Introduction to

INTERNATIONAL POLITICAL ECONOMY

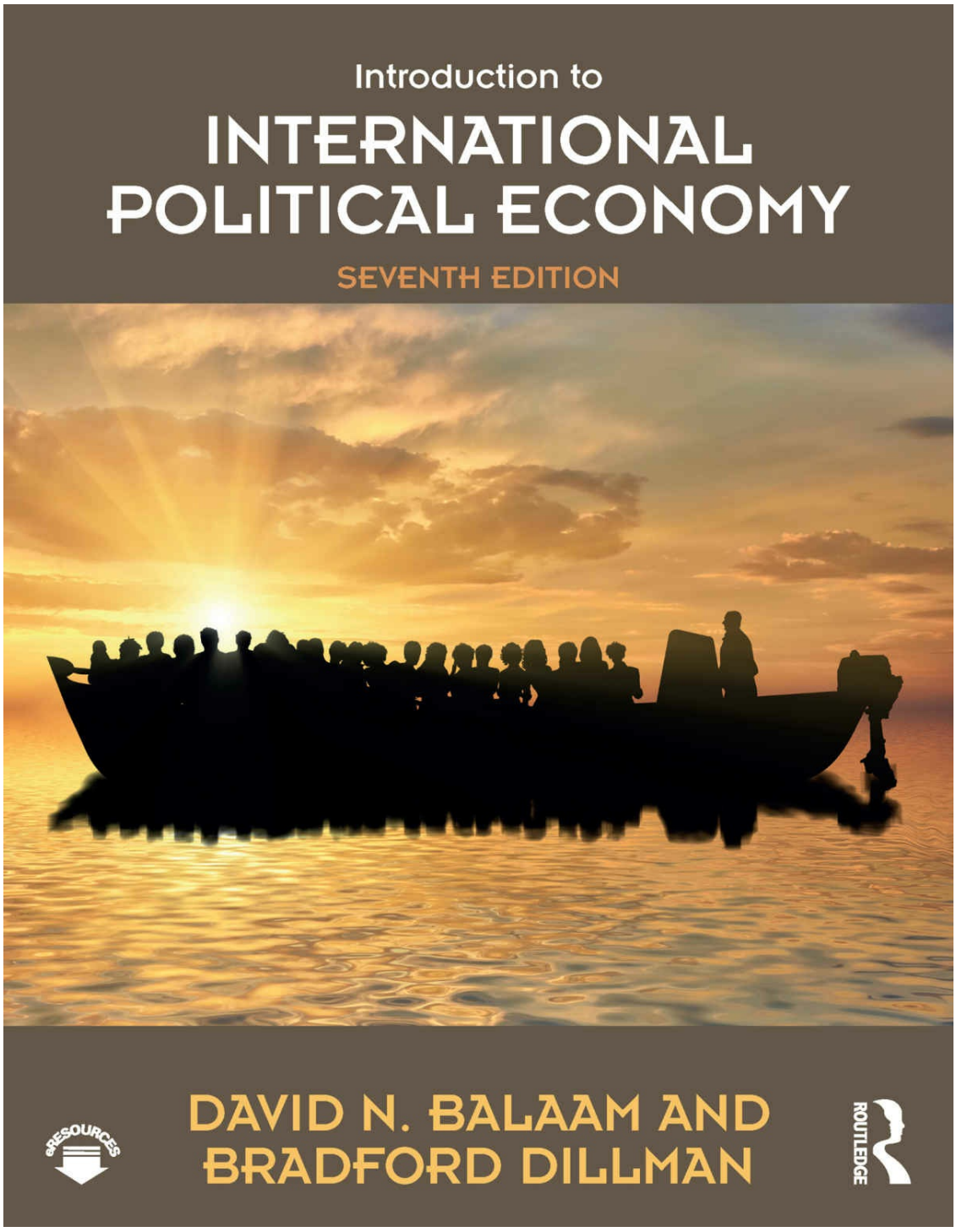
SEVENTH EDITION



eRESOURCES

DAVID N. BALAAM AND BRADFORD DILLMAN

ROUTLEDGE


Introduction to
INTERNATIONAL POLITICAL ECONOMY
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Praise for the Seventh Edition

Bar none, this is the best college-level textbook introduction to IPE on the market. Its great strength is not only its contemporaneity but also in its topical breadth and depth. Most importantly, Balaam and Dillman equip students with the necessary analytical tools to apply empirically what they have learned theoretically, bequeathing them an indispensable asset in the classroom and their careers.

Lukas K. Danner, *Florida International University*

The new edition of this leading textbook offers a much sought-after sweet spot for IPE courses. Balaam and Dillman thoroughly present the key theoretical debates in the field, and issue areas from international trade to global health are updated as well as historically grounded. At the same time, the material is well-organized and very accessible to students. These are the very attributes I aspire to when teaching IPE.

Glenn R. Fong, *Arizona State University Thunderbird School of Global Management*

Balaam and Dillman's is the best and most comprehensive textbook for students of IPE available on the market today. This new edition's expansive discussion of Constructivist and neo-Marxist contributions to the post-financial crisis debate and the search for alternatives to the liberal economic orthodoxy is a welcome contribution. But what really makes the text unique is the breadth of topics covered. The new empirical material on Trump, fake news, China, and the refugee crisis shows how the IPE toolkit is essential to understanding major contemporary developments in the global economy; and it is the only textbook to examine the illicit economy, the political economy of the Middle East, and global health. In short, this is an absolute mustread.

Huw Macartney, *University of Birmingham*

This textbook does what few do: It provides a solid theoretical understanding for the subject while giving students insight into why it matters. Balaam and Dillman bring theory to life by demonstrating how and why the principles of political economy affect the major processes and events of our time, from Brexit to BRICS to global health to global climate. Students will embrace this insightful, engaging, and relevant text.

Robert L. Ostergard, Jr., *University of Nevada-Reno*

A grasp of the global political economy has become indispensable for competent analysis of domestic and international politics. In its last iteration, Balaam and Dillman's by now classic book offers a compact—yet comprehensive—shortcut into the economic and political dynamics, exploring key theoretical perspectives and policy doctrines behind matters ranging from global production networks to the refugee crisis, the current predicament of the European Union, the tempestuous effects of information technology, and the rise of China.

Albena Azmanova, *University of Kent-Brussels School of International Studies*

The seventh edition of Balaam and Dillman's text is better than ever—revised extensively to bring the coverage of both theory and events right up to the present moment. The style is lucid, and the abundant new text boxes are carefully calibrated to explain complex concepts and issues in international political economy. In a field crowded with textbooks, I can think of no better introduction to the subject.

Benjamin J. Cohen, *University of California-Santa Barbara*

This classic text's updated new edition provides a comprehensive introduction to the theories, structures, and debates that today's world economy revolves around. Refined and carefully curated to sample cutting issues such as rising populism, illicit trade, climate change, and cyber warfare, the authors strike an impressive balance in showing both the order and tumult that characterizes today's IPE in a way few texts are able to deliver.

Jeffrey Lewis, *Cleveland State University*

The authors have once again produced a comprehensive text covering central theories, institutions, and issues pertinent to understanding the international political economy. The writing is lucid and easy to follow, and it is especially appropriate for the undergraduate student without a background in the study of IPE.

Ali R. Abootalebi, *University of Wisconsin-Eau Claire*

I have been using Balaam and Dillman's Introduction to International Political Economy since its first edition. Above all, the writing is very student-accessible, and the rich and diverse Discussion Questions and Suggested Readings features are a great aid to instructors.

Aguibou Y. Yansane, *San Francisco State University*

Balaam and Dillman have written an outstanding book on international political economy. It is particularly notable because of its unprecedented scope of coverage and the multiplicity of analytical vantage points provided. In addition to the expected chapters on trade, production, and finance, the authors also give prominent coverage to knowledge structures, energy and the environment, security structures, illicit global economy, and contemporary problems of health and refugees.

James A. Caporaso, *University of Washington*

Introduction to International Political Economy

In a revolutionary revision of this best-selling text, David Balaam and Bradford Dillman show how the postwar world order is at once under threat and yet resilient. This classic text surveys the theories, institutions, and relationships that characterize IPE and highlights them in the context of a diverse range of regional and transnational issues. *Introduction to International Political Economy* positions students to critically evaluate the global economy and to appreciate the personal impact of political, economic, and social forces.

NEW TO THE SEVENTH EDITION

- Streamlined yet comprehensive coverage—reducing the text from 20 to 17 chapters. There is also one unified chapter on global finance and a single chapter on energy and the environment.
- A new chapter on Constructivism shows sociological and ideational forces at work.
- A new chapter on Global Production encompasses transnational corporations and labor.
- A new chapter on Global Health incorporates food and refugee issues.
- Substantial revisions to 10 chapters, including new material on Brexit, the EU debt and refugee crises, populist-nationalist movements, inequality, trade conflicts and negotiations, cyber weapons, the rise of China, Middle East conflicts, and international responses to climate change.
- Significant focus throughout on President Trump's impact on U.S. foreign policy, international order, and global security.
- Extensive new graphs and tables of data, plus 27 fascinating new text boxes throughout.
- An author-written Instructor's Manual and Test Bank are provided along with additional online resources.

David N. Balaam is Professor Emeritus of International Political Economy and Politics and Government at the University of Puget Sound. He is currently an Affiliate and Part-time Instructor in the Jackson School of International Studies at the University of Washington.

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Introduction to International Political Economy

Seventh Edition

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PREFACE

By 2016 the spread of right-wing populist movements in Europe and the United States and authoritarian crackdowns in China, Russia, and Turkey had become deeply worrisome. The United Kingdom's vote on Brexit and the election of Donald Trump as president of the United States heralded a more tumultuous world with states that have greatly divided national polities. Like many others, we fear that democratic values and institutions are weakening around the world. Once-extremist views now circulate widely, and minorities and vulnerable peoples face greater dangers, including from their own governments. A number of political leaders show disdain for science and even basic facts. At the same time, there are many positive developments in the international system that may foster greater human security and enhance social well-being.

In this edition we have sought to make sense of these trends—their causes, dynamics, and likely consequences. We argue that the liberal world order, long dominated by the United States, is fraying. President Trump has clearly signaled that the United States will no longer shoulder many of its traditional international responsibilities. Trade liberalization has stalled and protectionism is rising. Washington has alienated traditional allies and turned away from multilateral security cooperation. The fragmenting European Union has been unable to take the reins of global leadership in the face of its disastrous Eurozone policies, Brexit, and the rise of national populism. China and Russia are stepping into the international vacuum in different ways. A newly assertive China under President Xi Jinping is offering leadership on global warming and trade while creating new institutions to expand its economic influence in developing countries. Russia is playing a more dangerous role by invading and annexing Crimea, supporting Syria's Bashar al-Assad, and carrying out elaborate cyber hacking and disinformation campaigns in the United States and Europe.

As readers of this edition will find, we see many threats to international security. The specter of nuclear war between the United States and North Korea is dismaying and horrifying. Damages from climate change are mounting. Globalization has stalled. Many international organizations are stuck with a myopic ideology of economic liberalization that is out of sync with national political demands, and these organizations are seemingly indifferent to the rising inequality that liberalization has fostered. While many in the lower and middle classes have faced stagnant wages and declining social mobility, a small elite in many countries is capturing a large share of income and concentrating wealth. As we stress, inequality has become a major international political and economic problem.

This edition places more emphasis on the role of ideas and norms than in previous editions. Populism, alt-right nationalism, and authoritarianism have appealed to a large segment of the populace in a number of countries, challenging democratic norms and weakening mainstream parties on the left and right. We see growing threats to long-established international norms, including those codified in international law. War crimes,

attacks on civilians, genocide, seizure of territory by force, and shirking of obligations to refugees are but some of the state policies today that violate fundamental human values. Skepticism about the benefits of globalization, free trade, and regional integration has grown tremendously. We hope that this edition succeeds in explaining how material struggles are bound up with battles over ideas.

As we also point out in the text, there are many positive developments throughout the international system. States, international organizations, and civil society groups are working tirelessly to preserve humanitarian norms, ensure democratic accountability, and protect the most vulnerable in the world. In the last thirty years there have been dramatic declines in the proportion of people living in extreme poverty in China and India. The Paris climate accord produced an international agreement to limit carbon emissions (although Trump pulled the United States out of the accord). Most developed countries have recovered significantly from the global financial crisis. Despite these rays of hope, we believe that systemic changes are producing a much more unstable and dangerous international order.

Our major goal is to provide students with the tools necessary to delve deeper into issues, develop their critical thinking skills, and understand many of the theoretical and policy dynamics of the global political economy. We offer a variety of perspectives so that readers will be able to form their own opinions about controversial issues. Each chapter begins and concludes with some thought-provoking theses; we hope that students and instructors will use them as springboards for debate and further research.

NEW TO THIS EDITION

This seventh edition of the text has major revisions and updates. Many of the chapters address changes in the international political economy during the first ten months of U.S. president Donald Trump's administration. We focus more closely on how structures of trade, production, and security are being transformed with the rise of national-populist movements and the growing importance of China. With a new chapter on constructivism, there is extensive discussion of the roles of ideas, norms, and information in global governance and systemic change. For the first time, the text includes thirty-six charts and graphs to better convey trends over time and highlight differences between countries and regions. With three new chapters, major revisions and additions in ten chapters, and twenty-seven new text boxes, the text covers many new topics. We comprehensively updated figures and data in every chapter.

The most substantial revisions to look for in the text are:

- Chapter 1, "What Is International Political Economy?" is a revised introductory chapter with a new focus on threats to the liberal postwar order arising from populist-nationalist movements and the communications revolution. A new section on Trump's character and personality stresses the importance of the individual level of analysis. There are new examples of causal arguments at each of the four levels of analysis and highlights of serious global problems since the financial crisis. In the chapter's conclusion—subtitled "Standing on the Precipice"—the authors pull all these subjects together and summarize the text's key arguments.
- Chapter 2, "Laissez-Faire: The Economic Liberal Perspective," is more concise and develops the concept of embedded liberalism more thoroughly.
- Chapter 3, "Wealth and Power: The Mercantilist Perspective," is more concise and includes a new section on neomercantilist policies related to digital technology. It includes short new sections on competition over Arctic resources and Trump's views of the state. A new text box highlights United States–China tensions over industrial policies.
- Chapter 4, "Economic Determinism and Exploitation: The Structuralist Perspective," has: new boxes on Antonio Gramsci and the transnational capitalist class; new overviews of the concepts of accumulation by dispossession, responsibilization, and the precariat; and a new, lengthy discussion of recent literature and data on U.S. and global inequality.
- Chapter 5, "Constructivism," is a mostly new chapter that incorporates some material from the sixth edition. Three new boxes analyze U.S. worldviews of China, how climate change is framed, and how indicators are used politically. There is significant theoretical discussion of norms and examples of their study in IPE. There are new sections on how national identity shapes foreign policy and on the process of securitization. Also added is coverage of the influence of economic ideas on state

policies.

- Chapter 6, "The Global Production Structure," incorporates some material on transnational corporations from the sixth edition into a significantly new chapter on global value chains, constraints on global market competition, and international investment agreements. There is extensive discussion of corporate tax avoidance and wrongdoing. New material also analyzes the effects of TNCs and automation on global labor. There is new material explaining how emerging economies and sovereign wealth funds are helping reshape global production patterns. New text boxes examine production of semiconductors, global value chains, and international tax scandals.
- Chapter 7, "The Global Trade Structure," succinctly contrasts the views on trade of all four IPE perspectives (including constructivism). A new section presents different explanations for the collapse of the Doha Round trade talks. New sections look at multilateral trade agreements such as TPP, TTIP, and TiSa, while highlighting the importance of negotiations over liberalization of trade in services. A new section surveys risks tied to trade liberalization, including the spread of pests, negative public health consequences, and anti-free trade backlash in the United States. Two new boxes look at the United States–China dispute over solar panels and socioeconomic effects of "trade shocks" on U.S. workers. The chapter has five new trade-related graphs.
- Chapter 8, "The International Finance and Monetary Structure," integrates and revises two chapters from the sixth edition. Discussion of exchange rates and monetary systems is clearer and more concise. We have added lengthy discussions of changes in global financial governance and contrasted views of IPE scholars on China's growing challenge to U.S. global financial dominance. There is a useful chronology of finance and monetary events since World War II and graphs of exchange rate changes since 2000. A new graph also shows different measures of the relative importance of the dollar, euro, yen, and renminbi.
- Chapter 9, "The Global Security Structure," is extensively rewritten, with a strong focus on realist perspectives and a history of changes in the security structure since the beginning of the Cold War. It includes a new assessment of the Obama administration's policies toward different conflicts in the Middle East and a chronology of post-Arab Spring wars in the Middle East. A lengthy new section analyzes the policies of the Trump administration regarding North Korea, the Middle East, Russia, China, and other security issues. For the first time we also focus on the growing importance of cyber weapons and cyber hacking as major security threats.
- Chapter 10, "The Knowledge and Technology Structure," has a new discussion of "fake news," state disinformation campaigns, state tensions over information sovereignty, and debates over global digital information flows. A revised and expanded section looks at state efforts to attract and retain global talent through education and immigration programs. A new text box examines how financialization affects national innovation. Four new graphs compare countries in R&D, foreign students, and patent applications.
- Chapter 11, "The Development Challenge," streamlines material from the sixth edition and includes new discussions of trends in global poverty. A new section critically

examines the emphasis on "good governance" by development institutions. Another lengthy new section reflects on "bottom-up" approaches to development focused on remittances, nudging, welfare-first, and empowerment of women. A short new section has a discussion of philanthrocapitalism. A final new section examines China's role in African development and building of infrastructure, as well as China's contribution to deindustrialization in parts of Latin America. Two new boxes survey debates over measuring poverty and social well-being in developing countries. Two new graphs display changes in manufacturing value added in select countries and major powers' foreign aid disbursements.

- Chapter 12, "The Fragmentation of the European Union: The Crossroads Redux," is significantly revised, with more history on the process of European integration after 1950. An expanded discussion of Greece traces the Eurozone–Athens crisis through 2017. A lengthy new section discusses the Brexit referendum and its effects on the European Union. We also examine other threats to the EU from populist movements and the refugee crisis. There are two new graphs on European government debt and a new box on child refugees in Europe.
- Chapter 13, "Moving into Position: The Rising Powers," has a new section providing an overview of the BRICs as a whole. The Russia section is expanded to include different interpretations of Russia's global goals and strategies. The Brazil section details the political fallout from the Operation Car Wash scandal and economic recession. The India section has updates on Narendra Modi's policies. Major additions to the China section contrast views of IPE scholars on the implications of China's rise for the global order and U.S. security. Also discussed are China's Belt and Road Initiative and foreign policy under President Xi. The chapter has five new graphs of economic trends in different countries.
- Chapter 14, "The Middle East and North Africa" is significantly updated, with a new focus on conflicts in Syria, Iraq, Libya, and Yemen. There is more focus on anti-democratic trends and regime crackdowns, as well as the jockeying between Russia, the United States, Iran, and Saudi Arabia.
- Chapter 15, "The Illicit Global Economy," has some new details on trafficking in different products and a new box on ivory trafficking.
- Chapter 16, "Energy and the Environment," combines material from two chapters in the previous edition with new material on the Paris Agreement and the Trump administration's environment and energy policies.
- Chapter 17, "Global Health: Refugees and Caring for the Forgotten," includes some material from two previous chapters, but the majority of the chapter is new material linking global health and the plight of refugees and other displaced people. Case studies look at Syria, South Sudan, Myanmar, and asylum seekers in the South Pacific. There are new boxes on war crimes in Syria and major humanitarian organizations.

FEATURES

While covering the "nuts and bolts" of IPE theories and issues, many of the chapters provide students with a historical context in which to understand the subject matter. More importantly, in contrast to other introductory texts, we challenge students to critically assess different theories and their explanations of IPE issues.

Part I of the book has five chapters that set out some basic tools for studying IPE. Chapter 1 introduces the fundamental elements of IPE, including four theoretical perspectives, four levels of analysis, and five international structures. Chapters 2, 3, 4, and 5 explore the four dominant analytical approaches to studying IPE: economic liberalism, mercantilism, structuralism, and constructivism.

Chapters 6–10 in Part II examine five structures that tie together a variety of international actors including nations, international organizations, nongovernmental organizations, and transnational corporations. Chapter 6 focuses on the global production structure, and particularly how transnational corporations have shaped its evolution. Chapter 7 traces changes in the global trade structure since the late 1940s, focusing significantly on agreements and disputes between states over trade rules. Chapter 8 outlines the international finance and monetary structure and analyzes changes in exchange rate systems, responses to financial crises, and challenges to the primacy of the U.S. dollar. Chapter 9 focuses on different phases of the post-World War II global security structure and argues that U.S. unwillingness under the Trump presidency to shoulder hegemonic responsibilities and the growing assertiveness of Russia and China increase global security risks. Chapter 10 examines struggles among international actors over information and technology, with significant attention to intellectual property rights.

In Part III we look at state–market interactions across different regions of the world. Chapter 11 examines the problem of development and some of the different strategies that less developed countries have used to "grow" their economies and address problems of debt and sustainability. Chapter 12 traces the integration process that has created the European Union and the serious challenges to European cohesion from the Eurozone crisis, Brexit, and right-wing populist movements. Chapter 13 covers domestic changes in Brazil, Russia, India, and China, focusing on what the rise of the countries means for global governance. Chapter 14 addresses the Middle East and North Africa, a region fraught with conflicts since 2011 and deeply penetrated by outside powers.

Finally, in Part IV we analyze important global problems and issues. Chapter 15 covers illicit activities involving trafficking of people, drugs, and other goods. Chapter 16 discusses the interconnections between global energy and environmental problems, employing many of the analytical tools developed earlier in the book. Chapter 17 examines global health problems, especially those affecting migrants and refugees.

All the chapters end with a list of discussion questions, suggested readings, and key terms that are in bold print in the chapter.

Visit the online resources at www.routledge.com/9781138206991 for the author-written

Instructor's Manual and Test Bank, plus key excerpts from the seventh edition.

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PART

I

Perspectives on International Political Economy

CHAPTER

1

What Is International Political Economy?



Standing on the Precipice.

Source: Shutterstock

The fate of our times is characterized by rationalization and intellectualization and, above all, by the "disenchantment of the world."

Max Weber[1]

In the last few years, a number of global problems and conditions have caused many people of different political stripes to become anxious, frustrated, and even angry. Consider some of the dramatic and distressing upheavals in the world recently:

- The unexpected election of Donald Trump as president of the United States;
- The retreat of democracy, political freedoms, and civil liberties in a number of countries;
- War and war crimes in the Middle East, particularly in Syria, Iraq, and Yemen;
- North Korea's development and testing of nuclear weapons and long-range missiles to carry nuclear warheads;
- The worst global refugee crisis since World War II; and finally
- The withdrawal of the United States from the Paris accord on global climate change.

IS THE POSTWAR WORLD ORDER OVER?

As writers and editors of this textbook, we believe that these issues are indeed legitimate reasons to feel anxious, if not greatly concerned or even frightened. Although many of these sorts of conditions have occurred before in the global political economy, what is different now is the growing feeling that rapid change is causing political, economic, and social instability. One way to try to make sense of things in the "age of anxiety" is to reflect on the extent to which these developments point to the breakdown of the "postwar world order." This term refers to a global management structure that began in 1944 when the allies met during World War II in Yalta to discuss the future of Europe.

For the past three-quarters of a century the world's "Great Powers" have avoided a nuclear war and another conventional war like World War II. At times the two superpowers—the United States and the Soviet Union—fought "proxy wars" indirectly against one another via surrogate states in order to limit the possibility of engaging one another directly. The postwar order has also promoted development in former colonies and conditioned the actions of international organizations and businesses by gradually expanding liberal international trade and monetary policies. Still another objective of the world order was to allow a space for nongovernmental organizations (NGOs) and civil society to affect issues such as political rights and liberties, education, the environment, and labor.

We may think of the postwar order as a global regime made up of rules, norms, and decision-making procedures. Regimes tend to sustain themselves over a period of time because states and other actors agree to behave in a certain manner, which becomes ingrained in policy ideas and processes. At the same time, we know that structures are not static but are *transformed* over time. A central issue this text addresses is the extent to which the third phase of the postwar order is ending and transitioning into a new order.

We argue that the upheavals mentioned above contribute to and reflect the unraveling of the international configuration of political and economic power that has been in place since 1944. We divide the postwar order into three distinct phases: 1944–1973, 1974–1991, and 1992–2017. A gradual redistribution of wealth and power within the postwar order shifted the values and goals of different actors within it. None of these phases has an abrupt beginning or end; some characteristics from one phase will persist into the next. However, we contend that there is a distinct zeitgeist and set of features in each phase.

We use an analytical approach that describes, explains and offers some solutions to the problems mentioned above. What follows is a discussion of key analytical tools and frameworks of analysis in IPE that can help students describe and explain issues mentioned throughout the textbook.

THE FIELD OF INTERNATIONAL POLITICAL ECONOMY

When defining IPE, we make a distinction between the term "international political economy" and the acronym "IPE." The former refers to what we study—a field of inquiry that focuses on actors and issues that are either "international" (between nation-states) or "transnational" (across the national borders of two or more states). Many analysts use the term "global political economy" instead of "international political economy" to label the study of problems such as climate change, hunger, and illicit markets that have spread over the entire world. More often than not, the two terms are used interchangeably.

In addition to the field of study just described, the acronym "IPE" also connotes a multidisciplinary method of inquiry. The primary objective of this textbook is to help you understand the interconnections between political, economic, and social topics that are not accounted for in separate disciplines. IPE combines and synthesizes a number of concepts, methods, and insights derived from economics, political science, and sociology. While drawing on history and philosophical ideas, it offers a more comprehensive and compelling explanation of global processes managed by governments, businesses, and social forces in different geographical areas. The four dominant IPE "perspectives" are discussed in detail below and outlined in Table 1.1.

IPE today also represents an effort to *return* to the kind of analysis done by political theorists and philosophers *before* the study of human social behavior became fragmented into discrete fields in the social sciences. Both Adam Smith and Karl Marx, for example, considered themselves to be political-economists in the broadest sense of the term. Although disciplinary specialization enhances analytical efficiency, a single discipline offers an *incomplete* explanation of global events. The tendency of disciplines is to "cram" data, ideas, and conditions into restricted intellectual and analytical boundaries. In some cases this results in a narrow- mindedness in which explanations lack complexity and factors that do not fit comfortably within a discipline's dominant framework are dismissed.

What are some of the central elements of the antecedent fields of study that contribute to IPE? First, IPE includes a *political* dimension that accounts for the use of power by individuals, domestic groups, states (acting as single units), international organizations, NGOs, and transnational corporations (TNCs). All these actors make decisions about the distribution of tangible things in the world such as money and products or intangible things such as security and innovation. In almost all cases, politics involves the making of rules pertaining to how states and societies achieve their goals. Another aspect of politics is the kind of public and private institutions that have the authority to pursue different goals.

Second, IPE involves an *economic* dimension that deals with how scarce resources are distributed in markets among individuals, groups, and nation-states. Today, markets are not just places where people go to buy or exchange things face-to-face; markets also exist online. The market can also be thought of as a driving force that shapes human behavior.

When consumers buy things, when investors purchase stocks, and when banks lend money, their depersonalized transactions constitute a vast, sophisticated web of relationships that coordinate economic activities all over the world. The political scientist Charles Lindblom makes an interesting case that the economy is actually nothing more than a system for coordinating social behavior. Agricultural markets shape what people eat, labor markets shape people's occupations and living standards, and relaxation markets even organize what people do when they are not working. In effect, markets often perform a social function of "coordination without a coordinator."[2]

Third, the works of such notables as Lindblom along with economists Robert Heilbroner and Lester Thurow help us realize that IPE needs to reflect on the *societal* dimension of different international problems.[3] Many IPE scholars argue that states and markets do *not* exist in a social vacuum. There are usually many different social groups *within* a state who share identities, norms, and associations based on tribal ties, ethnicity, religion, or gender. Likewise, a variety of transnational groups (referred to as global civil society) have interests that cut across national boundaries. A host of NGOs have attempted to pressure national and international organizations on such issues as climate change, refugees, migrant workers, and gender-based exploitation. All of these groups are purveyors of ideas that potentially generate tensions between them and other groups but play a major role in shaping global behavior.

Rather than using a single political, economic, or sociological approach, IPE employs a variety of theories and analytical tools that help us gain a more sophisticated understanding of the complex interrelationships between the state, market, and society in different nations. While this statement might sound a bit formal and confusing, keep in mind that we do not think you need to be an economics major or a finance specialist to understand the basic parameters of major IPE issues such as the global financial crisis and trade policy. In fact, this book is written for students who have limited background in political science, economics, and sociology, as well as for those who want to review IPE topics in preparation for graduate school. Those who study IPE are, in essence, breaking down the analytical and conceptual boundaries between politics, economics, and sociology to produce a unique explanatory framework.

Different Perspectives and Methodologies in IPE

The late political economist Susan Strange, a major force in the development of the field of IPE, suggests that we focus on a number of common conceptual issues and tools that cut across disciplinary boundaries. Her starting point for studying the relationships between states, markets, and society in the international political economy is to focus on the question of *cui bono?* (Who benefits?).[4] We then apply her framework to four dominant perspectives in IPE: economic liberalism, mercantilism, structuralism, and constructivism. A strict distinction between these perspectives is quite arbitrary and has been imposed by disciplinary tradition, at times making it difficult to appreciate their connections to one another. Each focuses on the relationships between a variety of actors and institutions. Each

perspective emphasizes specific values, actors, and solutions to policy problems but also overlooks some important elements highlighted by the other three perspectives (see Table 1.1).

Economic liberalism (particularly neoliberalism—see Chapter 2) is most closely associated with the study of markets. Later we will explain why there is an increasing gap between orthodox economic liberals, who champion free markets and free trade, and heterodox economic liberals, who support more state regulation and trade protection to sustain markets. Heterodox liberals stress that markets work best when they are embedded in (connected to) society and when the state intervenes to resolve problems that markets alone cannot handle. In fact, many heterodox scholars acknowledge that markets are the *source* of many of these problems.

TABLE 1.1

Perspectives on State-Market Relations

	Perspective				
	Neoliberalism	Social Democracy	Mercantilism	Structuralism	Constructivism
Closely Related Perspectives	■ Orthodox Economic Liberalism ■ Monetarism	■ Heterodox Economic Liberalism ■ Keynesianism	■ Developmental State Theory ■ State Capitalism	■ Socialism ■ Communism	■ Neo-Gramscianism
Role of the State	■ Laissez-faire ■ Minimal state intervention in the economy	■ The state promotes capitalism but manages the macroeconomy, sustains a large welfare state, and corrects market failures	■ An active state steers a mixed economy and promotes national industries and capital accumulation	■ The state controls the commanding heights of the economy and sets price and production levels through central planning	■ The state responds to norm entrepreneurs and diffuses norms globally ■ State identity and interests are shaped by interacting with others
Values	■ Economic efficiency ■ Competition ■ Free trade ■ Private property rights ■ Individual freedom ■ Open, rules-based international system	■ Democracy ■ Embedded liberalism ■ Full employment ■ Income redistribution ■ Social mobility ■ Open but stable and coordinated international system	■ National security ■ State sovereignty ■ Domestic stability ■ Managed economy ■ Trade surplus	■ Social equality ■ State ownership of the means of production ■ Self-sufficiency and autonomy from the international economy ■ Authoritarianism or totalitarianism (in practice)	■ Identity ■ Progressive norms ■ Dialogue and cooperation

Historical Thinkers	■ Adam Smith ■ David Ricardo ■ Friedrich Hayek ■ Milton Friedman	■ John Maynard Keynes ■ Karl Polanyi ■ James Galbraith	■ Alexander Hamilton ■ Friedrich List	■ Karl Marx ■ Vladimir Lenin ■ Antonio Gramsci	■ Karl Deutsch ■ Hedley Bull
Contemporary Thinkers	■ Douglas Irwin ■ Martin Wolf ■ Thomas Friedman ■ Theodore Moran	■ Joseph Stiglitz ■ Dani Rodrik ■ Jeffrey Sachs ■ Wolfgang Streeck	■ Ha-Joon Chang ■ Robert Wade ■ Robert Gilpin	■ David Harvey ■ Walden Bello ■ Robert Cox ■ John Bellamy Foster	■ Martha Finnemore ■ Kathryn Sikkink ■ Alexander Wendt
Policy Prescriptions	■ Lower taxation ■ Balanced budgets ■ Reduce the welfare state ■ Trade liberalization	■ State actively uses monetary and fiscal policies ■ Fair trade and some protectionism ■ Income redistribution ■ Strong regulation of corporations	■ Protectionist industrial and trade policies ■ Strategic trade practices, including export promotion ■ Autonomous state bureaucracy	■ State central planning ■ Single-party rule ■ Income redistribution ■ Radical change in the international system	■ States peacefully induce change through socialization ■ Develop institutions and communities of shared interests through discourse and persuasion
States Reflecting the Perspective	■ United States ■ Hong Kong ■ United Kingdom ■ Australia	■ Germany ■ France ■ Sweden	■ Japan ■ South Korea ■ China ■ Russia	■ China before 1982 ■ Former Soviet Union ■ Vietnam ■ Cuba	■ Foreign relations of all states

Many liberal values and ideas derived from such notable thinkers as Adam Smith, David Ricardo, John Maynard Keynes, Friedrich Hayek, and Milton Friedman are the ideological foundation of the popular globalization campaign (see Chapter 2). The famous laissez-faire principle that the state should leave the economy alone is attributed to Adam Smith.[5] More recently, economic liberal ideas have been associated with former president Ronald Reagan and his acolytes who contend that economic growth is best achieved when the government severely limits its involvement in the economy.

Orthodox liberals assume that people behave "rationally" under pure market conditions (i.e., in the absence of state intervention or social influences). Individuals will naturally seek to maximize their gains and limit their losses when producing and selling things. They have strong desires to generate wealth by competing with others in local and international markets. Orthodox scholars believe that people *should* strongly value economic efficiency—the ability to use and distribute resources effectively and with little waste. When an economy is inefficient, scarce resources go unused or could be used in other ways that would be more beneficial to society.

Mercantilism (also called economic nationalism) is closely associated with the political philosophy of realism, which focuses on state efforts to accumulate power and wealth to protect society from physical harm or the influence of other states (see Chapters 3 and 9). In theory, the state is a legal entity and an autonomous set of institutions that governs a specific geographic territory and people of a nation. Since the mid-seventeenth century, the state has been the dominant actor in the international community based on the principle that it has the authority to exercise sovereignty (final authority) over affairs within its territory.

States usually employ two types of power to protect themselves. Hard power refers to tangible military and economic assets employed to compel, coerce, influence, fend off, or

defeat enemies and competitors. Soft power is comprised of selective tools that reflect and project a country's cultural values, beliefs, and ideals. Through cultural exports, information flows, and diplomacy, a state can convince others that the ideas and values it sponsors are legitimate and should be accepted or tolerated. Soft power can in many ways be more effective than hard power because it rests on persuasion and mutual exchange.[6]

Structuralism is rooted in Marxist analysis but not limited to it (see Chapter 4). Structuralist ideas continue to be extremely important, even though they are not as politically popular as they were before the end of the Cold War. Phenomena that structuralists examine, including class divisions, exploitation, and imperialism, are not unique to capitalist societies. Scholars within this perspective show how the dominant *economic* structure of any society affects different social classes. They emphasize that markets have never existed in a social vacuum. Some combination of social, economic, and political forces establishes, regulates, and preserves these markets. As we will see in the case of the global financial crisis, even the standards used to judge the effectiveness of market systems reflect the dominant values and beliefs of those forces.

Constructivism is a relatively new and increasingly influential IPE perspective (see Chapter 5). It contends that norms, ideas, and discourse play important roles in shaping outcomes in the global political economy. Constructivists widen the study of IPE to include numerous nonstate actors and cultural values. They are particularly interested in how actors come to acquire their interests and understandings of the world in which they act. Constructivists believe that states and international organizations can change their goals as their conception of themselves and others changes. And when states come to share views about the nature of problems, they are likely to cooperate and ensure protracted peace. Today, however, many societies (including democratic ones) are becoming more polarized and authoritarian, in part as a reflection of shifting cultural norms and values, raising the prospect of more interstate violence.

Each of the four IPE perspectives helps us understand who benefits or loses from the international processes we observe, how actors acquire and use political power and economic resources, and what goals actors seek to achieve. In addition, IPE gives students the freedom to select analytical approaches that they feel are best suited to explaining a particular issue or problem. It is important to note that the way one explains a problem depends on the questions asked about it, the data available, and the theoretical outlook of the analyst herself. Benjamin J. Cohen, for example, sheds light on this issue in his discussion of the "transatlantic divide" between IPE scholars in the United States and Great Britain.[7] U.S. scholars tend to prefer IPE theories organized around issues of causation. Emphasis is placed on asking questions for which there is "hard" data. The goal is to test theories with statistical techniques and empirical evidence to determine what causes a particular "pattern of behavior." In contrast, British scholars tend to think of IPE in terms of problems that are not as easy to quantify or for which statistical tests are often not very useful.

Our methods are closer to those rooted in historical and philosophical understanding. At times we incorporate normative issues such as ethics and social justice. Our reasoned

explanations for global events and processes often point to a number of potential causes that are interconnected. While we present evidence from various social scientists about these causes, we do not seek to establish definitive laws or conclusions using a model drawn from the natural sciences. Nor do we make rigid assumptions about human behavior or causation. Instead, we strive to show readers how to look at global issues in critical ways and formulate plausible interpretations. We believe that what is most important is to learn how to explore complex interactions between social phenomena and recognize the kinds of evidence that inform scholars' assessments of different socio-political processes. In sum, we can say that IPE blends together distinct perspectives to produce more holistic explanations. It is more flexible than most disciplines because it asks the analyst to choose how something should be studied and with what tools. Hopefully, with a multidimensional outlook we can conduct better analysis that may result in more effective solutions to global problems.

We recognize that it is difficult to establish a *single* explanation of any IPE issue because each discipline has its own set of analytical concepts, core beliefs, and methodologies. However, we suggest that IPE is not a hard science and it may never establish a comprehensive theory with easily testable propositions about cause and effect. The world is its messy laboratory. Social science has always reflected this in its explanations of human behavior. We find that after experiencing an IPE course, many of our students feel that they have a better understanding of complex events and processes. They are able—metaphorically speaking—to graft different cuttings onto a branch to produce a new hybrid.

The Four Levels of Analysis

IPE theorists commonly use different levels of analysis in their research. In his famous book *Man, the State, and War*, Kenneth Waltz argues that explanations for causes of international conflict are located in different analytical levels of increasing complexity, ranging from individual behavior and choices (the individual level), to factors within states (the state/societal level), to the interconnections between states (the interstate level).[8] More recently, many have argued that the causes of specific problems are found at a fourth global level.

Depending on which level of generalization we choose, we can come to different explanations for global events and processes. The levels are not mutually exclusive; a good IPE scholar will look for explanations at all the levels. However, depending on what question is asked, one level usually provides better answers than others.

1. The global level is the broadest, most comprehensive level of analysis. We look at global economic constraints and opportunities resulting from changes in technology, global markets, and the natural environment. Global level factors cannot be traced to the actions of any one state, group of states, individual, or group. For example:
   - Thomas Friedman proposed that globalization is a "golden straightjacket"—investors will flee countries that fail to offer low inflation, a strong private sector, and free trade.
   - The development and proliferation of standardized shipping containers made

outsourcing more viable because loading, unloading, and transportation of manufactured goods became cheaper and easier. This new technology helped change where production occurs in the world.
   - Climate change is forcing a shift to new energy sources, thereby potentially hurting countries reliant on oil and coal while rewarding countries that invest in solar power and other forms of clean energy.
2. At the interstate level, we analyze how the relationships *between* states affect global outcomes. For example:
   - Alliances and the balance of power (distribution of power) between states profoundly shape what actions individual states can take and what threats they face.
   - The presence of a hegemon (a dominant power) gives us global public goods like security, free trade, and a top currency, while the rise of new powers such as China can lead to severe conflict with established powers.
   - States that weakly regulate transnational corporations and establish themselves as tax havens undermine the efforts of *other* states to sustain welfare programs and distribute a greater share of national income to workers. Thus, the inability of states to cooperate on tax and regulatory policies may spur a global "race to the bottom."
3. At the state-societal level, we analyze how bureaucratic decision making and the type of government shape outcomes. We also look at how lobbying, electoral pressures, culture, and a country's class structure determine foreign policy actions. For example:
   - U.S. farmers have considerable political power, despite being few in number, because each state gets two senators, magnifying the influence of less populated agricultural states. Therefore, the U.S. Congress gives large subsidies to American growers of cotton, corn, and other crops and maintains significant tariffs and quotas on imported agricultural commodities, all of which hurt farmers in poor developing countries.
   - Deregulated financial markets (due to the political power of Wall Street) and a cultural belief that the American Dream includes owning a home created systemic pressure to extend mortgages to subprime borrowers, laying a foundation for the global financial crisis.
   - Whether a country has a parliamentary or presidential system affects government stability and the ease of negotiating trade agreements.
4. At the individual level, we look at what individual policymakers do to cause or influence events. We try to understand the psychology, goals, and ideology of state leaders. Not all leaders react the same way to the same events and information. For example:
   - In the worldview of former Federal Reserve chairman Alan Greenspan and other acolytes of Ayn Rand, markets will self-regulate; thus, these policymakers paid scant attention to inherent systemic risks in financial systems that can trigger national and global economic crises.
   - The religious worldview of Iran's leaders and their threat perceptions shape Iran's actions in the Middle East. Similarly, ISIS's millenarian beliefs shape how it fights.

- The psychology of Trump profoundly influences how the United States acts. U.S. interests and strategies in the world reflect the president's narcissistic, aggressive, and impulsive disposition.[9]

The four levels of analysis help us organize our thoughts about the different causes of, explanations for, and solutions to a particular problem. Like the four IPE perspectives, each level pinpoints a distinct but limited explanation for why something occurred. One of the paradoxes of the level of analysis problem is that to get a bigger and more complex picture of a problem, one is tempted to look at all the levels for possible answers. However, mixing the levels usually produces no *single* satisfactory explanation of a problem. What to do? The level of analysis problem teaches us to be very conscientious about how we frame questions, what data we look at, and what we expect to find.

Figure 1.1 highlights the four levels of analysis and their connection to another conceptual organizing device (IPE structures) that we introduce next.

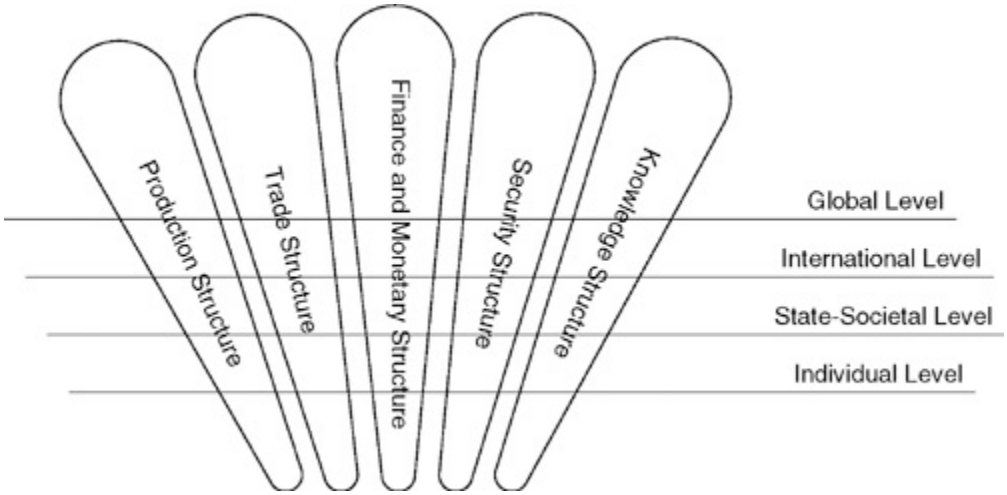


FIGURE 1.1
The Four Levels of Analysis and Five IPE Structures.

The Five IPE Structures

In the textbook we will often refer to five structures that were first outlined by Susan Strange: production, trade, finance, security, and knowledge. For Strange, these structures are complex arrangements that function as the underlying foundations of the international political economy. Each contains a number of state and nonstate institutions, organizations, and other actors that determine the rules and processes that govern access to production, trade, finance, security, and knowledge. In Chapters 6 through 10, we examine the rules and norms in each structure, how they were created, who benefits from them, and who is contesting them.

The "rules of the game" in each structure take the form of treaties, informal and formal agreements, and "bargains." They act as girders and trusses that hold together each of these five major structures. As one might expect, each IPE structure is often filled with tensions

because different actors are constantly trying to preserve or change the rules of the structure to better reflect their own interests and values. For example, actors may sometimes pursue free-trade policies and at other times erect protectionist trade barriers. Finally, issues in one structure often impact issues in another, generating a good deal of strain and even conflict between actors. According to Strange, many disputes arise when states try to "shape and determine the structures of the global political economy within which other states, their political institutions, their economic enterprises … [and] people have to operate."[10]

The five IPE structures are as follows:

The Production Structure. The issue of who produces what and on what terms lies at the heart of the international political economy. Making things and then selling them in world markets earns countries and their industries huge sums of money, which ultimately can shift the global distribution of wealth and power. As we will see in Chapter 6, in recent decades there have been dramatic changes in international rules that have shifted the manufacture of steel, furniture, electronics, household appliances, clothing, and other goods out of the United States and Western Europe. Many corporations that make these items have moved production to Mexico, China, Turkey, Poland, Vietnam, and other countries.

The Trade Structure. International trade agreements and national regulations shape the flows of goods and services across borders. While the rise of globally freer trade since the 1980s has helped many countries grow more quickly, many unions and manufacturers in Western countries have lobbied their governments for protectionist barriers against cheap imports in order to preserve jobs and profits. Since the 2010s a major battle over trade rules has emerged, pitting forces that want even more liberalization against those who want to reverse aspects of globalization.

The Finance and Monetary Structure. With perhaps the most abstract set of linkages between nations, this structure determines who has access to money and on what terms, and thus how capital is distributed between nations. In this respect, money is often viewed as a means, not an end in itself. Money generates an obligation between people or states. International money flows pay for trade and serve as the means of financial investment in factories, land, bonds, and other assets. Financial bargains also reflect rules and obligations, as money moves from one nation to another in the form of loans that must be repaid. The global financial structure (see Chapter 8) has been marked by the movement of "hot money" chasing quick profits from one country to another, in part because many political elites hold ideological beliefs opposed to strong international regulation of banks and corporations. Many scholars believe that under-regulated financial markets were in part responsible for financial crises in the 1990s in Mexico, parts of Asia and Latin America, and Russia, as well as for the global financial crisis. Some critics also charge that financial deregulation has intensified poverty and conflict in some of the depressed areas of the world.

The Security Structure. Feeling safe from the threats of other states and nonstate actors is perhaps one of the most significant concerns of nation-states and the people within them. At the global level, the security structure is comprised of those persons, states, international organizations, and NGOs that seek to provide safety for all people everywhere. In Chapter 9 we will discuss, among other things, the impact of the election of Donald Trump on the global security structure. Today many scholars are concerned that Trump is abandoning efforts by the United States to maintain a cooperative global multilateral order. Other scholars are troubled by the rising economic and military power of China and its territorial claims against India and countries around the South China Sea.

The Knowledge Structure. Knowledge and technology are sources of wealth and power for those who use them effectively. The spread of information and communications technologies has fueled industrialization in emerging countries and empowered citizens living under authoritarian regimes, as seen during the Arab Spring. International agreements and rules governing access to industrial technology related to such things as scientific discoveries, medical procedures, and new green energy often place low-income countries at a disadvantage. Increasingly in the world today, the bargains made in the security, trade, and finance structures depend on access to knowledge in its several forms. The knowledge structure includes institutions affecting intellectual property, technology transfers, and migration opportunities for skilled workers. The connection between technology and conflict has grown tighter in recent years, as is evident in the use of cyber weapons and drones and the efforts by North Korea to develop long-range nuclear weapons. New technologies have revolutionized strategic and conventional weapons.

THE GROWING INFLUENCE OF FACTORS INSIDE THE STATE

The Rise of Populism and Nationalism

Today we are witnessing the re-emergence of nationalism and a loss of faith in globalization. In the past decade there has been growing mass support for "populist-nationalist" parties and rulers in Russia, France, Hungary, Turkey, Egypt, Brazil, the Philippines, Venezuela, and most recently in the United States with the election of Donald Trump.

By the early 2000s both globalization and globalism (its supporting ideology) had come under attack for benefitting rich elites much more so than the working class and poor nearly everywhere.[11] Income inequality has risen significantly in many developed countries since the mid-1980s, including Germany and Denmark, and reached very high levels in Italy, the United Kingdom, and the United States by 2014.[12] For many middle-class and lower-class workers, average real wages have barely grown since at least the early 2000s. Wages actually fell in many places after the global financial crisis. For more than two decades many low-skilled and blue-collar workers have suffered as manufacturing jobs have moved to developing countries and automation has expanded. Moreover, a rising proportion of workers in developed countries are turning to self-employment or can only find temporary or part-time jobs that provide little security. There were at least two important effects of these developments: first, leaders and the masses focused more on issues such as jobs, border control, and preservation of socio-cultural values and identities; and second, xenophobia, racism, and fear of other religions increased. Problems that had been smoldering inside the state and society caught fire, threatening an end to the postwar order.

The IPE perspective of constructivism (see Chapter 5) helps us understand the rising popularity of populist-nationalism. It is also important to consider factors at the individual and state-societal levels of analysis. International affairs analyst Fareed Zakaria suggests that the new populism could pose a threat to democracy and western ideals.[13] It reflects a shift in soci-ety's values and culture such that individuals see themselves as under threat from external and internal forces. Many people have become suspicious of and hostile toward elites, mainstream politics, and established institutions.[14] The traditional left-right economic division in politics has been quietly shifting toward gender, religious, educational, and rural-urban divisions. Meanwhile, demographic changes and the digital revolution have helped sharpen social tensions.

A good reason to give more attention to what goes on inside the nation-state is that the domestic identity of people shapes the foreign policy of their country. The common sense of the masses—their belief systems and understandings of their own context—shapes and constrains how they and elites behave. And as political scientist Ted Hopf explains, how a

state understands its own identity affects how it understands and behaves toward other states.[15]

The Communications Revolution

Recent changes in how information is produced and communicated have contributed to the rise of populist-nationalism. Television channels and websites frequently add ideological commentary to reports. Social media in particular makes it easier to distort facts and generate stories that are untrue.

During the 2016 U.S. presidential election, the term "fake news" entered popular discourse in response to a slew of fictional articles that quickly spread throughout social media, mostly concerning presidential nominees Donald Trump and Hillary Clinton. From mid-2016 to early 2017, mainstream and left-leaning media often referred to alt-right news sources such as Breitbart News, Before It's News, and The Drudge Report as purveyors of fake news. Candidate Trump cited several stories from fake news sources during the election campaign. Once in office, members of the new administration sometimes distributed fake news stories to the public from the White House. However, alternative news outlets—and even Donald Trump and his former press secretary Sean Spicer—often described the mainstream media and politicians who speak publicly about the flaws of the new administration as spreading fake news.

Online articles that mimic the format of those from reputable news sources but have content that is partially or completely fabricated cause consternation for mainstream news outlets and social media companies. In November 2016 Buzzfeed reported that at least 140 political websites reporting fake news related to the U.S. election were being operated out of the town of Veles in Macedonia. Of those site controllers who were contacted, most said that their main motivation was to make money from advertisements via services such as Google's AdSense. In contrast, NPR interviewed Jestin Coler, the owner of several fake news sites operating out of Los Angeles, who said that he was a liberal, drawn to the work for its commentary on the gullibility of conservative audiences.

Fake news is often successful because many readers are not savvy enough to question the authenticity of the source. Stanford researchers have found that a majority of middle school, high school, and college students in twelve U.S. states are unable to distinguish sponsored content from real news, unable to identify biases in articles and tweets, and unable (or unwilling) to investigate further the credibility of online sources. They also found that students tend to trust pictures at face value.[16]

Cyber hacking is another method of distorting stories. A major controversy developed around the extent to which Russia hacked computer systems of both the Democratic and Republican election campaigns in order to help Trump prevail over Hillary Clinton. The FBI, Special Counsel Robert Mueller, and two congressional committees are investigating whether President Trump and/or his associates had knowledge of the hacking or were complicit in the effort. In 2017 some European governments accused Russia of hacking websites and spreading fake news before national elections.

Less Democracy and Fewer Rights

While shunning left-right labels and steering away from political dogmatism, populist leaders have nonetheless emphasized their own political power and authority. Most populist movements today are on the political right—often referred to as the "alt right." These parties and their leaders are often portrayed as illiberal and extremist because of their ideology and the "strong arm" tactics of state officials.[17] Even though Marine Le Pen, the leader of France's populist National Front, lost to Emmanuel Macron in the second round of the 2017 French presidential election, her party's popularity significantly increased. A few of the notable populist-nationalist parties on the left are Syriza in Greece and Podemos in Spain.

Table 1.2 lists the biggest populist parties in Europe, their leaders, and the percentage of seats they control in national legislatures (as of October 2017). These parties have gained strength since 2010, causing alarm for supporters of European integration.

Many people in the European Union and the United States support and respect the populist-nationalist movements. However, others are anxious about the movements because they seem to be pushing aside liberal democratic values and beliefs by drawing on people's fears, disillusionment with democratic systems, and exposure to fake news.[18] As a result of this development, state officials and the masses have been turning inward to focus on employment and preservation of their socio-cultural values. Likewise, there has been a rather dramatic rise in fear of immigrants from other nation-states.[19]

Another feature of rising populist-nationalism has been "strongman politics," understood at the first level of analysis. Populist leaders have always played a big role in history. Most often they:

- Promote new political, social, and economic ideas;
- Offer themselves as symbols of the body politic;
- Plan and strategize with disdain for democratic accountability; and
- Nurture a cult of personality.

TABLE 1.2

Major Populist Parties in Europe, October 2017

Country	Party	Party Leader	Percentage of Seats in National Legislature	Percentage of the Popular Vote in Most Recent Elections
Austria	Freedom Party (FPO)	Hein-Christian Strache	21	26
Denmark	Danish People's Party (DPP)	Kristian Thulesen Dahl	12	21
France	National Front (FN)	Marine Le Pen	1	9
Germany	Alternative für Deutschland (AfD)	Frauke Petry	13	13

Hungary	Hungarian Civic Union (Fidesz)	Viktor Orbán	67	45
Netherlands	Party for Freedom (PVV)	Geert Wilders	13	13
Poland	Law and Justice Party (PiS)	Jarosław Kaczynski	38	51
Switzerland	Swiss People's Party (SVP)	Albert Rösti	33	29
United Kingdom	UK Independence Party (UKIP)	Paul Nuttall	0	2

Leaders such as Hitler, Stalin, and Mao managed relations with other states in ways that reflected their totalitarian interests and values. Their personal character traits were tied closely to their foreign policies. Alt-right populist leaders today tend to have authoritarian proclivities, intolerance of criticism, and illusions of grandeur. They often tolerate racism and scapegoat immigrants and foreigners. However, they also appeal to mainstream voters by criticizing globalization and elite politics, calling for protectionism, promising jobs growth, and stressing the need to recover national sovereignty.

What are the effects of populist-nationalism on society today? Fareed Zakaria is interested in the impact on democracy. He maintains that democracy means more than elections or majority rule; it requires independent institutions such as the judiciary and the media to protect individual freedom and liberties. Zakaria also decries the recent decrease in the number of nations with democratic governments.

In its 2017 annual report, the watchdog organization Freedom House noted that 2017 was the eleventh consecutive year in which there was a decline in global freedom. In 67 countries freedom declined, while in 36 it made gains.[20] For example, Russian and Chinese leaders have targeted journalists, authors, and those promoting labor and women's rights. Hungary and Turkey are also two notable populist-nationalist countries in which there has been a decline in individual rights and freedoms along with increasing power of the leader of the nation. Hungary's Prime Minister Viktor Orbán declared his government to be an "illiberal" one and has weakened the role of the legislature and the courts. In 2015 Hungary and a few other EU countries (see Chapter 12) partially or completely closed their borders to immigrants. Orbán has forced immigrants waiting for a ruling on their asylum application to be held in sites that look astonishingly like concentration camps.

In Turkey, President Recep Tayyip Erdog˘an won a constitutional referendum in April 2017 that will eliminate the office of prime minister and transfer all executive power to the president, allowing him to appoint half the members of the highest court. Since an attempted coup in 2016, Erdog˘an has had tens of thousands of people arrested, some of whom have been sent to prison. He has also cracked down on Kurds in the southeast, reigniting violence.

During his presidential campaign, Donald Trump appealed to those who dislike or are afraid of immigrants. He promised to build a "beautiful" wall along the southern border to keep out "murderers and rapists." As president he imposed a ban on people from seven

Middle-Eastern countries coming into the United States, and he tried to reimpose the ban after the courts overturned it. Trump has attacked judges, implying that they were putting the United States in grave danger. Some argue that Trump has intentionally violated the U.S. constitution's emoluments clause, which bars presidents from accepting gifts from foreign sources, because he will not fully divest from his businesses scattered all over the world. Finally, Trump has violated the spirit of the law by appointing family members as personal advisers while they profit from their many businesses.

Anti-immigration policies have had consequences for local communities—and particularly for Muslims. In many countries there have been attacks on mosques, harassment of school children and their parents, and illegal discrimination. In France and some other EU countries, Muslim women have been barred from wearing face coverings and headscarves in some public spaces (see Box 1.1).

Trump: Character and Personality

The individual level of analysis provides a guide to some aspects of U.S. foreign policy and demonstrates the influence even one key leader can have on the global order. We have chosen to discuss the character and behavioral traits of Donald Trump because he is unlike any other U.S. president. He is admired by few outside the United States and disliked—if not loathed—by many. Soon after he assumed the presidency, *The Economist* depicted him on the cover of its magazine getting ready to toss a Molotov cocktail (a bottle with a lit, gasoline-soaked rag in it) with the heading "An Insurgent in the White House."[21]

During the election campaign, Trump promised to "shake up" the world order. In the first 100 days of his administration, he:

- Pulled the United States out of the Trans Pacific Partnership (TPP), a trade deal that the United States had negotiated with eleven other nations along the Pacific Ocean;
- Withdrew the United States from the Paris Accord on climate change;
- Declared NATO obsolete, then after meeting with the Director General of NATO, declared that it was no longer obsolete;
- Fired 59 cruise missiles at a Syrian base from which jets had flown to drop chemical weapons on a rebel-held town;
- Accused North Korea of continuing to develop nuclear weapons and threatened that if China did not do something about it, the United States would.

THE BURKINI: TO WEAR OR NOT TO WEAR?[a]

As the European Union's refugee crisis continues and concern over Islamic extremism increases, far-right political parties such as the Alternative for Germany and France's National Front have gained strength and more public recognition. A recent dispute in France shows the influence of rising rightist sentiments. In 2010, France instituted a controversial "burqa ban" with a €150 fine for anyone wearing clothing that covered the face in public. Some twenty French municipalities followed this up in July and August 2016 by passing restrictions on the burkini, a bathing suit that covers the entire body except for the face, hands, and feet. For many in France, the burkini is a symbol of the oppression of women and might damage French values of gender equality if worn publicly. Some officials claimed that the restrictions were only designed to protect recent Muslim immigrants from harassment and to help them integrate into society. Legally, the restrictions were based on the principle of *laïcité* (secularism), which is enshrined in the French constitution.

However, several local French courts later overturned some of the burkini bans, arguing that in order to invoke the principle of *laïcité*, an activity must pose "proven risks to public order," which some courts said the burkini did not. In response to the claim that such laws would reduce extremism among immigrants, France's Council of State said that the emotions resulting from terrorist attacks, such as the one carried out in Nice in July 2014, "do not suffice to legally justify the ban." Additionally, many humanitarian and social groups in France and abroad have harshly criticized the municipalities for creating a climate of mistrust that discriminates against Muslims and fosters extremism.

Other European countries have also passed laws restricting face coverings and headscarves worn by some Muslim women.[b] In Germany, however, anti-immigrant sentiments have not made their way into legislation in the same way. In 2016 Germany began debating a ban on the public wearing of the full-face veil. After World War II, Germany's system of government made it hard for the state to accumulate power, which may be why it has not been as easy as in France to pass draconian restrictions on religious clothing. However, in 2017 Germany's parliament banned government employees from wearing a face covering at work and prohibited the wearing of facial coverings while driving.

In 2016 the Bulgarian parliament instituted a nationwide ban on the wearing of full-face veils in public, despite the fact that only a small number of Roma Salafists in the city of Pazarjik were known to wear the garment. In Denmark there have been a number of attempts to legally restrict Islamic activities. Municipal governments have tried to require students to eat pork, ban women-only hours at swimming pools, and allow officials to strip valuables from incoming refugees in order to fund their relocation effort. Sweden and Denmark are both known for having a high level of

social services in exchange for high taxes, a delicate system that many fear is being exploited by recent immigrants. The European Court of Justice waded into the controversy over clothing worn by Muslims when it ruled in March 2017 that European employers can bar workers from wearing Islamic headscarves, but only as part of a wider policy of banning the wearing of all religious or political signs.

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[a]This box was written by Sam Phillips-Corwin and edited by Bradford Dillman.

[b]An overview of European "burqa bans" is at Liam Stack, "Burqa Bans: Which Countries Outlaw Face Coverings?" *New York Times*, October 19, 2017, at www.nytimes.com/2017/10/19/world/europe/quebec-burqa-ban-europe.html.

Academic and government critics of Trump often ask the questions: "Why is the president like this?" and "What is he trying to do?" Many find no rational pattern to his ideas, policies, and behavior as president. In Chapter 9 we look in more detail at Trump's role in the global security structure. Here we note some of the personal character traits and behavioral tendencies that social psychologists believe explain his behavior.

Supporters believe that, among other things, he:

- Gets things done;
- Focuses on the big picture and doesn't micromanage;
- Is a successful businessman with an extroverted personality; and
- Is tough but pragmatic and likeable underneath.

Detractors claim that he:

- Is politically inexperienced and frames everything as a business "deal";
- Has superficial knowledge about issues and doesn't focus on strategy;
- Is an insecure and impulsive narcissist with a volatile temper;
- Frequently exaggerates, brags, and lies;
- Compulsively tweets without considering the implications of his words; and
- Likes to threaten and bully others in order to try to get his way.[22]

Officials and experts are concerned about his policies and actions because, among other things, he:

1. Is a "daring and ruthlessly aggressive decision maker who desperately desires to create the strongest, tallest, shiniest, and most awesome result—and who never thinks twice about the collateral damage he will leave behind"[23];
2. Impulsively makes decisions and then reverses himself, leaving officials and the public baffled but also nervous about his intentions and ability to follow through on a policy;
3. Frightens people with his assertions that war with Islam and China are on the horizon;
4. Refutes basic scientific knowledge, such as by claiming that "global warming is an expensive hoax!"

We have reviewed some of the claims about Trump's personal disposition because his

character traits help explain some of the actions he took early in his presidency and policies he might pursue in the years to come. As we discuss in coming chapters, President Trump has intentionally upset long-standing international relationships and promoted some values that are profoundly at odds with prevailing global norms. However, it is important to keep in mind that scholars study forces at the other three levels of analysis that can constrain or even counteract the efforts of an individual leader. Domestic politics, democratic checks and balances, the international balance of power, and global economic forces—to name just a few factors—might ensure continuity in many aspects of international relations. The structures of production, trade, finance, security, and knowledge are like trees with deep roots—not easily knocked down by the winds of individual politicians or the storms of nationalist-populism. Readers of this textbook should consider all levels of analysis when forecasting the international political economy.

QUESTIONS TO CONSIDER

Having read our introduction to IPE structures and our brief application of the first and second levels of analysis to some of the notable issues that are discussed more fully in the rest of the textbook, you now have a sense of how IPE scholars examine the complex interrelationships in the world today. As you plunge into the chapters ahead, the terminology, concepts, and countries that still seem unfamiliar will become clearer, and you will become much more fluent in the specific language of IPE. There are many theoretical and policy issues that you will encounter, so we introduce here some main political economy questions that are highlighted in the text:

- In what ways are political structures and markets embedded in society and its cultural institutions?
- With the rise of global *production*, how have the gains from trade and growth been *distributed* between different social groups and countries?
- How do states balance their *domestic political needs* with their *international obligations*?
- How do *social groups and ideas* influence markets and states?
- What political, economic, and social forces underlie the recent increase in the number of authoritarian leaders and populist-nationalist groups all over the world?
- What are the causes and consequences of *inequality* between and within countries?
- How is the rise of *China, India, Russia, and Brazil* reshaping the global economy?
- What do *financial crises* reveal about the *nature of capitalism* and challenges of market *regulation*?
- Are *states losing power* relative to illicit markets and transnational corporations?
- How do *technological changes* affect political and economic processes?
- To what extent can *hegemons* and international institutions provide *global governance* and systemic order in the face of social and political resistance?
- What are the *analytical and policy linkages* between energy and the environment?

CONCLUSION: STANDING ON THE PRECIPICE

The postwar order that emerged between the late 1940s and the early 1970s is coming to an end. The redistribution of global wealth and power has impacted states and societies in ways unimagined even thirty years ago. In 1989 few could foresee that the Berlin Wall would soon fall and that the Soviet Union would dissolve a year later, let alone that the European Union would grow to 28 members. China was still a blip in global manufacturing and trade, and the key rising power was Japan, which some IPE scholars suggested would exercise global financial hegemony alongside U.S. military hegemony.

Since the 9/11 attacks on the Twin Towers and the Pentagon, the postwar global security structure has been undergoing a major transformation away from the peace and stability provided by the major powers—the United States, Russia, China, France, the United Kingdom, and Japan. As part of his "America First" campaign, President Trump has purposefully challenged traditional security policies by weakening U.S. opposition to Russia and taking the world closer to the edge of nuclear war than it has been in more than a generation by threatening to attack North Korea. Traditionally strong U.S. relationships with NATO, Mexico, and South Korea are fraying, leaving a leadership vacuum for China, Russia, and the European Union to fill. Many see another cold war looming between China, Russia, the United States, and their allies.

We also see signs of the end of the postwar order in the European Union, which used to be a model of an integrated community of states but is now threatened by Greek economic troubles and the British vote to leave the union. Authoritarian-nationalist parties and populist leaders in Europe and the United States are promoting anti-immigration and anti-globalization policies. Clearly, the global financial crisis of 2008–2009 increased skepticism towards free markets and imposed major costs on different social groups, many of whom are demanding a democratic role in shaping globalization's rules and rewards. To the dismay of traditional U.S. allies, Trump has raised the specter of a return to malevolent trade protectionism and has sought to roll back regulations on the banking industry put in place after the financial crisis. More broadly, many realists and economic liberals are critical of Trump's rejection of the post-World War II role the United States has played as an economic hegemon that ensures stability and an open global economic system.

The Middle East continues to experience terrorist attacks and major wars with no end in sight. The interventions of the United States, Russia, Saudi Arabia, and Iran have exacerbated social and religious divisions in the region. Hundreds of thousands of soldiers and civilians have been killed and injured in wars that have contributed to a global refugee crisis. At the same time, public officials are coming to grips with the idea that the war on terrorism may not be "winnable" because it is bound up with other intractable socioeconomic and political problems. Other important causes of national and personal insecurity have emerged, including cyber weapons, epidemic diseases, and climate change.

In just one generation hundreds of millions of people have been lifted out of abject poverty in countries such as China, India, and Brazil, and many of them can aspire to join

the middle class. Social mobility and rising consumption have changed many people's lives for the better in the developing world. However, many heterodox liberals and structuralists argue that progress in development may stall in the face of pressures on the earth's resources. A more realistic goal for many developing societies might be "sustainability," which implies scaling back consumption of some types of goods and services.

The rise of India and China is shifting the international balance of power even faster than expected and in ways that could increase North–South tensions. Rising powers have interests that international institutions have yet to accommodate. Long-term negotiations with Brazil, Russia, China, and India may convince developed countries to reform the liberal world order, but there are also many signs of intransigence on both sides that point to more threats to world peace.

Because of the interconnectedness of states and markets, international institutions *must* play some role in solving global problems. Paradoxically, precisely at a time when more collaboration between states is necessary, states seem less willing to cooperate in providing global governance. Changes in ideas at the social level have created tensions between many groups, including those who reject globalization and those who embrace social justice. At the same time, global climate change activists, refugee relief organizations, and other non-governmental organizations have become important purveyors of new ideas and norms.

Anti-austerity movements in many countries, marches for women's rights and racial justice, and protests against authoritarianism remind us of the salience of moral values in the global political economy. Historically, these struggles have occurred primarily through collective action of political parties, unions, and movements; meaningful change rarely comes from individual consumers making "better" choices in the marketplace or powerful elites voluntarily holding themselves to higher standards. Technological improvements and business innovations also do not suffice to prevent us from falling over the precipices we stand before, whether those are climate change or development bottlenecks.

We believe that state leaders will need to re-negotiate security, finance, trade, and knowledge rules in order to mitigate leading global problems. In addition, they will need to redistribute more income and wealth that has concentrated in the top 10 percent of many societies. Already, rising inequality is limiting social mobility and undermining the legitimacy of democracy. Moreover, modern society will be prone to more severe crises unless it can reverse the trend toward precariousness in employment, old age, and education. None of these changes will occur without political-economic conflicts that you will necessarily be involved in, whether directly or indirectly.

We end this chapter with two hopes that we have for you. We hope that you will help humanity find a way to raise standards of living without destroying the earth's environment, climate, and biodiversity. We also hope that as you devise solutions to contentious economic and political problems, you show compassion for the most vulnerable people in the world.

KEY TERMS

regime 3
international political economy 4
economic liberalism 5
globalization 8
mercantilism 8
realism 8
nation 8
state 8
sovereignty 8
hard power 8
soft power 8
structuralism 8
constructivism 8
level of analysis 10
IPE structures 12
global governance 21

DISCUSSION QUESTIONS

1. Pick a recent news article that focuses on an international or global problem, and give examples of how states, markets, and societies interact over this problem. How hard is it to determine the analytical boundaries between the state, market, and society in this case?
2. Review the basic elements of the four main IPE theoretical perspectives, the five IPE structures, the levels of analysis, and the types of power. Discuss the connection between each of the four IPE theoretical perspectives and your own values.
3. Choose a global event or process that you know something about and identify at least one factor at each level of analysis that helped cause it and shape its trajectory.
4. Based on what you have learned in this chapter and from reading newspapers, explain whether or not you believe that the world is standing on the edge of many precipices. Which of the global issues presented in this chapter are you most concerned about and why?

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CHAPTER

2

Laissez-Faire: The Economic Liberal Perspective



Demonstrators near the site of the USA Republican National Convention, July 2016.

Source: Shutterstock/EPA/Justin Lane.

> *A man's right to work as he will, to spend what he earns, to own property, to have the state as servant and not as master. […] They are the essence of a free economy. And on that freedom all our other freedoms depend.*
>
> Margaret Thatcher[1]

Like many other terms in international political economy (IPE), the generic term "liberalism" suffers from something of a personality disorder. The term means different things in different contexts. In the United States today, for example, a liberal is generally regarded as one who believes in an *active* role for the state in society, such as helping the poor and funding programs to address social problems. Since the mid-1980s, someone who has been thought of more narrowly as an *economic liberal* believes *almost* (but not exactly)

the opposite. For economic liberals (also referred to as neoliberals), the state should play a *limited* role in the economy and society. In other words, today's economic liberals have much in common with people who are usually referred to as "conservatives" in the United States, Europe, Canada, and Australia.

This chapter traces the historical rise of economic liberalism in eighteenth- and nineteenth-century England and in the United States and Europe since the Great Depression. We outline some of the basic tenets of capitalism, a focal point of liberal thought. Throughout the chapter, we also discuss the views of some of the most famous liberal political economists: Adam Smith, David Ricardo, John Maynard Keynes, Friedrich Hayek, and Milton Friedman. We then contrast the views of orthodox and heterodox liberals regarding the 2007–2008 financial crisis and globalization.

There are four main theses in this chapter:

- First, economic liberal ideas continue to evolve as a reflection of changes in the global economy and the power of different actors and institutions.
- Second, economic liberalism gained renewed popularity due to its association with the policies of the Reagan and Thatcher administrations, culminating in the globalization campaign of the 1990s.
- Third, orthodox liberalism has increasingly come under attack for its failure to predict or sufficiently deal with such things as the financial crisis and the effects of globalization.
- Fourth, we argue that, although weakened, laissez-faire ideas and policies are likely to remain popular in the United States and many other nations.

ROOTS OF THE ECONOMIC LIBERAL PERSPECTIVE

Essentially, the broad term "liberalism" means "liberty under the law."[2] Liberalism focuses on the side of human nature that is competitive in a constructive way and is guided by reason, not emotions. Although liberals believe that people are fundamentally self-interested, they do not see this as a disadvantage because competing interests in society can engage one another constructively. This contrasts with the mercantilist view, which, as we will see in Chapter 3, dwells on the side of human nature that is more aggressive, combative, and suspicious.

Classical economic liberalism is rooted in reactions to important trends in Europe in the seventeenth and eighteenth centuries. François Quesnay (1694–1774), who led a group of French philosophers called the Physiocrats or *les Économistes*, condemned government interference in the market, holding that, with few exceptions, it brought harm to society. The Physiocrats' motto was *laissez-faire, laissez-passer*, meaning "let be, let pass," but said in the spirit of telling the state, "Hands off! Leave us alone!" This became the theme of Adam Smith (1723–1790), a Scottish contemporary of Quesnay who is generally regarded as the father of modern economics. Smith and many since him, including David Ricardo, Friedrich Hayek, and Milton Friedman, admire the market, even while recognizing its abusive potential.

In his famous book *The Wealth of Nations*, Smith opposed the mercantilist state of the eighteenth century, established on the principle that the nation is best served when state power is used to create wealth and national security (see Chapter 3). He criticized Britain's Parliament for representing the interests of the landed gentry and monopolistic trading corporations, not those of the entrepreneurs and citizens of the growing industrial centers. Not until the 1830s was Parliament reformed enough to redistribute political power more widely. For classical economic liberals, individual freedom in the marketplace leads to an efficient allocation of resources and helps reduce potentially abusive state power. Most importantly, a "commercial society" (in Smith's parlance) should produce rising standards of living for all members of society.

Smith believed in the cooperative, constructive side of human nature. For him, the best interest of all of society is served by (rational) individual choices, which when observed from afar appear as an *invisible hand* that guides the economy and promotes the common good. He wrote:

> He [the typical citizen] generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its own produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, directed by an invisible hand to promote an end which was no part of his intention.[3]

Smith was writing at a time when the production system known as capitalism was replacing feudalism. What follows is a brief overview of some of the ideals and tenets of capitalism based on Smith's work—or at least the way many economic liberals today interpret his work.

The Dominant Features of Capitalism

The five main elements of capitalism are as follows:

- Markets *coordinate* society's economic activities.
- Extensive markets exist for the exchange of land, labor, commodities, and money.
- Consumer self-interests motivate economic activity, while competition *regulates* economic activity.
- Individuals have the freedom to start up new business enterprises without state permission.
- Individuals have the right to private property and are entitled to the income that flows from their property.

The first three tenets address the nature and behavior of markets. In the modern market, products and services are commodified—that is, a market price is established for goods and services as a result of producers setting prices for their goods and buyers paying for them. Another feature of capitalism is the existence of markets for land, labor, and money. The economic historian and anthropologist Karl Polanyi wrote extensively about how modern capitalism gradually came about in seventeenth-century Great Britain when land was privatized, people moved off the countryside and into small factories, and trade generated capital (money). Land, labor, and capital were all commodified, which provided the financial foundation and labor for the industrial revolution and the society that today we recognize as capitalist.[4]

When economists say that competition *regulates* economic activity, they are referring to the ways in which markets convert the pursuit of consumer self-interests into an outcome that inevitably benefits all of society. According to Smith, the pursuit of individual self-interest does not lead to civil disorder or even anarchy; rather, *self-interest serves society's interests*. Smith famously said, "It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our necessities but of their advantages."[5]

In a capitalist economy, self-interest drives individuals to make rational choices that best serve their own needs and desires. However, it is competition that *constrains* and *disciplines* self-interest and prevents it from becoming destructive to the interests of others. Under ideal circumstances, producers must compete with others, which forces them to charge reasonable prices and provide quality goods to their customers, or lose their business. Consumers also face competition from other consumers who may be willing to pay more for a product. Even if producers might want to push prices high and buyers might want to

push prices low, the force of competition keeps the pursuit of self-interest from going to the extreme.

Capitalism assumes that price competition also results in the *efficient* allocation of resources among competing uses. When economists say that markets coordinate society's economic activity, they generally mean that no one (especially the state) should be in charge of how resources are allocated. Market coordination entails a decentralized (spread out) resource allocation process guided by the tastes and preferences of individual consumers.

For capitalists, government intervention in the market generally distorts resource reallocation and frustrates the coordination function we have described. Competition also requires firms to produce efficiently, in the sense that it pays to adopt cost-saving innovations and to remain on the cutting edge of product and process innovation, the delivery of services, and the management of resources. The leaders of even the most powerful firms such as Microsoft, Ericsson, or Petrobras must keep one step ahead of technologically audacious newcomers if they wish to retain their share of the market.

The last two tenets of capitalism deal with the role of the state in establishing freedom of enterprise and private property. Freedom of enterprise means that businesses can easily channel resources to the production of goods and services that are in high demand while simultaneously intensifying competitive pressures in these industries. When individuals are free to make their own career choices, they naturally prepare for and seek out careers or lines of employment in which they are likely to be most productive. Likewise, as economic circumstances change, labor resources will be rapidly redeployed to growing sectors of the economy as individuals take advantage of new opportunities.

The income of those who own capital is usually in the form of profits (as opposed to wages). Capital goods—plants, equipment, and tools that workers need—are the important subset of all commodities that are required to produce other commodities. In a capitalist economy, the owners pay for the costs of production—the wages of the workers, the raw materials, and all intermediate goods used in production—and then sell the finished commodities on the market. Whatever is left over, the difference between the revenue and the costs, belongs to the capitalist owners. This is a legal right of ownership, referred to as capitalist property rights. A capitalist may completely own a business, a local bar, or a high-tech start-up, for example. In contrast, the owners of a corporation are those who own its stocks, which can be bought and sold on a stock market.

When property rights are less clear, the incentive to use resources efficiently diminishes. Private property—clear title to land, for example—also encourages the owner to make investments in improving the land and provides the owner the collateral with which to obtain the credit necessary to do so. Consequently, the resource owner makes every effort to ensure that the resource is used efficiently (i.e., profitably).

Freedom of enterprise allows entrepreneurs to test new ideas in the marketplace. In a dynamic world of changing tastes and preferences, the availability of resources and new technologies foments product and production process innovation. In such an environment, entrepreneurs must rapidly redeploy their resources to changing circumstances when new opportunities arise. Freedom of enterprise also allows firms to increase or reduce their labor

force as necessary. Because firms can easily expand and contract, the associated risk of changes is minimized, and competition is consequently enhanced.

What Smith is most known for, then, is the view that ideally a capitalist economy is largely self-motivating, self-coordinating, and self-regulating. Consumers determine how resources will be allocated; self-interest motivates firms and their workers to produce the goods and services consumers desire; the market coordinates economic activity by communicating the ever-changing tastes and preferences of consumers to producers; and competition ensures that the pursuit of self-interest serves social (consumer) interests.

Smith, the Cynic and Moralist

Smith is a complex, nuanced philosopher. In fact, some of the ideas in his other major work, *The Theory of Moral Sentiments*, appear to contradict the more orthodox liberal ideas with which he is most often associated, such as the metaphor of the "invisible hand." In this section we present some of Smith's lesser-known ideas about the role of the state, moral behavior, and the interests of market actors.

Smith recognized that the state has some necessary and legitimate functions in society, such as defending the country, policing, building public works, preventing the spread of diseases, enforcing contracts, and helping to achieve individual rights. Smith was also quite adamant in his distrust of businesspeople. One of his famous quotes is that "people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."[6] The pursuit of self-interest by a monopoly producer, for example, often leads to restricted output, higher prices for goods, and a consequent loss of social welfare. Smith also distrusted bankers and noted that employers always sought to keep wages low: "When the regulation … is in favor of the workmen, it is always just and equitable; but it is sometimes otherwise when in favor of the masters."[7]

Smith believed that merchants and trading companies often had disproportionate influence over the Parliament and could press their "private interests." They easily influenced the legislature to establish licenses, franchises, tariffs, and quotas that restricted competition. Often, their trading companies gained the sole right to sell products, keeping market prices above the natural price.

We see a similar dynamic today in the success of corporations in pushing governments to strengthen patents, which are legal, temporary monopolies on inventions allowing their owners to prevent others from using their inventions without their permission. Because patents limit competition, corporations can sometimes reap exorbitant profits from goods covered by them. For example, during the period 1996 to 2010 when Pfizer had a patent on Lipitor, one of the world's most popular drugs, cumulative sales of this cholesterol-fighting statin reached an astonishing $118 billion. Similarly, from just 2014 to 2016, Gilead Sciences had sales of $45 billion from just two extremely expensive patented drugs, Solvaldi and Harvoni, that are effective against Hepatitis C. Large firms are more likely to invest in costly new products if they are *guaranteed* captive markets through patents and

other forms of intellectual property rights. Thus, corporations hire major lobbying firms to press for legislation that helps preserve their competitive advantage over other companies.

While Smith *opposed* having the state try to direct investments because it might be counterproductive and unnecessary, he *supported* the state exercising vigilance, enforcing competition policies, and helping the market work properly. Today we would say that in capitalist economies Smith opposed rent-seeking (the manipulation of the market to reward powerful business interests). For Smith, the market's invisible hand cannot work for the benefit of all society if there isn't competition. He viewed the state (the *visible* hand?) as necessary to prevent capitalists themselves from destroying the market, and he also recognized that powerful political interests could use the state to create an unfair market.

In his often-overlooked book *The Theory of Moral Sentiments*, Smith argued that in a properly structured market, commercial activity would produce righteous and prudent people. Even as people pursue their self-interests, their passions are *restrained* by competition that induces them to best serve *the interests of others*, to behave honestly, and to gain a reputation for *fairness*. In a world of intense competition, commercial society was a way to channel self-interest into a less morally corrupt society than during feudalism. Smith believed that as the labor force grew in size, the welfare of "servants, laborers, and workmen of different kinds" should be the prime concern of economic policy. Sounding a bit like Marx, he insisted that "no society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable."[8] Smith was convinced that a commercial society (what we today call capitalism) with competition, a division of labor, and good governance would tend to produce "universal opulence" such that even the lowest classes would have a significantly higher standard of living.

THE TRANSFORMATION OF LIBERAL IDEAS AND POLICIES

Adam Smith's writings were part of a broader intellectual movement that engendered intense economic and political change in society. Classical liberals at the time included John Locke (1632–1704) in England and Thomas Jefferson (1743–1826) in the United States. Economic theorists tend to think of laissez-faire in terms of markets. However, this philosophy also implies that citizens need to possess certain negative rights (freedoms *from* state authority, such as freedom from unlawful arrest), positive rights (which include inalienable rights and freedoms to take certain actions, such as freedom of speech or freedom of the press), and the right of democratic participation in government, without which positive and negative freedoms cannot be guaranteed.[9] These classical liberal political ideas are embedded firmly in the U.S. Declaration of Independence and the Bill of Rights, which were becoming well known about the same time as Adam Smith's notion of consumer freedom.

Economic liberals expect that nation-states will find it worthwhile to act cooperatively and peacefully through harmonious competition. As we will see in Chapter 7, international trade is seen as being mutually advantageous, not merely cutthroat competition for wealth and power. What is true about individuals is also true about states. As Smith wrote, "What is prudence in the conduct of every family can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our industry, employed in a way in which we have some advantage."[10] Although Smith opposed most state restrictions on international markets, he *did* support the mercantilist Navigation Acts that protected British industries by requiring their goods be shipped to British colonies in British vessels.

David Ricardo (1772–1823) followed Smith in adopting the classical economic liberal view of international affairs. He was a particular champion of free trade, which made him part of the minority in Britain's Parliament in his day. He opposed the Corn Laws (see Box 2.1), which restricted agricultural trade. As one of the first to explore some of the precepts of a natural (scientific) law about trade, Ricardo argued:

> Under a system of perfectly free commerce, each country naturally devotes its capital and labour to such employments as are most beneficial to each. The pursuit of individual advantage is admirably connected with the universal good of the whole. By stimulating industry, by rewarding ingenuity, and by using most efficaciously the peculiar powers bestowed by nature, it distributes labour most effectively and most economically: while, by increasing the general mass of productions, it diffuses general benefit, and binds together, by one common tie of interest and intercourse, the universal society of nations throughout the civilized world.[11]

For Ricardo, free commerce produces efficiency, a quality that liberals value almost as

highly as liberty. Like Smith, he believed that individual success is "admirably connected" with "universal good." The free international market stimulates industry, encourages innovation, and creates a "general benefit" by raising production. In IPE jargon, economic liberals view the outcomes of state, market, and society relations as a positive-sum game, in which everyone can potentially get more by making bargains with others as opposed to not trading with them. Mercantilists, on the other hand, tend to view economic transactions as a zero-sum game, in which gains by one person or group necessarily come at the expense of others (see Chapter 3).

BRITAIN'S CORN LAWS

Britain's Parliament enacted the Corn Laws in 1815, soon after the defeat of Napoleon ended twelve long years of war. The Corn Laws were a system of tariffs and regulations that restricted grain imports into Great Britain. The battle over the Corn Laws, which lasted from their inception until they were finally repealed in 1846, is a classic IPE case study of the conflict between liberalism and mercantilism.

Why would Britain seek to limit imports of grain? The "official" argument was that Britain needed to be self-sufficient in food, and the Corn Laws were a way to ensure that it did not become dependent on uncertain foreign supplies. This sort of argument carried some weight at the time, given Britain's wartime experiences (although Napoleon never attempted to cut off food supplies to Great Britain).

There were other reasons for Parliament's support of the Corn Laws, however. The right to vote in Parliament was not universal, and members were chosen based on rural landholdings, not on the distribution of population. As a result, Parliament represented the largely agricultural interests of the landed estates, which were an important source of both power and wealth in the seventeenth and eighteenth centuries. The growing industrial cities were not represented in Parliament to a proportional degree.

Seen in this light, it is clear that the Corn Laws were in the economic interests of the members of Parliament and their allies. They were detrimental, however, to the rising industrial interests in two ways. First, by forcing food prices up, the Corn Laws indirectly forced employers to increase the wages they paid to their workers. This increased production costs and squeezed profits. Second, by reducing Britain's grain imports from other countries, the Corn Laws indirectly limited Britain's manufactured exports to these markets. The United States, for example, counted on sales of agricultural goods to Britain to generate the cash to pay for imported manufactured goods.

Clearly, the industrialists favored repeal of the Corn Laws, but they lacked the political power to achieve their goal. This changed, however, when the Parliamentary Reform Act of 1832 revised the system of parliamentary representation, reducing the power of the landed elites and increasing the power of manufacturers in emerging industrial centers.

In an act of high political drama, the Corn Laws were repealed in 1846, which changed the course of British trade policy for a generation. Although this repeal is often seen as the triumph of liberal views over old-fashioned mercantilism, it is perhaps better seen as the victory of the masses over the agricultural oligarchy. Britain's population had grown quickly during the first half of the nineteenth century, and agricultural self-sufficiency was increasingly difficult, even with rising farm productivity. Crop failures in Ireland (the potato famine) in the 1840s left Parliament

with little choice: either repeal the Corn Laws or face famine and food riots.

Cheaper food and bigger export markets helped fuel a rapid expansion of the British economy. Britain embraced a liberal view of trade for the rest of the century. Given its place in the global political economy as the *workshop of the world*, Britain found that liberal policies were the most effective way to build its national wealth and power. Other nations, however, felt threatened by Britain's power and adopted mercantilist policies in self-defense.

The Corn Laws illustrate how changes in the wealth-producing structure of the economy (from farm to industry, from country to city) led eventually to a change in the distribution of state power. The case also shows that the market is not apolitical; it is put in service of those groups that control the state and have the most social and cultural power.

Ricardo argued that these positive-sum payoffs of trade bind together the nations of the world by a common thread of interest and intercourse. As is often argued by those who support globalization today, free individual actions in the production, finance, and knowledge structures create such strong ties of mutual advantage among nations that military hostilities between them become much more unlikely.

JOHN STUART MILL AND THE EVOLUTION OF THE LIBERAL PERSPECTIVE

The liberal view has evolved over the years as the nature of state–market–society interaction has changed. John Stuart Mill (1806–1873), who inherited the liberalism of Smith and Ricardo, helped redefine it in his textbook *Principles of Political Economy with Some of Their Applications to Social Philosophy* (1848) (published the same year as Marx and Engels' *Communist Manifesto*).

Mill held that the liberal ideas behind European capitalism had been an important *destructive* force in the eighteenth century—even if they were also the intellectual foundation of the revolutions and reforms that weakened central authority and strengthened individual liberty in the United States and Europe. He developed a philosophy of social progress based on "moral and spiritual progress rather than the mere accumulation of wealth."[12] Mill doubted that the competition and economic freedom inherent in capitalism would automatically translate the pursuit of self-interest into society's welfare. At the time he was writing, many people were working in factories but living in more wretched conditions than those that existed in Smith's and Ricardo's times. Whole families worked six days a week for more than eight hours a day. Many were routinely laid off with little notice.

Mill acknowledged the problems created by the market's inherent inequality of outcomes. He proposed that the state should take definitive action to supplement the market, correcting for its failures or weaknesses. He advocated *selective* state action in some areas, such as assisting the poor, when individual initiative might be inadequate in promoting social welfare. He supported more decentralization of government and argued that parents should be required to educate their children, if necessary with support from the state.[13]

Mill's views on social issues reflect the evolution of liberalism in his time. The guiding principle was still laissez-faire, but in some circumstances limited government actions were desirable. The two key questions for Mill, as for liberal thinkers since his time, are:

- When is the government justified in using its *visible* hand to assist or replace the invisible hand of the market?
- How far can the state go before its interference with individual rights and liberties becomes abusive?

JOHN MAYNARD KEYNES AND THE GREAT DEPRESSION

One of the most influential political economists of the twentieth century was John Maynard Keynes (1883–1946)—pronounced "canes"—who developed a subtle and compelling strain of liberalism called Keynesianism. Like Mill, Keynes was concerned with the negative impact of markets on society. His ideas were especially popular from the 1930s through the early 1970s. The 2007–2008 financial crisis caused many experts to become more critical of laissez-faire ideas and look back to Keynes for an explanation of why crises occur and how to resolve them.

A civil servant, writer, farmer, lecturer, and Director of the Bank of England, Keynes refuted some of the principles of classical economic liberalism. He believed that the Great Depression was evidence that the invisible hand of the market sometimes errs in catastrophic ways. As early as 1926, he wrote:

> Let us clear from the ground the metaphysical or general principles upon which, from time to time, laissez-faire has been founded. It is *not* true that individuals possess a prescriptive "Natural liberty" in their economic activities. There is *no* "compact" conferring perpetual rights on those who Have or on those who Acquire. The world is *not* so governed from above that private and social interest always coincide. … Nor is it true that self-interest generally *is* enlightened; more often individuals acting separately to promote their own ends are too ignorant or too weak to attain even these. Experience does *not* show that individuals, when they make up a social unit, are always less clearsighted than when they act separately.[14]

Keynes argued that the market does not always translate the rational and selfish behavior of individual actors (consumers, workers, and firms) into an outcome that is socially optimal. He did not believe that the market is a self-correcting institution wherein deviations from full employment—something that resulted from an outside "shock" to the system—set in motion changes in prices, wages, and interest rates that quickly restore full employment.

In Keynes's view, individuals tend to make decisions that are particularly unwise when they are faced with situations in which the future is *uncertain* and there is no effective way to share risks or coordinate otherwise chaotic actions. Keynes emphasizes that it *is* possible for individuals to behave rationally and in their individual self-interest and yet for the *collective result* to be both irrational and destructive—a clear failure of the invisible hand. The stock market crash of 1929, the Asian crisis of 1997, and the 2007–2008 global financial crisis demonstrate what can happen when investors are spooked and stampede out of the market (see Chapter 8).

In these conditions, people often predict a very bleak future or at least find it difficult to "think rationally" about the future, leading to what Keynes calls a paradox of thrift. What is the rational thing to do when one is threatened by unemployment? One rational response

to uncertainty about your future income is to spend less and save more, to build up a cushion of funds in case you need them later (just as many people did during the 2007–2008 financial crisis). But if everyone spends less, then less is purchased, less is produced, fewer workers are needed, and income declines. Furthermore, the recession and unemployment that everyone fears will come to pass is in fact *sustained* by the very actions that individuals take to protect themselves from this eventuality. Keynes also worried about speculation in the international economy and the damage it could do if it was not regulated in some fashion. These conditions, then, make financial markets fragile and prone to economic disaster.

For Keynes, constructive state action enhances economic stability. He argued that organs of the state should regulate "many of the inner intricacies of private business" yet "leave private initiative and enterprise unhindered."[15] Within the system of capitalism, he envisioned working out "a social organization which shall be as efficient as possible without offending our notions of a satisfactory way of life."[16]

During the Great Depression, many states used monetary and fiscal policies to sustain wages for labor and to stimulate economic growth. Because businesses were afraid to invest, states needed to run a deficit temporarily—without worrying about inflation—in order to encourage production and consumption. In the United States, President Franklin Roosevelt adopted many other Keynesian policy suggestions including public works projects to stimulate employment, unemployment insurance, bank deposit insurance to improve investor confidence in banks, and social security.

Keynes also made clear that the state should use its power to improve the market, but *not* along the aggressive, nationalistic lines of mercantilism. He worried that under the strain of the Great Depression people could easily turn toward an ideology like Fascism or Nazism for solutions to their problems. He viewed the Soviet regime's repression and disregard for individual freedom as intolerable. He argued that a liberal system is one that respects individual freedom, not one that limits it for the sake of security. Beyond all else, Keynes was a moral humanist who wanted to get beyond the problem of accumulating wealth, which he viewed as "a somewhat disgusting morbidity," to a society where most people could instead spend their leisure time contemplating and living a good life.

Embedded Liberalism: Reconciling Domestic and International Interests

Keynes is also noted for the role he played in helping to reconstruct Western Europe after World War II and establish the new international economic order. At a meeting of the Allied nations at Bretton Woods, New Hampshire, in 1944, two new institutions were created to manage the postwar economy: the IMF and the World Bank. Three years later, the General Agreement on Tariffs and Trade (GATT) was created to manage international trade. Keynes headed the British delegation at Bretton Woods, and the institutional result, though not his plan, certainly reflected many of his ideas.

One of the problems that arose from the meeting was how to square two objectives that the Allies agreed were necessary to restore stability and economic growth in the

international economy while helping states recover from the war. On the one hand, Keynes believed that on the domestic front government action was both useful and necessary to deal with problems that the invisible hand did not solve. On the other hand, he envisioned an open international system in which market forces and free-trade policies would play major roles. The way to reconcile these two objectives was through creating a system that John Ruggie calls embedded liberalism in which strong international markets would be subject to political restraints and regulations that reflected domestic priorities.[17] In other words, the democratic state would intervene in the domestic economy and place some limits on international markets in order to protect society, but it would also support a broadly liberal market economy and relatively free trade.

On the international level, embedded liberalism was reflected in the Bretton Woods institutions through which states managed economic exchanges with peaceful cooperation. States agreed to work together to *gradually* reduce their trade and finance regulations so as to open their national economies as they recovered and became more competitive. Between the 1940s and the 1970s, tariffs and other barriers to free trade were progressively lowered. In order to avoid excessive exchange rate fluctuations, Western states set up a system of fixed exchange rates whereby currencies were pegged to the dollar and the dollar was pegged to gold. Importantly, states maintained capital controls to restrict the movement of capital across borders. A cornerstone of this system was multilateral cooperation to manage international economic relations.

Embedded liberalism was also based on a set of policies at the domestic level of each country. Broadly speaking, these policies rested on what has been called the Keynesian compromise—a sort of class compromise whereby owners of capital would share gains from growth and rising productivity with workers in the form of rising wages and benefits, while workers maintained social peace and accepted the legitimacy of the liberal capitalist system. Both sides accepted significant state intervention in the market economy to stabilize and strengthen it. Governments would use spending in times of recession to ensure full employment and increase demand, and they would expand social welfare programs to redistribute more income to the lower and rising middle classes, ensuring that these classes could consume the growing output of factories and fuel growth that brought profit to owners of capital.

The system of embedded liberalism relied on the government to protect society from the excesses of the market. Greater regulation of businesses, higher taxes on the wealthy, and greater state spending made capitalism more compatible with domestic stability and democratic demands. The state tried to compensate those groups that were hurt by trade liberalization and eventually freer flows of capital across borders. In the early days of the Cold War, economic productivity and GDP grew rapidly, as did international trade. The 1950s to the 1970s were regarded as a "golden age" of capitalism in both the United States and Western Europe. In places such as Great Britain, France, West Germany, and Sweden, the role of the state was emphasized to a greater degree, creating something akin to a democratic-socialist system. In the United States, state policy became much more activist than in previous decades. The U.S. federal government intervened in the economy at home

and abroad in various ways, such as by exploring space, promoting civil rights, implementing the Great Society antipoverty programs, helping the elderly with Medicare medical insurance, and regulating corporations.

Many political economists argue that this post-World War II system worked well because the United States bore the costs of maintaining the global monetary system and providing for the defense of its allies. As a result, Japan and Western Europe could spend more for their recovery while benefiting from a system of open trade, sound money, and peace that stimulated the growth of markets everywhere. More generally, hegemonic stability theory is the idea that international markets work best when a hegemon (a single dominant state) accepts the costs associated with keeping them open for the benefit of both itself and its allies by providing them with certain international public goods at its own expense.[18]

But as time went on, U.S., West European, and Japanese interests changed, and as they did, hegemony gradually became more expensive for all involved to sustain (or put up with, depending on one's perspective). By the late 1960s, economic growth was gradually shifting wealth and power away from the United States and toward Western Europe and Japan, changing the fundamental (cooperative) relationship of the United States to its allies. At the same time, the United States felt strongly that the costs of fighting the war in Vietnam were becoming prohibitive without more allied financial and political support.

THE RISE OF NEOLIBERALISM

In the late 1960s, President Nixon and others attacked Keynesianism and the cost of President Johnson's Great Society program, seeking to put more emphasis on economic growth instead of stability. As we discuss in Chapter 8, in 1973 the United States replaced its fixed exchange rate system with a flexible exchange rate system, which led to increased currency speculation and more money circulating in the international economy. That same year the oil price hikes by the Organization of the Petroleum Exporting Countries (OPEC) led to an economic recession in the industrialized nations, but also the recycling of massive amounts of OPEC's earnings into Western banks. Meanwhile, Western Europe, Japan, Taiwan, and South Korea were competing with the United States for new markets. Keynesian policies to deal with the recession generated stagflation—a combination of low growth and high inflation, which were not supposed to occur together.

In this environment of low economic growth and increasing competitiveness, Keynes's ideas were gradually replaced by those of the Austrian Friedrich Hayek (1899–1992) and the American Milton Friedman (1912–2006). Their orthodox liberal values favored "minimally fettered" capitalism—or a *limited* state role in the economy. Their increasingly popular ideas laid the intellectual groundwork for what became a distinct variation of economic liberalism called neoliberalism.

Hayek's most influential work, *The Road to Serfdom*, explored growing state influence that he felt represented a fundamental threat to individual liberty. In his view, allowing more government intervention to provide greater economic security was the first step on a slippery slope to socialism or fascism. He warned against reliance on "national planners" who promised to create economic utopias by supplanting competition with a government-directed system of production, pricing, and redistribution. Drawing on pre-Keynesian theories of economic liberalism, Hayek argued that the only way to have security *and* freedom was to limit the role of government and let the market provide opportunities to free individuals.

Contrasting the "collectivist" ideas of socialism with the virtues of an economy with real freedom, he wrote:

> The virtues which are held less and less in esteem … are precisely those on which Anglo-Saxons justly prided themselves and in which they were generally recognized to excel. These virtues were independence and self-reliance, individual initiative and local responsibility, the successful reliance on voluntary activity, noninterference with one's neighbor and tolerance of the different, and a healthy suspicion of power and authority. Almost all the traditions and institutions which … have molded the national character and the whole moral climate of England and America are those which the progress of collectivism and its centralistic tendencies are progressively destroying.[19]

Hayek warned that when a state overspends or prints too much money, it can easily cause

inflation that destroys an economy.[20] He chided social democrats for being unwilling to recognize that the price of a large welfare system is more government debt. A healthy economy requires that the state not interfere in private economic decisions. Instead of worrying about employment, the state should balance its budget, manage the money supply to control inflation, and encourage people to save. To do so requires taking control of the money supply out of the hands of politicians—lest liberty be lost when the majority pressures the government to spend more than it has.

Echoing Hayek's foundation, Milton Friedman wrestled with the problem of keeping government from becoming a "Frankenstein that will destroy the very freedom we establish it to protect." According to Friedman, government "is an instrument through which we can exercise our freedom; yet by concentrating power in political hands, it is also a threat to *freedom*."[21] In his book *Capitalism and Freedom*, he consciously returns to the classical liberalism of Adam Smith, stressing that capitalism preserves and protects liberty by naturally diffusing power.

In the early 1980s, Prime Minister Margaret Thatcher of Great Britain and U.S. president Ronald Reagan became the chief practitioners of policies derived from the ideas of Hayek and Friedman. Keynesianism was out of fashion. Thatcher's motto was TINA —"There Is No Alternative" to neoliberal economic policies. Neoliberalism emphasizes economic growth over stability. President Reagan promoted "supply-side economics," which is the idea that lower taxes rather than increased government spending will increase investment and spur job creation, thus generating higher demand and economic growth. The top income tax rate in the United States was cut in stages from 70 percent in 1980 to 33 percent in 1986.

Deregulation and privatization were also important elements of neoliberalism in the 1980s. Regulations on banking, energy, and investment were weakened or removed in order to promote greater competition and efficiency. Many national telecommunications, airline, and trucking industries were *privatized* (sold off to wealthy individuals or corporations) to allow for greater competition and freedom to set prices. Some public housing in Britain was privatized, and welfare programs in both the United States and Great Britain were "rolled back" (shrunk). Many neoliberals argued that the state was too big and had been captured by powerful special interests. They believed that a free market would redistribute income to those who are most efficient, innovative, and hard working. Although these policies might lead to greater income inequality, economic growth at the top of society would gradually "trickle down" to benefit labor and society's masses. Finally, the rule of thumb for both Reagan and Thatcher was that the state should lessen its interference in all areas of public policy except security, where both advocated a strong anticommunist stance.

It should be noted that many of Hayek's and Friedman's neoliberal views—and the ideals espoused by Reagan and Thatcher—are echoed by contemporary economic liberals such as Paul Ryan, who became the Speaker of the U.S. House of Representatives in 2015. Writing in 2011 in the conservative *Wall Street Journal*, Ryan argued that high-taxing, high-spending, highly indebted European states should not serve as models for good

government. Rather, he believes that American freedom could best be ensured by, among other things, limiting the size of the state and relying on "families, communities, churches and local institutions—and [on] the government only as a last resort."[22] "Paternalistic government," Ryan asserted, "will stand in the way of the pursuit of happiness and the good life."

GLOBALIZATION

While neoliberalism was spreading in the mid-1980s, the United States and other industrialized nations began promoting globalization—the extension of economic liberal principles the world over—as a process that would boost economic growth and bring democracy to those nations integrated into this capitalist structure. Emphasizing the role of unfettered markets (unchained by the state), globalization promised to enhance production efficiency, spread new technologies, and generate jobs in response to increased demand.

A confluence of changes in the world created a ripe environment for globalization to spread. A dramatic reduction in transportation costs boosted industrial outsourcing and trade. New digital technologies such as the Internet and fiber optics revolutionized communications and work processes, allowing information to move across borders quickly. *Speed* and the *death of distance* were becoming major features of end-of-the-century communications, commerce, and innovation. Moreover, holders of large pools of capital were searching for investment opportunities in new markets that promised higher rates of return than in the mature industrialized economies.

Along with these changes, the fall of the Berlin Wall caused a shift from a predominately Cold War world order (1947–1990), where states were preoccupied with territorial security and military power, to something more akin to a pluralistic world order in which economic issues dominated the global agenda. With the collapse of many communist regimes in the late 1980s, new governments in Eastern Europe and in newly independent countries of the former Soviet Union replaced centralized state planning with more market-oriented strategies and opened their economies to foreign investment and trade. In the late 1980s and throughout the 1990s, many of the newly industrializing states in east and southeast Asia grew quickly, adopting export-led growth strategies and integrating themselves into the new "global economy" through trade. And some leaders in Latin America began to support more market-friendly policies following crippling debt crises in the 1980s.

By the first half of the 1990s, many governments were implementing deregulation and privatization. Neoliberalism seemed to be practically and theoretically "triumphant." The Clinton administration also promoted globalization, negotiating a plethora of free-trade deals such as North American Free Trade Agreement (NAFTA) and helping create the WTO (see Chapter 7). Some Central and Eastern European states became members of the European Union's single market. Mexico, India, and China all adopted pro-market reforms, encouraged foreign investment, and massively boosted trade with the United States.

Many of the economic liberals who were analyzing the dizzying changes in the global economy in this period ascribed to globalization some combination of these characteristics:

- An *economic process* that reflects dense interconnections based on new technologies and the mobility of capital;
- The *integration* of national markets into a single global market;

- A *political process* that weakens state authority;
- A *cultural process* leading to complex cultural interconnections; and
- A process that *benefits* everyone economically and helps spread *democracy* in the world.[23]

New York Times columnist Thomas Friedman articulated the beliefs of many globalization enthusiasts, tying free trade and capital mobility to production efficiency and individual empowerment. In his popular book *The Lexus and the Olive Tree*, Friedman asserts that globalization often requires a "golden straightjacket"—a set of sovereignty-limiting, economic liberal policies that must be implemented if states want to realize globalization's benefits.[24] He believes that intensely competitive global capitalism drives individuals, states, and TNCs to continually produce new and better products. In his book *The World Is Flat*, he argues that new technological developments are leveling the global playing field, giving individuals in places like Bangalore and Beijing the ability to compete with and collaborate with individuals in Boston and Silicon Valley.[25]

QUESTIONING NEOLIBERALISM AND GLOBALIZATION IN THE 1990S AND 2000S

As early as the 1990s, anti-globalization activists and heterodox economic liberal scholars began pointing to mounting problems and unintended consequences that stemmed from neoliberal-inspired globalization. They proposed different solutions but shared the idea that markets need to be embedded in social and political institutions in order to have legitimacy and to resolve fundamental human problems. In the short run, unfettered global markets were hurting some of the world's poorest people and destroying the environment. In the long run, through outsourcing and environmental degradation, they might even undermine the prosperity of developed countries.

The Anti-Globalization Movement

As globalization grew in popularity, so did resistance to many of its effects. The political scientist Benjamin Barber argued that the forces of "McWorld" (globalization) were arrayed against the forces of "Jihad" that wanted to preserve national sovereignty and national solidarity.[26] Some critics saw globalization as merely a shibboleth of free-market champions —a wildcat version of capitalism that promised higher standards of living but increased the misery or marginalization of many people. Marxist political scientists Leo Panitch and Sam Gindin described globalization (driven in part by the U.S. Treasury and the Federal Reserve) as a process of spreading U.S. economic practices and institutions to foreign countries: "It was the immense strength of US capitalism which made globalization possible, and what continued to make the American state distinctive was its vital role in management and superintending capitalism on a worldwide plane."[27] According to Ignacio Ramonet, the former editor-in-chief of *Le Monde diplomatique*, economic and social Darwinism was driving society, causing excessive competition and consumption and forcing people to adapt to market conditions, at the risk of becoming social misfits and slowing the global economy.[28]

Anti-globalization protestors gained momentum in the 1990s. Much of their focus was on negative consequences of globalization, such as sweatshop conditions in poor countries, damage to the environment, and maldistribution of income.[29] Protesters denounced policies of the WTO, the IMF, and the World Bank that supposedly reflected an ideological obsession with neoliberal-ism and minimization of controls on transnational corporations. Many of these groups formed coalitions with labor, environmental, and peace activists and held massive demonstrations in cities around the world, capped by the violent "Battle of Seattle" at the WTO meetings in the spring of 1999. Even the 1989 pro-democracy protests in Beijing's Tiananmen Square and the 2011 Arab Spring can be interpreted as reactions to the imposition of globalization-oriented policies by authoritarian regimes. Major recessions in Mexico in 1994, Russia in 1998, and throughout much of Southeast and East Asia in 1997 and 1998 led some officials in developing countries to

question the merits of weakening regulations and encouraging massive capital flows across borders. Nevertheless, overall support for globalization among Western policy makers, business elites, and mainstream economists remained strong.

Liberal Critiques of Globalization

As we have emphasized in this chapter, economic liberal ideas have evolved over time as new scholars grapple with new problems. Many economic liberals who are inspired by Keynes disagree with elements of neoliberalism. While generally supporting globalization, they started to address the potential problems resulting from rapidly growing flows of goods and money across borders. By the mid-2000s, these critics, whom we label as "heterodox economic liberals" to distinguish them from neoliberalism-supporting "orthodox economic liberals," argued that globalization should be managed better. For example, Joseph Stiglitz, the former chief economist of the World Bank and Nobel Prize winner in Economics, criticizes IMF policies for making it difficult for many developing nations to get out of debt and benefit from globalization.[30] Economist Dani Rodrik points out that unchecked economic integration and free trade can threaten democratic politics. Markets, he argues, have to be "embedded in non-market institutions in order to work well."[31] They will not be viewed as legitimate unless they reflect individual countries' national values, social understandings, and political realities.

While arguing that open markets and technological change were bringing unprecedented opportunities to middle classes in China and India, Thomas Friedman acknowledged that globalization would generate opposition if it widened the rich–poor gap. In his 2008 book *Hot, Flat and Crowded*, he also discusses globalization's costs to the environment, including loss of biodiversity, climate change, and energy shortages. Sounding more like a mercantilist, he suggests that governments need to create incentives for technological innovation leading to widespread renewable energy.[32] In fact, in a chapter called "China for a Day (But Not for Two)," he muses that the United States should have a day of authoritarian government to force the country to adopt good energy policies and energy efficiency standards—and then revert back to democracy and free-market capitalism!

Another scholar who recognizes unsustainable consequences of global neoliberalism is David Colander, an economist at Middlebury College. He argues that in a global economy, the operation of what economists call the "law of one price" means that wages and prices in the world *in the long run* will become more equalized as technology and capital spread more production to other countries. As a result, the United States will gain less and less from trade, wages will inevitably go down, and growth will decline as the United States loses its comparative advantage in most industries. Moreover, Colander believes that trade and outsourcing—which have benefited the majority *in the short run*—will soon cause the United States "to enter into a period of long-run relative structural decline, which will be marked by economic malaise and a continued loss of good jobs."[33]

THE GLOBAL FINANCIAL CRISIS: A STAKE IN THE HEART OR JUST A SCRATCH?

The deep global recession in 2008 and 2009 seemed to shake the faith of even some of the most ardent proponents of unfettered capitalism. Before the crisis, Alan Greenspan, the Chairman of the U.S. Federal Reserve, regularly assured Congress that financial markets were relatively self-regulating and that rational, profit-maximizing financial actors would take all necessary precautions to ensure that excessive risk-taking and insufficient due diligence (regarding mortgage lending) would not be tolerated (although in 1996 he had famously cautioned about "irrational exuberance" in the stock market). In contrast, in testimony before Congress in October 2008, the clearly shaken former Chairman admitted that his faith in the self-regulating nature of financial markets had been misplaced—that "those of us who have looked to the self-interest of lending institutions to protect shareholders' equity, myself included, are in a state of shocked disbelief."[34] Greenspan blamed his state of incredulity on a "flaw in the [economic] model" "that defines how the world works."

The global financial crisis that started in 2007 brought to a head differences of opinion between orthodox and heterodox economic liberals about globalization, the causes of the crisis, and how best to respond to it. The crisis produced the most severe economic collapse since the Great Depression, convincing a number of policy makers that neither more globalization nor incremental, piecemeal reforms to globalization were enough to resolve contradictions that neoliberalism had created. This section focuses on the ideological debate between neoliberals and heterodox liberals, and not the specifics of the financial crisis itself. Before reading this section, instructors and students may want to read the more detailed coverage of the crisis in Chapter 8.

Biases in Free-Market Theories

As noted earlier, Keynes was adamant that markets are prone to failure, with the Great Depression being a prime example of that reality. Since his time, many governments became better at dealing with recessions that were considered a normal part of the business cycle. Using a variety of fiscal and monetary tools, they could tinker with supply and demand to right the economy through choppy waters.

In contrast, Milton Friedman and other economists associated with neoliberalism's Chicago School emphasized that the nation's money supply was the key to inflation and that the market is a self-correcting mechanism. A companion theory, the "Efficient Market Hypothesis," claimed that "at every moment, *shares price themselves* in the market through attracting the input of all information relevant to their value."[35] The implication of this theory was that policy makers should not worry about speculative bubbles or excessive risk-taking by big market actors because an efficient market with rational investors would tend to make these problems unlikely. And the general bias among economists in American

universities has been toward an acceptance of rational-choice assumptions and a belief in the benefits of free trade and free markets.[36]

Policies based on these neoliberal outlooks seemed to work for some time in the developed countries. The period from the early 1990s to 2007 was dubbed "The Great Moderation" because there was low inflation, low economic volatility, and stable growth in advanced industrialized countries. However, after the crisis *The Economist*, an economic liberal magazine, accused economists of being "seduced" by models that assume equilibrium in markets when in fact (as Keynes had maintained) many markets exhibit uncertainties (or disequilibrium).[37] The models encourage the mistaken belief that markets can carefully manage risk. According to *The Economist*, macroeconomists in academia and within central banks have been too preoccupied with fighting inflation and too cavalier about recurring asset bubbles in markets. Heterodox economic liberals also argued that free-market theorists have underestimated distortions in markets, overestimated markets' ability to self-adjust, and failed to account for the long-term problems resulting from markets' short-term incentives.

Despite heterodox criticisms, neoliberal ideas remained popular, especially among elites. Why? Part of the reason may be that free-market models have focused on economic growth instead of relative equality of income distribution. Ironically, the *promise* of greater wealth, faster growth, better jobs, and cheaper prices has been easier for the public to buy into than the alternatives of higher taxes for more social programs, slower growth for environmental sustainability, and collective sacrifice today to benefit future generations.

Moreover, the wealthy, who dominate the media and fund political parties and think tanks throughout the industrialized democracies, heavily promote laissez-faire policies. Simon Johnson, a former Chief Economist for the IMF, labels the private firms and actors who call the shots in Washington a "financial oligarchy"—an interconnected group of politically powerful people who move back and forth between Wall Street and Washington (and some university offices), "amassing a kind of cultural capital—a belief" that "large financial institutions and free-flowing capital markets were crucial to America's position in the world."[38] Chrystia Freeland, a former global editor at Reuters who became Canada's Foreign Minister in 2017, describes the same group and its global counterparts as a "plutocracy"—a class of super-rich oligarchs benefitting from tax breaks, government subsidies, and taxpayer-financed bailouts.[39]

We Are All Keynesians Now

Despite the financial crisis, orthodox economic liberals prefer to keep the main laissez-faire characteristics of the free market, subject to a few more reforms. They propose to:

- Limit government support for banks, infrastructure projects, and social welfare programs;
- Decrease regulation of the economy;
- Cut taxes of the wealthy and middle class to stimulate economic growth; and

- Foster *more* globalization, which is good for the United States and the world.

Many orthodox liberals blame the government, not banks, for the crisis. They claim that the Federal Reserve created the housing bubble beginning in 2001 by decreasing the cost of borrowing through interest rates. This put more money into the hands of homebuyers who could not afford payments in the long run. Orthodox liberals also argue that the crisis was an exceptional event in the history of capitalism, one that occurs very infrequently—due more to flaws in human nature than flaws in capitalism itself. They believe that governments need to cut budget deficits by imposing austerity, with the goal of reducing the trade deficit and increasing national savings. They fear that big stimulus spending by governments will generate inflation and more debt that future generations will have to pay off (by consuming less).

More broadly, orthodox liberals support what IPE scholars call the "new constitutionalism," which entails removing some sensitive economic issues from the realm of politics and placing their governance in the hands of independent bodies and the private sector. Once the rules are set for governing these issues, they become difficult for governments to change. For example, removing control over monetary policy from the executive or the legislature and lodging it in an independent central bank has meant that central banks tend to focus on keeping inflation low and prioritizing the needs of investors rather than implement Keynesian policies that often benefit workers. Similarly, the WTO is the institutional home of rules on trade and intellectual property; once states negotiated these technical rules in the GATT and TRIPS agreements, they are hard to change, and they make it hard for WTO members to reverse their free-trade obligations. Liberals like this because it locks in an open, rules-based, liberal world order. They believe that this "constitutionalization" is beneficial because it creates stable expectations for market actors and forces governments to stick to policies with long-term benefits rather than cave in to short-term political pressures.

In contrast, heterodox economic liberals gained a greater voice in public debates after the financial crisis. They propose that the state should:

- Spend more to grow the economy and create jobs, without worrying too much about inflation;
- Invest more in renewable energy, infrastructure, education, and health care;
- Break up big banks and impose tougher regulations on them; and
- Better manage globalization, but without stopping it.

Drawing on Keynes, heterodox liberals want a strong state, but not one that stifles the profit motive, economic freedom, and individual liberty. They are *not* opposed to globalization per se, but they would like to redistribute more wealth to the masses in industrialized nations and poor people in developing nations. They recognize the need to reform institutions like the World Bank, the IMF, and the WTO to get away from a "one-size-fits-all mentality" of how economies should be run. Related to this is a new emphasis on creating "policy space" for developing countries (at least in the short run) to be more

protectionist, restrict capital flows somewhat, and have more lax rules on intellectual property rights. They emphasize that developed countries should stop subsidizing their own industries, drop their remaining protectionist barriers to key LDC exports like textiles and agricultural goods, and accept more immigrants from poorer countries.

Many heterodox economic liberals prefer the kind of state–market relationship found in social democracies in Western Europe (see Box 2.2). For example, Nordic countries have high openness to the international economy (measured by the ratio of trade to GDP) and high public expenditures on social programs (measured by the ratio of spending to GDP), demonstrating that globalization and big government are compatible. Heterodox liberals also want to maintain different models of national capitalism within a broader global free-market economy, instead of trying to harmonize all major regulations across developed countries. When it comes to designing global institutions and rules, Dani Rodrik stresses the need for maintaining "escape clauses" and "opt-outs" so that individual countries can benefit from globalization in ways that are most consistent with their political realities, cultural needs, and resource constraints.[40]

ORDOLIBERALISM AND THE SOCIAL MARKET ECONOMY[a]

By the 1920s, economic liberalism in Europe, particularly in Germany's post-World War I Weimar Republic, had come to be associated with economic chaos, political corruption, and the exploitation of the working class.[b] In response to this perception and to Hitler's consequent rise to power, a small group of academics at Freiburg University developed a new conception of liberalism they called ordoliberalism. Walter Eucken (1891–1950), Franz Böhm (1895–1977), and Hans Grossman-Doerth (1894–1944) founded this school of thought. Ordoliberals believe that the failings of liberalism resulted from the failure of nineteenth- and twentieth-century laissez-faire policy makers to appreciate Adam Smith's insight that the market is embedded in legal and political systems.

Ordoliberal thought reflects the humanist values of classical liberalism, including the protection of human dignity and personal freedom. Ordoliberals believe that private decision making should guide resource allocation, that competition is the source of economic wellbeing, and that economic and political freedom are inextricable. Like classical liberals, they also believe that individuals must be protected from excessive state power and that political power should be dispersed through democratic processes that maximize participation in public decision making. They want to prevent special privileges and monopolies that rig markets in favor of dominant firms.

Ordoliberals do *not* believe that markets are naturally self-regulating or that deregulation is sensible policy. Instead, they stress that the state must establish and enforce appropriate rules in property law, contract law, trade law, and competition policy to govern the market process. With such a framework in place, the efforts of powerful firms to subvert the market process (via price controls, import restrictions, subsidies, restrictive licenses, etc.) will be deemed "unconstitutional." Politicians will be in a strong position to resist the special pleadings of powerful interest groups. A privilege-free economy that supports liberal values will be the highly desirable result.

Ordoliberalism does have an inherent ethical stance. Within an appropriate legal and political framework, market outcomes will likely be nondiscriminatory, privilege-free, and just.[c] Ordoliberals recognize, however, that some income redistribution will likely be called for, given the limited productivity of some individuals—often due to circumstances beyond their control.

Other German intellectuals, principally Alfred Müller-Armack (1901–1978), accepted key ordoliberal principles but argued that supplemental "social" policies are necessary to ensure that market outcomes will indeed be consistent with a "good" society. Müller-Armack is credited with developing the basis of the "social" market

economy that characterizes many modern European states.[d]

Ordoliberal thought has had a profound influence on economic and political policy in the European Union. Current European competition policy and enforcement of antitrust regulations clearly incorporate ordoliberal principles. By maintaining open markets, European competition authorities hope to foster economic freedom in the form of freedom of entry, thereby enhancing economic opportunity, promoting competition, and diffusing economic and political power.

Ordoliberal ideals have strongly shaped German policies toward the European Union and the Eurozone crisis. The belief in "sound money" has translated into an emphasis in the European Central Bank on controlling inflation rather than reducing unemployment and a German insistence that EU members be constitutionally bound to strictly control government budget deficits. In addition, a strong emphasis on personal responsibility (or liability) has made Germany reluctant to bail out banks or states that have engaged in risky behavior or reckless borrowing.[e] When it has accepted bailouts for Eurozone countries, Germany has insisted that they abide by strict conditions and undertake painful reforms.

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[a]Ross Singleton is the primary author of this text box.

[b]The discussion of ordoliberalism in this box is based largely on David J. Gerber, "Constitutionalizing the Economy: German Neo-Liberalism, Competition Policy and the 'New' Europe," *The American Journal of Comparative Law* 42 (1994), pp. 25–88.

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[d]Ibid.

[e]Mathias Siems and Gerhard Schnyder, "Ordoliberal Lessons for Economic Stability: Different Kinds of Regulation, Not More Regulation," *Governance* 27:3 (July 2014): 382, 385.

CONCLUSION

This chapter has explained how the ideas and values associated with the economic liberal perspective have evolved to reflect major political, economic, and social developments. Political economists Smith, Ricardo, Mill, Keynes, Hayek, Friedman, and others have debated the relationship of the state to society as capitalism has spread over large parts of the world, profoundly shaping global production and distribution.

During the Great Depression, a split emerged between Keynesians who supported a positive role for the state in the economy and orthodox liberals who saw the state's role in the economy as decidedly negative. In the 1980s, the chasm widened even more. The Reagan and Thatcher administrations implemented neoliberal policies, emphasizing economic growth alongside cuts in domestic welfare programs. Globalization and the current financial crisis have led to criticisms of neoliberal faith in markets. Many heterodox liberals maintain that some state intervention serves the public interest, especially when it protects social groups and countries from the negative effects of the seemingly Darwinian global economy. Orthodox liberals believe that austerity will lay a foundation for sustainable recovery.

Both orthodox and heterodox liberals ultimately believe that capitalism is a desirable system to maintain, despite the differences in how they propose to reform globalization and tackle the problems arising from trade and inequality. In that sense, they both place their faith in the ability of markets to promote the interests of most people in the world.

KEY TERMS

economic liberalism 26
rent-seeking 30
Corn Laws 31
positive-sum game 31
zero-sum game 31
Keynesianism 33
paradox of thrift 34
Keynesian compromise 35
embedded liberalism 35
hegemonic stability theory 36
public goods 36
neoliberalism 37
heterodox economic liberals 40
orthodox economic liberals 40
new constitutionalism 43
ordoliberalism 44

DISCUSSION QUESTIONS

1. What roles do self-interest, competition, and the state play in Adam Smith's views of the market?
2. Is Adam Smith the economic liberal many people assume he is?
3. Explain how the Corn Laws debate in nineteenth-century Britain illustrates the conflict between mercantilist and economic liberal views of international trade. Which side of the debate do you favor? Explain.
4. John Stuart Mill and John Maynard Keynes thought that government could play a positive role in correcting problems in the market. Discuss the specific types of "market failures" that Mill and Keynes perceived and the types of government actions they advocated.
5. Given the critiques of globalization, what kinds of changes to economic liberal policies would you recommend?
6. Compare and contrast orthodox and heterodox liberals in terms of values, ideas, and policies. Which do you favor?
7. Based on what you know about the 2007–2008 financial crisis, do you agree with the suggestion that it seriously undermined economic liberal ideas and policies?

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CHAPTER
3
Wealth and Power: The Mercantilist Perspective



Trade protectionism puts the U.S. behind a different kind of wall.

Source: Shutterstock

The United States desperately needs politicians with the courage to swim against the tide of popular rhetoric and outline a bolder vision for the State's dynamic role in fostering the economic growth of the future.

Mariana Mazzucato[1]

How often have you heard people say that they believe in free trade, but still support *some* state intervention in the economy? Politically, it makes sense for the state to assist businesses in certain cases, such as when farmers are hit by an unexpected drought. But is there an equally compelling case for the government to compensate manufacturing workers whose jobs move to Mexico? This was the question in March 2016, when 14,000 employees at Carrier, a manufacturer of heating and air-conditioning systems, were notified suddenly that the company was moving production to Mexico, where wages were lower.[2] Workers were furious that they would have to find new jobs in the U.S. Rust Belt, a region where good-paying manufacturing jobs have been disappearing since the 1980s.

During the U.S. presidential election campaign in 2016, both Democratic Senator Bernie Sanders and Republican entrepreneur Donald Trump mentioned situations like this one, arguing that U.S. free-trade policy—which was once popular among voters and still enjoys some bipartisan support in Congress—hurts U.S. workers. Trump called for high tariffs on imported goods made by U.S.-owned businesses in Mexico. Sanders blamed

corporate elites for moving jobs to developing countries under pressure from profit-hungry investors. Contrary to those who argue that the state should not intervene in the economy, both Sanders and Trump insisted that the U.S. government *should* do more to protect U.S. workers who had lost their jobs.

Throughout the world, farmers, car manufacturers, steel producers, start-ups, and other private enterprises often receive some type of state economic support. Usually it does not bother us unless we notice that inefficient businesses are supported by state subsidies or other protectionist measures. We tend to believe that it is appropriate for the government to help displaced workers, support businesses to become more internationally competitive, or protect companies that are vital to national security.

This chapter looks at the IPE perspective of mercantilism, which explains the compulsion of nation-states to use power to protect themselves and generate wealth for their citizens. Although neoliberal ideas replaced mercantilist ideas in popularity after the 1970s, mercantilism has made a comeback in recent years. Governments and populist-nationalist movements that criticize globalization often draw on mercantilist thought. Mercantilism emphasizes using the economy to help protect the nation-state from any number of real and imagined threats. As we discuss in Chapter 9, realism complements mercantilism, but emphasizes political and military instruments to achieve state security.

Classical mercantilism (from the sixteenth until the nineteenth centuries) focused on state efforts to generate trade surpluses by promoting exports and limiting imports. It was widely believed that trade surpluses strengthen a nation's economy, thereby contributing to its security and protecting certain public and private groups within society. Because no state could count on other states to guarantee its own territorial security, each state had to look to its own military power for protection, supported by its economy and wealth. State security and other political interests largely determined a country's economic policies. These harsh conditions imposed on states a potentially destabilizing zero-sum outlook whereby absolute gains by one state were interpreted as absolute losses for other states.

Because protectionist policies played a major role in escalating interstate tensions and violence that culminated in World War I and World War II, governments after 1945 placed a premium on defending the state and national firms *without* resorting to force. Beginning in the 1970s, scholars used the term "neomercantilism" to describe many defensive economic policies that states use to safeguard their societies in an interdependent and intensely competitive international political economy.

This chapter chronologically covers the evolution of ideas about mercantilism in the international political economy from the sixteenth century until today. We then explore why developed and developing nations have increasingly used neomercantilist policies in the face of globalization. We also examine how states are using a host of sophisticated technologies to defend their economies in an era when it has become increasingly difficult to determine whether or not competitors intend to physically harm one's state and its businesses.

The chapter has five theses:

- The history of mercantilism demonstrates that states have always been compelled to regulate markets, whether in pursuit of state security, to counteract some of the undesirable consequences of market operations, or to help markets grow in a stable manner.
- States promote open markets and free trade to the extent that these liberal economic policies further the economic interests of the state and dominant corporations.
- Paradoxically, because globalization has entrenched and exacerbated the insecurities of states and many social groups, it has *increased* the tendency of states to implement protectionist policies.
- In response to a growing number of international trade, finance, and industrial problems, states are likely to adopt a "managed" *mix* of both neoliberal and protectionist policies.
- Complex linkages between major international problems are making it more difficult for states to resolve disputes through intricate negotiations.

MERCANTILISM AS HISTORY AND PHILOSOPHY

For both mercantilists and realists, the nation-state is the primary unit of analysis. A nation is a collection of people who, on the basis of ethnic background, language, and history, define themselves as members of an extended political community.[3] The state is the legal identity of the nation, monopolizing the means of physical force in society and exercising sovereignty within a given territory.[4] Around the fifteenth century, the rulers of small European fiefdoms decided to consolidate their territories into larger domains in order to better protect themselves against enemies.[5] These new domains would become nation-states —France first, soon to be followed by England, Holland, Spain and Sweden. Germany and Italy would not be consolidated into national entities until later in the nineteenth century.

The economic historian Charles Tilly emphasizes that the constant need to prepare for war was the primary factor that motivated monarchs and other officials to organize their societies and to adopt measures that would help secure the nation.[6] In nation-states all across Europe, governments pushed harder and harder to extract income and resources from towns and cities to finance the state's growing demand for military security. Warrior-kings created bureaucratic agencies that performed a variety of functions related to keeping a budget, using money, and collecting taxes.[7] Many kings gave absolute property rights to nobles in return for their support in staffing the king's armies and collecting taxes.

Maintaining and expanding strong armies and navies was every nation-state's highest priority, but also very expensive. Thus, accumulating wealth and manipulating the economy and trade policy to maximize revenue became a key security strategy for any state. Mercantilism represented a set of ideal policies for achieving this. For example, the British Tudor monarch Henry VII tried to maximize the profitability of trade by taxing all imported wool products and subsidizing British wool exporters. His aim was to capture control of the woolen industry from Holland. For the next 100 years, England used these tactics to compete with and intentionally ruin woolen manufacturing in Belgium and the Netherlands.[8]

Mercantilist efforts dramatically altered the economic hierarchy of production in many societies. Whereas agriculture had constituted the dominant source of income for state treasuries, it was no longer enough. The state increasingly looked to merchants and their trade as a larger source of tax revenue. To promote economic growth, state bureaucracies connected small regional markets by promoting infrastructural development and establishing common currencies and weights. Along the way merchants acquired more property rights and rose to a higher social position.

Mercantilism and Colonialism

To many historians, mercantilism is synonymous with the first wave of exploration and imperialism from 1648 to the end of the Napoleonic Wars in 1815. Monarchs sent adventurers and conquerors on searches for gold and silver bullion to fill state coffers. They

also established colonies as a means to control trade and generate wealth and power. Colonies served as exclusive markets for the goods of the mother country and as sources of raw materials and cheap labor. To promote the development of their colonial empires, states often subsidized import and export merchants, who in turn favored a strong state that would protect their interests. Many states gave favored merchants monopolies over their industries. Dutch and British rulers also created charter companies and supported new manufacturing technologies to boost production in urban centers.

Economic historians Kenneth Pomeranz and Steven Topik have studied how the colonial powers used these mercantilist policies to move up the international economic hierarchy.[9] The dominant powers regularly used violence and occupation to harness advantages for their own traders and chartered companies. Slavery was integral to their strategy of building cheap labor forces to extract raw materials such as cotton, sugar, and tobacco from the New World. To help balance its trade deficit with India, Great Britain forced China to open itself to opium exports from India. European powers competed with each other to control access to raw materials like cocoa, rubber, tea and coffee. They also deliberately spread production of these commodities to areas under their control in order to tax them. To gain more territory and commercial advantages, they also committed genocide against indigenous peoples in the Americas and the Belgian Congo. For Pomeranz and Topik the spread of the free market via commerce depended on a "historic foundation of violence" where "bloody hands and the invisible hand often worked in concert; in fact, they were often attached to the same body."[10]

Even while pursuing economic growth through trade and colonialism, England's Prime Minister Robert Walpole (1721–1742) continued efforts to promote British demand for British-made goods such as wool in order to boost state revenue. The British wool and textile industries increased the profitability of land and generated taxable consumer goods. To protect British manufacturing interests, the government banned competitive imports into Great Britain from its colonies, which destroyed Irish mills and delayed the emergence of the U.S. textile industry. All of these efforts were directed at enhancing state wealth and power in an economically competitive and politically hostile international environment. Without these protectionist measures, Great Britain would not have been able to support its growing imperial power.

The Economic Liberal Challenge to Mercantilism

Between the 1840s and 1870s, economic liberal ideas attributed to Adam Smith and David Ricardo became more popular in Great Britain, gradually replacing mercantilism as this European power's core political-economic philosophy. Many policy makers accepted the idea that markets were self-adjusting and that the state should limit its interventions in the market. What accounts for the rise of these economic liberal ideas that challenged mercantilism?

Adam Smith's *The Wealth of Nations*, published in 1776, attacked mercantilism for causing production inefficiencies by restricting economic competition. But it wasn't until

the end of the Napoleonic Wars in 1815, when Great Britain had become the most efficient producer of manufactured goods, that officials and influential thinkers began to press for free trade. England finally adopted a free-trade policy in 1840, but did not completely eliminate its trade tariffs until 1860.

Contrary to conventional wisdom, Adam Smith was not a doctrinaire defender of free enterprise. He did champion individual (consumer) liberty and worried that state interventions could make an economy less productive, but he also had a protectionist side. He supported certain taxes, tariffs, and interventionist laws. Both Smith and Ricardo viewed free trade as a policy that, ideally, would benefit British manufacturers by *forcing* them to make their goods more competitive and thus more profitable internationally. Ricardo accepted exceptions to free trade "within narrow limits" until they were no longer necessary.

Clearly, then, free trade was *not* an ideological end in itself. By the late 1870s, in the face of rising European and American competition, wealthy British financiers and manufacturers actually joined working class groups in a movement *against* open market policies and in favor of trade protection. As more citizens gained the right to vote, the state came under pressure to provide them with more benefits. Finally, by the end of the century, economic nationalism (a people's sense of economic loyalty to their nation-state) became even more entrenched in international relations, which in turn helped generate a second wave of imperialism when Germany, Japan, Italy, and the United States began acquiring their own colonies.

Overlooked U.S. Protectionism

In the nineteenth century, emerging powers such as the United States and the German principalities protected themselves from what they perceived as Britain's aggressive economic liberal policies. Two important contributors to mercantilist thought at the time were the American Alexander Hamilton (1755–1804) and the German Friedrich List (1789–1846). In his *Report on the Subject of Manufactures* to the first U.S. Congress, Hamilton argued—in opposition to the ideas of Thomas Jefferson—that free-trade policies were not in the best interest of a young nation. Unless the U.S. government imposed taxes on imports, America's infant industries could never compete with Britain's mature industries in manufacturing all the goods and services that Americans demanded.[11] And unless the government subsidized American exports (and thus gained a trade surplus), the United States could not raise enough revenue to finance investments in infrastructure and the military. Hamilton also favored export subsidies because they offset subsidies that foreign states granted to their own domestic companies.

The nineteenth-century German political economist Friedrich List was an even more vigorous proponent of mercantilist policies. Exiled from his home—ironically, for his radical free-trade views—List came to the United States in 1825 and witnessed firsthand the results of Hamilton's economic nationalist policies: The United States was building up its independence and security. In "The Theory of the Powers of Production and the Theory of Values," List argued that "the power of producing [is] infinitely more important than

wealth itself."[12] In other words, it is more important to invest in the future ability to produce than to consume the fruits of today's prosperity.

Free-trade proponents, including Thomas Jefferson, believed that the United States could raise money quickly by specializing in agriculture, taking advantage of the new territory's abundant natural resources. But for List, the production of a wide variety of goods, along with investments in education and the development of new technology, was more important than investment in agriculture alone. List wrote that manufacturing and other occupations "develop and bring into action an incomparably greater variety and higher type of mental qualities and abilities than agriculture" and that "manufactures are at once the offspring, and at the same time the supporters and the nurses, of science and the arts."[13]

Hamilton and List shared a spirit of patriotic economic nationalism—a reaction to Great Britain's economic liberal ideas and free-trade policies. List argued that because Britain had more advanced technology and more efficient labor than the rest of Europe, its goods were more attractive to Europeans than locally produced goods. List also argued that in a "cosmopolitan" world there could be no free trade until states could compete with one another on an equal footing. He recommended that until the United States and Europe had "caught up" with Great Britain, they should protect their infant industries, gradually climbing to a level playing field with the British. Finally, according to Cambridge economist Ha-Joon Chang, to the extent that Great Britain fought against mercantilist policies in other countries, it was "kicking away the ladder" for those countries, opposing their use of the same policies Great Britain itself had used to achieve its wealth and power.[14]

Political scientist Mark A. Martinez also notes that markets and trade in the United States were never all that free.[15] During the War of 1812, Congress doubled tariffs on all goods, and high tariffs remained integral to U.S. economic development until World War II. The U.S. government practiced mercantilism when it expanded the nation's territory between 1800 and 1848 through a series of land treaties, wars, and negotiations. It brutally cleared new territories of native Indian tribes and incorporated the Louisiana Territory, Florida, Oregon, Texas, and the Mexican concession into the young republic. Later it encouraged explorers and settlers to cultivate these new lands to fulfill their Manifest Destiny. The Homestead Act of 1862 granted 160 acres to anyone who would clear and farm the land for five years. The federal government later sponsored the building of railroads and highways, a banking system, land-grant colleges, and many other infrastructure projects to expand economic prosperity.

By 1925 the United States was one of the fastest-growing economies in the world. Other countries—like Germany, Austria, Sweden and France—were also growing behind tariff walls. At the onset of the Great Depression, the Smoot-Hawley Tariff Act raised average U.S. tariffs to a record high of 48 percent. When many other nations adopted similar policies to protect their own industries, it was inevitable that conflicting protectionist policies would lead to global trade stagnation. It is easy to see why many economists blame

these high tariffs for contributing to the Great Depression (and, as a consequence, to World War II).

Keynes, the Great Depression, and the Postwar Order

In 1929 many people blamed banks and speculators for the stock market crash and the Great Depression (1929–1941), which subsequently increased unemployment and poverty in many parts of the world. Over the next decade many states erected high tariff barriers, boycotted other states' exports, and even went to war, partially in response to what were considered other states' aggressive mercantilist trade policies. Many lost faith in market capitalism, which led to increasing support for fascism in Europe and for revolutionary movements in Europe, Latin America, and Asia.

Recall from Chapter 2 that in the 1930s the ideas of John Maynard Keynes became popular because of pressure on the state to respond to the needs of more voters with higher expectations. This rendered laissez-faire ideology no longer politically acceptable. Keynes believed not only that markets sometimes fail, but that recessions and depressions can last a long time. To restore confidence in the capitalist system and weaken popular support for authoritarian leaders, he recommended that state officials deal with the negative social effects of the depression head-on and stimulate employment by injecting money into the economy.

President Franklin Roosevelt's New Deal reflected Keynesian ideas. Government-sponsored welfare programs that helped the United States recover from economic depression included: farm support measures that guaranteed high prices for major crops; a bank insurance policy; and the Works Progress Administration (WPA) and the Civilian Conservation Corps (CCC), which employed many Americans. After the war Congress passed the Employment Act of 1946, which made the federal government responsible for promoting "maximum employment" and "free competitive enterprise." The G.I. Bill also made education and home mortgages more affordable for millions of returning veterans.

Keynes's idea of a strong welfare state also gained traction in Europe. After the war, Britain's Labour Party developed a National Health Service to provide lifelong free healthcare for all and implemented plans for the New Towns Act to develop low-cost housing for the poor. The British government also nationalized many of its biggest industries to ensure high employment— something Keynes considered essential to a stable, functioning economy.

Despite its popularity, Keynesianism did not mean the end of "free market" ideology and policies. At the end of World War II, forty-four victorious Allied states gathered at the Bretton Woods conference to negotiate a new system of international economic cooperation. Keynes's ideas shaped the values, design, and role of the three Bretton Woods institutions that emerged from the conference: the General Agreement on Tariffs and Trade (GATT), the International Monetary Fund (IMF), and the World Bank. In what came to be known as the "Keynesian compromise," the major Western powers encouraged economic recovery in their post-war economies by employing various mercantilist policies that promoted employment and enhanced the purchasing power of the working class.

However, officials were cautious about pushing Europe and Japan to open up too quickly to international competition, lest such a move jeopardize their recovery and allow communism to gain traction in their countries. Significant reductions in trade-related protectionist measures would have to wait until Europe and Japan recovered enough to be able to compete on a "level playing field" with the United States. In addition, the IMF allowed governments to engage in currency discrimination until 1958. "Capital controls" that restricted the movement of money in and out of countries would survive into the early 1970s.

The Bretton Woods system's economic objectives complemented the political and military objectives of the United States and its allies. Western industrialized nations and Japan sought to preserve capitalism within their bloc while also "containing" international communism and restricting trade with Soviet bloc countries. There would also be no western economic liberal order without military power to back it up. The United States provided the preponderance of strategic military resources (including atomic bombs) to deter the Soviet Union from attacking Western Europe or Japan. The United States also provided other collective goods to its allies to earn their support for U.S. Cold War objectives. Marshall Plan financial assistance, food aid, and reduced import tariffs on Europe's exports helped U.S. allies' economies grow.

THE ENTRENCHMENT OF NEOMERCANTILISM IN THE 1970S AND 1980S

A significant shift in the international security structure in the 1970s and 1980s caused several major changes in the international political economy:

- More use of neomercantilist tools to protect states and international businesses from a variety of economic threats;
- Increased political saliency of international economic interdependence and dependence on oil and natural resources;
- Greater importance of international finance and trade agreements, especially to developing nations; and
- Increased investment in and attention to technological and information innovations.

After withdrawing most U.S forces from Vietnam in 1973, the Nixon administration attempted to reconfigure the bipolar (East–West) international security structure into a multipolar pentagonal balance of power system (see Chapter 9). The United States recognized the People's Republic of China (PRC) as one of the five major powers in a new international security structure where economic power took on as much importance as military power. The United States and the Soviet Union entered into a détente or period of "peaceful coexistence," putting less emphasis on major security issues. This restructuring of the security structure provided new investment opportunities for multinational corporations and opened the door to more trade and cultural exchanges between the West and the Soviet bloc countries.

Another major systemic transformation in 1973 gave developing nations a much stronger role in the international political economy. Members of the Organization of Petroleum Exporting Countries (OPEC) raised the price of oil dramatically, embargoed oil shipments to the United States and the Netherlands, and reduced oil shipments to the rest of the world by 25 percent. Prices hikes—which OPEC repeated in 1979—plunged the world into a prolonged recession.

This crisis gave OPEC great political and economic leverage over the West. All oil-importing states were more vulnerable to external economic threats than they had imaged themselves to be. The shift in control over oil prices and production levels suddenly became a major economic and security problem for NATO alliance members (who split over how to manage the crisis). The United States and its NATO allies considered but then ruled out a military response to OPEC's actions because they did not want to risk starting a war with the Soviet Union or a broader conflict in the Middle East.

With a new sense of power related to their control over a scarce resource (oil), the developing countries formed the "Group of 77" in the United Nations and demanded a New International Economic Order (NIEO). Among other things, they sought to gain more control over their own resources, end Northern trade practices that discriminated

again Southern states' agricultural exports, and provide more aid to oil-importing states. However, the United States, Europe, and Japan resisted changing the Bretton Woods system, and few of the NIEO reforms were ever implemented internationally.

By the end of the 1970s, increased interdependence (interconnections) between nations had left many of them feeling insecure and more economically vulnerable to the policies of natural resource exporters and the actions of multinational corporations. To reduce the United States' dependence on OPEC oil, President Jimmy Carter initiated a defensive-mercantilist campaign that included the creation of a "strategic petroleum reserve" and the development of the North Slope oil fields in Alaska. Congress also imposed fuel mileage requirements on automobile manufacturers to push them to design more fuel-efficient cars. Despite efforts like these, the oil-importing countries had little choice but to adjust their economies to the high price of oil while trying to decrease oil consumption to protect economic growth and jobs.

In the face of the declining utility of military weapons and violent conflict for advancing national economic interests, developed countries increasingly turned to neomercantilist finance, trade, and development policies to defend their economies and enhance the competitiveness of their domestic firms. Neomercantilism included efforts to generate economic growth, control the business cycle, and eliminate unemployment. Many governments increased spending on various social programs, imposed new regulations on industries, introduced some capital controls, and manipulated interest rates. Also, state industrial policies included subsidies for state-owned corporations and funding for research and development in the private sector. Some nations employed export subsidies to lower the price of goods, making them more attractive to importers overseas.

These neomercantilist policies were *intended* to reduce the vulnerability of states and international businesses to international competition without undermining a commitment to freer trade under the GATT. However, many of the sophisticated measures that states adopted caused tensions with trade partners. For example, the United States and the European Community countries heavily subsidized farm production and then used export subsidies to reduce their commodity surpluses and grab larger shares of export markets. Some states employed nontariff barriers (NTBs) such as complex health and safety standards, licensing and labeling requirements, and domestic content requirements to limit imports of certain commodities and manufactured goods. Similarly, some countries imposed import quotas to control the quantity of a particular product that could be imported. To this day the United States and the European Union still apply import quotas on many agricultural items to help their domestic producers compete with foreign producers. Yet another way to limit imports was through a Voluntary Export Agreement (VEA) whereby an exporter "voluntarily" complies with an importer's "request" that it limit exports, for fear that the importer might impose a more costly form of protection on the exporter's goods.

Japan Inc. and Reagan's Neomercantilism

The economic success of Japan also boosted use of neomercantilist policies and instruments

in the 1970s and 1980s. After World War II, Japan adopted a model of capitalism in which the state intervened proactively in the economy. The Ministry of International Trade and Industry (MITI) cooperated with business leaders and Liberal Democratic Party (LDP) members to carefully guide the development of many industries.[16] Selected companies received state and bank subsidies to make them more competitive with U.S. and European firms. During the post-war "economic miracle," Japanese companies also expanded their investment overseas.

Clyde Prestowitz argues that Japan did more than support its most competitive industries. Lacking a natural comparative advantage in the manufacture of certain products, it adopted a "strategic trade policy" to intentionally create competitive industries that could thrive in open international markets.[17] In addition, Robert Wade argues that Japan's "developmental state" strategy was later imitated by the Asian Tigers (South Korea, Hong Kong, Singapore, and Taiwan) and China.[18]

The increased use of neomercantilist policies became a major issue during the long Tokyo Round of GATT negotiations (1971–1978). The final agreement reduced tariff rates significantly and recommended that states limit the use of protectionist trade measures. Nevertheless, many Western states still felt pressure to limit imports and help domestic companies boost their exports.

As a reflection of greater interdependence, economic liberal ideas became more popular in the 1980s, setting the stage for a globalization campaign to integrate states into a global capitalist system. UK Prime Minister Margaret Thatcher and U.S. president Ronald Reagan reduced regulations on businesses, touted the benefits of free trade, and promoted democracy overseas. However, Reagan pragmatically employed trade embargoes against some countries and gave military aid to rebels called the Contras trying to overthrow the socialist Nicaraguan regime. To advance U.S. security interests, he also successfully pressured the IMF and World Bank to bail out countries such as Mexico and Brazil that experienced severe debt crises.

The United States also intervened indirectly in the economies of developing countries through IMF and World Bank Structural Adjustment Policies (SAPs) that required borrowers to implement neoliberal policies such as cutting spending on social programs. Many structuralists viewed SAPs as mechanisms for the United States, Europe, and Japan to increase their wealth and power in a growing capitalist empire. In many cases these neomercantilist policies made socioeconomic conditions worse in heavily indebted developing countries.

With globalization came greater political sensitivity to trade, which accounted for a growing proportion of GDP in many countries. The policies that states adopted in response to this sensitivity provoked disputes amongst trading partners. IPE scholar Robert Gilpin suggested that it is difficult for states to select the appropriate counter-responses in such disputes without knowing what other states' intentions are. He made a useful distinction between malevolent and benign mercantilism. The former is a more hostile version of economic warfare that nations employ to expand their territorial base or political influence at the expense of other nations. In contrast, benign mercantilism is more defensive in

nature, as "it attempts to protect the economy against untoward economic and political forces."[19] Of course, the problem is how to distinguish between the two in an environment where the difference seems to be a matter of degree rather than of kind.

For example, Reagan mixed economic liberal and mercantilist objectives at the start of the Uruguay Round of multilateral trade negotiations (1986–1994). One goal of the round was to "level the playing field" by cutting NTBs and other trade restrictions so that states could compete economically with one another following the same set of rules and policies. At the time, the United States and the European Community blamed their large trade deficits on Japan's aggressive export-led growth strategy and import restrictions. In its defense, Japan maintained that it sought only to strengthen its own national security through the use of benign neomer-cantilist industrial policies.

President Reagan threatened to punish Japan and Brazil for dumping their products on the market and using export subsidies to unfairly compete with the United States. U.S. officials pressured Japan and many of the newly emerging countries to lower their trade barriers and open their markets to more foreign (especially U.S.) investment. Washington and Tokyo had a series of trade disputes over items such as automobiles, rice, beef, and semiconductors. What one state regarded as a benign policy, another might interpret as malevolent behavior, especially when the policy of the first hurt "special interests" in the society of the second. And yet the United States often found itself limited in the amount of pressure it could put on its most important allies. For example, it needed Japan to invest in U.S. Treasury bonds and securities in order to help finance U.S. federal government spending. (Today, the United States depends heavily on China and Japan to purchase Treasury securities.)

NEOLIBERALISM, NEOMERCANTILISM, AND THE GLOBALIZATION CAMPAIGN

The end of the Cold War in 1990 led to an intensification of the globalization campaign and a tightening of connections between domestic and foreign policy issues. During the Clinton administration (1993–2001), many Western-headquartered corporations sought resources, markets, and cheap labor in places such as China and Southeast Asia. It was economically efficient and rational for companies to "outsource" production to Asia. Globalization complemented U.S. foreign policy objectives by integrating China and other developing countries into the global capitalist system and by increasing the likelihood that more countries would become democratic. By spreading the use of computers, the Internet, fiber optics, and other technologies of the digital revolution, globalization also contributed to advances in communications, travel, and consumer culture. At the same time, new technologies made it easier for countries and companies to engage in industrial espionage and theft of intellectual property.

There were still numerous trade disputes in the 1990s. An interesting case occurred in 1993 when the EU restricted imports of bananas from anywhere but British and French colonies in the Caribbean. The United States brought the case before a Dispute Settlement panel of the WTO in 1995 and 1997, which found that EU policies violated WTO rules by restraining imports of bananas from countries in Latin America where U.S.-owned multinational corporations dominated the banana sector. When the EU would not comply with the WTO finding, President Clinton imposed a WTO-authorized duty of 100 percent on imports of cashmere sweaters, cheese, wine, fruit, and toys from the EU. The dispute ended in 2009 when the EU agreed to gradually reduce tariffs on Latin American bananas.

The GATT Uruguay Round, which finally ended in 1994 and led to the creation of the World Trade Organization, produced some agreement on acceptable forms of retaliation against countries that were found to have violated WTO trade rules. However, this did not prevent a major dispute between the United States, the EU, and developing nations over genetically modified (GM) crops. In the 1990s the United States approved roughly 40 different GM crops for commercial use in food products. Advocates of GM crops in the World Health Organization, the UN Food and Agriculture Organization, and national science academies in China, the United Kingdom, and United States argued that GM crops were safe for human consumption, could increase global food production, and could help reduce use of toxic herbicides and insecticides.

Nevertheless, in 1998 the EU placed a moratorium on imports of GM crops and banned GM seeds and organisms from entering Europe. The EU argued that agriculture and food are intrinsic to European culture and that genetic modification corrupts the DNA of a crop, potentially undermining its quality and taste. Furthermore, there was no way to know what effects GM foods would have on human health over the long term. Likewise, the EU

protested that widespread adoption of GM crops would cause a loss of biodiversity. In support of the EU's policy, some African states let U.S. food aid rot in locked warehouses. The EU and most developing states are signatories of the 2000 Cartagena Protocol on Biosafety that allows countries to ban imports of genetically modified crops if there is not a scientific consensus that they cause no serious harm to the environment or people's health.

Supported by a number of Asian countries, U.S. agribusinesses and biotechnology firms argued that restrictions on GM crops limited consumer food choices and that there was no evidence that GM foods hurt consumers. The United States filed a formal complaint in the WTO seeking to overturn the EU's ban on genetically modified organisms. Furthermore, the United States argued that the EU ban was a form of trade protection that violated WTO agreements. American officials feared that EU restrictions would limit the growth of U.S. agricultural exports and reduce profits of American farmers and agribusinesses. In contrast, EU officials claimed that imports of GM grains would hurt both EU and African farmers by undermining local production.

Toward the end of the 1990s, globalization was reaching the apex of its popularity. Many developing countries wanted better terms of trade with the developed countries. They also expected to use subsidies and other export-enhancing measures to help their domestic companies compete better in the global economy. While many neoliberals proclaimed that globalization helped maximize economic efficiency, many neomercantilists (and structuralists as well) contended that globalization was *undermining* itself.[20] Just days before the 1999 WTO ministerial meeting in Seattle, President Clinton seemed to acknowledge that globalization was causing harm when he tempered his support for a free-trade agenda with a proposal to incorporate labor and environmental standards into future WTO agreements.

