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Globalization versus Internationalization, and Four Economic Arguments for Why Internationalization is a Better Model for World Community

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I. Introduction. -This discussion has three parts: first I will distinguish two concepts often confused, namely internationalization versus globalization. Second, I will consider four negative consequences of globalization which to my mind constitute four good reasons for rejection globalization, and in favor of internationalization as the model to follow. Third, I will consider the two most common objections to the case I have made against globalization (or for internationalization), and offer a refutation of each. No doubt there are other objections that I have not anticipated. Certainly there are various legitimate definitions of the term "globalization" corresponding to different purposes. My purpose is to consider critically the direction in which the world economy is being led by the IMF, the World Bank, and the WTO, and I define globalization in the way that to me at least most clarifies alternatives and policy choices faced by these institutions.

II. An Important Distinction.--The newspapers and TV say that if you oppose globalization you must be an "isolationist" or even worse a "xenophobe". Nonsense. The relevant alternative to globalization is internationalization, which is neither isolationist nor xenophobic. The media don't know the difference, so let us define the terms clearly:

Internationalization refers to the increasing importance of relations between nations: international trade, international treaties, alliances, protocols, etc. The basic unit of community and policy remains the nation, even as relations among nations, and among individuals in different nations, become increasingly necessary and important.

Globalization refers to global economic integration of many formerly national economies into one global economy, by free trade, especially by free capital mobility, and also, as a distant but increasingly important third, by easy or uncontrolled migration. Globalization is the effective erasure of national boundaries for economic purposes. National boundaries become totally porous with respect to goods and capital, and increasingly porous with respect to people, viewed in this context as cheap labor, or in some cases cheap human capital.

In sum, globalization is the economic integration of the globe. But exactly what is "integration"? The word derives from "integer", meaning one, complete, or whole. Integration means much more than "interdependence"--it is the act of combining separate albeit related units into a single whole. Interdependence is to integration as friendship is to marriage. Since there can be only one whole, only one unity with reference to which parts are integrated, it follows that global economic integration logically implies national economic disintegration -- parts are torn out of their national context (dis-integrated), in order to be re-integrated into the new whole, the globalized economy. As the saying goes, to make an omelet you have to break some eggs. The disintegration of the national egg is necessary to integrate the global omelet. This obvious logic, as well as the cost of disintegration, is frequently met with denial.

Denial aside, all that I have just said was expressed with admirable clarity, honesty, and brevity by Renato Ruggiero, former director-general of WTO: *"We are no longer writing the rules of interaction among separate national economies. We are writing the constitution of a single global economy."* This is a clear affirmation of globalization and rejection of internationalization as just defined. It is also a radical subversion of the Bretton Woods Charter. Internationalization is what the Bretton Woods Institutions were designed for, not globalization.

After the April 2000 disruption of its meetings in Washington DC, the World Bank sponsored an internet discussion on globalization. The closest they came to offering a definition of the subject under discussion was the following: *"the most common 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)".* Mr. Wolfensohn, president of the World Bank, told the audience at the Aspen Institute's Conference on Globalization, that *"Globalization is a practical methodology for empowering the poor to improve their lives."* That is a wish, not a definition.

Does economic integration imply or entail political and cultural integration? I suspect it does over the long run, but I honestly do not know which would be worse--an economically integrated world with, or without, political integration. Everyone recognizes the desirability of community for the world as a whole-- but we have two very different models of world community: (1) a federated community of real national communities (internationalization), versus (2) a cosmopolitan direct membership in a single abstract global community (globalization).

If the IMF-WB-WTO are no longer serving the interests of their member nations as per their charter, then whose interests are they serving? The interests of the integrated "global economy" we are told. But what concrete reality lies behind that grand abstraction? Not real individual workers, peasants, or small businessmen, but rather giant fictitious individuals, the transnational corporations.

