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Corso di Laurea Triennale in Scienze Economiche

Is Globalization still a good chance?

Challenges raised by making capital, goods and people free to move across the planet.

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Academic Year 2010–2011

Abstract

The aim of this dissertation is to analyze the globalization phenomenon under multiple points of view, highlighting opportunities and weaknesses of its main aspects: the free mobility of capital, goods and people.

The work starts with an overview of the main features provided by the economic theory and history. Free capital mobility is studied in order to illustrate foreign investment main implications. Then, murky protectionist barriers and new emerging mercantilist pressures are pointed up. Finally, the effects of migration flows on the labour market is examined.

A briefing over main social and political consequences ends the work. In particular, major institutional and unions' concerns about poverty and inequality are expressed. Since global-level reform attempts are often neglected, a new global governance long-run scenario is proposed as solution.

Contents

List of Figures

1 Globalization demystified

'The passion that surrounds the vague term globalization *is best seen as a proxy for the long-standing debate about free-market capitalism. The zero-sum mindset, the difference between Pareto superiority and common norms of fairness, and the belief that all outcomes are caused by an intentional agent often cause communication problems between noneconomists and free-market economists, who themselves often exaggerate what* 'free-market reforms' *can accomplish and endorse overly ambitious programs of change (*'shock therapy'*), underestimating problems of transition and the second best. Economists could try to understand the protests against* 'globalization' *rather than dismissing them out of hand.'*[1]

1.1 Definition

Amazingly, for so widely used a term, there does not appear to be any precise, widely agreed definition. Indeed, the breadth of meanings attached to it seems to be increasing rather than narrowing over time, taking on cultural, political and other connotations in addition to the economic one.

World Bank definition[2]:

> *The most common or core sense of economic globalization surely refers to the observation that in recent years a quickly rising share of economic activity in the world seems to be taking place between people who live in different countries (rather than in the same country). This growth in cross-border economic activities takes various forms: international trade, foreign direct investments and capital market flows.*

[1] *The New Palgrave Dictionary of Economics* definition of *globalization*
[2] PREM, Economic Policy Group and Development Economics Group, 2000

United Nations ECSWA definition[3]:

> *When used in an economic context, it refers to the reduction and removal of barriers between national borders in order to facilitate the flow of goods, capital, services and labour...although considerable barriers remain to the flow of labour.*

Jagdish Bhagwati definition[4]:

> *Globalization is often used to refer to economic globalization, that is, integration of national economies into the international economy through trade, foreign direct investment, capital flows, migration, and the spread of technology.*

Martin Wolf definition[5]:

> *Globalization is a journey. But it is a journey towards an unreachable destination, 'the globalized world'. A 'globalized' economy could be defined as one in which neither distance nor national borders impede economic transactions. This would be a world where the costs of transport and communications were zero and the barriers created by differing national jurisdictions had vanished. Needless to say, we do not live in anything even close to such a world. And since many of the things we transport (including ourselves) are physical, we never will.*

'Globalization' is a word that gets both its proponents and opponents very agitated. But what exactly is it? What is the globalization debate really about? The answer is that the globalization debate is about a surprisingly large number of issues, including some that lie outside of economics. A non-exhaustive list of issues follows[6]:

1. Liberalization versus regulation of international trade, capital movements, and migration;
2. Market imperfections that arise with (either domestic or international) goods markets, capital markets, privatization, macroeconomic crisis, intellectual property rights, and so on;
3. Evaluation of the performance of the International Monetary Fund and the World Bank, including their policy prescriptions (the 'Washington Consensus', 'shock therapy', or 'structural adjustment');
4. Effects of freer trade and capital movements on rich country workers (*out-sourcing*) and on poor country workers (*sweatshops*);

[3] Economic and Social Commission for Western Asia, 2002, p. 1
[4] Bhagwati, 2004
[5] Wolf, 2001, p. 178
[6] *The New Palgrave Dictionary of Economics*

5. Extreme world inequality and poverty;
6. Capitalism (*neo-liberalism*) versus alternative systems;
7. Westernization/Americanization versus local culture;
8. Unequal distribution of political power between the West (both Western governments and corporations) and the Rest;
9. Effect of global economic growth on the environment;
10. Western imperialism and military intervention in the rest of the world.

Economists (including those identified as globalization critics) have focused largely on the first five issues, while the non-economists, though not ignoring them, seem to have something else in mind about the last five.

1.2 Historical background

In a sense, there is nothing new about globalization. Ever, since human beings have exchanged goods, there has been trade among people.

The historical origins of globalization are the subject of on-going debate. Though several scholars situate the origins of globalization in the modern era, others regard it as a phenomenon with a long history. The most extreme proponent of a deep historical origin for globalization is Andre Gunder Frank; he argues that a form of globalization has been in existence since the rise of trade links between Sumer and the Indus Valley Civilization in the third millennium B.C.[7].

An early form of globalized economics and culture, known as *archaic globalization*, existed during the Hellenistic Age, when commercialized urban centers were focused around the axis of Greek culture over a wide range that stretched from India to Spain, with such cities as Alexandria, Athens, and Antioch at its center. Others have perceived an early form of globalization in the trade links between the Roman Empire, the Parthian Empire, and the Han Dynasty. The increasing articulation of commercial links between these powers inspired the development of the Silk Road, which started in western China, reached the boundaries of the Parthian empire, and continued onwards towards Rome. With 300 Greek ships a year sailing between the Greco-Roman world and India, the annual trade may have reached 300,000 tons[8].

The 19th century witnessed the advent of globalization approaching its modern form. Industrialization allowed cheap production of household items using economies of scale, while rapid population growth created sustained

[7] Frank, 1998 quoted in Wikipedia at http://en.wikipedia.org/wiki/History_of_globalization

[8] Lewis and Moore, 2009 quoted in Wikipedia at http://en.wikipedia.org/wiki/History_of_globalization

demand for commodities. Globalization in this period was decisively shaped by nineteenth-century imperialism. After the First and Second Opium Wars and the completion of British conquest of India, vast populations of these regions became ready consumers of European exports. It was in this period that areas of sub-Saharan Africa and the Pacific islands were incorporated into the world system. Meanwhile, the conquest of new parts of the globe, notably sub-Saharan Africa, by Europeans yielded valuable natural resources such as rubber, diamonds and coal and helped fuel trade and investment between the European imperial powers, their colonies, and the United States. By the end of the 19th century, world trade was already an unmissable feature of the new capitalist world order, and the first global trade unions, the international trade secretariats (now known as global union federations) were born in that era[9].

The first phase of 'modern globalization' began to break down at the beginning of the 20th century, with World War I, but resurfaced after World War II (see figure 1.1 on the facing page) This resurgence was partly the result of planning by politicians to break down borders hampering trade. Their work led to the Bretton Woods Conference, an agreement between the world's leading politicians to lay down the framework for international commerce and finance, and the founding of several international institutions intended to oversee the processes of globalization. Globalization was also driven by the global expansion of multinational corporations based in the United States and Europe, and worldwide exchange of new developments in science, technology and products, with most significant inventions of this time having their origins in the Western world. The International Bank for Reconstruction and Development (the World Bank), and the International Monetary Fund were created during this period.

Globalization has been facilitated by advances in technology which have reduced the costs of trade, and trade negotiation rounds, originally under the auspices of the General Agreement on Tariffs and Trade (GATT), which led to a series of agreements to remove restrictions on free trade. Since World War II, barriers to international trade have been considerably lowered through international agreements — GATT and its successor, the World Trade Organization (WTO). World exports rose from 8.5% in 1970, to 16.2% of total gross world product in 2001.[10] Since the end of the cold war in 1989-91, there has been an unprecedented expansion of cross-border investments combined with a world-wide shift towards privatization, deregulation and free markets. Central to this process have been a number of trends: a huge growth in foreign direct investment (FDI), the liberalization of international trade, massive cross-border financial flows and a revolution in information and communica-

[9]See 'Encyclopædia Britannica's Great Inventions' at http://corporate.britannica.com/press/inventions.html

[10]Figure 1.2 on page 12 shows the trade/GDP ratio outcomes in more and less globalized groups of countries.

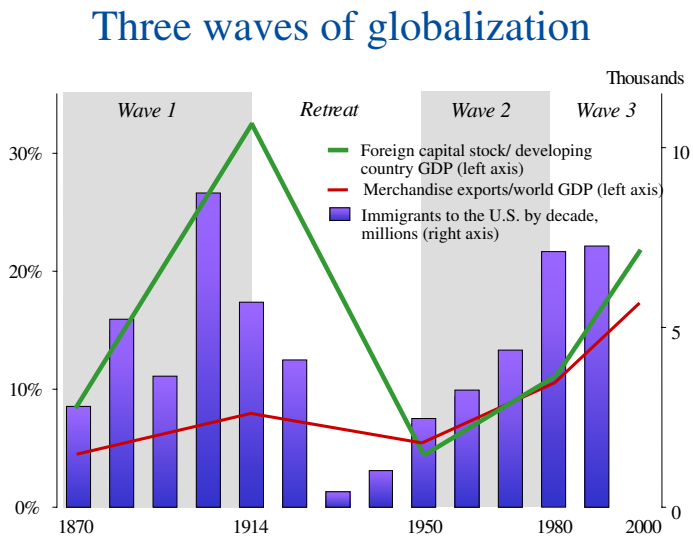


Figure 1.1: Source: World Bank, 2002, p. 4.

tion technology (ICT) which allowed work done using a computer to be moved to low wage locations for many job types, including accounting, software development, and engineering design[11]. The word *globalization* itself became popular in this period.

1.3 Why globalization?

The great hope of globalization is that it will raise living standards throughout the world, giving poor countries access to overseas markets so that they can sell their goods, allow in foreign investment that will make new products at cheaper prices, and open borders so that people can travel abroad to be educated, work and send home earnings to help their families and fund new businesses.
Stiglitz recognizes[12]:

> *I believe that globalization has the potential to bring enormous benefits to those in both the developing and the developed world. But the evidence is overwhelming that it has failed to live up to this potential.*

The goal is to increase material wealth, goods, and services through an international division of labour by efficiencies catalyzed by international relations, specialization and competition.

[11] The cost of a three-minute telephone call from New York to London fell from $317 in 1930 to $.30 in 1996 (in constant 1990 dollars).
[12] Stiglitz, 2006, p. 4

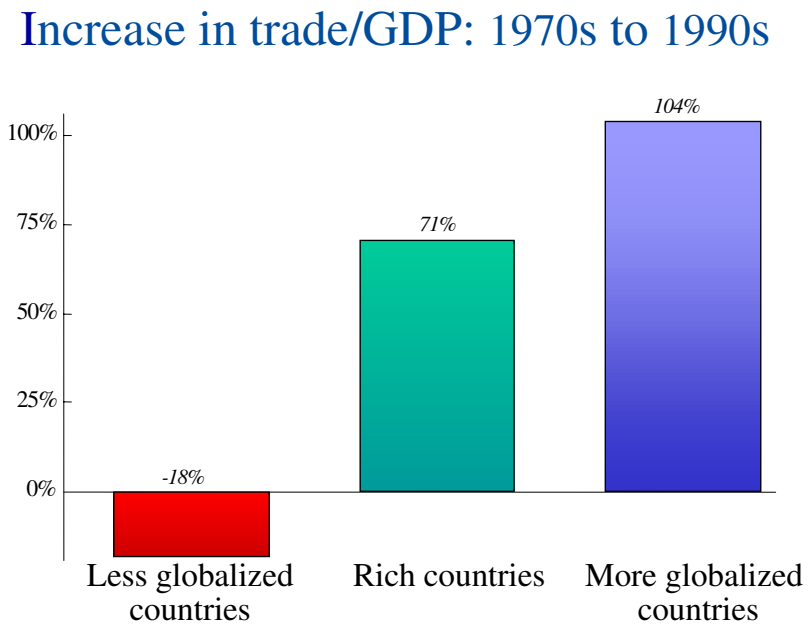


Figure 1.2: Source: World Bank, 2002, p. 2.

