"Globalization is on the whole a positive force for development and poverty reduction." Nicholas Stern, Chief Economist at the World Bank, 2002.

"[Globalization] is used in a normative sense to prescribe a strategy of development based on a rapid integration with the world economy: some see this as salvation, while others see it as damnation."
Deepak Nayyar, 2003.

ESSAY QUESTION: What is globalisation and how does it impact on development and poverty reduction? Do you agree that globalization is a positive force for development and poverty reduction? Substantiate your view.

You may draw from the chapter by Nayyar (provided) and other relevant sources to write the essay. The essay should be no more than 2000 words (approximately five A4 pages using 1.5 spacing). The essay is one of the criteria used in the process of selecting applicants for the Development Studies programme.

From: Chang, Ha-Joon. 2003. Rethinking Development Economics. Anthem Press: London.

GLOBALIZATION AND DEVELOPMENT*

Deepak Nayyar

This chapter endeavours to situate the process of globalization in the wider context of development. In doing so, it explores the implications of globalization for development in retrospect and prospect. The structure of the chapter is as follows. Section 1 sets out the essential meaning of development, in light of the very uneven development experience and the fundamental change in thinking about development strategies over the past fifty years. Section 2 outlines the dimensions and characteristics of globalization in our times. Section 3 examines the economic factors, the political conjuncture and the intellectual rationale underlying globalization. Section 4 explores the historical origins of globalization, comparing current trends in globalization with those of the late nineteenth century, and highlighting similarities and differences between the two. Section 5 discusses how globalization led to uneven development in the late nineteenth century. Section 6 considers the development experience of the world economy during the last quarter of the twentieth century, which suggests that the exclusion of countries and of people, attributable partly to the logic of markets, is a fact of life. It suggests that, without correctives, it would lead to uneven development now. Section 7 argues that sensible strategies of development in a world of globalization should create economic space for the pursuit of national interests and development objectives. In this task there is a strategic role for the nation state, both in the national and international context.

* This essay draws upon some earlier work of the author. See Nayyar 1995; 1997; 2000; 2001. The author would like to thank Ram Singh for helpful suggestions and valuable assistance.

1. Conception of development

There is a vast literature on economic development which is rich in both its range and depth. Yet there is not enough clarity about what development actually means. There are in fact many different views of what it constitutes, and these perceptions have changed over time. There is, however, an irreducible objective which may be construed as the essential meaning: development must bring about an improvement in the living conditions of people. It should, therefore, ensure the provision of basic human needs for all - not just food and clothing, but also shelter, health care and education. This simple but powerful proposition is often forgotten in the pursuit of material wealth and the conventional concerns of economics. Early literature on development emphasized economic growth and capital accumulation at a macro level; contemporary literature on development stresses economic efficiency and productivity increases at a micro level. Industrialization has always been seen as an essential attribute of development: emphasis has simply shifted from the pace of industrialization to the efficiency of industrialization.

The underlying presumption is that economic growth and economic efficiency are not only necessary but also sufficient to bring about an improvement in the living conditions of people. From time to time, dissenting voices questioned conventional wisdom about using economic growth, or increases in per capita income, as a measure of development, and instead suggested other indicators of development, such as reductions in poverty, inequality and unemployment, that would indicate changes in the quality of life.[1] But these aspects of development were largely ignored by mainstream economics because it did not make this distinction. Economic growth and economic efficiency, or for that matter industrialization, are means. It is development which is an end. Thus, in order to attain development, growth and efficiency need to be combined with full employment, poverty eradication, reduced inequality, human development and a sustainable environment. The purpose of development, after all, is to create a milieu that enables people, ordinary people, to lead a good life.

In conventional terms, the world has made enormous economic progress during the second half of the twentieth century. Over the past fifty years, world GDP has multiplied tenfold while per capita income has trebled.[2] The growth has been impressive even in the developing world, particularly when compared with the underdevelopment and the stagnation of the colonial era during the first half of the twentieth century. But such aggregates might conceal more than they reveal, for development has been very uneven between countries and within countries. The pattern of development has been such that it has led to an increase in the economic distance between the industrialized world and much of the developing world. It has also led to an increase in the economic distance between the newly industrializing countries, at one end, and the least developed countries, at the other. At the same time, economic disparities between regions and between people within countries have also registered an increase. In other words, many parts of the world and a significant proportion of its people have been largely excluded from development. This may be attributable to the logic of markets, which give to those who have and take away from those who have not, as the process of cumulative causation leads to market-driven virtuous circles and vicious circles. This may be the outcome of patterns of development where economic growth is uneven between regions and the distribution of its benefits is unequal between people, so that there is growing affluence for some combined with persistent poverty for many. This may be the consequence of strategies of development, as a similar economic performance in the aggregate could lead to egalitarian development in one situation, and growth which bypasses the majority of people in another situation.