INSECURITY IN A WIRED WORLD

The "hyper-globalized" and "wired" international economy in the 2000s was transformed by high-speed telecommunications systems, high-frequency banking and trading, and the continued miniaturization of electronic goods and military weapons. These digital innovations have rendered state borders more porous and left countries more susceptible to external threats such as cyberattacks that were unimaginable only a decade earlier. The emergence of new, more subtle neomercantilist intimidations in this context has also made it harder to determine the intentions of states and assess the effects of their measures on other states' economic and national security.

By the early 2000s, cyber weapons were being used routinely, especially against military targets. The United States, China, and Russia built up the strongest cyber capabilities in the world; Great Britain, Germany, and France used their offensive cyber capabilities less frequently than the other Great Powers. States, terrorist groups, and criminal hackers used digital tools to steal valuable information from international banks, major corporations, and utility companies. Adam Segal points out that for many industrialized states, "economic and technological sophistication are … sources of vulnerability."[21] Therefore, governments have to coordinate policies with private companies in the telecommunications, information technology, banking, energy, and transportation sectors in order to protect the economy as a whole.

The 9/11 attacks on the World Trade Center in New York and the Pentagon in Washington, DC profoundly influenced government policies toward information technology in the 2000s. Soon after the attacks, the United States invested billions of dollars to build a giant "Military-Internet Complex" designed to protect the United States from terrorist attacks and protect the U.S. economy and global businesses.[22] Since 2001 there have been many cyberattacks on states and businesses around the world. For example, in June 2013 a group called Citadel planted malware on some five million personal computers and used an army of "botnets" to attack the computer servers of major banks around the world and steal an estimated $500 million from bank accounts. Microsoft worked with law enforcement in dozens of countries to help wipe out Citadel.[23] To be clear, like many other states, the United States itself has routinely carried out cyber missions to steal information from foreign businesses, disrupt criminal organizations, and harm the economies of specific rival states.

The advanced industrialized nations face the challenge of competing with one another in high-tech, knowledge-based industries while trying to stem the loss of manufacturing industries to emerging economies with abundant, low-cost labor. In contrast, many developing countries struggle to secure a place for themselves in the hyper-competitive international economy. They must work within ideological and political constraints imposed on them by major powers and neoliberal institutions like the WTO, the World Bank, and the IMF. And yet many have still continued to use tried-and-true

neomercantilist policies like quotas, tariffs, and plain old arm-twisting. As we discussed earlier in the chapter, many of today's advanced industrialized nations used to be very protectionist. In light of this history, developing nations point out that developed nations are hypocritical when they command emerging countries to "do as we say, not as we did (and sometimes still do)!"

INDUSTRIAL, INFRASTRUCTURAL, AND STRATEGIC RESOURCES POLICIES IN DEVELOPED COUNTRIES

In this section we survey a variety of neomercantilist industrial, infrastructural, and strategic resources policies in developed countries, bearing in mind that many developing countries also have similar policies.

Industrial Policies

Today many nations adopt relatively benign industrial and infrastructure policies to enhance the competitiveness of their domestic industries and protect their economy from the perceived malevolent policies of other states. Industrial policies are usually acceptable to the international community; most experts agree that one of the state's primary jobs is to physically protect and encourage its economic growth.

National innovation projects are central features of industrial policies. They are often designed to encourage large-scale domestic manufacturing of cutting-edge products such as passenger airplanes. Many governments help fund R&D by domestic private companies. In the United States, the Department of Defense's Defense Advanced Research Projects Agency (DARPA) played an important role after 1957 in funding and promoting new technologies integral to computers, airplanes, civilian nuclear energy, lasers, and biotechnology.[24] DARPA has helped coordinate academic researchers, venture capitalists, and government officials to develop new technologies, many of which have military uses. Early in its history DARPA helped fund the development of semiconductors, computer chip fabrication, and technologies for the personal computer. Beyond funding basic research, DARPA has also helped commercialize many new innovations. Today it remains involved in research in military weapons but also in fields such as robotics and human-machine symbiosis that it anticipates could play a major role in both the economy and the military.

The Australian economists Linda Weiss and Elizabeth Thurbon emphasize how the U.S. government and others use procurement policies to create "national champions"—big, globally competitive companies like Boeing, Lockheed, Motorola, IBM, and Microsoft—that rely on the government to purchase their products. Even though it pressures other countries to open up their public works projects to U.S. companies, the United States implemented its own "buy national" procurement policy in the 2009 stimulus bill. The Australian economists conclude that "although subject to multilateral discipline, government procurement offers a powerful tool for national economic promotion in an era of economic openness."[25]

Another important component of industrial policy in many states is restrictions on foreign direct investments (FDI). Typically, states restrict what sectors of the economy foreign businesses can invest in and what maximum ownership share foreigners can have in domestic companies. The purpose of such restrictions is often to prevent foreign control of

strategically important or sensitive industries such as mining, banking, utilities, telecommunications, and mass media. For security reasons, many states do not want foreign businesses and investors involved in manufacturing weapons or high-tech goods used by the military. The restrictions can also give an advantage to domestic companies and domestic investors by limiting competition from foreigners.

States can also place various conditions on foreign companies, such as requiring them to form joint ventures with domestic manufacturers or mandating that they buy certain inputs from domestic companies. These policies are designed to provide domestic companies access to new foreign technology and increase their sales. States also sometimes impose conditions on foreigners' access to land and real estate. For example, in 2017 New Zealand barred foreigners from purchasing existing houses because foreign demand had already driven up prices so high that many New Zealanders could no longer afford to buy a house.

Depending on a variety of circumstances, industrial policies such as funding for innovation, government procurement, and limits on FDI are often viewed as more malevolent than benevolent protectionist measures. The United States–China spat over China's industrial policy (see Box 3.1) demonstrates that one state's proactive role in developing new technologies and thriving industries is another's national security issue!

UNITED STATES–CHINA TENSIONS OVER INDUSTRIAL POLICY

Beginning in 2009, U.S. and Chinese officials held annual talks called the "Strategic and Economic Dialogue" (S&ED). During the 2016 S&ED discussions, Obama administration officials complained that China's industrial policies caused overproduction of steel, aluminum, and other products that were being *dumped* on the international market. Several months earlier the U.S. government had slapped high tariffs on imported Chinese steel and pressed Beijing to let the renminbi's exchange rate fluctuate. In the talks U.S. Treasury Secretary Jacob Lew alleged that China's malicious industrial policies hurt other countries and that its overproduction had a "damaging and distorting effect" on global markets. U.S. solar panel companies, aluminum manufacturers, unions, and politicians including both Donald Trump and Bernie Sanders also complained publicly about the flood of cheap Chinese goods into the United States. Officials in Spain, Belgium, and other countries had a similar message: industries were laying off thousands of workers because they could not compete with Chinese goods.

In response to these complaints, President Xi Jinping said China would cut down production of steel and coal as part of an effort to reform the economy. Chinese leaders gave few specifics of how they would reduce industrial overcapacity, but they pointed to the need to increase China's own internal demand. China's finance minister Luo Jiwei noted that much of the overcapacity was due to Chinese government spending right after 2008 to help the global economy recover from the global financial crisis. He suggested that if reform was pushed too fast, it would generate massive unemployment and cause worker protests.

Encouraged by the Chinese government, Chinese state and private companies have been ramping up their overseas investments, including acquiring Western companies with technology that China wants to access. The Chinese FDI helps offset the huge U.S. balance of trade deficit, but it has also raised concerns among U.S. officials about security risks.

Both China and the United States have to tread lightly in the long-running dispute over industrial policy. For one thing, the United States has been dependent on China to continue purchasing and holding onto U.S. Treasury bonds and dollars. Obama calculated that pushing too hard on China would cause it to take an ever-harder line against the United States and its allies in East and Southeast Asia. China has reason to fear that U.S. protectionism could harm its export industries and lower its growth rate. For both countries, industrial policy is hard to separate from other economic and security issues.

Limits on FDI are usually acceptable if connected to what are perceived as legitimate security concerns. Ha-Joon Chang points out that the United States, Japan, and many countries in Europe had a wide variety of restrictions on foreign investments in the nineteenth century and in some cases into the 1960s.[26] During its "economic miracle" after World War II, Japan prohibited FDI in vital industries and limited foreign ownership in many industries at 50 percent. Instead of favoring foreign takeovers of local companies, it pressured foreign companies to license technology to local companies so that the Japanese could learn to manufacture products themselves. Finland had draconian restrictions on FDI until the 1980s: among other things, foreigners could not own more than 20 percent of a company, and foreign banks were completely prohibited. Despite economic liberal insistence on unfettered capital inflows, clearly the Japanese and Finnish models of economic success owed almost nothing to FDI.

Finally, Canadian political-scientist Patricia Goff reminds us that the purpose of helping one's own companies and industries is not necessarily just to save jobs, boost exports, or hurt foreigners.[27] In fact, the purpose may be much more defensive than anything else. Goff has examined how Canada and the European Union have both strongly protected their cultural industries—music, television, radio, film, and magazine publishing—from a U.S. onslaught over the last sixty-five years. They use public ownership of some culture industries (like public television), tax incentives for local private investment in movie production, public loans and grants for artists, minimum local content requirements (on TV and radio programming), and ownership rules to preserve and nurture domestic culture producers. Canada and the EU have these policies not so much to keep out foreign cultural products as to promote their own distinct national identity, cultural diversity, and social cohesion. Preserving "cultural sovereignty" in the face of globalization's homogenizing effects is an eminently political goal, vital for nurturing a democratic citizenry that is well informed about its own history and values.

Strategic Resources

Access to and control over strategic resources has been a top concern of industrialized nations for many decades. They fear that being "cut off" from energy, minerals, and metals will cripple their economies and weaken their war-fighting ability. Because complex interdependencies between states are not always symmetrical (felt equally), dependence on any resource or vulnerability to a supplier is usually regarded as a national security threat. For example, for a period in 1973 and 1974, Arab members of OPEC placed an embargo on oil exports to the United States, the Netherlands, and Denmark, causing severe oil shortages and plunging most Western countries into recession. And as we discuss in Box 3.2, China recently used its near-monopoly control over rare earth minerals as leverage in a maritime dispute with Japan, stoking security fears in many Asian countries and causing the world's major importers of rare earths to seek new non-Chinese sources of these critical minerals.

Many industrialized states seek to minimize the risks of cutoffs or other supply

disruptions by developing political and military alliances with governments that control important resources—even if those governments are undemocratic and seriously violate human rights. At the same time, many states have established stockpiles of resources and encouraged the expansion of domestic mining and hydrocarbons extraction by offering subsidies to national companies and leasing public lands to them at a low cost. In the 1970s the U.S. government built a costly Strategic Petroleum Reserve that can cover national oil needs for 90 days. More recently it started stockpiling tantalum (a key ingredient in cell phones and electronic equipment) and dozens of other minerals and metals used in electronics and weaponry. Even the U.S. Centers for Disease Control and Prevention manages a Strategic National Stockpile, a repository of medicines and vaccines for use in case of a national emergency such as an epidemic or bioterrorist attack.

In the last two decades, China has signed long-term oil supply agreements with countries in Africa and Latin America as a way of getting "first dibs" on global commodities instead of buying them through short-term contracts in futures markets. As we discuss in Chapter 13, Chinese companies have also significantly expanded investment in resource exploration and production in many developing countries. Like China, many industrialized nations encourage their national companies to diversify suppliers overseas, buy foreign resource-extracting companies, and purchase concessions (exploration and production rights) in other countries. In recent years, foreign oil companies have been scrambling to buy concessions to explore offshore West Africa, where many think vast oil deposits may exist.

THE STRUGGLE OVER RARE EARTHS

When the Japanese coast guard seized a Chinese fishing trawler in September 2010 near disputed islands in the East China Sea, little did Tokyo know that it would lead to a global dispute over rare earth metals—more than a dozen minerals used in electronics, wind turbines, electric cars, and weapons systems. Beijing responded by temporarily cutting off rare earth exports to Japan—which had relied on China for 90 percent of its rare earth imports—sending Japanese manufacturers into a panic and dramatically pushing up prices for rare earths in global markets. Beginning in 2011 the Chinese government established export quotas on the minerals, a violation of WTO trade rules. Japan and the United States scrambled to find new sources and institute recycling programs in order to reduce dependence on China, which produced 97 percent of the world's supply in 2010.

Many analysts interpreted China's moves as a classic form of malevolent mercantilism whereby a state uses control of strategic resources to punish its rivals. According to Jane Nakano, the dispute "severely reduced Japan's comfort with China as a trade partner … and transformed Sino-Japanese economic relations from a mutually prosperous rivalry to one with an undertone of mistrust."[a] By reserving more rare earths for its domestic producers, Beijing seemed intent on forcing overseas manufacturers that needed the minerals to move some of their factories to China—thereby facilitating a transfer of technologies to China from these high-tech companies and boosting Chinese production of key components used in the electronics and clean energy industries.[b]

Japan and the United States interpreted China's manipulation of rare earth markets as a potential threat to national security and an early warning of how this rising power might defy trade norms in the future. They responded with their own defensive neomercantilist countermeasures. The Japanese government funneled huge subsidies to corporations to help them develop new rare-earth recycling processes and signed new agreements with the likes of Vietnam, Australia, and Kazakhstan to jointly develop new mines. In the United States, the mining company Molycorp reopened a huge rare-earth mine in Mountain Pass, California that has been closed in 2002 for environmental reasons (although it shut down again in 2015). The Department of Energy funded research at the Critical Materials Institute to find more efficient ways to use rare earths and to create substitutes for them. Together with Japan and the European Union, the United States filed a formal complaint with the WTO, which ruled in 2014 that China's export quotas violated GATT rules. China eliminated the quotas in 2015.

Private market actors around the world are moving rapidly to diversify supplies of rare earths like neodymium and beryllium, on land and from the seabed, to destroy China's monopoly.[c] By 2016, growth of production in countries such as Australia,

Russia, Brazil and Canada had lowered China's share of global production to 83 percent. However, when China started cracking down on illegal mining in 2017, prices of rare earths rose sharply again, raising new concerns that Beijing could use control of supplies for geopolitical purposes.[d]

The minerals dispute can be seen as part of a wider struggle among East Asian nations to control the East and South China Seas. In recent years, China has asserted ownership over numerous small islands in these waters that are also claimed by Japan, Taiwan, the Philippines, and Vietnam. The trawler incident occurred near the Senkaku Islands, controlled by Japan since 1895. Chinese nationalists seized on rare earths as a way to try to weaken Tokyo's position on the islands. When the Japanese government bought the Senkaku Islands from their private Japanese owners in September 2012, street protests erupted in China, and Japan sent many coast guard vessels to the waters to warn off Chinese Navy ships near the islands.[e] An informal Chinese boycott of Japanese goods in late 2012 caused sales of Nissan, Toyota, and Honda cars in China to plunge, and Panasonic estimated that the boycott would cause billions of dollars in profit losses—the second worst yearly losses in the Japanese company's history.[f] The rare earths story reminds us that states worry deeply about strategic resources and are willing to play risky games of brinksmanship to advance their economic interests and security.

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National conservation programs and a switch to domestic alternatives to imported strategic resources are also ways that states reduce dependence on foreign resources. During the Obama administration, the rapid spread of fracking allowed the United States to increase oil and gas production dramatically. U.S. businesses also began investing more in solar and wind power as market conditions for these sources of power improved (see Chapter 16). In contrast, Japan has not been successful in diversifying or reducing its energy imports. Although it invested heavily in energy efficiency and nuclear power beginning in the 1970s, more than 80 percent of its energy needs are met by imported oil, most of which still comes from the Middle East. After the 2011 Fukushima nuclear disaster, the share of Japan's domestic energy coming from nuclear power fell from 30 percent to less than 10 percent.

As the Arctic ice cover slowly disappears, countries with territory inside the Arctic Circle and who make up the Arctic Council—Canada, the United States, Russia, Sweden, Denmark, Norway, Iceland, and Finland—are eager to develop its potentially lucrative offshore and onshore oil and natural gas fields.[28] As expected, environmental groups and supporters of alternative energy in many of these states have been fighting against these plans to expand hydrocarbons and mineral extraction in the Arctic. As Russia and Norway have moved swiftly ahead with oil and gas development to their north, President Obama and Canadian Prime Minister Justin Trudeau announced in late 2016 that they would bar new oil and gas exploration in their respective countries' Arctic territorial waters. In contrast, President Trump has discussed the need to reduce U.S. dependence on Middle East petroleum and has expressed hope that the United States will become a major oil exporter in the future. His administration believes that the federal government should continue to subsidize domestic oil and natural gas production.

Trump and the State

It is easy to assume that U.S. president Donald Trump is a mercantilist because he likes to frame negotiations and deals in zero-sum terms: one side wins, the other loses. However, it is not at all clear that Trump can deliver foreign policy "wins" for the United States that enhance its national security. Many realist critics believe that his approach to international relations is actually threatening U.S. security. As we discuss further in Chapter 16, most energy experts now argue that, because energy markets are shifting away from oil and coal towards renewables, it does not make much sense for Washington to try to prop up inefficient domestic oil and coal industries that are unlikely to create many new jobs. Moreover, the carbon emissions from these old industries are a major cause of climate change, which will physically hurt not only all Americans but everyone else in the world.

Trump's views of the state sometimes align with those of neomercantilists, as when he stresses the need for the state to protect domestic companies from foreign competition, modernize the military, and massively increase spending on infrastructure. In many other ways, Trump's views are not mercantilist. During the election campaign, he castigated the U.S. government as inefficient and even malicious. He often characterized Washington as a swamp of entrenched bureaucrats and privileged elites which needed to be drained. As president, he has been slow to appoint senior administrators to manage key government agencies. His rhetoric suggests that, unlike mercantilists, he views the government apparatus with suspicion, not as an instrument to attain lofty national goals for the environment, health, or innovation.

Finally, Trump's outlook on the U.S. state has affected the way other states view him and the United States—as malevolent agents who only care about winning instead of reaching compromises that are acceptable to all parties. This is also reflected in Trump's expressed contempt for some international organizations and his willingness to withdraw the United States from painstakingly negotiated international agreements such as the Trans Pacific Partnership and the Paris climate accord.

CONCLUSION

Mercantilism has evolved over the years and adapted to changing conditions in the international political economy. Classical mercantilism focused on threats to a nation's security by foreign armies and how states often resist the influence of foreign firms and international institutions. It also presumed that states would seek to generate trade surpluses as a means of supporting military power. Both mercantilists and their realist cousins assert that states *can* and should use the economy, either legally or illegally, as a means to generate more wealth and power.

The onset of complex interdependence between states in the 1970s and the spread of globalization in the 1980s and 1990s tightened the connections between domestic and global policy issues. Today, all states routinely use protectionist measures to assist some of their manufacturing, agricultural, and service sectors. Ironically, to some extent the *success* of globalization helped undermine the openness of the international political economy. As national industries have become more sensitive to and dependent on foreign markets, they have lobbied their governments for protection from the new vulnerabilities and competition they face.

Voters and citizens want to be shielded from the excesses of the market at the same time that they want competitive markets to work better! Thus, managing the international economy remains a complicated task that befuddles politicians and academics alike.

As examinations of policies related to trade, national security, cyber security, the environment, and health policy demonstrate, states are finding more sophisticated ways of protecting themselves and domestic groups from foreign pressures. However, it is often difficult for states to determine who initiated a cyberattack and how badly they were damaged.

The spread of populist-authoritarian governments and more intense global interdependence portends increased tensions and violence between states. For both mercantilists and realists today, globalization, financial crises, and the industrialized nations' dependence on foreign natural resources show that self-regulating markets cannot adequately protect society. And yet state interventionist policies often fail to accomplish their objectives and can sometimes cause great damage to a society. Nevertheless, the state can still be an agent for positive change in the global political economy, depending on who controls the levels of power.

KEY TERMS

mercantilism 50
classical mercantilism 50
zero-sum 50
neomercantilism 50
nation 51
state 51
economic nationalism 53
infant industries 53
Keynesian compromise 55
malevolent and benign mercantilism 58
industrial policies 62
DARPA 62
procurement 62
strategic resources 64

DISCUSSION QUESTIONS

1. Each of the IPE perspectives has at its center a fundamental value or idea. What is the central idea of mercantilism? Explain how that central idea is illustrated in the mercantilist period of history and in recent neomercantilist policies.
2. What is the difference between benign and malevolent mercantilism in theory? How could you tell the difference between them in practice? Find a newspaper article that demonstrates the tensions between these ideas, and explain how the issue is dealt with by the actors in the article.
3. What potential political and economic drawbacks are there with governments "picking winners" and providing loans and subsidies to strategic industries?
4. Explain four or five ways that globalization has changed the face of mercantilism and neomercantilism.

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CHAPTER
4
Economic Determinism and Exploitation: The Structuralist Perspective



UN Anti-Racism Day demonstration, in London, March 2017.

Source: Shutterstock/Dinendra Haria.

> *Capital is dead labour, that, vampire-like, only lives by sucking living labour, and lives the more, the more labour it sucks. The time during which the labourer works, is the time during which the capitalist consumes the labour-power he has purchased of him.*
>
> Karl Marx[1]

If you take some time to look at income trends in the United States, you will find that for many people in the last few decades, the American Dream is just that: a dream. Ten million more Americans were living in poverty in 2015 compared to 1999.[2] The median U.S.

income in 2015 was still slightly less than the median income in 1999 (in 2015 dollars). The financial crisis in particular hurt the poorest Americans: incomes of the bottom 10 percent of households were still lower in 2015 than they had been in 2007. Even so, there were several glimmers of hope. The Census Bureau reported that the median U.S. income grew by 5.2 percent from 2014 to 2015 to reach $56,500. The number of people without health insurance fell from 49 million in 2010 to 28 million in 2016, largely due to the Affordable Care Act.[3]

How are we to make sense of these trends? The structuralist perspective offers a way to recognize their underlying logic. With a focus on economic power and class conflict, structuralism has its roots in the ideas of Karl Marx. While most structuralists do not share the commitment to a socialist system as envisioned by some Marxists, they do believe that the current global capitalist system is exploitative and can be changed into something that distributes economic output in a more just manner. Indeed, the structure in structuralism is the global capitalist economy, which shapes society's economic, political, and social institutions and imposes constraints on what is possible.

Plenty of scholars claim that the demise of socialism in the former Soviet Union and Eastern Europe and China's transition to a mixed economy mean that "Marx is dead." However, the global financial crisis highlighted not only the failures of free market capitalism but also the political clout of the economic elite. Outside the seats of official power, millions of citizens continue to protest against free-trade organizations and U.S. imperialism. Those who feel excluded from economic progress or who reject the legitimacy of globalization have marked their dissatisfaction in various ways, including by joining leftist social movements, supporting populist politicians, and voting for Brexit.

The structuralist perspective has no single method of analysis or unified set of policy recommendations. Rather, it is the site of an active debate that forces us to ask important questions. What are the historical events that created the capitalist structure? How does the global capitalist system operate? How are resources allocated? What comes next and how do we get there? Moreover, this critical perspective challenges the existing state of affairs. The main theses of this chapter are as follows:

- First, many see in structuralism not only the tools to conduct a scientific analysis of existing capitalist arrangements but also the grounds for a moral critique of the inequality and exploitation that capitalism produces.
- Second, this framework of analysis allows us to view IPE "from below," that is, from the perspective of the oppressed classes and the developing nations.
- Third, it raises issues about human freedom and the application of reason in shaping national and global institutions.
- Finally, structuralism views capitalism and other modes of production as driven by conflict and crisis and subject to change. The structure that exists now emerged at a particular time and may one day be replaced by a different system of political economy.

After outlining some of the major ideas, concepts, and policies associated with both Marx

and Lenin, we explore recent theories of dependency, the modern world system, and neoimperialism. We also discuss some structuralist arguments about the 2007–2008 financial crisis and inequality trends around the world.

FEUDALISM, CAPITALISM, SOCIALISM—MARX'S THEORY OF HISTORY

The first great scholar to pioneer a structural approach to political economy was Karl Marx (1818–1883). Born in Germany, Marx did his most significant work while living in England, spending hours on research at the British Museum in London. Many of his views reflect the conditions he and his collaborator Friedrich Engels observed in English mills and factories at the height of the Industrial Revolution. Adults and children often labored under dreadful working conditions and lived in abject poverty. Marx's theory of history, his notion of class conflict, and his critique of capitalism must all be understood in the context of nineteenth-century Europe's political and economic climate.

Marx understood history to be a dynamic, evolving creature, determined fundamentally by economic and technological forces. He believed that we can objectively explain these forces just like any other natural law through a theory of historical materialism, which takes as its starting point the notion that the *forces of production*, defined as the sum total of knowledge and technology contained in society, set the parameters for the whole political-economic system.[4] As Marx put it, "The hand mill gives you society with the feudal lord, the steam mill society with the industrial capitalist."[5] At very low levels of technology (primitive forces of production), society would be organized into a hunting-gathering system. At a higher level, we would see an agricultural system using steel ploughs and horses, oxen, or other beasts of burden. This technological advancement (although still considered primitive by modern standards) causes a change in the social relations in society, specifically the emergence of feudalism. Instead of hunters and gatherers banding together in small-scale tribes with a relatively equal division of the economic output, feudalism is characterized by a large stratum of peasant-farmers and a small aristocracy. The key Marxist claim is that changes in technology *determine* changes in the social system. Thus, Marx has been considered a *technological determinist*, at least within his theory of history.

Marx sees the course of history as evolving from one system of political economy (or "mode of production," in his words) to another due to the growing contradiction between the forces of production and the property relations in which they develop. In each of these modes of production, there is a dialectical process whereby inherently unstable opposing economic forces and counterforces lead to crisis, revolution, and the next stage of history. Over long periods, the forces of production will continually improve because technology is simply an aspect of human knowledge. Once a discovery is made, whether the smelting of copper and tin into bronze or the development of a faster computer processor, knowledge of it tends to be retained and can be improved upon by subsequent generations. Human knowledge and technology have a ratchet-like quality—they can go forward a bit at a time but will not go backward.

For Marx, the agents of change are human beings organized into conflicting social classes. Because class relations change more slowly than technological development, social

change is impeded; capitalism gradually produces a face-off between the bourgeoisie and the proletariat. According to Marx, the bourgeoisie are wealthy elites who own the means of production—or what today are big industries and financial institutions. In British society, the bourgeoisie also made up the Members of Parliament and thus controlled the government—or state, as Marx would refer to it. In Marx's day, the proletariat were the exploited workers (including their fam-ilies) in Britain's mills and factories, who received very low wages and sometimes died on the job. Gradually, it was thought, workers would realize their common interests and would press on the bourgeoisie for higher wages and better working conditions.

Marx identified three objective laws that would, at some point, destroy capitalism from within:

- First, *the law of the falling rate of profit* asserts that over time capitalists replace workers with machines and other labor-saving devices, increasing unemployment. Because surplus value (profit) can only come from exploiting living labor, the lower proportion of living labor compared to machines causes the rate of profit to decline.
- Second, *the law of disproportionality* holds that capitalism, because of its anarchic, unplanned nature, is prone to instability. During a period of economic boom there will be overproduction such that capitalists cannot sell everything they produce at profit and workers cannot afford to buy everything that they make. This disproportionality between supply and demand causes recession (economic bust) as many firms go out of business and unemployment increases, but it also prepares the conditions for another cycle of overproduction to occur. Periodic booms and busts increase social unrest and destabilize the capitalist economy. In response to these disequilibriums, governments will often increase social spending or create a military–industrial complex to increase consumption.
- Third and finally, *the law of concentration* holds that capitalism creates increasing inequality in the distribution of income and wealth. As the bourgeoisie continue to exploit the proletariat and as weaker capitalists are swallowed by stronger, bigger ones, wealth and the ownership of capital become increasingly concentrated and centralized in fewer and fewer hands. Marx viewed these as objective, inescapable features of the capitalist mode of production, which he predicted would result in the ultimate collapse of the system.

For Marx, capitalism is a *necessary* stage in history, which builds wealth and raises material living standards. It transforms the world and in so doing breaks down feudalism, its historical antecedent. It creates the social and economic foundations for the eventual transition to a "higher" level of social development. Marx argued that when class conflict becomes so severe that it blocks the advance of human development, a social revolution will sweep away the existing legal and political arrangements and replace them with ones more compatible with continued social and technological progress. In this way, history has already evolved through distinct epochs or stages after primitive communism: slavery,

feudalism, and capitalism. Marx and Engel's *Communist Manifesto*, published in 1848, called for a revolution that would usher in a new epoch of history—socialism—which would, after yet still another revolution, finally produce pure communism.

As we will discuss in the next section, neo-Marxists and structuralists still accept the notion of exploitation, although it has been separated from Marx's labor theory of value, which argues that the value of a commodity is related to the amount of labor required for its production. Also, most neo-Marxist scholars no longer accept the claim that capitalism will inevitably destroy itself. Rather, it is generally accepted that Marx's mathematical analysis that produced this prediction was simply erroneous.[6] Socialism may be a possible future, but it would have to be a political choice, not something imposed on society by Marx's deterministic laws of historical epochs. Nonetheless, many other ideas from Marx or from the school of thought he established contribute to an explanation of phenomena we still observe today in the international political economy.

SOME SPECIFIC CONTRIBUTIONS OF MARX TO STRUCTURALISM

Here we explore four ideas that are found in varying degrees within Marx's work and that have been further developed by neo-Marxists and other structuralists. Some ideas that Marx considered to be of great importance are no longer regarded as useful, and many of his ideas have been modified (and hopefully improved) by subsequent scholars, which can be seen as part of the normal development in any field of academic inquiry. The following four Marxist ideas are central to contemporary structuralist analyses of the international political economy: the definition of class, class conflict and the exploitation of workers, capitalist control over the state, and ideological manipulation.

The Definition of Class

To understand the Marxist notion of class, we must first define *capital*. Capital, what Marx called the means of production, refers to the privately owned assets used to produce commodities in an economy. Automobile factories are capital, as are all the machines and tools inside them. A computer, when owned by a company, is capital. So are the desks, filing cabinets, cranes, bulldozers, supertankers, and natural resources like land and oil. Almost all production requires both workers and physical assets, and in modern economies, production processes can indeed be very capital-intensive.

When we speak of "capital goods," we mean more than simply the existence of such productive assets. Humans have used tools for much longer than capitalism has existed and socialist societies have machines and factories just like capitalist ones. To call an asset capital also means that it is privately owned, that somebody has legal ownership and effective control over that asset. In many cases today that ownership is merely a piece of paper or a computerized account representing stock in a corporation. The property rights in a capitalist society dictate that the owners of capital will receive the profits from the sale of commodities produced by the capital they own and the labor they hire.

Class is determined by the ownership, or lack of ownership, of capital. A minority of people will own a disproportionate share of the productive assets of the society; they constitute the capitalist class, also referred to as the bourgeoisie. In the United States, for example, the wealthiest 10 percent of the population owns 81 percent of stocks, leaving 19 percent of this financial asset for the remaining 90 percent of society.[7] Real estate, excluding a household's principal residence, has a similarly unequal distribution. Financial securities and business equity are even more concentrated, with the top 10 percent owning 94 percent of the total. The majority of the population owns very little capital, and indeed, many people own no productive assets; they constitute the working class, known as the proletariat. Note that workers may own houses, cars, appliances, and so on, but these are simply possessions, not productive assets. They cannot be mixed with labor to form a commodity that could be profitably sold on a market. Implicitly, if not explicitly, Marxists

regard the original distribution of assets as unjust, noting that historically a small number of people confiscated large amounts of land and other resources by means of violence and coercion. Thus, the contemporary consequences of this distribution are criticized for moral reasons.

Class Conflict and the Exploitation of Workers

For households in the capitalist class, profits are the leading source of income. For example, if the average return in the stock market is 5 percent per year and a capitalist household owned $50 million worth of stock in various corporations, then the income produced by that ownership would be $2.5 million in one year ($50 million times 0.05). This leaves the original $50 million intact and it comes without any requirement that the capitalists actually perform any work.

Workers, on the other hand, have little or no capital and therefore must sell their labor to capitalists if they are to receive an income. In other words, businesses hire workers and pay them a wage or salary. For Marxists, this inevitably leads to the exploitation of workers because of their weak bargaining position. In a capitalist economy, there is always a certain level of unemployment, even when there is sufficient idle machinery that could put everybody to work if put into operation. The presence of unemployed workers functions to keep down the wages of the employed—if one worker does not accept the going rate, then he or she can be easily replaced. Thus, unemployment allows capitalists to dominate workers and serves as the foundation for their exploitation.

The exploitation of workers by capitalists is a specific instance of power relations more generally. To say that actor A has power over B is to say that A is able to get B to act in ways that promote the interests of A and are contrary to B's.[8] This does not necessarily mean that B has literally no choice but simply that the options are configured to benefit A. When the armed robber tells the hapless victim, "Your money or your life!" the victim could choose the latter. Nonetheless, it is the case that the robber, due to the presence of a gun, has power over the victim because in either scenario the robber will make off with the money. The victim is coerced into making the least bad choice.

Many workers are in a similar situation: either accept low wages or starve! Capitalism depends on "the existence of workers who in the formal sense, voluntarily, but actually under the whip of hunger, offer themselves."[9] Joan Robinson, the famous socialist-leaning post-Keynesian economist, captured the position of workers by remarking that the only thing worse than being exploited under capitalism is not being exploited. In other words, the worst outcome for those in the working class is to be unemployed, and it is the fear of unemployment that forces workers to accept low wages. Workers technically do have a choice, but the game is structured such that the best choice is still a bad choice for them, yet a good one for the capitalists. In sum, exploitation means that capitalists, because they have greater labor market power, are able to expropriate a share of the economic output that should belong to workers.

We should be clear that class conflict does not necessarily mean a state of warfare or even

hostility of any sort. In fact, many individuals may not even recognize the conflicting nature of their relationship with the other class. Class conflict usually results in a gain for one side at the expense of the other. The degree to which individuals in different classes act upon this fact is hard to predict. Furthermore, even when the conflict is recognized, it is possible that a compromise between classes can be found. In welfare states such as France, Germany, and Sweden, organized labor renounces the goal of a socialist society and offers a relatively harmonious relationship with business in exchange for high wages, adequate unemployment compensation, universal health care, and generous pensions.

Because workers are exploited, they share an objective economic interest in changing the economic system, while capitalists will have an interest in maintaining the status quo. The presence of an "objective" interest does not necessarily mean that workers will actually form a socially and politically active movement. Workers may not subjectively recognize their common objective interest due to false consciousness (discussed in the section "Ideological Manipulation"). Alternatively, workers may recognize their common interest but be unable to organize due to suppression of unions or the result of collective action problems. In Marxist language, workers are often a class *in itself* without becoming a class *for itself*.

The central idea, however, is that the relationship between capitalists and workers is built upon an objective division of the economic output of a society into wages and profits. The actions of individual workers and capitalists will depend on many concrete historical variables, leading to revolution, class compromise, or passivity. Regardless of the way in which the conflict plays itself out, class conflict is a fundamental objective characteristic of capitalist societies.

Capitalist Control over the State

The *state* is the organization that governs, by force if necessary, a population within a particular territory. Despite globalization, the modern state is still usually the most powerful organization within any society, typically possessing the strongest tools of repression in the form of military and police forces. Based on its powers, the state also exercises tremendous influence in picking economic winners and losers through taxation, spending, and regulations. Some of its most important regulations involve labor issues such as the minimum wage, child labor laws, and the ease or difficulty in forming labor unions. While states are not omnipotent, they do have the ability to help their friends and punish their enemies. It is therefore reasonable that both capitalists and workers would seek to "capture" the state, to apply the capacities of the state to their particular interests.

In the struggle to control the state, capitalists and workers have very different resources. The capitalist class has greater financial resources, and this often translates easily into influence in the political system. Capitalists are typically able to donate more money to pro-business candidates. Corporations and wealthy elites fund policy-proposing think tanks such as the Brookings Institution or the Heritage Foundation. Furthermore, the state depends upon businesses to generate tax revenue and employment; a climate that is too anti-business will cause capital to flee elsewhere or at least reduce investment. Thus, even without direct attempts by capitalists to influence the state, many policies will promote

their interests regardless.

For workers to turn their greater numbers into political power, the state must allow for strong democratic institutions. In Western European countries that have proportional representation voting, workers' parties (Social Democratic or Socialist Parties) often win majorities or significant pluralities. Whereas capitalists have the power to relocate or reduce investment, workers may also attempt to influence a political system through strikes and protests. Often a strike is the response of a single union to a particular grievance with a firm, but when a large segment of the population is involved in a general strike, the entire economy can be halted and governments can be forced to respond to working-class demands. It is no surprise to Marxists that general strikes, and even more limited secondary or sympathy strikes, have been made illegal in the United States.

In their search for profits, capitalists in the rich states not only exploit domestic workers but workers in other countries as well. The international situation is complicated because capitalists in any country are not only in conflict with their own workers but also have a complex relationship with capitalists in other countries. Meanwhile, capitalist firms do compete with other firms both domestically and internationally, yet they also form alliances with those firms on issues that impact the functioning of the global capitalist system. Thus, depending on the issue, capitalists in New York or London often form alliances with the local capitalist elite in other parts of the world in order to keep profits up, workers weak, and wages down.

Ideological Manipulation

Power derives from the control over hard resources, like capital or the military, and the ability to force others to act in certain ways by structuring the choices of the weaker to the benefit of the stronger. Yet structuralists also accept that power is exercised through the deployment of ideology. An important goal of capitalist ideology is to give *legitimacy* to the capitalist economic system by controlling people's hearts and minds. Once the working class believes that the system is legitimate, it will believe that it is appropriate and just. While democratic societies possess arsenals of surveillance and repression, they tend to be less intrusive than those found in authoritarian systems. In a democracy, because citizens participate in fair elections, the leaders typically earn the consent of the led, including even those who voted for a different candidate or party.

When individuals regard a democratic political system as legitimate, they are also likely to believe that the capitalist system itself is proper and just. A belief by workers in the legitimacy of capitalism ensures that (1) they will not seek to replace it with something else (e.g., socialism) and (2) they will work harder within the present system, thus increasing the income of the capitalists who generally do not have to use force. Marxists would say that, in effect, workers consent to their own exploitation. Given the importance of legitimacy, the capitalist class will actively seek to create an ideology in society that gives legitimacy to pro-capitalist institutions (see Box 4.1).

In his political economy writings, well-known public intellectual Noam Chomsky argues that the consent of the proletariat to their own exploitation must be "manufactured" by

powerful interests in society, including the state and the corporate media. He writes, "One of the prerogatives of power is the ability to write history with the confidence that there will be little challenge."[10] For example, political elites in the United States use the threat of foreign enemies to draw attention away from internal, class-based conflicts. For much of the twentieth century, the Soviet Union and communism served that function. Writing on the George W. Bush administration, Chomsky observes, "Manufactured fear provided enough of a popular base for the invasion of Iraq, instituting the norm of aggressive war at will, and afforded the administration enough of a hold on political power so that it could proceed with a harsh and unpopular domestic agenda."[11] Little changed under the Obama administration except that Iran and the Islamic State replaced Iraq as the targets of propaganda. Chomsky and his colleague Edward Herman have also created a propaganda model to explain the ways in which the "free press" in liberal, capitalist societies—especially in the United States—reports on events in ways that ultimately serve the interests of large corporations and the state.[12]

ANTONIO GRAMSCI AND INTELLECTUAL HEGEMONY

One of the most influential structuralists of the twentieth century—and one whose ideas are particularly relevant to the global political economy of the twenty-first—is the Italian Marxist Antonio Gramsci (1891–1937). He lived in a time of tremendous economic and political tension, witnessing the rise of fascism in the 1920s and 1930s and the intense conflicts among nations and between classes. He proposed a philosophy of praxis—that we should demonstrate our beliefs through our actions. He edited an intellectual journal, *Ordine Nuovo* (*The New Order*), and led worker protests in the Italian industrial center of Turin, especially against the manufacturing giant FIAT. These activities drew the attention of Italy's fascist government, which imprisoned him. In his *Prison Notebooks*, Gramsci attempted to revise Marxist theory to account for changing conditions in the advanced industrial world. He died in prison at the age of 46.

According to Gramsci, the dominant class in society maintains its position in two different ways: through coercion and through consent. Coercion is an obvious mechanism, applying economic and political power directly to keep the subordinate class in line. For example, police and manufacturer-backed thugs employ violence against protesting workers.

Coercion is a powerful tool, Gramsci said, but ideas are even more powerful means to rule over the masses. The dominant class produces and promulgates an ideology that supports and legitimizes its interests. These popular ideas permeate society through education and the communications media. Once the subordinate class comes to accept this worldview, whether intentionally or by osmosis, as common sense, its thoughts and actions are brought into line with the interests of the dominant class. Police are not so necessary because the idea of taking actions that oppose the dominant class is not part of society's accepted values and norms.

In Gramsci's view, there are no truly independent intellectuals. Traditional intellectuals, such as professors, like to "put themselves forward as autonomous and independent of the dominant group,"[a] but this self-image is inaccurate, as all intellectuals are products of particular historical events and social relationships. Civil society institutions, including universities, the arts, mass media, and religion, are the spheres through which consent to rule by the dominant class is produced and social control exercised. What is needed is for workers to develop, from within their own class, organic intellectuals who remain connected to their class while providing organization, leadership, and a vocabulary that challenges the ideology of the dominant class and articulates a different vision of the future. If they can also win over many of the traditional intellectuals, the formulation of a counterhegemonic ideology becomes all the more likely. Schools, newspapers, songs, and coffee shops will then

reverberate with debate and demands for change.

References

[a]Antonio Gramsci, *Selections from the Prison Notebooks*, Quintin Hoare and Geoffrey Nowell Smith, transl. and eds. (New York: International Publishers, 1971), p. 7.

The superior financial resources of the capitalists typically ensure that pro-capitalist messages—the benefits of free trade, the need for low taxes on the rich, the desirability of limited government, and the problems with unions—will be stronger than a competing set of beliefs favored by workers. Workers, of course, are not powerless and at certain times on certain issues may succeed in persuading the public. But the game is biased in favor of capitalists.

It is a great tragedy, according to Marxists, that capitalists not only exploit workers but also manipulate their beliefs so that they become ignorant of, or apathetic about, their own exploitation. Workers' belief in the legitimacy and benefits of capitalism is *false consciousness*. Is it possible that people could be fooled about what their own self-interest is? We should recall that the rule by monarchs in the Middle Ages in Europe was at least partially legitimized by an ideology promoted by the Catholic Church asserting a Divine Right to govern: to challenge the rule of the aristocracy was to offend God.

LENIN AND INTERNATIONAL CAPITALISM

Vladimir Lenin (1870–1924) is best known for his role in the Russian Revolution of 1917 and the founding of the Soviet Union. In many ways, he turned Marx on his head, placing politics over economics when he argued that Russia had gone through its capitalist stage of history and was ready for a second, socialist revolution. Lenin is also known for his views on imperialism based on Marx's theories of class struggle, conflict, and exploitation. In his famous book *Imperialism: The Highest Stage of Capitalism* (initially published in 1917), Lenin explains how, through imperialism, advanced capitalist core states expanded control over and exploited what his contemporaries called "backward" colonial regions of the world, leaving them unevenly developed, with some classes to prosper and others mired in poverty.[13] By the end of the nineteenth century, new colonies were established mainly in Central and Southern Africa, and they became sources of cheap labor and raw materials, and an outlet for industrial investment of the advanced capitalist nations.

The critical element fueling imperialism, in Lenin's view, was the centralization of market power into the hands of a few "cartels, syndicates and trusts, and merging with them, the capital of a dozen or so banks manipulating thousands of millions."[14] Because capitalism led to monopolies that concentrated capital, it gradually undermined the ability of capitalists to find sufficient markets and investment opportunities in industrial regions of the world. Of course, profit-seeking capitalists were unwilling to use their surplus capital to help the proletariat purchase more goods and services and raise their living standards. To prevent capitalism from imploding, Lenin and others argued that imperialism therefore was a necessary outlet for surplus finance. Imperialism allowed rich capitalist nations to sustain their profit rates, while keeping the poorer nations deep in debt and dependent on the rich nations for manufactured goods and financial resources.

For Lenin, imperialism also signified the monopoly phase of capitalism or "the transition from capitalism to a higher system," by which he meant that the presence of monopolies and imperialism that followed was yet *another* epoch of history between capitalism and socialism, unaccounted for by Marx.[15] Finally, imperialism helped convert the poorer colonial regions into the new "proletariat" of the *international capitalist system*. According to Lenin, "Monopolist capitalist combines—cartels, syndicates, trusts—divide among themselves, first of all, the whole internal market of a country, and impose their control, more or less completely, upon the industry of that country," generating a world market.[16]

It is not surprising that Lenin's theory of imperialism was very influential, especially among intellectuals in the less developed countries, where his views shaped attitudes toward international trade and finance. In these countries, communist revolutionaries like Mao Zedong in China, Ho Chi Minh in Vietnam, and Fidel Castro in Cuba fought "wars of national liberation" against capitalist imperial powers. However, most contemporary structuralists no longer believe that the falling rate of profit for capitalists will cause the collapse of the capitalist mode of production.

IMPERIALISM AND GLOBAL WORLD ORDERS

In this section, we explore structuralist theories of dependency, the modern world system, and neoimperialism that trace their analytical approaches and policy prescriptions to both Marx and Lenin.

Dependency Theory

A structuralist perspective that highlights the relationships between core and peripheral countries is called dependency theory. It argues that the structure of the global political economy essentially enslaves the less developed countries of the South by making them reliant to the point of being vulnerable to the nations of the capitalist core of the North. Theotonio Dos Santos sees three eras of dependence in modern history: colonial dependence (during the eighteenth and nineteenth centuries), financial-industrial dependence (during the nineteenth and early twentieth centuries), and dependence today based on multinational corporations.

Andre Gunder Frank, who has focused attention on dependency in Latin America, is noted for his "development of underdevelopment" thesis.[17] He argues that developing nations were never "underdeveloped" in the sense that one might think of them as "backward" or traditional societies. Instead, once great civilizations in their own right, the developing regions of the world *became* underdeveloped as a result of their colonization by the Western industrialized nations. In order to escape this underdevelopment trap, a number of researchers, including Frank, have called for peripheral nations to withdraw from the global political economy. In the 1950s and 1960s, the leadership of many socialist movements in the Third World favored revolutionary tactics to change the fundamental dynamics of the world capitalist system.

Some dependency theorists have recommended other strategies by which developing nations could industrialize and develop. Raul Prebisch, an Argentinean economist, was instrumental in founding the United Nations Conference on Trade and Development (UNCTAD). The developing nations that have joined this body have recommended policies that would help redistribute power and income between North and South. Many dependency theorists, however, have been more aggressive about reforming the international economy and have supported the calls for a "new international economic order" (NIEO), which gained momentum shortly after the OPEC oil price hike in 1973.

Modern World System Theory

One fascinating contemporary variant of the structuralist perspective focuses on the way in which the global system has developed since the middle of the fifteenth century. This is the modern world system (MWS) theory originated by Immanuel Wallerstein. Capitalist in nature, the world system largely determines political and social relations, both within and between nations and other international entities.

According to Wallerstein, the world economy provides the sole means of organization in the international system. The modern world system exhibits the following characteristics: a single division of labor whereby nation-states are mutually dependent on economic exchange; the sale of products and goods for the sake of profit; and the division of the world into three functional areas.[18] The capitalist core states of northwest Europe in the sixteenth century moved beyond agricultural specialization to higher-skilled industries and modes of production by absorbing other regions into the capitalist world economy. Through this process, Eastern Europe became the agricultural periphery and exported grains, bullion, wood, cotton, and sugar to the core. Mediterranean Europe and its labor-intensive industries became the semiperiphery or intermediary between the core and periphery.

According to Wallerstein, the core states dominate the peripheral states through unequal exchange for the purpose of extracting cheap raw materials instead of, as Lenin argued, merely using the periphery as a market for dumping surplus production. The semiperiphery serves more of a political than an economic role; it is both exploited and exploiter, diffusing opposition of the periphery to the core region.

Wallerstein accepts the realist notion that the world is politically arranged in an anarchical manner—that is, there is no *single* sovereign political authority to govern interstate relations. However, much like a Marxist-Leninist, he proposes that power politics and social differences are also conditioned by the capitalist structure of the world economy. Capitalists in the core use state authority as an instrument to maximize individual profit. Historically, the state served economic interests to the extent that "state machineries of the core states were strengthened to meet the needs of capitalist landowners and their merchant allies."[19] Wallerstein also argues that state machineries have a certain amount of autonomy.[20]

One problem with Wallerstein's theory is precisely what makes it so attractive: its comprehensive, yet simple way of characterizing IPE. Many criticize his theory for being too deterministic, in terms of the constraining effects of the *global* capitalist system. Nation-states, according to Wallerstein, are not free to choose courses of action or policies. Instead, they are relegated to playing economically determined roles. Finally, Wallerstein is often faulted for viewing capitalism as the end product of current history. In this sense, he differs from many structuralists who feel that political-economic systems are still a choice people have and not something structurally determined.

Neoimperialism and Empire-Building Redux

The term neoimperialism describes a newer, subtler version of imperialism that structuralists claim the United States has been practicing since the end of the Vietnam War in 1975. Neoimperialism differs from classic imperialism in that states no longer need to occupy other countries in order to exploit or control them.

Harry Magdoff (1913–2006), who edited the socialist journal *Monthly Review*, provides a good example of the older, *orthodox* version of Marxist-Leninist ideas related to U.S.

imperialism. In his 1969 book *The Age of Imperialism: The Economics of U.S. Foreign Policy*, Magdoff established some of the same themes adopted by dependency and MWS theorists —especially those that focused on capitalism's expansive nature. He argued that the motives behind U.S. efforts to promote the economic liberal policies of the GATT, the IMF, and the World Bank could not be separated from U.S. security interests. During the Cold War, U.S. intervention abroad was not the result of one leader's decision, but the result of underlying structural forces.

Contrary to realists who argue that the United States intervened in Vietnam and other developing nations to "contain communism," Magdoff claims that the United States was motivated by a breakdown of British hegemony, coupled with the growth of monopoly capitalism.[21] President Eisenhower had earlier linked maintaining access to the natural resources of Indochina (Vietnam, Laos, Cambodia, and Thailand) to U.S. security interests. But in his farewell address, Ike warned of a military–industrial complex that exaggerated the strength of enemies in order to justify military spending.

Although U.S. hegemony declined in the 1970s due to the effects of the 1973 OPEC oil crisis and the U.S. public's opposition to military intervention outside the U.S. "sphere of influence" in Europe, Japan, and Latin America, by the late 1970s a more classic type of imperialism resurfaced in the Carter Doctrine, which proclaimed U.S. willingness to intervene in the Persian Gulf to protect U.S. oil interests. In 1979, the Iranian Revolution overthrew the U.S.-backed Shah of Iran, threatening U.S. influence in the Middle East. Soon after, the CIA supported efforts of the Mujahedeen in Afghanistan against the Soviet occupation.

In the 1980s, as part of the Reagan Doctrine, the United States renewed its efforts to intervene in developing nations. Reagan assisted Saddam Hussein in the Iran–Iraq war, unsuccessfully intervened in Lebanon in 1983 and 1984, and sold advanced weapons to Saudi Arabia. To contain communism in the Western Hemisphere, Reagan backed the *contras* in Nicaragua and supported pro-Western authoritarian regimes in Guatemala and El Salvador.

After the fall of the Soviet Union in 1991 and the Persian Gulf War in 1991, Bush ushered in what many structuralists view as a "new age of imperialism." Because the Soviet threat was gone, the globalization campaign provided the United States and other industrialized nations with an opportunity to penetrate peripheral states via trade and investment. The Washington Consensus—an understanding that economic liberal reforms promoted growth in developing countries—became the rationale for IMF, World Bank, and WTO policies.

Throughout the 1990s, President Clinton promoted economic liberalism with *selective* military intervention abroad. His campaign of "engagement and enlargement" mixed hard and soft power to explicitly draw other countries into the global capitalist economy while expanding the scope of democracy. Based on some of the lessons learned in Vietnam, Clinton was not as overtly interventionist as Reagan. However, the U.S. military hit targets in Iraq, Sudan, Somalia, and Afghanistan. In cases where U.S. interests were not as clear, such as Rwanda, the United States failed to intervene to save hundreds of thousands who

died in a campaign of genocide. Clinton's preference for multilateral (relatively equal) relations with U.S. allies set the tone for joint NATO operations in the Balkans and for intervention in Kosovo in 1999.

Neoconservatives such as Charles Krauthammer and Max Boot deplored the fact that when the Soviet Union fell, the United States failed to capitalize on a "unipolar moment" by imposing its (benevolent) will on the rest of the world.[22] After 9/11, many policy officials encouraged the new Bush administration to seize the moment and make maintaining U.S. hegemony—especially against "Islamo-fascism"—a central premise of U.S. foreign policy. Issuing a new Bush Doctrine that brazenly proclaimed that the United States "will not hesitate to act alone," the Bush II administration invaded Afghanistan and Iraq.[23] In essence, when it came to security, the United States could do what it wanted, whenever it wanted, and with whatever instruments it chose. It also promoted the moralistic idea that the U.S. principles of liberty, equality, and individualism could not be questioned.[24]

Contrary to the expectations of many Americans, Barack Obama did not fundamentally change the global role of the United States. Going beyond the militarism of the Bush administration, he escalated the use of military drones to conduct extra-legal assassinations.[25] Instead of repealing the PATRIOT Act, he reauthorized the law.[26] The United States continued to give billions of dollars in aid to Israel—despite its illegal settlements in the occupied Palestinian territories.[27] Obama also negotiated the Trans Pacific Partnership and promoted other free-trade agreements. Structuralists argue that militarism and empire-building are endemic to the American polity because the political structure operates on behalf of those with wealth and power. Empire serves the interest of capitalists.

TRENDS IN CONTEMPORARY CAPITALISM

Structuralists recognize that study of the global economy cannot be divorced from the study of the mechanisms of contemporary capitalism. Scholars have been particularly interested in understanding the methods for extracting value from workers, ways in which capitalism disciplines individuals, and changing class structures. In this section we start with an analysis in Box 4.2 of the transnational capitalist class (TCC), which exercises structural power over political and economic institutions and spreads a powerful worldview. We then review three processes that structuralists identify as critical for the TCC's success and the functioning of today's global capitalism: accumulation by dispossession, responsibilization, and the rise of the precariat.

Classical Marxism focuses on capitalist accumulation as a process through which the owners of the means of production extract surplus value from workers. The Marxist geographer David Harvey focuses on another mechanism of profit accumulation that he calls accumulation by dispossession, which involves transferring assets from public or communal control to private ownership.[28] This mechanism is predatory: it relies on seizure, thievery, and fraud, sometimes accompanied by violence. It takes many different forms, including privatization of state assets, liquidation of workers' pensions, and financial speculation. Individuals are also saddled with debt (like home mortgages), then driven into insolvency and dispossessed of what they own through bankruptcy. Even heavily indebted nations are forced into structural adjustment, wherein they must sell off state assets, extract more taxes, and cut social spending in order to pay creditors. In many developing countries, "land grabs" have become a highly contested form of dispossession whereby peasants and indigenous peoples are violently forced off of land that is then transferred to private ownership. Harvey stresses that dispossession is occurring on a global scale, requiring state power and enforcement.

THE TRANSNATIONAL CAPITALIST CLASS

A group of structuralist sociologists identifies the rise of a transnational capitalist class (TCC) as one of the most important developments in contemporary capitalism. This class primarily consists of the owners and managers of transnational corporations and financial institutions. They control most global financial assets and most of the stock in TNCs listed on exchanges around the world. What makes them different from capitalists before the mid-1970s is that they make money globally, not just in one national economy. Although the TCC traditionally draws its elites from the "triad" countries (the United States, the European Union, and Japan), it is joined by a growing number of billionaires and millionaires from the BRICs countries and other emerging nations. As such, some TCC scholars claim that TCC members do not have any particular loyalty to the nations from which they come or in which they are based. William Carroll finds evidence for this thesis within the North Atlantic ruling class, but he thinks there are still many business communities that have a strong national or regional focus.[a]

The TCC is highly concentrated and interconnected. Its members are often in interlocking directorates of TNCs, meaning that corporate directors simultaneously serve on the boards of multiple corporations. They own shares in some of the same large companies and own bonds issued by many of the same countries. Many in the inner elite are products of business schools, share similar lifestyles, and lead the boards of a host of similar social organizations. Nevertheless, different segments of the TCC do not always share the same interests.

William Carroll and Jean Philippe Sapinski identify three key transnational "policy-planning" bodies through which the TCC develops class cohesion and promotes its worldview: the International Chamber of Commerce (ICC), the Mont Pèlerin Society (MPS), and the World Economic Forum (WEF).[b] The MPS developed among anti-Keynesian economists who later formed a network of free-market think tanks. The WEF brings together elite capitalists every year in Davos, Switzerland, to discuss global issues. There are many other networks through which the TCC spreads ideas and coordinates policies.

Leslie Sklair portrays the TCC as made up of four "fractions" that complement each other:

- The owners of TNCs;
- Globalizing politicians and bureaucrats who seamlessly move between jobs in government and the corporate sector and negotiate international political agreements on trade and finance;
- Globalizing professionals (such as lawyers) with technical skills; and
- A consumerist fraction of retailers and the media, who spread an ideology of

consumption.[c]

William I. Robinson asserts that the TCC has more than just structural power over national governments and the working class. It also exercises authority through transnational state apparatuses such as the IMF, the OECD, the WTO, and even the European Union. These apparatuses "promote the conditions for capitalist globalization" but also try to fix the problems that capitalism creates.[d]

Globalization is the political project of the TCC, which turns countries into self-marketers that compete for investments and showcase their advantages to TNCs. The TCC has rolled back the welfare state throughout the Global North. It generates considerable profits through financial speculation and operating the infrastructure that states need for repression, war, and mass surveillance.[e] To accumulate on a global scale, it requires free trade, weak capital controls (financial mobility), and strong protections for private property. It must also have mechanisms to force debtors—whether governments, companies, or individuals—to repay what they have borrowed.

What is the alternative to capitalist society run by the TCC? Sklair envisions a transition to "networks of relatively small producer-consumer co-operatives (PCC)" detached from the global market and the state.[f] He also stresses the importance of struggling at the level of ideas to reject the TCC's "culture-ideology of consumerism" in favor of a "culture-ideology of human rights and responsibilities."[g]

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[c] Leslie Sklair, "The Transnational Capitalist Class, Social Movements, and Alternatives to Capitalist Globalization," *International Critical Thought* 6:3 (2016), p. 331.

[d] William I. Robinson, "Global Capitalism: Reflections on a Brave New World," *Great Transition Initiative* (June 2017), at www.greattransition.org/publication/global-capitalism.

[e] Ibid.

[f] Sklair, "*The Transnational Capitalist Class*," p. 337.

[g] Ibid., p. 338.

Contemporary capitalism also forces individuals to become "responsible" for their own self-governance and risk management. In her 2015 book *Undoing the Demos: Neoliberalism's Stealth Revolution*, political scientist Wendy Brown argues that the neoliberal form of capitalism undermines traditional economic solidarity, replacing it with responsibilization. Instead of being protected from the depredations of the market through unions or other organizations that engage in collective action, individuals have become isolated units. As "responsibilized" people they have to cultivate their "human capital,"

compete with others, "self-invest wisely," and become self-reliant.[29] In other words, the individual lives in service to the economy: "Instead of being secured or protected, the responsibilized citizen tolerates insecurity, deprivation, and extreme exposure to maintain the competitive positioning, growth, or credit rating of the nation as firm."[30]

With the spread of responsibilization, the state is no longer willing to bear as much of the cost of nurturing citizens' human capabilities or sustaining households. For example, individuals are forced to pay for an ever greater share of their education, health coverage, and retirement. They cannot expect the state to provide public entitlements. In fact, the state imposes a seemingly permanent austerity as it slims down and devotes itself to ensuring macroeconomic growth rather than regulating the private sector. Brown argues that we end up with a form of governance that "promulgates a market emphasis on 'what works'" and "eliminates from discussion politically, ethically, or otherwise normatively inflected dimensions of policy, aiming to supersede politics with practical, technical approaches to problems."[31] Ultimately, she claims, the neoliberal form of capitalism threatens democracy and popular sovereignty. However, it seems clear that society is also resisting responsibilization and market dominance. We see this in the rise of anti-austerity parties and right-wing populist parties in Europe and the United States. They are manifestations of what political economist Karl Polanyi described as a "countermovement"—an effort to re-embed the market in society.

In addition to dispossession and responsibilization, a third trend in today's capitalism is what Guy Standing describes as the rise of the precariat, a large social class that has insecure work without benefits.[32] It includes immigrants, young college graduates, and people who have lost their jobs to outsourcing and automation. Many of them work in part-time jobs, temporary positions, para-professional jobs, and as independent contractors, often lacking stable work hours. Unlike the old industrial working class, the precariat has no employer-provided benefits (like health insurance, pension contributions, and training), and it cannot count on the state for unemployment benefits or social assistance. In the face of these conditions—and knowing that it has few opportunities for social advancement—its members experience what Standing calls the four *A*s: anger, anomie, anxiety, and alienation.

The precariat emerged in the era of globalization after 1975, as capitalists demanded a flexible labor force and strove to dismantle the public sector. The precariat only has wages —and stagnant wages at that—while plutocrats and salaried workers in the state bureaucracy and corporate upper management take a growing share of national income. The precariat erupts from time to time, as in anti-austerity protests and the Arab Spring, but it is politically divided and rejects mainstream political parties. For Standing, to create security for the precariat and restore their citizenship rights, the state needs to provide a basic income to every adult in society, whether they work or not.

INEQUALITY AND THE FINANCIAL CRISIS

For structuralists, the financial crisis of 2007–2008 and the subsequent Great Recession brought into stark relief the contradictions in globalization. In this section we review their assessments of the financial crisis and connect it to the renewed focus on inequality as a fundamental outcome of contemporary capitalism.

Structuralist Views of the Financial Crisis and Its Aftermath

From a structuralist perspective, the financial crisis was an inevitable consequence of the increasing power of the capitalist class over the last forty years, not an unfortunate result of some "bad behavior" by an assortment of bankers and elected officials. Many structuralists say that we need to look at the rising inequality of income and wealth in the United States after 1970 to help explain why the financial system imploded. The share of total national income going to the richest 20 percent of Americans grew from 43 percent in 1968 to 50 percent in 2010, while the share going to the poorest 20 percent fell from 4.2 percent to 3.3 percent in the same period.[33] Adjusting for inflation, the median earnings of a full-time, year-round male worker were actually higher in 1973 than in 2008.[34] Over this 35-year period, the richest Americans claimed a large proportion of the increase in new income produced by the economy.

At the same time, American households loaded up with debt. From 1989 to 2007, the mean level of mortgage debt for the middle class, defined as those between the 40th and 60th income percentiles, increased from $45,000 to $104,000.[35] When housing prices started falling in 2006, many homeowners owed more on their mortgages than they could get by selling their houses. Credit card debt, on the other hand, is not backed up by any assets and is simply a promise to pay out of future income. Although the amounts are smaller, the mean credit card balance more than doubled, from $2,600 in 1989 to $5,600 in 2007, for those in the middle 20 percent of the income distribution.

Initially, debt provided a boost to the economy because it increased consumption, but households eventually had to spend a larger portion of their income to service their debt instead of purchasing goods and services. From a structuralist viewpoint, then, the U.S. economy was operating on an unstable foundation of debt and inequality; the unexpected drop in housing prices caused a ripple effect leading to a banking crisis and deep recession. While the government bailouts improved the balance sheets of banks and other financial institutions, the amount of debt held by the average household remained at a very high level.

Of course, the forces at work in the United States were also operating on a global level. In other words, class conflict is international. Using transnational financial institutions, rich countries have lent money to poor countries, setting into motion a stream of payments back to the rich. This dynamic has also occurred between wealthy countries, as when northern European creditors lent heavily to countries such as Greece, which since 2010 has

lacked sufficient income to repay its lenders. Once in crisis, the indebted countries are forced to adopt austerity measures that shift spending away from social programs and squeeze ordinary citizens in order to pay foreign creditors. The result is accumulation by dispossession, which none of the mass protest movements were able to stop.

Rediscovering Inequality

The financial crisis and the slow, anemic recovery afterwards brought renewed attention to some of the structuralist ideas that had been ignored by many IPE scholars in the 1990s and 2000s. Suddenly, the global system looked unstable and dysfunctional. Structuralists could explain some of its underlying contradictions. They could also claim that Marx and Engels were right when they wrote in the *Communist Manifesto*, "The executive of the modern state is but a committee for managing the common affairs of the whole bourgeoisie." When the crisis hit, states around the world immediately showed themselves to be the handmaids of capitalist elites, providing massive bailouts to financial institutions and key corporations while hanging the lower and middle classes out to dry. Meanwhile, the popular slogan of the Occupy Movement—"We Are the 99%"—signaled rising class consciousness. Then, the election of Donald Trump, the vote for Brexit, and the rise of populist parties demonstrated to many structuralists that the ideological and political hegemony of capitalists in the core countries was weakening.

It is in this context that scholars and international institutions suddenly "re-discovered" the underlying problem of inequality that they had been ignoring for decades but that structuralists had always claimed was an inherent feature of capitalism. Why does inequality matter now? Certainly there is a moral case against it. Political theorists and pundits have also focused on its political effects. Because concentration of wealth has so plainly translated into disproportionate political influence by elites and corporations, it is hard to make the case that democracy is thriving in Western countries. The majority of citizens—even those who vote—have little influence over public policies compared to the moneyed class. Finally, there is growing recognition that inequality is weakening capitalist economies by suppressing consumer demand.

It was the left-leaning (but non-Marxist) French economist Thomas Piketty who brought inequality back into the academic and public mainstream with the 2014 publication of his influential book *Capital in the Twenty-First Century*.[36] He lays out empirical evidence supporting the claim that over the long term the rate of return on capital tends to exceed the rate of economic growth. In other words, the rate of return the wealthy earn from their investments exceeds the rate of growth of GDP. Unless governments mitigate this tendency through policies of taxation and redistribution occurs in a social welfare economic will increase.

Piketty believes that public investment levels and access to education profoundly shape trends in inequality. After World War II, beliefs about inequality changed, and the spread of unions and communism helped foster progressive taxation. The war—and efforts to recover from it—also made state involvement in economic and social affairs more pervasive, which supported the rise of the welfare state. But globalization and deunionization after the

1970s weakened the political power of workers in developed countries, while the rising wealth of the top 10 percent magnified their influence over government policies. More recently, the rising cost of higher education in the United States has weakened social mobility.

Structuralists and non-structuralists continue to debate trends in global inequality. The non-structuralist scholar Branko Milanovic persuasively argues that, if one looks at the changes in distribution of income of all households in the world, global inequality decreased between 1988 and 2011, mostly due to the rapid rise in incomes in Asian middle classes.[37] However, he points out that even as incomes of many in Asia (especially in China) have risen significantly, in Western countries during the same period, the lower and middle classes had mostly stagnant incomes while the wealthiest had growing incomes. In other words, inequality within the Western countries is worsening as Asia overall is starting to catch up with the West.

However, structuralist anthropologist Jason Hickel points out that inequality between the rich countries and most peripheral countries has worsened. Between 1980 and 2014, the absolute gap between per-capita GDP in the United States and per-capita GDP in regions other than East Asia nearly doubled.[38] Thus, even though incomes have recently grown relatively faster in some developing countries than in developed countries, it will take a long time for developing countries to close the absolute income gap with developed countries. The international NGO Oxfam, which regularly supports structuralist arguments, also points to data indicating high levels of global inequality:

- The accumulated wealth of the world's richest 1 percent is equal to the wealth of half of humanity.
- Labor's share of income as a percentage of GDP has fallen in most of the world since 2000.
- Labor productivity has grown much faster than wages.[39]

The mostly developed countries in the Organisation for Economic Co-operation and Development (OECD) progressively lowered inequality from the end of World War II until the late 1970s, but since the 1980s inequality has risen significantly. In light of this, many non-structuralists have begun to accept the argument of structuralists and Keynesians that inequality is hurting national economies. For example, the OECD "finds consistent evidence that the long-term rise in inequality of disposable income observed in most OECD countries has indeed put a significant brake on long-term growth."[40] Surprisingly, it argues that higher taxes and transfer payments do not necessarily lower economic growth; rather, they enable the poorest 40 percent to gain more education and skills that enhance social mobility. Similarly, the IMF's studies of advanced economies indicate that "if the income share of the top 20 percent (the rich) increases, then GDP growth actually declines over the medium term, suggesting that the benefits do not trickle down."[41] There is higher GDP growth when the bottom 20 percent gains a greater share of a nation's income—a finding consistent with structuralist thought.

Japan has historically been more egalitarian than most industrialized countries, but economic stagnation since the early 1990s has caused inequality to rise. Among other trends, it is harder for young workers to support Japan's rapidly aging population, and nearly 40 percent of workers are in the precariat, earning less than $20,000 a year.[42] Shinzo Abe, who served briefly as Japan's prime minister in 2007 and returned to power in 2012, has boosted stimulus spending and instituted quantitative easing, under which the Bank of Japan has bought up hundreds of billions of dollars worth of government bonds, to increase demand and growth.

Most of Latin America has seen a modest decline in income inequality since the mid-1990s, perhaps due to a preponderance of leftist governments. For example, Brazil's leftist president Luiz Inácio Lula da Silva pursued social policies such as Bolsa Família that raised incomes of the lower classes between 2003 and 2011.

In contrast, inequality has become a serious problem in China. Between 1978 and 2015, the real pre-tax income of China's top 1 percent grew by an astounding 1,898 percent, while that of the bottom 50 percent grew by 401 percent.[43] So, while most Chinese incomes were rising, they were rising much more quickly at the top. A 2015 report from Peking University based on a survey of 15,000 households found that the top 1 percent of households control one-third of China's wealth while the bottom 25 percent of households control only 1 percent of the wealth.[44]

As we indicated at the beginning of this chapter, inequality has worsened significantly in the United States. In recent years, French economists Thomas Piketty, Emmanuel Saez, and Gabriel Zucman have compiled some of the most comprehensive data on wealth inequality and national income distribution, much of which is published on the site World Wealth and Income Database (http://wid.world). Their startling findings support some of the claims of structuralists. Between 1980 and 2014, the real pre-tax income of the top 10 percent of American earners grew by 121 percent, while that of the bottom 50 percent grew by just 1 percent.[45] Simply stated, "The bottom half of the adult population has … been shut off from economic growth for over 40 years, and the modest increase in their post-tax income has been absorbed by increased health spending."[46] The bottom 50 percent of the population earned just 19.3 percent of after-tax U.S. income in 2014, while the top 1 percent earned 15.7 percent (see Figure 4.1). Emmanuel Saez estimates that the top 1 percent of Americans captured 55 percent of all the gains in income between 1993 and 2014.[47]

If we look at wealth inequality rather than income inequality, the class disparities are even starker. The median wealth (assets minus debts) of middle-income Americans (defined as households of three earning between $42,000 and $126,000 in 2014 dollars) was nearly the same in 2013 as it had been in 1983.[48] The financial crisis of 2007–2009 wiped out most of the earlier gains of this class. Meanwhile, the top 1 percent of Americans increased their share of the country's net personal wealth (assets minus debts) from 23.5 percent in 1980 to 38.6 percent in 2014 (see Figure 4.2).[49] The bottom 50 percent essentially holds no net wealth.

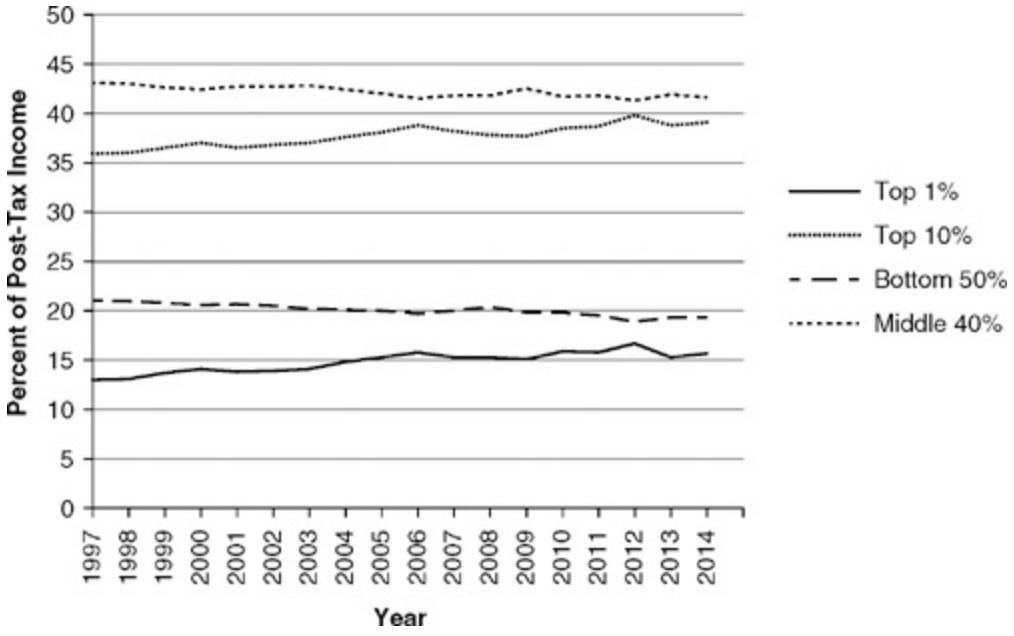


FIGURE 4.1
Proportion of Total Post-Tax Income Accruing to Different Segments of the U.S. Population, 1997–2014.

Source: Data from Thomas Piketty, Emmanuel Saez, and Gabriel Zucman, "Distributional National Accounts: Methods and Estimates for the United States," Working paper (revised July 6, 2017), Main data, at http://gabriel--zucman.eu/usdina/.

How do we explain all these trends in inequality? Many economic liberals attribute part of the rise in inequality to increased automation and other technological changes that disproportionately benefit people with the highest skills and education. In contrast, structuralists emphasize that capitalism has an inherent tendency to concentrate ownership of capital. They note, however, that changes in the balance of power between classes can redistribute income in society. In this sense, changes in inequality are as much a product of political struggles as they are a result of economic forces. Structuralists contend that the rise in inequality in industrialized countries is due in part to a strategic political campaign by capitalists to weaken labor's power, downsize the welfare state, and lower taxes on the wealthy, all legitimized by the ideology of neoliberalism. The wealthiest in the world are also skilled at tax avoidance, using legal loopholes and illegal tax evasion. Even as labor productivity has grown significantly, gains have been taken by the elites rather than passed on to workers through higher wages and benefits. The lowering of top marginal income tax rates and capital gains taxes in the United States, along with dramatic hikes in salaries of CEOs, has left the top 1 percent with much more after-tax income. Political and ideological transformation will need to occur before inequality can be lowered through tax and spending policies.

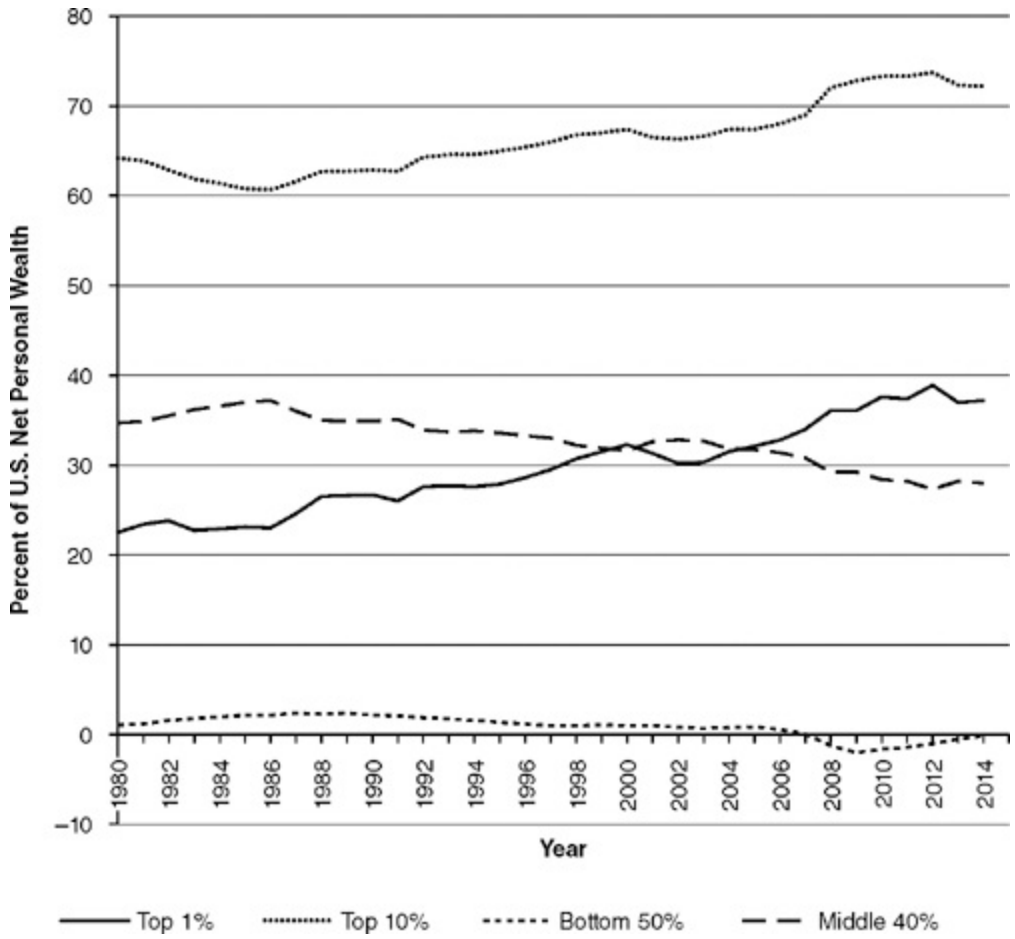


FIGURE 4.2
Proportion of Net Personal Wealth Held by Different Segments of the U.S. Population, 1980–2014.

Source: Data from World Wealth and Income Database, at http://wid.world/country/usa/.

CONCLUSION: STRUCTURALISM IN PERSPECTIVE

In this chapter, we separated Marx's four main contributions to IPE—the definition of class, class conflict and the exploitation of workers, control of the state, and ideological manipulation—from his theory of history, which predicted the inevitable collapse of capitalism and its replacement with socialism (and ultimately communism). Structuralists, drawing upon core ideas from Marxism, emphasize the class-based nature of the contemporary international political economy. One cannot understand domestic economic policies or the international political economy without recognizing the conflict derived from the division of the economic output into profits and wages.

Structuralists reject the optimistic liberal interpretation of free trade and deregulated markets, asserting instead that the disparities in power between capitalists and workers, and the rich and poor countries, produce exploitation, inequality, and poverty. The capitalist system tends to reproduce itself such that those who begin with more power and wealth are able to maintain that position at the expense of labor and the poor. Accumulation by dispossession transfers communal assets to private control, while responsibilization transfers the management of economic risks to individuals, many of whom are in the growing precariat. Theories about imperialism, dependency, and modern world systems demonstrate that, given states' vastly unequal starting places, it is naïve to believe that free markets operate on a level playing field that will somehow lead to the end of poverty. This is because key states and international institutions are seen as largely responding to the pressure of the transnational capitalist class, which seeks profits wherever they can be found.

The structuralist version of anti-globalization calls for greater unity among workers from all countries. Even Marx implied that not all decisions must be seen as beyond our collective control when he stated that "men make their own history, but & they do not make it under circumstances chosen by themselves, but under circumstances directly encountered, given and transmitted from the past."[50] Thus, for many structuralists today, a deep understanding of the economic structure *permits* the exercise of human freedom, understood as the application of human reason to the shaping of our world. Of course, not every change is possible; but some very substantial improvements almost certainly are, particularly a reduction in inequality. The precondition for such action will be the development of a new consciousness—one that sees the free-market version of globalization as simply ideological manipulation by those in power with an economic interest in perpetuating the status quo.

KEY TERMS

structuralism 72
historical materialism 73
dialectical process 73
bourgeoisie 74
proletariat 74
false consciousness 77
dependency theory 81
modern world system (MWS) 82
core 82
periphery 82
semiperiphery 82
neoimperialism 83
transnational capitalist class (TCC) 85
accumulation by dispossession 84
interlocking directorates 85
responsibilization 86
precariat 87

DISCUSSION QUESTIONS

1. Summarize the four main contributions of Marxism to contemporary structuralism.
2. What are the essential characteristics of neo-imperialism, dependency theory, and the modern world system approach?
3. To what extent does capitalism limit democracy and popular participation in political decision making?
4. Why can't the working classes effectively resist dominant forms of repression and exploitation?
5. What are some of the most important causes of and trends in inequality since the 1980s?
6. Are there realistic alternatives to the current form of global capitalism, and if so, how might they be brought into existence?

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CHAPTER
5
Constructivism



The fourteenth meeting of the States Parties to the Anti-Personnel Mine Ban Convention in Geneva in November 2015.

Source: AP Photo/Keystone/Salvatore Di Nolfi.

> *It is interests (material and ideal), and not ideas which have directly governed the actions of human beings. But the "worldviews" that have been created by ideas have very often, like switches, decided the lines on which the dynamic of interests has propelled behaviour*.
>
> Max Weber[1]

The perspectives of economic liberalism, mercantilism, and structuralism capture many, but not all, of the important elements of IPE. One of the main intellectual projects of contemporary IPE is to expand its domain to include actors, frameworks, and ways of thinking that cannot easily be classified under the three main perspectives. In this chapter we highlight some of the ways in which IPE can be more inclusive—"without fences," as Susan Strange would say—by honestly confronting a broader range of important issues without necessarily abandoning IPE's intellectual roots.

Constructivism is a vibrant theory that focuses on the beliefs, ideas, and norms that shape the views of officials, states, and international organizations (IOs) in the global system. It identifies an important role for global civil society in molding the identity and interests of actors that wield enormous economic, military, and political power. As in the case of the three dominant IPE perspectives, constructivism has many different viewpoints and variations.

Constructivists reject the realist assertion that by simply observing the distribution of

military forces and economic capabilities in the material world we can explain how states will interact. Institutions like the state, the market, or IOs are constructed in a social context that gives them meaning. How power is used, what goals states have, and how countries relate to each other depend on the ideas that actors have about those things. As actors interact, they may create or change their own identity and purpose.

Several puzzling aspects of recent U.S. foreign policy illustrate how constructivism helps us understand that threats, friends, and enemies are socially constructed. Terrorism has been perceived as a major threat to the United States since 9/11, with significant government resources spent fighting it. Between 2001 and 2014, 3,043 Americans died from acts of terrorism on U.S. soil; however, CNN points out that during this same time period, 440,095 Americans were killed by firearms.[2] Objectively, guns are a vastly larger threat to people than terrorism, and yet the fight against terrorism commands a vastly disproportionate amount of attention and resources.

Many observers have been startled by how rapidly Trump magnified threats from certain groups, cast previous U.S. rivals as friends, and alienated long-time U.S. allies. For example, even though the number of unauthorized immigrants from Mexico in the United States fell by more than 1 million from 2007 to 2014, perceptions of these immigrants as a problem grew. Even though Russia's political system and foreign policy have been based on values and interests perceived by most as antithetical to those of the United States, Trump has in many instances praised Vladimir Putin and cast Russia as a potential ally. Meanwhile, in the first few months of his presidency, Trump castigated historical friends of the United States such as Mexico, Australia, and Germany.

Constructivists help explain these puzzles by stressing that relations between countries are not simply a product of balance of power and immutable national interests. Friends and rivals are to some extent a reflection of our worldviews and our identities—that can change and be shaped through our discourse. Additionally, problems in the world are not self-evident; society chooses them and defines what it is that makes them problems—sometimes on the basis of perceptions and prejudices that are not grounded in "objective" information. In a sense, ideas and values can take on lives of their own, becoming real forces for change (or stability) in international relations.

KEY IDEAS IN CONSTRUCTIVISM

In this section, we explore the emergence of constructivism and present some of its broad ideas. Realism and liberalism have traditionally dominated IPE—particularly American IPE. They are rationalist perspectives, in that they portray actors as making strategic decisions on the basis of all available information to advance their material interests such as profit, power, and re-election. They often assert that institutions and structures constrain actors and shape their choices. Constructivist studies expanded rapidly in the field of international relations in the 1990s, focusing predominantly on human rights and security. The end of the Cold War and the upsurge in globalization changed the nature of global problems and created optimism that nonstate actors could promote a more ethical international system. Within the social sciences generally, there was an emphasis on interrogating our assumptions and recognizing that the social position of researchers shapes the knowledge they produce.

Constructivists were dissatisfied with realist assertions that the distribution of material resources is always the key determinant of outcomes in the global political system. They also disputed the assumptions of rational choice economics that actors are always self-interested and seek to maximize utility. Instead, they contended that identities that actors hold—shaped by interactions with other actors—inform their choices between right and wrong, and between appropriate and unwarranted. They found that in many cases actors will conform to social norms even when they have the power not to or when it does not benefit them materially. For example, scholars Martha Finnemore and Kathryn Sikkink developed an influential explanation of how "norm entrepreneurs" influence states to adopt and internalize new norms and values.[3] Barry Buzan, Ole Wæver, and Jaap de Wilde created an influential framework for explaining how non- military issues such as the environment and immigration come to be seen as security threats.[4] Alexander Wendt argued that the ideas states have about international politics are formed through social interactions.[5]

Although IPE has been slow to take up constructivism, by the 2000s there was much more application of it to studies of environmental issues, finance, and governance. In 2010 Rawi Abdelal, Mark Blyth, and Craig Parsons published the edited volume *Constructing the International Economy* in which they urged fellow political economists to use constructivism's insights to explain economic outcomes. Today, IPE constructivists pay significant attention to nonstate actors, focus on how ideas and identities form, and explain how the beliefs of states and international organizations change. They use more sociological and non-materialist approaches than other schools of thought. Four basic assumptions of constructivism applied to IPE are as follows:

- Ideas, norms, and identities of groups and states are socially constructed.
- Ideas and values are social forces that are as important as military or economic factors.
- Conflict and cooperation are products of values and beliefs.

- Some international political changes are driven by changes in the beliefs and identities of actors over time.

In the rest of the chapter, we introduce some key concepts in constructivism and provide many examples of how this perspective studies norms, security, and economic ideas.

Conceptual Tools

Constructivists have developed a number of conceptual tools to explain how norms and language shape outcomes in the global political economy. In this section, we look at several: problematization, framing, discourse analysis, and metaphors.

Problematization

Problematization is a process by which states and advocacy groups construct a problem that requires some kind of coordinated, international response. Constructivists argue that problems exist because we talk them into existence. Consider these questions: How do you know what you should care about or be worried about in the world? Which problems does your country focus on and which does it not? The problems we care about are a reflection of our social environment, our culture, and the beliefs we share with others in our society. They are often "constructed" by political elites and powerful lobbying organizations; we rarely choose them ourselves.

Constructivists trace the process by which "problems" become defined as problems. Today, many in the international community define the following as problems: global warming, drug trafficking, Islamic terrorism, and North Korean missiles. These "problems" are not just "out there"; they become what we make them to be through processes of deliberation. It is our perception of the problems that determines what countermeasures we will adopt against them. Some phenomena can exist for many years before they come to be defined as "problems." For example, German political scientist Rainer Hülsse points out that the OECD countries talked the money-laundering problem into existence in recent years, even though the common practice of laundering the proceeds of crime had never been perceived as a big issue before.[6] Similarly, Peter Andreas and Ethan Nadelmann note that until the twentieth century, drug trafficking and drug use were not considered crimes that required a global prohibition regime.[7] Sometimes people will construct what most of society considers as "false" problems. For example, medical experts have found no evidence that vaccines cause autism, yet a growing number of parents refuse to vaccinate their children.

Constructivists also suggest that states have choices in terms of who they identify with. Enemies have to be defined into existence. We make enemies and friends through a discursive, deliberative process informed by our culture, history, prejudices, and beliefs. Why has Iran been problematized as a pariah in the world in the last three decades? Haggai Ram argues, for example, that Israel has constructed an anti-Iran phobia, viewing Iran as posing an existential threat, in part because of completely unrelated anxieties over ethnic

and religious changes within Israeli society.[8] In a similar way, countries create enemies by projecting their own fears on others (as Trump has on immigrants) and by attributing the characteristics of monsters, madmen, and new Hitlers to leaders of other countries (such as Syria's Bashar al-Assad).

Framing

Framing is the process of defining what the essence of a global issue is: what is causing it, who is involved, what its consequences are, and what the best approach to addressing it is. All actors frame through language, reports, propaganda, and storytelling. Frames are always political constructs or lenses that may or may not be the "right way" to interpret a complex problem. Frames make us see a problem in a certain way as opposed to another, and therefore they greatly influence how we understand how we should behave toward it (see Box 5.1). By exploring framing and framers, constructivists help explain who influences the global agenda and how our approach to problems changes over time.

FRAMING CLIMATE CHANGE

For many people, climate change is a reality caused by humans. To head off an excessive rise in global temperatures, they insist there must be a reduction in carbon emissions and a switch to renewable energy sources. This framing of climate change is based on scientific methods and interpretation of scientific data. It identifies the causes and consequences of a phenomenon and recommends certain policy responses. It is the dominant frame that the Intergovernmental Panel on Climate Change espouses, and it informed the 2015 Paris climate accord and Al Gore's popular 2006 documentary, *An Inconvenient Truth*.

Nevertheless, a significant proportion of people do not accept this frame. They believe that climate change is not happening or that it is due to natural causes. They do not believe that it will be a significant risk to humans in the coming decades or that limiting carbon emissions is necessary. For example, in 115 tweets on climate change by Donald Trump since 2011, the current U.S. president describes global warming as a "canard," "based on faulty science," and an "expensive hoax."[a]

Law and psychology professor Dan Kahan writes, "Social-science research indicates that people with different cultural values … disagree sharply about how serious a threat climate change is. People with different values draw different inferences from the same data."[b] A group of communications scholars summarizes their research on climate change attitudes, showing that "how people 'frame' an issue—i.e., how they mentally organize and discuss with others the issue's central ideas—greatly influences how they understand the nature of the problem, who or what they see as being responsible for the problem, and what they feel should be done to address the problem."[c] In general, how one views climate change depends on one's social group, social identity, political identity, religion, etc. Climate change is both a "scientific fact" and a "social fact" rooted in culture and values.

International organizations and advocacy groups try to convince people of the urgency of climate change by framing it in different ways. They use frames of public health, environmentalism, risk, social justice, and morality, among many others. In addition, the Obama administration spun the U.S. response to climate change as an opportunity to boost the economy by investing in new, profitable, job-creating renewable energy industries. French president Emmanuel Macron argued that we all have a "responsibility" to combat climate change to "make our planet great again."

Some states and IOs have been framing climate change as a security threat. While scientists have defined climate change as an environmental problem through their definitive research since the 1980s, the recent "securitization" of the issue has changed the way we understand and respond to it. International relations scholar Julia Trombetta shows that by tying climate to security, the European Union, the United States, and the UN Security Council emphasize that it could cause violent conflicts,

threaten island nations, spark mass migration, and undermine food supplies. Thus framed, climate change propels them to cooperate at the interstate level by focusing on risk management, precautionary policies, and carbon emissions reductions.[d] Similarly, political scientist Denise Garcia argues that by reframing climate change as a security threat, states have come to recognize that they must work multilaterally to solve such a complex problem. In so doing, states have begun to understand security in a new way —less as safety from territorial aggression and more as ensuring global human security through mutual action and reciprocal responsibilities.[e]

References

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[b]Dan Kahan, "Why We Are Poles Apart on Climate Change," *Nature* 488 (August 12, 2012): 255.

[c]Edward Maibach, Matthew Nisbet, Paula Baldwin, Karen Akerlof, and Guoqing Diao, "Reframing Climate Change as a Public Health Issue: An Exploratory Study of Public Reaction," *BMC Public Health* 10 (2010), p. 2.

[d]Maria Julia Trombetta, "Environmental Security and Climate Change: Analysing the Discourse," *Cambridge Review of International Relations* 21 (2008): 585–602.

[e]Denise Garcia, "Warming to a Redefinition of International Security: The Consolidation of a Norm Concerning Climate Change," *International Relations* 24:3 (2010): 271–292.

For example, in early 2017 President Trump and French presidential candidate Marine Le Pen framed immigration and free trade as harmful to national vitality rather than as sources of economic growth. In another example, by framing deforestation and the loss of biodiversity as caused by corruption in poor countries, we overlook an alternative understanding that global environmental destruction is rooted in consumption patterns in rich industrialized countries. The frame that we adopt will define how we interpret our own behavior.

In the last few decades, "conflict resources" have been framed as causing some wars in Africa. Transnational advocacy groups claim that combatants in places such as Sierra Leone and the Congo gain money from control of diamonds, timber, and minerals to buy weapons used to destabilize governments and terrorize civilians. We are led to believe that conflict can be reduced by cutting off combatants' ability to sell natural resources in international markets. The Kimberley Process is one such approach to conflict reduction arising from the framing of "blood diamonds" (see Chapter 15). Critics argue that although the frame of "conflict resources" may have gotten countries and companies to "do something" about Africa, it obscured the more important reasons for conflict rooted in colonial history, ethnic rivalries, and bad governance.

Discourse Analysis

Discourse analysis helps us understand where important concepts come from and how they shape state policies, sometimes in very undesirable ways. Some constructivists trace changes in language and rhetoric in the speeches of important officials to understand the role of ideas in foreign policy. Officials talk their state's interests into existence, sometimes by adopting a discourse that resonates with important lobbying groups or sectors of public opinion. We look at three examples of foreign policy issues that constructivists have

interpreted through discourse analysis: Islamic terrorism, torture, and the clash of civilizations.

International politics professor Richard Jackson shows us that the way in which academics and states talk about problems affects the range of possibilities for actions. Through discourse analysis, he claims, we can understand the "ways in which the discourse functions as a 'symbolic technology,' wielded by particular elites and institutions, to: structure … the accepted knowledge, commonsense and legitimate policy responses to the events and actors being described; exclude and de-legitimize alternative knowledge and practice; naturalize a particular political and social order; and construct and maintain a hegemonic regime of truth."[9] He finds that an academic and political discourse about "Islamic terrorism" draws upon and reinforces historical stereotypes about Muslims, obscures understanding of the workings of Islamist movements, and paints a threat to Western civilization as so great that only counterterrorism or eradication are seen as appropriate responses to the "Enemy." This discourse has informed the European and American military responses to the Islamic State, closing off alternative understandings of how and why the militant group arose.

Richard Jackson has also used discourse analysis to explain how political elites in the United States repeatedly used a "highly-charged set of labels, narratives and representations" in such a way that "the torture of terrorist suspects became thinkable to military personnel and the wider public."[10] In other words, official U.S. public discourse in the 2000s created the conditions for a "torture-sustaining reality" in the United States by using language that dehumanized suspected terrorists and made the public—despite minority opposition—willing to accept the necessity to abuse them. Without assessing the power of this discourse, it is hard to explain how the United States could adopt a set of practices so at odds with its moral values.

Similarly, constructivists have analyzed how political scientist Samuel Huntington's concept of the *clash of civilizations* became a popular way in the 1990s to explain the roots of global conflicts. The more this clash of civilizations rhetoric was used to describe relations between countries, the more it became a sort of self-fulfilling prophecy that constructed conflict itself. In effect, the clash exists because we believe it exists and we act on that belief. The clash discourse has become accepted as the truth—a causal explanation—even in the face of overwhelming social scientific studies that find no significant link between religious beliefs and terrorism and that point out the difficulty in even ascribing a common set of values to huge groups of people like the "Islamic world" or the "West."

Analyzing Metaphors and Categories

Closely related to discourse analysis is the study of metaphors and categories that we apply to things in the social world. Constructivists note that, although we often choose metaphors and categories without political intent, sometimes ideologically motivated actors deliberately "code" the social world with the intent of changing it. For example, the European countries that had the worst debt crisis in 2010—Portugal, Italy, Ireland, Greece,

and Spain—were lumped together under the undignified acronym "PIIGS" to imply that they had bad economic policies. Samuel Brazys and Niamh Hardiman find that repeated use of the term "PIIGS" in the media in 2009 and 2010 associated all five countries with economic crisis and peripheral status, masking significant economic differences between the countries.[11] Initially the term was "PIGS," but an "I" was later added for Ireland. After this happened, the Irish-German bond yield spread increased, thereby exacerbating Ireland's financial troubles. Perceptions of similarities between countries in PIIGS—even though not based on well-founded economic data—caused financial markets to treat them as similarly risky, worsening the Eurozone crisis.

Jim O'Neil, a former chief economist of Goldman Sachs, coined the acronym "BRICs" in 2001 to refer to the large industrializing countries of Brazil, Russia, India, and China (after 2010, some changed it to the "BRICS" by adding South Africa). The term—with its metaphorical suggestions of solidity and construction associated with "bricks"—caught on and is widely used today, even though the countries have very dissimilar economies. By the late 2000s, the four countries were actually coordinating some initiatives as if were a distinct bloc.

Similarly, Robert Ward, the editorial director of the Economist Intelligence Unit, coined the term "CIVETS" in 2005 to refer to the emerging markets of Colombia, Indonesia, Vietnam, Egypt, Turkey, and South Africa. Several investment banks began offering funds that invested in the CIVETS (a civet is a cat-like animal that produces a musk used in perfume). The *Financial Times* journalist Elaine Moore states that although terms like CIVETS "have been backed up by economic analysis, they have also been criticised as marketing ploys to make investors feel more relaxed about putting money in countries they know relatively little about."[12] All of the groupings of countries are essentially arbitrary, but once the metaphorical terms become widely used, many people come to believe that there are commonalities among the countries, and they act on this belief, whether it is in the form of investors putting money in a CIVETS fund or leaders of the BRICS establishing a multilateral New Development Bank to fund infrastructure projects. As Brazys and Hardiman argue, terms such as BRICs and PIIGS "not only shape the way we think about and discuss groups of state actors in the global economy, but do so in ways that have real consequences for the markets' treatment of the countries in question."[13] The key point to remember is that how we categorize things and the words we employ to make sense of them have consequences.

DYNAMICS OF NORMS

Constructivists have made an important contribution to IPE by explaining how norms influence the behavior of states and markets. Martha Finnemore and Kathryn Sikkink state the common definition of norms as "standard(s) of appropriate behavior for actors with a given identity."[14] Constructivists believe that norms guide the choices of states and international organizations by constraining their understanding of what is "normal" vs. "aberrant," right vs. wrong, and acceptable vs. out-of-bounds. Because norms are shared values, it can be difficult for a state to violate them without threatening its own identity and risking opprobrium from other states. Many international norms are well known. For example, the norm of state sovereignty is a shared belief that every state has the right to exercise exclusive control over its own laws and territory. And a human rights norm enshrined in the UN's Universal Declaration of Human Rights (Article 3) is that "everyone has the right to life, liberty and security of person." In this section we introduce constructivist ideas about how global norms emerge, spread, and (sometimes) wither away.

Models of Norm Life Cycles

Finnemore and Sikkink have presented an influential model of three stages through which international norms typically go.[15] First, "norm emergence" occurs when norm entrepreneurs frame an issue and convince a core set of states to champion a norm. Second, once a critical mass of states brings the norm to a tipping point, a "norm cascade" kicks in, whereby previously reluctant states in quick succession formally accept the norm, often because they want other states to see them as legitimate members of the international community. Finally, as all states "internalize" the norm, it gains a taken-for-granted quality and there is no longer much international debate about it. States willingly comply with the norm because they view it as appropriate and moral.

Influential constructivists Margaret Keck and Kathryn Sikkink complement this model by explaining how norms spread around the world.[16] They specify how transnational advocacy networks (TANs) spread information, employ powerful symbols, leverage the power of sympathetic states, and hold states accountable for adhering to norms. They also describe a "boomerang pattern": if domestic groups in a country cannot convince their government to accept a norm, they work with international groups in their network to lobby other governments and IOs to put pressure on the reluctant government to bind itself to the norm.

Thomas Risse, Stephen Ropp, and Kathryn Sikkink add a "spiral model" to the study of norms.[17] In the area of human rights, they observe that an authoritarian state will often deny that it is violating human rights or claim that the norm of human rights is superseded by some other norm, before eventually making tactical concessions in the face of international pressure. Eventually, the state liberalizes, starts to internalize the norm of human rights protection, and finally adheres to it in practice. The spiral model has been

influential because it explains the process by which states are socialized to comply with a variety of international norms, even if those norms initially conflict with the states' material or political interests.

Actors That Spread Norms

A variety of international actors spread norms and try to socialize states to behave in conformity with them. We will focus on three "actors" that feature prominently in constructivist literature: transnational advocacy networks, epistemic communities, and IOs.

Transnational Advocacy Networks

Political scientists Margaret Keck and Kathryn Sikkink coined the term transnational advocacy networks (TANs) to describe "those actors working internationally on an issue, who are bound together by shared values, a common discourse, and dense exchanges of information and services."[18] These interconnected groups include NGOs, trade unions, the media, religious organizations, and social movements that frame new issues and try to get states to accept new norms and interests, often involving "rights" claims. TANs act as "norm entrepreneurs," using testimonies, symbolism, and name-and-shame campaigns to create a shared belief among political elites that, for example:

- Human rights protection is a state obligation.
- Torture is never acceptable.
- Debt relief for poor countries is "the right thing."
- Human trafficking is a new form of slavery.

According to Keck and Sikkink, TANs rapidly communicate information, tell stories that make "sense" to audiences far away from a problem, and hold states accountable for the principles that they have already endorsed in their own laws and international treaties.

The International Campaign to Ban Landmines (ICBL) demonstrates how TANs can successfully reframe issues. Antipersonnel landmines (APLs) have a long history of use in conventional wars and low-intensity conflict settings. They were particularly popular during the 1970s and 1980s, when insurgent groups took advantage of their low price and ease of use. After the Cold War, many considered APLs to be unacceptable weapons because they "do not distinguish between civilians and combatants; indeed, they probably kill more children than soldiers."[19] With publicity from such celebrities as Princess Diana and Linda McCartney, the ICBL rapidly gained popularity after 1991 and convinced the UN in 1997 to establish the Convention on the Prohibition of the Use, Stockpiling, Production and Transfer of Anti-Personnel Mines and on their Destruction—known more commonly as the Mine Ban Treaty.

Among the factors that led to its quick ratification were the efforts of treaty supporters to change the views of the security officials in different states regarding the need for landmines. During the campaign, the International Committee of the Red Cross commissioned a retired British combat engineer to analyze the military utility of APLs; he

found them not to be as useful as had often been assumed. NGOs also informed the public and state officials of the horrible effects of APLs, including the loss of a leg or arm by civilian noncombatants. In addition to lobbying, the ICBL shamed officials who resisted the discontinuation of landmines. In 1997 the ICBL was awarded the Nobel Peace Prize for its work. As of 2017, 162 countries had ratified the Mine Ban Treaty (although Russia, China, India, and the United States are not signatories). The treaty significantly lowered global deaths from landmines and led to the destruction of at least 50 million stockpiled landmines.

Epistemic Communities

Other nonstate actors that diffuse ideas internationally are "epistemic communities," defined as "professionals with recognized expertise and competence in a particular domain and an authoritative claim to policy-relevant knowledge within that domain or issue-area."[20] These global networks of experts—often scientists—have detailed knowledge about complex issues and share common understandings of the truth about these issues, based on the standards of their profession. Although epistemic communities are not political actors in a formal sense, political elites rely on them for advice and policy options. Thus, these experts can have the ability to "educate" power holders about what problems exist, how important they are, and even what can be done about them.

For example, Peter Haas has shown how atmospheric scientists around the world studying the ozone layer disseminated the consensus scientific evidence about the effects of chlorofluorocarbons (CFCs) on ozone depletion. In coordination with colleagues in the UN Environmental Programme and the U.S. Environmental Protection Agency, scientists provided an impetus to international negotiations on the Montreal Protocol to ban CFCs. Similarly, Haas points out that many international regimes that regulate global environmental problems such as climate change and acid rain have come about through a process in which epistemic communities teach policy elites and international institutions the scientific consensus on environmental issues. In other words, epistemic communities provide political negotiators "usable knowledge"—defined as knowledge having credibility, legitimacy, and saliency—that persuades them to adopt sustainability treaties even though the negotiators may have been politically reluctant to do so initially.[21]

There are many other epistemic communities, ranging from arms-control experts to development experts. Networks of economists spread the ideas of John Maynard Keynes in the 1930s and 1940s, laying the foundation for trade and financial policies adopted at Bretton Woods after World War II. Similarly, Latin American economists (sometimes called the "Chicago Boys") had an important role in spreading neoliberalism in their home countries in the 1980s. Analyzing the ideas these economists were socialized to believe in during graduate school in the United States, political scientist Anil Hira shows how they formed "knowledge networks" that rationalized the adoption of structural adjustment policies in Chile and other Latin American countries in the 1980s.[22]

International Organizations

In addition to TANs and epistemic communities, international organizations also socialize states. In other words, IOs help shape what a state *is* (its identity), *wants* (its interests), and *does* (its policies). The knowledge and expertise that IOs have tend to give them legitimacy. IOs that constructivists have studied include the International Committee of the Red Cross (ICRC), the World Bank, and the United Nations. Martha Finnemore finds that individuals in the ICRC over many years convinced states that they should abide by humanitarian limits during war.[23] A number of states have internalized and followed these norms of wartime behavior, even though they would have more immediate success by flouting them. Some IOs use technical assistance and training programs as ways to diffuse norms.[24]

Although the general public often perceives the UN as weak and ineffectual, it has had an important role in spreading norms of gender equality and women's empowerment. Its panoply of conferences, commissions, and protocols has not changed gender policies overnight, but it has set the stage for states to engage in a dialogue about women's rights when they otherwise might not have. As the belief has spread that a respectable, "modern" member of the international community must accept the goal of greater gender equality, recalcitrant states find it ever more costly and isolating to resist the gender mainstreaming discourse.

Constructivists also point out that states often find themselves constrained by their own self-proclaimed values. Martha Finnemore points out that a "unipole" like the United States spreads liberal norms in an effort to legitimize its own behavior and reinforce its soft power.[25] It was very successful in doing so through the Bretton Woods institutions. However, the United States weakens its soft power when it violates the very principles it has convinced its own people and other countries it stands for. For example, the United States was viewed as hypocritical for proclaiming its values of humanitarianism but breaking them by enforcing sanctions on Iraq from 1991 to 2003 that caused many civilians to die. And while proclaiming the importance of international law, the United States launched military action against Serbia in 1999 and Iraq in 2003 without the formal sanction of the UN Security Council. States are haunted by their own principles and are usually less likely to violate them when they might lose legitimacy or be accused of hypocrisy.

Norm Life Cycles

Constructivists have applied models and concepts to explain the emergence, diffusion, and life cycles of a wide range of international norms. By looking at examples from the IPE literature, we hope that readers will better appreciate the role of ideas in shaping international dynamics.

Political scientists Devin Joshi and Roni Kay O'Dell explain how, beginning in the 1990s, the United Nations spread a new understanding of international development that was not focused solely on economic growth.[26] The norm of "human development" emerged in part out of the writings of Indian economist Amartya Sen, who viewed

development as requiring the expansion of human capabilities and freedoms. In 1990 the United Nations issued its first annual Human Development Report (HDR), which championed ideas such as democracy, human rights, gender equality, cultural diversity, and market regulation. The HDR includes a Human Development Index (HDI) that seeks to measure human capabilities. Joshi and O'Dell find that newspapers around the world have played an important role in diffusing and legitimizing ideas in the HDRs and the HDI, "thereby challenging older ideas that development is identical to indicators such as GDP and PCI [per capita income]."[27]

At the heart of the global debt regime is a norm that sovereign borrowers (i.e., states) have to pay back their loans. It doesn't matter if the loans were incurred by a previous regime or government—the norm of "sovereign debt continuity" still applies. Law scholar Odette Lienau traces how this norm came to prevail in international finance—to the point of being taken for granted—in the post-World War II period.[28] The norm is based on a particular notion of state sovereignty and on how creditors are organized. But it seems unfair that, following a social revolution or overthrow of a dictatorship, the successor government is responsible for prior debts. What if the populace never consented to or benefited from the previous government's debt? What if lenders should have known that their loans would be squandered by corrupt elites? These cases could justify repudiation or forgiveness of debt incurred by a government's predecessors on the basis that it is "odious." Since the 1990s, according to Lienau, alternatives to the debt continuity norm have begun to emerge based on political discourses stressing good governance, democracy, and popular sovereignty. Lienau's point is that the norm of sovereign debt continuity is a construct grounded in political ideas and historical circumstances; a new norm of "odious debt" is in the making as a result of changes in political values and notions of fairness. As a result, there is a possibility that elimination of debt inherited from corrupt, authoritarian regimes will become more widely accepted.

Many constructivists have studied how norms affect the ways in which global environmental problems are managed. Canadian political scientist Hevina Dashwood shows why Canadian mining companies framed their policies of corporate social responsibility with the norm of "sustainable development."[29] The spread of the idea of sustainable development in the 1990s by NGOs and some national governments helped convince mining companies to get serious about corporate social responsibility. Dashwood argues that the companies spearheading the adoption of sustainable development had leaders who believed it was the right thing to do. They acted as norm entrepreneurs, pushing for higher standards within industry associations and socializing other mining company executives. By the mid-2000s a tipping point was reached, after which a norm cascade led the majority of mining companies to adopt corporate social responsibility policies.

Dashwood acknowledges that companies may start talking up a norm for the purpose of public relations, not really believing in it. But a key constructivist point is that the practice of discussing a norm "as if" it matters and "going through the motions" of caring often habituate actors to a norm. As Dashwood states, "Policies that were initially adopted for

instrumental, strategic reasons, may subsequently be sustained through conviction of their normative validity. Firms' identities may be transformed where they wish to be seen as good corporate citizens, as opposed to corporate pariahs."[30] Nevertheless, many mining firms have not yet gone through the last stage of the norm cycle, which is internalization of the norm. This would require moving from talk to action, i.e., reaching a point where the norm becomes so much a part of the DNA of the company that it actually changes its practices.

In recent years, the public has become more concerned with the ways that multinational corporations (MNCs) operate outside of their main consumer markets in developed countries. Civil society groups want more information about the global supply chains of MNCs, in part so that consumers can make more informed choices when purchasing goods. Lena Partzsch and Martijn Vlaskamp argue that a new "foreign accountability norm" has emerged that holds MNCS "accountable for socially and/or environmentally harmful practices regarding natural [resource] extraction abroad."[31] The norm creates the expectation that companies will exercise due diligence within their supply chains to identify and minimize the risks of contributing to illegal logging, human rights abuses, and armed conflict. The norm holds MNCs accountable for their own conduct and the conduct of their suppliers in foreign countries. It is now less acceptable for a company to be willfully ignorant of where its supplies ultimately come from.

Partzsch and Vlaskamp follow the foreign accountability norm's life cycle through the stages of norm emergence, norm cascade, and norm internalization. The NGO Global Witness and the liberal think tank Center for American Progress (via its Enough Project) have put pressure on producers of computers and cell phones to avoid conflict minerals such as gold, tantalum, and tungsten from uncertified mines in the Democratic Republic of the Congo and surrounding countries. Some industry groups representing MNCs have also spread the norm. It has been incorporated into some laws, including the 2008 U.S. Legal Timber Protection Act and the 2010 EU Timber Regulation. The 2010 U.S. Dodd-Frank Act requires importers of gold, tungsten, tin, and tantalum ores to report if the ores originate in the Democratic Republic of the Congo and neighboring countries and to report what due diligence they undertook to ensure that the minerals from these areas did not fund armed groups. In 2017 the EU approved a similar Conflict Minerals Regulation. The foreign accountability norm has affected commercial relationships in global supply chains and reinforced the trend toward third-party certification of goods such as conflict-free diamonds, fair-trade coffee, and dolphin-friendly tuna.

Contestation of Norms and Norm Death

As the literature on norms has grown, scholars have identified some of its limitations and sought to extend constructivist thought to new issues. One prominent criticism of constructivists is that they tend to study norms that have successfully been accepted at the global level but ignore norms that never made it to the stage of a norm cascade, let alone internalization. International relations constructivists have focused especially on cases where

norm entrepreneurs successfully spread liberal Western norms regarding human rights, the environment, and arms control. But we are now more aware that norm entrepreneurs promote many norms that fizzle out. An adequate theory of norm life cycles requires us to account for why many new norms stall.

Political scientist Charli Carpenter seeks to understand why some issues of human security lead to the construction of global norms but other issues turn out to be "lost causes" that never capture the attention of global leaders.[32] For example, norms against the use of "killer robots," child soldiers, and landmines have widespread international support, but norms to prevent male circumcision and language extinction have little traction globally. Similarly, Carpenter points out that a communicable disease like HIV/AIDS is at the top of the global health agenda, while "tuberculosis and Type 1 diabetes get only limited attention; nondisease health issues such as maternal mortality and the right to pain relief get even less."[33] Why do some normative ideas thrive while others remain marginal? In the area of human security, Carpenter argues that powerful organizations like Amnesty International, the Red Cross, and Human Rights Watch have to "adopt" the new ideas in order for them to have a chance of being turned into global norms. Well-established NGOs and UN agencies are "gatekeepers" that determine what issues will lead to campaigns for global agreements on norms. The organizations decide what "matters" and play a key role in framing how elites and the general public understand human security problems. They tend to adopt issues that have obvious victims and perpetrators, emotional appeal, and credible solutions.[34] Constructivists in general believe that problems are socially constructed in a politicized process; from the large pool of issues that could be identified as human security problems, only a few will make it to the international agenda.

Like Carpenter, Australian international relations scholar Alan Bloomfield urges us to pay greater attention to cases where there is a failed attempt to change status quo norms. He argues that "norm antipreneurs" sometimes successfully prevent normative change. He sees antipreneurs as often having a strategic advantage when emerging alternative norms have little credibility or socio-institutional support.[35] For example, state antipreneurs have an advantage when they can exercise vetoes in existing institutions or defund institutions that are receptive to new norms.[36] Context matters for whether antipreneurs can thwart normative change. In the face of war, financial crisis, or rapid technological change, norm entrepreneurs have a greater window of opportunity to overcome antipreneurs' resistance.

Political scientist Clifford Bob has studied many antipreneurs that act globally.[37] He explains how the U.S. gun lobby has allied with conservative groups and sport-shooting groups in the Global South to resist norm entrepreneurs who are promoting global gun control. He also examines how Western evangelical Christians and other conservative religious groups have allied with the Vatican and governments of Muslim-majority countries in an informal "Baptist-Burka" network to resist laws and norms promoting toleration of homosexuality. Bob stresses that right-wing TANs act just like progressive TANs to promote and resist norms, drawing on scientific expertise and using framing, rhetorical strategies, and counter-shaming.[38] He sees conflicts between rival issue

entrepreneurs as constantly "peppered with hyperbole and Manicheanism."[39] As they interact through language, "both sides shape one another's demands, behavior and identity."[40]

Realist scholars have criticized constructivists for overestimating the power of ideas and norms. They argue that states often adopt new norms not out of moral conviction but because the norms will promote their self-interests. In response, constructivists increasingly accept that we should examine how norms interact with material calculations and institutional dynamics to alter state behavior.

Critics also claim that constructivists overlook the many ways in which states conveniently ignore norms that they have formally accepted. There are many examples of states breaching norms in times of crisis or when it serves the interests of policy makers. Constructivists counter that violations of norms are not necessarily evidence that the norms are irrelevant. States may violate widely accepted norms less frequently or may do so only temporarily in order to minimize international opprobrium. More recently, constructivists also stress that states and local communities may "practice" norms differently, depending on their domestic institutions and local context.[41] In other words, states may have different interpretations of what a norm means and in what context it is applicable; thus they may implement the norm differently without necessarily intending to reject it. These instances of different practice can actually be productive if they lead to international debates that clarify a norm.

Finally, constructivists have been criticized for implying that in the last fifty years or so the developed countries have inexorably adopted more progressive global norms. For example, Ryder McKeown argues that the norms literature overly focuses on "nice norms" and fails to consider that norm-induced moral change "may be shallow and fleeting."[42] The recent rise of populism and trade protectionism is a reminder that societies can also reverse liberal norms.

Some constructivists have tried to explain why democratic states in particular are willing to violate norms that were previously deeply entrenched. In other words, how is it that something unthinkable becomes thinkable and do-able by a state? Julia Schmälter explains how the European Union has eroded its long-supported belief that there is a "collective responsibility to protect people in need of international protection from persecution or serious harm in their home countries."[43] In the face of the current refugee crisis, the EU has made it difficult for refugees to exercise the right to seek asylum by quickly returning them to their home or transit countries and making it much more difficult to even get to the EU in the first place.

Finally, Christopher Kutz describes a process he calls "norm death." For at least two decades before 2001, the United States had strongly supported and adhered to norms prohibiting assassination and interrogatory torture. The categorical prohibitions, claims Kutz, were derived from values of military honor and human dignity. After 9/11, civilian leaders shifted to a utilitarian logic, emphasizing the U.S. right to self-defense and calculating how many U.S. lives could be saved if torture and targeted killings were used.

Kutz fears that the death of the anti- assassination norm and the normalization of drone-based killing can cause more interstate violence by "lowering the bar in terms of when state interests justify war."[44]

CONSTRUCTIVIST VIEWS ON CONFLICT, COOPERATION, AND SECURITY

Whereas realists argue that the balance of power conditions states' behavior, constructivists suggest that conflict or cooperation between actors is a product of their different values, beliefs, and interests. One of realism's central assumptions is that a potentially anarchic "self-help" world forces all actors to make security their first priority, lest they be attacked by others. Realists contend that social factors such as beliefs and values will always be overwhelmed by the structural realities of an anarchical, self-help world.[45]

In contrast, constructivist Alexander Wendt argues that "structure has no existence or causal power apart from processes. Self-help and power politics are institutions, not essential features of anarchy. Anarchy is what states make of it."[46] In other words, for Wendt, we do live in a self-help world only because over time states have come to "believe" that self-help is a consequence of anarchy.

Constructivists have found that sometimes seemingly implacable rivals cooperate because they come to have a shared understanding that they are part of a "security community"—a group with a sense of shared moral purpose and mutual trust. Israeli political scientist Emanuel Adler looks at how the Organization for Security and Co-operation in Europe (OSCE), set up in the mid-1970s as a process by which the Cold War sides could cooperate on security matters in Europe, eventually became a transmission belt for liberal ideas about freedom of the press, arms control, and protection of human rights.[47] Interactions within the OSCE between governments, NGOs, and experts spread a new idea that how a country treats its citizens within its own borders is a legitimate diplomatic concern of other states.

This idea conflicted with traditional notions of state sovereignty, opening up the way for cooperation on security issues and constraining states in the Warsaw Pact, perhaps even supporting their prodemocracy movements. After the collapse of the Berlin Wall, the OSCE helped convince Eastern European states to commit to free elections and protection of minority rights. Constructivists argue that the OSCE shapes what a "normal" European country believes are its obligations to other states and its own citizens, irrespective of the country's historical rivalries or military power. As more states formally commit themselves to these obligations and discuss them, it becomes harder to violate them—not so much because of the "costs" of doing so but because of the shock it would pose to a country's own identity.

When it comes to weapons of mass destruction like nuclear and chemical weapons, constructivists help us understand why powerful states have not used them since World War II, despite these weapons' obvious military utility. International relations scholar Nina Tannenwald analyzes the "nuclear taboo"—the strongly held norm among the permanent members of the Security Council that first use of nuclear weapons is unthinkable.[48] Even Israel and India, which face neighboring enemies, have apparently internalized the norm that the use of nuclear weapons would be morally unacceptable. Tannenwald argues that

the acceptance of the taboo—generated by a grassroots antinuclear weapons movement around the world—is what constrains states from employing nuclear weapons more than the fear that an enemy would retaliate with devastating effects.

Similarly, international relations theorist Richard Price looks at how use of chemical weapons by Great Powers has become almost unthinkable. The stigmatization of their use is at odds with their obvious effectiveness. Price explains how nonuse springs from a country's understanding of itself: "Abiding by or violating social norms is an important way by which we gauge 'who we are'—to be a certain kind of people means we just do not do certain things."[49] The widespread condemnation of Bashar al-Assad's regime for using chemical weapons in 2013 and 2018 demonstrated the power of the chemical taboo.

National Identity and Foreign Policy

Constructivists expect national identity to shape a state's interactions with other states. A state's identity has many elements, some of which may be contradictory, and the identity can change over time. Presumably, political elites who make decisions affecting international relations have been socialized into the identity that circulates within their nation-state. Identity can be rooted in language, ethnicity, and religion, but also in understandings of what the political, social, or economic essence of one's country is. For example, a state might have an identity as a Western liberal democracy, a peaceful rising power, or an Islamic republic. It is important to note that a state might invoke different elements of its identity with different countries.

International relations scholar Ted Hopf argues that domestic identity shapes a country's foreign policy. He also claims that the masses' belief systems constrain how elites behave. Identity relations between states will shape how they understand each other's actions and behave toward one another. States could understand themselves and other states on the basis of religion, level of 'civilization,' enduring enmity, and enduring amity (among other bases).[50] For example, Hopf states, "We would hypothesize that whether or not a country identifies with capitalist modernity would be an important predictor of environmental treaty ratification, as would the centrality of scientific ideas to a country's identity."[51] He adds, "Once one has uncovered a prevailing discourse of national identity, one can expect that discourse to both persist over time and explain a broad range of outcomes, regardless of who is making foreign policy in that state."[52] (See Box 5.2 for a discussion of how U.S. worldviews affect U.S. policies toward China.) For example, one might explain the long-enduring friendship between the Anglosphere countries (the United States, the United Kingdom, Canada, Australia, and New Zealand) as based in "identity relations that make the use of force against one another virtually unthinkable."[53] Similarly, identity relations might explain why large German investments in the United States are seen as unremarkable, but an effort by a Dubai company, Dubai Ports World, to buy a U.S. port operator in 2006 evoked strident opposition in the U.S. Congress.

U.S. WORLDVIEWS OF CHINA

Many realists predict that established states will use force against rising states, or at least seek to balance against them. Realist political scientist John Mearsheimer has stated adamantly that the United States and China will enter into a security competition. Because China will inevitably become more aggressive as it seeks regional hegemony, the United States, with Asian allies, will try to slow its rise, leading to potential war.[a] A more liberal realist, Charles Kupchan, expects the rise of China to produce a multi-polar world order in which China will have much more influence in international institutions but will not necessarily become democratic.[b] He believes that cooperation between the West and China is possible, even if liberal international norms do not remain dominant. Cooperation will become more likely, he asserts, if the United States comes to understand that its values and models of governance, capitalism, and modernity are not universal.[c]

Chengxin Pan, an international relations scholar at Australia's Deakin University, provides a deeper constructivist understanding of how the worldviews of American elites shape U.S. foreign policy towards China. He argues that many U.S. government officials and American mass media outlets see China as a threat. This "cognitive habit" focuses on the dangers of China's military rise and on how China is undermining the U.S. economy. In contrast, another group of U.S. officials and businesspeople view China as an opportunity—a large export market and a place to make handsome profits from offshore production. They expect that the more China is integrated into multilateral institutions, the more it will become a "responsible stakeholder" in the world.[d]

American actors use the (perceived) China threat to advance their domestic political and economic interests. For example, organized labor blames corporations for unpatriotically siding with China and demands protection from unfair competition, while big business uses the China card to extract wage concessions from workers. The military–industrial complex also lobbies for high military spending to keep ahead of China's growing military capabilities. Pan even argues that Sinophobes in academia and think tanks constitute an epistemic community that supports fearmongers in government and "lays the foundation for military Keynesianism."[e]

The discursive effect of the China threat is to create a self-fulfilling prophecy wherein containment is the logical foreign policy response.[f] American discourse and containment moves (in the South China Seas, for example) evoke a nationalistic Chinese response, which in turn boosts the China threat discourse in the United States. American and Chinese actions are co-constituted; each country responds to the other's worldviews. Pan's constructivist claim is that there is no pre-determined enmity between the two countries; instead, "perceiving China as a threat and acting

upon that perception help bring that feared China threat closer to reality."[g] Ultimately, the representation a country makes of another is never fully objective; rather, it reflects the "self-imagination, desire, and power" of the country making the representation.[h]

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[c] Charles Kupchan, "America's Place in the New World," *New York Times*, April 7, 2012.

[d] Chengxin Pan, *Knowledge, Desire and Power in Global Politics: Western Representations of China's Rise* (Cheltenham, UK: Edward Elgar, 2012), p. 38.

[e] Ibid., pp. 76–77, 82.

[f] Ibid., pp. 86–87.

[g] Ibid., p. 105.

[h] Ibid., p. 148.

We can see identity playing an important role in U.S. relations with the Middle East. For example, if the United States invokes its identity as Western, secular, and democratic in contradistinction to a Saudi Arabia it understands as Muslim, authoritarian, and unfriendly, it may perceive dependence on oil imports from Saudi Arabia to be a potential security problem. In contrast, if the United States and Canada share a similar identity, then the United States may not view dependence on Canadian oil imports as a threat to national security. As political scientist Sebastian Herbstreuth argues, because the United States has a "moral geography" that represents the Middle East as a hostile cultural "Other," it views dependence on oil imports from the region as a danger.[54] Similarly, British international relations scholar Greggorio Bettiza shows that by imagining the Muslim world as a distinct community, U.S. experts have drawn a boundary between it and other imagined civilizations, providing a frame of reference through which to interpret events in Muslim-majority countries and, in some cases, justifying violent actions against it.[55] U.S. foreign policy might be very different if American experts adopted non-civilizational discourse to conceptualize people with different identities.

Securitization

A significant body of work with constructivist underpinnings is securitization theory—also known as the Copenhagen School—which emerged in the late 1980s and was popularized by Barry Buzan and Ole Wæver. Securitization occurs when elites, through discourse, construct an issue as a security threat; if the public agrees with the discourse, leaders can undertake exceptional measures against the security problem—such as suspending civil liberties—that the public wouldn't normally sanction. Issues like immigration, the drug trade, cyber hacking, and climate change can be securitized even if they don't have a military dimension. What is important for securitization is that elite groups use speech acts

to define a problem as an existential threat to the state or society, and that a community collectively accepts the security framing. Constructivists often use discourse analysis to explain how securitization occurs.

Securitization can be problematic when it diverts us from understanding problems through alternative frames. For example, we could view the drug problem primarily as a public health issue, or we could frame immigration as an economic benefit to destination countries. Securitization often causes governments to address an issue with military and law enforcement instruments that may be inappropriate or expensive compared to alternative instruments. During the 2016 presidential campaign, Donald Trump tried to securitize Muslims and Latin American immigrants. While many Americans did not accept this discourse, enough did to lend momentum to extraordinary measures President Trump proposed or enacted, such as building a wall on the Mexican border and preventing many Muslims from traveling to the United States. Critics argue that these measures, which they view as costly responses to non-existent security threats, will provoke countermeasures from others overseas that will weaken the ability of the United States to achieve its foreign policy goals.

Securitization of migration in Europe, about which much has been written, connects to debates in the European Union about crime, the welfare state, and cultural identity. Jef Huysmans argues that, among other things, securitization "renders suspicion into an organizing principle of sociality through diffusing uncertainties and risks."[56] Thus, securitization and the security practices that accompany it, such as surveillance, alter how we interact in society and potentially harm democracy. In contrast, securitization of some issues, such as infectious diseases and climate change, doesn't necessarily lead to a militarized response; it can raise the priority of the issues and compel states to mitigate potential risks in the future. Because securitization affects what resources a state will use and how, it has implications for government spending. For example, an expected peace dividend after the Cold War never materialized in the United States; arguably, supporters of the military–industrial complex "constructed" new security threats such as terrorism, Iraq, the Taliban, China, and failed states in order to keep Congress from slashing the defense budget.

We can also securitize an anticipated future event. Geographer Andrew Baldwin identifies two narratives about large-scale human migration caused by climate change. Each narrative "authorizes a different politics."[57] A "sovereigntist" narrative casts migration caused by climate change as a future threat to national security and international order, requiring states to prepare now to strengthen borders or use military force. A "liberal" narrative sees climate-induced migration as a development problem that will necessitate better international governance and acceptance of managed migration. How we imagine the future (which is not yet a reality) affects the actions states will take today. Similarly, international relations scholar Maria Julia Trombetta says that to securitize climate-induced migration is to turn its victims into perpetrators, while to frame this migration as a human security issue is to emphasize protecting vulnerable people.[58]

ECONOMIC IDEAS IN CONSTRUCTIVIST IPE

Economic ideas strongly shape government policies. Constructivists seek to explain from where these ideas originate and how they become accepted by states and IOs as the self-evident justification of policies. This may require studying the influence of academic economists, treaty negotiations, or internal deliberations of a big organization like the World Bank. Although many competing ideas float around in the policy world, those that become dominant are very resistant to change. Sometimes it takes a traumatic event—a war, a financial crisis, or the collapse of the Berlin Wall—to get organizations to accept alternative ways of viewing the world and defining their role within it.

The Power of Economic Ideas

John Maynard Keynes's ideas spread rapidly after World War II and became the underpinning of the Bretton Woods institutions (see Chapter 2). But a new neoliberal discourse rose to challenge these ideas in the 1970s and 1980s, spread by American economists who constructed a different worldview about the role of the state in an economy. The IMF in particular spread the notion that capital mobility—i.e., unrestricted flows of private capital across borders—was a necessary policy for every state that wanted to develop rapidly. IPE scholar Jeffrey Chwieroth finds that IMF staff—made up mostly of economists—brought to the IMF neoclassical economics ideas that they had been trained to believe in during graduate school.[59] The organizational culture in the Fund privileged economic theory, which had turned against Keynesianism and capital controls by the 1970s. Chwieroth's broader point is that the preferences of international organizations are shaped in part by intra-organizational processes in which culture, beliefs, and expertise of staff are important. However, shocks such as the 1997 Asian financial crisis and the 2007–2008 global financial crisis increased opportunities for New Keynesians among the IMF staff to endorse capital controls in certain conditions. In the 2000s there were more disagreements among staff, also reflecting changing ideas within the economics profession about what unfettered markets lead to.

Similarly, in the 1990s the World Bank began to change some of its views on development in the face of sustained efforts by TANs, which slowly convinced it that promoting environmental and social norms like sustainable development, poverty alleviation, and gender equality were part of its mission—indeed even critical to its own identity and purpose as an organization.[60] Political scientist Catherine Weaver argues that the World Bank's thinking on what is necessary for development has shifted somewhat from neoliberal orthodoxy to ideas about good governance.[61] Empirical evidence of the failure of structural adjustment programs and the success of state- interventionist policies in East Asia changed thinking. In addition, pressure from lower-level staff and the appointments of James Wolfensohn as President and Joseph Stiglitz as Chief Economist fostered ideological acceptance that issues like corruption, rule of law, and public

administration problems needed to be incorporated into Bank development policies. Even as ideas changed, Weaver contends that the Bank's unwillingness to hire non-economists who understand the cultural and political aspects of development has limited the effectiveness of its good governance programs.

Constructivists can also help explain how neoliberalism came to triumph in countries such as the United Kingdom, Canada, Australia, and New Zealand in the 1980s and 1990s. Jonathan Swarts asserts that all countries have a "political-economic imaginary"—that is, a "set of interrelated ideas" about "the appropriate extent and form of state regulation of economic life and the legitimate objectives of state economic policy."[62] Elected officials such as Britain's prime minister Margaret Thatcher and Canada's prime minister Brian Mulroney changed their nations' political-economic imaginary. How did they do it? Swarts identifies some key mechanisms they used: persuasion; rhetorical coercion (such as arguing that "there is no alternative" to neoliberalism); appeals to material self-interest; and coercion (imposing laws that people have to comply with such as privatization of state-owned enterprises and labor market deregulation). Eventually, most political parties came to accept the neoliberal imaginary; it assumed a taken-for-granted nature. As a result, argues Swarts, "the language of the 'free' market, the priority placed on growth and efficiency, and the acceptance of market logic as factual and uncontested have become firmly entrenched in the political-economic imaginaries of the Anglo-American democracies."[63] However, in the 2010s Donald Trump and France's Marine Le Pen have used the same kinds of mechanisms as Thatcher and Mulroney to spread a new imaginary centered on economic populism, anti-immigration, and anti-globalization.

Economic ideas don't only come from academics, international organizations, and politicians. They also accrete from the everyday actions of ubiquitous markets. Political philosopher Michael Sandel describes how market values have permeated society in the last 30 years, reaching into "spheres of life traditionally governed by nonmarket norms."[64] Private military contractors, prison contractors, and for-profit colleges now provide services that used to be within the government's purview. Sperm, women's eggs, and the right to pollute can now be bought and sold. Before the 2000s, college football bowl games were simply named after bulk commodities like sugar, cotton, oranges, and roses, but now private businesses can buy official naming rights, such that at the end of 2016 we could watch the Rose Bowl Game Presented by Northwestern Mutual, the Capital One Orange Bowl, the Allstate Sugar Bowl, and the Chick-fil-A Peach Bowl. Few readers of this textbook are probably aware that before the 1980s, U.S. regulations prevented pharmaceutical companies from advertising their prescription drugs directly to consumers (and it wasn't until 1997 that drug ads became common on television in the United States).

Sandel worries that these changes enhance inequality, corrupt public life, and sometimes devalue the things that enter into markets. He argues that the reach of markets should be determined by political debate, informed to a much larger extent by moral and ethical reasoning.[65] As we become habituated to pervasive markets, it becomes harder to imagine

(or remember) that there are other ways we could choose to distribute certain goods and services, such as by merit, need, or lottery.[66] Efficiency is a value that markets are good at maximizing, but if a polity values propriety or something else in social relationships, it may want to keep commercialization at bay.

Finally, our understanding of the economy depends to a significant extent on what we measure and how we measure it (see Box 5.3). Quantitative measures and indicators construct the knowledge upon which decisions are made about finance, trade, global health, and other facets of the global political economy. Indicators come into existence through a social process involving choices of how to measure, what to include and leave out, and what assumptions to make.[67] They often reflect the interests of powerful political actors.

CONSTRUCTIVIST VIEWS OF MEASURES AND INDICATORS

We encourage readers to cultivate the habit of assessing measures and indicators that economists and political scientists often take for granted. Daniel MOgge argues that everyday macroeconomic indicators like GDP, inflation, and deficits are powerful ideas that shape policy choices and the distribution of resources in a society.[a] For example, GDP gives us a sense of how well an economy is doing, but it does not measure environmental destruction that accompanies economic growth. Inflation is a measure of the annual average rise in prices for a basket of goods. Governments often use it to determine how much to increase social spending, and companies rely on it when deciding on salary increases. But inflation is a blunt measure. As Mügge points out, depending on what a household consumes at its level of income, the national inflation rate can underestimate or overestimate the effects of price changes on it.

Constructivists stress that indicators are often subject to political manipulation and have political effects because of the way they influence perceptions of how well a government is managing the economy. When we use a measure we should consider whose interests it serves best and what assumptions lie behind it. Controlling the criteria of indicators and publicly issuing the indicators give some organizations significant influence. For example, Lorenzo Fioramonti points out that credit ratings have become "an all-powerful weapon in contemporary global politics."[b] They affect the rate of interest that companies and countries pay when they borrow. Global investors in stocks and government bonds make decisions based in part on information from the three main credit ratings agencies—Standard & Poors, Moody's Investor Services, and Fitch Ratings. As the financial crisis showed, credit rating agencies do not necessarily issue credible ratings. They misled investors by giving high ratings to many risky bundles of mortgage-backed securities. And during the height of the Eurozone crisis, ratings downgrades of some Eurozone countries caused borrowing costs to rise, thereby making economic conditions worse. In that sense, the indicators helped produce the very outcome they were ostensibly claiming to predict independently. Fioramonti believes that credit rating agencies essentially shift some control of macroeconomic policies away from the people and their government, thereby weakening democracy. He does not think so much power over perceptions in capital markets should be in the hands of just a few private companies using myopic algorithms.

Many indicators are designed specifically to produce political effects. For example, Transparency International's widely cited Corruption Perceptions Index puts pressure on governments to tackle corruption.[c] The World Bank's "Doing Business" rankings, which since 1993 have been compiled from a set of indicators of the "ease of doing

business" in each country in the world, have goals that include "encourag[ing] economies to compete towards more efficient regulation" and "offer[ing] measurable benchmarks for reform."[d] Critics point out that the rankings promote neoliberal ideals and "ignore the social benefits of regulation."[e] A. T. Kearney's Foreign Direct Investment Confidence Index and the OECD's FDI Regulatory Restrictiveness Index can affect how much foreign investment a country attracts. Even indicators of climate change may affect how seriously states try to move from carbon-based to renewable energy. In all of these examples, indicators do more than just explain; they have a performative function that guides states toward particular goals.

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The Role of Economic Ideas in the Global Financial Crisis

Economists have more influence on public policies than any other group of social scientists. Daniel Hirschman and Elizabeth Popp Berman describe one of the important ways in which economists affect politics: they shape the "cognitive infrastructure of policymaking with their styles of reasoning or policy devices."[68] Components of economic thinking, including cost-benefit analysis, marginal thinking, and concepts such as efficiency and externalities, also influence the way lawyers and non-economists in government think about policy issues.[69] For example, Keynesian ideas deeply influenced post-World War II policy makers, and the "efficient market hypothesis" led officials to lighten regulations on financial markets in the 1990s. According to Hirschman and Berman, supposedly technical policy devices such as GDP and the inflation rate actually all "involve political and moral choices," and their use by policy makers deeply affects the distribution of resources in society.[70]

Some constructivists blame economists for having ideological blinders that prevented them from predicting a crisis. A discursive analysis of internal government documents or official reports of government economic agencies can show us how leaders' ways of thinking predispose them to have certain priorities but blind them to certain kinds of information. For example, Stephen Golub, Ayse Kaya, and Michael Reay find that before the financial crisis the U.S. Federal Reserve was guided by a paradigm that made it unwilling to try to detect bubbles in the economy or take action against them before they burst.[71] The Fed generally was not looking for evidence that there were systemic risks in the financial sector. A different mindset might have led the Fed to seek better information and act preventatively.

Economic ideas also shaped how governments responded to the financial crisis. The post-2009 European response has been puzzling. Eurozone countries stuck with austerity policies, even in the face of evidence that these policies were making economic conditions worse in many countries. How can we explain this? Political scientist Sebastian Dellepiane-

Avellaneda points to the dominance of the idea of "expansionary fiscal contractions" as a key driver of Eurozone governments' behavior.[72] In the 1990s, an influential group of Italian economists—many of whom graduated from Milan's Bocconi University—developed the argument that during a recession it is not wise for a government to increase spending and borrowing; rather, cuts in government spending and increased taxes (also called "fiscal consolidation" or austerity) are most likely to produce economic growth. In other words, austerity is good, budget deficits are bad. They also assert that it is more effective to cut spending than to raise taxes (particularly on the rich). Finally, they say that voters do not punish leaders who carry out austerity; in fact, voters sometimes even reward them electorally.

These ideas directly contradict Keynesian ideas that recommend government stimulus spending during a recession. The so-called "Bocconi Boys" and other economists who believed in the benefits of expansionary fiscal contractions constituted an epistemic community, spreading their ideas in academic journals and in publications of the European Union, the IMF, and the OECD that were directed at policy makers. Many EU policy makers did not really believe that austerity would produce painless economic expansion, but they went along with the idea because it framed policy debates and facilitated some of their policy goals, such as small government.[73] Although the idea of expansionary fiscal contractions has not been as influential in the United States as in the European Union, pressures in the U.S. Congress for balanced budgets, a lower federal deficit, and lower taxes on the wealthy echo some of its themes.

Finally, it seems clear that the ideas of German academics and policy makers shaped the European Union's response to the euro crisis. In post-war Germany, ordoliberalism, which stressed balanced budgets and state-enforced rules for competition, became the dominant economic view (see Chapter 2). Stability became a culturally ingrained value. According to Matthias Matthijs and Kathleen McNamara, the German narrative of the euro crisis was a "morality tale of Southern profligacy vs. Northern thrift."[74] The authors state how the narrative categorized EU countries: "Hard work, prudent savings, moderate consumption, wage restraint, and fiscal stability in Germany were seen as Northern virtues and were juxtaposed to the Southern vices of low competitiveness, meager savings, undeserved consumption, inflated wages, and fiscal profligacy in the Mediterranean."[75] This framing made austerity the logical solution to financial crisis instead of issuance of Eurobonds and debt forgiveness. It also ignored the possibility that Germany and other Northern creditors may have irresponsibly lent too much to debtor countries. As Mark Blyth pithily points out, "It is manifestly impossible to have over-borrowing without overlending."[76]

CONCLUSION

Ideas are very powerful and *should* be taken seriously. Constructivist theory challenges us to think about IPE in new ways. As John Maynard Keynes noted famously in the closing pages of his *General Theory*,

> the ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back.[77]

A good IPE analyst asks how an issue comes to our attention, how we talk about it, and whether there are alternative ways to interpret the issue. How are ideas generated, diffused, and adopted? How do governments determine what their "national interests" are? How would the world be different if 9/11 were constructed as a crime rather than an act of war? How would we have reacted to the global financial crisis if we came to believe that it was caused by overlending, not overborrowing? Would there be a militarized war on drugs in Latin America if we conceived of the drug "problem" as created by U.S. demand, not Latin American supply?

Constructivism provides us tools to better understand many global issues. It focuses on how framing an international issue in a certain way necessarily means that some information gets excluded or hidden from public view. It encourages us to consider what ways of seeing get lost and whose voices are silenced by the way a problem is rendered. It directs our attention to actors and forces that have been overlooked in the liberal, mercantilist, and structuralist perspectives. In so doing, it shows us that states and markets are not the only shapers of the world; other actors such as norm entrepreneurs and social movements also propagate new norms that states may eventually accept, internalize, and craft their policies upon. It reminds us that the study of IPE cannot be divorced from moral and ethical questions. Unless we grapple with the different ways that people perceive the world, we will find it hard to explain what motivates their behavior.

KEY TERMS

constructivism 98
norm entrepreneurs 99
problematization 100
framing 100
discourse analysis 102
norms 104
norm cascade 104
boomerang pattern 105
spiral model 105
transnational advocacy networks (TANs) 105
epistemic communities 106
odious debt 108
norm antipreneurs 110
security community 111
nuclear taboo 112
securitization 114
capital mobility 116
expansionary fiscal contractions 119

DISCUSSION QUESTIONS

1. Identify some norms that many states or societies have *not* accepted and internalized. What factors explain the resistance to these norms? Do you think global norm entrepreneurs will be able to overcome some of this resistance?
2. What criticisms can be made of constructivism? Do constructivists underestimate the importance of material power in affecting global issues?
3. What tools do we have to measure whether norms actually influence an actor's outlook and actions?
4. Identify problems that have been securitized or that elites have attempted to securitize. Do you agree that these problems constitute serious threats to the state or society? What are alternative ways to frame and discuss these problems?
5. What elements of culture or national identity in your country seem to strongly shape its relations with other countries?
6. What elements of social life do you think should be off limits to market mechanisms?

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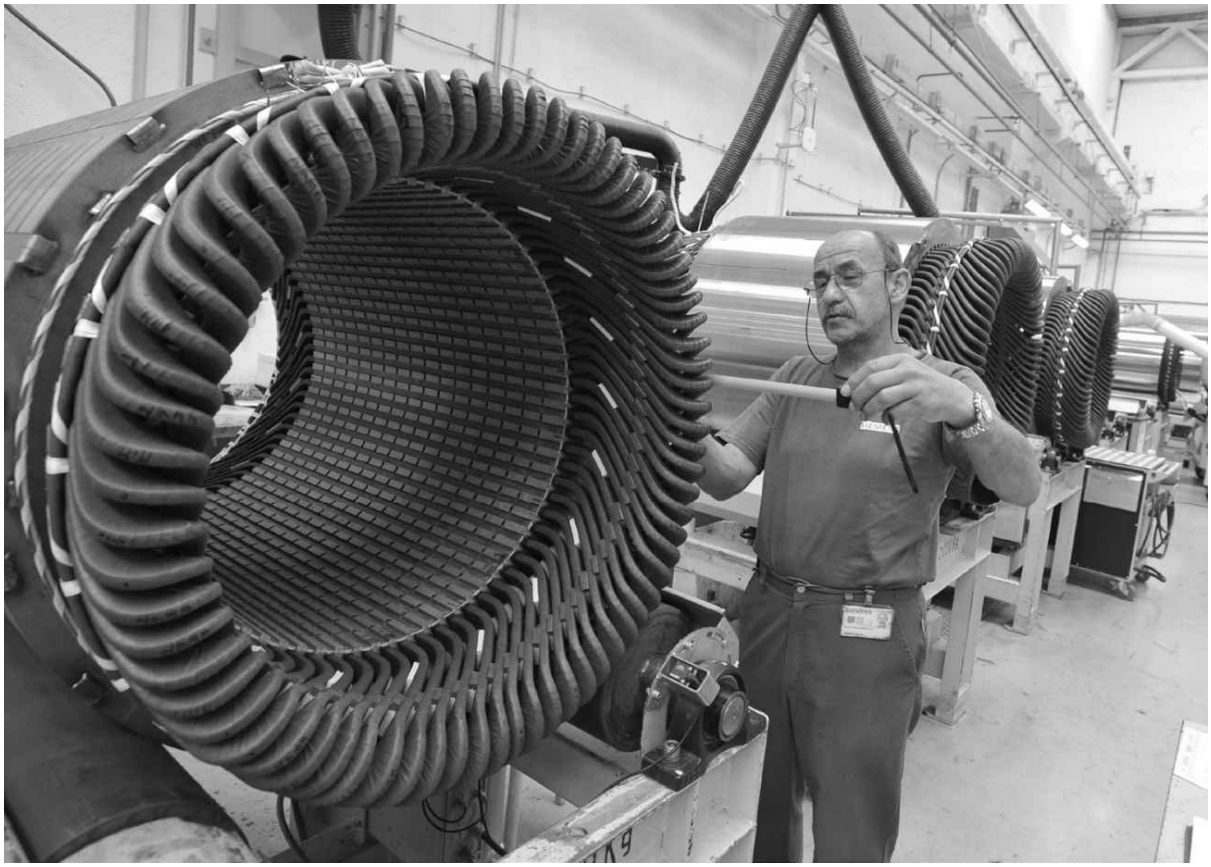
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PART
II
Structures of International Political Economy

CHAPTER 6
The Global Production Structure



A Siemens Electric Machines production plant in Drasov, Czech Republic.

Source: AP Photo/CTK/Igor Zehl.

It isn't inevitable that we have a globalization which is used by the cor- porations not to pay taxes. It is not inevitable that we have a form of globalization in which corporations use the threat of moving jobs abroad to lower wages.

Joseph Stiglitz[1]

Dan DiMicco, the former CEO of U.S. steelmaker Nucor, served as a trade advisor to the Trump campaign in 2016 and was considered for the position of U.S. Trade Representative in the Trump administration. His 2015 book *American Made: Why Making Things Will Return Us to Greatness* presaged many of the neomercantilist arguments that Trump would

espouse on the campaign trail. Echoing the productivist philosophy of Alexander Hamilton and Friedrich List, DiMicco states, "A country that doesn't create or make or build things is a country doomed to mediocrity. Manufacturing, and the innovation that comes with it, is indispensable to the vitality of a great nation."[2] He recommends spending at least $3 trillion to rebuild U.S. infrastructure, which will create jobs and revive the middle class. He envisions funding coming from taxes and a national infrastructure bank capitalized by public funds, hedge funds, pension funds, and sovereign wealth funds.[3]

DiMicco traces the U.S. industrial decline back to deliberate policies by Germany and Japan to keep the deutschmark and the yen undervalued relative to the dollar—until Ronald Reagan persuaded the two countries to revalue their currencies in 1985. He stresses how important it is for the United States to use protectionism selectively: "Reagan often said he was a free trader, but he knew how to use a tariff when it counted. For example, to save the great American Harley-Davidson motorcycle company, Reagan persuaded Congress to impose a 45 percent tariff on Japanese motorcycles."[4] In DiMicco's view, all countries try to advance their own interests by breaking free-trade rules, often with impunity. He describes the Chinese as "mercantilist and predatory competitors" who have deliberately undervalued their currency, imposed restrictions on foreign companies, and dumped products in U.S. markets.[5]

DiMicco reminds us that the United States, like other industrialized countries, is in a long war to preserve and expand its production capabilities. Countries struggle to reshape the global production structure—a set of relationships between states, corporations, and workers that influences what is produced, where, and by whom. After World War II, the United States dominated global production. By the 1970s, Europe and Japan had re-emerged as economic powerhouses. In the era of globalization since the 1980s, South Korea, China, and some other developing countries have rapidly industrialized and captured a rising share of global production.

This chapter advances several key arguments about the production structure:

- A small number of middle-income developing countries are attracting the lion's share of production that is leaving the Global North.
- A growing proportion of global production is organized in complex global value chains (GVCs) dominated by transnational corporations (TNCs).
- While often relying upon states and seeking benefits from them, TNCs nevertheless undermine state authority by engaging in tax avoidance and wrongdoing.
- Changes in global production have tended to weaken labor, thereby increasing inequality and the social vulnerability of workers.

GLOBAL PRODUCTION

Transnational corporations (TNCs) play a major role in shifting global production around the world. For several decades after World War II, it was common for many final goods to be produced entirely in individual countries. Most goods and services used in production would circulate within factories or between them in developed countries. As foreign direct investment (FDI) grew, TNCs expanded outside their own home countries to build manufacturing facilities and set up offices. Eventually they started to contract with other companies overseas for goods and services—a process called outsourcing.

Today, the majority of the world's exports are intermediate goods—inputs, parts, and components used in the production of finished goods. For example, steel is an intermediate good used in the production of cars. Whereas in the past many manufacturers did everything "in-house," now they have broken the manufacturing process into tasks that are spread around the world, necessitating more trade to bring these tasks and parts together into final products. For example, Boeing's 787 Dreamliner commercial jet is assembled in Everett, Washington and North Charleston, South Carolina, but many of its component parts are manufactured in other parts of the country and outside the United States. Although many companies save money by outsourcing, Boeing went billions of dollars over budget on the Dreamliner and had to delay its unveiling by three years in part because many foreign suppliers could not produce components with the correct specifications fast enough.[6]

In the last two decades, many manufacturers around the world have shifted to using robots and automated assembly lines to make and assemble a wide variety of high-value merchandise. The digital revolution has given rise to many new products and services. Computers and digital technology have also changed the way products are designed and built, increasing the productivity of individual workers. In his book *The World Is Flat*, Thomas Friedman shows how the rapid spread of production processes throughout the world has empowered individuals to collaborate better—while also forcing them to compete more with one another.[7]

Foreign Direct Investment

Changes in where production takes place are frequently tied to changes in patterns of foreign direct investment. FDI consists mostly of overseas investments by foreign companies in factories, mines, and land. About two-thirds of existing FDI is in developed countries, while one-third is in developing countries. The biggest *senders* of FDI in the world are corporations in the United States, the United Kingdom, Germany, and Japan. Between 1990 and 2016 the value of annual global FDI *inflows* increased enormously from $205 billion to $1.75 trillion. Historically, most inward flows of FDI were concentrated among the developed nations, especially the United States and the European Union (see Figure 6.1). Surprisingly, foreign companies invest very little in Japan, the world's third

largest economy. As late as 2000, developed countries received 81 percent of annual FDI inflows—in large part because they have historically had the richest markets, the most skilled labor forces, and the highest productivity. However, by 2016 they took in only 59 percent, as investment rapidly spread out to every continent, especially Asia. Beginning in the 1990s, East Asia (especially China) and Latin America (especially Brazil) attracted a growing share of total world FDI. By the mid-2000s India began to attract a modest amount of FDI for its growing services industry. However, the 52 poorest countries in the world, many of which are in sub-Saharan Africa, still receive only 2 percent of global FDI inflows, undermining their future development prospects.

Economic liberalization and technological change are key drivers of the growth of foreign investment. Since the early 1980s, many countries have allowed freer trade and capital mobility that TNCs desire. Countries that enter regional economic groups such as the North American Free Trade Agreement (NAFTA) and the European Union adopt liberal trade and investment rules. China's entry into the World Trade Organization (WTO) in 2001 accelerated its inward FDI flows. Countries such as India and Japan that have been slow to abandon mercantilist regulations are disadvantaged in the competition for FDI.

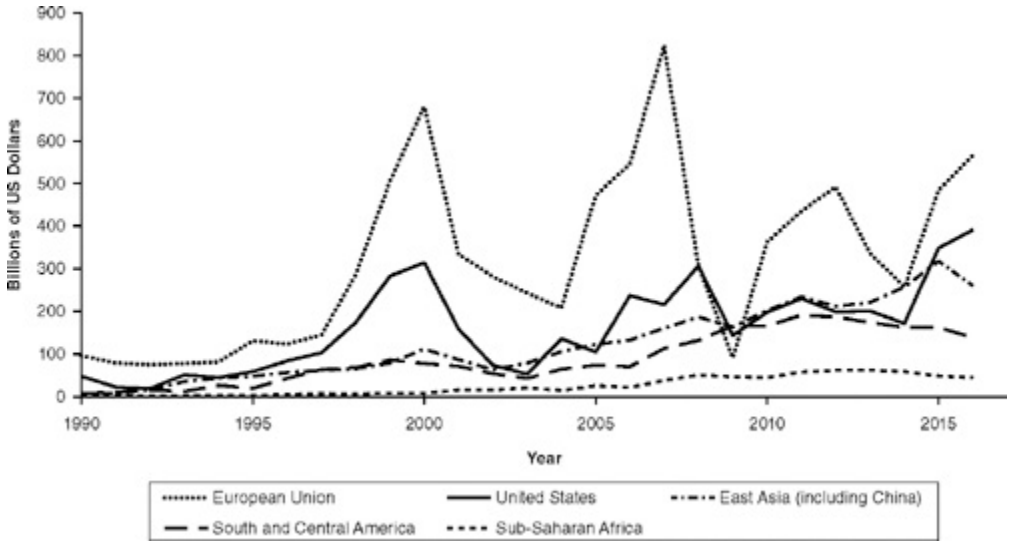


FIGURE 6.1
Net Inflows of Foreign Direct Investment, 1990–2016 (USD billions).

