Part I
ECONOMICS

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Economic Globalization

The nature and extent of global economic integration is subject to intense dispute (Held and McGrew, 2003, part 4). At issue is whether it is accurate to talk of the emergence of a single borderless global economy; how far such an economy is driven by the new processes of the electronic, information order; and the degree to which the new global economy places constraints on progressive economic and social policy. For some, the new geography of the world economy heralds the emergence of a 'single, planetary scale worldwide economy' (see Dicken, 1998). Led by the growing interlinking of global and local production systems, the new economic order is increasingly integrated across space, real and virtual. Multinationals and global production networks, working on products as diverse as cars, computers and clothes, are reshaping economic activity. The result is a novel form of economic globalization, mediated by the global infrastructures of information and communication, functioning as a unit in real or chosen time (Castells, 2000). Regional differences still matter, and many are marginalized and excluded. But, according to the theorists of the global economy, the current world economic order operates with a different form and logic from those found in earlier centuries.

This view is challenged by those who argue that economic globalization is far more limited than is often realized (Hirst and Thompson, 1999; Gilpin, 2001). While they accept that the links between national economies have become more marked, they find that the 'new global economy' is less integrated and inclusive than in the late nineteenth century. Distance and national borders are still 'powerful barriers to economic interaction' (CEPR, 2002). In addition, governments are not as constrained by the open world economy as is often claimed. Macroeconomic policy, along with the social policies underpinning the welfare state, remains the preserve of government. Global markets have not triumphed over states.

The three chapters which follow will not seek to unravel this controversy at length (Held et al., 1999, has sought to do this). Rather, they will seek to depict some of the core trends in the organization of production, trade and finance; the extent to which these are asymmetrical and stratified across countries and regions; and the leading policy and political challenges. The argument is that, irrespective of precisely how one resolves the controversy about economic globalization, clear transformations have occurred in the world economy and they require a new policy mix. The problems of economic globalization are sufficiently urgent to warrant a new political response.

Production, trade and finance

National economies are heavily enmeshed in the global system of production and exchange. Central to this system are rapidly developing multinational corporations (MNCs). Through foreign direct investment or subcontracting arrangements, companies can site almost any value-added activity in any location in the world, subject to adequate infrastructure and human capital reserves. Products that two decades ago were produced in one country are now routinely made up of components that have crossed dozens of borders before they are finally assembled. A new highly specialized geographic division of labour has emerged, recasting the nature and form of production systems. Multinationals span every sector of the global economy – from agriculture to manufacturing and finance – and they have taken economic interconnectedness to new levels. Foreign direct investment (FDI) reached three times as many countries in 2000 as it did in 1985 (UNCTAD, 2001b, p. 4). At present, 60,000 multinational corporations, with nearly 820,000 foreign subsidiaries, sell 15,680 trillion dollars of goods and services across the globe each year, and employ twice as many people as in 1990 (Perraton et al., 1997; UNCTAD, 2001b). Multinational corporations account for about 25 per cent of world production and 70 per cent of world trade, while their sales are equivalent to almost 50 per cent of world GDP (Goldblatt et al., 1997; UNCTAD, 2001b). A quarter to a third of world trade is intrafirm trade between branches of multinationals. While global exports and trading relations are more important than ever in the world economy and to individual countries for their general prosperity, transnational production is even more significant. To sell to another country you have increasingly to invest and have a presence there. To do business with many countries, slicing up the value chain can be a distinct competitive advantage.

The majority of the assets of multinationals are generally found in OECD countries and in a relatively small number of developing ones, but their impact is growing everywhere. Through their production, investment and marketing activities, multinational companies, as a recent Oxfam report put it, 'are linking producers in developing countries ever more closely with consumers in rich countries' (2002, p. 8). From women workers in Bangladesh's garment factories, to workers in China's special economic zones and workers in the free trade zones of Central America, global production networks are generating dense patterns of economic interdependence. Of total world foreign direct investment in 2000, 95 per cent went to 30 countries (UNCTAD, 2001b, p. 5). However, over the last few decades, developing economies' share of foreign investment flows (inward and outward) and of world exports have increased considerably (Castells, 2000; UNCTAD, 1998a, 1998b). The newly industrializing countries of East Asia and Latin America have become an increasingly significant destination for OECD investment and an increasingly important source of OECD imports (Dicken, 1998). By the late 1990s almost 50 per cent of total world manufacturing jobs were located in developing economies, while in 2000 over 65 per cent of developing country exports to the industrialized world were manufactured goods – a thirteenfold increase in less than four decades (UNDP, 1998; World Bank, 2002). For some products, developing country exports account for a half or more of world exports (UNCTAD, 2002b).