Uneven development has its consequences. Poverty, inequality and deprivation persist. And there is poverty everywhere. One eighth of the people in the industrialized world are affected by, or live in, poverty. Almost one third of the people in the developing world - an estimated 1.5 billion - live in poverty and experience absolute deprivation insofar as they cannot meet their basic human needs. The same number does not have access to clean water. As many as 840 million people suffer from malnutrition. More than 260 million children who should be in school are not. Nearly 340 million women are not expected to survive to the age of 40. And, as we enter the 21st century, more than 850 million adults remain illiterate. Most of them live in the developing world. But, in a functional sense, the number of illiterate people in the industrialized countries - 100 million - is also large.[3]

It is clear that the development experience of the world economy since 1950 has been uneven and mixed. The attempts to analyse what turned out right and what went wrong have led to both diagnosis and prescription. This in turn has meant a fundamental change in thinking about development strategies.[4] In the postcolonial era, which began soon after the end of World War II, most underdeveloped countries adopted strategies of development which provided a sharp contrast with those of the first half of the twentieth century. For one, there was a conscious attempt to limit the degree of openness and integration with the world economy, in pursuit of a more autonomous development. For another, the state was assigned a strategic role in development because the market, by itself, was not perceived as sufficient to meet the aspirations of latecomers to industrialization. Both represented points of departure from the colonial era, which was characterized by open

economies and unregulated markets. In the early 1950s, this new approach also represented a consensus in thinking about the most appropriate strategy of industrialization. Despite a few voices of dissent it was, in effect, the development consensus at the time. 40 years later, in the early 1990s, perceptions about development apparently arrived at the polar opposite. Most countries in the developing world, as also in the erstwhile socialist bloc, began to reshape their domestic economic policies so as to integrate much more with the world economy and to enlarge the role of the market vis-a-vis the state. This was partly a consequence of internal crisis situations in economy, polity and society. It was also significantly influenced by the profound transformation in the world economic and political situation. The widespread acceptance of this approach, it would seem, represented a new consensus in thinking about development, which came to be known as the Washington Consensus. Although there was considerable dissent, this remained the dominant view, in part because it was propagated by the IMF and the World Bank, which exercised enormous influence on economies in crisis. However, this belief system was somewhat shaken by the financial crisis in Asia, and the Washington Consensus has also lost some of its lustre as the development experience during the 1990s has belied expectations. Its prescriptions are now subjected to question.[5] And the questions have not come from its critics alone.[6]

In spite of the paradigm shift from the development consensus of the 1950s to the Washington Consensus of the 1990s, the degree of openness vis-a-vis the world economy and the degree of intervention by the state in the market have remained the critical issues in the debate on development. The past fifty years have of course witnessed a complete swing of the pendulum in thinking about these issues. But the complexity of reality is not captured by either consensus. The reality, however, is clear. The exclusion of countries and of people from development has become much less acceptable with the passage of time. The proposition that economic growth, or economic efficiency, will ultimately improve the lot of the people is, obviously, far less credible 50 years later.

2. Contours of globalization

Globalization means different things to different people, and the word 'globalization' is used in two ways, which is itself a source of some confusion. It is used in a *positive* sense to *describe* a process of increasing integration into the world economy. It is used in a *normative* sense to *prescribe* a strategy of development based on a rapid integration with the world economy: some see this as salvation, while others see it as damnation.

Even its characterization, however, is by no means uniform. Globalization can be described, simply, as the expansion of economic activities across national boundaries. In this elementary sense, the world economy has experienced a progressive international economic integration since 1950. However, there has been a marked acceleration in this process of globalization during the last quarter of the twentieth century. There are three economic manifestations of this phenomenon - international trade, international investment and international finance - which also constitute its cutting edge. But there is much more to globalization than this. The term refers to the expansion of economic transactions and the organization of economic activities across political boundaries of nation states. More precisely, it can be defined as a process associated with increasing economic openness, growing economic interdependence and deepening economic integration in the world economy.

Economic *openness* is not simply confined to trade flows, investment flows and financial flows. It also extends to flows of services, technology, information and ideas across national boundaries. But the cross-border movement of people is closely regulated and highly restricted. Economic *interdependence* is asymmetrical. There is a high degree of interdependence among countries in the industrialized world, but considerable dependence of developing countries on the industrialized countries, and much less interdependence among countries in the developing world. It is important to note that a situation of interdependence is one where the benefits of linking and costs of delinking are about the same for both partners; where such benefits and costs are unequal between partners, a situation of dependence is implied. Economic *integration* straddles national boundaries as liberalization has diluted the significance of borders in economic transactions. Globalization is, in part, an integration of markets (for goods, services, technology, financial assets and even money) on the demand side, and, in part, an integration of production (horizontal and vertical) on the supply side.

The gathering momentum of globalization has brought about profound changes in the world economy. It is worth highlighting the characteristics of these changes.[7] An increasing proportion of world output is entering into world trade, while an increasing proportion of world trade is made up of intra-firm trade. Between the early 1970s and the late 1990s, the share of world exports in world GDP rose from 1 /8 to almost 1/5.[8] The share of intra-firm trade in world trade, which was 1/5 in the early 1970s, rose to 1/3 in the early 1990s.[9] The significance of international investment flows also registered a rapid increase. Between 1980 and 1996, the stock of direct foreign investment in the world as a proportion of world output rose from less than 5% to more than 10%, while world direct foreign investment flows as a proportion of world gross fixed capital formation rose from 2% to almost 6%.[10]

The growth in international finance has been explosive, so much so that, in terms of magnitudes, trade and investment are now dwarfed by finance. The expansion of international banking is phenomenal, while the international market for financial assets has experienced a similar growth. There is a growing international market for government bonds;[11] the size of international foreign exchange markets is staggering. Global foreign exchange transactions have soared from $60 billion per day in 1983 to $1500 billion per day in 1997.[12] By comparison, in 1997, world GDP was $82 billion per day and world exports were $ 16 billion per day, while the foreign exchange reserves of all central banks put together were $1550 billion.[13]

3. Origins and foundations

The origins of globalization need to be analysed in terms of the economic factors underlying the process, the political circumstances that have enabled it to gather momentum and the intellectual rationale that is now almost prescriptive. We will consider each of these issues in turn.