III. Four Negative Consequences of Globalization

1. Standards-Lowering Competition. Globalization undercuts the ability of nations to internalize environmental and social costs into prices. Economic integration under free market conditions promotes standards-lowering competition (a race to the bottom). The country that does the poorest job of internalizing all social and environmental costs of production into its prices gets a competitive advantage in international trade. More of world production shifts to countries that do the poorest job of counting costs-- a sure recipe for reducing the efficiency of global production. As uncounted, externalized costs increase, the positive correlation between GDP growth and welfare disappears, or even becomes negative. We no longer know if growth is economic or uneconomic.

Another dimension of the race to the bottom is the increasing inequality in the distribution of income in high-wage countries, such as the US, fostered by globalization. In the US there has been an implicit social contract established to ameliorate industrial strife between labor and capital. Specifically, a just distribution of income between labor and capital has been taken to be one that is more equal within the US than it is for the world as a whole. Global integration of markets necessarily abrogates that social contract. US wages will fall drastically because labor is relatively much more abundant globally than nationally. It also means that returns to capital in the US will increase because capital is relatively more scarce globally than nationally. Theoretically, one might argue that wages would be bid up in the rest of the world. But the relative numbers make this a bit like saying that, theoretically, when I jump off a ladder gravity not only pulls me to the earth, but also moves the earth towards me.

2. Sacrifice of Competitive Structure of National Market. Fostering global competitive advantage is used as an excuse for tolerance of corporate mergers and monopoly in national markets (we now depend on international trade as a substitute for domestic trust busting to maintain competition). It is ironic that this is done in name of deregulation and the free market. Chicago School economist and Nobel laureate Ronald Coase in his classic article on the Theory of the Firm, said " *--Firms are islands of central planning in a sea of market relationships".* The islands of central planning become larger and larger relative to the remaining sea of market relationships as a result of merger. More and more resources are allocated by within-firm central planning, and less by between-firm market relationships. And this is hailed as a victory for markets! It is no such thing. It is a victory for corporations relative to national governments which are no longer strong enough to regulate corporate capital and maintain competitive markets in the public interest. Of the 100 largest economic organizations 52 are corporations (by sales) and 48 are nations (by GDP). One-third of the commerce that crosses national boundaries does not cross a corporate boundary, i.e., is an intra-firm non market transfer. The distribution of income within these centrally planned corporations has become much more concentrated. The ratio of salary of the Chief Executive Officer to the average employee has passed 400 on its way to infinity--what else can we expect when the chief central planners set their own salaries! Need I mention Enron?

3. Excessive National Specialization. Free trade and free capital mobility increase pressures for specialization according to competitive (absolute) advantage. Therefore the range of choice of ways to earn a livelihood become greatly narrowed. In Uruguay, for example, everyone would have to be either a shepherd or a cowboy in conformity with the dictates of competitive advantage in the global market. Everything else should be imported in exchange for beef, mutton, wool, and leather. Any Uruguayan who wants to play in a symphony orchestra or be an airline pilot should emigrate.

Most people derive as much satisfaction from how they earn their income as from how they spend it. Narrowing that range of choice is a welfare loss uncounted by trade theorists. Globalization assumes either that emigration and immigration are costless, or that narrowing the range of occupational choice within a nation is costless. Both assumptions are false.

While the range of choice in earning one's income is ignored by trade theorists, the range of choice in spending one's income receives exaggerated emphasis. For example,the US imports Danish butter cookies and Denmark imports US butter cookies. The cookies cross each other somewhere over the North Atlantic. Although the gains from trading such similar commodities cannot be great, trade theorists insist that the welfare of cookie connoisseurs is increased by expanding the range of consumer choice to the limit.

Perhaps, but could not those gains be had more cheaply by simply trading recipes? One might think so, but recipes8640 (trade related intellectual property rights) are the one thing that free traders really want to protect.

4. Further Enclosure of the Knowledge Commons in the Name of Trade-Related Intellectual Property Rights. Of all things knowledge is that which should be most freely shared, because in sharing it is multiplied rather than divided. Yet, our trade theorists have rejected Thomas Jefferson's dictum that *"Knowledge is the common property of mankind"* in exchange for a muddled doctrine of "trade related intellectual property rights" by which they are willing to grant private corporations monopoly ownership of the very basis of life itself--patents to seeds (including the patent-protecting, life-denying terminator gene) and to knowledge of basic genetic structures.