The contemporary globalization of production is thus not just an OECD phenomenon, but embraces all regions and continents.

This picture of the transnational organization of production, impressive though it is, does not fully depict the importance of multinational corporations to global economic change. For multinationals form economic relationships with smaller national firms and link them into transnational production chains. They often control the global distribution and transport networks on which independent exporters depend, especially in developing countries, and are of fundamental importance in the creation and transfer of technology across borders. While multinationals typically account for a minority of national production, they are concentrated in the export industries and in the most technologically advanced economic sectors. Hence, as Ulrich Beck put it, 'there is only one thing worse than being dominated by MNCs, and that is not being dominated by MNCs!' (2001).

Linked to the global production system is an extensive network of trading relations. If, in the past, international trade formed an enclave largely isolated from the rest of the national economy, it is now integral to the structure of national production in modern states. All countries are engaged in international trade and nearly all trade significant proportions of their national income. The historical evidence shows that, both in absolute terms and in relation to national income, international trade has grown to unprecedented levels. Measured as a share of GDP, trade levels now are much greater among OECD states than they were in the late nineteenth century (Held et al., 1999, ch. 3). Moreover, as barriers to trade have fallen across the world (in general, tariffs have declined substantially and transportation costs have decreased), global markets have emerged for many goods and, increasingly, services. World trade (trade in merchandise and services) in 1999 was valued at over $6.8 trillion with exports having grown, as a percentage of world output, from 7.9 per cent in 1913 to 17.2 per cent in 1998 (Maddison, 2001).

During the postwar period, an extensive network of international trade emerged which enmeshed most states – developed and developing – in complex webs of global and regional economic relations. Although there are major trading blocs in Europe, North

America and Asia-Pacific, these are not regional fortresses. While they operate complex systems of incentives and disincentives to trade (see chapter 2), these blocs remain open to competition from the rest of the world. As far as economic activity is concerned, regionalization and globalization appear to be mutually reinforcing (Hettne, 1998). This is because regionalism has principally been a vehicle for the liberalization of national economies, a strategy which has taken precedence over the protection of markets (Gamble and Payne, 1991; Hanson, 1998). Through the 1980s and 1990s, developing countries and the transition economies of the former communist bloc have become more open to trade as well. Their share of world trade has risen significantly, particularly in manufactured goods. Across many regions the expansion of trade has been associated with economic growth and rising standards of living. While there is no automatic link between increased trade and reduction of poverty, well-managed integration into global trade networks can lead to higher wages, higher income and a decline in poverty (cf. World Bank, 2001; Oxfam, 2002).

Alongside transnational production and trade networks, the dynamics of finance have become central to economic globalization. World financial flows have grown exponentially, especially since the 1970s. Daily turnover on the foreign exchange markets exceeds $1.2 trillion, and billions of dollars of financial assets are traded globally, particularly through derivative products (BIS, 2001). Few countries are now insulated from the dynamics of global financial markets, although their relationship to these markets differs markedly between North and South (see below). International banking, bond issues and equities trading have risen from negligible levels to historically significant levels measured in relation to world and national output, respectively. The level of cross-border transactions is unprecedented. Where once international financial markets operated to fund wars, trade and long-term investment, a substantial proportion of their activity is now 'speculative'; and this constitutes a significant development. To say that it is speculative, however, is not to say that it is the same as gambling. Many financial institutions and multinational corporations are drawn into the foreign exchange markets in order to hedge against changes in currency valuations and protect their long-term trading position; and financial resources flow across borders, of course, in search of productive investments and future trade opportunities (cf. Strange, 1996). Nonetheless, the annual turnover of foreign exchange markets now stands at an extraordinary figure in excess of sixty-two times the value of world trade. (It was thirteen times world trade in 1979.)

