

Globalization and multilateralism are in crisis.*

Alejandro Díaz de León
Governor, Banco de México

Trade tensions have become a major obstacle to global economic growth, with significant effects on manufacturing production, investment, and business confidence. Current purchasing manager surveys show that a contraction in manufacturing may already be underway. Disruptions in global value chains have affected the most globally integrated processes and dampened business investment. These adverse impacts have been more severe in economies more open to trade and with large export volumes to the United States.

Markedly weak investment stands out as one consequence of a highly uncertain environment due to trade and geopolitical tensions. In the last few years, particularly in Mexico, these factors have triggered a strong pushback on investment, directly in manufacturing, but also, indirectly, in services.

The baseline scenarios for global growth have already been affected and large downside risks prevail, as a more hostile environment to trade and investment seems to be more permanent. This is especially so since recent trade tensions are related not only to bilateral trade deficits, but also to technology supremacy and immigration issues, as is the case with Mexico regarding the latter factor.

The multilateral institutions, strategies, and approaches put in place since Bretton Woods seventy-five years ago face deep structural challenges. Arguably, globalization and multilateralism are in crisis, both from the heightened pressure from protectionists and nationalist agendas and from the accumulated costs and tensions derived from global imbalances, associated in part with some countries' use of managed exchange rates and export-led growth strategies.

To attain growth and development, market economies need to engage with each other in a mutually constructive, predictable, and evenhanded way. History and theory show that national interests are best served by international cooperation. Multilateralism seeks to find solutions to global externalities through cooperative approaches that improve both national and global outcomes. This can be considered as an effort to procure much-needed global public goods, not only to address old challenges such as an evenhanded and balanced approach to trade, flexible

* Published in *The International Economy*, Summer 2019.

exchange rates, foreign direct investment, and the international financial architecture, but also new ones, such as climate change and more inclusive growth and development.

An issue that has gained increased attention is the role of monetary policy and its implications, spillovers, and tradeoffs for foreign exchange dynamics, trade performance, and growth. An extreme and narrow view considers competitive devaluations, race-to-the-bottom policies, and even so-called currency wars. These arguments misunderstand currency markets and the role of the exchange rate, and may lead to the confusion that monetary policy should set real exchange rate objectives for competitive purposes.

In this regard, history and theory provide ample evidence that monetary policy should focus on attaining low and stable inflation, hence contributing to output smoothing and financial stability, and not on targeting the exchange rate. To this end, central bank independence is of paramount importance in attaining a well-focused, medium-term-oriented monetary policy, with ample and much-needed distance from political cycles.

We must not forget that on the road to development, at both the national and global levels, we need to reconcile individual (national) interests with the common (global) good. History has taught us that short-sighted approaches lead to mirages at best, or extremely painful lessons at worst.