Global Economy
Lecture 2

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Bases for the Emergence of the Phenomenon of Economic Globalisation

Advantages and Disadvantages of Globalisation

Globalisation Indices

Globalisation – (KOF Swiss Economic Institute)

- The process of creating networks of connections among actors at intra- or multi-continental distances, mediated through a variety of flows including people, information and ideas, capital, and goods.
- Globalisation erodes national boundaries, integrates national economies, cultures, technologies and governance, and produces complex relations of mutual interdependence.

- The International Monetary Fund defined "**economic globalisation**" as: "a historical process, the result of human and technological progress.
- It refers to increasing integration of economies around the world, particularly through trade and financial flows.
- The term also refers to the movement of people (labour) and knowledge (technology) across international borders."

- **Internationalisation** refers to an increase in transactions and interdependencies between countries.
- **Liberalisation** denotes the process of removing officially imposed restrictions on movements of resources between countries.
- **Universalisation** describes the process of dispersing various objects and experiences to people at all inhibited parts of the earth.
- **Westernisation** is interpreted as a particular type of universalisation, in which social structures of Western societies are spread across the earth.

Bases for the emergence of the phenomenon of economic globalisation

Bretton Woods Institutions and GATT

Trade Liberalisation

Liberalisation of Capital Movements

Technological Change Over the Past 100 Years

Bretton Woods Institutions: International Monetary Fund (IMF)

- Three main objectives:

➢ to promote international monetary cooperation;

➢ to facilitate the expansion of international trade;

➢ to promote exchange rate stability.

IMF

- The primary role of the IMF is providing short- and medium-term financial assistance to the members that have temporary problems with a balance-of-payments equilibrium.

- The resources for the IMF credits come from quota subscriptions paid by the members.

IMF

- Each member country pays the amount of money proportionate to its economic size that is measured by national income and trade volume.

- The size of quota is adjusted to the economic power of a country at intervals of 5 years.
- A 25% of quota is paid in SDRs (Special Drawing Rights) or in international currencies. The remaining 75% a country pays in its own currency.

