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ABSTRACT

For most of the present century, the world has been on economic roller coaster. However, it has been an increase in innovative capacity that has provided the main engine of growth. The globalizing economy of the new century is but the latest stage in the enlargement of the spatial dimension defining economic activity. The role of foreign trade, foreign direct investment, and cross-border strategic alliances is now crucial. The increased integration of financial markets and the trans-nationalization of production by multi-national corporations (MNCs) have combined with an on going convergence in technical know-how among OECD countries to make competition between firms extremely fierce.

In the new millennium, the main challenge is for poor countries worldwide to seize opportunities opened up by globalization. However, the spread of various ideological and cultural impulses is just as important as economic impulses. Of course globalization makes overall national governance more difficult. The benefits and costs of global mobility applied to trade, finance, technologies and ideas differ among different countries. While the neo-liberals advocate free trade and laissez faire, they do not support the free movement of people. The world of 2007 is a very different place to the one most of us was born into. These days, knowledge and intellectual labor is mobilized on a collective basis. This more flexible approach to value-added activities has a variety of spin-off effects. The post-Fordist production system is upgrading the quality of several types of labor. The spatial implications of a globalizing economy are universally stressed. On the other hand, various downsides of globalization have also been underlined by several social scientists the world over. There exists a sort of global paradox as Naisbitt (1994) put it. This includes an increase in structural unemployment, increasing hardships in the world and especially the third world. Life styles also continue to change as recently exemplified by the altering societal structure in Central and Eastern Europe.

The Globalization Syndrome of a New Millennium:
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Introduction

It was recently suggested that the world has been, for most of the present century, on an economic "roller coaster". The world today stands on the threshold of a new era. As John Dunning (1994) pointed out, notwithstanding the dramatic social and political events of last century, it has been growth in the world's capacity to innovate new goods and services which has provided the main engine of economic growth as exemplified by steam engines, eletricity, computers, micro-chips, lasers and also the continuous upgrading of human skills. In many respects, the globalising economy of new century is just the latest stage of enlarging the spatial dimension of economic activity. It is only in our lifetime that the role of trade, foreign direct investment (FDI), and cross-border strategic alliances has become so crucial for development.

The global age

The dominant feature of the world economy is its increasing globalization and the growing fear of its consequences for developed countries. It also reveals a marked reversal of attitudes within the two groups of countries from the time of Raul Prebisch. Without question the pace of globalization has accelerated. Both world trade and investment has seen greater transactions and flows. Even after adjusting for growing national incomes, economic activities are increasingly conducted within the global arena. Even this index misleads in conveying the implications of globalization. These averages tell us little about the "margin" and about what global competition offers in terms of both vulnerability and opportunity to producers.

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[1] This paper was written for the 14th World Congress of Economics, Marrakech, Morocco, and also presented later at Delhi, Aligarh Muslim University and IISE, Lucknow. For hard-hitting and unending dialogue and discussions, my grateful thanks are due to our beloved director-Dr. Girish Bihari Saxena, Drs. Mansoor Ali, R P Dubey, AM Singh, Secretary – Firdaus Siddiqui, and Shive Kumar Tiwari of my Institute. Useful comments were made by several noble souls – Sir Hans Singer, David Evans, David Wall of Sussex, Grazia Letto-Gillies, Timothy Shaw of London, John Dunning of Reading, Neelambar Hatti of Lund, Magnus Blomstrom of Stockholm, Jacob Kol of Rotterdam, Surendra J. Patel, Karl Sauvant, Richard Kozul-Wright, M. Shafaeddin of UNCTAD, Geneva, Rajneesh Narula of Oslo, Kunibert Raffer of Vienna, B. Hoekman of World Bank, Welf Werner of Berlin, Norman Girvan of Jamaica, Ricardo Ffrench Davis of Chile, H. Hirakawa of Nagoya, Edward Chen and Leonard Chen of Hong Kong.

The increased integration of the world's financial markets and increased transnationalization of production by MNCs (both of which are phenomena of globalization), have combined with the convergence in technological ability and know-how among the OECD countries to make competition among firms across countries extremely fierce. Firms in different countries can access similar technologies, borrow at similar interest rates and produce where it pays a little more to do so in a manner that was difficult a decade ago. Also margins of competitive advantage have become thinner; in the old days, we used to call such industries 'footloose'. Professor Jagdish Bhagwati (1996) calls this phenomenon 'kaleidoscopic comparative advantage'. This gives meaning to the notion that the globalization of the world economy has led to fierce competition among firms. Do globalization and development reinforce one another? Are they mutually compatible? What opportunities are opened and what constraints are imposed by globalization on the ability to undertake such autonomous national development? What are the main institutional challenges of globalization?

