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Ecological Economics 31 (1999) 31–37

ECOLOGICAL  
ECONOMICS

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## COMMENTARY

# Globalization versus internationalization — some implications<sup>☆</sup>

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Received 20 January 1999; accepted 14 July 1999

### Abstract

For all the sins historically committed by the nation, it is still our basic locus of community and policy. Although national boundaries are changeable, they are far from arbitrary either historically, culturally, or politically. The nation, along with international federations of nations, must not be sacrificed to the unexamined ideal of 'globalization' which, when examined, turns out to be unfettered individualism for corporations on a global scale. Paradoxically, globalization even undercuts our ability to deal with irreducibly global problems such as climate change, because nations with porous borders are not able to carry out any effective national economic policies, including the ones that they agreed to in international environmental treaties. The IMF and the World Bank are abandoning internationalization and promoting globalization, contrary to the interests of their member nations, and to the intent of their charter. © 1999 Elsevier Science B.V. All rights reserved.

*Keywords:* Globalization; Integration; Internationalization

### 1. Introduction

Globalization, considered by many to be the inevitable wave of the future, is frequently confused with internationalization, but is in fact something totally different. Internationalization refers to the increasing importance of international trade, international relations, treaties, al-

liances, etc. Inter-national, of course, means between or among nations. The basic unit remains the nation, even as relations among nations become increasingly necessary and important. Globalization refers to global economic integration of many formerly national economies into one global economy, mainly by free trade and free capital mobility, but also by easy or uncontrolled migration. It is the effective erasure of national boundaries for economic purposes. International trade (governed by comparative advantage) becomes interregional trade (governed by absolute advantage). What was many becomes one.

<sup>☆</sup> I am grateful for comments from M. Wackernagel, J. van den Bergh, J. Bhagwati, and D. Rodrik. They are not responsible for any errors, nor do they necessarily agree with this essay, in whole or in part.

The very word 'integration' derives from 'integer', meaning one, complete, or whole. Integration is the act of combining into one whole. 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. By disintegration I do not mean that the productive plant of each country is annihilated, but rather that its 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.

In the classical 19th-century vision of Smith and Ricardo, the national community embraced both national labor and national capital, and these classes cooperated, albeit with conflict, to produce national goods — largely with national natural resources. These national goods then competed in international markets against the goods of other nations, produced by their own national capital/labor teams using their own resources. This is internationalization as defined above.

In the globally integrated world of the late 20th century, however, both capital and goods are free to move internationally. One little-noticed, but important consequence of free capital mobility is to totally undercut Ricardo's comparative advantage argument for free trade in goods, because that argument was explicitly and essentially premised on capital being immobile between nations.<sup>1</sup> But the conventional wisdom seems to be

that if free trade in goods is beneficial, then free trade in capital must be even more beneficial! In any event, it no longer makes sense to think of national teams of labor and capital in the globalized economy. Instead, we have global capitalists competing with each other for both laborers and natural resources, as well as markets, in all countries.

## 2. Globalization and the IMF

The subject of the IMF October 2, 1998 Economic Forum was 'Capital Account Liberalization: What's the Best Stance?'. Speakers included professors Jagdish Bhagwati and Richard Cooper, and high-ranking IMF staff. In question-and-answer period, I asked the following question:

The IMF, along with most economists, has long championed free trade (liberalization of the current account) on the grounds of mutual benefit from trade based on the comparative advantage argument originated by Ricardo. Yet if you read Ricardo, you find that his comparative advantage argument was explicitly and necessarily premised on capital immobility between the trading countries. If capital were mobile we would be in the world of absolute advantage (international trade would be no different from interregional trade). If the IMF now wants freely-mobile capital (liberalization of the capital account), does that not undercut the traditional comparative advantage argument for current-account liberalization by abolishing a necessary premise? Now that the IMF is explicitly committed to free capital mobility, does it plan to abandon the comparative advantage argument for free trade on current account and argue henceforth in terms of absolute advantage?

The question was given a short answer by Bhagwati more or less as follows: We have learned a lot in the 200 years since Ricardo, and the gains from trade have nothing to do with comparative advantage which only has to do with

<sup>1</sup> Immobile capital does not mean that producer goods cannot be exchanged — machines and tractors, 'materialist capital' can be traded just like shoes and wheat. What is immobile is capital in the 'fundist' sense, money, or liens on the future product of the deficit country. Immobile capital in the fundist sense is the same thing as balanced trade on the current account, i.e. trade which requires no compensating liquid transfer on capital account. Textbook demonstrations of comparative advantage are usually in terms of barter examples. Barter is always balanced trade, ergo by implicitly assuming balanced trade the examples also tacitly assume immobile capital. But conscious awareness of this assumption seems to have been lost in extending the results of the model to the real world. See Chapter 11 of Daly H.E., Cobb, J.B., 1989; 1994. For the Common Good, Beacon Press, Boston, MA.

the pattern of trade — what is produced where. All we are interested in is maximizing gains from trade, and that requires free trade in capital as well as goods. Forget about comparative advantage and absolute advantage and just focus on the welfare gains from trade.