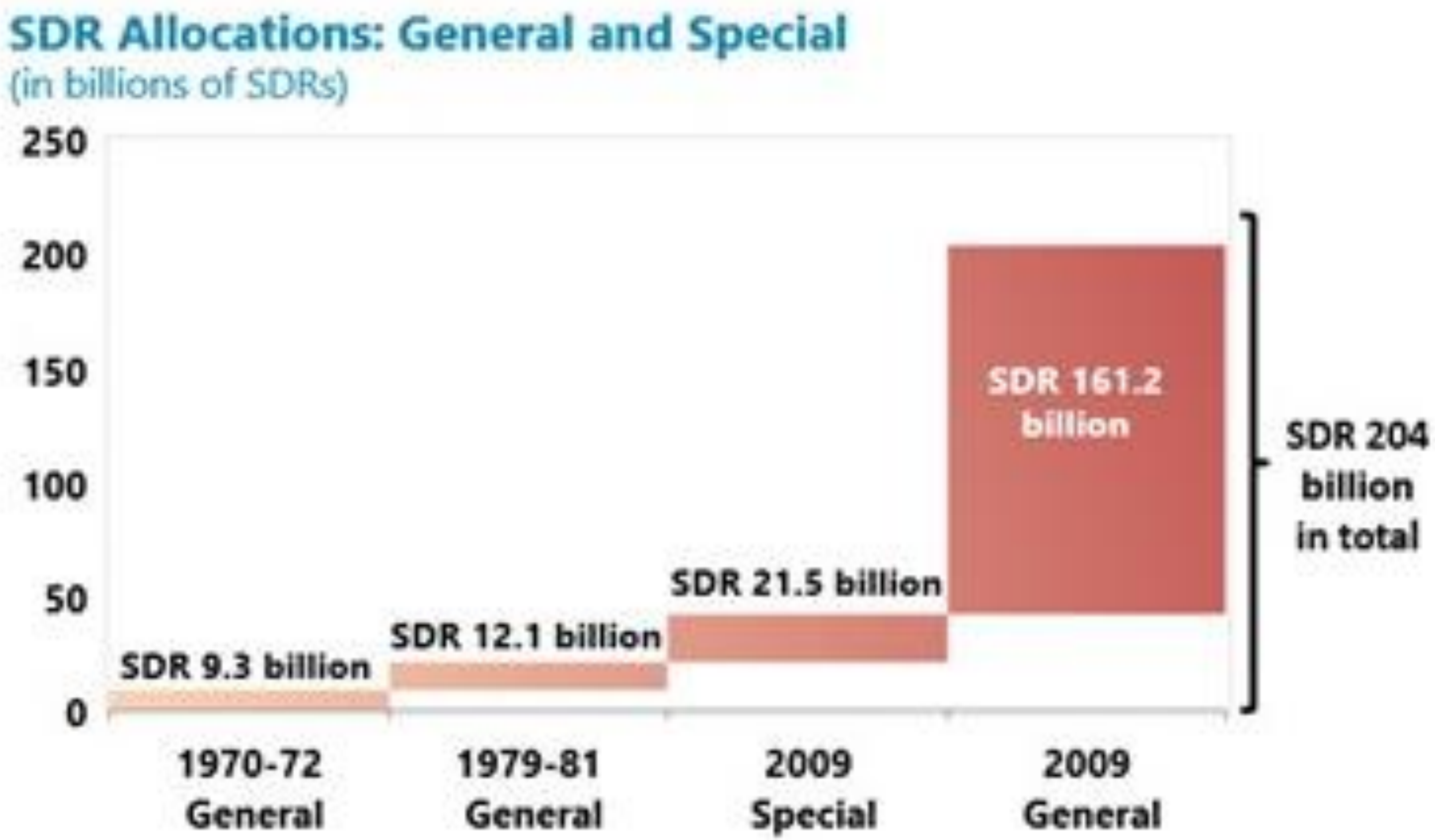
https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/14/51/Special-Drawing-Right-SDR

SDR

Currency	Weights determined in the 2015 Review	Fixed Number of Units of Currency for a 5-year period Starting Oct 1, 2016
U.S. Dollar	41.73	0.58252
Euro	30.93	0.38671
Chinese Yuan	10.92	1.0174
Japanese Yen	8.33	11.900
Pound Sterling	8.09	0.085946

https://www.imf.org/en/About/Factsheets/Sheets/2016/08/01/14/51/Special-Drawing-Right-SDR

SDR



Source: IMF, Finance Department statistics.

IMF

- The quota determines the voting power of a country. In result the members of the Fund do not have an equal voice. The largest shareholders have big influences on the IMF’s decisions.
- In 2016 the major shareholders were **United States** (17.46 per cent of the total IMF quotas), **Japan** (6.48%), **China** (6.41%), **Germany** (5.60%), **France** (4.24%), **United Kingdom** (4.24%), **Italy** (3.17%), **India** (2.76%), **Russia** (2.71%), and **Saudi Arabia** (2.10%).
- Turkey (0.98%), Poland (0.86%), Azerbaijan (0.08%)

World Bank (WB)

- Main objective initially was to assist in the reconstruction and development of damaged economies by facilitating the investment of capital for productive purposes.

- Responsible for providing finance and advice to countries for the purposes of economic development and poverty reduction, and for encouraging and safeguarding international investments.

World Bank (WB) - group of five international organizations

1. **International Bank for Reconstruction and Development (IBRD)** lends to governments of middle-income and creditworthy low-income countries.
2. **International Development Association (IDA)** provides interest-free loans and grants to governments of the poorest countries.
3. **International Finance Corporation (IFC)** helps developing countries to achieve growth by financing investment, mobilizing capital in international financial markets and providing advisory services to business and governments.

