THE DRIVERS OF GLOBALIZATION

Presentation to a Regional Defence Seminar
hosted by the Australian Department of Defence

Cypress Lakes Resort, New South Wales

Monday 20 November 2000

Saul Eslake

Chief Economist
Australia & New Zealand Banking Group Ltd

What is 'globalization'?

'Globalization' has come to mean many things. To many people, globalization is synonymous with – as Thomas Friedman put it in *The Lexus and the Olive Tree* – "the spread of free-market capitalism to virtually every country in the world"[1].

Indeed, it is for precisely that reason that many of the opponents and critics of globalization take the view which they do. Many of them associate globalization not only with 'free-market capitalism', but also with other things to which they are remorselessly and sometimes violently opposed, such as environmental degradation, child labour, genetically modified foods and the spread of what they regard as 'American culture'. They see globalization as a sinister force, imposed on unwitting or unwilling governments and citizens by a combination of corporate and financial elites bent on subverting democracy, avoiding taxes, reducing wages and oppressing the poor in as many countries as possible.

Globalization is, in my opinion, none of these things, and is responsible for none of these outcomes. 'Free-market capitalism' has not spread to every corner of the world[2]. Globalization's more enthusiastic proponents, of whom Friedman is one, do their cause no good at all by promoting such simplistic or triumphal notions of what it entails.

In my view, globalization is not an ideology, or a set of outcomes, but a *process*. It is, as the *Penguin Dictionary of Economics* defines it, "the geographical dispersion of industrial and services activities (for example research and development, sourcing of inputs, production and distribution) and the cross-border networking of companies (for example through joint ventures and the sharing of assets)"[3].

Or it is, in the words of the International Monetary Fund, "the rapid integration of economies worldwide through trade, financial flows, technology spillovers, information networks, and cross-cultural currents"[4].

Alternatively, globalization is, instead, simply the logical extension of the tendency towards increasing specialization and trade which has been going on almost since mankind first walked on the surface of the earth.

At the dawn of human civilization, small groups of individuals – families and tribes – were almost entirely self-sufficient. They grew, gathered or hunted their own food; they made their own clothes; they erected their own housing; they provided their own transport; they created their own entertainments; they enforced their own laws and customs; and they defended themselves against marauders and predators.

As human beings learned more about themselves and their environment, they discovered that some people were able to do some things better (that is to say, to higher quality or at lower cost) than others.

---

[1] Friedman, Thomas (1999), *The Lexus and the Olive Tree* (Harper Collins, London), p. 8.

[2] See, for example, Henderson, David (2000), *Anti-Liberalism 2000*, Institute of Economic Affairs Wincott Lecture, October; available at http://www.iea.org.uk/pdf/wincott.pdf.

[3] Bannock, G., RE Baxter and E Davis (1998), *The Penguin Dictionary of Economics*, 6th edition (Penguin Books, London), pp. 176-77.

[4] International Monetary Fund (1997), *World Economic Outlook* (Washington DC), May, p. 3.

They learned this because they found that they possessed, or could acquire, special skills; because they stumbled across previously unknown or unharnessed resources; and because they invented new machines and devised new processes for producing known goods and services more effectively, or new ones entirely. These discoveries, moreover, tended to be self-reinforcing.

Thus, some people continued as farmers; others became builders; still others, butchers, bakers and candle-stick makers; in more modern times physicists, currency-traders, computer programmers and, so as better to understand these processes, economists. And in order to survive – so that the farmer had clothes to wear, the builder had food to eat, the tailor had some place to live – individuals learned to trade with one another.

Adam Smith may not have coined the phrases 'specialization' and 'division of labour' to describe this particular aspect of human evolution until 1774, but it had been going on for a long time before he did.

In much the same way, humans discovered that some things could be done more effectively, at lower cost, or both, acting in groups rather than individually. From such discoveries (and, it must be acknowledged, from the periodic exercise of brute force) came concepts of nationhood.

And what has been true for individuals throughout human history has, by and large, also been the case for nations.

That is, nations also have different endowments of human talents and natural resources; those different endowments have been shaped in different ways by their different historical experiences. And the peoples of many (though not all) nations have discovered – either through their own experiences, both positive and negative, or through observing those of others – that much can be gained (in terms of material living standards, opportunities for leisure, and other pursuits) by seeking to exchange the goods and services in whose production they have particular advantages for those in whose production the people of other nations are similarly advantaged.

Thus, nations have traded with one another – or, more accurately, the people of nations have traded with the people of other nations – since time immemorial.

The extent and pattern of trade among nations has not, of course, been determined simply by differences in endowments of natural or human resources. Throughout human history there have been barriers to exchanges of goods and services for one another, for cash or for credit, both within nations and among them.

These barriers have been of three types: physical – for example, high mountains, harsh deserts and wide oceans; economic – for example, when the cost of transporting goods from one place to another exceeds the difference between the cost of producing them in each; and political – such as laws which prohibit outright trade in particular goods and services, or with particular countries, or which impose such high taxes on cross-border transactions as to render some or all of them uneconomic.

I would thus describe 'globalization' as the process which barriers to the exchange of goods and services among far-flung nations are being either dismantled or overcome.

Globalization then and now

Viewed in that light, although the word itself may be of fairly recent provenance, 'globalization' as a process is far from being a recent development.