Source: Data from UNCTAD, *World Investment Report 2017*, Annex Table 1, at http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx.

IPE scholars recognize that there are different reasons why individual corporations decide to invest overseas and ramp up production outside of their home country. Most importantly, manufacturers and service providers want to be close to their customers. But some TNCs from the Global North also want to exploit low wages or cheap natural resources in the Global South.

Some FDI is an unintentional result of mercantilist policies designed to keep out foreign

products. A foreign firm can get around a country's tariff barriers by establishing a factory in that country; in a sense, this transforms the foreign firm into a domestic firm. In the early 1980s, for example, the United States negotiated an export agreement with Japan that was intended to protect U.S. automobile manufacturers while they developed more fuel-efficient models. The agreement put numerical limits on car exports from Japan to the United States. The limits did not apply, however, to automobiles assembled in the United States and sold by Japanese firms, so long as most of the parts came from the United States or Canada. Honda, Toyota, and Nissan all began to invest in production facilities in North America so that they could expand their market shares despite the trade barriers. Today, Japanese companies produce in North America most of the cars they sell in North America, thanks to tens of billions of dollars of investments since the 1980s and the development of deep ties with suppliers of auto parts throughout the NAFTA countries (Canada, Mexico, and the United States).

TNCs are especially sensitive to foreign exchange (FX) rates because their costs and revenues are denominated in different currencies. An unexpected shift in exchange rates can raise effective costs and reduce revenues. TNCs can reduce exchange rate risks by establishing production facilities in each of their major consumer markets so that costs and revenues largely accrue in the same currency. TNCs also have a strong incentive to invest overseas when their home country's currency is overvalued.

FDI may also be influenced by location-specific advantages. For example, a powerful impetus for a lot of Chinese FDI in Africa and Latin America is to directly access natural resources—especially minerals. In addition, TNCs often want to invest where many other firms are located, so that they can benefit from the pool of highly trained individuals in that area and the intense competition and constant innovation that is built into this environment. Some of the places in the world that have the right technological and human environment to make a firm very competitive are California's Silicon Valley, China's Pearl River Delta region, and the Indian city of Bangalore.

To summarize, TNCs invest abroad to gain a competitive advantage, to be closer to customers, to get around trade barriers, to mitigate currency risks, and to take advantage of special production environments.

Mercantilist Concerns about Changes in Global Production

Changes in global production can be clearly seen in GDP figures (see Table 6.1). The World Bank reports that in 2016 the world's GDP totaled $76 trillion, with the United States accounting for 24.5 percent of the world's output and China accounting for 14.8 percent. The seventy-eight high-income countries had $47 trillion or 64 percent of total output (down from 78 percent of the total in 2005).[8] The 109 middle-income countries accounted for $27 trillion or 37 percent of the total. Sadly, the thirty-one poorest countries accounted for only $405 billion or less than 1 percent of the world's total output. Undoubtedly, middle-income countries like China, Brazil, and India are producing a growing share of the world's goods and services, while the United States, the European Union, and Japan—especially since the onset of the global financial crisis—are producing a

smaller proportion of the world's output.

TABLE 6.1

Gross Domestic Product of the World's Ten Largest Economies, 2016

Country	GDP (billions of U.S. dollars)	Percentage of World GDP
United States	18,569	24.5
China	11,199	14.8
Japan	4,939	6.5
Germany	3,467	4.6
United Kingdom	2,619	3.5
France	2,465	3.0
India	2,264	3.0
Italy	1,850	2.4
Brazil	1,796	2.4
Canada	1,530	2.0

Source: Data from World Bank, *World Development Indicators*, at http://databank.worldbank.org/data/download/GDP.pdf.

Production is such a highly charged political issue because it affects, among other things, national security, trade, employment, and income. For example, a contentious issue in the developed countries is offshoring—when corporations move their manufacturing or certain business functions overseas. Beginning in the 1980s, many companies moved factories to Asia and Latin America to take advantage of cheap, plentiful labor. Free-trade agreements and lower transportation costs made it more efficient to produce clothing, household goods, and electronics overseas and export the items back to the United States and Europe. By pushing U.S. manufacturers to offshore and outsource to China, retail chains like Wal-Mart and Target boosted profit margins substantially. (In 2016, Wal-Mart and Target imported by ship to the United States the equivalent of 1,382,200 cargo containers!)[9] Although liberal economists tout the greater global efficiency and cheaper prices for consumers, critics argue that it is destroying American manufacturing and driving down wages of blue-collar workers. Today, many companies are also offshoring and outsourcing services—everything from customer service, data processing, back-office work, tax preparation, and insurance claims processing.

Mercantilists worry about the long-term consequences of outsourcing and offshoring. Losing the ability to manufacture items used by the military can weaken a country's national security (see Box 6.1). In addition, former Intel CEO Andy Grove warns that when factories move oversees, there is less innovation and fewer jobs in the United States. And because the process of scaling—which means turning new ideas into mass produced

products—occurs less in the United States, the result is this: "As happened with batteries, abandoning today's 'commodity' manufacturing can lock you out of tomorrow's emerging industry."[10] Similarly, Eamonn Fingleton believes that companies should protect their expertise (like trade secrets and patents) and manufacturing capacity while investing in new technology. He argues, "In discussions of the unintended consequences of globalism, the transfer abroad of valuable production technology is the elephant in the room. It is consistently ignored in all standard theoretical accounts of free trade."[11] In particular, he laments Boeing's outsourcing of manufacturing of parts and components for its airplanes. More than one-third of the 777 "Dreamliner" is manufactured in Japan, which is becoming a global aerospace leader. Fingleton explains that Boeing transferred some of its most advanced technology, including wing-making expertise, to Japanese suppliers.[12] Boeing is losing its manufacturing capacity and enabling its future competitors.

SECURITY IMPLICATIONS OF SHIFTS IN PRODUCTION OF SEMICONDUCTORS

It is easy to see how the production and security structures are intertwined. In the commercial economy, semiconductors (including chips, microprocessors, and integrated circuits) are central to electronic devices such as cell phones and computers. They are also vital to militaries because of their role in weapons systems, aviation, satellites, and information processing. Countries must be concerned with having continued access to advanced semiconductors, particularly components with military applications. Thus, when calculating a country's war-fighting capabilities, it matters greatly who produces the semiconductors and where.

The production of semiconductors has become globalized. The United States was the world's dominant chip manufacturer until it was overtaken by Japan in the 1980s. As Japan's share of global semiconductor manufacturing declined in the 1990s, more production shifted to Taiwan and South Korea. By 2007, Japan and the United States each accounted for only about one-quarter of global production. By 2015, only 17 of the world's 94 most advanced semiconductor fabrication plants were in the United States.[a] The actual design of integrated circuits—which is highly skilled and highly profitable—has mostly stayed in the United States, where companies account for 70 percent of global revenues from design activities.[b] And U.S.-controlled companies are responsible for 50 percent of global semiconductor sales. Nevertheless, the trend is for more design to move to the Asia-Pacific region. Today, Intel (a U.S. company) and Samsung (a Korean company) are the world's biggest sellers of semiconductors.

Since the early 2000s, China has increased its capacity to design and manufacture chips, aided by a migration of Taiwanese semiconductor companies to the mainland. Expanding its domestic semiconductor industry aids China's military modernization and reduces its foreign dependency. In 2014 the Chinese government announced an ambitious plan to invest up to $150 billion in the domestic semiconductor industry to become the dominant player in every aspect of the global industry by 2030. On the other hand, the relative decline in U.S. chip manufacturing and the outsourcing of more production and design to Asia presents a national security challenge, as the United States could be vulnerable to a disruption in chip imports. Monique Ming-chin Chu points out that for cost and quality reasons, the U.S. military increasingly relies on non-domestic "certified" producers in Asia (except for components destined for "mission-critical" systems).[c] Producers in adversarial countries could clandestinely modify integrated circuits to make them useful for "information warfare."[d] Of course, China already faces the same security problems because it still has to import the majority of semiconductors it needs.

In a report to President Obama in January 2017, a U.S. advisory council warned

that China's deliberate policies to build a large semiconductor industry are "distorting markets in ways that undermine innovation, subtract from U.S. market share, and put U.S. national security at risk."[e] It stressed the need for the United States to maintain its technological lead in semiconductors and incentivize U.S. chip manufacturing. In the long term, the balance of power between countries can be altered by the globalization of production of advanced technology goods such as semiconductors.

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[b] Monique Ming-chin Chu, *The East Asian Computer Chip War* (Abingdon: Routledge, 2013), p. 89.

[c] Ibid., p. 108.

[d] Ibid., p. 282.

[e] Executive Office of the President, President's Council of Advisors on Science and Technology, "*Ensuring Long-Term U.S. Leadership in Semiconductors*," January 2017, p.2. At https://obamawhitehouse.archives.gov/sites/default/files/microsites/ostp/PCAST/pcast_ensuring_long-term_us_leadership_in_semiconductors.pdf.

Mercantilists may find some solace in an incipient countertrend that business journalist Charles Fishman examined in 2012: insourcing.[13] Changes in the global economy have incentivized U.S. companies such as General Electric, Apple, Whirlpool, and Sleek Audio to bring some of their manufacturing capacity back to the United States. The surge in natural-gas production in the United States has decreased the cost of operating plants. Just as wages of Chinese workers are rising quickly, the weakening of American labor unions and the increasing number of so-called right-to-work states has significantly lowered U.S. labor costs. Mechanization and higher efficiency in U.S. industries make wages a less important cost in overall production. Although there is unlikely to be a boom in U.S. manufacturing, despite President Trump's best efforts, it is ironic that some of the same globalization forces that spurred outsourcing two decades ago are now—in reverse—spurring insourcing.

LARGE TRANSNATIONAL CORPORATIONS AND COMPETITION

What exactly are TNCs? What determines where they produce things? How much power do they have? To what extent can their interactions with nation-states and workers be regulated by formal global regimes? TNCs (also called multinational corporations or MNCs) are corporations that operate across national borders. Their foreign investments have grown dramatically over the last sixty years, fueled by the spread of economic liberalism and by changes in international transportation and communications technologies. They have been the main engines of global capitalism. TNCs have always been controversial because their global reach can make them difficult for nation-states to control. Most TNCs today are private companies, although there are also large state-owned TNCs. They invest in production, research, distribution, and marketing facilities abroad, often transferring technology in the process.

How Large Are TNCs?

The tens of thousands of TNCs account for about one-quarter of global gross domestic product (GDP) and one-third of world exports. Table 6.2 lists the fifteen largest nonfinancial TNCs in 2016, as compiled by the United Nations Conference on Trade and Development (UNCTAD), ranked according to foreign assets owned. All are headquartered in developed countries, and most are in the petroleum, mining, automobile, or telecommunications industry.

Although ranking TNCs according to the value of their foreign assets is a good approach if one wants to stress the size of their foreign investments, large firms that do not invest abroad heavily would appear very low in the ranking. There are several other ways to measure the relative size of TNCs and highlight their other characteristics. The biggest TNCs are commonly listed by the size of their market capitalization, i.e., the total value of all their shares on public stock markets. Capitalization tends to be much more volatile than foreign assets owned, but it provides a good measure of how investors perceive the future prospects of particular TNCs. For example, the financial crisis caused a 42 percent drop in the market value of the 500 largest companies from $26.8 trillion in 2008 to $15.6 trillion in 2009, but by 2015 their total market capitalization had soared to $32.4 trillion.

Table 6.3 lists the top fifteen publicly traded corporations in the world at the end of March 2017, based on market capitalization. Note that U.S.-based companies are dominant, there are only two Chinese companies, and there are no European-headquartered firms. Five of the top six TNCs (Apple, Alphabet, Microsoft, Amazon, and Facebook) are technology companies, as are the two Chinese corporations (Tencent and Alibaba). Their focus on software, electronics, or e-commerce indicates how important the digital revolution has been. The meteoric rise in market capitalization has been extraordinary. In 2009 Apple was worth $94 billion, Amazon was worth $31 billion, and

Tencent was worth only $13 billion. Because the technology companies and banks usually make most of their revenue from selling services rather than manufacturing physical goods, they often do not need to make heavy investments in plants and factories overseas.

TABLE 6.2

Fifteen Largest Nonfinancial Transnational Corporations in 2016, Ranked by Foreign Assets

TNC	Headquarters Country	Foreign Assets (billions of U.S. dollars)
Royal Dutch Shell	Netherlands/United Kingdom	350
Toyota	Japan	304
BP	United Kingdom	235
Total SA	France	233
Anheuser-Busch InBev	Belgium	208
Volkswagen	Germany	197
Chevron	United States	189
General Electric	United States	179
Exxon Mobil	United States	166
Softbank	Japan	146
Vodafone	United Kingdom	144
Daimler	Germany	139
Honda	Japan	130
Apple Computer	United States	127
BHP Billiton	Australia	119

Source: Data from UNCTAD, *World Investment Report 2017*, Annex Table 24, at http://unctad.org/en/Pages/-DIAE/World%20Investment%20Report/Annex-Tables.aspx

A third methodology for ranking the world's largest TNCs combines the size of the companies' assets, market value, profits, and revenues. Using these metrics, Forbes finds that in early 2017 four of the world's ten biggest public companies were Chinese banks. This is not surprising given the size of the Chinese market and low level of competition in the Chinese financial system. Technology companies do not rank so high with this methodology because they tend to have much lower profits or total assets than banks and companies that manufacture goods. Generally speaking, whichever method one uses to rank TNCs, those corporations from the United States, the European Union, Japan, and China dominate the top 50. However, it should be kept in mind that many of the world's large businesses do not engage in substantial amounts of FDI and do not, therefore, rank among the leading TNCs.

TABLE 6.3

Fifteen Largest Global Publicly Traded Companies by Market Value, March 31, 2017

Company	Country of Headquarters	Market Value (billions of dollars)
1. Apple	United States	754
2. Alphabet	United States	579
3. Microsoft	United States	509
4. Amazon	United States	423
5. Berkshire Hathaway	United States	411
6. Facebook	United States	411
7. Exxon Mobil	United States	340
8. Johnson & Johnson	United States	338
9. JPMorgan Chase	United States	314
10. Wells Fargo	United States	279
11. Tencent Holdings	China	272
12. Alibaba	China	269
13. General Electric	United States	260
14. Samsung	South Korea	259
15. AT&T	United States	256

Source: Data from PriceWaterhouseCoopers, "Global Top 100 Companies by Market Capitalisation," Updated March 31, 2017, at www.pwc.com/gx/en/audit-services/assets/pdf/global-top-100-companies-2017-final.pdf.

Trends in Competition between Corporations

For economic liberals, competition is a cornerstone of any free market. For many global products, including online services, cell phones, clothing, and automobiles, global companies compete fiercely over price, quality, and market share. After all, globalization has been portrayed as a process that increases competition, often to the benefit of consumers everywhere. The emergence of large TNCs headquartered in emerging countries —especially China—has increased competition in some global industries. Nevertheless, it is ironic that after more than three decades of neoliberal reforms in much of the world, competition in many national industries and in some global industries has actually decreased. Due to mergers and acquisitions (M&As) among TNCs, there are fewer and larger companies in many sectors. In 2015, global M&As (half of which were in the United States) reached a record $5 trillion, showing that large firms were increasing their market power by buying up smaller ones.[14] Another cause of reduced competition is the global strengthening of intellectual property rights, which we discuss in Chapter 10. Market consolidation allows large corporations to abuse their market position and flex their political power vis-à-vis governments—behavior that does not surprise structuralists.

The concentration of global producers of agricultural inputs provides a revealing

example. In 2015, the Chinese state-owned chemical company ChemChina made a $43 billion bid for the Swiss company Syngenta, one of the largest producers of agrochemicals and seeds in the world. The same year, German agrochemical and pharmaceutical company Bayer made a $66 billion deal to buy U.S. biotechnology seed producer Monsanto, the most costly takeover by a German company ever. In 2016, U.S. companies Dow and Dupont agreed on a $130 billion merger to form a massive seed and chemical company. Soon thereafter in 2016, Canada's two largest fertilizer companies, Agrium and Potash, announced a merger. (At the time of writing in 2017, EU and U.S. authorities had not yet approved all of these mergers.) These mergers in the agrobusiness sector follow similar consolidation among global pharmaceutical companies several years earlier. In both industries, many of the companies rely heavily on patents that they are determined to protect around the world. Regulators are concerned not just with antitrust issues, but also how the M&As will affect jobs, innovation, and prices. When a TNC headquartered in one country seeks to acquire a TNC in another, policy makers must consider the national security implications as well.

One way we measure corporate market concentration is by looking at how many firms in an industry account for what share of the market. President Obama's Council of Economic Advisors found that concentration in the United States has increased, as large firms account for a larger share of revenues in a number of industries. For example, the share of all U.S. deposits held by the ten largest banks increased from 20 percent in 1980 to 50 percent in 2010 (right after the financial crisis).[15] The most profitable non-financial companies were making much higher returns on invested capital in 2014 than in 1990, and fewer new firms were being created in the United States than in the past—both signs that competition is decreasing.[16]

Greater concentration of producers can have many negative effects on nations. Heterodox liberal scholar Joseph Stiglitz argues that oligopolistic markets in many sectors of the U.S. economy, including pharmaceuticals and health insurance, contribute to rising inequality.[17] Concentration has also led to higher prices for airline travel, cellular phone service, and textbooks. There are similar trends in many other developed countries. In some cases large corporations illegally conspire in ways that hurt workers and consumers. For example, the largest manufacturers of LCD panels were found to have colluded to fix the price, causing consumers to pay more for notebook computers and televisions.[18] In 2015 a group of Silicon Valley technology firms (including Apple, Google, and Intel) paid $325 million to settle a class-action lawsuit alleging that they had colluded in the 2000s not to "poach" each other's workers in order to keep workers' salaries lower throughout the industry. Governments can enhance competition through anti-trust actions, but U.S. officials are less politically committed to doing so than their EU counterparts—partly because of the staggering amount of corporate money and lobbying in the U.S. political system.

GOVERNANCE OF TNCs

In their ordinary business operations TNCs create complex relationships with their suppliers, distributors, and other economic partners around the world. In addition, because they produce and trade throughout the world, TNCs want governments to maintain a stable, liberal international order. In this section we examine two important mechanisms by which production and economic activities connected to it are "governed"—that is, subject to rules and regular patterns of behavior. First, governance can result from the strategic decisions of thousands of networked private companies in global value chains. Second, governance can be based on international investment agreements that are the result of state-to-state negotiations. In both cases we can say that global production is coordinated and rule-bound, shaping the relative gains and losses of different countries.

Global Value Chains

It was common decades ago for large companies to be vertically integrated, meaning they owned most of their supply chain, from the production of materials to manufacturing to wholesale distribution. Since the 1980s, production has increasingly been organized in global value chains (GVCs) (also called "global production networks" (GPNs)) that encompass "the full range of activities that firms and workers perform to bring a product from its conception to end use and beyond."[19] GVCs link together many companies in a division of labor that spans different countries. We can say that each GVC is "governed" because typically there is a lead TNC that plays a dominant role in organizing firms in a complex supply chain. For example, in the case of smartphones, Apple performs the designing, branding, patenting, logistics, and retailing associated with iPhones, but it depends on Japanese, Taiwanese, German, and South Korean companies to produce many components, which are exported to China. A Taiwanese-owned company named Foxconn that is contracted to Apple owns the manufacturing facilities in China where hundreds of thousands of its workers actually assemble the components into final products that will be exported to Apple retailers and Apple's authorized sellers. Very little value is added in China; most of the profits go to Apple and suppliers of components. The final market for products from GVCs is predominantly developed countries, although emerging countries are a rapidly growing destination for some goods from GVCs.

Three important questions to ask are: (1) Which countries and companies gain the most profit from the entire value chain? (2) How do GVCs affect employment and economic development in different countries? (3) How can companies in a GVC move from just doing low-wage assembly or making low-technology components to making cutting-edge components or even designing and branding their own products? Political economists believe that in order to answer these questions we have to understand how GVCs are governed.

Often, the buyer at the end of the GVC, such as Apple or a big retailer like Wal-Mart,

orchestrates the chain and has a decisive influence on which countries and firms can be part of it and what price suppliers will receive. In turn, the supplier's price will affect the wages that are paid to workers in manufacturing facilities. In other cases, the brand owner or retailer may not be in control if it is heavily dependent on just a few large suppliers that cannot easily be replaced. As we discuss in Box 6.2, GVCs raise important questions about which firms are responsible for governing working conditions and business practices in the global supply chain. Some scholars argue that lead firms should be legally and ethically accountable for the practices of their suppliers and contractors overseas.

GVCs have contributed to rising inequality in developed countries by concentrating benefits in the hands of large firms that have cut blue-collar jobs in developed countries and shifted production to contractors in developing countries. Andy Grove, a long-time leader of Intel who died in 2016, argued that outsourcing U.S. production to Asian contractors reduces U.S. manufacturing employment and threatens the United States' ability to remain a technologically innovative country.[20] Many Japanese electronics companies also outsource electronics production to contractors in China. Lead firms in GVCs are even affecting service workers in developed countries as they shift customer service, computer programming, and back office work (such as IT support and payroll) to developing countries. For example, India has some of the world's largest business process outsourcing (BPO) companies providing services to Fortune 500 companies, in part because India's service workers earn wages much lower than those in Europe and the United States.

ACCOUNTABILITY IN GLOBAL VALUE CHAINS

Many TNCs coordinate transnational networks of contractors and suppliers. Nike, for example, is a high-profile TNC, but it owns very few production assets either outside or inside the United States. Most of its products are manufactured and distributed by foreign-owned firms under contract to Nike. Everything from production of raw materials, to apparel sewing to distribution is coordinated by Nike through chains of contracts and business relations with other firms. The assets that Nike absolutely controls and guards jealously are its brand name, its image, and the famous "swoosh" trademark.

Global value chains raise the question of whether or not TNCs are accountable for what is done in their subcontracting firms. TNCs might not be *legally* accountable for their suppliers' actions, but they sometimes must establish accountability for actions of other firms in order to have credibility with consumers and legitimacy in their negotiations with other actors that are concerned about corporate social conduct.

For example, NGOs such as Global Exchange, the Clean Clothes Campaign, and the United Students Against Sweatshops have pressured lead TNCs in shoe and apparel GVCs to eliminate sweatshop conditions among suppliers. Since the 1990s, for example, Nike has been accused of tolerating serious abuses of workers in the plants run by its Asian contractors. In September 2002, twenty-six apparel companies signed an agreement to establish a monitoring system that would oversee working conditions in their subsidiaries in developing countries. Some 250 U.S. companies, including Apple and Nike, have created codes of conduct for their subcontractors. [a] In 2013 an eight-story garment factory in Bangladesh called Rana Plaza collapsed, killing more than 1,100 workers and severely injuring more than 2,000. The shocking event motivated American and European companies that had contracted with garment suppliers in the Plaza building to sign agreements to upgrade safety and oversight in Bangladesh's garment industry.[b]

Kate Macdonald, who has studied corporate efforts to govern garment and coffee supply chains, notes that large retailers have significant influence on living standards and working conditions of workers through GVCs because the retailers "control the terms of exchange such as supplier prices, production and delivery standards."[c] As a result, transnational activists argue that corporations are responsible for what goes on in their supply chains. The fair-trade coffee movement is also predicated on the belief that coffee commodity buyers and roasters need to raise and stabilize the incomes of coffee farmers. Many TNCs have taken the issue of accountability seriously in order to protect their reputations. They have voluntarily adopted corporate social responsibility (CSR) codes whereby they try to address key social and environmental issues in their business practices. The NGO Business for Social Responsibility argues that CSR can have a positive effect on businesses by reducing operating costs,

enhancing brand image, increasing sales and company loyalty, and raising productivity and quality.[d]

It remains to be seen, however, whether the CSR movement will create widespread changes in TNC governance. Some scholars believe that voluntary CSR will result in only marginal changes in business conduct.[e] Robert Reich, for example, argues that "companies are neither moral nor immoral" and that deep structural forces drive the behavior of TNCs, not the ethics of their top executives.[f] Reich and others advocate multilateral and national regulations that would apply to all corporations. As GVCs become more important in transnational production, accountability within them will continue to be a central issue on the public policy agenda.

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Gary Gereffi, a leading scholar of GVC governance, argues that "today, nations seek to industrialize by simply joining a supply chain to assemble final goods or make specialized inputs; they no longer try to build single-nation supply chains from scratch."[21] Even so, these industrializers do not want to remain forever at the bottom of the value chain doing low-cost, low-profit work. They want to move up the value chain to do more profitable tasks such as high-tech manufacturing, design, marketing, and research and development.[22] For example, South Korea's Samsung and LG for many years were contract manufacturers for Japanese companies. As they developed their own research and development, they became global brands in their own right. Today they now lead GVCs and contract out manufacturing of many components to companies in China.

Investment Agreements

In the mid-1990s, the Organisation for Economic Co-operation and Development (OECD) sponsored talks between business and government leaders over a Multilateral Agreement on Investment (MAI). The intent was to create a regime to govern FDI in the same way that the WTO governs international trade. Although the OECD's attempt to negotiate a final version of the MAI failed in 1998, there have been many subsequent efforts to create binding rules and voluntary guidelines for investment. TNCs wanted to be assured of "national treatment," meaning that, while a state has the right to regulate inward investment at the border, once that investment has been made the state must treat the local subsidiary of a foreign TNC the same way it treats similar domestic firms. There must be no domestic discrimination against TNC affiliates, even if this means giving them tax preferences and subsidies intended for domestic firms only. TNCs believe that recognition of this principle would make FDI more efficient and less vulnerable to political forces.

Instead of one global agreement on FDI, UNCTAD reports that as of 2016 there were over 2,300 active bilateral investment treaties (BITs) and nearly 300 regional investment agreements, creating a complex hodgepodge of rules and standards. This governance system does not prevent states from engaging in "beggar thy neighbor" bidding wars to attract TNCs, nor does it facilitate enforcement of uniform labor and environmental standards in TNC operations. However, the regional and bilateral investment agreements typically guarantee foreign investors national treatment, protection from expropriation, and compensation for government actions that undermine the value of their investments or expected future earnings. They have provisions specifying the rights of foreign investors and procedures for resolving disputes between TNCs and host states.

Normally, when TNCs feel that their rights have been violated, they take their disputes to be settled in the courts of their host countries. But these courts may not always treat TNCs fairly or impartially. Thus, a growing number of investment agreements today have a controversial mechanism for adjudicating disputes called investor–state dispute settlement (ISDS). Under ISDS, TNCs can take their disputes directly to independent international arbitration bodies that issue binding rulings that can sometimes compel states to award damages to foreign investors. TNCs generally like ISDS because the arbitration bodies can act quickly and without political bias, ensuring that states abide by standards of treatment outlined in signed agreements. Many states agree to ISDS because it reassures TNCs and may encourage more FDI.

Many developing countries signed BITs with ISDS provisions in the 1980s and 1990s, not realizing the extent of the risk of being sued by TNCs. Until these countries started to face investor claims, which mushroomed after 2000, their officials had seen BITs as "little more than diplomatic tokens of goodwill" which would send a positive signal to foreign investors but entail no real liabilities or legal significance.[23] Today, some officials are more likely to see ISDS as a threat to state sovereignty.

Critics contend that ISDS gives corporations the right to potentially overturn government regulations designed to protect the environment, workers' rights, and public health. It seems undemocratic to let decisions with important economic consequences be made outside of domestic courts by international arbitrators who are not accountable to citizens of host countries. Because arbitration proceedings are conducted in private and rulings are sometimes not made public, there appears to be a lack of transparency. When TNCs damage the environment, contribute to human rights violations, or help cause financial crises, people hurt by the TNCs do not have recourse to arbitration bodies; only states and corporations can bring matters before them.

There have been several controversial ISDS cases in recent years. In 2009, Uruguay required cigarette packs to have a health warning that covers 80 percent of the packaging. In 2011, Australia required cigarette packs to have plain, standardized packaging and graphic health warnings. Phillip Morris brought Australia and Uruguay to arbitration tribunals, arguing that the countries' anti-smoking regulations damaged the company's investments and violated their trademark rights. It lost both arbitration cases. In 2016 TransCanada, a Canadian pipeline operating company, filed for arbitration with the U.S.

government under provisions in the NAFTA treaty. The company sought $15 billion in compensation for losses due to the Obama administration's decision to reject the Keystone XL pipeline that TransCanada was expected to build. TransCanada dropped the cases in early 2017 after President Trump green-lighted the pipeline.

RELATIONS BETWEEN STATES AND TNCS

Apart from business leaders and economists, who tend to view the growth of TNCs as the natural consequence of emerging regional and global market structures, most authors interpret the expansion of TNCs as a decisive shift in the balance of power in the global economy. They argue about who will benefit from this shift and how. In this section we focus on their observations about the changing relationships between states and TNCs. Some political economists view states as exercising significant control over TNCs, including through their ability to tax and regulate corporate producers. Moreover, states use TNCs to advance their foreign policy interests. Other IPE scholars emphasize that transnational corporations are gaining the upper hand over states by extracting subsidies and other resources and threatening to move operations to other countries if laws and regulations are not to their liking.

TNCs as Tools of National Power

TNCs and FDI were distinctive elements of the first modern era of globalization, which reached its zenith about a hundred years ago and ended with the opening shots of World War I. In his book *Imperialism_ The Highest Stage of Capitalism*, V. I. Lenin focused on this era's "finance capitalism," not TNCs *per se*, but his conclusions are easily applied to TNCs. Lenin argued that colonial imperialism had been replaced by economic imperialism. Foreign armies and occupying forces were no longer necessary because the same result (exploitation by and dependency on the capitalist core) could now be accomplished by foreign investors and corporations.

U.S. TNCs were especially focused on foreign expansion in the immediate post-World War II years, leading many to view TNCs as tools of U.S. hegemony during the Cold War era. U.S. foreign policy created opportunities for U.S. firms to expand abroad, and U.S. investments created economic interests favorable to U.S. policies. Business and the flag were mutually supportive.

For example, in his 1975 book *U.S. Power and the Multinational Corporation*, IPE scholar Robert Gilpin mentions the role that Boeing played in U.S. relations with China in the 1970s. President Richard Nixon went to China in 1972 in a move to solidify U.S. hegemony relative to the USSR. He also went to sell airplanes, specifically Boeing 707s. Although American and Chinese officials made endless toasts, it was the aircraft sale that sealed the deal by providing meaningful economic benefits to both countries. Chinese purchases of Boeing aircraft later in the 1970s and Deng Xiaoping's 1979 tour of Boeing assembly facilities near Seattle were symbolic of China's commitment to modernization and the U.S. government's commitment to closer diplomatic relations with China.

Today the IPE discussion tends to focus more on how the United States advances its national interests through U.S.-based information technology companies and financial institutions than through U.S. manufacturers and energy companies. U.S.-based content

providers and social media companies dominate the Internet. For example, by the beginning of 2017, California-based Facebook had more than 1.8 billion monthly users, up from 1.1 billion just four years earlier. By the end of 2016, YouTube (owned by Google) had a global audience that watched over 1 billion hours of videos every day. To the extent that these TNCs present ideas in ways that cast a favorable light on the United States, they are a source of what Joseph Nye calls "soft power."[24] Some have argued that this soft power advantage is even more important to U.S. foreign policy in the long run than is U.S. military dominance.

Many benefits also accrue to countries whose financial institutions dominate global financial services. IPE scholar Jan Fichtner places the United States in a group he calls "Anglo-America," consisting of English-speaking countries (United States, United Kingdom, Ireland, Canada, Australia, New Zealand, and UK dependencies) with similar forms of capitalism, common law legal systems, intelligence cooperation, and deep financial ties.[25] He contends that Anglo-America as a whole has structural power in global finance. For example, the majority of trading in foreign exchange and over-the-counter (OTC) interest rate derivatives occurs in New York and London (NY–LON). Anglo-American currencies constitute 70 percent of all official foreign exchange reserves (dominated by the U.S. dollar). By 2013, Anglo-American corporations accounted for slightly more than half of the market capitalization of publicly listed corporations on global stock markets.[26] Fichtner finds that "the vast majority of countries have their largest bilateral financial relations [i.e., external deposits of banks, direct investment, and portfolio investment] with Anglo-America."[27] The Cayman Islands (a UK overseas territory) is the home of the majority of the world's hedge funds, most of whose assets are invested in and managed in the United States.[28] In 2014 Anglophone countries had half of the world's financial wealth, despite constituting only 6–7 percent of the world's population.[29] All of these data point to the continuing hegemony of the U.S. and Anglophone TNCs in global finance.

TNCs Gaining Leverage over States

Both states and TNCs control valuable resources, and they need each other. States want the investments and technologies that TNCs can offer. TNCs, for their part, desire access to the natural resources, skilled labor, and national markets in different states. (A state that fails to adequately educate and train many of its citizens and thus offers mainly unskilled labor has little to bargain with and can expect to attract sweatshop-type FDI.) Since each side has much to offer and much to gain, it would seem that mutually advantageous agreements should be easy to achieve. But it is not as simple as that.

TNCs typically seek favorable tax treatment, state-funded infrastructure, and perhaps even weakened enforcement of some government regulations. A weak state, or one with few productive resources and a weak market system, may be at a fundamental disadvantage in negotiations with TNCs. And because all states are competing for TNCs' investments, individual governments are often forced to grant many concessions to attract FDI. This is true both in less developed countries (LDCs) and in advanced industrial economies. The

lesson seems clear: TNCs are "footloose" and have many possible investment options, whereas states are rooted, like trees, in the territory they control. The corporations have a tremendous advantage and negotiations can be very one-sided. However, this need not always be the case; if states make their own investments in education, resources, infrastructure, and so forth, then they can have the upper hand.

TNCs have also become adept at extracting assistance from the government of the country in which they are headquartered. Governments will extend financial benefits to their domestic corporations because, as we noted above, the corporations can enhance countries' power in the world. Many forms of assistance today are allowed under international trade agreements, but some, like agricultural subsidies, are contested in international negotiations. It is often difficult to distinguish between assistance designed merely to serve domestic public purposes and assistance intended to help domestic corporations compete "unfairly" with foreign ones. Assistance can distort markets and channel resources to politically well-connected elites.

The advocacy organization Good Jobs First finds that between 2000 and 2015, the U.S. federal government provided large corporations at least $45 billion in grants and special tax credits.[30] In addition, assistance in the form of loans, loan guarantees, and bailout money to financial institutions in the midst of the financial crisis amounted to trillions of dollars-although it should be noted that most of the loans were repaid to the government. Whether one should interpret grants and tax credits as "corporate welfare" or good investments depends on one's assessment of who got the money and what it was used for. For example, some of the largest grants and credits authorized by the Obama administration's 2009 stimulus bill went to companies developing renewable energy to help mitigate climate change. In contrast, five of the wealthiest TNCs in the world—Google, Apple, Amazon, Facebook, and Microsoft—have received more than $2 billion in subsidies from state and local governments in the United States to build data centers.[31]

The German automaker Mercedes-Benz has also been very successful in extracting aid from government. In the early 1990s it announced plans to build a factory in the United States to produce a Mercedes sports-utility vehicle (SUV). It published its requirements for the FDI project and invited a large number of state and local governments to make bids for the factory. By 1993 the list was narrowed to three potential factory sites in South Carolina, North Carolina, and Alabama. All three states have right-to-work laws that limit union power. Alabama won the bidding by pledging to Mercedes a package worth $253 million.

The Alabama–Mercedes story highlights the bargaining power TNCs often have in negotiations with states. Alabama gave Mercedes tax abatements on machinery and equipment, improved highways and other infrastructure the company needed, and spent money on education and training that would benefit the company. The University of Alabama even agreed to run a special "Saturday School" to help the children of German Mercedes managers keep up with the higher standards in science and math back home in Germany. Alabama even offered to name a section of an interstate highway "the Mercedes-Benz autobahn." All of this was paid for by the taxpayers of Alabama. The governor of North Carolina was particularly upset by a tax break the Alabama legislature passed (labeled

by some the "Benz Bill"), which allowed Mercedes to withhold 5 percent of employees' wages to pay off Mercedes debts.

It is not surprising that a Mercedes executive claimed it was "Alabama's zeal" that was the deciding factor. In return, 1,500 workers got good-paying jobs, with the likelihood that thousands of other new jobs would be created in supplier firms, restaurants, and the like. In the following years, Alabama courted other TNCs, convincing airplane maker Airbus and carmakers Honda, Hyundai, and Toyota to build large assembly plants in the state. For Alabama and the TNCs, state financial aid created a long-term win-win relationship.

TNCs OUT OF (STATE) CONTROL?

A number of scholars contend that TNCs are increasingly escaping effective state control, as evidenced by their ability to avoid some taxation and engage in wrongdoing. Whereas states and TNCs have often mutually benefited from their courtship, in recent years the globalization of production has allowed many corporations to minimize their obligations to society and cause actual harm to some countries.

Tax Avoidance

TNCs seek to lower their tax bill or even evade taxes in order to increase profits and stay competitive globally. States often compete for foreign investment by offering lower corporate tax rates than other states. The paradox is that when states lower corporate tax rates to woo FDI, lower tax receipts make it more difficult to provide public goods that TNCs value, such as infrastructure, education, and social welfare. If all states lower corporate taxes, they all end up with less money. It is hard for all states to agree together not to lower corporate tax rates.

The Big Four global accounting firms advise TNCs on how to reduce their global taxes and take advantage of differences between countries' regulations. This reflects a more general view among many business elites that laws and regulations are "red tape" and "market barriers" rather than mechanisms to protect the public and achieve democratically determined social goals.

Corporate tax evasion and tax minimization strategies have become highly politicized. When successful, they increase income inequality and the tax burden on labor and households. Relative rates of taxation on TNCs have a bearing on the distribution of resources between and within countries. Government efforts to close corporate tax loopholes resemble a game of whack-a-mole. TNCs can use creative accounting to change where they pay most of their taxes even if they do not change where they produce or sell goods and services.

What methods do corporations use to lower their taxes? In recent years scholars have focused extensively on their use of tax havens, transfer pricing, and tax inversions. We believe that students of IPE need to be familiar with these complex methods in order to understand better the dynamics of globalization.

Tax havens are countries or jurisdictions where corporate tax rates are low and financial regulations are often relatively lax. TNCs often try to direct as much of their global profits as possible to these havens. This usually requires moving profits on paper between various affiliates of a TNC, even if the profits end up in places where the TNC does not engage in any production, have many employees, or sell many goods. These affiliates take a variety of forms, including parent companies, subsidiaries, and shell companies that do little more than facilitate business transactions. Governments find it difficult to trace all these interconnected parts of TNCs.

Economist Kimberly Clausing finds that overseas affiliates of U.S. TNCs report the majority of their income in a handful of small tax havens such as Singapore, Luxembourg, and Ireland, where few of the affiliates' employees actually work.[32] In the United States, two-thirds of Fortune 500 companies are incorporated in the tiny state of Delaware, a notorious tax haven. Delaware levies no income tax on corporations that do business outside the state, and it exempts from taxation earnings from trademarks, copyrights, and leasing. Other U.S. states accuse it of depriving them of billions of dollars of corporate tax revenue.

The European Parliamentary Research Service estimates that EU member states lose between $55 billion and $76 billion every year due to corporate tax avoidance. Since 2010, European tax officials have persistently investigated the tax practices of (among others) Google, Apple, Starbucks, Amazon, IKEA, Microsoft, and Gap. These corporations have used subsidiaries and shell companies to channel earnings to low- or no-tax countries such as Ireland, the Netherlands, Luxembourg, and Bermuda. The United Kingdom, France, and Italy have demanded back taxes, often ranging in the hundreds of millions of dollars for individual companies. The effective tax rates of many of these companies have been low relative to their level of sales and number of employees in various EU countries. For example, Google routes most of its billions of dollars of global (non-U.S.) royalties from intellectual property to a subsidiary in Bermuda, where there is no corporate income tax. The subsidiary is registered to a post office box in the capital Hamilton!

A 2016 investigation of TNC taxation in New Zealand by the *Herald* (NZ) newspaper found that the subsidiaries of 20 TNCs that had combined annual sales of $10 billion in New Zealand managed to pay almost no corporate income tax there in 2014.[33] The affiliates claimed a profit rate in New Zealand of only 1.3 percent, even though their parent companies (including ExxonMobil, Apple, Google, and Chevron) averaged profit rates of over 20 percent. This kind of profit shifting puts solely domestic companies at a competitive disadvantage.

Another TNC practice that is gaining increased attention in recent years is transfer pricing. When affiliates of the same TNC trade with each other, the prices they charge often do not reflect the true market value of the goods and services. Why would a TNC declare artificial import and export prices? Typically, a TNC is trying to lower its bill for tariffs on imports. It is also a way to transfer profits (on paper) from a company unit in a high-tax country to a unit in a low-tax one, thus reducing the TNC's global tax bill. For example, a TNC can transfer control of its patents, trademarks, and other intellectual property to a shell company in a tax haven, then license the use of the intellectual property to other parts of the company at high fees so that more profits end up in the tax haven. Governments have a hard time detecting most mispricing because it is very expensive to audit companies in a world with such diverse transactions and high volumes of trade.

One of the most controversial ways to lower taxes is through a tax inversion, by which a large corporation in one country sells itself to (or buys) a smaller corporation in another country and then reincorporates there. Nothing about the operations of the corporation change, but the tax home is relocated to a lower-taxing country. Since 2012, a number of

U.S. TNCs, including Medtronic and Burger King, have reincorporated in low-tax countries to avoid U.S. taxes on their global revenues. Pharmaceutical company Pfizer tried to carry out an inversion with the Irish company Allergan in 2016, even though more than 40 percent of Pfizer's drug sales are in the United States. There was such a firestorm of criticism in the United States that the U.S. Treasury Department changed rules to make inversions less attractive. In large part due to inversions, Ireland's GDP in 2015 grew by an astonishing 26 percent, but this was an increase on paper, not in the real Irish economy.

U.S.-based TNCs engage in a unique form of tax avoidance due to particulars in U.S. tax laws. U.S.-based TNCs and their overseas affiliates do not pay U.S. corporate income tax on foreign profits until they repatriate the money to the United States. Unhappy about the U.S. corporate tax rate of 35 percent, these TNCs have accumulated over $2 trillion in tax-deferred overseas earnings. In 2015, Apple and Pfizer each had approximately $200 billion in tax-deferred offshore profits, and Microsoft and General Electric each held more than $100 billion. If they were to bring these profits back to the United States, they would pay tens of billions of dollars in U.S. corporate income tax (although they would be credited for taxes already paid to foreign governments so that there would not be double taxation). The U.S. Treasury and the U.S. economy would benefit from the repatriation of these earnings. In the past, Congress has established temporarily lower corporate tax rates to encourage repatriation. For example, a repatriation holiday in 2004, when the corporate income tax rate was temporarily set at 5.25 percent, spurred U.S. TNCs to bring back $362 billion. At President Trump's urging, Congress passed another repatriation holiday in its December 2017 tax bill, which lowered tax rates on U.S. corporations'repatriated profits to between 8 and 15.5 percent.

Kimberly Clausing estimates that worldwide corporate tax avoidance deprived governments of at least $280 billion in tax revenues in 2012; the U.S. government alone lost revenues of between $77 billion and $111 billion.[34] Most of us would expect governments to crack down on this in order to boost government revenues (and perhaps give tax relief to lower-income households). But absent institutionalized sharing of information between sovereign states, it is difficult to detect tax avoidance. Many forms of tax minimization are technically legal. And some governments fear that crackdowns will scare away investors.

So what are governments doing? For a number of years, the OECD has been trying to tackle base erosion and profit shifting (BEPS)—their term for the process whereby TNCs artificially shift profits to low-tax locations where they have very little real economic activity. Many TNCs establish a legal "tax home" that is different from the countries where most of their employees and sales exist. The OECD's efforts paid off in 2017 when nearly 70 countries signed a Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI). The MLI includes a number of rules to reduce corporate tax avoidance. Notably, the Trump administration decided that the United States would not sign the Convention.

Recent tax scandals (see Box 6.3) have spurred some governments to work harder to stop tax cheats. International civil society groups such as the Global Alliance for Tax Justice have

also pressured states to crack down on corporate tax avoidance, which disproportionately hurts low-income countries. Some scholars call for taxing TNCs on the basis of where their real economic activity is, measured by sales, assets, or employees. For example, each country could be assigned a proportion of a TNC's global income equal to the proportion of the TNC's global workforce in that country. That would make it much harder for TNCs to minimize taxes. Since 2015, EU banks have had to report their profits and taxes paid on a country-by-country basis. In 2016, the EU Commission issued an Anti Tax Avoidance Directive to help officials better combat the tax avoidance strategies of TNCs.

INTERNATIONAL TAX SCANDALS

Since 2010 a number of whistleblowers have leaked documents from banks and law firms that have caused global tax scandals. The scandals reveal methods by which TNCs and wealthy individuals evade taxes and the involvement of government officials in facilitating or participating in tax evasion. The globalization of production and finance have made it easier for companies to use shell companies and tax havens to disguise their profits and shift them to low-tax jurisdictions.

In a major scandal in 2014 called LuxLeaks, the International Consortium of Investigative Journalists (ICIJ), using 28,000 pages of documents leaked by a PricewaterhouseCoopers whistleblower, revealed that in the 2000s the Luxembourg tax authorities had issued secret tax rulings to more than 340 TNCs which helped them save billions of dollars on their global tax bills. [a] Basically, these authorities helped corporations such as Apple, FedEx, IKEA, Fiat, and Pepsi move profits through Luxembourg to avoid taxation elsewhere. In 2015, the EU Commission began investigations of tax avoidance deals between Amazon and Luxembourg, McDonald's and Luxembourg, Apple and Ireland, and AB InBev and Belgium. Some American officials believed that the Commission was deliberately targeting mostly U.S. companies. In late 2016, leaked German diplomatic cables revealed that former long-time Luxembourg prime minister Jean-Claude Juncker had thwarted efforts to reduce harmful tax competition in the European Union. [b] Ironically, he has been president of the EU Commission, which in 2016 drafted a plan to reduce corporate tax avoidance in the European Union! A group of European civil society groups contended in a 2016 report that, despite the LuxLeaks scandal, European governments, led by Luxembourg and Belgium, issued hundreds more secret tax rulings favorable to TNCs between 2013 and 2015. [c] This demonstrates that EU governments are competing for TNC taxes by offering the lowest tax rates, even if it deprives other governments of legitimate tax revenues.

In a different case, between 2007 and 2013 U.S. authorities investigated Swiss banks for helping thousands of U.S. citizens hide income from the Internal Revenue Service. Authorities eventually fined some banks hundreds of millions of dollars for facilitating tax evasion and reached agreements with dozens of others to divulge information in order to avoid prosecution. As a result of pressure on these banks and the Swiss government, the U.S. government recovered more than $8 billion in taxes and penalties from more than 50,000 U.S. citizens. Another Swiss tax scandal called "Swiss Leaks" erupted in 2015 when the ICIJ released documents detailing that the Swiss branch of global bank HSBC held more than $100 billion in private banking accounts of thousands of wealthy non-Swiss account holders suspected of hiding income from their governments' tax authorities. [d]

Finally, another extraordinary tax scandal unfolded in 2016 when the ICIJ obtained

11.5 million documents called the Panama Papers. [e] The documents were from Mossack Fonesca, a large offshore law firm that helped wealthy global elites take advantage of tax havens in Panama and elsewhere. The ICIJ has collaborated with many journalists to analyze the Papers. They reveal that politicians and businessmen from around the world had Fonesca set up offshore companies in the British Virgin Islands, Wyoming, and other tax havens. They suggest that nefarious activities, including tax evasion, embezzlement, bribe-taking, and money laundering, are routinely conducted by wealthy elites. Among other things, the Papers describe shell companies owned by 29 billionaires, dozens of public officials around the world, and the leaders (or their close associates and relatives) of China, Mexico, Syria, Saudi Arabia, Iceland, Russia, Ukraine, and Pakistan. For many, it is distressing to learn of tax evasion at the highest levels, corruption at the heart of political life, and widespread illegal business actions.

References

[a] For more details of the scandal, see the website of the International Consortium of Investigative Journalists at www.icij.org/project/luxembourg-leaks.

[b] See Simon Bower, "Jean-Claude Juncker Blocked EU Curbs on Tax Avoidance, Cables Show," *The Guardian*, January 1, 2017, at www.theguardian.com/business/2017/jan/01/jean-claude-juncker-blocked-eu-curbs-on--tax-avoidance-cables-show.

[c] European Network on Debt and Development (Eurodad), "*Survival of the Richest: Europe's Role in Supporting an Unjust Global Tax System 2016*," 2016, at http://eurodad.org/files/pdf/5846bcd64c8af.pdf.

[d] For more details of the scandal, see the website of the International Consortium of Investigative Journalists at www.icij.org/project/swiss-leaks.

[e] For more details of the scandal, see the website of the International Consortium of Investigative Journalists at https://panamapapers.icij.org/.

Corporate Wrongdoing

While globalization of production has made it more challenging for states to tax TNCs, corporate wrongdoing seems to have increased as governments reduce some forms of regulation and economic oversight. The global financial crisis weakened liberal arguments that the market should be left to its own devices, in part because the crisis provided evidence that financial institutions, credit ratings agencies, and insurance companies commonly carried out imprudent policies and broke laws in a number of cases. Since 2008, even broader critiques have been leveled at corporations. Investigations have uncovered corporate manipulation of markets and instances of outright criminality by some of the world's leading corporations.

A shocking example of market manipulation was discovered in financial markets in 2012. The London Interbank Offered Rate (LIBOR) is set each day by the world's largest banks. Each bank independently estimates a rate at which it could borrow from other banks. Their offers are averaged to produce the LIBOR, a benchmark rate in financial markets upon which interest rates are set for mortgages, credit cards, student loans, and corporate loans. The banks were found to have been conspiring since 2003 to manipulate the LIBOR up and down in order to enhance their profits. The banks paid more than $6 billion in fines for these actions. In 2014, many of the same banks were found to have manipulated another benchmark rate in the foreign exchange market. Five banks paid fines and penalties of nearly $9 billion for this misbehavior. These brazen acts of criminality by the world's most important banks, on top of the misbehavior that led to the financial crisis, demonstrated that state regulations were too lax and that powerful market actors could thwart competition with relative ease.

Another example of audacious corporate wrongdoing was Volkswagen's manipulation of software in vehicles to disguise the fact that its diesel automobiles did not meet U.S. and

EU emissions standards. In mid-2016, VW reached a settlement with the U.S. government to pay penalties of nearly $16 billion. At the end of 2016, VW pled guilty to criminal charges in the United States and agreed to pay $4.3 billion more in fines. Six of its German executives were indicted in the United States on criminal charges. In many other corporate scandals, executives have avoided criminal charges and prison. The centrality of these corporations to the global economy and employment seems to have dissuaded officials from penalizing the companies in a manner that would destroy their commercial viability.

Although we cannot easily calculate how pervasive corporate crime is in the world, we do have information on cases of corporate wrongdoing prosecuted in developed countries. For example, through analysis of data from the U.S. Department of Justice and U.S. regulatory agencies, Good Jobs First has calculated that from 2010 to mid-2016, U.S. and foreign corporations paid penalties in the United States of over $190 billion for various offenses. Banks accounted for $160 billion of the fines and settlements for: abuses in the mortgage and securities sectors; violations of U.S. sanctions on countries such as Iran and Sudan; manipulation of the foreign exchange market rates and the LIBOR rate; and helping U.S. citizens evade taxes.[35] Other fines and penalties levied on corporations in the second half of 2016 included:

- A $40 million U.S. penalty on Princess Cruise Lines for a years-long scheme of illegally discharging waste into the ocean through a ship's "magic pipe";
- A $7.2 billion U.S. penalty on Deutsche Bank related to pre-2008 mortgage-backed securities;
- A $3.2 billion fine by the United States and Brazil on Odebrecht SA, a large construction company, for bribery;
- Fines of $205 million on Brazilian aircraft maker Embraer for paying bribes through its U.S. affiliate to government officials in four countries; and
- Fines in 2016 worth $7.7 billion imposed by governments around the world on corporations engaging in anti-competitive (cartel) practices, including price-fixing.

Structuralists Steve Tombs and David Whyte make one of the most radical critiques of corporations, arguing that criminality is at the heart of global corporations. They point out that the lead corporations in global supply chains put so much pressure on suppliers to lower costs that the suppliers often must break the law to stay in business.[36] They note that social harms caused by corporations are often not defined as crimes. Tombs and Whyte also recount "everyday" corporate crimes in the United Kingdom, including financial fraud, price-fixing, food poisoning, pollution, and causing work-related diseases and deaths. These crimes, they argue, "magnify existing social divisions and in equalities" because disempowered groups in society are the "most victimized."[37]

THE EFFECTS OF TNCS AND AUTOMATION ON WORKERS

The globalization of production has had profound effects on workers in both developed and developing countries. While highly skilled workers tend to benefit from the spread of global value chains, the effects on low-skilled workers varies from region to region. There is less need for unskilled workers in industrialized countries, in part because industry has shifted to emerging countries and because new technologies—especially computers and robotics—make it possible to automate repetitive production tasks. Economist David Autor points to evidence that computerization is making even middle-skilled workers such as clerical workers, travel agents, store salespersons, and warehouse workers increasingly unnecessary.[38]

In the face of these trends, a number of economists worry that as automation becomes more widespread, a growing segment of the population in developed countries will not be able to find employment, even if they try to increase their skill levels. Many highly efficient production facilities will simply not need as many workers, even though they produce more goods. This could also become a worse problem in developing countries, where robotics and information technology may even make once-attractive cheap labor unnecessary. The urban poor and migrants from rural areas will find it harder to find manufacturing jobs that in previous generations were crucial to upward social mobility in places such as Mexico and China. The economic, social, and political consequences could be dramatic. The viability of pension systems could be threatened if a much smaller proportion of the population pays payroll taxes. Mass unemployment would lower overall demand, making it harder for companies to sell goods and services. Income inequality between low- and high-skilled workers would increase even more. Paradoxically, campaigns to raise the minimum wage to help low-skilled workers could incentivize companies to invest in even more job-replacing information technology and machinery.

Effects of Automation and Globalized Production on Workers in Developed Countries

Many scholars argue that technology and changes in the production structure are increasing inequality. Economist Richard Freeman argues that unless the "prosperity that the robots produce" is shared, we "risk producing a new robot-age feudalism, with workers captive to a small number of overlords who own robotic technology."[39] Redistribution of gains accruing to owners of capital has already proven politically difficult in developed countries, despite a financial crisis and growing inequality.

Political scientist Ronald Inglehart shows that automation and outsourcing have eliminated many manufacturing jobs in developed countries, with displaced workers often turning to more precarious, lower-paying jobs in services.[40] High-tech industries are not employing a larger share of the total workforce, and computer-based "expert systems" are

even replacing many middle-class skilled workers. The gains from productivity growth are mainly captured by elites. Inglehart observes, "As expert systems replace people, market forces alone could conceivably produce a situation in which a tiny but extremely well-paid minority directs the economy, while the majority have precarious jobs, serving the minority as gardeners, waiters, nannies, and hairdressers—a future foreshadowed by the social structure of Silicon Valley today."[41]

One outcome of automation and production outsourcing is the rise of what British economist Guy Standing calls the "precariat"—those with flexible labor contracts, temporary jobs, or part-time jobs who lack an occupational identity.[42] They usually do not receive non-wage benefits such as pensions from their employers, and they might not be eligible for state benefits like unemployment insurance. Standing describes them as "denizens"—inhabitants lacking the full rights of citizens. Despite their insecurity, they tend to reject mainstream politics and labor unions, turning instead to protests and anti-austerity movements. Standing expects this precar-iat to experience an increase in anxiety, anomie, alienation, and anger.

The OECD confirms some of Guy Standing's observations about the precariat. One-third of all jobs in OECD countries are now "non-standard"—defined as temporary and part-time jobs and self-employment. From 1995 to 2013, more than half of all new jobs created were "non-standard."[43] In addition, economists Angus Deaton and Anne Case find evidence suggesting a link between the declining fortunes of blue-collar U.S. workers and health.[44] Demographic data shows a dramatic rise in the mortality rate of white Americans aged 44 to 54 from 1998 to 2015, especially due to drug and alcohol abuse and suicide. These "deaths of despair" seem to be tied in part to declining prospects for good jobs, they claim_ "Ultimately, we see our story as the collapse of the white, high-school-educated working class after its heyday in the early 1970s, and the pathologies that accompany that decline"[45]

To the extent that globalization of production contributes to wage stagnation and declining union membership in developed countries, it helps cause other social problems. Wage inequality tends to be higher in countries with fewer labor unions and with fewer collective agreements between management and unions that apply to an entire industry, not just to union members.[46] And wage stagnation since 1980 may be one of the key reasons why the personal savings rate in the United States has plummeted while household indebtedness has soared.[47] These findings challenge claims that globalized production leads to social betterment.

Globalization has created intense competition, threatening traditional industries in developed countries that typically employ older workers and creating more insecure employment for younger workers. In combination with demographic changes that have increased the proportion of elderly people in developed countries, these factors are undermining retirement incomes. Structuralists view exploitation not only occurring during workers' participation in the labor force but also in retirement. Income security in old age usually requires a pension, whether provided by the state or a previous private

employer. In the United States, a growing proportion of the labor force, especially those in the precariat, receive no pension from their employer. Rana Foroohar argues that "our retirement system has been hijacked by finance."[48] Workers are now responsible for funding a greater share of their pensions, all the while paying high fees to those who manage their retirement funds. Many private companies have switched from defined-benefit to defined-contribution pensions such as 401(k) plans that shift risks from companies to employees.

In addition, governments in developed countries have promised workers public pensions far in excess of the money they are setting aside to fund these commitments in the future. Demographic trends promise a crisis in the near future in Europe, Japan, and even China, where rapidly aging populations will have to be supported in retirement by a proportionally smaller active labor force. To deal with pension and social security solvency problems, some governments have already cut pension payments or signaled that cuts will be inevitable in the future. Facing bankruptcy, the U.S. city of Detroit and the territory of Puerto Rico have significantly reduced payments to retirees. Many corporations have used bankruptcy proceedings to shed obligations for so-called "legacy costs" such as health care and pensions that previous workers—now retirees—were promised. To many workers, it feels as if their nest eggs have been stolen from them.

One proposed response to the dystopian trends discussed in this section is the establishment of a "guaranteed basic income" that would provide every citizen of a country a minimum income, regardless of whether or not they were working.[49] In 2015, Switzerland had a referendum on such a scheme, but it was soundly rejected. In 2017, Finland became the first European country to launch a guaranteed basic income. The two-year pilot program gives 2,000 unemployed Finns each about $587 per month, even if they find a job. Proposals for a guaranteed minimum income are also being considered elsewhere (mostly at a sub-national level). Even if adopted in other countries, there would be difficult political choices, such as how a guaranteed basic income would be funded and whether it would be extended to resident non-citizens.

TNCs and Workers in Developing Countries

IPE scholars also study how globalized production is affecting labor in developing countries. Liberal scholars stress that globalization has created unprecedented job opportunities for labor in developing countries, raising the living standards of tens of millions of people. However, structuralist scholars argue that globalized production fails to lift many workers out of poverty. Nicola Phillips and Fabiola Mieres point out that lead firms in GVCs continuously force producers and suppliers to cut costs.[50] The intense competition among many suppliers leads them to limit labor costs and try to prevent labor from having a collective voice (e.g., in strong unions). According to Phillips and Mieres, "A direct consequence of this imperative is the global expansion of precarious, insecure and exploitative work, performed by a highly vulnerable and disenfranchised workforce, of which informal, migrant, and contract workers have come to be the primary

constituents."[51]

The globalization of production affects workers' rights in various ways. Developing countries that participate in global value chains through subcontracting to their domestic firms tend to have weak labor rights and suppress labor's income. Despite this, some IPE scholars have found that the affiliates of TNCs in developing countries tend to pay higher wages than domestic companies. However, Layna Mosley and David Singer stress that local governments, institutions, and choices of labor unions determine how globalized production will affect labor.[52] And TNCs will have varying effects on labor depending on TNCs' home countries, what kind of goods the TNCs manufacture, and which countries their main consumers are in.[53]

Kate Macdonald finds that TNCs have helped improve working conditions at the bottom of garment and coffee chains but have done little to raise basic incomes of workers.[54] She also finds that corporate supply chain initiatives rarely support the organization or unionization of workers and farmers. In contrast, NGO-led fair-trade initiatives do raise workers' incomes. Her results suggest that nonstate schemes to improve supply chains do not usually empower workers at the bottom of the chains or enhance their economic status. We may be placing too much faith in voluntary corporate social responsibility schemes to change socioeconomic conditions.

From a Marxist perspective, Benjamin Selwyn sees lead firms using global production networks to increase exploitation of workers.[55] While TNCs take advantage of cheap labor by moving production to developing countries, they can also resist demands for higher wages and benefits in developed countries just by threatening to outsource more production. And cheap imports from Asia also help companies slow or eliminate wage growth in developed countries. Dividing the labor force across different countries in the production chain also helps prevent labor solidarity.[56]

THE CHANGING PRODUCTION STRUCTURE: EMERGING ECONOMIES AND SOVEREIGN WEALTH FUNDS

Change and uncertainty are the hallmarks of this period of transition in the global economy and international relations. Nevertheless, we can identify some powerful currents that are likely to affect the pattern of FDI flows and perhaps the behavior of TNCs. The developments we discuss here raise many crucial questions, making this an exciting time for students of IPE to study global production.

In response to intensified competition and changes in communications and transportation technologies, global value chains have multiplied, linking together multiple partners and suppliers from around the world to collaborate and share in the finance, design, and production of new products. Lead TNCs like to coordinate these chains without owning most of the firms in them in order to spread the potential risks of operating in a more competitive and uncertain environment. When there are changes in global demand, TNCs find it easier and less costly to disentangle themselves from relationships with suppliers than to close a wholly owned affiliate. And depending on the complexity of the product, TNCs can gain cost and skill advantages by outsourcing sizeable chunks of their operations.

A potentially game-changing development, as we have alluded to already, is the spectacular economic growth of countries like China and India. Just as the rise of Japan and the newly industrialized countries spawned successful competitors to Western TNCs in previous years, we are now seeing enterprises from countries like Brazil, Russia, India, and China (the BRICs) challenge the dominance of Western TNCs. Whereas global business used to be a "one-way street" benefiting Northern TNCs, it is now a two-way process, with TNCs from the North and the BRICs "competing with everyone from everywhere for everything."[57]

For example, developing countries are no longer just large recipients of FDI; they are becoming global investors themselves. FDI outflows from developing countries were 26 percent of world outflows in 2016, compared to just 15 percent in 2006.[58] However, if we look at the 100 largest non-financial TNCs in the world as measured by their foreign assets, we find that 92 are still based in a developed country.[59] To join the top 100 foreign asset holders, TNCs from developing countries such as China will need to make large overseas investments for many more years. They are far behind.

Whereas some TNCs are delinking their interests from those of their home countries, others are stealthily being used by states for offensive mercantilist purposes. For example, state-owned TNCs, as their name implies, are majority owned or wholly owned by a country's government. More than half of China's outward FDI is attributable to state-owned enterprises.[60] This control enables the Chinese state to underwrite the development of "national champions" to compete against traditional TNCs in world markets and to

direct foreign investment to resource-rich countries, thereby ensuring access to the minerals, energy, and agricultural products that are necessary to fuel China's spectacular economic growth.

State-owned enterprises from China and other countries have gained a much larger share of international mergers and acquisitions in recent years. As such, they have raised a number of questions, such as whether they receive unfair support from their home government when making overseas acquisitions and whether they have non-commercial goals such as espionage and acquiring sensitive technology. Similarly, sovereign wealth funds (SWFs), which are quasi-independent bodies that manage pools of capital on behalf of governments, have become important shapers of global production. They tend to be managed by financial experts who ultimately answer to political elites but who act autonomously within a set of state directives. The amount of assets controlled by SWFs rose from just $500 million in 1990 to almost $7.4 trillion in early 2017. SWFs can be used for mercantilist purposes, but they also usually have mandates to seek high returns. Scholars have debated whether they are used to advance countries' geopolitical interests or simply act like private investment funds to maximize returns. China's China Investment Fund has played an important role in financing Chinese projects in Africa and has acquired stakes in foreign companies to secure China's access to raw materials.[61] Norway's Government Pension Fund—the world's largest SWF—acts as an agent of Norwegian foreign policy through the assets it chooses to invest in, the pressure it places on companies in which it holds stakes, and the divestments it makes from companies tied to human rights violations or illegal activities. For example, it has recently divested from fossil fuel companies, from companies tied to economic activities in Moroccan-occupied Western Sahara, and from more than two dozen Asian companies causing deforestation.

Often lacking accountability to regulators and voters, SWFs pose risks because of their secrecy and potential investments in strategically important industries.[62] Larry Summers, the former director of the National Economic Council in the Obama administration, sees a potential threat to the liberal global system from mercantilist actions by foreign governments which, as he puts it, might ask an "airline to fly to their country, want a bank to do business in their country, or want a rival to their country's champion disabled."[63] Defenders of SWFs and state-owned TNCs point out that they have been operating for some time with no evidence that they are pursuing anything other than healthy financial returns.

Does the emergence of the BRICs, SWFs, and state-owned TNCs as important sources of FDI change the role of privately owned TNCs in the global economy? Will the state-owned TNCs act with greater concern for labor and environmental rights than private TNCs or will they be compelled to behave like all the others by the pressures of global competition? Whether SWFs and TNCs from emerging countries end up rewriting the rules of the liberal global system or not, there is little doubt that they symbolize a rebalancing of power relations in that system.

CONCLUSION

The global production structure has undergone rapid change in the last few decades. TNCs have been driven to invest abroad by the competitive environment found in transnational markets, the policy liberalization that encourages that competition, and the technological changes that make foreign investment more efficient. Although the majority of FDI flows between developed countries, a much larger proportion now ends up in developing countries, fueling industrialization in Asia and Latin America. Liberals view these changes as increasing global growth and benefiting consumers, yet mercantilists worry that they are leading to deindustrialization that hurts workers and increases inequality in developed countries.

TNCs often hold significant foreign assets. Technology and financial corporations have grown much faster than traditional manufacturers, indicating that service-based industries are becoming much more globalized. Many TNCs govern complex global value chains linking suppliers and assemblers around the world. Countries strive to upgrade their position in GVCs to capture more profits from R&D, design, and branding. TNCs depend on stable rules governing property rights, trade, and investment protection. They rely on states for a rule of law and many subsidies, but at the same time they actively seek to avoid state taxation and sometimes manipulate global markets. In some industries, production has become more concentrated in the hands of a smaller number of large corporations, raising questions about how competitive some markets really are.

Globalized production, automation of manufacturing, and the digital revolution are placing many stresses on workers. Job insecurity, lack of adequate pensions, and the rise of precarious employment are factors leading some scholars to advocate for a guaranteed basic income as a way to ensure social equity and sufficient consumer demand. Meanwhile, the shift of production to China and the growth of sovereign wealth funds are threatening the dominance of the EU, the United States, and Japan over the global production structure.

Finally, we have to ask what long-term impacts the 2008 financial crisis and the recent wave of populism will have on FDI and TNCs. Declining support among elites and citizens for the globalization of production might mean a period of retrenchment, with less open borders, less international trade, and less FDI. Public skepticism about the actions of large corporations and banks, including TNCs, may galvanize politicians to more severely regulate their activities. History reminds us that in response to severe economic crises, political forces can reshape the international order, as they did for example in the 1930s.

KEY TERMS

transnational corporations (TNCs) 127
foreign direct investment (FDI) 128
intermediate goods 128
outsourcing 128
offshoring 131
scaling 132
vertically integrated 137
global value chain (GVC) 137
corporate social responsibility 138
investor–state dispute settlement (ISDS) 140
tax havens 144
transfer pricing 145
tax inversion 145
base erosion and profit shifting (BEPS) 146
precariat 150
guaranteed basic income 151
sovereign wealth funds (SWFs) 153

DISCUSSION QUESTIONS

1. Why do TNCs engage in foreign direct investment? Explain whether or not the following statement is accurate: "Most TNCs invest in less developed countries because of the low wages that they can pay there."
2. Explain recent changes in the pattern of FDI and in the organization of TNCs. What are some of the implications of these changes?
3. In what ways are global value chains beneficial to developed and developing countries?
4. How should leaders of developed countries respond to the effects of globalized production on their domestic corporations and workers?
5. Discuss the ways in which states and TNCs are mutually reliant on each other. How has the balance of power between the two changed in the last two decades?

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CHAPTER 7
The International Trade Structure



A cargo ship in the Port of Tacoma in Washington State.

Source: Shutterstock/AP Photo/Ted S. Warren.

Responding to the economic and political crises of our day requires that we restore a healthy balance between an open global economy and the prerogatives of the nation state. That requires us to be honest about trade's consequences —not just the economic opportunities they create for our businesses and consumers, but the stresses they generate for our social compacts.

Dani Rodrik[1]

Donald Trump made opposition to free trade a cornerstone of his presidential election campaign. As president, he has begun to make good on his promises, abandoning the Trans-Pacific Partnership Agreement (TPP) and negotiating with Canada and Mexico to revise the North American Free Trade Agreement (NAFTA). In the summer of 2017 the

Trump administration suggested it might investigate Chinese trade practices—including theft of intellectual property from U.S. corporations—as a lead up to unilateral U.S. actions to punish China. Many economic liberal scholars worry that the United States and China will get into a harmful trade war.

The tensions over trade are a sign of rising resistance to the postwar liberal world order. The negotiation of many multilateral, regional, and bilateral free-trade agreements during the heyday of globalization from 1990 to 2008 reflected confidence that expanded imports and exports would raise economic growth rates in most countries. After the global financial crisis that started in 2007, citizens of developed industrialized countries became more nationalistic and demanded greater trade protectionism. Political parties on the left had traditionally harbored reservations about free trade's effects on labor and the environment, although they also promoted new trade agreements. The political right in Europe and the United States had traditionally pushed for more free trade. However, in the 2010s important segments of both the left and right blamed globalization for destroying national industries and good jobs. Populists and nationalists in the EU found that bashing free trade appealed to those who felt left behind during European integration. Candidate Trump found free trade to be a convenient scapegoat to explain the demise of the American dream. Ironically, China has now positioned itself as the defender of free trade even though for decades it has carefully managed its trade with the rest of the world.

The unprecedented increase in trade in the last 50 years has created high levels of interdependence between countries. The United States and its allies formed the General Agreement on Tariffs and Trade (GATT) in 1947 to lower trade barriers and promote the West's political objectives during the Cold War. With the creation in 1995 of the World Trade Organization (WTO), which administers the revised GATT and other trade agreements, global trade liberalization accelerated. Yet, since the 2000s new multilateral trade negotiations at the WTO have been virtually deadlocked. Regional trade blocs such as the European Union and the Gulf Cooperation Council have been facing crises. The United States and the United Kingdom are now upsetting some of their long-standing trade relationships.

This chapter surveys a variety of changes that have occurred primarily in the post-World War II global trade structure. Competition, technology, and state power shape how the "game" of trade is played. In addition, large corporations that import and export affect trade through their established business practices, alliances with other companies, and lobbying of government officials. For developed and developing countries alike, export-based industries are major sources of income and employment, making trade one of the most politically contentious issues in the international political economy.

Based on these trends, national economies have become much more reliant on—and sensitive to—trade. As Figure 7.1 indicates, international trade as a percentage of world GDP rose from 39 percent in 1990 to 58 percent in 2015. Since 1990, trade has become a very large component of EU GDP, reflecting the deep integration of this trading bloc. China's trade-to-GDP ratio skyrocketed from 1990 to 2008, but it has declined significantly since then, not because China is trading less but because its domestic economy

has become much larger. The United States has a relatively low ratio because its domestic economy is the largest in the world. Because trade creates economic and social interdependence, states are compelled to regulate it in order to maximize its benefits and limit its costs to their countries. As a result, one state's trade policies can easily impose socioeconomic adjustment costs on other states. Without a set of international trade rules, nationalistic trade policies could easily undermine the global production structure.

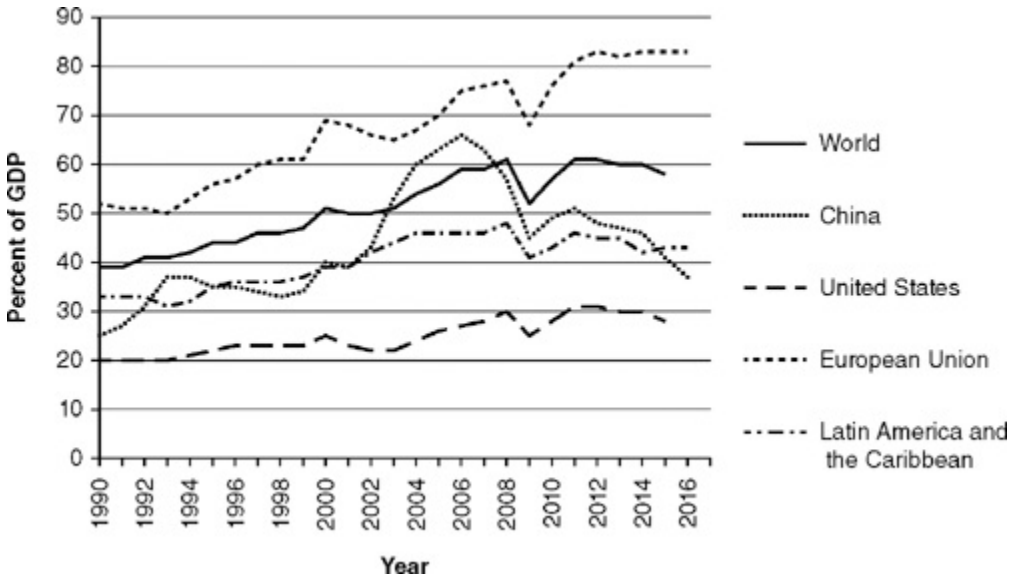


FIGURE 7.1
Trade (Exports + Imports) as a Percentage of GDP for Selected Countries and Regions, 1990–2016.

Source: Data from World Bank, *World Development Indicators*, at http://databank.worldbank.org/data/reports.aspx?-source=…series=NE.TRD.GNFS.ZScountry=.

We present five major theses in this chapter:

- Free trade is an aspiration, not a reality. All trade is shaped to varying degrees by the distribution of power between states and by state laws, regulations, and policies. To fully understand trade, we have to consider the political context in which it occurs,
- Trade controversies today are rooted in efforts by businesses and nation-states to capture the benefits of imports and exports while limiting trade's negative effects on producers and society.
- The negative effects of the global financial crisis and neoliberalism have accelerated resistance to further liberalization of trade in manufactured goods and agricultural products, especially in the highly industrialized countries. Global trade negotiations are at an impasse.
- The "losers" under the current trade system are increasingly well organized politically, increasing the chances that their demands for better controls on both production and globalization will have political traction in the coming years.

- The digital revolution has made liberalization of trade in services an important issue in international trade negotiations. Countries with leading technology-based corporations are spearheading the effort to gain access to new markets for digitally delivered services throughout the world.

PERSPECTIVES ON INTERNATIONAL TRADE

Each of the IPE perspectives views trade through a different lens. Today, a majority of academics and elites in developed countries still favor progressive reductions in barriers to imports and exports. And yet, as we will see, most nations tend to behave in a mercantilist fashion, adopting protectionist measures when their national interests are threatened. Some nations are concerned that trade may be more exploitative than mutually advantageous.

Economic Liberal Views on Trade

Many economic liberal ideals about trade are rooted in the late eighteenth- and early nineteenth-century views of Adam Smith and David Ricardo, who were reacting to what they viewed as mercantilist abuses at the time. They proposed a liberal theory of trade that dominated British policy for more than a hundred years. Smith, of course, generally advocated laissez-faire policies (see Chapter 2). Ricardo went one step further; his work on the law of comparative advantage demonstrated that free trade increased efficiency and had the potential to make every country better off. It mattered little who produced the goods, where, or under what circumstances, as long as individuals were free to buy and sell them on open international markets.

The law of comparative advantage suggests that nations should specialize in and export what they are relatively highly efficient at producing and import what they are relatively least efficient at producing. In modern economic discourse, we say that a country should specialize in producing a good if it can produce the good at a lower "opportunity cost" than other countries. The law of comparative advantage invites countries to compare the cost of producing an item themselves with the availability and costs of buying it from others, and to make a logical and efficient choice between the two. All countries should gain from trade if they follow their comparative advantage. In Ricardo's day, as we saw in Chapter 2, the law of comparative advantage specified that Great Britain should import food grains rather than produce so much of them at home, because the cost of imports was comparatively lower than the cost of local production.

Despite the rise in anti-globalization discourse in the last decade, many officials and scholars still believe that the benefits of a liberal, open international trade system far outweigh its negative effects.[2] For example, many studies find evidence that increased trade reduces the likelihood of war between countries. Economic liberals also emphasize that it is rational for states to agree on a common set of international rules that will maximize the gains from trade in a competitive global economy. With reduced tariffs and more common regulations, trade will increase and production will become more efficient in all countries. Liberals emphasize that trade liberalization can reduce poverty in developing countries by increasing growth. According to Daniel Nielsen, observational analyses mostly find that trade has positive effects on poverty reduction, but these effects are contingent on other measures being taken such as government investments.[3]

A common criticism of liberal trade agreements is that they prioritize business over the environment, but liberals assert that there is no necessary connection between trade and ecological harm. Samuel Barkin states that multilateral trade treaties generally *do not* prevent states from enacting environmental protection policies (unless the policies are discriminatory to foreign companies). Growth of production and consumption is what increases environmental harm, not so much trade rules. Ironically, he argues, global trade that is *least* governed by multilateral trade institutions, including trade in natural resources, agricultural goods, and illegal goods, is connected to the most severe environmental damage.[4]

Mercantilist Views on Trade

From the sixteenth through the eighteenth centuries, there were no international trade rules as we know them today. Early European states aggressively sought to generate trade surpluses. To help local industries get off the ground, leaders discouraged imports so that people would have to buy locally produced goods. Mercantilists used trade to enhance their wealth, power, and prestige in relation to other states. In their fabulous collection of vignettes about trade since the 1400s, historians Kenneth Pomeranz and Steven Topik point out that states often adopted a mix of mercantilist, imperialistic, and free-trade policies to advance their interests, depending on their level of economic development and changes in technology.[5] They argue that "there are virtually no examples of successful industrialization with pure free trade (or for that matter with pure self-sufficiency). Even in the heyday of free trade, the United States and Germany achieved their impressive late nineteenth- and early twentieth-century growth behind high tariff walls; many other countries also had some kind of protection."[6]

As we outlined in Chapter 3, Alexander Hamilton and Friedrich List challenged liberal trade doctrine. From their mercantilist perspective, free trade was merely a rationale for England to maintain its dominant advantage over its trading partners on the continent and in the New World. For Hamilton, supporting U.S. infant industries and achieving national independence required the use of protectionist trade measures. Likewise, List argued that polices such as import tariffs and export subsidies were necessary if Europe's infant industries were to compete on an equal footing with England's more efficient enterprises.[7] More importantly, List maintained that in order for free trade to work for all, it must be preceded by greater equality between states or at least a willingness on their part to share the benefits and costs associated with trade.

Today's neomercantilists challenge the assumption that specialization in comparative advantage unconditionally benefits all of the parties engaged in trade. People employed in different industries or sectors of any economy can be expected to resist being laid off or moving into other occupations as comparative advantages shift around to different nations. In many cases, states can intentionally create comparative advantages in the production of certain goods and services by providing cheap loans and export subsidies to domestic producers.[8]

Moreover, the political reality in democratic nations is that many domestic groups and businesses expect the government to protect them from import competition (see Box 7.1). Presumably, politicians fear the wrath of constituents who face layoffs or competition from cheaper imports. For example, consumers who benefit from a small saving on the price of an imported article of clothing or furniture due to free trade usually do not speak as loudly as displaced workers or companies losing their market share to imports.

Trade protectionism is also associated with a fear of becoming too dependent on other nations for certain goods, including food and items related to national defense. For example, Japan and China have worried that too much dependence on other states for energy imports can lead to economic and political vulnerability. As mercantilists see it, economic liberal theories of trade cannot account for the real political world in which states constantly manipulate production and trade.

THE SOLAR PANELS TRADE DISPUTE: GREEN PROTECTIONISM IN THE UNITED STATES?

The global race to increase use of renewable energy has caused trade frictions between many countries. The European Union, the United States, China, and India are particularly determined to expand domestic manufacturing capacity in the fiercely competitive solar power, wind power, biofuels, and energy storage sectors. Governments have used the alibi of fighting climate change to justify protecting their renewables manufacturers with tariffs and subsidizing the development of clean energy technology. However, in the case of solar panels, many argue that protectionism will slow down the transition to a carbon-free future.

In 2011 a consortium of U.S. solar panel manufacturers called the Coalition for American Solar Manufacturing (CAS M) petitioned the U.S. government over what they claimed were unfair Chinese trade practices leading to a surge in imports of cheap Chinese solar panels.[a] After investigations by the U.S. International Trade Administration and the Department of Commerce—and under pressure from lawmakers led by Oregon Senator Ronald Wyden—the Obama administration in 2012 imposed average tariffs and countervailing duties of 30 percent on imported solar panels from leading Chinese manufacturers. It determined that the Chinese manufacturers received illegal export subsidies from Beijing and dumped (sold below cost) their products in the United States, both violations of WTO agreements.

Like many states, China subsidizes its panel manufacturers directly with tax credits and low-cost loans from state banks and indirectly by guaranteeing an inflated price for the energy that solar power producers feed into the electricity grid.[b] In retaliation for the U.S. decision, China in 2013 imposed tariffs and duties of up to 57 percent on imports of U.S.-made polysilicon, a key raw material in solar cells. In 2013 the European Union also imposed tariffs on Chinese solar panels, but later reached an agreement with some Chinese producers for a floor on their panel prices.

To get around U.S. tariffs, Chinese companies built some production facilities in Taiwan for solar cells that were then assembled into panels in China. The United States raised tariffs even more in 2015 and shut down this loophole by extending tariffs to Taiwan and all panels from China, no matter where the component cells were manufactured. Chinese companies are now scaling up new solar factories in Southeast Asia (especially Malaysia). Scholars at Stanford University who study the solar industry argue that, ironically, U.S. tariffs "are forcing the Chinese solar industry to grow leaner and stronger."[c] They argue that because China has economies of scale and efficient supply chains that make it a low-cost producer, the United States will best serve its national interest by focusing on solar R&D and solar panel deployment, not manufacturing.[d]

The latest chapter in this trade war occurred in 2017, when manufacturers Suniva and SolarWorld petitioned the U.S. International Trade Commission to investigate imported solar cells for causing serious injury to the U.S. solar industry. The value of solar panel imports to the United States rose dramatically between 2012 and 2016. By 2016 U.S. manufacturers produced less than 5 percent of the world's solar cells, while Chinese companies produced more than 65 percent.[e] Sixteen Senators and fifty-three Representatives urged the USITC to reject the petition, as did several free-market think tanks. However, the most important opponent of tariffs has been the powerful Solar Energy Industries Association (SEIA), which represents companies that sell, install, and service solar systems. Employing the majority of workers in the U.S. solar sector, SEIA companies believe that fewer power companies and households will install solar panels if the United States raises tariffs.[f] A glut of cheap Chinese panels makes switching to renewable energy much more cost-effective, creates good jobs in the solar installation industry, and accelerates the clean energy transition.

In September 2017, the USITC ruled in favor of Suniva and SolarWorld, finding that surging imports had caused serious injury to the U.S. solar manufacturing industry. Under the 1974 Trade Act, the U.S. president can impose temporary import duties (safeguard measures) on many countries based on such a finding.

Thus, the solar industry in the United States is split between a small group of manufacturers who want protectionism and a large group of installation companies who want free trade. President Trump has promised to tackle China's unfair trade practices, but letting China win the solar trade war and sacrificing American solar manufacturers would probably do more to create jobs and cheaper energy.

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[a] *Solar cells are grouped together to form solar panels (also called solar modules).*

[b] See Keith Bradsher, "When Solar Panels Became Job Killers," *New York Times*, April 8, 2017, at www.nytimes.com/2017/04/08/business/china-trade-solar-panels.html.

[c] Jeffrey Ball, Dan Reicher, Jiaojing Sun, and Caitlin Pollock, *The New Solar System_ China's Evolving Solar Industry and Its Implications for Competitive Solar Power in the United States and the World*, Stanford University, Steyer-Taylor Center for Energy Policy and Finance (March 2017), p. 42.

[d] See James Osborne, "Trump's Solar Plan Has Industry Nervous," *Houston Chronicle*, July 27, 2017, at www.houstonchronicle.com/business/article/Solar-panel-made-in-China-Think-again-11489592.php.

[e] Joe Ryan and Jennifer Dlouhy, "This Case Could Upend America's $29 Billion Solar Industry," *Bloomberg Business week*, June 15, 2017, at www.bloomberg.com/news/articles/2017-06-15/this-case-could-upend-america-s-29-billion-solar-industry.

[f] See Ana Swanson, "Solar Trade Case Weighs Whether Protection Will Save or Sink Industry," *Washington Post*, August 15, 2017, at www.washingtonpost.com/news/wonk/wp/2017/08/15/solar-trade-case-weighs-whether-protection-will-save-or-sink-industry/.

Contemporary mercantilists support liberal trade to the extent that it serves the interests of one's nation-state. Countries will support trade liberalization in areas where their producers benefit but will try not to liberalize sectors where their producers will face strong competition. Some economists also argue that historically high tariffs did not prevent countries from growing fast. In fact, the economist Dani Rodrik, a supporter of managed globalization, points out that in the past, some high-tariff countries grew faster than those without tariffs.[9]

Malaysian economist Martin Khor argues that trade liberalization needs to be calibrated to the development needs of countries, with attention to timing its implementation to support other industrial policies. Developing countries that open up to free trade without appropriate institutions or local industry strength can be made worse off, as when competition from cheap imports drives small companies and farmers out of business.[10] Similarly, Ha-Joon Chang explains that the developed states are "kicking away the ladder" (taking away the choice to protect) from the developing nations, even though few of today's industrialized countries actually practiced free trade in the nineteenth and early twentieth centuries.[11]

Structuralist Views on Trade

Structuralists argue that economic problems in the major European powers historically drove them to engage in imperialism. Mercantilist policies that emphasized exports became necessary when capitalist societies experienced economic depression. Manufacturers overproduced industrial products, and financiers had a surplus of capital to invest abroad. Colonies were places to dump goods and invest in industries that profited from cheap labor

and access to inexpensive natural resources. Trade helped imperial countries dominate and subjugate their colonies.

Lenin and other Marxist theorists argued that national trade policies mostly benefited the dominant class in society—the bourgeoisie. Toward the end of the nineteenth century, capitalist countries used trade to spread capitalism into the colonies. Lenin attempted to account for the necessity of states with excess finance to take colonies in order to postpone revolution at home. The "soft" power of finance as much as the "hard" power of military conquest helped to generate empires of dependency and exploitation.

More recently, Immanuel Wallerstein stresses the linkages between core, peripheral and semi-peripheral regions of the world. Patterns of international trade are determined largely by an international division of labor between these three regions that drives capitalism to expand globally. Free-trade policies and the integration of global markets are extensions of the same economic motives of imperial powers of the nineteenth and twentieth centuries. Similarly, dependency theorists argue that peripheral nations and regions became underdeveloped after being linked with industrialized nations through trade.[12]

Structuralists today also warn against the terrible consequences weak Southern states face when powerful Northern states use trade as a political instrument. In the 1980s, the Reagan administration applied trade restrictions on nations that supported communist revolutionary movements (Vietnam, Cambodia, and Nicaragua), sponsored terrorism (Libya, Iran, Cuba, Syria, and Yemen), or enforced racial segregation (South Africa). During the 1990–1991 Persian Gulf War, the United Nations Security Council imposed trade sanctions against Iraq to force it to pay reparations to Kuwait and eliminate weapons of mass destruction. In 2006, 2013, and 2017, the UN Security Council imposed sanctions against North Korea for its development of nuclear weapons and ballistic missiles testing. In recent years, the United States, the European Union, and their allies—sometimes with UN backing—have also imposed stringent sanctions on Iran, Syria, the Gaza Strip, and Myanmar.

Critics of trade sanctions view them as morally repugnant because they inflict pain on ordinary people and usually do not cause any real change in a targeted state's policies. In fact, economic sanctions have unintentionally helped prop up authoritarian leaders who resist the sanctions imposed by "imperial aggressors." Dominant states like to use trade sanctions to discipline or send a distinct message to other countries because they are a cheap substitute for military action. However, structuralists view them as simply an updated instrument of imperialism that is almost always directed against developing countries.

Structuralists agree with mercantilists that free trade has never really existed. Bill Dunn also argues that among its many weaknesses, the theory of comparative advantage does not account for the *long-term* effects of trade specialization.[13] Countries that get stuck exporting agricultural goods and raw materials over a long period may fail to develop or adopt new technologies and may face an ever more difficult task diversifying their economy. This leaves them vulnerable to volatilities in global commodities prices and boom—bust cycles of growth. Moreover, after surveying economic literature and conducting some econometric tests, Dunn concludes that countries that have greater openness to trade tend

to have only slightly higher growth rates than those that are less open.[14]

As Figure 7.2 shows, China grew its share of world merchandise exports from just 1.2 percent in 1983 to 13.6 percent in 2016, a testament to its astonishing industrialization. Six other emerging East Asian countries nearly tripled their share of world merchandise exports from 3.6 percent in 1973 to 9.9 percent in 2016. However, Africa and Latin America failed to gain a larger share of world merchandise exports, an indication that they are falling behind relatively in terms of industrialization and competitiveness. The EU, China, Japan, the United States, and South Korea together account for 74 percent of the world's exported manufactured goods.

In contrast, if we look at the merchandise exports of the Middle East and Africa, we find that in 2016 more than 60 percent of all their exports were fuel and minerals (see Figure 7.3). Likewise, for South and Central America, 70 percent of their merchandise exports were fuel, minerals, and agricultural products. Structuralists would point out that this heavy reliance on exports of commodities in the Middle East, Africa, and Latin America mimics the pattern seen during the colonial era and shows how far behind these regions have become in manufacturing compared to Asia.

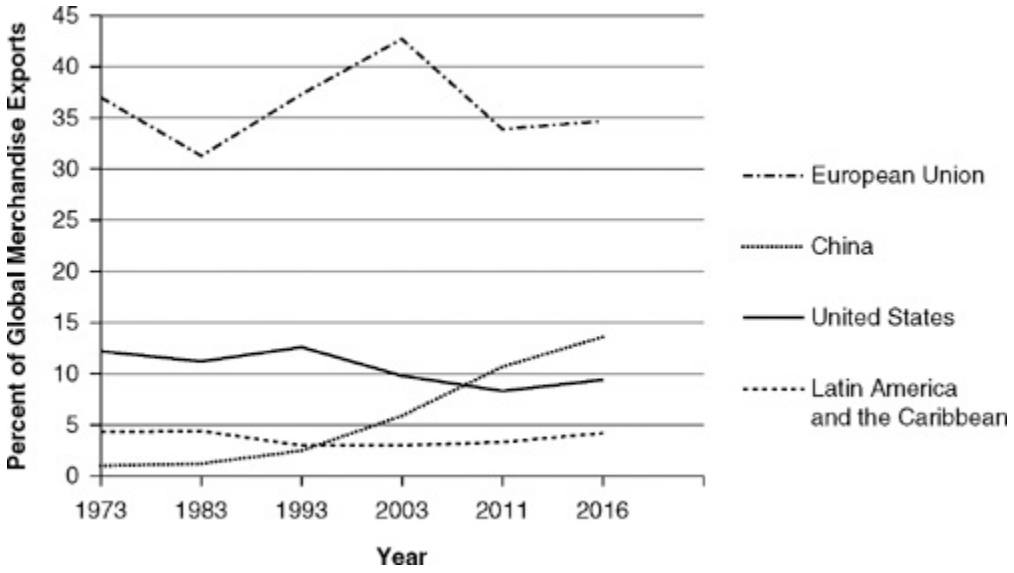


FIGURE 7.2
Merchandise Exports of Selected Countries and Regions as a Percentage of Global Merchandise Exports, 1973–2016.

Sources: Data from World Trade Organization, *World Trade Statistical Review 2017* (2017), p. 100, at www.wto.org/english/res_e/statis_e/wts2017_e/wts17_toc_e.htm; and World Trade Organization, *International Trade Statistics 2012*, p. 62, at www.wto.org/english/res_e/statis_e/its2012_e/its2012_e.pdf.

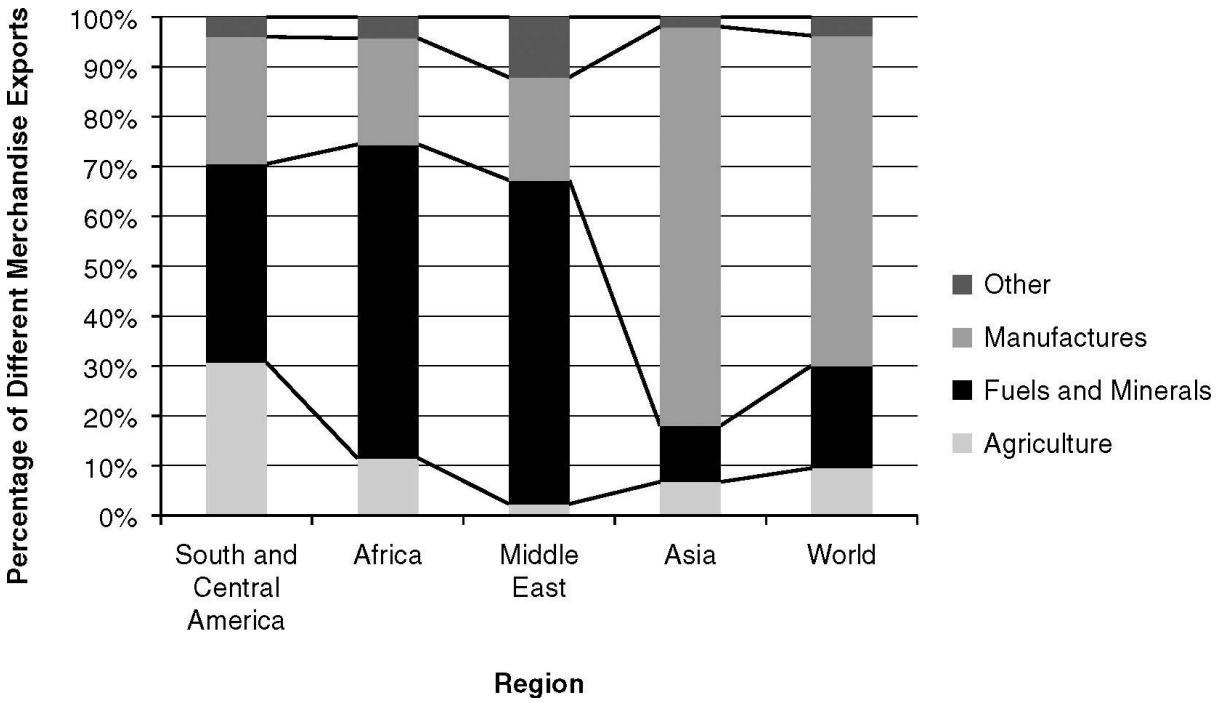


FIGURE 7.3
Composition of Merchandise Exports for Selected Regions, 2014.

Sources: Data from World Trade Organization, *International Trade Statistics 2015* (Geneva: World Trade Organization, 2015), p. 72, at www.wto.org/english/res_e/statis_e/its2015_e/its2015_e.pdf.

The Middle East, Africa, and Latin America are also vulnerable to swings in global prices for primary products. Volatile export prices have sometimes caused severe economic recessions, triggered debt crises, or led to unsustainable economic growth. In Figure 7.4, we show global price indices for energy, food, and raw materials (like timber, cotton, and rubber), adjusted for inflation. Notice that prices for food and raw materials generally fell from the early 1980s to around 2000, grew briskly from 2000 to 2011–2012, and fell again after 2011–2012. Prices for energy rose sharply from 1973 to 1981 (due to OPEC) and from 1998 to 2013 (as China grew quickly), but prices fell from 1982 to 1998 and after 2013. Countries that export mostly manufactured goods and services are much less prone to boom—bust price cycles than exporters of agricultural goods and natural resources.

Constructivist Views on Trade

Unlike the other IPE perspectives, constructivism does not prescribe how states should approach trade policy. It focuses more on ideas about trade and the norms that underpin the trade system. Constructivists believe that any trade system is rooted in a shared understanding of what John Ruggie calls its "legitimate social purpose."[15] These shared understandings emerge and change through dialogue and in response to changing social values. How different states conceive of trade, talk about it, and understand its purposes will affect what kinds of rules they adopt to regulate it. Epistemic communities (such as economists, lawyers, and development experts) help redefine states' trade interests, identify

problems, and teach state officials the best means to achieve specific goals.

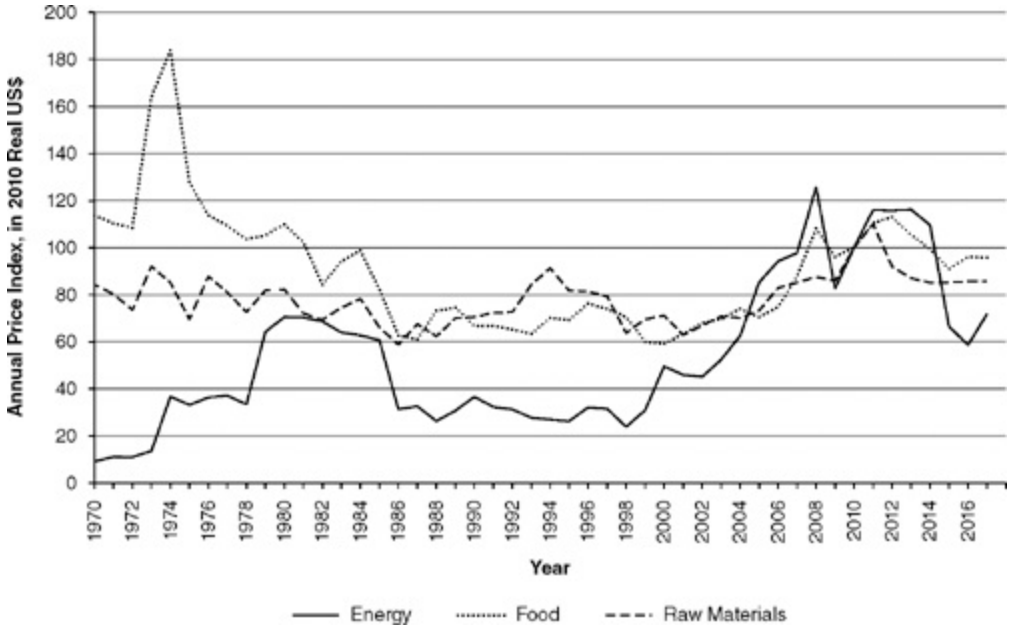


FIGURE 7.4
Commodity Price Indices for Energy, Food, and Raw Materials, 1970–2017.

Source: Data from World Bank, *World Bank Commodity Price Data (The Pink Sheet)*, at www.worldbank.org/en/research/commodity-markets.

Constructivists believe that civil society groups have a role in changing the way developed countries think about globalization and "free trade." Since the 1990s, many NGOs with structuralist views have focused attention on the connection between trade and issues such as the environment, labor conditions, poverty, and human rights. Groups like Oxfam acquire first-hand information about the effects of Northern trade policies on developing nations and publicize it in speeches, newspapers, journals, and on their websites. They also cast light on the ethical and judicial dimensions of outsourcing and trade-induced job displacement. One influential effort to change trade norms is the fair trade movement, which seeks to give workers in developing countries higher prices for certified goods such as coffee, chocolate, handicrafts, and timber.

As we discussed in Chapter 5, constructivists show how transnational advocacy groups have socialized states to heavily regulate or ban the export and import of goods such as conflict minerals, illegally harvested timber, and landmines. As we discuss in Chapter 15, civil society groups were instrumental in creating a new regime to ban the export and import of blood diamonds, and they have convinced states to prevent trade in ivory and endangered species. The key argument for constructivists is that trade does not simply reflect material interests and ideas about global efficiency; notions of corporate responsibility, environmental stewardship, conflict prevention, and fairness also shape trade rules.

Constructivists also examine how countries and actors that we perceive as lacking power

in the international trade structure have sometimes been relatively successful in resisting dominant trade norms. For example, Robin Dunford examines how, in the face of free trade, land grabbing, and other global processes that have hurt small farmers, a grassroots peasant movement led by La Vía Campesina has created and diffused a norm of "food sovereignty," meaning the right to produce food for oneself in the territory where one lives.[16] The norm has reshaped UN discussions about global agriculture, and many states have incorporated it into their laws. As Dunford stresses, food sovereignty emphasizes collective property and the rights of peasants and indigenous peoples to access land, reject genetically modified seeds, farm sustainably, and produce for the local market.[17] The norm challenges energy-intensive, export-oriented food systems and their beneficiaries, such as large landowners and TNCs that sell patented seeds and chemicals. Interestingly, governments of some of the world's largest food exporters, such as the United States, Canada, Brazil, and Argentina, tend to be most resistant to the norm.

Another constructivist approach to trade is to analyze the way we talk about it. For example, international political economist Rorden Wilkinson argues that metaphors, historical stories, and "common sense" are employed to preserve a status quo trade system in which developed countries benefit more than developing ones.[18] The dominant trade discourse shapes how we act; it excludes some voices and makes deep reforms difficult. The metaphor "a rising tide lifts all boats" suggests that free trade benefits all countries equally, obscuring the fact that gains from trade have been unequally distributed across countries. When trade talks stall, the "bicycle metaphor" is frequently evoked, suggesting that unless the "bicycle" continues to move forward with more trade liberalization, it will fall over and there will be a "breakdown of the multilateral trading system and something akin to the nightmare of the 1930s."[19] These metaphors and other ways of talking about trade, according to Wilkinson, are ideologically motivated misreadings of the history of the multilateral trade system that make it hard to consider alternative ways of governing trade.

GATT AND THE LIBERAL POSTWAR TRADE STRUCTURE

Before World War II, trade rules largely reflected the interests of the dominant states, especially Great Britain, France, and Germany. Sometimes these rules were enforced at the point of a gun, as when the United States forced Japan to open its doors to U.S. trade in the 1860s and when the European powers forced open China and the Ottoman Empire in the nineteenth century. During the Great Depression of the 1930s, protectionism spiraled upward. International trade decreased by an estimated 54 percent between 1929 and 1933, strangled in part by the Smoot-Hawley tariff hikes in the United States and onerous trade barriers enacted elsewhere. According to some historians, the decline in trade helped generate the bleak economic conditions that fueled the rise of ultranationalist leaders such as Mussolini and Hitler. It is important to note that it was not until 1934 that the United States officially adopted a policy of moving toward free trade in an effort to generate economic growth.

The structure of the post-World War II political economy was established in 1944 at the Bretton Woods Conference in Bretton Woods, New Hampshire. There, allied leaders, led by the United States and Great Britain, created a new liberal economic order that they hoped would prevent the kinds of economic conflicts in the interwar period that led to World War II. In conjunction with this effort, the United States promoted the establishment of an International Trade Organization (ITO) to oversee new trade rules that would gradually reduce tariffs and subsidies. However, the ITO never got off the ground because a coalition of protectionist interests in the U.S. Congress signaled that they would not ratify the agreement, effectively killing it. President Harry Truman advanced an alternative structure for trade negotiations under the GATT. In 1948, the GATT became the primary organization responsible for the liberalization of international trade.[20] Through a series of multilateral negotiations called rounds, the world's main trading nations agreed to reduce their own protectionist barriers in return for freer access to the markets of others. During the Cold War, most communist countries refused to join the GATT.

Two basic principles of the GATT are reciprocity and nondiscrimination. Trade concessions are reciprocal—that is, all member nations agree to lower their trade barriers together. The loss of protection for domestic industry is offset by greater access to foreign markets. Nondiscrimination has two components: most favored nation (MFN) treatment and national treatment. MFN treatment means not giving preferential treatment to the imports of one country over those of another. National treatment requires that a country treat imported goods the same as equivalent domestically produced goods.

In the early rounds of GATT negotiations, members peeled away protectionist barriers, especially for manufactured goods, and international trade expanded dramatically. The United States made deeper cuts in its tariff rates than its European allies did in theirs. Keep in mind that as an organization the GATT could not enforce its own rules; rather,

members were responsible for fulfilling trade obligations based on trust and diplomacy. Policy decisions were made through consensus, and thus policy implementation often reflected a combination of political and economic interests. The GATT agreement allowed exceptions from its general trade rules for regional trade agreements (RTAs) and products such as textiles and agricultural goods. At first, these exceptions allowed many of the war-ravaged nations to resolve balance of payments problems. In the case of agriculture, they also reflected U.S. insistence on the right to subsidize farmers and place quantitative restrictions on imports of agricultural goods. RTA members could lower their tariffs on imports from other members but not offer the lower tariffs to states outside the RTA—an exception to the principle of MFN treatment.

Mercantilism on the Rebound

Western industrialized economies grew rapidly in the post-war era, as did trade volumes and productivity rates, but the OPEC oil crisis in 1973 caused economic recession, bringing the "golden age of capitalism" to an end. In the 1970s international trade continued to grow, but not at the rate at which it had earlier. By 1973 the level of tariffs on industrial products had decreased to an average of about 10 percent. At the same time, however, countries devised new and more sophisticated ways to bolster their exports and limit imports. The GATT's Tokyo Round (1973–1979) addressed the growing number of non-tariff barriers (NTBs) that many believed were stifling world trade. Rules were established to limit a range of discriminatory trade practices involving export subsidies, countervailing duties, dumping, government purchasing, government-imposed product standards, and licensing requirements on importers.

Many liberal trade theorists at the time argued that the Tokyo Round did not go far enough in dealing with NTBs or with enforcing GATT rules, even though it brought average tariff levels down to 6 percent. By the 1980s trade accounted for an increasingly higher percentage of GDP in the industrialized nations: around 20 percent for the United States and Japan, and an average of 50 percent for members of the EU. Trade policy continued to be a source of tension among the industrialized nations, reflecting their increasing dependence on trade to help generate economic growth.

Japan, the quintessential mercantilist nation among GATT members, benefited from the liberal international trade system. By the 1970s, its export-led trade strategy began to bear fruit. Its Ministry of International Trade and Industry (MITI) helped pick corporate winners that it believed would prosper in the international economy if given state assistance. The Japanese state helped firms in ways that would put them in a strong competitive position.[21] Japanese automobile, semiconductor, and consumer electronics industries in particular ratcheted up production and exports of high-quality goods.

The term "strategic trade policy" became synonymous with efforts by states to stimulate exports and hinder foreign access to domestic markets through non-tariff measures. Proactive strategic trade policy often involved extending support to infant industries and providing export subsidies to large companies. It also included "the use of threats, promises, and other bargaining techniques to alter the trading regime in ways that improve the

market position of one's national corporations."[22] In the United States, for instance, Section 301 of the 1974 Trade Act authorizes the president to order the U.S. Trade Representative to investigate countries for engaging in unfair trade practices that violate trade agreements, create significant market barriers, or inhibit U.S. exports. Under Section 301 the president can impose unilateral sanctions on countries that do not eliminate their unfair practices. After a 1988 amendment to Section 301, the USTR also has to prepare an annual report detailing how well foreign countries protect U.S. companies' intellectual property rights. The legislation was designed to put pressure on countries to negotiate with the United States to change their policies. In another example, France in 1982 sought to protect its VCR manufacturers from Japanese competition by requiring all imported VCRs to go through a tiny inland customs office in Poitiers where officials deliberately stalled the clearing of imports.[23] Also, Europe and the United States in the 1980s negotiated voluntary export restraints (VERs) with Japan in order to limit the number of automobiles it exported to their markets.

All of these forms of trade protection in the 1970s and 1980s seemed to compromise the goal of a liberal (open) GATT system. There was relatively free trade, in that tariffs on manufactured goods were quite low, but GATT members also emphasized the need for a level playing field based on the removal of other market barriers. The United States, facing a burgeoning trade deficit, pushed aggressively for expanded market access. Some trade negotiations moved from the multilateral arena of GATT to the bilateral level.

Early North–South Trade Issues

After the OPEC nations dramatically raised the price of oil in 1973, a coalition of developing nations in the UN called the Group of 77 (G77) demanded a new international economic order (NIEO).[24] They complained that they faced declining terms of trade, meaning that the prices of imported manufactured goods were rising relatively faster than the prices of primary commodities they exported, such as raw materials, food, and minerals. The G77 sought more access for their primary commodities into the markets of the Northern industrialized countries. Members also proposed creating cartels like OPEC to manage the price of other global commodities. The G77 also demanded a "code of conduct" for transnational corporations to give developing nations greater economic sovereignty.

Given the global distribution of political power at the time, these demands produced no fundamental changes in GATT, IMF, or World Bank policies. The United States and other developed countries responded that, rather than trying to change system rules, developing nations should become more integrated into the international economy. Because trade is supposedly an "engine of growth," developing nations would benefit from trade efficiencies if they brought down tariff barriers and opened their economies to foreign direct investment (FDI). As the globalization campaign took off in the 1990s, the World Trade Organization and the World Bank contended that developing nations would grow fastest if they focused on manufacturing goods for export.

The Uruguay Round

Eager to reinvigorate trade liberalization, GATT members launched the ambitious Uruguay Round of trade negotiations in 1986 in Punta del Este, Uruguay. A final agreement was reached in 1994 between 123 countries, and the new World Trade Organization came into existence in 1995. The Uruguay Round established new rules and principles to limit protectionist measures such as dumping (selling goods at below fair market prices) and the use of state subsidies. It lowered average tariff rates to 3.9 percent on manufactured goods traded between developed countries. Going beyond previous trade rounds, it also addressed a wide range of sensitive issues such as: market access for textiles and agricultural goods; intellectual property rights; restrictions on foreign investments; and trade in services.

For the first time, GATT trade negotiations dealt with the contentious issue of agriculture in a comprehensive manner. All the major producers and importers of agricultural products routinely employ measures that distort agricultural markets. The United States and the Cairns Group (composed of Australia and seventeen other pro-free-trade countries) initially led a radical effort to phase out all agricultural subsidies. But after resistance from U.S. farm groups, the United States only offered to gradually eliminate its domestic farm programs and agricultural trade support measures. EU efforts to significantly reduce agricultural subsidies were complicated by the Common Agricultural Policy (CAP), a community-wide program that France in particular did not want to see gutted. It took almost five years to bring the EU's farm program in line with GATT reform proposals.

After many difficult talks and numerous compromises, Uruguay Round negotiators finally reached a consensus on agriculture in November 1993. They agreed that all countries were to reduce their use of agricultural export subsidies and domestic assistance gradually over a period of years. Countries were allowed to convert nontariff import barriers into tariff equivalents, which were then to be reduced in stages. However, because of the strength of farm lobbies and the importance of agricultural exports in many countries, the method for calculating tariff equivalents in most cases actually set new tariff levels higher than they had been, effectively nullifying efforts to reduce farm support. Protectionism remained a key feature of agricultural trade.

The Uruguay Round produced dozens of agreements on a host of other issues, including safeguards, rules of origin, technical barriers to trade, and textiles and clothing. It institutionalized a set of global trade rules and regulations. One important agreement was the extension of "tariff bindings" from manufactured goods to all agricultural goods. A "bound" tariff is the highest tariff rate that a country will charge for a particular kind of commodity. A country can (and often does) apply a lower tariff in practice, but once it offers a bound rate, it cannot go over that binding again. The idea of tariff bindings is to make tariffs more predictable and make it easier for countries to progressively lower tariffs in future negotiations.

In addition to the revised GATT, a new General Agreement on Trade in Services (GATS) liberalized trade in banking, insurance, transport, and telecommunications services by applying the principles of national treatment and most favored nation to them. And a

new agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) required countries to maintain minimum standards for protection of patents, copyrights, and trademarks—and to effectively enforce those standards (see Chapter 10). Many delegates expected that remaining disputes over agriculture and services would be dealt with more directly in a future round of trade negotiations.

The final agreement of the Uruguay Round launched the new World Trade Organization, which by 2016 had 164 members accounting for over 97 percent of global trade. Headquartered in Geneva, Switzerland, its primary job is to implement the GATT, GATS and TRIPS agreements. It serves as a forum for negotiating new trade deals, resolving disputes, and providing technical assistance to developing countries. Theoretically, WTO decisions are made by a consensus of the members. Its decision-making structure includes a Secretariat (administrative body), a Ministerial Conference that meets at least once every two years, and a General Council that meets several times a year in Geneva.

The WTO uses dispute settlement panels to adjudicate trade disputes, giving it an enforcement mechanism that the GATT did not have. Each impartial, three-person panel of experts reviews and issues a ruling on the case submitted to it. Participants in a dispute can appeal a panel's findings. If a country refuses to change the policies that a panel finds violates WTO rules, the winning party is authorized to impose trade sanctions on it. Several high-profile cases over the years include judgments against the EU for banning imports of hormone-treated U.S. beef and genetically modified crops. In addition, a long-running dispute over subsidies to aircraft manufacturers was adjudicated by panels that found the United States and the European Union had improperly subsidized Boeing and Airbus, respectively.

Another high-profile case involved U.S. subsidies to cotton farmers. In 2002, Brazil formally challenged these subsidies at the WTO, arguing that they violated several WTO agreements, caused Brazilian cotton farmers to lose market share, and lowered global cotton prices. A WTO dispute settlement panel ruled in favor of Brazil in 2004, as did the Appellate Body in 2005. After the United States essentially failed to comply with the ruling, the WTO in 2009 authorized Brazil to impose countermeasures, which Brazil decided would include retaliatory tariffs on imported U.S. goods and temporary suspension of U.S. patents on pharmaceuticals and chemicals. In 2010, the United States reached an agreement with Brazil to pay it $147 million per year until Congress brought U.S. cotton subsidies in compliance with WTO rulings. In 2014, following further U.S. foot-dragging, the countries reached an agreement whereby the United States would pay Brazil a lump sum of $300 million and reduce some subsidies to U.S. cotton farmers (but not eliminate them) in exchange for Brazil dropping the WTO case. Although the outcome was a victory for Brazil, continued U.S. government support for farmers lowers the price of U.S. cotton exports, hurting growers in India and Africa.

Since the founding of the WTO, trade disputes have become more complex, technical, and politicized. However, most states have either implemented the rulings of dispute resolution panels or arrived at satisfactory resolution of trade spats through negotiations.

The Doha "Development Round"

The next round of multilateral trade negotiations were to begin in late 1999 in Seattle, but the WTO's Ministerial Conference suspended talks following violent demonstrations led by anti-globalization protestors. The "Battle of Seattle" emboldened other global activists concerned about violations of human rights in sweatshops, agribusinesses in developing countries, effects of corporations on the environment, lack of transparency in WTO decision making, and a host of ethical issues.[25] Critics questioned whether the WTO would deal with these problems or respect national sovereignty.

After the events of 9/11, WTO members pushed to restart talks. At the 2001 ministerial meeting in Doha, Qatar (far away from protestors), the multilateral Doha Round officially began. From the outset, many developing countries complained that they had not seen significant gains from the agreements reached in the Uruguay Round. They also argued that before new trade agreements could be reached, the developed nations would have to make a concerted effort to include developing nations in the negotiations process. In recognition of these concerns, the round was nicknamed the Doha Development Agenda.

At Cancun, Mexico, in November 2003, ministerial talks broke down once again. Headed by Brazil, India, South Africa, and China, a negotiating group called the G20 (not to be confused with the financial G20) focused on cutting farm subsidies in the rich countries. As a bloc, they dismissed 105 proposed changes in WTO rules that would have provided developed countries more access to their markets.[26] To restart the talks, the United States offered to cut farm subsidies if others did the same. However, the U.S. commitment to trade liberalization seemed hollow, given that Congress had passed a 2002 Farm Bill appropriating $190 billion over ten years for subsidies and other aid to farmers. Critics pointed out that farm subsidies caused overproduction and the dumping of excess commodities onto world markets, thereby distorting world commodity prices and depressing prices farmers in developing countries received for their crops. Late in 2005, the G20 again pushed the United States and the EU to cut domestic agricultural support significantly.

The developed countries insisted on greater non-agricultural market access (NAMA)—meaning that developing countries (with exceptions for the poorest) should lower their tariffs on industrial imports dramatically. Many developing countries believed that these reductions would hurt their national industries and impede development in the long run. Developed countries also wanted greater protection for their intellectual property. Negotiators failed to reach consensus on specific measures regarding "cultural products" (such as movies), insurance companies, banking across national borders, and protectionist "local content" legislation.

Why Did the Doha Round Fail?

After ministerial meetings in 2015 to try to bridge long-standing disagreements, the Doha Round unofficially came to an end. Why did fourteen years of efforts end in failure? There is certainly no shortage of post-mortems. Like the Uruguay Round, the Doha Round was

structured as a "single undertaking," meaning that there could be no separate, provisional agreements; in other words, "Nothing was agreed until everything was agreed." With this rigid negotiating principle, countries could *not* opt out of sectoral agreements to which they strongly objected.

Conflicting interests between Northern industrialized countries over the distribution of gains and losses from trade liberalization also led to Doha's demise. Both the United States and the EU were reluctant to eliminate most of their protection for agriculture, services, and government procurement. They also did not want competition in their agricultural markets from developing countries, which likewise did not want to open up their markets fully to Northern manufactured goods and services. Political economists Valbona Muzaka and Matthew Bishop point out that developing countries view developed ones as hypocritical: "The intellectual gymnastics performed by the EU and the US to justify subsidies to agriculture and other strategic sectors (not least the financial and automotive sectors) betrays their commitment to the principle of free trade and free market logic."[27]

A bigger problem with the Doha Round, according to Muzaka and Bishop, was lack of a widely shared social purpose for trade liberalization.[28] Developing countries believe that the trade rules a country follows should reflect its level of development and particular needs. For all countries to have an equal chance of benefiting from trade, there have to be differential obligations for different groups of countries; therefore, wealthy countries should make the most concessions, not the poorest or industrializing ones. Developing countries want to extend the "special and differential treatment" they already have in WTO agreements so that they can protect infant industries, maintain high tariffs on agricultural imports, and subsidize local industries. Developed countries are willing to grant these exemptions from general WTO rules to the poorest countries, but not to middle-income developing countries such as China, Brazil, India, and Indonesia.

Structural changes in the global economy also help explain the Doha impasse. Canadian trade scholar Robert Wolfe says that an underappreciated factor causing failure is the rise of China as a dominant trader by the late 2000s. Developing countries fear that trade liberalization will increase the already strong competition they face in their own markets from Chinese imports.[29] Despite its economic prowess, China still wants to be treated as a developing country that is not obliged to fully reciprocate the commitments that the developed countries make in trade agreements.

More broadly, the rise of China, India, and Brazil has brought a shift in global power. Northern elites repeatedly blame these three countries for being so intransigent and so unwilling to grant greater market access that they halted the momentum for multilateral trade liberalization. Canadian political economist Kristen Hopewell rejects this claim. Instead, she argues that WTO negotiations came to a deadlock because, paradoxically, Brazil, India, and China have for the most part embraced liberal trade rules and norms, not because they have rejected them.[30] The GATT/WTO was constructed in a context of U.S. hegemony, but now that there has been a shift in power towards the BRICs, they are better able to call out U.S. practices that are inconsistent with WTO norms and demand that the

United States (and Europe) reduce protectionist barriers that matter to Brazil, India, and China. In effect, says Hopewell, the WTO-based trade order is a Frankenstein that is turning on its creator.[31] The contradictions in the WTO are causing a breakdown, but not because Brazil, India, or China is anti-capitalist or anti-trade.

Hopewell claims that Brazil, India, and China now have enough power to demand that their own interests be properly addressed; they are no longer willing to let the United States and Europe dominate the WTO. They want more market access for their exports—even while remaining selectively protectionist. The power shift makes it difficult for the United States and the European Union to demand further trade liberalization in emerging economies without simultaneously liberalizing sectors of their own economies. Just as the developed countries preserved the ability to protect certain sectors of their economies when creating the GATT and the WTO, Brazil, India, and China in the Doha Round sought to retain the ability to protect some of the least competitive sectors of their own economies. Just as developed countries have used the trade system to promote their most competitive exports, Brazil, India, and China in the Doha Round promoted their own dynamic export sectors (agribusiness for Brazil, services for India, and manufactures for China).

TRADE LIBERALIZATION OUTSIDE THE WTO

With little progress in the Doha trade talks, developed countries shifted their attention to multilateral, regional, and bilateral trade agreements where they have more leverage to promote liberalization. These agreements have fewer members, less bureaucracy, and more room to account for the idiosyncrasies of partner states. Multilateral trade agreements are struck between multiple countries that have a set of common interests but that aren't necessarily geographically related. Regional trade agreements are based on formal intergovernmental collaboration between two or more states in a geographic area.[32] In this section, we first account for the rise of regional trade agreements. We then examine the Trans-Pacific Partnership, an ambitious regional agreement negotiated in the 2000s. Finally, we discuss recent efforts to liberalize trade in services through regional and multilateral negotiations.

Regional Trade Blocs

Regional trade agreements (RTAs), often also called free-trade agreements (FTAs), reduce trade barriers between member countries but often do not extend these trade concessions to nonmember nations. The number of RTAs grew prodigiously after the end of the Cold War. The WTO lists 279 RTAs in force in June 2017 (although most of these are bilateral FTAs). They cover at least 60 percent of world trade.

The biggest RTAs by far are the European Union and the North American Free Trade Agreement (NAFTA). Other large blocs are Asia Pacific Economic Cooperation (APEC), the Central American Free Trade Agreement (CAFTA), Mercosur, and the Association of Southeast Asian Nations (ASEAN). In 2015, 63 percent of EU exports and half of NAFTA members' exports were intraregiona1.[33] The EU, NAFTA, and ASEAN accounted for 58 percent of all global merchandise trade (imports and exports) in 2016. The EU alone accounted for 34 percent of global merchandise trade, compared to NAFTA's 17 percent and ASEAN's 7 percent.[34]

Why were RTAs so popular? Have they been good for trade? Technically, RTAs violate the GATT and WTO principle of nondiscrimination, and yet they are legal entities. Article 24 of the GATT and Article 5 of the GATS permit them, as long as they remove tariffs and other barriers on "substantially all the trade" within the bloc. In some cases RTAs have generated more efficient production within the bloc, either while infant industries are maturing or in response to competition from outside industries. In many cases they have attracted FDI when investment rules are harmonized and simplified. Many economic liberals view regional trade blocs as stepping stones toward the possibility of a global free-trade zone as they gradually deepen economic integration. However, not all economic liberals support RTAS. The noted supporter of globalization Jagdish Bhagwati believes that bilateral and regional free-trade agreements generate a "spaghetti bowl effect" of multiple tariffs and preferences, making it harder to eventually reduce trade protection measures

significantly.[35]

Mercantilists tend to focus on the political rationale behind RTAs as well as the way in which they serve a variety of political and economic objectives. For some nations they can be bargaining tools to prevent transnational corporations from playing one state off against another. A classic case, for example, was one of the arguments President Clinton made in support of U.S. efforts to help organize NAFTA—that the United States should be able to penetrate and secure Mexican markets before the Japanese did.[36] He suggested that if the United States did not quickly bring Mexico into its trade orbit in 1993, Japanese investments in Mexico would negate U.S. influence over Mexico's future trade policies.

To date, regional and multilateral free-trade agreements pushed by the European Union, the United States, and Japan exclude the three most important developing countries: China, India, and Brazil. The only bilateral free-trade agreement between countries in these two groups is between the European Union and India. What does this tell us? The developed countries want to advance beyond WTO standards to liberalize investment and remove many "behind-the-border" regulations. They hope that the new liberal standards they negotiate will then be incorporated into future WTO agreements. The most important emerging countries have the power to resist the developed countries' demands for trade liberalization that go beyond commitments already in WTO agreements. Clearly, China, India, and Brazil have become major trading countries, but they are reluctant to sign agreements that do not match their development needs or that do not seem likely to provide them long-term gains. They demonstrate the shift in global economic power that is partly the cause of stalled multilateral trade negotiations. China, India, and Brazil seem to have more interest in signing FTAs with other developing countries and groups such as ASEAN and Mercosur. The overall result of this power shift is a movement away from globalization of trade to regionalization of trade.

It is also important to realize that regional and multilateral agreements negotiated in the last decade encompass much more than traditional trade agreements used to.[37] As we discuss below, liberalization of trade in services is a much more important factor. In addition, agreements now typically address issues that are somewhat related to trade but that have little to do with tariffs. For example, they typically include provisions to protect the rights of foreign investors (as discussed in Chapter 6), reduce regulations and licensing requirements, protect workers' rights and the environment, strengthen intellectual property rights, and restrict subsidies to domestic companies. In theory, these new kinds of provisions help level the competitive playing field between domestic and foreign companies. Many of them are called "behind-the-border" measures to distinguish them from traditional "at-the-border" measures such as tariffs and quotas. However, changes to behind-the-border rules can be very intrusive, threatening social practices, social protections, and political sovereignty. Trade negotiators face strong political pressure from lobbying groups that support or oppose behind-the-border measures.

The Trans-Pacific Partnership

After seven years of negotiations, twelve countries (Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam) signed an agreement in February 2016 establishing the Trans-Pacific Partnership (TPP). Some of its most important objectives were to:

- Significantly liberalize trade in agricultural goods, manufactured goods, and services;
- Strengthen intellectual property rights protections;
- Open government procurement markets; and
- Weaken preferential treatment governments give to state-owned companies.[38]

In his first week in office, President Trump officially withdrew the United States from the TPP, effectively killing it. Nevertheless, many of its elements are likely to appear in future regional agreements.

A big impetus for forming the TPP was to create a strategic counterweight to China, whose rising economic and military power the United States and most TPP countries are increasingly worried about. Without China as a member, the TPP could strengthen U.S. and Japanese economic ties with Asian countries, making them potentially less vulnerable to pressure from China. President Obama acknowledged this after the TPP's full text was published in late 2015:

> The TPP means that America will write the rules of the road in the 21st century. When it comes to Asia … the rulebook is up for grabs. And if we don't pass this agreement—if America doesn't write those rules—then countries like China will. And that would only threaten American jobs and workers and undermine American leadership around the world.[39]

U.S. supporters of the TPP also saw it as a way for the United States to gain trade advantages over Japan and the EU in Asia. That the TPP broadly reflects U.S. trade priorities is clear: a comparison of the TPP text with the text of 74 preferential trade agreements (PTAs) signed by Pacific Rim countries since 1995 finds that the content and text of the TPP—especially in sections on controversial issues—"are taken disproportionately from earlier US trade agreements."[40]

Big importers, retailers and important business associations representing large companies mostly supported the TPP, but many small and medium-sized companies voiced opposition because they feared import competition and did not expect to gain much from exporting.[41] A powerful Japanese farm lobby opposed liberalizing imports of agricultural goods in the TPP. Paul Krugman contended that TPP was not actually focused on promoting free trade because the big TPP countries already have low tariffs and thus would gain very little extra economic growth from the agreement.[42] Civil society groups were particularly concerned that TPP's intellectual property rights provisions would impede access to low-cost generic medicines. Similarly, Dani Rodrik claimed that provisions in the TPP and a proposed United States–EU trade agreement strengthening patents and

copyrights, harmonizing domestic regulatory rules, and giving corporations the right to use international arbitration panels to seek compensation from governments for violating the agreement "seem to be about corporate capture, not liberalism."[43] From a more structuralist perspective, Lori Wallach criticized the secretive negotiating process that produced a "smorgasbord of corporate goodies" and a "backdoor mechanism for the corporate-favored-versions of non-trade policies."[44]

By abandoning the TPP, Trump has opened the way for a competing mega-regional trade agreement to potentially fill the void in Asia. In 2012 the ten members of ASEAN began negotiating the Regional Comprehensive Economic Partnership (RCEP) with China, Japan, India, South Korea, Australia, and New Zealand. Beijing has strongly supported the RCEP, seeing it as a means to weaken U.S. influence in Asia and promote China's economic and geopolitical power. If completed, the RCEP will lower tariffs and trade barriers among members, but it will probably not require countries to strengthen intellectual property rights, liberalize their domestic economies, or promote higher labor and environmental standards. In this sense, RCEP reflects China's goal of relatively open trade with preservation of state sovereignty rather than the traditional U.S. agenda of deep, intrusive economic liberalization. If RCEP succeeds, the United States could find itself increasingly excluded from Asia's growing regional production and trade networks.

TTIP, TiSA, and Liberalization of Trade in Services

Although the TPP is unlikely to have much economic significance without U.S. participation, the Trump administration has not explicitly rejected two other major trade agreements that have been in negotiations since 2013. The first is a mega-regional deal called the Transatlantic Trade and Investment Partnership (TTIP) between the United States and the EU. The second is the Trade in Services Agreement (TiSA), a multilateral deal between the United States, the EU, and 21 mostly high-income countries (noticeably absent are the BRICS countries). If finalized, these agreements would, like the TPP, significantly expand trade liberalization (including liberalization of services) among like-minded developed countries. Negotiations were suspended after Trump won the U.S. presidential election in November 2016, but there is some chance that they will resume.

Some scholars argue that the TTIP, TiSA, and TPP are efforts by the largest OECD states to establish WTO-plus trade rules that can eventually serve as the starting point for new multilateral agreements in the WTO. It may give these states more leverage to convince recalcitrant developing countries like China to accept the rules. According to Daniel Hamilton and Steven Blockmans, part of the appeal of TTIP is that it would "enhance the attractiveness of the transatlantic model of liberal democratic economies" and help solidify U.S. and EU standards globally—not just for trade, but also for treating intellectual property, services, and state-owned enterprises.[45] Future negotiations in the WTO and multilateral forums would thus place pressure on non-TTIP countries to accept these already-established higher liberal trade standards in order to compete on a level playing field for markets in the developed countries.

Negotiations over the TiSA have proceeded with little fanfare, but the proposed deal would potentially mark a major step forward for liberalization of trade in services such as finance, transportation, energy, education, tourism, and construction. Countries have many complex regulations governing domestic services that are difficult to harmonize and reduce compared to tariffs on manufactured goods. Although the 1995 GATS agreement did lower some barriers to trade in services, it left out many sensitive service sectors. For example, it does not cover "services supplied in the exercise of government authority," including health, educational, and social services. In addition, individual governments can decide which sectors they want to liberalize, leaving many services with high tariff-equivalent barriers. Negotiators hope that TiSA will be a template for a stronger WTO services agreement that is needed in a world where services are a major component of global GDP and where digitization and global value chains have made many services newly tradable across borders.

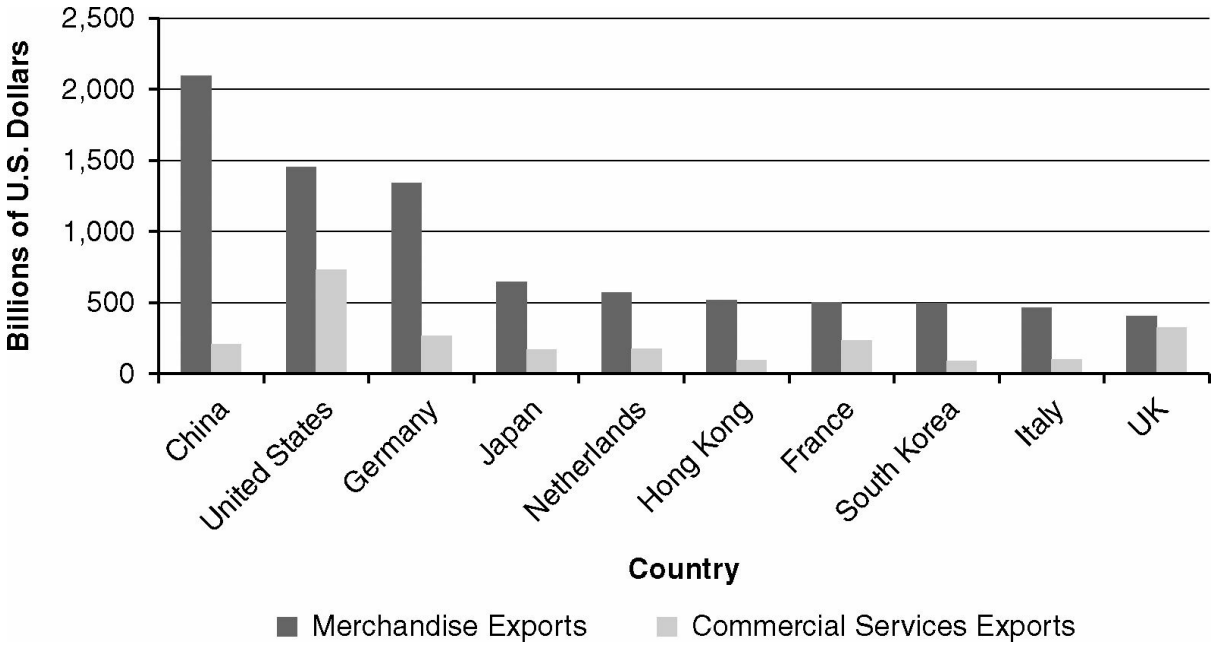


FIGURE 7.5
Merchandise Exports and Commercial Services Exports of Selected Countries, 2016.

Source: Data from World Trade Organization, *World Trade Statistical Review 2017* (2017), p. 102, at www.wto.org/english/res_e/statis_e/wts2017_e/wts17_toc_e.htm.

Why is TiSA potentially so important? First, it is designed to increase competition by requiring each country to give national treatment to foreign services providers in sensitive sectors such as banking, e-commerce, retail sales, and telecommunications. A second issue is how much control governments will be able to maintain over critical public services related to health, education, and the environment. Some countries have public monopolies or state-owned companies that dominate these services; the United States in particular would like to expand the scope for competition from private foreign providers in these areas. As Figure 7.5 shows, the United States is already the world's largest exporter of commercial

services, and it hopes to capitalize on its prowess by expanding market access in China, South Korea, and European countries that have less competitive services providers. Some critics of TiSA fear it would lead to a privatization of many public services, including postal services and health care.

Third, digital information flows are one of the fastest-growing segments of global trade. Cloud-based computing, digital entertainment, and online retailing are valuable services that states need to regulate. For the United States and the European Union, the free flow of information through the Internet is a geopolitical goal; breaking down authoritarian governments' "digital protectionism" is a means to create pressures for political freedom. However, states do not want their own national providers to be eliminated by foreign competitors. Some countries, including in Europe, have adopted data localization requirements to force companies to host data on computer servers only in the country where the data comes from. Other restrictions prohibit foreign companies from transferring and storing data overseas where foreign intelligence agencies might have access to it. The revelations by Edward Snowden of NSA surveillance added national security and privacy concerns to economic worries about liberalizing online services. As in the TPP, the United States wants to prevent TiSA countries from requiring foreign companies to establish data servers in-country. It also wants to allow companies to do business in foreign countries through online platforms without having a physical presence in those countries.

Political economist Patricia Goff reminds us that governments often regulate services for reasons that may have little to do with traditional protectionism_ they may want to advance public health, ensure quality standards, or preserve a certain way of life. For example, some countries limit the size of retail stores and the hours they can operate to preserve the vibrancy of the downtown areas of cities. Liberalization of services in pursuit of trade-related goals or efficiency may make it harder to achieve other public goals.[46]

THE RISKS OF TRADE LIBERALIZATION

The agreements discussed above that constitute the global trade structure promise that trade liberalization will increase economic growth, boost the efficiency of production networks, and stimulate more FDI. Nevertheless, societies also have other goals, including job security, stronger democracy, and environmental protection, that trade liberalization does not promote. In fact, the architects of the global trade structure tend to ignore the risks that come with trade liberalization or deny that trade expansion can make large groups of people worse off. In this last section of the chapter we consider interdisciplinary scholarship that identifies clear risks and negative effects of greater trade openness on some economies and societies. To the extent that a liberal trade structure increases global consumption, it contributes to climate change and deforestation as demand for wood products and palm oil grows. Trade expansion worsens the problem of invasive species and increases consumption of foods that harm public health. Moreover, trade shocks resulting from a surge of cheap imported goods can have devastating socioeconomic consequences for some regions of a country. By analyzing these risks, we can better assess the true costs and benefits of trade liberalization.

Trade and Pests

Most people do not realize that trade introduces many non-native pests and pathogens into countries, causing long-term damage to their economies and ecologies. This problem has always existed historically, but several changes in the last thirty years have significantly increased the costs and risks due to trade-related invasive species. First, the volume of trade has skyrocketed since globalization boomed in the 1990s. Between 2000 and 2016 alone, the value of global merchandise trade jumped by more than 140 percent. Second, closely related to this trend is the rapid rise in containerized shipping, which is the main method by which goods are exported and imported. Ubiquitous shipping containers harbor many pests, as do the wood pallets used to move goods. Third, the increase in exports of timber and agricultural goods provides a particularly important vector for the spread of pests and pathogens.

Countries cooperate closely to minimize the spread of invasive species through trade, particularly on the basis of rules enshrined in the International Plant Protection Convention and the WTO's Agreement on the Application of Sanitary and Phytosanitary Measures. Nevertheless, the unintentional spread of pests is a growing, expensive problem. Forest ecologist Gary Lovett and his colleagues have illustrated this in studies of the effects on the United States of trade in live plants and use of wood packaging materials in international shipping. They estimate that U.S. local governments, the federal government, and homeowners spend billions of dollars every year dealing with damage to forests and urban and suburban trees from trade-introduced pests.[47] Many measures that would reduce the spread of pests are very costly and would require more trade restrictions.

Public Health Risks

In recent years there has been growing interest in the relationship between trade liberalization and public health.[48] Adrian Kay, Helen Walls, and Phillip Baker find that trade and investment liberalization in Asia has contributed to an increase in cardiovascular disease, cancer, diabetes, and respiratory disease.[49] Why might this be the case? Liberalization gives "transnational risk commodity corporations" greater market access in upper-middle-income and lower-middle-income countries where consumption of tobacco, alcohol, and fatty foods has been rising. For example, liberalization of retailing allowed "supermarketization" in Asia, which increased availability of innutritious food.[50] Interestingly, one of the reasons why India has one of the world's lowest per-capita rates of consumption of processed foods and sodas is because it restricts foreign retailers in its markets. Other scholars have shown that countries in a free-trade agreement with the United States have "a 63.4% higher level of soft drink consumption per capita" than countries without such an agreement.[51]

Similarly, trade liberalization increases consumption of highly processed foods and sometimes increases food insecurity if farmers switch to growing cash crops for export and governments reduce subsidies to farmers. Michelle Sahal Estimé, Brian Lutz, and Ferdinand Strobel find that imported foods in the Pacific Island nations are mostly "energy-dense, nutrient-poor processed foods" that contribute significantly to high rates of obesity and diabetes.[52] Palm oil was imported after 1965, and trade and investment liberalization in the 1990s allowed for the entry of global food companies with unhealthy cereal-based products.[53]

Besides trade liberalization's effects on alcohol consumption, tobacco use, and diet, there are important consequences for access to medicines. As we discuss in Chapter 10, trade agreements that strengthen protection for pharmaceutical patents increase the costs of medicines and health care. Finally, there are complex pathways through which trade affects the social determinants of health, such as income, employment, inequality, and social protections.

The Socioeconomic and Political Repercussions of Trade Liberalization

The election of Donald Trump, the British vote to leave the European Union, and the spread of populism in Europe have brought renewed attention to trade issues that liberal IPE theorists have written about for a number of years. Many economic liberals argue that all countries will gain from multilateral trade liberalization over the long term if they specialize in their comparative advantage.

THE EFFECTS OF TRADE SHOCKS IN THE UNITED STATES

In 2016 and 2017, liberal economists David Autor, David Dorn, and Gordon Hanson published several studies on the impacts of trade that sparked considerable debate in the United States. They were interested in how China's entry into the WTO affected the United States and some countries in Europe after 2001. Chinese exports of manufactured goods rose sharply in the 2000s, inflicting an unprecedented "trade shock" on labor markets in developed countries. In U.S. regions with industries that had the highest exposure to Chinese import competition, workers experienced significant unemployment and lower earnings. There was an increase in public transfer payments to displaced workers, but the transfers were far less than the workers' lost earnings. The authors conclude that in the United States, "Labor-market adjustment to trade shocks is stunningly slow, with local labor force participation rates remaining depressed and local unemployment rates remaining elevated for a full decade or more after a shock commences."[a] Workers in industries highly affected by trade cannot easily find jobs at comparable wages in other sectors in their region, and they are slow to move to more dynamic parts of the country. They disproportionately bear the burden of losses from trade.

In a subsequent article, Autor, Dorn, Hanson, and Kaveh Majlesi find that in U.S. congressional districts most exposed to Chinese import competition—and experiencing its localized economic effects—voters between 2002 and 2010 moved from supporting moderates in their party to candidates on the political extremes.[b] Majority non-Hispanic white districts supported more far-right Republicans while majority non-white districts voted for more left-wing Democrats. The trade shock from China in the 2000s explains at least some of the increase in political polarization in the U.S. Congress, and it may connect to the strong anti-free-trade discourse in the 2016 U.S. presidential campaign.

In a third study, Autor, Dorn, Hanson and two other colleagues find that U.S. manufacturing firms "whose industries were exposed to a greater surge of Chinese import competition from 1991 to 2007 experienced a significant decline in their patent output as well as their R&D expenditures."[c] As competition cut their profit margins, firms cut back spending on developing new technologies, potentially hurting long-term innovation in the United States.

Finally, in a related fourth study, Autor, Dorn, and Hanson find that in U.S. regional economic zones that experienced significantly higher competition from imported Chinese manufactured goods from 1990 to 2014, males were disproportionately hurt. Male unemployment rose; the relative wages of men declined; male deaths from drug and alcohol abuse rose; marriage rates fell; and there was a

"sharp jump in the fraction of children living in impoverished and single-headed households."[d] Trade shocks had a significant effect on household structure.

All four of these studies show that trade liberalization can have strong effects on politics, innovation, and the lives of some people. Economic liberals emphasize that, in response, we should not kill the goose (free trade) that laid the golden egg (higher *national* growth and consumption), but ensure that the government taxes the winners to provide much more trade adjustment assistance to the part of the population that loses from trade.

References

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Economic liberals do acknowledge that in the *short term* there will be some clear winners and losers from trade liberalization. For example, many firms try to compete with imports by cutting costs and turning to automation and labor-replacing machinery, forcing redundant workers to seek less secure or less well-paying jobs in the service sector. Uri Dadush points out that increased trade also tends to worsen inequality, particularly between skilled and unskilled workers, and in many developing countries trade has held down wages of unskilled workers.[54] Nevertheless, the expectation is that workers in manufacturing sectors facing significant import competition will move to other sectors where their skills can be used more productively, so that unemployment or declines in income should eventually be offset by new opportunities. Moreover, many economic liberals insist that governments should compensate workers during adjustment to import competition until gains from trade are widely shared. In practice, governments often fail to muster the political will and economic resources to counter "trade shocks" or help those who lose from trade openness (see Box 7.2). But, say economic liberals, that is not a reason to reject free trade; it is a reason for governments to distribute some of the gains from trade to displaced workers through job re-training programs, education benefits, or relocation assistance.

Trade liberalization has been a politically contentious issue in many countries, especially since the emergence of neoliberalism in the 1980s. However, we argue that the political repercussions of trade have grown steadily since the global financial crisis, causing severe tensions in the U.S. political system and fissures in the global trade order.

President Obama tried to manage political risks by balancing free-trade promotion with selective protectionism. While negotiating in the Doha Round and promoting the TPP and TTIP, the Obama administration slapped tariffs on Chinese-made tires and steel and took trade enforcement measures against the EU, India, and other countries. Presidential candidate Hillary Clinton dropped her support of the TPP in an effort to mollify

Democrats angered by trade deals and to attract moderate middle-class Republicans.

Channeling the anti-free-trade anger of white blue-collar workers and rural dwellers, candidate Trump threatened to use trade as an economic weapon against China, Mexico, and other countries. He promised to impose more tariffs and renegotiate trade deals to protect American workers and boost manufacturing at home. He perceived U.S. trade deficits with China, Japan, and South Korea as evidence that these countries were gaining at U.S. expense. In typical mercantilist fashion, he viewed trade as a zero-sum game in which the United States had to seize trade advantages from foreign countries.

In his first nine month in office, Trump proved to be unlike traditional establishment Republicans who support the WTO and RTAS. Instead, he set out to destabilize the liberal world trade order, especially by defending state sovereignty against the authority of international organizations such as the WTO. Lacking a coherent trade policy, he had little appreciation for how trade policy affects international currency values, global investments, and other economic issues. He gravitated to tariffs, trade sanctions, and various trade threats as tools to promote U.S. interests, without appreciating that reciprocity in trade relations had historically advanced U.S. goals around the world. By positing trade as solely about America first, Trump signaled his unwillingness to use persuasion or make sacrifices to maintain U.S. hegemony. Instead, he alienated key U.S. trading partners and brought many multilateral and regional trade negotiations to a halt.

The Trump administration's overall trade policies are influenced by three long-time trade protectionists: Commerce Secretary Wilbur Ross, U.S. Trade Representative Robert Lighthizer, and trade adviser Peter Navarro. As deputy USTR in the Reagan administration, Lighthizer played a major role in negotiating "voluntary export restraints" with Japan and other countries to reduce U.S. imports of steel and semiconductors. The Trump administration withdrew the United States from the TPP, put negotiations with the EU over TTIP on hold, and began negotiations with Canada and Mexico to revamp NAFTA. Canadian and Mexican officials repeatedly balked at U.S. proposals designed to change NAFTA provisions in favor of U.S. companies. At various times, Trump threatened to impose a border tax on Mexican imports and completely withdraw from NAFTA. His administration rattled Canadians by imposing a 300 percent duty on aircraft produced by Canadian manufacturer Bombardier. By threatening to withdraw from the Korea–United States Free Trade Agreement, the administration convinced Seoul to begin negotiations with Washington to revise the agreement, which Trump blamed for the large U.S. trade deficit with South Korea. Responding to U.S. manufacturers, the administration set in motion processes that could lead to anti-dumping duties on imported steel, aluminum, solar panels, and washing machines.

There are major political risks from all of these neo-mercantilist trade initiatives. Narratives about the dangers of free trade may have mobilized disgruntled workers, but the appeals to nationalism also fuel xenophobia. Traditional pro-business Republicans in the U.S. Chamber of Commerce have been alarmed by anti-free-trade rhetoric and threats to integrated supply chains in North America. Ironically, farmers in rural areas that voted heavily for Trump may end up worse off; by September 2017 U.S. agricultural exporters

were beginning to lose market share to competitors in Mexico, Japan, and other countries in the TPP.[55] Moreover, precipitating trade wars with other countries in an effort to reduce the U.S. trade deficit could easily backfire, causing the EU, China, and Japan to retaliate in ways that hurt American exporters and raise prices for American consumers.

CONCLUSION: THE INTERNATIONAL TRADE STRUCTURE AT A CROSSROADS

In this chapter we have emphasized that free trade is an ideal, not a reality. The post-World War II trade structure led to progressive lowering of many barriers to trade in manufactured goods, greater convergence on trade norms and rules, and peaceful resolution of many trade disputes. Trade liberalization has undoubtedly expanded global trade and increased competition to lower prices for many goods and services. At the same time, many barriers to trade in agricultural goods and services have remained, and the digital revolution is forcing states to negotiate new rules to govern the rapid expansion of trade in services that threaten vested interests in societies. States are still adept at fashioning non-tariff barriers to protect domestic firms. Most countries still use subsidies, export credits, selective tariffs, behind-the-border regulations, and other measures to manage trade relations. There are also many losers from trade who lobby for less liberalization and more protective barriers. In the last decade they have become more powerful political forces against globalization in the United States, Britain, and the European Union.

Through many rounds of multilateral negotiations, the industrialized nations have liberalized trade in pursuit of economic growth and peaceful international relations. Most states still have a major interest in negotiating bilateral, regional, and multilateral agreements that open up new trade opportunities, make global value chains more efficient, and encourage more foreign investment. But it is somewhat of a misnomer to describe the results of negotiations as "free-trade" agreements, because they are just as much about "managed trade" and "fair trade." Powerful domestic business lobbies, interest groups, and political leaders shape these agreements to maximize their own gains and deflect trade costs onto other domestic groups and foreign countries.

The economic liberal trade order now faces its greatest threats in decades. Large segments of the population in developed and developing countries now question the benefits of free trade. The stalemate in the Doha Round was the clearest global signal that the momentum for trade liberalization had peaked. Among other things, rising inequality, deindustrialization, stagnant wages, and lower social protections in the developed countries produced a surge in economic nationalism.

As a result, in the last decade Northern states have shifted attention away from the multilateral trading system and the WTO toward more bilateral and regional trade agreements. RTAs simultaneously embrace both the principle of free trade and the practical need for protectionism, making them acceptable to some mercantilists and economic liberals. The focus on regionalism to some extent also reflects the fact that trade within global value chains has become more regional than truly global. Japanese TNCs developed Asian production networks, especially in electronics and automobiles, followed in recent years by Korean and Taiwanese TNCs. American TNCs have dominated production networks with Mexico, Canada, and Central America, while German firms dominate

networks with Central and Eastern Europe.

However, right-wing parties in Europe and the United States have rather successfully disseminated narratives about the dangers of globalization, regionalism, and free trade. By so doing, they have convinced many voters that tariffs and other protectionist policies will boost domestic employment and restore many sovereign powers that states seemingly have lost. In the United States, Trump has signaled that he is willing to destabilize the global economy and shirk traditional American hegemonic responsibilities in the trade, finance, and security structures. As a result, China has an opening to grab the reins of global economic leadership and reshape trade rules and relationships to better reflect its global vision.

The international trade system which for more than three decades combined increased trade liberalization with politically managed trade relationships is facing a strong challenge from mercantilist political forces. We can expect to see more fissures in international trade institutions such as the WTO and in regional trade blocs such as NAFTA and the EU. Tit-for-tat trade retaliation will likely increase, and trade flows will change in response to new trade restrictions. The trade road ahead promises to be rocky.

KEY TERMS

Trans-Pacific Partnership Agreement (TPP) 160
General Agreement on Tariffs and Trade (GATT) 160
law of comparative advantage 162
neomercantilists 163
fair trade 169
food sovereignty 170
reciprocity 171
nondiscrimination 171
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DISCUSSION QUESTIONS

1. Why is trade so controversial?
2. Compare the perspectives of mercantilists, economic liberals, structuralists, and constructivists on trade.
3. What are some of the basic features of the GATT and the WTO? Why did the Doha Round end in failure?
4. Do you see RTAs as being primarily liberal or mercantilist in nature? Why did they proliferate? Are they in decline?
5. How has the United States used trade as a tool to achieve its foreign policy objectives?
6. Why might some states be averse to significantly liberalizing trade in services?
7. Assess the socioeconomic and political repercussions of both trade liberalization and trade protectionism. Which policy do you think would best serve your nation's interests: more free trade or less free trade? Explain your reasoning.

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CHAPTER 8
The International Finance and Monetary Structure



Financial Markets in Frankfurt, Germany.

Source: Shutterstock/A P Photo/Michael Probot.

We recognize insanity, or madness in a man or woman, by erratic, unpredictable, irrational behaviour that is potentially damaging to the sufferers themselves or to others. But that is exactly how financial markets have behaved in recent years.

Susan Strange[1]

Beginning in the late 1980s, cross-border flows of finance (investment) increased rapidly, making possible the expansion of trade and accelerating the process of globalization, but also creating some of the problems that led to the global financial crisis of 2008. When the debt bubble in the U.S. housing market burst, international credit markets froze up and the global banking system nearly collapsed. By 2009 the United States and the European

Union (EU) had some of the highest rates of unemployment since World War II. The U.S. government's emergency interventions in the economy saved big banks and the automobile industry, but many households struggled for years with lower incomes and high monthly debt repayments. The crisis also left many new, heavily indebted college graduates struggling for years to find rewarding jobs with good pay and benefits.[2]

Finance, money, and debt are interrelated in a structure that shapes cross-border flows of capital, the relative value of national currencies as expressed in foreign exchange rates, and government borrowing. Most states are very reluctant to hand responsibility for managing their financial, monetary, and economic affairs over to other states or international organizations. Why do states guard this sovereign power so jealously? As one expert notes, "In all modern societies, control over the issuing and management of money and credit has been a key source of power and distributional consequences have been immense."[3] For this reason, the global finance and monetary structure is often full of tensions that render it difficult to manage effectively.

We begin by explaining the basic features of money and exchange rates. We then move on to discuss three distinct international monetary and finance structures that have existed since the nineteenth century. We describe the major state actors and institutions in each structure and the interplay of markets, political forces, and social forces that have shaped policies and accounted for the shifts from one structure to another. After exploring some of the causes and consequences of three major international financial crises (the Mexican "peso crisis" in 1994, the Asian financial crisis in 1997, and the global financial crisis in 2008), we examine the characteristics of today's finance and monetary structure. We end by contrasting views on whether or not the U.S. dollar is likely to remain the world's top currency.

