Globalization: overview

Economics, Globalization

IntroductionGlobalizationis not a single concept that can be defined and encompassed within a set time frame, nor is it a process that can be defined clearly with a beginning and an end. Furthermore, it cannot be expounded upon with certainty and be applicable to all people and in all situations.

Globalization involves economic integration; the transfer of policies across borders; the transmission of knowledge; cultural stability; the reproduction, relations, and discourses of power; it is a global process, a concept, a revolution, and " an establishment of the global market free from sociopolitical control. " Globalization encompasses all of these things. It is a concept that has been defined variously over the years, with some connotations referring to progress, development and stability, integration and cooperation, and others referring to regression, colonialism, and destabilization.

Despite these challenges, this term brings with it a multitude of hidden agendas. An individual's political ideology, geographic location, social status, cultural background, and ethnic and religious affiliation provide the background that determines how globalization is interpreted. In 1995, Martin Khor, President of the Third World Network in Malaysia, referred to globalization as colonization.

Concurrently, Swedish journalist Thomas Larsson, in his book The Race to the Top, The Real Story of Globalization (2001) stated that globalization: " Is the process of world shrinkage, of distances getting shorter, things moving closer it pertains to the increasing ease with which somebody on one side of the world can interact, to mutual benefit, with somebody on the other side of the world" " Globalization is a process that encompasses the causes, course,

and consequences of transnational and transcultural integration of human and non-human activities’’.

Economic globalization Economic globalization takes many forms. It may involve trade between individuals or businesses in one country with those of another. Globalization of this sort is as old as recorded history. Ancient coastal tribes traded with those in the mountains and deserts, each gaining prized goods they could not otherwise have enjoyed. Today, we take for granted the fact that much of what we consume or use originated elsewhere, often in a strange foreign land.

Or businesses may decide to produce their products not only at home but also in other countries, either to evade the tariffs or quotas of countries where they wish to sell their products, or to cut their costs of production by, say, hiring cheaper labor. Then globalization involves the bundling together of financial capital, technology, and other strategic inputs in order to transfer them as direct foreign investment (hereafter, direct investment) in another country. Direct investment implies control over the assets transferred abroad.

Foreign investments that don't involve control are called foreign portfolio equity investments (hereafter, portfolio investment). They are more likely to be made by financial institutions or investors like pension funds, insurance companies or investment trusts, which are interested only in a return on their investments commensurate with the risks they are taking. If returns fall or risks rise, portfolio investment is much less dependable than direct investment as a source of longer-termfinancefor a country's development.

The activities of transnational corporations are a still deeper form of globalization. They coordinate their activities with many entities throughout the world, producing in many places with complex networks of production and finance. This form of globalization has recently been named " alliance capitalism," in order tostressthe growing importance of strategic alliances between business entities, as businesses search for ways to protect their competitive advantages and global market positions.

Governments also compete for economic advantage globally. They often support private research and development activities, finance worker retraining, protect theenvironment, and promote inter-firm alliances. When governments decide it is in their interest to cooperate rather than compete, they may form supranational organizations, like the International Monetary Fund (IMF) and the World Trade Organization (WTO), or less formal regional bodies, in order to achieve shared objectives, e. g. stable macroeconomic conditions, more growth through trade, or " market-friendly" economies. Globalization trends * Rapid growth of trade Since the Second World War, trade between nations of goods and services has grown much faster than world economic output, primarily for three reasons. First, rapid improvements in transportation and communications made it easier and cheaper to reach new markets. The cost of a three-minute telephone call between New York and London, for example, has fallen from $55 (in 2002 dollars) in 1950 to less than $1 today.

Second, successive rounds of tariff negotiations have virtually eliminated border barriers among developed countries, and many less developed countries have unilaterally reduced their tariffs and quotas, even without

prodding from the IMF or World Bank. Third, processing trade - trade that involves goods whose components cross borders more than once before reaching final buyers - expanded rapidly. An F-140 Ford truck is assembled from parts originating in at least forty-five countries. Trade is widespread for almost all nations, and its importance is rising virtually everywhere.

A quick review of the labels in one's clothing is a good reminder of the pervasiveness of trade. Trade between nations also has been transformed in recent years, from transactions over which national governments exercise significant control - international trade, if you will - to a form of globalized trade engineered and managed by large, dominant transnational corporations - transnational trade. Well over one-third of all US imports and exports, for example, take place between the divisions and subsidiaries of the same company.