Let me read to you an extended passage from a book by an economist whose name will be familiar to nearly all of you:

> "The inhabitant of London could order by [a relatively new technology] … the various products of the whole earth, in such quantity as he might see fit, and reasonably expect their early delivery on his doorstep; he could at the same moment and by the same means adventure his wealth in the natural resources and new enterprises of any quarter of the world, and share, without exertion or even trouble, in their prospective fruits and adventures … He could secure, forthwith, if he wished it, cheap and comfortable means of transit to any country or climate without passport or other formality … Most important of all, he regarded this state of affairs as normal, certain and permanent, except in the direction of further improvement … The internationalization of the ordinary course of social and economic life … was nearly complete in practice."

You could be forgiven for thinking that this was an excerpt from a recent book describing the dismantling of barriers to trade and investment, the spread of the internet and business-to-consumer e-commerce, and a comfortable consensus about the desirability and inevitability of globalization. In fact, the 'new technology' referred to in this passage was the telephone; and the author was John Maynard Keynes, writing nearly eighty-one years ago about 'that age which was came to an end in 1914' in the book that first established his reputation, *The Economic Consequences of the Peace*[5].

Or consider this:

> "In place of the old wants, satisfied by the production of the country, we find new wants, requiring for their satisfaction the products of distant land and climes. In the place of the old local and national seclusion and self-sufficiency, we have intercourse in every direction, universal interdependence of nations."

That sounds, perhaps, like the US isolationist and failed Presidential candidate Patrick Buchanan. In fact, it's Marx and Engels, in *The Communist Manifesto*, written in 1848[6].

Many aspects of what we today refer to as 'globalization' proceeded at least as rapidly in the four decades before the outbreak of World War I as they have over the past two decades.

---

[5] As reprinted in *The Collected Writings of John Maynard Keynes*, Volume II (Macmillan, Cambridge, 1971), pp. 6-7.

[6] Marx, Karl and Engels, Friedrich (1848), *The Communist Manifesto* (Penguin Classics, London, 1985), p. 84.

The increase in world trade as a share of world GDP was proportionately greater between 1870 and 1913 than it has been since 1975[7]. Net capital outflows from the United Kingdom – then the largest source of international investment – averaged 4.6% of British GDP between 1870 and 1913 – more than for any large economy today, including Japan[8].

This was also a period of rapid technological change – in which new means of transport (think of the steamship and refrigeration) were coming into vogue; new means of communication (the telegraph and the telephone) were spreading; and the costs of both were falling.

Indeed, Kevin O'Rourke and Jeffrey Williamson, in their detailed study of this period published last year, conclude that it was falling transport costs, rather than trade liberalization, which was responsible for the dramatic expansion of trade during this period[9].

Like the past decade, this was also a period of considerable financial instability, especially in emerging markets. By one count there were 32 separate currency crises in 16 different countries, including Australia – then an 'emerging market' – between 1882 and 1913[10]. In most cases, the economies affected by these crises bounced back surprisingly quickly – as most of the Asian countries have done from the 1997-98 crisis.

But in others (and Australia's experience in the 1890s is a case in point), the effects were severe – highlighting the need, which still exists, for effective supervision of financial institutions by national authorities, and the importance of devising more effective arrangements for governing international capital flows, and in particular for preventing if possible, and where not, better managing the consequences of, major upheavals in international financial markets.

It was also a period in which erroneous conclusions were drawn about the implications of economic interdependence. Just as Thomas Friedman argues – rather fatuously, in my opinion – that "no two countries that both had McDonald's had fought a war against each other since each got its McDonald's"[11], so too was it argued before 1914 that the "elaborate interdependence, not only in the economic sense, but in every sense" among the Powers of that era guaranteed "the good behaviour of one state to another"[12].

And, just as we see today, it was a period in which 'globalization' prompted a political backlash.

---

[7] Maddison, Angus (1995), *Monitoring the World Economy 1820-1992* (OECD, Paris).

[8] Baldwin, Richard and Martin, Phillippe (1999), *Two Waves of Globalization: Superficial Similarities, Fundamental Differences*, NBER Research Working Paper 6904 (NBER, January).

[9] O'Rourke, Kevin, and Williamson, Jeffrey (1999), *Globalization and History* (MIT Press, Cambridge), pp. 29 and 35.

[10] Bordo, Michael, and Eichengreen, Barry (1999), 'Is Our Current International Economic Environment Unusually Crisis Prone?', in David Gruen and Luke Gower (eds.), *Capital Flows and the International Financial System* (Reserve Bank of Australia, Sydney, 1999), pp. 50-69.

[11] Friedman, *op. cit.*, p. 196.

[12] Angell, Norman (1913), *The Great Illusion*, (London), quoted in Niall Ferguson (1998), *The Pity of War* (Penguin Books, London), p. 21.

As O'Rourke and Williamson document, continental European governments began raising tariffs in the late 1870s and 1880s, when the impact of cheap grain from the Americas, Russia and Australia began to make itself felt in European markets. The United States raised tariffs as a revenue measure during the Civil War, and kept them high for a long time thereafter. Canada adopted an explicitly protectionist policy after 1878. Tariffs rose in Latin America from the 1870s onwards. In Australia, Victoria raised its maximum tariff from 10% in 1865 to 45% by 1893, and as the dominant colony was then able to impose its protectionist policies on the rest of Australia after Federation in 1901. Britain finally succumbed to the protectionist tide in the first decade of the twentieth century. The only part of the world where trade barriers did not increase significantly after the 1870s was Asia – and that was due to colonial policies or 'unequal treaties', rather than the decisions of sovereign rulers[13].