World Bank (WB) - group of five international organizations

4. **Multilateral Investment Guarantee Agency (MIGA)** offers political risk insurance (guarantees) to investors and lenders.
5. **International Centre for the Settlement of Investment Disputes (ICSID)** provides international facilities for conciliation and arbitration of investment disputes.

International Monetary Fund	World Bank
• oversees the international monetary system	• seeks to promote the economic development of the world’s poorer countries
• promotes exchange stability and orderly exchange relations among its member countries	• assists developing countries through long-term financing of development projects and programs
• assists all members – both industrial and developing countries – that find themselves in temporary balance of payments difficulties, by providing short- to medium-term credits	• provides to the poorest developing countries whose per capita GNP is less than $1,165 (2018) a year special financial assistance through the International Development Association (IDA)

International Monetary Fund	World Bank
• supplements the currency reserves of its members through the allocation of SDRs (special drawing rights)	• encourages private enterprises in developing countries through its affiliate, the International Finance Corporation (IFC)
• draws its financial resources principally from the quota subscriptions of its member countries	• acquires most of its financial resources by borrowing on the international bond market
• employs about 2,400 staff, 189 member countries	• has a staff of 9,000 from more than 170 member countries, 189 member countries

The General Agreement on Tariffs and Trade (GATT)

- The objectives of the GATT (1947) were to establish an orderly and transparent framework within which barriers to trade could be gradually reduced and international trade expanded.

- The principal mechanism for progress on trade liberalisation within the GATT has been periodic multilateral negotiating rounds.

- The primary focus of the GATT rounds has been the promotion of multilateral tariff reductions, and the extension of the agreed reductions to all members.

GATT/WTO

- The GATT was a set of rules, a multilateral agreement, with no institutional foundation, only a small associated secretariat.

- The World Trade Organization (WTO) came into being in 1995. It is the successor to the GATT.

- The WTO is the international organization dealing with the global rules of trade between nations.

- The WTO has **164** (July 2016) members accounting for over 95% of world trade. Over 20 others are negotiating membership.

GATT/WTO – Observers (22)

- Algeria, Andorra, Azerbaijan, Bahamas, Belarus, Bhutan, Bosnia and Herzegovina, Comoros, Equatorial Guinea, Ethiopia, Vatican, Iran, Iraq, Lebanese Rep., Libya, Sao Tome and Principe, Serbia, Somalia, Sudan, Syria, Timor-Leste, Uzbekistan.

Principles of the WTO’s trading system

1. Trade without discrimination
2. Freer trade: gradually, through negotiation
3. Predictability: through binding and transparency
4. Promoting fair competition
5. Encouraging development and economic reform

Principles of the WTO’s trading system

Trade without discrimination

- **Most-favoured-nation (MFN):** treating other countries equally. Countries cannot normally discriminate between their trade partners. If a country grants someone a special favour (such as a lower customs duty rate for one of their product) it has to do the same for all other GATT/WTO members.

- **National treatment policy**: treating foreigners and locals equally. Imported and locally produced goods should be treated equally - at least after the foreign goods have entered the market.

Principles of the WTO's trading system

Freer trade: gradually, through negotiation

- Trade barriers coming down through negotiation.

Predictability: through binding and transparency

- Foreign companies, investors and governments should be confident that trade barriers (including tariffs and non-tariff barriers) should not be raised arbitrarily; tariff rates and market-opening commitments are "bound" in the WTO.

Promoting fair competition

- Discouraging "unfair" practices such as export subsidies and dumping products at below cost to gain market share.

Principles of the WTO’s trading system
Encouraging development and economic reform

- The trading system should be more beneficial for less developed countries - giving them more time to adjust, greater flexibility, and special privileges.
- Decisions in WTO are typically taken by consensus among all member countries and they are ratified by members’ parliaments.
- Trade friction is channelled into the WTO’s dispute settlement process where the focus is on interpreting agreements and commitments, and how to ensure that countries’ trade policies conform with them.