1.3.1 Washington Consensus

The term Washington Consensus was coined in 1989 by the economist John Williamson to describe a set of ten relatively specific economic policy prescriptions that he considered constituting the standard reform package promoted for crisis-wracked developing countries by Washington, D.C.-based institutions such as the IMF, World Bank, and the US Treasury Department. The prescriptions encompassed policies in such areas as macroeconomic stabilization, economic opening with respect to both trade and investment, and the expansion of market forces within the domestic economy. Subsequently to Williamson's work, the term Washington Consensus has commonly come to be used in a second, broader sense, to refer to a more general orientation towards a strongly market-based approach. The Consensus, as originally stated by Williamson, included the following broad sets of relatively specific policy recommendations[13]:

1. Fiscal policy discipline, with avoidance of large fiscal deficits relative to GDP;

2. Redirection of public spending from subsidies (especially indiscriminate subsidies) towards broad-based provision of key pro-growth, pro-poor services like primary education, primary health care and infrastructure investment;

3. Tax reform, broadening the tax base and adopting moderate marginal tax rates;

[13] Williamson, 1990 Chapter 2

4. Interest rates that are market determined and positive (but moderate) in real terms;

5. Competitive exchange rates;

6. Trade liberalization: liberalization of imports, with particular emphasis on elimination of quantitative restrictions (licensing, etc.); any trade protection to be provided by low and relatively uniform tariffs;

7. Liberalization of inward foreign direct investment;

8. Privatization of state enterprises;

9. Deregulation: abolition of regulations that impede market entry or restrict competition, except for those justified on safety, environmental and consumer protection grounds, and prudent oversight of financial institutions;

10. Legal security for property rights.

Though many concerns have been expressed about policies themselves, a more emblematic criticism was related to the uniqueness of the recipe. Strategies would probably need to be tailored to the specific circumstances of individual countries, rather than applied just as a single *one size fits all* formula. According to Stiglitz, the treatment suggested is too simple: one dose, and fast-stabilize, liberalize and privatize, without prioritizing or watching for side effects[14]. Rodrik pointed out what he claimed was a factual paradox[15]: while China and India increased their economies' reliance on free market forces to a limited extent, their general economic policies remained the exact opposite to the Washington Consensus' main recommendations. Both had high levels of protectionism, no privatization, extensive industrial policies planning, and lax fiscal and financial policies through the 1990s. Among other results of the recent global financial crisis, has been a strengthening of belief in the importance of local development models as more suitable than programmatic approaches. Some elements of this school of thought were summarized in the idea of a *Beijing Consensus*, which suggested that nations needed to find their own paths to development and reform.

1.4 Main actors of the globalizing process

A number of global institutions have come into existence in the last six decades, in response to the acceleration of interdependence on a worldwide

[14]Refer to the interview with Lindsey Schoenfelder, Stiglitz, 2002 quoted in Wikipedia at http://en.wikipedia.org/wiki/Washington_Consensus

[15]**Rodrik:goodbye**

scale, both between human societies and between humankind and the biosphere, whose role mainly consists in regulating globalization on a global scale. The first of these, known as international financial institutions, are the International Monetary Fund (IMF) and the World Bank. Both were created around the end of the second world war during the Bretton Woods Conferences. They both aim to ensure financial stability and economic growth around the world.

The IMF specifically focuses on the stability of the international monetary and financial system by monitoring and advising countries on policies that are conducive to their goals, providing technical and even financial assistance.

The World Bank, which cooperates closely with the IMF, promotes long-term economic development and poverty reduction. For example, it builds schools and hospitals, provides clean water and electricity, and helps fighting the spread of epidemics.

By the way, the main actor of globalization itself is the World Trade Organization.

1.4.1 W.T.O. - World Trade Organization

The *World Trade Organization* (hereinafter, WTO) is an organization that intends to supervise and liberalize international trade. The organization officially commenced on January 1st, 1995 under the Marrakech Agreement, replacing the General Agreement on Tariffs and Trade (GATT), which commenced in 1948. The organization deals with regulation of trade between participating countries; it provides a framework for negotiating and formalizing trade agreements, and a dispute resolution process aimed at enforcing participants' adherence to WTO agreements which are signed by representatives of member governments and ratified by their parliaments. The WTO actually consists of 153 members, representing more than 97% of the world's population, and 30 observers, most seeking membership. The organization is currently endeavoring to persist with a trade negotiation called the Doha Development Agenda (or Doha Round)[16].

Doha Development Round

The Doha Development Round or Doha Development Agenda (DDA) is the current trade-negotiation round of the WTO which commenced in November 2001. Its objective is to lower trade barriers around the world, which will help facilitate the increase of global trade. Since 2008 talks have stalled over a divide on major issues, such as agriculture, industrial tariffs and non-tariff barriers, services, and trade remedies. The most significant differences are between developed nations led by the European Union, the United States,

[16]For further reading see Wikipedia definition at http://en.wikipedia.org/wiki/World_Trade_Organization

and Japan and the major developing countries led and represented mainly by Brazil, China, India, South Korea, and South Africa. The most recent round of negotiations, 23–29 July 2008, broke down after failing to reach a compromise on agricultural import rules. During 2011 annual conference of the World Economic Forum in Davos British Prime Minister David Cameron called for the Doha talks to conclude by the end of the year, saying that:

> *We've been at this Doha round for far too long. It's frankly ridiculous that it has taken 10 years to do this deal.*[17]

Similar comments were made by German Chancellor Angela Merkel and former WTO director-general Peter Sutherland[18].

[17] Cameron, 2011

[18] For further reading see Wikipedia definition at http://en.wikipedia.org/wiki/Doha_Development_Round

2 Free movement of capital

> FDI is a key driver of international economic integration.
> With the right policy framework, FDI can provide financial stability, promote economic development and enhance the well being of societies.
>
> OECD, 2008, p. 4

The liberalization of capital markets around the globe has meant that increasingly wealth flows freely across borders and giant global corporations can invest where they want, namely wherever they stand the chance of reaping profits. It is this growth of foreign direct investment more than anything else that characterizes the new era and distinguishes it from the previous periods.
As with many of the other aspects of globalization, foreign investment is raising many new questions about economic, cultural, and political relationships around the world. Flows of investment and rules which govern or fail to, can have profound impacts upon such diverse issues as economic development, environmental protection, labour standards, and economic and political stability.

2.1 F.D.I. - Foreign Direct Investment

Foreign direct investment reflects the objective of establishing a lasting interest by a resident enterprise in one economy (*direct investor*) in an enterprise (*direct investment enterprise*) that is resident in an economy other than that of the direct investor. The lasting interest implies the existence of a long-term relationship between the direct investor and the direct investment enterprise,

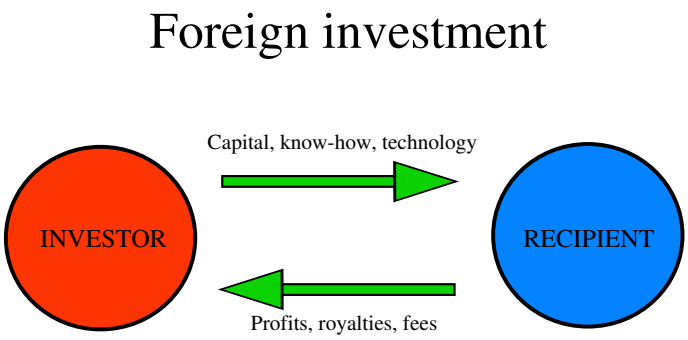


Figure 2.1: Source: The Levin Institute, 2011.

and a significant degree of influence on the management of the enterprise.[1] The direct or indirect ownership of 10% or more of the voting power of an enterprise resident in one economy by an investor resident in another economy is evidence of such a relationship.[2] FDI is calculated to include all kinds of capital contributions, such as the purchases of stocks, as well as the reinvestment of earnings. These latter along with transfer of assets between a parent company and its subsidiary, often constitute a significant part of FDIs level. Figure 2.1 shows such a mechanism. When people think about globalization, they often first refer to the increasing volume of trade in goods and services. Trade flows are indeed one of the most visible aspects of globalization. But many analysts argue that international investment is a much more powerful force in propelling the world towards closer economic integration. Investment can alter entire methods of production through transfers of knowledge, technology, and management techniques, and thereby can initiate much more change than the simple trading of goods. Over the past years, foreign investment has grown at a significantly more rapid pace than either international trade or world economic production generally.
Dunning[3] has identified four primary reasons for corporate foreign investments:

1. *Market seeking*: Firms may go overseas to find new buyers for their goods and services.

2. *Resource seeking*: The foreign facility may be able to obtain superior or less costly access to the inputs of production (land, labour, capital, and natural resources) than at home.

3. *Strategic asset seeking*: Firms may seek to invest in other companies

[1] OECD, 2008, p. 48

[2] Somebody may argue that in some cases an ownership of as little as 10% of the voting power may not lead to the exercise of any significant influence while on the other hand, an investor may own less than 10% but have an effective voice in the management. Nevertheless, the recommended methodology does not allow any qualification of the 10% threshold and recommends its strict application to ensure statistical consistency across countries.

[3] Dunning, 2002 Chapter 6

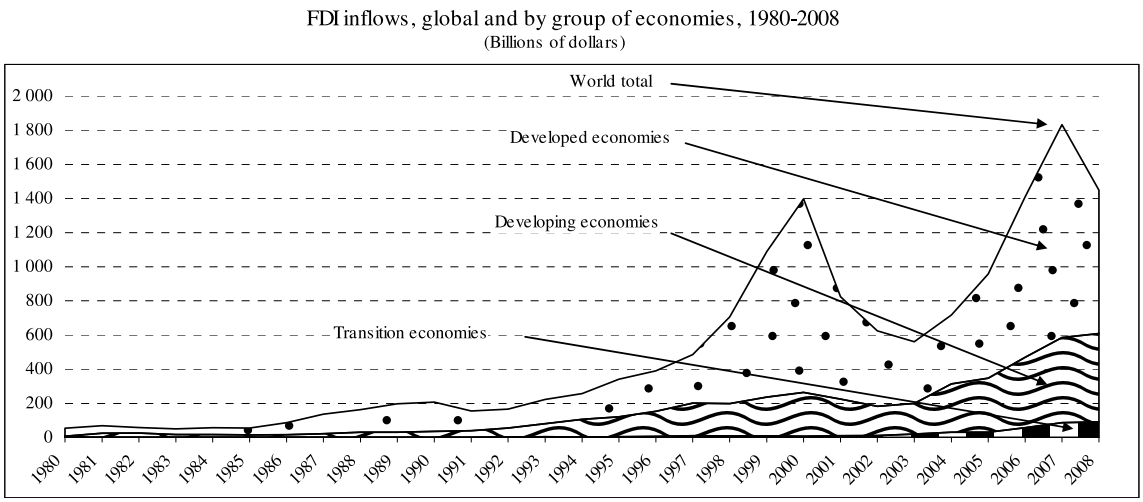


Figure 2.2: Source: UNCTAD, 2009.

abroad to help build strategic assets, such as distribution networks or new technology.

4. *Efficiency seeking*: Multinational companies may also seek to reorganize their overseas holdings in response to broader economic changes. Fluctuations in exchange rates may also change the profit calculations of a firm, leading the firm to shift the allocation of its resources.

The tremendous growth in levels of foreign direct investment is a recent phenomenon and is one of the most powerful effects, and causes, of globalization. In 1982 the global total of FDI flows was $57 billion. By the end of 2007 it reached $1.5 trillion, breaking the record established in 2000, nearly 30 times the level 25 years earlier (see figure 2.2).

Due to the recent global financial and economic crisis, however, FDI flows have decreased to an estimated $1.4 trillion in 2008. According to the UNCTAD[4], the global expansion of FDIs is currently (2007) being driven by over 79,000 transnational corporations with more than 790,000 foreign affiliates, generating 82 million jobs, representing an estimated 11% (around $31 trillions) of global GDP in 2007, one fifth of which representing exports.

2.1.1 Foreign Investment and Labour Market

In the classical view, capital flows induced by foreign investments lead to the creation of new jobs, through the mechanism illustrated in figure 2.3 on the following page. A positive side effect of helping entrepreneurs get started is the creation of jobs, which leads to increased income levels and thereby to increased consumer demand. Such demand in turn triggers opportunities for other enterprises and, through this multiplier effect, the capital that comes

[4]UNCTAD, 2008b, p. 9 and following statistical data

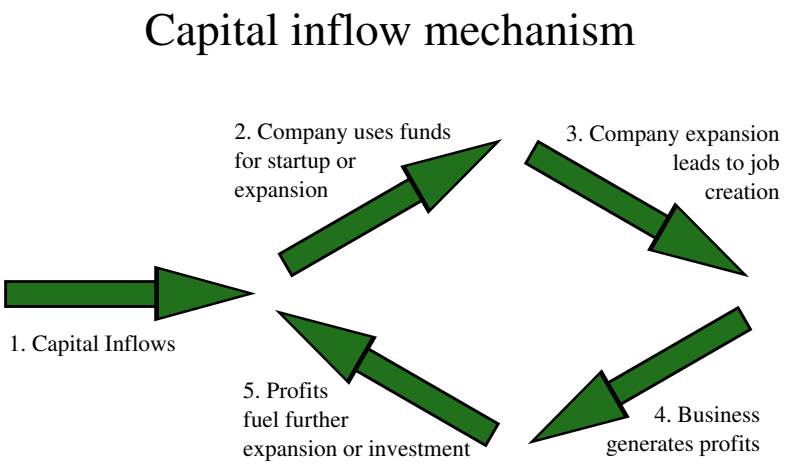


Figure 2.3: Source: The Levin Institute, 2011.

with foreign investment often helps produce economic growth. This pattern applies in both developed and developing countries[5].

The world's largest recipient of foreign investment is the United States. Over the past several decades, the hundreds of billions of dollars of foreign capital that has been invested in the United States has been of tremendous benefit to the U.S. economy, strengthening the dollar, and helping to bring down interest rates by increasing the supply of capital for loans to business and individuals.

