1. The future of globalisation*

Paul Hirst and Grahame Thompson

Before we consider the future of 'globalisation' we must define its nature and outline its past. This is a complex and contested concept. If we take growing international interconnectedness – increasing flows of trade, investment and communications between nations – to be what most people mean by the term, then 'globalisation' has been happening for the last 50 years. Moreover, new technologies – long distance jets, satellites, IT, fibre optic cables – have made international travel, media and financial exchanges far easier, enabling dramatic increases in traffic volumes. The key questions are threefold. First, are these economic and social processes linking nations since 1945 unprecedented? Second, are these processes developing at the expense of state and national governance, that is, are national economies dissolving into a global marketplace and relations between states becoming secondary to more complex interactions between a variety of economic, social and political agencies? Third, is international economic interconnectedness set to increase or decrease?

THE HISTORY OF GLOBALISATION

Naturally these questions are almost impossible to answer in the scale of a short chapter. We are sceptical about many of the claims in the literature, in particular that national economies are dissolving. We refer readers to what we judge to be the best presentations of both sides of the debate (Held et al., 1999; Hirst and Thompson, 1999).

Here we shall focus on two primary issues: the future of international governance and the likely limits to economic globalisation. The first thing to note is that although we have had a long period of growing international interconnectedness there is no reason to assume that such processes will continue indefinitely or that they have an inherent dynamic that prevails over all countervailing forces. Globalisation has a history. The 50 years between 1950–2000 are not remarkable when compared with the period 1850–1914 – in that period flows of merchandise trade, capital investment and labour migration were all comparable to or greater than those of today (Hirst and Thompson, 1999, ch. 2). Technological change in the form of international telegraph cables unified markets and led to price and interest rate convergence of a kind that has never been equalled since. Financial integration was far greater, and levels of capital export from the major lender countries unprecedented. Economic convergence in prices and wages across the Atlantic was largely achieved by vast flows of surplus labour from Europe to the New World (O'Rourke and Williamson, 1999). This process is not operating on the same scale today. Migration flows are relatively smaller and the pressure in all developed countries is to further restrict migration. If the key engine of international convergence in the first great phase of globalisation no longer operates, that is because it was one of the first targets of an antiglobalisation public policy backlash. Most major recipient countries followed

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

the lead of the USA in the early twentieth century in restricting migration. Globalisation processes were under challenge well before 1914. Many countries introduced protective tariffs, seeking to protect farmers against the competition of American wheat or to shelter emerging manufacturing sectors (James, 2001).

Thus 1914 shattered a world order that was slowly unravelling under the pressure of competing national policies. In the inter-war period attempts to recreate the institutions of the *belle époque,* including the Gold Standard, failed. The result was a period of intense antagonistic competition to monopolise markets and raw materials. The experience of the 1930s confirmed that if free trade has its problems then generalised competitive protectionism is a disaster. This should be borne in mind when 'anti-globalisers' criticise the WTO and favour the 'localisation' of trade. The world order created by the USA after 1945 attempted to address the sources of the earlier crisis and to institutionalise international economic liberalism. One should remember that this was only possible because of the Allied military victory and the unassailable economic dominance of the USA. Globalisation was restored by military force and national policy; it was not a 'natural' state of affairs. It also rested on a huge asymmetry; in that the new dominant power, the USA, was willing to accept the costs of creating the new regime and to tolerate national protectionist strategies on the part of its clients like Japan and South Korea. This was similar to British policy during the Pax Britannica.

The situation is now different. The USA is militarily dominant in a way no power has been in modern history. North America is the world's largest economy, but the USA is no longer willing to act as it did in the immediate post-1945 period. The USA is a major capital importer, it treats the value of the dollar as a matter of national economic management, (though it can also afford to operate a policy of 'benign neglect' in respect to the international value of the dollar because its exports still only comprise about 15 per cent of GDP), its foreign aid is derisory, and it promotes trade liberalisation in areas where it has a huge competitive advantage, but is unwilling either to open its own markets in key sectors or to allow national strategies of protection for emerging competing industries in developing countries. All the major industrial powers, with the partial exception of the UK, created their manufacturing sectors under a protectionist regime; Germany, Japan and the USA included. Current WTO rules prohibit such strategies and force most developing countries into manufacturing for export markets in relatively low value niches. The implication is that current processes of 'globalisation' are unlikely radically to diminish the gap between the developed and the developing worlds.

If 'globalisation' is conceived as a process that promotes cross-border exchanges and transterritorial agencies at the *expense* of nation states then it would be deeply problematic. If all states, including the most powerful, were to cease to be the primary political actors across borders, being displaced by companies, NGOs, regional governments, networks, international agencies, and so on, then one could anticipate a severe anti-globalisation 'backlash' as nationally-rooted publics experience a loss of the benefits of domestic governance and increased exposure to international pressures. If the majority of states cease to be effective actors, but the G7 still dominate in terms of economic governance and the USA alone dominates militarily, then Western and American dominance will be resented, resisted and challenged both nationally and transnationally in an increasingly unequal and conflictual world. This shows that there are inherent limits to globalisation conceived as a process that leads to the decline of national economies and state power. A truly

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

global market system, in which international competitive pressures and market forces subsume national economies, and in which transnational agencies and networks reduce states to the equivalent of local authorities, would be vulnerable to multiple political and social threats that it had no means to counter: international terrorism, commercial piracy, crime, protest movements and national backlash strategies of local withdrawal from the global system. The complete victory of extreme economic liberalism in both policy and fact would most likely spell the end of the system, not as in 1914 in inter-state war, but in a series of terrorist outrages, local economic crises – like that in Argentina – major crises in the financial markets, and the re-politicisation of national governance, leading to the restoration of distinctive local policy regimes.