Tensions and dilemmas of globalization

Several issues arise. One tension of globalization is due to the fact that in a more interdependent world economy, any global or regional shock (for example, the Asian or Russian crisis of l997–98) is rapidly propagated to other economies. The contagion mechanisms lead to a decline in import volumes or changes in the real price of goods (oil, copper, timber for example). Moreover, there is ample evidence to show that uncertainty and volatility penalize capital formation and prosperity. In several cases this instability originates from abroad. In this new millennium, these are the questions which are of primary relevance. The events of the past few years in world economy indicate what the main challenge is. Lesser developed countries (LDCs) must somehow come to seize the opportunities opened by globalization.

Trade is only one and not necessarily the most important among the many manifestations of interdependence. Others include the flow of factors of production, capital, technology, enterprise and various types of labor across frontiers. There is also the exchange of assets, the acquisition of legal rights, and greater flows of information and knowledge (Streeten 1989). The global flow of foreign exchange has reached the incredible figure of over $1 trillion per day. The MNC has become an important agent of technological innovation and technology transfer. In 2003 the sales of more developed countries (MDCs) amounted to $l3 trillion. Their sales outside their home countries are growing 25–35 percent faster than their exports. Globalization is now seen as a disciplinary force for governments that undertake unsustainable policies. High fiscal deficits and unsound financial policies lead to inflationary pressures. Current account deficits or high real interest rates tend to be penalized by international investors and global capital markets. The room for populist or unsustainable policies is much narrower in a globalized world. But its other side is that the fiscal policy tends to lose its capacity to act as a counter-cyclical instrument for full employment. The fact is that international financial markets are very sensitive to the specifics of a country's fiscal policy. These investors use it as indicating the degree of "macroeconomic

responsibility" of a given government. This tends to encourage governments to follow austere fiscal policies in order to satisfy financial markets. It does induce governments to undertake pro-cyclical fiscal policies by cutting fiscal spending or raising taxes in downturns.

Institutional challenges

The strategic question is how to manage the negative side effects of globalization including the exacerbation of volatility at both the national and international level. Hence the need to recognize that free trade and financial integration (two key elements of globalization) are different in terms of their contribution to stability, growth and social welfare. It is an unfortunate non-historical touting of current globalization trends that has led critics to call it "globalony"[2]. In spite of rising unemployment, the political forces of nationalism are still losing out to the economic forces of globalization. Besides the interdependence of trade, finance and direct foreign investment (DFI), there are educational, technological, ideological, and cultural as well as ecological, legal strategic impulses that are rapidly being propagated throughout the world. Money and goods, images and people, sports and religions, guns and drugs can now be moved quickly across national frontiers.

With global satellite communication systems, instantaneous communication from any part of the world to any other becomes possible, but there has been no corresponding globalization of economic theory. We hear a lot about the creation of a borderless world and the end of the nation state. It is true, satellites and the Internet have greatly increased the speed at which communication of cultural and other informational impulses are propagated all over the globe. Also it has become almost a cliché to say that international interdependence has increased and will continue to grow. This is meant to refer to trade, DFI, flows of money and capital and the migration of people. The world has actually been shrunk by advances in technology (the jet, telex, satellite TV, super tankers). By reducing the cost of communication, technology has helped to globalize production and finance. In turn, globalization has stimulated technological progress by identifying competition. Competition in turn has forced the introduction of new technology. History may not have ended but geography, if not coming to an end, certainly matters less now. Unfortunately the interaction of globalization and technology has brought new problems. The international spread of ideological and cultural impulses is as important as that of economic impulses. Attitudes of the young everywhere to dress styles, hairdos, jeans, jogging as well as other fashions have become global. There is no doubt that technology, communications and market forces are unifying the world. Correspondingly, ethnic, religious and racial tensions are breaking up the world into small fragments.

Globalization makes national governance more difficult; monetary and fiscal policies run up against the impact of global tides as people, international banks, and

[2] For a skeptical treatment of the claims of globalization, see Wade (1996), Nayyar (1996).