For all that, there are also some important differences between the globalization of the period before the First World War and that of today.

First, the composition of international trade is very different from a century ago. In 1913, primary commodities accounted for nearly two-thirds of international merchandise trade, and manufactured goods for just over one third. By the end of the 1990s, these proportions had been more than reversed, with manufactures now accounting for more than three-quarters of world trade in goods and primary commodities less than one quarter. And although it is only fairly recently for most countries that trade expressed as a share of GDP has exceeded its 1913 levels, trade in goods expressed as a share of total goods production is for most countries substantially higher than it was a century ago[14].

Similarly, trade in services is much more important than it was in the pre-1914 era.

Second, the nature of international capital flows is very different from what it was in the period before the First World War. In that era, foreign investment was overwhelmingly portfolio investment – that is, purchases of stocks and bonds – rather than, as is increasingly the case today, direct investment by companies in the establishment, expansion or acquisition of branches, subsidiaries and affiliates in other countries. And, at least in the case of British investment, it was fairly narrowly concentrated – about 70% of it went into infrastructure, especially railroads, and nearly all of the lending was to governments[15].

Moreover, most of the capital flowed to labour-scarce and resource-rich countries (as the US, Australia and Argentina then were) rather than to relatively poor and labour-abundant countries (as is often the case today).

Third, the globalization of the late nineteenth and early twentieth centuries involved massive movements of people, as well as goods and capital. Around 60 million Europeans migrated to the Americas, Australia, New Zealand and South Africa during the century after 1820.

---

[13] O'Rourke and Williamson, *op. cit.*, pp. 54, 95-96 and 114-117.

[14] Crafts, Nicholas (2000), *Globalization and Growth in the Twentieth Century*, Working Paper No. 00/44 (IMF, Washington DC, March), p. 26.

[15] Crafts, *op cit.*, p. 28; O'Rourke and Williamson, *op. cit.*, pp. 211-2.

These migrations had the effect of reducing inequality in some European countries and dramatically increasing it in the United States and other receiving countries[16]. As a result, 'New World' countries began closing their doors to immigration from the late 1880s onwards, and especially after the First World War. Some of this, especially in Australia, was racially motivated. And although immigration restrictions have been relaxed by these countries to some extent since the Second World War, the level of immigration remains substantially smaller than a century ago. Many more people would like to migrate to the United States, Australia and other 'rich' countries than the governments of those countries will permit to do so.

One of the reasons why it is now so common for companies to move operations from countries where labour is relatively expensive to countries where labour is relatively cheap is that rich country governments are far less willing to allow cheap labour to move from poor to rich countries than they were a century ago.

Fourth, the globalization of a century ago involved a significant amount of coercion, either through colonial expansion, as in Africa, the Indian sub-continent and South-East Asia, or through 'gunboat diplomacy' and 'unequal treaties' as in the case of Japan and China. Not surprisingly, this promoted a considerable degree of lasting resentment among the peoples at the receiving end of this form of globalization, and probably explains a good deal of the search for self-sufficiency among post-colonial nations in the decades immediately following the Second World War.

By contrast, the globalization of today has been very much facilitated by voluntary decisions of a majority of the world's governments to open their doors to international trade and investment.

Despite these differences, there remain important lessons to be drawn from the experience of the previous episode of globalization. Although globalization undoubtedly brings significant economic benefits to a large number of people, it can also bring increased inequality, both among and within nations. It can cause heightened political and financial instability. And, notwithstanding the frequency with which it is asserted that globalization is 'inevitable' and 'unstoppable', a key lesson of history is that it can not only be stopped, but thrown into reverse, if governments so choose.

Drivers of contemporary globalization

There are four separate but inter-dependent factors shaping the speed and extent of globalization in the contemporary era:

- first, *improvements in transport and communications technologies* which have the effects of increasing the range of, speed with and distance over which items – including information – can be transmitted from one place to another, and reducing the cost of such transmission;

- second, *changes in individual tastes and preferences* which have generally been in the direction of favouring greater choice and diversity in the range and origin of goods and services;

[16] O'Rourke and Williamson, *op. cit.*, pp.145-83.

- third, *changes in public policies* which have, for the most part, been in the direction of removing barriers to the movement of goods, services and capital across national borders; and
- fourth, *changes in the strategies of corporations* which have increasingly emphasized the pursuit of scale and of reductions in operating costs.

Technology

More than thirty years ago David Landes, Professor of History at Harvard University, in his study of technological change and industrial development in Western Europe since 1750, *The Unbound Prometheus*, observed that "technological change is not a smoothed, balanced process"[17]. More recently, US Federal Reserve Chairman Alan Greenspan has made much the same point, noting that "technological innovation … arguably comes in bunches as new discoveries feed on one another to push forward innovation until the effects of the initial stimulus finally peter out"[18].

Some of the technologies which have facilitated the rapid growth of international trade in goods are not especially new, but rather represent progressive extensions of previously known technologies to the point where they have lowered costs sufficiently to render feasible trade which was previously uneconomic.

Thus, the typical 1950 merchant steamer of 5-8,000 tons has given way to containerized cargo carriers displacing 100-150,000 tons, while dockside operations have been substantially mechanized and integrated with land transport networks[19].

It is difficult to imagine how world trade in automotive products could have risen by nearly two-thirds between 1990 and 1998 without such improvements in sea transport.

