

# What factors have contributed to globalisation in recent years?

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**Globalisation** can be defined: as *the growing interdependence of world economies*.

This definition has two main features:

- *Firstly, the fact that globalisation is not an end result, but is a **continuing process** that keeps growing and gathering pace*
- *Secondly, there is the idea that globalisation leads to world economies becoming more **reliant** upon each other.*

The first writer to use the term globalisation in anything like its modern form was the American economist Theodore Levitt in 1983. He argued that all around the world people's tastes seemed to be converging and that firms were now beginning to offer standardised products in all countries.

The question to be addressed here is *how* this emerging trend came into being, thus it is important for us to understand the factors driving this process of globalisation. We will consider the reduction and removal of trade barriers; transport costs; growth of the internet; growth of multinational corporations; and the development of trading blocs.

## The Reduction and Removal of Trade Barriers

Since the end of World War II, the General Agreement on Tariffs and Trade (GATT) and its successor, the WTO, have reduced tariffs and various non-tariff barriers to trade, enabling more countries to exploit their comparative advantage.

Developing countries continue to drive the global recovery, but their output growth is also expected to moderate to 6.0 per cent during 2011-2012, down from 7.0 per cent in 2010, because of the slowdown in the advanced countries and phasing out of stimulus measures. Developing Asia, led by China and India, continues to show the strongest growth performance, but some moderation (to around 7 per cent) is expected in 2011 and 2012.

## High unemployment is the Achilles heel for the recovery

The Uruguay Round of trade negotiations (1986-94) was the real watershed for global trade. Here, a large package of measures was agreed, which freed up trade in both goods *and* in services. As a result, the volume of world trade rose by 50% just in the 6 years following the conclusion of the Uruguay Round.

Equally important is the *number* of countries taking part in free trade negotiations. In 1948, when the GATT treaty became effective, there were only 23 Contracting Parties to the agreement. Just over 60 years later, there are now 153 member states of the WTO who all enjoy the benefits of free trade based on the principle of comparative advantage.

Accordingly, between 1948 and 2008, trade rose from only 5% to a massive >25% of world GDP. This means countries are becoming more and more reliant upon each other for their export earnings, income and employment. This exposes them to the *international trade multiplier*, where domestic business cycles become vulnerable to changes in the level of economic activity in the rest of the world.

However, the recent global recession brought international trade onto a downhill path. With world demand for all goods and services in decline and a temptation by many countries to impose protectionist barriers in order to protect jobs, the WTO in 2009 forecast a 9% fall in global trade flows. This is the first time since the end of World War II that trade has gone into decline and has been termed 'deglobalisation'.

### **Transport Costs**

Improvements in containerisation have drastically lowered freight charges. For example, over the last 25 years, sea transport unit costs have fallen by over 70%, while air-freight costs have fallen by 3-4% year-on-year. The result has been a boost in trade flows, as transport costs are now less likely to cancel out the gains from comparative advantage.

However the rise in sea and air transport has also caused great concern over the negative externalities of global trade. Indeed recent estimates that CO2 emissions will rise by >70% by 2020 have led to calls for green taxes on shipping transport. If these go ahead, they will partially offset the falls in transport costs, hence the process of globalisation will be dampened to some extent.

### **Growth of the Internet**

The growth of the internet has increased e-commerce, enabling firms of all sizes to compete more easily in global markets. Essentially, the internet acts as a 24-hour shop front allowing *consumers* all over the world to buy products online and around the clock, from whoever happens to be offering the best deal. For the *firm*, it therefore provides cheap marketing with global reach, such that even small local businesses can afford to serve customers abroad.

Accordingly, the internet gives all firms - both domestic and MNCs alike - easier access to foreign markets. We now find that international trade is no longer the sole preserve of the larger firm. It can now even be undertaken by, say, a local antiques shop, which can either set up its own website or sell through an online auction like eBay. The end result is of course that more countries become interdependent and reliant upon each other for the sale and provision of goods and services.

However, despite the 'global reach' of the internet, which ostensibly makes it a potent driver of globalisation, we see a very uneven spread of internet usage around the world. The figures below demonstrate how effectively the developed countries are embracing the World Wide Web as a tool for wealth creation, while the developing countries are being left behind to varying degrees.

