FTAs are bad for global efficiency (i.e., the principle of single price is at the core of the efficiency of the market economy and this is eroded by the "spaghetti bowl" phenomenon) but can be good if among equals.

Bilateral FTAs can be "WTO-plus" (i.e., provisions in FTAs that go beyond WTO obligations, providing freer access for goods and services) and "WTO-minus" (i.e., provisions in FTAs that erode rights to take specific actions in pursuit of development objectives). "WTO-plus" measures could include obligations in areas where the application of the MFN clause has proven technically or politically difficult, such as action on Sanitary and Phyto-Sanitary Standards, liberalization of Movement of Natural Persons, commitments on government procurement, and exchange of Mutual Recognition Agreements. "WTO-minus" measures could include erosion of the right to impose compulsory licensing of patents or performance requirements on foreign investors. (This particular policy flexibility is under threat in bilateral FTAs.)

Developed countries can exercise their advantage of being larger and more advanced a lot more easily in the bilateral context,

such that failure to conclude an FTA could lead to withdrawal of support in international relations and domestic politics.

Based on the foregoing, is the world truly flat? Perhaps it is, from the perspective of developed countries. The world seems unflat, however, for developing countries. As noted by Martin Khor (2005), the "equal treatment" of parties that are not of equal capacity is likely to have unequal outcomes.

For the Philippines, the following data are indeed telling:

Free Trade Agreements

Philippines	ASEAN (AFTA)	1992	Regional Trade Agreement
	Global System of Trade Preferences (GSTP)	1992	Inter-Regional Trade Agreement
	China	2002	ASEAN plus Agreement
	Closer Economic Relations (CER) Australia and New Zealand	Negotiation in progress	ASEAN plus Agreement
	India	Negotiation in progress	ASEAN plus Agreement
	Japan	Negotiation in progress	ASEAN plus Agreement
	Japan	Signed in September 2006; For ratification	Bilateral Free Trade Agreement
	Rep. of Korea	Negotiation in progress	ASEAN plus Agreement

Comparative Economic Performance: 1998 – 2003

Indicator	1998	1999	2000	2001	2002	2003
Foreign Direct Investments (Billion US Dollars)	0.88	2.11	1.40	0.86	1.43	1.49
Exports (Billion US Dollars)	29.50	35.04	38.08	32.15	35.21	35.75
Unemployment Rate (percent)	9.60	9.40	10.10	9.80	10.20	10.20

We have had FTAs since 1992. But while foreign direct investments and exports may have increased, unemployment also increased. Imports may have something to do with it.

Outsourcing

And what about outsourcing? Outsourcing generates jobs according to Friedman. Fine. But outsourcing *per se* is not without issues and concerns. The low hiring but high turnover rate in Philippine call centers is indicative. The low hiring rate (between three percent and five percent of applicants per year) indicates the need for government intervention in the area of education and training, and private investments in human capital. The high turnover rate (estimated at 20%) reflects the demand for voice.

Perhaps theory can help explain social phenomenon. James March and Herbert Simon (1958) developed a model for employee voluntary turnover. Based on the model, turnover is affected by two factors, that is, ease of leaving and desirability of leaving a firm. Ease of leaving a firm is primarily determined by alternative employment opportunities outside the firm. This means that the more attractive the labor market is outside the firm, the higher the probability of leaving. The desire to leave is a function of dissatisfaction at the current job; that is, the higher the dissatisfaction level, the greater the probability of leaving. However, if there is opportunity for employees to voice out dissatisfaction, it would lead to changes in work conditions. Employees might choose the "voice" rather than the "exit" option.

Is there an empirical basis for this seeming demand for "voice?" In a 2005 study, Philippine call center workers were asked if they would be interested to join an affordable, principled and efficient workplace union. Fifty one percent of those surveyed gave affirmative answers.

INTERESTED TO JOIN AFFORDABLE, PRINCIPLED AND EFFICIENT UNION	TOTAL	%
No	45	45%
No answer	3	3%
No comment	1	1%
Yes	52	51%
GRAND TOTAL	101	100%

A closer look at the respondents who said they were interested in joining a union reveals the following:

- 50% were males while 48% were females.
- 85% finished a bachelor's degree.
- Work typology for a big majority was customer service.
- 42% experienced moderate pressure at work while 33% encountered heavy work pressure.
- With regards to the degree of workplace satisfaction, 44% were neither happy nor unhappy while about 6% were unhappy.
- Only 13% experienced problems when taking breaks.
- 3 out of 4 (75%) rendered night work during the 12 midnight to 6 o'clock a.m. interval
- A substantial minority (42%) said their health was affected by working night shifts.
- Almost all were never trade union members, but 71% had general knowledge about trade unions.
- A big majority (62%) had an average monthly take home pay of P15,000 or below.
- A big majority (62%) also said that salary/wage rate negotiation is the most important role of trade unions.

In other words, doubts are being raised as to the quality of jobs being generated by the industry.

Race to the Bottom

Cost is the main driver for the forms of collaboration identified by Friedman. Even Friedman admits to this. Most companies, whether local or multinational, compete on the basis of cost. While regulatory measures are intended to protect the vulnerable, they also represent costs. And costs are uneven across countries. This fuels the desire for flexibility not only among companies, but also among countries. Flexibility can lead to reduction of regulatory measures, say, on hours of work, minimum wages and occupational safety and health, which is why it has the tendency to become, as Justice Brandeis of the US Supreme Court puts it, "a race to the bottom." In this sense, regulatory measures become a comparative advantage. From the viewpoint of development administration, this is a major area of concern. After all, development is about raising the quality of lives.

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