MNCs manage to avoid intended results by sending or spending their money abroad or attracting money from abroad. The difficult task that lies ahead is to build modernity on tradition. In the post-war era, Japan succeeded in doing just this. However, neither all tradition nor all modern movements should be welcomed uncritically. This suggests that currently there is a perception that sees a greater degree of globalization and integration than has in fact occurred. As Paul Streeten (2000) pointed out, foreign direct investment (FDI) is a smaller proportion of GDP than it was before 1914. Transnational corporations (TNCs) are more domesticated than some of the studies suggest and most of them hold most of their assets and have most of their employees in their home country. That is also where most of these corporations conduct the bulk of their R&D. This is confirmed by the fact that in the second half of the 1980s, 90 percent of US patents taken out by 600 of the world's largest firms listed the inventor as a resident of their home base (Wade 2004).

Strategic decisions and innovations come from the home country. However, this may be replaced by a wider spread of R&D due to the convergence of computer and control technology. The movement of people continues to be severely restricted, much more than it was in the 19th century. But those reports claiming "Sovereignty at Bay" (Vernon 1971), "The Twilight of Sovereignty" (Winston 1992) or foresee "a borderless world" are somewhat premature. The illusion of increasing globalization arises from a short run perspective that looks only at the last 50 years (at the beginning of which nations were closed as a result of Great Depression and the Second World War). Views on the benefits and costs of global mobility of such different items as trade, finance, technology, and ideas really differ. In a much-quoted passage, John Maynard Keynes (1933) wrote: "Ideas, knowledge, art, hospitality, travel- these are things which should of their nature, be international. But let goods be homespun whenever it is reasonably possible and above all, let finance be primarily national".[3] Today it is more fashionable to explore "cultural imperialism" or the homogenization of TV and mass media and the global spread of mass culture. There are attempts to try and confine culture to local knowledge, activities and products, while at the same time suggesting free trade in goods and services.

While neo-liberals advocate free trade and a good deal of laissez faire, they do not support the free movement of people. The 18th century economist François Quesnay added "laissez passer" to laissez faire. This unfortunately is forgotten today due to the fear that it will raise population growth in poor countries or would interfere with cultural values or social stability. Globalization can be considered as per its impact on several objectives: (1) growth and productivity; (2) employment and skills; (3) wages and inequality of income and wealth; (4) technological innovations; (5) cultural autonomy and diversity; (6) human security. As Dani Rodrik points out, "Yet, at the same time, those who seek to disembarrass a country from its entanglements should be slow and wary. It should not be a matter of tearing up roots but of slowly training a plant to grow in a different direction."[4]

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[3] See further in Keynes (1933b; 1982).

[4] D. Rodrik, "Has globalization gone too far?" IIE, Washington, March, l997.

Age of alliance capitalism: towards flexible production

The very success of any organizational structure sows seeds of its own demise. The emergence of new forms of economic organization is captured in the concept of flexible and innovation-led production and alliance capitalism (Piore and Sabel 1984; Ruigrok and Van Tulder 1995) Today's world is a very different place to the one into which most of us were born. The production of goods is no longer the major focus of economic activity. Services now account for 60 percent of GDP of developed countries and one half for lesser developed countries (World Bank l999). The economic prosperity of a nation is less determined by its natural resources and more by its stock of knowledge, skills and expertise and capability of its people to organize these assets. It is not just competitiveness and development that is at the top of any agenda but sustainable competitiveness and development. We have plethora of books and documents on globalization (see, for instance, 'Global Trap', 'False Dawn', 'Turbo Capitalism', 'Global Paradox' in Naisbitt (1994)). Among the many definitions of globalization, my preference is for the one given by Anthony McGrew (in Globalization and the nation states, 1992), "Globalization refers to the multiplicity of linkages and interconnections between the states and societies which make up the present world system. It describes the process by which events, decisions, activities in one part of the world come to have significant consequences for individuals and communities in distant parts of the globe. Globalization has two distinct phenomena: scope and intensity. On the one hand, it defines a set of processes which embrace most of the globe or which operate worldwide; the concept thus has a spatial dimension. On the other, it also implies intensification on levels of interaction, interconnectedness or interdependence between states and societies, which constitute the world. Alongside stretching goes a deepening of global processes."