The economic factors which have made globalization possible are: the dismantling of barriers to international economic transactions; the development of enabling technologies; and emerging forms of industrial organization. Globalization has followed the sequence of deregulation in the world economy. Trade liberalization came first, which led to an unprecedented expansion of international trade between 1950 and 1970. The liberalization of regimes for foreign investment came next, while a surge in international investment began in the late 1960s. Financial liberalization came last, starting in the early 1980s. This had two dimensions: the deregulation of the domestic financial sector in the industrialized countries and the introduction of convertibility on capital account in the balance of payments. These did not occur simultaneously. The United States, Canada, Germany and Switzerland removed restrictions on capital movements in 1973, while Britain and Japan did so in 1979 and 1980 respectively, and France and Italy made the transition as late as 1990. The globalization of finance, which has happened at a scorching pace since the mid-1980s, is not unrelated to the dismantling of regulations and controls.

The technological revolution in transport and communications has been a crucial factor in globalization. The second half of the twentieth century has witnessed the advent of jet aircraft, computers and satellites. The synthesis of communications technology, which is concerned with the transmission of information, and computer technology which is concerned with the processing of information, has created information technology that is remarkable in both scope and speed. These technological developments have had a dramatic

impact on reducing geographical barriers. The time needed is a tiny fraction of what it was earlier, while cost incurred has been sharply reduced.

New forms of industrial organization have played a role in making globalization possible. The emerging flexible production system, shaped by the nature of technical progress, the changing output mix and the organizational characteristics (based on Japanese management systems) is forcing firms to constantly choose between trade and investment in their drive to expand activities across borders. The declining share of wages in production costs, the increasing importance of proximity between producers and consumers and the growing externalization of services are exercising a strong influence on the strategies and behaviour of firms in the process of globalization.

The politics of hegemony or dominance is conducive to the economics of globalization. The process of globalization, beginning in the early 1970s, has coincided with the political dominance of the United States as superpower. This political dominance has grown stronger with the collapse of communism and the triumph of capitalism, while political circumstances have transformed the concept of globalization into a Virtual ideology[5] for our times. Dominance in the realm of politics is associated with an important attribute in the sphere of economics. For globalization requires a dominant economic power with a national currency which is accepted as the equivalent of international money: as a unit of account, a medium of exchange and a store of value. This role is being performed by the US dollar.

Economic theorizing often follows in the footsteps of political reality. It should come as no surprise, then, that recent years have witnessed the formulation of an intellectual rationale for globalization that is almost prescriptive. Globalization is perceived as a means of ensuring not only efficiency and equity but also growth and development in the world economy, and the analytical foundations of this world view are provided by the neoliberal model. Orthodox neoclassical economics suggests that intervention in markets is inefficient, while neoliberal political economy argues that governments are incapable of intervening efficiently. The essence of the neoliberal model, then, can be stated as follows. First, the government should be rolled back wherever possible so that it approximates to the ideal of a minimalist state. Second, the market is not only a substitute for the state but also the preferred alternative because it performs better. Third, resource allocation and resource utilization must be based on market prices which should conform as closely as possible to international prices. Fourth, national political objectives, domestic economic concerns or even national boundaries should not act as constraints. In conformity with this world view, governments everywhere, particularly in the developing countries and the former communist countries, are being urged or pushed into a comprehensive agenda of privatization (to minimize the role of

the state) and liberalization (of trade flows, capital flows and financial flows). It is suggested that such policy regimes would provide the foundations for a global economic system characterized by free trade, unrestricted capital mobility, open markets and harmonized institutions. The ideologues believe that such globalization promises economic prosperity for countries that join the system and economic deprivation for countries that do not.[14] It needs to be stressed that this intertwined normative and prescriptive view of globalization is driven in part by ideology and in part by hope. It is not borne out by experience.

4. Historical parallel

There is a common assumption that the present set of circumstances, with globalization changing the character of the world economy, is altogether new and represents a fundamental departure from the past. However, such an assumption is incorrect: globalization is in fact nothing new. There was a similar phase of globalization which began a century earlier, around 1870, and gathered momentum until 1914, when it came to an abrupt end. The period from 1870 to 1914 was also the age of *laissez-faire*. Government intervention in economic activity was minimal and the movement of goods, capital and labour across national boundaries was almost unhindered. It was believed that the virtuous circle of rapid economic growth and the process of international economic integration in this era were closely related.

In many ways, the world economy in the late twentieth and early 21st centuries resembles the world economy in the late nineteenth century.[15] The parallels between the two periods are striking. The integration of the world economy through international trade at the turn of the nineteenth century was about the same as it was towards the end of the twentieth. For 16 major industrialized countries, now in the OECD, the share of exports in GDP rose from 18.2% in 1900 to 21.2% in 1913, even though tariffs were then much higher.[16] The story was about the same for international investment. In 1913, the stock of direct foreign investment in the world economy was 9% of world output.[17] At constant prices, total foreign investment in the world economy in 1914 was 4/5 of what it was in 1980.[18] What is more, the stock of foreign investment in developing countries was probably equal to about 1/4 their GDP at the turn of the century, and at constant prices, in 1914, this stock was almost double what it was in 1980.[19] The integration of markets for international finance was also comparable. The cross-national ownership of securities, including government bonds, reached very high levels.[20] International bank lending was substantial and, in relative terms, net international capital flows were much bigger than they are now. The only missing dimension was

international transactions in foreign exchange (given the regime of fixed exchange rates under the gold standard).