During the last couple of decades, major trade liberalization reforms have been carried out in developing countries too, especially in Latin America, North Africa and South and South-East Asia. Available evidence shows that, during and after most of the trade liberalization episodes, there was not a major contraction in manufacturing employment. A cross-country analysis[6] of a series of case studies, conclude that trade liberalization in developing countries in general does not result in employment losses even in the short run. The results of their analysis are summarized in figure 2.4 on the next page. Manufacturing employment was higher after liberalization in 12 out of the 13 cases reported, the exception being Chile.

2.2 F.P.I. - Foreign Portfolio Investment

Foreign portfolio investment, on the other hand, is a category of investment instruments that are more easily traded, may be less permanent, and do not represent a controlling stake in an enterprise. These include investments via equity instruments (*stocks*) or debt (*bonds*) of a foreign enterprise that does not necessarily represent a long-term interest.

[5] The Levin Institute, 2011

[6] Papageorgiou, Choksi, and Michaely, 1990 quoted in Turrini, 2002

Employment in manufacturing during episodes of liberalization
(Thousands of workers)

Episode	Year before liberalization	Average for liberalization period	Year after liberalization
Argentina 1 (1967-1970)	1 836	1 847	1 914
Argentina 2 (1976-1980)	1 863	2 099	2 132
Brazil (1965-1973)	1 780	2 182	3 397
Chile 2 (1974-1981)	515	487	351
Peru (1979-1980)	675	717	736
Philippines 1 (1960-1965)	1 456	1 647	1 825
Philippines 2 (1970-1974)	2 056	2 313	2 596
Rep. of Korea 2 (1978-1979)	2 000	2 196	2 099
Singapore (1968-1973)	61	139	210
Sri Lanka 1(1968-1970)	74	108	97
Sri Lanka 2 (1977-1979)	112	134	155
Turkey 1 (1970-1973)	485	551	651
Turkey 2 (1980-1984)	799	829	n.a.

Figure 2.4: Source: Papageorgiou, Choksi, and Michaely, 1990 quoted in Turrini, 2002.

Until the 1980s, commercial loans from banks were the largest source of foreign investment in developing countries. However, since that time, the levels of lending through commercial loans have remained relatively constant, while the levels of global FDIs and FPIs have increased dramatically. Over the period 1991-1998, they comprised 90 percent of the total capital flows to developing countries. Over the period 1996-2006, investment outflows from the United States more than doubled.[7] According to IMF regional statistics, nations in Latin America, the Middle East, and Europe relied mostly on FPIs as the source for capital flows, Asia received most of its investment from FDIs, and Africa received most of its capital inflows from development assistance.

2.2.1 Volatility

The difference between FDI and FPI can sometimes be difficult to discern, given that they may overlap, especially in regard to investment in stocks. One of the most important distinctions between portfolio and direct investment to have emerged from this young era of globalization is that portfolio investment can be much more volatile. Changes in the investment conditions in a country or region can lead to dramatic swings in portfolio investment. For a country on the rise, FPIs can bring about rapid development, helping an emerging economy move quickly to take advantage of economic opportunity, creating new jobs and significant wealth. However, when a country's economic situ-

[7]For more detailed statistical data refer to IMF, 2007

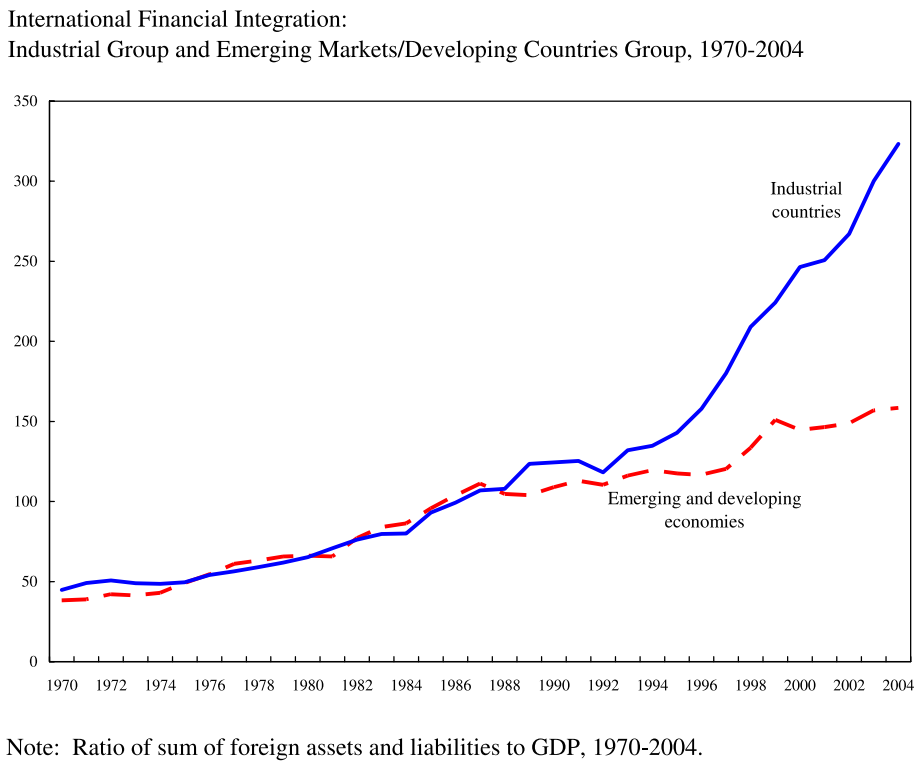


Figure 2.5: Source: Lane and Milesi-Ferretti, 2006, p. 35.

ation takes a downturn, sometimes just by failing to meet the expectations of international investors, the large flow of money into a country can turn into a stampede away from it. By contrast, because FDI implies a controlling stake in a business, and often connotes ownership of physical assets such as equipments, buildings, and real estate, FDI is more difficult to pull out or sell off. Consequently, direct investors may be more committed to managing their international investments, and less likely to pull out at the first sign of trouble. This volatility has effects beyond the specific industries in which foreign investments have been made. Since capital flows can also affect the exchange rate of a nation's currency, a quick withdrawal of investment can lead to rapid decline in the purchasing power of a currency, rapidly rising prices, hence inflation. In short, such quick withdrawals can produce widespread economic crisis.

2.2.2 Interconnectedness between national economies

The rapid financial globalization of the past three decades, reflected in the seven-fold increase in the external assets and liabilities of nations as a share of GDP[8], has been accompanied by an increase in financial interconnectedness (see figure 2.5). Countries have become more and more inter-linked with each

[8] Lane and Milesi-Ferretti, 2006, p. 15

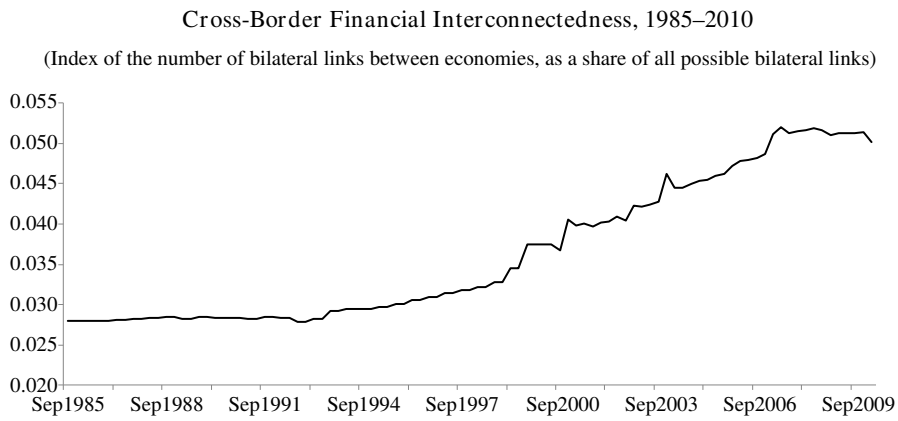


Figure 2.6: Source: Moghadam and Viñals, 2010, p. 4.

other[9], particularly since the mid-1990s, as the asset and liability management (ALM) strategies of their sovereigns, financial institutions, and corporations have become increasingly global in nature (see figure 2.6). Globalization has brought benefits, such as a wider choice for consumers and operators, more efficient intermediation of savings, and pooling of risks. It has also brought vulnerabilities. Countries are financially interconnected through the ALM strategies of their sovereigns, financial institutions, and corporations. The speed with which illiquidity and losses in some markets can translate into global asset re-composition is evidence both of the risks associated with interconnectedness and of the efficiencies of the transmission and intermediation process. Shocks in one part of the system can be amplified and transmitted through common intermediaries pursuing global ALM strategies that collectively become overexposed to risk in the upswing of a credit cycle and overly risk-averse in a downswing. Understanding the nature of these interconnections is essential for tracking the build-up of systemic risk concentrations, identifying the fault lines along which financial shocks propagate, and enhancing macro-prudential surveillance and policy making.

The global financial system is highly concentrated. Global financial intermediation is carried out predominantly by about 20 key large complex financial institutions[10] (hereinafter LCFIs), operating in a handful of jurisdictions and transacting over a few payments and settlement platforms (see figure 2.7 on the following page). They dominate the markets for debt, equity securities, syndicated loans, securitization, structured financial products, and OTC derivatives. They comprise bank as well as non-bank institutions, such as investment banks, money market funds, and structured investment vehicles (SIVs). They are the main counterparties for large insurers and some of the biggest broker dealers. Shadow institutions, associated with the LCFIs in the

[9] Moghadam and Viñals, 2010, p. 4

[10] The term large complex financial institution was coined by the Bank of England and refers to those institutions that are among the largest participants in a number of capital market activities measuring relative business size.

Key LCFIs

(Defined by top book runners)

		International Bonds	Structured Finance	US ABS	Syndicated Loans	Equities		
		(All currencies)	All Intl Issuers			Asia-Pacific	Europe/Middle East/Africa	US
Institution	Country	Rank	Rank	Rank	Rank	Rank	Rank	Rank
JPMorgan Chase 1/	US	1	2	3	1	8	1	1
Barclays Bank PLC	UK	2	3	1	15			7
Deutsche Bank AG	Germany	3	9	5	8		4	10
Bank of America	US	4	4	2	2	6	3	4
HSBC	UK	5	6		24		10	
Credit Suisse Group	Switzerland	6		7	18			6
Citigroup 1/	US	7	7	4	6	4	7	9
UBS	Switzerland	8						
BNP Paribas	France	9			7			
RBS	UK	10	5	6	12		9	
Goldman Sachs	US	11		10	13	1	2	3
Morgan Stanley	US	12		8	22	10	6	2
Credit Agricole SA	France	14			9		5	
Lloyds Banking Group	UK		8					
Rabobank	Netherlands		10					
Wells Fargo	US			9	10			8
State Street 1/	US							
BNY Mellon 1/	US							

1/ Some of the largest holders of custody assets.

Figure 2.7: Source: Moghadam and Viñals, 2010, p. 8.

run up to the crisis, typically borrowed short term, such as in money market and commercial paper markets, to invest longer term in instruments such as mortgage-backed securities.[11] Growth in financial institutions' indebtedness to other financial institutions was the key cause of interconnectedness, which linked the fortunes of many financial institutions to the performance of only a few of the largest banks.

[11] Moghadam and Viñals, 2010, pp. 6-8

3 Free movement of goods

> Trade is not the cause of the current economic crisis, but is likely to be one of its most important casualties.
>
> Steven Yeo, in Baldwin and Evenett, 2009, p. vii

Trade is the mechanism through which growth and prosperity are transmitted between countries[1]. Every day billions of dollars of goods and services are bought and sold around the world, giving consumers access to new products and generating wealth and prosperity for the people and businesses that make them. According to OECD analysis[2], a 10% increase in trade is associated with a 4% rise in per capita income.

The G20 Summit held in November 2008 recognized[3] '*the critical importance of rejecting protectionism and not turning inward in times of financial uncertainty*' and pledged to '*refrain from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing World Trade Organization (WTO) inconsistent measures to stimulate exports*' and agreed to '*strive to reach agreement this year on modalities that leads to a successful conclusion to the WTO's Doha Development Agenda*'.

3.1 Murky protectionism

There is a broad consensus among economists that protectionism is not welfare-enhancing. However, the perception that free trade has a favourable effect on growth and ultimately benefits all participants is not always shared among the

[1] S. Crean in Baldwin and Evenett, 2009, p. 23
[2] OECD, 2010
[3] Leaders of the Group of Twenty, 2008

general public, and calls for protectionism are not rare in the policy debate, particularly in times of economic and financial stress. This concern is raised, in particular, by the contemporary crisis during which protectionist pressures are presumably mounting and by the failure to complete the Doha Round of trade negotiations according to schedule.

Protectionism entails substantial long-run costs. The general case for free trade was made as early as the nineteenth century by classical economists such as David Ricardo, who focused on the notion of comparative advantage. Using a simplified representation of two economies with two sectors each, Ricardo showed that both countries were better off if each specialized and traded in the sector where it had a comparative advantage (*i.e.* higher productivity)[4].