The argument offered to support this grab, this enclosure of the knowledge commons, is that, unless we provide the economic incentive of monopoly ownership for a significant period of time, little new knowledge and innovation will be forthcoming. Yet, as far as I know, James Watson and Francis Crick, who discovered the structure of DNA, do not share in the patent royalties reaped by the second rate gene-jockeys who are profiting from their monumental discovery. Nor of course did Gregor Mendel get any royalties--but then he was a monk motivated by mere curiosity about how Creation works! The globalizers seem to have forgotten a basic economic principle--that public goods, which are inherently non-rival and non-excludable, cannot be efficiently allocated by the market.

Once knowledge exists, its proper allocative price is the marginal opportunity cost of sharing it, which is close to zero, since nothing is lost by sharing it. Yes, of course you do lose the monopoly on the knowledge, but then economists have traditionally argued that monopoly is inefficient as well as unjust because it creates an artificial scarcity of the monopolized item.

Of course the cost of production of new knowledge is usually not zero, even though the cost of sharing it is. This allows biotech corporations claim that they deserve a twenty year monopoly for the expenses they incur in research and development. Of course they deserve a profit on their efforts, but not on Watson and Crick's contribution without which they could do nothing, nor on the contributions of Gregor Mendel, and all the great scientists of the past who made the fundamental discoveries.

Also the main input to the production of new knowledge is existing knowledge. To the extent that existing knowledge is made artificially expensive, then so is the production of new knowledge.

Furthermore, economist Joseph Schumpeter emphasized, being the first with an innovation already gives one a temporary monopoly. In his view these recurring temporary monopolies were the source of profit in a competitive economy whose theoretical tendency is to compete monopoly profits down to zero, which is the very definition of allocative efficiency.

Believe it or not, most important discoveries were made without the benefit of granting monopoly ownership of the knowledge to the discoverer. Can you imagine such a thing--scientists motivated by the pure love and excitement of discovery, and content with a university salary that puts them only in the top ten percent, but not the top one percent, of income recipients!!

As the great Swiss economist, Sismondi, argued long ago, not all new knowledge is a benefit to mankind. We need a social and ethical filter to select out the beneficial knowledge. Motivating the search for knowledge by the purpose of benefiting mankind rather than by securing monopoly profit, provides a better filter.

This is not to say that we should abolish all intellectual property rights--that would create more problems than it would solve. But we should certainly begin restricting the domain and length of patent monopolies rather than increasing them so rapidly and recklessly. And we should become much more willing to share knowledge. Freely shared knowledge increases the productivity of all labor, capital, and resources. It also subsidizes the production of new knowledge. International development aid should consist far more of freely shared knowledge, and far less of foreign investment and interest-bearing loans.

In support of this policy recommendation let me offer my favorite quote from John Maynard Keynes, one of the founders of the recently subverted Bretton Woods Institutions:

" I sympathize therefore, with those who would minimize, rather than those who would maximize, economic entanglement between nations. Ideas, knowledge, art, hospitality, travel--these are the things which should of their nature be international. But let goods be homespun whenever it is reasonably and conveniently possible; and, above all, let finance be primarily national."

IV. Two Common Objections Recognized and Refuted.

Having now offered four good reasons against globalization (for internationalization) it remains to confront the two most common objections that are sure to be raised. The first is that the comparative advantage argument of David Ricardo proved once and for all that free trade, and by extension free capital mobility, is mutually beneficial, so any contrary conclusion must be wrong. The second is that is that whatever the problems with globalization the extra growth it stimulates is worth it. Let us deal with each briefly.

1. Comparative Advantage Proves that Global Integration is Beneficial.--Since I am an economist, and really do revere David Ricardo, the great champion of classical free trade, I think it is important to point out that if he were alive now, he would not support a policy of free trade and global integration as it is understood today.