This distinction is important for the reason that it signals a transfer of power and control away from national governments that, for all their failures, can be influenced by the general public. Transnational corporations, on the other hand, are not set up to serve others than their stockholders. * Even faster growth of foreign direct investment By latest count, there are at least 39, 000 transnational corporations owning production facilities outside their home country.

Direct investments by these large firms, which are growing more than twice as fast as trade, are probably the best indicators of the growth of deep cross-border economic integration. In fact, worldwide sales of the foreign subsidiaries of transnational enterprises now exceed the value of all internationally traded goods. Most direct investment decision-makers are in

the leading industrial countries, although investment decisions by firms in developing countries like South Korea, Taiwan and Brazil are increasing quite rapidly.

The largest 100 transnational corporations (excluding those in banking and finance) are estimated to control about one-third of the assets held by transnational corporations abroad. Foreign direct investment also is a primary means of transferring technology across borders. In this case, the technology is transferred within the firm, where it becomes part of the investing firm's significant and continuing financial stake in the success of a foreign affiliate.

It, too, has been growing rapidly - by some measures even faster than trade; but its growth has been concentrated in relatively few large firms with strong technological and brand-name assets. * The flood of portfolio investment across borders Encouraged by " market friendly" policies of developing countries - policies often imposed on debtor nations by the International Monetary Fund - individual investors, pension plans and mutual funds increased their stakes five-fold in the equity shares and bonds of third world companies in the early 1990s.

Such rapid growth contrasted sharply with the experience of the 1980s when equity investments were rare and many poor countries staggered under the weight of the debts they owed to outsiders. But by 1997, equity investors suddenly began to reassess the risks of their exposure, and the Asian crisis was born. In retrospect, the flow of portfolio investments was too fast to be absorbed into productive activities. It created bubbles in stock and real

estate prices and encouraged luxury consumption that gave the illusion of prosperity unrelated to real increases in productivity.

The faster portfolio investments flowed into Thailand, Malaysia, Indonesia, South Korea, and Hong Kong, the fastermoneywas sucked out of the productive sector to join the speculation. When investors finally sensed their risk, they rushed to pull their money out. Hence, the flood of portfolio investments reversed direction by the end of 1997, ushering in severe recessions in many countries from which few have fully recovered. Or consider the Russian crisis of 1998, the Brazilian crises of 1999 and 2002, and the ongoing Argentine crisis, all of them aggravated by fickle changes n the attitudes toward risk and reward of foreign investors. A rumor can trigger a self-fulfilling speculative attack, e. g. on a currency, that may even be baseless and far removed from the economic fundamentals. This can cause a sudden shift in the herd's intentions and lead to unanticipated market movements that create severe financial crises. (For deeper analysis of the financial aspects of globalization, see the essay on " Casino Capitalism") * The proliferation of business alliances

Cross-border agreements between firms based in different countries have become increasingly important complements to traditional trade and direct investment activities, with the range of such agreements growing ever wider. Their rapid growth since about 1985 is explained by the fact that technological changes are becoming more deeplyscience-based and that in some fields - notably information technology - few (if any) large firms are any longer capable of generating all the research needed to remain competitive.

Thus, many transnational corporations have been driven to mutual sharing of knowledge about new technologies, production processes and distribution techniques with others. A flurry of mergers and acquisitions in the late 1990s, boosted direct investment flows substantially, despite a slowdown in global economic activity. * The institutions of globalization As transnational trade and investment soared in the last fifteen years, so, too, did the regulatory machinery for assuring their continued growth.

During this period, the World Trade Organization emerged as the dominant arbiter of trade; the IMF was transformed into a bank of last resort; the IMF and the World Bank sorted out their respective roles in deeply indebted countries; the Organization for Economic Cooperation and Development (OECD) negotiated a Multilateral Agreement on Investment (MAI) designed to restrict a nation's ability to regulate foreign investment; and the sophistication of business alliances between dominant corporate players metastasized throughout the multinational business community.

The Benefits of Globalization Globalization has led to growing competition on a global basis. While some fear competition, there are many beneficial effects of competition that can increase production or efficiency. Competition and the widening of markets can lead to specialization and the division of labor, as discussed by Adam Smith and other classical economists writing on the benefits of a market system. Specialization and the division of labor, with their implications for increases in production, now exist not just in a nation but also on a worldwide basis.

Other beneficial effects include the economies of scale and scope that can potentially lead to reductions in costs and prices and are conducive to

continuing economic growth. Other benefits of globalization include the gains from trade in which both parties gain in a mutually beneficial exchange where the " parties" can be individuals, firms and other organizations, nations, trading blocs, continents or other entities.