<b>Internet Usage</b>		
<b>(Users as a Share of Total Population)</b>		
<b>Country</b>	<b>1998</b>	<b>2010</b>
UK	13.7%	82.5%
Australia	22.4%	80.1%
Germany	9.9%	79.1%
Japan	13.4%	78.2%
USA	30.3%	77.3%
France	6.3%	68.9%
Argentina	0.8%	64.4%
Saudi Arabia	0.1%	38.1%
Brazil	1.5%	37.8%
China	0.2%	31.6%
Philippines	1.1%	29.7%
Nigeria	0.0%	28.9%
Uganda	0.1%	9.6%
Sri Lanka	0.3%	8.3%
India	0.1%	6.9%
Senegal	0.1%	6.6%
Malawi	0.1%	4.6%
Mozambique	0.1%	2.8%
Madagascar	0.1%	1.5%
Niger	0.1%	0.7%

*Source: Adapted from [www.internetworldstats.com](http://www.internetworldstats.com)*

This is perhaps understandable: given the costly infrastructure and the hardware required to access the internet, poor countries such as those in Sub-Saharan Africa will clearly have little incentive to take part in the internet revolution. Not surprisingly, these regions will continue to focus on basic survival needs rather than investing in sophisticated IT equipment, until such time as they can adequately address their more immediate concerns.

Quite apart from this, there are censorship laws in many Middle Eastern and Asian countries (such as Saudi Arabia and China) which further limit the ability of the internet to forge links between world economies.

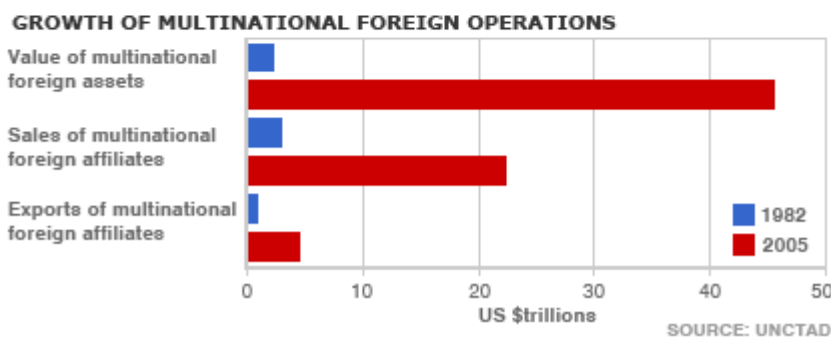
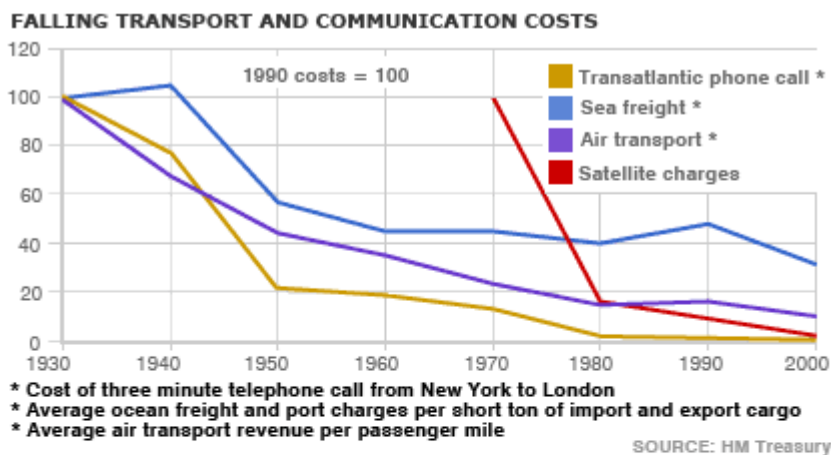
Accordingly, while the internet revolution has propelled us into a whole new era of globalisation over the past 15 years or so, this has mainly been skewed towards the rich liberal democracies, whose political and economic infrastructures have been more receptive to this relatively new technology. It is therefore arguable that the growth of the internet has made a substantial, though imbalanced contribution towards the process of globalisation.