In this chapter we make six arguments:

- First, after World War II the United States practiced "hegemony on the cheap" while seeking to stabilize Western capitalist economies and contain communism.
- Second, independence among states increased in the 1970s and 1980s, and financial globalization in the 1990s and early 2000s compelled many states to liberalize international currency and finance markets.
- Third, increasingly deregulated global capital markets contributed to a series of financial crises in the 1990s and eventually caused a financial meltdown in 2007 that spread from the United States to other countries.
- Fourth, since the mid-1970s the United States has run huge deficits in its current account that have been offset by large inflows of capital from abroad, especially from Japan, China, and oil-exporting countries.
- Fifth, the growth of nationalist-populist movements in the United States and Europe may destabilize the global finance and monetary structure.
- Sixth and finally, the rise of a more financially assertive China points to more tensions over trade, finance, and debt, but the dominant global role of the U.S. dollar is unlikely to end any time soon.

Finally, as in prior chapters, we use the four major IPE perspectives to help us understand some of the controversial aspects of the finance and monetary structure. In Box 8.1 we provide a chronology of important financial and monetary events since World War II.

CHRONOLOGY OF MONEY AND FINANCE EVENTS

1944	The International Monetary Fund and the World Bank are created at the Bretton Woods Conference.
1947–1971	The qualified gold standard and fixed exchange rate systems run their course.
1948	Marshall Plan aid begins flowing to Western Europe to help recovery.
1958	Western European countries remove many restrictions on convertibility of their currencies into dollars and other foreign currencies.
1971	U.S. president Nixon unilaterally breaks the Bretton Woods agreement by closing the gold window, devaluing the U.S. dollar, and imposing a surcharge on all Japanese imports into the United States.
1973	The float or flexible exchange rate system is established.
1980s	The IMF extends major assistance to debt-ridden developing countries such as Brazil and Mexico while demanding adoption of structural adjustment programs.
1985	The G5 countries agree in the (New York) Plaza Accord to manipulate exchange rates by depreciating the U.S. dollar relative to the yen and the Deutsche mark.
1973	The Maastricht Treaty establishes a formal process for completing the European Economic and Monetary Union (EMU).
1994–1995	The Mexican Peso Crisis.
1997–1998	The Asian Financial Crisis.
1998	The European Central Bank (ECB) is created.
2002	Euro notes and coins are introduced into the Eurozone.
2008	Severe problems in the U.S. housing market and banking system trigger a global financial crisis that lasts into 2009.
2010	The Greek debt crisis begins. The IMF and the ECB extend loans to Greece in return for its implementation of austerity measures.
2016	In a referendum, voters in the United Kingdom approve withdrawal (Brexit) from the European Union.
2017	British Prime Minister Theresa May applies for Great Britain's withdrawal from the EU. > The Chinese renminbi is added to the IMF's basket of reserve currencies (the Special Drawing Rights basket).

CURRENCIES AND FOREIGN EXCHANGE: THE BASICS

In a barter economy, goods and services held by one person are exchanged for those held by another person. Because this kind of economy is inefficient and limits long-distance trade, economic historians and anthropologists believe that money was introduced to facilitate transactions between more people over greater distances. By the second millennium C.E., the Babylonians had clear laws on the composition and use of money. In his famous work *Politics,* the Greek philosopher Aristotle included a discussion of money in his chapter on political community. Today, most national governments have an official bank that prints and distributes money. In monetary unions like the European Community, member states have a common currency and share responsibility for printing and distributing money within the union.

Money is usually accepted as a store of value; a customer can present it to a business in exchange for a good or service. Businesses usually also accept payments we make with credit cards, debit cards, or even PayPal because they can convert these payments at a bank into money taken from our accounts. When people lose faith in the value of their currency, as in Weimer Germany during the interwar period and in contemporary Venezuela, the currency becomes less reliable as a store of value and is less likely to be accepted by sellers of goods and services. As a result, it may become difficult for people to buy daily necessities except by resorting to barter.

When parties in one country want to buy goods or financial assets from another country, they have to convert their local currency into the currency of the sellers. These transactions contribute to setting currency exchange rates that affect the value of everything a nation buys or sells on international markets. Those rates also impact the cost of credit and debt, and the value of foreign currencies held in national and private banks. Exchange rates are important to banks, investors, and travelers. Each day major international banks and brokerage firms buy and sell millions of dollars, British pounds sterling, yen, euros, and other currencies. A change in the value of one currency compared to another can cause large gains or losses for financial institutions. States are normally concerned about how short- and long-term shifts in the relative values of currencies will affect imports and exports.

When a currency's exchange price rises—that is, when the currency becomes more valuable relative to others—we say that it appreciates. When its exchange price falls and it becomes less valuable relative to other currencies, we say it depreciates. For example, on New Year's Day 2014, €1 exchanged for $1.36, but by New Year's Day 2017 €1 exchanged for just $1.05. Over this three-year period, the euro depreciated against the dollar by 23 percent, meaning it became relatively less valuable. So, for a European tourist holding euros, it was much cheaper to visit the United States in 2014 than in 2017. If you look in any major newspaper, you can see current foreign exchange rates. As you can imagine,

exchange rate fluctuations also carry implications for banking, debt, and trade.

Banks care about exchange rates because they have to trade currencies to support their clients. Many large banks also have "trading desks" that specialize in making bets on the direction of currency markets. They will make promises to exchange a certain amount of one currency for another at a future time based on their prediction of how currencies will shift against each other. This kind of currency futures contract can yield a big bank millions of dollars in profits, but it can also cost them dearly if they are wrong about the direction of currency markets. For example, in 2002 Allied Irish Bank lost $700 million because a single "rogue" trader made bad foreign exchange bets. The trader did seven years in prison for trying to hide his losses from management.[4]

Another important feature of foreign exchange is related to how hard or soft a currency is. Hard currency is money issued by large, wealthy countries with stable political systems, well-governed economies, and strong militaries. Such countries include the United States, Canada, Japan, Great Britain, Switzerland, and members of the Eurozone (European countries that use the euro—see Chapter 12). A hard-currency country can generally exchange its own currency directly for other hard currencies, and therefore for foreign goods and services—giving that country and its businesses a distinct advantage in world markets. Hard currencies such as the U.S. dollar, the euro, the British pound, and the yen are easily accepted for international payments.

A soft currency is not widely accepted outside its home country, usually because foreigners believe that political and economic conditions in the country will make the value of the currency unstable or because the volume of international trade in that currency is too small to establish a reliable market value. Many less developed countries (LDCs) have soft currencies, as their economies are relatively small and less stable than those of other countries. A soft-currency country usually must acquire hard currency (by exporting or borrowing) in order to purchase goods or services from other nations.

A key point to remember is that the exchange rate is just a way of converting the value of one currency into another. What matters is the *acceptability* of the currency to the actors (banks, tourists, investors, and state officials) involved in a transaction and how much its value *changes* over time. Many political and economic forces affect exchange rates. These include:

- Whether a currency is considered to be hard or soft;
- Currency appreciation and depreciation;
- Currency exchange-rate manipulation;
- Whether one's currency is fixed to the value of another currency;
- Interest rates and inflation; and
- Speculation.

Changes in currency values have profound political and social consequences; they create winners and losers in domestic markets that are connected through trade and finance. If a nation's currency appreciates, companies that export goods and services will be hurt as their

products become relatively more expensive internationally. However, importers in the same country (con-sumers of foreign goods and services and companies using foreign inputs in their production processes) will benefit because imports become cheaper.

Exchange rates are often set by supply and demand in the market. However, a central bank can also intervene in currency markets, sometimes surreptitiously, buying up its country's own currency or selling it in an attempt to alter its exchange value. When the demand for a country's currency declines, a central bank can use its foreign reserves to buy (demand) its own currency, pushing up its value.

For many states, an *undervalued currency* that discourages imports and increases exports can be good for some domestic industries and shift the balance of international trade in that state's favor. However, an undervalued currency makes goods such as food or oil that must be imported more expensive. Undervaluation can also reduce living standards and contribute to inflation.

Sometimes LDCs intentionally overvalue their currency to make imported goods such as machinery, arms, food, and oil cheaper, but at the expense of making the country's exported goods less competitive abroad. In practice, it is hard for LDCs to reap the benefits of overvaluation in any meaningful way because their currencies are usually soft and not used much in international business and finance. In some cases, developing countries with overvalued currencies have unintentionally damaged their domestic agricultural sectors as consumers became dependent on artificially cheap imported foodstuffs.

Two other important variables that impact exchange rates are inflation and interest rates. All else being equal, a nation's currency tends to depreciate when that nation experiences a higher inflation rate than other countries. Inflation—a rise in overall prices—weakens the real purchasing power of money within its home country. It may also make the currency less attractive to foreign buyers and cause its foreign exchange rate to depreciate. Likewise, interest rates influence the desirability of purchasing assets in a particular currency. For example, when interest rates declined in the United States in the 1990s and 2000s, the demand for dollars to purchase U.S. government bonds and other interest-earning assets decreased, pushing the dollar's exchange rate to a lower value. In the same way, higher U.S. interest rates increase demand for the dollar, as dollar-denominated investments become more attractive to foreigners.

Finally, one of the major currency and finance issues that concerned John Maynard Keynes (see Chapter 2) was speculation, which is betting that the value of a currency will go up or down in the future. As mentioned above, many individuals and financial institutions look to make profits by trading in currencies based on expectations of future foreign exchange rates.

As we discuss later in the chapter, capital that moves quickly in and out of a country is called hot money. When foreign investments pour into a country, they often push up prices for stocks, bonds, and houses well beyond what is reasonable. These price bubbles can burst when investors rapidly pull their money out in anticipation that market prices will fall.

THREE FOREIGN EXCHANGE RATE SYSTEMS

Since the nineteenth century, there have been three structures and sets of rules related to foreign exchange rates.[5] The first system was the gold standard, a tightly integrated international order managed by Great Britain that existed until the end of World War I. The second was the Bretton Woods fixed exchange rate system created by the United States and its allies as World War II ended and managed by international institutions, most notably the IME. The current system we live with is the flexible (or floating) exchange rate system, which the IMF and other international institutions have roles in managing. As we explore some of the basic features of these systems, we will also highlight capital mobility across national borders, an issue directly related to currency exchange and debt.

Phase I: The Classic Gold Standard and Its Collapse

We tend to think of the related issues of interdependence, integration, and globalization as post-Cold War phenomena, but from the end of the nineteenth century until the end of World War I, the world was perhaps even more interconnected than it is today. Large cross-border flows of money made it hard for countries to "buffer" their domestic policies from the consequences of international financial and monetary changes. The leading European powers also invested heavily in their colonies, building infrastructure to tie those societies to world markets. The currencies of most nations were part of a fixed exchange rate system that linked currency values to the price of gold, thus the "gold standard." Similar to the European Union today, some countries in specific geographic regions created "monetary unions" in which their currencies would circulate.[6]

The gold standard system was a *self-regulating* international monetary order rooted in classical liberal ideas. Different currency values were "pegged" (set) to the price of gold. If a country experienced a balance of payments deficit—that is, if its outflow of money exceeded its inflow of money—corrections occurred almost *automatically* via wage and price adjustments (see Box 8.2). A country would also try to narrow its deficit by selling some of its gold, raising interest rates, and cutting government spending. Higher interest rates were supposed to attract short-term capital that would help finance, or balance, the deficit. In effect, domestic monetary and fiscal policy was "geared to the external goal of maintaining the convertibility of the national currency into gold."[7] Before World War I Great Britain's pound sterling was the world's strongest currency. As the world's largest creditor, Great Britain loaned money to other countries to encourage trade when economic growth slowed. It functioned as the global hegemon in trying to smooth out problems in this largely "self-regulating" system.

The gold standard had a stabilizing, equilibrating, and confidence-building effect on the system. It died by the end of World War I, although Britain tried to resurrect it again in the mid-1920s before finally abandoning it at the beginning of the Great Depression. After World War I Britain became a debtor nation, no longer holding onto huge reserves of gold

or sterling (silver), and the U.S. dollar displaced the pound as the world's strongest and most trusted currency. However, according to many hegemonic stability theorists, the United States failed to meet the international leadership responsibilities commensurate with its economic and military power after World War I, which contributed to the severity of the Great Depression.[8]

Heterodox liberals argue that the gold standard faced severe problems when the extension of the electoral franchise in industrialized countries and the growth of organized labor created pressures on governments to avoid the automatic policy adjustments that the gold standard required in order to meet domestic needs. Some states preferred to depreciate their currencies to stimulate exports rather than slow the growth of their economies or cut state spending. Many states tried to insulate their economies from international financial forces by adopting "capital controls" (limits on how much money could move in and out of the country). Even Keynes supported these measures, saying, "Let finance be primarily national."[9]

The structuralist Karl Polanyi argued that by the end of World War I, 100 years of relative political and economic stability ended when economic liberal ideas no longer seemed appropriate given world events and social conditions.[10] The negative effects of the gold standard, combined with the profound social and economic disruptions of World War I, led to increased demands for relief from a brand of capitalism that periodically failed, as evidenced during the Great Depression.

Phase II: The Bretton Woods System and Fixed Exchange Rates

During the Great Depression, the international monetary and finance structure was in a shambles. Some of the highest trade tariffs in history and the non-convertibility of currencies increased hostility amongst the European powers, ultimately contributing to the outbreak of World War II. As it became more likely that the Allied Powers would prevail in World War II, the United States and its allies met in Bretton Woods, New Hampshire in July 1944 to devise a plan for European recovery and a new postwar international monetary and trade system that would encourage growth and development. In an atmosphere of cooperation, the fifty-five participating countries wanted to avoid a return to the high unemployment rates and the malevolent competitive currency devaluations of the 1930s. Keynes, Great Britain's representative, believed that unless states coordinated their actions for mutual benefit, their individual efforts to gain at the expense of their competitors would eventually hurt them all and return the world to conflict.

BOX 8.2 THE BALANCE OF PAYMENTS

The balance of payments registers all of the international monetary transactions between the residents of one country and those of other countries in a given year. In other words, it is an accounting of the total inflows of payments to a country and the total outflows of payments from a country. These inflows and outflows are recorded in the *current account* and the *capital and financial account.*

In the current account, inflows come from sales of goods and services (exports), receipts of profits and interest from foreign investments, and unilateral transfers of money or income from other nations. These transfers include foreign aid a nation receives and money migrants send home to friends and families. Outflows in the current account are purchases of goods and services from other countries (imports), payments of profits and interest to foreign investors, and unilateral transfers to other nations.

When a state has a *current account surplus,* its receipts are greater than its expenditures, so that on net these international transactions increase national income. However, when a nation has a *current account deficit,* outflows are greater than inflows in a particular year, and the net effect of these international transactions is to reduce the national income of the deficit country.

What is commonly referred to as the *balance of trade* (or *trade balance) is* usually analyzed *separately* from other items in the current account. It registers a nation's receipts from exports minus payments for imports. The trade balance is usually the biggest component of a country's current account balance.

The other account in the balance of payments—the *capital and financial account*—registers international transactions involving financial assets, including net foreign investments, borrowing and lending, sales and purchases of assets such as stocks and real estate, and official foreign exchange reserves held by a country's government. If there is a net inflow of money to the capital and financial account, foreigners are net purchasers of a country's financial assets. If there is a net outflow (deficit) of funds, the country has increased its net ownership of foreign financial assets.

Normally, a surplus in one account must be offset by a deficit in another—establishing an accounting balance of zero. A nation with a current account deficit must either borrow funds from abroad or sell assets to foreign buyers to pay its international bills and achieve an overall payments balance. A current account deficit also *requires* a capital account surplus in order to balance the two accounts. Likewise, a current account surplus generates excess funds that can purchase foreign assets. There are many political consequences of any nation's balance-of-payments status. For instance, if a state has trouble covering a trade deficit by borrowing from abroad or attracting foreign investment, it will need to increase output at home to generate more exports, and/or it will have to decrease consumption of imported goods.

Responding to balance-of-payments crises requires states and their societies to make difficult political and social choices about who will benefit and lose. Increasing output, for instance, might mean forcing workers to accept lower wages, giving tax incentives to businesses, or removing regulations. Decreasing consumption might also involve raising taxes and cutting government programs, and a country often needs to raise interest rates to attract savings and encourage foreign investment. In these circumstances, it is easy to see why currency devaluation is so attractive to states, as it can quickly generate more exports by making goods less expensive. However, such a move is also likely to invite retaliatory devaluation by other states, negating the economic gains of the first state and causing international tension.

In 2016, the United States had a current account deficit of $452 billion, while Germany had a current account surplus of $290 billion.

At Bretton Woods the Great Powers created the International Monetary Fund (IMF), the World Bank, and what would later become the General Agreement on Tariffs and Trade (GATT). The World Bank was to promote economic recovery immediately after the war and then turn its energies to addressing long-term economic development issues. Mercantilists and realists believe that the Great Powers primarily wanted the IMF to ensure a stable international monetary system. Under pressure from the United States, the IMF adopted a modified version of the former gold standard's fixed exchange rate system that was more open to market forces, but *not* divorced from politics. At the center of this modified gold standard was a fixed exchange rate mechanism that set the value of an ounce of gold at U.S. $35. The values of other national currencies would fluctuate against the dollar as supply and demand for those currencies changed. Additionally, governments agreed to intervene in foreign exchange markets to keep the value of currencies no more than 1 percent above or below the fixed exchange rate (called "par value").

If supply and demand conditions caused the value of any currency to move beyond the band limits, central banks were required to buy up excess dollars or sell their own currency until the currency value moved back closer to par value, reestablishing a supply—demand equilibrium. As in the earlier system, central banks could also buy and sell gold to help settle their accounts, which the United States often did. Confidence in the system relied on the fact that U.S. dollars could be converted into gold at a set and guaranteed price, and at the end of the war, the United States started with the largest amount of gold backing its currency. This arrangement stabilized the Western monetary system, which desperately needed the members' confidence and a source of liquidity to boost recovery in Europe and Japan.

From the economic liberal perspective, John Maynard Keynes was instrumental in convincing the Allied powers to construct a new international economic order based on liberal ideas. The "Keynesian compromise" allowed individual nation-states to *continue* regulating domestic economic activities within their own geographic borders. Among other things, states could maintain capital controls, which are rules limiting the amount of

money coming into or leaving a country. In the international arena, the IMF collectively managed financial policies with the goal of eventually expanding international financial markets and trade. The IMF also sought to ensure nondiscrimination in the conversion of currencies and increase the amount of liquidity in the international financial system. These goals complemented U.S. liberal values and policy preferences at little cost to the United States. The IMF provided *temporary* assistance to all debtor countries while they adjusted their economic structures to the emerging international economy.

At the Bretton Woods conference, Keynes wanted to create an institution that could provide generous aid to both the victors and the vanquished nations after World War II. He especially wanted to prevent a repeat of the brutal and ultimately destructive terms the victors imposed on the losers at the end of World War I. On the issue of debt he was adamant that creditors *should* help debtors make adjustments in their economies. However, U.S. Treasury official Harry Dexter White's plan for the newly created IMF and World Bank was to put nearly *all* of the adjustment pressure on debtor countries, without any symmetric obligation for creditors to make sacrifices.

Many structuralists argue that the Bretton Woods institutions were vessels for the values and policy preferences of the major powers, especially the United States.[11] Once the Cold War began in 1947, the United States consciously embraced the role of the Western hegemon by providing collective goods such as economic assistance and security for its allies. In the emerging "grand bargain," the United States provided financial assistance to Japan and Europe via the Marshall Plan. Moreover, many U.S. corporations invested in Western Europe, providing the allies with scarce liquidity. The United States also protected the Europeans from a possible Soviet invasion and from Soviet efforts to help communist parties get voted into power legally in Italy or France. The United States deployed U.S. troops, heavy armaments, and eventually short- and medium-range nuclear missiles to bases in Great Britain, West Germany, and Turkey to contain the USSR.

These U.S. moves opened up opportunities for U.S. exports and investments while advancing the broader U.S. objective of preserving capitalism in Western Europe and Japan. In return, Western Europe accepted U.S. efforts to *divide* the West from the Soviet-dominated Eastern Bloc and to limit capital movements into and out of the communist nations. Meanwhile, U.S. allies accepted the dollar as the "top currency" used in trade and financial investments. This saved the United States a good deal of money on foreign exchange transactions and helped it maintain the strength of the U.S. dollar against other currencies. Finally, because its international market value was fixed to gold, the dollar became the main reserve currency held in central banks as a store of value.

Hegemony on the Cheap: The Bretton Woods Bargain Comes Unstuck

During the heyday of the Bretton Woods system from 1956 to 1964, the United States benefited from providing collective economic goods and military defense for its allies. However, according to Benjamin Cohen, the transatlantic political-economic "bargain" gradually became "unstuck."[12] The Europeans increasingly criticized the United States for

abusing its hegemony over its allies without immediate penalty. By printing more money, the U.S. government could spend freely on domestic programs such as the Great Society and, at the same time, fund the Vietnam War. This allowed the United States to run a deficit in its balance of payments and to export its inflation to its allies. The Europeans pressured the United States to cut back on government spending or to sell its gold in order to repurchase surplus dollars. At one point, French president Charles de Gaulle complained that France had no choice but to underwrite the U.S. war in Vietnam by holding weak U.S. dollars in its banks as required instead of converting them to gold, which would have forced the United States to curb its ambitions in Vietnam or would have nearly emptied the U.S. gold reserve.

Although Western Europe's economic recovery weakened their demand for U.S. dollars by the 1960s, the agreement to fix the value of the dollar to gold made it impossible to devalue the dollar in response. The monetary and finance structure had become *too* rigid, making it difficult for states to promote their own interests and values. In effect, the *success* of the fixed exchange rate system was also undermining the value of the U.S. dollar and weakening U.S. leadership of the transatlantic alliance.

Unexpectedly, to prevent a recession at home, President Richard Nixon *unilaterally* decided in August 1971 to make dollars nonconvertible to gold. The United States devalued the dollar, and to help correct its deficit in the balance of payments, it imposed a 10 percent surcharge on all Japanese imports coming into the United States. Some scholars have suggested that by making these moves the United States purposefully abandoned its role as a benevolent hegemon for the sake of its own interests. Both the United States and Western Europe accused one another of not sacrificing enough to preserve the fixed exchange rate system. From the U.S. perspective, Western Europe should have purchased more U.S. goods to help the United States correct its balance-of-payments problems. On the other hand, the Europeans argued that trade was not the primary problem. Instead, the United States needed to cut its spending and get out of Vietnam—two things that were politically unacceptable to the Nixon administration.

Phase III: The Flexible Exchange Rate System and the Changing Economic Structure

The effort to reform the monetary system in 1973 led to the flexible exchange rate system, also known as a managed float system. The major powers authorized the IMF to widen the trading bands so that market forces could more easily determine changes in currency values. Some states independently floated their currencies, while many of the countries that joined the European Economic Community (an early version of the European Union) coordinated their policies regionally. Many states still had to deal with balance-of-payments issues, but the framework for collective management was meant to be less constraining on their economies and societies.

Several other developments contributed to the end of the fixed exchange rate monetary system. In the early stages of the Bretton Woods system, policy makers intentionally limited the movement of private finance and capital between countries for fear that

financial crises like those in the 1920s and 1930s could easily spread from one country to many others. By the late 1960s, there were rising private capital outflows—especially from the United States—in the form of direct investments by MNCs, portfolio investments (such as purchases of foreign stocks by international mutual funds), and commercial bank lending. Flexible exchange rates complemented the relaxation of capital controls, and global liquidity increased.

The adoption of the flexible exchange rate system reflected several other political and economic developments, including the growing influence of the Japanese and West European economies and the rise of the Organization of Petroleum Exporting Countries (OPEC). By the early 1970s, Japan's rising living standards and high rates of economic growth had turned Japan into a major player in international monetary and finance issues. Robert Gilpin and other realists make a strong case for the connection between the diffusion of international wealth at the time and the emergence of a new multipolar security structure that would be cooperatively managed by the United States, the Soviet Union, the EU, Japan, and (later) China (see Chapter 9).[13]

The rise of OPEC and large shifts in the pattern of international financial flows after oil price increases in 1973–1974 and 1978–1979 helped produce a *global* financial network. As OPEC states demanded dollars as payment for newly expensive oil, the demand for U.S. dollars increased, which helped maintain the dollar as the top currency in the international economy. Many of the OPEC "petrodollars" were then deposited back into Western banks, from which they were recycled in the form of loans to developing countries. However, between 1973 and 1982, the debt of non-oil exporting developing nations increased from $130 billion to $612 billion, generating debt crises in Latin America and Africa in the 1980s.[14]

In the 1970s and early 1980s, trade imbalances in the developed countries contributed to "stagflation" (slow economic growth accompanied by high unemployment and inflation). Beginning in 1979, the U.S. Federal Reserve focused on fighting domestic inflation by raising interest rates to tighten the money supply, which slowed down the economy and contributed to an international recession. At this time a change in the dominant political-economic philosophy occurred in Great Britain and the United States. The prevailing Keynesian orthodoxy was swept aside in favor of the neoliberal ideas of Friedrich Hayek and Milton Friedman (discussed in Chapter 2).

The Iron Lady and the Cowboy

In the early 1980s the governments of Prime Minister Margaret Thatcher and then President Ronald Reagan privatized national industries, deregulated financial and currency exchange markets, took steps to weaken labor unions, cut taxes at home, and liberalized trade policy. Theoretically, these measures were supposed to produce increased savings and investments that would stimulate economic growth. In 1983, economic recovery did begin, but many experts suggest that growth was due more to a significant drop in world oil prices than neoliberal policies.

Despite his laissez-faire rhetoric, Reagan raised defense spending significantly as part of a renewed Western effort to contain the Soviet Union and top communist expansion in developing countries. A larger defense budget and a strong dollar led to record U.S. trade deficits, especially with Japan. Instead of cutting back on government spending or raising taxes in order to shrink the U.S. trade deficit, the Reagan administration pressured Japan and other states to revalue their currencies. Many mercantilist-oriented trade officials also accused Japan, Brazil, and South Korea of not playing fair when they refused to lower their import barriers or reduce their export subsidies.

By 1985, the United States had become the world's largest debtor nation, financing its deficits by borrowing some $5 trillion from other countries.[15] U.S. companies complained that the overvalued dollar caused a flood of cheap imports that was destroying domestic industries, and demands for protectionism grew. The United States pressed the other G5 states (Great Britain, West Germany, France, and Japan) to meet in September 1985 in New York, where they agreed to intervene in currency markets to *collectively manage* exchange rates and lower U.S. trade deficits. The Plaza Accord committed the G5 to work together to "realign" the dollar so that it would depreciate in value against other currencies, which in the long run may have contributed to Japan's slow growth in the 1990s. The Accord is an example of what Benjamin Cohen characterizes as a monetary hegemon's ability to delay and deflect the costs of adjusting to external imbalances.[16]

THE ROARING NINETIES: GLOBALIZATION AND FINANCIAL CRISES

The Reagan administration's neoliberal ideas continued to influence developments in the international finance and monetary structure in the 1990s and into the early 2000s. Economic liberal policies and development strategies served as the basis of the "Washington Consensus" and the globalization campaign. By the end of the Cold War in 1990, many of the controls on private capital flows had been removed. In 1997, for example, net private capital flows to developing countries amounted to $304 billion, compared to net official flows of only $40 billion. This money bolstered economies in Southeast and East Asia that emphasized export sales. Revolutionary advances in electronics, computing, and satellite communications enhanced the integration of national economies and further globalized the monetary and finance structure. Increased public and private finance also helped generate tremendous increases in the volume and value of international trade.

In the early 1990s, the dollar continued to lose value against the currencies of major U.S. trade partners. The U.S. Federal Reserve Board decreased interest rates to improve exports and expand growth. By the mid-1990s, the U.S. economy had recovered; inflation fell, consumers spent more, and foreign investors increased demand for dollar-denominated assets. The newly created European Central Bank (ECB) maintained price stability for its members and helped insulate European currencies from changes in the value of the U.S. dollar. From 1995 to 2002 the dollar sharply increased in value, partly in response to the financial crises we discuss blow.

The Peso Panic of 1994

As globalization took off during the Clinton presidency, investors poured money into a select group of developing nations that were ill prepared to regulate their booming financial markets. The Mexican Financial Crisis of 1994–1995 was the first crisis in the new era of *global* finance and investment.

In anticipation that the North American Free Trade Agreement (NAFTA) would improve Mexico's prospects for political stability and economic growth, large investors jumped into Mexican real estate, stocks, and bonds, driving prices up sharply. In this euphoric phase, the economic ambitions of fund managers were disconnected from political and social realities in Mexico. The wheels fell off the wagon in 1994 when a rebellion broke out in the poor region of Chiapas and the ruling party's presidential candidate was assassinated. Suddenly, foreign investors began shifting funds out of Mexico, which put pressure on Mexican officials who wanted to keep their exchange rate fixed to the dollar. The government had an obligation to give investors U.S. dollars when they sold their Mexican stocks, bonds, and pesos. As this pushed up the value of the dollar, the Mexican government knew that its banks would soon run out of U.S. dollars. To stem the outflow of money, Mexican officials raised interest rates to make rates of return on foreign

investments higher. But because this move made bank loans more expensive for borrowers, the Mexican economy slowed down.

Investors continued the stampede out of Mexico, triggering a drastic depreciation of the peso in late 1994 and a severe recession in 1995. The United States organized a massive bailout in coordination with the IMF, funneling billions of dollars of loans to Mexico. Although Mexico avoided total economic collapse, its inflation rate doubled and unemployment jumped to 7.6 percent by August 1995. Mexico's GDP fell off dramatically in 1995, effectively wiping out the short-term economic gains from the NAFTA boom. Exports recovered due to the peso's lower value, but a credit crunch and higher poverty gave the country what critics called a "tequila hangover."

The Asian Financial Crisis

Less than two years after the Mexican crisis, the Asian financial crisis struck, causing economic damage that lasted for years afterwards in East and Southeast Asia.[17] It demonstrated how easily crises could occur—even in states with otherwise sound economic policies—when global market actors lose confidence in a government's ability to manage its finances or live up to external expectations. The sudden collapse in value of Thailand's currency, the baht, on July 2, 1997 started a chain reaction of economic, political, and social effects in Indonesia, Malaysia, Taiwan, Hong Kong, and South Korea and threatened to unleash a worldwide recession.

One of the main causes of the crisis was an inflow of investment capital to Thailand, where interest rates were *higher* than those in the United States. A fixed exchange rate of 25 baht per U.S. dollar encouraged Thai finance companies to borrow U.S. dollars on global markets, convert them to Thai baht, and lend them out at a higher interest rate in Thailand. Banks and borrowers used the funds to expand businesses, purchase property, and even speculate in Thai stocks. Consequently, inflated prices led to business bubbles.

Problems developed when some Thai banks were found to have many bad loans on their books—loans that were unlikely to be repaid on time and perhaps could never be repaid at all. International investors became concerned about the health of the Thai economy and began to pull their funds out of Thailand, causing the Thai government's supply of dollar reserves to be drawn down. When everyone tried to pull out quickly and unexpectedly, it was impossible for the Thai government to pay everyone in dollars.

These conditions were perfect for a speculative attack, which is essentially a confrontation between a central bank, which pledges to maintain its country's exchange rate at a certain level, and international currency speculators, who are willing to wager that the central bank is not fully committed to its exchange-rate goal. Hedge funds and other private investment funds typically bet heavily against a currency that appears to be trading at a higher price than is justified by political-economic conditions. As long as investment capital is freely mobile between countries, currency crises caused by speculative attacks and investment bubbles are unavoidable.

When the Thai government was forced to abandon its fixed exchange rate of 25 baht per dollar in July 1997, investors started to pull funds out of Malaysia, Indonesia, the

Philippines, and South Korea. When the dust settled in 1998 in these countries, their currencies had lost between 40 and 70 percent of their value against the dollar and their stock market indexes had plunged 30 to 50 percent. The human costs of currency speculation were very real. Many businesses went bankrupt because they could not possibly repay their U.S.-dollar loans at the new exchange rates. Many people in Southeast Asia had acted rationally and worked hard but found themselves deep in debt, their life savings wiped out, and with few prospects for short-term recovery. The losses in Thailand were enough to lower the average per-capita income by about 25 percent in one year, which for many felt like the Great Depression in the United States in the 1930s.

The Asian financial crisis was followed by similar crises in Russia in 1998 and in Argentina between 1999 and 2002. The IMF and other international financial institutions responded to all these crises by extending loans to troubled countries, but the relatively meager aid came after much of the damage had already been done. Moreover, the conditions attached to the loans aggravated the economic downturns, thus tarnishing the IMF's credibility as a good manager of the global financial system.[18] Emerging countries became convinced that the IMF's prescriptions for budget cuts, higher taxes, unregulated financial flows, and privatization were inappropriate for a country during a financial crisis. Even if these measures (structural adjustment policies) that were demanded by the IMF might have paid off in the long run, in the short run the economic pain and severe political instability were too much for a society to tolerate. Throughout most of the 2000s, many developing countries shunned the IMF as best they could by building up foreign currency reserves in case they faced financial problems. It was not until the global financial crisis of 2007 that developed countries would begin to understand why emerging markets rejected their Washington Consensus and neoliberal policies.

THE GLOBAL FINANCIAL CRISIS OF 2007: THE BUBBLE BURSTS

During the 2000s many mortgage companies and big banks earned big profits from the fast-growing home real estate market. They offered a wide range of new products such as ARMs (adjustable rate mortgages) and subprime mortgage loans to attract first-time buyers, many of whom had weak credit scores and unstable incomes. Banks and lenders packaged these risky loans (along with loans to more creditworthy borrowers) into "mortgage-backed securities" and then resold them to other banks, hedge funds, and foreign financial institutions. Many investors throughout the global financial system viewed mortgage-backed securities and other kinds of collateralized debt obligations (CD Os) as good investments with the potential for high returns. In reality, many of the underlying loans that were bundled into securities had a high risk of default.

A few experts warned public officials about a growing real estate bubble, but their forebodings attracted little attention until the subprime mortgage market started to crumble. By early 2007 a slew of large mortgage companies with portfolios of subprime loans worth $13 trillion—20 percent of U.S. home lending—filed for bankruptcy. In addition, Merrill Lynch, Citigroup, and other large financial institutions reported billions of dollars of losses on sub-prime mortgage investments. By the end of 2007, the U.S. Federal Reserve and the European Central Bank attempted to stabilize the financial system by injecting several hundred billion dollars into the money supply for banks to borrow at a low rate.

By the summer of 2008 many analysts recognized that banks would eventually not be able to cover their toxic securities, making them increasingly risky investments. Because big banks in the United States, Europe, and Japan were intensely interconnected, losses tied to U.S. mortgage securities and other risky investments spread throughout the world banking system. Growing corporate and consumer debt added to concerns. The real estate bubble began to tear in July 2008 after panicky investors started unloading their stocks in the government-backed Fannie Mae and Freddie Mac loan agencies, which together owned or guaranteed $6 trillion of the $12 trillion mortgage market in the United States. Congress hastily passed a "rescue plan" to try to assure investors that the loan agencies would remain solvent, but many investors began seeking safer havens for their money.

In September, when the U.S. government refused to rescue Lehman Brothers, a big investment bank, it collapsed and filed for bankruptcy, scaring investors. Stock markets plunged and global credit markets froze up, almost overnight. However, the Fed did rescue the American International Group (AIG), one of the world's largest bank insurers, pumping in $85 billion to become an 80 percent owner of the company. AIG had been heavily involved in issuing credit default swaps (CDSs)—contracts that insure banks against borrower defaults and that also allowed investors to bet on the possibility that companies would default on their loans. The Fed's help to AIG—which eventually became a nearly

$150 billion bailout package—was a hedge against the possibility that its failure would cause the entire global financial system to collapse.

Meanwhile, many big banks merged: Bank of America took over Merrill Lynch and Bear Stearns; JPMorgan Chase absorbed Washington Mutual; and Wachovia merged with Wells Fargo. Ironically, this process made too-big-to-fail banks even bigger! Most of them had billions of dollars of toxic assets (mainly home mortgages) on their books. Many were also overleveraged—they had borrowed too much money in relation to their own capital held in reserve and were reluctant to lend to one another or to smaller banks on "Main Street" that financed local businesses and home sales. When manufacturers and service providers could not find capital to borrow, they started laying off workers. As personal incomes dropped, consumers cut spending significantly, drove up their personal debt by using credit cards, and hoarded what cash they had left. Between September 2008 and September 2012, 3.8 million U.S. property owners lost their homes to foreclosures. Mortgage and bank defaults also rose to record levels in England, Ireland, Iceland, Italy, and Eastern Europe where banks were stuck with properties they were forced to auction off at huge losses.

On October 3, 2008, President Bush signed the Emergency Economic Stabilization Act to create the Troubled Assets Relief Program (TARP), which authorized $700 billion of taxpayer money to buy up bad assets in banks in the hopes of keeping credit moving. Soon U.S. officials injected $245 billion of TARP money into U.S. banks, $70 billion more into AIG, and $80 billion into Chrysler, GM, and GMAC (GM's finance corporation). It is important to note that TARP was not a government giveaway: banks eventually repaid loans to the U.S. Treasury, and the government sold the last of its shares and equity stakes in automobile companies by 2015, earning a small $5 billion profit on the program.[19] Similarly, by 2017 the government had earned a large profit from its ownership of stocks in Fannie Mae and Freddie Mac.[20]

In November 2008, leaders of the G20—a group of twenty countries with the world's largest economies—met in Washington, DC. Although they failed to agree on detailed proposals to reform international financial markets, it marked the first time that leaders of emerging countries such as the BRICs, South Korea, and Saudi Arabia were invited to work closely with the United States, Japan, and Europe to address global financial problems. In November, the U.S. Federal Reserve continued to play the role of "lender of last resort" by extending hundreds of billions of dollars in emergency credit to banks, in the hopes that this new money would resolve their liquidity problems and encourage them to make more home, student, auto, and small business loans.

Upon assuming the presidency in January 2009, Barack Obama promised to impose tough sanctions on banks that had "nearly destroyed the economy" and focus on putting people back to work, building new infrastructure, and supporting middle class priorities in education and health care. In February Congress approved the American Recovery and Reinvestment Act, a $787 billion stimulus spending package. By this time financial turmoil had induced a global economic recession with dizzying job losses, record home foreclosures, and a substantial increase in poverty. Public confidence in governments' handling of economic affairs faltered so much that ruling parties and coalition governments were ousted

in 2009 in countries such as Iceland, Latvia, and Japan. (Many even argue that the shockwaves released by the financial meltdown contributed to the rise of anti-establishment nationalism in Britain, France, and the United States in 2016–2017.)

The Obama administration's 2009 stimulus bill and bailouts of banks and automobile companies helped bring the U.S. economy out of recession. The Federal Reserve also pumped money into the U.S. economy through three rounds of quantitative easing (QE) between 2008 and 2014. Through QE the Fed bought large amounts of U.S. Treasury bonds and mortgage-backed securities. Only in 2017, when the Fed had accumulated $4.5 trillion in assets, did it announce plans to taper off the QE program. The Fed also kept interest rates low to encourage investment. Although Republicans worried that inflation would rise significantly, it averaged less than 2 percent annually from 2013 to 2016. By the time Obama left office, the unemployment rate had steadily fallen from 10 percent in late 2009 to 4.8 percent in January 2017. Although a strengthening dollar benefited the wealthy, it increasingly hurt U.S. exporters and caused U.S. manufacturers to face stiffer competition from imports. During the 2016 presidential campaign, trade deficits and rising inequality led Hillary Clinton, Bernie Sanders, and Donald Trump to reject the Trans-Pacific Partnership (TPP) trade agreement.

The Struggle to Reform the Financial System in the United States

The political struggle to stabilize and then reform the U.S. financial system was in full force from 2009 until at least 2011. Heterodox liberals and structuralists argued that policies and beliefs that had emerged in the 1990s and spread in the 2000s needed to be changed. Many blamed officials in the Clinton and George W. Bush administrations and in the Federal Reserve under Alan Greenspan for believing that markets were efficient, self-regulating, and capable of accurately assessing financial risks and setting prices. Nobel Prize–winning economist Paul Krugman said that in retrospect these beliefs were "dangerously simplistic, naïve, and ahistorical."[21] Once officials lifted many regulations, financial institutions proceeded to take on excessive debt and engage in imprudent lending. For example, by repealing the Depression-era Glass–Steagall Act in 1999, the U.S. Congress allowed commercial banks with deposits insured by the FDIC (Federal Deposit Insurance Corporation) to become affiliated with investment banks that made many high-risk investments. Moreover, a deregulated system opened the door for individuals and companies to engage in irrational, unethical, and even illegal behavior with seeming impunity.

In the first year few years of the Obama administration, neo-Keynesian heterodox economists such as Paul Krugman, Robert Reich, Brad DeLong, and Joseph Stiglitz argued that government must correct the fundamental flaws of unregulated capitalism. Their main assertions were the following:

- Austerity measures weaken demand, thereby stalling economic recovery.
- Government deficit spending boosts demand and creates jobs.
- Moderate inflation is not a problem in the short run.

- Increased state investments in education, infrastructure, and renewable energies produce more long-term growth.
- The wealthy and major corporations should be forced to pay higher taxes.

According to political scientist Henry Farrell and economist John Quiggin, the crisis re-opened the door to re-acceptance of these Keynesian ideas amongst a network of expert economists whose policy proposals spread like wildfire to Washington, DC, Brussels, and Berlin.[22] Neo-classical economists who dominated the U.S. economics profession were suddenly on the defensive as a number of their prominent members, including Martin Feldstein and Larry Summers, publicly supported fiscal stimulus. Europeans who suddenly switched to supporting deficit spending and massive central bank intervention in financial markets included IMF Director-General Dominique Strauss-Kahn and popular *Financial Times* columnist Martin Wolf. Even the conservative Central Bank went with stimulus spending.

However, the heterodox liberal ascendancy did not last long: by 2010 the EU was switching to austerity as the dominant response to the burgeoning Eurozone crisis. In the United States, Republicans gained control of the House after the 2010 elections and thwarted many of Obama's policies. At this time and for the rest of the Obama presidency, Republican deficit hawks and many orthodox economic liberals argued that there should be dramatic cuts in government spending to help the economy recover. Politically pragmatic to a fault, President Obama agreed with Republicans in 2010 to support an extension of the Bush tax cuts for two more years in exchange for an extension of unemployment benefits for only a few months.

Heterodox liberals specifically criticized the Obama administration for pandering to economic elites. For example, in her 2012 book *Bull by the Horns*, former FDIC chair Sheila Bair criticized Secretary of the Treasury Geithner for throwing money at banks with almost no strings attached, refusing to support mortgage modifications in loans for struggling homeowners, and watering down financial reforms.[23] The Obama administration refused to impose tighter limits on executive pay and bonuses in exchange for government bailouts. CEOs' compensation continued to grow: in 2011, the "median pay of the nation's 200 top-paid CEOs was $14.5 million."[24] In contrast, struggling homeowners failed to receive significant mortgage relief such as a lowering of principal owed. The administration also refused to prosecute Wall Street insiders. After 2008, banks continued to engage in illegal practices such as robo-signing, whereby they foreclosed on homeowners with falsified or unverified documentation. Not until 2012 did the federal government and state attorneys general negotiate a $25 billion settlement over these fraudulent practices with the five largest banks in the United States.

To critics, measures that Congress adopted to reform the banking and finance sectors were quite timid. Despite Senate Republican opposition, a Consumer Protection Financial Bureau (CPFB) was finally set up to conduct risk assessment of the financial system. In 2010 Congress approved the Dodd-Frank Act, a law that, among other things, required banks to keep more capital and collateral in reserve and to allow the Commodity Futures

Trading Commission to regulate some types of derivatives trading. One of the law's most controversial proposals was the Volcker rule, which prohibited banks from owning hedge funds and engaging in certain risky trading. Despite these changes, in 2012 JPMorgan Chase lost at least $6.2 billion on a complicated hedging strategy that went bust. Its CEO Jamie Dimon had bitterly opposed regulations of the banking system that would limit the use of derivatives, at one point calling them "un-American."

Some critics blamed the banking industry for blocking major financial reforms. Simon Johnson and James Kwak pointed out that a "new American oligarchy" of six megabanks spent tens of millions of dollars opposing strong regulations. Structuralists such as Robert McChesney argued that the United States was stuck with an undemocratic system of influence peddling—a "dollarocracy"—whereby corporate lobbies got favorable treatment from lawmakers that exacerbated political and economic inequality.[25]

The Dollar Goes Wobbly: The Only Game in Town

Before the financial crisis, many officials and experts were worried that high levels of U.S. domestic spending, continued U.S. trade deficits, and the costly wars in Afghanistan and Iraq would cause excessive inflation, more U.S. debt, and a weakening in the value of the dollar. Rather than sharply cutting spending, the United States relied chiefly on external sources of finance (especially from China, Japan, Germany, and Saudi Arabia) to cover its budget deficits, something even the neoliberal Fred Bergsten argued was risky and unsustainable.[26] Many structuralists argued that excessive spending led to "economic overextension" or an "overstretch" which often accompanies imperial policies and gradually weakens an imperial power.[27]

Many European officials felt confident that the euro would eventually become as important as the U.S. dollar in the global political economy, given the size of the EU market and its population. When the euro was officially rolled out in 2002, it was valued at almost one-for-one against the U.S. dollar. By late 2007, the dollar had dropped in value to only €0.7 (see Figure 8.1). The dollar also fell sharply in value against the yen from 2007 to 2011 (see Figure 8.2). In 2007, some OPEC members— especially Venezuela and Iran—pushed for oil to be priced in euros or a basket (weighted average) of currencies. Only Saudi Arabia's intervention on behalf of the United States prevented this.

When unemployment went up during recessions in the early 1980s and after 2007, trade became more of a concern. Since small changes in exchange rates could have large effects on levels of imports and exports, some U.S. officials accused China of purposefully keeping down the value of its currency in order to increase its exports, at the expense of U.S. workers. Between 1994 and 2010, the United States and other nations pressured Beijing to abandon the practice of pegging the yuan (also known as the renminbi) to the U.S. dollar. The Chinese did revalue the yuan several times between 2005 and 2007 (see Figure 8.3), but not enough to make a significant dent in the U.S. trade deficit with China. When the global financial crisis came to a head in 2008, Chinese officials once again pegged the yuan to the dollar to stop a further appreciation of the yuan from hurting China's exports and

economic recovery. To counter what they believed was classic competitive devaluation, the U.S. House and Senate in 2010 and 2011, respectively, passed bills (neither of which became law) imposing a tariff on imported goods from a country with a fundamentally undervalued currency.

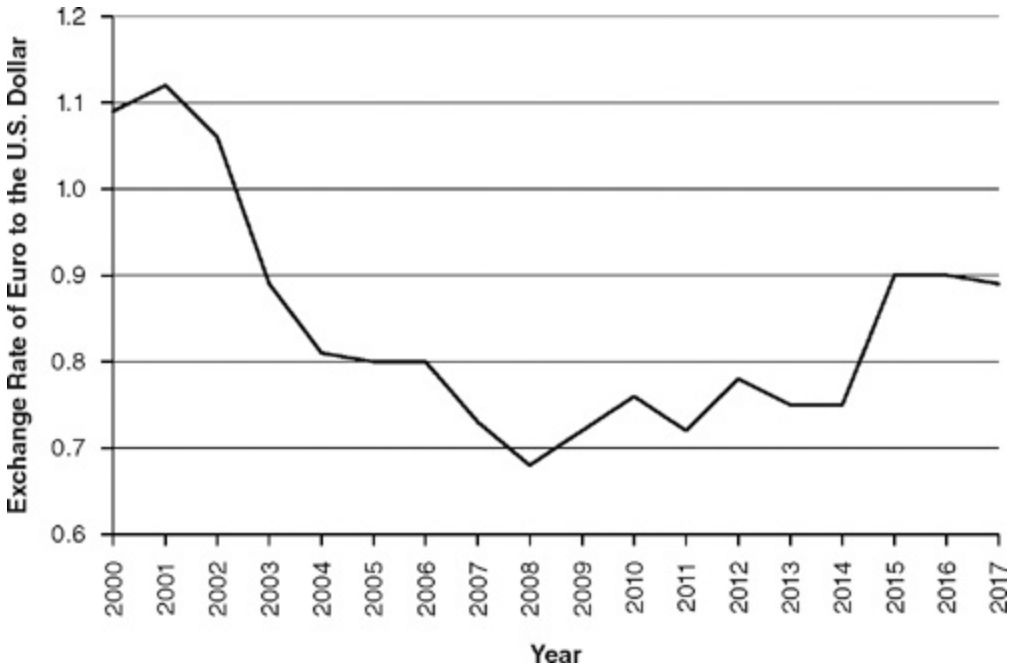


FIGURE 8.1
Annual Average Exchange Rate of the Euro to the U.S. Dollar, 2000–2017

Source: Data from IMF, "International Financial Statistics," at http://data.imf.org/?sk=388DFA60-1D26-4ADE-B505-A05A558D9A42.

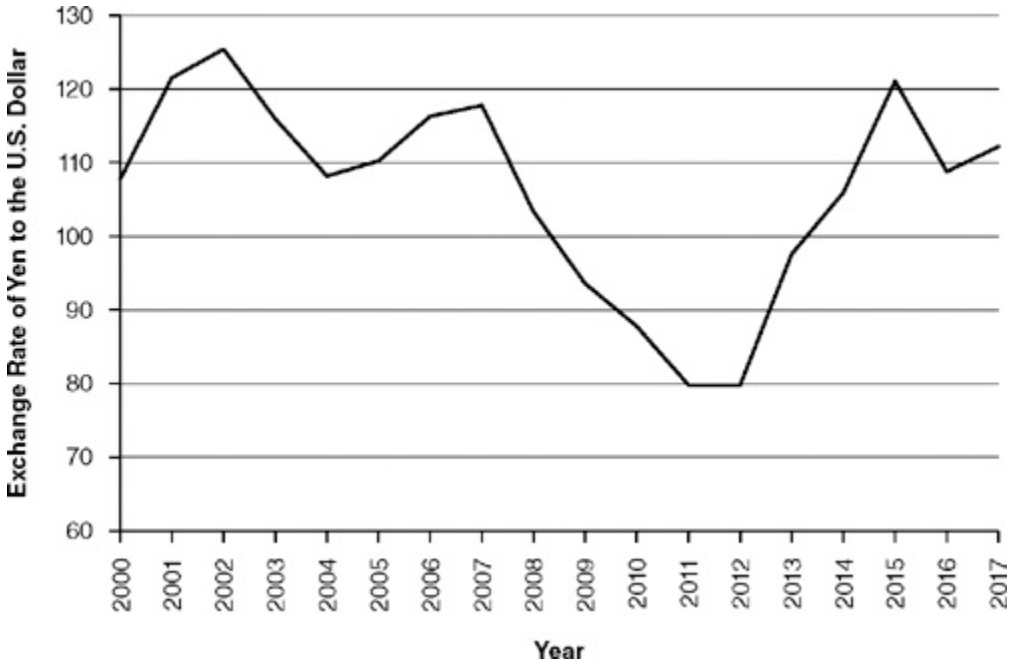


FIGURE 8.2
Annual Average Exchange Rate of the Japanese Yen to the U.S. Dollar, 2000–2017

Source: Data from IMF, "International Financial Statistics," at http://data.imf.org/?sk=388DFA60-1D26-4ADE-B505-A05A558D9A42; and OECD, "National Accounts Statistics," at www.oecd-ilibrary.org/economics/data/aggregate-national-accounts/ppps-and-exchange-rates_data-00004-en.

China abandoned the peg in 2010, but U.S. officials again pressured the IMF and the U.S. Treasury to brand China a "currency manipulator," which would entitle those hurt by China's actions to initiate remedial countermeasures. President Obama brought up the issue with Chinese officials at the 2012 APEC meetings in Vladivostok, Russia. Likewise, candidate Mitt Romney promised to label China a currency manipulator if he were elected president in 2012. And yet many U.S. companies operating in China benefited from the undervalued yuan. It was also hard to distinguish defensive from malicious intentions behind exchange rate manipulation. The Obama administration was reluctant to bring the issue to a head because of potential political and economic retaliation from Beijing.

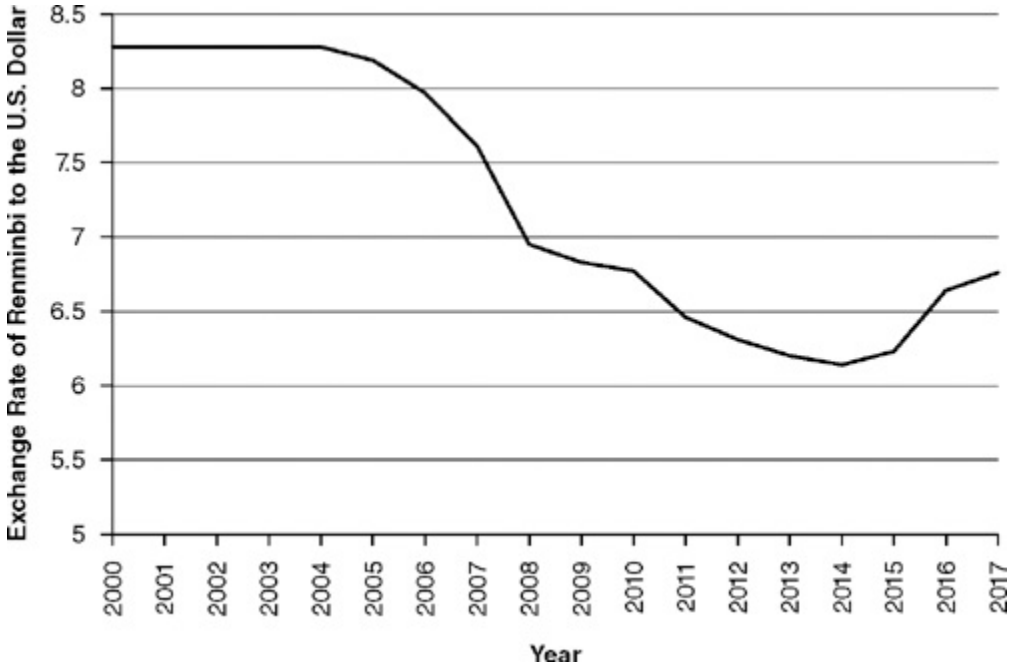


FIGURE 8.3
Annual Average Exchange Rate of the Chinese Renminbi to the U.S. Dollar, 2000–2017

Source: Data from IMF, "International Financial Statistics," at http://data.imf.org/?sk=388DFA60-1D26-4ADE-B505-A05A558D9A42; and OECD, "National Accounts Statistics," at www.oecd-ilibrary.org/economics/data/aggregate-national-accounts/ppps-and-exchange-rates_data-00004-en.

Right after the financial crisis, China, Brazil, France, Japan, Russia, and some Persian Gulf countries grumbled about the possibility of pricing oil in a basket of currencies or gold instead of the U.S dollar. According to political economist Barry Eichengreen, in 2009 the most widely considered replacements for the U.S. dollar as a top reserve currency were:

- The euro or Chinese yuan;
- A supranational currency such as Special Drawing Rights (SDRs); or
- A basket of currencies and/or gold.[28]

For Eichengreen and others, the Eurozone predicament (see Chapter 12) precluded the euro from becoming anything more than a reserve currency in the EMU. By 2012 over half of China's official reserves were stuck in U.S. dollars. The Chinese renminbi was still not fully convertible, which deterred many countries from using it for reserves, trade, and bank payments. To change this, China would have to open its capital markets even more, reform its banking system, and shift away from its export-led growth strategy. Fearful of the political risks that these reforms might unleash, China made only modest efforts to push the yuan beyond its major role in the Asian region.

Contrary to the expectations of many observers, investors did not flee from the dollar during the financial crisis or afterwards as the U.S. economy gradually recovered. Investors continued to view the U.S. economy as a safe haven for their money. The realist Gabor Steingart of Germany's *Der Spiegel* magazine argued that the United States was considered safe because "one can almost completely rule out the possibility of political unrest in the United States."[29] Furthermore, many states and individuals viewed U.S. Treasury Bills (T-Bills) as stable purchases, given that the U.S. government was quite unlikely to default on its debt. Countries also liked to hold U.S. Treasuries as reserves because they kept their value over time, paid interest, and were highly liquid (easily sold for cash). To repeat, one of the privileges of being a global hegemon and holding the world's reserve currency was that the U.S. Treasury could repay international debt simply by printing more national currency.

Steingart also likened the U.S. economy to an "economic giant on steroids," dependent on investment shots from countries with surplus capital. Similar to the "grand bargain" between the United States and its allies during the Cold War, the United States still provided collective security goods for the international community by combating terrorism, assuming much of the costs of intelligence gathering, and providing forces and weapons to attack suspected terrorists. Allies and others help pay for these services and prop up the U.S. dollar in the global economy to the extent that they continue to invest in and purchase U.S. goods and services.

STRUCTURE MANAGEMENT

After President Nixon ended the convertibility of the dollar into gold in 1971, the United States could not so easily impose its rules and norms on the international finance and monetary structure. Some experts assumed that the postwar system of U.S. hegemony would be replaced by a multilateral order of major powers balanced against each other. In 1976 the United States, the United Kingdom, Germany, France, Japan, Italy, and Canada created the Group of 7 (G7) as a forum for their finance ministers, central bank presidents, and political leaders to discuss and coordinate monetary, energy, and economic policies. It was renamed the G8 in 1997 when Russia joined this group of democracies and leading economies, but Russia was kicked out after invading Crimea in 2014.

The global financial crisis of 2007–2008 spurred the creation of another forum called the G20 to account for the growing economic importance of countries such as Brazil, China, India, and South Africa. The G20 replaced the G8 as the forum in which leaders of the world's largest economies negotiated and coordinated policies toward finance, money, and debt in order to prevent future crises. Some expect the G20 to play a greater role in regulating cross-border capital transfers and exchange rates, all the while trying to coordinate macroeconomic policies in ways that reconcile domestic support for national economies with the goal of an open multilateral system.

There are many other lesser-known international organizations that cooperate on international financial and banking issues.[30] The Bank for International Settlements (BIS) is an invitation-only group comprised of sixty central banks that promotes cooperation on global monetary and financial affairs and seeks to ensure financial stability. The Basel Committee on Banking Supervision, made up of forty-five members from some twenty-eight states, sets standards for proper supervision and regulation of banks, including how much capital banks should hold. The International Organization of Securities Commissions (IOSCO) promotes standards for the regulation of securities and futures markets.

Since the 1970s the IMF's main roles have been to loan money to countries with balance-of-payments problems and to monitor the financial and economic policies of individual states. In this sense, the IMF is like a central crisis manager for developing nations that must usually meet IMF conditions in order to receive emergency assistance or debt rescheduling from other global lenders. As we noted in the discussion of the Asian financial crisis, many of these nations have accumulated large foreign exchange reserves to use in the case of external shocks so that do not have to turn to the IMF.

The BRICS countries have insisted on playing a bigger role in negotiations on monetary and finance structure rules. Given their growing influence in the global economy and their unwillingness to support strict economic liberal policies of the IMF, they have made management of the finance and monetary structure more difficult.[31] Over time, a more multipolar and multilateral system might produce a new order that satisfies their interests.

A Declining United States and a Rising China?

Soon after Donald Trump won the U.S. presidential election in 2016, he bragged about how well the economy was doing as reflected in rising stock market prices and increased consumer confidence. He promised that his administration would achieve 4 percent growth in GDP and create 25 million new jobs in ten years by cutting taxes and funding "massive" infrastructure projects to the tune of $500 billion.

By November 2017, many economists continued to worry about the effects of Trump's policies on global financial stability and U.S. leadership of the global political economy. While many businesspeople and investors supported a tax cut bill working its way through Congress in late 2017, many fiscal experts questioned how large tax cuts for the wealthy could be supported without raising taxes on the middle class, cutting government spending significantly, and raising the national debt. Trump's promised increases in military and infrastructure spending also seemed likely to raise the debt. More broadly, it appeared that Trump did not appreciate the benefits that accrued to the United States from being the hegemonic manager after World War II. Critics worried that Trump's policies could undermine the stability of the global finance and monetary structure, just as they were doing to the trade and security structures. They made the United States look weak, untrustworthy, and unwilling to play a major role in managing global finance.[32]

The global finance and monetary structure is inherently susceptible to shocks that could quickly cause a great recession or even a great depression. As the Asian and global financial crises showed, contagion from one country to another occurs rapidly. U.S. leadership (or lack thereof) will strongly shape how future shocks will affect other countries. Just some of the potential triggers of a financial shock are:

- Weak regulation of the major banks;
- A continued rise in the U.S. debt-to-GDP ratio (it has risen steadily from 54 percent in 2001 to 103 percent in 2017);
- A substantial weakening of the dollar due to U.S. tax cuts and increases in government spending;
- Special counsel Mueller's indictment of President Trump and/or Trump's impeachment; and
- A new war in East Asia (North Korea) or the Middle East.

Jonathan Kirshner argues that the global financial crisis delegitimized the model of financial liberalization and unfettered flows of capital that the United States promoted in the world after the end of the Cold War. He sees a "new heterogeneity of thinking" outside the United States about how best to manage global financial affairs.[33] Many countries—China most notably-want to reduce reliance on the U.S. dollar and the U.S. economy, increase policy autonomy, and maintain (or reintroduce) capital controls so that money cannot always move freely into and out of countries.[34] Kirshner asserts that greater heterogeneity of thought, in the context of a relative decline in U.S. political power and divergence in security interests of major powers, will increase conflicts "over global macroeconomic

governance and contestation over burdens of adjustment."[35] And as the dollar declines in importance, the United States will have less global political influence and will find it more difficult to sustain large budget and trade deficits.

Kevin Gallagher finds evidence of the new heterogeneity of thinking in the form of new capital controls that emerging and developing countries put in place from 2009 to 2012. These controls included limits on the amount of money that could move in or out of a country, taxes on certain investments, and regulations on foreign exchange derivatives markets. South Korea, the BRICS, and other emerging countries then successfully pressured the IMF, the WTO, and the G20 to accept the legitimacy of capital controls under certain conditions.

Finally, President Xi of China has promoted internationalization of the renminbi, including by convincing the IMF in 2016 to add the renminbi alongside the dollar, pound, euro, and yen to its special drawing rights (SDR) basket. The continued increase in the use of the renminbi reinforces China's rise as a major economy with more important global responsibilities. It also reflects Xi's desire to rejuvenate the nation and see China become a "mighty force" "moving closer to center stage and making great contributions to mankind."[36]

Undiminished U.S. Structural Power?

Many IPE scholars argue that the United States is likely to play a dominant role in managing the finance and monetary structure for many years to come. The global importance of the U.S. dollar is one important reason why. Carla Norrlof points out that the United States has currency influence and monetary capabilities far greater than any other country.[37] There is simply no currency that has the potential to rival the dollar anytime soon. As Figure 8.4 shows, the U.S. dollar constitutes 64 percent of the world's official foreign reserves and is the currency used in 40 percent of all international trade payments. More than 85 percent of foreign exchange transactions involve the dollar and another currency. And nearly half of all global debt securities are denominated in dollars. The euro is clearly the second most important global currency, but falls far behind the dollar except as a means of payment in international trade. The Eurozone crisis of the early 2010s dashed its hopes of rivaling the dollar soon. In comparative terms, the Chinese renminbi has very little use in global finance, except as a means of trade payments in Asia.

Eric Helleiner also points out that the global financial crisis did not significantly transform global economic governance.[38] One reason for a lack of change, says Helleiner, is that no other country has the level of military power, importance in trade, or deep financial markets as the United States. Second, because U.S. financial markets are so big, the United States (with support from the United Kingdom) was able to ensure that reforms to international financial standards reflected U.S. interests. After the crisis, it supported some modest "macroprudential" regulations at the domestic level and in the Basel Committee to enhance financial stability, but only to the extent that they did not constrain U.S. financial policy autonomy or hurt profits of U.S. financial institutions.

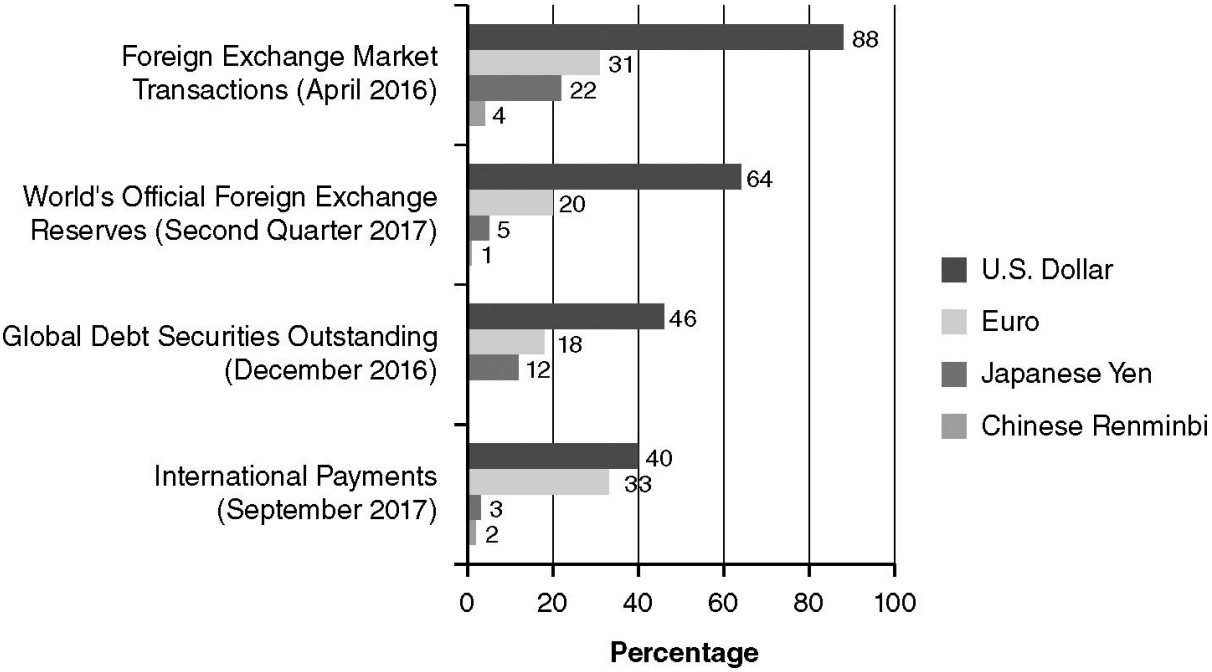


FIGURE 8.4
Share of Use of Different Currencies in Global Forex Transactions, Reserves, Debt Securities, and International Payments

Source: IMF, "Currency Composition of Official Foreign Exchange Reserves (COFER); Bank for International Settlements, BIS Quarterly Review (September 2017); Bank for International Settlements, "Triennial Central Bank Survey: Foreign Exchange Turnover in April 2016" (September 2016), p. 5; and SWIFT, "RMB Tracker" (October 2017), p. 5.

As was made clear during the global financial crisis, the United States is the only country capable of acting as a "lender of last resort" in times of financial instability. According to Daniel McDowell, the U.S. Federal Reserve stabilized the global system by providing massive amounts of liquidity to central banks in 2008 and 2009.[39] Through a mechanism called currency swaps, it extended emergency credit worth up to $600 billion to fourteen foreign central banks that desperately needed dollars to keep their domestic banks and businesses solvent. During the height of the Eurozone crisis in 2011 and 2012, the European Central Bank again borrowed $100 billion from the Fed through currency swaps. The ability of the Fed to essentially "print" dollars on demand reflected and reinforced U.S. structural power.

Like Norrlof and Helleiner, Benjamin Cohen and Barry Eichengreen believe that the dollar is very likely to remain the world's indispensable currency. Cohen argues that "the United States is alone among nations in offering the complete package of power resources associated with top currency status."[40] He sees the euro and the yuan as "seriously handicapped": among other things, the structure to manage the euro is flawed, and China lacks the "instruments of statecraft" and the financial openness necessary to manage the yuan's internationalization.[41] Eichengreen emphasizes that China is reluctant to make serious financial and political reforms—includ-ing reducing capital controls and opening its

financial markets fully to foreign investors—that would accelerate the yuan's internationalization.[42] In light of this, Eichengreen predicts that "it will take a generation before the renminbi begins to play the kind of global role that the dollar does."[43]

CONCLUSION

In the United States and Western Europe, post-World War II monetary and finance policies were heavily influenced by fresh memories of the Great Depression. The Bretton Woods system (1947–1971) stabilized monetary relations and generated confidence in U.S. leadership by fixing the value of the dollar to gold and limiting exchange-rate fluctuations. Reflecting acceptance of the Keynesian compromise, the IMF, the World Bank, and the GATT allowed Western European countries and Japan to retain protectionist institutions and policies as they gradually reduced capital controls and lowered tariff rates. However, pressures in the system mounted by the late 1960s, in large part due to U.S. overspending and overvaluation of the dollar.

In 1973 the Bretton Woods fixed exchange rate system gave way to a flexible exchange rate system with less U.S. influence over exchange rates and capital transfers. The 1970s were marked by increasing interdependence, high inflation, and two international recessions related to high oil prices. In the 1980s, the spread of neoliberal ideas and the onset of the globalization campaign spurred deregulation of finance, currency exchanges, and trade. Financial crises erupted in Mexico, Brazil and a number of other developing countries that had borrowed heavily from international commercial banks and could not afford repayments.

After the Cold War ended in 1990, continued liberalization enabled large increases in flows of investments around the world, including foreign direct investment and purchases of stocks and government bonds in emerging markets. "Hot money" and international speculation helped trigger major financial crises in Mexico, Southeast Asia, and Russia. The IMF and Western governments provided financial assistance to debtor states on condition that they continue to repay creditors and impose austerity on their societies. As China was becoming a major manufacturer and exporter, the United States relied on countries such as China, Japan, Germany, and Saudi Arabia to offset its growing debt and high levels of domestic consumption with purchases of U.S. property and Treasuries.

The heyday of globalization from the late 1990s to 2007 saw high growth rates in much of the world, but in the United States and Europe growing consumption rested on a foundation of higher government and consumer debt. Extraordinary profits by financial institutions derived more from risky financial transactions and trade in complex derivatives than from productive investments in the real economy. The global financial crisis started in the United States in 2007 after a real estate bubble burst, nearly collapsing the global financial structure and raising serious challenges to the United States' privileged position as a global financial hegemon.

Today's global political economy is much more integrated than it was twenty-five years ago. The continuing redistribution of wealth and political power has made it more difficult to manage the finance and monetary structure. Many states would like a truly multilateral institution to regulate finance and exchange rates, and produce rules for handling debt that reflect the interests of debtors as much as creditors. In contrast, some countries prefer to let

a hegemonic power with a strong economy and currency maintain a stable international order.

Recently, China's growing power and large trade surpluses with the United States have generated hostile protectionist reactions by many U.S. political leaders. More than ever, currency fluctuations and capital mobility affect domestic employment and investment. While there is evidence that the financial crisis has weakened confidence in the U.S. dollar, it seems highly unlikely that the euro, much less the Chinese renminbi, will rival or replace the dollar anytime soon. Even so, the United States needs other countries to help finance its deficits, which, para-stands stands to further undermine U.S. authority and financial leadership.

Many states and international financial institutions remain worried that another great recession could be ignited by a debt crisis in Europe, a deflated stock market bubble, a rapid slowdown in Chinese growth, or a political event such as a war in Asia or the Middle East. Many officials and experts are concerned that U.S. president Trump's isolationist and nationalist policies could cause the postwar order to break down. Without more statesmanship and multi-lateralism on Trump's part, markets may lose trust in the United States, causing greater instability in the global financial system.

KEY TERMS

currency exchange rates 195
appreciate 195
depreciate 195
speculation 197
hot money 197
gold standard 197
fixed exchange rate system 197
flexible exchange rate system 197
balance of payments 198
Keynesian compromise 200
capital controls 200
reserve currency 201
subprime mortgage loans 206
toxic securities 206
quantitative easing 208

DISCUSSION QUESTIONS

1. Outline the political, economic, and institutional features of the gold standard, the fixed exchange rate system, and the flexible exchange rate system. What are some of the political and economic advantages and disadvantages of each system?
2. What are the institutional features of the IMF, and what role does it play in helping countries with balance of payments problems?
3. If the U.S. dollar depreciated dramatically relative to the Chinese renminbi, what effect would this likely have on consumers and businesses in each country? When is a falling dollar good or bad for the United States; and for China?
4. How have globalization and economic liberal ideas shaped developments in the finance and monetary structure? Cite specific examples from the chapter and in news articles.
5. What specific political and economic factors have contributed to the United States' huge current account deficit? Is it rational for countries to invest large amounts of money in U.S. Treasuries (i.e. loan to the U.S. gov-ernment)?
6. How would the global financial structure likely be affected by a growing perception that the U.S. political economy is becoming unstable?

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6. Two examples of these unions were the Latin Monetary Union, which in 1865 included France, Switzerland, Belgium, and Italy; and the Scandinavian Union, which in 1873 included Sweden, Denmark, and later Norway.
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10. See Karl Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time* (Boston, MA: Beacon Press, 1944).
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CHAPTER 9
The Global Security Structure



Meeting of the Global Coalition to Defeat Isis in Kuwait.

Source: AP Photo/dpa/Gustavo Ferrari.

Realism is a sensibility, not a specific guide of what to do in each crisis. … And it is a sensibility rooted in a mature sense of the tragic—of all things that can go wrong in foreign policy… Trump has given no indication that he has thought about any of this.

Robert Kaplan[1]

At the beginning of Chapter 1 we suggested that the post-World War II international order created by the United States and its allies might be ending. We discussed a number of issues, including the 2016 election of Donald Trump as president of the United States, that were causing the world order to appear more "unhinged" and creating widespread anxiety. After seven months in office, Trump had indeed shaken up the global security structure (GSS). He entered a standoff with North Korea's president Kim Jong-un, promising to meet North Korean threats with "fire and fury like the world has never seen." His "secret plan" to knock out ISIS in the Middle East consisted of indiscriminate bombing. Upset with his generals for not "winning" the war in Afghanistan, Trump nevertheless agreed with them to dispatch more U.S. troops there, just as Obama did.

The primary objective of this chapter is to explain why, parallel to the unraveling of the postwar world order, the current GSS has been coming to an end. Traditional security issues such as conventional war and nuclear weapons have increasingly been supplanted by other priorities such as terrorism and cyber weapons, although the nuclear threat has re-emerged with the standoff between Trump and Kim Jong-un. It is important to note that throughout the book we address other non-military global security issues that affect the GSS, including poverty, hunger, health, migration, and the environment.

In this chapter we discuss two varieties of realism_ classical and neorealist, putting them into perspective with other theoretical orientations such as structuralism. We provide historical overviews of three global security structures that correspond to the three phases of the postwar order discussed in Chapter 1. We also shed light on how and why each of these configurations of military power and economic wealth has shifted over time to produce a new arrangement (structure) that still reflects some elements of the structure before it.

In the last part of the chapter we contrast how Presidents Obama and Trump have recently dealt with some "hotspots" in the world. We end with an overview of seven systemic security issues intertwining Russia, the United States, and China.

The major arguments that we make in this chapter about the current global security structure are the following:

- Realism continues to have significant explanatory power in the case of security issues.
- The first two phases of the postwar GSS witnessed a transformation away from a bipolar structure in the 1950s, 1960s and early 1970s to a multipolar security structure that lasted from 1973 until the end of the Cold War in 1991.
- The third phase of the postwar GSS has exhibited quasi-unipolar and quasi-multipolar traits. Since the 9/11 attacks in New York and Washington, DC, the structure has been developing a more indefinite and unstable configuration of wealth and power.
- This changing configuration both reflects and has helped engender the rise of national populism, the alt-right, and authoritarianism in Russia, Europe, the United States, and some developing countries.
- The third phase of the GSS has seen the development of more sophisticated cyber weapons whose use increases the risk of a real war.
- The Trump administration has severely weakened U.S. power and authority, destabilized the GSS, and provided an opportunity for China to emerge as a global hegemon.
- While another Cold War between the United States and Russia and a new one between the United States and China seem likely, there is also a chance of a conventional and even nuclear war involving some configuration of these three superpowers and their allies.

CLASSICAL REALISTS AND NEOREALISTS

For centuries, leaders and academics have viewed national and international security issues through the dominant paradigm of realism.[2] In general, realists believe that a state's military capabilities and economic strength determine the likelihood of its survival against external threats. Classical realism is rooted in the ideas of Thucydides, Machiavelli, and Hobbes; more recent realists are George Kennan, Hans Morgenthau, and Henry Kissinger. They articulate the sources of conflict between states and how individuals and political institutions acquire power in order to assure the survival of the nation-state (or other dominant political institution) and its people.

Classical realists assume that:

- State survival depends on the ability to defend the institutions, territory, people, and skies above sovereign states.
- Power springs primarily from military capabilities and can be used to pressure other states to do things they would not do otherwise.
- The drive for national security always takes precedence over ideological principles and motives.
- The global security structure *conditions*, but *does not always determine*, the choices and behavior of security organizations and national leaders.
- State leaders often choose to go to war to readjust or maintain the balance of power between states or to establish a new configuration of power amongst the stronger members of the state system. The number of states in a global security configuration is not as important for its management as the relationship of states to one another.
- Dominant imperial powers tend to become the enemy of all others.

Neorealists criticize classical realists for oversimplifying the motives of states and decision makers—for portraying them as continually struggling for power, for the sake of power.[3] They generally assume that:

- Each state in the international system today is a unitary and rational actor.
- Because the global security structure lacks a single sovereign to regulate it, states can use force whenever they want to.
- This makes it impossible to guarantee the *absolute security* of any state, which in turn *compels* states to make security their primary objective.
- States form alliances to protect themselves, generating a systemic configuration of military power.
- The systemic structure constrains decision makers' options and choices.
- A change in the global security structure occurs when there is a *shift* in the military and economic power capabilities of the states in that configuration of power.

It is important to note that neorealists differ from classical realists in two major ways. Neorealists minimize the role of individual actors in the global security structure, focusing more on how the structure itself shapes outcomes. In contrast, classical realists tend to focus on things *inside* a state that influence its behavior, such as ideology, public opinion, and human calculations.

Second, neorealism does not usually study the security structure's origins or how it changes. Quite often a war changes the security structure. Actors are *assumed to perceive and interpret* the significance of other states' actions or capabilities in predictable ways. As we discuss in the history review below, many classical realists believe that states and decision makers can *purposely change* the relationship of major powers in today's security order. This demonstrates that the structure itself does *not* condition actor behavior as much as neorealists assume it does.

In Box 9.1 we provide a chronology of security developments after World War II as context for discussions in the next sections.

THE POSTWAR CHRONOLOGY

Phase I: The Cold War and Bipolarity (1944–1973)

1944	The Bretton Woods Conference held in New Hampshire creates the International Monetary Fund, the World Bank, and the ITO (replaced by General Agreement on Tariffs and Trade in 1947).
1945	At the Yalta meeting in the Crimea, Eastern Europe and Germany are carved up into "spheres of influence."
	The United Nations Charter is signed in San Francisco. The United States drops atomic bombs on Hiroshima and Nagasaki.
1947	The Cold War begins. The Marshall Plan sends financial and material aid to Europe.
1948	Communist forces take control of China.
1949	NATO is created.
1950	The Korean War starts, ending in a stalemate in 1953.
1955	The Warsaw Pact is created.
1956	The Soviets crush the Hungarian uprising.
1962	The Cuban Missile Crisis. The strategic doctrine of mutually assured destruction (MAD) becomes entrenched.
1964	The United States sends ground troops into South Vietnam.
1968	The Tet Offensive in Vietnam signals the United States' impending loss of the war. The Soviets suppress dissidents in Czechoslovakia.

Phase II: Multipolarity, Détente, and Neoliberalism (1974–1991)

1972	The United States and U.S.S.R. sign the SALT I and ABM treaties. Détente (peace- ful coexistence) between the United States and the Soviet Union begins.
1973	The end of the Vietnam War and the beginning of the OPEC oil crisis. Energy becomes a major security issue.
1975	Henry Kissinger tries to implement a cooperative multipolar system between the United States, the U.S.S.R., Japan, Europe, and the PRC to manage international security.
1978	China begins economic reforms. The second OPEC oil crisis begins.
1979	The Soviet Union invades Afghanistan and ends détente with the United States. The Shah of Iran is overthrown and Ayatollah Ruhollah Khomeini comes to power.
1983	The United States invades Grenada to overthrow a pro-socialist government.
1987	The United States and the USSR sign the Intermediate-Range Nuclear Forces (INF) Treaty. The United States, the USSR, and their allies agree to reduce the number of offensive weapons deployed in Europe.
1989	The United States invades Panama. The Berlin Wall is penetrated.
1990	Iraq invades Kuwait. The U.S.S.R. disintegrates. War breaks out in the Balkans.
1991	The Cold War officially ends. The United States leads a UN-sanctioned military force to eject Iraqi troops from Kuwait.
1993	The United States leads multilateral forces' intervention in Somalia on a humanitar- ian

	mission, which turns into a military mission. President Clinton withdraws U.S. forces in 1993.
1994	The UN fails to stop a genocide in Rwanda.

Phase III: Quasi-Unipolarity, Globalization, and Increasing Nationalism (1992–2017)

1997–1998	The Asian financial crisis starts in Thailand and spreads to many East and Southeast Asian nations.
1999	NATO forces intervene in Kosovo.
2001	The 9/11 attacks in New York and Washington, DC. President Bush declares a global war on terrorism and the United States invades Afghanistan.
2003	The United States and coalition partners invade Iraq.
2007	The global financial crisis starts in the United States and spreads to the rest of the world.
2010	The Arab Spring starts in Tunisia and spreads to Egypt, Libya, Syria, Bahrain, and Yemen.
2011	Libya's Colonel Qaddafi is driven from office. The Syrian uprising turns into a civil war.
2013	The economic crisis in Greece intensifies.
2014	The Islamic State of Iraq and Syria (ISIS) takes territory in northern Iraq and parts of Syria and declares a caliphate. Russia annexes Crimea and moves artillery and personnel into eastern Ukraine.
2014–2016	A record number of refugees and migrants leave the Middle East and Africa for Europe.
2016	After a referendum, Great Britain begins negotiations to leave the EU (Brexit).
2017	U.S. president Trump withdraws from the Paris climate accord. U.S. president Trump and North Korean president Kim Jong-un engage in nuclear brinksmanship.

THE THREE PHASES OF THE POSTWAR SECURITY STRUCTURE

Phase I: Cold War Bipolarity, 1945–1973

In the first phase of the postwar GSS there was a bipolar distribution of power and wealth between the United States and the Soviet Union. Many classical realist historians and political scientists place the origins of the Cold War in the postwar division of Europe. At the Yalta Conference in 1945, Roosevelt, Churchill, and Stalin discussed "spheres of influence" in the postwar world. The Soviet army occupied Eastern Europe and the United States and Britain dominated Western Europe. The United States also occupied Japan.

Neorealists tell a simpler story: the Cold War resulted from the collapse of the old order. The erosion of the British and French colonial empires and the collapse of the German and Japanese regional empires created power vacuums that the United States and the Soviet Union filled, first in Europe and then throughout the world. The natural result was competition between two hegemons with sharply contrasting ideologies (democracy vs. communism) and economic systems (capitalism vs. state socialism).

Did the Cold War have to occur? According to most neorealists, the Cold War was inevitable; the two superpowers mirrored each other's actions in ways that entrenched bipolarity. In 1949 the United States formed a military alliance with Western Europe and Canada—the North Atlantic Treaty Organization (NATO). In 1952 the Soviet Union organized the Warsaw Pact alliance with Central and Eastern European socialist states. In the tight bipolar security structure that followed in the 1950s and 1960s, each superpower also tried to create political "spheres of influence" among newly independent developing nations (the Third World).

Alternatively, realists argue that the Cold War was not inevitable because actors had choices. For example, Daniel Yergin argues in his book *Shattered Peace* that the two hegemons missed an opportunity to prevent the Cold War.[4] The U.S. State Department did not trust the Soviet Union and discounted the effectiveness of diplomatic initiatives to change Soviet behavior. In addition, classical realist George Kennan argues that U.S. policy makers could have treated the status of Berlin and Eastern Europe as an essentially political problem instead of deciding to build up conventional and nuclear weapons.

Through the Eisenhower, Kennedy, and Johnson Administrations (1953 until 1969), the emphasis in American foreign policy was to stay ahead of the Soviets. Given the limited military and political utility of nuclear weapons, the United States *accepted* Soviet hegemony over Eastern Europe and *intentionally shifted* its focus to deterring an invasion of Western Europe by threatening the Soviets with massive retaliation via nuclear weapons if there were such an attack.

The Korean War that started in 1950 led U.S. and Soviet officials to accept two informal rules. The first was not to directly engage the forces of the other superpower because it

could easily lead to total war. Instead, proxy wars were carried out through surrogate states. The second rule was that conflict with your opponent's surrogate should not escalate into nuclear war. President Truman worried that a nuclear U.S. response to North Korea's attack would cause the Soviet Union to respond with atomic weapons. Thus, he organized a United Nations peacekeeping effort to defend South Korea. These "rules" were later applied to U.S. intervention in Vietnam during the 1960s and to the Soviet Union's intervention in Afghanistan in the 1980s.

In the Vietnam War, President Johnson began to escalate military involvement in 1965, with troop levels exceeding 500,000 by 1968. Despite the effort to drive Communist forces out of South Vietnam and support the government there, the United States eventually withdrew and the Southern government collapsed in 1975. Though they supplied arms, aid, and training to the Viet Cong, neither the Soviet Union nor China ever directly intervened to oppose U.S. forces.

In Afghanistan, the Soviet Union deployed its first troops in 1979, marking the beginning of a nine-year intervention in support of the Soviet-allied government against a growing Islamic fundamentalist movement. If Vietnam was America's quagmire, then Afghanistan was the Soviet Union's quagmire. The Reagan administration provided arms and assistance to the Mujahideen to help them resist the Soviet Union. Soviet forces withdrew in 1989, having lost the conflict. An unintended effect of U.S. support for the Afghan Mujahideen was the spread of jihadism in the Muslim world. In any case, the bipolar rule that superpowers do not directly confront each other was observed throughout the Cold War era—with one near miss.

JFK, the Cuban Missile Crisis, and the Entrenchment of Bipolarity

The most intense crisis between the Superpowers during the Cold War came in 1962. President John F. Kennedy took office in 1961, promising to take a tougher stance against international communism than Eisenhower and close the *supposed* gap between the number of U.S. and Soviet nuclear missiles. Kennedy green-lighted a botched, CIA-sponsored invasion of Cuba by anti-Castro patriots at the Bay of Pigs that humiliated the United States. With that embarrassment fresh in his mind, he was eager to restore the United States' reputation for resolve.

The opportunity soon came when the Soviet Union tried to alter the bipolar balance of power by placing medium-range nuclear missiles in Cuba, just 90 miles from Florida. For the United States, this was a provocation too great to overlook. The Kennedy administration threatened to use force if the Soviets did not remove their missiles.[5] Both sides expected that any use of force would inevitably escalate into a full thermonuclear war, which neither wanted.

Neorealists might have predicted that in response to provocative Soviet behavior, the United States would be compelled to attack Cuba, which indeed was the choice of an advisory committee of U.S. military officials. Ultimately, President Kennedy chose not to employ military force. Why? Classical realists would argue that the president was aware that

the use of force could have easily led to nuclear war with incalculable costs. Instead, Kennedy chose to "think outside the box." Aside from threats to destroy Soviet missiles in Cuba, he also pursued "back channel" diplomacy to convince the Soviets to stand down. Initially, he ordered a naval blockade of Soviet ships moving more missiles into Cuba, leaving the Soviets with the choice of starting a war by running the blockade. In a move designed to allow Khrushchev to save face within the governing circle of the Soviet Union, Kennedy secretly agreed to remove U.S. missiles from Turkey in exchange for the Soviets withdrawing their missiles from Cuba. Khrushchev withdrew his missiles.

The way Kennedy and Khrushchev handled the situation became the model for dealing with similar situations in the future. The Cuban Missile Crisis demonstrated that structural conditions alone could *not* ensure international security and did *not* completely dictate outcomes. Leaders' choices made a dramatic difference in the resolution of the crisis. Afterwards, mutually assured destruction (MAD) became one of the foundations of U.S. and Soviet national security policies. No rational leader would start a war if the obvious costs of engagement vastly outweighed the potential gains. Interestingly, for MAD to prevent an initiation of war, each side *must allow the other to maintain* the capability to knock out major weapons and cities. The Cuban Missile Crisis and the tenets of MAD took on renewed significance in the era of Trump and Kim Jong-un.

Phase II: The Weakening of Bipolarity, 1973–1991

By 1973, President Nixon's National Security Adviser Henry Kissinger believed that the international security order was shifting away from bipolarity to multipolarity due to the redistribution of political and economic power. Western Europe and Japan had fully recovered from World War II. China was viewed as an influential player in Asian security relations that could help end the Vietnam conflict and influence North Korea. Kissinger convinced Nixon to open up economic opportunities with China and use Beijing as a counterweight to Moscow.

Multipolarity did not just appear in one day. It required a proactive and contemplative hegemon (the United States) to lead the other four members to manage political, economic, and security issues cooperatively. With the end of U.S. involvement in the Vietnam War in 1973, Kissinger helped advance multipolarity via shuttle diplomacy, which kept him busily moving between national capitals to make sure leaders were on the same page.

A crucial part of multipolarity was arms control negotiations between the two superpowers to maintain rough parity in nuclear weapons. The superpowers started talks on the first Strategic Arms Limitations Treaty (SALT I). At Kissinger's urging, Nixon accepted détente (peaceful coex-istence) with the Soviet Union, which resulted in grain sales and cultural exchanges. The two sides also informally agreed not to interfere in the other's sphere of influence in developing nations. As China, India, Pakistan, and Israel began to acquire nuclear weapons, they also cooperated to prevent the proliferation of nuclear weapons to more states.

A major thorn in the side of Kissinger's plan was the oil crisis of 1973, triggered by the

Organization of Petroleum Exporting Countries (OPEC), which destabilized both the international security and economic structures. Suddenly, the oil producers had a "weapon" against industrialized countries dependent on oil imports. OPEC raised the price of oil dramatically, causing a global recession. Resource dependency raised awareness of international economic interdependence, which in turn paved the way for many developing nations to play a bigger role in the international political economy. In sum, OPEC tightened the connections between international politics and economies during the 1970s and further loosened bipolarity by weakening U.S. hegemony.

The structural shift toward multipolarity continued through the presidencies of Jimmy Carter, Ronald Reagan, and George H.W. Bush. Carter made promotion of human rights a touchstone of his foreign policy, which some saw as a rejection of realist values. However, challenges from the second oil crisis of 1979, the Iranian Revolution, and the Russian invasion of Afghanistan each forced Carter to set aside his human rights emphasis. He responded to the second oil crisis in 1979 by decreasing U.S. dependence on Middle Eastern oil, including by imposing energy efficiency measures on the nation. When the Soviet Union broke one of the major rules of détente by invading Afghanistan in 1979, Carter threatened to not forward the SALT II agreement to the U.S. Senate for approval if the Soviets did not withdraw. They did not and détente was derailed. Carter again looked weak when Islamic revolutionaries drove the Shah of Iran from power in 1979 and took 58 U.S. embassy officials hostage for 444 days.

Ronald Reagan was something of a throwback figure who had forged his political reputation as an anticommunist. His nationalistic appeal—to "make America proud once again"— sounds familiar today. He intended to reclaim U.S. military, economic, and political supremacy over the U.S.S.R. Labeling the Soviet Union the "evil empire," his administration intentionally sought to reimpose a bipolar framework on the international security structure. Reagan himself was strongly influenced by hardcore anticommunists and neoconservative advisors who saw the United States as the world's policeman. By 1984, all arms control talks with the Soviet Union had ceased. Kissinger's carefully conceived multipolarity faded and bipolar politics regained primacy.

In his second term, Reagan did an about-face and developed a personal friendship with Soviet Premier Mikhail Gorbachev that resulted in a series of new arms control agreements. Personally, Reagan found the idea of MAD morally repugnant, even if the purpose was to deter an enemy from attacking first. He tried to replace MAD with a Star Wars program—a space-based defensive system to knock out long-range strategic weapons before they could reach orbit. Because the plan intimidated the Soviets, he even offered them a Star Wars system of their own. In his second term, Reagan also returned to détente, emphasized neoliberalism through the IMF, the WTO, and the World Bank, and laid a foundation for the revival of multipolar diplomacy.

However, he simultaneously called for the support of anticommunist forces in the Third World. Implementation of this "Reagan Doctrine" led to: a U.S. invasion of Grenada to oust a Marxist regime; support for pro-Western authoritarian regimes in El Salvador and Guatemala; backing for right-wing rebels fighting against the Marxist Nicaraguan

government; and weapons shipments to anticommunist forces in Afghanistan and Angola.

George H. W. Bush, who had served as Ambassador to China and the UN, embraced multipolarity in full. He worked through the UN to establish a multinational force to drive Iraq out of Kuwait in 1991. He sent U.S. troops into Somalia as part of a UN peacekeeping mission to deal with starvation. With the collapse of the Soviet Union in 1991, the Cold War evaporated and Bush's "New World Order" emerged.

Phase III: The End of The Cold War and Gss Instability: A Unipolar or Multipolar World?

Not long after the collapse of the Soviet Union, the neorealist John Mearsheimer predicted that we would "soon miss the Cold War" because that bipolar system provided a manageable order during a reasonably stable and relatively peaceful phase in the history of global security.[6]

President Clinton continued to emphasize multilateral cooperation. During the Balkans wars, he supported West Europeans taking the lead but also took military action against Serbs in Bosnia. A UN peacekeeping force was eventually deployed in Bosnia to keep the peace. By the end of his term, Clinton contributed U.S. forces to a multilateral force including Russian and E.U. soldiers that took military action against Serbs in Kosovo and helped establish a coalition government there.

A big supporter of neoliberalism and globalization, Clinton worked to strengthen international organizations such as the IMF, the World Bank, and the new World Trade Organization (WTO). He worked to gain Senate ratification of the North American Free Trade Agreement (NAFTA) and the WTO agreements.

Globalization helped transform the GSS into a less orderly configuration with more flexible rules and more nonstate actors threatening security. By the mid-1990s, technological innovation had made conventional weapons more lethal. The proliferation of small arms helped destabilize many developing nations.[7] After an Islamist group bombed the U.S. embassies in Kenya and Sudan, Clinton responded with cruise missile attacks on sites in Sudan and Afghanistan, foreshadowing the challenge of international terrorism that the second Bush administration would face.

GEORGE W. BUSH: AMERICAN UNIPOLARITY AND NEOCONSERVATIVES

George W. Bush jettisoned multilateralism soon after entering office in 2001. His neoconservative advisors wanted Washington to act unilaterally as a benevolent global hegemon promoting capitalism and democracy everywhere.[8] In a sense, the "neocons" were old-school realists fixated on military capability as the sole defining quality of power. However, they were also ideologues who saw the United States' moral correctness as inherently justifying U.S. actions. The 9/11 attacks on the Pentagon and the Twin Towers in New York led the new president to attempt to reorder the security structure along unipolar lines, but with terrorism replacing communism as the main external enemy.

Two days after 9/11, *New York Times* columnist Thomas Friedman suggested that these assaults were the beginning of World War III, pitting the United States "against all the super-empowered angry men and women out there," especially from "failing states in the Muslim and third world."[9] The head of al-Qaeda, Osama bin Laden, took credit for the attacks. Bush responded forcefully. On October 7, 2001, the United States and some NATO allies invaded Afghanistan, quickly driving the governing Taliban—which was protecting bin Laden and al-Qaeda—into the hills of eastern Afghanistan and Pakistan.

Even as bin Laden escaped to Pakistan, the Bush administration turned its attention to removing Saddam Hussein from power, arguing that he had weapons of mass destruction (WMD). Acting against the wishes of Germany and France, a "coalition of the willing" made up primarily of forces from the United States, Britain, and Eastern Europe invaded Iraq in March 2003 under the guise of taking out Hussein and removing WMD. After a relatively quick military victory that toppled Hussein and his Baathist party, the coalition forces and private military contractors (PMCs) encountered strong resistance from insurgent groups, including ex- Baathists, foreign fighters, and Sunni and Shia militias. While Hussein was captured and executed, WMD were never found.

By 2006, the Iraq War had become a quagmire, if not a fiasco.[10] Especially problematic was the sectarian violence between Sunnis, Shiites, and Kurds, along with Iran's growing influence in Iraq. U.S. unilateralism alienated coalition partners who began refusing more financial assistance, troops, and diplomatic support in Iraq and Afghanistan. Widely circulated photos that showed American soldiers abusing and torturing Iraqi men in Abu Ghraib prison damaged the United States' public image. Suspected al-Qaeda and Taliban militants taken to Guantanamo Bay in Cuba were subjected to practices illegal under the Geneva Convention. States and international organizations condemned the U.S. practice of "rendition"—transferring suspected terrorists to places like Egypt and Eastern Europe where laws against torture were ignored and access to the Red Cross was denied.[11] Between 2007 and 2008, President Bush sent 30,000 more U.S. troops to Iraq as part of a "surge" to reverse deteriorating security conditions. Drones—small aircraft or unmanned aerial vehicles (UAVs)—began to be used for aerial reconnaissance and targeting suspected

terrorists with guided missiles.

Many classical realist critics considered the 9/11 attacks to be acts of terrorism—not a declaration of war against the United States. They took issue with the administration's unipolar, neoconservative outlook and rejected the idea that the United States was "chosen by God" to lead a moral crusade against terrorists. Another criticism was that U.S. leaders misidentified the true nature of the threat and adopted a war strategy instead of a coherent nation-building plan. Finally, many were critical of the new Bush Doctrine, which proclaimed that the United States would preemptively attack countries that harbored terrorists or that looked as if they might attempt to harm the United States.

By the time the Bush administration left office, critics argued that it had tried to construct a security structure that was inappropriate for the twenty-first century. The wars in Afghanistan and Iraq increased U.S. debt before the global financial crisis of 2008. So outsized were Washington's hegemonic ambitions and so overstretched was the U.S. economy that, ironically, it depended on China's purchases of U.S. Treasuries to help finance its wars.

In the end, Bush's efforts to bring about a unipolar hegemonic order went unrealized. Some would argue that Osama bin Laden's goal of drawing the United States and its allies into a politically and economically draining war in the Middle East worked. The increased role of insurgent movements and terrorist groups, especially in the Middle East and Africa, introduced unpredictable elements that the existing GSS, whether perceived as unipolar or multipolar, did not have a capacity to address.

BARACK OBAMA: TURNING AGAIN TO MULTILATERALISM

During the Obama administration, the GSS continued to shift towards a multilateral structure between the three major nuclear superpowers—Russia, China, and the United States—along with a number of other powers including Germany, Great Britain, France, and Japan. This transformation reflected a diffusion of military, economic, and social influence such that minor powers could play bigger roles in the GSS. Compared to his predecessor, Obama attempted to better align American foreign policy with this structural evolution. However, he was still sometimes comfortable "going it alone" with little public support from allies.

In his first year in office in 2009, Obama reset relations with Russia, which went well at first as he and President Dmitry Medvedev reached an agreement on further reductions in their countries' nuclear arsenals. When Putin won the 2012 presidential election, things changed; even though he shared an interest with the United States in fighting terrorism and preventing nuclear proliferation, he had reasons to resent the West. First, it admitted former Soviet allies into NATO after the Cold War, despite having assured Russia that it would not. Second, the West interfered in Central Asia and ex-Soviet republics that were economically important to Russia and where Russian-speaking minorities lived. Third, the United States and the European Union attempted to influence Russian domestic policies regarding corruption, state control of energy resources, and political opposition to Putin.

Emboldened by Russia's large oil revenues, Putin wanted to reestablish Russia as a major power with a role in negotiating international political and economic issues. When Ukrainians overthrew the corrupt regime of President Victor Yanukovych, Putin sent "resistance fighters" (Russian troops) into Eastern Ukraine to defend the Russian diaspora living in the border region between Russian and Ukraine. He then sent troops to seize Ukraine's Crimea region, which had a majority of ethnic Russians, and annexed it to Russia. Many believed that Putin's primary objectives in the region were to bring Ukraine back into Russia's sphere of influence, break up NATO, and remove U.S. and European sanctions on Russia.

As relations between Moscow and Washington soured, Russia also stepped up cyberattacks against the United States and adversaries in Ukraine. The Obama administration, like governments in other parts of the world, used national cyber capabilities for defensive and offensive purposes (see Box 9.2).

CYBER WEAPONS[a]

By the time President Obama took office, many states were using communications technology for international surveillance, information collection, and espionage. Increasingly, states have also been using cyber tools for nefarious purposes such as harming infrastructure or people in other countries.[b] States with sophisticated cyber weapon capabilities included the United States, China, Russia, Israel, India, Iran, North and South Korea, the Philippines, Great Britain, Germany, and the Netherlands.

The Obama administration quietly developed more defensive and offensive cyber capabilities and even carried out cyber operations that could be considered "acts of war." For example, the United States and Israel developed the Stuxnet virus and in 2010 introduced it into computers at an Iranian uranium enrichment complex, causing almost 20 percent of the facility's centrifuges to break down.[c] For its part, Iran cyber-attacked the United States in 2014, shutting down the casino servers of the Hotel Sands in Las Vegas owned by Sheldon Adelson.[d] Right after the November 2016 U.S. elections, Iran also damaged thousands of computers at Saudi Arabia's General Authority of Civil Aviation headquarters and erased their critical data.[e]

Since 2014, Russia has launched a string of cyberattacks on Ukrainian companies, utilities, and government offices. Many agree that Russia has used Ukraine as a "test lab" for its cyber weapons that could be applied elsewhere.[f] Ukrainian security services also assert that a 2017 cyber attack with Russian involvement was designed to destroy data, disrupt institutions, and induce panic in the population.[g] In 2016 and 2017 Russia carried out aggressive cyber campaigns in Europe and the United States designed to sway voters to support Moscow's preferred candidates. During the 2016 U.S. presidential election, suspected Russian hackers targeted Democratic and Republican party records, state election systems, voter registration databases, and a voting-software company.[h] Before he left office, Obama warned Putin that if Russia continued to interfere in American voting, the United States would consider offensive cyber operations against it.

Many Chinese hackers are connected to the People's Liberation Army, even though they work in a variety of companies. As we discuss in Chapter 10, China frequently steals information and intellectual property from foreign companies. It has attacked and planted malware in the computer systems of utilities companies in Canada, the United States, and Europe. Although Obama warned President Xi in 2013 that continued hacking could severely damage U.S.-Chinese relations, Chinese hacking and theft of information are unabated.[i]

Some realists and many structuralists have been critical of surveillance activities by

the NSA, the CIA, and other American intelligence agencies that include spying on German Chancellor Angela Merkel and intercepting Brazil's mail and telephone records, which is a breach of international law. With the imprimatur of the president and many in Congress, the NSA and the CIA also collected information on U.S. citizens.[j] Shadowy, virtual conflicts are likely to proliferate. Cyber capabilities have grown so quickly that the GSS has not yet established effective international norms to constrain nefarious state-led cyber activities. Cyberspace is a Wild West where the powerful use their capabilities to harm weaker opponents.

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[a] This box was written by Dan Pearson and edited by Bradford Dillman.

[b] See World Economic Forum, "*Who Are the Cyberwar Superpowers*?" May 4, 2016, at www.weforum.org/agenda/2016/05/who-are-the-cyberwar-superpowers/.

[c] See Kim Zetter, "An Unprecedented Look at Stuxnet, the World's First Digital Weapon," *Wired Magazine* online, November 3, 2014, at www.wired.com/2014/11/countdown-to-zero-day-stuxnet/.

[d] Adam Segal, *The Hacked World Order: How Nations Fight, Trade, Maneuver, and Manipulate in the Digital Age* (New York: PublicAffairs, 2016), p. 97.

[e] Sewell Chan, "Cyberattacks Disrupt Saudi Aviation Agency," *New York Times*, December 2, 2016.

[f] Andy Greenberg, "How an Entire Nation Became Russia's Test Lab for Cyberwar," *Wired Magazine* online, June 20, 2017, at www.wired.com/story/russian-hackers-attack-ukraine/.

[g] Pavel Polityuk, "Ukraine Points Finger at Russian Security Services in Recent Cyber Attack," *Reuters*, July 1, 2017, at www.reuters.com/article/us-cyber-attack-ukraine/ukraine-points-finger-at-russian-security-services-in-recent-cyber-attack-idUSKBN19M39P.

[h] For a detailed description and assessment of the Russian role in the election, see Eric Lipton, David Sanger, and Scott Shane, "The Perfect Weapon: How Russian Cyberpower Invaded the U.S.," *New York Times*, December 14, 2016, at www.nytimes.com/2016/12/13/us/politics/russia-hack-election-dnc.html. See also Nicole Perlroth, Michael Wines, and Matthew Rosenberg, "Russian Election Hacking Efforts, Wider Than Previously Known, Draw Little Scrutiny," *New York Times*, September 1, 2017, at www.nytimes.com/2017/09/01/us/politics/russia-election-hacking.html.

[i] Ibid., p. 133.

[j] See Shane Harris, "Giving in to the Surveillance State," *New York Times*, August 23, 2012.

The Middle East Quagmire

Throughout the rest of Obama's presidency, the Middle East continued to be a very violent region where scores of groups with religious, tribal, or national identity engaged in conflict. Divisions between Sunnis, Shia, Islamists, secularists, and others intensified immensely over the years. Many groups were allied with an outside major power, and there were many shifting alliances between groups.

Below we focus on a number of "fronts" in the region marked by violence and war during the Obama presidency: 1) the Arab Spring; 2) the reemerging wars in Afghanistan and Iraq; 3) the war against ISIS; 4) the civil war in Syria; and 5) tensions related to Iran. Note that in Chapter 14 we focus on other factors in the Middle East that contribute to conflict such as religion, political repression, and national rivalries.

According to *New York Times* reporter David Sanger, when Obama became president in 2009 he faced difficulty reconciling the need for cuts in defense spending with his promise to keep the United States in a position of global leadership.[12] Sanger also maintains that when "confronted with a direct threat to American security, Obama showed that he was willing to act unilaterally—in a targeted, get-in-and-get-out fashion that at all costs avoided

messy ground wars and lengthy occupations."[13] Domestically, however, the president also faced pressure from Congress to get the United States out of Iraq, where six years of war had resulted in limited success. Many NATO states were also weary of allied troop losses and the apparent futility of state-building, and mounting expenses of war throughout the Middle East, Between 2001 and 2014, an estimated 8,292 coalition soldiers (mostly from NATO members) died in the Iraq and Afghanistan conflicts, including 6,845 American soldiers.[14]

Under these constraints, Obama attempted to pursue a more nuanced military strategy than the Bush administration to deal with insurgents and terrorists in fragmented countries such as Afghanistan, Iraq, Mali, and Somalia. Upon the advice of General David Petraeus, in 2009 Obama ordered his own surge of 30,000 more U.S. troops into Afghanistan to "finish the job" that Bush had started. However, when the surge officially ended in 2012, U.S. and NATO forces were no closer to defeating the Taliban.

Meanwhile, in 2011 the Arab Spring movements ousted four Arab dictators and caused the Syrian regime to launch violent crackdowns against protesters. Although the United States had for many years encouraged democratization in the Middle East, the instability that spread after the Arab Spring threatened U.S. national security interests. It is helpful to review the following chronology in Box 9.3 to gain some perspective on major events in the Middle East since the historic Arab Spring that began in late 2010.

Soon Obama was divided between support for revolutionaries who overthrew Qaddafi and his fear of getting stuck in Libya if the mission failed. With France playing a prominent role in Libya, Obama decided to lead NATO "from behind," providing allies with crucial logistics and refueling services but letting them do most of the bombing. Today, some political scientists contend that the overthrow of Qaddafi without NATO's willingness to put troops on the ground resulted in a power vacuum and failed state in Libya, which has since allowed ISIS to gain a foothold in the war-torn country.[15]

In other parts of the Middle East, Obama also shifted his strategy to rely more on drones, joint strike forces, and cyber weapons. The CIA and the U.S. military carried out hundreds of covert drone strikes in at least seven countries in the region: Afghanistan, Pakistan, Syria, Iraq, Yemen, Somalia, and Libya. Why did drones become so popular? In 2011 drones gathered intelligence for the successful raid on Osama bin Laden's compound in Pakistan and pinpointed targets for NATO jet strikes in Libya. Despite the psychological trauma some drone pilots experienced, the remotely controlled vehicles helped decrease the number of troops needed on the ground, caused less collateral damage than traditional bombing, and helped cut military expenditures. U.S. joint strike forces also worked with military contractors that used drones in "snatch, grab, and assassinate" operations in Pakistan and elsewhere.

CHRONOLOGY OF WAR IN THE MIDDLE EAST

2010

- The Arab Spring mass demonstrations start in Tunisia and spread to other M ENA countries.

2011

- Egyptian president Hosni Mubarak is overthrown.
- Libyan revolutionaries depose Muammar Qaddafi with help from NATO.
- U.S. Navy Seals kill Osama bin Laden, the mastermind of the 9/11 attacks, in Pakistan.
- The Free Syrian Army begins fighting against the Assad regime.

2012

- Obama officially ends the war in Iraq and withdraws all troops. He also begins to draw down U.S. troops in Afghanistan.

2013

- The Islamic State of Iraq and Syria (ISIS) splits from Syria's Nusra Front, an al-Qaeda affiliate.
- Although Obama in 2012 had established a "red line" warning Syria's Assad not to use chemical weapons, Syrian forces attack civilians in a Damascus suburb with sarin gas, killing hundreds.
- Under U.S. and Russian pressure, Syria agrees to give up all chemical weapons.

2014

- ISIS, already controlling part of Syria, seizes Mosul and other parts of Iraq and declares a caliphate.
- The United States and coalition partners begin bombing ISIS.

2015

- Russia begins assisting the Assad regime with troops and airstrikes against rebels.
- For the first time, Turkey takes military action against ISIS in Syria.

2016

- Turkey's president Recep Tayyip Erdoğan prevails after an attempted coup

d'état.
- After a long siege, Syria recaptures all of Aleppo. Thousands of civilians die.

2017

- Russia and Turkey cooperate to try to find a political settlement for the Syrian conflict.
- Trump orders a cruise missile attack on a Syrian air base after Syrian forces use chemical weapons on civilians in the town of Khan Sheikhoun.
- The Iraqi army and Kurds defeat ISIS in Mosul.
- Trump withdraws support for CIA-sponsored rebels in Syria.
- Trump reluctantly decides to send 4,000 more troops to Afghanistan.
- U.S.-backed forces recapture Raqqa, the de facto capital of ISIS in Syria.

Obama continued the Bush administration policy of preventing prosecution of CIA employees who had waterboarded terrorist suspects and violated international laws. His administration also detained insurgents in Afghanistan in a "black jail" run by U.S. Special Operations Forces. Additionally, the National Defense Authorization Act of 2012 authorized the president to order the detention of terrorism suspects (including U.S. citizens), strip them of their legal protections, and try them in military or federal court. Under the PATRIOT Act, the president could force companies to turn over information related to citizens' finances, communications, and associations. Secret courts issued secret warrants to pursue individuals deemed to be aiding or abetting hostile foreign governments or organizations.

Syria

Many experts suggest that the center of the Middle East morass was Syria. Bashar al-Assad's father, Hafez al-Assad, was a brutal dictator but also a secular modernizer of Syria. Resistance to President Bashar al-Assad's regime began in 2011 when the Free Syrian Army (FSA) and other revolutionaries tried to gain control over much of the country outside of the capital Damascus.[16] Lacking an effective central command, many of these groups splintered, and Assad labeled them all terrorists. Regime forces often struck rebels from the air using barrel bombs and chemicals such as chlorine that killed and maimed thousands of civilians.

As the Iraq war was winding down for the United States in 2011, al-Qaeda in Iraq (a predecessor of ISIS) sent fighters into Syria to join the fight against Assad. It soon split from the Nusra Front and declared itself ISIS. By 2014 it had control of some areas in Syria and then seized a wide swath of territory in Iraq, including the city of Mosul, where it declared a caliphate. By 2015 ISIS dominated much of eastern Syria, including most of the cities along the Euphrates River.

Mass media around the world focused on ISIS's brutality, horrific executions, and war

crimes against Christian and Yazidi minorities. ISIS also claimed responsibility for a number of terrorist attacks in the Middle East, Europe, Africa, South and Southeast Asia, and the United States. A coalition of fighters representing different states, tribes, and ethnic and religious communities formed to gain territory back from ISIS and destroy the group. The coalition members had some overlapping interests, but at the same time they also had conflicting goals. For example, despite their mutual antagonism, both Iran and the United States helped Iraqi forces push back ISIS.

In 2013 the Assad regime attacked civilians in a suburb of Damascus with sarin gas, killing 1,500, including at least 400 children. Before the attack, Obama had warned Syria that if it crossed a "red line" by using chemical weapons, the United States would respond with force. However, at the last minute Obama decided not to follow through with air strikes when it became apparent that U.S. allies and a majority in Congress were opposed to attacking Syria. Instead, Secretary of State John Kerry and Russian foreign minister Sergey Lavrov floated a proposal to Syria to remove all its chemical weapons, which Assad unexpectedly accepted.

The agreement opened up a debate in the U.S. administration between hawks who argued that Obama should have responded to Syria's use of chemical weapons with force in order to demonstrate U.S. resolve, and those who argued that "coercive diplomacy" with the threat of force could achieve goals that military power alone could not accomplish.[17] For the duration of Obama's second administration, many Republicans criticized the president for damaging U.S. credibility by not acting militarily when Assad crossed the "red line." Some charged that the decision made the United States look like a reluctant hegemon and also made U.S. allies in the Middle East question whether the United States would honor its commitments to them.

The conflict in Syria generated a deeper split between Shia and Sunni Muslims in the region. Sunni-majority countries such as Turkey and Saudi Arabia aided the rebels, while Iran and its Shia Lebanese ally Hizballah supported Assad, whose regime is dominated by Alawites, a sect close to Shiism. Both Iran (a Shia Islamic Republic) and Saudi Arabia (a conservative Sunni kingdom) aspire to leadership of the Muslim world and have different visions of regional order.

By the middle of 2015, the days of the Assad regime seemed to be numbered. However, Assad benefited from two major changes. First, while Turkey opposed the Assad regime, it was more concerned with preventing Syria's Kurdish forces (YPG) from strengthening their control in northern Syria because they were aligned with the PKK, a Kurdish rebel group that Turkey viewed as terrorists because of their attacks inside of Turkey.

Second, in the fall of 2015, Syria's longtime ally Russia unexpectedly intervened, sending jet fighters, battle tanks, artillery, helicopters, and some 2,000 troops to prop up the Assad regime. President Putin claimed that the move was simply to join in the effort to knock out ISIS, and yet Russian jet fighters mostly attacked anti-Assad rebels instead of ISIS. Some realists worried that Putin's actions enhanced the risk that Russian and U.S. military forces might engage one another, possibly setting off a war. Brian Williams and Robert Souza suggest that Putin intentionally sought to bolster "his image domestically as a strong leader

… able to stand up to the West."[18] While helping Syria in its fight against "international jihadists," Putin was also eager to project Russian power abroad shortly after annexing Crimea and intervening in eastern Ukraine.

With the help of Russian troops and bombers, Assad's forces expelled all rebels from Aleppo, Syria's largest city. Intermittent ceasefires allowed some civilians to leave the city where international rescue agencies tried to provide aid during one of history's most intense humanitarian disasters (see Chapter 16).

Meanwhile, the United States continued to assist moderate rebel groups and conducted air strikes against ISIS. Deploying a "light footprint" strategy that limited the number of U.S. "boots on the ground," Obama used small contingents of about 3,000–3,500 U.S. military advisors and trainers in Iraq. Even so, Senator John McCain and other Republicans criticized President Obama for "surrendering" the Middle East to Putin and weakening U.S. hegemony in the region.

Surprisingly, Turkey pivoted and agreed to assist the coalition in taking on ISIS in northeast Syria. Relations between Russia and Turkey would warm to the point that when a Turk assassinated a Russian official in an Istanbul museum, both states played down the event for the sake of continuing to cooperate in an effort to defeat ISIS.

By mid-2016, 300 U.S. military personnel were in Syria to help in the war against ISIS and Assad.[19] In late 2016 a coalition of Iraqi troops, Iraqi Shia militias, and Iraqi Kurds—backed by the United States and Iran—began a major campaign against ISIS that resulted in its ouster from Mosul and most other areas of Iraq. With help from the United States, forces led by Syrian Kurds retook Raqqa and other ISIS-held cities in Syria's Euphrates River Valley in 2017.

Iran: The Gamble

By 2015, international sanctions to punish Iran for its nuclear program had cut the country's oil exports in half and deprived it of much-needed foreign investment. Washington had also orchestrated the assassinations of Iranian scientists and the installation of the Stuxnet virus in a number of Iranian computer systems. These actions, along with a steady drumbeat of war talk from Israel and the Obama administration's repeated threats to strike Iran ("all options are on the table"), probably increased Tehran's sense of insecurity and made it more agreeable to an accord. In July 2015 the United States joined Russia, China, Germany, France, the United Kingdom, and the European Union in reaching an agreement with Iran to curb its production of nuclear materials that could be used to make nuclear weapons. Iran agreed to cut its enrichment capacity (centrifuges) drastically and reduce its stockpile of enriched uranium. The deal allowed Iran to access more than $50 billion in long-frozen assets and sell its oil in the international marketplace. Tehran hailed the deal as vindication of its power and influence in the world.[20] Secretary of State John Kerry got credit for cobbling together an international coalition, backed by the UN's International Atomic Energy Agency (IAEA), to prevent Iran from building any nuclear weapons. Nuclear-related sanctions on Iran were officially lifted in January 2016, but the

United States retained some sanctions related to Iran's human rights violations and support for terrorism.

Some realists argued that the agreement checked Iran's new weapons capabilities for at least five more years. However, many hawks such as former U.S. Ambassador to the UN John Bolton chastised Obama for trusting Iran. Neocons and the political right represented by John McCain asserted that Obama and the left were relinquishing the United States' global hegemonic position. In December 2016, Congress renewed for ten years the Iran Sanctions Act, which technically did not violate the nuclear agreement with Iran.

Toward the end of the Obama administration, most experts felt that the jury was still out on the Iranian deal. David Sanger submits that "Iran gave up 98 percent of their nuclear material and dismantled thousands of centrifuges and filled the core of a major plutonium reactor with cement."[21] Despite criticism from Prime Minister Benjamin Netanyahu, the deal pleased many Israelis because it reduced the threat of an attack on them by Iran. Of course, critics point out that Iran is still testing advanced missiles and other weapons.

ENTER DONALD TRUMP

When Trump took office in 2017, he stated that he was inheriting a big foreign policy "mess" from President Obama. However, just eight months into the Trump administration, a chorus of officials and experts agreed that the new president had put forward no coherent views about the world and had already created messes of his own. Below we use a realist lens to examine a number of important issues that Trump and the leaders of the other major powers (Russia, China, Great Britain, France, Germany, and Japan) must deal with related to management of the GSS: North Korea's nuclear weapons, Middle East conflicts, the rise of China, Russia's military actions, terrorism, cyber weapons, and global climate change.

An examination of Trump's public statements and actions suggests that his views of the world are rooted in three primary factors:

- The interests of his business empire;
- His nationalist-authoritarian outlook; and
- His desire to scrap the liberal international order.

First, Trump is above all else about himself and the businesses he owns or derives income from all over the world. After becoming president, he continued to refuse to release his income tax records or divest fully from his business interests. He also made his son-in-law Jared Kushner, who has no experience in international affairs, a senior advisor and point man for diplomacy in the Middle East.

Second, Trump's nationalist-authoritarian traits, which we discussed in Chapter 1, inform his "Make America Great Again" campaign and his pledge to always put the United States first. These vague ideas have played well with his base, who blame globalization for job losses, dislike immigrants, and feel overlooked by elites since the financial crisis. Trump also admires the governing style of Putin, Egyptian president Abdel Fattah el-Sisi, and other "strongmen." He routinely attacks the press, Congress, and government agencies including the Justice Department, the FBI, the CIA, and the courts. He appears to have little interest in promoting democracy, and economic or the rule of law.

Third and finally, Trump has been explicit about changing the world order. Roger Cohen argues that Trump is not interested in a rules-based international order or in sustaining U.S. hegemony.[22] Rather, as his September 2017 speech before the United Nations demonstrated, he views the United States as the most powerful nation in a world where every sovereign country looks out for itself. His approach to foreign policy is largely transactional; he is not interested in assuaging traditional U.S. allies or spreading U.S. values "but ensuring that the United States would achieve concrete results that could be measured in dollars and cents."[23] Deals (especially economic ones) with other governments must profit America, a compulsion that can easily conflict with the security objectives of the State Department and national intelligence agencies. In addition, Trump has given no

indication that he envisions a bipolar or multipolar structure that would manage global security.

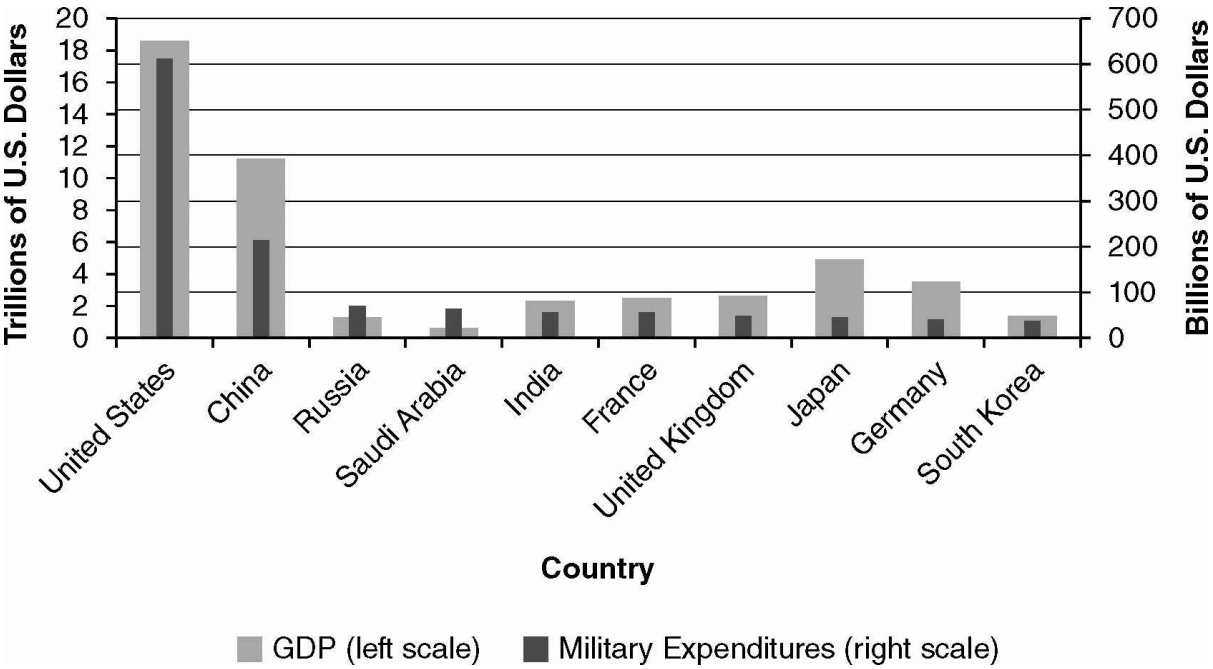


FIGURE 9.1
Military Expenditures and GDP of Major World Powers in 2016 in Current U.S. Dollars.

Sources: Data from Sipri Military Expenditure Database, at www.sipri.org/sites/default/files/Milex-constant-201S--USD.pdf; and World Bank, at https://data.worldbank.org/indicator/NY.GDP.MKTP.CD.

As mentioned earlier, many realists view the current GSS as much less stable than previous ones. Instead of a traditional balance of power, there is more of a multilateral relationship between the three superpowers and major powers. Among the three superpowers, China and the United States have strong militaries and economies, while Russia has military muscle but a weak economy (see Figure 9.1).

Domestically, Putin is relatively secure. Despite his popular support, a weak economy is his Achilles heel. A prominent role in managing the GSS provides him with the opportunity to build public support for his effort to recover the prestige Russia lost after the end of the Cold War, President Xi of China is also relatively secure. He is a confident player in the global order who is usually willing to work with others. However, there will be more threats to domestic economic stability as China shifts focus away from exports to domestic consumption.

Trump is the most unpopular and unpredictable of the three presidents. He leads a deeply divided society. He is more comfortable dealing face-to-face with foreign leaders. Others tend not to trust him. He is viewed as a mercurial bully who lacks deep understanding of many global issues. While some hawkish realists like the president's renewed emphasis on military power, many realists would agree with Robert D. Kaplan,

whom we quoted in the opening of the chapter, that Trump is dangerously lacking a regard for the facts, a sense of history, or an international vision. Although some realists claim that Trump is an isolationist, historian Stephen Wertheim views him as a militarist, warmonger, and predator.[24] The ongoing North Korean missile crisis has so far revealed Trump's traits of impulsiveness and ahistoricism.

SEVEN SECURITY ISSUES TO WATCH

What follows is an examination of how Presidents Obama and Trump have dealt with seven systemic security issues that deeply implicate Russia, the United States, and China.

The North Korean Missile Crisis

North Korea has had a nuclear weapons program for decades. The Bush and Obama administrations attempted to use carrots (promises of food aid) and sticks (international sanctions) to convince Pyongyang to abandon nuclear weapons. North Korea withdrew from the Nuclear Non-Proliferation Treaty in 2003 and tested a nuclear device in 2006. The Six-Party Talks that went on for five years until 2008 failed to rein in Pyongyang. The North Koreans conducted nuclear tests in 2009, 2013, 2016, and 2017.

North Korea has also worked hard to develop intercontinental ballistic missiles (ICBMs) that can threaten the United States. The test of an ICBM on July 29, 2017 led many analysts to conclude that North Korea could soon deliver a warhead inside the United States as far as Chicago. On August 5, the UN Security Council voted unanimously to impose tough economic sanctions on North Korea for continuing to test its long-range missiles. Restrictions on its exports of coal, iron, and seafood and on its Foreign Trade Bank were expected to reduce its export revenues by up to one-third. U.S. Secretary of State Tillerson said that the United States was open to a possible dialogue with Pyongyang if it stopped its provocative acts.

Trump soon thereafter warned North Korea to stop making threats against the United States lest they "be met with fire and fury like the world has never seen."[25] His advisors were caught off guard by Trump's "improvised" comments and tried to reframe them in less bellicose terms. Nevertheless, the Korean People's Army issued a statement warning that it would "turn the U.S. mainland into a theatre of nuclear war."[26] Several days later Trump ominously stated, "Military solutions are now fully in place, locked and loaded, should North Korea act unwisely." Kim Jong-un later described Trump as "a mentally deranged U.S. dotard."[27]

To no one's surprise, much of the world feared that either leader might be tempted to launch a preemptive strike that would lead to a conflict killing millions on the Korean peninsula and possibly in Japan and on Guam. Trump supporters largely agreed with the president that the "strategic patience" policy of the previous three administrations to denuclearize North Korea had not stopped North Korea from building more nuclear weapons and dramatically improving its missile technology.

Many realists expect that, in the face of the overwhelming military power of the United States, Kim will back down because he knows that engaging in an actual confrontation would mean the certain end of his regime and the destruction of his country. However, North Korea unexpectedly tested a medium-range ballistic missile over northern Japan on August 29. Then, on September 3, North Korea tested a nuclear device underground,

which many scientists agreed was likely a hydrogen bomb. Oddly, Trump accused the United States' steadfast ally South Korea of appeasing North Korea, On September 11, the UN Security Council unanimously adopted new economic sanctions on North Korea that reduced oil exports to the country by one-third, banned all of their textile exports, and banned new contracts for their workers abroad. China and Russia accepted these measures after Washington agreed to water them down.[28]

Critics of sanctions argue that they will only feed into Kim's paranoia that other states are out to get him. He does not trust others to keep their word; he might believe that the United States will turn on North Korea after he agrees to get rid of his WMDs. No matter the pain inflicted on the North Koreans, Kim seems intent on building nuclear weapons as a deterrent and defense against the United States.[29] At the same time, Trump appears to be unconditionally committed to North Korea giving up its nuclear arsenal. Among other things, Beijing is concerned that war could mean refugees flooding into China. Russia does not want the United States to dominate the Korean peninsula.

Without knowing how the Korean crisis will end, it raises questions about the theory of deterrence and realist notions of rationality. In theory, deterrence means preventing an opponent from initiating a war or conflict by threatening them with unacceptable consequences (massive destruction) if they launch an attack. Most experts agree that deterrence requires the following:

- Possession of military capabilities (weapons) and the economic means necessary to produce those weapons;
- The will to use those weapons; and
- Communication of one's capabilities and intentions to the opponent.

An important question is whether, despite the saber-rattling, deterrence will work. Kim continued to challenge Trump and his allies throughout 2017, even though they can obliterate North Korea. Some realist theorists of deterrence believe that Kim is indeed rational and will not risk losing control over his country; at some point he will negotiate a peace treaty if it provides North Korea with more food aid and ends U.S.-South Korean joint military exercises. Therefore, according to deterrence theory, Trump should continue to try to convince Kim that failure to give up his arsenal will ultimately cost him his regime and kill millions of his people. This creates a conundrum in that the slightest miscalculation by either side of the other's behavior could result in preemptive or retaliatory nuclear attacks on North and South Korea, Japan, and Guam.[30]

In effect, rational thinking—choosing to maximize one's gains and minimize one's losses — could logically lead to nuclear war, an outcome most would agree is nonsensical because it is so horrific and immoral.

There are still some options to help resolve the North Korea crisis:

1. The United States could do more to engage in diplomacy with North Korea to produce a peace agreement that recognizes Kim's regime and assures him that it will

not seek regime change. It could also lift sanctions in exchange for North Korea discontinuing its missile tests while working on the eradication of the North's nuclear program.

2. China and Russia could do more to bring Kim to the table by way of rigid economic sanctions together with efforts to hammer out a security agreement that helps him feel secure.[31]
3. A proposal offered years ago by political scientist Kenneth Waltz is to allow for the slow proliferation of nuclear weapons, even to a country such as North Korea, in the expectation that it would raise the costs of waging war against any nuclear power so high that none would start a war.[32] Former National Security Advisor Susan Rice offers a similar recommendation: knowing that Kim will not give up his nuclear weapons, the United States should tolerate their existence and rely on mutual deterrence to dissuade North Korea from ever using them against the United States or its allies.[33]
4. When all else fails, there could be direct negotiations between the relevant leaders or a summit of world leaders.

Finding a solution to this crisis inevitably depends on the intentions of Kim and Trump. One has to wonder if either really wants peace. The impulsive and pugnacious actions of both leaders seem designed to rally their domestic supporters rather than achieve peace. Meanwhile, Kim must decide if anything will make him feel secure enough to stop testing his missiles and perhaps give up his arsenal. Why is Trump expecting Kim to give up his entire nuclear arsenal in the first place? Why shouldn't Israel or France give up theirs, too? Why not try for a deal like Obama got with Iran? Or is Trump's ulterior motive to use the North Korean situation to distract from the "Russiagate" investigation? Finally, would Trump really consider killing millions of people to demonstrate how tough he is to his political base?[34]

In a surprise development in April 2018, North Korean leader Kim and South Korean president Moon Jae-in held a summit in the Demilitarized Zone between their two countries, where they vowed to negotiate a peace treaty. Trump announced his willingness to hold talks with Kim later in the year.

The Middle East: Continual War

That same evening at Mar-a-Lago, Trump made a 180-degree change in his plans to limit U.S. involvement in the Middle East and launched 59 cruise missiles at a Syrian airfield after viewing TV images of children dying from a nerve agent dropped by Syrian jets on a small city in northern Syria. Trump delighted his U.S. supporters, who cheered him for finally standing up to Assad. To critics, Trump merely used the opportunity to get his first big "win" to show off for his base.

Interestingly, despite Trump's desire for closer United States—Russia relations, the attack made it harder for Washington and Moscow to cooperate in the fight against ISIS. It

also increased the possibility that U.S. and Russian fighters would encounter one another and lead to conflict between the two superpowers. Some critics noted that, although the strike was symbolic and measured, there was no overall political-military strategy to go along with it.

Trump changed U.S. policy in Syria by cutting off assistance to U.S.-backed resistance forces trying to depose Syrian president Assad. However, he continued Obama's policy of allying with a force led by Syrian Kurds to push ISIS out of the cities and towns it controlled. He also continued U.S. assistance to Iraqi forces to liberate Mosul and other Iraqi cities from ISIS. By October 2017, Kurdish-led forces had seized Raqqa, the capital of the ISIS caliphate in Syria. Trump allowed U.S. generals more freedom to bomb ISIS in urban areas, causing many deaths of civilians in Syria and Iraq.

Like Obama, Trump does not want to risk the United States losing Afghanistan after so many years of war. After berating his generals for not being able to "win" in Afghanistan, the president reluctantly agreed with them to send 4,000 more U.S. troops to help 11,500 "trainers" already there. In a formal speech before U.S. troops, Trump said that the new goal was to defeat the Taliban (which controlled 60 percent of the country) and al-Qaeda. U.S. forces will train Afghan units and help hold the capital city Kabul.[35] He also stressed that U.S. forces would only pull out of Afghanistan after effectively meeting these goals, suggesting that U.S. involvement in the war would go on indefinitely. He also wanted Pakistan to deny the Taliban safe havens and do more to help fight terrorism in their country. Finally, Trump dismayed Pakistani officials when he invited India to help the United States in Afghanistan, generating questions about his awareness of the long history of bad relations between Pakistan and India.

On balance, it appears that these policies will only perpetuate the U.S. stalemate in the Middle East and Afghanistan. Paradoxically, a continued American presence is likely to allow Russia to increase its role in the region as a counterweight. As we discuss in Chapter 13, Russia's Middle East interests are both geopolitical and economic, including a desire to build gas pipelines to and within the region. A Russian diaspora lives in many states along Russia's borders, where terrorists also have a history of challenging Russia's influence. Although Moscow supports the global war on terrorism, it also supports the Syrian regime known for practicing state terrorism.

The Rise of China

Some realists fear that China is bent on confronting the United States and its allies in the Pacific region. China vehemently opposes independence for Taiwan, over which it claims sovereignty. It also claims islands and territorial waters in the South China Sea close to Taiwan, the Philippines, Vietnam, and Malaysia.[36] Early in his administration, Trump pursued the same basic objectives related to China as Obama, although he used more bellicose language. In early 2017 Trump insisted that the United States would not accept militarization of the islands in the South China Sea. Trump withdrew from the Trans-Pacific Partnership (TPP), one of whose political objectives was to undercut China's

economic influence in the region. He challenged China's trade policy and its new Asian Infrastructure Investment Bank (AIIB), which all the ASEAN countries became members of. Nonetheless, after President Xi's visit with Trump at his Mar-a-Lago resort where Trump declared that they had the "most beautiful" chocolate cake dessert, the United States–China relationship warmed a bit. Xi has played an important role in trying to settle the North Korea missile crisis.[37] It is clear that the reduction of the U.S. hegemonic role in Asia provides China with an opportunity to have greater influence over economic and security issues in the region.

In the realm of global security, the U.S. Department of Defense sees little evidence that Beijing is willing to risk a direct military confrontation with the United States or its neighbors.[38] Its primary military concerns—to deter a Taiwanese declaration of independence and win any conflict in the Taiwan Strait—are hardly malevolent. Commensurate with its role as a dominant regional power with growing global interests, its military modernization is focused on dealing with potential threats in its immediate periphery.

Russia's Sphere of Influence: Ukraine and the Baltic States

The realist school of thought interprets Russian actions as based on a calculated strategy to enhance national power, preserve sovereignty, and balance against the United States. Moscow is engaged in a "new imperialism," defying some of the key norms of the liberal world order such as the inadmissibility of the acquisition of territory by force and the obligation to protect human rights, even in wartime. In this view, Russia is a "revisionist" power rather than a responsible international stakeholder. To ensure its security it needs to maintain spheres of influence along its borders. Russia has been increasingly using military force to defend its interests in Syria and Ukraine. Russian missiles are deployed close to the border with Poland and Lithuania, violating the Intermediate-Range Nuclear Forces Treaty.

In 2017 Russian and Belarusian troops, tanks, and planes engaged in large joint military exercises called *Zapad* 17 (West 17) along the borders with Poland, Finland, and the Baltic states, worrying some that the exercises would give cover for Russia to permanently increase its military forces in Belarus. In response, NATO bolstered deployment of troops and equipment to Poland and the Baltic states, while Sweden held its own large military exercises with NATO participation. Each side seemed to be demonstrating that it could deter aggression from the other, but the exercises could also be read as dry runs for invasion in the future.[39]

Both Russia and the United States are modernizing their nuclear arsenals, while China is upgrading its navy. Russia is concerned about U.S. missile defense systems that are becoming more accurate. The United States expects to spend $1 trillion on more sophisticated cruise missiles, ICBM replacements, submarines, and bombers for its strategic nuclear triad.

In 2010 the United States and Russia signed the Strategic Arms Reduction Treaty (START) that gave both countries until 2018 to cut their strategic nuclear warheads to

1,550 and their strategic launchers to 800—the lowest numbers in decades. In a January 2017 call with Russian president Vladimir Putin, Trump criticized the new START proposal because he believes it benefits Russia more than the United States. However, several former U.S. defense officials point out that the modernization of U.S. nuclear weapons will increase U.S. offensive nuclear capabilities.[40] Some realists argue that the modernization program will contribute to more waste, destabilize relations between the superpowers, and promote a new arms race. Questions abound as to whether these modernized weapons are meant strictly for deterrence and whether they will be included in new arms control talks. Meanwhile, President Trump has suggested that nuclear weapons could be used for nuclear war rather than simply for deterrence, an idea that is almost universally rejected as irrational and immoral.

Trump has been soft on Russia in almost every policy area, including intervention in Ukraine, annexation of Crimea, cyber hacking in the United States and Europe, and repression of Russian protestors. Some assert that this softness stems from previous business connections that Trump administration officials had with Russia. Trump tried to build a hotel in Moscow and may have received loans from Russian banks and oligarchs. Trump's former campaign chairman Paul Manafort worked for three years for the pro-Moscow Ukrainian politician Viktor Yanukovych. And when former Secretary of State Rex Tillerson was CEO of Exxon-Mobil, the corporation lost a $500 billion deal with Russia's state-controlled oil company Rosneft when Western sanctions were imposed on Russia in 2014; better relations could revive business opportunities.

At a G20 summit in July 2017, Putin and Trump appeared to get along well. However, as the Russiagate investigation progresses, Congress has blocked Trump from lifting sanctions. The Russian president ordered Washington to cut 755 employees from its diplomatic staff in Russia. Tensions have also risen between NATO and Russia. Although Merkel supports expanding a gas pipeline from Siberia to Germany, Trump has promised to help Poland and Eastern European countries break their dependence on Russian energy supplies.

Despite the West's rising tensions with Russia, it is perhaps reassuring that the behavior of the major powers mimics that of the East and the West during the Cold War, when each side deterred the other. Putin has resorted to playing his military cards carefully while working with other major powers to keep Russia at the forefront of managing the GSS.

Cyber Weapons and Warfare

Under President Trump, cyberattacks are generating many national security problems and harming businesses while also helping transform the GSS. Trump adamantly denies that he or his campaign staff played a role in Russia's hacking of the 2016 election, which continues to be investigated. In September 2017 Facebook revealed that a Russian company had purchased advertising space on its network between 2015 and 2017 and set up hundreds of fake accounts to spread disinformation designed to weaken support for the U.S. political system and intensify political polarization in United States and Europe.[41]

Facebook and other social media companies now face intense scrutiny as to how they regulate information content and advertisements, raising questions about how to balance national security and free speech. Some believe that cyber interference is undermining the political, economic, and social foundations of their society.

The United States has also identified the Moscow-based company Kaspersky Lab as a possible threat to U.S. security. The company sells antivirus and security software products used by 400 million people in the world and in U.S. federal government agencies. Kaspersky Lab, whose founder was trained by the Soviet secret police (KGB), supposedly has ties to Russian intelligence, which could use the company's software to monitor data transmissions or even shut down the U.S. electrical grid, pipelines, and telecommunications networks.

The point here is that the world increasingly relies on information technology to manage national security and public infrastructure, creating vulnerability to crippling cyberattacks that could spark a war. These are reasons why it might be prudent to regulate Internet and information technologies to try to control cyberwarfare. Jared Cohen does not believe that states will give up their cyber weapons, but he suggests that instead of waiting for a major crisis, governments should establish norms and rules to reduce cyber conflict and guide conduct when attacks occur.[42] He would like to see states create an international body that can investigate attacks and establish a framework for sanctions on guilty parties.

Adam Segal doubts that states can agree to rules and norms that serve their geopolitical interests. He notes that cyberattacks are often closely tied to espionage, which states have historically failed to regulate. He also warns that militaries "are rushing to develop powerful cyber weapons without any agreement on how and when they might be used or any deep understanding of the consequences they might unleash."[43]

The difficulty in getting states to agree on rules for cyberspace was made clear in 2012 when countries met under the auspices of the ITU (the UN's International Telecommunications Union) to consider revisions to the International Telecommunication Regulations that would affect governance of the Internet. The contentious negotiations at the ITU conference revealed a "digital cold war" between liberal democracies and authoritarian states over the openness of cyberspace.[44] The United States, the EU, Japan, Australia, and New Zealand expect the Internet to be relatively open and governed by multiple stakeholders, including nonstate actors. The BRICs countries, developing countries, and non-democratic countries insist on stronger intergovernmental control of cyberspace through the ITU and more national sovereignty over the Internet so that governments can control domestic information technology markets with filters, censors, and barriers.

Terrorism

When most people think of terrorism these days, it is "radical Islamic" or "Jihadi" terrorism, but there are many types of it everywhere, including state-sponsored terrorism. Russia has a long history of dealing with terrorists. When it occupied Afghanistan from

1979 to 1989, it dealt with the Mujahideen, whom the United States supported with weapons and aid. More recently, Chechen rebels have launched terrorist attacks on Russian schools and targets in Moscow. Meanwhile, Russian retaliation against terrorists has been brutal. On the international level, Putin has been promoting the new UN Office of Counter-Terrorism, which the UN General Assembly established in 2017 to coordinate counter-terrorism efforts of member states.

Terrorism is not as big an issue for China as it is for the other two superpowers, although Beijing has cracked down on Muslim Uighur activists in the northwest region of Xinjiang that it claims are terrorists. Terrorism remains a major security issue for the United States and its NATO allies, even though relatively few people have been killed in terrorist incidents in these countries. President Trump has made dealing with terrorism one of his key foreign policy objectives. However, his policies of keeping U.S. forces in Afghanistan and Iraq, bombing ISIS heavily in Syria, and helping African countries fight domestic Muslim rebel groups may create a backlash of more terrorism in the future.

On the whole, dealing with terrorism requires more than national crusades against political revolutionaries; states must also improve the quality of life for millions of people who feel exploited or lack social mobility. While the "war on terrorism" can never be won, more can be done locally and nationally to deal with its social, political, and economic roots, which does not appear to be in the geopolitical interests of the major world powers.

Climate Change

Climate change threatens the security of every individual in the world, and yet it has only recently generated the kind of interest on a global level that many insist that it deserves. An ever-mounting and overwhelming body of scientific evidence demonstrates that climate change is rea1.[45] Some of the most intense hurricanes in history struck the Caribbean in 2017. Polar icecaps continue to melt at historically unprecedented rates, threatening low-lying island nations. Droughts around the world have become more severe and long-lasting.

With these and many other examples, Russia, China, and the United States all signed the 2015 Paris climate accord—the first global agreement of its kind—to tackle climate change. Not surprisingly, soon after his election President Trump, after much hullabaloo, withdrew the United States from the Paris accord, establishing the United States as a rogue nation on climate change policy. As in other areas, the Trump administration made clear that the United States was no longer willing to shoulder global responsibilities. Trump also opened the door ever wider for China to gain the reins of global leadership on this and other issues.

CONCLUSION: GETTING TO PEACE AND STABILITY

One of the main themes of this chapter has been the breakdown of the postwar global security structure (GSS). Realists argue that with no global order, there is no security for nation-states. Early in the chapter we explained the decline of the bipolar security structure under Presidents Johnson and Nixon and then a number of gyrations in the security structure under unilateralists such as Presidents Reagan and George W. Bush and multilateralists such as Presidents George H. W. Bush, Bill Clinton, and Barack Obama, President Trump, however, has intentionally rejected multilateralism and adopted the policy of "America first," especially when it comes to hegemonic management responsibilities. He has combined the unipolarity of the George W. Bush presidency with neo-isolationism. Nine months into office, Trump was still following many of President Obama's policies—minus Obama's knowledgeable and calm demeanor and the global respect he had garnered.

For many realists, an important question today is whether the United States, Russia, China, and other major powers have the capacity and will to manage the current GSS or construct a more stable and secure one. The three superpowers share a number of common characteristics. Domestically, both Putin and Trump play to bases that are nationalist and authoritarian in outlook and that oppose immigration and globalization. Under Xi the Chinese have become more nationalistic, but they still support globalization. In all three superpowers there is a high level of economic inequality. At the international level they each have large military and cyber-warfare capabilities, which they seem increasingly willing to use in aggressive, provocative ways.

Russia seeks to play the role of a global manager, as demonstrated in its annexing of Crimea, intervention in Ukraine, and support for Syria. It has a rational interest in creating a multipolar world where it can be a more relevant stakeholder. Dmitri Trenin points out that because Russia cannot flex nearly the same amount of political or economic power as the United States or China, it must rely on its comparative advantage—military action—to advance its interests, which also weakens its claim to be helping stabilize the GSS.[46] By all indications, China—with the world's second largest economy—wants to be a dominant regional player and continue to extend its economic influence in many parts of Asia, Latin America, South Asia, and the Middle East.

The United States, on the other hand, is the wild card among the major powers. Because the Trump administration has caused the United States to lose its international credibility and reputation as a global stabilizer, the GSS could be unstable for the next few years. There is greater risk that states will misinterpret the military and cyber actions of adversaries. While bogged down in the Middle East, the United States seems intent on standing up to the "bad guys" in North Korea, Iran, and Venezuela—but not to the authoritarian populist leaders in Turkey, Hungary, and the Philippines.

To achieve the goals of peace and security, states must cooperate and build trust. Because the global security structure is currently weak and war is so costly, the major powers have a

strong incentive to reconfirm old norms or establish new ones through a conscious and diligent multilateral process. Most importantly, they need to agree on rules to limit the risk of nuclear and cyberwars and find a path to new arms control agreements. It is an open question whether the Trump Presidency will allow for more cooperation or trust, though many of the early signs are less than reassuring.

KEY TERMS

global security structure (GSS) 222
classical realism 222
neorealism 222
balance of power 223
North Atlantic Treaty Organization (NATO) 226
Warsaw Pact 226
massive retaliation 226
Cuban Missile Crisis 227
mutually assured destruction (MAD) 228
détente 228
neoconservative 229
weapons of mass destruction (WMD) 230
drones 231
unmanned aerial vehicles (UAVs) 231
red line 236
deterrence 241

DISCUSSION QUESTIONS

1. Pick a significant security event and discuss how a classical realist and a neorealist would explain it. Discuss which outlook is closest to your own view and why.
2. In what ways do Trump's outlook on and policies toward global security issues differ from those of previous U.S. presidents?
3. Describe some of the main changes in the global security structure after World War II. Why did these changes occur?
4. What are the risks in today's global security structure that could cause a new armed conflict that involves Russia, China, or the United States? What can states and international organizations do to reduce the likelihood of conflict?
5. What do you consider to be the most important ethical and moral questions that relate to the use of drones, cyber weapons, and nuclear weapons?

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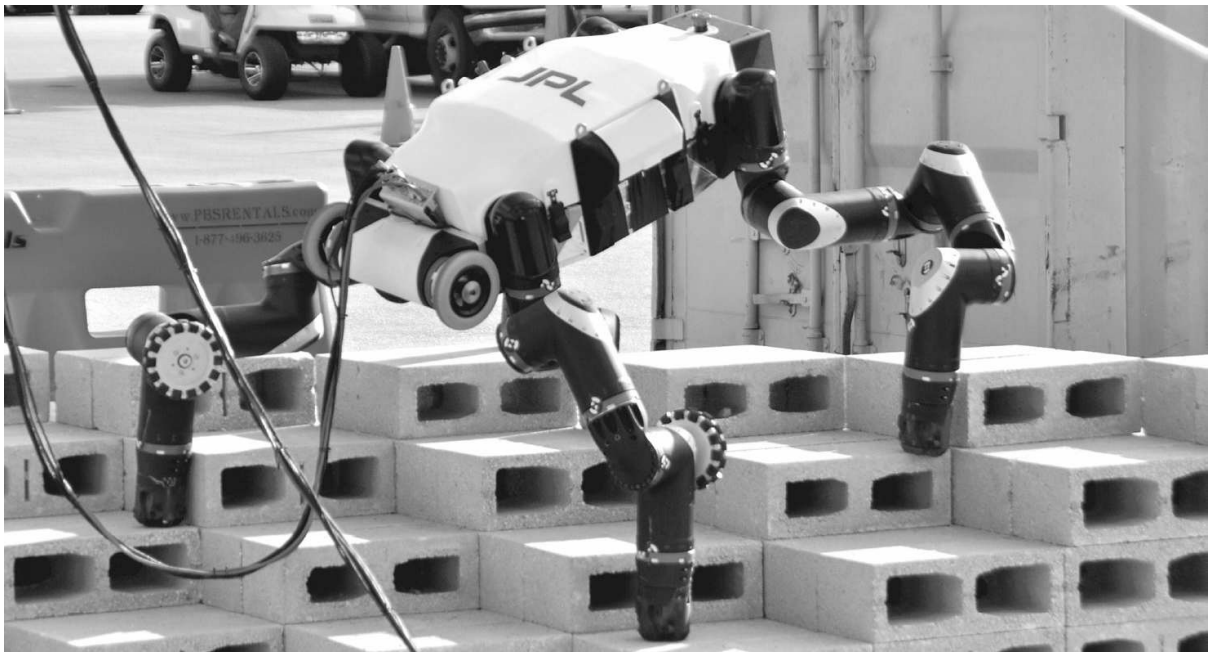
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CHAPTER
10
The International Knowledge Structure: Controlling Flows of Information and Technology



The Florida DARPA Robotics Challenge.

Source: AP Photo/Yomiuri Shimbun/Tatsuo Nakajima.

> *He who receives an idea from me, receives instruction himself without lessening mine; as he who lights his taper at mine, receives light without darkening me.*
>
> Thomas Jefferson[1]

As an intelligence contractor working at the National Security Agency (NSA), Edward Snowden downloaded an estimated 1.5 million secret documents and, after fleeing the United States in May 2013, began sharing them with journalists. Newspaper reports based on the documents revealed, among other things, that the NSA collects vast amounts of data on phone and Internet activities of Americans and foreigners, spies on the leaders of close U.S. allies, and taps into a large proportion of the world's information and communications infrastructure. If it is true that knowledge is power, then the information scooped up by the NSA surveillance system gives the United States an unparalleled

advantage in global security and commercial affairs. At the same time, the Snowden affair demonstrates how the digital revolution makes it hard for governments to prevent the theft and dissemination of large amounts of sensitive information. Other high-stakes global struggles over knowledge are shaping the future of competition, freedom, and security.

This chapter examines the rules and institutions that determine who generates, distributes, and benefits from knowledge. In the first section, we identify key actors and issues in the international knowledge structure. Next, we discuss how states and corporations work within it to control information flows, generate technological advances, and attract highly trained workers. In the second half of the chapter, the focus turns to intellectual property rights (IPRs) such as patents, copyrights, and trademarks that regulate use of inventions and creative works. We contrast different perspectives on whether or not the system of IPRs is fair and beneficial to most countries and citizens. We also discuss international agreements regulating IPRs.

We posit that there are four important trends in the knowledge structure that will affect countries in unsettling and potentially liberating ways:

- Knowledge and technology are becoming important determinants of power. Economic success and military might are less dependent on control of land or natural resources and much more based on human capital in such areas as engineering, information and communication systems, and basic scientific research.
- Given the pace of technological change, profits in the global economy are shifting to those who own knowledge and control the *distribution* of knowledge-intensive goods and services.
- Governments often try to limit many kinds of cross-border information flows and use subsidies, selective protectionism, and intellectual property laws to decisively affect who benefits from interconnected knowledge.
- There are growing tensions globally between owners of IPRs and individuals who believe that many forms of knowledge should be in the public domain. International intellectual property rules that ignore social demands for low-cost and easily accessible music, software, movies, medicines, and technology will be hard to enforce.

THE INTERNATIONAL KNOWLEDGE STRUCTURE: ACTORS AND RULES

The international knowledge structure is a web of rules and practices determining how knowledge is generated, commercialized, and controlled. *Knowledge* is an umbrella term we apply to many different things, including information, technology, and intellectual property. Information is data that people produce, share, and recombine to serve economic, cultural, and political goals. Technology is scientific knowledge used to produce goods and services. Intellectual property consists of inventions, artistic works, and symbols that governments have granted monopoly rights to for limited periods.

As you can imagine, rules governing flows of knowledge create rights, incentives, and prohibitions. Powerful states and multinational corporations create these rules and seek to convince the rest of the world of their legitimacy. At the same time, many social forces resist knowledge controls through political action and lobbying—and sometimes they are willing to defy laws to get what they believe is their due. Rules that we look at include national laws governing information and control of data; bilateral and multilateral agreements that determine what obligations a state has to protect the intellectual property of other countries; and shared norms about the moral obligations of producers and consumers of knowledge.

Individuals navigate the knowledge structure to educate themselves, enjoy entertainment products, and engage in political action. They tend to view relatively unrestricted access to knowledge as a basic human right. As profit-making entities, companies are keen to commercialize the knowledge they produce, and they constantly need new technology to compete successfully. States want to foster their own technological development and force other states to comply with certain rules. At the global level, international organizations teach countries how to cooperate with one another over knowledge and enforce negotiated rules. Many NGOs are also trying to change the rules to better serve the interests of the poor and the oppressed.