The open international economy is not a 'natural' state of affairs, to which the world reverts by economic logic when the distorting influences of politics on markets are removed. Rather it depends on state power; economic liberalism has to be instituted and defended. If it is to survive then its negative effects have to be ameliorated by public policy. Economists have had to learn this the hard way, but few really understood the extreme fragility of markets and the dependence of economics on state power before September 11. Globalisation can go backwards: it can be impeded – as the backlash policies of the late nineteenth century showed; and it can be reversed – as the inter-war years demonstrated. The current 'anti-globalisation movement' is a noisy sign of widespread dissatisfaction, but the real backlash would come from conventional politicians and would start to show in new state policies. Such policies would include both national measures and the advocacy of changed policies in international forums like the WTO by states and groups of states. Such policies may be difficult to distinguish in the first instance from the re-regulation that is necessary to counter the negative consequences of excessive economic liberalism. A major backlash against international openness by states, and by legitimate and non-legitimate non-state and transnational actors, can only be prevented by a judicious mixture of appropriate force and governance measures that stabilise markets and protect citizens against unacceptable insecurity and risk. Both dimensions of policy are necessary, and both will be expensive – military action and social solidarity need to go together; the latter is essential to underpin and legitimate the former. The future of the open international trading system in the immediate future (the next 25 years) thus rests on appropriate political policies and in the actions of the major nation states, and the USA in particular.

THE FUTURE OF GLOBAL GOVERNANCE

However, it would be foolish to look at immediate events alone, and not also long-term trends (Hirst, 2001). The threats to global stability are multiplying and are likely to become more severe as the twenty-first century progresses. The most serious are only indirectly connected to the current open international economy but create a context in which at worst it could fail and break down. Many of these threats are unlikely to become critical in the next 30 years, and so are beyond the scope of normal political calculation, yet they require action now if there is to be any prospect of forestalling or even mitigating them.

The most serious is climate change, which is likely to become progressively worse as the century unfolds and to have destabilizing effects by mid-century and catastrophic

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

consequences by 2080.[1] The consequences – turbulent weather, inundations due to rising sea levels, desertification and water shortages, loss of farm land, and the spread of disease – are likely to develop in chaotic and unpredictable ways that will not be amenable to adaptation by the kind of incremental action policy makers are used to. This will affect both developed and developing countries, but the latter are likely to suffer more, as they have fewer resources to respond to the consequences, and they have large populations. A worsening environment is likely to be associated with the displacement of large numbers of climatic refugees, adding to the existing and growing migratory pressures from poorer countries. It is also possible that current UN estimates that the world's population will peak in 2040 and then decline may prove to be wrong, not least because they are based upon optimistic assumptions about economic development. Insecurity and persistent poverty will lead to people having more children rather than fewer – thus population pressures may well be another source of turbulence, making the effects of climate change on the displacement of peoples worse.

The odds are that the current extreme inequality of global income distribution will continue (Wade and Wolf, 2002). That for the majority of the world's poor this will be the result of a failure of domestic economic development rather than direct exploitation by the rich will not make their lot easier to bear. It is prudent to assume that the normal economic processes will not transform the bulk of the world from developing to developed status without the need for other forms of intervention. Most of the population of Africa, and the majority in East and South Asia and Latin America will remain poor – part of the 80 per cent who share just 14 per cent of world GDP. It is highly unlikely that the major developing nations – Brazil, China, India, Indonesia or Nigeria – will effect the same transition to advanced industrialism as Japan or South Korea (Hirst and Thompson, 1999, ch. 5). Uneven industrialisation heavily oriented toward export markets will leave huge populations in excluded rural areas and urban slums.

Such problems, and more immediate ones like transnational crime syndicates or AIDS, are frequently cited by advocates of greater global governance as demonstrating the inherent limitations of the nation state. Yet they are also beyond the scope of action by any foreseeable global or transnational institutions. To cope with climate change or global inequality in a serious way, supranational institutions would require coercive powers over states and the ability to command resource redistribution, chiefly at the expense of the top 20 per cent of the world's population represented by the countries of the OECD. Yet these countries, singly in the case of the USA, collectively in the case of the rest, have the power to resist such coercion and to refuse redistribution. Far from legitimating a move toward cosmopolitan governance and a new international order these emerging global threats all but paralyse political will. If anything they focus political and business elites on the short-term, because to confront the long-term consequences of doing little now is almost unthinkable. For example, the Kyoto accords on climate change, if implemented, would have the effect merely of modestly offsetting the impact and onset of global warming. Hence the resistance in the USA of having to bear the short-term costs of an emissions reduction policy.

Power in governing the international economy is likely to remain in the hands of the wealthy nations and the supranational bodies that they control and fund, like the IMF or the World Bank. It is also likely that the exercise of that power will be challenged by major non-OECD states like China, India and Russia, and by protest movements and

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

NGO coalitions across the globe. It is obvious that the actions of the major powers and the supranational agencies that they control will be less legitimate and that wider forums, like the WTO, will become more conflictual as the less developed nations vigorously defend their interests.