There are striking similarities in the underlying factors which made globalization possible then and now.[21] There were almost no restrictions on the movement of goods, capital and labour across national boundaries, so that there was no need to dismantle barriers or liberalize regimes for international economic transactions. The advent of the steamship, the railway and the telegraph brought about a revolution in transport and communications.[22] This led to an enormous reduction in the time needed, and the cost incurred, in traversing geographical distances. Emerging forms of industrial organization performed a critical role. In the late nineteenth century, the advent of mass production was characterized by a rigid compartmentalization of functions and a high degree of mechanization. Mass production realized economies of scale and led to huge cost reductions compared with craft manufacturing.[23] Apart from dominance in the realm of politics, *Pax Britannica* provided a reserve currency, the pound sterling, which was the equivalent of international money. For this was 'the age of empire' when Britain more or less ruled the world.[24]

There are also important differences between the two phases of globalization. I would like to highlight four such differences: in trade flows, in investment flows, in financial flows and most important, perhaps, in labour flows, across national boundaries.

There are differences in the composition of trade and in the channels of trade. During the period from 1870 to 1913, an overwhelming proportion of international trade was constituted by inter-sectoral trade, where primary commodities were exchanged for manufactured goods. The trade was to a significant extent based on absolute advantage derived from natural resources or climatic conditions. Although trade flows were in the domain of large international firms, it was not intra-firm trade.

Differences also exist in the geographical destination and the sectoral distribution of investment flows. In 1914, the stock of long-term foreign investment in the world economy was distributed as follows: 55% in the industrialized world (30% in Europe, 25% in the United States) and 45% in the underdeveloped world (20% in Latin America and 25% in Asia and Africa). It is clear that developing countries are now far less central to the process.[25]

In 1913, the primary sector accounted for 55% of long-term foreign investment in the world, while transport, trade and distribution accounted for another 30%; the manufacturing sector accounted for only 10% and much of this was concentrated in North America or Europe.[26] The primary sector is now far less significant, while the manufacturing sector is much more important. In financial flows, there are substantial differences in the destination, the

object, the intermediaries and the instruments. In the last quarter of the nineteenth century, capital flows were a means of transferring investible resources to underdeveloped countries or newly-industrialized countries with the most attractive growth opportunities. The object was to find avenues for long-term investments in search of profits. Banks were the only intermediaries between lenders and borrowers in the form of bonds with very long maturities. Securitization of long-term bonds with sovereign guarantees was provided by the imperial powers or the governments in the borrowing countries.

But there is a fundamental difference between the two phases of globalization. It is in the sphere of labour flows. In the late nineteenth century, there were no restrictions on the mobility of people across national boundaries. Passports were seldom needed, and immigrants were granted citizenship with ease. Between 1870 and 1914, international labour migration was enormous. During this period, about 50 million people left Europe, of whom 2/3 went to the United States while the remaining 1/3 went to Canada, Australia, New Zealand, South Africa, Argentina and Brazil.[27] This mass emigration from Europe amounted to 1/8 of its population in 1900. But that was not all: beginning somewhat earlier, following the abolition of slavery in the British empire, about 50 million people left India and China to work as indentured labour on mines, plantations and construction in Latin America, the Caribbean, Southern Africa, South East Asia and other distant lands.[28] The destinations were mostly British, Dutch, French and German colonies. In the second half of the twentieth century, there was a limited amount of international labour migration from the developing countries to the industrialized world during the period 1950-1970. Since then, however, international migration has been reduced to a trickle because of draconian immigration laws and restrictive consular practices. The present phase of globalization has found substitutes for labour mobility in the form of trade and investment flows. For one, industrialized countries now import manufactured goods that embody scarce labour. For another, industrialized countries export capital which employs scarce labour abroad to provide such goods.

5. Uneven development

The ideologues believe that globalization led to rapid industrialization and economic convergence in the world economy during the late nineteenth century. In their view, the promise of the emerging global capitalist system was wasted for more than half a century, first by three decades of conflict and autarchy that followed World War I and subsequently, for another three decades, by the socialist path and a statist world view. The return of globalization in the late twentieth century is thus seen as the road to salvation. The

conclusion drawn is that globalization now — as much as then — promises economic prosperity for countries that join the system and economic deprivation for countries that do not.[29] For those who recall the development experience in the late nineteenth century, it should be obvious that the process of globalization will not reproduce or replicate the United States everywhere, just as it did not reproduce Britain everywhere a century earlier. This historical example reveals how globalization was already associated with uneven development, and is bound to produce uneven development now, not only between countries but also within countries.