The international knowledge structure affects production, trade, finance, and security. For example, the high costs of the arms race, which was also a technology race, contributed to the pressures that brought the Cold War to an end in the late 1980s, Advances in information and communications technology (ICT) have made it more difficult to regulate the global financial system. The race to develop new energy technologies will determine which countries dominate production of electric cars. Clearly, nations and transnational corporations that want to win—or just hold their own—in the game of global competition will have to gain access to the best technology.

THE IPE OF INFORMATION

The digital revolution has profoundly increased the quantity of information and the ease with which it is disseminated. Information can both empower and disempower. Governments can use it to police society. Corporations extract it from people to make profit. Citizens can hold elites accountable with it. Many struggles over information play out in the global arena.

State Efforts to Control Information Flows

Social media has opened up new forms of national and cross-border communication. Its political power became clear during the Arab Spring in early 2011. Internet access and widespread cell phone ownership allowed millions of Egyptians to share information via Facebook and text messaging. The regime of Hosni Mubarak was so desperate to counteract social media that it shut down mobile phone and Internet services for a week.[2] Opposition forces in Syria have posted many YouTube videos online that have been picked up by international news media. The shaky videos and photos from cell phones have revealed regime abuses and made martyrs out of ordinary people. The ability to use social media has weakened authoritarian regimes' information monopolies and sustained on-the-ground political activism. Western governments also find it harder not to respond to the outrage of their own citizens who can gain up-to-the-minute information from social media and satellite television.

Regimes have fought back by using advances in technology to control and suppress information. China has built the "Great Firewall" to filter access to foreign social media platforms and politically sensitive information on the Internet. Police and intelligence agencies extensively wiretap cell phones and monitor communications infrastructures. In countries like Russia and Iran, governments use legal sanctions and harassment of journalists to restrict private television and newspaper companies. Even governments in democratic countries often punish whistle-blowers and leakers of classified information (see Box 10.1).

WIKILEAKS

If you want an unvarnished, behind-the-scenes look at the conduct of war, diplomacy, and foreign policy, you might want to peruse some of the millions of secret documents released by Wild Leaks. Your faith in humanity and the moral uprightness of your country might be shaken. You can watch a video of a U.S. Apache helicopter gunship mowing down over a dozen unarmed civilians in Baghdad in 2007.[a] You can read Hillary Clinton's assessment that donors in Saudi Arabia—a close ally of the United States—are the "most significant source of funding to Sunni terrorist groups worldwide."[b] You can find that the International Committee of the Red Cross uncovered evidence of widespread ill treatment and torture of Kashmiri prisoners by Indian security forces in the first half of the 2000s, leading it to conclude that the Government of India condones torture.[c] You can examine U.S. military documents revealing widespread human rights abuses by Iraqi forces that the United States failed to investigate and numerous incidents of American troops killing Afghani civilians.[d] You can peruse thousands of files documenting commercial transactions between Western companies and many of the most repressive governments in the world.[e]

The guiding force behind WildLeaks is Julian Assange, a brash Australian committed to increasing government transparency and uncovering conspiracies of the powerful. He has taken it upon himself to de-naturalize government narratives about foreign affairs. Relying on a network of volunteers and whistleblowers to provide his organization secret documents, he publishes them digitally through servers in many different countries to prevent any particular state from suppressing access to them. At the height of his influence between 2009 and 2012, Assange published hundreds of thousands of U.S. military documents and diplomatic cables dating back almost a decade that U.S. soldier Chelsea Manning had leaked and thousands of sensitive documents and emails from private companies, politicians, the United Nations, and the Syrian government.

In a relentless effort to undermine Wild Leaks, the U.S. government successfully pressured Pay Pal, Visa, Mastercard, and U.S. banks to stop processing supporters' donations to it. After being accused of rape and sexual molestation in Sweden, Assange moved to Great Britain. When a court ordered him extradited, he fled to the Ecuadorian embassy in London, where he has lived since 2012. However, that did not stop Wild Leaks from publishing many more documents. In 2016 it released thousands of emails—many of which were embarrassing—hacked from the Democratic National Committee and John Podesta, Hilary Clinton's campaign manager. Clinton partially blames WildLeaks for her loss in the U.S. presidential election.[f] In 2017 Wild Leaks released thousands of documents from the CIA detailing how it hacks computers and smart devices and installs malware on

networked devices.

Wild Leaks' exploits demonstrate the ability of a small group of cyberactivists and whistleblowers to use digital technology to easily spread unprecedented amounts of sensitive information that threaten a country's national security, undermine a TNC's reputation, or potentially endanger the lives of individuals. WildLeaks bypasses mainstream journalists to propagate information in the service of explicit political agendas. It has shown the increasing difficulty states have in controlling information and exercising their traditional sovereign powers in cyberspace. It reminds us of the abuses of government power and the conniving of private interests that classical liberals since Adam Smith have warned us about.

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Democratic and authoritarian regimes are also installing ever more futuristic surveillance systems, not just to prevent crime but to monitor communications of citizens, gather overseas intelligence, and enhance border control. Documents leaked by Edward Snowden show that the NSA has sophisticated tools to electronically gather information from smart devices, computers, undersea cables, and Internet systems around the world. China and Russia are also skilled at overseas cyber espionage directed at both governments and corporations. Although states have not agreed to any treaties prohibiting the common practice of cyber hacking for intelligence gathering, in 2015 the G20 countries pledged not to conduct commercial cyber espionage, including theft of intellectual property and trade secrets. Nevertheless, agreements like this and bilateral pledges not to hack are not enforceable.

The traditional method for states to influence people in other countries is through the dissemination of propaganda. Since 2005, the Russian government has funded a Kremlin-friendly international television network called Russia Today (RT). Alongside this channel are state-owned European broadcasters such as Britain's BBC and Germany's Deutsche Welle.

Recently, "fake news" has emerged as a worrisome form of propaganda. Many politicians around the world, most notably Donald Trump, try to discredit critical (but fact-checked) reporting by mainstream news outlets by calling it fake news. However, a more insidious kind of fake news comes from governments that spread fabricated or misleading stories via social media and non-mainstream websites, seeking to alter political outcomes in other countries. Fake news is appealing to those who do not trust mainstream institutions; unfortunately, to the extent that that the world is entering an era of post-truth politics, many people judge the "veracity" of information based on its conformity with their partisan leanings or personal beliefs.

Although many governments conduct disinformation campaigns, Russia is one of the most sophisticated operators. For many years it has waged "information warfare" against ex-Soviet republics such as Ukraine. Its sophisticated campaign in 2016 weakened support for

candidate Hilary Clinton and helped Donald Trump. Russia and Russian-linked groups spread disinformation to foment anti-immigrant sentiment in Germany. More generally, some believe that fake news is to undermine democratic institutions in the West.

It is difficult to pinpoint the state initiators of fake news and equally hard to counteract it without threatening the principle of free speech. Many countries have laws penalizing those who spread false information, but they are of little use against foreign adversaries. It seems unlikely that there will be much international cooperation to combat fake news in cyberspace. Some Western governments have pressured Facebook and other media companies to filter out false and inflammatory information from their networks, but authoritarian regimes have done the same as a means of political censorship.

Alongside the "offensive" state uses of information are more "defensive" government policies. The Snowden revelations have induced more states to invoke the norm of information sovereignty—that is, the right to control flows of information into and within their country. Many Western countries criticize information sovereignty as protectionist and in conflict with the "freedom to connect," while its defenders believe that it preserves national security and protects consumers. A prominent example of information sovereignty is data localization, a government requirement that companies store and process all information on a country's citizens within that country. This means that TNCs and providers of cloud-based services cannot centralize information from their global customers or easily move it across borders; instead, they have to host data from individual countries on local servers in those countries. For example, the provinces of British Columbia and Nova Scotia in Canada require that any personal data collected by public bodies, such as health care agencies and public universities, must be stored in Canada. Russia, China, India, and some other countries have much stronger localization requirements.

In contrast, the United States argues that information should be treated as a neutral commodity subject to free trade so that there is economic efficiency. Shawn Powers and Michael Jablonski argue that U.S. promotion of free flows of information serves U.S. economic and geopolitical interests, particularly because American corporations are already dominant in cyberspace and digital services.[3] Cloud-based computing, digital entertainment, and online retailing are some of the fastest-growing and valuable services exports for developed countries. In 2015 the United States had a surplus in trade of digital and digitally enabled services of $166 billion, mostly from providing financial services and licensing intellectual property.[4] In negotiations with other countries over new trade agreements, the U.S. Trade Representative has tried to prevent any barriers to digital trade. For example, it insisted that the Trans-Pacific Partnership prohibit data localization requirements (with some exceptions) and customs duties on digital imports such as online games and videos.

Many Europeans resent the hegemony of American tech giants such as Google, Apple, Facebook, and Amazon (GAFA), whom they accuse of engaging in anti-competitive behavior and failing to respect consumers' privacy. China has worked diligently to build domestic alternatives to GAFA, in part to capture some of the enormous profits that would otherwise go to foreign companies and to nurture its own technological development. Like

many other countries, it has reason to worry that reliance on software, hardware, and online services from U.S. tech companies makes it vulnerable to U.S. spying. By 2017, domestic company Baidu controlled more than 75 percent of China's search engine market, and Chinese company Alibaba controlled more than half of China's e-commerce market. Google and Amazon have basically lost the Chinese market.

For most countries, the battle between information sovereignty and unfettered information flows has high stakes. Online services are fast-growing in developed and emerging economies. Perhaps even more importantly, the Internet of Things (IoT) revolution is in progress. Soon many everyday objects around us—like cars, refrigerators, and houses—will have networked sensors sending out valuable information about us. Governments will inevitably need to establish rules that determine who gets to collect, store, process, and sell this "big data". As they do so, they will face conflicting interests: local vs, foreign companies, businesses vs, consumers, and surveillance vs. privacy.

Information in the Hands of Private Actors

The digital revolution also allows private corporations to gather unprecedented amounts of consumer data that can be used in ways contrary to the public interest. Struggles between states and TNCs over how this information is used are part of a wider battle over regulation of the market. Many governments worry that private control of technology can lead to anti-competitive behavior, threats to privacy, and concentrations of power. For example, the European Commission has spearheaded efforts to prevent Microsoft from abusing its control over computer software and to force Facebook to protect users' personal data. Different legal obligations and cultural expectations across countries make it difficult to create global standards. Some states try to harness the power of their information-technology companies to hurt rivals overseas. For example, U.S. politicians in October 2012 accused two Chinese companies, Huawei Technologies and ZTE, which supply equipment used in telecommunications and mobile phone networks, of being threats to U.S. national security because the Chinese government might use them to steal intellectual property from U.S. companies and conduct cyberwar-fare in the event of a conflict.[5]

Structuralists John Bellamy Foster and Robert McChesney worry that corporations have crushed the liberating potential of the communications revolution, turning the Internet into an oligopolistic sphere from which they can extract exorbitant profits and threaten democracy.[6] Thrown by the global wayside are net neutrality, quality journalism, and the public domain. Similarly, Shoshana Zuboff has coined the term "surveillance capitalism" to describe a vast networked system for extracting data about all aspects of people's lives and turning that data into corporate profits.[7] The data come from IoT devices, government records, online transactions, and "digital exhaust" from all online activity. Because there are few rules regulating surveillance capitalism, it replaces public oversight with private corporate authority.

Equally troubling is how corporations and states work hand in glove to enable greater state surveillance. Canadian political scientist Ron Deibert critiques tech companies for

supplying information and information-gathering tools to governments that use them to censor civil society and violate human rights: "Products that provide advanced deep packet inspection, … content filtering, social network mining, cellphone tracking, and even computer attack targeting are being developed by Western firms and marketed worldwide to regimes seeking to limit democratic participation, isolate and identify opposition, and infiltrate meddlesome adversaries abroad."[8]

However, global civil society is fighting back. Some groups are promoting new privacy norms that would prevent companies from gathering certain kinds of customer data. Others seek to weaken intellectual property rights and make the results of all government-sponsored research freely available. There are even efforts to force companies to allow interoperability of their products with those of rivals to strengthen competition. Jennifer Shkabatur points out that new information technologies allow international organizations (IOs) to more easily monitor states' compliance with their international obligations to protect the environment, public health, and human rights.[9] This might increase pressure on states to be more transparent and accountable.

THE IPE OF INNOVATION AND TECHNOLOGY ADVANCEMENT

In this section we examine how countries try to foster innovation and turn knowledge into comparative advantage in the global economy. We find states playing a surprisingly large role in coordination of research and development (R&D) with market actors. Some developing countries are closing the knowledge gap with wealthier countries while gaining a bigger share of global production, but the United States and the European Union are fighting hard to continue attracting the world's most highly skilled workers.

A key historical and theoretical question is this: What have been the appropriate roles for governments and market actors in fostering innovation? A growing number of political economists such as Joseph Stiglitz, Ha-Joon Chang, and Dani Rodrik believe that states need flexibility to craft policies in sync with their particular national needs. With regard to knowledge governance, they argue that one size does not fit all. Some states try to substitute for the private sector in research and development, some partner with it in a variety of ways, and some simply clear away obstacles in the way of private innovators. Most states want to nurture those who turn technological innovations into lucrative exports. Some major powers are willing to spread knowledge around the world by educating foreigners in their universities and encouraging outsourcing by their TNCs. But at the same time many nations are intent on staying one step ahead of rivals in innovative fields, including military technologies.

Government Innovation Policies in Developed Countries

Technologically advanced countries are playing a game of global "keep-up," not "catch-up." They want to stay competitive in knowledge-based industries and nurture "creative industries," where value added per worker is high and positive spillovers into other sectors of the economy are great. Some of these signature industries include telecommunications, biotechnology, health care, and defense. Innovation is often premised on political openness, vast educational opportunities, labor mobility, and other characteristics that only a limited number of countries can quickly turn to their advantage.

These nations recognize that technological progress is a key determinant of economic growth. Although today private companies account for the majority of investments in research and development, governments nurture innovation through public spending, subsidies, and intellectual property rights (discussed later in this chapter). Many states historically have built technology infrastructures, especially in times of national emergency or interstate rivalry. For example, in the nineteenth century the U.S. government founded land-grant colleges throughout the country to spur transformation in agriculture, industry, and engineering. Massive investment in the Manhattan Project during World War II gave the United States superiority in nuclear technology. As part of its political rivalry with the Soviet Union during the Cold War, the United States boosted its leadership in space

technology via the Apollo Project and military spending on satellite systems. From 1990 to 2003, the U.S. Department of Energy and the National Institutes of Health funded the Human Genome Project, which has produced major benefits for commercial innovation in molecular medicine and the life sciences industries.

Governments often identify new R&D needs and provide resources for huge leaps forward in areas such as energy and medical research. This can be done by direct funding to universities, government research labs, and private companies. Sociologist Henry Etzkowitz stresses how this funding can produce a triple helix—a university–industry–government relationship that accelerates innovation.[10] For example, the Bayh-Dole Act of 1980 gave U.S. universities and federal labs the right to patent inventions funded with public money and license the patents to private companies. Examples of government-assisted innovation in U.S. universities include Google online searching (hatched at Stanford University) and storm-tracking radar (developed at MIT).

Innovation scholar Mariana Mazzucato has made some of the most forceful arguments about the critical role of the state in fostering innovation.[11] She believes that public investments in research have been the source of some of the most important technological breakthroughs since the 1950s in fields such as computing, aviation, biotechnology, green energy, and nanotechnology. States often take on the role of entrepreneur, channeling government spending, venture capital, and loans into visionary projects with high risks but potentially long-term gains for society. For example, in 1958 the U.S. government created an agency within the Department of Defense called the U.S. Defense Advanced Research Projects Agency (DARPA) to finance research by industries and universities into technology of use to the military. Technological spin-offs from its continuing sponsorship of research include the Internet, virtual memory, computer networking, integrated circuit design, and voice-to-text software.

After World War II, the U.S. federal government funded about two-thirds of all U.S. R&D, but in recent years this has declined to only one-fourth as private industry has boosted its own investment. In the EU countries, government funds one-third of all R&D, while in Russia the government accounts for a full 70 percent of all R&D. For more than fifty years, the United States has led the world in overall combined government-private R&D. In 2013, it accounted for 27 percent of global R&D spending, compared to 20 percent by China, 10 percent by Japan, and 6 percent by Germany (adjusted for PPP).[12] (See Figure 10.1.)

To gain a sense of how committed a country is to future innovation, we can also measure the ratio of its R&D spending to GDP (see Figure 10.2). The United States' robust ratio of 2.8 percent in 2015 lagged behind Japan's 3.3 percent but was much higher than the EU's 2 percent. Notably, the Chinese and South Korean governments have devoted extraordinary amounts of money to technological advancement. China's R&D spending rose from just 0.9 percent of GDP in 2000 to 2.1 percent in 2015, while Korea's rose from 2.3 to 4.2 percent. The United States is losing its large technological lead over China, as technological dynamism continues to shift to the East Asian region. R&D has become more internationalized since the 1990s, with TNCs shifting some of it to countries like

China and India with large markets and large pools of skilled, lower-cost researchers.

Mazzucato laments that although governments bear much of the risk when funding basic research, private companies reap all the profits by commercializing products derived from this research. Like many others, she argues that large state-funded R&D will be vital to developing green technologies to head off catastrophic climate change; already about 50 percent of R&D spending on renewable energy around the world comes from public agencies.[13]

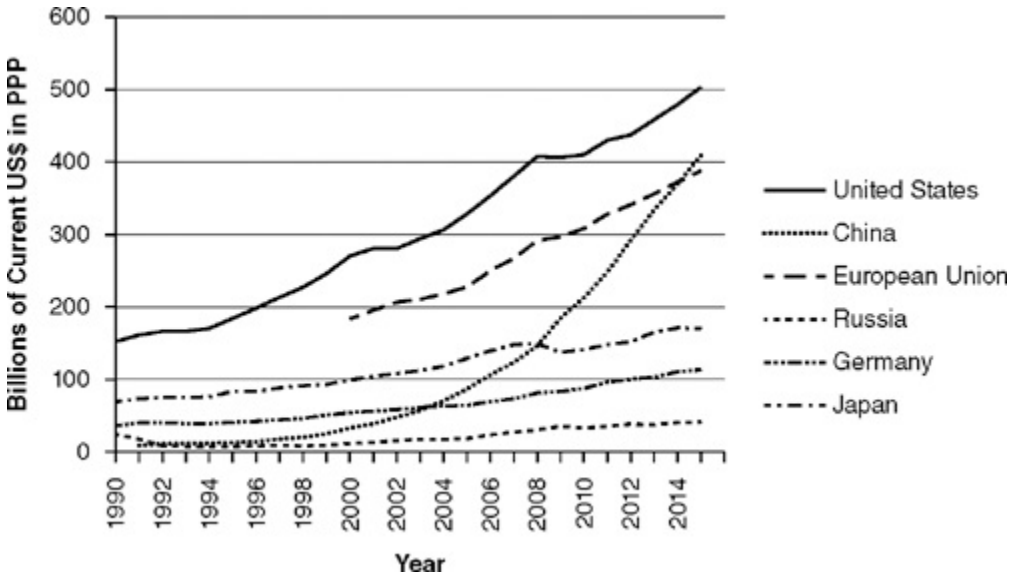


FIGURE 10.1
Domestic Expenditures on Research and Development for Selected Countries and the European Union, 1990–2015.

Source: Data from Organisation for Economic Co-operation and Development, Main Science and Technology Indicators, OECD.stat.

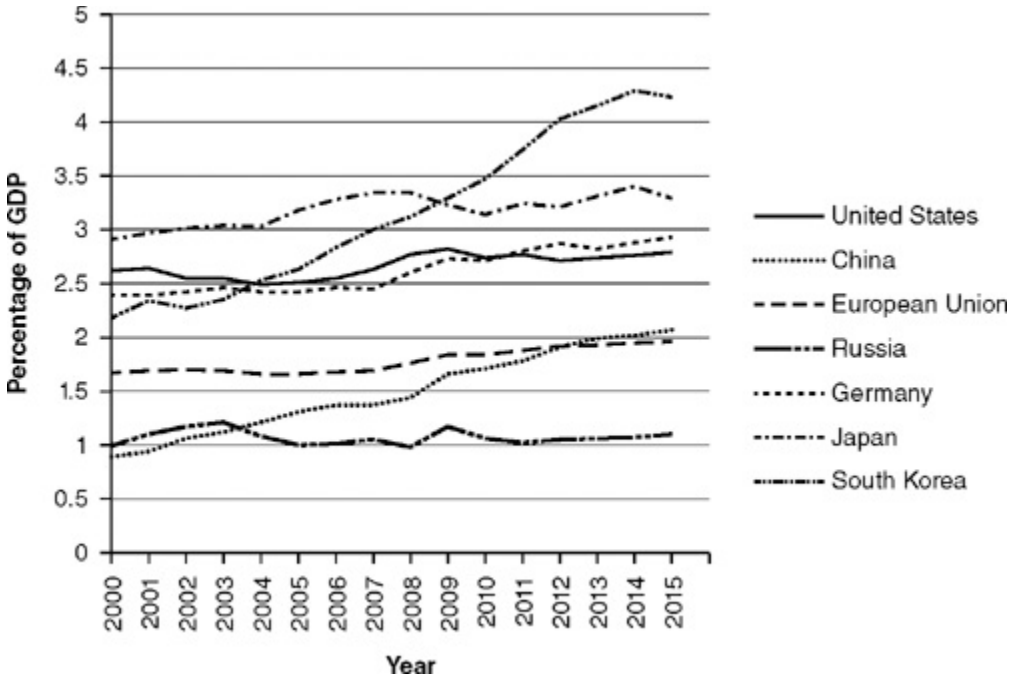


FIGURE 10.2
Domestic Expenditures on Research and Development as a Percentage of GDP for Selected Countries and the European Union, 2000–2015.

Source: Data from Organisation for Economic Co-operation and Development, Main Science and Technology Indicators, OECD.stat.

Italian economists Daniele Archibugi and Andrea Filippetti also warn that the increasing "privatization of research activity and knowledge" might lower long-term growth and innovation.[14] OECD countries now rely on the private sector for more than two-thirds of R&D spending. Archibugi and Filippetti argue that private companies often avoid basic research that leads to radical breakthroughs, focus on profitability instead of crucial social needs, and slow down knowledge sharing with patents and trade secrets. Many scholars also argue that the "financialization" of developed economies is hurting technological innovation (see Box 10.2).

THE EFFECTS OF FINANCIALIZATION ON INNOVATION

An important focus of recent structuralist and mercantilist literature is financialization, a process of accumulation whereby pursuit of financial gains causes companies to neglect production and reinvestment in technological innovation. Capitalist elites in advanced economies have become more like a rentier class, making money with money (often borrowed money) and shifting investments out of the "real economy."

In the last few decades, U.S. corporations have distributed a large proportion of their profits to shareholders through dividends and stock buybacks, leaving less to invest in long-term productive activity. This trend is influenced by the emergence of "shareholder value theory" which sees the main purpose of corporations as maximizing returns to shareholders. Scholars Mariana Mazzucato and William Lazonick argue that this has negative long-term effects on corporate profitability, national innovation, and national competitiveness.[a]

Similarly, Rana Foroohar, a global business columnist at the *Financial Times*, blames the decline of the U.S. economy on financialization.[b] Corporations cut spending on research while taking on debt and distributing profits to top management and shareholders rather than investing in their companies or paying workers more. Foroohar asserts that management is focused more on boosting short-term profits and "shareholder value" than building better products.[c] Iconic American companies such as Ford, GM, HP, and Xerox went into decline after penny-pinching to please Wall Street. Giants such as GE, Kodak, and BP relied on financial engineering to meet quarterly earnings, becoming more like banks than manufacturers. Garnering profits from trading in derivatives and lending money to customers and other businesses, they turned from "makers" into "takers," says Foroohar, losing market share to foreign corporations.

In the present era, U.S. corporate investment in worker training and human capital is a much lower priority. Research and development (R&D) is more likely to be outsourced than done internally; it is less risky to buy up small companies that have already developed promising technology. Stock buybacks tend to drive up share prices, rewarding remaining shareholders and executives with stock options. Another practice of "impatient" investors, especially private equity funds, is to "asset strip"—that is, sell off parts of corporations or load them with debt until they go into bankruptcy. Stripping R&D divisions can undermine a company's ability to develop new technologies.

A Reuters investigation in 2015 found evidence of significantly increased stock buybacks by U.S.-based TNCs. In a sample of 1,900 companies, share buybacks and

dividends as a percentage of capital spending rose from 38 percent in 1990 to 113 percent since 2010.[d] Companies that buy back shares (which was prohibited before 1982) spend less than 50 percent of their net income on R&D today, compared to more than 60 percent in the 1990s. Corporations often borrow money to finance stock repurchases, thus driving up their debt and increasing pressure to cut costs by shrinking their workforce and reducing R&D. Reuters also finds that between 2009 and 2015, non-financial U.S. corporations borrowed $1.9 trillion to help pay for $2.2 trillion in stock buybacks.[e] Serving the short-term interests of big investors and corporate managers may come at the expense of the economy's long-term health.

A key question is whether governments should incentivize corporations to channel profits into more productive uses. In some recent instances, corporations have laid off thousands of workers while buying back billions of dollars' worth of their own shares. Economic liberals believe that decisions on profit use should be left to market actors, while economic nationalists countenance a role for government in pursuit of what it considers the public interest. Inequality would fall and workers would benefit more if profits were reinvested in R&D, capital spending, and higher wages. Foroohar, Mazzucato, and Lazonick reflect the thinking of Friedrich List in stressing the importance of manufacturing and re-investing for long-term growth.

References

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[b] Rana Foroohar, *Makers and Takers: The Rise of Finance and the Fall of American Business*, 1st ed. (New York: Crown, 2016).

[c] Rana Foroohar, *Makers and Takers: The Rise of Finance and the Fall of American Business*, 1st ed. (New York: Crown, 2016), p. 69.

[d] Karen Brettell, David Gaffen, and David Rohde, "As Stock Buybacks Reach Historic Levels, Signs That Corporate America Is Undermining Itself," *Reuters*, November 16, 2015, at www.reuters.com/investigates/special-report/usa-buybacks-cannibalized.

[e] Karen Brettell and Timothy Aeppel, "Buybacks Fueled by Cheap Credit Leave Workers out of the Equations," *Reuters*, December 23, 2015. www.reuters.com/investigates/special-report/usa-buybacks-workers/.

Governments foster technological progress in many other ways than just R&D spending. Scholars Jakob Edler and Luke Georghiou argue that public procurement has been an important means by which governments generate demand for innovative products.[15] Tax rebates to consumers and businesses that purchase innovative products also encourage faster commercialization of the products. Since 2004, Germany has accelerated development of renewable energies by guaranteeing to producers of solar and wind power an above-market price for the energy they contribute to the electricity grid. Japan adopted a similar pricing system in 2012 to spread renewable energy sources after the Fukushima disaster caused the shuttering of nuclear power plants.

In addition to fostering innovation, developed states seek to prevent the diffusion of some forms of advanced technology to other countries. During the Cold War, the United States forbade the export of weapons systems (and information related to them), nuclear technology, and dual-use technologies to the Soviet Union. It also established deemed export controls that limit the transfer of export-controlled items or protected technical information to foreigners working or studying in the United States. Universities and private contractors have to obtain licenses to allow foreigners to access this information.

By requiring licenses and approvals for certain lists of exports, the United States has tried to limit technology transfer to its rivals. When sharing advanced technology with close allies like Japan, Britain, and Germany, the United States has sought to ensure that they also restrict its re-export. This requires close multilateral cooperation, especially among NATO members, to harmonize all their export controls.

In recent years the Committee on Foreign Investments in the United States (CFIUS), an inter-agency group that vets proposed foreign investments in the United States for potential national security risks, has nixed some Chinese purchases of U.S. companies. In 2016 it rejected an effort by Chinese investors to buy LED lighting company Lumileds,

which was later taken over by a U.S. private equity fund. CFIUS was apparently concerned that the sale would give China access to technology about a material called gallium nitride that can be used to make advanced microchips with military applications. In the same year, efforts by Chinese companies to buy U.S. chip maker Fairchild Semiconductor and part of hard-drive manufacturer Western Digital fell through because of expected rejection by CFIUS. The U.S. impulse is to use national security as a pretext for "defensive" mercantilism. It should be noted, however, that China also uses similar national security arguments. After Edwards Snowden leaked documents about NSA surveillance, China began pressuring banks, SOEs, and state institutions to replace foreign-made computer software and servers with Chinese-made ones.[16]

However, geopolitical and economic changes since 1990 have weakened the West's technological oligopoly. As French political scientist Hugo Meijer argues, since the collapse of the Soviet Union, the United States has much less control over transfers of dual-use technologies to China. He identifies four main factors causing this trend: "the weakening of the multilateral institution governing export controls, the commercialization and global diffusion of technology, China's growing indigenous capabilities, and the domestic pressures to liberalize export controls that resulted from the thickening of Sino-American economic relations."[17] Private companies on the cutting edge of information, communications, and satellite technologies need to find export markets for dual-use products in order to remain profitable. Export controls hamper their ability to compete globally. According to Meijer, in the trade-off between economic interests and national security, the U.S. lobby promoting exports of dual-use technology is beating out the lobby of "Control Hawks."

Closing the Knowledge and Technology Gap

Economist Joseph Schumpeter (1883–1950) believed that only firms with some degree of monopoly power would likely have the *incentive* and the *ability* (in the form of monopoly profits) to invest in risky, expensive, and long-term R&D projects. Thus, he contended that many industries were likely to be monopolistically structured. However, over time, technologically audacious newcomers would displace once-dominant firms. "Gales of creative destruction," he predicted, would destroy established monopolies and create new dominant firms.

Because of economies of scale, competition in many industries today is not for market share but for the market itself. Competition is a "winner take all" or at least a "winner take most" proposition, as Schumpeter expected. This reality has obvious political-economic implications. Mercantilist-minded policy makers will put in place industrial policies to foster the development of national champions that dominate high-tech industries. Even liberal-minded policy makers recognize the importance of creating conditions that will promote entrepreneurs capable of competing in knowledge industries—conditions described in Michael Porter's bestseller *The Competitive Advantage of Nations*.[18] The ability to acquire, create, and control technology has become central to international competition

in the twenty-first century.

Even if countries cannot expect to have globally dominant firms, they seek to advance technologically in global value chains, which account for "the full range of activities that firms and workers do to bring a product from its conception to its end use and beyond."[19] As we discussed in Chapter 7, many firms are linked in a global division of labor in which Western firms engage in high-knowledge functions such as finance, basic research, design, and marketing, while developing countries perform low-value functions such as low-wage manufacturing and raw materials processing. LDCs want to move up the value chain to more profitable activities, but to do so they need to close the technology gap with developed countries by acquiring know-how.

Taiwan and South Korea have followed Japan's example for how to move up the value chain by creating national champions through deliberate industrial policy and strategic trade policies. Their companies moved from manufacturing or assembling parts to developing technology and designing products. Finally, they became leaders in some industries, accumulating patents and controlling their own brands.

China is following the Japanese and Korean models of creating national champions. In 2015 President Xi announced an ambitious "Made in China 2025" program designed to turn China into a technological powerhouse in industries such as aviation, robotics, semiconductors, and electric vehicles. It encourages national companies to conduct more R&D and buy overseas high-tech assets. Foreign companies complain that the "Made in China 2025" initiative is protectionist because it unfairly gives preferential treatment to Chinese companies in government finance and procurement.

Struggles over Education and Skilled Workers

Innovative societies require more than just good institutions and R&D spending; they also need well-educated workers and skilled professionals. Over the long term, they must teach their own citizens the skills needed in knowledge-intensive industries. Not only is it the percentage of students in higher education that counts, but also what they study, how well they learn, and their financial condition at the time of graduation. Struggles over knowledge embodied in people extend to higher education and visa policies.

Labor mobility is a critical contributor to an innovative society, particularly the ability of individuals to move from one company to another and to set up new businesses. Economists and geographers have found significant innovation in regional high-tech clusters with high labor mobility like Silicon Valley and North Carolina's Research Triangle. Similarly, innovation is spurred by in-migration from other countries, that is, international labor mobility.

Countries seek to attract gifted foreign students to their institutions of higher education. The United States, Canada, and the United Kingdom are top competitors, doubling their foreign student populations since 2000 (see Figure 10.3). However, the United Kingdom's enrollments have plateaued since 2010 and may fall precipitously after Brexit. In 2016–2017, there were nearly 1,079,00 foreign students in American universities, nearly double

the number ten years earlier.[20] Almost 60 percent of these students came from the top four sending countries: China, India, Saudi Arabia, and South Korea. More than half were studying business, engineering, and math and computer science. Foreign students make up a vital percentage of all students in graduate programs in the United States. They earned more than one-third of PhDs in science and engineering fields in 2013 and more than half of all doctorates in engineering, economics, and computer sciences.[21]

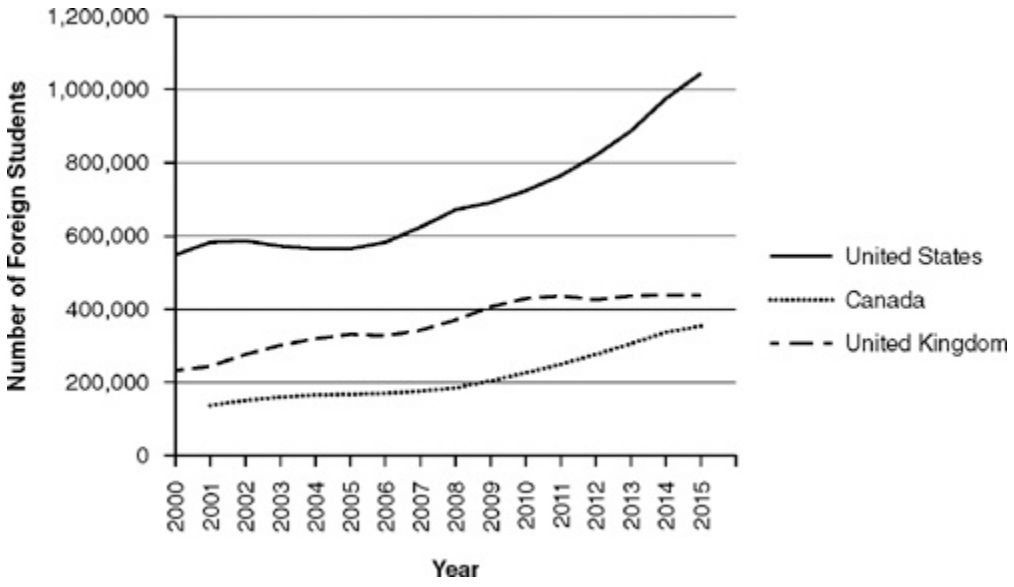


FIGURE 10.3
Foreign Students Studying in the United States, Canada, and the United Kingdom, 2000–2015.

Sources: Data from "A World of Learning: Canada's Performance and Potential in International Education," Canadian Bureau for International Education (2013, 2016); Institute of International Education, www.iie.org/Research-and-Insights/Open-Doors/Data/International-Students/Enrollment-Trends; and Higher Education Statistics Agency (HESA), at https://institutions.ukcisa.org.uk/Info-for-universities-colleges--schools/Policy-research--statistics/Research--statistics/International-students-in-UK-HE/.

The U.S. economy benefits from harnessing the skills of these graduates who remain in the United States and enter the labor force, often with permanent residency. A program called Optional Practical Training allows foreign students to work in the United States for up to a year after graduating (up to three years for STEM majors). The number of OPT approvals soared from roughly 28,000 in 2008 to 137,000 in 2014.[22] In an effort to change views toward immigrants, the U.S. think tank National Foundation for American Policy reported in 2016 that 51 percent of non-publicly traded U.S. startups valued at over $1 billion, including SpaceX and Uber, were founded by an immigrant.[23]

Although anti-immigrant sentiment has grown in the United States and Europe, almost all developed countries still seek to attract high-skilled immigrants. More than ever, they compete fiercely for the world's best scientists, engineers, entrepreneurs, and other professionals. However, in the race for global talent, English-speaking countries are the

undisputed winners. By 2010, the United States, the United Kingdom, Canada, and Australia had absorbed 70 percent of all high-skilled immigrants that moved to OECD countries.[24] India, China, and the Philippines have been the largest exporters of skilled immigrants. In their visa policies, many developed countries are making immigration easier for highly educated workers and harder for those with low skills. For example, from 2011 to 2015 nearly half of all immigrants to the United States were college graduates, compared to only 27 percent from 1986 to 1990.[25]

The United States' H1-B work visa program has become highly politicized, as U.S. tech industries, which benefit the most from it, complain that the U.S. government does not issue enough H1-Bs, while critics complain that it allows companies to replace U.S. tech workers with much cheaper foreigners. The signature European Union program to attract highly skilled immigrants is based on a 2009 Directive on Highly Qualified Workers that offers relatively easy access to a work permit called a "Blue Card." After its Brexit vote, Britain is facing the prospect, according to some estimates, of eventually losing half of its EU immigrants with graduate degrees who currently work in areas such as finance and health care. While visa policies are important, there are many other factors that determine a country's attractiveness to global talent, including low taxes, startup culture, high salaries, and world-class universities.

Developed countries also face competition from emerging economies—especially China, India, and South Korea—that are convincing more of their students studying abroad to return home after graduation. Their return is a very important mechanism of technology transfer and a way to reverse brain drain. Many are working in startups and new research labs set up by the likes of IBM, GE, and Cisco. Vivek Wadhwa finds that many young, professional Indians and Chinese who studied in the United States see better opportunities for professional advancement at home and a better quality of life and better family values in their native countries than in the United States.[26] This indicates the rising standard of living for the upper classes in Asia's rising powers (see Chapter 13). The "land of opportunity," as the United States likes to call itself, has a lot of new competition.[27]

In recent years, one of the most peculiar ways that countries have tried to attract global talent is by offering citizenship or residency to high-net-worth foreign nationals. So-called economic citizenship programs are attractive to newly wealthy Chinese and Russian businesspeople who want to travel more freely across borders, find a safe haven for assets, and limit their taxes.[28] Many European states see these programs, which resemble historical efforts by states to poach talent from other countries, as easy ways to attract foreign investment and bolster entrepreneurship. In the United States, foreign nationals who invest as little as $500,000 (as of 2016) in projects that create a minimum number of jobs can receive an EB-5 visa entitling them to a "green card" and a potential path to American citizenship. After 2010, many foreign nationals seeking the EB-5 visa pooled their investments in commercial real estate projects such as hotels and apartment complexes. This "cash-for-citizenship" program has been very popular with mainland China investors. Nearly 35,000 Chinese investors received permanent U.S. residency through the program

from 2012 to 2016. Chinese citizens alone were granted 86 percent of all the EB-5 visas in this period. Critics contend that the program has significant fraud and fails to create many jobs.

THE IPE OF INTELLECTUAL PROPERTY RIGHTS

In addition to R&D, technology, and skilled workers, intellectual property rights (IPRs) are a key component of the knowledge structure today. Patents, copyrights, and trademarks are the most important forms of IPRs, but states have also assigned rights to such things as geographical indications, industrial designs, and trade secrets. IPRs are government-granted rights to control—for a limited amount of time—the use of inventions, creative works, and company names and logos. The kinds of things states deem worthy of granting rights to, as well as the strength and length of protection, have varied significantly over the last 200 years. Control of ideas and the products that are associated with them has important effects on innovation and the distribution of wealth.

There are a number of ways in which countries coordinate their IPR policies, such as through the Trade-Related Aspects of Intellectual Property Rights (TRIPS) agreement of the WTO, which requires countries to provide a minimum level of IPR protection and enforcement. However, it is important to remember that individual states define IPRs in different ways that reflect historical differences in their legal traditions and political evolution.

Patents confer the exclusive right to make, use, or sell an invention for a period usually of twenty years (counted from date of filing). Without these rights, many companies would be unable to capture all of the benefits of their R&D expenditures and therefore might not find it worthwhile to invest in innovation. While the criteria for gaining a patent vary from one country to another, usually the invention must be new, useful (have some kind of industrial application), and nonobvious to someone who is skilled in the field. In exchange for the temporary monopoly on the use of the invention, an inventor must disclose the details of it in writing to the public. Companies can make their own patent-protected products, license the use of their patents to others, or even sell their patents.

Countries place many restrictions on patents. For example, EU members do not offer patents for computer programs, methods for treatment of the human body, or inventions whose commercial exploitation conflicts with public policy. And governments will sometimes override patents in times of national emergency such as war.

Patents provide a rough measure of how technologically innovative a country is. Figure 10.4 shows how many patent applications were filed by residents out of every one million of the population in their country in 2015. South Korea and Japan lead the world, followed by Switzerland, the United States, and Germany. China will soon catch up to Germany and the United States, given its explosion in patenting in the last ten years.

Copyrights protect the *expression* of an idea. They are provided to authors of artistic works like books, movies, television programs, music, magazines, photographs—and even software in a growing number of countries. Copyrights generally allow an owner to prevent the unauthorized reproduction and distribution of an original work. The WTO's TRIPS agreement requires members to offer copyright protection that lasts at least the life of the author plus fifty years. In the United States and Europe, protection lasts for the life of the

author plus seventy years—and in the United States corporate works (works for hire) are protected for ninety-five years. Lengths of protection have grown longer in the last 100 years while the value of trade in copyrighted products has mushroomed. Many critics argue that there is no economic justification for copyrights to last so long. In the United States, the major copyright industries—movies, music, book publishing, and software—contribute to about 6.9 percent of overall GDP—more than $1.2 trillion annually.[29]

Governments provide exceptions to copyrights so that we can make use of copyrighted material in certain circumstances without paying or asking permission from the copyright holder. For example, it is considered "fair use" in many countries to reproduce or use a portion of a work for criticism, parody, news reporting, or teaching. Similarly, it is usually legal to reproduce or record a book, song, or TV program for personal, noncommercial use. And under the first sale doctrine, once we purchase a legal physical copy of a copyrighted item, we are free to sell it or rent it to whomever we want.

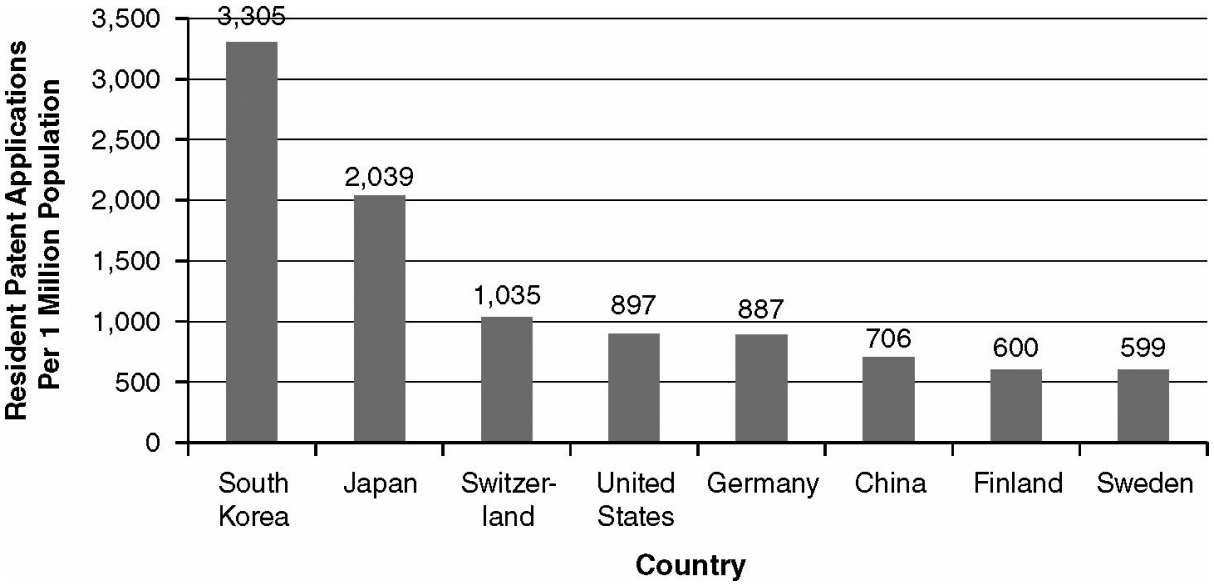


FIGURE 10.4
Resident Patent Applications Out of Every One Million of the Population in Selected Countries, 2015.

Source: Data from World Intellectual Property Organization, *World Intellectual Property Indicators 2016* (Geneva: WIPO, 2016), p. 54, at www.wipo.int/edocs/pubdocs/en/wipo_pub_941_2016.pdf.

Trademarks are signs or symbols (including logos and names) registered by a manufacturer or merchant to identify its goods and services. Protection is usually granted for ten years and is renewable. Examples of trademarks include the Nike swoosh, the brand name Kleenex, and MGM's lion's roar. They are essential for the efficient functioning of the market because they help prevent unfair competition from imitators and consumer confusion about the true source of a product.

Theoretical Perspectives on Intellectual Property Rights

With the definitions of IPRs in mind, we contrast six key theoretical arguments about IPRs and their effects on the global knowledge structure.

1) Economic liberals (which critics call "IP maximalists") view property rights as fundamental to the functioning of a market system because they incentivize the efficient use of resources and establish a direct link between effort and reward. Knowledge is potentially expensive to develop, but it can be copied cheaply. This potentially leads to market failure, because there will be free riders—users of knowledge who do not pay for its creation. Consequently, in order to make enough profits to recoup investments in R&D, firms need to be able to legally deny the use of new inventions and creative works to consumers and other firms that do not pay.

When a government provides the creators of knowledge a legal, but temporary, monopoly, they will increase the amount of innovation. As a result, consumers worldwide supposedly get a wider variety of new products at reasonable prices. IPR enforcement also ensures that consumers will have higher quality and safer products than would otherwise be the case. And countries that protect intellectual property tend to attract more FDI and benefit from more technology transfer, in part by signaling that they are business-friendly.

2) Mercantilists see the process of technological innovation in a much different light. Nations must develop and then closely guard their own technology while simultaneously acquiring other countries' technology. The protection of IPRs for domestic firms is clearly appropriate, but equal protection for technology owned by foreign firms is not always in the national interest. As early mercantilists Friedrich List and Alexander Hamilton argued, free trade benefits nations that lead in manufacturing at the expense of nations trying to catch up. Similarly, international conventions that protect IPRs will benefit those nations with advanced technological capabilities at the expense of less technologically developed nations. In this regard, mercantilist and structuralist thought is similar.

Peter Yu points out that when it comes to technological laggards, they need to fight for more "policy space" in IPRs, that is, the ability to craft their own intellectual property laws based on their own "conditions, capabilities, interests and priorities."[30] Others argue that IPR laws should reflect developing countries' own histories and needs because "the adverse consequences for welfare and growth generated by the current IPR regime (including the TRIPS agreement) are worse for the developing than for the developed countries; the existing regime poses formidable impediments to closing the knowledge gap, which is so essential to developmental success.[31] From a mercantilist perspective, many countries can make the best use of their limited resources by stealing intellectual property. Why? Because their businesses will save on R&D and absorb technology faster; their citizens will get much cheaper products; and the government will not have to spend money on a bureaucracy to protect the IPRs of foreigners. The Chinese seem to have taken this lesson to heart, just as previous generations of Japanese, Koreans, and Americans did.

3) Structuralists contend that developed nations use IPRs to monopolize global markets and extract excessive profits from emerging economies. The capitalists that hold IPRs behave like international monopolists and cartels. They are not really interested in competition, which they will sacrifice on the altar of rent-seeking and litigation. As

international relations scholar Carolyn Deere Birkbeck notes, 90 percent of global cross-border royalties on intellectual property and technology licensing fees go to just ten developed countries.[32]

Economic geographer Christian Zeller claims that capitalists want to appropriate, control, and commodify intellectual creativity everywhere that it exists.[33] They always seek to create private property rights from "socially-produced knowledge." Capitalists dispossess "researchers, skilled workers, and also rural communities" of the "knowledge and information which they generate in collective work," transferring the rents to "venture capital, investment funds and license companies."[34] In this structuralist vision, the real creators of knowledge—farmers, indigenous peoples, scholars, and hardworking employees—never really reap the fruits of their creativity.

Other structuralists view the global IPR rules as mechanisms for the United States and other developed countries to promote their own economic dominance. According to Blayne Haggart and Michael Jablonski, "U.S. copyright and Internet policy should be thought of as logically reinforcing elements of a single policy designed to maximize the economic power and influence of the United States and its Internet and copyright firms."[35]

Beyond these three perspectives, there are other complex and overlapping points of view on IPRs from the constructivists, "balancers," and "abolitionists."

4) As we discovered in Chapter 5, constructivists see our social world as constructed: what we value and the interests we have are defined by our shared discourse about them. We have constructed a discourse that something called "intellectual property" is like real "property" and that there are "rights" we should ascribe to that property. While today it may seem natural to see most creative ideas and knowledge-based products as having rights attached to them, historically that was not the case.

Constructivists trace over time how we define IPRs and talk about them; by so doing we better understand whose interests in society are being served by this discourse. Since the 1980s, powerful economic lobbies have defined IPRs as an international trade issue. They frame intellectual property as something that belongs to hard-working people who seek a just reward for their efforts. Creators are pitted against forces described as "pirates" and "counterfeiters" who unjustly take what is not theirs and hurt honest people and companies.

Debora Halbert describes a similar framing of IPRs. The United States has spread a narrative that theft of intellectual property is a threat to national security that justifies "expanding U.S. military oversight of cyberspace" and "public/private information sharing," both actions that threaten "free sharing of information, and even technology transfers."[36] In contrast, Madhavi Sunder argues that if we look at intellectual property through a cultural perspective, we can redefine its purpose to mean empowering the poor so that they can enjoy a livelihood, fairly participate in cultural production, and preserve their cultural diversity from the onslaught of profit-driven, globalized, mass culture.[37]

Constructivists also explain that other social forces are trying to offer an alternative set of ideas about how knowledge is created and circulated in the world. For example, according

to legal scholar James Boyle, postmodernists offer us the argument that "all creation is re-creation" and "there is no such thing as originality, merely endless imitation."[38] In this discourse, no one truly owns their creative output because it is built on the ideas of many people who preceded them. As Newton said, "If I have seen further it is only by standing on the shoulders of giants." If creation is cumulative and informed by everyone around us and before us, then it is hard to argue that anyone should have exclusive ownership of knowledge.

5) A different perspective on IPRs comes from "balancers" who want to strike an appropriate balance between individual rights and communal rights. They want to make sure that individuals can be creative and free while still respecting the legitimate economic rights of others. James Boyle, for example, stresses that a large "public domain" and liberal "fair use" rules encourage creative activity. Similarly, Kembrew McLeod and Peter DiCola assert that artistic creativity has always relied upon borrowing, sampling, ripping, and imitating. Therefore, to criminalize these actions when they occur without "permission" is to impede artistic creation itself.[39]

Balancers want to prevent IPR holders from stifling competition or excessively suing others for alleged infringement. Boyle points out that many copyright industries tried in the past to resist new technologies—including the Xerox machine, the VCR, and TiVo—that threatened their business model. More recently, an innovative startup company called Aereo began offering a low-cost monthly service that allowed customers to capture live TV broadcast signals on tiny antennas and stream them through the Internet to their home computer or mobile device. Cable companies and all the major TV broadcasters succeeded in crushing the company after the Supreme Court ruled in 2014 that Aereo was guilty of infringing their copyrights.

Balancers want to limit the length and scope of IPRs. Political economist Herman Schwartz explains why limits make sense: strong IPRs concentrated in the hands of large corporations allow them to extract rents from society and move control of these rights to different parts of the world in order to avoid taxes; the results are slower growth and higher inequality.[40] Balancers abhor the "permission society," where individuals constantly have to ask copyright holders for permission and pay to access almost every cultural product. Balancers like David Bollier assert that societies need to preserve a large public domain from which everyone can draw freely. He touts sharing and peer production through networks where oppressive copyright laws are unenforceable.[41] There is also an "Open Science" movement encouraging less patenting by scientists and the free circulation of scientific publications (especially if the underlying research in the publications was publicly funded).

6) The last main perspective is that of the "abolitionists," who want to see the elimination or radical reduction of IPRs. Economists Michele Boldrin and David Levine argue that IPRs distort markets, undermine competition, and reduce innovation.[42] They find that in the absence of IPRs, markets still reward innovators who produce goods and services at reasonable prices for consumers. In many sectors of the global economy such as

the fashion industry, database services, software development, and agriculture, there have been significant technological breakthroughs and thriving markets even in the absence of IPR protections.

The Politics of IPRs in Developed Countries

The United States, the European Union, and Japan have largely shaped the global rules governing IPRs. They have defined the scope of IPRs, signed international agreements, and set up multilateral institutions to enshrine the rules in international relations. They seek to enforce these rules, using political lobbying and international diplomacy.

The United States has taken the lead in promoting the protection of IPRs, under relentless pressure to do so in the last thirty years from powerful businesses groups such as the International Intellectual Property Alliance (IIPA), the Motion Picture Association of America (MPAA), and the Pharmaceutical Research and Manufacturers of America (PhRMA). These groups contend that strong IPRs are the key to innovation and international competitiveness. Foreign firms that infringe on IPRs by merely copying original technological innovations can underprice the U.S. firms that incurred the original development costs. Business lobbies estimate the overall losses to U.S. businesses from foreign infringement of IPRs in the tens of billions of dollars every year.

As political scientists Susan Sell and Aseem Prakash have documented, the pro-IPRs movement in the United States was spearheaded by a network of corporations mostly in the software, video, music, agricultural chemicals, and pharmaceutical industries. They have developed alliances with counterparts in Europe to successfully frame IPRs as rights—not government-granted privileges—and to spread a discourse about the dangers of "piracy" to free markets.[43]

Their most important goal was to create a set of enforceable international minimum standards for IPRs. In the 1980s there were already multilateral IPR agreements in existence, including the 100-year-old Berne Convention on copyrights and the Paris Convention on patents and trademarks. In 1967, the World Intellectual Property Organization (WIPO), a UN agency, was created to monitor adherence to these conventions. But the business networks and U.S. and European governments were dissatisfied because the conventions had low standards and did not have enforcement mechanisms.

During the Uruguay Round of trade negotiations from 1986 to 1994, the United States and other developed nations insisted on the establishment of TRIPS, which WTO members would be obliged to accept, along with the new GATS and the revised GATT. TRIPS requires countries to provide a minimum level of intellectual property protection and adhere to the Berne and Paris Conventions. It was a coup for major intellectual property producers because it tied IPRs to trade and established a mechanism for binding dispute resolution. Many developing countries did not like the agreement and had little role in crafting it, but they accepted it as a price to pay for gaining other trade benefits within the WTO. TRIPS also expanded the kinds of intellectual property protected to include geographical indications (GIs), plant varieties, and trade secrets.

Not surprisingly, the developed nations have sought to enhance the international protection of IPRs beyond just the TRIPS standards. They strengthened WIPO, which administers several dozen international agreements on IPRs. In 1996, WIPO produced two treaties that harmonize the protection of IPRs on the Internet and thereby promote international electronic commerce. In 2000, WIPO also adopted a Patent Law Treaty to harmonize patent application procedures across countries.

The United States pressures countries with weak IPR laws. Special Section 301 of the 1988 Omnibus Trade and Competition Act requires the United States Trade Representative (USTR) to create annually a "watch list" and a "priority watch list" for countries that have shortcomings in the protection of IPRs. After investigating the policies of an offending country, the USTR may negotiate a bilateral agreement or institute trade sanctions. The USTR's 2017 Special 301 Report places thirty-four countries on the priority watch list or the watch list, including the five largest countries in the world other than the United States (China, India, Indonesia, Brazil, and Pakistan) and America's three biggest trading partners—Canada, China, and Mexico. Collectively, these countries hold 4.3 billion of the world's 7.3 billion people! As in the past, it seems that the United States has trouble finding more than a handful of important countries that live up to its self-declared IPR standards.

With little prospect of getting more protections for IPRs through the WTO or WIPO, developed countries have sought higher standards—called TRIPS-Plus—in bilateral, regional, and plurilateral agreements that exclude contrarian countries like India, China, and Brazil. TRIPS-Plus standards typically include stronger protections for pharmaceuticals, better enforcement of IPR rights, and higher penalties for infringement. "Forum shifting" enables countries to pick and choose where they can obtain the most leverage to advance their TRIPS-Plus goals. For example, developed countries negotiated a voluntary agreement called the Anti-Counterfeiting Trade Agreement (ACTA) to ratchet up the fight against counterfeit goods and copyright- infringing actors. Actions like these are part of what Susan Sell has described as an ongoing campaign by powerful political actors and business groups to tie IPRs to security issues, lost business revenues, and lost taxes.[44] In the face of citizens' protests and street demonstrations, the EU Parliament rejected ACTA in 2012, so it never came into force. At the same time, two bills in the U.S. Congress—the Stop Online Piracy Act (SOPA) and the PROTECT IP Act (PIPA)—that would have dramatically expanded penalties for online copyright violations touched off unprecedented social opposition. Wikipedia, Reddit, and BoingBoing voluntarily went dark on January 18, 2012, while big Internet companies like Google, Facebook, and Craigslist directed millions of users to lobby Washington against these so-called censorship bills—both of which were withdrawn in the face of this first-ever Internet "blackout."

The defeats of ACTA, SOPA, and PIPA by no means ended U.S. and European efforts to impose global rules protecting IPRs. Sociologist Natasha Tusikov examines how U.S. and European governments, in cooperation with multinational companies, pressured Internet "macrointermediaries" to adopt measures designed to impede copyright and trademark infringement worldwide.[45] The macrointermediaries include: search engines and

advertising platforms like Google, Yahoo, and Microsoft; social media platforms like Facebook; payments processors like Visa, Mastercard, and PayPal; marketplaces like eBay and Taobao; and domain registrars like GoDaddy. In "secret handshake deals" with governments and rights holders, the intermediaries agree to surveil their systems, remove suspected infringers, deny access to sites selling pirated or counterfeit goods, and cut off vital services to Internet sites that violate IPR rules. The cooperation between governments, IP rights holders, and intermediaries amounts to a regime of private governance that doesn't rely on legislation, avoids public accountability, and violates people's privacy.

Conflicts over IPRs between developed countries still exist, given the centrality of knowledge and technology to competitive advantage. For example, Japan and the European Union provide protections for fashion designs (of clothing, bags, and accessories) for three and ten years, respectively, but the United States gives no IPRs to fashion designers. Shobita Parthasarathy explains that the United States and Europe have different cultural views about innovation that affect how they approach patentability of biotechnology, genes, and life forms.[46] The United States has a "market- making" approach that allows patenting of most kinds of new technology with limited concern for the potential moral and health consequences of commercializing products based on this technology. In contrast, Europe's "market-shaping" approach means the state considers public opinion and potential social consequences of technology when deciding what should be patentable. More so than in the United States, European patent institutions seek to protect against "affronts to public morality, inequitable distribution of goods, risks to national security, and…infringements of human rights."[47]

North–South Conflicts over IPRs and Patented Medicines

Developing nations have increasingly resisted the IPR norms that developed countries promote. They want more flexibility to craft their *own* IPR standards consistent with their specific national needs. They have forcefully demanded recognition of their right to make use of already-existing flexibilities in the TRIPS agreement. They have also sought to redefine principles of intellectual property law to include promotion of human rights, public health, and education. Finally, some countries are seeking to extend IPRs to biodiversity and traditional knowledge.

Like developed countries, developing countries have engaged in forum shifting to promote their views in the most sympathetic international organizations where they have the most leverage. Argentina and Brazil spearheaded a Development Agenda for WIPO that was formally adopted by the WIPO General Assembly in 2007. The Agenda is a set of forty-five recommendations under which WIPO is supposed to encourage technology transfer to developing countries, recognize that intellectual property rules should account for different levels of development, and make sure that IPRs not just focus on economic growth but serve a variety of social goals. In 2013 WIPO members agreed to the Marrakesh Treaty that allows institutions to make and import material adapted for the blind and visually impaired without permission from copyright holders.

One of the most successful efforts by developing countries to challenge TRIPS has been in the areas of access to medicines. Many poorer countries after 1994 felt that TRIPS unfairly constrained their ability to manufacture or import generic versions of expensive, life-saving pharmaceuticals. By framing IPRs as a health and human rights issue, they have been able to create a strong global coalition in favor of patients' rights.

The debate first erupted in the mid-1990s in South Africa, which was experiencing an HIV/AIDS epidemic. The patent-protected antiretroviral drug "cocktail" that held the disease in check cost about $15,000 per patient per year in the United States. Consequently, only the richest South Africans could afford the treatment. Generic versions of the drug cocktail produced in India cost only $200. India did not issue patents on pharmaceuticals at the time, and this allowed the development of a competitive generic drug industry. South Africa's government voted in 1997 to permit imports of cheap generic antiretroviral drugs from India and to allow compulsory licensing of patented antiretrovirals in South Africa. A compulsory license is a license a state grants to a domestic private company or government body, with or without the consent of the rights holder, to produce and sell a good under patent. Compulsory licensing is allowable under TRIPS if a government first negotiates with the patent holder and provides reasonable compensation to it. Thirty-nine pharmaceutical companies from around the world responded to South Africa's Medicines Act with a lawsuit to try to block the law. Activists around the world, incensed by this legal action, rallied against the lawsuit with the slogan, "Patient Rights over Patent Rights." The pharmaceutical companies withdrew the lawsuit in 2001 in an effort to avoid a public relations disaster.

Developing countries then successfully pressured WTO officials at ministerial meetings in Doha in November 2001 to affirm that TRIPS does not prevent them "from taking measures to protect public health" and that they have a right to issue compulsory licenses, especially in the face of national emergencies or conditions of national urgency like widespread HIV, malaria, tuberculosis, and other epidemics. This interpretation of the TRIPS agreement, called the Doha Declaration, was a breakthrough for the poorest countries.

However, it still did not resolve many disputes over IPRs and the right to health. Many countries do not have companies with sufficient technological capacity to produce generics under compulsory licenses for their own domestic market. Developing countries insisted that they should be able to import generic versions of patented medicines from countries such as India and Brazil without violating trade laws. After much hemming and hawing by the United States, the European Union, and Big Pharma, WTO members in 2003 agreed to this waiver. The Doha Declaration was formally incorporated into the TRIPS agreement in 2017, marking the first time that the WTO agreements have been amended.

A global coalition called the Access to Medicines campaign that emerged from the South African debate is led by NGOs and developing countries.[48] They seek to discredit big pharmaceutical companies for focusing on monopoly patents rather than saving lives. They were instrumental in getting the WTO TRIPS Council to exempt the poorest countries from enforcing TRIPS' pharmaceuticals provisions until 2033. Under intense pressure

from activists, pharmaceutical companies have pledged hundreds of millions of dollars for HIV/AIDS assistance in developing countries. Major manufacturers of antiretrovirals have drastically reduced the price per dose they charge poor countries through discounting and voluntary licensing programs. Private companies have also partnered with NGOs and governments in multilateral initiatives such as the Global Fund to Fight AIDS, Tuberculosis, and Malaria (to increase funding and access for health care) and the Global Alliance for Vaccines and Immunization (to increase research on "neglected" diseases and delivery of patented vaccines at affordable prices).

It is hoped that a combination of more generics, more voluntary cooperation by Big Pharma, more foreign funding, and more flexibility in IPR laws can make essential medicines more accessible throughout the world. India continues to irk the United States and Big Pharma with its high patent standards, but it helps ensure a vibrant generic drugs industry. This was illustrated in 2013 after Gilead Sciences introduced a new vaccine called Solvaldi (sofosbuvir) to treat Hepatitis C, a terrible liver disease affecting 175 million people worldwide. Gilead initially marketed sofosbuvir in the United States for $84,000 for a full treatment. Soon thereafter, it licensed several Indian companies to make a generic version that sells for between $300 to $900 for a full treatment and can be exported to the poorest countries in the world. Many other methods to ensure low-cost drugs for developing countries have been proposed, including patent pools and an international fund to subsidize research on tropical diseases.

Struggles over Traditional Knowledge

Another IPR struggle between South and North is over traditional knowledge (TK), which is the accumulated knowledge and practices of indigenous communities as they relate to plants, plant uses, agriculture, land use, folklore, and spiritual matters. Indigenous peoples around the world over many generations have developed deep understandings of their physical environments and the plants they use for food and medicine. They have developed a wide variety of plant diversity through harvesting and breeding practices. In fact, many of the major food crops in North America and Europe originally came from these local communities.

Northern companies often appropriate TK for their own selfish purposes. As Madhavi Sunder notes: "The poor's knowledge is often considered simply the discovered bounty of nature—age-old knowledge that, remarkably, has remained static over millennia, and thus 'raw material' waiting to be turned into 'intellectual property' by entrepreneurs, largely from the Global North."[49] The economic value of TK is potentially very high. Billions of dollars' worth of prescription drugs sold every year are derived from tropical plants whose medicinal properties were learned from indigenous peoples. Countries like Brazil, India, the Philippines, and Indonesia have begun insisting that those who want to find local plants with chemicals that can be used in medicine must get permission, acknowledge the source of subsequently patented materials, and share benefits with the local communities whose traditional knowledge they initially relied upon. Developed countries have resisted this norm, partly because extending legal protection to TK promises to redistribute some of the

gains from global innovation to poorer countries.

Many countries in the South are also trying to protect TK from appropriation and misuse by nonindigenous groups. This is an effort to give new cultural rights to indigenous peoples. Through the WIPO and in individual countries like Canada, there are campaigns to give indigenous peoples copyrights over their own folklore and artwork—including stories or sacred texts passed down over generations. Maoris in New Zealand and Native Americans have fought to prevent words and symbols associated with their people from being used as school mascots and corporate brand names. Similarly, some indigenous communities are seeking to establish their own trademarks over collective symbols and to apply design protections for handicrafts and carpets. India is rapidly creating a digital library of its traditional knowledge—including 1,300 yoga poses—so that non-Indians cannot patent, copyright, or trademark any of it.

CONCLUSION

Whether viewed from a liberal, mercantilist, or structuralist perspective, knowledge and technology form a critical basis of wealth and power. In this era of global hypercompetition, companies and policy makers understand that knowledge and technology confer significant advantages on countries. Governments have power to control flows of information across borders by, among other things, censoring the Internet and requiring data localization. Conversely, they undermine these controls through often successful espionage against other governments, as WikiLeaks and Edward Snowden have revealed. Transnational corporations sometimes work hand in glove with governments to accumulate information on nationals and foreigners, with important consequences for human rights.

Traditionally, states have funded basic scientific research and nurtured companies that produce breakthrough technologies. In recent years, however, financialization may be weakening the commitment of U.S. companies to invest in long-term innovation. Meanwhile, China and other countries in Asia are determined to become technological powerhouses in order to reduce reliance on Western TNCs. U.S., British, and Canadian universities continue to attract many of the brightest students from around the world. Countries strategically use visa policies to attract skilled workers and wealthy entrepreneurs in a race for global talent.

That the protection of IPRs has risen to the status of a major foreign policy concern for the United States, Europe, and Japan is not surprising. The knowledge structure clearly constrains actors' options and conditions their behavior. It affects which countries will turn innovation into higher productivity, greater market share, and increased exports. It also helps determine the distribution of benefits by shaping prices and productive capacity.

The debates and struggles over IPRs will continue for many years. There is greater recognition by some economic liberals that too many IPRs can have negative consequences for development.[50] People insist on being able to share content with others around the world, instantaneously. Governments will have a nearly impossible task putting that genie back in the bottle through rigid enforcement of IPRs. Developing countries have sought to weaken global norms favoring IP maximalism, yet TRIPS and TRIPS-Plus agreements are still dominant.

Key questions concerning the future knowledge structure include the following: How will resistance to globalization affect the creation and dissemination of knowledge? Will stricter enforcement of IPRs help or hinder the poorest nations of the world? Will the United States continue to dominate science and technology? Will competition for new technologies lead to a new era of economic nationalism? The answers to these questions will have profound effects on the lives of present and future generations.

KEY TERMS

intellectual property rights (IPRs) 253
information sovereignty 257
data localization 257
Internet of Things (IoT) 258
research and development (R&D) 259
triple helix 260
financialization 262
deemed export controls 264
Committee on Foreign Investments in the United States (CFIUS) 264
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compulsory license 275
traditional knowledge 276

DISCUSSION QUESTIONS

1. What do you consider to be legitimate reasons for governments to restrict flows of information between countries?
2. Do the immigration, higher education, and economic citizenship policies of developed countries serve the interests of developing countries?
3. What are some of the reasons why developed countries try to restrict other countries' access to their technology? Does this behavior contradict economic liberal principles?
4. Why are intellectual property rights important in global markets?
5. What are the arguments both for and against stronger protections of IPRs in poor countries? Do wealthy countries have a moral obligation to transfer technology to poorer countries at low or no cost?
6. What are some of the most important ways that a country can nurture an innovative, technologically advanced society?

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PART III
States and Markets in the Global Economy

CHAPTER
11
The Development Challenge



Cars drive on a newly built highway over the Villa 31 slum in Buenos Aires, Argentina in 2015.

Source: AP Photo/Natacha Pisarenko.

Development is no more than a myth which helps underdeveloped countries to conceal their misfortune and developed countries to soothe their conscience.

Oswaldo de Rivero[1]

Many people in the world still do not have their basic needs met, let alone experience

economic prosperity. An obvious question is this: Given the great amount of wealth produced each year, why have so many nations remained impoverished or "underdeveloped"? Development promises an improved standard of living and longer life, but it often has costly tradeoffs. There are intense debates in IPE about the essential prerequisites for development.

This chapter examines political-economic dilemmas that the least developed countries (LDCs) have struggled with. We begin by describing the common attributes of developing nations. We then outline the period in the 1950s and 1960s when many LDCs emerged from colonialism into a world of growing markets, transnational corporations, and the Cold War. Three options presented themselves to LDCs: accept the reality of the international system, try to change it, or drop out of it. Development strategies were influenced by the assumptions and policies associated with economic liberalism, mercantilism, and structuralism. The heart of the chapter focuses on these strategies, including their flaws. After discussing development goals that the UN has set for the poorest countries in the last two decades, we end with a review of debt problems and the challenge a rising China poses to developing countries.

WHAT ARE DEVELOPING NATIONS?

The countries commonly referred to as the LDCs, the South, or the developing countries have diverse histories, cultures, economies, and political systems. The characteristics that they do share, however, are important:

- High instances of poverty;
- Lack of a sizeable middle class;
- Relatively low literacy rates;
- Hunger;
- High instances of infant mortality;
- Poor infrastructure; and
- Weak governments.

Hundreds of millions of people are constantly at the mercy of natural and man-made threats. One measure of the material living standards in a country is income available per person per day to spend on food, shelter, health care, education, and so forth. In industrialized countries, this figure is relatively high. Per-capita income in the United States, for example, is about $130 per day on average. An income of $130 per day can provide a comfortable and healthy lifestyle by global standards. By comparison, many in the South have a per-capita income of $2 per day or less, and hundreds of millions live on less than $1 per day.

Table 11.1 shows the incidence of severe poverty in the Global South. The first three columns show the proportion of the population living on less than U.S. $1.90 per day in 1990, 2005, and 2013. An income of $1.90 a day is a critical point in discussing real poverty. Less than this amount means inadequate diet, high infant mortality, and shortened life span. In 2013, nearly 766 million people (13 percent of the developing world's population) still lived on less than $1.90 a day. The deepest, most persistent poverty is in sub-Saharan Africa and South Asia. The good news is that extreme poverty has declined significantly in several regions, most notably East Asia. The bad news is that the overall figures are still high. Many readers of this book are able to feed their pets better than many parents in LDCs are able to feed their children.

TABLE 11.1

The Incidence of Extreme Poverty in Developing Countries in 1990, 2005, and 2013

Regions	1990	2005	2013	1990	2005	2013
East Asia and Pacific	60	18	4	84	43	16
Europe and Central Asia	2	5	2	10	11	6
Latin America and the Caribbean	16	11	5	30	21	11
Middle East and North Africa	6	3	–	24	18	–
South Asia	45	34	15	78	70	50
Sub-Saharan Africa	54	50	41	74	73	65
All Developing Countries	42	24	13	65	48	32

The next three columns in Table 11.1 show the population percentage living on less than the equivalent of $3.10 per day in 1990, 2005, and 2013. The difference between existing on $1.90 per day and $3.10 per day is significant. With $1.90 or less, a person struggles to survive. Considering the conditions of poverty we are discussing here, $3.10 a day buys a little more than bare subsistence and therefore offers the possibility of better health and human dignity. Of course, $3.10 a day is a small amount to most in industrialized countries, yet nearly 1.9 billion people in the developing countries (one third of the population) must try to get by on less than that amount. Note that, according to this indicator ($3.10 per day), the incidence of poverty is much more geographically widespread, with high poverty rates not just in South Asia and sub-Saharan Africa but also in East Asia and Latin America. As we discuss in Box 11.1, scholars disagree on how best to define and measure poverty.

There is widespread agreement about the need to improve the living standards of much of the world's population. Escaping poverty is the desirable face of economic development, but as we discuss later, there are many costs that must be borne in economic, social, and environmental terms to achieve this goal.

LDCs FROM INDEPENDENCE TO THE WASHINGTON CONSENSUS

As colonialism disintegrated during the mid-twentieth century, new nation-states emerged into an international order shaped by the Cold War between the United States-led "First World" and the Soviet Union-led "Second World." For the newly formed nations in Asia, the Caribbean, and Africa—and for relatively poor but long-independent nations in Latin America—economic development was practically a universal goal. By the 1980s, a neoliberal perspective on development had become pervasive.

ALTERNATIVE WAYS OF MEASURING POVERTY IN DEVELOPING COUNTRIES

One of the biggest disputes in development studies is how to measure and interpret changes in global poverty rates. While most governments and scholars rely on World Bank poverty data, considered the "gold standard," some critics question its reliability or support other ways of measuring poverty. (A different but related debate in IPE is over what factors *cause* changes in poverty rates.) Why the controversy? For starters, it is very expensive and difficult to survey households in those countries that have large numbers of poor people. For example, economic historian Morten Jerven argues that because so many African states lack the capacity to collect reliable data on income or GDP, much of what we think we know about socioeconomic trends in Africa is based on unreliable statistics.[a] A second problem is that because countries use different currencies, incomes have to be converted into a common currency and adjusted for differences in purchasing power within countries. It is a difficult process based on assumptions that not all experts agree on.

According to the World Bank, the *number of people* in the developing world living in extreme poverty was cut by more than half between 1990 and 2013 (from 1.84 billion to 766 million), and in the same period the *proportion of people* living in extreme poverty fell from 42 percent to 13 percent.[b] The most extraordinary decline has been in China, where the incidence of extreme poverty declined from 67 percent in 1990 to just 2 percent in 2013. Southeast Asia (including India) and Latin America have made considerable progress, but the decline is only modest in Africa.

Trends in poverty are based on an International Poverty Line (IPL), initially set at $1 per day in the early 1990s. The IPL makes it possible to compare *extreme* poverty across countries. It is based on an average of the national poverty lines of the 15 poorest countries. It is periodically updated to reflect changes in the cost of living around the world. The most recent IPL is $1.90 per day, based on purchasing power parity in prices from 2011 surveys. Anthropologist Jason Hickel notes that if we remove China from our calculations, the number of people in developing countries living on less than $1.90 a day was about the same in 2010 as it was in 1990: 1 billion.[c] And many of those who have moved out of extreme poverty are bunched together in the area of $1.90 to $3.10 per day—still quite poor and vulnerable.

Different countries have their own national poverty lines, so what "poverty" and "needs" mean and how they are experienced varies by country. In that sense, the IPL is arbitrary. Scholars don't agree on what we should consider minimal needs to be. If we say that the minimum income necessary to meet one's needs is $3.10 per day (in 2011 PPP), trends in poverty reduction since 1990 do not look as impressive: over one-third of the developing world's population—2.1 billion people—lived on less than

$3.10 per day in 2013. Hickel points out that if we use Peter Edward's "ethical poverty line"—a minimum income one would need in order to achieve a "normal human life expectancy of just over 70 years"—then about 4.2 billion people, or nearly 60 percent of the world's population, live in poverty.[d] The ethical poverty line is $7.40 per day in 2011 PPP.

Instead of measuring poverty based simply on income, experts at the University of Oxford and the United Nations Development Programme created the Multidimensional Poverty Index (MPI) in 2010. The MPI measures overlapping forms of deprivation related to health, education, and standard of living. For example, it includes low levels of schooling, malnutrition, and lack of access to clean water and electricity. Using MPI, the 2016 UN *Human Development Report* finds that 1.5 billion people in 102 developing countries (29 percent of their population) suffer from multidimensional poverty, while another "900 million people live close to the threshold of multidimensional poverty and risk falling into poverty after even a minor setback in health, education, or livelihood."[e] Measuring poverty broadly through the MPI shows that there are twice as many very poor people in the developing world than the World Bank's income-based measure indicates.

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Neocolonialism and Dependency

In the 1960s, a controversial book entitled *The Wretched of the Earth*, written by Martinique-born psychiatrist Frantz Fanon, emerged as a seminal treatise on efforts to overcome the shackles of colonialism.[2] In it, Fanon analyzed the struggle against colonial repression with a discourse on imperialism and nationalism. Many students and scholars regarded Fanon's writing as a compelling call for the people throughout the Third World to fight against—and even to violently oppose—Western domination. For our purposes, it is worth noting that Fanon also critiqued the elites in newly independent countries who, as a social class, appeared corrupt and unlikely to genuinely pursue nationwide development.

Fanon highlighted concerns about Third World cultural liberation. The language of the colonizer, which the colonized societies had been compelled to adopt, remained a powerful influence. Newly independent LDCs often viewed former colonial powers with disdain and suspicion. They blamed colonial exploitation for their economic "backwardness." Development—characterized by a growing and prosperous economy—was crucial in order to establish a national identity and ensure political stability. Because many LDCs approached development as a resistance to Western cultural domination, they advocated caution before adopting a Western outlook on it.[3] Likewise, LDCs that supported the Soviet bloc preferred non-Western development strategies.

The 1955 Afro-Asian Bandung Conference in Indonesia led to the eventual formation in 1961 of the Nonaligned Movement (NAM), which sought to position itself outside the sphere of the Cold War scenario. Many leaders and intellectuals argued that LDCs were trapped in a capitalist system dominated by institutions that favored the developed countries.[4] Consider the Western oil companies, for example. For much of the twentieth century, seven major oil companies controlled the exploration, processing, and supply of oil in a number of oil-rich regions. These "Seven Sisters," as they were known, divided market share, regulated supply, and preserved their control over resources in developing countries.

Supported by their respective home governments, these oil companies also negotiated terms (involving some royalties for the host country) that ensured the companies' dominance over oil exploration and distribution in the international market.

Compounding such domination by multinational corporations (MNCs) was a restrictive system of trade, finance, and technology transfer that made LDCs economically vulnerable. As producers of raw materials and primary goods, LDCs lagged far behind the industrialized nations in the production of value-added products. Developed countries' control of the international financial system meant that they could manipulate the LDCs' access to funds for economic development. As Argentine economist Raul Prebisch argued, the development dilemma in Latin America was inextricably linked to factors *outside* the region.[5]

Early dependency theorists made a distinction between *un*development and *under*development. The former was characterized by lack of development, while the latter was the outcome of a process that further undermined LDC economies and simultaneously made the industrialized world more prosperous. Andre Gunder Frank also argued that underdevelopment in LDCs was a *by-product* of the development process in industrialized regions.[6] He claimed that the global capitalist order was organized such that the metropolis states exploited the satellite states by extracting economic surplus from them. Osvaldo Sunkel and Pedro Paz also argued that "both underdevelopment and development are aspects of the same phenomenon, both are historically simultaneous, both linked functionally and therefore interact and condition each other mutually."[7]

Dependency theorists suggested that the LDCs are locked in an unequal exchange relationship because international prices for the manufactured goods that they import generally rise faster than the prices for primary products and raw materials that they export. Many dependency theorists also argued that the political and economic strings attached to foreign aid reinforce a dominant–subordinate relationship between the developed and less developed nations.[8]

Many LDCs turned to international organizations to change the structures of the global economy. In 1964, seventy-seven LDCs that became known as the Group of 77 (G77) spearheaded the establishment of the United Nations Conference on Trade and Development (UNCTAD). They sought to make UNCTAD—which holds a major conference every four years—a mechanism for negotiations between the LDCs and the developed countries. Despite developed countries' resistance to UNCTAD initiatives, LDCs were gradually able to secure some concessions and preferential tariffs for their exports.

In 1974, LDCs made a historic attempt at the UN General Assembly to establish a New International Economic Order (NIEO) that was designed to accelerate the pace of development. Industrialized countries saw the NIEO as a radical effort to undermine the market-oriented global economic system and to redistribute global wealth and power.[9] In the face of their opposition, efforts by LDCs in the 1970s to change the system generally failed.

The Market Unleashed

In the 1980s, the Reagan administration influenced the IMF, the World Bank, and the GATT to bring LDCs into closer alignment with free-market ideology and U.S. foreign policy objectives. This period saw the introduction of structural adjustment programs (SAPs) with stringent conditions that LDCs had to adopt to ensure continued IMF and World Bank financial assistance. Some of the more controversial conditions, which were part of the so-called "Washington Consensus" on reforms necessary for development, include:

- Currency devaluation;
- Raising interest rates;
- Cutting government subsidies;
- Privatization of public companies;
- Reduction of the government budget deficit; and
- Adoption of free-trade policies.

By the 1990s, the collapse of communism gave even more momentum to the U.S.-led chorus touting the virtues of free trade and globalization. Indeed, it was during the early 1990s that India, China, and the "Asian Tigers" began to emerge as economic successes in their own right. The dominant Washington Consensus asserted that developing countries needed to take advantage of global resources and market opportunities. More and more of the resources for development came from financial markets, not from official aid. To repay their debts, nations had to earn more from exporting—but on what terms?

As during the early 1970s, LDCs felt that the rules of international trade and financial organizations were unfavorable to their interests. Among other things, they were frustrated that their attempts to export more agricultural products were often undermined, ironically enough, by heavily state-subsidized agriculture policies in the United States and the European Union. Hypocritically, developed countries protected their own markets for sugar, beef, cotton, corn, and fresh produce while demanding that developing countries lower tariffs on imported goods. LDCs brought their demands for more access to rich countries' markets to the Seattle WTO meetings of 1999 and then more forcefully to the Doha trade meetings of 2001. They could not just walk away from global markets, but they also needed rules more favorable to their interests.

In addition to promoting free trade, the Washington Consensus made a strong case for economic development through capital mobility—the free movement of funds into and out of a country. These investment funds come primarily from foreign direct investment, commercial bank loans, and purchases of stocks and bonds. Some are long-term and stable while others are short-term and volatile. Some go to purchase productive assets and help companies raise money to expand, while others are simply speculative. The risk is that short-term speculative funds—what Keynes called "hot money"—will rush in and out of LDCs, creating a cycle of booms and busts. With capital mobility came financial instability and the possibility of a devastating crisis necessitating an IMF bailout package.

HOW TO DEVELOP? THE CLASSIC IPE DEVELOPMENT STRATEGIES

Determining the appropriate strategies for development remains a hotly contested issue in IPE. Broadly speaking, political economists have debated the relative merits of economic liberal, mercantilist, and structuralist strategies. Many countries have shifted from one strategy to another as the global economy changes and new governments come to power. Later in the chapter we discuss development strategies pursued since the 1990s, including export-oriented industrialization, reprimarization, and sustainable development.

The Economic Liberal Perspective

The economic liberal perspective on development requires that LDCs integrate themselves into the global market economy by emphasizing their comparative advantages. As their economies grow from exporting, they will be able to acquire more foreign technology and make new investments in manufacturing. As "latecomers," LDCs can use the market to industrialize while learning from the policy mistakes of the now developed nations.

The liberal perspective largely de-emphasizes the importance of *global* structural conditions in thwarting development in LDCs, focusing instead on *internal* conditions. Other variants of this perspective emphasize the *social* impediments to development, such as poor education systems, health problems, and corruption.

MNCs can be a major source of capital, jobs, and technology. Liberals do not believe that developing countries have to enter into a "race to the bottom" in the form of very cheap labor and lax regulations to attract foreign direct investment (FDI). More importantly, MNCs want growing markets, political stability, and good government institutions. Most MNCs invest in industries that pay more than sweatshop-level wages. Even when their investments do go into low-wage and low-skill industries, they frequently do not operate sweatshops directly but rather contract with local suppliers who do. Economic liberals also argue that MNCs actually have better working conditions and environmental policies than local firms in poor countries.

International business scholar Theodore Moran believes that there are viable strategies to improve working conditions in LDCs, such as adopting global labor standards and integrating sweatshop concerns into WTO agreements.[10] He argues that a passive strategy that counts on sweatshop earnings to "trickle down" is wrongheaded. Instead, he proposes that developing countries need to proactively create the right policy environment if they want to generate the highest gains from MNCs' FDI and attract progressively higher-skill industries and jobs. That means limiting corruption, establishing pro-business regulations, supplying infrastructure, partnering with MNCs to provide vocational training, and employing "light-form industrial policy" that does not rely on subsidies and protectionism.[11] He cites experiences in Costa Rica, Malaysia, and the Dominican Republic as evidence that these strategies can help LDCs to move beyond sweatshops and

upgrade their manufacturing base.

Part of the appeal of the economic liberal outlook lies in the interpretation that the United States and other industrialized nations went through "stages of growth" that LDCs will replicate. According to early development theorist W. W. Rostow, development requires LDCs to undergo evolutionary changes in their socioeconomic system.[12] Traditional society has low levels of economic productivity and constrains individuals through rigid social values. Increases in education, entrepreneurship, and infrastructure expand the level of commercial activity.

In the "take-off" stage, new industries increase rapidly as the entrepreneurial spirit becomes more dominant. An emerging capitalist class propels industrialization and the adoption of economic innovation. An increase in savings and investment sustains the drive to economic maturity. In the final stage of mass consumption and self-sustained growth, major sectors of the economy are able to supply goods and services for a large cross-section of the population. Rostow perceives the stages of development as universal, implicitly assuming that developing countries will become modern, industrialized nations like England or the United States.

The liberal development strategy prioritizes open markets and free trade. Exports will serve as the "engine to growth," with the state guiding the economy toward efficient allocation of resources. Foreign aid helps meet important strategic needs. While conceding that in the initial stages only a small elite will likely benefit from free trade, proponents of this model are convinced that the lower classes will move out of poverty as the economy matures. They see validation for their ideas in the development of states such as Japan, Taiwan, South Korea, Hong Kong, and Malaysia that opened themselves to international trade and supported growth of the private sector.

The Structuralist Perspective

Marxists and other structuralists assert that the core countries dominate the peripheral countries and foster a relationship of dependency. The developed nations' "neoimperial" connections to the periphery via trade, aid, and FDI often produce dual economies. One part of an LDC's economy consists of wealthy elites who are well connected to transnational elites in the core, whereas the other part is full of the masses, whose futures remain bleak. For ardent structuralists, the liberal trickle-down market model ultimately benefits only elites and core nations and does not produce wider societal development.

During the Cold War, many Soviet-bloc countries and their LDC counterparts such as North Korea, Cuba, and Vietnam prioritized industrialization and also emphasized isolation from the capitalist global economy. LDCs were exhorted to overcome dependency by closing the economy (autarky), rejecting international aid, and nationalizing the local holdings of TNCs. Instead of producing for export, LDCs were supposed to protect and provide subsidies to domestic industries. Furthermore, the state was urged to distribute income more equitably and provide basic health and welfare programs. Structuralists also emphasized greater collective efforts among LDCs to gain international leverage to promote better terms of trade.

Many non-communist countries such as Brazil, Mexico, Egypt, and Algeria adopted a variation of this model in the form of import-substitution industrialization (ISI), a nationalistic strategy designed to minimize the adverse effects of dependence on foreign capital and markets. They were convinced that specializing in primary commodity products was an inherent disadvantage because adverse terms of trade would drain foreign exchange. The first stage of the import-substitution strategy, which was well underway in the 1950s and 1960s, involved promoting local manufacture of consumer goods (such as processed foods, textiles, and footwear) and curtailing foreign imports.

However, significant differences affected the ISI strategies in East Asia compared to those in Latin America and the Middle East. Historically, the resource-rich, quasi-socialist Middle East countries and the agriculture-rich Latin American economies were more dependent on primary exports than their East Asian counterparts like Taiwan and South Korea.[13] Diversifying away from deeply entrenched, primary-product economies was difficult. Furthermore, protectionist policies in Latin America displaced the foreign share of the consumer market, while in East Asia the focus was on enhancing the international competitiveness of locally produced goods. Hence, by the late 1960s, as South Korea was promoting its exports while maintaining some barriers on imports, Brazil and Mexico were borrowing from abroad to finance the deepening of their ISI. The second stage of import substitution involved expanding the role of state-owned enterprises, boosting the manufacture of labor-intensive consumer goods, and diversifying into capital-intensive goods such as steel and automobiles.[14] While East Asian NICs pursued ISI for only a short period, countries in Latin America and the Middle East stuck with it well into the 1970s. They ended up with heavily indebted and inefficient industries that could not compete internationally.

The Mercantilist Perspective

Mercantilists consider international trade as essential to national development. However, they are generally not enthusiastic about the limited-government doctrine typically associated with the liberal perspective. They believe that the state has a critical role to play in coordinating a trade strategy. Several developing countries in East Asia such as South Korea, Taiwan, and Singapore adopted strategies that, while quite diverse, are generally termed export-oriented industrialization (EOI). This mercantilist-oriented strategy calls for the state to promote exports in selected sectors of the economy.

First, the export-oriented East Asian newly industrializing countries (NICs) changed the fundamental composition of their production. Prior to the 1960s, like other developing countries, South Korea and Taiwan began promoting manufacture of labor-intensive consumer goods by protecting "infant" industries from foreign competition. By the late 1960s, South Korea and Taiwan began to increase their international market share by promoting the export of domestically manufactured durable goods. State intervention again played a strategic role in launching this export-promotion effort. Raw material imports necessary for manufacturing were encouraged, and selected domestic manufacturing

industries were targeted with fiscal incentives to stimulate the level of exports. By devaluing their national currencies, these East Asian countries made their exports more internationally competitive and imports less attractive to domestic consumers.[15] Therefore, the NICs purposefully *created* comparative advantages for their manufactured products.

Figure 11.1 gives an indication of the significantly different manufacturing trajectories of Asian countries compared to Latin American countries. During the 1970s, South Korea expanded into heavy (technologically intensive) industries including steel, petrochemicals, and automobiles. These efforts to restructure the economy bore fruit. Manufacturing's share of GDP in South Korea climbed from 12 percent in 1960 to 24 percent by 1980 and 29 percent by 2016. Thailand followed a similar trajectory. Both countries became major exporters of manufactured goods. In contrast, in Brazil and Argentina, where ISI was important for a long time, manufacturing as a percentage of GDP was high in the 1960s and 1970s, but began a significant decline in the 1980s. By 2016, manufacturing contributed to only 12 percent of Brazil's GDP.

Another major component of the mercantilist export-led growth strategy involved promoting a high level of savings and investment (including intense efforts in research and development). A combination of factors contributed to this process. In South Korea, the raising of interest rates increased household savings. The government also helped establish private banks and financial institutions, which allowed it to increase its oversight of savings in the economy.[16] The growth of financial institutions in Singapore and Hong Kong was also crucial to capital formation—the process of building up a country's stock of equipment, machinery, buildings, and other productive assets.

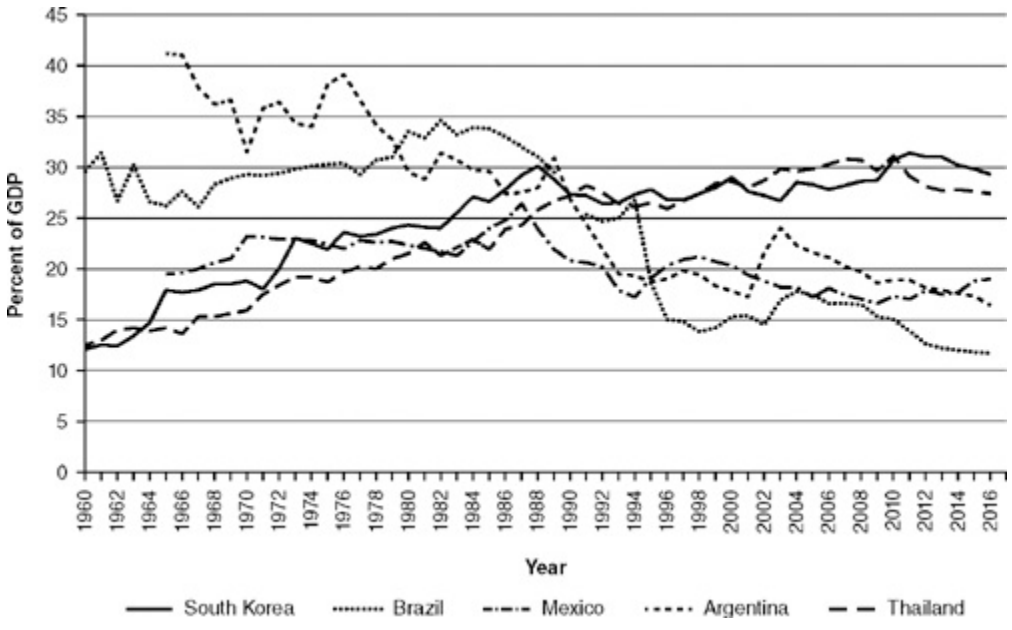


FIGURE 11.1
Manufacturing Value Added as a Percentage of GDP for Selected Countries, 1960–2016

Source: Data from World Bank, *World Development Indicators*, at http://data.worldbank.org/indicator/NV.IND.MANF.ZS?locations=BR&page=1.

The inflow of foreign capital and aid to East Asia also impacted the capital formation process. South Korea's dependence on foreign aid was especially crucial following the Korean War in the 1950s. According to one estimate, approximately 70 percent of South Korea's domestic capital formation came from foreign aid during the 1950s.[17] Taiwan's domestic capital formation also depended heavily on foreign capital during the same period —about 40 percent was externally financed. Recall that this was when South Korea and Taiwan underwent structural transformation by using protective measures to insulate their newly emerging light-manufacturing industries from foreign competition.

The East Asian NICs also invested heavily in education and job training to produce a literate and skilled workforce, which promoted growth in productivity, more industrial flexibility, and greater equality. They didn't simply "roll back the state" and let free competition reign. The state was instrumental in setting export-oriented development policies to maximize the benefits of industrialization.

THE EAST ASIAN MIRACLE AND THE ASIAN FINANCIAL CRISIS

What were the lessons learned from the debate between import-substituting industrialization and export-oriented growth? The answer to this question depends on whom you ask and when. By the early 1990s, the evidence seemed to favor an export-oriented strategy based on the dynamic growth experience of the East Asian Tigers—and the Southeast Asian "Tiger Cubs" (Thailand, Indonesia, the Philippines, and Malaysia) that followed in their path. In *Looking at the Sun*, James Fallows argues that the East Asian system of state-led, export-oriented economic growth proved superior to both the ISI strategy and liberal laissez-faire policies.[18]

A number of IPE scholars attribute the East Asian miracle not just to export orientation but to the broader role of the "developmental state." They stress that political institutions were crucial to sustained economic transformation. In Japan, which Chalmers Johnson first described as a "developmental state," elite bureaucratic agencies formulated policies in coordination with private firms to guide new investments.[19] In his study of Taiwan and South Korea, Robert Wade describes how the state "governed the market," using bank credit and industrial policy to force firms to export more, become globally competitive, and move into new industries.[20] Developmental states recruited public-minded, well-educated officials from elite universities and gave them autonomy from political parties to distribute subsidies to private firms in exchange for these firms meeting strict performance goals. In contrast, non-developmental states in Latin America borrowed heavily from abroad to build domestic industry, leading to opportunities for corruption and devastating debt crises.

The World Bank released a study titled *The East Asian Miracle* that sought to assess the lessons learned from import-substituting industrialization versus export-oriented growth.[21] It noted that the "East Asian Miracle"—high growth without great inequality—was due in part to East Asian governments avoiding inefficient wage, price, and exchange-rate distortions. They promoted high rates of saving so that investment was possible without large foreign debts. According to the World Bank, the contest between state-led import-substitution industrialization and state-led export-oriented growth showed that the key to success was not so much what the government did but what it *avoided* doing.

Many East Asian scholars point out that the World Bank report blamed any East Asian failures on the state and credited all successes to natural market forces. The scholars argue that many of the positive factors in Asian economic development, such as high savings rates, strong education systems, and relative income inequality, were *dictated by state actions*, not because the state took a hands-off approach. In other words, the East Asian economic development was very much the result of carefully crafted mercantilist policies.

The Asian financial crisis that began in 1997 reopened the debate over development strategies. Some argued that the crisis was caused by unwise state involvement in the economy (often called *crony capitalism*). Others claimed that "premature globalization"—

opening up to global financial markets before necessary domestic institutions were in place —made the Asian economies unusually susceptible to financial crises.

This was an important debate to resolve. Do laissez-faire policies produce rapid growth, as the World Bank report had suggested? Or do they open up an economy to instability and crises, as the 1997 Asian financial crisis seemed to indicate? The debate was in full swing in the 1990s, and it continues to this day. At the time of the Asian financial crisis, neoliberalism had become the dominant development strategy. As we discussed in previous chapters, it stressed a greater role for the domestic private sector, less government intervention, encouragement of foreign investment, less trade protectionism, and freedom of global capital flows. For neoliberalism's proponents, the collapse of the Soviet bloc underscored the superiority of free market capitalism. With Japan entering a long period of slow growth after 1989 and much of East Asia in crisis in 1997, it seemed that the mercantilist developmental state model was flawed, too. Moreover, countries such as Mexico, India, and Algeria that had followed ISI experienced debt crises or balance of payments problems in the 1980s and 1990s that hampered growth.

Some economic liberal scholars recognize that development requires an important state role, but emphasize that success requires large private firms to upgrade technologically. In their comparison of South Korea and Brazil, Thomas Hannigan, Ram Mudambi, and Ahreum Lee argue that the reason Korea caught up to the developed countries and Brazil got stuck in a "middle income trap" is that the former maintained an "outward-oriented economy" with technological specialization and government nurturing of "national champions" (large domestic companies) with funding tied to their performance.[22] To catch up, economies also need to access the technology of TNCs through involvement with global value chains. Brazil chose ISI, with little impetus for firms to become globally competitive. It neglected "fundamentals" such as infrastructure and education, while few national champions emerged to develop technological capacities.

Cambridge University economics professor Ha-Joon Chang argues that neoliberals have hurt developing nations by opposing their regulation of inward direct investments and obsessing about the need for privatization.[23] Many neoliberals also exaggerated the importance of corruption, the lack of democracy, and an assortment of cultural issues that presumably act as barriers to change. Chang stresses that developing countries must use free trade policies in conjunction with a variety of protectionist policies (including import substitution) to "create the space in which their producers can build up their productive capabilities before they can compete with better producers from abroad."[24] This is what the Japanese did with their car industries for almost forty years, and South Korea did with steel, shipbuilding, autos, and electronics. Moreover, he points out that most developing countries had higher growth rates during their ISI period than after they switched to neoliberal policies. For example, while per-capita income in Latin America grew at 3.1 percent annually during the "bad old days" of protectionism in the 1960s and 1970s, growth in the "good old days" of neoliberalism, from 1980 to 2004, slowed to an average of 0.5 percent per year.

In addition, some scholars contend that it is a myth that the developed economies

achieved success through the methods they preach to the LDCs today. Instead, writes Ha-Joon Chang, "Almost all of today's rich countries used tariff protection and subsidies to develop their industries. Interestingly, Britain and the USA, the two countries that are supposed to have reached the summit of the world economy through their free-market, free-trade policy, are actually the ones that had most aggressively used protection and subsidies."[25]

As we explain below, the debate about development today is less focused on ISI vs. EOI due to changes brought by globalization in the 2000s. Some mercantilists and liberals have converged on several arguments. They tend to agree that the key to development in LDCs is not simply more government or less government; rather, it is *good* government. Smaller government (and supposedly a more unregulated market) is not necessarily better government if it sacrifices social goals and institutions. Some scholars stress the importance of taking into consideration the unique circumstances, economic challenges, and resources of each country when considering appropriate strategies. Others stress that the new problems poorer states face regarding energy, the environment, and financial stability will limit their ability to choose different courses of action.

DEVELOPMENT AND GLOBALIZATION

As LDCs entered the twenty-first century, globalization created new problems and opportunities. Pressure from global civil society and failures of structural adjustment led the IMF and the World Bank to offer some new ideas and policies for development. We start this section with a discussion of "top-down" policies focused on improving how the state functions, how it manages the overall economy, and how it relates to society.

Top-Down Approaches to Development: The Turn to "Good Governance"

The IMF has argued that the conditions it attaches to its loans steer countries toward long-term growth. Critics claim that IMF policies disproportionately hurt the poorest segments of society and cause unnecessary shocks that leave economies reeling for years. After the Asian financial crisis in 1997 and 1998, the IMF's credibility with developing countries plummeted. Many countries accumulated foreign reserves in order to avoid having to turn to the IMF in times of economic trouble. Since the Great Recession of 2008–2009, the IMF has moderated its neoliberal dogma, cognizant that it lost many of its former borrowers. Alexander Kentikelenis, Thomas Stubbs, and Lawrence King point out that the IMF has rhetorically conceded that:

- Governments may need to increase spending during a crisis, not cut it;
- High income inequality hurts growth;
- Capital controls may be beneficial in some circumstances; and
- Social protections need to be strengthened.[26]

However, in their analysis of the conditions attached to IMF loan agreements with countries between 1985 and 2014, Kentikelenis, Stubbs, and King find that the IMF continued to demand the same kinds of reforms after the Great Recession that it had before. Its new rhetoric did not reflect its practice, leaving countries with many of the same constricted policy choices as always. In developing countries since 2010—and even in European countries caught in the Great Recession—the IMF has pushed for labor market "liberalization," including cuts in public sector wages and cuts in the number of public workers. It has failed to treat the maintenance of social protections for the poor as a high priority.[27] Kentikelenis, Stubbs, and King conclude that the IMF practices "organizational hypocrisy" and has been "adept at introducing ceremonial presences of reform."[28]

The World Bank has a more important and direct role in development than the IMF. Recognizing that the market-oriented reforms of the 1980s and 1990s were insufficient to create development success, the Bank began to accept that the state must play an important role in fostering long-term growth. China and Brazil demonstrated that success rests on some unorthodox policies such as state direction of some investments.[29]

However, structuralist scholar Toby Carroll laments that in recent years the World Bank

has come to understand development as promotion of private sector activity and "deep modernization" rather than industrialization and reduction of vulnerability within poor countries.[30] He criticizes the World Bank's International Finance Corporation (IFC) for fostering the growth of "financial intermediaries" in the Asia-Pacific region. The alleged purpose of these intermediaries is to provide finance to individuals and small- and medium-sized enterprises that have traditionally been denied bank credit. The new buzzwords "financial inclusion" and "access to finance" signify that development is about getting money to the "little guys."[31] The IFC provides loans to and invests in banks that do the actual lending to citizens in their country. Carroll portrays these IFC efforts as promoting international capital accumulation through finance, not contributing to real development.

One of the biggest top-down changes to development policies began in the 1990s, coming into full bloom in the 2000s. The World Bank promoted a new narrative of "good governance" that emphasized how improving government institutions could make developing economies work better. The basic idea is that governments themselves in developing countries have to undergo reforms in order for their economic policies and international aid to be effective. Good governance requires better public sector management through rule of law, lower corruption, and judicial predictability. It also necessitates more government accountability to civil society—especially by allowing social groups more participation in decision making. Importantly, good governance means that the state should create the conditions for markets to function better—by promoting competition, stronger private property rights, and better financial oversight. This perspective is compatible with economic liberal approaches to development, but it stresses better government, not less government.

The IMF and the World Bank now require countries seeking financial aid as well as debt relief to prepare Poverty Reduction Strategy Papers (PRSPs) that outline how they plan to tackle poverty over a number of years. Because the PRSPs are formulated through a process involving governments, civil society groups, the IMF, and the World Bank, it is hoped that they will support good governance and ensure that the poor benefit from IMF and World Bank funding, rather than bear the brunt of cuts in social spending, as was common under structural adjustment programs.

Development economist Nancy Birdsall claims that good governance tends to come from demands of a growing middle class in developing countries.[32] She stresses that it is the income-secure middle class that pushes for good economic administration and is willing to pay taxes for public goods. She defines the income-secure middle class as living in households with a daily income per person of at least $10 (in 2005 PPP). In contrast, households where the daily income per person is from $4 to $10 are materially vulnerable "strugglers" who tend to gravitate to populism and dominate in protests such as the Arab Spring. Birdsall claims that once at least 20 to 25 percent of a developing country's population is in the secure middle class (as is the case in Turkey, Brazil, Mexico, and South Africa), demands for good government are likely to be sustained.

In their influential 2012 book *Why Nations Fail: The Origins of Power, Prosperity and Poverty*, economist Daron Acemoglu and political scientist James Robinson present a more

theoretical argument in support of good governance, asserting that good institutions are the key to economic success.[33] Extractive institutions, which draw resources and income from the masses to benefit just a small elite, suppress innovation over the long term. In contrast, inclusive political and economic institutions are necessary for long-term growth. Political pluralism, open media, and citizens' empowerment tend to foster economic institutions such as property rights, competition, and enforcement of contracts that support growth and prosperity. Given how important historically-generated institutions are, Acemoglu and Robinson doubt that foreign aid can do much to solve development problems if a country has extractive institutions.

Political scientists Richard Doner and Ben Ross Schneider connect good governance to the ability of developing countries to escape what is called the "middle-income trap," a condition wherein after a period of rapid growth their per-capita GDP gets stuck in the range of $1,000 to $12,000 for many years, if not decades.[34] In order to transition to a high-income country (as South Korea, Singapore, and Taiwan did), developing countries need to increase productivity growth—a process called "upgrading" in which value-added activities in industry increase and the proportion of high-skilled jobs grows. The problem for middle-income countries such as Turkey, Brazil, Mexico, Malaysia, and South Africa is that upgrading is a Herculean task. Some necessities of upgrading include large investments in education, R&D, and vocational training. Coordinating these kinds of changes nationally requires effective institutions that can handle complexity.

A country that cannot create the elements of good governance such as effective state agencies and public–private networks is unlikely to escape the middle-income trap. Doner and Schneider say that good governance requires a political coalition between several large social groups such as industrialists and workers that can agree to focus on long-term gains and cooperate over the distribution of resources during the transition. Many political dysfunctions can impede the formation of stable, cooperative coalitions, including populism and kleptocratic leaders.[35] Doner and Schneider also find that social groups are fragmented when a country has high inequality, a large informal economy, and many TNCs. Under these conditions it is hard for businesses and workers to create common interests within their social group or with other social groups.

Only 13 countries escaped the middle-income trap in the 1980s and 1990s. Some, such as Hong Kong, Mauritius, and Singapore, had small populations that made social cohesion stronger. Others, such as South Korea, Taiwan, and Israel, faced major security threats that "greatly facilitated elite cohesion and coalition building."[36] Today's large middle-income countries face more challenging global conditions. It remains to be seen if they can form the social and political coalitions necessary to support stronger state institutions and large investments in human capital.

Bottom-Up Approaches to Development

As early as the 1990s, the World Bank and many NGOs recognized that top-down approaches to development, whether focused on macroeconomic policies, good governance,

or foreign aid, had flaws. In response, they also crafted more bottom-up approaches that emphasized changing the behavior of individuals, empowering groups in society, and making markets more "inclusive." Part of the reason for this shift was a growing belief that development involves much more than just economic growth (see Box 11.2). It also reflected a desire to work around corrupt, authoritarian governments in developing countries and make individuals agents for change. Many believed that enhancing entrepreneurship and self-help in society would create pressures for better governance and free up underutilized human resources to foster self-sustaining growth. This change in thinking was also occurring at a time when remittances from workers overseas back to their home countries were rapidly growing. Officially recorded remittances to developing countries mushroomed from $77 billion in 2000 to $429 billion in 2016. A number of scholars believed that this privately controlled money could allow households to improve their standard of living more effectively than foreign aid or government programs.

One of the World Bank's key changes is articulated in the 2015 *World Development Report*. According to Ben Fine et al., rather than concentrating on funding large-scale infrastructure, the Bank now focuses on "nudging"—making "minor changes to context that make it easier for the poor to choose better options."[37] While continuing to promote the market, it is also relying on insights from behavioral economics and psychology to help the poor change their preferences, i.e., to act more "rationally" to achieve their goals. An example of nudging is giving poor people small cash payments each time they test HIV-free —as a way to incentivize safe sex practices. Fine et al. say this approach ignores the structural factors contributing to poverty and essentially blames the poor for making choices that perpetuate their poverty. It promises solutions at the individual level through application of supposedly universal principles from behavioral economics. The problem, say Fine et al., is that "the more we nudge, the less we need to budge in the face of worsening inequalities and the continuing assault of finance on living standards and democratic accountability."[38]

ALTERNATIVE WAYS OF MEASURING SOCIAL WELL-BEING

Gross domestic product (GDP) is probably the most widely used measure in the social sciences. It is the sum total of the goods and services produced in a country over a given time period. Many assume that it measures the health of an economy and how well off its people are. However, a number of scholars in recent years have criticized our overreliance on GDP and have called for better ways to measure well-being and development. Political economist Lorenzo Fioramonti argues that GDP privileges only priced goods and services while ignoring unpriced transactions and "bads" such as pollution and depletion of natural resources.[a] It leads to an obsession with continual growth. For example, GDP in China has grown dramatically, bringing hundreds of millions of people out of poverty, but it does not reveal the massive environmental damage in China or how growth has increased global warming. The RAND Corporation calculates that the costs of air, water, and soil pollution in China —principally in health costs, lower worker productivity, and agricultural damage— equaled about 10 percent of GDP annually between 2000 and 2010 (and they will continue to rise in the future).[b] GDP alone gives us a partial, and in some ways misleading, understanding of what is happening to China's society. Reliance on GDP leads us to value material consumption.

In 2009, a Commission on the Measurement of Economic Performance and Social Progress (CMEPSP) headed by economists Joseph Stiglitz, Amartya Sen, and Jean-Paul Fitoussi published a major report calling for new ways of measuring well-being.[c] Surveying critiques of GDP, they note that because GDP does not measure the value of non-market work such as unpaid household and family care work, it implicitly suggests that these tasks are not important for the "real" economy. GDP also tells us nothing about how unequally the fruits of growth are distributed; as a result, a fast-growing economy could be benefiting a relatively small elite while failing to benefit the majority of the population due to inequality. Moreover, GDP cannot measure sustainability—humanity's ability to preserve the environment, natural resources, and standards of living for future generations. The CMEPSP recommended that we use many different measures of quality of life, particularly focused on conditions and capabilities at the household level, to better assess economic and social performance.

Social scientists have created more comprehensive indicators that encourage us to value more things. For example, in 1990 the United Nations Development Program (UNDP) began publishing the Human Development Index, which is a composite measure of a country's well-being based on literacy, school enrollment, life expectancy, and GDP per capita. It focuses attention on the need to expand choices and freedoms for citizens of developing countries.[d] And since 2012, an independent group called the

Sustainable Development Solutions Network (commissioned by the UN Secretary General) has published an annual World Happiness Report that measures overall happiness of countries based on surveys of people's *subjective* life satisfaction. Surprisingly, the 2017 report ranks Costa Rica as having a happier population than the United States, while Brazil, Mexico, and Guatemala rank much higher than Italy, Japan, and China.[e]

The debate about GDP reminds us that how we choose to measure a society's performance shapes what policies governments will pursue and what they will ignore. Development encompasses many more changes in society than just economic growth.

References

[a] Lorenzo Fioramonti, *How Numbers Rule the World: The Use and Abuse of Statistics in Global Politics* (New York: Zed Books, 2014).

[b] Keith Crane and Zhimin Mao, "Costs of Selected Policies to Address Air Pollution in China" (Santa Monica, CA: RAND Corporation, 2015), p. 3, at www.rand.org/pubs/research_reports/RR861.html.

[c] Joseph Stiglitz, Amartya Sen, and Jean-Paul Fitoussi, "*Report by the Commission on the Measurement of Economic Performance and Social Progress*" (2009), at http://ec.europa.eu/eurostat/documents/118025/118123/Fitoussi+Commission+report.

[d] See http://hdr.undp.org/en/content/human-development-index-hdi.

[e] See http://worldhappiness.report/ed/2017/.

Sociologists Kevan Harris and Ben Scully also see evidence of a more bottom-up approach in the Global South since the 1990s with the spread of large-scale social assistance programs targeting the poorest segments of the population. The programs include "anti-poverty transfers of cash and in-kind goods, targeted expansions of access to health care and education, employment guarantees, and pensions for the elderly poor."[39] Examples include Brazil's Bolsa Família and China's rural health care programs. Brazil's program has a strong element of nudging, in that small payments to families are contingent on them vaccinating their children and ensuring that their children attend school regularly. Harris and Scully interpret these kinds of programs as representing a partial shift in development strategy from "growth first" to "welfare first," or from an emerging belief that "improved welfare might itself be an engine of development—a prerequisite to, and not an outcome of, high levels of growth."[40]

In the 2000s, the World Bank and many NGOs touted the importance of increasing the poor's "financial inclusion," i.e., access to financial services such as savings accounts, credit, and money transfer services. The idea is to provide opportunities for grassroots entrepreneurship in the informal economy—the part of the economic system that operates outside of direct government control. In his popular book *The Mystery of Capital*, published in 2000, Peruvian economist Hernando de Soto argues that capital is the key to unlocking grassroots economic growth potential—an idea that the supporters of microcredit agree with.[41] De Soto notes that in many LDCs the poor often do not have any *property rights* to the land they work on or the makeshift houses they live in. Without formal legal title to this capital, it is impossible to secure credit to expand a business or to build a permanent house. If capitalism is to work for the poor, de Soto claims, then the poor need to become capitalists, and that requires that they have rights to the capital they already use.

The Bottom-Up Approach of Empowering Women

Another way of increasing financial inclusion is by extending microcredit to the poor to

give them a chance to participate in the market economy. The idea of microcredit is that development can grow from the bottom up.[42] Microfinance provides credit to people to start their own small businesses, thus enabling the poor to lift themselves from poverty through their own initiative. When they repay their loans, this enables others to access credit, too. The most famous example of microcredit is the Grameen Bank, which was founded in Bangladesh by Professor Muhammad Yunus in 1976. Microcredit loans are very small, often just $20 or $50, with over 95 percent of the borrowers being women. Social pressures among groups of borrowers lead to high rates of repayment.

People who are used to living in societies where credit is readily available may find it difficult to appreciate how even a little credit can benefit people in very poor parts of the world. A small group of women can use a loan to purchase fabric or other raw materials that are then processed into finished goods sold in local or regional markets. Without funds for the raw materials, the market value of their labor cannot be realized. The small incomes that are thus generated can change both the economic status of their households and their social status.

Probably the most important example of the shift to a bottom-up approach to development is the focus on strengthening the role of women. As early as the 1970s, development scholars and feminists had spread a discourse about the importance of integrating women into development programs to increase their productivity and improve social equity. By the 1990s, feminists advocated for a rights-based approach to gender equality that addressed the political bases of gendered hierarchies and unequal global economic structures. International organizations now argue that "investing" in women and "empowering" girls through education will accelerate economic growth. Drawing on women's underutilized skills and making women full participants in a market-based economy can help bring about socioeconomic change. The World Bank and NGOs have expanded programs to ensure that women and girls in developing countries have access to education and health care. TNCs such as Nike and Coca-Cola have launched campaigns to transform girls' lives.

However, some feminist political economists have criticized this efficiency-based approach to gender equality and development that emerged in the 2000s. This approach to women is instrumental: women are the means by which development goals can be achieved. Increasing the role of women in the economy has been popular because it seems apolitical. It doesn't require addressing global power inequalities or changing labor laws. Exploitative relationships between North and South that disproportionately hurt poor women and girls can conveniently be ignored.

Feminist scholars have been particularly critical of global corporations' campaigns to empower women in the Global South. TNCs maintain that promoting gender equality is compatible with maximizing profit. This approach is neoliberal in that it relies on individual women taking advantage of opportunities afforded to them to become entrepreneurs. In 2008 Goldman Sachs started its "10,000 Women" campaign with the goal of providing women entrepreneurs in developing countries access to business management education and credit. In 2008 Nike launched its "cause marketing" campaign

called "The Girl Effect" to spread awareness of the need to educate girls in order to combat poverty. And Coca-Cola in 2010 launched its "5 by 20" campaign to empower women economically in 44 countries. Sofie Tornhill criticizes these kinds of corporate programs for stressing women's self-help and development of human capital while ignoring the need for structural change, higher salaries, and political rights for women in the development process.[43]

Similarly, Adrienne Roberts contends that corporations have helped create a project of "transnational business feminism" that uses gender equality as a "means of legitimizing and depoliticizing the exercise of private power."[44] The World Bank in the mid-2000s began promoting the idea that gender equality is "smart economics." It argues that investing in women and empowering them economically enhances economic efficiency and raises productivity in developing countries. Along with other international organizations, international financial institutions, NGOs, and TNCs, the World Bank continues to make the "business case" for gender equality so that women can compete in product, financial, land, and labor markets. Roberts refutes the idea that integrating women into labor markets empowers them. She points out that women often end up in low-paying, part-time jobs with little job security.[45] More important than what corporate feminism promotes is what it remains silent about: corporate tax avoidance that makes it harder for developing countries to fund social programs.

Although critical of corporate feminism, Sylvia Chant says there is much to celebrate about the heightened attention in the last 30 years to improving the lives of women and girls during the development process.[46] The Millennium Developments Goals and the Sustainable Development Goals are but two of the important initiatives through which international agencies have sought to improve the health, educational, and income prospects of women and children. Nevertheless, says Chant, the Global North's discourse on Global South girls tends to portray them as "victims" of their own cultures who need to be "aided by their First World sisters and corporate saviours."[47] The "smart economics" discourse places the onus "on girls and women to be responsible economic actors and altruistically give back to their families in ways that boys and men do not—or are not exhorted to do—to the same extent."[48]

Development Goals and Foreign Aid in the New Millennium

Just as development theory has changed since the late 1990s, so have development goals. Despite years of debates about competing strategies, poverty, child malnourishment, and disease have remained endemic in many parts of the world, especially Southeast Asia and sub-Saharan Africa. Scholars and aid donors now recognize that development is much more than an economic issue. For example, the costs of ignoring public health issues are high. In sub-Saharan Africa, more than 25 million people are infected with HIV, and nearly two-thirds of new infections occur there. The AIDS epidemic has claimed millions of lives, impacted agriculture, and put enormous strain on government resources.

Attention to poverty and health care–related problems increased following the UN's

establishment of the Millennium Development Goals (MDGs) in 2000. This initiative helped refocus the international community's commitment to addressing dire economic and human conditions in the poorest nations. The Millennium Development project pursued the following eight broadly defined goals:[49]

1. To eradicate poverty and extreme hunger by half
2. To achieve universal primary education
3. To advance gender equality and empower women
4. To reduce child mortality by two-thirds by 2015
5. To reduce by two-thirds the maternal mortality ratio
6. To reduce the spread of HIV/AIDS and malaria by half by 2015
7. To secure environmental sustainability
8. To develop a partnership for development that includes an open, rules-based, and nondiscriminatory trade and financial system.

American economist Jeffrey Sachs is a strong advocate for greater commitments from industrial nations toward achieving the aforementioned goals. Sachs's advocacy of the MDGs is based in part on a critique of past strategies—like the structural adjustment programs—pursued by the IMF. In his book *The End of Poverty*, Sachs asserts that the "main IMF prescription has been budgetary belt tightening for patients much too poor to own belts. IMF-led austerity has frequently led to riots, coups, and the collapse of public services."[50] He believes that development experts need to emulate a *clinical* approach practiced in medicine, finding specific treatments for specific economic illnesses.

In 2015 the UN General Assembly replaced the MDGs, which had set the global development agenda in the 2000s, with the Sustainable Development Goals (SDGs). With 17 broad goals and 169 specific targets, the SDGs emphasize sustainability, inclusion, and lowering inequality. In his newest book, *The Age of Sustainable Development*, Sachs supports the emphasis on "socially inclusive and environmentally sustainable growth."[51] He frames sustainable development as a more holistic approach to development that places economic growth alongside the need to conserve the Earth's resources and ecosystems for future generations and reduce inequalities so that all groups in society can enjoy rising living standards. He is optimistic that equity and efficiency are complementary and that new energy technologies will help mitigate climate change, as long as we undertake the political work of instituting good governance.

Sachs and many other development scholars argue that more foreign aid from wealthy states to the poorest nations is a necessary but not sufficient condition for development. Summarizing the empirical studies of a broad array of economists, Martin Ravallion, a former head of the World Bank's research department, and Steven Radelet, a former chief economist at USAID, state that aid boosts economic growth and living standards and saves millions of lives by improving health.[52] Figure 11.2 shows that major donors have increased net Official Development Assistance (ODA), especially since 2000. The United

Nations has for decades set a target for wealthy countries to contribute foreign aid amounting to at least 0.7 percent of their gross national income (GNI). Among major donors, the United Kingdom, Germany, the Netherlands, and Sweden have met this target, with major aid increases since 2000. In 2016, Germany and the United Kingdom disbursed $24 billion and $20 billion, respectively. The United States is the world's largest aid donor, spending $29 billion in 2016, with major increases for health and humanitarian funding since 2000. However, this amount represents less than 0.2 percent of U.S. GNI, about the same low percentage that Japan spends on development assistance.

Long-standing literature in political science and economics questions whether foreign aid actually helps poor countries develop. Most wealthy countries use foreign aid to pursue their own national security goals, and recipients are often required to use aid to buy goods and services from businesses in the donors' countries. Economist William Easterly argues in his book *The White Man's Burden* that foreign aid is frequently eaten up by corrupt governments, and he calls on "utopian social planners" in wealthy countries to adopt much more humble programs to help developing countries.[53] Similarly, Nobel Prize-winning economist Angus Deaton argues that it is an illusion to believe that we can eliminate global poverty "if only rich people in rich countries were to give more money to poor people in poor countries."[54] He contends that aid fuels corruption and helps keep in power the very regimes that capture most of the aid. Berhanu Nega and Geoffrey Schneider agree that poor governance allows elites to capture most aid—an example of a process economists call "rent-seeking."[55] However, they criticize the neoliberal emphasis on bypassing corrupt governments by channeling foreign aid through NGOs, community-based organizations and social entrepreneurs that engage in development work. These organizations have a "notorious problem of scaling up," i.e., extending their programs on a national scale.[56] Even microfinance—whatever merits it may have—cannot solve poverty problems. Nega and Schneider believe that development requires structural transformation, which only the state can accomplish.

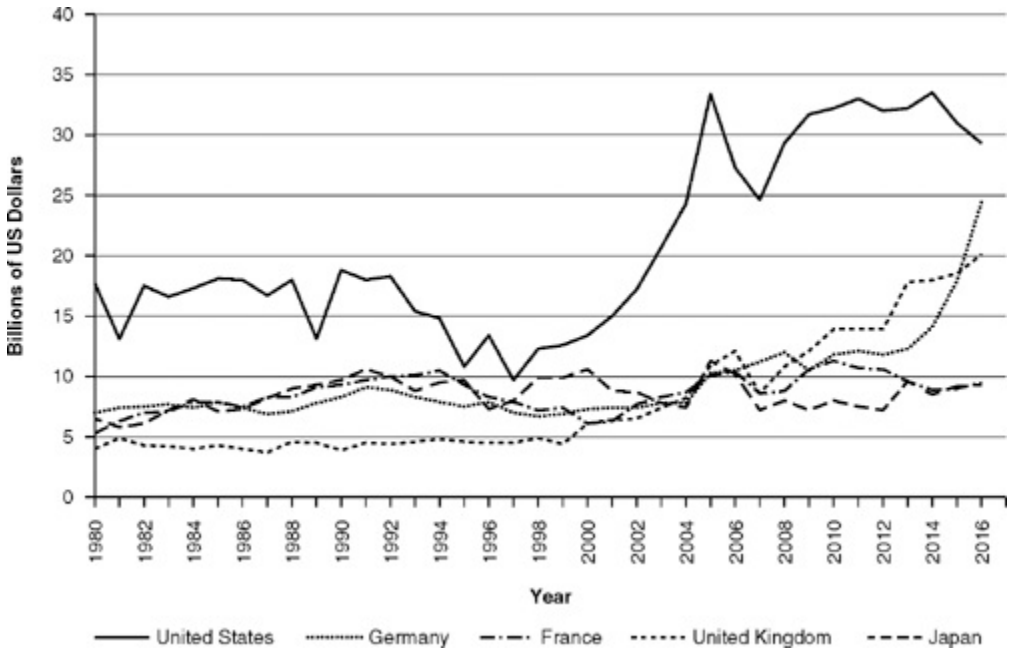


FIGURE 11.2
Disbursements of Net Official Development Assistance (in billions of U.S. dollars), 1980–2016

Note: Figures are in constant 2015 U.S. dollars. Disbursements include bilateral and multilateral ODA.
Source: Data from Organisation for Economic Co-operation and Development, at OECD.stat.

A number of scholars also criticize a new approach to development in which wealthy donors and foundations fund market-oriented projects that were shown to be effective in randomized trials. They claim that this "philanthrocapitalism," which is a non-governmental form of foreign aid, de-politicizes development and misleadingly offers "magic bullet" technical solutions to complex socioeconomic problems. Donors are typically unaccountable to the people they claim to help. Some forms of philanthrocapitalism include "social entrepreneurship," in which a profit-oriented venture focuses on serving a social need. The Bill and Melinda Gates Foundation, a well-known conduit of philanthrocapitalism, has distributed more than $36 billion in grants since its establishment in 1994, much of which benefits global health initiatives. Alongside philanthrocapitalists are a growing number of development organizations led by celebrities such as Matt Damon, Ben Affleck, Madonna, and Bono. These non-traditional development actors support programs promoting humanitarianism, human rights, and education for girls.

Japhy Wilson offers a cautionary tale about philanthrocapitalism.[57] He has studied the Millennium Villages Project (MVP), a development program funded by wealthy individuals and corporations. Started in 2006 and led by Jeffrey Sachs, it channeled subsidies and microcredits to poor farmers in African villages, hoping to develop their sustainable business capabilities. In his study of an MVP village in Ghana, Wilson found that the proliferation of gold mining by international mining companies led to the

dispossession of many poor farmers, and the project failed. Wilson argues that philanthrocapitalism of the kind he saw in the MVP performs a "social fantasy" in which MNCs and billionaire philanthropists believe that they have the knowledge and resources to end extreme poverty without compromising their wealth.[58]

The Burden of Long-Term Debt

Despite the global spread of the Washington Consensus, by the 1990s many poor countries had failed to reap any of its promised benefits. Instead, forty of the world's heavily indebted poor countries (HIPCs)—primarily in Africa—found themselves saddled with long-term debt due to borrowing from the World Bank, the IMF, and international banks. They simply could not sustain debt repayments. Some of these states complained about odious debt, or obligations to outside creditors that were incurred by a former corrupt regime. Iraq's Saddam Hussein, Ethiopia's Mengistu Haile Mariam, and Chile's Augusto Pinochet allegedly fit in this category.[59] Debt-relief mechanisms of the global finance and monetary structure were not designed for the poorest states.

In 1996, after pressure from popular movements in both the North and South, creditors launched the HIPC Initiative under the direction of the World Bank. The goal was cancellation of the debt of the world's poorest countries, but by 1999 only four countries had received debt relief, and the rise in interest payments owed on the debt wiped out any gains.

In 1999, during massive demonstrations at the G7 meeting in Cologne, Germany, supporters of Jubilee 2000 targeted IMF and World Bank practices. Jubilee 2000 was a coalition of NGOs, churches, and labor groups that wanted to advance global justice by pressuring the industrialized nations to cancel the debt of twenty countries by 2000. At the G7 meeting, state leaders pledged to write off $100 billion of poor-country debts.

Since 2000, the IMF, the World Bank, and the developed nations have responded to the goal of debt relief through the HIPC Initiative, freeing up money that can be devoted to poverty reduction. At the June 2005 G8 meeting (including Russia), members also pledged to fund 100 percent debt relief for some of the world's poorest countries through a program called the Multilateral Debt Relief Initiative (MDRI). Obtaining debt relief grew easier as World Bank policy shifted from support for neoliberal "one size fits all" policies to a more bottom-up approach with emphasis on human development.[60] By the end of 2008 the debt of thirty-five poor countries in the HIPC Initiative had been cut by more than 50 percent. By the end of 2015, 36 countries had received debt relief worth $99 billion as a result of both the HIPC and MDRI initiatives.

TABLE 11.2

External Debt Service and GNI of the Poorest Countries

External Debt Service as a Percentage of Exports

Country	GNI per Capita (2015)	2000	2005	2010	2015
Burundi	206	40.9	40.5	2.4	13.5
Liberia	308	–	.05	1.4	8.2
Central African Republic	330*	–	–	–	–
Congo, Dem. Rep.	356	–	7.9	3.1	3.7
Niger	380	8.0	6.8	1.8	7.5
Guinea	392	20.7	18.8	6.3	4.1
Malawi	477	13.5	12.5	1.7	4.3
Togo	540*	6.6	2.5	2.6	3.5
Mozambique	503	9.4	3.2	3.3	9.5

Note: Countries shown are the world's ten poorest, ranked by gross national income (GNI) per capita measured in constant 2010 U.S. dollars using the Atlas method (*in current U.S. dollars).

Sources: Data from World Bank, *International Debt Statistics 2017*; and World Bank, *World Development Indicators Online* (accessed May 28, 2017).

As Table 11.2 shows, the debt service ratio (annual payments of principal plus interest as a percentage of exports) in the nine poorest countries in the world fell dramatically between 2000 and 2010, once HIPC and MDRI relief was finalized. However, the ratio climbed again dramatically between 2010 and 2015, as many of the countries borrowed heavily from global investors and as prices for commodity exports such as oil and gas fell after 2013. Debt service ratios are likely to grow in coming years, causing some countries to once again have debt problems. In May 2017, the IMF and the World Bank reported that 21 low-income countries were at high risk of debt distress, while 4 others (Zimbabwe, Grenada, Sudan, and South Sudan) were already experiencing debt crises.[61] The drag of debt on development still hasn't gone away.

China's Influence on Development

The rise of China since the 1990s has significantly altered the global context in which development occurs. In this section we consider how its demand for raw materials, exports of manufactured goods, and growing overseas investments create new opportunities for—and constraints on—other developing countries. For those who value more South–South interaction, China has provided a successful non-Western model of growth that spreads benefits to poor countries. To China's detractors, its involvement in Africa and Latin America amounts to neocolonialism that is distorting development and creating new dependency.

Few countries, big or small, have developed as rapidly as China in the last 40 years. What can we learn from China's model that can inform current debates about development? Economist Mark Weisbrot makes three important observations:

1. China did not precipitously open itself to foreign imports; it removed protectionism slowly, maintaining average tariffs of more than 40 percent as late as 1992.
2. The Chinese state retained a large role in the economy, even as markets were liberalized; for example, in 2010 it still owned more than 40 percent of the assets of major industrial companies.
3. The Chinese state imposed requirements on foreign investors and used industrial policy to create comparative advantages in new industries.[62]

The success of these mercantilist policies seems to validate arguments about the need for a developmental state in other parts of the Global South. Moreover, argues Weisbrot, the surge in per-capita growth rates in Africa, Asia, and Latin America from 2000 to 2010—despite the Great Recession—owed a lot to China's rapidly growing imports from these regions.[63]

China's growth model—sometimes dubbed the "Beijing Consensus"—provides an alternative to the policies associated with the neoliberal Washington Consensus of the 1980s and 1990s, when structural adjustment and privatization were in vogue. It is also an alternative to the revised bottom-up ideas that the World Bank began touting in the 1990s. In what way? Ironically, China harkens back to the World Bank's pre-1970s ideas, which recommended industrialization and investment in large infrastructure projects, not nudging the poor or trying to guide social development. Economist and IPE scholar Dani Rodrik cites Ethiopia, India, and Bolivia as countries prioritizing public investments in growth-enhancing infrastructure such as power plants and roads.[64] Since 2007, Chinese contractors have obtained the lion's share of large construction projects in Africa, building railways, ports, dams, and power plants.

In 2015 China set up the Asian Infrastructure Investment Bank to help fund these kinds of large projects in Asia that the World Bank and other foreign aid donors have lost interest in. Western countries have particularly eschewed big dams, even though low-cost financing is available and poor countries need the water and energy that hydropower projects provide. Political economist Sanjeev Khagram uses a constructivist perspective to explain why.[65] In the 1980s and 1990s, transnational activist groups spread new norms about environmental protection, human rights, and the rights of indigenous peoples. When combined with political activism, these norms convinced organizations like the World Bank to support fewer dams. In recent years, scientists have influenced the debate, questioning whether dams help mitigate climate change. Nevertheless, some developing countries—particularly non-democratic ones such as China—have contested the new norms, accelerating their construction of huge dams like the Three Gorges Dam and others in Asia and Africa that provide a cheap source of renewable energy. In contrast, many developed countries are actually starting to remove dams. Between 2011 and 2014, two large dams were removed from Washington State's Elwha River in response to tribal and environmental interests. Similarly, by 2020 four hydroelectric dams are scheduled to be removed from the Klamath

River, which winds through Oregon and northern California, boosting salmon habitat.

What's more, China's voracious demand for raw materials provides a boon for countries rich in oil, iron ore, alumina, copper, and arable land. Africa has benefited most significantly: China is now the second largest trading partner with the continent after the United States. From 2000 to 2013, Beijing committed more than $30 billion in official development assistance to Africa and nearly $60 billion in concessional state funding.[66] In 2015 President Xi pledged $60 billion more in loans and export credits. Critics see China's engagement in Africa as causing instability and undermining local manufacturing. But according to international development scholar Deborah Brautigam, China should not be interpreted as a "rogue donor" bent on ruthless exploitation of the continent.[67] Rather, it has a "win-win" relationship with its African partners. Aid and investment—without a lot of political and economic conditions attached to them—create opportunities for more business in natural resources and construction. She points out that China is usually no worse than Western donors and TNCs on issues like corporate social responsibility and environmental stewardship. Its lack of emphasis on democracy and labor rights simply reflects its own internal priorities for growth and collective sacrifice, as well as its belief in non-interference in the domestic affairs of other countries.

However, China's so-called "win-win" relationship with Africa and other parts of the developing world has its drawbacks. In his examination of economic relations between China and Latin America, Kevin Gallagher argues that the "China Boom" is undermining Latin America's industrialization.[68] Manufacturing as a share of the overall Latin American economy has been declining since the 1990s. De-industrialization is partly due to Chinese imports taking market share away from domestic producers. More importantly, the competitiveness of Latin America's exports has declined dramatically, as Chinese manufacturers, helped by low labor costs and an undervalued currency, have been taking away Latin American manufacturers' foreign markets. Electronics from Mexico, clothing from Central America, shoes and steel tubes from Brazil—these and many other exported manufactured goods are now replaced by Chinese goods in Europe and the United States.[69]

Simultaneously, Latin American economies have become reliant on exports of primary commodities, a process called "reprimarization" that is returning Latin America to the kind of dependency that theorists in the 1970s criticized. Chinese FDI in Latin America, Africa, Central Asia, and Southeast Asia is driving the extraction of minerals, energy, timber, and agricultural goods for export, causing widespread environmental damage and fueling corruption among political elites that welcome Chinese companies. The model causes boom–bust cycles of growth because exports are tied to global commodities prices. The going was very good for developing countries in the 2000s as China's growth pulled commodities prices much higher. However, the slowdown in Chinese growth (and other factors) caused global prices of many primary products to drop drastically from 2011 to 2016, hurting developing countries.

CONCLUSION

The search for a single solution to development problems has given way to a realization that there is no one foolproof strategy for all developing nations, nor might there ever be one. In the case of the world's poorest nations, especially those in sub-Saharan Africa, economic development has been modest at best. In many cases, these nations have encountered problems associated with stringent demands made on them by the major powers, the WTO, the IMF, the World Bank, and even the UN. In addition, a myriad of factors within their own societies act as barriers to change, including geographic location and government corruption.

The ISI model gave way to EOI, then to a liberal model in the 1980s and 1990s stressing the need to privatize and open up markets. In the 2000s many developing countries rode the wave of globalization. The going was good when China was growing and its demand for energy, minerals, and food boosted exports from Latin America, Africa, and Southeast Asia. The poorest countries also got some relief from their oppressive foreign debts. The new top-down approach to good governance and the bottom-up approach to social empowerment complemented each other, although each had its weaknesses. Sustainable development is more or less the official goal of international institutions, along with more reliance on private philanthropy.

Acute poverty and political conflicts in Africa remind us that the goal of development is not just having a higher income; it is also about having a better life, with rights and opportunities. Perhaps we should remain optimistic after all. Many states, IOs, and NGOs are heavily invested in trying to promote meaningful change in developing countries. Indeed, much progress has been made in reducing extreme poverty and lowering malnutrition.

However, former Peruvian diplomat Oswaldo de Rivero has a bleaker view of the future than most. In his book *The Myth of Development*, he describes most of the "developing" countries as having "non-viable national economies." Constraints on food, water, and energy mean that the planet will not be able to support vastly more urban dwellers with high standards of living. He argues that the physical-social imbalance caused by growing populations placing unsustainable demands on the world's resources means we must "abandon the elusive agenda of the wealth of nations for a more realistic search for the survival of nations."[70]

KEY TERMS

ethical poverty line 285
Multidimensional Poverty Index (MPI) 285
United Nations Conference on Trade and Development (UNCTAD) 287
New International Economic Order (NIEO) 287
structural adjustment programs (SAPs) 288
Washington Consensus 288
capital mobility 288
import-substitution industrialization (ISI) 290
export-oriented industrialization (EOI) 291
developmental state 293
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middle-income trap 296
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odious debt 304
HIPC Initiative 304
debt service ratio 305
reprimarization 307

DISCUSSION QUESTIONS

1. How serious is the problem of global poverty today? Explain citing data from this chapter.
2. What do you consider to be the best ways to measure and define poverty and social well-being in the developing countries?
3. Briefly trace how the issues regarding economic development have changed since the postcolonial days of the 1950s and 1960s. In particular, discuss the tensions between import-substitution industrialization and export-oriented growth, and between the advocates of the Asian Miracle and those who favor the Washington Consensus.
4. Some argue that developing countries need good government more than they need less government or more government. What are the characteristics of good governance with respect to economic development?
5. For what reasons might foreign aid of various kinds (ODA, Western economic advice, philanthrocapitalism, and Chinese investment) not be so beneficial to poor countries?
6. What approach to development would you recommend to a poor country? What considerations inform your recommendation?

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CHAPTER

12

The Fragmentation of the European Union: The Crossroads Redux



An AfD demonstration against German Chancellor Angela Merkel.

Source: AP Photo/Sipa USA/Omer Messinger.

It's not often that one decision can cripple your own economy, damage global investor confidence, imperil one of the most successful alliances in modern history, foster the rise of ultra-nationalists, precipitate the possible breakup of your own country, deeply divide your own party and cause a great schism between voters of every ideological stripe, but this is one of them.

Peter Bergen[1]

The European Union (EU) faced an unprecedented crossroads on June 23, 2016, when a

majority of voters in Great Britain voted in a referendum to support the United Kingdom's exit ("Brexit") from the EU. The result genuinely shocked many EU observers who feared what Brexit might mean for the British economy and Britain's relationship with the EU. Would businesses in London move to the continent? Would Britain be able to keep its trade relationship with the EU? Would more member states follow the UK and leave the EU, possibly breaking it up altogether?

The EU is clearly facing many challenges, including its continuing financial crisis, the recent massive increase in the number of migrants entering the EU, terrorism, and the growing influence of populist/nationalist parties. Because Greece has had trouble reforming its economy and reducing its debt, some European leaders have suggested that it should be pushed out of the European Economic and Monetary Union (EMU) or "Eurozone." "Euroskeptics" complain about the authoritarian attitude of European Commission officials in Brussels, the lack of national sovereignty and autonomy, and austerity policies that have hurt the working class and the poor. Still others claim that the EU has damaged the social and cultural fiber of their individual countries. In the past, many European officials enthusiastically pursued integration, that is, moving toward a federalist type of union, but current problems are blocking further integration efforts and even fragmenting the union. (See Figure 12.1.)

In this chapter we explain how the EU got into this position and what its member states are doing about it. We start with a brief outline of the history of the EU since the end of World War II, explaining why integration moved forward in fits and starts but now seems to be waning. Second, we examine the controversial Brexit situation and the tensions over a potential Greek withdrawal from the Eurozone ("Grexit"). Third and finally, we discuss what the EU and the integration process might look like in the near future.

The theses of this chapter are:

- While the EU integration process has been relatively successful, integration alone cannot solve certain community problems.
- Once again, EU is at a crossroads; failure to resolve critical problems is undermining its authority and credibility.
- Brexit seems irreversible; Grexit from the Eurozone is still quite possible; Hungary, Poland, France, and possibly Italy might leave the Eurozone.
- To save the EU, members will need to *weaken* its powers and authority while emphasizing a more cooperative "European Community" similar to the way it was before the 1990s. This would better reflect the interests of member states instead of supranational objectives.

THE COMMUNITY BUILDING PROJECT: A COMPLICATED HISTORY

When the Soviet Union did not withdraw from Eastern Europe after World War II, many Europeans worried that the Soviet Union would invade Western Europe or attempt to bring it under the Soviet sphere of influence. In 1946 British Prime Minister Winston Churchill warned of an "iron curtain" coming down between West and East, and in 1947 the distinguished U.S. diplomat George Kennan wrote of the United States' need to "contain" the Soviet Union. It became clear that the political, military, and economic interests of Western Europe and the United States were inseparable. After a bad European winter in 1947, the U.S. Marshall Plan provided European nations with nearly $13 billion in aid (equivalent to more than $100 billion today) to rebuild infrastructure and industries. Some of the funds provided humanitarian assistance to the suffering masses who otherwise might have been susceptible to the spread of pro-communist political sentiment, especially in France and Italy where communist parties were legal.



FIGURE 12.1
The European Union, including Dates of Entry

In a speech in Germany in 1946 Churchill suggested that Europe should "provide a structure under which it can dwell in peace, in safety and in freedom" by building "a kind of United States of Europe."[2] Two of the most prominent founding fathers of the European Union were the statesman Robert Schuman (also the French foreign minister between 1948 and 1952) and the economist and diplomat Jean Monnet. Both of these integration visionaries drew up the internationally renowned Schuman Plan. It proposed "a single unit" that was "independent of national control"[3] to manage production of coal and steel—the most important materials for the armaments industry—so that Germany and France would not be able to fight a war against one another again.

In 1951, France, Germany, Italy, and the Benelux states (Belgium, the Netherlands, and Luxembourg) created the European Coal and Steel Community (ECSC), the first supranational institution in postwar Europe (see Box 12.1 for a chronology of key events in European integration after 1951). With the ECSC came four rudimentary institutions that later served as models for the institutions of today's EU (discussed in Box 12.2): a commission that became the European Commission (EC); two assemblies with appointed officials that became the European Parliament (EP); a council of economic ministers that

became the Council of Europe; and a court that became the European Court of Justice (ECJ).

CHRONOLOGY OF THE EUROPEAN COMMUNITIES/ EUROPEAN UNION

Year	Event
1951	The of Paris establishes the ECSC.
1952	In Paris, the six members of the ECSC sign the European Defence Community (E DC) treaty, which the French National Assembly rejects in 1954.
1957	France, Germany, Italy, and the Benelux countries sign the Treaty of Rome, which creates the European Economic Community, and the Euratom treaty, which establishes the European Atomic Energy Community.
1960	The European Free Trade Association goes into effect.
1962	The Common Agricultural Policy (CAP) is implemented.
1963	French president Charles de Gaulle vetoes the UK's membership in the EEC.
1965	French president Charles de Gaulle begins a 6-month boycott of European institutions to protest supranational proposals.
1968	The Customs Union begins; all internal customs duties and quotas are removed, and a common external tariff is established.
1973	Denmark, Ireland, and the United Kingdom join the EC.
1979	The European Monetary System is established to coordinate exchange rates.
1981	Greece joins the EC
1985	The European Council agrees on the Single European Act, which goes into effect in July 1987.
1986	Spain and Portugal join the EC.
1989	Communist regimes collapse in Central and Eastern Europe.
1990	East and West Germany are reunified.
1992	The European Council signs the Treaty on European Union in Maastricht, making completion of the Economic and Monetary Union (EMU) a formal goal.
1995	Austria, Finland, and Sweden join the EU.
	The Schengen Agreement (which abolishes all border controls) is implemented by seven EU member states: Germany, France, the Benelux countries, Spain, and Portugal.
1997	The European Council agrees on the Treaty of Amsterdam to strengthen EU institutions.
2000	The European Council agrees on the Treaty of Nice to prepare the EU for further enlargement.
2002	Euro banknotes enter circulation and replace the national currencies of 12 countries.
2004	Ten new members join the EU: Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia.
	The European Council signs the treaty establishing a Constitution for Europe.
2007	Bulgaria and Romania join the E U.
2009	The financial crisis begins in Europe. The Treaty of Lisbon, ratified by the parliaments or people of 27 member states, goes into effect.
2010	Greece threatens to default on its debt and gets a €110 billion rescue package from the EU and the IMF.

2011	Germany suggests that Greece take an "orderly exit" from the EMU.
2012	Greece and the Troika agree on a second bailout.
2015	The EU immigration crisis peaks. Hungary and other countries close all or some of their borders to migrants.
	Greece receives a third loan.
2016	The UK votes to leave the E U. Greece receives a fourth loan from the EU and IMF.

Sources: Neill Nugent, *The Government and Politics of the European Union* (Durham, NC: Duke University Press, 2006); website of the European Union, at http://europa.eu.

Jean Monnet was also very interested in helping France build its own A-bomb as part of the proposed European Defence Community (EDC). After two years of negotiations, the French National Assembly let the EDC treaty die. When West Germany joined NATO, the EDC became a moot point, which left the United States to call the shots about when and how to use nuclear weapons in Western Europe. The fact that NATO's Supreme Allied Commander always has to be an American attests to that fact, even today.

Economic and trade officials focused mostly on the benefits from eliminating barriers to trade and creating a common market. Established by the 1957 Treaty of Rome, the European Economic Community (EEC) sought to:

- Gradually eliminate quantitative trade restrictions (quotas) and other protectionist trade measures between member states;
- Gradually end border inspections or custom fees between EEC members;
- Promote large-scale production to make products cheaper and more competitive; and
- Ensure the complete free movement of goods and people (especially employed persons), services, and capital (to a large extent).

To help make it work, the "Common Market" (another name for the EEC) required a common external tariff around it to protect all EEC producers from outside countries who could send goods to it via the countries with the lowest tariffs. The Common Market created tensions because companies in many countries faced more competition from other EEC producers. Trade losers in different countries sought state protection to sustain their incomes, jobs, or way of life. EEC officials found it politically difficult to reconcile the interests of free trade supporters with those of unions and other strong "special interest" groups that screamed for protection.

For example, French farmers wanted a customs union that would mean bigger markets for their foodstuffs, while smaller German farmers feared that they would not be able to compete with French farmers backed by strong agriculture associations. To protect German farmers, the EEC established a system of expensive commodity price supports called the Common Agriculture Policy which, together with protective trade barriers against foreign agricultural imports, helped guarantee less efficient agricultural producers in Germany and

other states higher commodity prices. Likewise, less efficient industrial producers in France and other states benefited from production subsidies and import barriers. For many, the CAP that went into effect in 1962 was the "glue that helped keep the EEC together."

CAP is an example of how integration worked. According to the noted integration theorist Ernst Haas, functionalism is the idea that success in dealing with a problem in one policy area, such as support for domestic agriculture, would "spill over" into other policy areas such as support for agricultural trade and marketing. In turn, those policies might lead to cooperation on economic development and environmental policies. Those who supported functionalism believed that integration would move forward as the EEC solved more problems.

Great Britain initially chose to stay out of the EEC because it was reluctant to cede decision-making power to EEC officials or to share it with the French and the Germans. Great Britain was also unwilling to give up its "imperial preferences"—preferential trade policies with its Commonwealth nations. Moreover, on two occasions (in 1963 and 1967) French president de Gaulle vetoed Britain's entry into the EEC because he believed it would weaken France and because he believed British economic institutions were not compatible with the Common Market. He also viewed the British as a potential U.S. "Trojan horse" in the EEC because of its historical with the United States.

While de Gaulle did support integration, he was very suspicious of unelected bureaucrats in Brussels who threatened France's sovereignty. His ideas about integration were grounded in intergovernmentalism, where national governments are the primary actors who make decisions by converging national interests. De Gaulle also opposed efforts by the European Commission to increase their power, especially at the expense of member states. He insisted on the principle of unanimity in the Council of Ministers—i.e., a veto for each state—as a way to preserve France's interests.

Opposing de Gaulle was Walter Hallstein, another central figure in European integration. Monnet handpicked him to be the president of the EC (1958–1967). A German professor of law who worked on the Schuman Plan, Hallstein asserted that the signers of the Treaty of Rome had intended to create a federation,[4] which he argued could be sustained only if European nations constantly strove for an "ever closer union." As a functionalist, Hallstein developed a set of legal principles and guidelines that justified the European Commission taking management responsibility away from national state bureaucracies and making the EC the brains of the EEC.

Upset that Hallstein was trying to increase the power of the European Commission, de Gaulle pulled French ministers from Brussels for six months. The "empty chair" crisis incapacitated the EEC until members agreed in the "Luxembourg compromise" to the principle for majority voting, but allowed states to veto decisions that threatened their vital national interests. Hallstein and others blamed de Gaulle for slowing up the integration process.

In a critical accounting of EU history in his book *The EU: An Obituary,* the historian John Gillingham argues forcefully that Hallstein's position actually helped turn the idea of a federated political system into a "deeply ingrained way of official thinking: frontal in

approach, blind to alternatives, and increasingly out of touch."[5] After de Gaulle retired in 1969, national differences remained about how and in what policy areas the EEC could integrate further to achieve a political federation. And yet that goal would increasingly conflict with the functional objective of for to solve common

While integration did spur economic growth in the late 1950s and 1960s, disparities amongst the various states' economic philosophies and administrative methods made it difficult to harmonize their policies. Countries' different standards of living created different interests. Executive power was divided between the Council and the Commission. The EC could only coordinate policy, not enforce it.[6] Relations between the EC and Council of Ministers were often tension-filled. The weak European Parliament gave rise to the perception of a democratic deficit (citizens lacking a role in decision making and EC institutions that are not accountable to the people).

The 1970s and Early 1980s: Integration Slumps

During the era of "Europessimism" or "Eurosclerosis" in the 1970s and early 1980s, integration did not make the progress many had predicted it would. Gillingham paints a bleak picture of the EEC at the end of the 1960s: a "Most Imperfect Union" and a "partly built house" that could not collect taxes, frame a budget, or force compliance with its decisions.[7] The Commission sought to build up its power and authority by regulating producer cartels in shipbuilding and textiles, and working its way up to automobiles, defense, and chemicals. Executive power was shared between the Council and the Commission, leaving the EC "on a mission but without means to pursue it and with major obstacles facing it."[8]

Agreement was elusive in the 1970s, given conflicting policies among the members concerning unions, wages, and economic stimuluses. Domestically, the state-directed economic models of German corporatism and French *dirigisme* were not working well, in part due to the decreasing popularity of Keynesian monetary policy.

Other problems in Western Europe reflected major changes in U.S. foreign economic policy that started in the late 1960s. The United States was running a high deficit in its balance of payments brought on by spending for Vietnam and fighting domestic poverty at home. A weakening demand for U.S. dollars generated inflation and began to slow economic growth in Europe. Facing domestic recession in 1971, President Nixon acted unilaterally by suspending the convertibility of U.S. dollars to gold. He devalued the dollar in order to generate more exports and cut the U.S. trade deficit. European allies perceived Nixon as making an America-first decision and abandoning the United States' hegemonic responsibilities.

To decrease U.S. power over European economies, the EEC took initial steps to create an Economic and Monetary Union (EMU), but the project was abandoned in 1973. At about the same time, the 1973 OPEC oil crisis deepened international interdependence and triggered major economic recessions in Europe, the United States, and elsewhere. EEC states faced hard choices concerning how to adjust their economies to the reality of high

energy prices. In the face of balance of payments deficits, many members employed non-tariff barriers (NTBs). Détente between the United States and Soviet Union also opened up the possibility of more Western, especially German, trade with Eastern European nations.

Great Britain finally entered what came to be called the European Community (EC) in 1973, along with Ireland and fellow European Free Trade Association member Denmark. Britain took the leap only after two controversial referenda and a series of painful negotiations. Greece entered the EC in 1981, followed by Spain and Portugal in 1986. For the last three, their rewards for moving from authoritarian government to democratic institutions were the Common Market and closer economic ties, which were intended to solidify democracy and protect them from communist influences. Nevertheless, the entry of four largely agricultural economies into the EC and the CAP put severe fiscal strains on the other nations in the short run.

In the early 1980s, neoliberal ideas promoted by Prime Minister Margaret Thatcher of Great Britain were washing over much of Europe. Her economic philosophy, which espoused privatizing state enterprises, reducing market regulation, and promoting free trade, became all the rage and accelerated globalization (see Chapter 2). U.S. president Reagan also applied neoliberal ideas to the U.S. economy, and continental Europe felt pressure to adopt more neoliberal policies.