Current levels of cross-border financial flows can induce rapid and volatile movements in the prices of assets, which can increase risks to financial institutions, as the 1998 crisis at the Long Term Capital Management hedge fund and the recent (2001–2) fluctuations in global stock prices (especially in the high-tech sector) both illustrate. In addition, they can reinforce the tendency of financial markets to short-termism, bubbles and overshooting, accentuate the propensity of funds to rapid 'reversibility' faced with uncertainty and risk (especially when trouble in one market leads foreign investors to exit others), and can weaken the prospects of stable, long-term capital flows to the developing world (see Griffith-Jones, 2002; Griffith-Jones and Spratt, 2002). Fluctuations in markets for risk and capital can 'destabilize markets for goods and services, and divert resources from productive activities to unproductive trading in existing assets' (Kay, 2003b, p. 46). As one commentator put it, 'the claims of enormous benefits from free capital mobility are not persuasive. Substantial gains have been asserted, not demonstrated' (Bhagwati, 1998, p. 7).

While free capital markets and the cross-border flows of financial resources do not shape the terms of national economic policy in a straightforward way, they can radically alter the costs of particular policy options and, crucially, policy-makers' perceptions of costs and risks (see Held et al., 1999, ch. 4). Perhaps a key difficulty for policy-makers in these new circumstances is the uncertainty surrounding market responses. There has been a growth of perceived risk in this regard because markets are more liquid than ever before and are an enhanced source of instability. Accordingly, the costs and benefits of pursuing certain policies become fuzzier, and this encourages political caution and 'adaptive policies' – economic and social policies which seek to anticipate market responses.

The 1997–8 East Asian crisis illustrated clearly the changing nature and impact of global financial markets. While the relationship between global financial integration and financial crises is complex, the financial disruption triggered by the collapse of the Thai baht demonstrated new levels of economic interconnectedness (see Bordo et al., 2001; CEPR, 2002, pp. 43–52). The Asian 'tiger' economies had benefited in the 1990s from the rapid increase of financial flows to developing countries and were widely held as models of development for these nations. But the heavy flows of short-term capital were quickly reversed, causing currencies to fall dramatically and far in excess of any real economic imbalances. The effects were disastrous for many East Asian countries. For example, Indonesia's GDP fell in 1998 by 15 per cent, plunging tens of millions of people into poverty and reversing years of successful poverty reduction efforts. In Thailand GDP fell by 8 per cent, causing unemployment to rise and real incomes to decline (Griffith-Jones and Spratt, 2000). The effects of the crisis were experienced worldwide. The inability of the international financial regime (the IMF, Bank for International Settlements (BIS), etc.) to manage the turmoil quickly and effectively created a wide-ranging debate on financial institutional architecture. The latter led to institutional innovations like the Financial Stability Forum and the G20, both convened in 1999 to enhance financial stability and to advance international financial reform. Another important development arose in the 1990s from the recurrent exchange rate crises which became a dominant feature of the global financial system. Between 1990 and 1999 the percentage of countries operating floating exchange rate regimes increased from 21 per cent to 41 per cent (*Financial Times*, 8 Jan. 2002, p. 10). In the context of the growing scale and intensity of global capital flows, the choice that countries faced became increasingly one between (managed) floating rates and monetary union – illustrated by the launch of the euro and discussion of dollarization in parts of Latin America.

It is still too early to be one hundred per cent sure about the full impact of 9/11 on the world economy, but it does seem as if recent global economic trends are broadly unaltered. Since 9/11 the trends towards economic globalization – greater international production, higher trade flows and more integrated product and financial markets – have continued with two important qualifications.[1] The first of these concerns the US. The US has been a major source and recipient of global flows and a major driver of the processes of economic globalization, including greater liberalization and increased market openness. However, 9/11, corporate scandals and the bursting of the dotcom bubble have combined to end the boom of the 1990s and to slow down the development of global economic flows. The second qualification concerns developing and transition countries: global flows to many of these have recently been badly hit by financial crises in Mexico, East Asia, Russia and elsewhere. The integration of developing and transition countries into the world economy is highly volatile and uneven.

Yet global trends in trade have largely continued unabated. The year 2000 recorded the highest levels of trade growth since 1990 and the ratio of world trade to GDP reached 29 per cent. During the 1990s the trade growth of less developed countries more than doubled and stood at more than twice world trade growth. While 2001–2 saw a marked decline in trade growth in the OECD countries and, particularly, in Africa, East Asia and Eastern Europe maintained their trade growth. Overall, the share of developing countries in world trade continued to rise, even though exports from developing economies are still concentrated in a small number of countries and primary goods exporters continue to be marginalized in world economic developments.