The economic consequences of globalization in the late nineteenth century were, to say the least, asymmetrical. In this era, most of the gains from international economic integration accrued to the imperial countries which exported capital and imported commodities. There were a few countries like the United States and Canada - new lands with temperate climates and white settlers - which also derived some benefits. In these countries, the preconditions for industrialization were already being created; this process was strengthened by international economic integration, and was reinforced by direct foreign investment in manufacturing activities stimulated by rising tariff barriers, combined with technological and managerial flows. The outcome - industrialization and development - did not happen everywhere. Development was uneven in the industrial world, and much of southern and eastern Europe lagged behind. This meant divergence rather than convergence in terms of industrialization and growth.[30] There was, in fact, an increase in economic inequalities between countries and within countries. The income gap between the richest and the poorest countries, for instance, which was just 3:1 in 1820, more than doubled to 7:1 in 1870 and increased further to 11:1 in 1913.[31] Countries in Asia, Africa and Latin America, particularly the colonized, which were also a part of this process of globalization, were even less fortunate. Indeed, during the same period of rapid international economic integration, some of the most open economies in this phase of globalization - India, China and Indonesia - experienced deindustrialization and underdevelopment. We need to remind ourselves that, in the period from 1870 to 1914, these three countries practised free trade as much as the United Kingdom and the Netherlands, where average tariff levels were close to negligible (3-5%); by contrast, tariff levels in Germany, Japan and France were significantly higher (12-14%), and tariff levels in the United States were very much higher (33%).[32] What is more, these three countries were also among the largest recipients of foreign investment.[33] But their globalization did not lead to development. The outcome was similar elsewhere: in Asia, Africa and Latin America. So much so, that between 1860 and 1913 the share of developing countries in world manufacturing output declined from over 1/3 to

under 1/10.[34] In these economies, export-oriented production in mines, plantations and cash-crop agriculture created enclaves which were integrated with the world economy in a vertical division of labour. But there were almost no backward linkages. Productivity levels outside the export enclaves stagnated at low levels. They simply created dualistic economic structures where the benefits of globalization accrued mostly to the outside world and in small part to the local elites.

The growing inequalities between and within countries, particularly in the industrial world, were perhaps a significant factor underlying the retreat from globalization after 1914. The following passage, written by John Maynard Keynes in 1919, vividly highlights the benefits of globalization for some people and some countries, but also recognizes how economic and political conflicts associated with the process stopped what had seemed irreversible at the time.

> What an extraordinary episode in the economic progress of man that age was which came to an end in August 1914. The greater part of the population, it is true, worked hard and lived at a low standard of comfort, yet were, to all appearances, reasonably contented with this lot. But escape was possible, for any man of capacity or character at all exceeding the average, into the middle and upper classes, for whom life offered, at a low cost and with the least trouble, conveniences, comforts, and amenities beyond the compass of the richest and most powerful monarchs of other ages. The inhabitant of London could order by telephone, sipping his morning tea in bed, the various products of the whole earth, in such quantity as he may see fit and reasonably expect their early delivery upon his doorstep; he could at the same moment and by the same means adventure his wealth in the natural resources and new enterprises of any quarter of the world, and share, without exertion or trouble, in their prospective fruits and advantages; or he could decide to couple the security of his fortunes with the good faith of the townspeople of any substantial municipality in any continent that fancy or information might recommend. He could secure forthwith, if he wished it, cheap and comfortable means of transit to any country or climate without any passport or other formality, could despatch his servants to the neighbouring office of a bank for such supply of the precious metals as might seem convenient, and could then proceed to foreign quarters, without knowledge of their religion, language or customs, bearing coined wealth upon his person, and could consider himself greatly aggrieved and much surprised at least interference. But most important of all, he regarded this state of affairs as normal, certain, and permanent, except in the direction of further improvement, and any deviation from it as aberrant, scandalous and avoidable. The projects and politics of militarism and imperialism, of racial and cultural rivalries, of monopolies, restrictions and exclusions, which were to play the serpent to this paradise, were little more than amusement of his daily newspaper, and appeared to exercise almost no influence at all on the ordinary course of social and economic life, the internationalization of which was nearly complete in practice[35]

The process of globalization has led to uneven development, now as much as then. The reality that has unfolded so far clearly belies the expectations of the ideologues.

6. Globalization, development and exclusion

The development experience of the world economy from the early 1970s to the late 1990s, which could be termed the 'age of globalization', provides cause for concern, particularly when it is compared with the period from the late 1940s to the early 1970s, which has been described as the golden age of capitalism. Any such periodization is obviously arbitrary, but it serves an analytical purpose.[36]

Available evidence suggests that the past 25 years have witnessed a divergence, rather than convergence, in levels of income between countries and between people. Economic inequalities have increased during the last quarter century as the income gap between rich and poor countries, between the rich and the poor within countries, as well as between the rich and the poor in the world's population, has widened,[37] and income distribution has worsened.[38] The incidence of poverty increased in most countries of Latin America and Sub Saharan Africa during the 1980s and in much of Eastern Europe during the 1990s, Many countries in East Asia, South East Asia and South Asia, which experienced a steady decline in the incidence of poverty, constitute the exception. However, the recent financial meltdown and economic crisis in South East Asia has led to a marked deterioration in the situation. In the developing countries, employment creation in the organized sector continues to lag behind the growth in the labour force, so that an increasing proportion of workers are dependent upon low productivity and casual employment in the informal sector. Unemployment in the industrialized countries has increased substantially since the early 1970s and remained at high levels since then, except in the United States, while there has been almost no increase in the real wages of a significant proportion of the workforce in many industrialized countries. Inequality in terms of wages and incomes has registered an increase almost everywhere in the world. Over the same period, the rate of

growth in the world economy has also registered a discernible slowdown. And the slower growth has been combined with greater instability. It would seem that, in some important respects, the world economy fared better in the golden age than it has done in the age of globalization.