Similarly, without the rapid growth of air cargo services made possible by the introduction of wide-bodied jets, it would not have been possible for Israel to become a leading exporter of cut flowers to the United States, or for Australia to become a leading supplier of fresh tuna to Tokyo's sushi markets.

The last decade has however seen the rapid introduction and evolution of a range of new technologies, particularly in the transmission and processing of voice, text and data. In very simple terms, these new technologies have greatly expanded both the range of material which can be transmitted electronically from one point to another and the distance over which it can be transmitted; and they have drastically reduced the cost of transmission. Moreover, the number of people able to make use of these technologies has grown exponentially.

Though it is still far too early to make a definitive judgement, it seems increasingly plausible that the internet and the technologies associated with it represent a discontinuity similar, in at least some ways, to electricity or the telephone.

---

[17] Landes, David S. (1969), *The Unbound Prometheus* (Cambridge University Press), p.3.
[18] Greenspan, Alan (2000), "Global Economic Integration: Opportunities and Challenges", Remarks at a Symposium sponsored by the Federal Reserve Bank of Kansas City, August; http://www.bog.frb.fed.us/boarddocs/speeches/2000/20000825.html .
[19] Mussa, Michael S. (2000), "Factors Driving Global Integration", Paper presented to a Symposium sponsored by the Federal Reserve Bank of Kansas City, August; available at http://www.kc.frb.org/publicat/sympos/2000/s000draft.htm .

Indeed even *The Economist*, long a sceptic of much of the hype associated with the information technology revolution, now concedes that “the Internet may be different”[20].

The IMF’s Chief Economist, Michael Mussa, suggests that the most important effects of improvements in communications technologies have been on trade in services:

> “For a variety of services, modern communications technology makes it possible and cost efficient to separate production and use it in ways that were not previously feasible. Design of new computer chips can be done in Silicon Valley and implemented in production facilities in East Asia. Software can be written under contract in India or Ireland and e-mailed back to the United States. Doctors can diagnose patients using transmitted MRI images and other data. Financial services are a particularly important area where modern communications technology is helping to transform the arena for international trade in services.”[21]

However, these new technologies have affected trade flows in ways that go beyond cost reductions and efficiency gains. They are also changing the way people think about where they can buy and where they can sell. Consider this example provided by Peter Drucker:

> “A mid-sized company in America’s industrial mid-west, founded in the 1920s, used to have some 60% of the market in inexpensive dinnerware for fast-food eateries, school and office cafeterias, and hospitals within a hundred-mile radius of its factory. China is heavy and breaks easily, so cheap china is traditionally sold within a small area. Almost overnight, this company lost more than half its market. One of its customers, a hospital cafeteria where someone went surfing on the internet, discovered a European manufacturer that offered china of apparently better quality at a lower price and shipped cheaply by air. Within a few months the main customers in the area shifted to the European supplier. Few of them, it seems, realize – let alone care – that the stuff comes from Europe.”[22]

Experiences such as this have become, if not ubiquitous, then at least common-place. Drucker goes on to conclude:

> “In the mental geography of e-commerce, distance has been eliminated. There is only one economy and one market … The competition is not local any more – in fact, it knows no boundaries.”[23]

Tastes

A second key driver of the current experience of globalization – and one which is often overlooked by its critics – is the way in which people all over the world have acquired a generally increasing taste for the products and experiences of people in other parts of the world.

---

[20] *The Economist* (2000), 11 November, p. 22.
[21] *Ibid.,* pp. 16-17.
[22] Drucker, Peter (1999), “Beyond the Information Revolution”, *Atlantic Monthly* (October), p. 50.
[23] Drucker, *op. cit.,* p. 51.

Advances in transportation and communications – and reductions in their cost – have clearly played a role in this process, by making it possible for more people to experience more of more parts of the world, either personally through travel or vicariously via television, cinema, the internet and other media. For example, in 1978, 290 million people or about 6½% of the world's population took an international trip. By 1996, the number of international travellers had doubled, to over 10% of the world's population. By 2020, this figure is expected to have increased to over 20%.

Education has had a similar effect. Education increases people's appetite for variety and diversity. It enhances their ability to make comparisons and choices between alternatives. It reduces their tolerance for shoddy or needlessly expensive goods and services.

Almost inevitably, the search for alternatives leads people to look beyond the peripheries of their own nations – for products as basic as food and beverages or as complex as motor vehicles; for services ranging from films to accounting advice; and for different avenues for investment. In this sense, globalization is an extension of freedom: as John Micklethwait and Adrian Wooldridge note in their recent book about globalization, *A Future Perfect,* "globalization by its very nature … helps to hand the power to choose to the individual"[24].

Government policy

The third key driver of the contemporary wave of globalization, without which much of it would not have been possible, is changes in government policies. For the most part, these have been in the direction of reducing barriers to the movement of goods, services and capital (though generally not people) across national boundaries.

Of greatest importance has been the removal or reduction of government-created barriers to trade, such as tariffs and quotas.

For the first four decades after World War II, trade liberalization was largely confined to trade in manufactured goods among the industrial countries. Since the mid-1980s, however, a growing number of developing countries have also reduced barriers to merchandise trade, while industrialized and to a lesser extent developing countries have also taken steps to liberalize trade in services.

Although trade in agriculture and textiles remain significant exceptions to this general trend, Michael Mussa estimates that artificial barriers to international trade from government policy interventions have fallen by between 80 and 90% since World War II[25].