3.1.1 Evidence from the past

Times of economic and financial stress seem to be particularly conducive to protectionist policies. This is suggested by several historical episodes; for example, many governments resorted to protectionist measures in the wake of the 1929 financial crisis in an effort to shield their domestic economies from the effects of the Great Depression. Such measures included higher import tariffs[5] but also exchange rate devaluations aimed at gaining export price competitiveness at the expense of trading partners (also known as *beggar-thy-neighbour* policies). This considerably hampered trade flows, which fell by 66% between 1929 and 1933[6]. While these policies failed to deliver economic prosperity in the countries that initiated them, they also triggered a spiral of reactions across countries, which contributed to the rise in nationalism in Europe and the rest of the world. The widespread perception that protectionist policies were not successful and led to rising tensions across countries explains to a large extent the fact that the world has experienced a clear trend towards globalization since the Second World War. Recently, however, the question has arisen as whether the trend towards free trade, that has been observed in recent decades, will come to a halt or even be reversed.

Mexican former President Ernesto Zedillo claims[7]:

> *What we do know with certainty is that protectionism could derail all those efforts applied on the fiscal and monetary fronts. Despite the multitude of statements against protectionism made by leaders and their finance and trade ministers in recent months, it would be irresponsible not to recognize that the mercantilist spectre is knocking at everybody's door. Unfortunately, as the recession gets worse, protectionist forces will become even stronger. A perverse*

[4]For the original literature refer to Ricardo, 1817

[5]In the United States, tariffs were raised sharply on a wide range of goods following the Smoot-Hawley Tariff Act of 17 June 1930.

[6]For a detailed account of protectionism during the Great Depression, see Kindleberger, 1986

[7]TAIT Lecture delivered at the The Graduate Institute, Geneva on February 24th, 2009, quoted in Baldwin and Evenett, 2009, p. 15

cycle of feedback between recession and protectionism is no longer an historical reminiscence of the 1930s but a possible scenario now in the months and years to come. We could soon find ourselves regretting how little, or in fact nothing, states have done to improve the institutions created mostly in the second half of the 20th century to manage the process of global integration. For it is a fact that in the last ten years as globalization accelerated dramatically, the process of international reform stalled.

3.2 Assessing global trends in protectionism

> We are still far from the day when we buy from across the globe as easily as across the country.
>
> FRANKEL, 2000, p. 4

Barriers to trade in goods and services can be divided into two broad categories: quantitative and qualitative. The former include mainly tariffs, but also import quotas and limitations, subsidies and exchange controls. Such barriers are relatively straightforward to measure, in part because they are usually publicly announced. Qualitative barriers are more difficult to detect. These consist in government policies and regulations that directly or indirectly hinder free trade. They include, for instance, competition policy, industrial policy, discriminatory treatment towards foreign capital, customs valuation and classification, industrial standards and quality standards[8].

3.2.1 Tariff measures

Average import tariffs on manufactured goods have declined in recent years. According to the United Nations Conference on Trade and Development[9] tariffs fell over the period 1990-2006 in both the major advanced economies (the United States, the EU and Japan) and in large emerging economies such as Brazil, Russia, India and China (often referred to as the BRICs[10])(see figure 3.1 on the next page). Tariffs are still markedly higher in the emerging economies, but the gap between advanced and emerging economies has been decreasing over time. However, one needs to take into account the fact that emerging markets have gained market share since 1990. For instance, the BRICs accounted for around 5% of world trade in 1990, against nearly 14%

[8] ECB, 2009, pp. 85-100

[9] UNCTAD, 2008a, pp. 222-240 quoted in ECB, 2009

[10] The concept (together with the acronym) was introduced by the bank Goldman Sachs in the early 2000s. These countries are usefully considered together given their large economic and demographic size, their systemic importance and their strong growth performance.

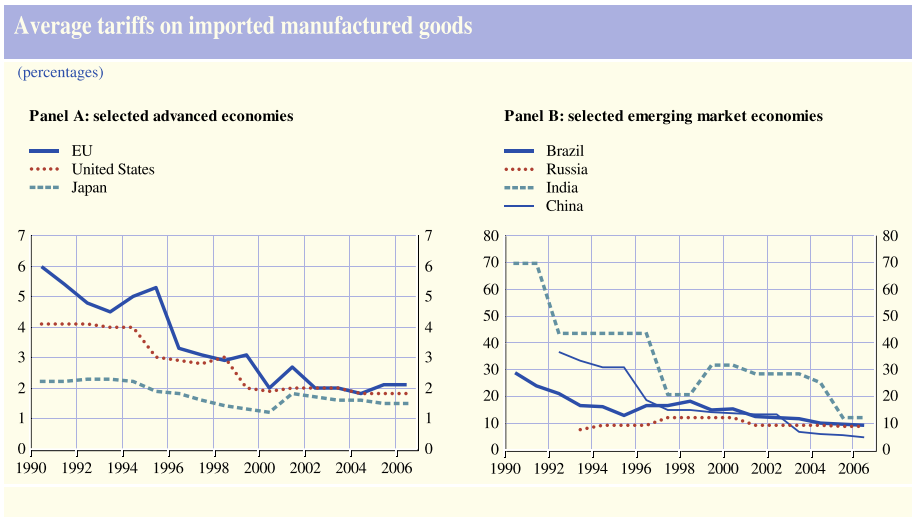


Figure 3.1: Source: ECB, 2009, p. 91 based on UNCTAD, 2008a data.

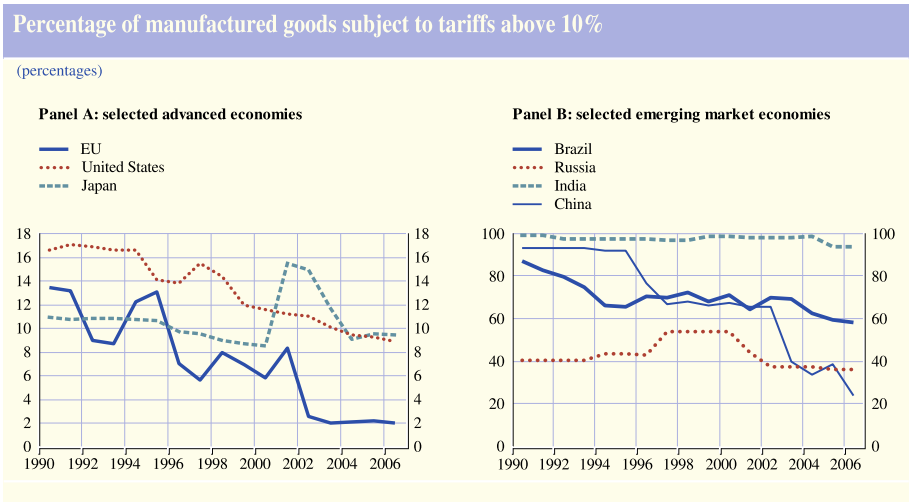


Figure 3.2: Source: ECB, 2009, p. 92 based on UNCTAD, 2008a data.

now, the counterpart of this rise being a fall in the market share of advanced economies. The growing market share of the BRICs, whose tariffs are higher, may therefore increase perceived protectionism. In addition, progress in tariff reduction has varied considerably across sectors, and developments in average tariffs may hide significant differences in the treatment of individual products. A declining average may be misleading if countries maintain very high tariffs on certain strategic products (see figure 3.2). The distribution of tariffs across countries is characterized by an important difference between the emerging market economies, where around 60% of tariffs are above 10%, and the advanced economies, where this share is below 20%. Although emerging economies have been reducing average tariff levels, they still apply high tariffs to most manufactured goods.

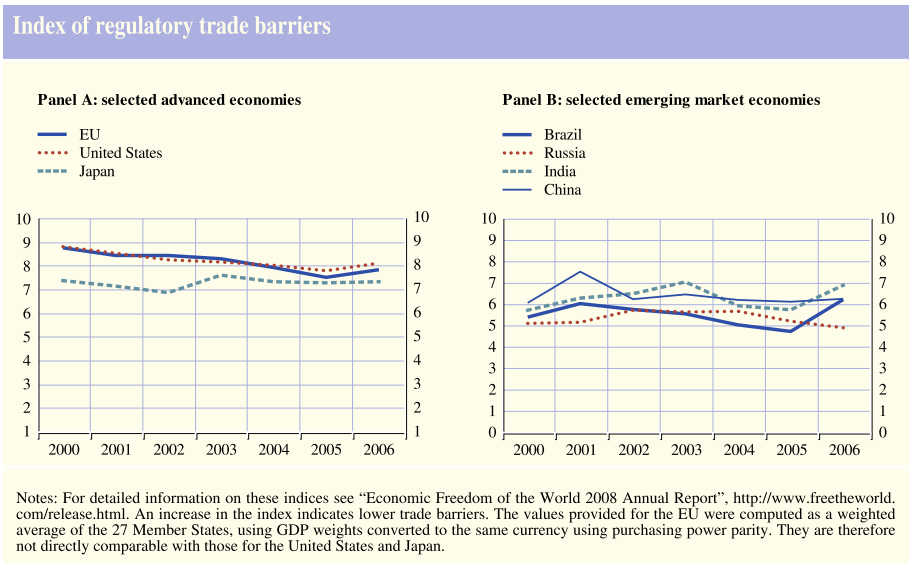


Figure 3.3: Source: ECB, 2009, p. 93 based on Fraser Institute data.

3.2.2 Non-tariff measures

Tariffs provide only a very partial indication of the degree of protectionism. Countries are unlikely to increase tariffs by a large amount as these are capped through international agreements in the context of the WTO. Protectionist measures are more likely to come in the form of non-tariff measures, which are more difficult to quantify. Such barriers include export subsidies, which should, theoretically, be easy to quantify. But subsidies can also take very indirect forms (such as funding for research programs that enhance productivity). Alternatively, they can be aimed at supporting local producers against foreign competitors. As non-tariff measures include various government policies and regulations that cannot be quantified directly, official data on this type of barrier are indeed very scarce and mainly confined to cross-country comparisons at a given point in time, which does not allow an assessment of trends over time. Some private sector institutions provide quantified indices based on surveys, such as the ratings developed by the Fraser Institute. Although these measures are subject to caveats, they constitutes useful proxies to assess non-tariff barriers. Indicators provided by the Fraser Institute suggest that non-tariff barriers have remained broadly stable in both advanced and emerging economies since the early 2000s (see figure 3.3). The conclusion may be that policymakers are led to lower specific trade barriers that can easily be calculated (tariff ones) and to maintain the others untouched (non-tariff ones).

Figure 3.4: Source: ECB, 2009, p. 98 based on WTO data.

3.2.3 Trade agreements

Indirect measures of protectionism are more difficult to quantify, but they can be gauged by considering a range of unofficial indicators.

One important factor that suggests a rise in protectionist pressures is the fact that multilateral trade negotiations have not proceeded as planned and have given rise to market disagreement between key global trading partners. As already stated[11], first in July 2006 and subsequently in July 2008, the Doha Round was indefinitely suspended; it still remains unclear whether negotiations will resume.

A further indirect measure of protectionist pressures is the proliferation of regional trade arrangements (RTAs) over time. While promoting free trade, such agreements do so at regional or bilateral level rather than at global level and can therefore be seen as an obstacle to free global trade (see figure 3.4). Other examples of murky protectionism witnessed in recent months are not direct violations of WTO obligations. The system has been challenged not only by what countries have failed to do, but also by the damage they have done through the proliferation of discriminatory trade agreements (DTAs) that for the most part run head on against the essential principles of reciprocity and non-discrimination upon which the entire system should rest. They are abuses of legitimate discretion which are used to discriminate against foreign goods, companies, workers and investors. Examples include abuses of health and safety regulations, and clauses in stimulus packages that confine spending to

[11] Cfr. Chapter 1

Support for globalisation in selected regions of the world

(percentage of positive answers to the question "Is trade with other countries good?")

	2002	2007	Variation
United States	78%	59%	-19
EU[1)]	87%	77%	-9
Latin America[2)]	76%	76%	0
Asia[3)]	84%	83%	-1
Africa[4)]	91%	87%	-3

Note: Figures may not add up due to rounding.
1) Arithmetic average of Germany, France, Italy and the United Kingdom.
2) Arithmetic average of Argentina, Bolivia, Mexico, Brazil, Peru and Venezuela.
3) Arithmetic average of Bangladesh, Pakistan, China, India, Japan, Korea and Indonesia.
4) Arithmetic average of Kenya, Ghana, Tanzania, South Africa, Côte d'Ivoire, Nigeria and Uganda.

Figure 3.5: Source: ECB, 2009, p. 99 based on Pew Global Attitudes Project, 2007 data.

domestic producers. DTAs have taken attention and political capital that could have been used to improve the multilateral system and, by aggravating the discrimination instilled in trade preferences, they have made the hurdles to achieve much higher multilateral agreements.