It is obviously not possible to attribute cause-and-effect simply to the coincidence in time. But it is possible to think of mechanisms through which globalization may have accentuated inequalities. Trade liberalization has led to a growing wage inequality between skilled and unskilled workers not only in industrialized countries but also in developing countries.[39] As a consequence of privatization and deregulation, capital has gained at the expense of labour almost everywhere, for profit shares have risen while wage shares have fallen.[40] Structural reforms, which have cut tax rates and brought flexibility to labour markets, have reinforced this trend. The mobility of capital combined with the immobility of labour has changed the nature of the employment relationship and has reduced the bargaining power of trade unions. The object of managing inflation has been transformed into a near-obsession by the sensitivity of international financial markets, so that governments have been forced to adopt deflationary macroeconomic policies that have squeezed both growth and employment. The excess supply of labour has repressed real wages. Financial liberalization, which has meant a rapid expansion of public as well as private debt, has been associated with the emergence of a new rentier class, and the inevitable concentration in the ownership of financial assets has probably contributed to a worsening of income distribution.[41] Global competition has driven large international firms to consolidate market power through mergers and acquisitions, a process which has made market structures more oligopolistic than competitive. The competition for export markets and foreign investment between countries has intensified in what is termed ca race to the bottom', leading to an unequal distribution of gains from trade and investment.

Globalization has indeed created opportunities for some people and some countries that could not have been considered three decades ago. But it has also introduced new risks, if not threats, for many others. It has been associated with a deepening of poverty and an accentuation of inequalities. The distribution of benefits and costs is unequal. There are some winners: more in the industrialized world than in the developing world. There are many losers: numerous both in the industrialized world and in the developing world. It is perhaps necessary to identify, in broad categories, the winners and the losers.[42]

The winners are asset-owners, profit-earners, rentiers, the educated, the mobile and those with professional, managerial or technical skills, whereas asset-less, wage-earners, debtors, the uneducated, the immobile and the semi-

skilled or unskilled are the losers. If we think of firms, large, international, global, risk-takers and technology-leaders are the winners, whereas small, domestic, local, risk-averse and technology-followers are the losers. If we think of economies, capital-exporters, technology-exporters, net lenders, those with a strong physical and human infrastructure, and those endowed with structural flexibilities are the winners, whereas capital-importers, technology-importers, net borrowers, those with a weak physical and human infrastructure, and those characterized by structural rigidities are the losers. It should be said that this classification is suggestive rather than definitive, for it paints a broad-brush picture of a more nuanced situation. But it does convey the simultaneous, yet asymmetrical, inclusion and exclusion that characterizes the process of globalization. It is not surprising, then, that the spread of globalization is uneven and limited both among people and across countries.[43]

Joan Robinson once said: 'There is only one thing that is worse than being exploited by capitalists. And that is not being exploited by capitalists.' Much the same can be said about markets and globalization, which may not ensure prosperity for everyone but may in fact exclude a significant proportion of people. Markets exclude people as consumers or buyers if they do not have any incomes, or sufficient incomes, which can be translated into purchasing power. Such people are excluded from the consumption of goods and services which are sold in the market. This exclusion is attributable to a lack of entitlements.[44] Markets also exclude people as producers or sellers if they have neither *assets* nor *capabilities;* people experience such exclusion if they do not have assets, physical or financial, which can be used (or sold) to yield an income in the form of rent, interest or profits. Even those without assets, however, people can enter the market as sellers, using their labour, if they have some capabilities. Such capabilities that are acquired through education, training or experience are different from natural abilities which are endowed. But the distribution of capabilities may be just as unequal, if not more so. It is these capabilities which can, in turn, yield an income in the form of wages. Hence, people without capabilities, the poor, who cannot find employment, are excluded. In fact even people with capabilities may be excluded from employment if there is no demand for their capabilities in the (labour) market. In the ultimate analysis, such capabilities are defined by the market: that is the problem.

Globalization has introduced a new dimension to the exclusion of people from development. Exclusion is no longer simply about the inability to satisfy basic human needs in terms of food, clothing, shelter, health care and education for large numbers of people. It is much more complicated. For, coupled with globalization, the consumption patterns and lifestyles of the rich have increasingly powerful demonstration effects. People everywhere, even the

poor and the excluded, are exposed to these ever-expanding frontiers of consumer choice because the electronic media has spread the consumerist message far and wide. This creates both expectations and aspirations. But the simple fact of life is that those who do not have the incomes cannot buy goods and services in the market. When the paradise of consumerism is unattainable, which is the case for common people, frustration or alienation is often created. The reaction of people who experience such exclusion differs. Some seek short cuts to the consumerist paradise through drugs, crime or violence. Some seek refuge in ethnic identities, cultural chauvinism or religious fundamentalism.[45] Such assertion of traditional or indigenous values is often the only thing that poor people can assert, for these values contribute identity and meaning to their lives. Outcomes do not always take these extreme forms, although globalization inevitably tends to erode social stability.[46] Thus, economic integration with the world outside may accentuate social tensions or provoke social fragmentation within countries.