The reason is simple: Ricardo was very careful to base his comparative advantage argument for free trade on the explicit assumption that capital was immobile between nations. Capital, as well as labor, stayed at home, only goods were traded internationally. It was the fact that capital could not, in this model, cross national boundaries, that led directly to replacement of absolute advantage by comparative advantage. Capital follows absolute advantage as far as it can within national boundaries. But since by assumption it cannot pursue absolute advantage across national boundaries, it has recourse to the next best strategy which is to reallocate itself within the nation according to the principle of comparative advantage. The whole reason-to-be of comparative advantage is that it is a clever second-best adaptation to the constraint of internationally immobile capital. Comparative advantage is an argument for internationalization, not for globalization.

For example, if Portugal produces both wine and cloth cheaper than does England, then capital would love to leave England and follow absolute advantage to Portugal where it would produce both wine and cloth. But by assumption it cannot. The next best thing is to specialize domestically in the production of cloth and trade it for Portuguese wine. This is because England's disadvantage relative to Portugal in cloth production is less than its disadvantage relative to Portugal in wine production. England has a comparative advantage in cloth, Portugal a comparative advantage in wine. Ricardo showed that each country would be better off specializing in the product in which it had a comparative advantage and trading for the other, regardless of absolute advantage. Free trade between the countries, and competition within each country, would lead to this mutually beneficial result.

Economists have been giving Ricardo a standing ovation for this demonstration ever since 1817. So wild has been the enthusiasm for the conclusion that some economists forgot the assumption upon which the argument leading to that conclusion was based; namely, internationally immobile capital. Whatever the case in Ricardo's time, in our day it would be hard to imagine anything more contrary to fact than the assumption that capital is immobile internationally. It is vastly more mobile than goods.

The argument for globalization based on comparative advantage is therefore embarrassed by a false premise. When starting from a false premise, one would have a better chance of hitting a correct conclusion if one's logic were also faulty--the errors might cancel out! But unfortunately for the globalizers Ricardo's logic is not faulty

To use the conclusion of an argument that was premised on capital <u>immobility</u>, to support an argument in favor of capital <u>mobility</u>, is too illogical for words. To get away with something that illogical you have to hide it under a lot of intimidating, but half-baked mathematics.

2. <u>Growth Will Compensate</u>.--Some globalists will admit that the problems just outlined are real, but that whatever costs they may entail are more than compensated by the welfare increase from GNP growth brought about by free trade and global integration. While it may be true that free trade increases GDP growth (debatable but I will accept it for now), the other link in the chain of argument, that GDP growth increases welfare, is devoid of empirical support in the US since 1947.

It is very likely that we have entered an era in which growth is increasing environmental and social costs faster than it is increasing production benefits. We measure the latter but not the former, so we can't be sure. Growth that increases costs by more than it increases benefits is <u>uneconomic</u> growth, and should be called that. But Gross National Product can never register uneconomic growth because nothing is ever subtracted. It is much too gross.

Although economists did not devise GNP to be a direct measure of welfare, nevertheless welfare is assumed to be highly correlated with GNP. Therefore if free trade promotes growth in GNP, it is assumed that it also promotes growth in welfare. But the link between GNP and welfare has become very questionable, and with it the argument for deregulated international trade and capital flows, and indeed for all other growth-promoting policies.

Evidence for doubting the correlation between GNP and welfare in the United States is taken from two sources.

First Nordhaus and Tobin (1972) asked, "Is Growth Obsolete?" as a measure of welfare and hence as a proper guiding objective of policy. To answer their question they developed a direct index of welfare, called Measured Economic Welfare (MEW) and tested its correlation with GNP over the period 1929-1965. They found that for the period as a whole GNP and MEW were indeed positively correlated -- for every six units of increase in GNP there was, on average, a four unit increase in MEW. Economists breathed a sigh of relief, forgot about MEW, and concentrated on GNP.

