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Inequality between States: The Price of Economic Globalization

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Abstract

According to Gruber "Equitable growth was a product of good institutions" (2011, 581). The domestic institutions and policies are rooted in states' responses to colonialism and the power structure of the world system. The key effect of domestic institutions and policy within the consequences of the globalization of the trading system is economic inequality between states. This paper analyzes the current situation wherein inequality between is clearly seen. Such inequality is the price of economic globalization.

Key words: Economic globalization, trading system, inequality between states, Asian economic growth, international institutions, domestic policies, rich getting richer.

Globalization: Wide Range of Effects on Different Countries

Post World War II economic globalization has had such a wide range of effects on different countries worldwide because of variation in domestic institutions and economic policy. According to Gruber "Equitable growth was a product of good institutions" (2011, 581). These domestic institutions and policies, in turn, are rooted in states' responses to colonialism and the power structure of the world system. The key effect of domestic institutions and policy within the consequences of the globalization of the trading system is economic inequality between states.

Domestic Institutions and Economic Policy as the Independent Variable

The independent variable that best explains variation among states is domestic institutions and economic policy. Domestic institutions provide the environment that dictates how well a state will do in the international economy, while economic policy decides how the state will interact through trade, or lack thereof for that matter. Since "the West colonized the entire world" (Nau 2015), all the least developed countries (LDCs) and middle income countries

(MICs) are former colonies. According to Nau, “emerging from colonization by the Western world, developing nations seek independent futures and fear neocolonialism, or dependence on global markets that embody historical oppression” (2015, 389). In addition, due to the overarching fact that some states are more powerful than others because of processes throughout history, “core states have a permanent advantage in producing monopoly products and use their clout in global markets to protect patents and other privileges that produce disproportionate profit” (Nau 2015, 461). Aware of their position in relation to the powerful core states and affected by their past experiences with colonialism, countries in Asia, Latin America, and Sub Saharan Africa formed their policies that dictated how they reacted to globalization.

Asia’s Economic Growth

Asia experienced extreme economic growth from 1965 until 2010, and overcame two economic crises. For example, “From 1990 to 2010, China and India, where 40 percent of the world’s population resides, grew by 10 and 8 percent per year, respectively. No country in the world grew as fast as China, and no country with the same poverty rates and population, except China, grew as fast as India” (Nau 2015, 391).

However, China and India were not the only ones to grow, in fact, all twenty three economies in Asia grew faster than all other regions of the world (Nau 2015, 391). This means even the smaller states prospered. Between 1974 and 1989, Indonesia’s economy grew by 54 percent (Ross 2012, 635). Several studies have attributed this strong record to its wiser policies including “the more deliberate pace of its windfall spending, larger investments in its agricultural sector, and its strict policy of maintaining a balanced budget” (Ross 2012, 635). Ross states “the Malaysian government, in particular, deserves credit for building a well-diversified economy and a strong manufacturing sector” (2012, 635). Furthermore, Malaysia “has received roughly as much inward FDI as the whole of sub-Saharan Africa” (Wolf 2002, 6). Asia was able to achieve this kind of economic growth because of their overall congruent policies of reliance on “export led development to exploit foreign markets” (Nau 2015, 397). According to Nau the governments of the leading Asian countries of Japan, Hong Kong, South Korea, Taiwan, and China were successful because “they intervened domestically to create internationally competitive industries; they did not intervene internationally to coddle inefficient domestic industries" (2015, 397).

A Niche to Attract Others

Asia recognized the potential advantages to finding a "well-established niche to attract others" (Gruber 2011, 586) and did just that. Asia recognized that they possessed a labor cost advantage. For example, "in the late 1990s, the average worker in manufacturing in China cost only $730 per year, while in Germany the average worker cost $35,000 per year and in the United States $29,000 per year" (Nau 2015, 349). In addition, Wolf states that "China's average incomes per head are only a tenth of those of the US" (2002, 3). This allowed Asian countries to flourish in the manufacturing sector that developed countries were starting to leave as they became more service and technology based in their workforces.

While this advantage allowed many Asian countries to enter the global trading system, it also exacerbated inequality between countries.

Rich Gets Richer

According to Gruber, "the rich (firms) get richer, and the countries in which they are located get richer too" (2011, 587). Milner states that East Asian states grew at an extraordinary rate of 5.6 percent in the 1980s and 6.4 percent in the 1990s. In those same time frames developed countries grew at 2.5 percent annually and 1.8 percent, respectively. This was in high contrast with the growth rates of developing countries, at 0.7 and 1.7 percent (2005, 540). The developing countries were growing much more slowly than both developed and East Asian countries and thus, "falling further behind the rich countries, increasing the gap between the two" (Milner 2005, 540). In addition, "in 1820 the richest country had three times the income that the poorest did; in the early 1990's this number was thirty" (Milner 2005, 540). This was due to the pairing of developing countries diminished growth under their domestic policies with the rapid growth of rich countries using their power advantage in the world trading systems.

Export-Oriented Development Strategies

Asian economic policy "pursued export-oriented development strategies that exploited economic competition in open international markets" (Nau 2015, 391). While Asia's domestic policies remained geared toward export-led development, Latin American countries focused on import substitution policies. According to Nau, "these policies called for developing local industries to substitute for imports" (2015, 406).