7. The state and development in the context of globalization

At the start of the 21st century, the facts of life in the world economy are clear. The name of the game is globalization , and no country wishes to be excluded from it: even large countries cannot afford to opt out. The choice, then, is between a market-driven, passive, insertion into the world economy and a selective, strategic, integration into the world economy. The sensible choice would be to opt for the latter. But is it possible to contemplate correctives that would make this market-driven process more people-friendly so that the outcome is globalization with a human face? The object of such a design should., be to provide more countries with opportunities to improve their development prospects and more people within these countries with opportunities to improve their living conditions.

Globalization has reduced the autonomy of the nation state in matters economic, if not political, but there remain degrees of freedom which must be exploited in the pursuit of development. The ideology of globalization seeks to harmonize not only policy regimes but also institutions, including the economic role of the state, across the world. This is a mistake, because the role of the state in an economy depends on both level of income and stage of development. The object of any sensible strategy of development in a world of liberalization and globalization should be to create economic space for the pursuit of national interests and development objectives. In this task, there is a strategic role for the nation state, not only in the sphere of domestic economic policies but also in the arena of economic and political interaction with the outside world.[47]

Consider the national context. First, in countries that are latecomers to industrialization, the state must create the conditions for the development of industrial capitalism. In the earlier stages of industrialization, this means creating a physical infrastructure through government investment, investing in the development of human resources through education and catalysing institutional change, say, through agrarian reform. In the later stages of industrialization, this means using strategic industrial policy for the development of technological and managerial capabilities at a micro level, establishing institutions that would facilitate, regulate and govern the functioning of markets, and evolving strategic interventions interlinked across activities to guide the market in the pursuit of long-term development objectives. It must be emphasized that the benefits of integration with the world economy would accrue only to those countries which have laid these requisite foundations. Indeed, creating the preconditions and using strategic intervention are essential for internalizing (maximizing) the benefits and externalizing (minimizing) the costs of globalization.

Second, in the search for foreign investment, the state must resist the temptation to provide incentives and concessions. Indeed, wherever possible, the state must bargain with large international firms. Such an approach would not only improve the distribution of gains from economic transactions with transnational firms but also ensure that their activities are conducive to development. The reason for this is simple. Transnational corporations are in the business of profit while governments are in the business of development. For large countries, this means strategic negotiations in the sphere of trade and investment. For small countries, this means a conscious decision to opt out of 'a race to the bottom'. But this can only be done by governments and not by individuals or firms.

Third, the state must ensure a prudent macro management of the economy, particularly in the sphere of government finance, for two reasons. First, it saves governments from being forced into stabilization and adjustment programmes that come with high conditionality which, in turn, reduces degrees of freedom in the pursuit of development objectives. For another, it reduces the vulnerability and problems associated with rapid integration into international financial markets through portfolio investment or capital account convertibility. The bottom line is that such prudence can enable a country to avoid some of the costs of integration through globalization and, at the same time, to obtain some of the benefits by retaining the freedom to create the necessary conditions.

Consider the international context. In a world of unequal partners, it is not surprising that the rules of the game are asymmetrical in terms of construct and inequitable in terms of outcome. The strong have the power to make, and

the authority to implement the rules. Conversely, the weak can neither set nor invoke the rules. The problem, however, takes different forms: there are different rules in different spheres, there are rules for some and not for others, and the agenda for new rules is partisan.

The existing (and prospective) rules of the WTO regime allow few exceptions and provide little flexibility to countries that are latecomers to industrialization. In comparison, there was more room for manoeuvre in the erstwhile GATT, *inter alia,* because of special and differential treatment for developing countries. The new regime is much stricter in terms of law and its implementation. The rules on trade in the new regime will make the selective protection or strategic promotion of domestic firms vis-a-vis foreign competition much more difficult. The tight system for the protection of intellectual property rights might pre-empt or stifle the development of domestic technological capabilities. The possible multilateral agreement on investment, when it materializes, will almost certainly reduce the possibilities of strategic bargaining with transnational firms. Similarly, commitments on structural reform, an integral part of stabilization and adjustment programmes with the IMF and the World Bank, inevitably prescribe industrial deregulation, privatization, trade liberalization and financial deregulation. Taken together, such rules and conditions are bound to curb the use of industrial policy, technology policy, trade policy and financial policy as strategic forms of intervention to foster industrialization. It must be recognized that such state intervention was crucial for development in the success stories among late industrializers during the second half of the twentieth century.[48]

In the changed international context, nation states in the developing world must endeavour to influence the rules of the game so that the outcome is more ' equitable. It need hardly be said that the nature of the solution depends upon the nature of the problem. Where there are different rules in different contexts, it is necessary to make such rules consistent. Where there are rules for some but not for others, it is necessary to ensure that the rules are uniformly applicable to all. Where the agenda for new rules is partisan, it is imperative to redress the balance in the agenda. However, fair rules are necessary but not sufficient. For a game is not simply about rules; it is also about players. And, if one of the teams or one of the players does not have adequate training and preparation it would simply be crushed by the other. In other words, the rules must be such that newcomers or latecomers to the game - for example, developing countries - are provided with the time and the space to learn so that they are competitive players rather than pushover opponents.

There is a clear need for greater consistency in the rules of the multilateral trading system embodied by the WTO. If developing countries provide access to their markets, this access should be matched with some corresponding

access to technology. If there is almost complete freedom for capital mobility, the draconian restrictions on labour mobility should at least be reduced. Similarly, the rules of the multilateral financial institutions, implicit in the conditionalities of the IMF and the World Bank, applicable only to deficit countries or to borrowing countries, should be reshaped so that the standardized and inflexible package of policies is not imposed on countries irrespective of time and space, particularly where some elements of this package are not consistent with national development objectives in the long term.