3.2.4 Evidence from survey data

Turning now to evidence from survey data, globalization is perceived differently across countries and population segments. Even though surveys are carried out using a small sample of the population, they still provide a useful indicator of the general perception of this phenomenon. The Pew Global Attitudes Project[12] shows support for trade globalization to be falling significantly in the EU and the United States, and by a smaller amount in emerging market economies and developing countries (see figure 3.5). In fact, support for trade globalization seems to be high in emerging market economies and developing countries (particularly in Asia and Africa, with above 80% of the population agreeing with the statement that trade with other countries is good). As regards the rest of the world, globalization finds wide support in Asia, notably China, Korea and Thailand (with, respectively, 87%, 86% and 75% of the population supporting globalization)[13]. This support is somewhat lower in India (54%). In 2008[14], 39% of EU citizens considered globalization "a good oppor-

[12] Pew Global Attitudes Project, 2007 quoted in ECB, 2009

[13] The Chicago Council on Global Affairs, 2007, p. 8 quoted in ECB, 2009

[14] This and other interesting statistic data are available in European Commission, 2008, p. 33 quoted in ECB, 2009

tunity for national companies thanks to the opening-up of markets", while 43% considered it a "threat to employment and national companies" and 18% responded "don't know".

Finally, surveys among business leaders suggest that protectionism is perceived as a significant threat. In a comprehensive survey of more than 500 global business leaders by *The Economist* in autumn 2006, almost half of the respondents indicated that protectionist measures were increasing.

4 Free movement of people

Many critics of trade liberalization, such as Noam Chomsky, Tariq Ali, Susan George, and Naomi Klein, see globalization as a way to open the labour market of underdeveloped economies to exploitation by companies from more developed economies. The prescribed reductions in tariffs and other trade barriers allow the free movement of goods across borders according to market forces, but labour is not permitted to move freely due to the requirements of a visa or a work permit. This creates an economic climate where goods are manufactured using cheap labour in underdeveloped economies and then exported to rich First World economies for sale at what the critics argue are huge markups, with the balance of the markup said to accrue to large multinational corporations. The criticism is that workers in the Third World economy nevertheless remain poor, as any pay raises they may have received over what they made before trade liberalization are said to be offset by inflation, whereas workers in the First World country become unemployed, while the wealthy owners of the multinational grow even more wealthy.

4.1 Labour market

During the last 20 years, a generalized reduction in the aggregate demand for labour paralleled the developments in international trade. The unemployment rate has been growing on average across countries. The increase in unemployment has been more substantial in developed countries. While in the average OECD country the unemployment rate grew by more than 2% between 1980 and 1997, in the average non-OECD country unemployment grew by less than half a percentage point. The share of wage income in total income has also been falling on average. The fall, again, is more substantial in developed economies. These aggregate figures, however, mask important differences across countries. Within developed countries (aggregate) labour demand has been falling more substantially in continental Europe; within developing countries, Latin America and sub-Saharan Africa experienced the

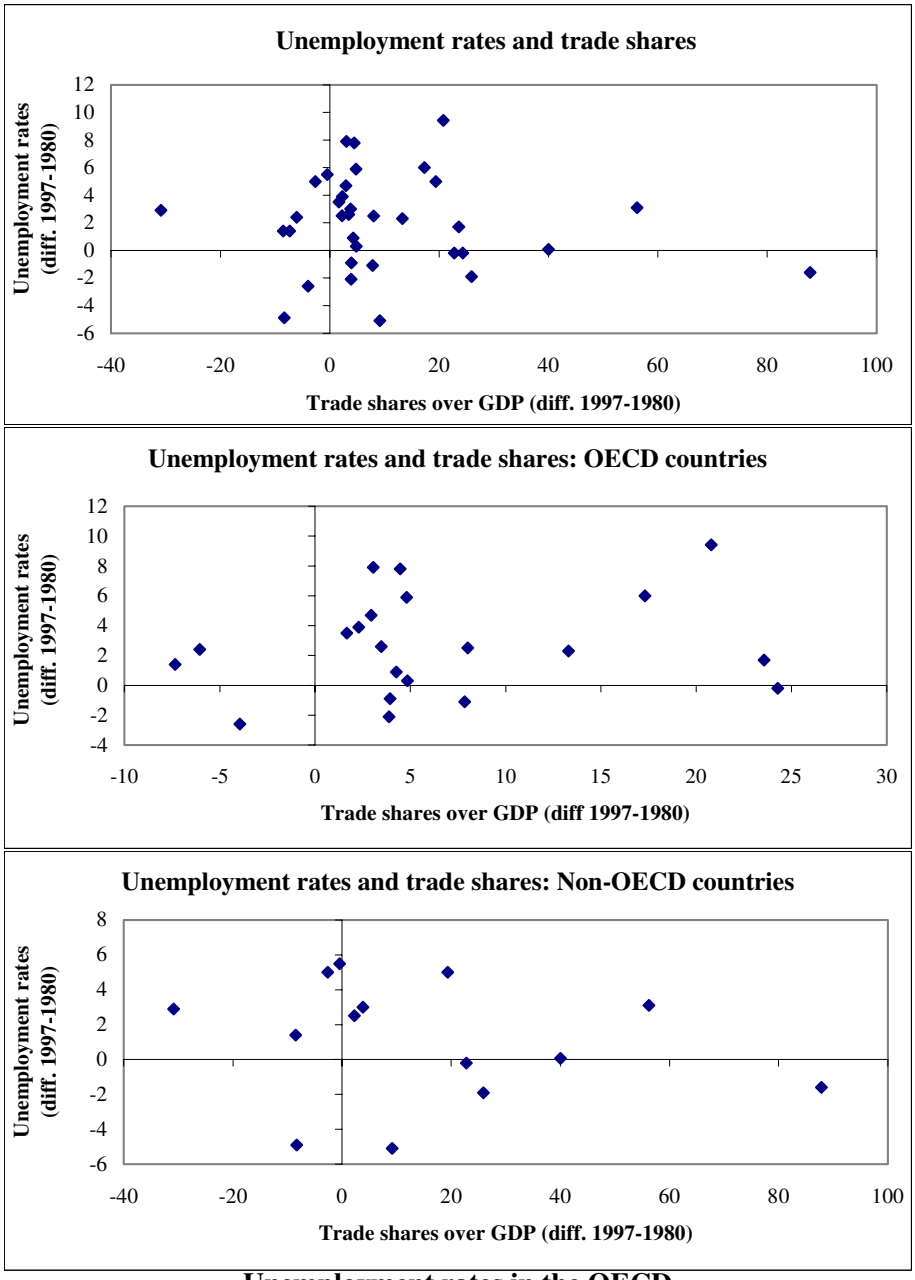
major employment losses.

Figure 4.1 on the facing page illustrates the cross-country relationship between changes in trade openness (as measured by the ratio of trade to GDP) and unemployment rates over the period 1980-1997, as calculated by Turrini[1]. When the sample includes all countries, the relationship appears very weak (the correlation coefficient between the two variables is close to zero). If the sample is restricted, respectively, to OECD and non- OECD countries a clearer pattern emerges. In OECD countries there is a slight positive correlation between changes in trade openness and unemployment (with a correlation coefficient of 0.16), whereas the correlation is negative for non-OECD countries (with a coefficient of -0.5). A similar pattern is observed with regard to the wage share in total income (see figure 4.2 on page 36). For the whole sample of countries, the correlation between changes in trade openness and wage share is very weak, while for OECD countries it is negative (-0.3) and for non-OECD countries it is slightly positive (0.11). The co-evolution of unemployment rates and wage shares of income can be attributed to many different factors. However, there is a *prima facie* indication that the effects of growing trade integration on labour demand may have been quite different in developed and developing countries, that is to say, while increased trade is coupled with falling labour demand in developed countries, this does not seem to be the case in developing countries.

4.2 Immigration and unemployment in Europe

Does Europe's economy need immigrant workers? It has to be said that with the spectre of demographic ageing and the ongoing recruitment problems in certain sectors where growth is dependent on a plentiful supply of skilled workers, the issue of migration is once again back at the very heart of public debate. As the European Commission says, immigration is both a challenge and an opportunity for the European Union. In a context of Europe's ageing societies and growing market needs, the demand for immigrants is set to increase. Europe will probably have to rely more on immigration to balance supply and demand on the labour markets and, more broadly, to support its economic growth. Identifying the labour needed and selecting the immigrants to meet those needs is the strategy currently governing Europe's immigration policy. Yet, with an unemployment rate of almost 8% among its resident population in 2005, and unemployment among non-EU nationals almost twice as high, we have to question whether there really is a demand for labour in Europe that immigrants might fill. Are immigrants capable of meeting the manpower needs of Europe's economies? Does immigration influence the employment conditions of native workers, and if so, to what extent?

[1] Turrini, 2002, pp. 4-8



Unemployment rates in the OECD

	1973	1979	1985	1989	1993
OECD	3.3	5.1	7.8	6.4	8.0
OECD Europe	3.0	5.6	9.9	8.5	10.4
Of which EU	2.7	5.4	10.5	8.7	11.0

Note: Table entries are unemployment rates expressed as percentages.

Figure 4.1: Source: TURRINI, 2002, pp. 5,8.

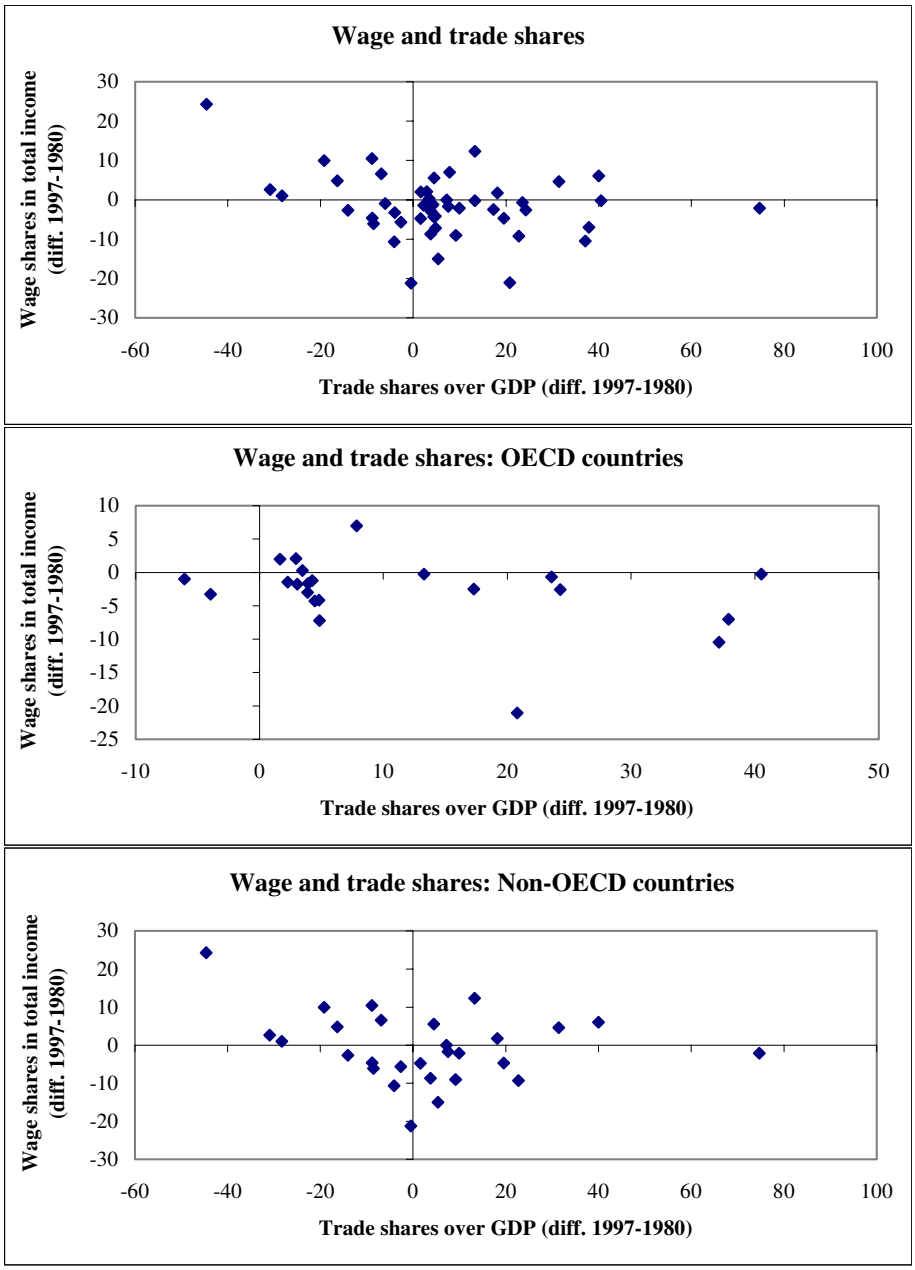


Figure 4.2: Source: TURRINI, 2002, p. 6.