Governments have also increasingly sought to remove or reduce impediments to cross-border investment, and in many cases to facilitate or encourage it. For example, the most recent United Nations Conference on Trade and Development (UNCTAD) *World Investment Report* notes that:

[24] Micklethwait, John, and Wooldridge, Adrian (2000), *A Future Perfect* (Crown Business, New York), p. xxvi.
[25] Mussa, *op. cit.,* p. 18.

- countries made 1,035 changes in laws relating to foreign direct investment in the period 1991 to 1999, and of these 974, or 94%, were favourable to foreign investors; and

- the number of bilateral investment treaties between countries increased from fewer than 500 in 1990 to 1,982 at the end of 1999[26].

It is worth emphasizing that these have been the decisions of sovereign – and, increasingly, democratically-elected – governments, acting in accordance with what they perceive to be their nations' best interests.

Most of these countries have done so after experiencing for themselves the consequences of choosing different policies. For the industrialized economies, the conscious decision to bring down trade barriers was a direct response to the disastrous consequences of the protectionist policies which they pursued between the two World Wars.

Australia's own experience provides a salutary example of the learning process. Together with New Zealand, Australia consciously opted out of the successive rounds of trade liberalization in which the rest of the developed world engaged during the 1950s and 1960s. We did so largely because these 'trade rounds' did not include agricultural goods: in other words, much as some argue we should be doing today, we held back our 'bargaining chips', such as they were, in the hope that by so doing, others would eventually make more favourable 'concessions' to us.

Between 1950 and 1973, the share of exports in Australia's GDP rose by only 2 percentage points – less than half that for the world as a whole, and by the end of that period was no higher than it was in 1929. While many Australians look back on this period as a 'golden age', the Australian economy actually grew more slowly – stripping out the effect of our above-average rate of population growth – than that of the rest of the developed world. Our productivity growth performance during the 1950s and 1960s was below that of almost every other developed country except the United States[27].

It was during this so-called 'golden age' that most of Australia's long slide down the rankings of national living standards occurred. We slipped from 4th among a sample of 28 developed and developing nations in terms of per capita GDP in 1950 to 14th by 1975, and have remained in the mid-teens ever since. Using instead the somewhat broader UNDP Human Development Index, which includes measures of life expectancy, literacy and school enrolment as well as per capita income, Australia slipped from 2nd to 12th over this period[28].

---

[26] United Nations Conference on Trade and Development (2000), *World Investment Report 2000* (UN, New York & Geneva), p. 6.

[27] Commonwealth of Australia, *Report of the Committee of Economic Inquiry* (Sir James Vernon, Chairman), May 1965, Volume I, pp. 94-95; W.E. Norton, *The Deterioration in Economic Performance*, Reserve Bank of Australia Occasional Paper No. 9 (Sydney, 1982), p. 68.

[28] Author's calculations, based on Crafts (2000), op. cit., p. 7, and United Nations Development Program (2000), *Human Development Report 2000*, pp. 178-81.

This experience has provided a major imperative for the comprehensive program of program of economic liberalization and deregulation which Australia has followed since mid-1980s. And, over that period, Australia's relative ranking in terms of the UNDP's Human Development Index has risen from 11th in 1985 to 4th by 1998.

Similarly, for majority of developing and post-Communist countries, the decision to open their doors to cross-border trade and investment came after decades of consciously seeking self-sufficiency, with generally poor results, especially when contrasted with the experience of the small number of East Asian countries who pursued a very different course.

It is *precisely because* the governments of so many countries have observed for themselves the different consequences of opting out of, and choosing to be part of, globalization, that the process of globalization has become, indeed, global, over the past twenty or so years.

This is often overlooked by people in Western countries who, whilst often claiming (without any authority) to be speaking or acting on behalf of people in developing countries, are increasingly seeking to call a halt to, or reverse, the process of globalization.

The Prime Minister of India, Atal Behari Vajpayee, speaks – with all the authority that a fair and democratic election provides – for more of the world's poor than anyone else on this earth. This is what he says: "All of us should realize that globalization is an irreversible phenomenon. No country can keep away fully from it without hurting itself"[29].

In the 1970s a Brazilian sociologist, Fernando Henrique Cardoso was a leading proponent of self-sufficiency on the part of developing countries. But as the twice-elected President of Brazil, the world's fourth most populous developing country, he now says: "if Brazil is not prepared to be part of the global economy, it has no way of competing … It is not an imposition from the outside. It's a necessity for us"[30].

The outgoing President of Mexico, Ernesto Zedillo, who unlike some of his predecessors, was freely and fairly elected, says:

> "What is now clear from the historical evidence of the last century is that in every case where a poor nation has significantly overcome its poverty, this has been achieved while engaging in production for export markets and opening itself up to the influx of foreign goods, investment and technology; that is, by participating in globalization"[31].

Moreover, the views of elected leaders such as these are overwhelmingly supported by hard evidence. Let me cite just three comparatively recent examples.

---

[29] Quoted in *The Financial Times*, 3 August 2000.

[30] Quoted by Mark Moffett, 'Foreign Investors Help Brazil's Leader Tame its Raging Inflation', *The Wall Street Journal*, 15 December 1995, p. A-1.

[31] Remarks at the World Economic Forum, 28 January 2000.

A study of 150 countries by two leading US academic economists, Jeffrey Frankel and David Romer, concluded that increasing the trade share of GDP by 1 percentage point raises per capita income by between ½ and 2 per cent[32].