Globalization is leading to the structural transformation of firms and nations and also creating new relationships and dependencies. As one scholar put it, the global financial integration is the "end of geography" (O'Brien l992). The main causes of globalization are well known. One is the pressure on firms (by consumers and competitors) to continually innovate with new products while upgrading quality or reducing the price of existing goods and services. The rising costs of R. and D. also force firms to curtail the scope of their value-added activities and also to search for wider markets. As a result there has been an emergence of strategic alliances and networks. Another cause of globalization is the renaissance of market-supporting policies by national governments and the growth of market-led regional integration. The privatization, liberalization, and deregulation of services, all worked to stimulate cross-border corporate integration within TNCs. Moreover, there have been several underlying changes in the organization of economic activity. At the micro-level, changes are best demonstrated by a more flexible, systematic approach to production and also a growing need to form close relationships among firms to fully capture the benefits of globalization.

Several forces are really at work, forcing the firms to replace Fordist or mass production systems. Price competition has become less critical. Quality and other forms of non-price competition has become the most vital characteristic. Moreover, we observe an increasing trend toward fault-free products, continuous product improvement and innovative new goods. Moreover, new technologies developed during the 1990s (computer-aided designs and miniaturization), are forcing firms to engage in more quality-control and employ additional multi-purpose machinery. As Kenney and Florida (1993) have said, "the factory is becoming a research lab - a setting for both process and product innovations" (p. 303). In this new era, knowledge and intellectual labor has become mobilized on a collective basis. This more flexible approach to value-added activity has several spin-off effects on fabricating sectors. To improve quality, performance or reliability of finished goods requires a simultaneous improvement in the quality of components. The growing integration between the innovation and production functions of firms, the desegregation of the value-chain and the miniaturization of key components and the importance of networks and licenses to knowledge-sharing has several implications for ecosystems and organization of firms.

The post-Fordist production system is upgrading the quality and status of some selected segments of the labor force. Labor is now regarded more as a multi-functional asset, rather than as a cost and as a participant in wealth-creating process. Hence the quid-pro-quo of industrial relations has also changed. These new features of flexible or innovation-led economic systems are likely to have far-reaching implications for future globalization and sustainable development. Flexible systems are challenging the dominant mode of organizing production. Its deepest roots can be seen in the Japanese auto industry. Today the label 'Toyotism' is synonymous with concepts of demand-driven production, pull through workflow, and total quality management. This globalization of activity, along with network-related flexible production systems is changing the face of capitalism for the good. In the Triad countries, governance of production relies as much on the discipline of mutual trust, consensus and the readiness to exchange ideas and share tasks. Alliance capitalism is also reconfiguring the location of production. How much it decentralizes the key wealth-creating activities of firms depends on the nature of the alliances formed. Two primary implications of globalization are: (1) the cross-border mobility of created assets (knowledge and information) is widening the location options faced by firms and TNCs; (2) the kind of complementary assets required by firms to create or sustain their own core competence and exploit them are influenced by actions of governments; hence the ensuing more cooperative partnerships between the public and private sector.

Combining both global and local dimensions to multinational business strategy is increasingly important. Akita Morita, former Chairman of Sony coined the term "glocalization" to show a situation where firms worked in two dimensions at once, global and local. Hence there are many spatial implications to a globalizing economy. At one extreme, we have examples of world financial markets integrating. At the other end, even the most globalized firm must respond to a range of government laws. As Walter Wriston (1992) observed," the new world financial market is not a geographical location to be found on a map, but rather more than 200,000 electronic monitors in

trading rooms all over the world that are linked together" (Kobrin, 1993). Debates continue as to whether structural integration of regions is a building bloc or a stumbling bloc to globalization. I however feel that in its historical development it has been a little of each. The available evidence suggests that firms initially choose to extend their territorial boundaries by trading with or investing in neighbors. Unfortunately there also exist critical areas of tension between regions that could lead to regional fortresses. Most of these are a reflection of institutional or structural impediments that cannot be removed easily within existing regimes, as John Dunning (1994) observed.