Principal forum for trade liberalisation

- Eight rounds of multilateral trade negotiations under the General Agreement on Tariffs and Trade (GATT) have significantly decreased trade barriers.

- Successive GATT rounds cut tariffs and liberalised trade.

GATT/WTO Trade Rounds, 1947-2010

Name of round	Period and number of parties	Subjects and modalities
Geneva	1947 (23 countries)	Tariffs: item-by-item offer-request negotiations
Annecy	1949 (33 countries)	Tariffs: item-by-item offer-request negotiations
Torquay	1950-1951 (34 countries)	Tariffs: item-by-item offer-request negotiations
Geneva	1956 (22 countries)	Tariffs: item-by-item offer-request negotiations
Dillon Round	1961-62 (45 countries)	Tariffs: item-by-item offer-request negotiations motivated in part by need to rebalance concessions following creation of the EEC (European Economic Community)
Kennedy Round	1964-67 (48 countries)	Tariffs: formula approach (linear cut) and item-by-item talks. Non-tariff measures: antidumping, customs valuation

GATT/WTO Trade Rounds, 1947-2010

Name of round	Period and number of parties	Subjects and modalities
Tokyo Round	1973-79 (99 countries)	Tariffs: formula approach with exceptions Non-tariff measures: antidumping, customs valuation, subsidies and countervail, government procurement, import licence, product standards, safeguards, special and differential treatment of developing countries.
Uruguay Round	1986-94 (103 countries in 1986, 117 as of end -1993)	Tariffs: formula approach and item-by-item negotiations. Non-tariff measures: all issues, plus services, intellectual property, preshipment inspection, rules of origin, trade-related investment measures, dispute settlement, transparency and surveillance of trade policies.
Doha Round	2001- (150 countries as of beginning 2007)	Tariffs: formula approach and item-by-item negotiations. Non-tariff measures: trade facilitation, rules, services, environment.

- Whereas the volume of international commerce grew by only 0.5% annually between 1913 and 1948, it grew at an annual rate of 7% from 1948 to 1973.

- The value of world trade has increased from US$ 57 billion in 1947 to US$ 6 trillion in the 1990s.

- Average tariff levels of the United States and other industrialised countries on imported products have dropped from about 40% to only 6%, and barriers to trade in services have also been lowered.

International Capital Liberalisation

- The 1960s and 1970s, when most countries still maintained restrictive regimes.
- Since its establishment in 1961, the Organization for Economic Cooperation and Development (OECD) has promoted the progressive liberalisation of capital movements. The role of the United States in promoting capital liberalisation. Member countries voluntarily enter into obligations to liberalise capital movements.
- Regular examinations of capital controls were carried out by the **Committee on Capital Movements and Invisible Transactions** (CMIT), which requires countries to justify remaining restrictions.
- **The OECD Investment Committee** (2004)

International Capital Liberalisation

- In the 1980s, many advanced countries made significant progress in liberalising capital movements. Virtually all capital controls have now been abolished among industrial countries, and there are no formal barriers to cross-border flows of capital.

- The liberalisation of capital movements during the 1980s has been a global phenomenon in advanced countries.

- Throughout much of the 1990s, FDI outflows from the major industrialised countries to industrialising countries rose at approximately 15 per cent annually. FDI flows among the industrialised countries themselves rose at about the same rate.

Technological progress

- Automobile revolution (1940-1979)
- Information technology revolution (1980-)

- The rapid development of information technologies.

- Technological advances in transportation and communications have reduced costs and thus significantly encouraged trade expansion.

Forces driving globalisation

- Developments in transportation

  - Improvements in transport technology has "shrunk" the world.
  - 19th century steam engine → 20th century jet engine.
  - Countries have built efficient and integrated transportation infrastructure (e.g. airports, seaports, railways, highways to facilitate movement).
  - Increasing mobility of goods and people.