How should one understand Bhagwati's assertion of the irrelevance of comparative advantage? My best understanding, based on personal discussion, is the following — we should be only interested in 'gains from trade', — that means an increase in individual welfare (or factor incomes) resulting from trade and specialization, and we don't care about the pattern of economic activities among nations — what gets produced at home and what abroad. Bhagwati's perspective, and that of the IMF, is globally individualistic and cosmopolitan, not at all nationalistic. The classical economists like Ricardo, were nationalists, and that is why they were so devoted to comparative advantage. We are presumably beyond that now. We are cosmopolitan individualists on a global scale, interested in maximizing global product. Comparative advantage, because of its premised constraint on capital mobility, does not maximize global product. But absolute advantage, by relaxing that constraint, does. We are primarily interested in the global gains from trade, and only secondarily (if at all) interested in national gains and losses.

If this interpretation is correct then it means basically that Bhagwati has opted to make the case for free trade in terms of absolute advantage. Although he does not use the term, preferring to speak only of gains from trade, it comes to the same thing. Under this regime of capital mobility, absolute advantage governs and comparative advantage becomes irrelevant. There are indeed gains from trade — world product increases, even beyond what would obtain under comparative advantage. But we cannot say that each nation shares in the increased product, that no nation could be worse off as a result of free trade on both current and capital account. Under the comparative advantage argument you could say that each country must benefit from free trade on current account. That was precisely the appeal of the comparative advantage argument for free

trade and why it was continually used by economists and the IMF. Capital mobility undercuts that feature. It is still possible for all countries to benefit under absolute advantage, but that requires a redistributive mechanism for compensation of countries that lose by those that gain. No one wants to address this issue.<sup>2</sup> Better to pretend that countries don't matter — that all we care about is the global gain from trade, and not the pattern of production among nations. National community is completely abstracted from.

Now this position of Bhagwati, as I have interpreted it, is logically consistent — he has abandoned comparative advantage and made his case in terms of absolute advantage, even though he does not use the term. Other economists, in discussions with me on the same question, have clung to comparative advantage by denying that immobile capital is really a necessary premise. I believe that is quite wrong. But Bhagwati does not make that mistake. He seems to agree that capital mobility undercuts the comparative advantage argument, and is willing to give up comparative advantage in exchange for capital mobility. However, I doubt that he, or the IMF, has embraced the full consequences of this choice.

If the IMF explicitly embraces the globally individualistic view, then the IMF has a problem. The IMF is a federation of members and exists to serve the interests of its members. The problem is that the IMF's members are nations, not individuals, not even cosmopolitan, global individuals, nor transnational corporate 'individuals'. By pushing globalization (liberalization of both the capital and the current accounts), the IMF has long been subverting the independence of its member countries, serving the vision of a single, cosmopolitan, integrated, global economy (global-

<sup>2</sup> The move from comparative advantage to absolute advantage seems to be part of the general retreat from the Pareto to the Hicks-Kaldor welfare criterion. Just as the latter represents a retreat from the condition that no person be made worse off to a potential compensation rule, so the former is a retreat from the condition that no nation be made worse off by trade, to the condition that any nation losing by trade could be potentially compensated by gainers. In both cases compensation is only potential, and in the case of trade it is seldom even mentioned.

ization) — rather than the vision of its charter, a federation of nations cooperating as sovereign units to advance the national interests of all members (internationalization). The current drive to amend the IMF charter to include capital-account management (read liberalization) just makes de jure the existing de facto efforts to undercut the national foundations of its charter. The IMF's goal, and that of the World Bank and WTO, is an integrated global economy, not a federation of national economies, cooperating where it is in their best national interests to do so, as envisaged at Bretton Woods. This is the agenda that the IMF has adopted. It is quite contrary to its fundamental structure and original charter as a federation of economically separate nations.

If the IMF explicitly adopts the Bhagwati view that comparative advantage does not matter, that only the global gains from trade matter, and consequently that absolute advantage should displace comparative advantage as the rule, then the IMF really should explain to its member countries that their interests as national communities are no longer of concern to the IMF's cosmopolitan bureaucrat-economists. If the IMF no longer serves the interests of its member nations as envisioned in its charter, then whose interests is it serving?