The new global age

The dominant feature of the World Economy is increased globalization and also a growing fear of its consequences for developed countries. This attitude shows a marked reversal of attitudes in the north and south since the times of Raul Prebisch. Then the LDCs were skeptical and afraid of potential globalization, shying away from such integration with the world economy. Today those attitudes have yielded to a view that sees such policies as having a more benign impact on poor countries. As a result, one after another, these countries have changed policies to seek fuller integration within the global economy. That globalization has accelerated is hard to dispute. In both world trade and investment, there are greater transactions and flows suggesting that economic activities of nations are increasingly in the global arena. Jagdish Bhagwati (1996) suggested, even this index is misleading for the implications of globalization of trade and FDI. These averages tell us little about the 'margin' and about what global competition offers in terms of both opportunity and 'vulnerability" to producers. Looking at the changing realities of trade flows, trade in goods and services has continued to grow faster relative to national income throughout the postwar days. Successive rounds of reciprocal tariff and NTB reductions under GATT have been a major factor and the Uruguay round have further strengthened this trend, since it brings freer markets to new sectors. Hence in some respects, the rise in the share of trade to GNP has mostly restored world trade to its prewar situation. As Professor Jagdish Bhagwati (2004) recently suggested, this share hides the reality that the share of trade within the (immensely tradable) merchandise and primary goods sectors has grown perceptibly compared to both prewar and immediate postwar levels. In fact, by 1980, there was a vast increase in the exposure of tradable industries to international competition. This situation was truer of primary goods industries in prewar days but now characterizes most of the manufacturers today. But these shares don't continue to increase explosively; recent research suggests, they may have stabilized in the last decade.

Consequences of globalization

Just as globalization is qualitatively different from previous stages of internationalization, so its effects on development are also distinctive. John Dunning (1994) suggested that the international economic order of the 1970s was no longer

appropriate for the 1990s and certainly not the new century. But it is also the case that several political changes and technological advances of the last decade have provided a stronger basis for growth than has occurred at any other time since mid-1940s. The world now has the necessary knowledge, resources and experience. It has the technical means through which these assets can be transmitted between countries. Moreover, the growing "organ-centric" production systems, with its focus on smaller production runs, economies of scope and relational networking, its renewed reliance on the "putting out" of selected value-added activities and its greater respect for the individual in the work place, seem to be well suited to the needs and capabilities of the LDCs. We can see the fruits of Alliance Capitalism in Southeast Asia, where much of the expansion of cross-border activities has taken the form of networking by small firms. There is also a greater willingness by new MNCs based in China, Korea, Mexico and Thailand to collaborate with local firms than was the case for American and European firms during the l990s. But there are downsides to globalization also. As John Naisbitt (1994) observed, there is a "global paradox". The most visible downside is the increase in structural unemployment brought by competitive pressures and implementation of new technologies. We find, across the globe, for both rich and poor countries that change also is bringing economic hardships. This has altered the lifestyles of people and their expectations of future (as seen in Central and Eastern Europe recently). If global economic interdependence offers prospects of higher productivity and living standards, it also more closely links national economies to exogenous disturbances. The world economy of the new century is intrinsically more fragile and vulnerable than that of 30, 40, 50 years ago. It is the case no longer that only if the US sneezes, the world catches a cold. Economic shocks originating in any of the 5 or 6 leading countries are now instantaneously transmitted across the globe, with several devastating effects. Even being a part of a micro-net-work of value-adding activities can bring external costs as well as external benefits to participating firms (Dunning 1994). There is then a need for a more systematic approach to managing macro-economic affairs and the spatial implications of economic disturbances.

If globalizing the economy may lead to greater instability, it may also have unacceptable implications for national security or environmental erosion. Bad news travels just as fast as good news. We can draw attention to the Commission on Global Governance, set up in 1992 in Geneva, with a view to examining the implications of the kind of global integration being considered to govern the global economy. Its tasks go well beyond the economic implications of globalization. Its central concern is with the issues of peace, security, environment, poverty, democratic values and also the adequacy and transparency of existing institutions to cope with these issues. (In this commission, 29 members were drawn from every walk of life within 25 different countries.) While the forces of globalization have been leading to a convergence of the spending habits of consumers all over, they are also effectively exposing the differences in the way people think and behave. Not all countries welcome the effects of globalization, due to their fear that it may erode their traditional life styles. This leads to a global dilemma. One the one hand, a universality of such goods as cars, TVs, Sony Playstations, Coca Cola, hamburgers, jeans and services (tourism, sport, pop music) are leading to cultural convergence the world over. On the other, most people want to

remain loyal to their unique customs and institutions. Hence the task of resolving this dilemma is likely to tax the minds of scholars and politicians well into the new century. They seek to determine how to balance the advantages of sovereignty with those of interdependence, or of homogeneity with diversity.