The agenda for global governance is thus constrained by the inherent limits of truly authoritative global institutions, by the perceptions and interests of state elites in the G7, and by the mass attitudes of the populations of the OECD countries. A real world government would quickly become a tyranny – conservative in the defence of entrenched privilege in the hands of the rich, and confiscatory in the hands of the poor, and thus resisted and thwarted by the losers of either policy. The nation states, however powerful, cannot act alone, whilst nothing can be accomplished without their active support, legitimation and funding. That means that the agenda for strengthening international governance and mitigating those threats to stability that can be addressed in the short-term involves three dimensions. First, reinforcing those international institutions that can function effectively, and redirecting their policies. Institutions like the IMF are not inherently defective and it, for example, has a necessary role as an international lender of last resort. It is also necessary to expand the scope and power of other less headline-catching international institutions so that they are able to perform extended regulatory tasks, for example, beefing up the Bank for International Settlements' role in supervising national financial regulators so that the supervision of banks and other financial institutions is enhanced, and strengthening the ILO to negotiate new conventions on migration and international labour mobility and raising the floor of international labour standards. Second, promoting coordinated state action, whether by treaty or intergovernmental cooperation, for example, to tackle problems like international criminal and terrorist networks, to promote disease prevention and containment strategies, to pursue measures to combat global warming that can in fact be agreed (such as research and subsidies for non-fossil and renewable energy sources) and to raise the level of development aid. Third, to commit the major powers, and the USA in particular, to seek solutions where possible in a multilateral framework and for the powers to seek the widest legitimacy for their actions by strategies of consultation and coalition building.

Such measures would mean that when major global crises do occur, such as a sudden escalation of climate change or a major epidemic, then the states of the developed world can cooperate with others and that at least a minimum regulatory framework to ensure market stability and physical security is in place. Such measures amount to an extended version of 'business as usual', renewing the regulatory framework of multilateral international governance created after 1945. It would also mean a return to a policy of 'embedded liberalism', that is, market openness coupled with strong governance and social protection rather than contemporary economic liberal doctrine which is a mere use of political power to enhance the scope of market forces (Ruggie, 1998, ch. 2).

The prospect of such a policy of enlightened multilateralism on the part of the advanced countries, and the USA in particular, is poor. The main reason for such narrowly self-interested policies is that the present state of affairs is quite unlike 1945. The anti-globalisation movement and the terrorist threat are not a direct challenge to the system like that represented by the USSR and its allied communist parties. The former can still be dismissed as confused protest and indeed the movement does not have coherent alternatives to current institutions and their policies. The terrorist threat is a matter for

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

police and military action. The international economy in 1945 was at a virtual standstill and thus could be re-built from the ground up. Moreover, the major state elites are in fact satisfied with the high level of control they do in fact have, whilst often preaching impotence in the face of the forces of globalisation to their domestic publics. Global markets are not all-powerful; the scope of action by international agencies, inter-state cooperation and governance by states remains considerable. So far major financial crises have been contained. Concerted action by governments, central banks, financial market authorities and major companies prevented a disastrous panic in the aftermath of September 11. Even in recession, the G7 economies are not faced by immediate economic and social crisis.

One could thus conclude that 'globalisation' in the sense conceived by extreme economic liberals and their radical critics has not happened. The world, far from being an integrated system dominated by ungovernable market forces, is divided into three major trading blocs, dominated by nation states: NAFTA is centred in the USA, Japan is a bloc-sized national economy, and the EU is an association of states. Each bloc follows distinctive policies, and has distinctive problems and institutions of economic management. Most major companies hail from one of the three main blocs, and most companies have the bulk of their assets and the majority of their sales within one of the blocs.

International interconnectedness has not subsumed the distinctive national economies of, for example, Germany, or Japan or the USA. Hence the central powers in the system are neither likely to initiate a backlash against it nor are they likely to act on the scale necessary to counter the emerging global crisis and the current difficulties of the mass of the world's population outside the OECD. One might conclude that the current system is well enough governed and sufficiently beneficial to those on whose behalf it is governed that it will persist until problems accumulate that cause it to fail and a crisis that is beyond governance overwhelms the system. Unlike the 1930s or the period before 1914 the backlash against the international economy is not likely to start with the core states of the G7, but at the periphery.

This may seem pessimistic but it is highly likely that a crisis stemming from climate change, mass poverty in the developing world, and intense migratory pressures will overwhelm global institutions of governance and cooperation in the distant but foreseeable future, sometime in the second half of this century. Before then difficulties and conflicts will accumulate, weakening the will to cooperate and undermining any prospect of solidarity between rich and poor, developed and developing nations. In this context governance will be asserted at the level where the public can put pressure on leaders, in nation states. International agencies will be harder to sustain and transnational politics and institutions will decline in favour of state-based ones. States will seek to protect their populations and to monopolise and control the distribution of key resources. Faced with climate change political processes, rather than markets, will allocate scarce goods like food, shelter for the displaced, water and energy. States will seek to obtain these things by force, as will political movements. Those displaced by climate change are unlikely to be passive. At least some major states will fight over access to water and oil.

This is a bleak prospect, but it emphasises the continued relevance of classic international relations as a discipline, and of realism in particular. The military power of the West is overwhelming. The USA and its allies dominate the seas and international airspace. They thus control the major trade routes and access to the world trading

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

system. The already overwhelming military capacity of the USA is set to increase in the immediate future as the military exploit emergent technologies and utilise space as a new environment for intelligence, communications and weapons directed at earth. However, such power has its limits. The advanced economies are vulnerable to terrorism and will remain so, even if they adopt draconian measures that restrict the liberties of their own populations. Masses of migrants would be hard to contain, even with brutal and repressive policies of exclusion and frontier control. Advanced weapons may be ineffective against determined enemies with strong national cohesion and an effective military leadership with clear objectives. The USA, for all its recent victories, has not really faced such an enemy since Vietnam. Thus the bulk of the Iraqi army was ill-trained and poorly motivated, the Serbs increasingly hostile to Milosevic, and the Taliban a hollow regime based on savage repression. Moreover, at least some of the emerging technologies will be easy to copy and adapt by the less sophisticated powers. Intelligent mines and small remotely-piloted vehicles, for example, may make defensive strategies easier and counter Western offensive dominance, making it difficult for advanced armies to occupy territory without heavy casualties (Hirst, 2001).