An examination of the experience of 126 countries over 40 years by two researchers at the World Bank shows that openness to foreign trade benefits the bottom one-fifth of the population as much as it does the population as a whole. Indeed, they argue that "anyone who cares about the poor should favour the growth-enhancing policies of good rule of law, fiscal discipline and openness to international trade"[33].

And a study published earlier this year by the World Trade Organization confirms that, although most trade reforms do create some losers, trade liberalization is generally a positive contributor to poverty alleviation[34].

Indeed, if integration into the global economy were not a 'good thing' for nations which achieve it, why would countries, acting collectively, resort to the imposition of 'sanctions' – that is, externally imposed restrictions on trade and investment – on errant or pariah states?

Some Western critics, and many developing country governments, make the quite legitimate point that, to date, many aspects of the globalization process have been skewed towards the interests of developed countries. These include the unwillingness of most advanced countries to contemplate any meaningful reductions in their barriers to imports of agricultural products and the 'back-loading' of the removal of restrictions on textile imports under the Multi-Fibre Agreement – by contrast with the much speedier dismantling of barriers to trade in the products of greater interest to developed countries, including information technology products and financial services.

Despite this, the response of most developing country governments is to call for 'fairer' globalization – not for less of it, as has become increasingly common among non-government organizations in Western countries.

It surely says something rather telling about the motives of many of those in Western countries who seek to halt or reverse the process of globalization that they would impose their preferences over those of democratically elected governments of developing countries (let alone their own), and at such cost to the living standards of the people of developing countries.

Corporate strategies

The final important factor in the globalization of the past decade has been the imperatives facing corporate entities. While this could be a topic in its own right, two aspects of it are especially important in the context of globalization:

---

[32] Frankel, Jeffrey, and Romer, David (1999), "Does Trade Cause Growth", *American Economic Review* (June), pp. 379-99.
[33] Dollar, David, and Kray, Aart (2000), *Growth Is Good for the Poor* (Washington, World Bank, March); http://www.worldbank.org/research .
[34] Winters, L. Alan (2000), "Trade and Poverty: Is There a Connection?", in Ben-David, Dan et al., *Special Studies 5: Trade, Income Disparity and Poverty* (World Trade Organization, Geneva), pp. 46-69.

- the successful pursuit of low and stable inflation by policy-makers; and
- the growing importance of institutional shareholders.

For roughly thirty years up to the mid-1980s, companies in most Western economies could be reasonably confident of being able to raise their prices each year, in order to recover increasing labour and materials costs, or to absorb any inefficiencies in their operations. Moreover, faced with any increase in foreign competition, they could often go to their governments and seek increases in tariffs or 'voluntary export restraint arrangements', or – if there were enough of their peers in a similar position – maybe a devaluation of their country's currency.

By the early 1980s, a majority of Western governments and central banks had come to the conclusion that their previous tolerance for persistent inflation was harming their economic performance, and resolved to seek low and stable inflation as a policy goal. As part of that resolve, Western governments became generally less receptive to calls for policy decisions contrary to the goal of low and stable inflation – such as the imposition of higher trade barriers, or depreciation of their currencies.

Although it was, for the most part, not until the second half of the 1980s (or later, in some countries) that Western governments gained 'credibility' for this shift in policy – that is, until businesses, individuals and financial market participants became convinced that governments actually meant what they said in this regard – during the past decade corporate managers have increasingly understood that they are operating in a low-inflation environment.

This understanding has been re-inforced by the emergence of new technologies, and of substantial amounts of excess capacity in many industries, which have provided an additional source of downward pressure on prices.

Over roughly the same period, corporate managements have also faced growing pressure for higher returns from shareholders, who are increasingly likely to be institutional investors such as pension or mutual funds facing competitive pressures of their own to deliver higher returns.

The pressure to achieve higher returns in circumstances where it is much more difficult to raise product prices – indeed, where in many cases product prices are under downward pressure – has led an increasing number of companies to look for ways to reduce costs.

In many respects, governments have found themselves under similar pressures – to deliver higher standards of public services to more people whilst at the same time reducing taxes, or at least not increasing them.

For both corporations and governments, the drive to lower costs has in turn spawned a variety of management strategies such as 'out-sourcing' non-core activities to outside specialists, striving for economies of scale by acquiring and consolidating the operations of other businesses producing similar or compatible products, and shifting activities to locations where the most important inputs (such as labour or energy) may be obtained on the most favourable terms.

For each of these strategies, reaching across national borders is a distinctly possible outcome.

Once a company (or a government) has decided to ‘outsource’ its payroll system, its customer enquiries facilities, or its procurement function, to another organization, it is quite possible that the organization which wins the contract to undertake this activity may be foreign-owned, or even located in another country.

Once a company begins to consider expanding through acquisition, the possibility that it will consider an acquisition in another country increases.

Once a company has made the decision to consider shifting the location of an office or plant, it is almost inevitable that a location in another country will be among the possibilities.

And once one company in a given industry in a particular country has made the decision to deal with foreign suppliers, to make a cross-border acquisition, or to relocate an operation in another country, then competitive pressures are likely to ensure that other companies consider similar strategies.

Improvements in technology, and the increasing willingness of governments to permit, or even encourage, cross-border investment and trade, have of course also contributed to this trend.

More recently, the increasing importance corporations are placing on ‘created assets’ – knowledge, skills, brands etc. – has provided another impetus for cross-border investment.