Latin America

Latin American policies have been focused on centralized economic policies since before World War II as a reaction to decolonization, and the interference of the United States in the years following (Nau 2015, 405). Since Latin America was colonized in the 1500s, the majority of the countries were independent by the mid-1800s. This early decolonization led to unstable governments and dictatorial rule. For example, from 1900-1975 "only Colombia and Costa Rica had fewer than ten years of nondemocratic rule…. And all of the Central American countries except Honduras, clocked four decades or more [of dictatorial rule]" (Nau 2015, 405). These power focused governments practiced the policy of "financial repression" (Nau 2015, 407). State entities controlled and developed natural resources and set food prices low to feed the urban population (Nau 2015, 407).

The highly controlled policies of Latin America resulted in "no independent marketplace of any significance" (Nau 2015, 406). This is clearly observed in the Latin American countries' growth rates. Between 1950 and 1973 Latin American countries grew by 2.5 percent per year in real GDP per capita. This was less than half the growth rate in South Korea and Taiwan and one-third the growth rate later in China and Thailand (Nau 2015, 402). Asia displayed greater growth because "Asian governments took their development signals from international markets and intervened in domestic markets to achieve international competitiveness" (Nau 2015, 391). Asia was able to achieve economic growth because of their disciplined bureaucracy and stable governance, which Latin America was far from possessing.

Role of International Institutions in Relation to Domestic Policies

International Institutions like the GATT/WTO have the potential to be helpful, but only if a country's domestic policies are set up to allow for growth. For example, while South Korea (with a domestic policy geared toward export-led development) which was formerly considered a LDC, now has a per capita income of $30,000 (greater than 50 percent the United States) and is a member of the OECD, acts as a developed country, Mexico, Brazil, and Chile have per capita incomes that stand at 25 percent that of the United States (Nau 2015, 405). All of the aforementioned countries had joined the GATT/WTO before 1990, and Brazil, Chile, and South Korea had all joined by 1970. Countries like Mexico, Brazil, and Chile should have seen greater growth had these international institutions been effective. South Korea saw growth because its domestic institutions allowed it to profit from the international institutions, where the others' domestic policies were not prepared to allow them to do so.

Asia, Latin America and Sub-Saharan Regions

Not only is this variation in economic performance seen between Asian and Latin American states, but it is also apparent in Sub Saharan Africa. Western intervention is a fact of life in sub-Saharan Africa, much more so than in Asia, and even South America (Nau 2015, 413). The key difference between Sub Saharan Africa and Asia is that Asia meets the "pre-requisites" for growth as laid out by Wolf. Wolf states that in order to foster economic growth the domestic institutions must be able to support "a stable state; security of the person and of property; widespread literacy and numeracy; basic health; adequate infrastructure; the ability to develop businesses without suffocation by red tape or corruption; broad acceptance of market forces; macro-economic stability, and a financial system capable of transferring savings to effective uses" (2002, 6).

Lack of Basic Prerequisites

The majority of sub-Saharan Africa lacks these basic pre-requisites. For example, "sixteen of the twenty countries with the greatest regulatory obstacles are found in sub-Saharan Africa" (Nau 2015, 420). In addition, before 1990, only five sub-Saharan countries had ever held free elections with competing parties. The norm was one party rule under a strongman. (Nau 2015, 416). The same five countries that score high on political stability are also the only ones in sub-Saharan Africa to achieve a real per capita growth rate above two percent per year (Nau 2015, 419). Similar to Latin America, microeconomic policies in Africa constrain growth (Nau

2015, 420). This similarity is not surprising since both regions see a pattern of dictatorial, or near dictatorial rule, as reactions to their colonization history.

According to Nau, “starting a company costs more than five times as much in sub-Saharan Africa as it does in South Asia and thirty times as much as in industrialized countries” (Nau 2015, 420). This directly suffocates the local economy and exasperates the inequality between steadily growing and already ahead developed countries, and rapidly growing Middle Income Countries. Sub-Saharan countries’ share of world trade also dropped by two thirds- from 2.1 percent in 1975 to 0.7 percent in 1995 (Nau 2015, 420). Compared with the United States’ share of 10 percent (Milner 2005), the inequality is clear.

Importance of Domestic Policy

Even the International Monetary Fund agrees that domestic policy plays a major role, as its principle task is to “encourage sound domestic economic policies” (Nau 2015, 270). Driven by the hierarchy of power in today’s world, states choose their domestic economic policies which in turn determine how they react to globalization. This, however, does not provide an easy solution to the obvious inequality that plagues our international system. Globalization has no doubt escalated the levels of economic inequality between countries, but growth without inequality is near impossible and not realistic. Wolf states that “Economic growth is, almost inevitably, uneven. The result is growing inequality. To regret that is to regret the growth itself” (2002, 7). The world is nowhere near perfect, but lack of growth will not bring it any closer. In order to assuage the issue of inequality each country must look within itself in order to choose domestic policies that will best benefit the welfare of its citizens. Inequality between countries is a price worth paying for overall growth and development of the global community.

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