### **3. Globalization: between harmonization and standards-lowering competition**

When different national markets with different rules for the internalization of external costs merge into a single market, then the different rules of cost accounting present a big problem. Under globalization the market left to itself will resolve the difficulty by standards-lowering competition — the way of counting costs that results in the cheapest product will prevail. Capital will move to the country that does the least complete job of internalizing environmental and social costs. Consequently, globalization results in a larger share of world product being produced under regimes that externalize costs to the greatest degree, making it difficult to argue that globalization will increase efficiency, even recognizing the legitimate claims of absolute advantage!

Advocates of globalization often recognize this difficulty and counter it by a call for harmonization of cost-internalization standards. If all nations have the same internal cost-counting rules, then integration of their markets will be easier. Furthermore, the hope is that planned harmonization will converge toward the highest standards, contrary to the market process of standards-lowering competition. There is, no doubt, scope for such a strategy, but there are also limits stemming from the fact that there are good reasons for different countries to have different environmental and social standards, as well as big differences in the abilities of countries to enforce common standards. There is also the traditional free-trade argument that countries' differing tastes, factor endowments, and technologies are legitimate reasons for cost differences and trade. Why worry about harmonization?

Under the traditional comparative advantage (internationalist as opposed to globalist) regime, each country could indeed adopt its own separate rules of cost-accounting, reflecting its own values and traditions, and not worry about harmonization. As long as capital must stay at home, countries are not forced into a standards-lowering competition to attract and keep capital. Goods and services can be produced and freely traded according to comparative advantage even when trading partners have totally different ways of measuring costs. Remember that under comparative advantage what determines specialization and trade is a comparison across countries of internal cost ratios. Country A could measure costs in a-units, country B in b-units, and we could have:  $a = b$ ;  $a > b$ ; or  $a < b$ . The units in each country cancel out in calculating the internal cost ratios. Extremely different national philosophies of cost-accounting are compatible with the logic of comparative advantage. But for trade based on absolute advantage (globalization) there must be either planned harmonization or standards-lowering competition.

This is not to argue that there are no conflicts under comparative advantage-based trade. Country A may still have moral objections to, say child labor, and refuse to trade with country B that employs child labor. But as long as country A's

capital could not move to country B to itself take advantage of child labor and sell the resulting product back in country A, thereby forcing a lowering of standards regarding child labor in country A, then at least country A cannot claim to be forced into direct standards-lowering competition. Citizens of A might recognize that child labor in country B is the lesser of two evils for B, and be willing to import the products of child labor (with or without a compensatory tariff) but unwilling to enter into any closer integration that would severely undermine its own rules against child labor. As long as capital cannot move from A to B the objection of A to trading with B is much reduced, but not eliminated. A could say that they have every right to protect their own national standards against child labor which would be undercut by integration with B, but they do not feel an obligation to insist that B harmonize its standards with A. Alternatively, A may consider child labor so reprehensible that it refuses not only economic integration, but also even comparative advantage-based trade with B. In sum, comparative advantage, by allowing arms-length trade in goods, while rejecting the unifying embrace of capital mobility, allows countries a reasonable balance between diversity and homogenization, between undercutting one's own laws and imposing one's laws on other countries.

#### **4. Globalization as the abrogation of social contracts**

Section II already discussed the abrogation of the internationalist charter of the Bretton Woods Institutions by the recent globalist leadership of the IMF and World Bank.

Within the United States globalization implies the abrogation of another social contract. That is the implicit agreement between labor and capital over how to divide up the value that they jointly add to raw materials (as well as the value of the raw materials themselves, i.e. the uncounted 'value added' by nature to the indestructible building blocks of elemental atoms). That agreement has been reached nationally, not internationally. It was not reached by economic theory,

but through generations of national debate, elections, strikes, lockouts, court decisions, and violent conflicts. That agreement, in countries like the United States, on which national community and industrial peace depend, was basically that the internal division between labor and capital will be more equal than the world average. That agreement is of course necessarily repudiated by global integration. That is a very poor trade, even if you call it 'free trade'.

The economic integration of any high-wage country with an overpopulated world is bound to lower wages and raise returns to capital, widening the gap between labor and capital toward the more unequal world distribution. The population explosion in the third world has not until recently affected wages in the industrial world. Populous India was not allowed by the British to compete in global markets with its cheap labor, nor did the Chinese Communists seek to compete in world markets under the isolation policies of Chairman Mao. Nor had the World Bank yet become converted to the now incontestable orthodoxy of export-led development based on free capital mobility.