The SEA and Economic Union

Jacques Delors, the newly appointed president of the European Commission (1985-1995), sought to "reenergize" the European Community. A shrewd diplomat, he traveled from capital to capital to talk to governments and citizens about moving integration forward. Delors was known for trying to manipulate heads of state, often butting heads with Thatcher, who was suspicious of too much regulation by Brussels and its Eurocrats. Delors concluded that international trade, which Monnet had used to bring the EC together in the first place, would push integration forward. In 1985 he issued a "White Paper" proposing the completion of the Single European Market (SEM) inside the EC by 1993. Under his leadership, the EC identified some 270 areas where agreement was still needed to reach the 1957 of a true common market.[9]

At the end of 1985 the European Council agreed to the Single European Act (SEA), which went into effect in July 1987. Many of the features of the SEA sound quite similar to those of the early EEC:

- Member states committed to achieving an SEM inside the EC, with essentially the same four freedoms that they had agreed to twenty years ago: freedoms of movement for goods, services, people, and capital, even though this significantly limited their national sovereignty.
- The European Council would have a new qualified majority voting (QMV) rule.
- The European Commission, the European Parliament, and the ECJ would have more power and responsibilities.
- New policy areas for the EC to manage would include the environment, research and

technology, and "economic and social cohesion."
- Finally, EC members agreed to "forge a common foreign policy" based on intergovernmental cooperation rather than supranational coordination.[10]

Despite the SEA treaty, many trade restrictions still needed to be "harmonized" based on the principle of "mutual recognition," meaning that the standard for a good of one country had to be accepted everywhere in the Community—without objections! Hundreds of nontariff barriers that discouraged imports from other countries and protected domestic producers were kept in areas such as health, safety, and technical standards. The free movement of services, which represented an increasing proportion of world trade, was more complex than many had suspected. Areas such as banking, finance, and insurance were subject to regulations that varied considerably among nations.

To achieve the goal of the free movement of people would require a unified immigration policy. Given the present immigration crisis in much of the EU (see later), the likelihood of such a policy seems remote. The free movement of capital would require the dismantling of capital controls and investment regulations, which would affect flows of money into and out of a nation. Many nations had traditionally imposed capital controls to encourage domestic investment, promote financial stability, or reduce foreign exchange variations.

To achieve the objectives of the SEM, it was clear that economic integration necessitated some level of political integration. To foster political agreement, the SEA changed the requirement for a unanimous vote in the Council of the EU to approve most legislative decisions. The new QMV rule meant that a decision was taken (passed) if at least sixty-two of eighty-seven votes (= 71.26 percent) of the Council of the EU were in favor of a proposal. Votes were allotted to the twelve member states on the basis of their size. In addition to its practical advantages, the QMV had great symbolic value. It meant that, at least with respect to single-market economic legislation, European institutions were gaining in importance because it would now be possible to take decisions against the will of some opposing members.

Finally, the SEA enhanced the power of the EP. It would now be able to amend proposals from the Commission on a limited basis, and a majority of its members would have to approve the entry of new member states into the EC. In Box 12.2 we describe the main EU political institutions, most of whose current roles and powers were defined by the SEA.

Delors's initiative required each nation to sacrifice its interests on hundreds of small issues— many of which had important domestic political effects—in order to achieve the four freedoms. As expected, national sovereignty and community interests often conflict with one another. For example, environmentalism is an important social value in Germany, and the Green Party is a potent political force on some issues. Germany wants to have its own high environmental standards adopted as EU standards, but poorer countries such as Greece and Portugal have opposed these environmental regulations as too costly.

Another example involves the CAP, which came under fire in the 1990s. Thatcher complained that it was no longer affordable, given how large a percentage of the EU budget

it often accounted for. The British received only a small amount from it compared to the French and others. Also, the CAP's vast production subsidies often led to overproduction in the farm sector, which frequently necessitated selling off or dumping EU surplus commodities in foreign markets, which in turn drove down farm prices. Moreover, the CAP harmed poor farmers in LDCs by limiting their access to EU markets.

The SEA was a compromise between those who favored more integration leading to political union and those such as Britons and Danes who preferred an EC with limited obligations related primarily to a single market. The SEA increased the power and authority of EU executive agencies, setting up many future problems related to cooperation driven from the top of the EU and institutions with a democratic deficit.

EU POLITICAL INSTITUTIONS

European integration has always been as much a political process as an economic one. Since the 1950s, European elites have designed political institutions to make policies, settle disputes, and define their community's values and goals. They have tried to delicately balance national interests against European-wide interests. With both intergovernmental and supranational qualities, the EU institutions were designed so as not to be dominated by any one power or small group of member states. By the 1980s the major EU institutions looked the way they do now. Below is a description of the five most important institutions today.

- The European Council, comprising the heads of state and government of all member states, meets at least twice every six months. It engages in strategic decision making such as setting EU priorities, negotiating EU treaties, and agreeing on the EU's budget. The President of the European Council (currently Donald Tusk) is elected for a two-and-a-half year term, chairs European Council meetings, tries to build EU consensus, and represents the EU in foreign relations (along with the European "foreign minister" who is called the High Representative of the Union for Foreign Affairs and Security Policy).
- The Council of the European Union (or Council of Ministers) is composed of a single representative from each member nation and is the main lawmaking body of the E U. It makes key legislative decisions—often in cooperation with the Commission and the Parliament. It also plays an important role in deciding foreign, fiscal, and economic policies. Each EU member has a Permanent Representative in Brussels (the EU "capital") who does the day-to-day political and technical work of preparing decisions to submit to the Council of Ministers.
- The European Commission, composed of a president and twenty-seven commissioners (one for each member state), acts as the E U's executive cabinet. Each commissioner—appointed for a five-year term—has a specific "portfolio" of responsibilities such as competition policy, trade, or agriculture. Decisions are taken by absolute majority (with a strong tendency to achieve a *de facto* consensus). The Commission designs policy programs and budgetary proposals, monitors implementation of EU laws, and represents Europe in international organizations. It has a staff of more than 32,000 people.
- The European Parliament, whose members are directly elected by European citizens for five-year terms, has become like a traditional parliament. It has 754 deputies who are organized along political party lines and not according to national citizenship. It participates in drafting policy programs and European legislation and votes on the EU budget. Recently, the European Council has worked to increase the importance and influence of the EP in an attempt to make

the overall legislative process more democratic.
- The European Court of Justice (ECJ) is composed of twenty-seven judges and eight advocates-general who are appointed to six-year terms. It adjudicates legal conflicts between EU institutions and between the EU and member states. Because its decisions usually emphasize the priority of European law over national legislation, it is usually regarded as an important promoter of European integration.

Maastricht and Three More Treaties: Broadening and Deepening

With the fall of the Berlin Wall and the collapse of socialist regimes in Central and Eastern Europe starting in late 1989, the Western European countries faced a double challenge: reunification of the formerly socialist German Democratic Republic with the Federal Republic of Germany and applications for membership from most of the ex-Soviet bloc countries. The Treaty of Maastricht, which formally established the European Union in 1992, was mainly a result of negotiations during the process of German reunification. Prime Minister Margaret Thatcher and French president François Mitterrand were reluctant to accept a unified Germany, which invoked memories of German domination in Europe. France proposed a monetary union that it believed would chain Germany to the rest of the EU through a common currency and force Germany to give up the most powerful symbol of its economic strength, the Deutsche Mark.

In Maastricht, the Netherlands, in January 1992, twelve state leaders decided to:

- Transform the European Community into a European Union;
- Establish the Economic and Monetary Union (EMU) by 1999 to replace the members' national currencies with one common currency (the euro) in 2002;
- Establish a European Central Bank (ECB) that would be independent in its monetary policies from other European institutions and national governments and that would be committed to the of and
- Establish three foundational "pillars" of the EU dealing with different policy areas and different decision-making processes.

Along with the creation of the EU, the first pillar aimed to implement the EMU with a single currency and a single monetary policy. Money would be saved by eliminating the cost of currency exchanges. However, central banks would no longer be able to fine-tune their economies via interest rate adjustments.

Officials largely disregarded warnings about potential problems with the EMU, in part because of their belief that markets would not fail. The EMU lacked the conditions that economists consider necessary for an "Optimal Currency Area" (OCA),"[11] Although the EU had a single monetary policy when the financial crisis started in 2008, its lack of a common fiscal policy prevented it from raising taxes to cover state debt. Differences in

industrial specialization between countries, lack of labor mobility, and lack of a debt relief program also threatened the EMU's viability. The new ECB and its president were given limited powers. Because of its economic weight, Germany played a major role in choosing the bank's president, who was expected to emphasize controlling inflation over stimulating economic growth by pumping more money into the economy.

The second EU pillar, the Common Foreign and Security Policy (CFSP), was an effort to present a unified "voice" to the rest of the world. Diplomatic actions were to be based on unanimity of state officials, with the Commission limited to giving suggestions on issues like safeguarding common values, EU independence, strengthening security, and promoting peace and human rights. Despite the EU's good intentions, it was difficult to achieve a unified voice, as was evident in the Iraq crisis of 2003 and in Libya in 2011.

The third pillar, Justice and Home Affairs, was meant to increase cooperation around asylum, external border controls, immigration, drugs, and international crime.

"Opt-out" clauses were inserted in the Maastricht Treaty to help ensure that states would approve the agreement.[12] In a 1992 referendum, Denmark rejected the Treaty. The German Supreme Court also challenged it, citing the transfer of powers from German states to Brussels. Both countries eventually approved the Treaty while complaining about its complicated decision-making procedures. However, as Andres Staab notes, "the notion of European solidarity, of a one-size-fits-all Europe, was now gone."[13]

Gillingham points to the breakdown of the Brussels machinery in the early 1990s as a crucial moment in EU history. He criticizes the Maastricht Treaty for being bloated, which was Delors's doing. Different types of capitalism in the EU made it difficult to harmonize economies. Furthermore, the Brussels government machinery had become a "bewildering complex" backed up by "byzantine" and "opaque" procedures that lacked legitimacy, transparency, and accountability.[14]

In a series of three other major treaties after Maastricht, the EU attempted to strengthen the authority of the EC and European Council while giving the EP more power in relation to the Council. It also tried to push forward an agreement on the fundamental rights of EU citizens. The result so far has been about as "meaningless" as the three pillars.

The Treaty of Amsterdam began as an effort in 1997 to give teeth to the Maastricht Treaty. Its goals were to:

- Clarify European citizenship and people's rights;
- Provide for more cooperation between police and customs forces;
- Create a High Representative for Common Foreign and Security Policy (CFSP); and
- Expand EP powers.

Some portrayed this accord as a shift from the Treaty of Rome, which emphasized trade and the economy, to a focus on EU citizenship, employment, and cultural rights. To promote freedom of movement, the Treaty of Amsterdam officially recognized the 1995 Schengen Agreement. The High Representative for the CFSP did not give the EU a stronger voice in the world, but there was closer cooperation on immigration and asylum.

Some judged the Treaty of Amsterdam as an ambitious public-relations effort.

The Treaty of Nice (2000) deepened EU institutional authority and responsibilities in the expectation that new states would enter the EU. It extended EP powers to cover more issues and to limit the number of delegates to 732.

In December 2001, the European Council agreed to launch an effort to draw up a new European Constitution. Accordingly, in 2002 the EU tasked a European Convention with drafting a constitution for Europe. In 2004, the president of the convention, former French president Valéry Giscard d'Estaing, presented the result: a draft constitution that reflected a compromise between the need to streamline the decision-making processes, the desire for more political integration, and the fear of giving up too much sovereignty to the EU. The proposed constitution died in May 2005. It did not include a Charter on Fundamental Rights and was criticized for being too complicated.

The number of EU members increased from fifteen to twenty-five in 2004, and in 2007 Bulgaria and Romania joined the Union.

Finally, the Treaty of Lisbon was ratified in November 2009 and came into effect in December 2009. Its main features included:

- An EP having equal standing with the Council of the EU in most social, economic, and environmental policies;
- A new High Representative of the Union for Foreign Affairs and Security Policy to resolve frequent disagreements among Europeans on foreign policy;
- Abolishment of the complicated three-pillar structure;
- A legally binding Charter of Fundamental Rights; and
- A president of the European Council and an EU foreign minister.

During the 2000s the EU committed to collectively addressing climate change, terrorism, and the proliferation of weapons of mass destruction. But when the world financial crisis started in 2008, numerous cracks appeared in the Eurozone.

THE FINANCIAL CRISES IN THE EU

One of the major criticisms Europeans have of the EU is the failure of its finance and debt agencies to solve the financial crisis that started in Europe in 2008. The debate continues over what to do about the southern Mediterranean states that cannot manage their excessive debt levels. Should Greece be kicked out of the Eurozone or should the Greeks take leave themselves (Grexit)? There are different views about how to solve the debt issue. The austerity approach requires deep cuts in state spending and reforms of political and economic institutions to make them more efficient and effective. The Keynesian approach would be to stimulate economic growth through state spending, force creditors to take a "haircut" on some of their loans, and attract more investment. In the meantime, the intractable debt problems of some EMU countries are pushing them toward potentially defaulting on their debt or dropping out of the Eurozone.

The EMU: Good Intentions

When the European Monetary System became the Economic and Monetary Union (EMU) in 1999, it provided its eleven original members a detailed timetable to phase out national currencies and introduce the euro in 2002. Its regulations bound members to maintain a government deficit of no more than 3 percent of GDP, while gross public debt could go no higher than 60 percent of GDP.

When the euro first went into circulation it was quite successful. It competed with the U.S. dollar and speculators thought it could become the world's new top currency (see Chapter 8). Under the surface, though, things were not so great. As in many "hot economy" situations, debt levels were rising in many EMU states. Amazingly, the EMU's creators did not envision the possibility of a systemic crisis or the withdrawal of one or more of its members. In fact, the rules prohibited the bailout of any member. Many warned that the EMU was not an OCA. Lacking a common fiscal policy and other deficiencies made future major problems likely.[15]

Meanwhile, because of its strong economy, Germany played a major role in establishing a "convergence" interest rate near 1 percent for the ECB. The low rate was meant to generate political support for the EMU, but it would also encourage conspicuous spending and debt accumulation, especially in the southern Mediterranean states. Note that at first France and Germany routinely abused the gross public debt rule. (Later Germany would adopt a rigorous austerity and reform program of its own to make its trade more competitive.[16]) However, because most EMU countries had been doing quite well, no one seemed to care if countries violated the public debt rule. Multinational banks, other financial institutions, and private investors bankrolled IT industries, real estate and housing, tourism, pharmaceuticals, and infrastructure development. London, Paris, Barcelona, and Milan were places to hang out or buy a retirement condo (especially Paris). Spain and Portugal were nice places to join a country club.

By 2008 the U.S. financial crisis was bleeding into the EU, which already had problems of its own. The interbank lending freeze in the summer of 2007 had kept many countries from borrowing to cover their sovereign (public) debt. As the U.S. crisis worsened, European governments hurriedly attempted to support their banks as the impact of the crisis spread throughout the community. Because of tight interconnections between banks and financial institutions, some worried about contagion—that bankruptcies could easily spill over into other indebted countries and ignite a second Great Depression.[17]

Once the crisis started, rating agencies quickly downgraded Greece, Ireland, and Portugal. Before long investors were targeting the so-called PIIGS—Portugal, Ireland, Italy, Greece and Spain—and driving up their borrowing costs. In 2009 Greek president George Papandreou announced that Greece's level of debt was much higher than previously stated, which led some to argue that Greece might have gotten into the EMU under false pretenses. A close look at Greece's situation reveals that, as in other cases, rating agencies gave Greece high marks, enabling it to borrow excessively. In addition, access to easy credit had encouraged Greece to hire more government workers and increase pensions, welfare benefits and social services. If Greece was to avoid bankruptcy, it would need financial assistance from outside the country.

In May 2010, Greece was finally granted a bailout of €110 billion from the EC and the IMF, which along with the ECB became known as the Troika. Ireland and Portugal received smaller bailouts. All three "bailout" packages had controversial IMF-imposed conditions that required deep cuts in state pensions, aid to the elderly, and educational programs. A host of other measures aimed at significantly reducing state expenditures.[18] In all three states, the effects of such austerity led to huge demonstrations and in many cases riots and violence.

Greece's first bailout package in 2010 required it to lay off thousands of civil servants and decrease the minimum wage by more than 20 percent. Protests led to three deaths, igniting a fierce debate throughout the EMU between pro-austerity supporters and those who favored Keynesian policies that would supposedly help create jobs and preserve more social welfare benefits.

Surprisingly, Ireland accepted austerity measures more readily than the other heavy debtors. The "Celtic Tiger" had been a model of success with one of fastest growing economies in the world. Its sharp rise in sovereign debt, as in the United States, primarily reflected the collapse of real estate markets. The Irish had overbuilt new offices, homes, and apartments, generating a speculative bubble that burst in 2007. In 2008 a slowdown in the economy brought on mortgage defaults. Empty houses and boarded up buildings littered the landscape; entire neighborhoods were abandoned.

In a last-ditch effort to save confidence in its banks, in September 2008 the Irish government guaranteed all of the debt (€106 billion) of its six largest banks, which had financed much of the real estate bubble. Spain would later bail out its banks, too. Many structuralists note that the Irish government bailout was used to pay off the IMF and bondholders, making taxpayers essentially responsible for covering private debt.

Before the crisis, Portugal consistently ranked above many other member states in

percentage of high school graduates, ratio of exports to GDP, and measures of innovation. Its debt in 2007–72 percent of GDP—was lower than Greece's at 109 percent (see Figure 12.2). Still, the EC accused it of having a debt problem and too many bureaucrats with inflated wages and pension liabilities. Bond traders, credit ratings agencies, and investment speculators turned sour on Portugal.

In Portugal, Ireland, and Greece, austerity raised unemployment rates. In 2012, youth unemployment reached over 30 percent in Ireland and over 50 percent in Greece. Paul Krugman points out that before the crisis Spain had low debt and a budget surplus.[19] By 2012, however, it had the highest overall unemployment rate in the EU-24.8 percent—which in turn made the government afraid of the economic and social consequences of laying off state employees. Many young people emigrated from the EU and headed to Brazil, Canada, and Australia, possibly in response to the financial crisis. Others left urban areas to find work in the countryside, where chances of survival might be better. Meanwhile, debt increased and economic growth decreased in the short term.

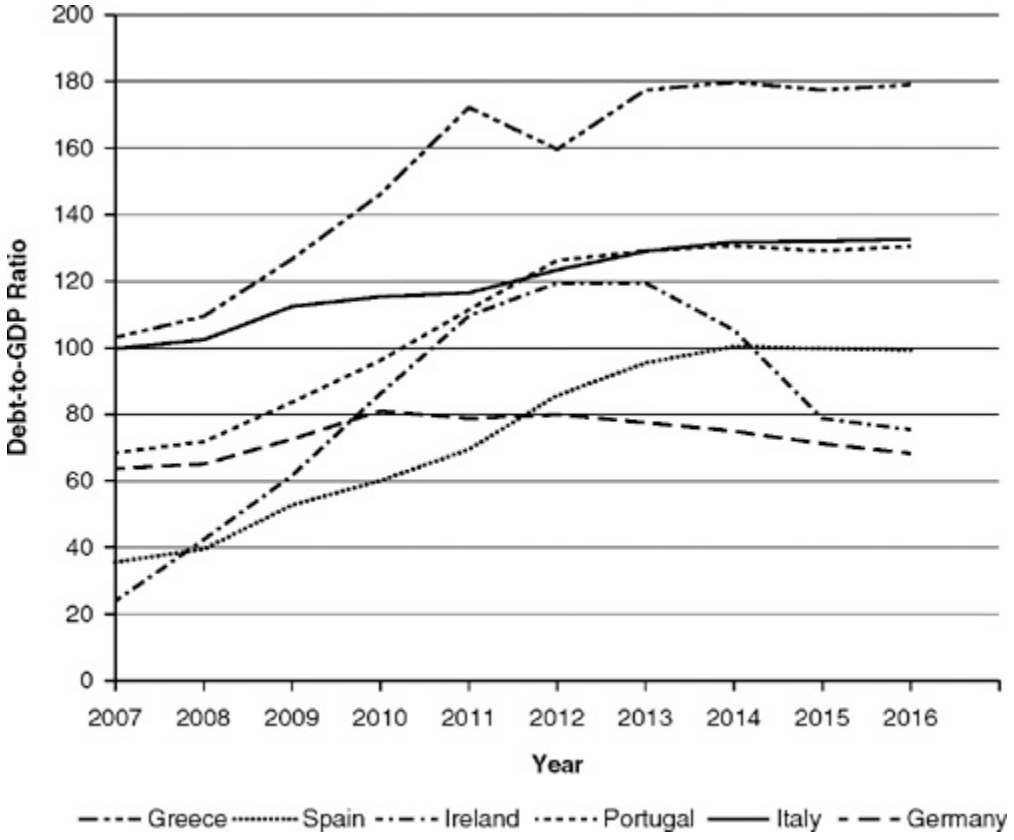


FIGURE 12.2
Ratio of Government Debt to GDP for Selected European Countries, 2007–2016

Source: Data from Eurostat, "Government Deficit/Surplus, Debt and Associated Data," at http://ec.europa.eu/eurostat/web/government-finance-statistics/data/database.

During debt negotiations, international lenders and some northern states (Germany in particular) argued that reform and austerity measures were the best way to reduce the levels

of sovereign debt, stabilize credit markets, and restore investor confidence in the poorer EMU countries. States had to be responsible for their debts and obey the rules for borrowers. However, as might be expected, borrowers argued for Keynesian measures to stimulate the economy and put money into the pockets of workers and the poor. Draconian cuts in social benefits met with strong public resistance in the form of protests, demonstrations, and even violence. By most measures, austerity was failing to achieve positive results.

The debt problem in Europe was not solely due to government profligacy; a more complicated story shows that structural conditions led countries to spend excessively before the crisis started. While the debt of the PIIGS and other states did reach high levels, officials did not view it as a problem until the recession crisis started in 2008. Figure 12.3 below highlights how much debt several Eurozone states had before the crisis and how much they had in 2010 and later.

Before the crisis began, Europe's banks and investors had profited greatly from investment opportunities in the south and elsewhere throughout the eurozone. Thus, structuralists and heterodox liberals charge that responsibility for debt problems must be shared by both lenders and debtors. Yet EMU policies involving Germany and the Troika favored the IMF and investors the most. According to some observers, much of the money investors made was moved into stronger economies or into Swiss or Cayman Islands banks, leaving the middle class and poor to pay the bill.

This raises the question of why Germany and the Troika, and the investors they supported, benefited so much while the masses in debtor states paid such a high a price. It must be acknowledged, however, that aside from Greece and Italy, the other three PIIGS gradually recovered. Growth turned positive in Ireland in 2013 and in Spain and Portugal in 2014. In fact, many officials praised Portugal, much to its displeasure, for being a model case for austerity.

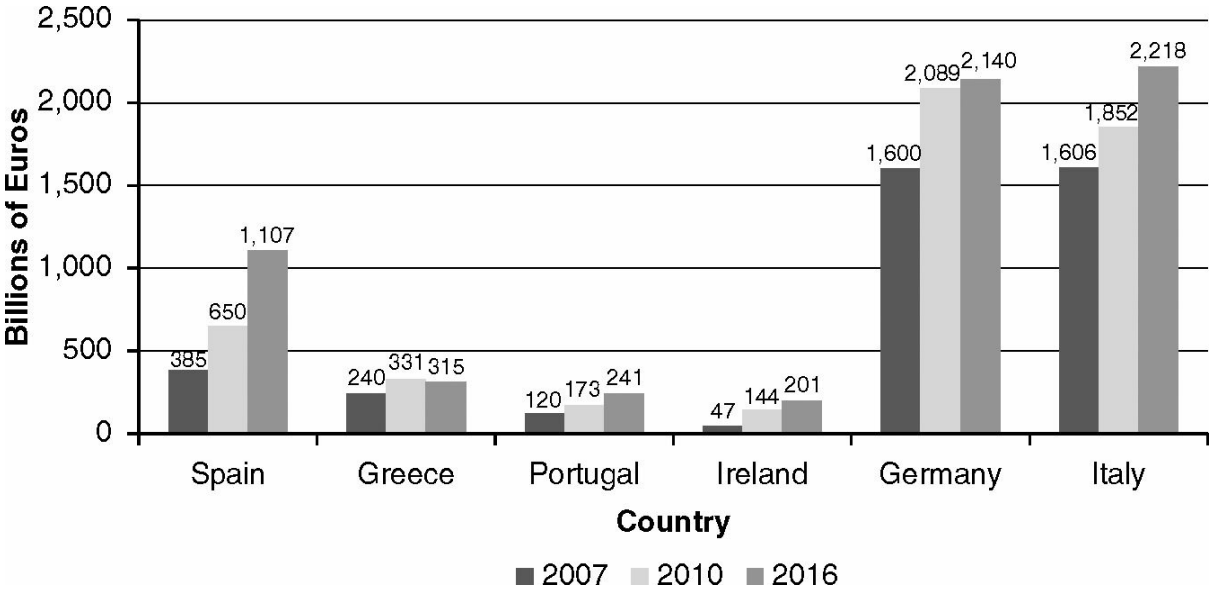


FIGURE 12.3

Government Debt of Selected European Countries in 2007, 2010, and 2016

Source: Data from Eurostat, "Government Deficit/Surplus, Debt and Associated Data," at http://ec.europa.eu/eurostat/web/government-fin ance-stat i st i cs/data/database.

THE LONG GREEK CRISIS

After two more bailout loans in 2012 and 2015, Greece remained the southern Mediterranean state with the highest level of debt as a percentage of GDP. In the first half of 2017 it again endured grueling negotiations with the Troika before the Eurozone members agreed to give it another loan worth €8.5 billion to head off a certain default. However, the Troika delayed until 2018 negotiations on providing Greece real debt relief, which most observers insist is necessary. As noted already, the Greek situation is one that many Euroskeptics mention in their criticisms of the EU, not so much for what Greece has done, but because the EMU cannot solve the problem.

After Greece's first bailout, it came as little surprise that the Greeks would soon need another one. The criticisms aimed at the Greeks were:

- should not have been into the EMU in the first
- They have always been profligate spenders;
- They assumed that they would be bailed out because they were "too big to fail" and because the Eurozone would fear contagion;
- Because they were not serious about implementing state reforms and austerity, they needed to be a lesson; and
- Their ineffective state administration badly needed to collect more taxes.

Economically stronger states such as Germany, Austria, and the Netherlands feared that rescuing weaker states like Greece would reward and perpetuate moral hazard, i.e., encourage weak states to continue their carefree ways with the confidence that the Eurozone would bail them out. The Germans also did not trust the Greeks to keep their agreement to implement more austerity and carry out government reforms in exchange for another bailout package. Former U.S. Treasury Secretary Timothy Geithner recounts that at a meeting in Canada in 2010, German finance officials told him (he is paraphrasing), "We're going to teach the Greeks a lesson…. They lied to us. They suck and they were profligate and took advantage of the whole basic thing and we're going to crush them."[20] Moreover, because Germany had the strongest economy, it would have to foot most of the bailout bill.

During negotiations for the second loan to Greece, relations between officials often became acrimonious and personal. French president Nicolas Sarkozy gave German Chancellor Angela Merkel a hard time, suggesting that France would support the interests of the southern states. At one point in 2012, German officials suggested that Greece leave the EMU (Grexit) and construct a new financial system based on its old currency, the drachma. They hoped that Greece would take an "orderly" exit from the Eurozone so as not to spook markets and risk another recession.

The Germans and Greeks carried on acrimoniously in their newspaper cartoons. In one case the Greeks doctored a photo of Merkel to show her in a Nazi uniform. They accused

her of using "jackboot" (strong arm) tactics to suppress the Greek people like the Germans did when they occupied Greece during World War II.

More seriously, some Greeks felt that the Germans had pushed austerity so far that Greece would be better off exiting the EMU so that it could devalue its own currency to regain some economic advantage.

In 2012, in the face of growing anti-austerity protests, Greece received a second bailout worth €130 billion that required more austerity measures. As part of this agreement, private investors agreed to take a 53.5 percent "haircut" (loss on their investments in Greek bonds) to reduce Greece's overall debt. On the weekend when the Greek Parliament approved austerity measures the burnt dozens of in Athens.

This time austerity cut deep. Education funding was cut sharply. Social services were reduced, including elderly care, transportation, garbage pickup, and maintenance of infrastructure and collective facilities. Once again the situation ignited a contentious debate over how to solve Greece's debt problem: should there be Keynesian stimulus or deep austerity? And once again the international press covered major demonstrations, riots, and sometimes violent street battles between police and protestors.

Some scholars blamed the northern nations and Germany for the continuing Greek debt crisis because:

- They demanded austerity and reforms that did not solve the debt problem. In fact, they made it worse.
- Germany's export-oriented growth policy gave it an unfair trade advantage over other states such as Greece.
- They refused to offer Greece significant debt relief.

Heterodox liberals and structuralists have consistently argued that austerity is the wrong policy for states saddled with so much debt. Deep cuts in state spending only undermine growth and raise unemployment rates, making it harder to shrink the principal on debt.[21] This vicious "debt cycle" drives up the cost of borrowing, which in turn generates the need for more borrowing. Another argument is that austerity excessively punishes the middle class and poor, which shrinks the economy and causes investors to lose even more confidence. Finally, austerity has proven to be nothing but a political, economic, and social disaster for Greece.

The ECB's president Mario Draghi famously said in 2012 that he would "do whatever it takes to preserve the Euro." His comment soon boosted the value of the euro. The small European Financial Stability Facility (EFSF) was replaced by the European Stability Mechanism (ESM), a permanent rescue fund that can loan up to €500 billion to countries in need. The IMF also created another fund to lend to European countries.[22] Draghi also proposed that the ECB should buy unlimited government bonds to help countries that abided by IMF conditions.

Some experts blame Germany's export-oriented trade policy for leading to a huge balance of trade surplus, which had the effect of reducing potential exports from debtor

countries such as Greece.[23] Instead of encouraging more domestic spending on imports from other EU states, Germany intentionally abdicated its hegemonic responsibility, which is to absorb some of the cost of maintaining economic stability by helping Greece and other states through economic recovery.[24] Finally, because Greece once again borrowed just enough to make do temporarily, it was clear that investors and the Troika did not think it was too big to fail.

The Greek economist George Zestos suggests that much of the problem surrounding the Grexit situation was Chancellor Angela Merkel's fault.[25] He gives six reasons, namely that she:

- Waited too long to address the crisis;
- Is "obsessed" with austerity;
- Has no empathy for Greeks;
- Lacks leadership and has advisors who cannot speak with one voice;
- Is giving up on German hegemony in the EU; and
- Faces a lot of domestic pressure from her own party and others.

Loans 3 and 4

Greece's continuing economic recession, high level of unemployment, and political conflict led to the need for still another loan in 2015 to deal with its debt. In the run up to the election in 2015 to replace outgoing president Karolos Papoulias, the left-wing Syriza party led by Alexis Tsipras promised to reverse the austerity measures under which Greece was living. In January 2015 Syriza won enough votes to organize a coalition government headed by Prime Minister Tsipras and his finance minister Yanis Varoufakis.

However, by the end of June 2015, after efforts to collect more taxes had largely failed, Greece was again close to defaulting on payment on an IMF loan and needed a new bailout. Tsipras imposed monetary controls limiting bank withdrawals by Greek citizens to no more than the equivalent of $66 a day. Tsipras scheduled a referendum to let the Greek people decide on whether to accept the austerity measures that the Troika demanded as a condition of the bailout. After Greeks voted 61 to 39 percent *against* austerity measures, firebrand Varoufakis resigned.

Meanwhile, Germany's Bundestag was wary of the deal and Merkel was concerned that it might affect her domestic support. Finland, Austria, and the Netherlands were all tough on Greece, but Spain and Italy argued for leniency for Greece. In the end, the Troika was apprehensive but did not want to risk the collapse of the EMU. Tsipras renegotiated an €86 billion bailout deal with even harsher austerity demands. He claimed that his motive was that he did not want Greece to leave the Eurozone. After the Greek Parliament approved the government's bailout measures, Tsipras resigned. In a snap election a month later, he became prime minister again and formed a coalition government that began implementing the new loan agreement. The measures included higher taxes for high- and middle-income people, increased deregulation, cut pensions further, and introduced new

taxes on cigarettes, coffee, beer, and wine.

In the spring of 2017 Greece was in trouble yet again. Greece's creditors were locked in a stalemate over its fourth bailout. The IMF and Prime Minister Alexis Tsipras insisted on significant debt relief, but Germany refused. Disagreements caused the bailout negotiations to be postponed. Greece experienced several days of strikes and demonstrations over newly implemented austerity measures.[26] In July 2017 European authorities agreed to give Greece new loans worth €8.5 billion.

Economic Problems in the Rest of the EU

Even outside Greece, a major factor contributing to growing skepticism of the EU has been its failure to solve key economic problems related to the financial crisis and the Eurozone. The Troika's policies helped produce short-term financial stability for northern states but long-term political-economic instability in the south. Paul Krugman argues that while U.S. employment returned to the pre-financial crisis level, most EU countries have still not fully recovered, which undermines support for the EU. Likewise, injections of money into the economy could not cure persistent deflation until early 2017.[27]

Many experts also maintain that tough austerity measures that the Troika and Germany imposed on heavily indebted states drove them deeper into debt. Looking into the structural economic conditions underlining the situation, *New York Times* reporter Jochen Bittner suggests that, until recently, many older people who supported the "ever-closer-union" ideology of past EU integration have become "angry older men" critical of the increasing *inequality* within the EU.[28] The lack of economic success has increased support for populist, anti-immigrant parties, the likes of which Europe has not seen since the Balkan wars in the 1990s.

EU leaders and businesses continue to emphasize reforms that come at the expense of the working class and poor. For example, the presidents of France and Italy have sought to change national laws that deal with the firing of employees. Reform supporters charge that if inefficient workers cannot be fired, they make businesses less competitive globally. On the other hand, critics charge that the goal here is to promote new EU rules on "economic governance" designed to undermine the Italian and French Socialist parties' efforts to protect collective bargaining and trade union influence.[29]

Criticisms of the European Commission have also steadily increased for many reasons. Gillingham notes that the EC has doubled the number of bureaucrats over the last 25 years to 45,000 and imposed burdensome regulations. One example is its detailed rules in areas such as food safety; in 2013 the EC proposed banning olive oil in re-usable bottles, but then withdrew its suggestion after much criticism. It also tried to set quotas for women on company boards. Other criticisms are that the EC is a corrupt, non-transparent organization with numerous bureaucratic turf wars. Giles Merritt argues that the EU is stuck in the twentieth century and needs to be reformed in order to deal effectively with severe issues such as global warming, terrorism, and mass migration. Without cooperation, the states of Europe are "doomed to irrelevance."[30]

THE EU IMMIGRATION CRISIS

In February 2015, a photo of the lifeless body of three-year-old Alan Kurdi, lying face-down on a Turkish beach, appeared in newspapers around the world. The boy and his family had been on their way to join relatives who had already migrated to Canada. Alan's mother and brother also drowned in the Mediterranean; only his father survived. The constructivist IPE framework (see Chapter 5) helps us understand how this image "framed" the immigration crisis for many European citizens. The image captured the plight of hundreds of thousands of refugees and migrants fleeing wars and poverty in the Middle East, South Asia, and Africa, trying to get to the nearest point in Greece or Italy.[31] Many of the migrants are children (see Box 12.3).

What started as relatively few migrants in 2013 turned into a flood by late 2015. The EU had a humanitarian crisis on its hands. In 2015 alone more than one million migrants risked their lives in the cold choppy waters of the Aegean Sea on the short trip between Turkey and Greece or on the Mediterranean between North Africa and Italy. That year, 3,771 drowned while traveling on these sea routes to Europe. Figure 12.4 and Figure 12.5 highlight some of the main countries in Europe where migrants claimed asylum and the top developing countries from which they came.

State officials complained of a lack of funds to support the rush of migrants coming into the EU. Some worried that the migrants could not be assimilated easily in a short period and would destabilize society. Hungary and others started closing down their borders, in violation of the Schengen Agreement's open borders policy. While many Europeans felt deep sympathy for migrants and worked tirelessly to help them, xenophobia and anti-Muslim views also increased, as did the fear of mass Islamification. Many officials insisted that immigrants seeking to improve their chances of a job should be sent back to their first entry point. According to the EU Dublin regulations, applicants for asylum were supposed to register in the first EU country they entered, where they needed to prove they were in severe danger if they returned home. For the vast majority of migrants, the first point of entry was Greece.

CHILD MIGRANTS IN EUROPE[a]

In 2016, more than 100,000 refugee and migrant children arrived in Europe, over one-third of whom were unaccompanied or separated from their parents.[b] Unaccompanied child migrants in Italy are most commonly boys aged 16–17 from West Africa and the Horn of Africa, while those in Greece are boys and girls most commonly from Syria, Iraq, and Afghanistan. In the first six months of 2017, another 12,000 unaccompanied or separated children arrived in Italy and Greece.[c] According to UNICEF, in 2015 and 2016 170,000 unaccompanied and separated children applied for asylum in Europe, and another 100,000 were detained when crossing the U.S.-Mexican border.[d] Gaining access to asylum and residence permits is a slow process, and often children do not understand how legal procedures work. While they wait, they live in makeshift "reception centers," overcrowded urban shelters, and sometimes on the street in destitution.

All child migrants face severe challenges on their journeys. Based on interviews of unaccompanied children, more than half traveled for over six months to reach Italy. They often migrate through irregular means, relying on smugglers and putting themselves at high risk of exploitation and abuse. According to the Alliance for Child Protection in Humanitarian Action:

> Separated children are among the most vulnerable of all children affected by emergencies. Having lost the care and protection of their families and caregivers just when they need them most, these girls and boys are at increased risk of physical and psychological harm, abduction, trafficking and unlawful recruitment or use by armed forces or armed groups, sexual abuse and exploitation, and permanent loss of identity.[e]

Many NGOs and UN agencies are pressuring national governments, the EU, and the G7 to do much more to support child migrants. For example, in March 2017 UNICEF was instrumental in convincing Italy's legislature to pass a law setting comprehensive standards of care for unaccompanied and separated children, including a strict prohibition on turning children away at the border and guarantees of access to basic health care. However, many contend that much more still needs to be done, including by passing comprehensive immigration reform. In the meantime, child migration is only expected to grow worldwide, as violence and poverty in many developing nations drives children to seek better lives abroad.

References

[a] This box was written by Kathleen Porcello and edited by Bradford Dillman.

[b] REACH, "*Children on the Move in Italy and Greece*" (June 2017), at https://reliefweb.int/sites/reliefweb.int/files/resources/reach_ita_grc_report_children_on_the_move_in_italy_and_greece_june_2017.pdf.

[c] UNHCR, UNICEF, and IOM, "*Refugee and Migrant Children in Europe—Accompanied*, Unaccompanied and Separated: Mid year Overview of Trends January—June 2017" (October 2017), at https://reliefweb.int/sites/reliefweb.int/files/resources/60348.pdf.

[d] UNICEF, "*A Child Is a Child: Protecting Children on the Move from Violence, Abuse, and Exploitation*" (May 2017), p. 12, at www.unicef.org/publications/files/UNICEF_A_child_is_a_child_May_2017_EN.pdf.

[e] Alliance for Child Protection in Humanitarian Action, "*Field Handbook on Unaccompanied and Separated Children*," April 2017, Foreword, at https://reliefweb.int/sites/reliefweb.int/files/resources/handbook-web-2-017-0322.pdf.

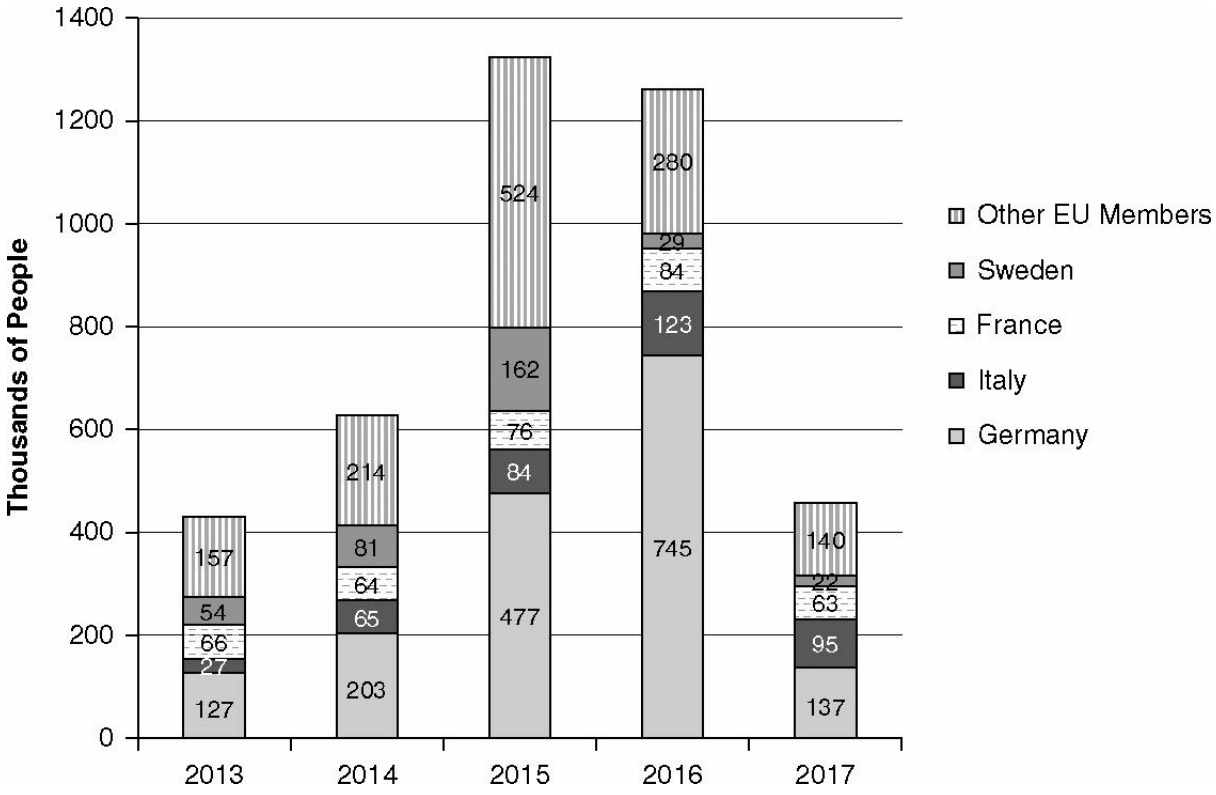


FIGURE 12.4
First-Time Asylum Applicants Per Year in the European Union (in thousands)

Note: Data for 2017 is for the first ten months of 2017.

Source: Data from Eurostat, at http://ec.europa.eu/eurostat/tgm/table.do?tab=table&init=1&language=en&pcode=tps00191&plugin=1.

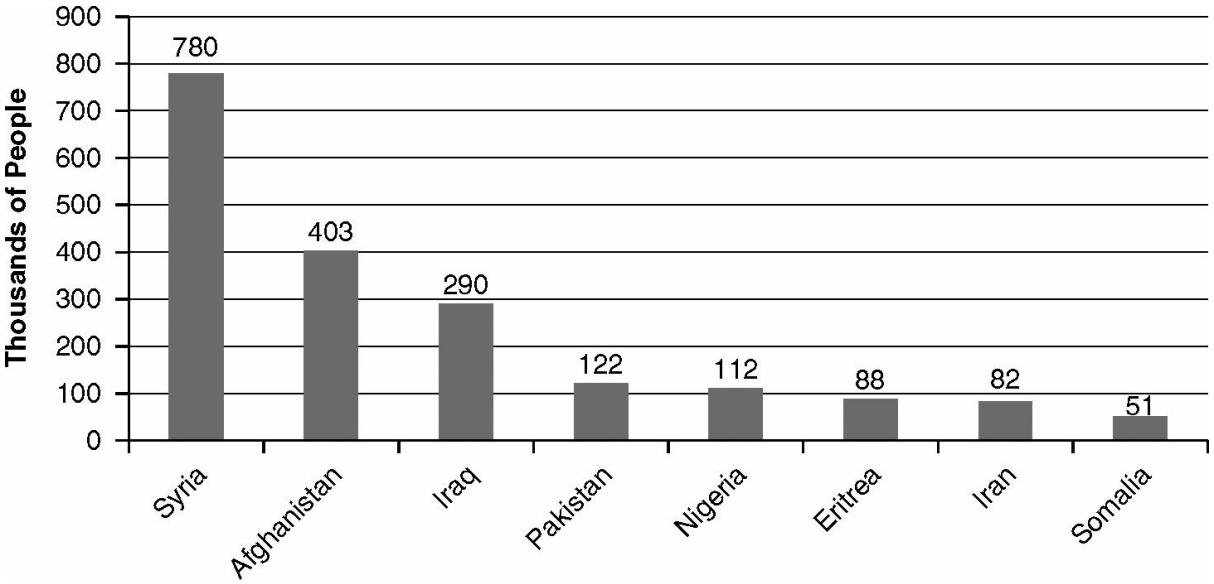


FIGURE 12.5
Number of First-time Asylum Seekers in the EU from the Top 8 Poor Developing Countries, January 2015–September 2017

Source: Data from Eurostat, at http://ec.europa.eu/eurostat/web/asylum-and-managed-migration/data/database.

Both the public and the European Commission were also shocked by the deaths of so many migrants from North Africa trying to reach Europe across the Mediterranean. In May 2015, the EC proposed taking in 20,000 African refugees over two years and distributing them across Europe. Italy, Germany, and Austria strongly supported what was essentially a quota plan for relocating 40,000 refugees across EU member states. Far-right Hungarian Prime Minister Victor Orbân called the plan "mad."[32]

By the spring of 2016 Greece had reached what it felt to be a limit. To care for the refugees, many states and non-governmental organizations (NGOs) set up temporary detention camps, which some critics viewed as prisons with horrible living conditions. The United Nations High Commissioner for Refugees (UNHCR) argued that this policy only created more hardships for both recipient nations and migrants. The EU did not have a plan, and many felt that something had to be done. As with the financial crisis, once again Germany's Chancellor Angela Merkel was looked to the most for regional leadership. Interestingly, she wanted to keep the EU open to migrants and argued that the EU was morally obliged to take them in. However, as we discuss below, her suggestions were met with growing resistance, especially from right-wing and nationalist far-right parties, many of whom had anti-immigrant and racist views. (See Table 1.2 in 1 for a list of and their leaders in the EU.)

Under pressure from German constituents and EU officials, Merkel worked with Turkey on an agreement to deport migrants and non-asylum-seeking immigrants back to Turkey in order to decrease the flow of them into Eastern Europe and relieve the humanitarian crisis. On April 4, 2016, the EU and Turkey both agreed that for each new migrant Turkey took

back, a Syrian would be allowed into Europe. Those returning to Turkey would either settle or be sent back to their home countries. The EU offered Turkey $6.6 billion to assist aid organizations dealing with their 2.7 million Syrian refugees.[33]

Immigration and Terrorism

Besides viewing migrants as a drain on national economies and communities, some European officials also feared that a certain number of them would eventually carry out acts of terrorism. As national leaders and right-wing political parties increasingly framed migrants as a security threat, the EU public became more receptive to strengthening border controls and limiting approvals for asylum. At the same time that the migrant crisis hit the EU between 2015 and mid-2017, a series of high-profile assaults and terrorist attacks occurred, reinforcing concerns about Muslim refugees.

- In January 2015 three French citizens of Algerian and Senegalese descent killed a total of 17 people at the headquarters of the satirical newspaper Charlie Hebdo and at a kosher grocery store in Paris.
- In November 2015 a group of ISIS-inspired assailants killed 130 people and wounded 600 in coordinated attacks in Paris.
- During New Year's Eve festivities at the end of 2015 in Cologne, Hamburg, and other German cities, some 1,200 women were sexually assaulted in public. Many of the men suspected of carrying out the assaults were North African and Arab immigrants.
- In March 2016 three ISIS-inspired terrorists killed 32 people in Brussels airport in Belgium.
- In July 2016 a French-Tunisian extremist killed 84 people in Nice, France by detonating three explosive devices and running over people in a tourist corridor along the city's waterfront.
- In May 2017 a U.K.-born suicide bomber killed 22 people and injured 120 at a pop music concert in Manchester, England.

It is important to note that most of the men who carried out terrorist attacks were not migrants who came in the wave between 2015 and 2017. Most were the children of immigrants from earlier years and held citizenship in EU countries. And yet, the combined effect of these acts was to compound fears of Muslims.

At least three other developments have increased prejudice toward asylum seekers from predominantly Muslim countries and increased concerns about citizens of EU countries who are Muslim. First, since 2011 thousands of individuals from the EU have travelled to the Middle East to train or fight with jihadist groups. European officials fear that many of these men will return to Europe with the intent to carry out terrorist attacks. This is one of the reasons why many EU states want more limits on the granting of asylum to Muslims and more surveillance of Muslims who have returned from extended stays in the Middle East and South Asia.

Second, the fear of terrorism has increased discrimination against Muslims and fueled

efforts to restrict the wearing of headscarves and other kinds of Muslim dress in schools, public buildings, and workplaces. As noted in Box 1.1 in Chapter 1, courts have overruled some restrictions on people's dress as unconstitutional, but the remaining restrictions have stigmatized Muslims.

Third and finally, anxiety about immigrants has helped increase support for far-right nationalist parties. Germany's AfD and the UK's UKIP have explicitly used terrorist attacks to generate more xenophobia and Islamophobia.[34] The AfD repeatedly criticized Chancellor Merkel's open-door policy during the migrant crisis, and even leading members of Merkel's own party, the CDU, and its sister party, the CSU, have called for limiting the number of new asylum seekers each year, speeding up deportations of rejected asylum seekers, and requiring would-be immigrants to secure a German job offer before being granted a visa. In a humiliating defeat in regional assembly elections in September 2016 in Merkel's home district in Mecklenburg-West Pomerania, her CDU party received 19 percent of the vote compared to the AfD's 21 percent.[35] Even though Merkel's CDU/CSU won parliamentary elections in September 2017 with 32.9 percent of the vote, it struggled for months to form a coalition government. Meanwhile, the anti-immigrant AfD surged in popularity, capturing nearly 12.6 percent of the vote and becoming the third largest party in the Bundestag.

BREXIT: A CRY OF ANGER

Many Britons felt strongly that even though the UK had a lot at stake if it left the EU, they were ready to accept the risks. Most of the "Leave" arguments echo criticisms Euroskeptics in general have of the EU. In the case of the UK, criticism of the handling of the financial crisis intensified between 2013 and 2015 at the same time as migrants surged into Europe. Before then, neither the Conservatives nor the Labour Party strongly objected to alternative right ("alt-right") criticism of immigrants, in part because attacks on them were not perceived as resonating with most of the public. In 2013 then Prime Minister David Cameron, in exchange for support for a Conservative bill, allowed for a referendum on UK membership in the EU to be held in 2016. The day after the referendum, Cameron resigned.

Shortly before the referendum, the United Kingdom Independence Party (UKIP) produced a poster showing a long line of refugees crossing a border into the EU that said: "BREAKING POINT: The EU has failed us all. We must break free from the EU and take control of our borders."[36] Many believe that this scare tactic of an invasion of the UK by migrants was the primary factor that helped tip the vote in favor of Leavers.[37]

Before the referendum, the main UK Leave arguments included:

- Great Britain is losing control of its borders and immigrants are destabilizing the UK's political, economic, and social systems.
- The EU has failed to deal with the financial crisis and the negative effects of globalization.
- EU bureaucrats have too much power and have failed to solve many pressing issues.
- The UK's sovereignty has been severely weakened by a supranational entity that does not reflect the UK's national interests.

Fear of the Immigrant Onslaught

Even though the UK is not a member of the Schengen Agreement, it has strict border controls. Many immigrants have sought entry into the UK since 2013. In 2015 thousands amassed in a makeshift camp called "the Jungle" on the French side of the border at Calais. Some 1,500 tried to walk through the Channel Tunnel under the English Channel into England. French officials eventually razed the camp and transferred its occupants to resettlement areas around France.

As on the continent, many Britons claim that migrants have been absorbing low-wage jobs and robbing locals of housing, education, health care, and other state benefits. In reality, the UK was relatively isolated from the rush of migrants to the continent in 2015 and 2016. In 2015 it had a net inflow of 332,000 legal immigrants, more than 40 percent of whom came from other parts of the EU. Net immigration fell to 248,000 in 2016.[38] Nevertheless, the proportion of foreign-born people in the total UK population rose from 7

percent in 1993 to 13.5 percent in 2015.[39] Supporters of immigration have argued that rich counties in the UK need migration to sustain public services and to fill jobs as the proportion of elderly in the population increases. Studies have found that non-EU migrants are net contributors to the economy and that migrants are not displacing other workers. In fact, by mid-2017 the unemployment rate was at 4.4 percent, its lowest since 1975.

Anti-neoliberalism and Anti-globalization

Like many others in the EU, Britons were very critical of EU institutions for muddling through the financial crisis. Some neoliberals claimed that a free Great Britain would be able to deregulate the market to unleash tremendous growth—something Paul Krugman calls "Voodoo economics wrapped in a Union Jack"[40] Many Britons have also complained that neoliberalism and globalization have not helped the working class. Traditional Labour party strongholds in the northeast and Wales have remained economically depressed areas, and many workers have seen their wages decline. Brexit was "a cry of anger and frustration from a class that felt alienated from those who wield power, wealth and privilege, both in their own government and in Brussels."[41]

Situations like this help explain why many people left the Labour party and voted Conservative—not because they necessarily viewed themselves as more conservative, but because they felt *betrayed* by Labour. According to Andrew Higgins, many were desperate for real jobs and a sense of community that they felt they had in the past. Even though studies suggest that only a quarter of Britons have the kind of jobs traditionally associated with the working class, 60 percent still consider themselves as working class. Higgins suggests that this disconnect between perceptions and objective conditions fueled nationalism and even xenophobia, leading to a desire to get back at EU and UK officials and immigrants.[42]

Many neoliberal economists also maintain that immigration is just a distraction from the central issue, which is that the UK's economy is inefficient. Structural economic weaknesses have left Britain less competitive than the United States, China, and other countries in the global political economy. Social democrats, however, argue that more needs to be done to reduce income inequality and address bread-and-butter concerns of the working class like low pay, the unavailability of social housing, and the lack of health services in working-class areas.

The Lack of Sovereignty and National Identity

Still another issue that helped Leavers win the Brexit referendum was the perceived loss of English identity and values.[43] For example, Steven Erlanger describes the situation of many (mostly white) people in Castle Point in the district of Essex who in the past were stuck working in drab places like the East End of London but were able to move out to places with single-family homes, amusement parks, football (soccer) pitches, and an assortment of ethnic restaurants. Over the years, many of these fiercely English and Conservative supporters of Brexit have lost their construction jobs in London to skilled immigrants

working for less pay. Self-reliant and independent, many are nostalgic for the past. They want direct connections with their legislators and an enhanced sense of control over their local communities, instead of "feeling exiled" in their own country.[44]

Rachael Donadio suggests that when the state and working class cannot fix the economy, it is easy to play the race and immigrant cards and revive a nationalist outlook.[45] A weak economy has helped polarize society even more: the less educated versus the more educated, the old versus the young, and the poorer versus the better off. A *New York Times* editorial sums up well the sentiments of many who voted for Brexit:

> It is about ill-defined frustration with the complexities of a changing world and a changing Europe, a loss of faith in mainstream politicians and experts, a nostalgia for a past when nations decided their own fates and kept foreigners out…. The European Union is the epitome of all that has gone wrong, an alien bureaucracy deaf to the traditions and values of its members.[46]

Remainers: An Agenda for the UK

Looking down the road, many Remainers from both sides of the political spectrum are worried that if and when Great Britain leaves the EU, it might:

- Lead to a loss of access to EU trade and investments, which could also undermine the city of London as a major player in global trade and finance;
- Spur Scotland to leave the UK;
- Weaken Britain's role in NATO and undermine transatlantic relations; and/or
- Undermine the UK as a bulwark of peace and democracy.

The primary economic concern of many UK officials and the public in the near term is whether or not Britain will have tariff-free access to the EU's single market. Some would like to see the UK get the same deal Norway has with the EU, whereby it has full access to the Common Market but no power in EU institutions. There has been much wrangling between Prime Minister May and Parliament and between May and the EU Commission about getting the "best deal" in trade. It must be noted, however, that Iceland, Norway, and Switzerland all have different trade arrangements with the EU, contribute to its budget, and accept the principle of free movement of people, a principle that pushed many Britons to vote to leave the EU in the first place.[47]

On March 29, 2017, under Article 50 of the Treaty of Lisbon, Prime Minister May formally applied for the UK to leave the EU. The complicated legal negotiations are expected to take up to two years to complete. EU officials continue to signal that the UK cannot "have its cake and eat it too." The UK is negotiating from a weak position when it comes to new agreements on trade, banking, and other issues.

On June 8, 2017, Prime Minister May called for a snap election to determine how firm a mandate she had to negotiate the terms of Brexit with the EU. Her Conservative party lost

seats in Parliament, leaving officials and the public even more confused about the UK's future. May has promised to carry on with a "hard Brexit," meaning a complete break with the EU. Supporters of a "soft Brexit" want to maintain some residues of EU policies that benefit the UK. By late 2017, it was clear that EU negotiators had the upper hand over the UK: they forced the May government to agree that in transitioning out of the EU, Great Britain would pay the EU near $60 billion through 2020, protect EU citizens' rights to work in the UK, and keep the border between Northern Ireland and the Republic of Ireland relatively unrestricted. Meanwhile, many worry that if UK businesses move to the continent, it could damage the City of London and its status as one of the financial capitals of the world.[48] By mid-2017 large banks had contingency plans to move significant numbers of their employees and even their headquarters to EU cities such as Frankfurt, Paris, Dublin, and Luxembourg—considered potential replacements to London as the financial center of Europe.[49] For many, doing business with the rest of Europe will most likely require them to be inside the EU so as not to have to pay duties.

Brexit could damage not only London but also Wales, northeast England, and Northern Ireland the most. Many poor areas are currently receiving EU support, which is likely to stop. Yet another big issue is the status of British expatriates working in Europe. Their rights, privileges, and benefits may diminish, and they may have difficulty obtaining visas to work in the EU. Still others are concerned about what Brexit means for other regions in the United Kingdom such as Northern Ireland and Scotland. If the UK leaves the EU the Scottish National Party is committed to independence, and most senior Scottish officials are committed to staying in the EU.

CONCLUSION: THE WAY FORWARD OR BACK?

Many accounts of EU history mention a few major problems that stand in the way of pushing integration along into the uncharted territory of a genuine union. Andreas Staab discusses what the EU must do to deal with the ongoing financial crisis in particular. His practical suggestions for preserving the EMU include collectively increasing funding for the ESM (European Stability Mechanism) and giving the ECB more authority to buy up government debt and issue Eurobonds backed by Eurozone members. The northern states have a responsibility to shift more funds to southern nations weighed down by high levels of debt that fuel Euroskepticism and that could easily tear the EU apart. Most importantly, they have a moral obligation to bear more of the cost of preserving the European integration project.

Gillingham argues that unification may not be the best outcome for EU members; he does not believe that the 28 members should seek to achieve the elusive dreams of Delors and other integration visionaries. He argues that from the start the EU has never been a cohesive body or agency. The benefits from cooperation around trade always bore the Community the most fruit. And when EC members faced a common security threat, the EC provided a cause around which they could rally and for which they made sacrifices.

Gillingham's proposal to deal with problematic issues is to pull integration back to where the Community elicits "active cooperation between well-disposed independent sovereign states." There should be a "network of purpose-based, practical, and results-oriented bilateral and multilateral agreements" grounded in a willingness of states to cooperate on shared self-interests.

For supporters of the EC (in contrast to the EU), all might not be lost. There is a possibility of cooperation based on a desire to retain the many benefits of the Common Market. Once again, there is a major security threat from Russia. At a May 2017 NATO meeting in Brussels and a G7 meeting in Sicily, Trump chastised NATO members for not spending the requisite 2 percent of their GDP on defense and hesitated to reaffirm the United States' commitment to Article 5 ("an attack on one is an attack on all"). Perhaps the EU cannot count on the United States any more. Germany and France will need to push for increased cooperation. But Germany must also act more like a hegemon and accept the costs of leading the EU, whether by importing more or cutting the debt burden of states such as Greece and Portugal.

KEY TERMS

European Union 313
Brexit 313
Economic and Monetary Union (EMU) 313
integration 313
Grexit 313
European Coal and Steel Community (ECSC) 315
European Commission (EC) 315
Council of Europe 315
European Economic Community 316
functionalism 317
intergovernmentalism 317
Single European Act (SEA) 319
Treaty of Maastricht 322
European Central Bank (ECB) 322
Troika 325

DISCUSSION QUESTIONS

1. Gillingham and other scholars believe that European leaders sometimes made unwise choices during the European integration process. What are some of those problematic choices and what effects did have?
2. After reading through the whole chapter, do you think Gillingham is correct in characterizing the EU as a nearly defunct institution that is no longer capable of dealing effectively with internal problems and coping with the pressures from the global system? List some examples to support your assessment, including from current news articles.
3. Who bears the most responsibility for the long Greek financial crisis and its consequences for Greek society and the Eurozone as a whole—the Greeks themselves, Germany, the ECB and the IMF, or others? Explain.
4. Brexit has been a controversial issue. Outline some of the reasons why a majority of British voters wanted to leave the EU and some of the arguments of those who wanted to remain. If you had a say in the issue, which side would you support and why?
5. How have the migrant crisis and terrorism affected political trends in the EU? Are the EU's responses to these and other problems consistent with its norms of human rights protection, democracy, and solidarity?
6. Do you think the EU will continue to fragment, or instead hold together without the United Kingdom and meet the challenges it faces?

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CHAPTER
13
Moving into Position: The Rising Powers



The presidents of Brazil, Russia, China, South Africa, and the Prime Minister of India pose for a group photo during the BRICS Summit in Xiamen, China in September 2017.

Source: AP Photo/POOL Kyodo News/Kenzaburo Fukuhara.

After years of preparing the ground, China is determined to take its place as a modern world power.

Tom Miller[1]

In the not-too-distant future we might look back on 2017 as the year that China truly became a Great Power. Until Donald Trump became U.S. president, China had been viewed as a rising challenger to the United States, but one that lacked some of the requisite characteristics of a global leader. Perceptions quickly changed in the turbulent months after Trump entered the White House. While Trump alienated traditional U.S. allies in NATO and the European Union, China's president Xi Jinping pushed ahead with his signature Belt and Road Initiative, a series of mega-infrastructure projects linking China more closely with its Asian neighbors, the Middle East, Russia, Europe, and even Africa. As Trump turned the United States inward economically, abandoning the Trans-Pacific Partnership, Xi defended free trade at the World Economic Forum in Davos, Switzerland. While Trump announced that the United States was withdrawing from the Paris climate accord, China emerged as the global leader against climate change, accelerating its lead as the largest investor in renewable energy in the world. While Trump stressed "America First," Xi

said in February 2017 that China "should guide the international community to jointly build a more just and reasonable new world order." On issue after issue, and in region after region, China seemed eager to fill the vacuum left by a retreating United States.

In truth, China has quite a way to go before it can surpass U.S. wealth, diplomatic influence, and military power. But the signs were clear by 2017 that the rise of the BRICS countries (Brazil, Russia, India, China, and South Africa) is reshaping geopolitical relationships and capital flows around the world.[2] Absorbing more raw materials and food, the BRICS are placing ever more strains on the global environment. They are creating a more multipolar world, which some hope will usher in an age of peace but others fear will lead to new arms races and monumental struggles over access to resources. Their development will determine whether hundreds of millions more people will gain some of the global wealth previously denied to them.

In this chapter we present a number of important theses about the rising powers:

- Their different paths reflect variations in each country's history, size, political system, and policy decisions.
- The experiences of countries in transition lead us to question some assertions in the IPE theories we discussed in the preceding chapters. For example, China shows that economic liberals' belief that capitalism and freedom go together may not always be true. On the other hand, some countries' phenomenal growth under market-friendly policies suggests that mercantilists overestimate the positive outcomes of state guidance of the economy. Many rapid reductions in poverty belie structuralists' belief that global capitalism locks poor countries into a vicious cycle of underdevelopment.
- The rising powers are ineluctably bringing intense competition to Europe, the United States, and Japan—areas that have been losing their labor-intensive manufacturing and some of their ability to dominate international institutions.
- The BRICS will increasingly modify some of the "rules of the game" affecting trade, finance, and security to reflect better their interests, but it is not inevitable that this will undermine the liberal world order or fundamentally threaten the security of the Western powers.

THE EMERGENCE OF THE BRICS

Brazil, Russia, India, China, and South Africa form an unlikely bloc. Their political institutions and histories are quite different. China and India each have more than 1.3 billion people, while Brazil, Russia, and South Africa have populations of 206 million, 142 million, and 55 million, respectively. But they each possess a large territory with abundant natural resources. Each has a significant industrial base (admittedly China's is much larger than the others') and a strong military. All have undergone dramatic economic transitions in the last thirty years as they have transitioned to market-oriented economies deeply integrated into the global capitalist system.

Collectively, the BRICS had higher average rates of growth than the United States, Japan, and the European Union from 1990 to 2017—earning the moniker the "emerging economies." The 2000s were the heyday of the BRICS, when they had some of the fastest growth rates in the world. Growth rates fell after 2010, but still remained robust in India and China. Russia and Brazil fell into recession in 2015 and 2016 as global commodity prices dropped and as Russia faced Western sanctions after its invasion of the Crimea. The BRICS nations' share of global GDP rose from 11 percent in 1990 to 25 percent in 2016.

The growing economic weight of the emerging powers has translated into greater influence in global governance. The BRIC countries began meeting informally in the mid-2000s, then held their first annual summit in 2009. In the wake of the global financial crisis, the four countries pressed for greater representation in international financial institutions. The grouping renamed itself the BRICS with the addition of South Africa in 2011. China and Russia have a strong role in global security issues as permanent members of the UN Security Council. The BRICS members established a New Development Bank (NDB) in 2014 to fund infrastructure projects in emerging economies. In 2016 the IMF approved quota increases for Brazil, Russia, India, and China, strengthening their voting power in the institution. Concomitantly, in 2014 the BRICS formed a Contingent Reserve Arrangement, a $100 billion reserve fund each country could draw on to address short-term balance of payments problems. This move was consistent with efforts by many middle-income countries in Asia and Latin America after the 1997–1998 Asian financial crisis to accumulate enough foreign reserves so as not to have to borrow from the IMF and the World Bank, institutions that had imposed punishing conditionality in previous decades. More generally, the changing global distribution of power in recent years has made it possible for the BRICS and other emerging powers to engage in "financial statecraft," defined as "the intentional use, by national governments, of domestic or international monetary or financial capabilities for the purpose of achieving ongoing foreign policy goals."[3] They have diversified their sources of foreign investment, accumulated foreign reserves as insurance in times of financial instability, and promoted reserve currencies other than the U.S. dollar.

Despite the rising prominence of the BRICS, some scholars caution against exaggerating their newfound power. China has an outsized role among the five, given that it has by far

the largest economy, the most foreign reserves, and the most extensive industrial base. According to Carla Norrlof, the U.S. dollar remains globally dominant, while the Chinese renminbi is unlikely to become an important global currency unless China makes deep reforms in its financial markets and lifts capital controls—moves that might weaken the political power of the Chinese Communist Party.[4] Similarly, Eric Helleiner argues that, although the BRICS have promoted a move away from the dollar, gained more influence in the IMF and the G20, and maintained some capital controls, they have not significantly diminished the "status quo" in which the United States, and to a lesser extent Japan and European countries, dominate global financial and monetary policies.[5]

TRANSITIONS IN RUSSIA

Although the Soviet Union came into existence in 1917, most communist or socialist regimes emerged after the end of World War II in Eastern and Central Europe, North Korea, China, Vietnam, and Cuba. For these states, political and economic power was rooted in a single party whose membership was generally limited to about 5 to 10 percent of the population. Some states developed "personality cults" around leaders like Stalin, Mao, Castro, and Kim Jong-il. Most of the means of production—factories, land, and property—were owned by the state. A large state bureaucracy determined which raw materials, goods, and services should be produced, in what amounts, and at what prices. This cumbersome system of central planning suffered from what János Kornai has described as "soft-budget constraints": state enterprises had little incentive to turn real profits when they could count on cheap state loans and perpetual debt forgiveness.[6]

It is important to remember that in their heydays from the 1930s to the 1970s, many socialist/communist economies generated high growth rates. The Soviets transformed their agrarian, preindustrial society into a military–industrial powerhouse in less than two generations. Contradictions grew worse throughout the 1970s and 1980s. Soviet General Secretary Mikhail Gorbachev responded to declining productivity and sluggish technological innovation with policies of glasnost (openness) and perestroika (restructuring) meant to reform communism, but regimes in Eastern Europe began to collapse in 1989 and by 1991 the Soviet Union had broken up into fifteen separate countries.

Almost all postcommunist countries in the former Warsaw Pact, including Russia, initially suffered severe economic decline and political upheaval. The World Bank estimates that at the start of the financial crisis in 2008 at least 40 percent of people in the postcommunist states (plus Turkey) were living on less than $5 a day. While the Baltic states (Estonia, Latvia, and Lithuania) joined the European Union in 2004, consolidating economic liberalism and social democracy, the transition results were more mixed in the Commonwealth of Independent States (CIS), which includes most of the ex-republics of the former Soviet Union including Russia, Belarus, Ukraine, Armenia, Azerbaijan, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, and Uzbekistan. On average, it was not until 2007 that the GDP in real terms recovered to 1989 levels in these countries.

Important sectors of the Russian economy were sold in the early 1990s to a handful of local investors with ties to the government and the old *nomenklatura* (senior Soviet bureaucrats). The result was the emergence of "oligarchs," a small number of individuals with huge influence in the economy, government, and the media. In the 1990s, Russia suffered a rapid decline in the standard of living as people found their savings wiped out and their salaries unable to keep up with rising prices. Male life expectancy declined precipitously. Although combined life expectancy for both sexes rose to seventy years by 2011, and the fertility rate recovered somewhat to 1.8 births per woman in 2016, political

economist Nicholas Eberstadt argues that the "dying bear's" "demographic disaster" deprives it of the human resources needed to significantly improve its economic performance and military prowess in the future.[7]

Putin's Revival of Russian Nationalism

The election of Vladimir Putin as president in 2000 brought an end to Russia's tentative experiment with weak democracy. According to political scientist M. Steven Fish, the failure of democracy in Russia is primarily due to incomplete economic reforms, a weakened legislature, and the curse of natural resource wealth.[8] Following a stint as prime minister from 2008 to 2012 under his presidential successor, Dmitry Medvedev, Putin was re-elected president in 2012. He turned more autocratic, launching crackdowns on opposition groups and independent media. He has surrounded himself with powerful political allies called the *siloviki*— officials in the Kremlin who have backgrounds in the secret police and intelligence services.

Russia's economy turned around by the start of the millennium, growing at a rate of nearly 7 percent a year from 1998 to 2008. Growth based on exports of oil and raw materials (rather than the development of a diversified market economy) made it possible to increase military spending and accumulate foreign reserves. The 2008 financial crisis revealed weaknesses in the Russian economy, such as weak industry performance, but the economy grew again from 2009 until 2014. Putin's strategy of nurturing state-controlled "national champions" in the energy, minerals, automotive, aerospace, and defense sectors is a risky proposition, given the volatility in world energy prices and the neglect of private sector manufacturing. Russia has lost a lot of potential foreign direct investment from transnational corporations fed up with the lack of rule of law and Kremlin interference in the market. For example, although Swedish retailer Ikea has spent more than $4 billion building fourteen popular malls and several factories in Russia since 2000, it has suffered from fraud, hundreds of legal disputes, and government officials' demands for bribes. Russian officials and crime groups make life difficult for foreign investors who do not accept corruption as a necessary part of business.

Political scientists Juliet Johnson and Seçkin Köstem argue that Russia now practices financial nationalism—a form of state capitalism in which the state uses its control over foreign exchange, credit creation, and the financial system to promote economic development.[9] It seeks to ensure economic sovereignty in a more globalized world. State-owned banks act as instruments of political patronage. Large accumulated foreign reserves from energy exports have helped the government weather economic crises such as the Great Recession.

After Putin annexed Crimea in 2014, Western countries imposed financial sanctions on Russia that made it difficult for state banks and energy companies to borrow in foreign credit markets. Combined with the Saudi-instigated plunge in oil prices, sanctions pushed Russia into a sharp recession. A rapid fall in the value of the ruble in late 2014 (and again in early 2016) led to large-scale capital flight, forcing the government to raise interest rates

and burn through foreign reserves to stabilize the ruble. GDP barely grew in 2014 and fell in 2015 and 2016.

Russia faces many challenges that will reduce its leverage in the international economy, particularly if oil and gas prices stay relatively depressed in the coming years. Once a proud superpower, it now has a GDP just one-tenth the size of the United States' GDP. It is far behind the West technologically, heavily reliant on the export of raw materials, and largely incapable of exporting competitive manufactured goods (other than weapons). Nevertheless, political scientist Rudra Sil argues that of all the BRICS countries, Russia has "the best prospects for boosting both its global economic clout and its population's living standards over the next quarter century."[10] Compared to China, India, and Brazil, it has much higher living standards and levels of education. With abundant natural resources and a powerful military, it does not face the kinds of difficult trade-offs that the other countries do in order to sustain growth.[11]

Interpreting Russia's Global Goals

Since reassuming the presidency in 2012, Putin has promoted a muscular form of nationalism in domestic and foreign affairs. His strategy, say Johnson and Köstem, is to strengthen the alliance of BRICS, develop economic ties with the Asia-Pacific region, and re-assert Russian dominance in the "post-Soviet space."[12] With the BRICS, Russia hopes to redistribute power to govern international finance. It wants to develop its Far East, especially as a supplier of energy and other raw materials to Asia. In 2015 it established an economic integration scheme called the Eurasian Economic Union (EEU) with Belarus, Kazakhstan, Armenia, and Kyrgyzstan "to counter the EU's Eastern Partnership and to boost Russia's global stance by making it the leader of a key regional organization."[13]

Generally speaking, Russian elites perceive the West as having taken advantage of Russia after the Cold War. They want to replace the liberal international order with a multi-polar system that tolerates state capitalism and authoritarian states. Military modernization is a means for Russia to reclaim its Great Power status. Military spending increased steadily from $43 billion in 2009 to $70 billion in 2016 (see Figure 13.1). Russia is building and refurbishing bases in the Arctic as melting ice makes the region more important for shipping and oil and gas extraction. Realists remain concerned about the security threats from an authoritarian Russia that claims spheres of influence around its borders and uses its oil-and-gas wealth to pressure European neighbors. Putin wants a proud Russia to reassert its own interests rather than simply conform to global liberal norms.

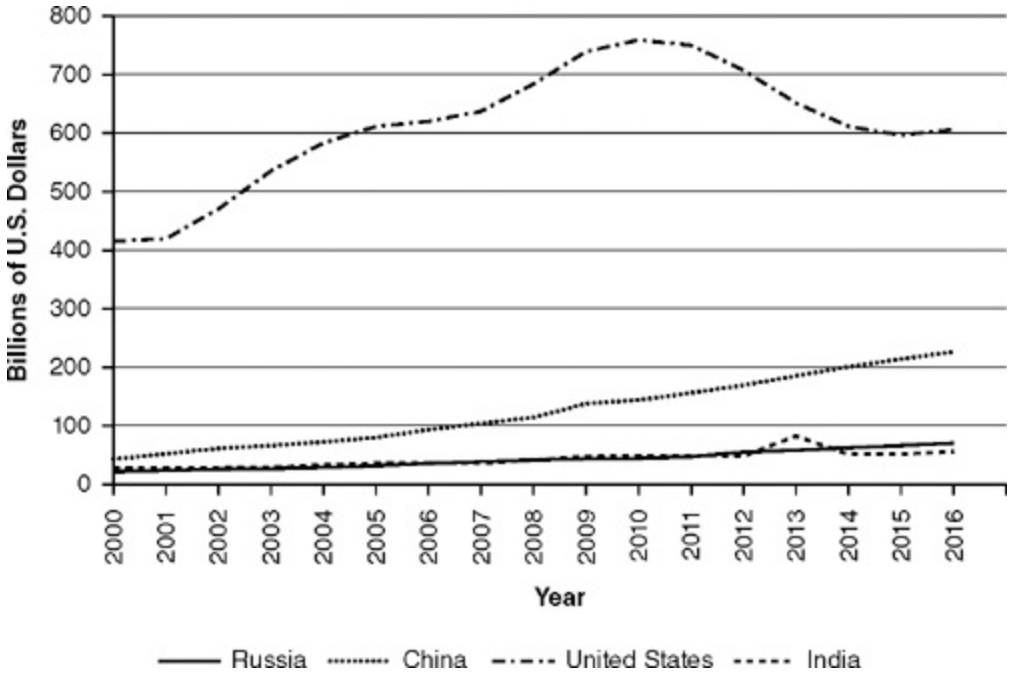


FIGURE 13.1
Military Spending of Russia, China, India, and the United States, 2000–2016 (in constant 2015 USD)

Source: Data from Sipri Military Expenditure Database, at www.sipri.org/sites/default/files/Milex-constant-2015--USD.pdf.

Russia's most significant influence on the international system since 2012 has been through its military interventions in Crimea, Ukraine, and Syria. These aggressive moves come on the heels of military modernization since the late 1990s, a brutal counter-insurgency in Chechnya in the 2000s, and an invasion of Georgia in 2008. What is motivating these and other Russian actions overseas? There are three broad schools of thought about its long-term goals: constructivist, realist, and defensive.

Constructivists interpret Russia's actions as flowing from culture and identity. Putin, like many other Russian elites, sees Russia as the natural leader in its region. There is a desire to restore Russian greatness and command the respect of the West. According to political scientist Nicola Contessi, Russia is discontented with the prerogatives the United States has in international institutions.[14] Ted Hopf argues that "the New Russia understands itself as equal to the West in many respects and superior in some. Imperial Russia becomes a Historical Other with which an authentic Russia can identify."[15] These self-understandings and the belief that Ukrainians and other ethnic Russians in neighboring states are fraternal people with shared culture make intervention seem legitimate.

Political scientist Agnia Grigas views Russia as a realist power, but one that rationally utilizes non-military means when possible to advance its long-term goals.[16] It is undertaking "reimperialization" in post-Soviet countries and cementing ties with ethnic Russians and Russian speakers in nearby countries to expand Russia's territorial control and

influence. For economic and security reasons, Moscow does not want more post-Soviet countries to accede to the European Union, and it seeks leverage over the energy resources and pipelines in their territories. Using soft power such as cultural and business policies, Russia has nurtured a community of Russian "compatriots" who identify with the Russian Federation. It appropriates the discourse of human rights to argue that Russian compatriots (e.g., in Ukraine) suffer discrimination and need its support. It has also granted passports—and hence dual citizenship—to many compatriots in former Soviet republics.

The third perspective understands Russian actions as more defensive. The expansion of NATO and the West's fomenting of regime change in Georgia and Ukraine spurred Moscow to strive for a new Great Power status.[17] After the fall of the government of Victor Yanukovych in Ukraine, Putin sent troops to occupy Crimea and provided military support to Russian-speaking separatists in eastern Ukraine. Similarly, Russia's direct entry into the Syrian war in September 2015 seemed to be a last-ditch effort to save its ally Bashar al-Assad from rebels supported by the United States and its Gulf Arab countries. Having been completely sidelined in the Middle East after the end of the Cold War, Russia was keen to reassert its presence there via Syria.

More broadly, Robert Legvold believes that a new Cold War has seen the West use economic coercion against Russia, such as kicking it out of the G8 and applying sanctions on its banking, natural resources, and defense industries. That a country as important as Russia has become the target of economic warfare may encourage China and Russia to "create institutions competing with, rather than complementing, the institutions that have been the cornerstone of the international economic order."[18]

BRAZIL: THE COSTS OF SUCCESS

To some people, Brazil conjures images of white-sand beaches, samba music, the extravagance of Carnivál, and the bikini-clad Girl from Ipanema (immortalized in a Frank Sinatra song). To others, it is better known for its high incidence of gun violence and one of the highest rates of income inequality in the world. Both of these idealized, polar-opposite images of Brazil obscure the country's complicated history. Nearly the size of the continental United States, it is a country of immigrants who came in successive waves from Europe, Africa, Japan, China, and even North America. Although it is a cultural "melting pot," lasting legacies of exploitation and poverty have yet to be overcome.

From Colonialism to Liberalization

From the sixteenth to the nineteenth centuries, Brazil was a Portuguese colony, enriching the crown with sugar and coffee from vast plantations on the coasts and gold mined by *bandeirantes* in the vast interior. After independence in 1822, most economic activity was concentrated on the coast; the interior of the country was (relatively speaking) sparsely populated.

Beginning in the 1930s, Brazil embarked on a successful program of import-substitution industrialization. From 1945 to 1980, its average annual rate of growth topped 7 percent. In 1956, President Jucelino Kubitschek made it his mission to integrate the vast countryside with the "modern" coastal cities by building a new capital called Brasília a thousand kilometers inland, filled with high-modernist buildings designed by architect Oscar Niemeyer.

A decade later, however, military officers overthrew the democratically elected government of João Goulart, ruling the country as a dictatorship until 1985. Despite political and cultural repression, the country experienced an economic boom in the 1960s and 1970s—creating strong manufacturing, agricultural, and technological sectors. However, growth depended on heavy borrowing from international creditors. By 1980, Brazil—like countries throughout Latin America—was on the verge of defaulting on its international debt. The IMF arrived with its classic bargain: financial bailout in exchange for strict structural adjustment.

The 1980s turned into the so-called Lost Decade. Brazil's rate of annual real GDP growth was less than 2 percent from 1980–1994. Although plagued by high inflation and high interest rates, Brazil eventually clawed its way out of crushing debt. Ironically, state investments in industry, agriculture, and energy during the import-substitution period had created a solid foundation for development when the global economy rebounded in the 1990s. Then, beginning in 1994, democratically elected president Fernando Henrique Cardoso—a former dependency theorist—accelerated reforms with his "Real Plan" which stabilized Brazil's currency, tamed inflation, and broke up state monopolies. Nevertheless, these reforms, especially fiscal austerity and tax increases, rankled the country's working

poor.

Following the re-election of Cardoso in 1998, Brazil began to be perceived as a model for stability and successful democratization within the Latin American region. It emerged as one of the world's most important exporters of agricultural products and ethanol.

The Rise of Brazil under Lula

Brazil's coronation as a major rising power coincided with the election of populist Labor Party candidate Luiz Inácio Lula da Silva as president in 2002. A long-time union leader admired by Brazil's urban poor, Lula grew up with little formal education and spent years as a manual laborer in the slums of São Paulo. He famously lost a finger to a lathe in an auto-parts plant at the age of fourteen. His election was part of a wave of victories for leftist Latin American presidents, including Hugo Chavez of Venezuela (elected in 1999), Evo Morales of Bolivia (2006), Cristina Fernandez de Kirchner of Argentina (2007), and Fernando Lugo of Paraguay (2008).

Despite his populist credentials, Lula also quietly embraced free trade and freer markets. In the World Trade Organization, Brazilian officials called for *more* market access and *fewer* trade barriers in the United States and Europe. Lula spent generously on social programs but also pushed for privatization and export-oriented growth. GDP grew at an annual rate of 4.8 percent between 2004 and 2008.[19] His crowning economic achievement was the Fome Zero (Zero Hunger) program, which quickly became one of the most comprehensive and well-known public assistance programs in the world. It includes a conditional cash transfer program called Bolsa Família (family grant), which provides cash assistance to needy families—but only if they meet certain conditions like school attendance, vaccinations, and regular medical and dental care for children. The program sharply reduced absolute poverty and improved health and education for young people.

During Lula's eight years in power, Brazil gained a global reputation for speaking out against the United States and Europe on behalf of developing countries. In return, U.S. president Barack Obama and British prime minister David Cameron acknowledged Brazil's newfound geopolitical status through strategic partnerships. Lula, and to a lesser extent his successor Dilma Rousseff, also championed South–South development cooperation, which included extending Brazilian technical assistance to Africa, Latin America, and the Caribbean.

The Environmental Costs of Economic Success

The expansion of agriculture has been one of the most impressive trends in Brazil's economy. IPE scholar Kristen Hopewell analyzes the ways in which Brazil constructed comparative advantage in agriculture and livestock through state intervention. She points out that it is "the first tropical country to join the ranks of the world's leading agricultural producers," surprisingly as a major grower of temperate crops such as soybeans, cotton, and corn.[20] Its agribusiness depends heavily on mechanization and chemicals. How did Brazil become an agricultural powerhouse? According to Hopewell, state-funded research centers

developed new plant varieties suitable to the tropics and made technical advances that turned what were wastelands into highly productive soil. The government also provided extension services and subsidized credit that allowed industrialized agriculture to spread rapidly, which helped support other industries such as food processing. In 2012–2013 Brazil overtook the United States to become the largest soybean exporter in the world.[21] The Brazilian case shows that agricultural transformation can be as important as industrialization to development and that the state can sometimes successfully create a country's comparative advantage in the global economy—a process that economic liberals do not recommend that a state try to undertake.

Despite this progress, Brazil's economic rise has caused conflict and contradiction. Especially controversial have been the environmental and human rights implications of agricultural growth. Since 2003, the land area in which soybeans and sugar cane are planted has increased by more than 30 percent, mostly in the central-west and northern regions of the country, which are home to the fragile ecosystems of the *cerrado* and the Amazon rainforest. Deforestation is one price Brazil has paid for the expansion of farmland and growth of agricultural exports. In addition, there have been violent conflicts between large producers and small farmers over access to land. The government has often failed to enforce the meager environmental regulations that exist.

Because the Amazon rainforest is the world's largest "carbon sink", Brazil finds itself at the center of major international environmental debates. Some scientists estimate that tropical forests—the "lungs of the world"—absorb as much as 20 percent of carbon emissions from the atmosphere every year. Their loss to large-scale timber extraction, agricultural expansion, and cattle-farming growth could drastically accelerate global climate change. The Brazilian federal government's crackdown on illegal logging helped reduce the rate of deforestation by at least two-thirds from 2004 to 2014, although deforestation rose sharply in 2015 and 2016 (see Figure 13.2).

Many of the environmental controversies that surround soybean production also apply to ethanol, a fuel Brazilian cars have been running on since 1978. Brazil is currently the second largest producer (and largest exporter) of ethanol in the world, using sugar cane as a feedstock. Agricultural development policies also often leave small-scale producers and indigenous communities without access to the land upon which they rely for their livelihoods. Conflicts over the right to land in the country's interior are often violent, and over the last twenty years more than 1,000 rural activists have been killed in these conflicts. Structuralists argue that the social and environmental costs of the country's economic success, including deforestation and land concentration, outweigh many of the gains. The bancada ruralista, a powerful agribusiness lobby representing large landowners in Brazil's Chamber of Deputies, along with mining, logging, and road-building companies, constantly push for relaxation of environmental protection laws.

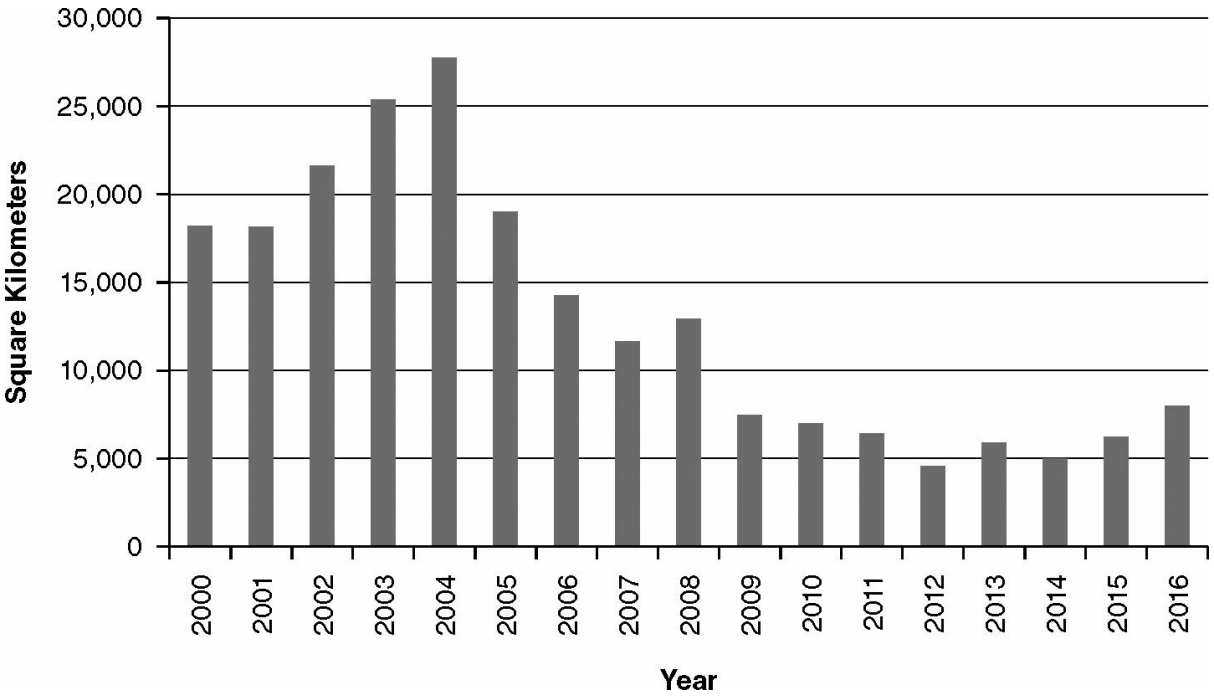


FIGURE 13.2
Land Area in the Brazilian Amazon Lost to Deforestation, 2000–2016

Source: Data from Program to Calculate Deforestation in the Amazon (PRODES), at www.obt.inpe.br/prodes/prodes_1988_2016n.htm.

Brazil's Economic and Political Headwinds

Brazil's economy has suffered ups and downs since the 2008 global recession. In 2009, Lula famously blamed the financial crisis on "white people with blue eyes" who "before the crisis appeared to know everything and now demonstrate that they know nothing" about the global economy.[22] Global demand for aircraft and basic commodities like soy, beef, iron ore, and energy helped keep Brazil's exports up from 2010 to 2012. Brazil's economic model embraces free markets and foreign investment, but also maintains large state-owned industries in strategic sectors like oil, electricity, and telecommunications. The giant state-owned development bank, BNDES, is the main source of long-term, subsidized credit for large public and private companies. Since discovering huge oil and gas deposits in deep waters off of the Atlantic coast in 2006, the state-owned energy company Petrobras has taken the lead in investing tens of billions of dollars to develop the deposits. With social programs like the Bolsa Família, Brazil managed to cut the poverty rate from 38 percent in 2001 to 25 percent in 2009. Like the other countries profiled in this chapter, Brazil has shown that economic development can occur without complete adoption of the principles of the Washington Consensus.

However, Brazil faces many current difficulties and sees storm clouds on the horizon. Like Russia, it has been hurt by lower global commodities prices and weaker Chinese demand. Brazil's GDP grew at an average rate of 3.1 percent in the 2000s but began a steady decline in 2011 as commodity prices fell. GDP contracted by more than 3.8 percent

in 2015 and 3.6 percent 2016, plunging the country into a severe recession and reversing many social gains under Lula. The unemployment rate reached more than 13 percent in early 2017. Inequality remains persistently high, contributing to class tensions. Ironically, Brazil now faces a health problem normally associated with affluence: obesity. According to a Ministry of Health survey in 2016, nearly 19 percent of Brazilian adults are obese and more than half are overweight—dramatically higher rates than a decade earlier.

Brazil has undergone simultaneous processes of deindustrialization and reprimarization as manufacturing's share of GDP has fallen since 1995 (although the absolute value of manufacturing has not fallen) and as the share of agriculture in GDP has stayed steady (see Figure 13.3). China is a significant cause of Brazil's relative deindustrialization. From 2003 to 2012, Brazil's exports of manufactures to China grew by only $1 billion, while its imports of manufactures from China grew by $30 billion.[23] As in other parts of Latin America, the flood of Chinese goods has hurt domestic producers. In addition, China's exports of manufactured goods to the United States, Europe, and Latin America are steadily replacing Brazil's exports to these same markets. Brazil is simply being out-competed. Finally, the boom from 2002 to 2011 in Brazil's exports of raw materials such as iron ore and soybeans—much of it going to China—caused the country's currency, the real, to appreciate in value, which also has made Brazil's manufactured goods less competitive in global markets.[24]

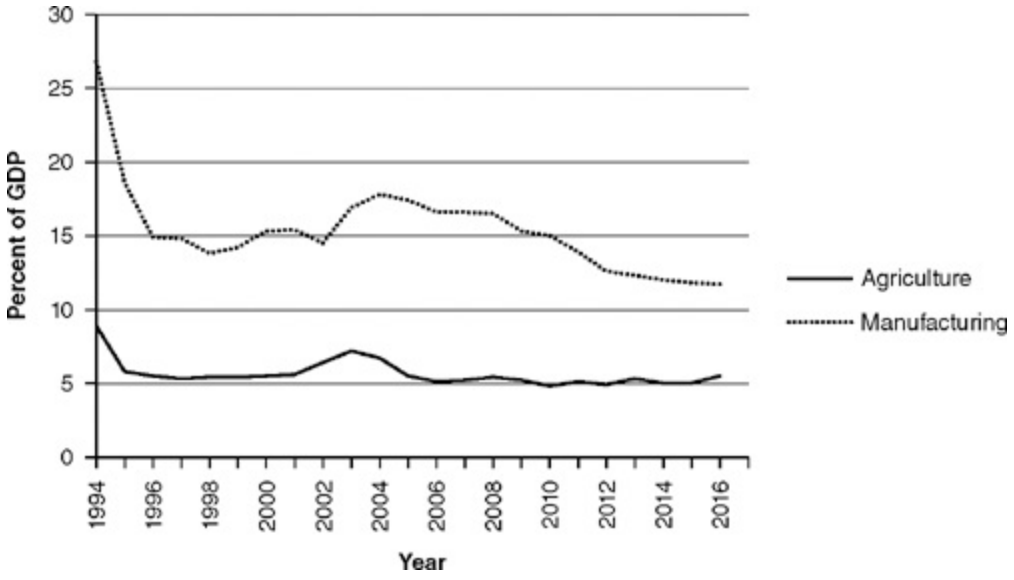


FIGURE 13.3
Contributions of Manufacturing and Agriculture to Brazil's GDP, 1994–2016

Source: Data from World Bank, *World Development Indicators*, at http://data.worldbank.org/indicator/NV.AGR.TOTL.ZS?locations=BR and http://data.worldbank.org/indicator/NV.IND.MANF.ZS?locations=BR.

Economic problems have contributed to dramatic political upheavals. In 2013 there were widespread protests over wasteful government spending, followed in 2014 by revelations of massive corruption. *Operação Lava Jato* (Operation Car Wash)—the name of a

corruption investigation—showed that political elites and officials from Petrobras, the giant state-owned energy company, took over $2 billion in bribes from private companies that were awarded contracts from Petrobras (see Box 13.1). The ongoing investigations have led to the ouster of some high-ranking officials, including Brazil's president, Dilma Rousseff, who was impeached in 2016. In 2017, federal prosecutors leveled corruption charges against Rousseff's successor as president, Michel Temer, who leads the Brazilian Democratic Movement party. The investigations have implicated leaders of major political parties and hundreds of corporate executives, many of whom have been jailed. Coming at a time of economic austerity, the corruption scandals have undermined faith in Brazil's democracy and much of the political establishment. The domestic fallout will be felt for years to come, and Brazil's stature in global institutions will be weakened.

INDIA: THE OTHER ASIAN TIGER

While Russia is sometimes viewed as an angry bear, India has often been portrayed as a caged tiger poised to leap to new economic heights. Since independence in 1947, it has all too often found itself in this poised stance: ready, but just not quite willing to jump. Despite progress in the recent past, this country of 1.3 billion suffers from an inefficient government bureaucracy and poor public infrastructure. It will need to sustain high economic growth rates and expand exports of manufactured goods if it hopes play catch up with China and bring hundreds of millions more Indians out of poverty.

BRAZIL'S OPERATION CAR WASH CORRUPTION SCANDAL

Operação Lava Jato (Operation Car Wash) began as a money-laundering investigation in March 2014 and has since turned into the largest corruption scandal in Latin American history. It has reshaped Brazilian politics. The investigation has been led by the Federal Police in Curitiba and overseen by federal judge Sérgio Moro, who has become one of the most popular figures in Brazil. At the heart of the scandal is state oil company Petrobras, whose executives awarded overpriced contracts to private construction companies in exchange for bribes and kickbacks that went to leading government officials and politicians. Kickbacks from private companies were often used to fund political parties' election campaigns.[a] More broadly, prosecutors have requested information from 33 countries, levied fines of over $26 billion, and identified hundreds of foreign companies suspected of making deals with public officials and executives of state enterprises.[b]

Investigators also discovered that Brazil's largest construction company, Odebrecht, had paid $800 million in bribes to Brazilian and other Latin American politicians in exchange for government contracts. Also caught up in *Lava Jato* was JBS, a Brazilian company that is the world's biggest meatpacker, whose owners admitted to bribing 1,893 politicians. JBS was swept up with dozens of other meatpackers in a related 2017 investigation, *Carne Fraca* (The Flesh Is Weak), revolving around bribes to top politicians and inspectors who allowed adulterated meat to enter the market. As a result, in June 2017 the USDA banned all imports of fresh beef from Brazil into the United States because of lax sanitary inspections. JBS also admitted to bribing pension funds and the big state development bank BNDES in order to gain access to low-interest loans so that JBS could go on a global acquisitions spree.

Judge Moro and prosecutors have investigated hundreds of politicians and businessmen. Moro has held many wealthy and powerful suspects in long, uncomfortable pre-trial detention to get them to accept a plea deal and turn on other people. Early on, many targets of the investigation were members of the ruling Workers' Party. Mass demonstrations in March 2016 by over a million Brazilians—many from the middle class—called for President Dilma Rousseff's impeachment. The Chamber of Deputies impeached Rousseff in May 2016 and the Senate removed her from office in August 2016 for violating budget laws.

Michel Temer was named president and assembled a right-wing coalition to carry out pro-market reforms, which included austerity and labor reforms, leading many Brazilians to view the impeachment as a rightist *coup d'état* designed to reverse the Workers' Party's progressive social and economic reforms.[c] Moro soon turned to politicians from other parties. He jailed Eduardo Cunha, the former speaker of the

Chamber of Deputies and indicted one-third of Temer's government ministers. By early 2017 federal prosecutors had charged over 200 people and were investigating nearly 100 legislators in connection with *Lava Jato*.[d] In June 2017, Temer was charged with corruption for taking a bribe from JBS. However, in August 2017 the Chamber of Deputies voted not to approve corruption charges against him, so it is unlikely that he will face trial. And in July 2017, former president Luiz Inácio Lula da Silva was convicted of corruption and money laundering and sentenced to more than 9 years in prison. Before the conviction he had announced his intention to run for president again in the 2018 election.

Political elites, including Temer, have been trying to shut down the Car Wash investigation. The Chamber of Deputies has twice voted on measures that would have given amnesty from prosecution to their own members. Brazilians are disillusioned with politicians in general and the way their democracy functions as a result of the scandal. The investigations indicate that there is systemic corruption in the Brazilian political system. According to *The Guardian* journalist Jonathan Watts, "Major companies and mainstream politicians have been utterly discredited. Voters struggle to find anyone to believe in. It is not just the establishment that is reeling, but the entire republic."[e]

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From Independence to a Mixed Economy

In the early years of colonization, Britain discouraged Indian manufacturing, and instead the British East India Company made India into a provider of raw materials for the factories of the United Kingdom. During the era of the British Raj from 1858 to 1947, Britain invested in a massive network of railways, roads, canals, and bridges to transport India's vast quantities of raw goods for subsequent export, mainly to England. The spread of property rights, the English language, and a broad political and legal framework aided the eventual emergence of India's democratic institutions.

Following independence in 1947, India's first prime minister, Jawaharlal Nehru, promoted an import-substitution-led model of growth. He drew inspiration from the Soviet Union and chose a path of modernization through industrialization. Although India chose a foreign economic model, the motives of its leaders were nationalist in nature.[25] All of the "commanding heights" of the economy essential to industrialization, such as steel, engineering, water, electricity, mining, and even finance, were dominated by public enterprises. A business environment with onerous protectionist policies and regulations came to be known as the "License Raj." India struggled to improve its agricultural sector, which was not only an important source of revenue and food security but the largest source of employment for its population.

Nehru hoped that by following a socialist development strategy, India would eventually

be able to compete globally once it had built up enough capital and infrastructure.[26] He realized that foreign investment was necessary, provided that it served the state's interests. These were the makings of a mixed economy. After experiencing a severe food shortage in the early 1960s, India started to use a new High Yield Variety (HYV) of wheat developed and funded in part by the Rockefeller Foundation. Confident of the potential to drastically increase agricultural productivity, New Delhi imported over 18,000 tons of Mexican HYV seed, distributed it across the Punjab, and made large public investments in agricultural research and agricultural extension services. Eventually (after a hiccup due to crop failure in the early 1970s), the country became not only an agriculturally self-sufficient nation but major food exporter. Aside from the high crop yields, this Green Revolution played an important role in stimulating investments in irrigation, transportation, and manufacturing of fertilizers and agrochemicals. Additionally, the Green Revolution shifted India's subsistence agriculture to a more capitalist model of farming.

The persistence of state planning throughout much of India's first four decades of independence reduced incentives for private investment. Inefficient public enterprises and restrictions on private enterprises during import substitution slowed the rate of industrial growth, as did India's wars with its neighbor Pakistan. During the first thirty years of independence, India averaged an annual economic growth rate of only 3.6 percent, and the annual GDP per capita growth rate was a mere 1.4 percent. These modest figures were sarcastically dubbed the "Hindu Rate of Growth." However, the growth rates were nearly four times greater than those under British colonial rule in the fifty years preceding independence.[27]

The Incomplete Reform Process

Despite a noticeable acceleration of growth in the 1980s following liberalization and a modest engagement with the global economy under Prime Minister Rajiv Gandhi, India faced a distortion of trade and aid due to the collapse of the Soviet Union, India's primary trading partner. Additionally, the 1990 Gulf War led to a spike in oil prices, driving India's balance of payments into a crisis in mid-1991. In response, India borrowed $6 billion from the International Monetary Fund and accordingly was required to adopt a series of reforms aligned with the Washington Consensus. The minister of finance at the time (and later prime minister), Manmohan Singh, devalued the rupee, reduced the number of industries reserved for the public sector, and allowed TNCs to have a 51 percent (majority) share in Indian firms. The five years following India's 1991 liberalization registered record high average annual growth rates of 6.7 percent.

Following reforms, Indian companies such as Infosys Technologies, Reliance Industries, Tata Motors, Wipro, and Jet Airways became familiar global names. Foreign direct investment inflows grew from less than $100 million in 1990 to $44 billion in 2016. Trade with the United States in goods and services has blossomed: in 2016 India's exports to the United States were worth $73 billion and imports from it were worth $42 billion, more than double the amounts in 2006. By 2016, its annual exports of software and information

technology services to the world reached more than $80 billion. As Figure 13.4 indicates, Indian exports have grown rapidly since 1990, reaching nearly $500 billion by 2016.

India's new development model tenuously combines protectionist state-led growth with neoliberal, market-driven growth. India has largely bypassed a labor-intensive industrial revolution, skipping instead to a services-driven economy and exports centered on capital-intensive goods like industrial machinery, pharmaceuticals, and refined petroleum products. This strategy's major weakness is that it is failing to provide enough jobs for those entering the job market each year. Agriculture, which employs half of all Indians, has been left behind. As many farmers fell deeply into debt and government subsidies declined between 1995 and 2010, 250,000 farmers committed suicide—"the largest wave of recorded suicides in human history."[28]

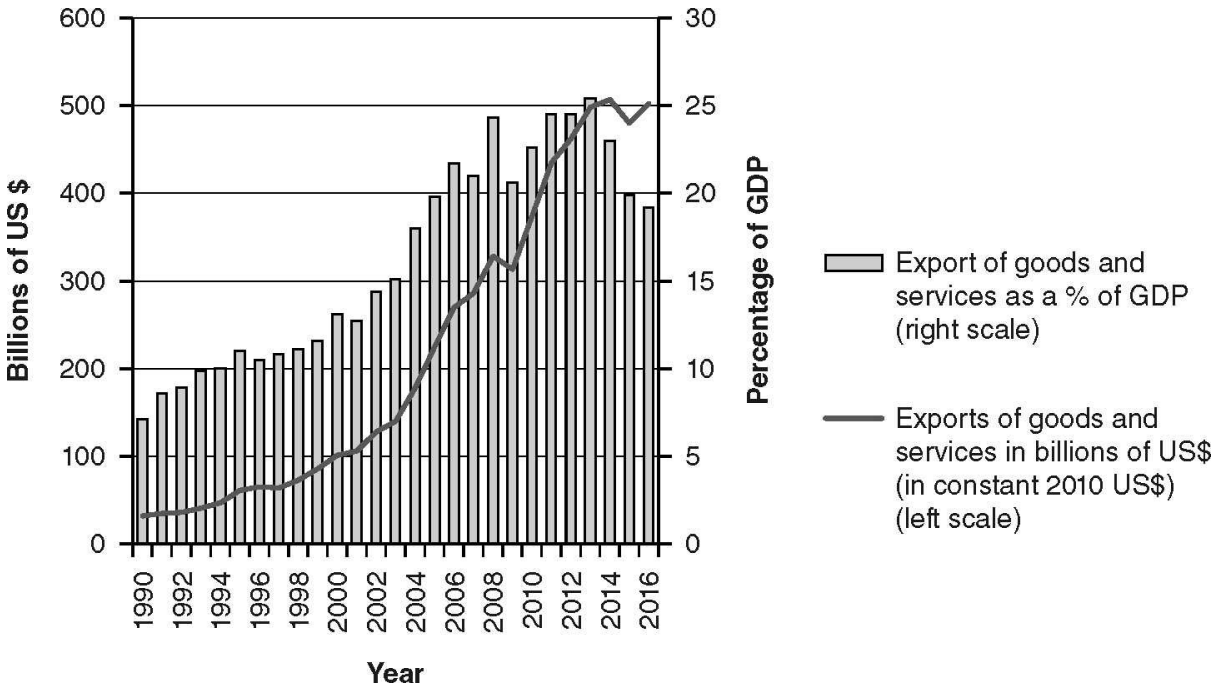


FIGURE 13.4
India's Exports of Goods and Services, 1990–2016

Source: Data from World Bank, *World Development Indicators*, at http://data.worldbank.org/country/india.

India is far behind China in terms of investments in infrastructure. While most Chinese are connected to the electrical grid, almost a third of Indians lack electricity in the home. Although India has a vibrant democracy, Jean Drèze and Amartya Sen state that there is "persistent *ineptitude and unaccountability* in the way the Indian economy and society are organized."[29] While real wages in the manufacturing sector grew steadily after 1990 in China, in India they grew barely at all. Drèze and Sen note that in agriculture and the informal sector, where most Indians work, wages are very low, even though India's GDP has grown briskly.[30] The authors emphasize that the Indian state needs to use gains from economic growth to provide much broader public services such as health care and

education that enhance human capital and social infrastructure.[31] For example, only in 2002 did the government legislate the right to free and compulsory education for all children aged 6–14 years. As more TNCs invest in India, they rapidly increase demand for a cheap, skilled, knowledgeable, English-speaking workforce.

Compared to the other BRICS countries, India has yet to go through "a phase of major expansion of public support or economic redistribution."[32] It compares poorly on measures of social wellbeing such as literacy, child immunization, and child nourishment. It has high inequality. Public spending on social services would enable faster growth and sustainable development, as long as the spending is redistributive and efficient.

Outlook for the Future

India's growth rate has been red hot since the new millennium, with GDP growing on average more than 8 percent annually from 2004 to 2011 and between 6.5 and 8 percent annually from 2013 to 2016. Liberal Indian billionaire Nandan Nilekani believes that India has a promising future due to its embrace of English, a demographic dividend (a large, young population), embedded democracy, and empowerment through technology.[33] However, India is still a very poor country: its GDP per capita in 2016 (in purchasing power parity) was only $6,100.

India has continued to grow amid the financial crisis that swept the world in October 2008. Its financial system has fortunately avoided a bad-loan culture, and its banks are sparsely connected to overseas credit markets. Banks in which the government still retains majority ownership control approximately 70 percent of total banking assets. As a consequence of its historically protectionist policies, India is less dependent on exports and thus less susceptible to global market turmoil.

Structuralists tend to pooh-pooh the India-rising hype, noting that caste and exploitation still leave many Indians in deep poverty. The flashy IT sector, which employs barely 2 percent of Indians, bypasses most of the population, especially in rural areas and urban slums. The proliferation of ultra-rich businessmen points to growing inequality of wealth. An iconic example of this disparity is the case of Mukesh Ambani, a corporate mogul whose personal wealth in 2017 was $30 billion, according to Bloomberg. His jarring, twenty-seven-story home in Mumbai, completed in 2010, has three helipads, many floors of parking, and six hundred servants. Novelist Arundhati Roy sees this as emblematic of a "trickledown," "gush-up" economy that "concentrates wealth on to the tip of a shining pin on which our billionaires pirouette" and that causes "tidal waves of money [to] crash through the institutions of democracy—the courts, Parliament as well as the media, seriously compromising their ability to function in the ways they were meant to."[34]

Scholars have debated whether or not India's democratic system has left it at a disadvantage in generating economic development compared to authoritarian China. Weak coalition governments and a federal system that gives considerable power to states have often made it hard to carry out decisive, transformative policies.[35] Lobbying groups have significant influence over government officials. Economist Amitendu Palit points out that

retailers, small manufacturers, and unions have opposed the lifting of protectionist barriers and implementation of reforms that would create more domestic competition.[36]

However, many observers believe the prospects for India's democracy and economy have improved since the election of Narendra Modi as prime minister in 2014, when his Hindu nationalist Bharatiya Janata Party (BJP) won a majority of seats in India's powerful lower house of parliament, the Lok Sabha. In June 2016 Modi pushed through new rules on foreign investment that allow foreigners to own up to 100 percent equity in defense companies in India; the previous cap was 49 percent. Because the government expects to contract for many big-ticket military supplies in the next decade, multinational defense companies may find it profitable to build new factories in India. In the past, single-brand foreign retail stores were required to buy 30 percent of their supplies from Indian sources; under new rules, single-brand foreign retailers (like Apple) that sell goods with advanced technology will get at least a 3-year exemption from the 30 percent requirement. These kinds of liberalizations have not impressed top U.S. Congressional leaders, who have urged President Trump to pressure Modi to remove more barriers to U.S. trade and investment.

Modi's government has had two major successes with domestic economic reforms. It convinced parliament to pass a measure instituting a national Goods and Services Tax (GST) in 2017 to replace a hodge-podge of state-level taxes that have impeded business growth and FDI. More dramatically, in November 2016 the Modi government announced a surprise policy of "demonetization" that withdrew the two highest notes from circulation, equal to 86 percent of Indian currency. Indians had until the end of 2016 to deposit their old notes in a bank account or exchange them for new bank notes. BJP officials justified the measure as a means to "flush out 'black money' or illegal wealth accumulated as proceeds of corruption and tax evasion."[37]

In assessing India's global position, realists hope that it will be a regional buffer against Islamic extremism in neighboring Afghanistan and Pakistan. Moreover, they see it as a close ally of the United States and a counterbalance to China. Indian strategists have watched with dismay as China has financed and built roads, railways, ports, and power plants in neighboring Central Asia, Pakistan, and Sri Lanka and boosted its naval presence in the Indian Ocean. The large gap in economic and military power between India and China, added to their longstanding territorial disputes, makes it likely the two countries will remain major Asian rivals in the coming years.

Economic liberals see in India proof that democracy and free markets can work together even in a very poor country. India has benefited from having a large diaspora of some 25 million Indians living in foreign countries, whose remittances to family back home amounted to $63 billion in 2016. While scholars used to believe that skilled Indians who emigrated overseas caused "brain drain," recent studies suggest that non-returnees often maintain ties to India through which they transfer back knowledge, expertise, and entrepreneurial skills.[38] In this sense, globalization that enables freer flows of people across borders has been good for India.

CHINA IN TRANSITION: AN ANALYSIS OF CONTRADICTIONS

In the last three decades, China has become a manufacturing powerhouse and an important global power. It has the second largest economy in the world. It has grown rapidly using a deft combination of economic liberal and neomercantilist policies. Its strengths, however, are counterbalanced with internal tensions due to constrained social and political freedoms. In its foreign policy, Beijing makes calculated realist decisions but also must cooperate with other nations that view its rise with increasing unease.

This section analyzes several contradictions that have emerged during China's development. First, Chinese leaders have fostered a consumer culture while relying on profoundly illiberal social controls and exploitative practices. Second, Beijing has presided over a broadly mercantilist system that nevertheless is fueled by global interdependence. Finally, the Chinese government has fostered cooperative relations with leading powers and adapted to global norms at the same time that it seeks to challenge the Western-led liberal international order. The tensions inherent in the pursuit of these contradictory policies have caused scholars to debate whether China's rise can continue to be peaceful and complement the growth of other countries, or whether a powerful China will inevitably clash with other countries such as the United States, shredding the fabric of global order.

The Roots of China's Rise: The Transition to a Socialist Market

Mao Zedong presided over nearly three decades of increasingly tenuous rule by the Communist Party. His Great Leap Forward (1958–1960), an attempt to organize citizens into *people's communes* of localized industrial production, undermined agriculture and led to a famine that caused the deaths of tens of millions of people. This was followed by the disastrous Cultural Revolution (1966–1976), in which Mao encouraged Chinese citizens to attack the party-state itself, which he claimed had become resistant to revolutionary change. By the late 1970s, China's economy was unstable, and the legitimacy of the Communist Party was in serious jeopardy.

Mao's death in 1976 instigated a power struggle that Deng Xiaoping eventually won. In 1978, Deng unveiled an economic reform program that combined elements of socialism with a greater role for markets and private property. The dissolution of communal farms raised food production and farmers' incomes, stimulating the growth of private rural enterprises. Farmers gained the right to sell their land (with restrictions) in the mid-1980s, and private businesses were gradually legalized. At the same time, Deng's "open door" policy lowered barriers to international trade and opened China to foreign investment. Unlike in the ex-Soviet bloc, however, the Communist Party did not give up power. Because of the party's centrality in facilitating development and the continued importance of state enterprises, China can be described as having a "socialist market economy."[39]

More than 250 million migrants from rural areas have moved to urban areas since

reforms began, filling many of the new jobs in export-oriented manufacturing facilities, the backbone of China's economy. The scale of China's export economy is astounding. Guangdong province in southeastern China is the largest manufacturing region. As early as 2007, *The Atlantic* correspondent James Fallows speculated that this one province in the Pearl River Delta employed more factory workers than the entire U.S. manufacturing sector.[40] Today, China's busiest port is Shanghai, at the mouth of the Yangtze River. It handles roughly 35 million shipping containers every year; in comparison, the United States' busiest port, Los Angeles, processed only 8.8 million containers in 2016.

Rapid growth has fueled tensions between the Chinese population and the Communist Party leadership. The government has gone to great lengths to censor expressions of dissatisfaction, often with police and military force. This was demonstrated in the 1989 Tiananmen Square crackdown against pro-democracy activists and the suppression of the Falun Gong religious movement in 1999. Beyond direct repression, however, China's leaders also understand that maintaining economic growth is key to maintaining political control.

Hu Jintao, who became China's president in 2003, advanced a set of policies designed to balance the imperative of rapid growth with the goals of decreasing income inequality and protecting the environment. Since becoming president in 2013, Xi Jinping has sought to reinforce the power of the Communist Part while pursuing a more assertive foreign policy. But officials have struggled as the annual growth rate of GDP has steadily declined since the global economic downturn in 2008, reaching 6.7 percent in 2016. At the same time that China adapts to global norms and institutions, it seeks to reform (and perhaps replace) those that it sees as standing in the way of its own aspirations for superpower status.

Fostering a Consumer Society Despite Repressive Policies

As Beijing learned during the global downturn, relying heavily on exports to consumers outside its borders has severe risks. Fostering higher domestic spending is in Beijing's interest because selling more Chinese goods inside China will provide a more reliable and stable economic model. However, there are many roadblocks on the way. Export-led growth has been ingrained with a host of social habits and cultural expectations—not the least of which is modest personal consumption. Even after three decades of growth, Chinese households still spend less and save far more than their Western counterparts. Chinese households save 30 percent of disposable income, while U.S. households save only 5 percent.

Still, consumerism has been developing in China's burgeoning metropolises. In the late 1990s, there were only a few malls in the country; there are now hundreds. By early 2017 there were 2,700 Starbucks stores in China, up from just 570 in mid-2012, and nearly 400 Wal-Mart Supercenters, clear indications of the rising income of the middle class. Helen Wang, author of *The Chinese Dream*, estimates that about 300 million Chinese can be considered part of the fast-growing middle class, most of whom live in big cities along the eastern and southern coasts.[41]

Structuralists point out that the middle class has been rising on the backs of the rural population. The government has deliberately exploited peasants to facilitate urban development, thus widening the social and economic gaps between China's coastal areas and its interior. In addition to imposing a highly regressive taxation system in the rural areas, it has confiscated land from as many as forty million peasants since the early 1990s with little or no compensation. Significant numbers of the rural-to-urban migrants, dubbed the "floating population," are excluded from many of the social services available to urban dwellers and often exploited by employers.[42] As the global economic downturn slowed growth in Guangdong and other provinces, China experienced tens of thousands of small protests in 2009 by laid-off workers, those whose land has been reclaimed by the government, and employees with a variety of workplace grievances. Ethnic tensions have erupted violently, including widespread protests by Tibetan minorities and clashes between Muslim Uighurs and Han Chinese in Western China.

Structuralists also argue that in its singular pursuit of industrialization the Communist Party has disregarded the health and safety of its own people, as is evident in the spread of lung diseases, poisonings, tainted products, water pollution, and workplace injuries. Three-fourths of the world's most air-polluted cities are in China, and 70 percent of its rivers are seriously polluted. The World Bank estimated that in 2013 alone, air pollution caused welfare losses in China equal to 9.9 percent of GDP.[43] And the combination of a one-child policy (which was phased out in 2015) along with access to ultrasound and abortion has meant that Chinese couples are having more boys than girls, such that the sex ratio imbalance has reached disturbing levels: 114 boys for every 100 girls under the age of fifteen. Surplus men and disappearing women will have negative consequences for social stability.

China has a notorious record of maintaining strict control over public discourse and exercising force when necessary to maintain conformity. The government widely restricts Web access, censors media, and monitors cell phones. The dilemma China faces is that direct state control over media access is increasingly at odds with the values and desires of an educated middle class.

Economic reforms have not been accompanied by much political reform. In fact, the Communist Party sees its ability to maintain economic growth as intimately tied to its ability to maintain political power. This raises the question of whether a mass consumer culture and widespread inequality are compatible with the continued rule of an information-shy, single party. At its General Congress in November 2012, the Chinese Communist Party (CCP) chose Xi Jinping to succeed Hu Jintao as party secretary. Xi has launched crackdowns on corruption, in part to consolidate his own power and in part to address the population's anger. Nevertheless, a survey in August 2015 by the Pew Research Center found that 84 percent of Chinese respondents believe that corrupt officials are a big problem.[44] But at the same time, 77 percent said they were better off than five years earlier, indicating how important economic growth is to ensuring the CCP's political legitimacy despite the anger at corruption and inequality.

The Unlikely Chinese Threat to the Liberal International System

What are the implications of China's mercantilist-nationalist policies in an era of global interdependence? Are China's currency manipulation, violations of the intellectual property rights of TNCs, and military build-up threatening to undermine economic liberal norms embodied in international institutions? Does China's seemingly inexorable rise in economic power mean economic decline for other countries? Economic liberals and some realists respond to these questions by arguing that China's economic decisions are intimately tied to—and limited by-its dependence on export markets. Far from being a threat, they maintain, China benefits the global economy and has an interest in preserving international cooperation and many liberal global norms.

Many Western states accuse Beijing of playing unfairly by keeping the value of the renminbi artificially low, providing export subsidies, and dumping products overseas. They see these mercantilist policies as representing a strategic threat to the economic and security interests of the United States, Europe, and Japan. China's increasing wealth has also led to its emergence as a potential counterweight to the United States in the Pacific. This has been a source of concern for many neoconservatives who believe the United States should use its global primacy to spread democracy.

However, economic liberals view China much differently. Columnist Thomas Friedman refers to the Sino-American relationship as a "de facto partnership between Chinese savers and producers and U.S. spenders and borrowers."[45] As a result of this partnership and China's exports to other countries in the world, Chinese banks hold vast reserves of foreign currency—$3 trillion by early 2017. At the same time, China holds $1.1 trillion in U.S. Treasury securities-making it the U.S. government's second largest creditor after Japan. These conditions are no reason for alarm; after all, Beijing is well aware that a quick sell-off of these assets would have unacceptably negative consequences for China's own economy and financial holdings. Former *Financial Times* journalist Guy de Jonquières goes so far as to assert, "Generally, China has proven a hesitant paymaster, apparently more interested in achieving secure prudential returns on its money than in using it to procure strategic geopolitical advantage."[46]

Ultimately, the realities of global economic interdependence constrain China's ability to act rashly and malevolently in pursuit of its own benefit. Indeed, leaders in Beijing have shown themselves to be pragmatic in foreign affairs. For example, China has good relations with Russia and pragmatic economic ties with the European Union. Another case in point: China actually helped pull the world out of the global financial crisis. But at the same time, China has many economic vulnerabilities that are politically difficult to correct, so it could face large economic setbacks in the future (see Box 13.2).

Adopting a constructivist perspective, scholars Rosemary Foot and Andrew Walter argue that China has moved significantly toward complying with global norms and institutions, many of which it had no role in creating.[47] It is broadly within the global mainstream on issues such as nuclear non-proliferation, climate change mitigation, and regulations on trade and banking. Foot and Walter acknowledge that it resists compliance with rules

against exchange rate manipulation, and it does not promote human rights. Nevertheless, it is generally committed to global order: "China's tolerance of norms, rules and standards produced by global economic institutions in which its influence has been negligible has in fact been remarkable."[48]

Similarly, many liberals believe that it is China that is accepting the developed world's consensus, not the developed world that is bending to the "Beijing Consensus." Political scientists Daniel Deudney and G. John Ikenberry are confident that China and Russia will eventually not be able to resist pressures for political liberalization.[49] Ikenberry stresses that there is a global order based on a commitment to openness, free markets, democracy, multilateralism, and rule-based behavior. Given that China has few close allies in the world, any effort to defy this order would cost Beijing dearly. Therefore, concludes Ikenberry, "China and other emerging great powers do not want to contest the basic rules and principles of the liberal international order; they wish to gain more authority and leadership within it."[50]

Shahar Hameiri and Lee Jones, who study how non-traditional security issues are governed, think that mainstream IPE theories tend to misinterpret Chinese actions by assuming that China is a centralized, unitary state. They argue that to explain rising China's behavior, we have to recognize that the Chinese state "has become fragmented, decentralized, and internationalized."[51] China's provinces now have significant economic and political power. Different levels of government compete, state-owned enterprises have become more autonomous, and agencies within the central government often have different foreign policy interests. As a result, "multiple state and quasi-private agencies, having become somewhat autonomous foreign policy actors, are pursuing uncoordinated and somewhat contradictory agendas overseas…."[52] With this in mind, China's foreign policies are not as calculated or strategic as realists and liberals portray them to be. For example, in the South China Seas, the Ministry of Foreign Affairs cannot ensure that its preferred cooperation with ASEAN and the Philippines is dominant. In another example, the People's Bank of China has promoted compliance with WTO obligations and the lifting of currency controls, only to face fierce opposition from ministries and domestic banks.[53] If Hameiri and Jones are right, then we cannot assume that China has a single-minded master plan to dominate the world. Whether China continues to act peacefully or turns more aggressive will depend on internal Chinese political dynamics and how other countries treat China.

Many economic liberal scholars argue that there is evidence that China's growth is good for the rest of the world and is likely to reinforce international cooperation. Chinese investments overseas, which have been growing since 2010 with Beijing's blessing, benefit developed countries, just as did the rise of Japanese investments overseas in the 1980s. For example, in recent years some of the capital flight from China has gone into housing and commercial real estate in North America, driving up prices sharply in Vancouver, Toronto, Seattle, Los Angeles, San Francisco, and New York. These are cities where Chinese nationals have been buying tens of billions of dollars of real estate since 2010. Notably,

when Canada's province of British Columbia imposed a 15 percent tax on new foreign buyers of homes in metropolitan Vancouver in 2016 (and Ontario did the same in Toronto in 2017), Chinese buyers shifted interest to cities like Seattle. Chinese citizens spent an estimated $27 billion on home purchases in the United States in 2015 alone.[54] Despite driving up prices for new North American homebuyers, these investments have helped revive the U.S. housing market and benefit existing homeowners.

WILL CHINA RULE THE WORLD?

In his 2016 book *The China Boom: Why China Will Not Rule the World*, Ho-fung Hung, a political economist at Johns Hopkins University, seeks to refute the conventional argument that China is an anti-status-quo power seeking to disrupt the liberal global order. It is the case, says Hung, that "the rise of China fomented a new, Sino-centric export-oriented industrial order under which most Asian economies increased the weight of their export of high-value-added components and parts (e.g., for Korea and Taiwan) and capital goods (e.g., for Japan) to China, where these capital goods and parts were employed and assembled into finished products to be exported to rich countries' markets."[a] But, ironically, China's development policies have actually helped reinforce American global dominance. By recycling export earnings into U.S. Treasuries, China perpetuates the dominance of the U.S. dollar and helps the United States live beyond its means through cheap credit. China needs free trade to ensure sufficient exports of manufactured goods to its main markets in Europe and America.

Many observers recognize that China's overreliance on exports and its large holdings of Treasuries created global economic imbalances that fed the 2008 financial crisis. Still, it is difficult for Beijing to challenge its politically powerful export interests by, for instance, allowing the renminbi to appreciate significantly. Excessive foreign exchange and lax bank lending to state-owned enterprises have created a credit boom in the last two decades, leading to land and real estate speculation and overinvestment in manufacturing.[b] Bad loans keep piling up in the banking system, but Xi, like Hu before him, is reluctant to carry out a major restructuring of banking. Industrial overcapacity due to the credit boom means excesses of steel and cement, idle factories, and large apartment complexes called "ghost cities" with hardly any residents. At the same time, China's wage suppression and forced savings, among other things, have dampened internal demand.

In the face of all these contradictions, Hung argues that the China boom is fading, with the possibility of a hard economic landing. A taste of this came in summer 2015 when Chinese stock prices fell sharply after having risen rapidly over several years due to monetary easing and individual investors pouring borrowed money into stocks. Despite massive government intervention to stabilize stock prices, they plummeted again in January 2016. One response of the government was to devalue the renminbi to stimulate exports, but with the effect of prolonging the export-dependent growth model. As Chinese stocks tanked, Chinese citizens moved large amounts of money out of the country. Capital flight in 2015 was some $700 billion, and large outflows continued into early 2016. China's foreign currency reserves fell from $4 trillion in June 2014 to $3 trillion in January 2017.

Hung argues that China needs a fundamental rebalancing of its economy away

from reliance on exports to an increase in domestic consumption. This rebalancing "requires a serious redistribution of income and capital, which in turn requires a difficult and unpredictable reshuffling of the social and political order that has prevailed since the Tiananmen crackdown in 1989."[c] This redistribution means raising labor's income, curtailing easy credit to poor-performing companies, and shifting resources from urban and coastal regions to rural and interior ones."[d] The "oligarchic party-state elite," state-owned enterprises, and exporters will resist reforms, so without liberalization to empower ordinary Chinese, it is hard to see how these changes can occur.

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[a] Ho-fung Hung, *The China Boom: Why China Will Not Rule the World* (New York: Columbia University Press, 2016), p. 80.

[b] For a discussion of China's economic fragilities, see Allana Krolikowski, "Brittle China? Economic and Political Fragility with Global Implications," *Global Policy* 8:54 (June 2017): 42–53.

[c] Hung, *The China Boom*, p. 12.

[d] Ibid., pp. 166–167.

What's more, China's voracious demand for raw materials provides a boon for countries rich in oil, iron ore, alumina, copper, and arable land. Africa has benefited most significantly: China is now the continent's largest trading partner and investor (see Figure 13.5). Since at least 2000, Beijing has provided African nations billions of dollars in aid and debt cancellation in exchange for access to their natural resources and markets. It has also pitched itself as a low-cost builder of roads, dams, and hospitals.

More broadly, the Chinese Development Bank and the Export-Import Bank, both established by China in 1994, have extended credit and loans worth tens of billions of dollars to Africa, Latin America, and other developing regions to support infrastructure and energy projects. In 2013 China formed a New Development Bank with other BRICS countries to finance projects in the developing world. And in 2015, China spearheaded the establishment of the Asian Infrastructure Investment Bank (AIIB), in part because it felt that its power in the World Bank and the IMF were not commensurate with its global economic standing. China's creation of multilateral institutions such as the NDB and the AIIB are means to universalize Chinese interests and help Chinese construction companies win large infrastructure contracts.[55] China's goals may be self-interested, but they could help stimulate global growth while posing no real challenge to existing global institutions.

Realist Views of China's Long Road to Great Power Status

Although most realists tend to raise alarm over China's rise (see the next section), some of them believe it will take many years before China will be able to rival the United States or impose its vision of global order. For example, political scientist Michael Beckley rejects the thesis that China's economic growth necessarily means the decline of the United States. He points to empirical evidence suggesting that the United States is actually gaining relative to China in areas such as wealth, innovation, and military capacity.[56] For example, from 1990 to 2016, GDP per capita (in PPP) rose from $23,954 to $57,467 in the United States, while China's rose from $1,526 to $14,401.[57] Both countries grew wealthier—and China

grew at a much faster pace—but in fact the absolute gap in wealth between them grew wider.

Similarly, realist political scientists Stephen Brooks and William Wohlforth persuasively argue that China's rise, impressive though it has been, does not mean that China is about to close its military, technological, and economic gaps with the United States. Even though China's military spending has increased significantly since 2000, U.S. military capabilities are dramatically superior on every measure and will remain so for decades, given the U.S. head start. Brooks and Wohlforth also point out that U.S. R&D spending is still twice as large as China's, and many of China's high-tech exports are produced by foreign-owned TNCs with imported parts.[58] U.S. economic power is much larger than GDP suggests because U.S. investors own many of the shares of the world's largest non-U.S. corporations.[59] Moreover, if we use a measure of "inclusive wealth," which is the stock of a country's manufactured capital, human capital, and natural capital, U.S. wealth in 2010 was $144 trillion compared to China's $32 trillion.[60] China has a long way to go to close the capabilities gap with the United States.

Like Brooks and Wohlforth, Thomas Christensen expects that it will be quite some time before China reaches the same level of combined economic, diplomatic, and military power as the United States.[61] Overly reliant on exports, China also suffers from a rapidly aging population and low levels of university and corporate innovation. The CCP faces many challenges in maintaining social and political stability. The United States has more than 60 formal security agreements with allies around the world, while China has security partnerships with only North Korea and Pakistan.[62] Given these conditions, it is hard to see how a growing China poses a threat to developed countries or world order.

Realist Perceptions of the Threats from a Rising China

Will China continue to rise peacefully, or is it likely to become more adversarial and aggressive toward established powers that it believes are hampering its rise to global prominence? Most realists believe that China seeks to undermine Western-dominated international institutions and that it poses as an ever-growing threat to the United States and its neighbors. Given that a state's internal political configuration shapes its foreign policy, they contend that a more confident, authoritarian China is by nature a more dangerous China.

In the South China Sea, Beijing has asserted claims over islands and territorial waters very close to Taiwan, the Philippines, Vietnam, and Malaysia. Fishing grounds, oil and gas deposits, and busy shipping lanes make these areas important. China has provoked disputes in the South China Sea by building seven artificial islands there between 2014 and 2017, around which it has claimed exclusion zones. Many of the islands have large airstrips and docking facilities suggesting that they are for military use.

In a major ruling in July 2016 in a maritime dispute between China and the Philippines, a tribunal of the Permanent Court of Arbitration at The Hague determined that there was no legal foundation for China's historic claims in much of the South China Sea and that its

island building violated the Philippines' sovereignty. China's angry rejection of the legally binding ruling raised questions about Beijing's commitment to international law and its long-term aims in the region. Some scholars interpret its moves as defensive in the face of Obama's military "pivot" to Asia. Nevertheless, Kun-Chin Lin and Andrés Villar Gertner argue that because of China's enhanced economic power, "the attitude underlying Chinese foreign policy has shifted from self-restraint to one of patronizing smaller powers in the region."[63]

Although China is the main trading partner of most Asian countries, its military modernization and increasing regional assertiveness have alarmed it neighbors, most of whom look to the United States for protection from, or as a counterbalance to, China. Political scientist David Shambaugh expects China's relations with neighbors to increasingly sour as China becomes stronger.[64] Asian countries are particularly concerned about the implications of China's "Belt and Road Initiative," announced with great fanfare in 2013. The Belt part involves building transportation and energy infrastructure throughout the Eurasian landmass to connect China to Europe. The Road part involves building new ports and facilities along maritime trade routes to better connect China to Africa and the Middle East.

Realist political scientist Jonathan Holslag portrays this initiative as a sign of China's shift from defensive to offensive mercantilism.[65] Taking advantage of trade openness, China hopes to expand its access to foreign markets and expand Chinese-controlled supply chains. It is using massive loans, trade credits, and political cajoling to forge energy and transportation "corridors" throughout Asia built primarily by Chinese contractors.[66] To secure raw materials, Chinese companies have been gaining more oil and minerals concessions in Asia and buying and leasing hundreds of thousands of acres of farmland in Laos, Cambodia, and Australia. Holslag sees evidence that a partly Sinophobic nationalism is rising in Japan, Malaysia, and Vietnam as China grows stronger.[67] He argues that even if China actually wants to continue to rise peacefully, it has strategic aspirations that will inevitably put it on a collision course with countries in Asia that will respond with heightened nationalism and balancing with help from the United States.

Longtime Asia analyst and former journalist Tom Miller views the Belt and Road Initiative as part of President Xi's geopolitical vision to rejuvenate the Chinese nation and "to return China to what it regards as its natural, rightful and historical position as the greatest power in Asia."[68] Most governments in Central Asian and ASEAN countries have welcomed the financing and infrastructure that come from cooperating with Beijing and Chinese companies. However, many citizens dislike the Chinese companies and immigrants, whom they perceive as exploitative and unscrupulous. Chinese companies fail to hire many local workers but handsomely bribe government officials. India and Vietnam, which have never had good relations with China, fear that the Belt and Road Initiative will enable China to project its military power and become a regional hegemon. Regardless of these regional misgivings, argues Miller, "as economic realities push China towards great-power status, China will have to project more political and military muscle across Asia—

whether it wants to or not."[69]

Western countries also worry that China is using overseas investments to advance its military and strategic goals. For example, with backing from state-owned banks and government investment funds, Chinese companies have poured billions of dollars into Europe and the United States in recent years as part of a mercantilist industrial policy to acquire advanced technology (see Figure 13.5). In 2016, a Chinese investment fund owned by a businessman and a local government tried to buy the German company Aixtron, a maker of cutting-edge tools used in production of semiconductors, but German authorities rejected the deal. In the same year, Australia invoked national security concerns when it halted an effort by companies from China and Hong Kong to gain a majority share of a 99-year lease for Ausgrid, the largest electricity supplier in Australia.

More broadly, realists question the sincerity of China's commitment to global norms, especially regarding trade and investment. China seems to flout these norms by essentially saying to TNCs: If you want access to our market, you have to transfer technology to Chinese firms. One surprising illustration of this is the film industry. Beijing has allowed only 34 foreign films in Chinese theaters every year, and the state has a distribution monopoly over them. However, Hollywood can go over this quota by co-producing films with Chinese film companies or selling rights to Chinese state-owned companies. Chinese policy amounts to infant industry protection, and co-production allows the Chinese to learn all aspects of the film industry from Hollywood. As a result, Chinese-produced films are gaining in production quality and domestic popularity.[70] Chinese domestic box office rose from $2.6 billion in 2011 to $6.6 billion in 2016.

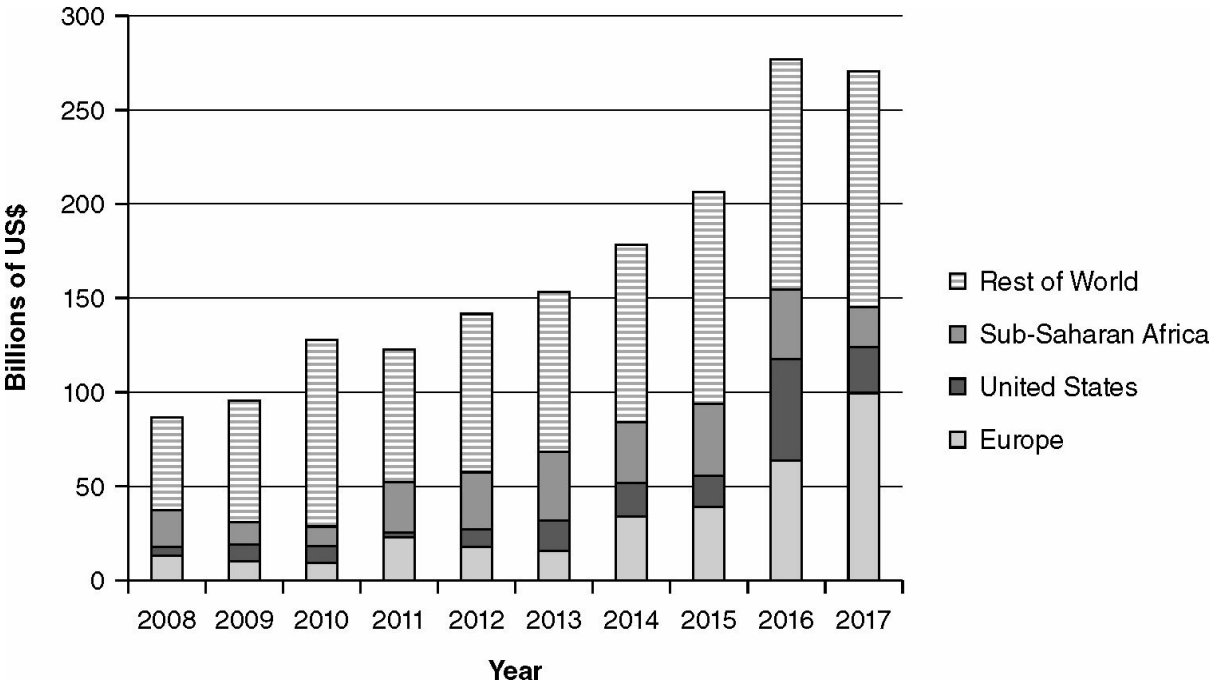


FIGURE 13.5
Value of New Chinese Investments and Construction Contracts in Europe, the United States, and the Rest of the World, 2008–2017

Note: Only includes investments of $100 million or more.
Source: Data from Chinese Global Investment Tracker, at www.aei.org/china-global-investment-tracker/.

China also regularly flouts WTO trade rules against dumping. In 2016 the *Washington Post* reported that iron ore-producing areas of Minnesota have lost thousands of jobs and billions of dollars as the slump in China's construction industry drives down the global price of iron ore, while China's steel manufacturing overcapacity leads China to dump steel in the United States, causing U.S. steel producers to lay off thousands of workers.[71] Even though the United States has over two dozen anti-dumping tariffs on imported Chinese steel, President Trump in July 2017 ordered an investigation of how steel imports are affecting U.S. national security. Trade disputes like this illustrate the Western belief that China is not committed to "playing by the rules."

Despite the sometimes alarmist predictions we have discussed in this section, it is important to recognize that political economists do not have a crystal ball to look into the future. Whatever form China's adaptation to global interdependence and global norms takes, we can be sure that China will be shaped as much by internal changes as by the way it is treated by its rivals in the rest of the world.

CONCLUSION

Most IPE scholars agree that the countries we have discussed in this chapter are reshaping the global economy and will play more powerful roles in the coming years. They often disagree, however, on what precisely those roles will be and whether or not they will lead to a more secure and equitable world. Broadly speaking, some IPE theorists fear the rising powers, while others see their success as laying the foundation for mutual benefit from globalization.

Each of the BRICS countries is finding its global niche. Due to its service-oriented growth model, India has been described as the "back-office" of the world. Because of its large FDI inflows and relatively open trade regime, China has become the world's industrial "workshop." Russia is a major energy producer and continental nuclear power with the ability and willingness to use military force in neighboring states. Brazil is coming into its own as a huge exporter of food and natural resources.

It was only in the 1980s and 1990s that each of these emerging powers began to undertake its unique version of market-oriented reforms. Along the way, Brazil has faced debt burdens, inequality, and renewed dependence on raw materials exports. Russia has suffered deindustrialization and various social ills, turning into an authoritarian state. For many years to come, it will struggle to deal with internal problems while pressing for a more multipolar world in which it is treated as an equal by the United States. India has left too many poor people by the wayside. China cannot shake off one-party rule and must grapple with inevitably slower growth and a rapidly aging population.

Nevertheless, China has performed dramatically better than the other countries since the late 1970s. It is the only BRICS country likely to become a global economic and geopolitical power. It has focused more heavily on education and literacy initiatives than India. Rural reforms have been deeper and more immediate than in Brazil and India. It has avoided Russia's dependence on energy and minerals—the so-called "resource curse." The CCP has been better able to effect top-down development as compared to democratic India and Brazil.

As each of the BRICS seeks regional dominance, there will be more tensions with their neighbors. The risk of armed conflict with the United States increases as China and Russia forge ahead with military modernization and assert their interests in flash points such as the South China Sea, Ukraine, and Syria. The BRICS will demand changes in global norms while they build parallel institutions such as the AIIB. They herald a more multipolar world.

KEY TERMS

BRICS 344
emerging economies 345
glasnost 346
oligarchs 346
perestroika 346
siloviki 347
national champions 347
Eurasian Economic Union (EEU) 348
Bolsa Família 351
bancada ruralista 353
reprimarization 353
OperaCdo Lava Jato (Operation Car Wash) 354
Green Revolution 357
demographic dividend 359
demonetization 360
floating population 362
Asian Infrastructure Investment Bank (AIIB) 366
inclusive wealth 367
Belt and Road Initiative 368

DISCUSSION QUESTIONS

1. How is China's reform experience different from that of Russia, Brazil, and India?
2. Which of the three core IPE theories do you feel best explains the contradictions in each country's development model? Why?
3. What similarities and differences exist in the economic and political models of the BRICS countries? What are the strengths and weaknesses of these models?
4. In what ways has state intervention helped and hindered the rising powers?
5. What are the most contentious issues between the BRICS countries and the United States? Do you believe that they can be resolved peacefully? Do you think the rising powers will change global norms significantly in the future?
6. Look at the "Made in …" labels on your clothes, electronics, and household possessions. What does this indicate about the role of the rising powers in global manufacturing?

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CHAPTER

14

The Middle East and North Africa: Things Fall Apart



A man carries a child after airstrikes hit Aleppo, Syria in April 2016.
Source: AP PhotoNalidated UGC.

The people want to bring down the regime!

Popular chant during the Arab Spring protests[1]

Words alone cannot convey the despair that has engulfed the Middle East and North Africa since 2011. Before reading this chapter, you might look at some images from the region that capture the plight of those caught up in war:

- In Damascus area hospitals in 2013, Syrians from the suburb of Ghouta struggle to survive after government forces attacked them with nerve gas.[2]
- In the blockaded, bombed-out Palestinian refugee camp of Yarmouk in Damascus, thousands of Palestinians line up for food handed out by the United Nations in 2014.[3]
- On a Turkish beach near Bodrum is the body of three-year-old Syrian Kurdish refugee Alan Kurdi, who drowned in 2015, along with his brother, before reaching safety on the Greek island of Kos.[4]
- Sitting dazed, covered in blood and dirt, in the back of an ambulance is five-year-old Omran Daqneesh, who was pulled from under the rubble of his house during a Syrian government offensive in 2017 to retake the city of Aleppo from rebels.[5]

There are many more images from conflicts outside Syria—in Gaza, Yemen, Iraq, and

Libya— showing humanitarian disasters and destruction. How did it come to this just a few years after the Arab Spring of 2011, when there was a tantalizing possibility of greater freedom and democracy?

This chapter begins by examining how the Middle East was historically integrated into the international economy and security structure during European colonialism and the Cold War. This is followed by a discussion of the causes of conflict and cooperation and an assessment of the challenges for countries swept up in the political revolution beginning in 2011. We then compare competing claims about whether the region is "falling behind" in the global economy or successfully integrating itself into the global trade and production structures. While you may find the references to so many countries overwhelming at first, we hope that by the end you will have a good understanding of the region's dynamics.

The chapter lays out several broad theses regarding tensions among states, markets, and societies in the Middle East and North Africa (MENA):

- International markets demand openness, while states jealously guard sovereignty. Until the Arab Spring political upheavals, the MENA had responded to these contradictory pressures by muddling through—adopting some economic liberalism and political reforms but resisting fundamental change. The Arab Spring unleashed expectations for freedom that will not be fulfilled anytime soon given a long history of unaccountable governments and social inequality.
- Civil wars and regional struggles for dominance have caused state failures in Syria, Iraq, Libya, and Yemen and have made Sunni–Shia animosity a key regional dynamic.
- Outside powers have contributed to the Middle East's horrendous problems by largely refusing to pressure regimes to negotiate peaceful solutions to political disputes.
- Despite serious problems, the Middle East is deeply embedded in global flows of finance, goods, and people.

AN OVERVIEW OF THE MIDDLE EAST AND NORTH AFRICA

This chapter focuses on the region that U.S. social scientists commonly refer to as the Middle East and North Africa, an area that is tied together by history, self-identification, and economic-political interactions. It includes Israel, Iran, and Turkey (predominantly non-Arab countries) and the numerous Arab states in the *Mashriq* (Syria, Lebanon, Jordan, Iraq, and the Palestinian Territories), in the Arabian Peninsula (Saudi Arabia, Yemen, Oman, Kuwait, Bahrain, Qatar, and the United Arab Emirates), and in North Africa (Egypt, Libya, Tunisia, Algeria, and Morocco). The distance from one end of the region to the other (Rabat, Morocco, to Tehran, Iran) is nearly 3,700 miles (see Figure 14.1).

In addition to official languages of Arabic, Farsi, Turkish, and Hebrew, the MENA also has millions of Kurdish speakers (especially in Turkey, Iran, and Iraq) and millions of Berber speakers (especially in Morocco and Algeria). Arabic is the most widely used language (even Iran, Israel, and Turkey have Arabic-speaking minorities), and the majority of people are Muslims. Of a total regional population of about 440 million people (excluding Turkey), there are about 15 million Christians and 6.5 million Jews. Substantial minorities of Christians live in Egypt, Syria, and Lebanon. Although 75 percent of Israelis are Jewish, 17 percent of Israeli citizens are Muslims. Most Muslims in the MENA are Sunni, but the majority of the population in Iran, Iraq, and Bahrain is Shi'ite.

MENA countries differ significantly in terms of level of development and relationship to the global economy. For example, Yemen, one of the poorest countries in the world, has a per-capita gross domestic product (GDP) of only $2,500, whereas Israel's per-capita GDP is $38,000—nearly the same as that of Italy.[6] Grouping countries on the basis of exports, GDP, and population yields four general categories of MENA countries (see Table 14.1). First are the big oil exporters of the Gulf Cooperation Council and Libya, with comparatively small populations and high per-capita GDP. A second group includes big oil exporters such as Iran, Iraq, and Algeria, with large populations and historically highly protectionist economies. Third are non-oil exporters such as Israel, Turkey, Jordan, Tunisia, and Lebanon, with significant agriculture, industrial exports, tourism, and openness to foreign direct investment. Fourth are the countries like Egypt, Morocco, Syria, Yemen, and the Palestinian Territories, with mostly large populations, low per-capita GDP, and high rates of rural poverty.

The Middle East as a whole lags behind every other major region of the world in terms of democracy. Freedom House, an independent organization that annually measures countries' political freedom, ranks only Israel and Tunisia (in the Middle East) as being "free."[7] Five countries—Turkey, Lebanon, Kuwait, Morocco, and Jordan—are assessed as only "partly free" because, despite elections, they limit political rights and civil liberties. All thirteen other countries (including the Palestinian Territories) are considered "not free."

THE MIDDLE EAST'S HISTORICAL LEGACY

To help us understand the roots of current conflicts and the structure of current markets, we need to know something about the history of the Middle East's contentious relations with the Western powers. Most of today's Middle East countries (except Iran and Morocco) were once part of the Ottoman Empire, which for hundreds of years was a commercial power in the Mediterranean and a military adversary of the European countries.

The Ottoman Heritage

By the nineteenth century, the Ottoman Empire had turned into the "sick man of Europe." European imperial powers extended their military and economic influence, gaining commercial concessions throughout the empire. France colonized Algeria in 1832, and in the 1880s Britain and France took control of Egypt and Tunisia, respectively, on the pretext that they were no longer able to pay their debts to European creditors. The Ottomans and local rulers in the Middle East tried with very limited success to keep up with the Europeans through defensive modernization—reorganizing their governments, adopting European military technology and legal codes, and building state-owned factories.

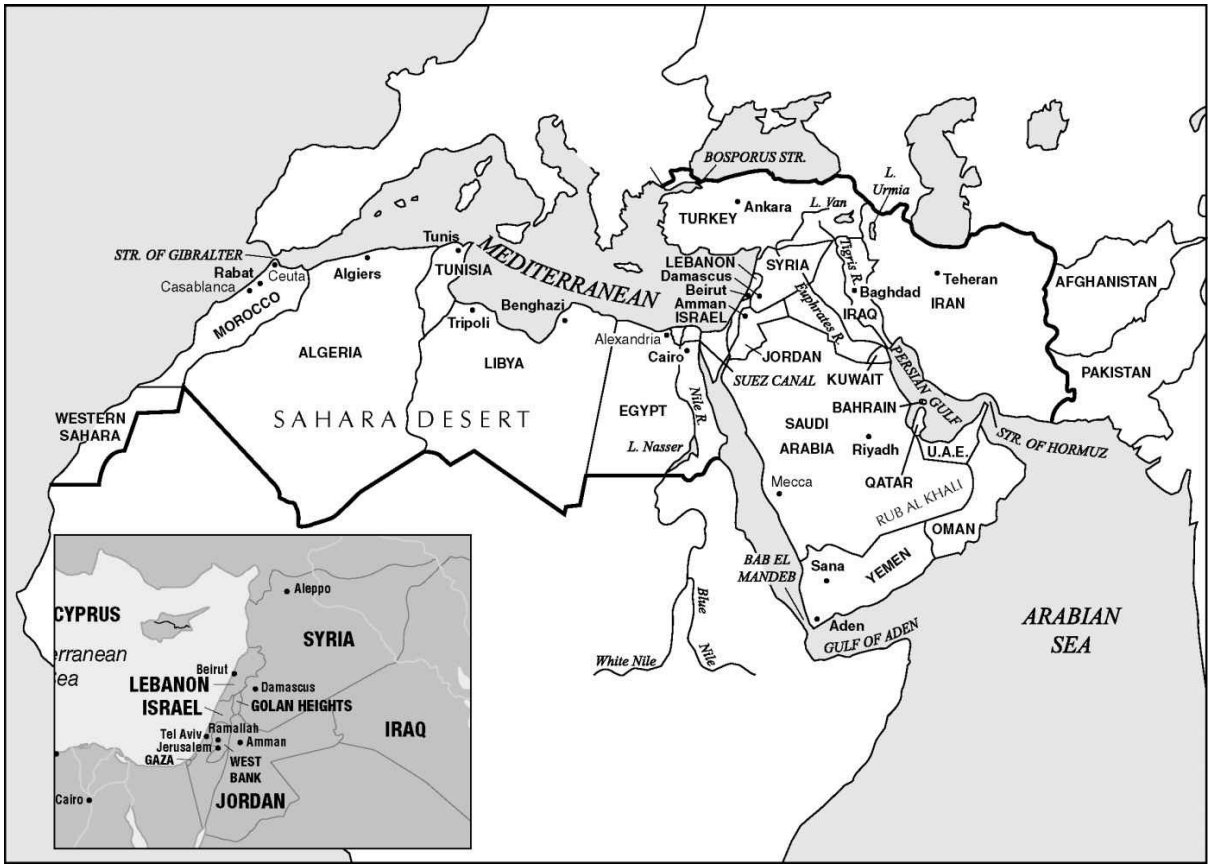


FIGURE 14.1
The MENA States

TABLE 14.1

Economic and Demographic Differences between MENA Countries

Country	2016 Population (in millions)	GDP per Capita in 2016 (in USD)
High-Income Oil Exporters		
Saudi Arabia	32.3	54,400
United Arab Emirates	9.3	72,400
Libya	6.3	11,200
Oman	4.4	42,700
Kuwait	4.1	73,800
Qatar	2.6	128,000
Bahrain	1.4	47,300
Middle- to Low-Income Oil Exporters		
Iran	80.3	17,000
Algeria	40.6	15,100
Iraq	37.2	17,400
Diversified Exporters		

Turkey	79.5	24,200
Tunisia	11.4	11,600
Israel	8.5	37,900
Jordan	9.5	9,100
Lebanon	6.0	14,000
Low-Income, Significantly Agricultural		
Egypt	95.7	11,100
Morocco	35.3	7,800
Yemen	27.6	2,500
Syria	18.4	–
Palestinian Territories	4.6	2,900

Note: GDP per capita figures are in purchasing power parity (PPP) in current US$. Year of data for Oman, Kuwait, Bahrain, and Iran is 2015; 2011 for Libya.