One should thus assume a highly conflictual world: with constant police action against terrorists, migrants and protestors, low grade wars and incursions by the USA and its allies in failed states and terrorist havens, conflicts between less developed states (increasingly over access to resources), the involvement of the great powers on behalf of their clients, and increasingly conflictual relations between major states over resources and trade. In this world order international norms and legal standards will most likely come under increasing pressure in matters of human rights, conflict and war. This will be a process similar to the widespread violation of the Hague Conventions during World War I. States will repudiate human rights conventions and international legal regulation, even as international lawyers attempt to complete the edifice they have been building since 1945. The USA already will not submit to the International Criminal Court, and without it the whole project of subjecting national political actors to common international norms is gravely weakened. Faced with terrorist outrages and masses of displaced persons, many states will be unwilling to continue to subscribe to international conventions and will slip into authoritarian regimes against outsiders, supported by their frightened citizens. Rules that only apply to some, the unlucky and defeated in the case of war criminals, or the lucky who happen to find one of the few liberal havens in the case of refugees, will cease to have general effect or credibility (Krasner, 1999).

If political norms increasingly cease to be accepted or followed, by contrast rules-based economic governance will remain strong. Indeed, this is the most likely dimension of global governance and re-regulation. The WTO is a rules-based organisation and it is impossible to open markets without common standards that apply to all and that are justifiable. Equally, tightening financial regulation and banking supervision, partly to prevent financial crises and partly to control terrorism and money laundering, will extend the scope of regulatory and rules-based supervision by national and international agencies. Companies are increasingly using international arbitration and supranational standards of commercial conduct to resolve disputes that span national jurisdiction. Thus in the short term we may see both more conflict in the political sphere and greater regulation and normalisation in the economic (Weiner, 1999).

Any argument about global governance must allow for the extreme variability of global

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

processes and the variety of global institutions. It is clear that on different dimensions and at different locations governance practices and outcomes can vary widely. We should, therefore, expect combined phenomena of integration and disintegration, increasingly effective governance on some dimensions and retreat on others, different mechanisms for different problems, both localisation and internationalisation. Unless this is recognised, the complexity of short-term outcomes may hide long-term trends toward conflict, localisation and chaos.

THE FUTURE OF THE GLOBAL ECONOMY

Even well before the events of September 2001 there were several indications that the rapid globalisation of economic activity experienced during the 1980s and the 1990s may have begun to stall. The rate of growth of the US economy was slowing, Japan's intractable economic problems were no nearer solution, and there was unease in Europe about its future economic prospects as the adoption of the euro loomed and growth faltered. But these essentially cyclical uncertainties were being bolstered by some potentially longer-term structural changes. Thus the world may be experiencing the final years of one of those periodic explosions in internationalisation that throw so much into confusion and seem to herald the complete transformation in the way societies are organised. There is beginning to emerge a serious questioning of the ability of the global economic system to sustain its seemingly as rapid integrationist trajectory.

In this section we examine the potential cyclical and structural constraints on the future growth of economic globalisation. We ask the question 'Are there any limits to economic globalisation?'. The strong globalisation thesis would seem to imply an ever-expanding universe of economic interdependency and integration between national economies, so that the significance of national borders for economic activity eventually disappears. The issues for us here are first, why should this be the case? and, second, is it happening?

Globalisation is here defined in strictly economic terms, basically as increasing trade interdependency and investment integration. The strong globalisation thesis contends that macroeconomic and industrial policy intervention by national governments can only distort and impede the rational process of resource allocation by corporate decisions and consumer choices, which are now made on a global scale. All corporate players need to do to prosper is to shake off their nationally orientated bureaucratic style of management, and the government intervention that goes along with it, and enter the new world of open global marketing and production networks. International markets provide coordinating and governance mechanisms in and of themselves: national strategies and policy intervention are likely merely to distort them. The era of effective national economies, and state policies corresponding to them, is over. The market will, and should, decide (Ohmae, 1990; 1995).

We have challenged this conception and we do not think the international economy looks anything like this (Hirst and Thompson, 1999; 2000), but it offers a powerful imagery and should not be ignored. It is thus worth confronting it in its own terms.

A key element in this challenge is to question the extent of contemporary trade globalisation. If we look at merchandise trade flows between the main economic blocs expressed

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

Table 1.1 Merchandise trade flows as a percentage of originating Triad bloc/country GDP (1998)

To	North America	Western Europe[a]	Japan (J)	East Asian Traders[b] (EAT)	J + EAT
From					
North America	3.8	2.0	0.7	1.1	1.8
European Economic Area[a] (EEA)	2.3	18.0	0.4	1.0	1.4
Japan (J)	3.3	2.0	–	3.0	3.0
East Asian Traders[b] (EAT)	10.7	6.9	4.1	na	na
J + EAT	14.0	8.9	4.1	na	na

Notes:
a. European Economic Area (EEA) = EU + Switzerland, Turkey, Norway, Malta, Liechtenstein and the states of the former Yugoslavia.
b. East Asian Traders (EAT): China, Hong Kong, Taiwan, Korea, Malaysia, Thailand and Singapore.
na = not available.