This orthodox model is supposed to lift the world's laboring masses (which now includes the minority of formerly high-wage workers) up from their subsistence wages. This can only be achieved by massive growth, we are told. But can the environment sustain so much growth? No, it cannot. And how will whatever growth dividend there is ever get to the poor, i.e. how can wages increase given the nearly unlimited supply of labor? If wages do not increase then what reason is there to expect a further fall in the birth rate of the laboring class via the 'demographic transition'? How could we ever expect to have high wages in any country that becomes globally integrated with a globe having a vast and increasing oversupply of labor? Why, in a globally-integrated world would any nation have an incentive to reduce its birth rate?

Global economic integration, far from bringing a halt to population growth, will be the means by which the consequences of overpopulation in the third world are generalized to the globe as a whole. The practice of limiting births in some

countries will be eliminated by a global version of the tragedy of the commons, rather than spread by demonstration of its benefits. In the global scramble to attract capital and jobs there will be a standards-lowering competition among weakened nations to keep wages low, and to reduce any social, safety, and environmental standards that raise costs.

One may ask if this emphasis on international standards-lowering competition is justified? After all, is there not also such a tendency in national markets as well? Yes, there certainly is, but within a nation we have many laws, institutions, and requirements, aimed precisely at preventing firms from competing by externalizing costs or by lowering standards. The point is that these laws and institutions are national — they do not exist at the international level.

Many demographers and economists, in their favorite role as 'valuefree' social scientists, have been reluctant to prescribe birth control to countries. If a country chooses many people, low wages, and high inequality over fewer people, higher wages, and less inequality, who is to say that is wrong? Let all countries make their own choices since it is they who will have to live with the consequences. That was a logically defensible position under internationalization, but not under globalization. The whole point of an integrated world is that these consequences, both costs of overpopulation and benefits of population control, are externalized to all nations. The costs and benefits of overpopulation are distributed more by class than by nation. Labor bears the cost of reduced wage income; capital enjoys the benefit of reduced wage costs, and no country has any incentive to limit population growth.

## 5. Globalization and the military

National disintegration caused by global integration is nowhere more striking than in its effects on that most nationalist of all institutions, the military. Military observers seem not to have paid much attention to how globalization blurs the issue of national defense as it erases the economic importance of national boundaries. As nations

cease to be separate, loosely-connected units, and become nodes in a tightly-integrated global network, as their boundaries lose economic significance, then do we really need to defend those boundaries? We will presumably no longer need customs officials or border guards. But what about the military proper? What precisely are they going to defend in a globalized world? The globe is not under threat of invasion. Do we imagine that national boundaries will long retain any political or cultural significance once their economic significance is gone?

With free trade in weapons and militarily relevant technology, and with easy migration of key military and scientific personnel, could the military effectively defend anything — even if it knew what it was defending?

Would anything count as treason anymore? For example, Hughes and Loral, nominally US companies, contract with China to send their expensive communications satellites into space on cheap Chinese rockets.

But it costs them a lot whenever a Chinese rocket blows up. To reduce that risk they transfer advanced rocket technology to the Chinese, technology which the Chinese can use in their own missile guidance systems and sell to other countries. If a Defense Department employee had sold China that information, would he not be charged with treason? Within the US Government the Commerce Department favors such deals, while the State Department has serious doubts.

Can the industrial part of the military-industrial complex globalize while the military part remains national? With the global mobility of capital comes the mobility of both the industrial base and the tax base that support the national military. Is not national defense a social good, just like welfare or environmental protection? Will not globalization undercut a nation's ability to tax capital to support its military, just as it undercuts a nation's ability to tax capital to support welfare and environmental programs? What's the big difference?

No doubt it is considerations such as these that lead some people to favor globalization. It is good, in their view, precisely because it makes the national military obsolete. Given the destruction and waste wrought by national militaries it is

hard not to have some sympathy with this position. But while globalization seems to make national militaries obsolete, it does not remove the need for appeal to force. Laws, contracts, and property rights still must exist and be enforced, even if they are global rather than national. Economic inequality and class conflict grow as the old national social contract between capital and labor dissolves along with the power of nations to guarantee it. Do the globalizers envisage a global government to enforce global laws with a global police force? Or do we, to avoid really big government, follow the privatization and deregulation model all the way, letting the military evolve into private Pinkerton guards hired by each global

corporation to protect its property and enforce its contracts? Global corporate feudalism?

I know that we have not arrived at this point yet. But make no mistake about the fact that globalization is being pushed hard by powerful transnational corporations, and that the weakening of the nation as a countervailing community power is part of the agenda. Conversion of the national military into a corporate police force is a possible corollary. Maybe globalization will stop before it completely disintegrates nations. But who or what will stop it? Reasons to stop it have been given above. Might the nationalism, or even patriotism, of the military slow the rush to globalize? So far it has not.