Status of natives and immigrants on the labour market in Europe

	Activity rate[1]		Employment rate[2]		Unemployment rate[3]	
COUNTRY	Natives	Immigrants	Natives	Immigrants	Natives	Immigrants
Austria	73.2	74.2	69.1	65.9	5.6	11.2
Belgium	66.8	56.2	60.4	44.6	9.5	20.6
Czech Republic	74.2	69.8	67.5	60.1	9.0	13.9
Germany	72.9	72.9	67.3	60.5	7.7	17.1
Denmark	82.6	59.3	79.7	54.4	3.5	8.2
Spain	62.1	69.3	53.5	57.7	13.9	16.7
Finland	73.9	62.7	64.8	46.0	12.1	26.6
France	69.2	69.5	61.0	56.0	11.9	19.5
UK	74.3	66.7	70.2	61.2	5.5	8.3
Greece	60.8	70.0	54.1	62.5	11.1	10.7
Hungary	59.0	58.6	53.0	54.6	10.2	6.9
Ireland	67.4	71.1	61.7	63.0	8.5	11.3
Italy	61.8	66.7	54.7	58.0	11.5	13.1
Luxembourg	61.5	70.2	60.0	67.5	2.4	3.9
Netherlands	76.7	64.2	74.7	59.9	2.6	6.7
Norway	74.6	60.8	72.2	55.6	3.1	8.7
Poland	64.8	41.6	51.0	35.8	21.3	14.0
Portugal	70.6	78.3	65.9	72.4	6.7	7.6
Slovak Republic	68.9	66.4	54.0	53.1	21.7	20.0
Sweden	75.8	56.9	73.6	52.4	2.9	7.8

[1] As a percentage of the population aged 15-64.
[2] As a percentage of the population aged 15-64.
[3] As a percentage of the active population aged over 15.

Figure 4.3: Source: KUPTSCH, 2010, p. 56.

Since the unemployment rate in an economy is the weighted average of the unemployment rates in the various categories of workers involved, immigration can affect it in two ways. First, if immigrants have a propensity to unemployment which is different from that of native workers, immigration has a composition effect which alters the average unemployment rate. Secondly, immigration can also affect unemployment rates in individual categories, and more particularly the propensity to employment of workers with productive characteristics similar to those of immigrants[2].

4.2.1 Immigrants' propensity to unemployment

Do immigrants have a different propensity to unemployment from that of native workers in Europe, and if so, why?

In the EU Member States the differences between the employment rates of native and foreign workers are neither on the same scale nor concurrent (see figure 4.3). In the southern countries (Portugal, Spain, Italy, Greece), the employment rate among the immigrant population is noticeably higher

[2] KUPTSCH, 2010, pp. 41-47

than that of the native population; in the Scandinavian countries and Poland the employment rate among native workers is significantly higher than that of immigrants. The differences in employment rates between communities may be explained by the differences between the participation rates and the average unemployment rates of their members. As regards the propensity to unemployment, however, the differences between communities are more or less unequivocal: in all the Member States, except for Poland, Hungary, Slovak Republic and Greece the unemployment rate among immigrant workers is always considerably higher than among their native counterparts. On average, the immigrant unemployment rate is 70% higher than among native workers, with immigrants having more than double the propensity to unemployment of that of native workers in all Scandinavian countries, Belgium, the Netherlands, Austria and Germany. The immigrant propensity to unemployment is thus considerably higher than among native workers in most European countries. The composition effect associated with this structural difference between the native and immigrant populations then helps to increase the average unemployment rate of Europe's economies. There may be two reasons for the differences in employment conditions between native and foreign workers. Firstly, the workers in these two communities may differ in terms of certain productive characteristics influencing productivity and employability. Some foreign workers could also be the victims of discrimination in recruitment: though productively identical, they could actually have less chance of employment. Determining which of these two possibilities applies means that individual productivity must first be estimated. When estimating individual productivity, reference is usually made to certain observable characteristics such as the level of qualification and experience. We must therefore recognize that, assuming that the same level of education gives a native worker and a foreign worker, who has studied in a country with a poorer education system, the same level of skills, may lead us to overestimate the productivity of the immigrant worker and, ultimately, to overestimate the potential scale of discrimination in recruitment. Bearing this reservation in mind, we can measure the relative distribution of the native and immigrant populations by declared level of qualification (see figures 4.4 on the next page, 4.5 on page 40 and 4.6 on page 40). Out of an average calculated for each country, immigrant workers have the same propensity as native workers to have acquired only the most basic level of education. However, there are considerable differences between countries. The proportion of immigrants with the most basic level of education is considerably smaller than for native workers in the southern European countries (Spain, Portugal, Italy, Greece), Hungary, the Czech Republic, the UK and Ireland. On the other hand, the EU Member States are more homogeneous when it comes to the relative share between communities of individuals with a tertiary level of education, immigrants having a 20% higher propensity than native workers, on average. The exception here,

Qualifications and unemployment rates of natives and immigrants in Europe

	Primary education		**Secondary education**		**Tertiary education**	
	Proportion	Unemployment rate	Proportion	Unemployment rate	Proportion	Unemployment rate
Austria						
Natives	33.4	9.9	55.7	5.1	10.9	2.2
Immigrants	49.4	14.0	33.9	9.4	11.3	6.7
Belgium						
Natives	46.5	14.1	30.1	9.8	23.3	4.5
Immigrants	53.3	26.5	23.8	20.8	23.0	12.2
Czech Rep.						
Natives	22.6	24.6	67.0	8.1	10.2	2.5
Immigrants	38.6	31.1	48.7	9.8	12.8	4.2
Germany						
Natives	24.2	11.9	56.5	8.2	19.3	3.9
Immigrants	45.8	21.6	39.3	15.0	14.9	12.7
Denmark						
Natives	37.6	5.1	42.6	3.3	19.9	2.2
Immigrants	36.9	10.7	39.2	7.8	23.9	6.0
Spain						
Natives	66.4	16.2	15.6	12.5	18.0	9.6
Immigrants	56.3	17.8	22.6	17.1	21.1	13.4
Finland						
Natives	40.3	18.7	36.3	13.0	23.4	5.7
Immigrants	52.6	27.4	28.5	27.5	18.9	23.9
France						
Natives	45.8	17.1	37.4	11.5	16.9	6.5
Immigrants	54.8	24.1	27.2	18.8	18.1	11.9
UK						
Natives	51.2	7.3	28.7	5.1	20.1	2.9
Immigrants	40.6	11.3	24.5	8.8	34.8	5.6
Greece						
Natives	52.5	10.7	33.5	13.2	14.0	7.8
Immigrants	42.7	10.8	41.4	10.9	15.9	10.0
Hungary						
Natives	45.1	19.2	44.2	9.0	10.7	2.2
Immigrants	41.1	11.1	39.1	7.8	19.8	2.9
Ireland						
Natives	47.8	14.6	29.5	6.0	22.7	3.5
Immigrants	29.6	18.1	29.3	11.1	41.1	7.5

Figure 4.4: Source: KUPTSCH, 2010, p. 58.

Qualifications and unemployment rates of natives and immigrants in Europe

	Primary education		**Secondary education**		**Tertiary education**	
	Proportion	Unemployment rate	Proportion	Unemployment rate	Proportion	Unemployment rate
Italy						
Natives	63.6	13.6	28.3	10.6	8.1	6.4
Immigrants	54.3	14.4	33.5	12.6	12.2	9.5
Luxembourg						
Natives	28.7	5.5	58.6	2.2	12.8	0.7
Immigrants	36.7	4.0	41.6	4.4	21.7	2.7
Netherlands						
Natives	40.5	4.3	40.6	2.1	18.8	1.5
Immigrants	49.2	9.7	31.6	5.0	19.2	4.3
Norway						
Natives	20.3	4.2	56.7	3.6	23.0	1.8
Immigrants	18.3	10.2	51.2	9.7	30.5	4.7
Poland						
Natives	31.2	29.6	58.4	22.7	10.4	6.9
Immigrants	47.9	15.0	40.3	17.8	11.9	6.6
Portugal						
Natives	80.0	7.2	12.2	6.9	7.7	3.2
Immigrants	54.7	8.8	25.9	8.1	19.3	4.4
Slovak Republic						
Natives	28.0	49.7	61.4	20.3	10.6	5.3
Immigrants	29.3	44.4	55.0	18.3	15.7	5.4
Sweden						
Natives	25.0	4.1	52.2	3.2	22.8	1.7
Immigrants	29.5	10.3	46.2	7.9	24.3	6.4

Figure 4.5: Source: KUPTSCH, 2010, p. 59.

Relative distribution of natives and immigrants by level of qualification

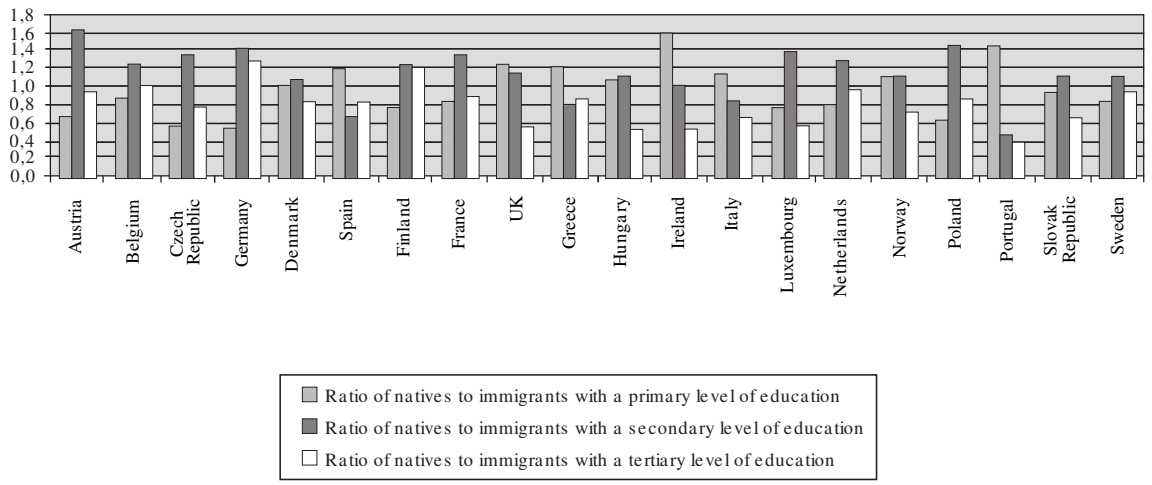


Figure 4.6: Source: KUPTSCH, 2010, p. 60.

however, is Germany, where the proportion of individuals with a tertiary level of education is almost a third higher among native workers. The selectivity of immigration with regard to qualification depends both on the demand for immigrants from the host countries and on the supply of immigrants from the countries of departure. In the host countries some of the factors involved are specific to the countries in question, linked to their colonial past or an immigration policy which may select potential immigrants on the basis of their qualifications. By contrast, when it comes to the supply of immigrants, the results of most empirical studies are unequivocal: the emigration rate among skilled workers is always much higher than among the total population, particularly in the least developed countries. Migration entails financial costs associated with transport and finding accommodation and a job, costs which people must be able to afford. It also entails psychological costs in being far from family and friends and inherent adaptation and integration problems. These financial and psychological costs decrease with the level of qualification. Skilled workers have, on average, a larger income, making it easier to fund migration, and a denser network of acquaintances, making it easier to find accommodation and employment; they also more often speak a foreign language, making it easier for them to adapt to a new environment. If we look at unemployment rates by level of qualification among the native and immigrant populations, we can see that for both communities the propensity to unemployment generally decreases with the level of qualification, though this link is more marked for native workers. Secondly, for any given level of qualification, the unemployment rate among foreigners is always substantially higher than among native workers. While there is no denying that discriminatory practices exist, it should be noted that certain characteristics, usually not observed, affecting workers' employability and productivity could help to explain some of the remaining differences. Native and immigrant communities may differ in their ability to speak the language of the host country, the sectors in which their job-seeking is focused, or the density of their mutual support networks, all factors which may influence their job opportunities and the effectiveness of the job-seeking process. Part of the greater vulnerability to unemployment of foreigners can be therefore explained by a lower level of apparent skills, rather than real ones.

4.2.2 The effect of immigration on job opportunities for native workers

Does immigration harm the job opportunities of native workers?
Some people think that immigrant workers are taking the place of native workers, so that immigration is helping to worsen employment conditions for natives. Is this true?