Sources: *WTO Annual Report 2000, Volume II, International Trade Statistics,* derived from various tables; *World Economic Indicators 2000*, World Bank, Table 4.2; *Taiwan Statistical Data Book 2000.*

as a proportion of the originating country or bloc GDP then, for the most part, quite low percentages of GDP seem to have been traded in 1998 (see Table 1.1).

Only Western Europe appears anywhere close to being an integrated trading zone, with 18 per cent of its combined GDP traded between the countries of Western Europe. Yet this is an artefact of national accounting and the EEA should be treated as a single quasi autarchic trade bloc. The only other relationship that appears significant is that between the East Asian traders and North America, where the former exported just under 11 per cent of their GDP to North America, mostly to the USA. However, look at the relationship between North America and Japan. Only 0.7 per cent of North American GDP was exported to Japan, while Japan exported 3.3 per cent of its GDP to North America. These are still quite small numbers.

Of course there are many objections that could be mounted to this way of measuring the extent of trade 'globalisation', and these are dealt with elsewhere (Hirst and Thompson, 2000; Thompson, 2001). Comparing merchandise trade and total GDP is not comparing like with like as total GDP is made up of many sectors, some of which have been expanding at a faster rate than the merchandise sector. But even when a proper comparison is made, only Western Europe displays a highly integrated trade environment (nearly 81 per cent of merchandise trade relative to merchandise GDP is inter-Western European trade). The other main trading blocs still remain surprisingly un-integrated on this traditional and long established measure of globalisation.

For economists these figures raise the question of the 'missing trade'. Why isn't there more trade in the international system? Broadly, the answer is that the lack of trade is because of the continued significance of national territories and national borders, a point we come back to in a moment.

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

In economics, national borders are viewed as an impediment and an obstacle to trade. They are an impediment to the development of market forces, so the advent of modern globalisation and a 'borderless world' would be a triumph from the point of view of those supporting the strong globalisation position mentioned earlier. The problem is to overcome these 'barriers' to trade.

How is international trade analysed in economics? When economic modelling techniques are applied to the specifics of international trade, these produce disappointing results in terms of explaining the amount, composition and direction of international trade flows. As just mentioned, these models would predict much higher levels of international trade. This has led to a great deal of soul searching amongst economists, and a resort to analysing 'what is in the data' rather than constructing further theoretical models. Thus despite the seeming sophistication of much international trade theory, when it comes to the empirical side of things the approach is still fairly simple. At heart it relies on operationalising a 'gravity' model.

Empirically, trade is traditionally modelled as positively related to some measure of the 'size' of the communities between which it takes place and negatively related to the distance between them. This is known as a 'gravity model'. But what has interested economists recently is a series of institutional, cultural or political and geographical variables that are also very important in determining trade. These can be expressed as a series of 'control' variables designed to capture other relationships between countries that might stimulate trade between them. These can include such aspects as whether countries share a common border, whether they share a common language, whether they have had colonial connections, whether they belong to a common trade bloc (for example, the EU, ASEAN, NAFTA), what the position is in respect to common jurisdictional standards and the legal enforceability of contracts between them, and finally whether they share a common currency.

The distance variable is the most consistent and significant of the variables explaining international trade (Leamer and Storper, 2001). Indeed, one of the most obvious constraints on an infinitely expanding international division of labour and a 'complete' globalisation is that the effects of distance cannot be entirely eliminated. Although there have been several 'communication revolutions' which have significantly reduced the costs of transporting over distance, eventually these will come up against the basic physical impossibility of total transport cost elimination, so here is one (fairly obvious) 'limit to globalisation' (see Obstfeld and Rogoff, 2001). Table 1.2 expresses the effects of distance on economic interactions for a range of variables: trade, FDI, equity flows and technology

Table 1.2 The effect of distance on economic interactions. Percentage reductions in the value of magnitudes relative to 1000 km

	Trade	FDI	Equity Flows	Technology Flows (R&D Stock)
1000 km	0	0	0	0
2000 km	58	25	45	35
4000 km	82	44	69	72
8000 km	97	58	83	95

Source: Calculated from Venables (2001).

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

flows. Economic interactions fall away dramatically with distance. For instance, if you add 7000 km distance between any nodal points, 97 per cent of trade disappears.

But an interesting feature of recent trade empirics is the central importance that has emerged for the 'cultural' or 'political' determinants of trade specified by the control variables just mentioned. For instance, once the contributions of, say, migration (which can be approximated by variables such as sharing a border, a common language or colonial experience), and different legal cultures have been accounted for in regression analyses, the specific contribution of GDP as such as a determinant of trade levels is severely limited, and indeed becomes less than 1 in many cases. We stress the significance of this in a moment.

The specific effect of national borders on trade and the globalisation debate can be taken up in the context of these empirical gravity model equations. There has recently been something of a test case analysis of this involving the border between the USA and Canada (McCallum, 1995; Engel and Rogers, 1996; Hel-liwell, 1998; 2000). If globalisation has emerged, then surely this border would have been one of the first to have lost its pertinence as far as trade, investment and migration is concerned. But it has not. Careful analyses have demonstrated the continued central importance of this border as an 'obstacle' to trade (and other flows) between the USA and Canada. This is the case as tariffs and quotas have been eliminated, NAFTA established, and other barriers removed. What these analyses do is begin to confront the mysteries of the 'missing trade' at the international level. Far from there being an 'excess' of international trade as many critics of globalisation believe from the economists' perspective, there is not 'enough' of it (and this goes for capital flows as well which, whilst not discussed here, are addressed in Hirst and Thompson, 2000 and Thompson, 2001).