Source: Data from *World Development Indicators*, at http://databank.worldbank.org/data/home.aspx.

Why was the Middle East unable to compete with Europe? In his influential book *What Went Wrong?*, historian Bernard Lewis points to a lack of separation of church and state, cultural immobilism, and lack of political freedom (especially for women) as factors that hindered modernization in the Muslim Middle East.[8] Some economic historians point out that Ottoman "capitulations"—special economic privileges and legal rights granted to Europeans over several centuries—prevented the region from imposing high tariffs to protect infant industries. Some Muslim reformist thinkers believed that Muslim societies needed to discard historical accretions in Islam and engage in *ijtihad* (reinterpretation of Islamic legal sources).[9]

Alternatively, political scientist L. Carl Brown argues that the Middle East got locked into a system of international diplomacy called the *Eastern Question Game*, in which outside countries continuously penetrated the region and jockeyed for power. The result of this mercantilist game was that Middle Eastern political leaders tended to favor "quick grabs," eschew bargaining, and treat politics as a zero-sum game.[10] As we will see later in the chapter, the kinds of explanations we have listed here are still in vogue today as interpretations of the roadblocks for Middle Eastern countries trying to adapt to globalization.

Twentieth-Century Colonialism and Its Aftermath

Although President Woodrow Wilson supported self-determination for states after World War I, the European powers carved up former parts of the Ottoman Empire—excluding Turkey, Iran, and Saudi Arabia—into colonies. They drew state boundaries and often exercised strong influence over monarchical regimes in "protectorates" and "mandates." The violence that colonial powers used against inhabitants seeking independence was often

ferocious, sometimes setting back industrialization and state formation for decades. For example, during the pacification of Libya from 1911 to 1933, the Italians killed most of the country's livestock and displaced, imprisoned, or killed a majority of the inhabitants.[11]

Soon after World War II, Zionists declared an independent Israel in the Palestine Mandate and rebuffed an invasion by Arab neighbors. By the late 1950s, most of the countries in the region were independent. Algerians, however, fought a brutal guerrilla war for independence from the French from 1954 to 1962, during which more than 750,000 people were killed (and many tortured by the French).

Many independent states still had to deal with a colonial legacy of exploitation and the lingering presence of European powers. In the Suez Crisis of 1956, for example, Israel, France, and Britain briefly invaded Egypt after President Gamal Abdel Nasser nationalized the Suez Canal. The oil industries were dominated by the West's "Seven Sisters," which for decades deprived Middle Eastern countries of a fair share of oil revenues.

Ordinary citizens had little role in governance, and there was a huge economic divide between urban and rural dwellers. Poor health care and poor education were the norm. Arab socialists and military officers who staged a series of *coups d'état* in the 1950s and 1960s sought to break the cycle of dependency and inequality they blamed on the West and its lackeys in the region. They implemented modernization programs, subsidized basic goods, and built state-owned industries. Their success, however, was tempered by the intrusion of the Cold War into the region.

The Cold War to the Arab Spring

Regimes relied on the superpowers for weapons and economic aid. Washington was more than happy to support authoritarian leaders like Iran's Mohammad Reza Shah Pahlavi as a bulwark against communism and to secure oil supplies. Moscow was eager to detach Third World countries from the Western orbit.

The Cold War had at least two lasting effects on the region. First, it eventually pushed the oil-producing states of the Organization of the Petroleum Exporting Countries (OPEC) to assert control over oil production and pricing. Responding to U.S. support for Israel in its 1973 struggle against Soviet allies Syria and Egypt, Arab members of OPEC nationalized oil companies and temporarily cut off oil exports to the United States. The net results in the 1970s and early 1980s were much higher oil prices and a massive transfer of wealth from industrialized nations to oil producers. Second, in their struggle against leftist political parties and Soviet proxies, the United States and its Middle East allies often accommodated conservative Islamist movements, even supplying massive amounts of weapons to the *mujahideen* (freedom fighters) in Afghanistan. The "blowback" from this marriage of convenience with Islamists would haunt the West in the 1990s and 2000s.

At the end of the Cold War in 1990, the United States emerged as the unrivaled external hegemon in the MENA. With EU support it liberated Kuwait from Saddam Hussein's occupation in the 1991 Gulf War. Violent organizations such as al-Qaeda and Hizballah also became the West's new bogeymen. Neoliberal economic policies spread in the face of a deep slump in oil prices that had begun in 1985. The 1993 Oslo Accords promised

peaceful relations between Israel and the Palestinians, but the Gulf states and Iran started an arms race. Military spending in the Middle East in the 1990s averaged about 7 percent of GDP, the highest rate of any region in the world.[12] MENA countries (excluding Turkey) increased military spending by 62 percent in real terms from 2002 to 2011.

From 2004 to 2014, dramatically higher oil prices allowed oil exporters to pay down foreign debt and boost government spending. Respectable growth rates were welcome news for the region's people. Although the impact of the 2008 financial crisis was limited, the Arab Spring aftermath and the drop in oil prices beginning in 2014 reversed economic progress in many countries.

From September 2001 to January 2011, the geopolitics of the MENA states was shaped by the crackdown on radical Islamists. Engaged with the war on terror and the occupation of Iraq, the United States suffered a sharp decline in its moral authority. At the same time, Israel in January 2009 launched a devastating attack on the Palestinian Islamist group Hamas in the Gaza Strip. The peace process between Israel and the Palestinian Authority came to a halt when Prime Minister Benyamin Netanyahu formed a right-wing government after Israel's elections in February 2009.

A new regional dynamic emerged in the mid-2000s as Shia Muslims in Iran, Lebanon, and Iraq flexed their political and military muscles. In Lebanon the powerful Shia militia Hizballah fought a thirty-two-day war with Israel in the summer of 2006. As Lebanon recovered, Hizballah rebuilt its weapons arsenal and gained one-third of the cabinet seats in a unity government following June 2009 parliamentary elections. Iran continued to develop its nuclear enrichment capability, raising tensions with the European Union, the United States, and Israel. By 2012, Iran faced sanctions that limited its oil exports and cut its access to the global financial system.

REGIONAL DYNAMICS AFTER THE ARAB SPRING

The entire Middle East and North Africa region has been transformed by events that began in Tunisia on December 17, 2010, when a police officer seized apples from Mohammed Bouazizi, a poor, unlicensed fruit vendor in the small town of Sidi Bouzid, and humiliated him in front of a group of other vendors. Shortly thereafter, Bouazizi doused his body with paint thinner and lit himself on fire in front of the city hall. He died three weeks later. A video of a small protest in Sidi Bouzid the day after Bouazizi's self-immolation spread through Facebook and eventually was shown on Al-Jazeera, the pan-Arab satellite television station. Protests erupted throughout Tunisia. In an extraordinary turn of events, President Zine al-Abidine Ben Ali fled the country on January 14, 2011, and his regime collapsed. The Arab Spring was in full swing.[13]

Peaceful protests and some violent demonstrations quickly spread throughout the Arab world, shaking the foundations of authoritarian governments. Three more of the longest-serving Arab dictators would soon lose power. Egypt's president Hosni Mubarak was forced out of office on February 11, 2011, after eighteen days of protests during which hundreds of thousands of Egyptians occupied Cairo's Tahrir Square. An uprising that began in Benghazi, Libya, on February 17, 2011, turned into a bloody conflict that eventually ended with the death of Muammar el-Qa-ddafi on October 20, 2011. Yemenis forced the resignation of their president Ali Abdullah Saleh in February 2012. Elsewhere, the Syrian regime clung to power by using severe violence against its own people. According to Raymond Hinnebusch, during the Arab Spring regimes and their domestic oppositions found it politically expedient to stir up sectarian identities, which created a vicious cycle of demonization between Shia and Sunnis. By fighting proxy wars in failed states such as Syria and Iraq, Sunni Saudi Arabia and Shia Iran made religion-based hatreds worse and fostered a "sectarian bi-polarization in the interstate power struggle."[14] (See Table 14.2.)

In Syria, the regime of Bashar al-Assad crushed Arab Spring demonstrators in 2011, setting off a civil war. His regime, dominated by an Alawite minority (Alwaites are an offshoot of Shia Islam), is supported by Iran (a predominantly Shia country), Lebanon's Shia militia Hizballah, and Russia. A variety of secular and Islamist rebel groups have been supported by the United States, Turkey, Saudi Arabia, and the UAE (see Table 14.2). In addition, the Syrian Kurds, supported by the United States, have established control in northern Syria and have retaken territory from the Islamic State (ISIS), a jihadist group that seized control of parts of Syria and Iraq in 2014. What has the contest in Syria produced? More than 500,000 Syrians have died and approximately 11 million people—half the country's population—are internally displaced or refugees in neighboring countries.

In Iraq, the U.S. invasion and occupation in 2003 severely weakened state authority and intensified sectarian identities. The Shia-dominated government of Nouri al-Maliki from 2006 to 2014 alienated most of the country's Sunni Arabs. In 2014 the Islamic State, which grew out of Sunni Iraqi terrorist groups, swept into northwest Iraq, seizing Mosul and Sunni-populated areas. Under the government of Shia Prime Minister Haidar al-

Abadi, the Iraqi army, with help from the United States, Iran, and Shia militias, launched a slow counter-offensive, finally retaking Mosul in 2017 (see Table 14.2). More than 3 million Iraqis are now internally displaced. Iraqi Kurds, who in 2003 solidified control over northeast Iraq with their own autonomous government, also helped push back ISIS, gaining more territory in the process, including (for a short time) the oil-rich region around Kirkuk. The deep divisions between Sunnis, Kurds and Shia make it unlikely that the central government in Baghdad will establish sovereign control over all of Iraq.

TABLE 14.2

Divisions between Countries and Groups in the Middle East

Pro-Sunni	Pro-Shia
1. Saudi Arabia, Egypt, the UAE, Jordan, Turkey, and Syrian rebels	1. Iran, Iraq, Syria, and Hizballah
2. ISIS, Jabhat Fateh al-Sham (former Nusra Front), and al-Qaeda	2. Houthis (Yemen) and Shia citizens of the GCC countries
3. U.S. and U K	3. Russia
Support Muslim Brotherhood	**Anti-Muslim Brotherhood**
1. Muslim Brotherhood parties, Hamas, Qatar, and Turkey	1. Saudi Arabia, the UAE, and Egypt
2. Some forces in western Libya	2. Palestinian Authority and General Haftar's forces in eastern Libya; Jordan, Kuwait, and Morocco are wary of the Muslim Brotherhood
3. None	3. United States and EU (wary of, but not hostile to the Muslim Brotherhood)
Pro-Kurdish	**Anti-Kurdish**
1. Kurdistan Regional Government, Syrian Kurds (PYD and YPG), and the Kurdistan Workers' Party (PKK)	1. Iraq, Turkey, and ISIS; however, Turkey is not hostile to the Kurdistan Regional Government in Iraq
2. Syrian regime (not militarily hostile to Kurds)	2. Iran
3. U.S., U K, and France; however, none of these states support the PKK or Kurdish independence	3. None
Jihadist	**Anti-Jihadist**
1. ISIS, al-Qaeda, and Jabhat Fateh al-Sham (former Nusra Front)	1. Syria, Iran, Iraq, Kurds, and the GCC countries
2. Some associated groups in Libya, Yemen, and the Sinai	2. All MENA countries (especially Algeria and Egypt)
3. Individuals transnationally	3. United States, EU, Russia, and Australia
Supports Israel	**Anti-Israel**
1. Israel	1. Palestinian Authority, Hamas, Hizballah, Iran, and Syria
2. Morocco, Egypt, and Jordan (not hostile to Israel)	2. Saudi Arabia, Algeria, and Iraq

3. U.S., EU, Canada, and Russia	3. Muslim-majority countries

Rows:

1. The key countries and groups on each side of the issue, some of whom are al lies.
2. Regional actors on each side that in most cases are not the dominant actors on the issue or are not allied with the key countries and groups.
3. Non-regional powers that support one side of the issue.

In Libya, after a rebellion started in the eastern city of Benghazi in early 2011, NATO launched a bombing campaign by air that helped bring down the Qaddafi regime. Militias spread throughout the country and two rival governments formed, one in the capital of Tripoli and another in the eastern city of Tobruk. UN-brokered negotiations established a Government of National Accord (GNA) in Tripoli in March 2016 headed by Fayez al-Sarraj. Despite enjoying support from the UN, the United States, and the European Union, the GNA is weak and lacks a national army. Its authority is contested by a self-declared National Salvation Government in the west and a government in the east called the House of Representatives allied to General Khalifa Haftar, who heads a group of militias called the Libyan National Army. Haftar's troops, who are supported by Egypt, the UAE, and Russia, control Benghazi and many of the important oil installations in the east. Both Haftar and the GNA have fought against Islamic State–linked fighters, especially in the city of Sirte.

Yemen has never had a strong central government. North and South Yemen were independent countries until reunification in 1990. After Saleh was ousted following the Arab Spring, Abd-Rabbu Mansour Hadi became president. He was ousted from the capital Sana'a following a coup led by Houthis, who are Zaydi Shia, and supported by troops loyal to ex-president Saleh. In 2015, Saudi Arabia and the UAE began a military campaign in support of Hadi, whose forces regained territory in the mostly Sunni south and east, and against the Houthis in the north, where most Zaydi Shia live. Meanwhile, al-Qaeda militants continued to have a significant presence in the south. By August 2017, more than 10,000 had died in Yemen, malnutrition was widespread, 20 million needed humanitarian assistance, and more than 500,000 had contracted cholera.

Although several states—particularly Lebanon and Yemen—also experienced periods of ungovernability as early as the 1970s, today's state failures in the MENA are unprecedented. Central governments have lost control of significant parts of national territory in Syria, Iraq, Yemen, Libya, and the Palestinian Territories. And on the periphery of the MENA are more failed states: Mali, South Sudan, Somalia, and Afghanistan.

The ouster of four presidents in the Arab Spring and the crackdowns in Syria and Bahrain unleashed violent conflicts involving regional and outside states, profoundly changing the geopolitical environment. We can discern some broad trends since 2011:

1. A number of countries have become relatively ungovernable due to state failure and

social divisions, causing severe humanitarian crises.
2. A Sunni–Shia rift has spread in the region, fueled by a dominant Saudi-Iranian strategic rivalry and the strengthening of sectarian identities during social breakdown.
3. Regimes in the MENA cannot agree on how to deal with Islamist movements, which range from the mainstream Muslim Brotherhood to the jihadist al-Qaeda and Islamic State.
4. Some authoritarian regimes have reconsolidated power, intensifying human rights abuses and dashing the Arab Spring's hopes for democracy.
5. U.S. legitimacy and influence with regional allies have deceased, despite the United States' deep military involvement, giving room for Russia to expand its role more than at any time since the end of the Cold War.

In the next two sections we discuss these themes, before turning to economic questions and the Middle East's integration into the global economy.

THE ROOTS OF CONFLICT

To understand why so much interstate and intrastate violence occurs, we will look primarily at political forces operating at the international and domestic levels. Given the many injustices in Middle East history, it is no surprise that there are lingering grievances. Conventional wisdom holds that ancient hatreds—traceable to Biblical times, the Crusades, or the Sunni–Shi'a split in early Islam—are at the heart of conflicts. This "clash of civilizations" explanation of global problems—popularized by the late political scientist Samuel Huntington—is tempting to accept. Although modern-day combatants frequently use imagery from holy texts to justify their struggles, we should be wary of using their worldviews as a basis for explaining conflict. It is more accurate to tie regional insecurity to three contemporary political factors: (1) the search by external powers for influence in the region; (2) aggression by regional leaders; and (3) oppressive regimes that foster Islamist violence.

Blaming the Outside World

Meddling by outside powers has often had terrible consequences. Slicing up territories or combining different ethnolinguistic and religious communities to create new states, the colonial powers ensured future strife. Western powers and some of their allies have acquired and/or used weapons of mass destruction. Spain was the first country to use WMDs in the region. Sebastian Balfour, a professor of contemporary Spanish studies, has documented Spain's extensive use of chemical weapons—mostly mustard gas—on rebels in Morocco's northern Rif region in the 1920s.[15] France in the late 1950s and early 1960s conducted seventeen nuclear tests in Algeria's Saharan desert during Paris' development of a nuclear weapons arsenal. It used napalm extensively against Algeria's *mujahideen* during the 1954–1962 War of Independence. Israel is the only country in the region that is known to possess nuclear weapons—perhaps 200 to 300.

During the Cold War, the Soviet Union and the United States sponsored different political forces. Staunchly anti-Israeli regimes found the Soviets eager to sell them military equipment. Monarchs such as the King of Jordan and the Saudi royals looked to the United States for a security umbrella against pan-Arab socialist regimes. Turkey and Israel got aid and weapons from Washington by touting their frontline role in the struggle against communism. Although Egypt under Anwar Sadat warmed up to the United States in the 1970s, Iran turned rabidly anti-American after the 1979 Islamic Revolution. Despite the prevalence of anti-Americanism today, the majority of regional governments have military ties and/or friendly relations with Washington.

Given the United States' deep military penetration of the MENA, countries trying to defy the hegemon's interests face potentially heavy costs. For example, Arab states squandered billions of dollars in their unsuccessful wars against U.S. ally Israel. Between March and October 2011, NATO launched 9,700 air strikes against targets in Libya in a

successful effort to help rebels overthrow Qaddafi.[16] Between August 2014 and August 2017, the international coalition against Islamic State, in which the U.S. military plays a dominant role, dropped more than 98,000 munitions on ISIS targets in Iraq and Syria.[17]

The United States and its allies have also imposed economic sanctions on some MENA countries, including cutoffs of aid, freezing of assets, trade embargos, and prohibitions on Western investments. Ostensibly designed to foster regime change or "better behavior," these sanctions have usually ravaged vulnerable populations without achieving their political objectives. For example, the UN's punitive (and corrupt) Oil for Food Program allowed Iraq to export only limited amounts of oil after 1992, and the profits were to be used to import food and medicine. This program resulted in the deaths of hundreds of thousands of Iraqi civilians between 1991 and 2003, and many more suffered malnutrition, disease, and poor health. According to the philosopher Joy Gordon, who carefully studied the program, so terrible was the humanitarian disaster it caused that the acts of U.S. officials who designed and enforced it are "tantamount to war crimes" under international law.[18] In addition, beginning in 2006 the UN Security Council imposed sanctions on Iran, including a ban on arms exports to it, to try to get it to stop uranium enrichment. The United States and the European Union went much farther, cutting off Iran's banks from international financial institutions and embargoing Iran's oil exports, causing Iran to lose at least $160 billion in oil revenue from 2012 to 2015. Iran's poorest citizens bore the brunt of the pain: By 2012, hundreds of thousands had lost their jobs, and prices of basic foodstuffs had risen quickly.[19] The UN, the United States, and the European Union lifted most of the sanctions in 2016 after an agreement was reached to curtail Iran's uranium enrichment program.

In recent years, the United Kingdom and France, the main former colonial powers in the MENA, have conducted military operations in the Middle East along with the United States. The biggest change, however, has been Russia's re-entry into the region for the first time since the collapse of the Soviet Union. Since September 2015, the Russian air force has conducted extensive operations in Syria to prop up the Assad regime and weaken rebels backed by the United States and Gulf Arab countries. Putin has nurtured more friendly relations with Iran, Turkey, and Egypt. What are Russia's goals? After years of being sidelined in the region by the United States, it is keen to shape political outcomes, especially in Syria, where it has a naval base and an air base. Just as importantly, for national security reasons it seeks to reduce the threat of Islamic terrorist groups from the Middle East spreading into its already unstable Northern Caucasus region.[20]

Many people in the Middle East blame outsiders for regional violence. Conservative analyst Daniel Pipes argues that for decades there has been a widespread political culture of conspiracism in Iran and the Arab countries, wherein the "hidden hand" of the West or Israel is seen lurking behind all the region's wars and other ills. This mind-set, he asserts, encourages extremism and "engenders a suspiciousness and aggressiveness that spoil relations with the Great Powers."[21] A Pew survey in Spring 2012 revealed that more than 80 percent of Turks, Egyptians, and Jordanians oppose U.S. drone strikes and view the

United States unfavorably.[22] In 2016, Zogby Research Services interviewed more than 7,000 people in eight Middle East countries, finding that large majorities in seven countries do *not* believe that either the United States or Russia "contributes to peace and stability in the Arab world."[23]

While there are many perspectives in the voluminous literature assessing the U.S. role in the Middle East, three stand out. The first blames the Obama administration for not intervening enough in the Middle East, leaving a vacuum filled by Russia, Iran, and jihadist groups. This perspective argues that Obama's withdrawal of troops from Iraq, failure to boldly support Syrian rebels, and refusal to punish Assad militarily for using chemical weapons opened the door to disorder. In contrast, Andrew Bacevich represents the second perspective in arguing that repeated U.S. military actions in the Middle East since 1980 have had uncontrollable negative effects, including weakening states, radicalizing opposition movements, and heightening sectarian animosity.[24] Like Bacevich, realist political scientist John Mearsheimer contends that U.S. efforts to promote regime change and democracy are examples of "social engineering" in the Arab and Islamic world that have all failed, helping engender instability and terrorism.[25]

A third perspective, drowned out by media coverage of regional conflicts and anti-American terrorism, points to the long-term state-to-state cooperation and positive relations between the MENA and Western powers. Almost all the countries in the Middle East have at some time benefited from their security relationship with the United States. In 1787, Morocco and the United States signed a Treaty of Friendship and Amity that is still in force today and that constitutes the longest unbroken treaty between the United States and another country. The United States helped liberate North Africa from fascism in World War II and supported Algerian independence from France. NATO undoubtedly secured Turkey, one of its founding members, from Soviet expansionism during the Cold War. Western weapons have helped Israel defend itself during wars, and many Gulf states believe that U.S. military power helps shield them from would-be regional aggressors.

Blaming "Aggressive" Regional Powers

The use of terms such as the "Mad Mullahs" (Iran's Shi'ite clerics), the "Butcher of Baghdad" (Saddam Hussein), and the "Mad Dog of the Middle East" (Muammar Qaddafi) implies that these "brutal" or "irrational" leaders were responsible for sparking conflict. Although demonizing Middle East leaders is not good social science, it is clear that aggression by regional powers has been as important a source of insecurity as superpower meddling or transnational terrorism. Aggression takes many forms, including territorial grabs, punitive strikes, and covert operations against neighbors.

For example, Saddam Hussein's opportunistic 1980 invasion of Iran sparked a terrible eight-year war during which Iraq used chemical weapons against Iranian troops. Iraq's 1990 occupation of Kuwait—partly due to Saddam's long-standing desire to gain ports on the Persian Gulf and dominate oil production—prompted a multinational counterattack led by 500,000 U.S. troops. On the other side of the Arab world, Morocco's 1975 takeover of the

large but sparsely populated Western Sahara stemmed in part from King Hassan II's desire to boost his domestic legitimacy and control the territory's valuable phosphates and Atlantic fisheries.

Some scholars argue that Iranian militarism and defiance of international norms are at the heart of some MENA conflicts. When the Shah of Iran was overthrown in 1979, the successor regime led by Ayatollah Ruhollah Khomeini sought to spread Islamic revolution by fomenting unrest among Shia in Arab Gulf states, supporting Hizballah in Lebanon, and sponsoring terrorist acts in the 1980s and 1990s. Hostile relations with the United States reached a new low in 2002 when President Bush named Iran as part of an "Axis of Evil" along with Iraq and North Korea. During the occupation of Iraq from 2003 to 2011, the U.S. government accused Iran of providing support to Iraqi insurgents and Shi'ite militias. Iran's development of ballistic missiles and uranium enrichment capacity suggested that it sought nuclear weapons.

Iran has clearly benefited from the fallout of the Arab Spring and is determined to be the regional hegemon. It provides strong military support to the Iraqi government, Assad's regime, Lebanon's Hizballah, and Shia militias in Iraq. It now has a string of Shia allies in an arc stretching through Iraq and Syria to Lebanon.

Since the Arab Spring, Saudi Arabia has become the Arab world's chief counterbalance to Iran, with which it has had a long rivalry. In 2011, Saudi and UAE troops intervened in Bahrain to crush a popular uprising by the country's majority Shia population against the Sunni monarchy. Aided by the UAE, Bahrain, and to some extent Egypt, Riyadh has provided weapons and money to anti-Shia forces in the MENA. In Yemen it has bombed Houthi forces and blockaded ports under their control. In addition to its interventions in the Arab world, the Saudis have nurtured a transnational Sunni identity that demonizes Shi'ites. Riyadh is aided in this process by ISIS and al-Qaeda, which also promote Sunni chauvinism. In a context of state breakdown in Syria, Iraq, and Yemen, and with Iran and Saudi Arabia fighting proxy wars through clients in these places, sectarian identities have hardened, causing more violence and making it more unlikely that legitimate central authority can be reestablished.

There is another manifestation of aggressive Saudi foreign policy in Riyadh's efforts to crush Muslim Brotherhood parties throughout the region. Saudi Arabia sees the Brotherhood version of political Islam as an existential threat to its regime. The Muslim Brotherhood, a conservative and mostly non-violent movement, combines provision of social services with political activism. Turkey and Qatar have supported Muslim Brotherhood parties throughout the Middle East, especially since the Arab Spring. In 2017, Saudi Arabia, the UAE, and Egypt, which all oppose the Muslim Brotherhood, precipitated a crisis with Qatar, placing an economic boycott on the country and demanding that it close Al-Jazeera and stop supporting the Muslim Brotherhood. This aggressive move, supported by Trump, demonstrates the continuing conflict over what role to allow mainstream Islamist political parties—often the largest opposition parties—to play in Arab politics.

Although most Americans do not perceive Israel as an aggressor, Arabs have long

portrayed it as a territorially expansionist power. During its war of independence, Israel fought against invading Arab armies and encouraged or forced some 700,000 Palestinians to flee, gaining control of 78 percent of Mandatory Palestine's territory. Israel's military superiority was proven in the 1967 Six-Day War when the Jewish state seized control of the rest of Palestine (the West Bank and Gaza), Egypt's Sinai Peninsula, and Syria's Golan Heights. It rebuffed an invasion by Egypt and Syria in 1973 but signed a peace treaty with Egypt in 1979. No sooner had it withdrawn from the Sinai in 1982 than it invaded Lebanon, occupying the southern part until 2000. It briefly re-invaded and heavily bombed Lebanon in 2006 during a month-long war in which Hizballah launched hundreds of missiles into northern Israel. In 2005, Israel withdrew from the Gaza Strip, but in the face of Hamas rocket attacks it re-invaded the Strip from December 27, 2008, to January 18, 2009.

While continuing to occupy the Golan Heights, Israel has durable peace treaties with Egypt and Jordan. Its threats since 2009 to take military action against Iran convince some critics that its penchant for militarism is alive and well. In contrast, Israeli leaders have consistently justified their military engagements on the basis of their inherent right of self-defense, including against Palestinian acts of terrorism and existential threats from Arab countries.

Israeli policies toward Palestinians provide the most persuasive evidence that Zionist expansionism is hindering conflict resolution. Israeli leaders have sanctioned occupation and transformation of Palestinian territories seized in 1967. By 2017 there were more than 600,000 Jewish settlers in the occupied West Bank and East Jerusalem. Whatever the security or religious justifications offered by the Jewish state, its relentless settlement expansion is a violation of international law.

If one agrees that the Israeli-Palestinian conflict is rooted in incompatible claims of Zionists and Palestinian nationalists to the same territory, its resolution requires the creation of two states alongside each other and mutual recognition of each side's sovereignty. A two-state solution was expected to result from the peace process that Israel and the Palestine Liberation Organization began with the Oslo Accords in 1993. Yet many now argue that a viable Palestinian state is impossible to create if Israel refuses to withdraw settlers, end its occupation, and allow a Palestinian state to control its own water, borders, and airspace. In the last decade, Israeli society and political parties have become more right-wing. Concerted efforts by Obama's Secretary of State, John Kerry, to broker a peace deal between Israelis and Palestinians came to naught in 2014. Near the end of his presidency, Obama signed a deal with Israel offering it $38 billion in U.S. military aid over ten years. With American support, and in a context of deep Palestinian divisions and Arab preoccupation with civil wars in the MENA, Israel will face little pressure to compromise with Palestinians.

Blaming Oppression (and Islamist Resistance to It)

Regional conflicts are also fueled by cycles of oppression, terrorism, and counterinsurgency within states. Leading participants in these terrible cycles are often

dominant ethnolinguistic and religious groups that subjugate weaker groups and minorities and that try to justify their own violence through "myths."[26] For years, secular Arab regimes claimed that they were fighting retrograde Islamic fundamentalists and terrorists, but when the Arab Spring started, it was really mass demands for freedom that they were trying to crush.

Violent repression of Kurds in Turkey, Iraq, and Syria has also historically been an important cause of intrastate and interstate conflict. The leftist Kurdistan Workers' Party (PKK), led by Abdullah Öcalan, has fought an insurgency against the Turkish army in Turkey's southeast since the 1980s. State failure in Syria after 2011 opened a window for Syrian Kurds, who had for decades been denied Syrian citizenship, to establish control over three cantons across northern Syria, which they collectively call Rojava. Turkey is hostile to Rojava because the main Kurdish military force there, the People's Protection Units (YPG), is closely tied to the PKK. However, the United States has strongly supported Syrian Kurdish fighters, who have been very effective in rolling back ISIS in Syria.

Iraqi Kurds were also long repressed by Saddam Hussein, who even used chemical weapons against them in the 1990s. After the U.S. invasion of Iraq, Iraqi Kurds consolidated control over northern Iraq, establishing an autonomous Kurdistan Regional Government (KRG). The United States has strong military ties with the KRG, and even Turkey has good economic and political ties with it. Iraqi Kurdish forces, the *peshmerga*, have been very effective in fighting against ISIS, but in the process have seized control of more territory in Iraq. The KRG's de facto autonomy and aspirations for independence create deep tensions with the Shia-dominated government in Baghdad, promising an indefinite fragmentation of Iraq.

Historically, civil wars involving religious extremists in Lebanon (1975–1990), Algeria (1992–2000), Iraq (2003–2011), and Syria (since 2011) have caused enormous loss of life. The Islamist militant groups Hamas and Hizballah utilize violence in pursuit of political goals. However, interpreting these groups as simply using terrorism for terrorism's sake or attacking foreign occupiers because they "hate our freedoms" is a convenient way of ignoring or discounting their stated goals. As sociologist Charles Tilly notes, "Properly understood, terror is a strategy, not a creed,"[27]

Some Islamists claim that they are fighting elites who have been seduced by poisonous, imported Western culture. Others seek the right to implement conservative social policies they claim are based on Islamic law. Shi'ites in Iraq and Lebanon (and to some extent in the Arabian Peninsula), seeking to reverse decades of Sunni (or Maronite Christian) discrimination, are claiming political power commensurate with their size of the population. Most Islamist movements use religion as a political tool, even if reasonable people believe that they misinterpret Islam. Although poor Muslims are usually the foot soldiers of radical Islamist movements, their leaders are often well educated (many have science and engineering backgrounds) and from the middle class, suggesting that they feel unfairly excluded from the ruling elite.

At another level of analysis, we can see these groups as reflecting a change of ideas within the Muslim world. In the last thirty years, militant Islamist movements have spread a

puritanical interpretation of Islam with emphasis on jihadist rhetoric and the forced application of Islamic law. ISIS emerged from Iraq when the United States severely weakened state institutions and the new Shia elites marginalized Sunnis. Islamic State spread a virulent anti-Shia ideology; once in control of large swathes of territory in Syria and Iraq in 2014, it also adopted genocidal policies towards non-Muslim minorities, especially Yazidis and Christians. State failures, a weakening of nationalism, and modern communications technologies created a fertile environment for the spread of transnational jihadist worldviews by ISIS and al-Qaeda affiliates.

In summary, why has Sunni Islamist radicalism spread and attracted adherents? We offer several explanations:

- Millions of Arabs who since the 1970s have migrated (often temporarily) to work in the conservative, oil-rich Gulf states have been exposed there to a more fundamentalist perspective on Islam.
- Gulf regimes and wealthy Gulf citizens have funded *madrasas* (Muslim schools) and charities throughout the Muslim world that have sometimes taught a chauvinistic form of Islam.
- Globalization empowers not just liberal, peaceful movements but their antithesis as well. Extremists are in some ways a reaction to the military and cultural interventions of Americans, Europeans, and Israelis, as well as the worsening inequality that comes from opening up to the global economy.
- Repression causes radicalization. Non-violent movements for political change, whether led by Islamists or others, have been crushed in Syria, Egypt, Bahrain, Saudi Arabia, and the Palestinian Territories. A segment of the population in these countries and elsewhere, inspired by al-Qaeda or ISIS discourse, perceives violence as a legitimate and effective response to government repression.

THE ARAB WINTER

As we have discussed above, the Arab Spring magnified underlying conflicts in the Middle East and created new ones, especially where states broke down and regional powers fought proxy wars. But the Arab Spring also raised high expectations for political change in the Arab world. Youth, workers, the middle class, and mainstream Islamists hoped for an expansion of political freedoms and a replacement of corrupt, repressive regimes with elected, legitimate governments. Events initially moved in this direction, but within a year or two, hopes were dashed as civil wars erupted and authoritarian regimes re-emerged. What happened? To answer this question requires looking at the historical baggage of authoritarianism, structural aspects of the region's political economy, and recent actions by regional powers.

Impediments to the Spread of Representative Government

A "Third Wave" of democratization that swept through much of the world from the 1970s to the 1990s bypassed the Arab countries. Until 2011, Israel and Turkey were the MENA's only electoral democracies, but even their political systems are not models of Western liberalism. Europe and the United States bear some of the blame for authoritarianism. Historian Rashid Khalidi argues that when European powers entered the region in the late nineteenth and early twentieth centuries, they actually halted an indigenous, incipient movement toward constitutional government and rule of law.[28] After World War II, the United States nurtured close relations with antidemocratic royal families in Iran and the Arabian Peninsula as a means of securing access to oil. In the context of the Cold War, the United States supported anticommunist leaders, going so far as to orchestrate a *coup d'etat* in Iran in 1953. Fear of Soviet expansionism led the United States to reward friendly dictators and turn a blind eye to their human rights violations. Despite George Bush's pretentions to spread democracy in the MENA in the 2000s, the United States tolerated regional allies' repression, particularly of Islamist parties.

When the Arab Spring broke out, there was a surprising disconnect between Western publics and their governments. Ordinary Europeans and Americans were electrified by the historic scenes unfolding night after night on television and spreading virally through social media. But the Obama administration and the French government initially hesitated to abandon friendly dictators and military elites in the region. While U.S. and EU leaders eventually supported transitions in Tunisia, Egypt, Yemen, and Libya, they turned their backs on Bahraini demonstrators who Saudi troops crushed. They also failed to put pressure on monarchical regimes, Iraq and Algeria to respect human rights and allow fair treatment of opposition political forces. Critics argue that this demonstrates the West's continuing hypocrisy on the issue of democracy: supporting the overthrow of rogue regimes in Syria and Libya but continuing business as usual with repressive royal families in the Gulf, Jordan, and Morocco. When Western powers have used military means to induce

regime change—by invading Iraq, bombing Libyan targets, and giving arms and logistical support to Syrian rebels—the unintended consequence has been to aggravate sectarian and tribal divisions, undermining the prospects for democracy.

Dependence on oil is another seemingly important reason for MENA resistance to democracy. Scholars use the term rentier state to describe a state that derives a large percentage of its revenues from the taxation of oil exports.[29] Iran, Iraq, Libya, Algeria, and the Gulf Cooperation Council have governments that meet the definition of a rentier state. Because they do not need to tax their citizens heavily, demands for representation are generally weaker. Oil concentrates resources in the hands of a small elite who buy political loyalty and foster political dependency. The curse of "black gold" is that the government controlling revenue from it seems to be much more resistant to democratization. Conversely, in 2017 the MENA's non-oil exporters were democracies (Israel and Tunisia) or had significant political pluralism (Turkey, Morocco, Jordan, and Lebanon).

Weak civil society may also explain why so many MENA countries have trouble democratizing. Civil society is made up of autonomous social groups such as private businesses, the press, labor, and voluntary associations that historically have been forces for political liberalization. These groups face significant legal restrictions in most MENA countries and often do not have the finances to sustain a long confrontation with the government. It could also be argued that powerful barriers to the entry of women into the workforce have prevented a strong, representative civil society from emerging.

Religious and cultural explanations of democratic weakness in the MENA are quite prevalent, but should be viewed with much caution. To the extent that it reaffirms patriarchy, delegitimizes minority rights, and devalues secular thought, political culture in predominantly Muslim countries creates an inhospitable environment for peaceful political competition. Governments often claim that Islamists are undemocratic forces that believe in "one man, one vote, one time." In other words, the Islamists supposedly support the idea of free elections if the elections will help them, but once in power they will presumably impose harsh Islamic law. Thus, authoritarian regimes (and secular political parties) argue that these allegedly undemocratic movements cannot be allowed to come to power through democratic means.

Jihadist groups like al-Qaeda and ISIS are inherently anti-democratic, and the fundamentalist Wahhabi version of Islam that Saudi Arabia propagates in the Muslim world does not tolerate social and ideological pluralism. However, most of the "mainstream" Islamist movements such as the Muslim Brotherhood are led by political entrepreneurs who seek to build large coalitions to win elections and improve their societies. Although conservative on gender issues and frustrated with Western policies, they generally espouse a commitment to free elections, rule of law, and social equity. Many mainstream Islamists also support economic liberalization. Political parties affiliated with the Muslim Brotherhood or that have an ideological affinity with it include Tunisia's Ennanda Party, Morocco's Justice and Development Party, and Hamas in Palestine. These parties and others in the Arab world have sometimes had important representation in legislatures.

Islamist parties were the best organized during the Arab Spring and initially did well in elections in Egypt, Tunisia, Libya, and Morocco. One of Tunisia's largest parties, Ennanda, has participated in coalition governments since 2011. Its moderation and respect for democratic principles has been an important reason why Tunisia has been the only country to emerge from the Arab Spring with a solid democracy. In Egypt, the Muslim Brotherhood's Freedom and Justice Party won 47 percent of parliamentary seats in 2012. Its candidate Mohamed Morsi was elected president in May 2012 and ruled until July 2013 when he was overthrown by General Abdel Fattah el-Sisi. For weeks, tens of thousands of Muslim Brotherhood supporters peacefully protested against the coup in Cairo's Rabaa al-Adawiya Square, until the military regime moved in, killing at least 800 people in cold blood. Sisi has thrown thousands of Islamists in jail, had many tortured, and crushed the Brotherhood. Saudi Arabia, Kuwait, and the UAE have given billions of dollars of aid to the Sisi regime to help keep the Egyptian economy afloat.

Sisi is just one of the leading faces of counter-revolution in the Middle East. The authoritarian revival has also played out—for different reasons and in different ways—in Syria, Iraq, Yemen, and Bahrain. Even in Turkey, Recep Tayyip Erdoğan, the leader of the Islamist-leaning Justice and Development Party (AKP), has turned significantly more authoritarian. Except for a brief period in 2015, AKP has held a majority in the Grand National Assembly, and Erdoğan easily won elections to serve as Prime Minister from 2003 to 2014. Although presiding over a decade of unprecedented economic growth, Erdogan became increasingly authoritarian after 2012, clamping down on the media, running for president in 2014, and securing a new constitution in 2017 to vastly increase the powers of the presidency. In a sign of his excess, he had a $615 million, 1,100-room presidential palace built on the outskirts of Ankara. Since a bloody coup attempt against his government in July 2016, Erdoğan has had over 50,000 people arrested and has fired or suspended tens of thousands of employees in the civil service, military, police, and education system.

Optimists dispute the assertion that nondemocratic values are pervasive in the region. Public-opinion surveys conducted in nine Arab countries in 2010–2011 and 2012–2014 show that large majorities believe that democracy is the best system.[30] Meanwhile, globalization and the communications revolution have undermined information monopolies that governments held until quite recently. However, a variety of surveys show that people in the Middle East have less progressive views on women's rights than in other regions. Moreover, data from the World Values Survey indicate that, compared to people in other countries at comparable levels of development, people in the Arab world have less preference for democracy and significantly higher levels of social and religious intolerance.[31]

In sum, there is not currently a fertile environment in the MENA for a push to democracy, despite popular mobilization during the Arab Spring. Other than Tunisia, the countries at the epicenter of the Arab Spring are in civil war or run by the military. Monarchical regimes in the Gulf, Jordan, and Morocco survived the Arab Spring through a mix of repression and cooptation. Governments in Israel and Turkey have become less

tolerant of dissent and liberal norms. Human rights violations and displacement of people have increased dramatically in many countries. The Arab Spring has turned into an Arab Winter.

INTEGRATION INTO THE GLOBAL ECONOMY

There is a significant debate among scholars about whether the MENA is "keeping up" with globalization or "falling behind" the rest of the world. In this section, we discuss the argument that the MENA is successfully integrating itself into the global economy and preparing for a sustainable future. The subsequent section will analyze the assertion that the region is becoming increasingly uncompetitive and marginal, failing to switch to high-growth economies that can resolve sociocultural problems. As will become evident, the MENA is a very diverse region with many kinds of ties to the global economy.

Oil, Industry, and Growth

Growth in many parts of the MENA is tied to hydrocarbons. The years 1973–1984 were a golden age for oil exporters that raised incomes dramatically. Adjusted for inflation, oil prices from 1985 to 1999 fell into a slump, lowering growth rates throughout the region. But after 2000, prices recovered nicely as a result of OPEC oil production cuts and rising demand from China. According to the World Bank, growth in the MENA (not including Turkey and Israel) averaged 5.1 percent from 2000 to 2007, one of the best spurts since the late 1970s. Despite the global financial crisis, growth from 2009 to 2010 in Iran and the Arab countries (not including Iraq, Libya, the Palestinian Territories, Qatar, and the UAE) averaged almost 3.5 percent. The turnaround in oil and gas revenues in the 2000s allowed many countries to rebuild infrastructure and boost employment.

Saudi Arabia has taken advantage of its abundant hydrocarbons to expand into energy-intensive industries that benefit from subsidized domestic oil. The country has become an exporter of cement, steel, and, especially, petrochemicals that China is gobbling up. Moreover, the Middle East in 2015 supplied more than half of China's crude oil needs and more than 80 percent of Japan's imported oil, making it vital to the global economy.

However, Saudi Arabia and all the other main oil exporters in the region remain rentier states. Despite decades of trying to diversify their economies, their growth and government revenues are still reliant on oil. The private sector in all these countries is heavily dependent on state contracts and favors, so leaders of large businesses tend to support ruling elites.[32]

Some non-oil exporters have found their own successful growth models. For example, in the space of less than twenty-five years, Dubai has transformed itself from a desert backwater into a global transportation, financial, and tourist hub (see Box 14.1). Turkey, Tunisia, Morocco, and Egypt have world-class tourism sectors. The financial crisis did not result in dire consequences for non-oil exporters because they had relatively low levels of foreign debt and were not exposed to the U.S. subprime market.

However, non-oil exporters have fared much worse since the Arab Spring due to political instability and conflict, a plunge in tourism, and a loss of foreign direct investment. In each of the years from 2012 to 2016, real GDP in the MENA grew at a rate of 3 percent or less, although rates varied significantly across countries.[33] Facing mounting economic problems,

Egypt was forced to turn to the IMF in late 2016 for a three-year, $12 billion bailout package. The Sisi regime imposed austerity measures in 2017, including a cut in fuel subsidies and a hike in taxes, that have also been deeply unpopular. On top of these problems, Egypt's military has a major role in the economy; it owns large tracks of land and runs many large companies. Sisi will find it difficult to take on the military and ex-military officers that siphon off significant resources from the economy.[34]

Israel and Turkey are standout cases, more globalized than other MENA countries. Israel has transformed itself into a diversified economy exporting mostly high-technology products, including advanced weaponry. Since the U.S. technology boom in the 1990s, more than 100 Israeli companies have raised significant capital by listing on the New York Stock Exchange. Some Israel-based companies are global players. For example, Teva is the largest generic drug manufacturer in the world. Israel has some of the highest numbers of engineers, scientists, and patent holders per capita of any country in the world. In their book *Start-up Nation*, Dan Senor and Saul Singer attribute Israel's economic dynamism to factors such as immigration policies, a unique combination of individualism and egalitarianism, and the effects of military service.[35]

Turkey's economy has performed remarkably since 2002, with GDP growing at over 5 percent per year on average. Under Prime Minister (now President) Recep Tayyip Erdogan, Turkish companies have invested heavily in the Middle East and Central Asia in construction and transportation. They are major exporters to Europe of manufactured goods like home appliances, televisions, clothing, and steel. Turkey's leading political economist, Ziya Önis, has described Turkey's current development phase as "regulatory neo-liberalism," whereby a popular ruling party, the Justice and Development Party, enforces macroeconomic reforms like privatization of state enterprises, grants power to independent state agencies, welcomes foreign investment, and prods big Turkish companies to transnationalize (expand markets overseas and partner with foreign multinationals).[36] However, growth slowed in 2016 and 2017 due to political instability and terrorism that hurt investment and tourism.

Trade and Investment with the World

MENA countries have been integrated into the global economy through the World Trade Organization and various free-trade agreements. Collectively, their most important trade and investment partner by far is the European Union. Beginning in 1995, the European Union flexed its soft power by offering Arab Mediterranean countries more market access, billions of dollars of aid, and billions of dollars of loans from the European Investment Bank. China, Japan, India, and the United States are also important trade partners of the MENA. The United States has signed bilateral free-trade agreements with five close MENA allies, including Jordan and Morocco. The region is a major importer of U.S. machinery, aircraft, cars, grain, and engineering services. Since 2001, foreign companies have garnered many contracts to supply, build, and operate new infrastructure projects. However, the combined effects of the global financial crisis, the Eurozone crisis, and the Arab Spring

aftermath have caused net foreign direct investments in the MENA to decline steadily from a high of 5.3 percent of GDP in 2006 to under 1 percent in 2015.[37] As Figure 14.2 indicates, FDI inflows dropped from $106 billion in 2008 to just $41 billion in 2016, indicating the extent to which TNCs are shying away from the region.

DUBAI: THE LAS VEGAS OF ARABIA

Two generations ago, Damascus and Cairo were the "happening" places in the Middle East in terms of political ferment, economic dynamism, and cultural attraction. A generation ago, Beirut, the so-called "Paris of the Middle East," was the place to go for tourism and trade. Now the most dynamic city-state in the Middle East is Dubai, a small desert patch on the conservative Arabian Peninsula. It is a wheeler-dealer's kind of place, open to big ambitions and grandiose schemes. How did this backwater become a financial, trade, and tourism hub in just three decades?

Dubai is one of seven sheikdoms that make up the loosely federated United Arab Emirates (UAE). It has a coastline only 45 miles long. Before the UAE's independence in 1971, Dubai City was a sleepy town known for pearl diving with a surrounding Bedouin population. Oil was discovered in the 1960s, and the emir at the time—Sheikh Rashid bin Said al Maktoum—built an international airport, dredged the main harbor for international shipping, and encouraged investment in high-rises and hotels.[a] His sons— realizing that limited oil supplies would soon diminish—set up free-trade zones, established incentives for international container business, and made sure there were no income or corporate taxes. Theirs has been a vision of a global entrepôt.

Openness to the world has been only part of the city-state's recipe for fast growth. Equally important has been the Maktoum family's own private investments throughout the emirates and their strong reliance on state ownership. As one author has noted, "Dubai is a leading case study in successful state capitalism…. [The Maktoum family's] city state has been aptly described as a family conglomerate run by Sheik Mohammed as ruler and CEO. He is the visionary behind the leading enterprises in Dubai, including investment, media and hotel companies, as well as Emirates Air."[b]

The results on the ground stagger the imagination. The sheikhdom is headquarters for Al Arabiyya, a Saudi-owned satellite TV network that is a strong rival of Al-Jazeera for the Arab news market.[c] It has two of the largest shopping malls in the world, an indoor ski slope, and Burj Khalifa, the tallest building in the world (which is twice as tall as the Empire State building). A massive real estate development called Palm Jumeirah sits on a huge artificial island off the coast. Despite having a population of only 2.8 million people (mostly expatriates), Dubai had 14.9 million visitors in 2016.

In Dubai, we see the conflation of mercantilist, liberalist, and structuralist forces.[d] The state has made growth possible through its investments and policies. The international market has swarmed in to take advantage of the city-state's deregulated, Las Vegas-style economy. But the whole edifice, a structuralist would point out, rests on exploitation of hundreds of thousands of poor Asian workers and thousands of prostitutes with no unions or political rights.[e] Like the real Las Vegas, Dubai was hard

hit by the global financial crisis in 2007. Real estate prices crashed, construction slowed or stopped on many big projects, many laborers left, tourism dropped, and the city-state was saddled with debt, requiring a bailout from Abu Dhabi. But Dubai's risky marriage with globalization now seems to be back on track.

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The Middle East is also a major importer of weapons from the United States, Europe, and Russia. From 2008 to 2015, Middle Eastern countries received delivery of weapons worth $112 billion, 46 percent of which were supplied by the United States.[38] The biggest arms importers in the Middle East between 2012 and 2016 were Saudi Arabia, the UAE, Algeria, and Turkey. Marxist economists Jonathan Nitzan and Shimshon Bichler have argued that U.S. arms sellers (the "Arma-Core") have a common interest with U.S. oil companies (the "Petro-Core") in the periodic outbreak of wars in the Middle East, because the resulting hike in oil prices after conflicts boosts their profitability.[39] In other words, when conflicts cause oil prices to rise, Middle Eastern countries invariably use the windfalls to buy more weapons. That is good for trade, but not necessarily for MENA growth.

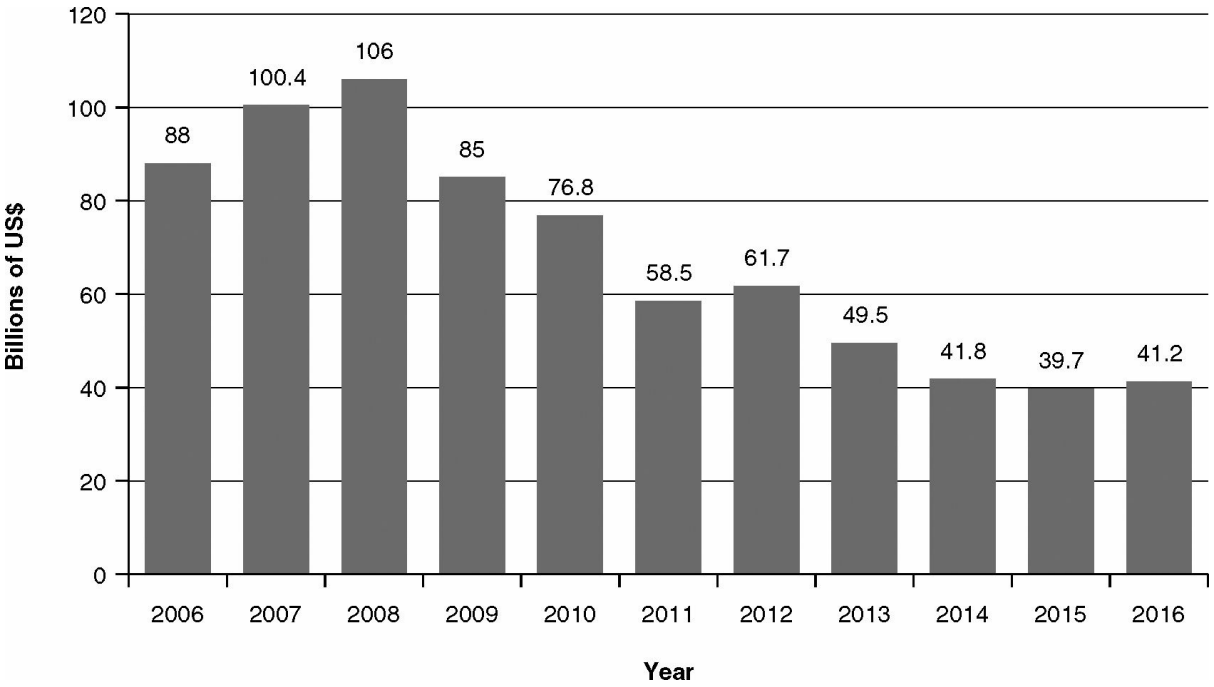


FIGURE 14.2
Foreign Direct Investment Inflows to the Middle East and North Africa, 2006–2016
Source: Data from United Nations Conference on Trade and Investment (UNCTAD), *World Investment Report 2017: Annex Tables*, at http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx.

Middle East oil exporters recycle some profits back to oil-consuming countries in the form of investments in stock markets, purchases of real estate, and deposits in Western banks. This petrodollar recycling, first witnessed in the 1970s (see Chapter 8), jumped into high gear again after 2000, tying the economic fortunes of some MENA countries closely to the international financial system. Many Middle East investments come from sovereign wealth funds (SWFs), which are large investment pools controlled by the governments of resource-rich countries. In 2016, the SWFs of Abu Dhabi, Saudi Arabia, Kuwait, and Qatar controlled global assets worth an estimated $2.2 trillion. When the financial crisis hit in 2007, MENA SWFs poured tens of billions of dollars into Western banks and companies. The liquidity was badly needed, but some U.S. and EU politicians—already concerned about dependence on OPEC oil—worried that MENA governments would use the SWFs to gain political leverage over their countries and potentially threaten national security.

Remittances—money transferred by foreign workers to their home countries—also connect people in Europe and the Middle East. Countries in North Africa rely on billions of dollars of annual remittances from workers in Europe to help with their balance of payments and to supplement the incomes of the poor. Egyptians in Europe, the Arab countries, and North America sent over $16 billion back to Egypt in 2016. In the same year, Lebanon and Morocco each received about $7 billion from compatriots around the world.[40] We can see how vital remittances are for smaller and poorer countries when

considering that they amount to over 10 percent of GDP in Lebanon, the West Bank and Gaza, Jordan, and Yemen. Without remittances, labor-exporting countries would have significantly worse current account deficits.

Globalization in the Gulf Cooperation Council, Jordan, and North Africa

The six countries in the Gulf Cooperation Council (GCC)—Saudi Arabia, the United Arab Emirates, Kuwait, Oman, Bahrain, and Qatar—are deeply integrated into the global economy not just through oil exports and SWFs but also via their labor markets. Alongside the indigenous population are expatriate (foreign) workers who make up about 70 percent of the entire workforce in these six countries and half of all the people living there.

Where do the expatriates come from? During the 1970s oil boom, three-fourths of immigrant workers came from fellow Arab countries. By the early 2010s, only about 30 percent of foreign workers were Arabs. The GCC countries have deliberately and progressively replaced Arab workers with Indians, Pakistanis, Bangladeshis, Filipinos, and other Asians. According to Giacomo Luciani, "The lack of a preference for other Arabs—or even positive discrimination against them—has been a huge lost opportunity for regional economic integration, including from the point of view of trade ties and capital movements (which migration would have facilitated)."[41]

Although the GCC benefits from the skills and low labor costs of its internationalized workforce, the region's ruling families are increasingly worried about the political and cultural dangers from heavy reliance on foreigners. Expatriate grievances have provoked some strikes and unrest. Asian women who work as nannies and domestic helpers often complain of physical and sexual abuse by employers. Some Gulf leaders worry that children raised by Asian nannies and taught by foreigners will lose their Arab and Islamic identity. They are also concerned about the large number of illegal aliens and "stateless" residents who are politically loyal to foreign countries.

Surprisingly, non-GCC countries are also turning to expatriate labor, even though their countries have high rates of unemployment. According to an extensive investigation by the U.S.-based National Labor Committee (NLC), tens of thousands of guest workers from Bangladesh, China, and India are working in Jordanian textile factories that export garments duty-free to the United States.[42] Many of the (often Asian-owned) companies, in which workers are frequently exploited in sweatshop conditions that the NLC asserts constitute forced labor, supply Wal-Mart, Target, L.L. Bean, and other U.S. retailers. Jordan has found that importing Asian workers has fueled export growth.

By 2015, there were 91,000 Chinese workers in Algeria—more than in any other African country—building highways, railroads, and public housing. In fact, Chinese construction companies have higher revenues in Algeria than in any other country on the African continent.[43] In May 2012, a Chinese construction company in Algiers started work on what will be the third largest mosque in the world—able to hold 120,000 worshipers! Throughout the MENA, the presence of so many non-national, non-unionized workers hampers the development of a powerful labor movement within civil society.

Interactions at the Human Level

In spite of its numerous conflicts, the MENA is tied to other countries through large cross-national human networks. Inter-Arab migration flows connect Arab countries, while Chinese and South Asian workers in the MENA have strong links to their home countries. Emigration and dual citizenship tie the Middle East to the United States and Europe more closely than many observers realize. The U.S. Census Bureau estimates that in 2015 the U.S. foreign-born population included more than 394,000 Iranians, 215,000 Iraqis, 186,000 Egyptians, 130,000 Israelis, and 120,000 Lebanese.[44] Between 2007 and 2016, the United States admitted 142,000 refugees from Iraq. According to Philippe Fargues, a leading French demographer, more than eight million first-generation immigrants from the Arab countries and Turkey were living in Europe in the late 2000s, including five million North Africans and three million Turks.[45] Many immigrants who came to Europe as temporary "guest workers" from the 1950s through the 1970s never left. Europe also experienced a surge in refugees from the Middle East beginning in 2015, causing political divisions between EU member countries (see Chapter 12). As is the case in the United States, many immigrants remain connected to their home countries through extended family ties and remittances.

Many American citizens live and work in the Middle East, and many Middle Easterners who have become naturalized U.S. citizens retain citizenship in their country of birth. In 2015, there were still over 40,000 U.S. troops deployed in the Persian Gulf region, though this was significantly down from the height during the Iraq war. When war broke out between Israel and Hizballah in July 2006, there were more than 25,000 Americans living in Lebanon. American forces evacuated 15,000 of these scared and displaced Americans, many of whom are dual citizens. An estimated 150,000 to 200,000 American Jews live in Israel, most of whom have gained Israeli citizenship under the Law of Return (which grants citizenship to Jews from anywhere in the world who settle in Israel). Surprisingly, 60,000 of these Americans live in the occupied West Bank.[46] For an examination of how education ties together citizens of the West and the Middle East, see Box 14.2.

FALLING BEHIND IN THE GLOBAL ECONOMY

Despite the MENA's seemingly successful integration into the global economy, there is a powerful counterargument that it is falling behind other developing countries and failing to move up in the global hierarchy. Many countries' economies are still dominated by inefficient state-owned enterprises and unprofitable public banks. Conflict and lack of industrial dynamism have stunted foreign investment. As the Arab Spring was starting, UN-Habitat identified problems compounded by rapid urbanization, including lack of adequate housing and serious water scarcity. Neglect of agriculture and lack of arable land mean that half of the MENA's caloric needs are met by imported food, making it vulnerable to rising global food prices.[47]

The Challenge of the Historical Legacy

As mentioned earlier, colonial powers left many unfortunate legacies, including many that hamper the MENA's adaptation to globalization. Some states' overdependence on a single, exported commodity, such as oil, cotton, or phosphates, slowed economic diversification. After independence, many development policies that were initially beneficial had outlived their usefulness by the 1980s. Agrarian reform and land redistribution lowered agricultural productivity. High tariff barriers protected inefficient domestic companies. Government subsidies and price controls misallocated resources. Nevertheless, Middle East growth rates in the 1950s and 1960s were remarkable in countries such as Israel, Syria, and Iran, and most countries dramatically increased literacy and access to health care. The 1970s witnessed another growth spurt fueled by oil revenues.

Development troubles came to a head in the early 1980s, when neoliberalism began sweeping through many parts of the world. From 1980 to 2000, per-capita GDP in the MENA (excluding Israel and Turkey) *failed to grow at all*, while in East Asia during the same period it expanded at an annual rate of 4.1 percent.[48] The wave of Western private investment spreading to Latin America and Asia simply bypassed the region. When was the last time you read about a U.S. company outsourcing to the Middle East?

From 2002 to 2012, the recovery in crude oil prices helped many economies grow. However, the MENA countries lack the kind of economic transformation seen in Asia. At the end of 2012, the price of crude oil was $105 a barrel, but by June 2017 crude prices had fallen drastically to just $46 per barrel. The unemployment rate in the Arab countries has been rising since 2010, reaching almost 11 percent in 2016.[49] The youth unemployment rate in Arab countries was 30 percent in 2016, the worst rate of any major region of the world. Of course, the dilemma for the MENA is that the world is moving towards renewable energy sources, which does not bode well for the MENA's economic prospects in the coming decades.

As of mid-2016, only a handful of countries in the world had yet to join the World Trade Organization, and a surprisingly large number are in the MENA: Algeria, Iran, Iraq,

Syria,Sudan, Libya, and Lebanon. As a whole, the region also has high average tariff levels. This indicates that many regimes are reluctant to adjust to international trade rules. The MENA has not significantly diversified its exports. Although trade openness can bring long-term benefits, the short-term consequences would be politically unpalatable for inefficient manufacturers—especially producers of textiles and consumer goods. Surprisingly little trade occurs *between* MENA countries. Arab countries' main exports are to the industrialized countries, and the main products they need to import are not produced regionally. Although the GCC countries have become major investors in other parts of the Arab world, they overwhelmingly invest in tourism, banking, and real estate rather than industries that are export-oriented. Regional integration will remain a hostage to war and historical grievances, forcing countries to look for commercial opportunities with the West and China rather than in their own backyard.

INTERNATIONAL EDUCATION AND THE MIDDLE EAST

Having citizens knowledgeable about other regions' languages and cultures is what political scientist Joseph Nye considers one source of a hegemon's "soft" power. For a region as important as the Middle East, it is surprising that so few Americans learn its primary languages—Arabic, Farsi, and Turkish—or study abroad there. In 2013, approximately 32,000 U.S. college students were taking Arabic courses— triple the number since 2002—but they represented only 2 percent of all U.S. college students taking foreign language classes.[a]

Studying abroad is another way to increase cultural understanding. Although the number of U.S. students studying in the Middle East steadily increased after 9/11, the overall number of Americans choosing to learn about the region firsthand is shockingly low in light of the MENA's strategic importance to the United States. In the 2015–2016 school year, only 6,044 Americans participated in a study-abroad program in the Middle East and North Africa—just 1.9 percent of the 325,339 U.S. students who studied overseas that year, mostly in Europe and Latin America.[b]

The United States—like Europe—has for decades attracted many of the best-educated Middle Easterners to study in its universities. Many of these students stay in the United States after their undergraduate or graduate training, contributing to the U.S. economy. International political and economic trends dramatically affect which countries in the Middle East send how many students to the United States. At the height of the second oil boom in the early 1980s, Middle East oil exporters flooded U.S. schools with students pursuing scientific and technical degrees (and English-language proficiency). By contrast, 9/11 caused a short-term decline in the number of Arabs studying in American universities, many of whom felt unwelcome or had trouble getting visas. However, by the 2016–2017 school year there were 52,611 Saudis studying in the United States, along with 12,643 Iranians, 10,586 Turks, and 9,825 Kuwaitis.[c]

Many Middle Easterners return home with their U.S. or European degrees, taking up important positions in the government and the business community. Europe and the United States hope that some of these individuals will become secular surrogates for the West. For example, Iraq's prime minister Haider al-Abadi has a PhD in electrical engineering from the University of Manchester. Jordan's King Abdullah II and the Emir of Qatar, Sheikh Tamim bin Hamad Al-Thani, attended England's Sandhurst Military Academy. Morocco's King Muhammad VI has a law degree from the University of Nice. In addition, branch campuses of American universities have mushroomed in the region. This new trend derives from the need to modernize higher education and have citizens master foreign languages and technical skills that are vital

to participating in the global economy. All of these educational ties have the potential to foster long-term cooperation and understanding between the West and the Middle East.

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Societal Problems

It has become increasingly fashionable to blame sociocultural factors such as underutilization of female human capital for the Middle East's catching-up problems. Few countries in the world have as dismal a record of female employment as the Arab Gulf countries, where women with citizenship constitute less than 10 percent of the total workforce. Even large countries such as Algeria and Iran have comparatively low female employment rates. In 2017, although three-fourths of men in Arab countries participated in the labor force, less than one-fourth of women did. According to the ILO, this gender gap in labor force participation in the Arab countries is the highest of any region in the world.[50]

It is inaccurate, however, to say that the Middle East lacks a culture of entrepreneurship. Economic dynamism in the private sector is particularly strong in Israel, Lebanon, Turkey, and Morocco. This may be due in part to the fact that large emigrant communities from these countries are present in many parts of the world, forging strong trade and investment links with partners "back home."

The worst perfoming economies in the region are Syria, Yemen, Libya, Iraq, and the Palestinian Territories. They will be hard-pressed to recover anytime soon from the tribulations of war and endemic poverty.

The economic and social devastation in Syria, documented by the World Bank, shows that the country will suffer for many more years.[51] GDP declined 63 percent between 2010 and 2016. Half of the population is displaced, including more than 4.5 million refugees in Lebanon, Turkey, and Jordan. The unemployment rate reached 53 percent by 2015. Much of the country's infrastructure is damaged or destroyed. On top of all these problems, violent groups extort money from almost everyone and traffic in drugs and antiquities. The international community will have to provide massive assistance to help this once-proud country recover.

Yemen has historically been a poor country with a large rural population. A majority of Yemeni males habitually chew *qat*, a mild narcotic, thereby lowering productivity and depleting family finances. The conflict since 2015 has caused most of the population to

suffer food insecurity and lack of access to clean water. Libya was relatively well off before 2011, with a small population and high oil revenues. While not as badly affected by war as Yemen or Syria, a large reduction in oil exports has hurt the economy. Iraq was beginning to recover from the U.S. occupation when Islamic State swept through part of the country in 2014. It remains deeply dependent on oil exports, and government spending will remain the only major driver of economic growth for years to come.

For at least two decades the West Bank and the Gaza Strip have been stunted by Israeli occupation and conflict with Israel. The territories are heavily dependent on international aid and remittances, and agriculture and manufacturing are significantly curtailed. Political economist Sara Roy has analyzed the terrible economic and social conditions for Palestinians caused by Israel's policy of imposing curfews and travel bans, expropriating land, destroying civilian infrastructure, and uprooting tens of thousands of olive and citrus trees.[52] An Israeli and Egyptian blockade of the Hamas-controlled Gaza Strip after 2006, coupled with Israeli military offensives there in December 2008 and January 2009, 2012, and 2014 have left two-thirds of the population living in poverty. According to the United Nations, the 2014 conflict in Gaza killed more than 2,200 Palestinians, destroyed or damaged more than 18,000 dwellings, and destroyed much of Gaza's infrastructure. More than 80 percent of residents there rely on food aid, and electricity is limited.

CONCLUSION

Conservative monarchies have survived the Arab Spring and are increasingly assertive in promoting the interests of Sunni Muslims, fueling more instability in Syria, Iraq, Yemen and Bahrain. The breakdown of central government authority in Syria, Iraq, Libya, and Yemen has given rise to militias and radical Islamists, spreading sectarian conflict and resulting in humanitarian disasters.

There are many contradictory trends in the MENA's political economy. Each country has its own unique set of state—society—market tensions. Israel and Turkey are faring much better than the other countries. The majority of countries face structural pressures from the international community. Forces from within society are clamoring for a role in reshaping governance, even if they disagree over what an ideal nation should look like. The genie of popular political mobilization is unlikely to go back in the bottle in countries swept up in the Arab Spring; without the opportunity for democratic participation, violence will fester.

Each of the main IPE perspectives interprets developments in the Middle East differently, based on different assumptions about history and what motivates actors. A mercantilist would probably attribute many of the conflicts and development outcomes discussed in this chapter to the struggle by states for power and protection of national interests. Economic liberal theorists stress the inevitability of MENA reforms as a result of global market forces. The dynamism of Dubai and Israel, as well as the democratic advances in Tunisia, suggest that people open to the world's ideas and goods are most likely to thrive. Structuralists could point to the MENA's weak industrialization and great disparities of wealth as evidence of the exploitation inherent in global capitalism.

The threat of more violence and disorder looms in many countries, where peace processes are stalled. The large countries of Turkey and Egypt have turned much more authoritarian rather than continuing transitions toward democracy. Our analysis of the region, nevertheless, does allow us to have some optimism. History does not have to repeat itself; the new generation in many countries is capable of overcoming old grievances. The Middle East's future will ultimately depend not on the actions of foreigners but on what Middle Easterners do to, and for, themselves.

KEY TERMS

Arab Spring 376
defensive modernization 378
mujahideen 381
Islamic State (ISIS) 382
jihadist 382
Oil for Food Program 385
Conspiracism 386
Muslim Brotherhood 388
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DISCUSSION QUESTIONS

1. Compare and contrast the economic conditions and development strategies of several MENA countries. Which countries are most prepared to face the challenges of globalization? Explain.
2. Are most of the MENA'S security problems due to foreign meddling or to the policies of domestic leaders? What are other important causes of MENA conflicts?
3. What characteristics of the Arab Spring are likely to facilitate or hinder the spread of democracy? What are the most appropriate ways in which the Western countries could facilitate the establishment of stable institutions in conflict-ridden countries?
4. What are the most important "human connections" between the Middle East and the rest of the world? Do you believe that individuals and nongovernmental organizations are able to influence changes in the region?
5. How will past and present human tragedies likely shape the perceptions of the next generation in the MENA?

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PART IV
Transnational Problems and Dilemmas

CHAPTER
15
The Illicit Global Economy: The Dark Side of Globalization



A firearm and 154 pounds of heroin seized by the Drug Enforcement Administration in May 2015, the largest ever such seizure in New York state.
Source: AP Photo/Mark Lennihan.

Behaving as if only the licit side of IPE exists because it is the easiest to measure and quantify is the equivalent of the drunkard saying that the reason he is stumbling around looking for his keys under the streetlight is because it is the only place where he can see. What we need are better fashlights so that we can also look for our keys down the dark alleys of the global economy.

Peter Andreas[1]

In April 2016, U.S. federal agents discovered a half-mile-long underground tunnel linking

two sites in Tijuana, Mexico, and Otay Mesa, California. Equipped with electricity, ventilation, an elevator, and a rail system, the "super tunnel" was the largest ever discovered on the border. A Mexican drug cartel used it for drug smuggling: agents seized 14,000 pounds of marijuana and 2,242 pounds of cocaine.[2] Between 2011 and 2016, agents discovered 67 tunnels along the United States–Mexico border, which they suspect were used to bring tens of millions of dollars worth of drugs into the U.S. market. Other parts of the world have smuggling tunnels, too. Facing an Israeli blockade after July 2007, Palestinians in the Gaza Strip have used tunnels under the border with Egypt to bring in everything from gasoline and cement to medicine and missiles. At one point the tunnels were the largest non-governmental employer in Gaza.[3] And in mid-2012, authorities uncovered a 700-meter tunnel under the Ukraine–Slovakia border for bringing contraband cigarettes into the European Union without paying customs duties.[4]

The tunnels are just some of the links in a vast illicit global economy that brings goods, services, and people across borders every day in defance of the laws of many states. Law enforcement offcials occasionally give the public a glimpse of the world of illicit actors and the threats they pose. Nevertheless, illicit international exchanges usually occur in a shadowy world that most consumers never see directly.

This chapter analyzes a broad range of illicit markets that pose signifcant challenges to governments and legitimate businesses throughout the world. The illicit global economy consists of economic transactions that states cannot easily regulate or tax. A variety of adjectives are commonly used to describe these global markets: *illicit*, *illegal*, *informal*, *black*, *gray*, *shadow*, *extrastate*, *underground*, and *offshore*. The processes going on in these markets include smuggling, traffcking, money laundering, tax evasion, and counterfeiting. The actors conducting these transactions make profts by breaking laws, defying authority, ignoring borders, and often using violence to exploit other people. In previous chapters, we suggested that illegal behavior (i.e., men and women behaving badly) was one of the causes of the global fnancial crisis and a common practice among many transnational corporations. Ironically, the global recession after 2008 also increased illicit transactions as more desperate and vulnerable people fell prey to traffckers and as struggling businesses tried to cut costs by skirting the law.

Until recently, IPE scholars left the study of the illicit global economy to other social scientists. Criminologists have for years studied transnational organized crime groups. Sociologists have looked at the social effects of criminal activities such as drug traffcking and prostitution. International relations experts have been examining the connection between money laundering and terrorism since 9/11. Comparative politics specialists have studied the effects of corruption on political development. And anthropologists have conducted research on informal markets in developing countries.

However, IPE scholars have increasingly recognized the theoretical and practical implications of the illicit realm. They have begun to synthesize the work of the other disciplines and branch out beyond the study of what is legal and easily measurable in the global economy. They realize that a close look at the illicit global economy helps us garner new insights into the relationships among states, markets, and societies.

Political scientist Peter Andreas notes that existing IPE perspectives help us understand some—but not all—of what we witness in the shadows.[5] Realists help us understand why security-obsessed states invest so much money and resources in international law enforcement. Liberal theorists help us understand under what conditions multilateral cooperation against crime will occur. Constructivists highlight the role that nongovernmental groups play in changing the public's perception of illicit transactions. And structuralists point out that countries that rely on exports of illegal resources are stuck in a dependent, exploitative relationship with the "core" countries.

However, the illegal economy also provides a challenge to the three main IPE perspectives. Although mercantilists stress the primacy of the nation-state, the illicit global economy is full of nonstate actors that sometimes thwart the rules and institutions of even powerful countries. Whereas liberals focus on the market's invisible hand and individual freedom, the illicit global economy is full of powerful, manipulative criminal hands. The open commercial interchange and deregulation that liberalism promotes are supposed to lead to peace and prosperity, but in the illicit realm unfettered trade can spread horrible confict, pervasive coercion, and social decay. Structuralists tend to portray capitalist, developed countries as exploiters of the developing countries, but in the illicit global economy, developing countries can sometimes take revenge on the North, as when China steals intellectual property or when secrecy jurisdictions (places with strong bank privacy laws) in the Caribbean attract billions of dollars from wealthy tax evaders.

In this chapter we make several arguments:

- Far from reducing black market activity, globalization gives criminals new ways to proft from their cross-border business.
- Well-intentioned attempts by governments to stop the supply of illicit products sometimes cause more harm than good.
- International cooperation against transnational crime is hard to sustain and often ineffective.
- Consumers bear as much responsibility as international suppliers for nurturing illegal commerce.
- The threats to national security, social well-being, and legal commerce keep growing.

THE ILLICIT ECONOMY IN HISTORICAL PERSPECTIVE

Illicit transactions did not suddenly appear a decade or so ago; there have been many illicit activities in history that have fundamentally shaped relations among states. Centuries ago, European rulers and Barbary Coast potentates authorized pirates to seize other countries' ships and split the booty with them. European countries colonized many parts of the world, seizing the territory and the property of their inhabitants. Although at the time the colonial powers tried to justify colonialism as a kind of civilizing mission, their activities amounted to little more than theft.

Historians Kenneth Pomeranz and Steven Topik argue that violence used to be an important way to gain "comparative advantage" and important commercial benefts in the world. Great Britain, Spain, other European countries, and the United States moved up the rungs of the ladder of development by engaging in land grabbing, slavery, looting, and dope peddling in their own countries and their colonial possessions. As both authors argue, "Bloody hands and the invisible hand often worked in concert: in fact, they were often attached to the same body."[6] They recount how Britain once forced China to buy opium; Belgium brutalized millions of Congo inhabitants and slaughtered elephants for ivory; Spain and Portugal literally plundered the Aztec and Inca civilizations; and U.S. entrepreneurs traffcked in slaves for decades.

Marxists, too, have long recognized that the development of capitalism is rooted in processes of primitive accumulation, whereby the upper classes coercively or violently seize assets (such as land) from other actors. Sociologist Charles Tilly famously asserted that state-making is quite similar to organized crime.[7] Just like crime bosses, would-be leaders centuries ago used violence against their rivals and extracted "protection money" that they used to expand their territory and make war. Eventually these state-makers gained legitimacy as kings and turned extortion into legal taxation, masking their sometimes violent and thuggish beginnings.

History shows us that leaders of states have often participated in or sanctioned violent illicit activities. At the same time, these leaders have the power to defne *what* is legal or illegal and *who* is a legitimate entrepreneur or an illegitimate one. We see that illicit activities can be very benefcial to some states while being simultaneously disastrous for others. Capitalism in its early stages was more like the Wild West than a contemporary, well-planned industrial zone.

Illicit transactions today often mirror, replicate, or repeat these historical processes, even though we often tend to give new names to modern processes. For example, human traffcking is a modern-day form of slavery practiced around the world. Today's drug lords expropriate from peasants and addicts alike, expanding their turf and productive apparatus as would-be kings once did. Corrupt leaders in places such as Nigeria and Iraq have stolen massive amounts of public resources, just as European powers stole from the colonies that

they were supposed to be helping. Some leaders in recent decades, such as Slobodan Milosevic in Serbia and Charles Taylor in Liberia, ran their states like criminal enterprises, working in cahoots with *mafosos* to keep their kleptocracies running before they were ultimately ousted by foreign countries. Israel's seizure for decades of Palestinian land is little different from state-sanctioned theft by pirates and imperialists hundreds of years ago. States and entrepreneurs today still sometimes use violence and coercion to harm their competitors. Although we like to think that the excesses of the past are limited today by international law, good government, and even globalization itself, the reality is that illicit history repeats itself (albeit with new names, new faces, and new *modus operandi*).

THE STAKES AND THE ACTORS

How big and how important is the illicit global economy? There are many disagreements about the answers to these questions, partly because extralegal transactions are so diffcult to measure. Governments and multilateral institutions often engage in hyperbole, sometimes either to tout their supposed achievements against the "bad guys" or to heighten threats for political reasons. Canadian economist R. T. Naylor warns us against having too much faith in estimates of the illicit economy's size, which often are based on bad information and false assumptions. For example, he notes that a widely cited estimate of annual global sales of illegal drugs at $500 billion was concocted by a UN offcial giving a speech in 1989 to grab public attention.[8]

Based on a 2011 meta-analysis of various crime studies, the United Nations Offce on Drugs and Crime (UNODC) estimates that the annual proceeds of drug traffcking and transnational organized crime are equal to 3.6 percent of global gross domestic product (GDP)—or about $2.1 trillion.[9] This estimate may be inflated because it includes the amount of taxes that multinational corporations and investors evade by shifting their money around different jurisdictions. Raymond Baker, a fellow at the Center for International Policy in Washington, DC, gives us a different calculation of "dirty money" that results from public corruption and criminal activities (other than tax evasion).[10] He estimates that annual cross-border sales (in 2005) of illegal drugs and counterfeit goods may amount to as high as $320 billion. Revenues from human trafficking could amount to $15 billion annually. International smuggling of arms, cigarettes, cars, oil, timber, and art may be worth as much as $110 billion annually.

"Guesstimates" though these figures may be, they indicate that the scale of the illicit problem has important implications for development, democracy, and security. The stakes are high. Baker believes that growing illegality is a major contributor to inequality and poverty in the world: "With common techniques and use of the same structures, drug dealers, other criminals, terrorists, corrupt government officials, and corporate CEOs and managers are united in abuse of capitalism, to the detriment of the rich in western societies and billions of poor around the world,"[11] Likewise, Moisés Naim, the former editor of *Foreign Policy* magazine, does not believe that democracy can emerge in countries dominated by powerful criminal networks.[12] The illegal economy can also undermine fragile new democracies by putting money into the hands of rivals of the central government, corrupting institutions such as the judiciary, and decreasing government efficacy. In all democracies, it lowers social trust and the belief that one shares the same values as one's fellow citizens.

Who are the central actors in the high-stakes illegal networks? We all have a tendency to believe that the main actors are *mafia* dons, drug lords, and other organized crime figures. The ruthless criminals of Hollywood movies do exist, but full-time gangsters are only one part of a much wider puzzle. Many participants have one foot in the legal world and one in

the illegal world, making it difficult to create a profile of the typical illicit actor. Participants include soldiers who loot, government officials who extort, CEOs who evade corporate taxes, bankers who loan to Third World dictators, and consumers who buy fake Louis Vuitton handbags. Even humanitarian workers in war-torn African countries have been known to participate in diamond trafficking.

Just as law-abiding citizens sometimes dabble in the black market, well-trained, "normal" economic actors such as accountants and computer programmers sometimes lend their skills to unethical or criminal operators. For example, anthropologist Carolyn Nordstrom has pointed out that "smugglers today are more likely to be armed with a degree from a leading ICT/computer technology course than an assault rifle."[13] The work skills that the world of international trade demands are also needed in the shadow economies.

There is often no clear wall between the licit and the illicit global economy. Buyers may not know (or not care to know) from whom their suppliers get products. A consumer may illegally download music at night and pay for licensed videogames the next day. A multinational corporation paying almost no taxes in the high-tax country where it is headquartered could be scrupulously paying corporate taxes in low-tax countries where its affiliates operate. Products that start out in some kind of shady operation often enter the "regular" market at a later point. Items produced in the legal market (such as cigarettes) may end up being smuggled across borders. Machine guns sold legally to an army in one country may end up in the arms of insurgents in a neighboring country.

STUDING THE ILLICIT ECONOMY: KEY FINDINGS

Studying cross-border illegal activities provides insights into problems we see in the global economy. Consider the following questions: Why do some kinds of market regulations have unexpectedly negative consequences? Why don't economic sanctions work well in changing the behavior of rogue regimes? Why aren't governments winning the war against drugs? Why did millions die from war in resource-rich Congo after 1998? In this section we examine six important analytical findings about the illicit global economy that help us answer important questions like these. These findings demonstrate the role that consumers, law enforcement, and globalization play in the growth of black markets. They also explain how illicit transactions affect war, development, and cooperation among states.

Six Degrees of Separation

"I am bound to everyone on this planet by a trail of six people," says one of the characters in John Guare's play Six Degrees of Separation.[14] In illicit markets, producers and consumers are also related to one another through a small number of people living in different parts of the world. Between a procurer and a consumer are financers, processors, shippers, importers, distributors, retailers, and other actors. If we look at international transactions involving the movement of goods and services, we see a global chain along whose links many points of illegality can occur.

The human connections in the chain reveal that none of us is completely divorced from the illegal world. Whether at the beginning, middle, or end of a chain of market interactions, we wittingly or unwittingly are involved in a process that may have been part of the extralegal world. Sometimes we can see our part in the chain, as when a drug user buys cocaine from a street seller. At other times, our part in the chain is largely invisible, as when someone buys a cheap piece of Chinese-made furniture that contains wood from an illegally logged region in Russia's Far East. The greater our degree of separation from the illicit part of a global commodity chain, the less we feel responsible for it.

Carolyn Nordstrom points out that ordinary consumers around the world are deeply complicit in smuggling. She found that in the African war zones where she did research, everyday, mundane commodities such as rice, cigarettes, vegetables, and antibiotics constitute a big chunk of unofficial trade.[15] One can hardly survive in some of these areas without buying smuggled, untaxed items in the informal economy. In developed countries, consumers of downloaded media, drugs, cigarettes, and art, to name just a few products, often know that they are buying knockoffs, pirated copies, untaxed items, or stolen property.

However, a countertrend is emerging. Multinational corporations and retailers are taking into consideration that increasing numbers of consumers want to separate themselves from unethical and illegal practices. The fair-trade coffee movement and the antisweatshop movement have conditioned consumers to think about the ultimate effects of their

domestic purchases on overseas workers. Similarly, businesses are keen not to be tainted by ties to illegal activities overseas that transnational advocacy groups are publicizing. For example, in the face of criticism that diamonds from some African countries were fueling wars, the De Beers company participated in a global scheme to track the origins of rough diamond purchases so as to weed out those coming from conflict zones (see Box 15.1).

DE BEERS AND BLOOD AND BLOOD DIAMONDS

Thanks to years of advertising by the De Beers Group, the world's largest diamond multinational company, most consumers are familiar with the phrases "A diamond is forever" and "Diamonds are a girl's best friend." In the last two decades, nongovernmental organizations that are critical of the connection between the diamond trade and African civil wars have spread two alternative slogans: "An amputation is forever" and "Diamonds are a guerrilla's best friend."They argue that the diamond industry has helped to finance rebel groups in places such as Sierra Leone, the Congo, and Angola, where millions of people have been killed, mutilated, raped, or displaced during civil war. The attention to blood diamonds (also called "conflict diamonds") has forced the diamond industry, as well as governments and multilateral institutions, to better regulate the international trade.

For many years, De Beers sold most of its rough diamonds through its London-based Diamond Trading Company (DTC). It sold diamond parcels at ten annual "sights" to approximately 125 "sightholders" who then took the diamonds to other cities, where they were repackaged for further sale to companies that then cut, polished, and resold the diamonds to independent retailers. Since 2014, De Beers has conducted its main sightholder sales in Gabarone, Botswana. As of 2002, De Beers reportedly controlled about two-thirds of the world's annual supply of rough diamonds.[a] Its share of the global market has declined over the decades, reaching less than 40 percent in 2017, but the rest of the industry still relies on its marketing to convince international consumers that diamonds are as rare as the love that inspires consumers to buy one.

Because of the difficulty of tracing the origin of any particular diamond and the ease with which diamonds can be moved, these gems became a form of currency for illegitimate actors. In the 1990s, DeBeers purchased some of its diamonds in Liberia, Guinea, and Cote d'Ivoire—countries that were transit points for diamonds smuggled from war-torn Sierra Leone. How did diamonds contribute to Sierra Leone's bloodshed? In 1991 a group of Libyan-trained rebels in Sierra Leone formed the Revolutionary United Front (RU F) and began attacking government forces.They seized some government-run diamond mines and over the next decade ran an illicit economy, smuggling diamonds to neighboring nations and trading them for weapons and drugs.The civil war unleashed by the RU F caused the death of more than 50,000 people and the displacement of more than two million. In January 1999 the RU F attacked Freetown, Sierra Leone's capital, and conducted Operation No Living Thing —murdering, raping, and mutilating hundreds of civilians.

The international community could no longer ignore the tiny West African country. The United Nations helped broker a weak peace accord between the RU F and the government of Sierra Leone. The UN Security Council adopted a diamond

embargo that banned the direct or indirect import of rough diamonds not sanctioned by the government of Sierra Leone. In 2000 the government of Sierra Leone and the Belgium Diamond High Council created a system under which each diamond arriving in Antwerp from Sierra Leone required a certificate of origin printed on security paper, registration through an electronic database, and electronic confirmation upon arrival.The RU F was quick to find a way around the new requirements, using Liberia and Guinea as cover for the export of illegally-mined diamonds into the legitimate market.This prompted the Security Council to impose sanctions against Liberia in May 2001, which included a ban against the export of rough diamonds.

In the face of the blood diamond problem, civil society groups such as Britain's Global Witness and Canada's Partnership Africa Canada joined diamond companies such as De Beers, the World DiamondCouncil, and dozens of governments to establish the Kimberly Process Certification Scheme (KPCS) in January 2003. KPCS members voluntarily collaborate to prevent illegal rough diamonds from entering international trade networks and to shun countries and companies that cannot certify that their diamonds are conflict-free.[b]

The Kimberly Process is a significant example of a global public—private partnership to combat an illicit activity. Blood diamonds are not completely out of the market: in the last decade they have funded violent groups in the Central African Republic and the government in Zimbabwe, which has committed severe human rights abuses and has violently monopolized the country's lucrative diamond industry and trade.[c] Although KPCS is not a panacea, it did help to foster peace in Sierra Leone and Angola, boost government revenues from legitimate exports, and make consumers more knowledgeable about where their products come from.

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Socially responsible investing is another mechanism through which people can separate themselves from some illegal markets by putting their money in investment funds that avoid companies or countries that are perceived as being socially or environmentally unethical. Related to this are a host of divestment-type movements led by local governments, pension funds, and boardrooms to avoid investing in places where the capital will benefit dictators or criminals. These types of divestment strategies often indirectly target companies and countries linked to illicit activities such as land expropriation and oil

corruption. Sometimes they go beyond divestment and turn into bans on doing any business or trade with certain companies and countries. Divestment strategies are basically a form of boycott that challenges economic liberal principles governing trade and capital flows.

The Unintended Consequences of Supply-Side Policies

Many scholars point to a strong tendency of governments to adopt policies targeting the supply side of illicit products through interdiction, repression, and eradication. Going after suppliers in foreign countries rather than consumers in one's own country is politically convenient, even though this focus has been shown in many cases to be more expensive and less effective. For example, the United States spends enormous funds trying to stop illegal immigrants from crossing the border with Mexico but significantly less money or effort punishing U.S. businesses that hire undocumented workers. Similarly, 55 percent of the U.S. federal government's drug control spending goes to supply reduction while only 45 percent goes to demand reduction.[16]In the global sex industry, law enforcement has a long history of cracking down on prostitutes rather than on the johns who pay for their services.

The reasons states mostly go after the supply side of illicit markets have a lot to do with the powerful political, economic, and cultural interests in a society. There is often a sacrifice of efficiency and social goals when powerful actors force governments to attack illicit problems in "someone else's backyard." When law enforcement tries to stop the supply side, it often does not achieve the intended results. In fact, there are often perverse consequences. Crackdowns in one area often simply displace illicit activity to another area —a phenomenon called the balloon effect. For example, a ratcheting up of policing on one part of a border causes smugglers to move to a less secure part of the border. In addition, a supply-side crackdown might drive an illegal activity further underground, making it even harder to control. And a campaign against suppliers can often increase violence and "turf wars" in a society.

Phil Williams points out that efforts to restrict activities create a restriction-opportunity dilemma: The more that countries try to impose arms embargoes or ban substances such as drugs or Freon, the more they "provide inroads for the creation of new criminal markets or the enlargement of existing markets." [17] A similar unintended outcome is called the profit paradox."[18] When states use law enforcement to try to prohibit drugs, the reduction of supply tends to drive up prices. This bolsters the profits of those entrepreneurs willing to take the risk to keep on supplying the black market. And the higher price encourages other would-be criminals to get into the business. One result is that, after a temporary lull, supply climbs up again as criminals find more ingenious ways of getting around prohibitions—and the price goes back down. Another possible result is that the most ruthless and violent criminals gain even more dominance of the illicit market. This dilemma is evident in many areas, leading some to argue in favor of decriminalization of certain types of illicit activity.

Globalization: The Double-Edged Sword

From studying illicit markets we learn that globalization is a double-edged sword: Open markets may increase global efficiency, but they also empower the bad guys. Although we still do not know if the ratio of illegal to legal business in the world is increasing, we can be sure that in some countries the ratio has risen. Technological change, which has become something of an object of devotion in Western societies, can also be a false idol. For each potentially desirable trend in neoliberal globalization, there is a criminal downside. This does not mean that the bad outweighs the good; rather that any compelling analysis of global change must account for negative externalities.

Naím points to the dark side of the end of the Cold War: The breakdown of the Soviet Union and the proliferation of weak, postcommunist states created new homes for illegal operations.[19] The transition to market economies gave rise to powerful *mafias,* influence peddling, and old-fashioned gangsterism. And some of the weak states that emerged from the collapse of the Soviet Union became smugglers' lairs. A case in point is Transdniestra, a sliver of Moldova that claimed independence in 1992 (even though no country has recognized its claim). It became a hub for trafficking of weapons, contraband, and stolen cars. And at the end of the Cold War, ex–Warsaw Pact countries off-loaded many small arms into Third World markets.

Many scholars identify global deregulation and privatization as culprits in the rise of the illicit. The opening of capital markets facilitated the flow of "hot" money around the world. Deregulation of airlines and shipping industries beginning in the 1980s fueled some forms of trafficking. The rapid-fire sale of state enterprises contributed to widespread corruption. Regional integration based on free-trade agreements weakened border control.

Businesses looking for technical solutions to smuggling, such as by embedding radio frequency emitters in products, often find themselves outsmarted by criminals. However, Peter Andreas points out that states are also taking advantage of technological innovations that accompany globalization to police the bad guys. For example, digitization enables government database mining, biometric identification, and better electronic eavesdropping.[20] Currency-printing innovations help governments stave off counterfeit paper money. Global positioning system (GPS) technology helps governments track criminal activities such as illegal timber harvesting and overfishing. And scientists expect to perfect rapid DNA testing that would help customs officials detect the origin and species of many plants and animals that smugglers fraudulently send across borders.

The Problem with Coordination between States

One of the important questions that IPE examines is why states succeed or fail in cooperating with one another. As we learned in earlier chapters, realists view states as constantly competing with one another, whereas liberals stress the ability of governments to coordinate their interactions peacefully. Another of the major findings from the study of illicit markets is that state makes coordinated policies against the shadows very difficult. Why is this so?

One major reason is that states are jealous of their sovereignty. They do not like

interference in their domestic affairs, and they do not want to be responsible for enforcing the laws of other states. In fact, they will sometimes take advantage of illicit activities outside their borders. Although illicit markets can threaten sovereignty, sovereignty can also shield black markets. For example, some states have become havens for criminal operations. They charge global outlaws a fee for protection behind their sovereign cocoon. In this kind of failed state, leaders can issue diplomatic passports to dubious businessmen and allow the establishment of servers to conduct Internet gambling or pornography distribution. In exchange for a payoff, they may look the other way as criminals use their territory to smuggle goods. Similarly, many transport companies register their ships and airplanes in countries where they actually conduct very little or none of their global business. These registration countries are supposed to be responsible for making sure that the ships and airplanes follow international regulations, but often the countries are just selling a flag of convenience and have no interest in investigating law-breaking by the transport companies.

These activities are part of a wider phenomenon that Ronen Palan calls the commercialization of sovereignty—the renting out of commercial privileges and protections to citizens and companies from other countries.[21] For example, a state can market itself as a place to disguise the origin of dirty money. Dozens of mostly small countries and territories are tax havens (also referred to as offshore financial centers or secrecy jurisdictions), where foreigners can park their money and conduct international financial transactions with very little regulation by local officials. These places—such as the Cayman Islands—attract money launderers and tax evaders who want to stay entirely out of the reach of their home governments. These sovereign jurisdictions benefit both indirectly and directly from global crime (as well as from legitimate international business).

In his book *Treasure Islands,* Nicholas Shaxson stresses that these havens are ubiquitous and integral to the operations of global capitalism. They are also to be found in many developed countries, including Switzerland, British overseas territories, and U.S. states such as Delaware and Nevada. He argues that they "provide wealthy and powerful elites with secrecy and all manner of ways to shrug off the laws and duties that come with living in and obtaining benefits from financial regulation, criminal laws, inheritance rules, and many others."[22]

Putting political pressure on sovereign states that ignore what companies do in their territory is one way of trying to shut down illicit networks, but it is not necessarily the most effective. The technique often backfires. Government officials in some states do not want to get rid of illicit transactions (especially if these leaders themselves are participating in illegal activities). Even if these leaders really do want to reduce corruption or shadow activities, they might not have the capacity to do so; or if they try to, they may end up being overthrown. In this latter case, punishing a government for not cooperating with the global community may have the unintended effect of weakening institution-building in poorer countries. The World Bank under its former president Paul Wolfowitz instituted a punitive model of anticorruption: cutting off aid to countries that failed to stop criminal activities that siphoned off foreign loans and development aid. The model was halted, in part, because it may have deprived weak but well-intentioned leaders of the very resources and

assistance they needed to fight the "bad guys" in their economy.

This raises the bigger question of under what conditions one country has the "right" to use force against another country in which illicit activities are occurring. If a state allows terrorists to launder money through its banking system, does an offended country have the natural right to use force against that state? Can one country use force to prevent massive counterfeiting of its currency in another country? If a country allows massive piracy and counterfeiting of the intellectual property of other countries to occur in its territory, is this tantamount to seizing foreign land in wartime?

There are many other reasons why states do not cooperate against crime. For one thing, illicit cross-border activities such as cigarette smuggling often occur precisely because laws or taxes differ from one state to another. Combating illegality would require states to better harmonize their legal systems, which is politically unpopular. It is also difficult for states to collaborate because there is no guarantee that they will actually honor the commitments they have made to other states. Third, effective international cooperation requires sharing information about one's citizens and companies, something states have always been reluctant to do because of privacy concerns or fears of espionage. This is a classic mercantilist impulse. Governments worry about how rival states will use sensitive information, however well-intentioned the initial cooperation.

Fourth, rival states sometimes encourage black market activities to undermine their enemies. For example, the Reagan administration sought to undermine the Soviets and leftist regimes by pouring weapons into Afghanistan, Angola, and Latin America, fueling arms bazaars that remained long after covert programs ended. Canadian economist R. T. Naylor reminds us that, as part of their mercantilist economic warfare hundreds of years ago, European powers tried to undermine rival states by encouraging counterfeiting, pirating, and the development of smuggling centers.[23] And Peter Andreas recounts some of the ways in which states instrumentalize illicitness to help themselves: by busting economic sanctions, selling nuclear technology, engaging in covert operations, and turning a blind eye to counterfeiting.

Fifth, it is hard to obtain serious cooperation from police forces and governments that are sometimes themselves complicit in illicit activities. In many weak states, officials protect crime syndicates in exchange for payoffs. And sometimes they are simply too afraid to take on criminal organizations and drug cartels. Former Colombian drug kingpin Pablo Escobar, for example, conducted a violent campaign against the government when it came after his cocaine empire in the 1980s and early 1990s. He ordered bombings of public facilities and assassinations of dozens of public officials.

In the absence of effective state cooperation, private companies and international civil society are trying to change norms and practices related to illicit activities. These voluntary efforts are not always successful, but they do put pressure on governments and influence public opinion. The private sector—worried about bad press and potential legal liability—has established codes of conduct and standards of behavior for big companies. For example, some of the world's largest private banks have voluntarily adopted regulations to minimize money laundering and other financial crimes. This is part of a broader, post-9/11 shift by

multinational corporations to know-thy-customer rules, whereby they more carefully screen their depositors, suppliers, and contractors. Even so, since 2011 U.S. officials have charged large banks—including Citigroup, HSBC, and Standard Chartered—with laundering the funds of drug traffickers, potential terrorists, and the government of Iran.

Name-and-shame campaigns also bring international attention to illegal and unethical practices. Transparency International is a prominent example of a group whose annual index of corruption—derived from surveys of businesspersons who conduct business in other countries—can pressure governments into trying to get out of the bottom of the rankings. The Tax Justice Network is part of a coalition of activists trying to embarrass and shame tax havens and TNCs that use shady global practices to avoid corporate taxes. Multilateral institutions such as the Financial Action Task Force (FATF) also blacklist countries that fail to adopt international financial standards. White listing is another inexpensive way for civic groups and governments simply to publicize companies with clean records in hopes that the market will shift toward their products and practices.

"Conflict Resources"

It has become increasingly clear since the 1980s that black market influences on natural resources have important effects on the global security structure. Weak governments and rebel groups in developing countries need money to buy weapons, pay off supporters, and finance their activities. Controlling the extraction and export of natural resources is an important way to guarantee a revenue flow. Insurgents also know that if they deprive the government of control over natural resources, they can achieve important political goals. International commodities dealers generally do not have any compunction about buying from criminal insurgents or corrupt governments.

As we mentioned in Box 15.1, several factions in the civil wars in Sierra Leone and the Central African Republic financed their fighting in part by illegally controlling diamond mining. Cambodia's Khmer Rouge relied on illegal timber and gem exports from the territory they controlled to fight the government in Phnom Penh in the 1980s and 1990s. During its long rebellion against the Colombian government, FARC *(Fuerzas Armadas Revolucionarias de Colombia)* raised money by taxing the drug trade.

In a particularly tragic case beginning in 1998, the Democratic Republic of the Congo was torn apart by militias and neighboring armies that jockeyed for control of rich mineral deposits. Armed groups with no legitimate claims to sovereignty engaged in the illegal extraction and export of minerals such as coltan, which is refined into tantalum, a high-value, strategic metal used in cell phones, computer chips, and aircraft engines. Facing intense scrutiny from global environmental and human rights groups, major cell phone manufacturers pressured their suppliers to avoid purchasing coltan/tantalum from the Congo, afraid that they would be accused of being responsible for some of the slaughter.

Scholar Michael Nest alerts us to the power of consumers in the big Western markets for electronics to pressure TNCs not to buy raw materials from conflict areas. But he finds that China—with more than 600 million cell phone users—has unfortunately been eager to do business with illegal coltan suppliers in Africa, counteracting the efforts of TNCs.[24]

Nevertheless, more governments around the world believe that pressuring companies to eliminate conflict minerals in their supply chains is an effective way to reduce violence and war in parts of Africa. As a result of the 2010 Dodd-Frank Act, U.S. companies are required to report to the Securities and Exchange Commission whether products they sell contain tantalum, tungsten, gold, or tin likely to have come from a conflict region.

Corruption Is Hampering Development

Political economists have spent decades correlating many factors with development success or failure, including the degree of trade openness, levels of political stability, and even the "squig-gliness" of borders. Corruption is thought to be a key factor hampering poor countries. For example, former leaders of Indonesia, the Philippines, and Nigeria skimmed billions of dollars from government coffers. An especially egregious example is the tiny country of Equatorial Guinea, ruled by dictator Teodoro Obiang since 1979. Despite being the third largest oil producer in Africa with a population of less than 800,000, the country has a high poverty rate. Most of the oil wealth—produced by the likes of Exxon Mobil and Marathon—falls into the hands of Obiang and his family.

Analysts of the illicit global economy agree that corruption is a big problem, but they argue that the cause of corruption is not simply bad leaders in developing countries. In other words, they find that corruption is a transnational process in which many legal and illegal actors are complicit. Therefore, the fight against it must focus on global actors.

Political scientist Jason Sharman uses a constructivist approach to explain the recent rise of a global norm against "grand corruption," a criminal phenomenon in which the ruler of a country systematically steals public funds.[25] Until the 1990s, Western banks gladly hosted corrupt money with few questions asked. Governments in developed countries also mostly ignored grand corruption in allied countries and the laundering of dirty money through Western financial institutions. This changed after 1990 with the rise of a global "anti-kleptocracy norm" that required states to prevent corrupt money from entering their financial system and to return any money to the country from which kleptocrats stole it. Sharman traces the rise of the norm against grand corruption to the end of the Cold War, when Western powers had less need to support corrupt dictators. Moreover, development experts and NGOs began to argue that corruption was a key reason why many countries were failing to develop. The anti-kleptocracy norm was institutionalized in the 2005 UN Convention Against Corruption and in nationallegislation in Europe and the United States that imposes legal obligations on banks. Sharman notes that despite some concerted efforts by Western countries to block dirty money and help victim countries recover assets, there remain many obstacles in the way of an effective global anti-corruption regime.

CASE STUDIES IN THE ILLICIT GLOBAL ECONOMY

Thus far we have looked at six significant analytical findings in studies of the illicit international economy. We have also estimated the stakes involved and identified some of the key players. Now we turn to some case studies—smuggling, drug trafficking, and human trafficking—to illustrate some of the general themes and to specify how and why illicit activities occur and with what social consequences.

Smuggling

Smuggling is one of the oldest professions in the world. Enterprising individuals seek to profit from transporting goods across borders in defiance of the rules that political leaders have imposed on exchanges. The objects of smuggling are as numerous as the techniques to avoid getting caught. Some of the most important smuggled items are oil, cigarettes, timber, counterfeit goods, antiquities, and animal parts.

Cross-border transactions are illegal only if states say they are illegal. In other words, states define what is smuggling and what is not, and these definitions often change over time. A product may be legal in the source country and illegal in the receiving country. Or it might be illegal in the source country and legal in the receiving country. Or it might be illegal in both countries. The particulars of each case will affect the scale of smuggling and the likelihood that states will cooperate to fight it.

What are the motives of those who engage in smuggling? Greed is an obvious reason. Smugglers are willing to take risks because they want to make higher profits than they could achieve through legal trade. However, keep in mind that mercantilist states also engage in smuggling for purposes of security. For example, the Chinese government and Chinese companies steal a lot of high technology from Western companies. In 2016 alone, German companies lost tens of billions of dollars to espionage, intellectual property theft, and data theft—a significant proportion of which was presumably conducted by Chinese hackers.[26] Governments also feel that they have a right to defy sanctions and embargoes imposed on them by hostile powers. Despite facing strict UN sanctions, Saddam Hussein smuggled oil out of Iraq and garnered billions of dollars to keep his regime afloat in the 1990s.

How do smugglers justify their actions? Often, they simply do not recognize the legitimacy of the political authority that is regulating trade or the legitimacy of a law that makes a particular type of trade illegal. For example, importers fed up with paying bribes to customs officials may see smuggling as legitimate avoidance of a predatory government. Similarly, some smugglers feel that import taxes are too high. Some smugglers simply do not recognize borders drawn by colonial powers. Others believe that they are supplying poor people with a product at a lower price, thus offering a sort of social service. In failed states or war zones, smuggling is sometimes the only way people can get access to food, medicines, and other necessities.

Smugglers take advantage of differing laws and regulations in neighboring countries to engage in arbitrage—buying a product in a lower-price market and selling it in a higher-price market. This opportunity for smuggling arises from price differentials resulting from cross-border variations in taxes, regulations, and availability. When governments restrict the supply of goods and services in the name of morality, public health, and environmental protection, they unintentionally encourage smuggling. For example, the U.S. government bans the reimportation of prescription drugs from Canada and Mexico, partly out of a concern for the safety of U.S. consumers and partly to protect the profits of U.S. drug companies. However, the lower prices of prescription drugs in Canada and Mexico have enticed many elderly Americans to look north and south for technically illegal sources. In a classic case, U.S. Prohibition in the 1920s spurred smuggling of alcohol from Canada. Borders in North America have always been quite porous.

Cigarette Smuggling

Tobacco is one of the most important smuggled products in the world. It is estimated that 11.6 percent of all cigarettes consumed in the world are smuggled and/or illegally produced, depriving governments of some $40 billion in taxes they are owed.[27] The National Research Council estimates that in the United States between 8.5 percent and 21 percent of all cigarettes sold are illegal.[28] Once cigarettes are "in transit" in the global trade system, smuggling allows distributors to avoid all taxes, thus enhancing profitability. Exported cigarettes often move through free-trade zones (FTZs), where regulations and customs controls are relatively weak and where taxes are not levied. Many cigarettes that end up in black markets around the world were trans-shipped through—or even manufactured in—large FTZs such as the Aruba Free Zone, the Colon Free Zone in Panama, and the Jebel Ali FTZ in Dubai.[29] For many years, major U.S. and European tobacco companies were actually complicit in the smuggling, because it was a way of opening up new markets.[30] In some developing countries, cigarette manufacturing, importing, and distribution are a state monopoly. Thus, competition from contraband cigarettes cuts into an important source of government revenue. (Developed countries often forget how much their treasuries relied on "sin" taxes on alcohol and tobacco before World War I.)

In a study of cigarette smuggling between the United States and Canada, Margaret Beare found that traffickers include Indian tribes, diplomats, soldiers, and tourists, who take advantage of special privileges they have under the law to move tobacco products across the border.[31] Canadian consumers have been very willing participants, partly because they view high taxes on cigarettes as unfair. Since 2003, the Canadian government and the European Union have sued major U.S. and Japanese cigarette manufacturers to force them to take steps to prevent smuggling of their products. This is a move to force manufacturers to take more responsibility for knowing what wholesalers do with tobacco products and what the chain of trade is from factory to the consumer. The World Health Organization has even proposed that every pack of cigarettes have an electronic mark on its packaging.

Another major impetus to smuggling is differential taxation—when taxes on the same product differ significantly from country to country. Even tax differences between states within the United States are an important cause of domestic black market operations. After 9/11, officials broke up many rings of people who were buying low-taxed cigarettes in NorthCarolina and Virginia and transporting them to high-tax states such as Michigan and New York, where they were sold at a markup in the black market. Since 2003, the U.S. Bureau of Alcohol, Tobacco, and Firearms has investigated more than 1,000 cases of cigarette bootlegging.

In 2012, member countries of the World Health Organization's Framework Convention on Tobacco Control adopted the Protocol to Eliminate the Illicit Trade in Tobacco Products, which will enter into force in 2018 if 40 countries have ratified it. The Protocol requires governments to establish a global system to track and trace cigarettes through their entire global supply chain in order to curtail the illicit trade. Despite the tobacco industry's objection to the Protocol, it has been signed or ratified by the world's biggest cigarette exporter, the European Union. However, big cigarette exporters such as Singapore, South Korea, the United States, Indonesia, and Ukraine have not signed the Protocol, which will undoubtedly undermine its global effectiveness.

Antiquities Smuggling

Antiquities are also big business for smugglers. Greece, Italy, Bolivia, and Thailand are among a number of countries that have laws severely restricting the export or sale of antiquities, which are considered part of their national patrimony. Nevertheless, the huge demand for art and antiquities in wealthy countries supports a thriving transnational trade in stolen cultural property. The trade is fueled by illegal excavations and looting that deprive countries of their culture and in many cases destroy knowledge about human history. Proceeds from antiquities smuggling often support warring groups. Simon Mackenzie points out that art dealers and collectors have a strong sense of entitlement to enjoy and preserve cultural items, and they take insufficient steps to verify the legal provenance of objects they purchase.[32]

The most important international agreements designed to control antiquities looting are UNESCO's 1970 Convention on the Means of Prohibiting and Preventing the Illicit Import, Export and Transfer of Ownership of Cultural Property and the 1995 UNIDROIT Convention on Stolen or Illegally Exported Cultural Objects. Some progress has been made in mitigating black market trade through the International Council of Museums' Red Lists of threatened archaeological objects. And the United States has in recent years signed Memoranda of Understanding with countries such as Peru, China, and Greece to ban importation into the United States of broad categories of archaeological items likely to have been looted. Although antiquities have historically moved from colonized and developing countries to Europe and the United States, in recent years China and the Gulf Arab states have become major markets for antiquities. China in particular is becoming the main destination for looted cultural property from South and Southeast

Asia.[33]

It remains difficult for countries to recover antiquities, in part because it is usually impossible to prove that they were stolen or where the illegal excavations occurred. Moreover, under the UNESCO and UNIDROT Conventions, a purchaser who exercises due diligence when buying an antiquity that is later found to be illegally excavated is entitled to compensation if the antiquity is returned to the source country. In recent years the Italian and Turkish governments have aggressively put pressure on major museums such as the Getty and New York's Metropolitan Museum of Art to return looted artifacts. An unfortunate side effect of the Arab Spring has been large-scale looting of major archaeological sites in Libya, Egypt, Iraq, and Syria.[34] TheUN Security Council passed Resolution 2199 in 2015 requiring, among other things, that UN members prohibit imports of Syrian and Iraqi cultural goods illegally taken from these countries, in order to deny funds to ISIS and other terrorist groups.

Illegal Timber Trade

The illegal timber trade is a subset of environmental crimes, which also include animal trafficking, illegal fishing, and hazardous waste trafficking. Interpol and the United Nations Environment Programme estimate that illegal logging accounts for between 15 to 30 percent of all global logging, with higher rates in tropical countries.[35] Some of the highest levels of illegal logging occur in Brazil, Indonesia, and Malaysia, the Democratic Republic of the Congo, and Papua New Guinea. Timber harvested illegally on state-owned land or in defiance of national regulations has always found hungry markets in Japan and the United States, but China has now become the main destination for illegal timber. The insatiable demand for paper and wood worldwide drives the market, which takes advantage of corrupt governments, civil conflict, and lax policing of enormous forested areas. The expansion of palm oil plantations in Indonesia and cattle farming in Brazil also contributes to illegal deforestation. Much illegal timber gets mixed with legitimately harvested wood at the time of export, making it difficult for importers to trace the true source of the product.

As countries like Indonesia and Thailand have been stripped of valuable forest cover, illegal logging has shifted to new areas like the Greater Congo Basin, Russia, Burma, and Papua New Guinea. This illicit market causes many follow-on problems that the global community must grapple with, including loss of biodiversity and increased global carbon emissions. Moreover, governments lose billions of dollars of tax revenue. Unfortunately, international efforts to suppress illegal deforestation have had limited effects. One treaty that countries have used in the fight is the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES), which obliges signatories to regulate the import and export of certain types of endangered tree species (as well as thousands of plant and animal species). In the United States, an amendment in 2008 to the Lacey Act—a long-standing environment protection law—criminalizes the importation of wood that was illegally harvested overseas and requires importers to declare the type of wood being brought in and its country of origin (see Box 15.2). Although many big

retailers like Home Depot, Wal-Mart, and Ikea now have much better supply chain systems to buy from sustainable forestry producers, wood from tropical countries still often comes from illegal sources.

Animal Trafficking

Smuggling of animals and animal parts is having a devastating effect on many species around the world. One of the difficulties in stopping wildlife trade is that the more endangered the animal, the higher the price for it and the greater the incentive to poach it, which accelerates its move toward extinction. All those who consume animal products are part of the chain of responsibility for poaching and illegal trade. Blame must be pointed in the direction of the fashion and cosmetics industry, tourists who buy trinkets made from animal parts, pet owners,and zoos.[36] Cultural beliefs produce avarice and covetousness that drive much of the poaching,argues R.T. Naylor in his book Crass Struggle.[37]

GIBSON GUITAR AND THE LACEY ACT

Some of the biggest names in classic rock music play Gibson guitars: Eric Clapton, Jimmy Page, Keith Richards, Angus Young, and Neil Young. So it was something of a surprise when in 2009 and again in 2011 agents from the U.S. Fish and Wildlife Service raided Gibson Guitars' factories in Nashville and Memphis, seizing wood used in guitar making. What had such an iconic American company done wrong? Federal authorities charged Gibson with importing ebony and rosewood in violation of the Lacey Act, a long-standing law amended in 2008 to prohibit the importation of any wood product illegally sourced in a foreign country.[a] Gibson's CEO Henry Juskiewicz vehemently contested the charges, but his company reached an out-of-court settlement in August 2012 in which it admitted to some wrongdoing and paid penalties of over $300,000. This case reveals how illicit logging collides with American manufacturing, environmental law, and U.S. domestic politics.

Rosewood and ebony have been used in guitars for a long time because of their durability and tonal quality. Unfortunately, the tree species these tropical woods come from are globally endangered due to overexploitation and illegal deforestation. Gibson imported ebony from Madagascar, even though it knew that the country had banned ebony exports. The guitar maker also imported ebony and rosewood from India, but the U.S. government dropped charges that those shipments had violated Indian laws. Among other things, the Lacey Act is designed to support forest conservation overseas and to shield U.S. sustainable forestry companies from having to compete unfairly with illegally sourced wood that drives down global prices.[b]

Gibson and its supporters took their case to the court of public opinion. How were they supposed to know whether or not one of their suppliers, or one of their suppliers' suppliers, had broken laws somewhere else in the world? They noted that because the Lacey Act *did* allow the import of finished ebony and rosewood (like fingerboards) but not unworked planks of wood—and because Madagascar and India allowed the export of finished but not unfinished wood—the net effect was to privilege wood crafters overseas using illegal wood and disadvantage wood crafting companies like Gibson in the United States. American companies thus lost high-skilled jobs, and countries with unenforced laws and corrupt governments could grow their workforce. Gibson claimed it was being "bullied" by an "out-of-control" federal government that was unfairly targeting small businesses. Juskiewicz made his case on conservative radio shows and Fox News, gaining support from Republican lawmakers.[c]

Gibson's critics blamed the company for profiting from an illegal market, deliberately mislabeling import records, and conveniently pleading ignorance about its supply chain.[d] They argued that it is the responsibility of any company to know where its supplies come from and to obey the laws that other countries have to protect their own forests. To deny that responsibility would open the door to any company to

import stolen goods, whether they be plundered antiquities, poached animals, or illegally sourced logs.

Before Gibson settled with the government, conservatives in Congress introduced bills in 2012 that would have watered down parts of the Lacey Act. An unlikely alliance of environmental groups, musicians, and U.S. timber companies lobbied to keep the Lacey Act strong.[e] The U.S. timber industry liked the Lacey Act because it served as a form of protectionism. Environmental groups like Greenpeace saw it as a tool in the global fight against deforestation. Even the Dave Matthews Band, Sting, Jack Johnson, Jason Mraz, Willie Nelson, and Maroon 5 signed a pledge supporting the Lacey Act and encouraging the use of only legally and sustainably harvested woods in musical instruments.[f] In the end, the Lacey Act was unchanged. The question remains whether most companies have the money or even the ability to police their supply chains back to the source of raw materials overseas. And will most guitar aficionados give up sonorous ebony and rosewood for sustainable tonewoods like maple, sapele, and African blackwood?

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Sadly, many of the most magnificent creatures in the world are headed for extinction, despite strict trade restrictions under the CITES Convention. The illegal ivory trade is responsible for drastic reductions in the number of elephants in Africa (see Box 15.3). After a multinational treaty to ban the trade of ivory came into effect in 1989, an unintended effect was an assault on hippopotamuses and walruses, whose tusks became a substitute for ivory. Only a few thousand tigers still exist in the wild, and they face the threat of being killed for their pelts and bones to use in "tiger wine." The graceful chiru, a small Tibetan antelope, is being hunted to extinction for its wool, which is smuggled into India and Nepal to make high-value shahtoush scarves. The pangolin, a small mammal that looks like an anteater, is illegally exported to China and Vietnam, where its meat is eaten as a delicacy and its scales are used in traditional Chinese medicine. The massive international

smuggling of more than 1 million African and Asian pangolins between 2000 and 2016, along with an even larger number of pangolins poached and eaten in source countries, is bringing the animal closer to the point of extinction.[38]

Given how much legal trade in animals and animal parts there is globally, many law enforcement agencies do not consider it a high priority to try to crack down on the illicit side of the trade. The CITES agreement has helped reduce global trade in many endangered species, although it is not a panacea, particularly when corrupt government officials and their criminal partners fail to enforce the treaty's rules. Moreover, some scholars argue that the international community's focus on complete bans on legal trade of some species and militarized responses to poaching end up "estranging [local] communities rather than giving them a stake in wildlife protection strategies."[39]

TRAFFICKING IN AFRICAN ELEPHANT IVORY[a]

Humans have driven many animals to extinction, but few have been pursued so relentlessly and simultaneously elicited as much sympathy as the African elephant. European colonial powers first triggered declines in the population of African elephants, but increasing demand for ivory caused elephant numbers to continue plummeting in many independent African countries in the 1960s and 1970s. The global community turned to the Convention on International Trade in Endangered Species of Wild Flora and Fauna, or CITES, to regulate the trade in ivory. Formed in 1973, the CITES treaty seeks to protect the world's endangered plants and animals by controlling their trade. Over-exploited plant and animal species are classified by three levels of restrictions: Appendix III (subject to some trade restrictions); Appendix II (cannot be traded without state-issued export permits); and Appendix I (almost all trade is prohibited due to threat of extinction).

In the mid-1980s the African elephant mortality rate reached a level twenty times what was considered sustainable for the population to survive.[b] In 1989, CITES member nations voted to move African elephants up from Appendix II to Appendix I, effectively banning almost all trade in African elephant ivory. Most nations considered a complete ban to be the only viable option to stop the devastation of African elephant populations. Zimbabwe was one of the few nations that protested the Appendix I listing, arguing that it penalized countries that allowed controlled hunting yet were able to keep their elephant populations at sustainable levels.

There is a clear dichotomy between what conservationists see as the appropriate course of action to combat the ivory trade and what is actually feasible in practice. While many Western nations and NGOs demand that African range states—the countries with elephant habitats—do more to conserve their elephants, range states often lack the resources or capacity to properly patrol their wildlife parks. Rangers often face great dangers in fighting poachers, and in some cases they take bribes and are complicit in poaching since their own wages are so low. Militias such as the Lord's Resistance Army in Uganda and the Janjaweed in Sudan are believed to control some elephant poaching operations. Civil wars in countries such as Mozambique and the Democratic Republic of the Congo made it nearly impossible for their governments to monitor and protect elephant habitats. Perhaps most importantly, high-level government corruption and weak law enforcement make it very difficult to stop the ivory trade or punish those responsible for it.

When the CITES ivory trade ban was passed in 1989, the United States, Japan, and European nations were responsible for the majority of the demand for ivory. Since then, demand from those regions has declined significantly. However, between 2006 and 2011 poaching levels rose sharply and remained very high through 2015. The primary cause? A growing market for ivory in China. An estimated 70 percent of

poached ivory ends up in China, some of which is openly sold in shops using false papers identifying it as antique.[c] Increased Chinese demand caused the average price per kilo of ivory to skyrocket, creating an incentive for even more poaching and smuggling. Chinese citizens are often implicated in the cross-continent smuggling of ivory as well. Many African range states have sizable numbers of Chinese expatriates who work on Chinese-sponsored development projects, creating a channel for ivory trafficking. In 2015 a prominent Chinese businesswoman living in Tanzania was arrested and revealed to be the leader of a large trafficking ring responsible for smuggling more than 700 elephant tusks out of Tanzania into China over a 15-year period.[d]

Educational campaigns and public pressure seem to be lowering Chinese demand for ivory. Surveys carried out in China by WildAid, a wildlife conservation group, showed that from 2012 to 2014 publicawareness that most ivory comes from poached elephants rose.[e] Bowing to international pressure, the Chinese government announced that it will close all it domestic licensed ivory factories and retail ivory sellers by the end of 2017.

Until recently, the United States was also a large market for illegal ivory, which was often falsely marked as antique to get around the ban. One 2014 study found that of the 1,250 ivory items found for sale in Los Angeles and San Francisco over a month-long period, the majority would be considered illegal under California law, and many had been artificially aged in attempts to pass them off as antiques.[f] In 2016, President Obama issued a near-total ban on U.S. domestic sales of ivory and restrictions on sales of antiques containing ivory.

As in other illicit markets, elephant poachers and traffickers take advantage of unstable governments, impoverished people, and the ever-increasing interconnectedness of the global economy to facilitate their illegal activities. International efforts to combat ivory trafficking are ongoing, but only about 415,000 elephants remained in Africa in 2016. The sobering conclusion of scholar and journalist Keith Somerville is this: "It is absolutely clear that twenty-seven years of banning the ivory trade and promoting militarised anti-poaching has not worked, and that demand reduction strategies have only shifted the focus of market demand rather than drastically reducing it."[g]

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Drug Trafficking

Drug trafficking is one of the most entrenched and lucrative illicit activities in the world. Although many drug plants, such as coca, marijuana, and poppies, are grown in developing countries and the refined drug products are mostly consumed in rich Northern countries, marijuana is one of Canada's largest cash crops, and in some states in the United States, it is also a key cash crop. The United Nations Office on Drugs and Crime estimates that about 5 percent of the world's adult population used illegal drugs at least once in 2015 (compared to 20 percent using tobacco, which helps explain why cigarette smuggling supplies a much larger market).[40] Most of the profits from the drug trade are at the retail end (in the North), where the markup on products is the greatest.

The global fight against drugs illustrates the enormous costs and limited success of supply-side policies. From 2009 to 2016, opium poppy cultivation in Afghanistan, the world's leading source of opium and heroin, grew by more than 60 percent, while heroin use in the United States doubled between 2007 and 2015. Between 2000 and 2016, the United States spent nearly $10 billion on Plan Colombia, an elaborate program to drastically reduce coca production in Colombia. Owing to massive aerial spraying and assistance to Colombia's military, the amount of coca cultivation in Colombia dropped by more than half by 2013, but there was no drop in the amount of global consumption, partly because cultivation expanded in Peru and Bolivia. Colombian cultivation then increased 30 from 2013 to 2015 crackdowns on in Peru and Bolivia.

Eva Bertram et al. have attributed these kinds of disappointing outcomes to the hydra effect, whereby an effort to stop drug production or trade in one area simply causes it to sprout up somewhere else.[41] Whatever success there has been in breaking up big cartels in South America has been offset by the spawning of a larger number of smaller trafficking groups. Colombian traffickers have resorted to using makeshift submarines to transport huge cargoes of cocaine to the United States. Mexico has also become a drug production and transit center as a result of crackdowns in South America. Mexican cartels now supply an estimated 70 percent of drugs imported by the United States.

In 2006, the Mexican government launched a major crackdown on drug traffickers, supported by some $2.8 billion that the U.S. Congress appropriated between 2008 and 2017 through the Mérida Initiative with Mexico. The violence between the Mexican army and cartels, and turf wars between Mexican traffickers themselves, caused an estimated 109,000 homicides between 2006 and 2016. In the first half of 2017, homicides in Mexico —mostly related to the drug war—were at all-time highs. The fight against the drug trade has strained the Mexican army and spread more crime into the United States. With the

trafficking come other social ills in Mexico, including widespread corruption and extortion.

Drug production and trafficking have had very negative effects on society, security, and government in developing countries (and in developed countries as well). Colombian economist Francisco Thoumi has documented the pervasive effects of drugs on the economies of the Andean countries (Colombia, Bolivia, and Peru).[42] Drug revenues have funded unsustainable real estate booms and other speculative investments. There has been a sharp decline in social trust, which makes it more costly for everyone to conduct normal business. Traffickers use drug export networks simultaneously to import contraband and weapons.

Thoumi argues that programs to encourage farmers to switch to alternative, legal crops have largely failed. Returns to farmers from illegal crops usually surpass potential revenues from food crops. The illicit industry also has profound environmental consequences. Drug production has spurred the destruction of rainforests as growers move into new territory. And in Yemen, the poorest Arab country, widespread cultivation of *qat*—*a* tree whose leaves are chewed for their narcotic effect—has put a strain on water resources and reduced the amount of acreage devoted to food crops.

In many parts of the world, guerrilla groups and paramilitaries have turned to drugs as an important source of revenue. Rebels in Colombia, Cambodia, and Afghanistan have all used drug revenue to buy weapons and finance their insurgencies. As countries in Central America have become key transit zones for drugs from South America, gun crimes and violence tied to the drug trade have spread in major cities. A significant proportion of those who end up in prison in developed countries have some connection to drug offenses.

Can drug trafficking be stopped? Probably not. David Mares points out that Northern countries have not had much success with unilateral threats to withhold aid from countries that fail to fight drugs seriously.[43] The United States sometimes threatens to "decertify" countries that do not adhere to U.S. priorities and to cut off aid and trade privileges. Multilateral police cooperation, border controls, spraying, and anticorruption programs may have some marginal benefits, but they rarely make a dent in overall drug flows. Even when crops are successfully sprayed and criminals jailed in supplying countries, corruption impedes criminal justice systems, and the profit motive leads to rapid relocation of destroyed crops and facilities.

Ultimately, any supply-side effort to combat elements of the drug production cycle faces two core challenges: weak governments and an end-user demand that creates tremendous financial incentives to continue producing at every level of the illicit supply chain. The European Union has focused many of its policies on the demand side, decriminalizing small-scale sales and use of marijuana. By 2016, an estimated 13 percent of all marijuana sales in the United States were conducted legally because of the many states that made sales and use legal. Many public policy specialists believe that demand reduction or harm reduction in consuming countries through public spending on health and education can be less costly and more effective in the long run. In 2011 a Global Commission on Drug Policy, whose commissioners included Kofi Annan, Paul Volker, Richard Branson, and former heads of government in Europe and Latin America, issued a report advocating an

end to the war on drugs, replacing it with policies of harm reduction, decriminalization, and regulation of legal drug sales.[44] Nevertheless the international treaties that require states to criminalize the manufacture, possession, and use of prohibited drugs still have strong support from a majority of governments.

Human Trafficking

According to the International Labour Organization (ILO), 25 million people globally are subjected to forced labor, including 4.8 million victims of forced sexual exploitation (mostly women and children).[45] Organized crime groups play an important role in the sex business. They include the Russian Mafia, the Chinese Triads, and the Japanese Yakuza. The former Soviet Union has been an important source of trafficked women since the collapse of communism sent economies in Russia, Ukraine, Moldova, and Belarus into a tailspin. Burma, Nepal, India, and Thailand are also important suppliers to the world's brothels. The trade is usually from poor countries to wealthier countries.

The roots of sex trafficking are in economic incentives, patriarchy, and poverty. Louise Shelley, an expert on transnational crime, argues, "Traffickers choose to trade in humans … because there are low start-up costs, minimal risks, high profits, and large demand. For organized crime groups, human beings have one added advantage over drugs: they can be sold repeatedly."[46] Where women and minors lack political rights, education, and legal protections, they tend to be victims of organized criminal networks. Global and national economic crises tend to disproportionately affect women and children, who are pushed into the international sex industry against their will. Child trafficking is practiced in many countries in which poor families place children into debt bondage or indentured servitude to an employer in another country. Even government officials and corrupt law enforcement personnel have become direct and indirect supporters of the exploitation of women and children by sex predators.

Illegal migration is another large and growing part of the human trafficking problem. David Kyle and John Dale point out a paradox: The more tightly a country controls its borders, the more would-be illegal border crossers have to turn to traffickers, and the higher the profits of professional smugglers.[47] In addition, scholars Douglas Massey, Jorge Durand, and Karen Pren argue that, beginning in the 1980s, the United States constructed a narrative of threat from Latino migration, put into place legal migration restrictions, and progressively militarized border enforcement. Ironically, these policies caused a net increase in illegal migration and a large rise in the number of undocumented people in the United States as "a circular flow of male workers going to a handful of states was transformed into a settled population of families the nation."[48]

Employers of undocumented residents in Europe and the United States share much of the blame for human trafficking. Powerful businesses need low-cost labor and are willing to break the law, absent credible threats of punishment. The United States and Europe are caught in a contradiction: Mercantilists and xenophobes want to restrict the flow of immigrants, but liberals who want flexible labor markets and low wages favor more

immigrants—legal or illegal.

How can human trafficking be diminished? One supposed way is to build border walls—a policy President Donald Trump advocates—and beef up interdiction at sea. An amnesty for undocumented workers and an expansive "guest worker" program are other possibilities. Advocates for prostitutes argue that if trafficked women in the sex industry were provided immunity from prosecution and protection from deportation, they would provide extensive evidence and testimony against organized crime figures. Some believe that consensual, commercial sex between adults should be decriminalized. R. T. Naylor, for example, believes that personal vice done voluntarily by adults should not be criminalized because there is no clear victim. A structuralist would argue, however, that personal choice is not really voluntary, especially in the case of poor people who are compelled to participate in illicit acts in order to obtain an income. Liberal theorists increasingly argue that labor migration is an inherent part of globalization, and states can reduce illicit flows by simply allowing more legal flows. Labor-importing countries would gain valuable, young, low-cost workers, and labor exporters would boost remittance flows to their economies.

International organizations, governments, and nongovernmental organizations (NGOs) have taken significant, albeit insufficient, steps in the last decade to tackle trafficking in persons. In 2000 the United Nations adopted the Convention on Transnational Crime and a related Protocol to Prevent, Suppress, and Punish Trafficking in Persons, Especially Women and Children. The United States ratified the convention and protocol in October 2005, joining more than 150 countries that are party to the convention. Other organizations that cooperate to combat the scourge of trafficking include the ILO and the Organization for Security and Cooperation in Europe.

Individual states have taken unilateral action to address the problem. In October 2000, the United States passed into law the Victims of Trafficking and Violence Protection Act, which, among other things, allows the president to impose sanctions on countries that do not meet minimum standards in fighting human trafficking. In 2017 the U.S. State Department determined in its annual *Trafficking in Persons Report* that twenty-three countries (including China, Russia, and Iran) have serious human trafficking problems and are not making concerted efforts to meet minimal standards for eliminating them, while forty-five more have significant trafficking problems. Each year the U.S. president can waive sanctions on countries with severe human trafficking problems by citing national security grounds. More than thirty countries—including the United States and many European countries—have extraterritorial laws that make it a crime for their citizens to in sex with children overseas.

NGOs have been very active against the sex trade and sex tourism industries. They publicize the poor records of governments, help women and children in danger, and lobby for better national and international legislation. The International Justice Mission, Amnesty International, and Anti-Slavery International are important organizations with anti-trafficking networks around the world. Many international charitable organizations also have programs to help victims. *New York Times* columnist Nicholas Kristof has for years raised awareness of sex trafficking, including in his co-authored, bestselling 2012

book, *Half the Sky: Turning Oppression into Opportunity for Women Worldwide*. Finally, the UN has a number of agencies that work with governments and NGOs to coordinate anti-trafficking initiatives.

CONCLUSION

This chapter has examined illicit international transactions that are sometimes overlooked by IPE scholars, who have only recently begun to draw on the work of criminologists, anthropologists, and legal scholars. It has shown that many illicit activities shaped the history of the global economy. The chapter also stresses that illicit activities are sometimes an unanticipated result of global free trade, and that the well-intentioned efforts of governments to halt black markets often have unintended negative consequences. Unless we recognize the terrible human exploitation that often takes place in the shadows, we cannot adequately assess the moral and ethical consequences of globalization.

The illicit global economy has important effects on the world's security, trade, and growth. It challenges the power of sovereign states and makes global governance more difficult. It is a network through which the world trades a wide array of products that threaten corporate bottom lines and public health. It often fuels conflict and violence, hinders development, and threatens the environment. It has the power to make the world both more equal and less fair. It shows us that globalization and technological innovation are not necessarily forces for the global good.

The illicit global economy blurs the line between the legal and illegal worlds of production, trade, and distribution. It makes it necessary for international organizations to establish and enforce new regulations and codes of conduct. It forces businesses to ask: What do I really know about my suppliers? How can I protect my reputation? It forces consumers to ask: Am I responsible for knowing where the products I buy come from? What degree of separation is there between me and others I am tied to in global commodity chains? Increasingly, international civil society is mobilizing to tackle illicit activities. NGOs realize that with pressure (and support) from the grassroots and from consumers, states and businesses can make more progress against illegal actors.

States still tend to rely on supply-side approaches to illicit problems. Their mercantilist reflex to repress and interdict clashes with the hidden hand of the market and the not-so-hidden power of transnational criminals. However, this hardly means that political authorities are helpless. Governments in Europe and North America are increasingly receptive to newer strategies such as decriminalization, harm reduction, and partnerships with civil society groups. If developing countries increase transparency and strengthen market regulation, they should be better able to keep illicit transactions in check.

KEY TERMS

secrecy jurisdictions 410
primitive accumulation 411
socially responsible investing 415
balloon effect 416
restriction-opportunity dilemma 416
profit paradox 416
flags of convenience 417
commercialization of sovereignty 417
tax havens 417
know-thy-customer 419
name-and-shame campaigns 419
anti-kleptocracy norm 420
arbitrage 422
Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES) 424
Lacey Act 424
hydra effect 429

DISCUSSION QUESTIONS

1. List some of the reasons why people participate in illicit markets.
2. How does a focus on illicit transactions help us explain development problems in the Third World? Is illicit activity an inherent aspect of global capitalism?
3. How are licit and illicit markets tied to each other? Are all those actors who benefit directly or indirectly from illicit transactions—even if they themselves don't engage in illegal acts— to be considered "guilty"? What responsibility do consumers and legitimate businesses have for illegal transactions and illicit networks?
4. On balance, does technological progress make illicit activities easier or harder? How can governments and corporations use technology to protect themselves from shadow actors?
5. How do the major findings about the illicit global economy confirm or challenge the key tenets of mercantilism, liberalism, and structuralism?
6. What are some of the unintended consequences of efforts to regulate the illicit global economy? How can states more effectively reduce the negative consequences of black markets?

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CHAPTER

16

Energy and the Environment: Navigating Climate Change and Global Disaster



Chinese workers install solar panels at a photovoltaic power station in December 2017.

Source: AP Photo/Imaginechina/Chen bin.

It's a stupid and reckless decision…. It undercuts our civilization's chances of surviving global warming, but it also undercuts our civilization itself.

Bill McKibben[1]

On June 1, 2017, U.S. president Donald Trump announced that he was withdrawing the United States from the Paris Agreement on Climate Change. The news shocked many citizens and officials in the 195 states that had agreed in Paris in 2015 to *voluntarily* meet

carbon reduction targets using methods of their own choosing. Public opinion polls taken right after the November 2016 election showed that nearly 70 percent of Americans supported the climate accord, while only 26 percent of Republicans opposed it. Even among Trump voters, a plurality (47 percent) supported the agreement.[2] Many corporations today have also gotten on board with the global campaign to curb greenhouse gases. Nevertheless, and despite so much scientific evidence that carbon emissions threaten the planet's survival in the next century, Trump remains a "climate change denier."

In this chapter we try to answer several major questions. First, why were past global attempts to reduce emissions largely unsuccessful? Second, what conditions made it possible for President Obama and the leaders of other nations to make a breakthrough in Paris in 2015? Third, what were the personal, political, and foreign policy factors that led President Trump to decide to abandon the Paris accord? Finally, what are the implications of the United States abdicating its role as one of the global leaders in the effort to curb greenhouse gases?

ORGANIZATION AND THESES

The first part of the chapter provides a brief overview of some key public and private actors involved in energy and environmental policies and some key concepts that scholars use. Next is a discussion of some interconnections between international energy and environmental policies, with an emphasis on shifts in market and political conditions since the 1960s. The third section discusses major political, economic, and social factors behind President Obama's decision to sign the Paris climate accord and President Trump's decision to withdraw from it. Finally, we end by pointing to implications of Trump's decision for global energy and environmental policies in the near future.

We offer five theses:

- The intersection of energy and environment trajectories has created an urgent need for states to limit global carbon emissions;
- Market conditions are now favorable for large investments in renewable energy to meet increasing energy demand and support the global climate change campaign;
- President Trump announced that the United States intends to pull out of the Paris Agreement mainly to give his political base a "win" and to spite "globalists," elites, and other nations.
- Trump's decision adds to the evidence that the third phase of the postwar global world order is passing.
- Regardless of U.S. politics and lack of U.S. leadership, the transition to renewable energy and stronger environmental protection is well under way in much of the world.

ACTORS AND CONCEPTS

Beginning in the 1960s, many actors became involved in managing energy and environmental issues, including nation-states, international organizations (IOs), nongovernmental organizations (NGOs), oil cartels, major oil companies, banks, international businesses, and noted individuals.

Nation-states deal with environmental problems in ways that reflect their different political, economic, and social institutions. In most industrialized nations, executives, legislatures, and judiciaries all shape energy and environmental regulations in ways that are quite contentious. On the whole, economic growth and industrialization in developed Western countries and formerly socialist countries were historically very costly to the environment. Likewise, many newly emerging economies such as China, Brazil, Indonesia, Thailand, and India have—until recently—largely failed to take the environment into account in their drive for development. Increasing international trade and investment have also boosted demand for energy resources. International economic interdependence and integration have compelled states to redefine national security in ways that better account for the environment.

International businesses have played a major role in polluting the planet, but many are also actively trying to mitigate climate change. Until recently, most businesses viewed environmental rules and regulations as costly and inefficient. But today, large companies are regular participants in international conferences on the environment, where they offer their knowledge and expertise to policy makers and form unlikely partnerships with governments and international organizations. Many major oil corporations such as ExxonMobil, Royal Dutch Shell, UNOCAL, BP, and ConocoPhillips have claimed that protection of the environment has been one of their primary goals all along. On the other hand, natural gas companies still oppose most environmental regulations on fracking and claim that gas is a relatively clean energy source compared to oil and coal.

In the last 30 years, NGOs have played an increasing role in writing, implementing, and monitoring environmental and climate change policies. Well-known environmental NGOs include the World Wildlife Fund (WWF), Greenpeace International, the National Geographic Society, Friends of the Earth, and the Sierra Club. The Climate Action Network (CAN), a worldwide network of over 1,100 NGOs in more than 120 countries, promotes "government and individual action to limit human-induced climate change to ecologically sustainable levels."[3] NGOs also work in partnership with states, I0s, and the private sector in the Global Environmental Facility (GEF), which funds environmental projects around the world. Some NGOs focus strictly on fundraising, organizing environmental projects, or campaigning at the global, regional, and state levels. For example, Greenpeace aims to influence national and international environmental legislation.

Other major actors in energy and environmental issues are national oil companies such as Saudi Arabia's Aramco, China's China National Offshore Oil Corporation (CNOOC),

and Brazil's Petrobras, all of which are key sources of government revenue. Because energy policies play an important role in state development strategies, many Middle Eastern and African "petrostates" have used their oil revenues to pacify burgeoning populations with subsidized food, gas, and other basic necessities. In other cases, leaders use oil revenues to purchase expensive weapons, bankroll extravagant lifestyles, and reward loyal political supporters.

A cartel is a group of firms or nations that cooperate with one another to control the production level and price of a commodity that is in short supply. A prominent example of one is the Organization of Petroleum Exporting Countries (OPEC), which drove up international oil prices in the 1970s (discussed in the next section). Cartels also exist for many strategic resources such as raw materials, minerals, and food commodities.

The United Nations has been more active than any other JO in dealing with environmental problems. In 1972 it created the United Nations Environment Programme (UNEP), which was tasked with enhancing cooperation between states and creating databases for scientific assessments of the environment. As the first UN agency to be headquartered in a Third World capital (Nairobi, Kenya), UNEP has built an extensive network of organizations and has coordinated many environmental projects. In 2000, at the Millennium Summit of the 55th UN General Assembly, world leaders established a set of Millennium Development Goals, one of which was ensuring environmental sustainability.

The connection of investment and trade policies to the environment has been a topic of negotiations in the World Trade Organization (WTO). WTO agreements such as GATT allow states to implement trade-restricting policies for environmental reasons, as long as environmental rules are not imposed arbitrarily and do not serve as a form of protectionism. In some cases, developing countries have even been exempted from GATT articles and some requirements of WTO agreements in return for pursuing certain national environmental goals. The WTO Secretariat also cooperates with and exchanges information with the secretariats of Multilateral Environmental Agreements (MEAs) such as the United Nations Framework Convention on Climate Change because some MEAs have trade-related environmental obligations that potentially conflict with WTO rules. The World Bank established a Global Environment Fund (GEF) to help developing nations bring proposed projects in line with international environmental standards.

The Intergovernmental Panel on Climate Change (IPCC) was established in 1988 under the auspices of the UNEP and the World Meteorological Organization. Made up chiefly of climate scientists from all over the world, the IPCC's role is "to assess on a comprehensive, objective, open and transparent basis the scientific, technical and socio-economic information relevant to understanding the scientific basis of risk of human-induced climate change."[4] Recently, climate change deniers have attacked the IPCC for concluding on the basis of high-range carbon emission models that by the end of this century, global warming could threaten the survival of our species.

Several other agencies that play a role in environmental management include the UN's Food and Agriculture Organization (FAO), which monitors global hunger and poverty in

developing nations, and the UN Population Fund, which has supported population-control programs in countries such as South Korea, China, Sri Lanka, and Cuba.

According to economists and political scientists, international organizations help states overcome the "free-rider" problem by promoting cooperation between them and assigning costs to each. Without cooperation, individuals, companies, and states will cause harm to the environment but wait for someone else to bear the costs of mitigating the harm. As free riders, they will kick the environmental can down the road, exclaiming, "Let someone else clean up the mess!" That someone else may be another country, taxpayers, or a future generation. For example, every company or individual that uses petrochemicals gets a direct and immediate benefit, but the costs seem negligible, diffuse, and hard to measure. However, we know that cumulatively the harm to the environment affects all the inhabitants of earth and may only become apparent in years to come. Thus, international organizations are mechanisms through which all polluters can agree to share the burden for reducing environmental harms.

Another important concept that applies to the environmental movement is Garrett Hardin's famous "Tragedy of the Commons," which describes the challenges of protecting "collective goods" that are shared by everyone and owned by no one.[5] In the late 1960s, Hardin applied the concept to world hunger and overpopulation. The concept can also be applied to the problems of energy production, carbon emissions, and global climate change. The tragedy occurs when states and companies all consume resources with no regard for their sustainability, causing them to ultimately become depleted. States can prevent overconsumption of a resource by agreeing only to use a certain amount of it, or they can assign property rights over resources to private entities with the expectation that these owners will manage the resources well in order to ensure long-term profits from them. Creating a market for the right to emit carbon is one way to try to prevent the tragedy of "overuse" of the atmosphere.

Economists also use the concept of "elasticity" to explain how energy consumers respond to price changes. The demand for oil is *inelastic* or relatively unresponsive to price changes *in the short run* because oil consumption is tied to relatively large capital expenditures on things such as automobiles, factories, and heating plants. In the short run, it makes little economic sense to respond to an oil price rise by buying more fuel-efficient replacements for these things. In the long run, however, stable high oil prices provide a strong incentive for new investments that reduce or replace oil consumption, and the demand for oil becomes more *elastic* or responsive to price changes.

States have an important role to play in preventing or correcting the environmental free rider problem, the tragedy of the commons, and the low price elasticity of oil. The market alone cannot solve these problems, which is why states need to nudge or force the market in a direction that corrects for them. At the same time, states and citizens must decide how to reconcile political freedoms with economic limits. It is also important to note that *individual* states lack the ability on their own to deal with *global* environmental problems. For example, because the carbon emissions of individual states cause "externalities" (negative effects) that spread across the world, all states have to join together to share the

costs of reducing climate change. Of course, large states have to do the most, but they cannot conduct successful environmental policies in isolation from others.

ENERGY AND ENVIRONMENTAL TRAJECTORIES: A BIT OF HISTORY

Technological advancements during the eighteenth and nineteenth century European industrial revolution brought new labor-saving goods to mass markets. The scale of manufacturing changed from small shops to large factories fueled by inexpensive natural resources and raw materials, many of which were extracted from Europe's overseas colonies. Meanwhile, industrialization and heavy dependence on coal spread air, water, and soil pollution across the European continent. The development of the gas-driven engine at the end of the nineteenth century rapidly increased demand for petroleum as the main fuel source in land transportation. Energy resources remained plentiful and relatively inexpensive.

Through the end of World War II, the United States was the world's largest producer of oil and was able to meet all of its oil needs domestically. Nevertheless, U.S. oil companies, like their counterparts in Europe, expanded oil production in the Middle East, Mexico, and South America. Although coal was more readily available, oil was more efficient and cheaper to produce and transport. After World War II, access to oil and coal played a strategic role in the recovery of industries in Europe, the Soviet Union, and Japan.

Historically, production, processing, marketing, and pricing of oil were dominated by the so-called "Seven Sisters"—American, British, and Anglo-Dutch multinational oil corporations (five of which were American).[6] Host nations were exploited by these oil companies, so in 1960 major oil exporters—most in the Middle East—formed the OPEC cartel to gain more control over the hydrocarbons located under their territory.[7] In 1969 Libya pressured Occidental Petroleum, a small U.S. company dependent on Libyan supplies, into granting it new price concessions. This precedent inspired other host countries to elicit bigger concessions out of the oil companies.

In Box 16.1 we provide a chronology of important energy and environment events and agreements after 1970 that we will discuss in the next sections of the chapter.

CHRONOLOGY OF SIGNIFICANT ENERGY AND ENVIRONMENT EVENTS AND AGREEMENTS

1972	The UN hosts the Conference on the Human Environment in Stockholm, Sweden. The conference announces an Action Plan for the Human Environment. The United Nations Environmental Program (UNE P) is created to help developing countries deal with environmental issues. The Club of Rome issues its *Limits to Growth* report.
1973	OPEC raises the price of oil, generating concerns about energy scarcity and spurring oil importers to adopt energy conservation policies and develop new energy sources.
1980	U.S. president Jimmy Carter commissions *The Global 2000 Report to the President*, which predicts continued population growth, depletion of natural resources, deforestation, air and water pollution, and extinction of some species.
1987	The Brundtland Report links development to environmental damage. The UN-sponsored Montreal Protocol to control *chlorofluorocarbons* that damage the earth's ozone layer goes into effect.
1992	The Earth Summit meets in Rio de Janeiro to focus on "sustainable development."
1997	The Kyoto Protocol is negotiated at the third Conference of the Parties (COP) of the UNFCCC.
2009	The UN FCCC's 15th COP meeting in Copenhagen produces a weak accord.
2011	The United Nations Climate Change Conference in Durban, South Africa ends with an agreement to start negotiations for a new legally binding climate treaty to be decided by 2015.
2012	The 18th COP meeting in Doha, Qatar ends with no significant agreement on climate change.
2015	The Paris Accord is signed in Paris, marking a major breakthrough in global efforts to reduce carbon emissions.
2017	U.S. president Donald Trump withdraws the United States from the Paris climate accord.

The OPEC Oil Crisis and the Energy Paradigm Shift

The year 1973 was a turning point for energy markets in the international political economy. A number of Arab states within OPEC imposed an oil embargo on the United States and the Netherlands for supporting Israel in the October 1973 war. Almost

overnight, OPEC used the "oil weapon" to increase the price of a barrel of oil in the international marketplace from $2.90 to $11.65 (a jump of over 400 percent), causing a recession in the Western industrialized nations that severely disrupted people's lives. The OPEC oil price hikes of 1973–1974 and 1979–1980 were like earthquakes—short, sharp jolts that shook many nation-states and international institutions, changing the global landscape for years to come. Many non-oil-exporting developing nations also faced dramatic increases in their oil import bills. Most of the major oil companies went along with the price hikes because they could easily pass the cost on to consumers. Collectively, OPEC members agreed to bring output lower than the amount that would be produced under competitive market conditions. By the mid-1970s, OPEC controlled oil prices, production levels, and royalty taxes as the developed world's reliance on petroleum imports increased.

The first Great Recession in 1973–1975 lowered demand for oil in industrialized countries as it hurt their economies. OPEC was also relatively vulnerable in that it did not want to enervate the developed countries so much that they would permanently limit their imports of oil. Also, as we note in Chapter 8, many of the U.S. dollars that went into OPEC countries' treasuries flooded back out to Western banks, which in turn loaned money to oil corporations and states investing in new fossil fuel production in Mexico, Angola, and the North Sea, all of which competed with OPEC oil. By driving a transformation in the global role and reach of Western banks, this "petrodollar recycling" helped create conditions for later instability in global financial markets.

These changes in oil markets caused a paradigm shift in the way state officials and consumers understood international energy issues. First, because many nations had become dependent upon Middle Eastern oil supplies, OPEC had a strategic weapon it could wield to not only enhance the wealth of its members but also achieve a variety of geopolitical goals. After the first oil shock, the United States more strongly supported Saudi Arabia's regional political preferences and relied on the Saudis to moderate the oil price demands of more radical OPEC members.

Second, until the 1970s, supplies of oil and other fossil fuels were assumed to be unlimited. The oil crisis brought about a realization that the earth's resources are finite. This popularized the argument that industrialization is exhausting the earth's resources and ruining the planet's air, land, and water ecosystems. In its 1972 *Limits to Growth* report, the Club of Rome speculated that the world would run out of oil in 28 years.[8] That same year the UN hosted a Conference on the Human Environment in Stockholm, Sweden, which produced an Action Plan on the Human Environment and spurred the creation of the UN Environment Programme to help developing countries deal with environmental issues.

Carter and Energy Independence

Instead of using force to counter OPEC's influence, the Carter administration adopted a series of measures to confront and adjust to the higher costs of energy. Labeling these conservation efforts "the moral equivalent of war," Carter joined other world leaders in calling for "energy independence." With Carter's backing, the U.S. Congress aimed to

reduce national energy consumption by lowering the highway speed limit to 55 miles per hour and offering tax incentives to homeowners who insulated their houses. The United States also created a Strategic Petroleum Reserve with enough inventory to temporarily meet national energy needs in the event of another crisis that cut off oil imports.

Carter was the first U.S. president to raise concerns about consumption habits and how they contributed to inefficient use of energy resources. He commissioned *The Global 2000 Report to the President*, which predicted continued population growth, depletion of natural resources, deforestation, air and water pollution, and extinction of some species.[9] Even though some critics dismissed Carter's concerns, energy sustainability and efficiency began to play bigger roles in comprehensive energy planning that included development of renewable energy resources. During his presidency, many college instructors required students to read E. F. Schumacher's book *Small Is Beautiful: Economics as If People Mattered*, which argued that modern economies running on cheap energy were unsustainable and that smaller, more appropriate technologies would help confront energy scarcity.[10]

In 1979, near the end of Carter's term, Iranian fundamentalists toppled the U.S.-backed Shah of Iran and took 52 U.S. embassy officials hostage, generating a second panic in world oil markets. The president's inability to rescue them, along with continued U.S. dependence on imported oil from the Middle East, made the president look weak. Many realists criticized Carter for "kowtowing" to OPEC and for weakening U.S. geopolitical interests in the Middle East and elsewhere.

The onset of the Iran—Iraq War in 1980 again destabilized oil markets and led to a 10 percent decrease in international production, pushing up the price of a barrel of crude to $42. In less than a decade, the oil-dependent economies of the world saw their import bills for petroleum climb by almost 1,200 percent. Major oil companies actually benefited from the Second Oil Shock because their long-term contracts gave them a supply of oil at a relatively cheap and stable price, which in turn they could sell at higher "spot market" prices. Likewise, non-OPEC oil producers could also put as much oil into the market as they wanted and receive a good price for it, which led some OPEC members to break their long-term contracts in order to sell their oil on the more lucrative spot market. The temptation of all oil exporters to expand output to raise more revenue weakened the OPEC cartel, and by 1982 a glut of oil on the market had driven down the price.

In sum, OPEC actions in the 1970s demonstrated how much economic and political power a small group of nations could have when they were able to exercise control over a critical scarce resource. Even though dependence on oil increased dramatically early on, OPEC's influence was ultimately limited due to the challenges of maintaining a cartel. Had Saudi Arabia not been a strategic partner of the United States that often kept the oil flowing, industrialized nations might have faced much worse energy market conditions. The increasingly complex interdependence among nation-states and markets was also making it difficult for any nation (even powerful Saudi Arabia) to completely control world oil prices.

The 1980s and 1990s: The Iran–Iraq and Persian Gulf Wars

Dependency and vulnerability would continue to shape global energy policies in the 1980s. A more chaotic oil regime and falling oil prices would also point to OPEC's declining influence. International oil production was partially disrupted by the Iran–Iraq War (1980–1988) and the Persian Gulf War (1990–1991), both of which caused divisions within OPEC.