Forces driving globalisation

- Developments in communications
  - Internet has enabled consumers to access information instantly, conveniently and efficiently.
  - Internet has transferred the way people communicate, do business, obtain information and purchase goods and services.

Transport and Communications Cost (constant US$)

Dollar D., *Globalization, Poverty, and Inequality since 1980*, The World Bank Research Observer, Fall 2005, 20(2), p. 148.

Year	Sea freight (average ocean freight and port charges per ton)	Air transport (average cost per passenger mile)	Telephone call (average price for a 3-minute call between New York and London)
1930	60	0.68	245
1940	63	0.46	189
1950	34	0.30	53
1960	27	0.24	46
1970	27	0.16	32
1980	24	0.10	5
1990	29	0.11	3

History of Globalisation

- The word "globalisation" has been used by economists since 1980s.
- The concepts did not permeate popular consciousness until the later half of the 1990s.

- Various social scientists have tried to demonstrate continuity between contemporary trends of globalisation and earlier periods.
- The first era of globalisation (in the fullest sense) during the 19th century was the rapid growth of international trade between the European imperial powers, the European colonies, and the United States.
- After World War II, globalisation was restarted and was driven by major advances in technology, which led to lower trading costs.

Waves of Globalisation

- 1st wave: 1870-1914
  - Falling tariff barriers.
  - Improved transportation.
- 2nd wave: 1945-1980
  - Agreements to lower barriers again.
  - Rich country trade specialisation.
  - Poor nations left behind.
- 3rd wave: 1980-present
  - Growth of emerging markets
  - International capital movements regain importance.
  - Foreign outsourcing.

Emerging markets

- **BASIC**,
- **BRICS**,
- **CIVETS** (Colombia, Indonesia, Vietnam, Egypt, Turkey, South Africa),
- **MINT** (Mexico, Indonesia, Nigeria, Turkey).

Early stages of globalisation

- An early form of globalised economics and culture existed during **the Hellenistic Age** (323 BCE-146 BCE). Trade was widespread during that period, and it is the first time the idea of a cosmopolitan culture (from Greek "Cosmopolis", meaning "world city") emerged.

- **The Silk Road -** The trade links between the Roman Empire, the Parthian Empire and the Han Dynasty.

- **The Age of Discovery -** brought a broad change in globalisation, being the first period in which Eurasia and Africa engaged in substantial cultural, material and biologic exchange with the New World.

How does globalisation affect economic growth?

- Up until the mid-1980s, studies of growth focused primarily on the accumulation of **physical capital** (DR)
- In the 1990s - **accumulation of knowledge** (embodied in textbooks, technology, human capital) (IR).
- The new models of knowledge accumulation highlight several potential links between international integration and growth.

Grossman, G.M., Helpman, E., Globalization and Growth, *American Economic Review: Papers & Proceedings 2015, 105(5): 100–104*

- The international exchange of goods and ideas affects the incentives for knowledge acquisition and on the efficacy of inventiveness and diffusion.

- **First,** integration of peoples and cultures facilitates the flow of knowledge across national borders.
- Foreign ideas may be useful for inventing new products, for improving existing products, or for producing goods at lower cost.

Grossman, G.M., Helpman, E., Globalization and Growth, *American Economic Review: Papers & Proceedings 2015, 105(5): 100–104*

- **Second**, integration of product markets via international trade affords those who invent or improve products a greater potential market.

- The incentives for innovation may intensify or diminish with integration, depending on whether the scale effect or the competition effect is more powerful.

Grossman, G.M., Helpman, E., Globalization and Growth, *American Economic Review: Papers & Proceedings 2015, 105(5): 100–104*

- **Third**, the integration of world markets has general-equilibrium implications for input prices and relative output prices.

- These price changes affect the cost of innovation as well as the relative attractiveness of alternative directions for industrial research.