Globalization can also result in increased productivity as a result of the rationalization of production on a global scale and the spread of technology and competitive pressures for continual innovation on a worldwide basis. The Costs of Globalization Globalization also has its costs, and these must be weighed along with its benefits in order to assess its true consequences. As growth of the world economy sputtered and disillusionment over the advantages of privatization grew during the last few years, the costs of globalization became more apparent.

Competitive pressures and more market-oriented policies create pockets of unemployment not easily corrected in the short-run. The structural changes causing unemployment tend to exaggerate the differences between those with theeducation, skills, and mobility to flourish in an unfettered world market, such as the owners of capital, highly skilled workers, and many professionals, and those without such attributes. Globalization has a way of eroding the bargaining power of groups that cannot move, leading to greater instability in their earnings and hours worked.

The apparent " losers," unlike the highly skilled " winners," are made increasingly anxious about their place in an integrated world economy, whether they are blue-collar workers in textile factories in the southern US or subsistence farmers in Mindanao. The best evidence of this is found in

growing income inequalities. The gap between rich and poor countries has long been the major source of inequality among people of the world.

Somewhat surprisingly, this gap has closed slightly over the past couple of decades. Income distribution within countries, on the other hand, has widened rapidly, and this has had a deleterious effect on many parts of the world. Almost everywhere in the west, despite " social safety nets," the youngest, poorest and least educated are significantly worse off than their counterparts were twenty years ago. Many poor countries also are becoming less egalitarian in the face of globalization.

The rural poor, especially the smallholders and the landless of Asia and Latin America, are being ruthlessly dispossessed and displaced. What forms of globalization are responsible for these disruptive changes in the markets for workers? Many people blame the changes in more developed countries on competition from low-wage countries. Most economists, however, blame the losses of lower-skilled workers on technological changes (e. g. , computerization) that are biased against the demand for low-skilled labor.

While both of these reasons no doubt have contributed to the widening of income-gaps within countries, the much larger reason appears to be the dramatic policy changes described as " liberalization" that commenced at the end of the 1970s. In the richer countries, these changes included a move from macroeconomic policies that tried to control the levels of aggregate demand (Keynesian policies) toward ones that tried to control money supplies (monetarist policies), and a shift from state-provided welfare toward pay-as-you-go social services.

At the same time, the public provision of basic services such as water and electricity, frequently at subsidized prices, has been replaced by privatized providers at " economic" prices; industrial interventionism and labor protection have given way to laissez-faire; and tax systems whose major purpose was to correct inequalities have been transformed into systems mainly intended to promote incentives and economic efficiency. There were parallel changes for developing countries, where policy was subject to the same paradigmatic shifts largely as a result of the influence of the richer countries, most directly through conditions mposed by the IMF and the World Bank. When in the 1980s many developing countries no longer could generate sufficient income to meet their debt obligations, they were faced with the choice of retreating into complete economic Isolation or seizing the life-line thrown them by the IMF and the World Bank - a life-line composed of " stabilization" and " structural adjustment" loans available only if they agreed to far-reaching and " market friendly" changes in national economic policies.

These stabilization and structural adjustment programs took scarce economic resources away from other possible uses by poor countries. Consider, for example, the costs of implementing western financial codes and standards, one of many requirements to be met. Here the choice for countries starved for development was between training more bank auditors and accountants in order to meet the standards of financial liberalization, and using these resources, say, to hire more secondary-school teachers or boost spending levels for the primary education of girls.

These programs seem to hit the poor the hardest, with the urban working class particularly at risk. Globalization also creates conflicts between governments over domestic social priorities and the social institutions that embody them. Indeed, it is precisely the convergence of the policies just mentioned that has forced countries into what Thomas Friedman calls a " golden strait-jacket" but others call a " toxic straight-jacket" - a standardization of policies world-wide that vastly narrows the ability of single countries to honor their more unique political and cultural preferences.

In Friedman's terms, " your economy grows but your politics shrink. " Deviate too far from the new globalization rules and a country soon will see its investors stampede away, interest rates rise and stock market prices fall. Put another way, the argument against unrestricted global freedom of trade and movements of financial capital is not primarily an economic one. Rather, it is that the economy should serve the needs of society, not society the imperatives of the market. There is not much doubt that free markets are the most economically efficient type of capitalism.

For most economists that ends the matter. Yet what " social market economies" do, like those of Japan and most of Europe, is in no sense irrational. Policies in those countries to maintain social cohesion are just as important as efficiency in the allocation of scarce resources. Consider, for example, the struggle the European Community has had over the harmonization of policies on employment, welfare, immigration, and competition in order to create a common market and a common currency and to remain internationally competitive.