After consistently growing faster than trade in recent years, financial flows have been slowing down. Since the 1997 East Asian crisis there has been a decline of financial flows to developing countries; portfolio flows to emerging markets fell after 1997 and, in net terms, banking flows to these countries have been negative. However, the major source of private capital flows to developing and transition economies after 1997 has been FDI. Although there has been continuous growth in FDI flows since 1991, these did fall in 2001 in response to the slowing of US economic activity and 9/11. However, the decline has been more marked in flows to developed countries (down 59 per cent) than to developing

[1] I should like to thank Jonathan Perraton for raising these points with me.

countries (down only 14 per cent) and to transition economies (where inflows have actually grown slightly). These figures illustrate the growing global integration of leading LDCs (less developed countries), reflecting the perception of increasing investment opportunities in these countries. It is perhaps surprising that the impact of the US economic slow-down and 9/11 on economic globalization has not been more significant.

It is easy to misrepresent the political significance of the globalization of economic activity. There are those who argue that social and economic processes operate predominantly at the global level, that national political communities are immersed in a sea of global economic flows, and that states are increasingly decision-takers in this context (see, for example, Ohmae, 1990; Gray, 1998). For many neoliberal thinkers, these trends are a welcome development; a world market order based on the principles of free trade and minimum regulation is the guarantee of liberty, efficiency and limited government (see Hayek, 1960, pp. 405–6). By contrast, however, there are those who are more reserved about the extent and benefits of the globalization of economic activity. They point out, for instance, that for all the expansion in global flows of trade and investment, the majority of economic activity still occurs on a more restricted spatial scale – in national economies and in the OECD countries – and that national and international economic management remain feasible (see Hirst and Thompson, 1999; cf. Perraton et al., 1997).

But neither the claims of the global enthusiasts nor those of their critics can be accepted straightforwardly, for both misstate much of what is significant for politics about contemporary economic globalization. Many states in the developed world continue to be immensely powerful, and enjoy access to a formidable range of resources, infrastructural capacities and technologies of regulation and coordination. The continuing lobbying of states and IGOs (for example, the WTO) by MNCs confirms the enduring importance of states and interstate organizations to the mediation and regulation of global economic activity. Yet it would be wrong to argue that economic globalization is a mere illusion, or an ideological veil that allows politicians to disguise the causes of poor performance and policy failure. Among the significant points to stress is the tangible growth in the enmeshment of national economies in global economic transactions – for nearly all countries a growing proportion of national economic activity involves economic exchange with an increasing number of countries. It is this broad increase in the extent, intensity and velocity of economic interconnectedness that has altered the relation between political and economic power. One shift has been especially noteworthy: the historic expansion of exit options in financial markets relative to national capital controls, national banking regulations and national investment strategies, and the sheer volume of privately held capital relative to national reserves. Exit options for corporations making direct investments have also expanded. As a result, the balance of power has, in principle, shifted in favour of capital, *vis-à-vis* both national governments and national labour movements (Goldblatt et al., 1997, p. 281). This does not mean that all business is 'footloose'; rather, it is the fact that businesses can potentially up and move (and a heightened awareness of this by many politicians) that is relevant.

How have government resources and expenditure patterns been affected by these economic transformations? The research and scholarly literature is by no means agreed on the matter. On the one hand, there are those who argue that because of the relative increase in capital mobility and enhanced global market integration, governments are induced to pursue greater fiscal austerity, greater labour market flexibility, a reduction of welfare costs and benefits, and a minimization of regulatory and tax burdens on business. Those who take this position tend to argue that the greater openness of economies is associated with lower rates of capital taxation; that there is a downward pressure on tax rates on all movable factors (on capital, on receipts from investment income and on the highest earners); and that the incidence of tax (where the cost of tax actually falls) tends to be increasingly on labour and other less mobile factors (see Rodrik, 1997; Ganghof, 2000; Hertz, 2001). In addition, a recent comprehensive analysis has found that year-to-year increases in total trade and international financial openness have been associated over the last three decades with less government spending (Garrett, 2000; Garrett and Mitchell, 2001). And another study has shown that in countries where trade union power, centralized collective bargaining and electorally inclusive institutions (proportional representation) are weak, and where public authority is dispersed or fragmented, international capital mobility is linked with pressure to reduce the public economy, social transfers and public consumption (see Swank, 2001).