Grossman, G.M., Helpman, E., Globalization and Growth, *American Economic Review: Papers & Proceedings 2015, 105(5): 100–104*

- **Fourth,** international interactions affect not only the incentives for creation of new knowledge, but also those for technological diffusion, with implications for productivity growth.

Grossman, G.M., Helpman, E., Globalization and Growth, *American Economic Review: Papers & Proceedings 2015, 105(5): 100–104*

Advantages of globalisation

- Productivity increases faster when countries produce according to comparative advantage.

- Global competition and cheap imports keep prices low and inflation at bay.

- An open economy encourages technological development and innovation with ideas from abroad.

Advantages of globalisation

- Jobs in export industries pay more than those in import-competing industries.

- Free movement of capital gives the developing countries access to foreign investment and keeps interest rates low.

- Increased competition among nations – countries that are better able to offer incentives to investors will be more successful in attracting investment and markets.

Advantages of globalisation

- Improvements in standards of living. As countries trade and open their doors to foreign investment, they earn more revenue. Free trade allows for a larger variety of foreign goods for the consumer to choose from.

- Increased awareness of foreign culture. Travel, the Internet, mass media (products of globalisation) allow people to learn more about foreign culture.

- Environmental management. Sustainable development as the key to further growth. Sources of alternative energy.

Disadvantages of globalisation

- Rules of the game are set by IMF, WTO and World Bank.
- Globalisation creates financial instability and foreign liabilities.
- Erosion of traditional powers and policies of nation-states by global bureaucracies.
- Widening income gap between the rich and poor.
- Brain drain

Disadvantages of globalisation

- Globalisation is leading to a global monoculture (cultural, social, political and economic homogenization).
- Loss of local culture. Global (Western) brands dominate consumer markets in developing countries. Creation of homogenous culture across the world. Spread of pop culture.
- Environmental degradation: deforestation and related problems (soil erosion, extinction of flora and fauna, flooding), global warming.

Globalisation Indices

- **A.T. Kearney/ Foreign Policy Globalisation Index (ATK/ FP),** 2002-2007 – First composite indicator measuring globalisation. Covers political engagement, technology, personal contact and economic integration on a global scale.
- **GlobalIndex,** 1970-2002 – Sociological index of globalisation covering the economic, sociotechnical, cultural and political dimensions of globalisation.
- **New Globalisation Index (NGI),** 1995-2005 – Comprehensive indicator measuring the economic, political and social aspects of globalisation controlling partly for geographical distances between countries.

KOF Index of Globalisation, 2007

- The KOF Index of Globalisation was introduced in 2002.
- KOF Swiss Economic Institute
- The overall index covers the economic, social and political dimensions of globalisation.
- Economic globalisation (37%), social globalisation (39%), political globalisation (25%).

KOF Index of Globalisation – Economic Globalisation

	Economic Globalisation	Weights
Actual Flows (50%)	Trade (percent of GDP)	19%
	Foreign Direct Investment, flows (percent of GDP)	20%
	Foreign Direct Investment, stocks (percent of GDP)	24%
	Portfolio Investment (percent of GDP)	17%
	Income Payments to Foreign Nationals (percent of GDP)	20%
Restrictions (50%)	Hidden Import Barriers	22%
	Mean Tariff Rate	28%
	Taxes on International Trade (percent of current revenue)	27%
	Capital Account Restrictions	23%

KOF Index of Globalisation – Social Globalisation

	Social Globalisation	Weights
Data on Personal Contact (33%)	Telephone Traffic	26%
	Transfers (percent of GDP)	3%
	International Tourism	26%
	Foreign Population (percent of total population)	20%
	International letters (per capita)	25%
Data on Informational Flows (36%)	Internet Users (per 1000 people)	36%
	Television (per 1000 people)	36%
	Trade in Newspapers (percent of GDP)	28%
Data on Cultural Proximity (31%)	Number of McDonald's Restaurants (per capita)	43%
	Number of **I**ngvar **K**amprad **E**lmtaryd **A**gunnaryd (per capita)	44%
	Trade in books (percent of GDP)	12%