In Japan, large corporations have started to dismantle the post-war practice of providing lifetime employment, one of Japan's most distinctive social institutions, in order to adapt to the pressures of globalization. In South Korea, labor unions have taken to the streets to protest the government's relaxation of firing restrictions. And Latin America countries are competing with each other to liberalize trade, deregulate their economies, and privatize public enterprises.

Efforts by developed countries in North America and Europe to " harmonize" labor standards are motivated only in part by the fear in developed countries of losing jobs to workers earning much less in developing countries. International labor standards have become a point of contention in trade disputes not only for economic reasons, but also because low wages and weak safety standards abroad violate thehuman rightsof workers. The US and others are finding it increasingly difficult to negotiate worker protections for the charters of multinational institutions like the World Trade Organization.

Thefailureof the WTO meeting in Seattle in December, 1999, was more the result of this policy straight-jacket than of the violent protests in the streets. Disagreements also are rising over the environmental consequences of globalization. Becausepollutionis generated most often by industrialization, the countries that are soon becoming the most industrialized, like China, Brazil, and India, are the likeliest sources of future global pollution. They are unlikely to throttle back their industrial plans in order to protect the environment, as some in the US and Europe have suggested.

That would raise their costs and erase their comparative advantage. Arguments in Kyoto at the December, 1997 Summit on GlobalClimate Changevividly illustrated the political tensions wrought by globalization, as has the abrogation of the Kyoto accords by the US administration recently The " invisible hand" of the market is acceptable to most people only if the losers from market forces are compensated by the winners. A central function of government has been to assist in this transfer by elping the losers to adjust to change - usually by means of unemployment compensation, severance payments, and adjustment assistance. In essence, governments have used their fiscal powers to insulate domestic groups from excessive market risks, particularly those originating in international transactions. This is the way governments have maintained domestic political support for liberalizing trade and finance throughout the post-war period. But recently, the idea of giving support to the losers has come under withering attack.

Employers no longer grant job security, partly for competitive reasons and also because they are more mobile and less dependent on the goodwill of local work forces. Governments are less able to help the losers because the slightest hint of raising taxes leads to capital flight in a world of heightened financial mobility. Moreover, the ideological onslaught against the welfare state has paralyzed many governments and made them unable to respond to the domestic needs of a more internationally competitive economy.

Accordingly, at the very time increased integration into the world economy has raised the need of governments to redistribute tax revenues or implement generous social programs in order to protect the vast majority of

the population that remains internationally immobile, governments find themselves less able to raise taxes. The heightened mobility of financial capital has led to competition among nations to attract foreign investment, and a key tool of competition is to offer a relatively low-tax environment. Tax competition, in turn, threatens to undermine the individual and corporate income taxes.

The US and other affluent countries have responded, first, by shifting the tax burden from (mobile) capital to (less mobile) labor second, when further increased taxation of labor becomes politically and economically difficult, by cutting the social safety net. This is bound to jeopardize social stability. Even governments with significant budget surpluses, like the United States until the aftermath of September 11, seem unwilling to protect the weak against the cruelties of the market.

Dealing with Globalizing world threats and injustice In a world in which market forces are subject to no overall constraint or regulation, justice and peace are continually at risk. Unregulated capitalism degrades the environment and kindles conflict over natural resources. It enriches the educated elites and owners of capital, often at the expense of less able and less mobile populations. By promoting minimal government intervention in the economy, it neglects those in greatest need. And in expanding parts of the world, it locks nation-states into competition not only for markets but for survival.

The global market as it is presently organized forces nations to become rivals for resources while creating weak methods for conserving them. History confirms that free markets are inherently volatile institutions, prone

to speculative booms and busts. Overshooting, especially in financial markets, is their normal condition. The recent Implosion of the tech stock bubble is just the latest example. To work well, free markets need not only regulation, but active management. During much of the post-war era, world markets were kept stable by national governments and by a regime of international cooperation.

Only lately has a much earlier Idea been revived and made into an orthodoxy that provided there are clear and well-enforced rules of the game, free markets can be self-regulating because they embody the rational expectations that participants form about the future. On the contrary, since markets are themselves shaped by human expectations, their behavior cannot be rationally predicted. The forces that drive markets are not mechanical processes of cause and effect, as assumed in most of economic theory. They are what George Soros has termed " reflexive interactions. Because markets are governed by highly combustible interactions among beliefs, they cannot be self-regulating. Thoughtful people have a right to be alarmed by the evidence that freer markets are unstable and that all people are not prospering from their spread. Whole communities, whole regions, whole nations are being marginalized by the inexorable forces of change brought on by economic integration. Povertyis rising, almost everywhere. Yet the power of governments to alleviate the suffering of those who are losing out is slipping away from them.