While the extent of these changes remains small, with patterns varying among countries (and foreign direct investment is not associated with such negative effects), these tendencies have led some to argue that they signal 'a gradual shift in the political economy of industrialized countries, away from an earlier "compensatory" approach to managing the effects of increased openness, towards more of a "competitiveness" model' (Ruggie, 2003, p. 99). In short, embedded liberalism and social democracy have gradually given way to a set of economic and social policies focused on market adaptation and flexibility (see Swank, 2002b).

Against these claims, there are those who take a much more cautious view of the research findings to date. They suggest that there is no firm evidence that economic globalization has led to a decline in taxes on company earnings, or in labour and welfare standards. They find no good reason for thinking that government regulatory capacity is diminishing in relation to corporations and markets. Those in this camp recognize that 'some corporations do indeed evade government taxation and regulatory control, and extreme vigilance is certainly required' (CEPR, 2002, p. 104). But they argue that there is no overall evidence that government regulation of business is weakening. In addition, these analysts recognize that while it is true that the share of business taxes has fallen in a number of countries, 'there is only weak evidence that greater mobility of capital has resulted in systematic changes in the tax structure, and no evidence at all that it has resulted in a fall in overall revenues compared to earlier periods. If anything, the continuing upward drift in the share of taxes in GDP suggests a strong underlying tendency for government to grow' (CEPR, 2002, p. 7; see also Garrett and Mitchell, 2001). The evidence in table 2 is relevant in this regard. This table compares, for a range of OECD countries, both overall tax burdens between 1970 and 1998, and the shares of profits and other taxes in the overall tax revenue

Table 2 Tax levels and composition for various OECD countries, 1970, 1980 and 1997–1998

	Tax burden (% GDP)			*of which: Profit taxes*		*Employment taxes*		*Sales/ VAT*	
	1970	*1980*	*1998*	*1980*	*1997*	*1980*	*1997*	*1980*	*1997*
Canada	31.3	30.3	43.4	11.6	10.3	44.6	51.4	32.6	24.4
France	37.4	43.6	50.9	5.1	5.8	55.6	54.6	30.4	27.8
Germany	37.2	43.9	44.8	5.5	4.0	64.2	65.5	27.1	27.7
Italy	27.9	32.4	46.4	7.8	9.5	61.1	58.8	26.5	25.9
Japan	19.7	25.6	30.8	21.8	15.0	53.4	57.4	16.3	16.5
UK	35.6	35.3	40.6	8.3	12.1	46.6	42.0	29.2	35.0
USA	28.9	30.0	34.4	10.8	9.4	65.3	63.2	16.6	16.7

Employment taxes include individual income taxes and social security contributions.
Source: CEPR, 2002, p. 84; derived from *Statistical Abstract of the United States: Comparative International Statistics*, various years

between 1980 and 1997. Although the 1980s were widely regarded as a tax-cutting period, the table discloses that

> in the main in industrialized countries the tax burden continued to rise steadily, as it had in the 1970s . . . . The share of business taxes in that burden fell in some countries, while taxes on employment rose in Canada, Germany and Japan. Overall there is only weak evidence that greater mobility of capital has resulted in systematic changes in the tax structure, and none that it has resulted in a fall in overall revenues. (CEPR, 2002, p. 85)

Accordingly, in this second, more sceptical view, global economic integration does not hinder the capacity of governments to regulate their economies and adjust their own policies to their particular economic conditions; moreover, it probably enhances this capacity in the long run because of benefits that derive overall from better economic performance. Again, it is stressed, the evidence is not yet strong in many areas and many of the measured effects must be regarded as tentative. But the main conclusion is that economic difficulties and domestic problems are often due to insufficient globalization rather than too much of it.

The debate about economic globalization and its policy impact needs to be broken down further if more analytical progress on these issues is to be made; for economic globalization embraces a diverse set of processes with uneven effects across the world's regions and countries. There are marked asymmetries of impact. These asymmetries often result in very little room to shape and manoeuvre policy in the poorest countries. This important finding arises from looking at patterns of globalization, stratification and inequality.