Thus, to an extent that was far less apparent during the pre-1914 phase of globalization, the contemporary experience of globalization has been shaped by the growth of multi-national corporations:

- there are now estimated to be nearly 49,000 transnational companies operating out of 15 developing countries, compared with just 7,000 at the end of the 1960s.

- the number of transnational companies operating world-wide is reported to be over 63,000; and they have nearly 690,000 affiliates operating in countries other than their own.

- total foreign direct investment (FDI) inflows have risen from around US$200bn in 1990 to $865bn in 1999. Unlike portfolio flows, FDI flows were almost entirely unaffected by the Asian financial crisis.

- the rapid growth in FDI has been largely due to rapid growth in cross-border mergers and acquisitions, the value of which increased from about $US150bn (about 0.6% of world GDP) in 1990 to $720bn (2.5% of world GDP) in 1999.

- the total stock of inward foreign direct investment has risen from about 9% of world GDP to more than 15% over the past decade[35].

[35] Figures are from UNCTAD, *op. cit.,* pp. 8-23.

There are two important implications of this proliferation of foreign direct investment for the structure of the world economy.

The first is that, to an ever-increasing extent, production processes are being *'sliced up'* so that, rather than being produced at a single location, more and more goods are being produced in a number of stages in a number of different locations, often in different countries.

The second is that an increasing proportion of world trade is *intra-firm* trade – that is, trade between different units of a single firm or, as is becoming increasingly common, between members of a strategic alliance of firms. As Paul Krugman has pointed out, "the value of trade involved in the global production of a final good may easily be several times the value added in all stages of production"[36].

Among other things, this 'slicing up' of production makes it increasingly difficult to determine where a 'product' actually comes from. That may in turn complicate the administration of bilateral free-trade agreements.

The interests of multi-nationals, like those of wholly indigenous organizations, do not always co-incide with the interests of the countries or communities within which they operate. They are motivated primarily by profit. For that reason, because they are usually large, and often simply because they are (in many instances) American, they have become ready targets for critics in Western countries who, it often seems, instinctively dislike the pursuit of profit, large organizations (other than those owned by governments) and anything American. Multi-nationals stand accused, in the eyes of these critics, of exploiting 'third world' labour, of despoiling the environment, and of abrogating the sovereignty of national governments.

This is despite the facts that multi-nationals generally pay higher wages to their employees in developing countries than indigenous firms do; that the most egregious examples of environmental despoilation in developing countries have been caused by state-owned entities, as in the former Soviet bloc or Mao's China; that, at least for developed countries, tax revenues have in recent years represented a higher percentage of GDP than ever before recorded[37]; and that many of these critics are themselves fervent advocates of over-riding the sovereignty of developing country governments when it comes to issues of labour standards, the environment or human rights.

But, as we have already seen, few of these critics are willing to let the facts – or any sense of consistency – interfere with a good story, or prevent a good demonstration.

It bears repeating that all of these factors driving the contemporary experience of globalization – technological change, changing individual tastes and preferences, changing public policies, and corporate strategies – are interdependent. The effect of each on the pace at which economies are integrating is greater than would have occurred had one or more of the others not also been a factor.

---

[36] Krugman, Paul (1995), "Growing World Trade: Causes and Consequences", *Brookings Papers on Economic Activity*, I, p. 334.
[37] OECD (2000), *Revenue Statistics of Member Countries*, as reported in *The Financial Times*, 3 November.

Thus, for example, while technology makes it possible to for a motor vehicle manufacturer to send complex design instructions by e-mail from Nagoya or Detroit to Malaysia or Thailand so that components can be manufactured there, and then sent for further processing in Mexico or Korea, it wouldn't happen if the governments of Malaysia and Thailand weren't willing to allow foreign-owned firms to establish factories within their borders, and repatriate their profits back to their headquarters; it wouldn't happen if the governments of the US and Japan imposed restrictions on imports of those products back into their countries (that's why it doesn't happen to nearly the same extent with agricultural products); and it wouldn't happen if consumers in the US and Japan had strong preferences for entirely locally-manufactured products.

Globalization and its critics

One of the most profound consequences of contemporary globalization has been that businesses generally face much more intense competition than ever before. Globalization, combined with technological advantage, have neutralized the advantages of incumbency and local dominance; it has undermined the importance of integration, and made firms vulnerable to 'cherry-picking' of their most profitable activities; and it has exposed them to much greater scrutiny from financial markets.

And since businesses pay taxes and employ people, globalization has also exposed governments, communities and individuals to greater competition. Governments find themselves in a form of competition with other governments to attract or to retain investment and jobs within their jurisdictions. And workers increasingly see themselves as being in competition, not just with the workers at the rival firm on the other side of town, but with workers in other countries.

Competition is, overwhelmingly, a positive force for economic and social progress. But it is also almost by definition discomforting, unsettling and, on occasion, disruptive. Because individuals are not equal in their endowments, however much we might wish to the contrary, individuals differ in their capacity to cope with competition, and the outcomes resulting from competition may often seem in some way 'unfair'.

Thus, Alan Greenspan is almost certainly right when he says that "it is the degree of unbridled fierce competition within and among our economies today – not free trade or globalization as such – that is the source of the unease that has manifested itself, and was on display in Seattle [in November last year]"[38].

From this perspective, the critics of globalization can be separated, at least notionally, into three groups: those who are opposed to competition on ideological grounds; those who perceive their commercial or financial interests to be threatened by the greater competition which globalization has fostered; and those who see the results of that competition as being, by their lights, unfair.