The end of the cold war and the concomitant growing pressures to achieve an "economic oneness" are refocusing attention on cultural, ideological and religious issues over which most wars have been fought. Battle lines being drawn are not mainly between haves and have-nots, but between groups of nations with different ways of looking at the world in this new millennium. Some analysis like that of Samuel Huntington (1993) on future relationships between cultures is not so optimistic. Contrasting with this pessimism, Dunning (1994) is equally assured that there is more in common among major ideologies and religions of the world.

Dominant organization system and internationalization

The dominant organization system now evolving is that of "Alliance capitalism". The unit of economic activity (the firm) with its view of fully promoting its own objectives needs to be part of a network or web of related activities. This concept can be extended to the global level as well. From the time of the Roman Empire and beyond, history is littered with the debris of once all powerful nations. For most of the 19th century Britain did rule the economic waves and sterling was the business currency of the world. Leadership then passed on to the US around 1870 and the mass production system became a symbol of its hegemony. Today there is no single dominant nation. It is most likely that leadership will be shared in the new century by the European Community, Japan the US and most probably China. Increased integration has its base in trade and interdependence which has gone far beyond merchandise trade. Internationalization today reaches into most areas of human endeavor. The focus is on achieving challenges for international agreement on trade and trade-related issues. This integration is not driven simply by 'supply-side factors' (the various business strategies of multinational firms). It is also impelled by demand side-consumers who want to travel widely, have wider choice, for instance to shop via the internet.

One aspect of integration stressed in this context is that it constrains the actions of national governments. Fiscal restraint is imposed by the discipline of international. Financial markets or labor standards are whittled away in a race to the 'bottom' by competing national jurisdictions. John Helliwell (2000) has summarized recent research looking into the extent to which national borders do or don't matter. He also examines the extent to which national policies are prescribed by the global environment. Recent Canadian evidence suggests that even when trade barriers are removed and distance and size are allowed for, trade between regions within countries is much larger than between countries. This suggests that borders are important. Economic agents are more likely to deal with their compatriots than with foreigners. Is this a bad thing (resisting globalization) or a good thing? John Helliwell also asks why it might occur and looks at a number of possible explanations: social capital, democratic institutions, or education.

He concludes that it is not a bad thing, but rather that it is evidence of the limits to global integration.

Moreover, Allan Mendelowitz (2000) suggested that recent and ongoing changes in communications, technology and the spread of the internet will change, rather irreversibly, many aspects of economic and social life. This change could be as fundamental as was the Industrial Revolution. It also renders economic geography much less significant than it has been in the past. Producers need not be near their consumers as every point in the cyberspace is as close as every other point. Hence the pace of change and its breadth is a source of fear for all of us. Even the most technologically adept now feel the pressure to keep up. The globalization we are experiencing in this new century is impacting on individuals in a way that is qualitatively different to that felt about 100 years ago. While in the last 50 years since 1950, world merchandise output multiplied over five times, world trade expanded by a multiple of 14. A similar trend is visible for capital flows. Our analysis must also include various services, physical capital investment, technology flows and human capital. At the heart of the global economy lies the reality of interdependence. Firms still want to remove barriers between states (border restrictions). But they are more interested in achieving liberalization 'behind the border', with a focus on issues like competition policy, investment policy, standards, intellectual property rights, and environmental regulations.

As John F Kennedy once observed, 'our most basic common link is that we all inhabit this planet. We all breathe the same air, we all cherish our children's future and we are all mortal.' As the African proverb relates, 'Rain doesn't fall on one roof alone'. Free movement of capital has several risks as shown by the Asian crisis. Zevin (1992) argued "While financial markets have certainly tended toward greater openness since the end of Second World War, they have reached a degree of integration that is neither dramatic nor unprecedented in larger historical context of several centuries". Jeffrey Sachs and Andrew Warner (1995) also have argued that 'the reemergence of a global, capitalist market economy since 1950s, in an important sense, re-establishes the global economy that had existed one hundred years earlier". Dani Rodrik's (1998) view is different claiming that "in many ways, today's world falls far short of the level of economic integration reached at the height of gold standard".