KOF Index of Globalisation – Political Globalisation

Political Globalisation	Weights
Embassies in Country	25%
Membership in International Organizations	28%
Participation in U.N. Security Council Missions	22%
International Treaties	25%

KOF Index of Globalisation, 2018

- Economic globalisation (33.3%), social globalisation (33.3%), political globalisation (33.3%).

KOF Index of Globalisation 2018 – Economic Globalisation

	Economic Globalisation	Weights
Trade Globalisation **(50%)**	Trade in goods	40.9
	Trade in services	45.0
	Trade partner diversification	14.1
Financial Globalisation **(50%)**	Foreign direct investment	27.5
	Portfolio investment	13.3
	International debt	27.2
	International reserves	2.4
	International income payments	29.6

KOF Index of Globalisation 2018– Social Globalisation

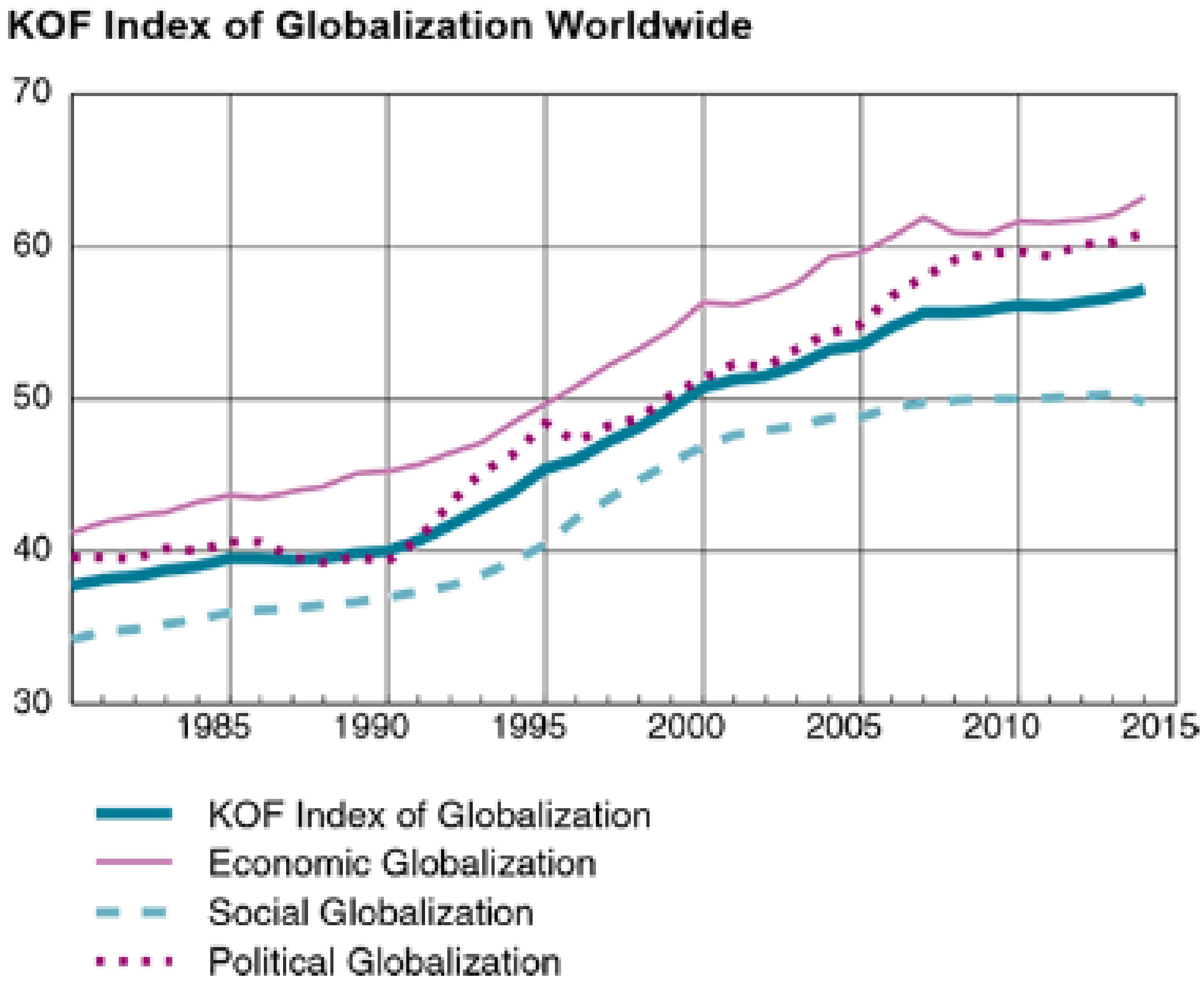
	Social Globalisation	Weights
Interpersonal Globalisation **(33.3%)**	International voice traffic	22.9
	Transfers	27.6
	International tourism	28.1
	Migration	21.4
Informational Globalisation **(33.3%)**	Patent applications	35.1
	International students	31.2
	High technology exports	33.7
Cultural Globalisation **(33.3%)**	Trade in cultural goods	22.6
	Trademark applications	13.3
	Trade in personal services	25.6
	McDonald's restaurant	23.2
	IKEA stores	15.3