What most analyses of the growth of international trade do is to look only at international trade without comparing it with what is going on in the home territory at the same time. International trade is expanding but so too is domestic trade, and it looks as though domestic trade is expanding at a similar rate to, or at a more rapid rate than its international equivalent (after accounting for the other control variables). We might need to be a little more cautious here, however, since these analyses were conducted for the very early years of NAFTA. Recent evidence suggests that cross-border US–Canada trade has grown considerably. Also, the full implementation of NAFTA does not take effect until 2008.

But overall, this particular border continues to be a remarkable 'barrier' to trade in and of itself, even after taking account of all the usual variables that might determine trade. What is more, there is evidence that the state boundaries *within* the US act as a 'barrier to trade' (Wolf, 1997), so the idea that it is tariffs and quotas or other at-border international impediments to trade which represent the main obstacles to international integration is further put into question. Moreover, differences in cultural and legal systems between these two countries – which might be thought to inhibit trade, as suggested earlier – also appear small in this particular case. What is more, these results are confirmed in the case of the other OECD countries though admittedly on the basis of less appropriate and reliable data (Wei, 1996; Helliwell, 1998).

In addition, there is good evidence that migration is a significant stimulus to trade (Casella and Rauch, 1997; Rauch, 1999). It is very significant, for instance, in the case of imports into the USA. Migration sets up networks of relationships across borders,

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

making it easier to establish a low transaction cost mechanism for the conduct of international trade (we come back to this in a moment). As long as countries maintain their commitment to regulate their populations in some sense (which is almost a defining feature of the notion of geographical 'territoriality'), then this situation will continue. In particular, in so far as countries continue to clamp down on international migration this could inhibit the further growth of international trade. So here is another potential 'limit to globalisation' and one that shows a major difference between integration processes today and those of the nineteenth century.

It seems that this particular point is crucial in the context of the jurisdictional consequences of borders; the fact that any movement across a national frontier involves the movement from one legal, regulatory and cultural jurisdiction to another. These jurisdictions proscribe, adjudicate and enforce a wide range of norms, rules, habits, networks and similar features, which involve much more than just the 'obstacles' to trade found at the point of the frontier. It is 'behind border' characteristics that are crucial. An interesting suggestion here is that it may be the state of the legal and administrative certainty associated with the enforcement of contracts (with respect to both trade and capital flows) that is the key to the OECD bias in international economic transactions. When a measure to represent this was introduced into the gravity model formulation this was found to account for such a significant proportion of the level of international trade that the impact of income *per se* was less than 1 (Anderson and Mar- couiller, 1999). Thus the implication here is that GDP growth has a less than proportionate impact on international trade growth; the bulk of the growth in international trade over the post-World War II period being accounted for by the 'one-off' impact of legal enforceability. This thereby points to a potential optimal level of international trade as this one-off boost to trade eventually exhausts itself.

Another important area of discussion involving gravity model type approaches to international trade revolves around the effects of common currencies on trade. An additional variable that can be included in the gravity model equations is one for countries sharing a common currency. There are 193 independent countries recognised by the UN but only about 120 different currencies operate. Many countries share a currency; and some have done so for a very long time. Under current circumstances, however, the issues are European Monetary Union and 'dollarisation'. In January 2002 12 EU member states adopted the euro. In addition there are a number of countries that have experimented with abandoning their own currency in favour of the US dollar, mainly in Latin America, or who have established a 'hard currency board' approach to monetary management. What are the effects of these policies on trade?

There seem to be very large trade gains to be made by adopting common currencies, as those countries that have done so trade with each other to a much greater extent than those with their own currency (other things remaining equal) (Rose, 2000; Rose and Wincoop, 2001). This has led to a number of suggestions for further dollarisation and even the adoption of a single world currency (Alesina and Barro, 2001; Dornbusch, 2001; Rogoff, 2001). The beneficial effects have to do with the macroeconomic discipline and stability that 'dollarisation' is supposed to instill in (mainly) small and wayward countries. However, these gains are disputed (Persson, 2001; Rose, 2001). On close scrutiny there is little evidence that the suggested welfare and growth benefits have actually materialised (though inflation has been lower) from these policies and we should remain very sceptical

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

BOX 1.1 TYPES OF TRADE

1. **THOSE GOODS EXCHANGED ON 'ORGANISED MARKETS'** (e.g. minerals, raw materials, primary agricultural products)
2. **THOSE GOODS EXCHANGED ACCORDING TO 'REFERENCE PRICES'** (e.g. processed raw materials, chemicals, basic standardized components)
3. **THOSE DIFFERENTIATED GOODS AND SERVICES EXCHANGED ON THE BASIS OF 'NETWORKS'** (e.g. complex manufactured goods and services)

Note: This schema is based upon Rauch (1999).

about such policy initiatives (Edwards, 2000; 2001). The recent case of Argentina should reinforce this vary cautious attitude towards currency boards and talk of full dollarisation. As the US dollar appreciated in value, the Argentine peso also appreciated in value because it was linked to it via a currency board. This made Argentine exports very internationally uncompetitive independently of what was actually going on in Argentina itself, which was one of the reasons undermining the stability of the Argentinian economy.

But independently of these disputes, as long as countries continue to maintain their own currencies – which for the foreseeable future looks highly likely for most countries – again there will be an added limit to the extension of 'trade globalisation'(Rodrik et al., 2004).

Let us now consider another way trade is analysed in respect to borders and the long-term impediments to ever greater globalisation, which can be illustrated by the schema of different types of trade shown in Box 1.1.