Why financial integration is greater today

In the late 19th century, international capital markets and information asymmetries were not the only factor contributing to the disproportionate importance of railway securities. American trans-continental railways were built only once in this period. However, manufacturing, financial and commercial sectors of the economy were growing every bit as fast as transport. Although a century ago, FDI in these sectors was much less, it was more pronounced, as Bordo, Eichengreen and Irwin (2000) have observed. Obstacles to the flow of information can also explain the disproportionate importance of debt as opposed to equity in Foreign Institutional portfolios. Debt reduces the risk to

investors when imperfect information creates agency problems. The pattern persists today as well.

Hence this globalization of commodity and financial markets is historically unprecedented. This integration of capital and commodity markets goes further and runs deeper than ever before. Moreover the advent of highly integrated commodity and financial markets has been accompanied by various trade tensions. As a result, financial instability shouldn't come as a surprise and problems could be even more serious in new century. Fears are also evident in the relation between globalization and world trade. These fears of rich countries follow from the changing realities of trade flows in the late 1990s and the new millennium. Trade both in goods and services during the postwar period had grown faster relative to national incomes. Moreover, successive rounds of tariff reductions have been a major factor, as it brings freer markets to new sectors while opening them wider in older ones. This rise in the share of trade to GDP has mostly restored trade to its prewar situation. For the US, the share of merchandise trade in national income was 6 percent in l913 and 7 percent in 1990. The difference isn't compelling. More pertinently, this share hides an important reality. The share of trade within the tradable merchandise and primary goods sectors has grown perceptibly, compared to prewar and the postwar levels (Bhagwati l996). In fact by 1980 there was a vast increase in the exposure of tradable industries to international competition. This is a situation that was truer of primary goods in prewar days and is now true for the manufacturing sector. But it is not true that these shares continue to increase explosively. In fact recent research suggests that they may have stabilized in the 1990s. Still we cannot ignore several realities of the global economy now. There has been substantial exposure to international competition. The fact remains that few industries today can pretend that they are safe from international competition and this awareness has helped define issues and demands for government action. National boundaries have disappeared with their former powers and functions being usurped on one side by the global economy and on the other by cities and regions. Kenichi Ohmae (1998) treats regional economies and multinationals as the chief building blocs of the modern world economy. If this is true, we could expect to find that national borders no longer mark separations in economic space.

Evidence for trade flows

Only in recent years has it been possible to measure the relative strength of domestic and international linkages. Even now most countries don't have systematic measures of internal trade flows and so they have no empirical basis for comparing domestic and international trading intensities. For Canada, John McCallum (1995) used a full set of inter-provincial trade data that could be compared with trade flows between Canadian provinces and US states. He compared the strengths of domestic and international trading intensities and came to a surprising conclusion. Based on the gravity model of trade flows, in 1988 Canadian provinces traded 20 times as intensely with each other as with the US states of comparable size and distance. The gravity model assumes that trade flows increase proportionately with the economic size of trading partners and

decreases proportionately with the distance separating them. These adjustments are essential if domestic and international trade intensities are being compared, since the effects of distance on trade would lead us to expect greater trade flows within a country because of the greater distances involved in foreign trade.

Over recent decades, the gravity model became the favored child of all main theories of trade. As James Anderson (1979) showed, the gravity model could be derived from expenditure-share equations, assuming commodities to be distinguished by its place of production. Elhanan Helpman (1984) also showed that gravity models could also be derived from models of trade in differentiated goods. Such trade must lie at the core of much of the manufacturing trade, given very large two-way flows of trade in industry data. Moreover, Deardorff (1998) showed that a suitable modeling of transport costs produces gravity equations as an estimation form. John Helliwell (2000) tells us that border and distance effects are a very long way from disappearing. The 'end of geography' is not yet in sight. The concept Helliwell brings to explain this is called 'social capital'. It is all about the transaction costs of economic life, a neglected topic in trade theory. Our capacity to build trusting relationships is limited like everything in life and it seems plausible that both shared values and 'culture' and physical proximity are important determinants. So we have an explanation for border and distance effects that dominates data on trade flows. This could be important since social capital may be, not just a useful supplement to the explanatory power of neoclassical theory, but it may be subversive of it. We can as well say, homogenizing the international institutional landscape will make the world a safer and simpler place for the multinational firms to roam in but we still require some demonstration of gains from such outcomes.