KOF Index of Globalisation – Political Globalisation

Political Globalisation	Weights
Embassies	35.7
UN peace keeping missions	27.3
International NGOs	37.0

KOF Index of Globalisation – World

Source: http://globalization.kof.ethz.ch



2018 KOF Globalisation Index

Source: http://globalization.kof.ethz.ch

Rank	Country	Globalisation Index, 2015
1	Netherlands	90.24
2	Switzerland	89.70
3	Sweden	88.05
4	Austria	87.91
5	Belgium	87.87
6	Denmark	87.85
7	France	87.34
8	Germany	86.89
9	Finland	85.98
10	Norway	85.81

Rank	Country	Globalisation Index, 2016
1	Switzerland	91.17
2	Netherlands	90.97
3	Belgium	90.50
4	Sweden	89.88
5	UK	89.35
6	Denmark	89.14
7	Austria	88.95
8	Germany	88.17
9	France	87.20
10	Finland	86.99

2018 KOF Index of Globalisation (2016)

Source: http://globalization.kof.ethz.ch

Rank	Country	KOF Index	Rank	Country	KOF Index
84	Azerbaijan	63.89	36	Japan	78.37
9	France	87.20	26	Poland	81.20
96	India	61.18	58	Turkey	70.51
22	Italy	82.59	23	US	82.10

2018 KOF Index of Globalisation: Economic Globalisation, Social Globalisation, Political Globalisation (2016)

Source: http://globalization.kof.ethz.ch

Rank	Economic Globalisation	Social Globalisation	Political Globalisation
1	Singapore	Luxembourg	Italy
2	Netherlands	Norway	France
3	Belgium	Monaco	Germany
4	Luxembourg	Switzerland	Netherlands
5	Hong Kong, China	Canada	Spain
6	Ireland	United Kingdom	United Kingdom
7	Malta	Denmark	Sweden
8	Switzerland	Sweden	Switzerland
9	United Arab Emirates	Ireland	Belgium
10	Estonia	Austria	Austria
	Poland (39)	Poland (51)	Poland (21)

Attitudes toward globalisation

Proponents of globalisation

The World Economic Forum

The anti-globalisation movement

100,000 protest in Seattle against the World Trade Organization Third Ministerial conference

The alter-globalisation movement

The World Social Forum