International trade can be divided into three categories. The first is that traded on organised exchanges, like primary products such as minerals and agricultural products, where price is established according to classic market mechanisms. Here one might think of markets like the Chicago grain markets, the London metal exchanges, and the Rotterdam spot market for oil.

The second category is intermediate goods that are traded according to 'reference prices' quoted in specialist publications and the like, such as chemicals and processed raw materials. For the prices of these goods you would consult a reference manual or trade price book. These are readily available in an openly published form.

The third type of trade is differentiated manufactured goods and services where there is no organised market or quoted reference prices. Here we do not find a uniform standard price but rather more 'one-off' pricing, differentiated according to complex networks of supply.

Unlocking the complex determinants of trade with respect to each of these categories is not easy (Rauch, 1999). Although the first, and to a lesser extent the second, of these categories display a high international trade to production ratio so that a high proportion of their output is exported, these are declining in importance as components of total international trade. These categories of trade are also less sensitive to the 'cultural variables' mentioned earlier in the context of the gravity model, so they are more closely correlated with the growth of wealth and income. But what has expanded rapidly is the third category, particularly complex manufactured goods. And this has a relatively low production to trade ratio, when all the other variables that determine trade have been

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

accounted for. The key here is these other cultural, political or geographical influences, which act at the expense of income growth as such. There is a great deal of production but relatively lower levels of it are exported abroad as a pure consequence of income growth, rather than as a consequence of other variables like distance, migration and legal similarities, and so on.

Thus we have a situation where those categories of trade with high income elasticity related production propensity to export are declining in significance, while that category with a lower income elasticity related production propensity for export is increasing in importance. Perhaps this is at least one of the reasons for the relative lack of international trade, as opposed to domestic trade within a country.

The reasons for these different propensities are interesting and important. Where there is an organised market for exchange, as in the case of the first category, the organisation of the exchange is relatively easy and cheap. Transaction costs are low. However, with sophisticated manufactured goods there are no organised markets to facilitate exchanges. Rather they are traded in the context of often one-off, lengthy and complex networks of supply and distribution. Manufacturers have to set up webs of distribution systems, which are often singular and unique for each particular category of good. They require the seeking out of trading partners and the securing of a network of participants, something, it might be added, that migration makes easier. Above all these systems are costly to set up and maintain – transaction costs are high. This may account for the lack of trading in these goods across frontiers relative to their trading at home, and put a limit on the extent of their expansion. It is just too costly, for instance, for US manufacturers to secure distribution systems for their goods in Japan, so there are low levels of US exports to Japan, as shown in Table 1.1 above.

An obvious question here is whether there is any empirical evidence to support these remarks.

Whilst there was a rapid growth in world trade for all the categories of trade mentioned in Box 1.1 over the 1970s and 1980s, there was a downturn in the growth of agricultural exports in the second half of the 1990s. But after a slowdown in manufacturing exports in the same period, these recovered in 1999–2000, mainly as a result of a rapid growth of exports from the emerging economies.

In case this seems deliberately to concentrate upon merchandise trade and leave out trade in services, which are thought to be growing at a faster rate, this latter claim is not in fact true. Trade in cultural goods, for instance, was also falling off in the late 1990s. Trade in services has remained at about 20 per cent of total world trade ever since 1975, so by concentrating only on merchandise trade we have covered the bulk of total world trade.

In this section we have argued three things. First, that far from market exchange sweeping unhindered across the globe there are likely to continue to be real limits to the further expansion of global trade, limits largely established by the continuing salience of national territories and borders.

Second, we have argued that the real constraints on any further development of global trade are more likely to be the institutional, cultural and political variables, or the geographical ones analysed above, rather than straightforward economic ones.

Third, there is some limited indication that overall world trade growth has slowed in recent years. Of course this may be mainly for cyclical reasons, but the analysis has also demonstrated that there are a potential set of more structural constraints that even in the

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

medium term could undermine an ever expanding international division of labour and trade integration.

If nothing else, these remarks indicate that there are good and interesting reasons still to take the issues of borders seriously in economics, despite the fashionable insistence that they are no longer significant in an age of globalisation.

CONCLUSION

In this chapter we have tried to look forward to the future of global governance and the future of the global economy. We have tried to demonstrate three things. That the current state of international interconnectedness is not unprecedented and that previous episodes of integration have generated a backlash and have ended in the regression of international trade and investment. That national states are not being overwhelmed and the future of extended multilateral governance does not look promising. In a turbulent physical and international environment the nation state may become more salient as a means of protection against global forces beyond supranational governance. That there may be inherent limits to the growth of international trade, that borders do matter, and that we may be approaching those limits. These messages are comforting neither to the advocates of the 'Washington Consensus' nor to their 'anti-globalisation' critics.

NOTES

* Reprinted by permission of Sage Publications Ltd (© *Cooperation & Conflict,* NISA – Nordic International Studies Association, 2002).

1. The evidence and probable consequences considered in the 2001 report of the UN Intergovernmental Panel on Climate Change and the 2002 report of the US National Academy of Sciences are compelling and disturbing.

REFERENCES

Alesina, A. and R.J. Barro (2001), 'Dollarization', *American Economic Review, Papers and Proceedings,* **91**, May, 381–5.

Anderson, J.E. and D. Marcouiller (1999), 'Trade, insecurity, and home bias: An empirical investigation', *NEBR Working Paper No.* 7000, Cambridge, MA.

Casella, A. and J.E. Rauch (1997), 'Anonymous market and group ties in international trade', *NBER Working Paper No. 6186,* Cambridge, MA.