[38] Greenspan, Alan (2000), "Technology and the Economy", Speech to the Economic Club of New York, 13 January. Available at http://www.bog.frb.fed.us/boarddocs/speeches/2000/200001132.htm

There is obviously a considerable degree of overlap among these three categories. One illustration of the extent of this overlap is provided by the intriguing case of Roger Milliken[39].

Roger Milliken is a billionaire textile magnate from Greenville, South Carolina. He is an unabashed right-winger. He once banned Xerox copiers from his offices because Xerox sponsored a documentary about civil rights. He has long been a generous patron of right-wing causes in the United States, such as the racist John Birch Society. He was instrumental in convincing South Carolina Senator Strom Thurmond to switch from the Democrats to the Republicans (and at 97, he's still there); and in having Barry Goldwater nominated as the Republican candidate for President in 1964. He was one of the first financial backers of former Republican Speaker Newt Gingrich.

Yet as a textile magnate, Roger Milliken is also one of the foremost protectionists in the United States. In particular, he has become a virulent opponent of the World Trade Organization and of 'globalization' in general. Like most right-wing extremists, he sees himself as the victim of a sinister conspiracy: in this case, to 'hand over' the American textiles market to developing nations in exchange for developing nations agreeing to protect the intellectual property of the pharmaceutical, software and entertainment industries[40].

As a result, Milliken has become a generous financier of anti-globalization advocates. He was one of the initial financial backers of the Economic Strategy Institute, a leading exponent of what came to be known as 'Japan-bashing' in the early 1990s. He is the most important contributor to the US Business and Industrial Council, a protectionist business lobby in Washington. He has given more than US$2 million to Pat Buchanan.

And it turns out that Milliken has also been financing the anti-globalization activities of organizations such as Public Citizen, headed by Lori Wallach, a close associate of Ralph Nader. Indeed the *New Republic* magazine reports that of "the anti-globalization eruptions of the 1990s … Milliken has been a major player behind each one".

There are two other profound ironies in Roger Milliken's active financial support of anti-globalization protests. The first is that he made his fortune by being the first major American textile manufacturer to use foreign-made equipment in his mills. (His much larger competitor at the time, the Draper Corporation, ended up being taken over by an Indonesian conglomerate). His subsequent purchases of textile manufacturing equipment from Switzerland and Germany have been so large that his suppliers established a full-time presence in South Carolina to service their equipment. And his home town of Greenville now has the highest level of foreign investment per capita in the United States.

The second irony is that the American textile industry which he seeks to protect, in part by funding groups which protest about the supposed exploitation of workers in developing economies, is itself one of the most egregious exploiters of poorly organized labour in the United States – as any visitor to the Los Angeles garment district could attest.

---

[39] The following draws heavily on Krugman, Paul (1997), "Who's Buying Whom?", *Slate*, 25 September; and Ryan, Lizza (2000), "Silent Partner", *The New Republic*, 10 January.

[40] *Textile World*, December 1999 (http://www.textileworld.com/magazine/9912/milliken.html).

Indeed Milliken fought a 25-year battle against a court order to give a group of his employees whom he'd fired after they voted to form a union in 1956 $5 million in back pay; and 144 of them died before he eventually complied.

Roger Milliken thus personifies the more general assertion made by the *Financial Times'* economics correspondent Martin Wolf that many of globalization's critics are "cranks, bullies and hypocrites"[41].

If those who sought to disrupt the meetings of the World Trade Organization in Seattle last November, the IMF and the World Bank in Washington in April and in Prague in September, and the World Economic Forum in Melbourne in September, were really motivated by concern for the poor of the developing world, they would instead have been protesting outside the embassies of the United States, the European Union and Japan, demanding that those countries remove their barriers against developing country exports – as the elected leaders of the developing countries themselves demand.

That is not to say that all of the critics of globalization are in the pay of industrialists who benefit from rich-country trade barriers, or that many of them are not sincere in their beliefs. Nor is to say that all of their criticisms are wrong. While globalization has improved the living standards of millions of people in developing countries, it is true that the benefits have accrued disproportionately to rich countries. And it is also true that, within rich countries themselves, globalization has created losers as well as winners, and that the winners have been disproportionately among those who are already comparatively well off.

There is also considerable truth in the charge that not enough has been done to ensure that private sector cross-border investors bear an appropriate share of the burden of resolving financial crises that are, in part, the result of their own investment decisions.

Governments, businesses and multi-lateral organizations need to respond to these concerns, not least because history clearly shows that governments can put the brakes on globalization if they think it is in their political interests to do so. The history also clearly shows that do so would be tragically contrary to the economic interests of their citizens. But history is, regrettably, littered with examples of governments taking political decisions which make their people worse off.

As Alan Greenspan said only last week,

> "In many important respects, the past half century has represented an uneven struggle to repair the close linkages among national economies that existed before the First World War. The hostilities bred of war, the substantial disruptions to established trading patterns associated with that conflict, and the subsequent poor economic performance over the next few decades triggered the erection of trade barriers around the world that have taken even longer to dismantle. To repeat that error would be a tragic act of foolishness and waste"[42].

---

[41] Wolf, Martin (1999), "In Defence of Global Capitalism", *Financial Times*, 8 December.

[42] Greenspan, Alan (2000), "Globalization", Remarks at the Banco de Mexico 75th Anniversary Conference, 14 November (http://www.bog.frb.fed.us/boarddocs/speeches/2000/200001114.htm.)