It needs to be said that governing globalization is just as important as reducing asymmetries in its rules. The momentum of globalization is such that the power of national governments is being reduced through incursions into hitherto sovereign economic and political space, without a corresponding increase in effective international cooperation or supra-national government which could regulate this market-driven process. Global governance, however, is not so much about world government as it is about institutions and practices combined with rules that facilitate cooperation among sovereign nation states[49].

Notes

1 See, for example, Baster 1972, Seers 1972 and Morris 1979. In recent years, this view has been put forward strongly by the UNDP in its *Human Development Reports.*
2 Gf. UNDP 1999, p. 25.
3 The evidence in this paragraph is from UNDP 1999.
4 For an analysis of contending views on openness and intervention, see Nayyar 1997.
5 See, for example, Killick 1984, Cornia et al. 1987, Taylor 1988, Bhaduri 1992, Cooper 1992, Taylor 1993 and Bhaduri and Nayyar 1996.
6 SeeStiglitz 1998.
7 For a detailed discussion, see Nayyar 1995 and 1997.
8 The export-GDP ratios are from UNCTAD, *Handbook of International Trade and Development Statistics* and UN, *Yearbook of National Accounts Statistics,* various issues.
9 UNCTAD 1994, p. 143.
10 UNCTAD 1998, pp. 385, 399.
11 For evidence on the growth of international finance, see Nayyar 1995 and 1997. See also UNDP 1999, p. 25.
12 Bank for International Settlements, *Survey of Foreign Exchange Market Activity,* various issues.
13 The value of world GDP and exports in 1997, reported by the UN, has been converted into an average daily figure for the purpose of comparison. The figure on foreign exchange reserves is from the *IMF Annual Report 1998.*
14 See, for example, Sachs and Warner 1995.
15 This historical parallel was the theme of my Presidential Address to the Indian Economic Association in December 1995 (Nayyar 1995).
16 Cf. Bairoch 1982 and Maddison 1989.
17 UNCTAD 1994, p. 130.

18 At 1980 prices, total foreign investment in 1914 was $347 billion (Maddison 1989). The actual stock of direct foreign investment in 1980 was $448 billion (UNCTAD 1994).
19 SeeNayyar 1997.
20 In 1913, foreign securities constituted 59% of all securities traded in London. Similarly, in 1908, the corresponding proportion was 53% in Paris. See Morgenstern 1959.
21 For a discussion of these underlying factors, see Nayyar 1995.
22 For example, the substitution of steam for sails, and of iron for wooden hulls in ships, reduced ocean freight by 2/3 between 1870 and 1900 (Lewis 1977).
23 The production of perfectly interchangeable parts, the introduction of the moving assembly line by Ford, and methods of management evolved by Taylor, provided the foundations for this new form of industrial organization. See Oman 1994.
24 Cf. Hobsbawm 1987.
25 The total foreign investment of $44 billion was distributed as follows: $ 14 billion in Europe, $ 10.5 billion in the USA, $8.5 billion in Latin-America, and $11 billion in Asia and Africa (UNGTAD , *World Investment Report*, 1994, p. 415).
26 See Dunning 1983.
27 Cf. Lewis 1978.
28 See Tinker 1974 and Lewis 1977.
29 The best example is Sachs and Warner 1995.
30 See Bairoch and Kozul-Wright 1996.
31 Maddison 1995.
32 See Maddison 1989 and Bairoch 1982.
33 Cf. Maddison 1989.
34 Cf. Bairoch 1982.
35 Keynes 1919, pp. 9-10.
36 The quarter century that followed World War II was a period of unprecedented pros perity, earning the title of the *golden age of capitalism.* See Marglin and Schor 1990 and Maddison 1982. The *age of globalization,* a phrase that has not been used, is suggested by the author in order to facilitate comparison.
37 For evidence, see UNCTAD 1997, UNDP 1999 and IMF 1997.
38 The ratio of the average GNP per capita of the richest quintile of the world's popula tion to that of the poorest quintile rose from 31:1 in 1965 to 60:1 in 1990 (UNCTAD 1997, p. 81) and 74:1 in 1997 (UNDP 1999, p. 3). The ratio of per capita income in the richest country to that in the poorest rose from 35:1 in 1950 to 44:1 in 1973 and 72:1 in 1992 (Maddison 1995 and UNDP 1999).
39 See UNCTAD 1997; Wood 1994 and 1997; Stewart 2000.
40 Some evidence is reported in UNCTAD 1997. See also Stewart 2000.
41 This argument is developed in UNCTAD 1997.
42 Cf. Streeten 1996, who draws up a balance sheet of globalization.
43 For a discussion, and evidence, on this issue, see Nayyar 2000.
44 This term was first used by Sen 1981 in his work on poverty and famines.
45 See Streeten 1996, who also cites Benjamin Barber *(Jihad vs Me World,* New York, Random House, 1995) on this issue.
46 See Rodrik 1997.
47 For a more detailed analysis, see Nayyar 1997 and 2000.
48 See Amsden 1989, Wade 1990 and Chang 1996.
49 Global governance is analyzed, at some length, in Nayyar 2002.

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