Evidence of this is that an appropriate balance is not being struck between the economic and non-economic aspirations of human beings and their communities. Indeed, the evidence is mounting that globalization's trajectory

can easily lead to social disintegration - to the splitting apart of nations along lines of economic status, mobility, region, or social norms. Globalization not only exacerbates tensions among groups; it also reduces the willingness of internationally mobile groups to cooperate with others in resolving disagreements and conflicts.

What, then, can be done to share the benefits of globalization more widely and to ameliorate its social consequences? The answer to this question is not to disengage altogether from the processes of globalization. That would be foolish as well as impossible. Many of the underlying changes that have occurred in the global economy are now irreversible. Rather, the question is how to engineer a new balance between market and society a balance that will require greater human control over the processes of change and the sharing of its fruit. The following recommendations are meant to help strike such a balance.

They do not conform precisely to proposals generated by either the human development consensus or the people-centered consensus, yet they draw from both groups. Nor do they represent a comprehensive blueprint for reform, which surely would include far more radical changes in the institutions of business, government and daily living than proposed here. Things that governments should do * Reform begins with a rehabilitation of the modern state In Liberia, Albania, Afghanistan, Tajikstan, Colombia, Siberia, Chechnya, and Somalia, the threat to peace and economic progress does not come from tyrannous or expansionist states.

It comes from the absence of effective government of any kind. The Washington consensus neglects the many ways unregulated world markets

threaten cohesion of society and stability in governments. The World Bank's recent repudiation of the dogma of minimal government is welcome; but it falls far short of the need to provide the institutions necessary to assure security from destitution, unemployment and exclusion. Develop a regulatory framework for coexistence and cooperation among the world's diverse economies As it is presently organized, global capitalism is supremely ill-suited to cope with the risks of geo-political conflict that are endemic in a world of worsening scarcities. If today's laissez-faire regime is not reformed, it is likely to fracture and fragment as mounting scarcities of resources and conflicts of interest among the world's great powers make international cooperation even more difficult. Free markets are creatures of strong governments and cannot exist very long without them. More efficient and generous systems of social insurance They would allow losers to secure more of the benefits of international economic integration and suffer less of its social costs. Indeed, the social welfare state is the flip side of the open economy; the more exposed is the economy to external shocks, the more certainly it will need a generous system of income transfers. Any movement towards freer trade and capital movements should be accompanied by more generous adjustment assistance policies, including unemployment benefits and retraining and relocation subsidies. Taxation of footloose capital movements Generous and appropriate systems of social insurance must be financed in some way. If national sources of taxation are no longer adequate to this task, then it may well be time to consider taxation of footloose factors at the global level, with revenue sharing among nations. The most radical

reform would involve outright restrictions on speculative capital transfers, with all their potential for abuse and corruption.

A more moderate reform might include measures designed to regulate the timing of capital transfers or ones that increase the cost of speculative transactions. Similarly, a uniform tax might be imposed on inter-currency transactions, e. g. , the " Tobin Tax. " 6 More exchange of information among tax authorities would be another step in the right direction. Better still; an international convention to restrict the ability of transnational firms to avoid taxation should be negotiated. * Global safeguards

A new system of global safeguards also is required to accommodate important differences in the social, political and cultural preferences of nations. Multilateral institutions like the WTO should permit selective disengagement from the discipline of multilateral treaties, under well-specified contingencies, when countries need breathing room to satisfy domestic requirements that are in conflict with trade policies, eg, to assist labor reallocation or to protect the environment. Similar provisions should be made in treaties governing foreign direct and portfolio investment. Reform IMF and World Bank conditional lending policies These multilateral agencies should replace bankrupt structural adjustment efforts with policies and programs that more adequately meet the needs of the poor and promote sustainable, participatory, and equitable development. Among the conditions that should be included in loan agreements are: 1. reduction of inappropriate levels of military spending 2. preservation of spending on basic needs, including education andhealthcare 3. ssurance of a safety net for those most severely affected by adjustment policies 4. prevention of adverse

environmental effects such as 5. deforestationand soil degradation 6. a system for monitoring and correcting (as may be necessary) the effects of adjustment policies These agencies also must be more accountable to the people affected by their policies and projects through increased transparency, greater access to information, and greater participation in the development of projects, programs, and policies.