Some twenty years later John Cobb, Clifford Cobb, and I (1989) 1 revisited the issue and began development of our Index of Sustainable Economic Welfare (ISEW) with a review of the Nordhaus and Tobin MEW. We discovered that if one takes only the latter half of the period (i.e., the eighteen years from 1947-1965) the correlation between GNP and MEW falls dramatically. In this most recent period -- surely the more relevant for projections into the future -- a six unit increase in GNP yielded on average only a one unit increase in MEW. This suggests that GNP growth at this stage of United States history may be a quite inefficient way of improving economic welfare --certainly less efficient than in the past.

The ISEW was then developed to replace MEW, since the latter omitted any correction for environmental costs, did not correct for distributional changes, and included leisure, which dominated the MEW, and introduced many arbitrary valuation decisions. The ISEW, like the MEW, though less so, was correlated with GNP up to a point beyond which the correlation turned slightly negative.

Measures of welfare are difficult and subject to many arbitrary judgments, so sweeping conclusions should be resisted. However, it seems fair to say that for the United States since 1947, the empirical evidence that GNP growth has increased welfare is very weak. Consequently any impact on welfare via free trade's contribution to GNP growth would also be very weak. In other words, the "great benefit", for which we are urged to sacrifice community standards and industrial peace, turns out on closer inspection not to exist. 2

One might object that although growth in rich countries might be "uneconomic", growth in poor countries where GDP consists largely of food, clothing, and shelter, is still very likely to be "economic". There is much truth in this, even though poor countries too are quite capable of deluding themselves by counting natural capital consumption as

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1 H. Daly and J. Cobb, For the Common Good, Beacon Press, Boston MA 1989, 1994.

2 Neither the MEW nor ISEW considered the effect of individual country GNP growth on the global environment, and consequently on welfare at geographic levels other than the nation. Nor was there any deduction for harmful products, such as tobacco or alcohol. Nor did we try to correct for diminishing marginal utility of total income (only for changes in distribution between rich and poor). Such considerations, we suspect, would further weaken the correlation between GNP and welfare. Also, GNP, MEW, and ISEW all begin with Personal Consumption. Since all three measures have in common the largest single category there is a significant autocorrelation bias, which makes the poor correlations with GNP all the more dramatic.

income. But, more to the point, the current policy of the IMF, WTO and WB is not for the rich to decrease uneconomic growth while the poor increase economic growth. Rather the vision of globalization is for the rich to grow rapidly in order to provide markets in which the poor can sell their exports. It is thought that the only option poor countries have is to export to the rich, and to do that they have to accept foreign investment from corporations who know how to produce the high-quality stuff that the rich want. The last thing poor countries are expected to do is to produce anything for their own people--those things are supposed to be imported.

The whole global economy must grow for this policy to work, because unless the rich countries grow rapidly they will not have the surplus to invest in poor countries or buy their exports. As a New York Times Columnist put it *"the only thing giving the world's poorest nations any hope at all"* is *"continued global economic growth led by import-happy Americans whose purchases help put food on the table from Bolivia to Bangladesh."* Ain't the world lucky we like to consume so much!

In an economically integrated world, one with free trade and free capital mobility, it is difficult to separate growth for poor countries from growth for rich countries, since national boundaries become economically meaningless. Only by adopting internationalization rather than globalization can we say that growth should continue in some countries but not in others. But the globalizing trio, the IMF, WTO, and WB cannot say this. They can only advocate continual global growth in GDP. The concept of uneconomic growth anywhere just does not compute in their vision of the world, which is the same world as that of the neoclassical economist.

That world is deaf to the prescient words of John Ruskin, who, in 1862, said,

"That which seems to be wealth may in verity be only the gilded index of far-reaching ruin....."

---John Ruskin, Unto this Last, 1862.

V. Summary.--- In sum. I have distinguished globalization from internationalization; offered four reasons for preferring internationalization and rejecting globalization; and have anticipated and refuted two common objections to my overall argument.

No doubt there are other objections that I have not anticipated. There always are!

3 NYT, 8/5/01, Section 3, p.4, "In Genoa's Noise , a Trumpet for Capitalism", by Daniel Akst.