Harris and Todaro[3] look at a dual economy where the host region is characterized by having a fixed minimum wage. In substance, because companies determine their labour demand in such a way as to make marginal productivity equal to labour costs, the level of employment there is wholly determined by technology and the level of the minimum wage. Given that unemployment is the result of the difference between labour supply and demand, and since all immigration increases the supply of labour without increasing demand, the end result is an increase in the level and rate of unemployment. This is, however, based on a static model where prices and wages in the host region are mainly exogenous and are therefore totally rigid in both the short and long terms. Neo-Keynesian models showing the short-term macroeconomic operation of an economy also assume that prices, wages and productive capital are rigid, but only in the short term. In the short term it is essentially the demand for goods from households, businesses and the State which determines production and employment. Unemployment is then the result of the difference between the labour demand needed to satisfy the demand for goods taking account of technology, and the labour supply, which is mainly determined outside the model. In the longer term, changes in the unemployment rate tend to cause wages and prices to adjust: the unemployment rate influences wage demands and wage trends affect prices. Inflation then retroacts on the demand for goods. In these neo-Keynesian models immigration may be classified as an exogenous increase in the labour supply. It instantly increases the number of workers without affecting the level of employment, since prices and wages are fixed. The influx of workers is thus reflected in an increase in unemployment, since the same number of jobs has to be divided between a larger number of workers. However, this increase is merely temporary. The increase in the unemployment rate curbs wage demands: wages drop, followed by prices. This then stimulates demand for goods and therefore for labour, which in turn helps to bring the unemployment rate down again. Eventually the reduction in prices is such that the initial effect on the unemployment rate is completely nullified. Immigration thus has only a temporary effect on the unemployment rate, and this effect diminishes as prices and wages quickly adjust. Cahuc and Zylberberg[4] estimated the French Phillips curve for period 1970-1998 and found that if immigration increases the growth rate in the active population by 1%, it will increase the unemployment rate by 0.625 percentage points in the short term. However, the estimate that it takes an average of less than six months for wages to adjust to prices suggests that this effect does not last long. If prices and wages can take a certain time to adjust, it also takes a certain time for a worker to find a job for which his/her skills are suited, and for a company to find a worker suited to the position it wishes to fill. As we can see from the matching models, these

[3] Harris and Todaro, 1970 quoted in Kuptsch, 2010
[4] Cahuc and Zylberberg, 2001 quoted in Kuptsch, 2010

adjustment periods mean that there are, at any given time on the labour market, unemployed job-seekers and job vacancies. In this context, if we take an influx of immigrants, the new arrivals may take a certain time to find a job that meets their expectations. Immigration is thus instantly reflected in an equivalent increase in the number of unemployed, boosting the unemployment rate. However, this increase in the recruitment pool also increases the probability that a company will quickly fill a vacancy, thereby reducing the cost. So, by increasing the profit associated with creating a job, immigration encourages this to happen. This process remains in operation for as long as the profit associated with advertising a vacancy remains positive, in other words until the unemployment rate returns to its initial level. To sum up, in equilibrium unemployment models, the equilibrium unemployment rates for particular categories of workers are independent of the size of the active population in question. The conclusion therefore has to be that the immigration of a certain type of workers increases the number of active persons of that type, but this increase has no effect on the long-term unemployment rate in the category of worker concerned, so where wages and prices take a certain time to adapt to changes in the economic environment and workers take a certain time to find a job for which their skills are suited, immigration is likely to increase the unemployment rate temporarily[5].

[5]For further reading refer to Kuptsch, 2010

5 Social matters

5.1 Major concerns

Many concerns have been expressed about globalization by unions and others. The International Labour Organization sponsored a World Commission on the Social Dimension of Globalization which issued a highly skeptical report[1] which consisted of prominent representatives of business, unions and government from the developed and developing world, called for the benefits of globalization to be shared more equally among nations and within nations.

> *The current process of globalization is generating unbalanced outcomes, both between and within countries. Wealth is being created, but too many countries and people are not sharing in its benefits. They also have little or no voice in shaping the process. Seen through the eyes of the vast majority of wemen and men, globalization has not met their simple and legitimate aspirations for decent jobs and a better future for their children. Many of them live in the limbo of the informal economy without formal rights and in a swathe of poor countries that subsist precariously on the margin of the global economy. Even in economically successful countries some workers and communities have been adversely affected by globalization. Meanwhile the revolution in global communications heightens awareness of these disparities. [...] These global imbalances are morally unacceptable and politically unsustainable.*

The commission surveyed 73 countries around the world. In every region of the world except South Asia, the United States, and the European Union, unemployment rates increased between 1990 and 2002. The Commission also found that 59% of world population were living in countries with growing inequality, with only 5% in countries with declining inequality. Even in most of the developed world the rich were getting richer while the poor were often not holding their own. While globalization may have helped some countries in

[1] World Commission on the Social Dimension of Globalization, 2004, p. x quoted in Stiglitz, 2006, pp. 7-8

terms of GDP, it have not helped most of the people even in these countries. The worry was that globalization might be creating rich countries with poor people. The Commission expressed[2] a number of concerns about globalization, including the following:

- Economic growth (as measured by gross domestic product) since 1990 has actually slowed down. This is not what globalization's advocates would have predicted;
- That growth is uneven, with some economies (such as China's) growing at unprecedented rates; the vast majority of developing countries growing quite slowly; finally, 23 countries actually experiencing negative economic growth;
- The income gap between rich and poor countries is growing;
- Short-term, speculative flows of capital have been prominent features of the new globalization and these have damaged the economies of developing nations;
- Unemployment rates have grown in the formal economies, as self-employment has. The unregulated, informal economy has grown quickly;
- While the absolute number of poor people has declined worldwide, nearly all of that decline is due to economic growth in one country – China. In many parts of the world, poverty continues to grow.

In general, those who are discontented with economic globalization do not object to the greater access to global markets or to the spread of global knowledge, which allows the developing world to take advantage of the discoveries and innovations made in developed countries. They usually raise other concerns[3]:

- The rules of the game that govern globalization are unfair, specifically designed to benefit the advanced industrial countries. In fact, some recent changes are so unfair that they have made some of the poorest countries actually worse off;
- Globalization advances material values over other values, such as a concern for the environment or for life itself;
- The way globalization has been managed has taken away much of the developing countries' sovereignty, and their ability to make decisions themselves in key areas that affect their citizens' well-being. In this sense, it has undermined democracy;

[2] World Commission on the Social Dimension of Globalization, 2004, pp. 35-49 quoted in Stiglitz, 2006

[3] Stiglitz, 2006, p. 9

- While the advocates of globalization have claimed that everyone will benefit economically, there is plenty of evidence from both developing and developed countries that there are many losers in both;

- Perhaps most important, the economic system that has been pressed upon the developing countries is unappropriate and often grossly damaging. Globalization should not mean the Americanization of either economic policy or culture, but often it does.

The last topic touches both those in developed and developing countries. The American model differs from that of the Nordic countries, from the Japanese and the European one; even if the American model has done well as measured by GDP, it has not done well in many other dimensions, such as the length and the quality of life, the eradication of poverty and even the maintenance of the well-being of those in the middle class; real wages in the US, especially for those at the bottom, have stagnated for more that a quarter century, and incomes are high as they are partly because Americans work far longer hours than their European counterparts. In many countries this aspect of globalization appears the most threatening, as local cultures and even languages are challenged by a new global culture, dominated by English language and largely American cultural products.

In addition to this, Unions have specific reasons to be concerned about the new globalization. Central to union concerns is a fear that globalization means a "*race to the bottom*", a world-wide lowering of wages and labour standards and a decline everywhere of independent, democratic trade unions. If corporations are free to always seek cheaper sources of labour, there is a fear that capital will flee high-cost developed countries where unions remain strong and flow towards union-free "*export processing zones*" and other havens of low-wage, union-free economies. Were that to happen, it would spell doom for unions everywhere.

Unions even heavily criticize institutions for seeming to impose a *neo-liberal* agenda (namely, the *Washington Consensus*) on countries in return for the services they offer, as already stated[4]. That agenda includes privatization of what were previously public services, labour market flexibility, liberalization of capital flows and trade, pension reform, and restrictive fiscal and monetary policies.

[4]Cfr. Chapter 1.

5.2 Possible policy implementations

5.2.1 International Labour Organization's agenda

The World Commission on the Social Dimension of Globalization[5] also noted many positive benefits to globalization, including an improvement in the quality of democracy and the forging of a greater sense of global community. It emphasized that there is no possibility of reverting to an earlier era, of stopping globalization, and focussed instead on proposals and recommendations to achieve a fair globalization.

- Improved governance at national and local level based on democracy and respect for human rights. Nations must provide essential services and social protection to their citizens, integrate the informal economies, promote sustainable development, make decent work a key goal of economic policy, empower local communities and so on;

- At global level, the Commission called for a number of reforms including reducing unfair barriers to market access (for developing countries), a more balanced strategy for growth and full employment, fairer rules for intellectual property, a more consistent and coherent framework for FDI, and reforms to the international financial system ensuring greater participation by developing countries;

- Reinforce the capacity of the International Labour Organization to promote respect for core labour standards. All relevant international institutions should play their part in promoting those standards. Technical assistance programs and training towards this end should be promoted. Where persistent violations of rights continues, the ILO should take action to secure compliance;

- Create fair and transparent rules for the cross-border movement of people, particularly protecting the rights of migrant workers and combating trafficking, especially of women;

- Establish a global forum for exchanging views and information on cross-border migration issues.

5.2.2 Unions' agenda

Unions have moreover encouraged the WTO to include a "social clause" in trade agreements to guarantee the rights of workers. The international trade union movement has pressured the WTO on a number of issues, including:

[5] World Commission on the Social Dimension of Globalization, 2004, pp. 142-147

- Calling for the reduction, or elimination, of agricultural export subsidies in developed countries;
- Dealing with the massive rise in unemployment due to the phasing out of the WTO's agreement on textiles and clothing;
- Coping with problems raised by intellectual property rights, and in particular, better and cheaper access to medicines to combat HIV/AIDS and other health problems in the developing world;
- Making sure that privatization of public services, especially in education and health, is not seen as the solution to all problems.

While at a global level, institutions like the IMF, World Bank and WTO have been subject to trade union pressure to recognize workers' rights and combat social injustice, unions have had considerably more success at regional level, most notably in the European Union. For many years now, workers' rights have been incorporated into European law, and European Works Councils represent an innovative approach to involving workers and their unions in the management of companies[6].

Corporate Social Responsibility

A method aimed to give globalization a "human face" is the promotion of corporate social responsibility (hereinafter, CSR), framework agreements between global union federations and multinational enterprises, and global campaigns. CSR has become increasingly fashionable in recent years as corporations seek to promote a better public image. This is often done through annual reports and social audits which reveal the extent to which a corporation promotes broadly-accepted values such as sustainable development, human rights, and so on. Unions have been very critical of CSR, seeing it as a poor substitute for genuine social dialogue and truly independent verification of corporations' compliance with accepted standards. There has been an increasing number of framework agreements signed in recent years between MNEs and global union federations. The agreements vary widely in scope, but usually include a corporation's acceptance of a legitimate role for unions and a recognition of core international labour standards, often mentioning ILO conventions 87 and 98 specifically.[7] While a national collective bargaining agreement can be enforced both in country's courts and by effective union action in the field (such as strikes), there is no clear enforcement mechanism for international framework agreements at present. In many cases, framework agreements and social dialogue are not enough, and unions are forced to launch global campaigns to

[6] ILO International Training Centre, 2011, pp. 4-12

[7] C87 is a convention concerning Freedom of Association and Protection of the Right to Organize; C98 is a convention concerning the Application of the Principles of the Right to Organize and to Bargain Collectively

pressure corporations and governments, sometimes to recognize even the most basic rights, such as that to join a trade union. Many such campaigns have targeted well-known multinational enterprises, while others have focused on countries with a poor record of respecting workers' and human rights, such as Belarus, Colombia, Iran and Burma.[8] Unions increasingly partner with others to reach a much wider public. Unions also partner with NGOs that focus on particular sectors, such as the Clean Clothes Campaign[9]. The same information and communication technologies that have made globalization possible, in particular email and world wide web, have created a new kind of global campaign which takes place primarily online. A number of global union federations have launched such campaigns using their websites and mailing lists, and several have partnered up with the news and campaigning website *LabourStart* to bring their concerns to a global online audience. These campaigns have had a powerful, and sometimes immediate, effect in many cases, leading to the release of jailed trade unionists, bringing corporations to the collective bargaining table, and achieving other union goals. The involvement of hundreds of thousands of trade unionists in these campaigns has created a world-wide grassroots activist network that was unimaginable only a few years ago.

[8]The ITUC publishes an annual report on violations of trade union rights around the globe.

[9]Formed in the Netherlands in 1989 it focuses on the improvement of working conditions in the garment and sportswear industries; the CCC works with a partner network of more than 250 organizations around the world.

6 A new World is possible

> It is clear that economic globalization has far to go befor the full efficiency benefits of economic integration are reaped.
>
> Rodrik, 2007, p. 198

There is definitely a demising process in the sovereignty of nation states. The emergence of global-oriented NGOs based on the Kantian philosophy of the world as *a community of free individuals*, is making nation borders weaker and no longer relevant. The European referendum for a European Law can be considered such a movement or tendency. The emerging of negotiations in the Persian triangle, supposed to constitute a more widely political and economic cooperation between Afghanistan, Iran and Tajikistan should be another example.