#### **Growth of Multinational Corporations (MNCs)**

An MNC is a firm which owns production facilities in at least one country outside its home state. MNCs are said to epitomise global interdependence, as they often span across a number of different countries, with sales, profits and a smooth flow of production being reliant on several countries at once. The question, however, is how MNCs have come about.

Firstly, with lower transport costs firms are more easily able to disperse their production processes around the world to take advantage of varying cost conditions. For example, it is now more viable for car manufacturers to produce simple components like windscreens and door mirrors in cheap labour countries, than to have these components transported into the UK where they are assembled onto the finished good. The transport costs are now so small (see above) that they no longer cancel out the cost savings from producing components overseas.

Secondly, falls in communication costs have also facilitated a dispersal of the production process. For example, when asked why there is an increasing number of Western MNCs relocating their ancillary services to India, most people will cite the country's cheap but increasingly educated workforce. However, the Indian workforce was both cheap and highly educated during the '80s and '90s, yet call centres have only been relocating there during the last 10 years. The reason would therefore seem to be falling telephone charges. With international calls to Asia costing only a few pence per minute (as opposed to a few pounds during the '80s and '90s), India's comparative advantage in labour intensive services is much clearer now and is no longer being cancelled out by high communication costs.



Both types of cost reductions (i.e. falls in transport costs and communication costs) are said to have caused the *death of distance*, which has enabled the so-called 'hollowing out' effect. Namely, company operations are being dispersed around the world as firms carry out *efficiency-seeking* FDI. Hence, MNCs based in the UK or US have become reliant upon factor inputs in a number of different countries. And nations which consume the goods produced by an MNC are effectively relying on a number of different countries, both for the production and delivery of the good **and** for the customer service that goes with it.

To illustrate the growth of MNCs, in 1969 there were around 7,000 of them in the world; today, there are 82,000 MNCs, whose subsidiaries and foreign affiliates are responsible for around 33% of world exports (UNCTAD: World Investment Report 2009). Furthermore, as the opportunities to outsource continue to grow, so does the number of new MNCs coming into existence.

### **The Development of Trading Blocs**

Also known as a 'regional trade agreement' (RTAs), a trading bloc is essentially a group of countries that remove tariffs and quotas on trade between themselves. In some cases, this abolition of internal barriers to trade is replaced with a common external tariff against non-members of the RTA.

In recent years, the number and size of trading blocs have increased dramatically. For example, between 1948 and 1994 the GATT received 124 notifications of RTAs; however, since the WTO was established in 1995, over 240 additional notifications have been received. This includes the establishment of new RTAs, as well as the accessions of new countries into existing ones like the EU (which, since 2004, expanded from 15 to 27 member states).

Trading blocs promote global interdependence through *trade creation*. Namely, where the dismantling of internal trade barriers causes a country to switch from purchasing goods from a high-cost producer (often in the domestic market) to a low-cost producer elsewhere in the trading bloc. An example can be seen with the UK's membership of the EU where, since 1973, consumers have had access to cheaper wine from France, free from any tariffs or quotas.

However, trading blocs do not always promote trade; those that impose a common external tariff against non-members also cause trade diversion. That is, where the common external tariff causes a country to switch from a low-cost producer outside the trading bloc, to a higher cost producer inside the bloc. Again, the UK's membership of the EU provides a good illustration of this. Before 1973, British consumers had easy access to agricultural products from New Zealand, especially lamb and apples. However, upon joining the EU all agricultural products from outside the bloc, including those from New Zealand, became subject to very high tariffs (all part of the Common Agricultural Policy). Many UK consumers have therefore switched to British or other EU produce, with the consequence that our reliance on countries outside the EU has fallen greatly.

### **Conclusion**

Since the end of World War II, and particularly in the past 10 to 15 years, we have seen the process of globalisation drive forward at an unprecedented rate. A large part of this is down to legal, political and technological developments which have facilitated trade across national boundaries, both in products and in factor inputs. However, when evaluating the effectiveness of these factors in promoting global interdependence, it is important to bear in mind that many of them have their drawbacks and limitations. Nonetheless, globalisation continues to gather pace in the 21st century and with technology becoming cheaper and more advanced, we can only expect the process of globalisation to propel further forward in the years to come.