Dornbusch, R. (2001), 'Fewer monies, better monies', *American Economic Review, Papers and Proceedings,* **91**, May, 238–42.

Edwards, S. (2000), 'Exchange rate regimes, capital flows and crisis prevention', unpublished mimeo, University of California, LA, August.

Edwards, S. (2001), 'Dollarization and economic performance: an empirical investigation', *NEBR Working Paper No. 8274,* May.

Engel, C. and J.H. Rogers (1996), 'How wide is the border?', *The American Economic Review,* **86**(5), 1112–25.

Held, D. and P. Hirst (2002), *Globalization: the Argument of our Time,* opendemocracy.net.

Held, D., A. McGrew, D. Goldblatt and J. Perraton (1999), *Global Transformations,* Cambridge: Polity Press.

Helliwell, J.F. (1998), *How Much do National Borders Matter?,* Washington, DC: Brookings Institution.

Helliwell, J.F. (2000), *Globalization: Myths, Facts and Consequences,* Toronto: C.D. Howe Institute.

Hirst, P. (2001), *War and Power in the 21st Century,* Cambridge: Polity Press.

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access

Hirst, P.Q. and G.F. Thompson (1999), *Globalization in Question: The International Economy ami the Possibilities of Governance* (2nd edn; 1st edn 1996), Cambridge: Polity Press.
Hirst, P.Q. and G.F. Thompson (2000), 'Globalization in one country: the peculiarities of the British', *Economy and Society,* **29**(3), August, 335–56.
James, H. (2001), *The End of Globalization: Lessons from the Great Depression*, Cambridge MA: Harvard University Press.
Krasner, S.D. (1999), *Sovereignty, Organised Hypocrisy,* Princeton, NJ: Princeton University Press.
Leamer, E. and M. Storper (2001), 'The economic geography of the internet age', *Journal of International Business Studies,* **32**(4), 641–65.
McCallum, J. (1995), 'National borders matter: Canada-US regional trade patterns', *The American Economic Review*, **85**(3), 615–23.
Obstfeld, M. and K. Rogoff (2001), 'The six major puzzles in international macroeconomics: is there a Common Cause?', in B. Bernanke and K. Rogoff (eds), *NEBR Macroeconomics Annual 2000,* Cambridge, MA: MIT Press.
Ohmae, K. (1990), *The Borderless World,* London and New York: Collins.
Ohmae, K. (1995), *The End of the Nation State*: *The Rise of Regional Economies*, London: Harper Collins.
O'Rourke, K.H. and J.G. Williamson (1999), *Globalization and History: The Evolution of the Nineteenth Century Atlantic Economy,* Cambridge MA: MIT Press.
Parsley, D.C. and S-J. Wei (1999), 'Border, border, wide and far, how I wonder what you are',*World Bank Policy Working Paper No. 2217,* Washington, DC: World Bank.
Persson, T. (2001), 'Currency unions and trade: how large is the treatment effect?', *Economic Policy,* No. 33, pp. 435–48.
Rauch, J.E. (1999), 'Networks versus markets in international trade', *Journal of International Economics,* **48**, 7–35.
Rodrik, D. (1999), *The New Global Economy and Developing Countries: Making Openness Work,* Policy Essay No. 24, Washington, DC: The Overseas Development Council.
Rodrik, D. (2000), 'How far will international economic integration go?', *Journal of Economic Perspectives,* **14**(1), Winter, 177–86.
Rodrik, D. with A. Subramanian and F. Trebbi (2004), 'Institutions rule: the primacy of institutions over geography and integration in economic development', *Journal of Economic Growth,* **9**(2), June, 131–65.
Rogoff, K. (2001), 'Why not a global currency?', *American Economic Review, Papers and Proceedings,* **91**, May, 243–7.
Rose, A.K. (2000), 'One money, one market: estimating the effect of common currencies on trade', *Economic Policy,* No. 30 (April), pp. 7–73.
Rose, A.K. (2001), 'Currency unions and trade: the effect is large', *Economic Policy*, No. 33, pp. 449–61.
Rose, A.K. and E. van Wincoop (2001), 'National money as a barrier to international trade: the real case of currency union', *American Economic Review, Papers and Proceedings,* **91**, 386–90.
Ruggie, J.G. (1998), *Constructing the World Polity,* London: Routledge.
Rugman, A. (2000), *The End of Globalization*, London: Random House Business Books.
Thompson, G.F. (2001), 'Are there any limits to globalization? International trade, capital flows and borders', mimeographed, Open University.
Van Wincoop, E. (2000), 'Borders and trade', *Federal Reserve Bank of New York,* April.
Venables, A.J. (2001), 'Geography and international inequalities: the impact of new technologies', background paper for *Globalization, Growth and Poverty,* World Bank, Washington, 2002.
Wade, R. and M. Wolf (2002), 'Are global poverty and inequality getting worse?',*Prospect,* March, pp. 1–8.
Wei, S-J. (1996), 'Intra-national versus international trade: how stubborn are nations in global integration?', *NBER Working Paper No. 5531,* Cambridge, MA.
Wei, S-J. (2000), 'Local corruption and global capital flows', *Brookings Papers on Economic Activity,* No. 2, pp. 303–56.
Weiner, J. (1999), *Globalization and the Harmonization of Law,* London: Pinter.
Wolf, H.C. (1997), 'Patterns of intra- and inter-state trade', *NBER Working Paper No. 5939,* Cambridge, MA.

Paul Hirst and Grahame Thompson - 9781788118606
Downloaded from Elgar Online at 06/20/2019 02:00:56PM
via free access