6.1 Nation-State Sovereignty under attack

According to some theorists, the growing dependence and interconnectedness between nation states makes governments weaker and less relevant than ever before.
The notion concept of *sovereignty* refers to the three-fold capacity of a state to claim absolute supremacy over internal affairs within its territory, absolute right to govern its people, and freedom from any external interference in the above matters.[1]
Stephen D. Krasner[2] agrees on the collapsing autonomy of states but denies that the impact of globalization on the nation-state could possibly lead to the death of state sovereignty.

[1] Wang, 2004, p. 473 quoted in Badakhshani, n.d.
[2] Stephen D. Krasner is Graham H. Stuart Professor of International Relations at Stanford University

> *Those who proclaim the death of sovereignty misread the history. The nation state has a keen instinct for survival and has so far adapted to new challenges, even the challenge of globalization.*[3]

The question is whether contemporary globalization is likely to differ from those former in terms of impact on the nation state. Today's globalization distinguishes itself from those of the past in terms of rapid communication, market liberalization and global integration of goods, services and production. Even though it might not be appropriate to compare the ancient world with today's modern nation states, we can find that an increasingly growing interdependence between these latter, actually leads to make the states compelled to build relations with other states in order to sell their goods, services, and develop a stronger and larger economy. Due to this interdependence one of the three features of a sovereign state, the absolute freedom from any external force, is undermined. Another aspect of sovereignty is the ability of a state to solve its domestic problems on its own; since problems and threats are getting more globalized, it is almost impossible for a state to act alone. This undermines the second notion of sovereignty which claims absolute supremacy over internal affairs within its territory. Hence globalization is definitely eroding sovereignty, along with national borders of nation states.[4]

6.2 Towards a Global Government

How global is the global economy in reality? Rodrik[5] argues that we are quite far, namely international economic integration remains remarkably limited, since:

- National borders seem to have a significantly depressing effect on commerce even in absence of formal tariff or non-tariff barriers, linguistic or cultural differences and exchange rate uncertainty, so that international price arbitrage in tradable commodities tends to occur very slowly;
- Investment portfolios in the advanced industrial countries typically exhibit large amounts of home bias, that is, people invest a higher proportion of assets in their own countries than the principles of asset diversification would suggest;
- Severe restrictions on the international mobility of labour are the rule rather than the exception.

While formal barriers to trade and capital flows have been substantially reduced over the last three decades[6], international markets for goods, services,

[3] Krasner, 2001 quoted in Badakhshani, n.d.
[4] See also Badakhshani, n.d.
[5] Rodrik, 2007, pp. 196-197
[6] Cfr. Chapter 3

and capital are not nearly as thick as they would be under complete integration. National borders demarcate political and legal jurisdictions. Such demarcations serve to segment markets in much the same way as transport cost or border taxes do. These transaction costs arise from various sources but perhaps the most obvious relate to the problem of contract enforcement. When one of the parties reneges on a written contract, local courts may be unwilling, and international courts unable, to enforce a contract signed between residents of two different countries. National sovereignty interferes with contract enforcement, leaving international transactions hostage to an increased risk of opportunistic behavior. This problem is most severe in the case of capital flows, and has the implication that national borrowing opportunities are limited by the willingness of countries to service their obligations, rather than their ability to do so. The presence of separate national monetary regimes provides another example of trade-restricting transaction cost. Rose[7] argues that countries that share the same currency trade with each other three times as much as countries that have separate currencies; moreover, the effects of exchange-rate volatility are comparatively minor. Hence, the jurisdictional discontinuity introduced by separate national currencies has a large negative effect on trade even when currency values are stable. If the depth of markets is limited by the reach of jurisdictional boundaries, does it not follow that national sovereignty imposes serious constraint on international economic integration? Can markets become international while politics remains local? In other words, what would politics look like in a world in which international markets had nothing to fear from the narrower scope of political jurisdictions?

6.2.1 The open-economy trilemma

A familiar result of open-economy macroeconomics is that countries cannot simultaneously maintain independent monetary policies, fixed exchange rates, and an open capital account. This result is commonly known as *inconsistent trinity* or *open-economy trilemma*. If a government chooses fixed exchange rates and capital mobility, it has to give up monetary autonomy; if it wants monetary autonomy and capital mobility, it has to go with floating exchange rates; if it wants to combine fixed exchange rates with monetary autonomy (at least in the short run), it better restrict capital mobility. By analogy, a different kind of trilemma may be constructed (see figure 6.1 on the following page)[8]: the three nodes of the extended trilemma are international economic integration, the nation-state, and mass politics[9]. The implied claim, as in the standard trilemma, is that we can have at most two of these three things. If we want true international economic integration, we have to go either with the

[7] Rose, 1999, pp. 22-23 quoted in Rodrik, 2007, p. 199

[8] Rodrik, 2007, pp. 199-202

[9] Mass politics refers to a political system where the franchise in unrestricted, there is a high degree of political mobilization, and political institutions are responsive to mobilized groups

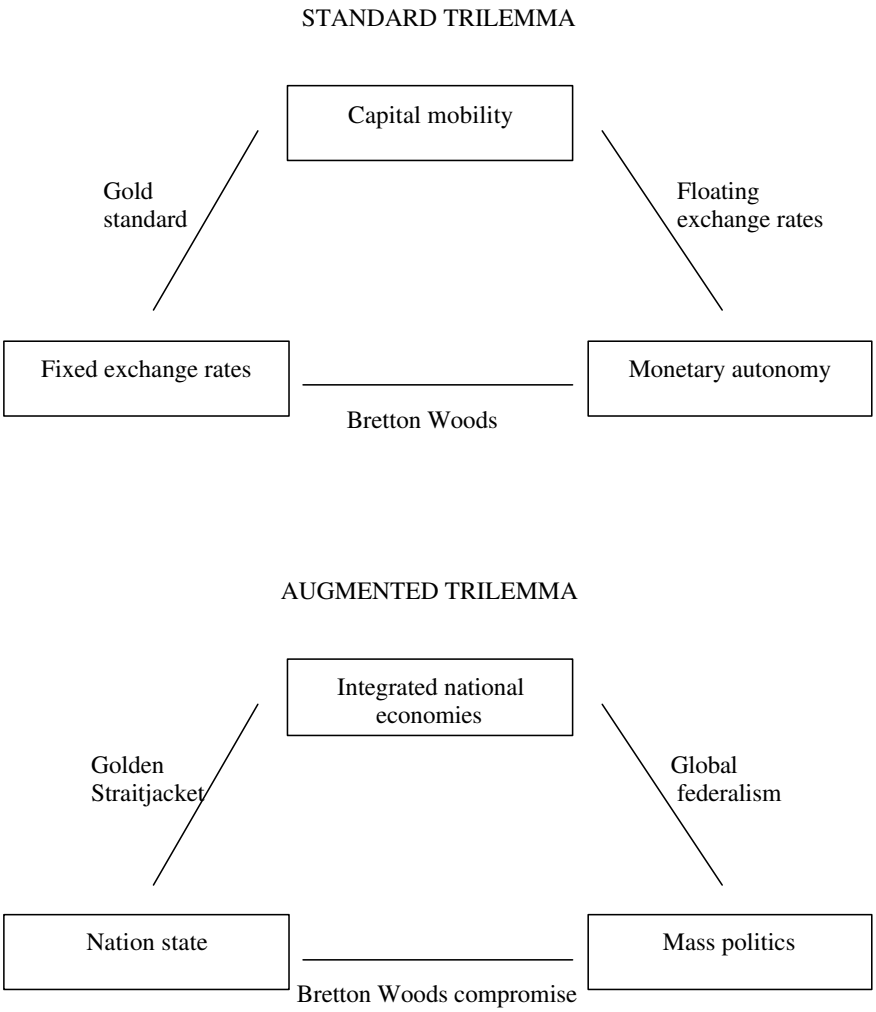


Figure 6.1: Source: Rodrik, 2007, p. 200.

nation-state, in which case the domain of national politics will have to be significantly restricted (*golden straitjacket*), or else with mass politics, in which case we will have to give up the nation-state in favour of *global federalism*. If we want highly participatory political regimes, we have to choose between the nation-state and international economic integration. If we want to keep the nation-state, we have to choose between mass politics and international economic integration.

6.2.2 The Golden Straitjacket

> Omnipotent markets mean impotent politicians.
>
> Wolf, 2001, p. 178

One of the two ways to achieve complete international economic integration is to maintain the nation-state largely as is, but to ensure that national jurisdictions, and the differences among them, do not get in the way of economic transactions. The overarching goal of nation-states in this world would be to appear attractive to international markets. National jurisdictions, far from acting as an obstacle, would be geared towards facilitating international commerce and capital mobility. Domestic regulations and tax policies would be either harmonized according to international standards, or structured such that they posed the least hindrance to international economic integration. The only local public goods provided would be those that are compatible with integrated markets.

It is not difficult to imagine a world of this sort; in fact, many commentators seem to believe we are already there. Governments today actively compete with each other by pursuing policies that they believe will earn them market confidence and attract trade and capital inflows: tight money, small government, low taxes, flexible labour legislation, deregulation, privatization, and openness all around. These are the policies that comprise what Thomas Friedman has aptly termed the *Golden Straitjacket*[10]:

> *As your country puts on the Golden Straitjacket, two things tend to happen: your economy grows and your politics shrinks. [...] The Golden Straitjacket narrows the political end economic policy choices of those in power to relatively tight parameters. This is why it is increasingly difficult these days to find any real differences between ruling and opposition parties in those countries that have put on the Golden Straitjacket. Once your country puts on the Golden Straitjacket, its political choices get reduced to Pepsi or Coke, namely to slight nuances of tastes, slight nuances of policy, slight alterations in design*

[10] Friedman, 1999 quoted in Rodrik, 2007, p. 202

> *to account for local traditions, some loosening here or there, but never any major deviation from the core golden rules.*

In such a world, Rodrik argues that the shrinkage of politics would be reflected in the insulation of economic policymaking bodies (central banks, fiscal authorities, and so on) from political participation and debate, the disappearance (or privatization) of social insurance, and the replacement of developmental goals with the need to maintain market confidence. Once the rules of the game are set by the requirements of the global economy, the ability of mobilized popular groups to access and influence national economic policymaking has to be restricted. The experience with the classical gold standard provides an apt illustration of the incompatibility. At the height of the gold standard, the limited domain of national politics (and its elite-based nature) ensured that domestic monetary policy could be entirely subjugated to the needs of maintaining the gold parities. By the interwar period, as the franchise was fully extended and labour became organized, national governments found that they could no longer pursue gold standard economic orthodoxy.

6.2.3 Global federalism

Consider an hypothetical perfectly integrated world economy. This would be a world economy in which national jurisdictions do not interfere with arbitrage in markets for goods, services or capital. Transaction costs and tax differentials would be minor; convergence in commodity prices and factor returns would be almost complete. The most obvious way we can reach such a world is by instituting federalism on a global scale. Global federalism would align jurisdictions with the market, and remove the 'border' effects. In the United States, for example, despite the continuing existence of differences in regulatory and taxation practices among states, the presence of a national constitution, national government, and a federal judiciary ensures that markets are truly national. The European Union, while very far from a federal system at present, seems to be headed in the same direction. Under a model of global federalism, the entire world, or at least the parts that matter economically, would be organized that way. National governments would not necessarily disappear, but their powers would be severely circumscribed by supranational legislative, executive, and judicial authorities. A world government would take care of a world market.

Can we envisage a world of global federalism, over the long-run?
Perhaps we could, based on the following reasoning. First, continuing technological progress will both foster international economic integration and remove some of the traditional obstacles (such as distance) to global government. Second, short of global wars or natural disasters of major proportions, it is hard to envisage that a substantial part of the world's population will want to give up the goodies that an increasingly integrated (hence efficient) world mar-

ket can deliver. Third, hard-won citizenship rights (of representation and self-government) are also unlikely to be given up easily, keeping pressure on politicians to remain accountable to the wishes of their electorate. Further, we can perhaps project an alliance of convenience in favour of global governance between those who perceive themselves to be the 'losers' from economic integration, like labour groups and environmentalists, and those who perceive themselves as the 'winners', like exporters, multinational enterprises, and financial interests. The alliance will be underpinned by the mutual realization that both sets of interests are best served by the supranational promulgation of rules, regulations, and standards. Labour advocates and environmentalists would get a shot at international labour and environmental rules. Multinational enterprises will be able to operate under global accounting standards. Investors will benefit from common disclosure, bankruptcy, and financial regulations. A global fiscal authority will provide public goods and a global lender-of-last resort will stabilize the financial system. Part of the bargain will be to make international policymakers accountable through democratic elections. National bureaucrats and politicians, the only remaining beneficiaries of the nation-state, will either refashion themselves as global officials or they will be shouldered aside.

Many things can go wrong with this scenario. One alternative possibility is that an ongoing series of financial crisis will leave national electorates sufficiently shell-shocked that they willingly, if unhappily, don the Golden Straitjacket for the long-run. Another possibility is that governments will resort to protectionism to deal with the distributive and governance difficulties posed by economic integration. For the near term, either one of these scenarios should be regarded as more likely than global federalism. But a longer time horizon leaves room for greater optimism.

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