Nature of the globalization process

We are still far from full economic integration, but we have gone a long way down that path. But have the impact of liberalization and changes in IT caused major qualitative or quantitative change in our economic lives? It is difficult to answer. As Paul Krugman (1998) and Dani Rodrik (2000) have suggested, today's trade and financial flows no more than match the degree of integration found in the World Economy 100 years ago. Still, if the domestic sectoral composition of output has shifted away from ' tradable' merchandise production to 'non-tradable' service industries (of which actual trade share is small but rising fast), why should we say that the overall economy has more globally integrated ? The actual nature of modern merchandise trade has features that in my view are not consistent with true long-run integration. The cost and time for transporting goods internationally has fallen a lot. This is of course one consequence. Moreover, about 60 percent of trade is intra-firm and much of those transactions and trade between firms is of semi-finished components. Such trade is facilitated by cheap transport and communications and motivated by cheap labor, such as the opportunities for 'mining' labor in the LDCs. Now several transactions are in fact part of the arbitrage process. There is more to free trade and globalization than some of us considered previously. Increased integration of world financial markets and increased internationalization of production by multinational firms have combined with convergence in technological

ability and know-how among the OECD counties to make competition among firms fierce. The margins of competitive advantage are now thinner. A slight shift in costs can now lead to shifting comparative advantage that is increasingly volatile. Three implications follow here:

1. Firms are more tempted to look over their rivals' shoulders and decry the extra edge in competition that amounts to unfair trade.
2. A sense of economic insecurity is now overtaking rich countries due to labor turnover and a reduction in the permanence of jobs.
3. This has led to a decline in the real wages of unskilled labor. The increased labor turnover means that workers spend less time in one job and so get less on the job training. This flattens their lifetime earnings curve.

The need for institutional innovations

International coordination has worked well in areas where advantages are great and visible. Examples are the wide scale adoption of the metric system or the adoption in 1884 of Greenwich Mean Time on which the world's time system is based. Other Institutions worked less well (UNCTAD and UNESCO) due to broad mandates, overlap with other organizations, differing perceptions about the future and overall objectives. International coordination and cooperation can take different forms. There can be full harmonization of policies, the adoption of commons standards such as the metric system. Or it can mean joint expenditures for common purpose in the case of international air traffic control. Or it may involve submitting to agreed rules or exchange of information on illegal capital flight or public health. Several innovations at global or transnational level could avoid the prisoners' dilemma outcomes, as Paul Streeten observed.[5] These would align modern technology and political institutions, would coordinate the four functions of a global system and also avoid negative-sum games to which prisoners' dilemma situations give rise. Streeten here is concerned for procedures, processes, rules, norms, incentives which imply changes in behavior forums associated with negotiations or explorations. A market is an institution. Many of these functions can be adopted by existing organizations. This would not entail any more coordination of the functions involved.

Emerging conclusions

It may be objected that these creative institutions are not designed on a drawing board but are a spontaneous response to various challenges. Many such designed institutions have failed (League of Nations, World Economic Conference of 1933, International Trade Charter, Special Drawing Rights). But multinationals, the Eurocurrency market, the globalization of the 24-hour capital market, and swap arrangements between central banks have been a success (none sprang from any grand design). Hence an appropriate

[5] See further in Streeten (1989; 2000).

reply now would be that these spontaneous institutions themselves need designed institutions to regulate them. The debt crisis was a direct result of unregulated recycling of OPEC surpluses by greedy lenders to profligate borrowers. If something like an International Investment Trust to recycle oil surpluses on acceptable terms had been there in the 1970s, this would have yielded a much better result. Moreover, utopian thinking can be useful for analysis. Just like a physicist who assumes an atmospheric vacuum to start afresh, policy makers can assume a policy vacuum. For long-term problems, utopianism may be useful. Also it gives a sense of direction. In a world that is regarded as the second best of all feasible worlds, everything becomes a necessary constraint and all vision is lost. Also excessive concern with the 'feasible' tends to reinforce the status quo. It is the case that a set of circumstances changes suddenly and that forces turn out to be favorable even to a radical innovation. No one really anticipated the end of communism, the disappearance of the Soviet Union, the re-unification of Germany, the breakup of Yugoslavia, the marketization of China, or the end of Apartheid in South Africa. Looking back we can say that ideas thought to be utopian have become realistic at moments in history when large numbers of people support them. For instance, there was the demand to end slavery. For all these reasons utopians shouldn't be discouraged from making proposals. Utopianism and idealism could turn out to be the most realistic vision indeed.

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