While President Reagan was in office, OPEC gradually lost control over international oil prices. With more oil coming on line in 1983, OPEC reduced the price of its "benchmark crude" for the first time in the organization's history. Fed up with other OPEC members that were producing over their quotas, Saudi Arabia flooded oil markets beginning in 1985 and drove crude oil prices down to $10 a barrel. Low oil prices throughout the rest of the 1980s punished highly indebted oil producers such as Nigeria, Algeria, Mexico, and Venezuela. By the end of the Iran–Iraq War in 1988, oil prices were actually below their 1974 level (when adjusted for inflation). This was a boon to oil consumers. Some argue the drop in oil prices did more to turn around the U.S. economy during the first Reagan administration than the president's free-market policies.

Low, stable oil prices helped many oil-importing emerging countries—especially the Asian Tigers and China—industrialize and grow. Yet weaker prices also softened the demand for alternative energies like nuclear, solar, and wind. At the time, energy and environmental trajectories were intersecting more than ever before, helping support the idea of a transition to renewable energy resources. In 1987 the UN-sponsored World Commission on Environment and Development released the "Brundtland Report," which linked sustainable growth and development to environmental protection, greater energy efficiency, and conservation of natural resources.[11] Opinion polls indicated that a majority of people in the developed nations supported raising taxes to deal with some of the environmental side effects of oil-fueled industrialization.

In 1990 it was "déjà vu all over again" when oil prices shot up due to military conflict between Iraq and Kuwait. Oil was both a source of discord and a tool used to fight the war. Iraqi president Saddam Hussein had accused Kuwait of cheating on OPEC oil production quotas and taking more than its share of oil from the neutral zone between the two countries, both actions that he claimed had deprived the Iraqi state treasury of billions of dollars of oil revenues. He justified his invasion of Kuwait in part over these actions. In early 1991, the United States led a UN-sanctioned military coalition in Operation Desert Storm to liberate Kuwait.[12]

The impact of the Gulf War on oil prices was short-lived. Shortly after the war, oil prices dropped back to their previous low levels. Saudi Arabia remained the linchpin in OPEC and a primary security interest of the United States. However, the Gulf War further reduced OPEC solidarity by driving a wedge between Saudi Arabia and Iraq. In turn, many oil companies invested heavily in the development of new oil reserves in non-OPEC nations, which increased oil supplies and further undermined OPEC's price-setting ability.

Rio: The Fork in the Road

In 1992 the UN Conference on the Environment and Development convened in Rio de Janeiro. This so-called "Earth Summit" was a game-changer to the extent that it officially focused on "sustainable development," i.e., ways to generate wealth and development while preserving the environment. Among those present were representatives of 172 states, 108 heads of state, and some 2,400 representatives of environmental NGOs. After hard negotiations, the Earth Summit issued declarations of principles and action plans related to sustainable development. Equally important, during the Summit two treaties were opened for ratification, and 153 states signed them_ the Convention on Biological Diversity and the UN Framework Convention on Climate Change (UNFCCC), which later became the basis of the Kyoto Protocol.

Rio was the first major environmental meeting to gain wide international press coverage, thereby raising awareness of global environmental issues. In some respects, however, Rio was a failure. In the assessment of Geoffrey Palmer, a former Prime Minister and Minister of the Environment in New Zealand, the UNFCCC had "no agreement on targets for reduction of emissions of greenhouse gas," and Rio's "sustainability paradigm" was "not embraced with sufficient determination, rigor or commitment to ensure that it happens."[13] Before the meeting, the United States had let it be known that it did not want to play a major role in managing the planet's environmental and ecological systems. Officials in the George W. Bush administration argued that compulsory cuts in emissions based on fixed timetables would threaten economic growth. They also asserted that technology and free markets could mitigate environmental problems better than coordinated efforts by nation-states. Other U.S. critics claimed that many of the international proposals to protect the environment were too costly and unfairly penalized American businesses. The Clinton administration (1993–2001) changed direction and tried to make the United States a major player in international negotiations over global environmental rules. To signal his commitment to international norms, Clinton signed the Law of the Sea Treaty in 1994 (although the U.S. Senate never ratified it).

During the 1990s, oil remained the world's biggest source of energy, even though it dropped from 45 percent of the world's total energy consumption in 1973 to 35 percent in 1996. Over the decade oil prices remained relatively low—roughly $10 a barrel less than they were in the 1980s—despite some price spikes in short periods of time. Starving for revenues, OPEC nations faced tough domestic economic conditions. With globalization in full swing, the Clinton administration promoted *deregulation* and trade liberalization, which helped boost economic growth in the United States and the rest of the world. Many U.S. companies and consumers benefited significantly from low oil prices, but U.S. imports of crude oil grew by more than 50 percent from 1990 to 2000. Despite the persistence of relatively low, stable prices, environmental awareness and interest in non-carbon sources of energy was growing.

Kyoto: Hitting the Wall

In 1997 the Conference of Parties of the UNFCCC took a major step forward in dealing with climate change by adopting the Kyoto Protocol, which required industrialized countries to reduce their greenhouse gas emissions by more than a third by 2012, or 5.2 percent below the 1990 level of emissions. Kyoto also introduced three major "mechanisms" to help countries meet their obligations in the Protocol: emissions trading (also known as cap-and-trade); emissions reduction through increased use of carbon sinks; and emissions credits for investing in "green" projects in developing countries. These mechanisms satisfied those who preferred mar-ket-based solutions to environmental issues.

Critics of the Kyoto Protocol questioned the practicality of emission limits and the usefulness of a cap-and-trade system. A key weakness in the agreement was that developing coun-tries—including Brazil, India, and China—were not bound to any emissions limits, even though their emissions were rapidly growing due to high economic growth rates. The issue of how much developing countries needed to cut emissions was deferred to future meetings of the UNFCCC Conference of Parties, and these countries were encouraged to set reduction targets. However, by 2016, China was the largest carbon emitter in the world, followed by the United States and India. President Clinton never sought Senate ratification of the Kyoto agreement as the Republican Chairman of the Senate Energy Committee had declared—probably accurately—that it would be "dead on arrival."[14]

In the years following Kyoto, the idea of sustainable development continued to catch on amongst many policy makers and NGOs that dealt with the interrelated issues of development, food, energy, and the environment. By the mid-2000s, many cities in the United States were adopting measures to mitigate climate change and protect the environment on their own.[15] By the early 2010s, there were a number of protests in China against big government projects with the goal of pressuring national and regional leaders to give local groups a bigger role in shaping policies on land use and pollution reduction.[16] Despite broad agreement about the worthiness of sustainable development, actually achieving it was another matter.

STUCK IN TRANSITION IN THE 2000S: THE ENERGY BOOM, VOLATILE MARKETS, AND DISPUTED FACTS

After the turn of the twenty-first century, the dramatic growth in world consumption—driven largely by China, India, and Brazil—increased demand for energy and contributed to a steady rise in oil prices. At the same time, these trends raised prospects that energy markets would be solid investment opportunities. From 2001 to 2011, China's oil consumption alone doubled from 4.9 to 9.8 million barrels a day. Likewise, China's economic success provided it with the means to invest in oil projects in other countries and develop alternative energy resources at home. Despite this backdrop of slowly improving chances for renewable energy, there was still little progress in meeting the key goals set out in the Kyoto agreement.

Nevertheless, the effects of greenhouse gas emissions were gradually becoming a key frame in international debate on the environment. For decades, scientists had been researching how carbon dioxide, nitrous oxide, methane, CFCs, and ozone trapped heat in the earth's atmosphere. The vast majority of scientists believed that *human* sources of greenhouse gases, such as deforestation and carbon dioxide produced by the burning of fossil fuels (coal, oil, and natural gas), were the main causes of global warming. Moreover, national leaders and officials at the World Health Organization recognized that terrible air pollution from coal-burning plants and other sources in China, India, and other developing countries was causing major health problems and cutting life expectancy.

In 2006, Lord Nicolas Stern, a former World Bank chief economist and the Chairman of the Grantham Research Institute on Climate Change and the Environment at the London School of Economics, issued a 700-word report on the economics of climate change that got a lot of press attention.[17] He concluded that, in the near future:

- All countries would be affected by climate change, and the poorest ones would suffer earliest and most;
- Warming of 3 or 4 degrees Celsius by the middle of the century would cause rising sea levels, heavier floods, and drought that could permanently displace 200 million people;
- Warming of 2 degrees Celsius could leave 15–40 percent of species facing extinction; and
- Deforestation would be responsible for more emissions than the transport sector.

The report also predicted that global warming could cost the world 5–20 percent of its economic output "forever," but that trying to forestall the crisis would cost only 1 percent of the world's GDP. Stern stated that an effective response required carbon pricing, a technology policy, and energy efficiency. Finally, Stern insisted that rich countries should honor pledges to increase overseas development assistance.

Former U.S. vice-president Al Gore became one of the biggest names in the global warming debate. He made it a personal goal to raise public awareness of environmental

problems. In 2006, he wrote and starred in a documentary that outlined evidence of global warming and warned of its potential catastrophic risks. *An Inconvenient Truth* went on to win an Academy Award, and in 2007 Gore shared a Nobel Peace Prize with the IPCC; he helped produce a sequel in 2017.[18]

Oil and Intervention: Iraq and Afghanistan

When the George W. Bush administration took office in 2001, it officially withdrew U.S. support for the Kyoto Protocol. Ten years later, Canada withdrew from Kyoto, and other big polluters refused to cap carbon emissions. Even so, support for the shift to "green energy" was advancing in many countries, albeit much more modestly than some state officials and environmental groups had hoped for.

After the terrorist attacks of September 11, 2001, there were fears that oil production in the Middle East would decrease because of the invasions of Afghanistan and then Iraq. The price of oil climbed steadily after the start of the Iraq war in 2003. Saudi Arabia periodically stepped in to increase production so as to stabilize the oil market. Higher oil prices were largely driven by increased demand in the emerging economies such as China, India, and Brazil, which incentivized the United States, Canada, and Russia to produce more of their own fossil fuels and to develop new oil fields.

Many structuralists and some realists criticized the United States for pursuing wars in Afghanistan and Iraq in order to promote U.S. oil interests.[19] "No blood for oil!" was the chant at many anti-war demonstrations in 2003. The press made much of the fact that when U.S. troops arrived in Baghdad they protected Iraq's oil ministry while its national museum was looted. Some critics argued that the United States wanted to establish a "heavy footprint" in the region in order to influence developments in the Caspian region, where new oil fields were being developed and where pipelines connecting Central Asia to Europe originated. Michael Klare made the case that this required the establishment of more U.S. military bases in the region. Given Saudi Arabia's refusal to allow U.S. bases on its soil, the United States resorted to positioning bases in Kyrgyzstan, Uzbekistan, Afghanistan, Iraq, and Pakistan, alongside those already in Kuwait, Oman, Bahrain, Qatar, and Turkey.[20]

Notably, between 2004 and 2007, global investments in renewable energy more than quadrupled, with solar, wind, and biofuels receiving 82 percent of this money.[21] Emerging economies such as China, India, Pakistan, and the Philippines set up national programs to promote renewable energy to meet the demands of their growing populations and larger middle classes. As its solar and wind energy industries blossomed, China exported cheap solar panels and wind turbines that were very competitive in global markets. Even the oil-producing countries on the Arabian Peninsula became hot spots for green technology deployment as they hoped to preserve their role as leading energy exporters.[22]

As late as 2008, many were concerned that a tipping point would soon be reached whereby oil supplies would begin declining, driving up oil prices even further. Geophysicist M. King Hubbert, working at the Shell Oil Company in the 1950s, first proposed the

controversial idea known as "peak oil" that the world would run out of oil at some point. He predicted a peak in U.S. oil production between 1965 and 1970. After 1970, U.S. oil production did decline until a small uptick occurred when oil was discovered in Alaska. Peak oil advocates believe that oil production *may* have already passed its peak in countries such as Argentina, Australia, Colombia, Cuba, Egypt, Iran, Libya, Russia, South Africa, and Yemen. However, the global financial crisis of 2008 weakened support for the peak oil argument. Scientific advances made it easier and cheaper to prospect for new oil reserves, and new drilling technologies reduced costs of oil and natural gas production.

2008: The Financial Crisis and the Energy Boom

Between 2002 and July of 2008, oil prices rose steadily until they suddenly spiked at $147 per barrel—nearly six times what they had been at the beginning of the Iraq war. The rise of gasoline prices to more than $4 a gallon in the United States ate up more of consumers' discretionary income. U.S. automakers GM and Chrysler filed for bankruptcy when fewer Americans purchased new vehicles. Airlines also suffered from rapidly rising fuel prices. The cost of transporting goods translated into higher prices for many agricultural commodities and higher food costs. Likewise, in many poorer countries, imported food staples doubled in price, sparking civil unrest and destabilizing many already fragile governments. All of these trends worsened the effects of the global recession.

Many government officials believed that one of the ways to combat high oil prices and market instability was to ramp up the production of fossil fuels like coal, oil, and natural gas. Likewise, with real estate markets in ruin, speculative capital flowed into the oil and natural gas fields of the major producers. Oil drilling spread to new areas of the United States, Canada, Brazil, Iraq, the Arctic, and the Gulf of Mexico (when a moratorium on drilling imposed after the 2010 BP oil spill was lifted), bringing more fossil fuels onto the market.

An important new technology that helped with extraction of natural gas was "fracking," which made headlines in 2008 because its injection of chemically treated and pressurized water into the earth to break open shale rocks to release oil and natural gas allegedly caused significant environmental damage.[23] Development of huge natural gas fields in North Dakota, Texas, Pennsylvania, and New York allowed the United States to overtake Russia as the world's largest producer of natural gas. Big natural gas producers were eager to "keep drilling" and to sell to countries in Asia and Latin America in particular.

Experts claimed that fracking could:

- Create 3.6 million new jobs by 2020;
- Decrease the U.S. trade deficit 60 percent by 2020;
- Decrease the use of coal and nuclear energy;
- Benefit chemical, pharmaceutical, and fertilizer industries; and
- Help the United States achieve energy independence.

In contrast, opponents of fracking argued that its problems more than offset its advantages:

- It contaminated water in nearby local streams, ponds, and lakes;[24]
- Fracked wells leaked 40 to 60 percent more methane, a powerful greenhouse gas, than conventional wells; and
- Fossil fuel companies do not create many jobs.

All in all, during the Bush administration (2001–2009) multinational energy companies increased their influence on energy and environmental policies in the United States and elsewhere. Between the 1990 and 2010 U.S. election cycles, individuals and political action committees affiliated with oil and gas companies donated $239 million to candidates and parties—75 percent of which went to Republicans. And in just the three election cycles from 2012 to 2016, donations from similar sources totaled $168 million, more than 85 percent of which went to Republicans.[25] High-paid lobbyists for oil companies enjoyed strong influence in Washington, DC (as they do today). They criticized environmental regulations for being too costly, hampering exploration, and destroying jobs. The oil lobby also worked to repeal or weaken industry oversight by executive agencies and Congress.

The Obama Administration: Pragmatic Progress or Squandered Opportunity?

As a presidential candidate, Barack Obama campaigned on the promise to promote alternative energy and protect the environment. He stated clearly that climate change was a real threat that had to be addressed through international negotiations and cooperation. After assuming office in 2009, Obama balanced support for continued fossil fuel production with promotion of renewables. Economic conditions during the Great Recession made a major push to reduce carbon sources seem too expensive and disruptive. At the same time, he funded projects that were "shovel ready" through the American Recovery and Reinvestment Act of 2009. Out of $787 billion in the ARRA package, $90 billion was earmarked for wind, solar, biomass, and battery projects, $11 billion went to modernizing the electrical grid, $14 billion went to tax incentives for businesses investing in renewables, and $6 billion went to boost energy efficiency. The Obama administration approved more oil and gas exploration on public lands while using ARRA to spur more renewables.

This mix of policies led to changes during the Obama years in the composition of U.S. energy sources (see Figure 16.1). From 2008 to 2016, coal's share in national electricity generation dropped from 48 to 30 percent. While partisan critics alleged this was the result of a "war on coal" driven by environmental regulation, in truth the new supplies of cheap natural gas were what was driving coal out of the market.

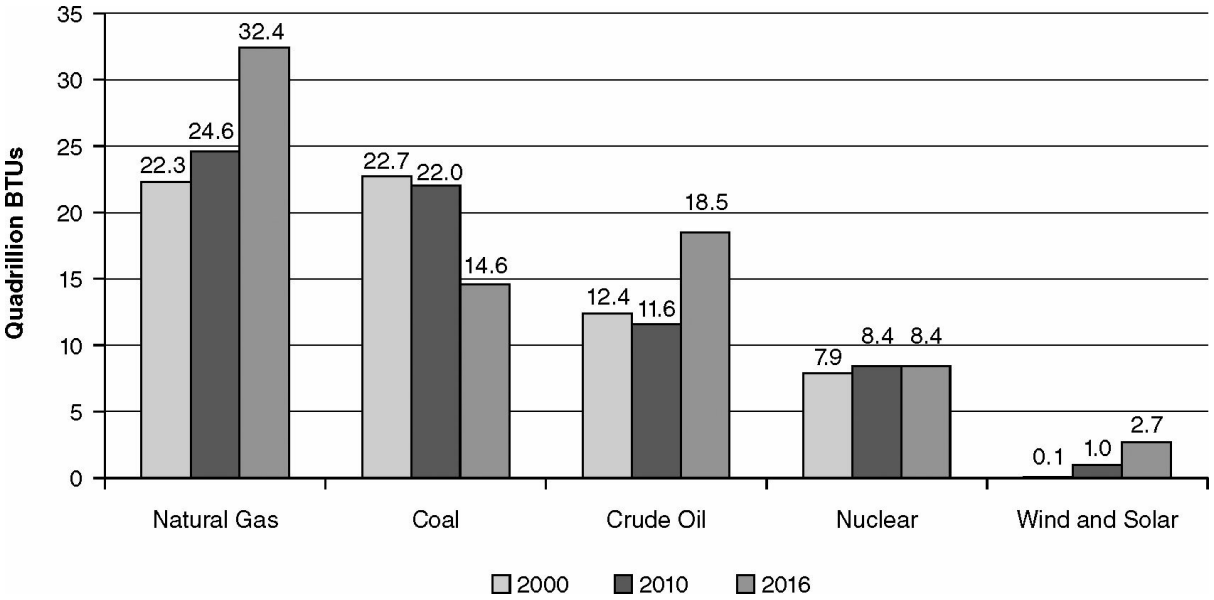


FIGURE 16.1
Selected Sources of U.S. Primary Energy Production, in Quadrillion British Thermal Units (BTUs)

Source: Data from the U.S. Energy Information Administration, at www.eia.gov/opendata/qb.php?category=711239

The Obama administration deserves some credit for the growth in renewables (not including hydropower), whose contribution to electricity generation rose from 3.8 percent in 2008 to 8.4 percent in 2016. Particularly striking was the growth in wind power's share of electricity output (from 1.3 to 5.6 percent). Overall U.S. energy production grew dramatically during the Obama years, from 73 quadrillion BTUs in 2009 to 84 quadrillion BTUs in 2016, which is ironic given that many Republicans criticized Obama for being an enemy of the fossil-fuel industry. As Figure 16.1 indicates, natural gas and oil production in the United States soared between 2010 and 2016, due in large part to the "fracking revolution" and incentives from high prices. The transportation sector's dependence on oil continued, but government tax breaks at the state and federal levels caused purchases of electric vehicles to mushroom. The total stock of electric cars in the United States rose from just 2,600 in 2009 to 564,000 in 2016.[26]

While the Obama administration accepted the science on global warming and had the best intentions to reduce U.S. carbon emissions, its policies made only small changes at the margins in carbon fuel sources. The need to support economic recovery after the Great Recession limited how aggressively renewables could be supported. Nevertheless, it is likely that investments made during the Obama years, particularly in advanced battery technology, will become essential components of a robust economy relying more heavily on electric vehicles and electricity from renewable sources.

While the U.S. was seeing coal decline as an energy source, it was still "king" in China; in 2016, China produced 45 percent of all the world's coal, followed far behind by India and the United States (see Figure 16.2). How important will coal be in the future? As late

as 2013, the U.S. Energy Information Agency projected that demand for coal would be nearly 40 percent higher by 2040; in 2017 it projected demand growth of only 1 percent. Why the drastic change? A big reason is that China and India have recently scaled back plans to build hundreds of new coal-fired power plants and are instead investing heavily in solar and wind power.

By 2016 nuclear power was producing 11 percent of the world's electricity output, slightly down from 13 percent in 2009 (see Figure 16.3 for a comparison of nuclear power generation in different countries). France derives 73 percent of its electricity from nuclear power, while the United States and the United Kingdom each derive 20 percent. Despite a desire in some countries to develop more nuclear energy, in the last decade only China and Russia have significantly expanded the amount of nuclear power that they generate. Between 2000 and 2017, China built thirty-five nuclear reactors and by late 2017 it had another nineteen under construction with plans for dozens more. Meanwhile, during the entire Obama administration the United States started building just two new reactors.

Proponents of nuclear energy point out that it is much "cleaner" than fossil fuels because it does not emit CO_2 (except for all the CO_2 emitted during the construction of nuclear facilities, the building of infrastructure to support them, and strip mining for the actual radioactive fuel). However, environmentalists point out that there are not viable means of safely disposing of highly radioactive waste. Three Mile Island, Chernobyl, and the meltdown of the four Fukushima power plants after an earthquake and tsunami in 2011 continue to scare people all over the world. When Japan took most of its nuclear reactors offline following the Fukushima disaster, its share of electricity from nuclear power fell from 30 percent to 2 percent. Germany has pledged to permanently close all its nuclear reactors by 2022. The U.S. nuclear industry remains dormant because there is little interest in funding large new plants.

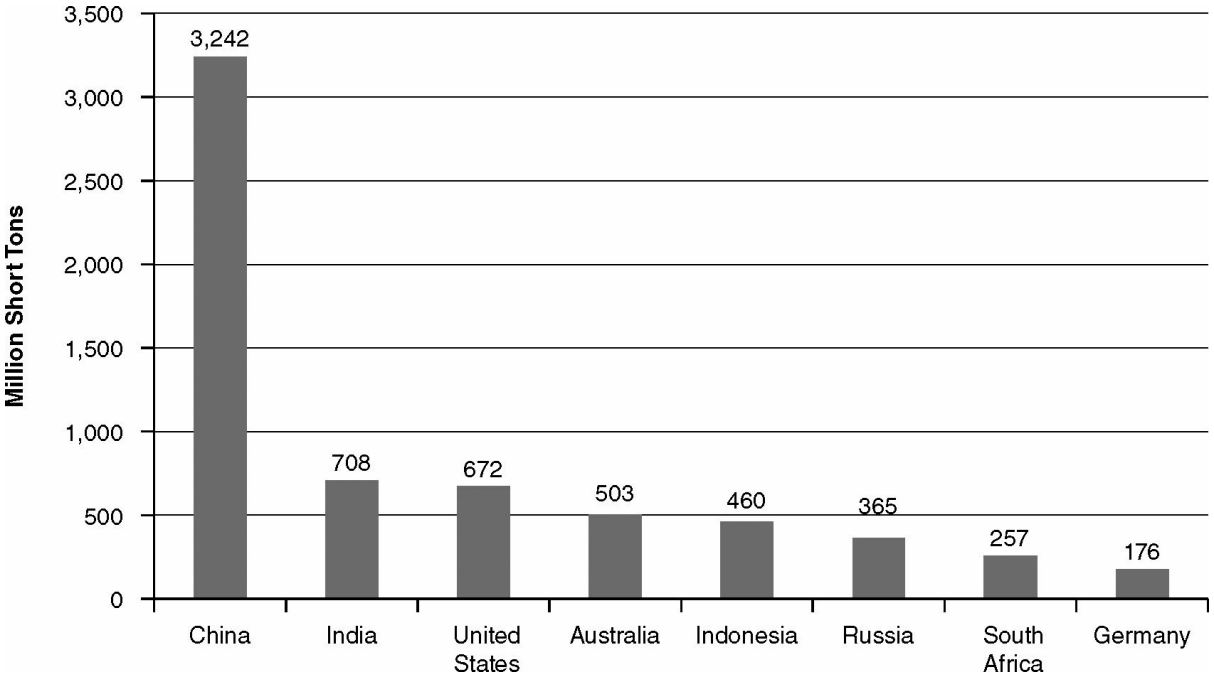


FIGURE 16.2
World's Top Eight Producers of Coal in 2016

Source: Data from International Energy Agency, "Key World Energy Statistics 2017" (2017), p. 17, at www.iea.org/-publications/freepublications/publication/KeyWorld2017.pdf.

Climate Change: Can We Save the Planet?

The Obama administration came to office determined to craft a global climate change agreement. Scientific warnings about the effects of climate change had grown direr and more certain. The first session of the UNFCCC Conference of the Parties (COP) after Obama took office was held in Copenhagen in 2009. Although Obama had hoped to hammer out a comprehensive agreement with binding limits on carbon emissions, the COP essentially ended up agreeing to continue to work towards an agreement. They did manage to "take note" of a non-binding "political accord" that Obama and several other leaders cobbled together on the sidelines of the conference. Although the voluntary accord "committed no one to anything,"[27] its main goals were these:

- Developed countries would reduce emission levels individually or jointly based on pledges made before the conference.
- Developed countries would raise $100 billion a year by 2020 to help poor countries fight climate change.
- New funds would be provided to help pay countries to preserve forests.
- The increase in global temperature should be kept below 2 degrees Celsius.[28]

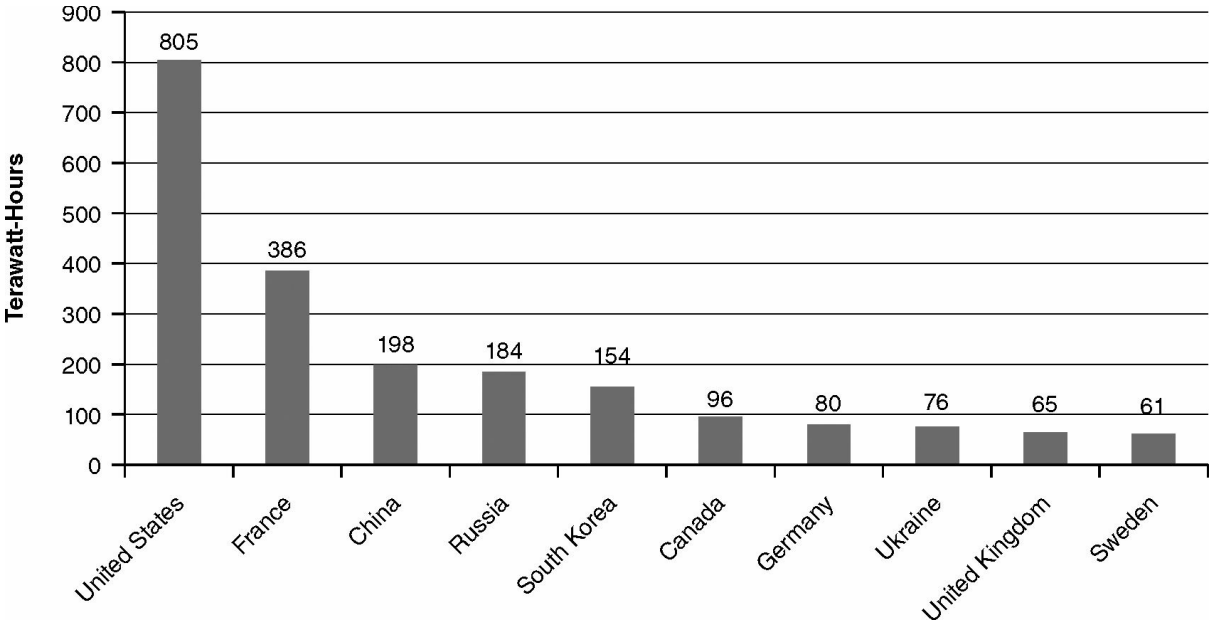


FIGURE 16.3
Nuclear Energy Generation in the World's Top Ten Producers in 2016

Source: Data from the Nuclear Energy Institute, at www.nei.org/Knowledge-Center/Nuclear-Statistics/World-Statistics.

Most criticisms of the Copenhagen accord came from EU members and poorer nations that felt left out of the negotiations. Many island nations felt the 2-degree Celsius target was too high and that, even if it were achieved, they would soon be inundated by rising seas. Realistically, the cuts in carbon emissions that countries offered at Copenhagen were not sufficient to hold back serious climate change.

Subsequent annual COP sessions in Durban in 2011 and Doha in 2012 failed to produce significant progress towards binding emissions limits or establishing a Green Climate Fund to support mitigation policies in developing countries. Developed countries argued that *all* countries needed to cooperate and sacrifice to stop global warming, while developing countries insisted that, because industrialized countries had been by far the world's main carbon emitters for decades, they should bear the costs of moving away from carbon fuels. China and India in particular resisted any limits on their emissions or choice of energy sources that would limit their economic growth.

This logjam finally broke at the 2015 COP in Paris, where 195 nations agreed to the goals of holding global temperature rise to "well below 2 degrees Celsius above pre-industrial levels" and cutting net greenhouse gas emissions to zero in the second half of this century. States specifically agreed to:

- Put forward their best efforts to reduce carbon emission through "nationally determined contributions" (NDCs) and to strengthen these efforts in the years ahead;
- Report regularly on their emissions and on their implementation efforts;
- Give an accounting every five years to assess the collective progress made by member

states; and
- Help poor countries adjust to the agreement and move toward renewable resources.

The nonbinding Paris Agreement pushed many countries to enact new clean-energy laws. The Obama administration negotiated hard in Paris for strong transparency and accountability measures to ensure that China and India follow through on their commitments. Among other things, China pledged to reach the peak of its emissions no later than 2030 and get 20 percent of its overall energy from renewable sources by then. India pledged to generate 40 percent of its electricity from renewables by 2030 and lower its "emissions intensity" (amount of emissions per unit of GDP) to well below its 2005 level. The United States set a target of reducing its greenhouse gas emissions to 26–28 percent below its 2005 levels by 2025. Many business interests supported the Paris Agreement because they more fully appreciated how much their financial success depends on environmental stability.

Consensus in Paris was possible because the agreement let each country set its own goals, so long as they put the world on a path to cutting emissions. While non-binding agreements are generally not strong, the transparency initiative, combined with changed attitudes about the effects of warming, made Paris a success.

The Paris Agreement officially came into force in 2016, and by the end of 2017 197 nations had formally ratified it. Paris gave climate scientists hope that the world would act collectively to avoid the worst dangers of warming, which could include the destruction of humanity itself. Obama described it as "an enduring global agreement that reduces carbon pollution and sets the world on course to a low-carbon future." Critics were not as enthusiastic. James Hansen, a leading climate scientist in the United States, dismissed the accord as "a fraud really, a fake…. It's just worthless words."[29] In a 2016 analysis, a group of scientists concluded that, taken together, the country targets were simply inadequate to limit warming to below 2 degrees Celsius.[30]

Climate Change Skeptics and Deniers

Even as the Obama Administration tried to forge climate agreements and change the U.S. energy mix, some in the United States raised doubts about the science regarding global climate change. Despite an overwhelming agreement among scientists across the planet, from a wide range of disciplines, about the causes and likely effects of climate change, some prominent skeptics question whether rising carbon levels are due to human causes and whether the rise in temperatures is a permanent long-term trend or just a normal, relatively short-term fluctuation when seen in historical perspective. Some go so far as to allege that an international cabal of scientists has tricked the world into believing that climate change is real and conspires to keep critics from being published in peer-reviewed scientific journals. Those skeptics who concede that the science is robust emphasize that, due to the high cost of reducing carbon gas emissions, the world would be better off investing in other challenges such as combating poverty than worrying about climate change.[31]

Climate scientists have repeatedly pulled apart the skeptics' claims. In 2011, an

independent group led by Berkeley scientist Richard Muller, funded in large part by oil billionaires, concluded that climate change is real and that the temperature records are reliable.[32] This has not stopped the same claims being made by the same handful of people for more than a decade.

It is no coincidence that much of the funding for the skeptics and the think tanks that house them comes from fossil-fuels corporations. For example, the conservative think tank The Heartland Institute, which is funded by wealthy climate change skeptics and major oil companies, spreads the message in K-12 schools that "the topic of climate change is controversial and uncertain," dissuading some teachers from imparting widely accepted scientific findings.[33] Other climate-change questioning think tanks such as the Competitive Enterprise Institute, the Annapolis Center, the Cato Institute, and the Heritage Foundation get funding from similar sources.[34]

The fossil-fuel industry's aid to skeptics and campaign financing for Republicans lawmakers, who held the majority of House seats for the last six years of Obama's presidency, (and the majority of Senate seats for the last two years) weakened initiatives on climate and energy. House and Senate Republicans attacked the Obama administration's efforts to boost renewa-bles and enter into global climate agreements. Senate Republicans would not ratify any of the international agreements negotiated by the Obama administration, and Republican majorities in Congress blocked climate change legislation. Any evaluation of the accomplishments of the Obama years must take account of the political effectiveness of the fossil-fuel industry's campaign to cast doubt on the science of climate change.

POPULISM AND DISCORD UNDER TRUMP

During the 2016 U.S. presidential campaign, candidate Donald Trump stated many times that he intended to withdraw the United States from the Paris Agreement, dismantle the Environmental Protection Agency (EPA), and reverse Obama-era restrictions on fossil-fuel production. As a candidate and later as president, Trump justified his positions by stating:

1. To "Make American Great Again," the United States needed to act tough and "win" negotiations both at home and on the global stage.
2. India and China have been unfairly taking advantage of other states because they have never been required to actually reduce the level of their carbon emissions.
3. The coal industry needs to be revived, in part to create more jobs.
4. Compliance with the Paris Agreement would hurt the U.S. economy.

After facing withering criticism in the first few months of his presidency, Trump was eager to demonstrate his authority and score a "win" in foreign policy, even in the face of public opinion polls in the United States and Europe that showed strong support for the Paris Agreement. Perhaps Trump also relished the idea that pulling out of the Paris Agreement would give EU officials, political elites, and "globalists" a "poke in the eye" for thinking that he was not smart or for treating him "unfairly."

Some neoliberals, such as George Schultz, a former Secretary of State under President Reagan, argue that leaving the Paris Agreement will cost the United States new investments and jobs in the renewable energy sector, weaken U.S. competitiveness, and increase future business risks.[35] From a realist perspective, the distinguished energy expert Michael T. Klare has challenged Trump's claim that the Paris Agreement is unfair to the United States; in reality, he says, it is the United States that has been imposing a burden on the rest of the world.[36] Similarly, heterodox liberal economist Joseph Stiglitz points out that the United States is the second biggest emitter of carbon dioxide in the world, and with the largest GDP in the world it can cope with climate change much more easily than developing countries.[37] Trump's decision to abandon the Paris Agreement may also push India, China, and other states to shirk their obligations under it, thus potentially wiping out recent progress toward stopping the atmosphere from warming over 2 degrees Celsius—the maximum level of warming scientists believe the planet can absorb without catastrophic consequences.

Nevertheless, the damage that Trump might do in the near future may be limited by the fact that:

1. Under terms of the Paris Agreement, the United States cannot officially withdraw from it until November 2020 (three years after announcing its intention to withdraw).
2. Almost all of the other members are currently committed to staying the course.
3. Other countries can impose carbon tariffs on the United States.[38]

"It's Gonna Be Beautiful: I Promise!"

To help coal producers in states like Pennsylvania and Ohio that he won in the 2016 election, Trump has moved to revive the coal industry, raise oil and natural gas output, and "bring back so many energy jobs." Klare maintains that Trump's underlying goal is to achieve U.S. energy independence so that an oil cartel or hostile oil exporter cannot hold the United States hostage in a crisis. In pursuit of this goal (and to reward business interests that support the Republican party) Trump has introduced measures to expand offshore drilling in the Arctic and Atlantic Oceans, open up more shale energy deposits for fracking, and grant coal companies new leases to mine on federal lands.[39]

Klare faults Trump for equating "mastery over oil in particular, and fossil fuels in general, with mastery of the world,"[40] Contradicting Trump's efforts to revive coal, many utility companies have been modifying their coal-fired plants to run on natural gas. The overproduction of oil and natural gas may also drive down their prices, causing worker layoffs and reducing state and local tax revenues. Ironically, surpluses have also motivated some major oil producers such as Saudi Arabia and the United Arab Emirates to invest more in renewable energy projects.

U.S. oil producers were exporting record amounts of oil by 2017, particularly to Canada, while Saudi Arabia focused on increasing sales to China, Japan, and other Asian countries. Liquefied natural gas (LNG) exports reached record highs in 2017, as Qatar, Australia, and the United States continued to ramp up production to meet growing Asian demand. At the same time, OPEC and Russia agreed to reduce their overall oil exports in 2017 and 2018 to help reduce the glut in the market and raise oil prices. Many producers and government officials also worry that the global market for fossil fuels is becoming glutted and that the demand for electric cars and solar power in particular could soon weaken the demand for oil and natural gas.[41]

Despite the Trump administration's withdrawal from the Paris Agreement and support for fossil fuels, corporations and most nations are forging ahead with efforts to limit carbon emissions. Nearly half of the Fortune 500 companies have set targets to reduce their emissions, while two dozen companies—including Google, Wal-Mart, and Bank of America—are seeking to power their companies with 100 percent renewable energy.[42] Germany, Royal Dutch Shell, Daimler, and An Liquide have together invested €1.4 billion in hydrogen cars. The CEO of Volvo, Hakan Samuelsson, announced that all new Volvo cars will be either hybrid or battery-powered by 2019. He also noted that "a much bigger risk would be to stick with internal combustion engines."[43] In 2017 the French government announced a plan to ban sales of all gas- and diesel-powered vehicles by 2040, and other European countries and China are planning for a similar target.[44] As Chinese companies ramp up their involvement in Africa, they are helping the continent expand use of renewable energy, especially hydropower (see Box 16.2).

Big investors and money managers on Wall Street are increasingly demanding more "socially responsible" investment portfolios that exclude or reduce holdings of stocks in corporations whose products and commodities release high amounts of carbon into the

atmosphere.[45] The movement that began on college campuses in 2011 to pressure institutions to divest their holdings of stocks in fossil fuel companies has spread to the business world. This trend is partially due to speculation that fossil fuel stocks are a losing bet in the long run. According to DivestInvest, a global organization that tracks investor efforts to promote a decarbonized global economy, by the end of 2017 nearly 780 institutions and 60,000 individuals with combined assets worth $5.6 trillion had committed to divesting from oil, gas, and coal.[46] Some of the largest pension funds in the United States, including the New York State and California State Teachers' retirement systems, have begun divesting.[47] Mindy Lubber, president of the environmental nonprofit Ceres, is optimistic about the future of green energy: "Investors are showing that they care. Consumers are voting with their pocketbooks. Companies are invested in this, and they're not moving backward."[48]

Since 2004, new investments have been pouring into renewables, indicating that a global energy transition is well under way (even though fossil fuels are clearly still dominant). In the face of severe pollution and growing energy needs, China has begun shifting major investments into wind, solar, and nuclear power. The Chinese Communist Party has embraced the goal of a much greener energy sector, not least because it wants China to be a leader in new energy technologies that spread in global markets. China's push into renewables depends on massive state investments and subsidies, which leads neoliberals and realists in other countries to complain that Chinese companies have an unfair advantage in exports of solar equipment, wind turbines, and other renewable energy products. Figure 16.4 shows four global regions where investments in renewable energy have been the largest. Although the United States and Europe soared earliest, China and other Asia-Pacific countries are on track to overtake these regions, especially as investments in Europe and the United States have slowed since 2011. Although Asia is the dynamic center of renewables, Latin America, India, and the Middle East have also been ramping up solar, wind, and biomass investments.

Blowing Up the EPA

Trump's decision to pull out of the Paris Agreement is in keeping with his efforts to defund and shrink the size of the U.S. Environmental Protection Agency (EPA) while also ridding it of Obama-era regulations and directives. Secretary of the EPA Scott Pruitt has moved to overturn the EPA's clean power plan to reduce greenhouse gas emissions from coal-fired plants and eliminate mandates on automobile manufacturers to achieve average fuel-efficiency standards of 54.5 mpg in all new cars by 2025. He has proposed to relax many regulations, including those on chemical emissions from industrial sites. As he snubbed many career EPA officials, Pruitt worked closely with President Trump in 2017 to propose cutting the agency's budget by 31 percent, making it the smallest since the agency was created in 1970.

ENERGY IN AFRICA, AND CHINA'S INVOLVEMENT

On the African continent, hydroelectricity is a promising source of renewable energy that could help the African Union achieve its Agenda 2063 development goals. Only 10 percent of Africa's potential hydropower capacity had been exploited, despite the fact that more than 600 million Africans live without electricity.[a] Policy makers from the African Union are paying particular attention to the Democratic Republic of the Congo's Grand Inga hydroelectric project on the Congo River, which, if successfully completed, could supply up to 40 percent of sub-Saharan Africa's electricity. However, like many hydroelectric projects, Grand Inga is extremely costly to build, and large-scale financing can only come from multilateral development banks. In 2016, the World Bank suspended its funding to the project. NGOs such as International Rivers oppose many large, new hydroelectric dams because they cause extensive environmental damage, flood large areas, displace communities, and reduce downstream water sources for agriculture.

Solar power currently plays a limited role in African development, but it is gaining attention because the continent has 320 days of bright sunlight per year and twice the level of solar irradiance as Germany. With backing from Chinese corporations, companies like Akon Lighting Africa are financing the installation of Chinese-built solar panels in small-scale power projects to bring electricity to African homes and communities.[b] One of solar power's main drawbacks for now is that its average cost of generating electricity exceeds the average cost of electricity generated from other grid technologies such as hydropower.

In 2009, China became Africa's largest trading partner. It also established a China—Africa partnership designed, among various things, to encourage the development of new energy sources. Since 2010, Chinese companies have invested billions of dollars in the African energy sector, especially in oil and gas extraction. However, from 2010 to 2015, Chinese contractors built more than half of sub-Saharan Africa's new hydroelectric power plants. Over the period 2010 to 2020, the EIA estimates that of all the new power plants that Chinese companies have built or are contracted to build in Africa, 49 percent of their power output will come from dam turbines and 44 percent will come from burning fossil fuels.[c] China is also an important supplier of wind turbines and solar panels to Africa.

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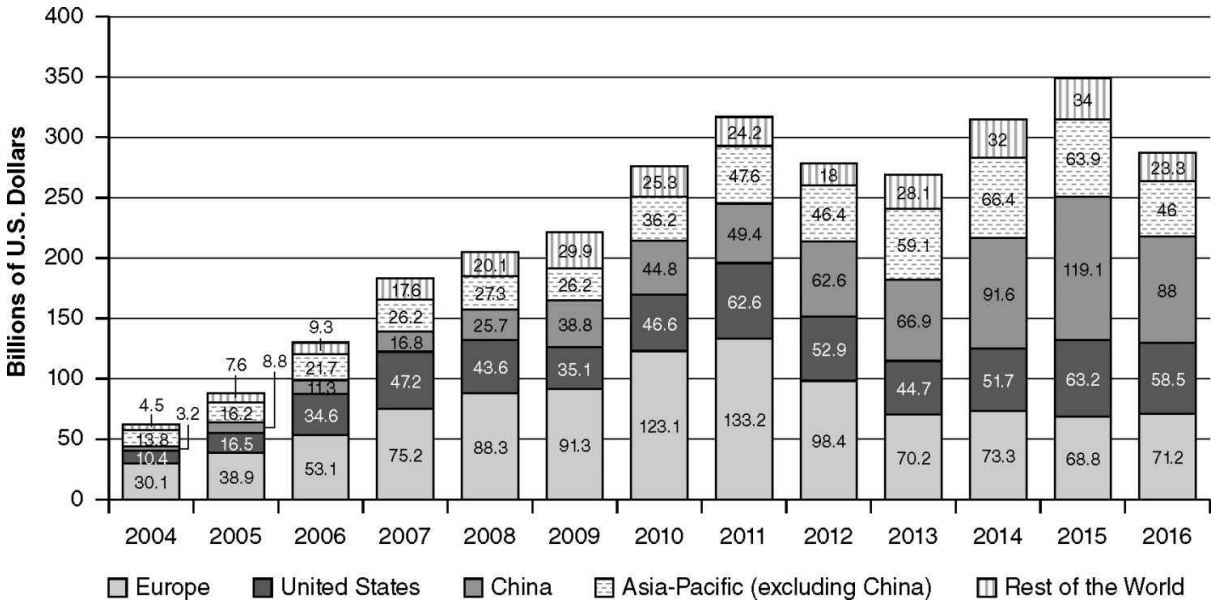


FIGURE 16.4
Global New Investments in Clean Energy (Solar, Wind, Biofuels, and Others), 2004–2016

Source: Data from Abraham Louw, "C lean Energy Investment Trends, 3Q 2017," Bloomberg New Energy Finance (October 5, 2017).

Critics have argued that dismantling the EPA might lead to increased air and water pollution in many parts of the United States. In justifying the United States' exit from the Paris Agreement, Trump claimed, "I was elected to represent the citizens of Pittsburgh, not Paris." Yet he is apparently unaware that over the past 30 years Pittsburgh has transformed itself from a highly polluted steel town into "a happening place" known for its higher education, tech industries, medical complexes, and over 13,000 renewable energy jobs.[49]

Former Florida governor and U.S. Senator Bob Graham argues that Trump's plan to open offshore areas to drilling will undermine critical environmental safeguards. He warns us to expect more disasters like BP's Deepwater Horizon explosion in the Gulf of Mexico in 2010 that killed 11 workers, released several million barrels of toxic crude into the ocean, and cost BP more than $60 billion in penalties and cleanup.

The renewable energy industry is a measurably more promising job creator in the modern economy. In 2016, the Department of Energy reported that renewable energy was responsible for 40 percent of the 1.9 U.S. million jobs in the power generation, mining, and fuel extraction industries combined. The solar industry alone employed more than twice as many Americans as the coal industry.[50] Trump's policies seem designed to discourage business investments in renewables, meaning a loss in future technological spin-offs from development of renewable energy sources and products. For these and other reasons, many states, businesses, and interest groups are moving forward with renewable energy investments despite the lack of support from Washington.

CONCLUSION: PEEKING OVER THE PRECIPICE

After World War II, industrialization and the drive for economic growth in Europe, the United States, and Japan resulted in major increases in fossil fuel energy production. Oil was relatively cheap until OPEC used it as a weapon in 1973 to counter the economic and geopolitical policies of Europe and the United States. The 1970s also witnessed awareness of the tightening connection between fossil fuels and "spaceship earth."

As industrialization and globalization accelerated in the 1980s and 1990s, environmental problems became more global and interconnected, causing conflicts with development, energy, and national security goals. After the Rio summit in 1992 produced the UNFCCC, mounting scientific research pointed to climate change as a scientific fact and spurred a sense of urgency to develop alternative energy sources. At the 1997 Kyoto meetings, nation-states agreed on the need to lower carbon emissions and created a number of market-based mechanisms to help make that possible.

With high oil prices before the financial crisis in 2007, major oil producers continued to push for increased production. Natural gas production increased dramatically along with criticism of the impact of fracking on the environment. Major debates about peak oil and the evidence for and against climate change reflected political ideologies. The financial crisis made addressing environmental issues financially and socially more difficult, while also weakening support for a global accord on climate change at meetings in Copenhagen, Durban, and Doha.

By 2015, market conditions for fossil fuels had shifted once again: the world was drowning in oil and natural gas due to increased production in African states, Russia, and the United States, resulting in a buyer's market. At the same time, as technological advances made renewable energy more efficient, effective, and less costly, there was more optimism that green energy could meet rising demand for energy while reducing emissions of greenhouse gases.

Surprisingly, in 2015 almost all countries signed the Paris Agreement, through which they agreed to voluntarily comply with emissions reduction targets. The effects of climate change were clearer than ever: major ice sheets in the Arctic, Greenland, and Antarctica were melting quickly; major droughts persisted in many places; and scientists documented record-high temperatures nearly everywhere. Many major corporations accepted this evidence and invested more in green energy. There was strong public support for the Paris Agreement and efforts to deal with climate change.

From a global perspective, the overall supply of energy is no longer the problem; instead, the problem is that fossil fuels are still the dominant sources of energy. And yet, U.S. president Trump "threw a monkey wrench" into global environmental cooperation, adding to the evidence that the postwar era is ending. Under his leadership the United States risks perpetuating a global tragedy for the sake of isolating itself from the rest of the world while pursuing energy and environmental goals that no longer reflect global political, economic, and social conditions. He has ceded leadership on global energy and environmental policies

to China and Germany, and perhaps even France, where new president Emmanuel Macron pledged to "Make Our Planet Great Again."

KEY TERMS

Paris Agreement on Climate Change 437
renewable energy 437
climate change 438
cartel 438
Organization of Petroleum Exporting Countries (OPEC) 438
Intergovernmental Panel on Climate Change (IPCC) 439
Tragedy of the Commons 439
Earth Summit 444
sustainable development 444
UN Framework Convention on Climate Change (UNFCCC) 444
Kyoto Protocol 445
cap-and-trade 445
oil 447
fracking 448

DISCUSSION QUESTIONS

1. Do you think that nation-states are capable of solving global environmental problems, or should we look to international organizations to play a dominant role? What factors have limited international cooperation to combat climate change?
2. What responsibility do developing countries have for solving global environmental problems? What is the responsibility of developed nations?
3. What are the causes and effects of major increases and decreases in oil prices historically?
4. What do you think are the global implications of the rise of the United States as a major natural gas producer and the rise of China as a leader in the solar and wind power industries?
5. How do you explain the frequent tendency of the United States to have different views from other countries on energy and environmental issues? What pressures might the United States face if it continues to pursue Trump's energy and environment policies?
6. One of the theses we offered at the start of the chapter is that the transition to renewable energy and stronger environmental protection is well under way in much of the world. Assess the evidence for and against this argument.

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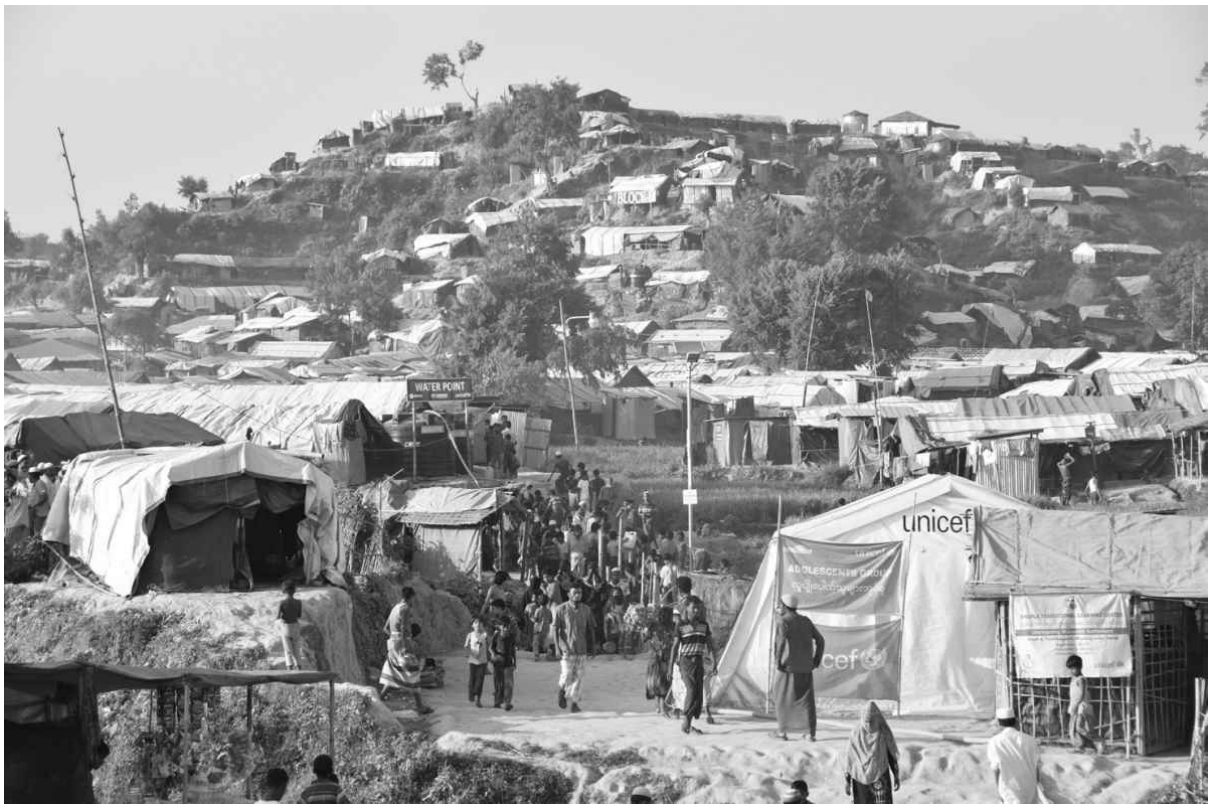
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CHAPTER
17
Global Health: Refugees and Caring for the Forgotten



A Rohingya refugee camp in Bangladesh, November 2017.

Source: AP Photo/Kyodo Extra.

Global health is an attitude. It is a way of looking at the world.… It is a statement about our commitment to health as a fundamental quality of liberty and equity.

Richard Horton[1]

Since 2013, millions of refugees and migrants have fled wars and poverty in the Middle East and Africa, many trying to get to one of the small islands off the coasts of Greece and Italy. To escape drought, hunger, and violent conflict, hundreds of thousands of South

Sudanese have fled to Uganda, Kenya, and Ethiopia. By October of 2017, more than 800,000 Rohingya people had fled persecution in Myanmar, ending up in Bangladesh, where hundreds of thousands of Bangladeshis themselves have been displaced by typhoons.[2] In still another dramatic situation, roughly 1,500 displaced people have lived for four years in isolated conditions on two small islands in Papua New Guinea, waiting to be placed somewhere safe in the world.

The global community appears to have become numb to all of these refugees who are in the news so much. Many people want to ignore their plight or just let someone else deal with them. Nevertheless, for years many individuals, states, international organizations (IOs), and nongovernmental organizations (NGOs) have been trying to help the displaced. So why are things not getting better for so many "forgotten" people?

Since World War II, state officials and academics have blamed various causes for the rising number of displaced people: war and other forms of conflict; lack of foreign aid and food aid; famine; drought; underdevelopment; overpopulation; weak state institutions; corruption; and environmental destruction.

In recent years, IPE scholars and medical researchers have shown a greater appreciation for "global health," which concerns not just physical medical problems and infectious diseases that people face everywhere in the world, but also trauma and psychological injury.[3] A global health perspective also suggests that coordinated efforts at the local, national, regional, and global levels are necessary to treat many of the problems associated with international migration. We also argue that migration is a problem for the whole world, not just for a few. The plight of migrants and refugees is interconnected with many IPE issues such as global security, the distribution of global wealth and power, and social transformation.

This chapter begins with a brief discussion of the connection between IPE and global health studies. We then describe some of the different categories of migrants, how many there are, where they come from, and their destinations. We then examine major causes of people's displacement and some health care actors that are caring for migrants in four geographic regions: the Middle East, Africa, South Asia, and the South Pacific. Finally, we discuss some solutions to the health problems of the displaced.

There are five theses in this chapter:

- The concept of global health makes clear that the refugee problem is a health problem for the whole world.
- Poverty, drought, hunger, and conflict are the biggest direct causes of migration.
- International and nongovernmental organizations provide the most (and best) humanitarian assistance to migrants and refugees.
- States have political and moral obligations to resolve the political causes of humanitarian crises and to do much more to help humanitarian IOs and NGOs address the physical and mental health needs of refugees.
- Finally, to mitigate migration and displacement, sustainable development approaches are superior to market-oriented economic approaches.

As in the other chapters, we employ the four IPE perspectives to sharpen our analyses and raise a number of theoretical issues.

THE FORGOTTEN

Many readers of this textbook are familiar with debates about immigrants in the developed countries. Economic globalization has spurred flows of immigrants to countries such as the United States, Germany, Italy, Spain, and France, where low birth rates make the need for foreign workers increasingly important.[4] Some immigrants are highly-skilled and well educated, while others are unskilled workers in food services, the garment industry, meatpacking, and agriculture. Most countries have well-developed regulations for the management and protection of legal immigrants who move *into* a new country for the purpose of settling, finding employment, and becoming a resident.

In recent years, nationalist political parties that want to restrict immigration and tighten border controls have been gaining popular support. Heated debates in the United States, Europe, and Australia have centered on the economic, social, and political implications of immigrants. Given that one of the chief functions of the modern state is to control its borders and protect its citizens' rights, some see unauthorized and even authorized immigration as a threat to national security and sovereignty.

In UN parlance, international migrants are people living in a country other than their country of birth. There were 244 million migrants in 2015, many of whom reside legally in countries where they work or study. Approximately 50 million of these migrants are considered "irregular"—having moved illegally or in an unregulated manner to another country in search of jobs or other economic opportunities. Another group of migrants—more than 22 million—are refugees who have unwillingly fled from persecution, conflict, or famine in their home country. Although many people use the terms "immigrants," "migrants," irregular migrants," and "refugees" interchangeably, in this chapter we use the term "migrants" to refer primarily to irregular migrants and refugees. We will also focus on displaced people, who include refugees who have fled to another country and internally displaced people (IDPs) *inside their own country* who have unwillingly left their homes.

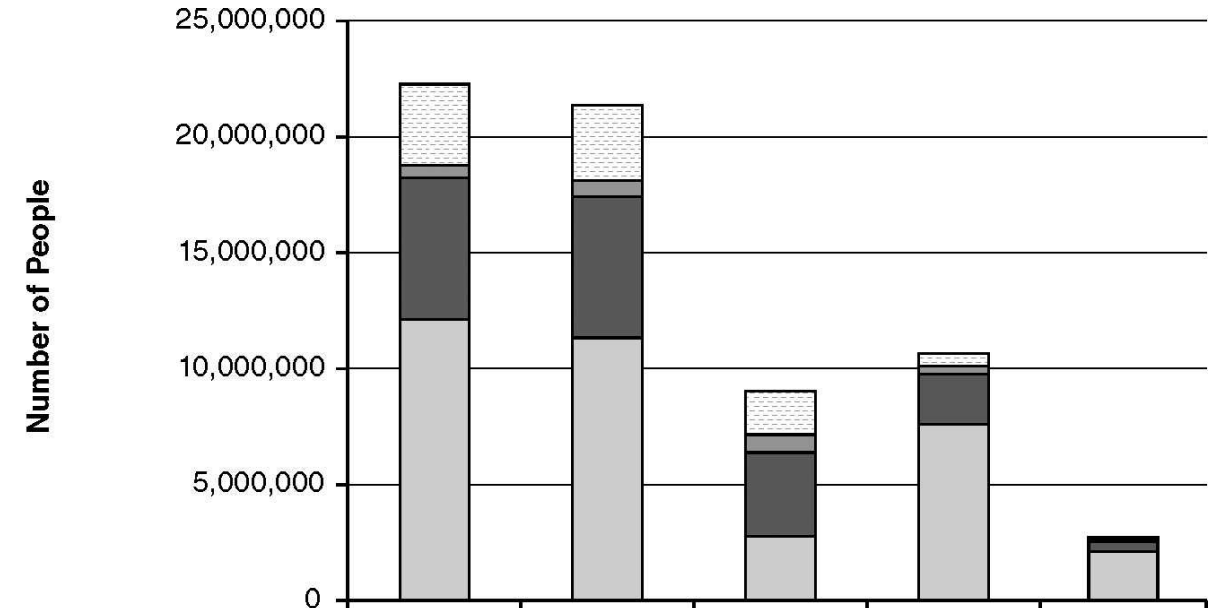
Several international conventions specify the responsibilities of receiving states to protect migrant workers' rights, including the International Labour Organization's (ILO) 1949 Migration for Employment Convention, the ILO's 1975 Migrant Workers (Supplementary Provisions) Convention, and the United Nations 1990 International Convention on the Protection of the Rights of All Migrant Workers and Members of Their Families. Following high-level meetings in September 2016, 193 members of the UN General Assembly issued the New York Declaration for Refugees and Migrants in which they pledged, among other things, to protect the safety and human rights of all migrants and to cooperate on meeting the humanitarian and development needs of all refugees and migrants.[5] Recently, states have also placed special emphasis on assisting displaced children and making refugee psychological disorders a major health issue worthy of attention and help.[6]

The increased scale of transnational migration from developing countries can be seen in

new travel routes or "trails" from Syria through Turkey to the EU and from poor, conflict-ridden states in Africa to Libya and across the Mediterranean. The United Nations High Commissioner for Refugees (UNHCR) estimates that by the end of 2016 there were 65.6 million forcibly displaced people in the world, 40.3 million of whom were displaced within their own country and 22.5 million of whom were refugees living outside of their home country.[7] Although many IDPs and refugees are living in camps, the majority eke out a precarious existence in and around cities and villages. Some are living in developed countries, but most are in poor developing countries that face the ravages of drought, hunger, disease, and war. Although international organizations and nongovernmental organizations care for these people, much of the world has largely forgotten them. Thav have little hope for resettlement or a normal life.

Refugees are often unable or unwilling to return to their country of origin because of fear of persecution related to their religion, nationality, ethnicity, or political opinion. For example, a South Sudanese victim of ethnic violence who moves to a temporary camp in Uganda or Kenya is considered a refugee. Often the UNHCR is responsible for negotiating a permanent resettlement destination—either in Uganda or in another country—for this person. More than half of all the world's refugees are under the age of 18. More than 80 percent of the world's refugees live in developing countries. Asylum seekers are refugees who claim to face persecution in their home countries. They usually seek legal protection from a court within the nation in which they wish to reside. (In the case of the EU, they must file for asylum in the first EU country in which they arrive.) In the OECD countries, nearly 550,000 of the roughly 5 million people who were classified as new permanent migrants in 2015 were refugees. Nearly 300,000 of these "humanitarian migrants" gained official permission to stay in Germany and the United States.[8]

Figure 17.1 contains estimates of the number of IDPs, refugees, and other "peoples of concern" in different regions of the world that we discuss later in the chapter. Box 17.1 notes some important humanitarian organizations giving care to displaced people.



	Middle East and North Africa	Africa	Asia and Pacific	Latin America and the Caribbean	Europe
Other People of Concern	3,505,845	3,252,929	1,867,719	547,774	68,162
Asylum Seekers	543,201	704,349	769,791	321,343	132,908
Refugees	6,097,683	6,079,728	3,636,960	2,199,961	411,710
IDPs	12,129,833	11,333,466	2,748,671	7,584,816	2,117,957

FIGURE 17.1
Internally Displaced People, Refugees, Asylum Seekers, and Other People of Concern in World Regions, End of 2016

*Source:*Data from United Nations High Commissioner for Refugees (UNHCR), "Global Trends: Forced Displacement in 2016," June 2017, p. 70, at www.unhcr.org/5943e8a34.pdf.

THE CAREGIVERS

Here we identify some of the most active international organizations, nongovernmental organizations, and human rights groups that provide care for refugees and other displaced people and try to protect them from harm.

IOs

The *Office of the United Nations High Commissioner for Refugees* (UN HCR) tries "to ensure that everyone has the right to seek asylum and find safe refuge in another State" and provides refugees "critical emergency assistance such as clean water, sanitation and healthcare, as well as shelter … and sometimes food."[a]

The *United Nations International Children's Emergency Fund* (UNICEF) "promotes the rights and wellbeing of every child," focuses on "reaching the most vulnerable and excluded children," and works with other organizations to "overcome the obstacles that poverty, violence, disease and discrimination place in a child's path."[b]

The UN *World Food Program* (WFP) provides humanitarian food assistance to more than 80 million people each year in 80 countries, many of which are plagued by conflict.[c]

The *World Health Organization* (WHO) directs international health within the UN system and sets global health norms and standards and monitors their implementation.[d]

Established as a UN agency in 1951, the *International Organization for Migration* (IOM) is the leading migration organization and works closely with the UN HCR, states, and NGOs on the problem of resettlement. It has operations in 186 states.[e]

NGOs

Save the Children is a popular international NGO that provides emergency food, health care, shelter, sanitation, and education for children in 120 countries.

Médicins Sans Frontières (MSF) or Doctors Without Borders is an international association of doctors and health care workers that assists "populations in distress" and war victims, observing "strict neutrality and impartiality in the name of universal medical ethics and the right to humanitarian assistance and claims full and unhindered freedom in the exercise of its functions."[f]

Oxfam runs anti-poverty programs and provides clean water and sanitation services to fight diseases in developing countries.

Based in Geneva, Switzerland, the *International Committee of the Red Cross* (ICRC) is the oldest humanitarian institution protecting victims of international and internal armed conflicts, including prisoners of war, the wounded, refugees, and civilians.

The *International Rescue Committee* (IRC) provides humanitarian aid to refugees

and helps the poor access primary health care.

Mercy Corps is an international non-profit organization based in Portland, Oregon that provides emergency relief in conflict areas and helps rebuild communities.

Human Rights Groups

Human Rights Watch (HRW) is a fiercely independent NGO that opposes human rights abuses anywhere in the world and reports violations of the laws of war and international humanitarian law to states and UN agencies.

Physicians for Human Rights (PHR) documents and forensically investigates genocide, crimes against humanity, war crimes, wartime rapes, and attacks on health care facilities and health care workers in conflict zones.

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REIMAGINING GLOBAL HEALTH

As we discussed in Chapter 5, constructivism highlights the way in which framing creates a narrative about the causes and nature of a problem and how to solve it. Constructivism also helps us understand why certain health problems get more attention than others and why governments fund much more research and treatment for certain diseases and illnesses than others. As one would suspect, threats to developed countries usually get more media attention and command more state resources than medical problems in developing nations.

In this era of globalization and interconnectedness, public health has emerged as a major global issue. In the not-too-distant past, most infectious diseases were confined to relatively small geographical areas and occasionally spread to whole geographic regions. In recent years, however, some infectious diseases such as HIV/AIDS, Ebola, SARS, H5N1 (bird flu), and H1N1 (swine flu) have spread quickly, threatening the lives of people in different parts of the world. Sophisticated global communications networks allow us to see the effects of certain maladies up close. Framing some diseases as *global* health problems also makes them everyone's problems. Hopefully, framing the problems of refugees and migrants in this manner will pressure states and individuals to commit to finding better solutions.

Constructivists believe that norms play an important role in shaping state behavior. In the 1990s, norm entrepreneurs in the United States and the World Health Organization (WHO) secretariat worked to persuade states to accept new principles of behavior in the face of pandemics. They employed a "global health security discourse" that stressed the *collective* security threats that diseases pose.[9] In 2005 states accepted a new set of norms in the revised International Health Regulations specifying how they were to cooperate in the face of infectious disease outbreaks. It was expected that they would report outbreaks, share disease information with other states, deal with outbreaks at the source instead of at borders, and seek to minimize disruptions to travel and trade.

During the outbreak of Ebola in Sierra Leone and Liberia in 2014 and 2015, the WHO was roundly criticized for its slow response and its failure to declare it a "public health emergency of international concern" early on. Countries affected by the virus had not received help to build up their public health capabilities, as had been promised in the International Health Regulations. Some governments were so worried that Ebola could spread to their country that they imposed trade and travel bans on Ebola-affected countries in excess of WHO recommendations.[10]

In contrast, during the Olympic Games in Brazil in 2016, the norms associated with dealing with infectious diseases worked well to produce coordinated responses and information sharing in the face of the Zika outbreak. Brazil and other countries in Latin America did not try to cover up or minimize the Zika problem, nor did the international community isolate Brazil or disrupt flows of people to and from the Games. State responses, such as warning pregnant women not to travel to certain areas, were calibrated on the basis of scientific risk assessments, not irrational fears or political expediency.

Material self-interest or lack of capacity caused some states to violate the norms associated with controlling the disease, but many states seemed to reflexively abide by the norms because they believe it is what "responsible" states should do, even if they experience short-term costs.[11]

In the case of refugees, realists might point out that some states have yet to realize that it is in their political and economic interests to establish norms to assist displaced people. Instead, some states continue to ignore the refugee problem. One reason in recent years is the growing popularity of nationalist and authoritarian regimes that care little or have contempt for the displaced.

This stands in marked contrast to the early post-World War II period, when the first foreign aid initiatives to improve health in developing countries focused on supplying vaccines. In the case of smallpox, vaccines succeeded in eliminating the disease. Development and food aid in the 1950s and 1960s aimed to reduce displacement caused by overpopulation. The Western-led foreign aid regime also saw poor health and hunger as impediments to economic growth that were derived from economic inequality. Many experts also began to realize that, while certain illnesses might be cured from the top down, *overall health* could only be maintained by communities from the ground up—with well-trained local health workers, equal access to healthcare, medical treatments that were sensitive to local cultural norms, and provision of public goods such as education, housing, and nutrition.

In 1978, at the International Conference on Primary Health Care in Alma-Ata, the capital of the Soviet Republic of Kazakhstan, a broad coalition of nations agreed that what was really needed to improve health worldwide was *universal primary health care.* As an ideal this came close to the contemporary concept of "global health." However, many Western aid experts saw universal primary health care as too ambitious to implement. At the Rockefeller Foundation's Bellagio Conference in Italy in 1979, they proposed a more limited, actionable plan called *selective primary health care* that identified specific health problems whose solutions would save a high number of lives per dollar spent. In the 1980s they implemented this plan mostly by focusing on four interventions in poor countries: growth monitoring of infants, oral rehydration for infants, breastfeeding promotion, and immunizations (GOBI).[12]

While the experts debated, the global recession in 1982 ushered in a new era of frugal public spending in Western countries. Aid organizations such as the World Bank became more cautious about their spending and ended up pursuing selective primary health care, citing its cost-effectiveness. Structural adjustment programs (SAPs) imposed by the IMF and the World Bank in the 1980s and 1990s required austerity measures and cuts in social programs that increased social distress in developing countries and weakened their health care systems. In the minds of free-market economists, the proper role of the government was to offer cost-neutral healthcare programs that would pay for themselves by charging nominal fees, while educating the public as to which medical services were important and necessary. Many aid institutions and NGOs embraced Reagan's "small-government" economic philosophy across the board, altering the nature of all foreign aid. UNICEF

advocated for more health safety nets during structural adjustment and promoted targeted child survival programs.

Some structuralist critics of market-based approaches to health care argued that they didn't adequately address the failings of healthcare *systems* in developing countries – and that fees for medical services were driving poor patients away, making underlying health inequalities worse. Colin McInnes and Kelley Lee maintain that today much health care continues to be based on promoting competition among health care providers, creating public–private partnerships, and expanding the role of market forces in health care allocation. In practice, this has meant: many governments provide fewer health care benefits and services; medical research concentrates on health problems in developed countries; and pharmaceutical companies use patents to keep the prices of medicines so high that many poor people cannot afford them.[13] In light of these deficiencies, many global health experts have tilted back toward the integrative vision (also called the "horizontal" approach) proposed at Alma-Ata. Similar to many "food first" policy supporters, they focus on fair and equitable access to health care rather than policies dominated by an economic narrative.

However, since the 2000s, the major global health *donors* have been reluctant to significantly increase funding for programs that primarily seek to strengthen national healthcare *systems* and expand access to primary health care services over the long term in poor countries. Instead, their increased funding to multilateral international organizations such as the WHO and the World Bank is now typically discretionary, meaning that these IOs can only allocate the money for purposes that the donors specify.[14] The United States, some European countries, and private donors such as the Bill and Melinda Gates Foundation seek considerable control over how their funding is used, and they want to be able to measure and monitor the effectiveness of global health interventions. For these and other reasons, major donors now strongly favor a "vertical" approach to global health in which they voluntarily fund narrowly targeted diseases or causes (like maternal and newborn health) in the hopes of saving or improving the most lives.

The vertical approach is evident in two major health alliances that expanded in the 2000s: the Global Fund to Fight AIDS, Tuberculosis, and Malaria; and the Global Alliance for Vaccines and Immunization (Gavi). Both seek to reduce the number of people in poor countries who contract infectious diseases and increase the survival rate of those who become infected. Both are "public–private partnerships" in which UN agencies, national governments, NGOs, and private corporations work together to achieve particular health goals. Like businesses, both alliances stress cost-effectiveness and demonstrable results. Gavi's support is critical in enabling UNICEF to provide immunizations to tens of millions of children. The Global Fund gives grants to governments and NGOs to carry out HIV/AIDS, TB, and malaria treatment and prevention programs.

The financial aid that state and multilateral development agencies give to low- and medium-income countries for health promotion is commonly referred to as development assistance for health (DAH). The Institute for Health Metrics and Evaluation (IHME), a health research center at the University of Washington, tracks long-term trends in this aid,

which is either disbursed bilaterally to governments in developing countries or through intermediaries such as UN agencies, NGOs, and public–private partnerships.[15] Today nearly 36 percent of the money that poor countries spend on health comes from DAH. The annual amount of DAH transferred from rich to poor and medium-income countries rose steadily from about $llbillion in 2000 to nearly $36 billion in 2011; annual DAH then flatlined at about $36 billion from 2012–2016. The United States has for years been the largest donor of DAH; in 2016 it gave nearly $13 billion, which amounted to one-third of all global DAH. The biggest providers of DAH after the United States are the United France, and the Gates Foundation.

International migration and global health are clearly important subjects for IPE. Several questions we analyze below are:

- Under what conditions does migration occur?
- Who bears responsibility for migrant health care?
- What forms of global governance would be effective in regulating migrants' movements rights, and health care?

REGIONAL CASES OF DISPLACEMENT: WHERE TO GO?

Most of the world's migrants and refugees are found in and around poor developing nations, especially "failed states" such as Syria and South Sudan with high rates of poverty, poor health care, malnutrition, and armed conflict. Since the 1990s, civil wars have contributed greatly to starvation and displacement in places such as Ethiopia, Sierra Leone, Rwanda, Sudan, South Sudan, Angola, Liberia, Syria, Afghanistan, and Iraq. For example, following the Rwandan genocide, Tutsi forces fled to neighboring countries such as the Democratic Republic of the Congo, fighting government forces over control of minerals and other natural resources and forcing many people to seek shelter in refugee camps.

After the regime of Muammar Qaddafi collapsed in 2011, Libya descended into a state of chaos and armed violence, with no central government able to control the country. Tens of thousands of migrants from *other* troubled countries in East Africa, the Middle East, and sub-Saharan Africa flowed into this cauldron, all seeking to eventually get to Europe. Many died in the desert just trying to reach Libya. The migrants from Nigeria, Ethiopia, Somalia, Sudan, and elsewhere pay smugglers to take them across the Mediterranean Sea by boat, usually to land on Italian shores where they can claim asylum. Many never make it to safety in Europe. The International Organization for Migration estimates that from January 2014 to December 2017 between 8,400 and 13,400 people perished while making the Central Mediterranean crossing, mostly from drowning.[16]

Tens of thousands of these refugees have also been rescued from rickety and overcrowded boats by the Italian navy, other European navies, and ships from NGOs such as Save the Children, Proactiva, and SOS MEDITERRANEE. In mid-2017 Italy reached a deal with Tripoli's UN-backed government and militias that control boat smuggling to have them prevent refugees from setting sail from Libyan ports and detain those found in boats in Libyan coastal waters. Boat arrivals to Italy plunged, but at the cost of severe abuse of thousands of refugees in Libya by militias.[17] After CNN documented instances of refugees being auctioned off as slaves in Libya, the UN Security Council in December condemned these human rights abuses and called for an investigation.[18]

Unfortunately, migrants in other regions of the world often face similarly bad conditions. In the rest of this section we will examine four recent cases (Syria, South Sudan, Myanmar, and the South Pacific) where violence and armed conflict have displaced people and threatened both their physical and mental health.

Syria's Civil War

Wars in Afghanistan and Iraq after 9/11 and in Syria and Yemen after the Arab Spring have caused a dramatic rise in the number of displaced people in the Middle East. Turkey and Libya have become gateways for record numbers of migrants trying to enter EU countries. Syria experienced a severe drought from 2007 to 2010 that displaced as many as 1.5 million

people from rural agricultural regions to precarious conditions in urban areas.[19] In 2011 a brutal civil war started when the Free Syrian Army (FSA) and other resistance groups tried to overthrow the regime of President Bashar al-Assad (see Chapters 9 and 14). The Syrian government received military support from Iran, Russia, and Lebanon's Hezbollah. In 2014 the Islamic State of Iraq and Syria (ISIS) took control of some areas in Syria and then seized a major part of Iraq, including the northern city of Mosul.

The Syrian Observatory for Human Rights estimates that by late 2017 nearly 500,000 Syrians had died in the civil war, and many more had been injured. The UNHCR estimates that by the end of 2017 approximately 6.1 million Syrians were internally displaced and 5.4 million had fled the country. There were 3.2 million Syrian refugees in Turkey, 1 million in Lebanon, 655,000 in Jordan, and 244,000 in Iraq (see Figure 17.2). These countries have strained to provide them basic education, health care, food, and affordable housing. Many refugees in Turkey made the short channel crossing to get to Greece.

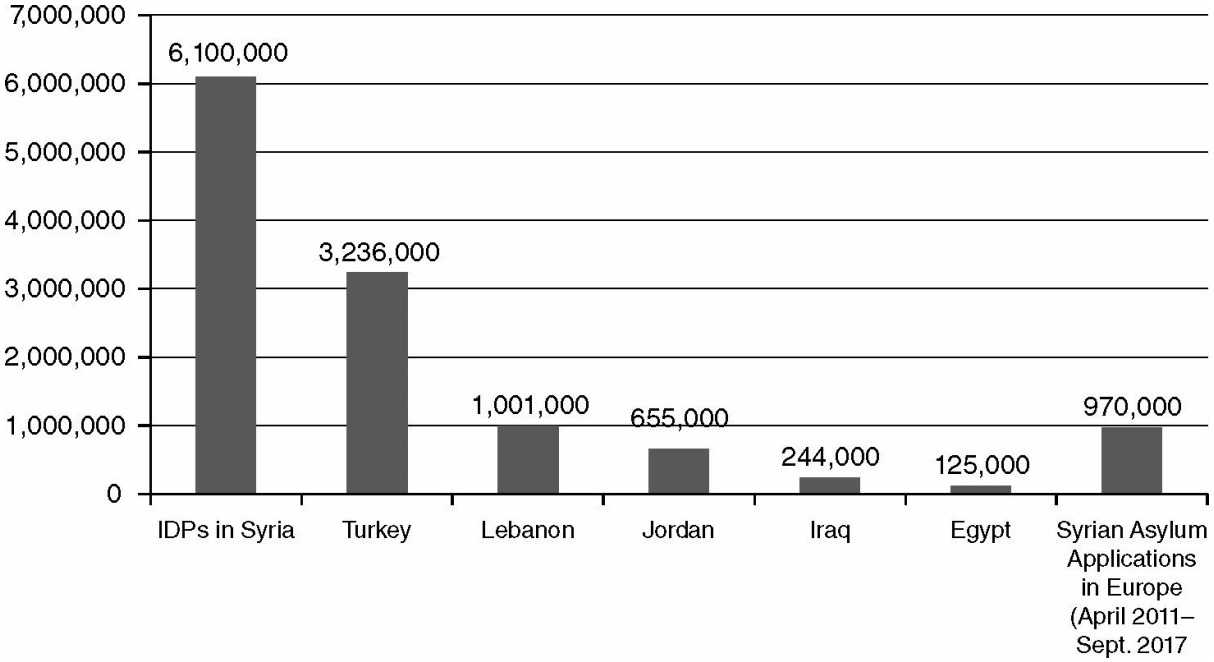


FIGURE 17.2
Internally Displaced Syrians and Registered Syrian Refugees in Main Countries in September 2017

Source: Data from United Nations Office for the Coordination of Humanitarian Affairs (UNOCHA), "2018 Humanitarian Needs Overview: Syrian Arab Republic" (November 2017), p. 11, at https://reliefweb.int/sites/reliefweb.int/files/resources/2018_syr_hno_english.pdf.

Women, children, the elderly, and the disabled have been the most vulnerable to malnutrition. Syrian refugees overall also have many non-communicable diseases such as diabetes and cancer for which they do not receive proper care.[20] Many humanitarian IOs and NGOs have increasingly recognized the need to treat psychological trauma, particularly

in children. Although Assad's forces have frequently struck rebel-controlled areas with barrel bombs and chemicals such as chlorine, killing and maiming thousands of civilians, there is little prospect that the UN Security Council will ask the International Criminal Court in the Hague, the Netherlands, to prosecute Assad and other regime officials for these and other war crimes that we describe in Box 17.2.

WAR CRIMES IN SYRIA

Since 2011, states and nonstate actors, including ISIS and militias, have committed shocking war crimes in Syria.[a] To date, none of the perpetrators of these crimes have been held to account. Russia's veto power on the UN Security Council makes it unlikely that cases involving the Syrian government and its allies will be referred to the International Criminal Court.

The lack of any justice for victims and their families is a problem in itself, but violations of international humanitarian law with impunity threaten the legitimacy of the international security order. The norms governing war are weakened, as are a whole host of human rights norms.

In August 2011 the UN Human Rights Council established an Independent International Commission of Inquiry on the Syrian Arab Republic (IICIS) to investigate human rights violations and try to identify those responsible. The Commission has documented many war crimes against civilians in Syria by regime forces, including use of chemical weapons (sarin and chlorine), siege warfare, denial of food, and forced displacement of civilians.[b]

The horror of the Syrian civil war became clear in early 2013 when global media showed videos and pictures of several dozen bodies strewn along the banks of the Quieq River in Aleppo. With gunshot wounds in the head and wrists tied behind their backs, the men had apparently been detained by government forces in a regime-held section of Aleppo before being executed and dumped in the river. There was also suspicion that the perpetrators of the murders were the *shabiha*, an Alawite militia allied with the Assad regime that is responsible for crimes throughout the country. Between January and March 2013 more than 230 bodies of murdered men were pulled out of the Queiq in the rebel-held section of Aleppo.[c]

In 2014 a former Syrian forensic photographer code-named "Caesar" fled Syria with more than 50,000 photos he had taken of dead bodies while he was employed by the Syrian military police between 2011 and 2013. The photos were taken at two military hospitals where bodies had been brought from various detention centers run by the Syrian security services. Human Rights Watch found the photos to depict nearly 7,000 unique bodies, many of which showed signs of torture, beatings, or starvation.[d]

Since 2013, Syrian government forces have besieged dozens of towns outside of their control as part of a "surrender or starve" strategy. The sieges, which include cutoffs of food and medicine, captured international attention in late 2015 when pictures spread of emaciated people in the town of Madaya, where at least 65 people died of starvation or malnutrition between November 2015 and May 2016.[e] As in other places, government forces circled the town with landmines and prohibited most humanitarian food deliveries.

During the siege of eastern Aleppo, Syrian and Russian forces indiscriminately bombed civilian areas and destroyed all medical facilities, reducing much of the city to rubble and killing hundreds of civilians. In April 2017 Syrian forces used sarin gas in Khan Sheikoun, killing 87 civilians and wounding an estimated 500 people.

In the months-long assault on the ISIS stronghold of Raqqa in 2017, U.S. airstrikes killed hundreds of civilians. The American bombing, in conjunction with attacks on the ground led by Syrian Kurdish forces, caused nearly 200,000 people to flee the Raqqa area.[f]

In early 2017, Amnesty International estimated that since the start of the Syrian rebellion 5,000 to 13,000 Syrian detainees had been executed by hanging at Saydnaya prison, a notorious facility controlled by the Syrian military where detainees are also systematically tortured.[g]

There are many troubling questions raised by these war crimes. Why don't the Great Powers care enough to do anything about them? How can nonstate actors like ISIS and the *shabiha* be held to account? Have constructivists overestimated the power of norms to constrain state actions? Does realpolitik always trump humanitarian law? Is the international security structure really designed to protect civilians in civil wars?

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[a] For a harrowing account of human rights atrocities early in the Syrian conflict, see Janine di Giovanni, *The Morning They Came for Us: Dispatches from Syria* (New York: Liveright, 2016).

[b] *Reports of the IICIS can be found* at www.ohchr.org/EN/HRBodies/HRC/IICISyria/Pages/IndependentInternationalCommission.aspx.

[c] See Human Rights Watch, "*Syria: A Stream of Bodies in Aleppo's River*," June 4, 2013, at www.hrw.org/news/2013/06/04/syria-stream-bodies-aleppos-river; and Luke Mogelson, "The River Martyrs," *The New Yorker*, April 29, 2013' at www.newyorker.com/magazine/2013/04/29/the-river-martyrs.

[d] See Human Rights Watch, "*If the Dead Could Speak: Mass Deaths and Torture in Syria's Detention Facilities*," December 2015, at www.hrw.org/news/2015/12/16/syria-stories-behind-photos-killed-detainees.

[e] Physicians for Human Rights and the Syrian American Medical Society, "*Madaya: Portrait of a Syrian Town under Siege*," July 2016, at www.sams-usa.net/wp-content/uploads/2016/09/Madaya-report_FINAL_v2.pdf.

[f] Louisa Loveluck, "U.S.-led Airstrikes Are Killing Hundreds of Civilians in the Battle for ISIS-held Raqqa, Groups Say," *Washington Post*, August 23, 2017, at www.washingtonpost.com/world/middle_east/us-led-airstrikes-are-killing-hundreds-of-civilians-in-the-battle-for-isis-held-ragga-this-summer/2017/08/22/8c520948--872d-11e7-96a7-d178cf3524eb_story.html; and United Nations, Human Rights Council, "*Report of the Independent International Commission of Inquiry on the Syrian Arab Republic*," August 8, 2017, A/H RC/36/55.

[g] Amnesty International,"*Human Slaughterhouse: Mass Hangings and Extermination at Saydnaya Prison, Syria*," February 2017, at www.amnesty.org/en/documents/mde24/5415/2017/en/.

Overcrowded refugee camps in the Middle East often have poor sanitation and provide limited food and shelter. Refugee aid in Syria has often been provided in collaboration with the UNHCR, the International Federation of Red Cross and Red Crescent Societies, and the Syrian Ministry of Local Administration. Other key IO caregivers are the WHO, the UN World Food Program, and Save the Children. NGOs are also active. The UK-based

charity Hand in Hand for Syria provides on-the-ground aid including food, water, sanitation, and medical assistance. The International Medical Corps (IMC) helps refugees in Syria and surrounding countries with medical care. The Syrian American Medical Society sends doctors on periodic medical and surgical missions to refugee camps in Syria, Jordan, Turkey, Lebanon, and Greece. Syrian Civil Defense, more commonly known as the White Helmets, operates in rebel-held areas of Syria, rescuing people from bombed buildings and helping civilians hurt during fighting. It claims to have saved tens of thousands of lives since its formation in 2014.[21]

Since 2014, *Médicins Sans Frontières* (Doctors Without Borders) has operated a handful of hospitals in rebel-held regions in northern Syria where it provides emergency care, including surgeries. It has also run some mobile clinics and distributed large amounts of medical supplies. In other parts of Syria, particularly in areas that are besieged, it gives financial support, medicine, supplies, and training to dozens of medical facilities that have provided a wide range of medical services to tens of thousands of people. In Jordan, Lebanon, and the Kurdish region of Iraq, MSF runs medical facilities that offer primary, reproductive and mental health care to Syrian refugees. It also has a reconstructive surgery center and an emergency surgical facility in Jordan. The Syrian government has never authorized MSF to operate in Syria, and regime and Russian forces have repeatedly bombed and shelled its medical facilities, killing dozens of its staff and patients.[22]

Supported by a large budget and international resources, the WHO works with the Syrian government and local health care partners to distribute medical equipment, train Syrian medical staff, gather health information, and provide many health care services to millions of Syrians. However, the WHO and NGOs do not always have access to besieged areas and refugee camps, especially in rebel-held areas.

Apart from health and human rights problems facing displaced Syrians, many state officials fear that jihadist groups are recruiting some of the refugees spread across the Middle East.[23] Critics suggest that hyping this concern about "radicalization" hurts the relief efforts of humanitarian organizations and makes it harder to resettle refugees and convince governments to let them remain indefinitely. As we discussed in Chapter 12, the EU has attempted to reduce the number of migrants and asylum recipients in Europe, causing many displaced Syrians and other migrants in countries such as Greece, Turkey, and Italy to fear that they will be forced back to their home countries where they might face reprisals and death.

The Obama administration admitted 22,921 Syrian refugees into the United States in 2015 and 2016, but only 4,298 were admitted in the first nine months of 2017 as President Trump capped the number of global refugees allowed into the United States and issued an executive order (contested in courts) temporarily banning Syrian refugees on security grounds.[24] Even after Trump lifted the ban in October 2017, very few Syrians were admitted.

Interestingly, in early 2017 President Trump also called for the creation of several large "safe zones" for Syrian refugees in Syria (financed by the Arab Gulf states) so that the

refugees wouldn't need to be admitted into the United States or Europe. The idea went nowhere. Instead, stepped-up U.S. bombing of ISIS-held cities in northeast Syria, in conjunction with a Kurdish-led ground assault on the cities, created new refugee flows and humanitarian disasters. More importantly, in 2017 Russia, Turkey, and Iran reached an agreement to establish four "de-escalation zones" in rebel-held areas, where rebel and regime forces were to cease hostilities for six months and allow food and humanitarian aid to reach approximately 2.5 million Syrians. However, the agreement has been repeatedly violated. By the end of 2017 the Assad regime had regained control of significant parts of Syria, but there still was no end in sight for the conflict or the suffering of displaced Syrians.

South Sudan

Sudan and the countries in the Horn of Africa (Somalia, Ethiopia, Eritrea, and Djibouti) have a history of hunger caused by drought, flooding, conflict, and war. Following a decades-long civil war in the Sudan, South Sudan broke away and became an independent country in 2011. Starting out as one of the poorest countries in the world, it has consistently ranked at or near the bottom of the Fragile States Index, which compares countries' political, economic, and social stability.[25] South Sudan's two dominant ethnic groups, the Dinka and Neur, have fought over power and resources for many years. In 2013 an attempted coup ignited a civil war that left thousands dead and displaced many. When a peace agreement collapsed in 2016, violence spread again, with ethnic cleansing carried out mostly by government forces loyal to President Salva Kiir verging on genocide.

In the face of horrible human rights abuses including murder, rape, and torture, hundreds of thousands of people have fled to Uganda, Kenya, and Ethiopia, where they have strained refugee camps and health services. South Sudan has a population of 11.3 million, with nearly 2 million internally displaced people (see Figure 17.3). There is only one doctor per 100,000 people and very little access to water. Deadly diseases such as malaria are widespread. Food shipments into South Sudan have been blocked and aid workers attacked. Drought also continues to plague parts of the country. By September 2017, nearly 6 million South Sudanese—more than half the population still in the country—were in a state of severe food insecurity.[26]

Conditions in Uganda are a bit better: it has one doctor for 24,000 people! It is caring for some 1.2 million refugees, nearly two-thirds of whom are children under the age of 18.[27] Uganda has some of the most generous resettlement policies of any country. Many South Sudanese refugees are placed on "agricultural settlements" where they can grow their own crops of corn and beans and receive supplemental food from the UN's World Food Programme (WFP).[28] Uganda also provides health care and education, and refugees have the right to work and own businesses.

The WFP distributes large amounts of food in South Sudan. The International Rescue Committee has been one of the largest aid agencies in the country for over 25 years (even before independence), running health clinics, providing clean water, and protecting

women. MSF runs health clinics and hospitals in a number of cities and refugee settlements where it provides primary, maternal, and nutritional health care. It also treats patients with HIV/AIDS in many camps and helps survivors of sexual violence. It has been critical of the lack of aid and water shortages (only 7 liters per person available per day). In 2017 UN agencies earmarked $1 million for reproductive health care, but the UN Population Fund said they needed four times as much.

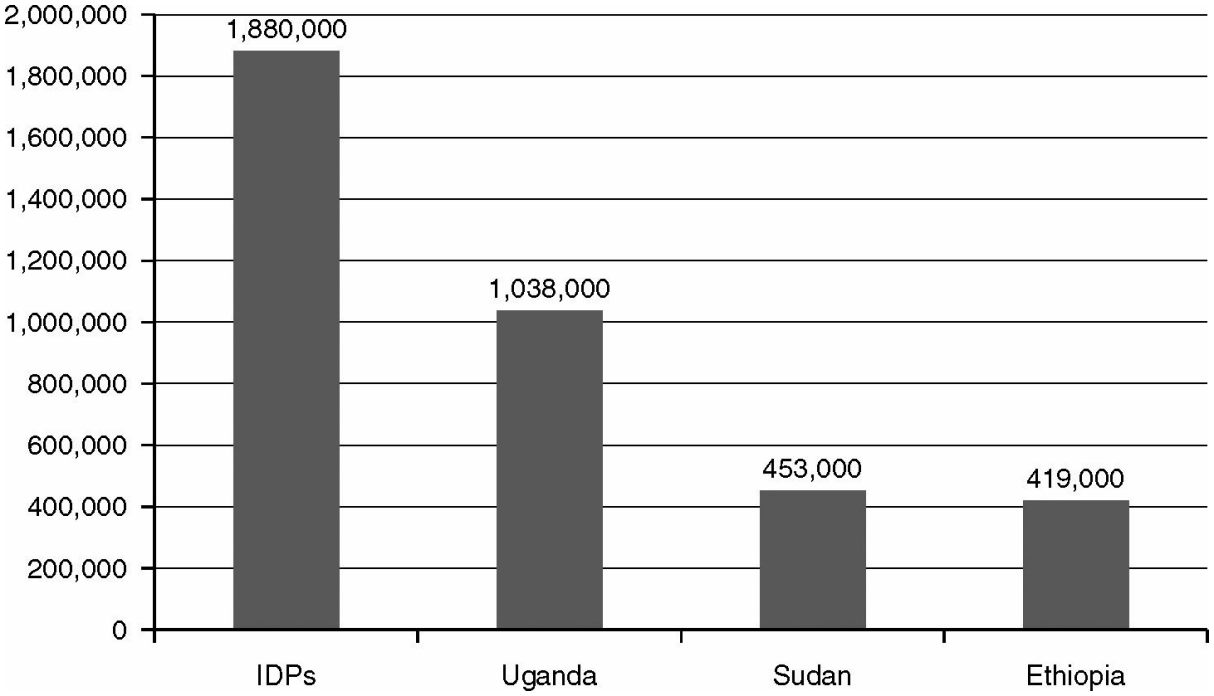


FIGURE 17.3
South Sudanese Internally Displaced Persons and Refugees in Uganda, Sudan, and Ethiopia in October 2017

Source: Data from UN High Commissioner for Refugees (UNHCR), at https://reliefweb.int/sites/reliefweb.int/files/resources/UNHCR%20SSD%200perational%20Update%20No%2021%20-%201%20-15%20November%202017.pdf.

Manus Island and Nauru: Moral Stains

Australia has sought to dissuade refugees from seeking to come to its country by boat and claim asylum. Beginning in 2001 it set up so-called "regional processing centers" for refugees in the independent island country of Nauru and on Manus Island in Papua New Guinea. The facilities—actually detention centers—were closed in 2007 but reopened in 2012. Migrants who do reach Australia have been transferred to the island centers while their applications for asylum are processed. Australia pays Nauru and Papua New Guinea to allow the centers on their territory, and it also bears the cost of running them.

The clear intention of the Australian government has been to make conditions in the centers so bad that detained asylum seekers will accept to go back home and would-be asylum seekers will not set out in a boat for Australia in the first place. The UNHCR,

numerous humanitarian organizations, and Australian activist groups have repeatedly condemned the Australian government for blatantly violating the human rights of migrant asylum seekers by keeping them in prison-like conditions on the islands for up to four years. Australian officials maintain that they are being tough in order to dissuade migrants from coming, thereby reducing the amount of human trafficking by boat and preventing more migrants from drowning at sea.

As of October 2017, more than 700 asylum-seeking men were held on Manus Island, where they waited for a decision from Australian officials about their applications and where they would go next. Another 400 or so displaced families, women, and children from countries such as Sudan, Iran, Afghanistan, Yemen, Myanmar, and Indonesia were held on Nauru with no resolution of their requests for asylum.[29] Living in physically challenging and mentally traumatic conditions, the asylum seekers have staged demonstrations and hunger strikes and even rioted. Based on its regular visits to Nauru and Manus Island, the UNHCR reported to the Australian Senate in late 2016 that conditions in the detention centers had contributed to the refugees' "mental health deterioration as well as self-harm, abuse and neglect."[30] More specifically, UNHCR medical experts who surveyed 234 refugees and asylum seekers found that more than 80 percent of them were suffering from depression or post-traumatic stress disorder.

Australian legal groups have sought to help the asylum seekers. In June 2017 the Australian government settled a class-action lawsuit filed on behalf of 1,905 current and former asylum seekers who claimed they had been falsely imprisoned and suffered physical and mental injuries. It agreed to pay the detainees $54 million in damages.

Before President Obama left office, he made a "one off" agreement with Australian Prime Minister Malcolm Turnbull that the United States would take in the asylum seekers from Nauru and Manus Island. President Trump blasted the agreement early in his administration, but the United States admitted 54 of the asylum seekers in October 2017 and agreed to allow in nearly 200 more in January 2018.

After the Supreme Court of Papua New Guinea ruled that the detention of refugees on Manus Island was illegal, Australia shut down the detention center in October 2017. By December 2017 hundreds of asylum seekers had been forced into an unsafe temporary transit center elsewhere on the island, waiting for officials in Australia to find countries where they could permanently resettle.

South Asia: The Rohingya

Since the 1970s the Rohingya Muslims in the western Rakhine state of Myanmar have been a heavily persecuted minority. The Burmese military periodically cracked down on them, causing hundreds of thousands to flee to neighboring countries. The Myanmar government has for many years denied them citizenship and legal rights.[31] Although the current round of military violence against the Rohingya began in October 2016, it did not reach a crescendo until after August 25, 2017, when the Arakan Rohingya Salvation Army (ARSA) attacked several dozen police outposts and an army base. The ARSA claimed that

its actions were justified in order to protect Rohingya from Burmese security forces.

Soon thereafter, state security forces and Buddhist mobs went on a rampage in Rakhine State. Within a week, tens of thousands of Rohingya were pouring into Bangladesh, describing massacres and torching of villages.[32] Within a month, Human Rights Watch had documented through satellite imagery the destruction of 284 Rohingya villages, and it estimated that 400,000 had already fled to Bangladesh.[33] Based on a survey it conducted in camps, Doctors Without Borders conservatively estimates that more than 6,700 Rohingya were killed in the first month after August 25, including at least 730 young children.[34]

By mid-December there were more than 630,000 refugees in Bangladesh, many of whom were placed in old refugee camps that already had almost 500,000 people in them, living in extremely poor conditions. Most are overcrowded with poor shelters comprised of bamboo poles and plastic sheeting for a roof. By December 2017 at least 240,000 displaced Rohingya were still in Myanmar, living precariously in temporary camps. Meanwhile, Myanmar authorities have blocked many IOs and NGOs from assisting in the care of the Rohingya people still in Myanmar.

Many aid agency officials claim that Myanmar security forces have committed crimes against humanity—murders, rapes, executions, forced population transfers and deportation, and persecution—as defined by the Rome Statute of the International Criminal Court. A top UN official and Human Rights Watch have suggested that organized, state-sponsored acts committed during the ethnic cleansing of the Rohingya people may constitute crimes against humanity, and possibly genocide.[35]

Myanmar state officials do not recognize the Rohingya as one of the legitimate "national races" of the country, thereby rendering them effectively stateless. Many human rights supporters are confounded by the behavior of the Nobel Peace Prize laureate and de-facto leader of Myanmar, Aung San Suu Kyi, who praised the military for "acting with great courage" and showed no sympathy for the Rohingya. Some former Western supporters of Suu Kyi believe that she has abandoned her principled position as an international champion of human rights, while others view her as a powerless president under the thumb of the military who is trying to preserve a chance for democracy in a country where the majority Buddhists deeply disdain the Rohingya.[36]

The Rohingya in Bangladeshi refugee camps are highly dependent on food aid and medical assistance from international organizations. Doctors Without Borders provides water and sanitation assistance and treatment for trauma related to sexual assault and rape. Its health clinics and other medical facilities treated more than 140,000 patients between late August and early December 2017. The IOM provides health care and sanitation assistance and also works to protect young girls and women from trafficking.

The global humanitarian organization Action Against Hunger distributes food and clean water daily in camps in the Cox's Bazar region of Bangladesh, where most refugees are living. It has screened tens of thousands of children for malnutrition and has admitted those in most dire straits to nutrition programs.[37] It works closely with UNICEF. The UNHCR provides clothing to refugees and delivers material to build better shelters. Local

Bangladeshi humanitarian groups also work with UN agencies, NGOs, and the Bangladeshi government to provide relief and vaccinate children. Given poor water and sanitation conditions, diarrheal illnesses and dysentery have been common.

It must be noted that Bangladesh is constructing a huge camp in Kutapalong next to the border with Myanmar where it plans to concentrate many Rohingya refugees. It also has plans to move some 100,000 to an uninhabited, flood-prone island in the Bay of Bengal. Nevertheless, the Bangladeshi government has kept its borders open to the Rohingya refugee seekers and insists that it respects their rights to health and work until they can be relocated. Despite their desperate needs, the Rohingya will need to move on at some point, but they really have nowhere to go.[38]

The situation of the Rohingya from Myanmar who fled to Bangladesh is another example of ethnic- and religious-based conflict in which there have been severe violations of human rights leading to killing and displacement of many people. Inadequately funded international humanitarian agencies have worked valiantly to meet some of the basic needs of the refugees, including their need for medical care and psychological treatment, but conditions in camps are still grim. What will happen to the stateless Rohingya if Myanmar won't take them back and Bangladesh doesn't want them to stay? Will they be warehoused in camps indefinitely, like so many other refugees around the world, or will they have the chance to integrate into Bangladeshi society or move to safety in developed countries? And how will the international community hold Burmese officials and military officers accountable for actions that have harmed so many people?

HEALTH CARE SOLUTIONS FOR REFUGEES AND OTHER DISPLACED PEOPLE

The health care problems of migrants and refugees are often interrelated with other structural problems such as the lack of development, lack of foreign and food aid, overpopulation, drought, and armed conflict. Most experts believe strongly that tackling health problems requires states, IOs, NGOs, and individuals to provide displaced people with physical and medical assistance. Our broad policy recommendations for refugees are these:

1. The problems of displaced people should be considered global health issues.
2. Economic development alone will not fix these problems, but promotion of long-term sustainable development will help significantly.
3. Food aid should be used in short-term emergencies and provided for as long as need exists.
4. Governments must ensure food security and should promote local, sustainable energy resources.
5. States and IOs need much more funding to provide short-term humanitarian aid to refugees and to them resettle.
6. Borders should be kept open to allow migrants to relocate where they will not be persecuted or treated inhumanely.
7. Although camps or "safe zones" are necessary temporary fixes during a crisis, in the medium term refugees require decent accommodations in an environment that allows for free movement and self-sufficiency.
8. States, IOs, and NGOs need to constantly reassess how technology-based interventions impact the social and economic well-being of refugees.
9. Refugees should have the right to return to their homes and recover their property; if these are not possible, refugees should be compensated for their losses.
10. The major powers should do more to resolve conflicts that cause peoples' displacement.

Paul Farmer also recommends some important policies to help poor and displaced people:

1. Institutions that the poor themselves identify as representing their interests should be favored.
2. All humanitarian organizations should do more to buy locally and hire mostly local staff.
3. International organizations should co-invest with governments to build strong civil services and work with them to provide cash to the poor.
4. International non-state service providers need to be better regulated.

We employ the four IPE frameworks to provide some political, economic, social, and ethical contexts for the proposals put forward above. Because the problems of the poor and displaced have complex political and socioeconomic causes, simple formulas such as more foreign aid, market liberalization, or providing people with netting to prevent mosquitos from spreading malaria are often not effective. As you read this last section in the book, consider which proposals for refugees you find most compelling and which IPE perspectives inform your views.

Economic Development

The record numbers of migrants from the Middle East and Africa fleeing to neighboring countries and Europe lead us to ask why development programs have often not been very successful and how they can be improved. In the 1950s and 1960s, many experts believed that if newly independent countries adopted Western-style economic and political institutions, economic growth and development would follow. But as we discussed in Chapter 11, there were many different possible paths to development and better population health that relied on many different kinds of institutions. Import-substitution industrialization and socialism in parts of Latin America and Asia were some of the alternative models.

In the late 1980s, neoliberalism gained popularity as globalization intensified. After the fall of the Soviet Union in 1991, some countries in East Europe, Latin America, and Southeast Asia did make economic gains under neoliberal policies, but many other developing countries ended up with more inequality, social divisions, and armed conflict that spurred migration. Many Afghanis, Rwandans, Mexicans, Salvadorans, Guatemalans, and Hondurans fled their homeland in the face of poverty and violence. By the 2000s, criticism of neoliberal policies was widespread, and strategies toward development and displaced people became less ideological and more pragmatic. IOs, NGOs, and even private enterprises played an increasingly bigger role in humanitarian relief.

New debates arose in the 2000s about how best to approach development as well as meet the needs of the world's most vulnerable people. Economist William Easterly popularized the argument that over-bureaucratized, inefficient, and sometimes corrupt IOs and NGOs often do little to help countries develop. He claims that UN and other public aid agencies often eat up billions of dollars in development assistance, and donors' domestic and foreign policy interests often lead them to channel foreign aid to countries that do not need it the most. He cites the example of African countries that have received massive foreign aid and yet remain in "abysmal straits," while those who received little to no aid are well on their way to development. He also does not like Western "planners" working on development from the top down. Instead, he would have foreign aid bypass state agencies and development organizations and go directly into the *private* sector where "searchers" such as Muhammad Yunus of microcredit fame invest it with local entrepreneurs.[39] In Figures 17.4 and 17.5, we provide data on how much official development assistance (ODA) is disbursed by the biggest donors among the OECD countries. In 2015, of the $106 billion in ODA from all OECD countries, 12.7 percent was humanitarian aid to developing

countries and 11.6 percent was assistance to refugees living in OECD countries themselves.

While economic development can certainly help all people in the long run, many development experts now recognize that it only *indirectly* mitigates displacement problems and does little in the short run to help displaced people with poverty, hunger, and health problems. In the humanitarian cases we analyzed in the previous section, the most urgent issue is what to do now when so many people are desperate for medical attention, food, water, shelter, and other basic essentials. Many experts also agree that although many of the poorer states receive foreign and food aid, they remain "failed" countries in all senses of the word.

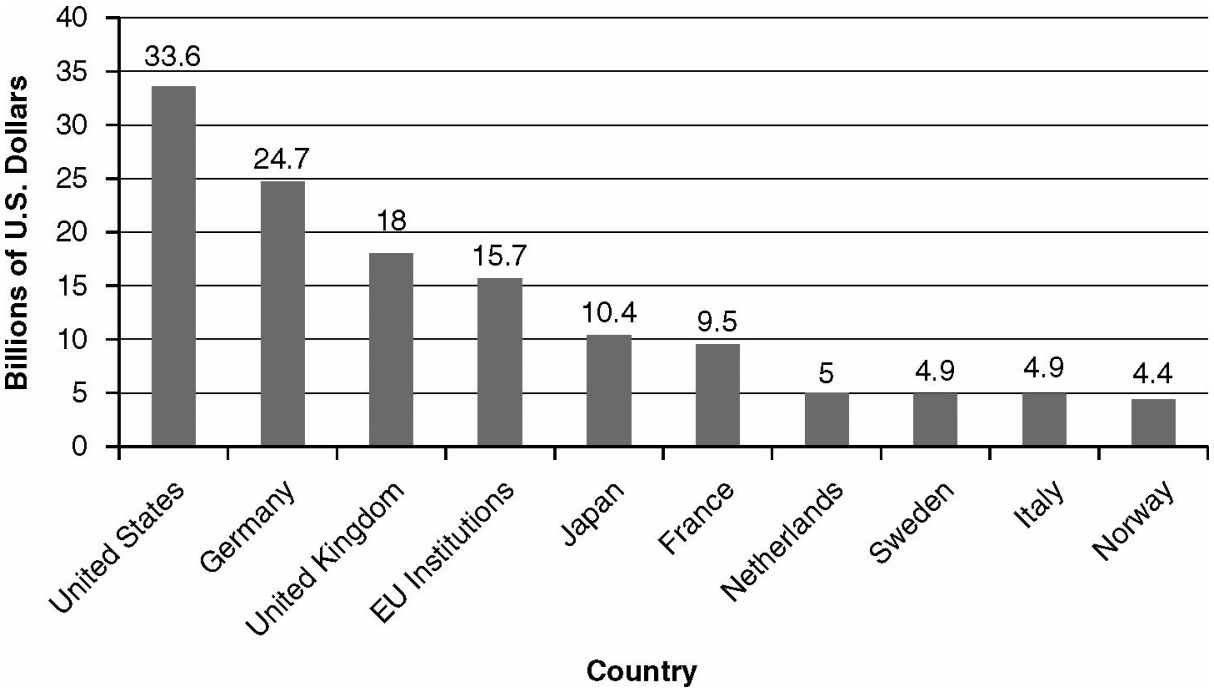


FIGURE 17.4
Disbursements of Net Official Development Assistance (in billions of current dollars), 2016

Note: Disbursements include bilateral and multilateral ODA.

Source: Data from Organisation for Economic Co-operation and Development, OECD.stat.

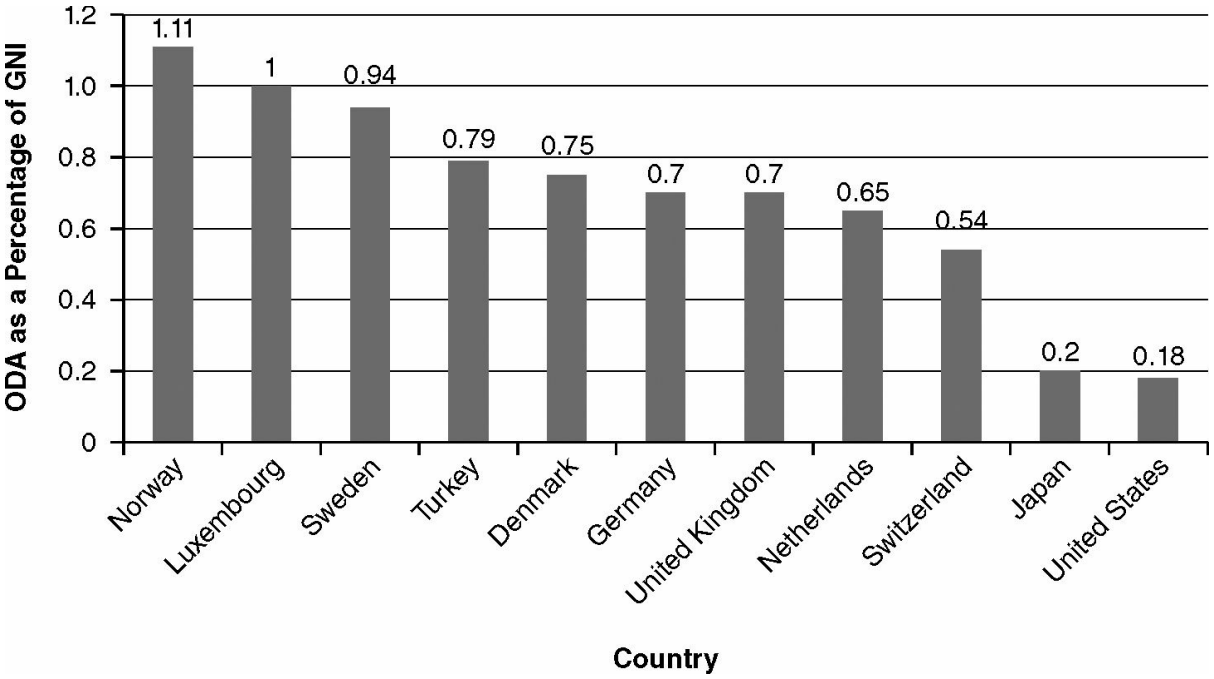


FIGURE 17.5
Official Development Assistance (ODA) as a Percentage of Gross National Income (GNI) among Largest Donors in the OECD, Japan, and the United States, 2016

Note: Disbursements include bilateral and multilateral ODA.

Source: Data from Organisation for Economic Co-operation and Development, OECD.stat.

Paul Collier puts forward a slightly different approach to economic development is his book *The Bottom Billion.*[40] The former World Bank director of research praises globalization for creating huge opportunities for about four billion people in developing countries, but he also criticizes it for leaving a billion people stuck in a poverty trap. The bottom billion are stymied by political, economic, and geographical problems that markets alone cannot overcome, including civil war, lack of natural resources, being landlocked, and corruption. To help solve these problems, Collier recommends some decidedly state interventionist policies, including: military intervention in some failed states to restore order, allowing for temporary trade protection, and setting up new international charters to promote norms and standards that help reformers in the poorest countries. He also firmly believes that the application of some Western agricultural technology will be necessary to boost food output in the poorest countries.

In contrast, U.S. economist Jeffrey Sachs has promoted development by focusing more directly on needy people. He was a special advisor to the United Nations Secretary General on the Millennium Development Goals, a UN initiative in 2000 designed to, among other things, dramatically improve health in poor countries and cut extreme poverty and hunger in half by 2015. In his best-known work, *The End of Poverty: Economic Possibilities for Our Time*,[41] Sachs criticizes IMF austerity policies that hurt the poor so much by promoting

privatization of health services and charging user fees for health and education. He argues that many environmental factors limit the effectiveness of aid, including droughts, hostile climate, mountainous terrain, and the lack of rivers or access to the sea. He also believes that development policies have to be tailored to the specific conditions in different countries.

Sachs doubts that promoting markets is the best way to help the poor. Employing the old economic argument that poor families are caught in a poverty trap, he wants to see foreign aid "overhauled into an efficient, transparent, and accountable system that effectively channels resources to the people who need them the most."[42] He decidedly wants better health care and more basic services for the poor. Toward these ends, Sachs promoted the "Millennium Villages" project in Africa, which included the distribution to the poor of non-indigenous hybrid seeds, fertilizers, and trucks to yield bumper crops that could end hunger. Although conditions in some of the Millennium Villages improved, the overall project was economically unsustainable and mostly failed to achieve its main goals.[43] Sachs now promotes the UN's new Sustainable Development Goals, adopted in 2015 and designed to promote a more holistic form of development from the bottom up that preserves natural resources and reduces social inequality (see Chapter 11).

Food Aid

In the 1950s and 1960s, hunger was viewed primarily as the result of overpopulation and inadequate food production in the "underdeveloped" nations. The solution seemed fairly simple: Western countries and UN "relief" agencies would provide food aid to help "fill in" until countries could "take off," grow enough to feed themselves, and continue to develop on their own.[44] It was not long before many realized that economic development would not be easy to achieve. In 1954, PL (Public Law) 480—the "Food for Peace" program—made U.S. food aid available to needy states, but as realists would point out, it was usually given to countries such as India and South Vietnam in pursuit of U.S. anti-communism foreign policy objectives. Food aid also prepared these states for future sales of U.S. commodities and helped accomplish the domestic objective of helping U.S. farmers clear away surplus production that was driving down the price of domestic commodities.

In the 1960s, the Ford Foundation and the Rockefeller Foundation supported research in Mexico and the Philippines for a "Green Revolution" that produced new high-yield varieties of wheat, rice, and corn that required less water and could survive in hostile growing conditions. Many experts, including Sachs, claim that the Green Revolution helped millions of people in developing nations avoid hunger. The Green Revolution required intensive use of fertilizers and pesticides, which caused health and environmental damage. Later, economic liberals argued that it was rational for a country just to import food if it lacked a natural comparative advantage in food production. However, many structuralists criticize the Green Revolution for introducing to Third World nations a U.S. model of agricultural production that is heavily dependent on capital, chemicals, and water.[45]

In 1973 and 1974, world commodity production plummeted in many of the world's biggest agricultural countries, contributing to starvation in Ethiopia and elsewhere and generating major concern about a "world hunger" problem. Mass starvation was triggered by drought in east Africa and monsoons and civil war in Bangladesh in 1974. In response to growing concern about the food crisis, the biologist Garrett Hardin published his famous work on "lifeboat ethics" in which he argued that it was ethical to let the hungry in developing nations die rather than give them aid that would not sustain them over the long run. Overpopulation was threatening the ability of commodity producers to keep up with demand. The solution: governments must *impose* population control on their societies and cut off food aid to the starving, all of whom were trying to climb onto the rest of the world's lifeboat.[46]

Many critics argued that even if the world did have a finite amount of resources, the earth had not reached the point where there were just enough resources available for a certain number of people to live comfortably while others perished. Critics asked: Must those in the industrialized nations live as lavishly as they do compared to people in developing nations? Should not the "haves" share more with the "have-nots"? How can the major commodity producers such as Canada, the United States, and the EU justify their huge surpluses while so many people in the developing regions of the world were malnourished or starving?

In the 1970s, the structuralist-oriented Food First movement led by Frances Moore Lappé and Joseph Collins criticized these arguments about food aid and shifted the focus of the hunger problem to political and economic factors that determined who would eat how much and at what price.[47] Along with many structuralists, they argued that some states had become dependent on food imports and food aid instead of using their scarce financial resources to produce food for themselves. Imported and donated food also drove down domestic food prices and acted as a disincentive for domestic producers, who left rural areas to settle in urban slums, adding to the growing number of displaced people. Lappé and Collins recommended that aid-dependent states cut themselves off from the industrialized states and adopt Food First or "self-reliance" production methods. Self-reliance would also enhance the political and economic independence of developing nations and limit the influence of international agribusiness corporations and protectionist trade policies in the West.

Throughout most of the 1980s, the Sahel, Southeast Africa, and South Asia experienced several rounds of mass starvation and hunger. Many states in Africa also had to deal with drought and high rates of HIV infection and other diseases. Private organizations, including World Vision, MSF, and Oxfam, were often unable to do much to halt the spread of hunger and the medical issues that came with it. This decade also saw a shift in emphasis from mainly increasing commodity production to acceptance of the idea of "food security," which the FAO defines as existing "when all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food that meets their dietary needs and food preferences for an active and healthy life."

As globalization took off in the mid-1980s, the United States and some other developed

countries ardently promoted "trade, not aid" as a means for development, which they hoped would help stem the flow of migrants out of poor nations. In 1992 the United States once again used food aid to serve both ethical and strategic objectives, this time by sending a military force (backed by a UN resolution) into Somalia to feed millions of starving people during a civil war. Following an ambush that killed seventeen U.S. soldiers, the multilateral force withdrew and Somalia became a prime example of a yet another "failed state" suffering hunger, famine, instability, and war.

In 1996, the FAO sponsored a World Food Summit in Rome, where 187 states pledged to reduce the number of hungry people in the world by half within twenty years. This development (and health) objective became the basis of the Millennium Development Goals of 2000. Interestingly, by 2015 the *proportion* of the world's population that was malnourished had dropped by half even if, but the *absolute number* of hungry people only fell from 991 million in 1990 to 780 million in 2015.[48]

In the late 1990s, the goal of "food sovereignty" started to become popular in poorer parts of the world, especially in Latin America. It means the right to produce one's own food on one's own territory, but also the right to decide for oneself what to produce and by what methods.[49] Food sovereignty emphasizes collective, not individual, property and the rights of peasants and indigenous peoples to access land, reject genetically modified seeds, farm sustainably, and produce healthy foods for the local market. The norm poses a challenge to the energy-intensive, agro-industrial, export-oriented food system and those who benefit from it, such as large landowners and TNCs that sell patented seeds and chemicals. Many states have enacted the concept into laws, even if governments of some of the largest food exporters such as the United States, Canada, Brazil, and Argentina tend to be most resistant to the norm.

Unexpected food shortages between 2005 and 2012 helped generate another world food crisis and helped clarify the relationships between food aid, hunger, and health. Dramatic spikes in world food prices in 2008 and 2011 were not due to real production shortages as much as to a perfect storm of factors including speculative investment, income growth in emerging economies, biofuel production, and the persistence of drought, famine, and war. Record-breaking drought in 2012 in the U.S. breadbasket demonstrated that the global food system had become more vulnerable to environmental shocks, with potentially dramatic effects on the price and availability of food, especially for the world's poorest people.

The 2008 financial crisis also led to dramatic cutbacks in food aid. Financial speculation in commodity production pushed investors in countries such as China, the United Arab Emirates, South Korea, the United Kingdom, and the United States to buy up commodity-producing land in countries such as Sudan, Indonesia, the Philippines, Tanzania, and the Democratic Republic of the Congo.[50] Other influences on global food production and distribution were the use of agricultural commodities to make biofuels and the wider cultivation of genetically modified crops that reduce water usage and maintain soil fertility. The biggest failures in relieving hunger continued to be in sub-Saharan Africa, where high-yield cereals have not produced as much increased output as elsewhere. Moreover, although

there has been some success in reducing the number of deaths from malaria, diarrheal illnesses, and HIV/AIDS, these and other communicable diseases are still widespread in many poor countries.

The Influence of Individuals

The connection between war, hunger, and diseases is obvious. People who are hungry are least likely to respond to medication, if they can afford it. When societies and their governments collapse, calamities are most likely to result. But unlike in previous decades, academics and global health practitioners today are taking a more critical look at the role of nonstate actors such as corporations, charities, and individuals. In an increasingly globalized world, the state is only one level at which to analyze health outcomes.

Individuals who provide medical information in the field about diseases and hunger are also important global health actors. Constructivists would also remind us how much certain people, including relief workers and doctors, can shape our beliefs about refugees and the displaced. In the 1950s one such person was Dr. Tom Dooley, who worked in Laos and became a source of inspiration for many. Today many motion picture stars and musicians frame health and refugee issues in ways the public can relate to and that generate support for certain policies.

A particularly influential individual today is Dr. Paul Farmer, an anthropologist, physician, and humanitarian who provides health care in poor developing countries. He co-founded "Partners in Health," an organization that focuses on international social justice and health. Farmer's personal mission derives from his sense of medical and moral duty. A university professor at Harvard University, he currently lives with his wife and three children in Kigali, Rwanda, where he practices internal medicine and heads up a project to fight infectious diseases. He is committed to the idea of "accompaniment," which means "supporting developing country partners—public and private—until they have the capacity to deliver services and improve livelihoods in the long term."[51] Foreign contractors and NGOs work together to promote projects of all kinds, "adapting to the local context" and "following the lead of local partners."[52] Thus, Farmer recommends doing as much as possible to support local jobs, education, and health care.

Another influential person is the philanthropist Bill Gates, a co-founder of Microsoft who, now in retirement, is very active in global health. Along with his wife Melinda, he has brought attention to many health and development problems and inspired other wealthy philanthropists to support global health programs. His influence is channeled through the Bill and Melinda Gates Foundation, which he founded in 2000. With an endowment of over $40 billion, it is the world's largest private funder of global health programs. It also funds research to develop new vaccines. In 2016 it spent $2.9 billion on health initiatives mostly focused on preventing infectious diseases and improving the health of children and newborns in poor countries. It now spends more each year than the WHO. It is also ramping up spending to help tens of millions of poor women gain better access to contraceptives. Structuralist Jacob Levich criticizes the Gates Foundation as representative

of today's "Big Philanthropy" that runs roughshod over poor countries' national sovereignty and "underwrites vertical initiatives potentially profitable to Western-based transnational corporations—for example, vaccines and other pharmaceuti-cals—instead of supporting primary care and strengthening national health systems."[53] In contrast, Chelsea Clinton and Devi Sridhar defend the Gates Foundation, contending that it has clearly "played a vital role in global health and can aptly claim credit for saving untold lives, including through its strong support of Gavi."[54]

U.S. president Donald Trump is now also influential; he is trying to change the norms and values related to U.S. foreign aid and refugees. He has proposed cutting U.S. foreign aid by 31 percent in 2018, even though current annual U.S. foreign aid of more than $30 billion is less than 1 percent of the U.S. federal budget. For former presidents, foreign aid was one of the key pillars of U.S. soft power, designed to showcase U.S. values and leadership, help lift millions out of poverty, promote development, and achieve national security objectives such as combating terrorism, particularly in the Middle East and Africa. Yet Trump rarely mentions the need to promote poverty reduction, human rights, or social justice values. He argues that it is time for the United States to invest in its own infrastructure and "stop sending aid to countries that hate us."[55]

According to Andrew Natsios, former head of the U.S. Agency for International Development (USAID), Trump is clearly demonstrating that the United States is withdrawing from an active leadership role in the world.[56] Natsios believes that Trump is making a serious mistake to overlook threats to U.S. national security interests

> such as the spread of infectious diseases such as Ebola and Zika; the threat of radical Islamist terrorist movements across North Africa, which are destabilizing to our friends and allies; the mass-migration crisis that is changing the face of American and European politics; an aggressive and expansionary Russia that's preying on weak states, such as Ukraine; and the growing number of fragile and failing states.[57]

CONCLUSION

In this chapter we dealt with three interrelated issues: IPE outlooks on global health; the broadly defined health conditions of displaced people and refugees from Syria, South Sudan, Myanmar, and on two South Pacific islands; and proposals to deal with refugee health issues.

Global health is increasingly receiving needed attention from academics and global governance officials. Health issues need to be seen as interconnected with development, food policy, and armed conflict. They should be examined all the way from the level of individuals in refugee camps to the global level of analysis. States are not the only providers of global health solutions; doctors, researchers, community groups, philanthropists, corporations, IOs, and NGOs also have important roles to play in improving the physical and mental health of the poor and displaced. All of these actors are working in an increasingly integrated manner to mitigate poverty and find more systemic solutions to problems of food insecurity, drought, and overpopulation.

Finally, we would like to add that the lack of justice and humane treatment for many displaced and distressed people remains a problem in itself. Violations of international humanitarian law with impunity threaten global security and the legitimacy of international norms. In many conflicts today we have seen egregious human rights abuses, which leading powers have done little to stop. Regrettably, under President Trump the United States is returning to a policy of isolation and accepting that we live in a world that treats its people poorly—when, in fact, caring for the forgotten is part of the essence of humanity. Other countries are doing a better job of this—and we hope that all of us, as global citizens, will rise to the occasion and help to lift the fortunes of others around the world in the years to come.

KEY TERMS

migrants 466
refugees 466
displaced people 466
internally displaced people (IDPs) 466
United Nations High Commissioner for Refugees (UNHCR) 466
asylum seekers 467
World Health Organization (WHO) 469
Bill and Melinda Gates Foundation 471
development assistance for health (DAH) 471
White Helmets 476
Manus Island 478
Food for Peace 484
Green Revolution 485
lifeboat ethics 485
Food First 485
food security 486
food sovereignty 486
accompaniment 487

DISCUSSION QUESTIONS

1. Outline several ways in which global health interconnects with IPE. Discuss some of the ways in which one helps "reimagine" the other.
2. Choose one of the four cases about refugees and outline some of the policy issues that the four IPE perspectives would highlight in that case.
3. Which policy outlook on foreign and food aid do you prefer: that the developed nations should provide more or less relief to developing nations?
4. Which of the 14 policy recommendations for refugees do you like the most? Explain using examples from the reading.
5. Read the last paragraph of the chapter again. Do you agree with the authors' assessment about values, norms, and human rights in the global political economy today? Explain your answer with references to any chapter in the textbook.

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GLOSSARY

Accompaniment An approach to improving health care in poor countries that Paul Farmer has popularized. It encourages foreign health organizations to build long-term partnerships with governments and communities in poor countries in order to strengthen their local and national health care systems and improve social conditions of the poor that profoundly shape health outcomes.

Accumulation by dispossession A term coined by Marxist geographer David Harvey to describe a predatory process by which public and communal assets are transferred to private ownership and control. In this process capitalists use fraud, theft, and predatory practices to accumulate assets. Mechanisms of dispossession include land seizures, indebtedness, privatization, and intellectual property rights.

Anti-kleptocracy norm A global norm that obliges states to prevent corrupt money from entering their financial system and to return corrupt money to the countries from which government officials stole it.

Appreciation A term used in foreign exchange markets to describe the rise in value of one currency relative to another. Currencies tend to appreciate when the demand for them increases. If a country's currency appreciates too much, it will cause that country's exports to decrease. See *Depreciation*.

Arab Spring Protests and popular uprisings that started in Tunisia and spread to Egypt, Libya, Syria, Yemen, and several other Arab countries in 2011, causing regime changes and/or sparking civil war.

Arbitrage Buying a product in a lower-price market in order to sell it in a higher-price market. When a state's laws, taxes, and regulations make the price of a good in its country much higher than in neighboring countries, smuggling tends to occur.

Asian Infrastructure Investment Bank (AIIB) A Chinese-led multilateral financial institution established in 2016 that funds large energy, transportation, and infrastructure projects in Asia. With more than fifty countries as members, the AIIB is viewed as a mechanism for China to expand its influence in Asia and as a rival to the Western-controlled World Bank and the Japanese-led Asian Development Bank.

Asylum seekers Displaced people who cannot return to their home country because of fear of persecution on account of their race, religion, nationality, membership in a particular social group, or political beliefs. Asylum seekers apply for permanent residence in countries other than their own.

Austerity Deep cuts in government spending— especially during a recession—designed to reduce a government's budget deficit or free up resources to repay debts to creditors.

Austerity policies typically include increased taxes, layoffs of state workers, and reductions in spending on public goods, social programs, and pensions that disproportionately hurt the poorest segments of society.

Balance of payments (BoP) A financial tabulation of all international economic transactions between a nation and other nations in a given year. These transactions are recorded in a nation's current account, capital account, and financial account. How much money flows into or out of a country annually impacts the value of its currency, interest rates, and trade policy, among other things. Ideally, countries would earn as much as they spend.

Balance of power A popular and controversial realist theory that ascribes to states a certain amount of strength and influence based on a variety of tangible and intangible factors. In theory, states cluster (or ally with one another) based on shared national interests — in opposition to states with conflicting interests. Peace among nations is usually associated with an *approximate equilibrium* in the distribution of power between nations in this system. This distribution of power results in a bipolar (2), tripolar (3), or multipolar (3+) structure. Others argue that peace is achieved when a hegemon, or dominant power, orders the security structure—referred to as unipolarity or hegemony.

Balloon effect A phenomenon when a crackdown on drug production or trafficking in one place simply causes it to pop up in another place instead of disappear.

Bancada ruralista A powerful rural caucus in Brazil's Congress that represents the interests of large agricultural landowners and often opposes the interests of environmentalists and indigenous peoples.

Base erosion and profit shifting (BEPS) A term describing tax avoidance strategies whereby corporations and investors shift their profits to jurisdictions with low tax rates. OECD countries are trying to limit these strategies so that corporations pay more taxes in the countries where they actually conduct most of their normal business activities.

Beijing Consensus The Chinese model of economic development combining authoritarian, one-party rule and capitalism while preserving substantial state intervention in the economy and large state-owned enterprises in strategically important industries. China presents this mercantilist model to other developing countries as superior to the economic liberal "Washington Consensus" promoted by the IMF, the World Bank, and Western countries.

Belt and Road Initiative A Chinese foreign policy initiative launched in 2013 to fund tens of billions of dollars' worth of new infrastructure projects in Central Asia and in cities along the coast of the South China Sea and the Indian Ocean. It is viewed as a plan to tie Asian economies closely to China, boost Chinese exports, and expand Beijing's geopolitical influence. Also called the "One Belt, One Road Initiative" and the "Silk Road Economic Belt and the 21st Century Maritime Silk Road Initiatives."

Benign mercantilism A defensive strategy through which a state seeks to protect the domestic economy against damaging international political and economic forces. What one nation intends as benign can be interpreted by another as malevolent (hostile).

Bill and Melinda Gates Foundation A private foundation founded by Bill and Melinda Gates and headquartered in Seattle, Washington. With an endowment of over $40 billion, the foundation funds major international health initiatives, including efforts to eliminate malaria and limit the incidence of HIV/AIDS and tuberculosis in developing countries.

Bipolarity The condition of an international security structure that is managed by two centers of power. Theoretically, each dominant state or "pole" and those states in its "sphere of influence" compete with others to keep the distribution of power relatively equal between them.

Bolsa Família A widely praised Brazilian antipoverty program begun in 2003. The Brazilian federal government provides low-income families a monthly cash grant on the condition that their children attend school and get regular medical care and required vaccinations.

Boomerang pattern A process in which an advocacy group in one country works with transnational civil society to lobby the governments of other countries to pressure the advocacy group's government to conform to a norm.

Bourgeoisie In Marxist analysis, the bourgeoisie is the capitalist class, made up of those who own the means of production. In everyday language, this term often refers to the wealthy and cultural elites of society who have the preponderance of political power.

Brain drain The exodus of highly educated, professional migrants out of their country of origin toward economic or social opportunities in another country.

Bretton Woods system A set of international institutions created during meetings in July 1944 among representatives of the Allied Powers of World War II (including the United States, Britain, France, Canada, the Soviet Union, and many smaller states). The Bretton Woods agreements created the International Monetary Fund and the International Bank for Reconstruction and Development (which later became part of the World Bank) with the goal of maintaining a stable international financial and monetary system. With the creation in 1946 of the General Agreement on Tariffs and Trade, which many scholars consider the third pillar of the Bretton Woods system, the victors in World War II had established a liberal economic order.

Brexit An abbreviation of "British exit," which refers to the United Kingdom's decision in 2016 to leave the European Union. Negotiations between the UK and the EU over their post-Brexit relationship began in 2017. Britain's official withdrawal from the EU is expected in March 2019.

BRICS (Brazil, Russia, India, China, and South Africa) An acronym for five emerging market economies with large populations and prospects for becoming major global or regional powers in the coming years. The countries, which often coordinate policies in international organizations, established a New Development Bank to fund infrastructure projects in developing countries.

Cap and trade A controversial mechanism introduced in the Kyoto Protocol that permits countries to buy and sell carbon emissions allowances in the international market or swap

them with one another. States would not be allowed to go over their carbon emissions cap without purchasing (or trading for) a portion of another state's emissions quota. Some states have also set up their own national cap and trade programs.

Capital controls Government regulations that limit flows of money and investments into or out of a country. The goal of capital controls is to maintain orderly international capital movements and prevent financial and foreign exchange instability.

Capital mobility The relatively unrestricted movement of money and financial assets into and out of a country.

Carbon sinks Typically, forests and large bodies of water that absorb considerable amounts of carbon dioxide from the atmosphere. Planting forests became an acceptable method of offsetting carbon emissions for countries that are party to the Kyoto Protocol.

Carbon tax A controversial policy that levies a tax on the amount of carbon produced by an industry or nation-state, thereby requiring air polluters to pay more for the negative effects of carbon-based energy and giving them an incentive to switch to renewable energy sources.

Cartel A group of firms or nations that cooperate with one another to control the production level and price of a commodity that has a limited number of supply sources. The Organization of Petroleum Exporting Countries (OPEC) is an example of an oil cartel that in 1973 drove up the price of oil to punish states that supported Israel during its Six-Day War with Arab states.

Chlorofluorocarbons (CFCs) CFCs are compounds of atoms of chlorine, fluorine, and carbon found in cleaning solvents, refrigerants, and aerosols. They are known to deplete the ozone layer around the earth and to contribute to global warming.

Civil society Relatively autonomous organizations in society that represent the interests of citizens, engage in civic activities, and sometimes serve as a counterforce to government. It includes religious institutions, nongovernmental organizations, labor unions, and the private media.

Classical mercantilism State policies that historically focused on intentionally gaining national wealth and power at the expense of other states. These measures included export subsidies, import barriers, and other efforts to generate trade surpluses and protect domestic producers.

Classical realism A theory that asserts that the most important actors in international relations are states, which cause wars and international conflicts as they promote their national interests and seek to enhance their power over other countries.

Climate Change An increase in the temperature of the earth's atmosphere due to human activity. Some contest the scientific evidence of warming.

Cold War A phrase first used by Bernard Baruch in 1948 to describe the military and political confrontation between the United States and the Soviet Union and their respective allies that did not turn into a (hot) military conflict, many theorists argue, because of the devastation associated with the use of nuclear weapons. Nonetheless a period of great

tensions and *threats* to use military force.

Commercialization of sovereignty The process whereby a state sells commercial privileges, diplomatic passports, and other protections to citizens and companies from other states.

Committee on Foreign Investments in the United States (CFIUS) A U.S. government inter-agency committee that assesses the national security implications of specific foreign investments in U.S. companies. When a foreign person or foreign company (especially one controlled by a foreign government) seeks to buy part or all of a U.S. company, CFIUS determines if the foreign buyer might gain control of advanced technology, classified information, critical infrastructure, or military-related assets that would impair national security. If so, CFIUS can prevent the foreign merger, acquisition, or takeover of the U.S. company.

Common Market A level of economic integration in the European Community (now the EU) beyond a customs union. A common market promotes the freedom of movement of capital, labor, goods, and services. Until the 1990s, the common market was also the popular name of what was essentially the European community.

Compulsory license A license that a government grants to a local private company or state agency to produce and sell a good under patent, often without the permission of the patent holder, in order to lower the price of the good or increase its supply. International agreements give governments the right to issue compulsory licences in specific circumstances.

Conditionality Politically sensitive conditions that the International Monetary Fund attaches to short-term loans that it gives to government borrowers. The conditions often require states to implement domestic economic reforms, cut government spending, and increase taxes, with the aim of improving *current account* balances. See *Structural Adjustment Policies*.

Conspiracism A political culture widespread in Iran and Arab countries that blames covert Western and Israeli manipulation for regional and national problems. Some scholars worry that this mind-set encourages extremism by engendering permanent suspicion toward the West and Israel.

Constructivism A school of thought in international political economy that focuses on the beliefs, ideas, and norms that shape the interests and actions of state officials and international institutions. States are not only political actors, but also social actors insofar as they adhere to rules and norms that reflect society's values. Norms and identities are not static but are the result of ongoing social construction; they influence the relationships between states.

Contagion The spread of a financial crisis from one national economy to other national economies through international linkages such as currency, money, commodity markets, and shifting market psychology.

Convention on International Trade in Endangered Species of Wild Fauna and Flora

(CITES) An international treaty that entered into force in 1975 that requires states to regulate imports and exports of specific plants and animals in order to reduce the likelihood that they will become endangered or extinct.

Copyrights Government-granted rights to producers of books, movies, television programs, music, photographs, and software to prevent others from reproducing or publishing their work without permission.

Core A term used in modern world system analysis in reference to the developed capitalist part of the global economic system, also known as the North. The *periphery*, or South, refers to the less developed regions of the system.

Corn Laws British protectionist trade barriers on imported grains from 1815 to 1846. The high tariffs benefited domestic farmers and landed elites but caused the price of food to be high. When manufacturing interests gained control of Parliament, the Corns Laws were repealed, signifying the emergence of economic liberal ideas about free trade.

Corporate social responsibility Practices of TNCs and domestic businesses that demonstrate respect for communities, social needs, and the environment. Corporations often voluntarily adopt these practices because they generate business for the corporations and enhance their reputation.

Council of Europe A European intergovernmental organization created in 1948 to protect parliamentary democracy and human rights. It is independent from the EU and has 47 member states.

Council of the European Union Also called the Council of Ministers. The main lawmaking body of the EU, composed of a single representative from each member nation. The Council decides European legislation often in cooperation with the Commission and the Parliament. Its most important decision-making powers are in foreign policy, fiscal policies, and economic policies.

Countervailing duty A duty that a government imposes on imports to offset the subsidies that another government gives to its exporters. Designed to protect domestic companies from unfair import competition.

Cuban Missile Crisis A two-week confrontation in October 1962 between the United States and the Soviet Union that brought both countries to the brink of nuclear war. After U.S. President John F. Kennedy ordered the Soviet Union to remove medium- and intermediate-range nuclear missiles from Cuba and ordered a naval blockade of the island, a tense standoff ensued. It ended when the Soviet Premier Nikita Khrushchev agreed to withdraw the weapons (and the United States secretly withdrew Jupiter nuclear missiles from Turkey).

Customs union A group of nations that agree to eliminate trade barriers among themselves and adopt a unified system of external trade barriers. The Treaty of Rome created a customs union in the form of the European Economic Community.

Data localization A legal provision requiring that personal information about citizens or residents of a country be processed and stored in that country only and not transferred

outside its borders. Restricting companies from transferring sensitive data about a country's citizens—like financial, medical, and educational records—to other countries is partly designed to reduce cybercrime and boost personal privacy.

Debt service ratio The ratio of a country's annual payments of principal and interest on foreign debt to the country's annual export earnings. Countries with high debt service ratios cannot sustain them for very long and have to reschedule the debt, seek loan forgiveness, or secure new loans to cover payments on previous loans.

Deemed export controls U.S. government regulations requiring universities and companies doing business in the United States to obtain a license before allowing a non-U.S. person access to certain technology or information. These mercantilist-type controls are designed to prevent foreign nationals (especially those who are scholars, students, or company employees) from accessing advanced technology and intellectual property related to, among other things, U.S. national security, nuclear weapons, advanced computing, and chemical and biological warfare.

Defense Advanced Research Projects Agency (DARPA) A U.S. Department of Defense agency that funds cutting-edge research into new technologies with potential military applications. Created at the height of the Cold War in 1958, the agency funded programs that produced the Internet, GPS, drones, and other technologies that are the basis of many modern industries.

Defensive modernization Efforts by the Ottoman Empire and some Arab rulers in the nineteenth century to catch up with Europe's growing imperial power by reorganizing their government, military, economy, legal system, and other institutions.

Demographic dividend The future accelerated economic growth expected when a country such as India or Turkey transitions to having a population in which the share of healthy working-age individuals is larger than the share of children and the elderly.

Demonetization An Indian government program begun in late 2016 that removed high-value currency notes from circulation. By stripping 1,000- and 500-rupee notes of their status as legal tender, the government aimed to crack down on black market wealth and increase tax revenues.

Dependency theory A theory of the relationship between industrialized (*core*) nations and less developed (*periphery*) nations that stresses how the many linkages between them make less developed countries dependent on and subordinate to richer nations. These linkages include trade, finance, and technology.

Depreciation A term used in foreign exchange markets to describe when the value of one currency falls relative to the value of another currency. See *Appreciation* and *Devaluation*. Currency depreciation can be both a benefit and cost to a nation. It tends to cause an increase in a nation's exports, and it makes imports more expensive.

Détente A period of relaxing of tensions and improved relations between two adversarial powers. Détente between the United States and the Soviet Union started in 1969 and reached its high point from 1972 to 1975 when the two countries signed arms control

agreements and the Helsinki Final Act, which reduced mutual threats in Europe. Détente ended after the Soviets invaded Afghanistan in 1979.

Deterrence Preventing an opponent from initiating a war by threatening them with unacceptable consequences (massive destruction) if they launch an attack. During the Cold War, both the United States and the Soviet Union maintained their security through deterrence because each could credibly threaten to devastate the other if it launched a nuclear first strike.

Devaluation Also termed currency depreciation. The process in which a government deliberately reduces the value of its domestic currency relative to the value of foreign currencies. Devaluation increases the prices of imported goods, while making exports relatively less costly for foreign buyers.

Development assistance for health (DAH) Financial aid that multilateral development agencies and wealthy countries give to low- and middle-income developing countries for disease treatment and prevention and health promotion.

Developmental state An interventionist government that uses financial, fiscal, and investment policies to foster rapid industrialization. Its bureaucracy guides private sector investments, supports industries most likely to promote national development, and encourages exports by private companies. The term is usually used to describe four post-World War II Asian states: Japan, South Korea, Taiwan, and Singapore.

Dialectical process A process whereby contradictions between two conditions or opposing forces result in something new. A thesis, countered by its antithesis, produces a synthesis of the two. This idea was made popular by Karl Marx, who believed that history unfolded through a dialectical process, with the conflict between capital and labor driving the process today.

Discourse analysis A method used by constructivists to trace changes in language and rhetoric in the speeches and works of important actors at the state or international level. The focus is mostly on officials who talk their state's interests into existence, sometimes by adopting a discourse that resonates with an important lobbying group or sector of public opinion.

Displaced people People who have fled from or been forced out of their homes—often because of war, famine, or natural disaster. They may be displaced to a foreign country or to another area in their own country.

Dispute settlement panels Panels of the World Trade Organization composed of three impartial trade experts who rule on trade disputes. After a panel rules that a WTO member state has violated WTO rules, if that member state does not change its policies to comply with the panel's recommendations, the WTO can authorize trade penalties against it.

Dodd-Frank Act Regulations the U.S. Congress passed in 2010 in response to the Great Recession to prevent another financial crisis. The Volcker rule, for example, named after Paul Volcker, a former chairman of the Federal Reserve, prohibits banks with federally insured deposits from engaging in proprietary trading, i.e., making risky investments with

their own money, and limits how much these banks can invest in hedge funds and private equity funds.

Doha Round Officially called the Doha Development Round. Trade negotiations between WTO members that began in 2001 and that aimed to lower tariffs on manufactured goods and reduce trade barriers in sensitive areas such as services and agriculture. The frequently deadlocked negotiations ended in 2015 without a new multilateral trade agreement.

Drones *See unmanned aerial vehicles (UAVs)*.

Dual use technologies Products and technologies that are primarily for civilian and commercial use but which also have military applications. Many governments prevent companies from exporting sensitive dual use technologies without a license.

Dumping When an exporter sells a product to a foreign country for a price below the normal market price, often with the purpose of gaining more market share.

Earth Summit The 1992 meeting in Rio de Janeiro—officially titled the UN Conference on the Environment and Development—that focused on ways to sustain economic development while preserving the environment. At the meeting, 153 states signed the UN Framework Convention on Climate Change, an agreement on cutting greenhouse gas emissions that resulted in the Kyoto Protocol in 1996.

Economic and Monetary Union (EMU) Also called the Eurozone. The agreement of many European countries to adopt a common currency—the euro— which was introduced in 2002. There are 19 members of the Eurozone. Since the global economic crisis, some states have reconsidered whether it is beneficial to stay in the EMU.

Economic citizenship When a government offers citizenship or permanent residency to foreign nationals on the condition that they invest a minimum amount of money for specified purposes in the country.

Economic liberalism The ideology and IPE perspective that holds that nations are best off when the state's role in the economy is minimized. Economic liberalism derives in part from fear of state abuse of power and in part from the philosophy of individualism and liberty of the Enlightenment. Economic liberal ideas have been popular since the late 1970s and served as the foundation for the policies associated with globalization.

Economic nationalism A mercantilist philosophy promoting state intervention in the market in order to increase national wealth and power. Alexander Hamilton and Friedrich List are two famous proponents of economic nationalism. The term also refers to a people's sense of economic loyalty to their nation-state.

Economic union A degree of economic integration that goes beyond that found in a customs union. An economic union eliminates both tariff and nontariff barriers to trade and finance among a group of countries. It also delegates a good deal of political and economic authority to a central political agency or group of institutions. See the *European Union (EU)*.

Embedded liberalism Under the Bretton Woods economic system, democratic states

would intervene in their domestic economies and place some limits on international markets to protect society, but they would also support a liberal international system that brought down trade barriers and allowed freer flows of finance between countries.

Emerging economies Developing countries with large populations, sustained high rates of economic growth, considerable industrialization and foreign investment, and market-oriented policies. They include China, India, Indonesia, Malaysia, Mexico, the Philippines, Thailand, Vietnam, Argentina, and Brazil. By the late 2000s, many of these nations played an increasingly large role in international institutions. Also called *emerging market economies* and *emerging markets*.

Epistemic communities Networks of experts with authoritative knowledge on particular international problems who often frame the problems for policy makers and the public, explain their causes and effects, and offer solutions to them. For example, an epistemic community has mobilized around the issue of global climate change, with many scientists, nongovernmental organizations, and the media bringing attention to the threat and advocating solutions.

Ethical poverty line (EPL) Peter Edward defines it as the minimum income an average person needs to earn in order to have a normal lifespan (approximately 70 years). Today's EPL is variously estimated to be between $4 and $7.40 per person per day (in purchasing power parity).

Eurasian Economic Union (EEU) A Russian-led economic union created by treaty in 2014. Members include Russia, Belarus, Kazakhstan, Kyrgyzstan, and Armenia. Although economic cooperation is limited in the union, Russia sees the organization as a means to strengthen its regional hegemony.

European Central Bank (ECB) Established in 1998, the ECB works with national banks to define and implement the single monetary policy of the Eurozone. It conducts foreign-exchange operations and manages foreign reserves with the objective of promoting financial stability.

European Coal and Steel Community (ECSC) A supranational authority established in 1952 by France, West Germany, Italy, and the Benelux countries to govern their coal and steel industries. It was hoped that this initial economic integration in Europe would make another war unlikely.

European Commission An executive body created in 1967 whose commissioners are appointed by EU member states but who are not responsible to them. Commissioners propose new laws, make budget proposals, and run the day-to-day operations of the EU.

European Economic Community (EEC) The first European "Common Market," originally with six members: France, West Germany, Italy, Belgium, the Netherlands, and Luxembourg. Created by the Treaty of Rome in 1957, the EEC reduced trade barriers amongst its members and established a common tariff to protect its producers. In 1967, the EEC merged with the European Coal and Steel Community and the European Atomic Energy Commission to become the European Community.

European Parliament (EP) An institution unlike a traditional parliament. Its elected representatives from EU member states sit with their peers from the same party in other states, rather than with their national colleagues. The EP helps draft policy programs and European legislation, cooperates with the Council of Ministers in drafting European legislation, votes on the EU budget, and approves and controls the European Commission.

European Union (EU) The successor organization to the European Community as defined by the 1992 Maastricht Treaty. The EU is not yet a union in the formal sense because it preserves some member states' sovereign rights. At the same time, in some policy areas the EU has true supranational institutions with authority over member states.

Expansionary fiscal contractions The controversial idea that cuts in government spending during a recession will cause increased aggregate consumption and investment, thus spurring economic growth.

Export subsidies Direct or indirect government payments to producers that effectively reduce the price of their exported products, making them more attractive to potential foreign buyers.

Export-oriented industrialization (EOI) An economic development strategy that focuses on manufacturing goods for export to global markets. Popular amongst many emerging market economies such as South Korea, Taiwan, and China. Contrast this policy with *Import-substitution industrialization*.

Fair trade An initiative spearheaded by nongovernmental organizations to provide higher prices to producers of certified commodities such as coffee, cocoa, and timber in developing countries. Fair trade tries to ensure that small farmers and producers have stable incomes, safe working conditions, and environmentally sustainable practices.

False consciousness A belief of the workers in the legitimacy of capitalism. With superior financial resources, the capitalists spread procapitalist ideology and values—the benefits of free trade, the need for low taxes on the rich, the problems with unions, and so on—which are stronger and more pervasive than alternative values favorable to workers. According to Marxists, capitalists not only exploit workers but also manipulate their beliefs so that they accept their own exploitation and fail to perceive their own true interests.

Financialization A process of capitalist accumulation in which corporations and financial institutions focus on making short-term financial gains, boosting stock values through stock repurchases, and extracting value from companies rather than reinvesting profits in new production facilities, human capital, and research and development. Some scholars also define financialization as the increase in the size and power of the financial sector relative to the productive sectors of the economy.

First sale doctrine The legal doctrine conferring on the purchaser of a legally produced copyrighted work the right to sell or dispose of that copy of the work without permission from the copyright owner. This doctrine is crucial for library book lending, used books and records stores, and DVD rental companies like Netflix.

Flags of convenience Some countries register airplanes and ships of companies that

conduct most of their business (licit or illicit) elsewhere in the world. In exchange for offering flags of convenience (registration), host countries typically receive lucrative fees from the companies.

Flexible exchange rate system Theoretically, fixed exchange rates are determined by international agreements among states, while flexible exchange rates are determined by market forces, with the value of currencies relative to others changing frequently. Even with the flexible (floating) exchange rates after 1971, central banks commonly buy and sell their nation's currency in order to affect its exchange value.

Floating population Poor peasants from China's rural areas who have migrated to big cities where they often work for relatively low wages in factories and the service sector. Estimated as numbering over 250 million, the migrants are often exploited and denied social welfare benefits because the government has not officially authorized them to reside in urban areas.

Food First A thesis introduced in the 1970s by Frances Moore Lappé stating that hunger is actually caused by income inequality and unjust land distribution rather than lack of food production or overpopulation. According to the proponents of this theory, hunger is *not endemic* to less developed countries, but is a *byproduct* of their political and economic relationships with the industrialized nations.

Food for Peace Also known as Public Law (PL) 480. A U.S. food aid program begun under the Eisenhower administration to sell and donate surplus U.S. agricultural commodities to strategically important developing countries such as India, South Vietnam, Cambodia, and Egypt. In the early years, recipients could purchase U.S. wheat and other commodities at low prices in their own local currency. Renamed the Food for Peace Act in 2008.

Food security The condition when all the people of a country have access at all times to enough food to live an active and healthy life.

Food sovereignty A concept stressing the rights of farmers in developing countries to control their own land, seeds, and water and to grow their own diverse and nutritious foods. It also includes the right of local communities to control their own systems of food and agricultural production and consumption in the face of pressures from transnational agribusinesses.

Foreign direct investment (FDI) Investments made by a company (often a transnational corporation) in production, distribution, or sales facilities in another country. The term *direct* implies that the parent company with headquarters in one country has managerial control over assets in a different host nation. Examples of FDI are when a corporation builds a new factory in a foreign country or buys an already existing company overseas.

Foreign exchange rate The rate at which one nation's currency can be converted into another nation's currency. Exchange rates continuously change as a result of the supply and demand for money, which in turn helps establish the price of goods and services in each country.

Forum shifting A practice in which a state shifts its agenda from one multilateral forum to another in hopes of achieving the best outcome for its national interests. For example, if a state is facing resistance to its trade goals in the WTO, it might switch to promoting the same goals in a regional trade agreement where other states are more accommodating. The practice can lead to a proliferation of sometimes contradictory international agreements on a specific issue.

Fracking Formally called hydraulic fracturing. A process whereby highly pressurized fluids are injected into underground rock formations to fracture the rocks and release natural gas and oil that is then collected at the earth's surface. Widespread use of the process caused U.S. production of natural gas to rise significantly after 2009.

Framing A term that constructivists use to describe the process by which global actors define the essence of a particular problem: what is causing it; who is involved with it; what its consequences are; and how to resolve it. Framing occurs through discourse and is designed to create a specific understanding of a problem and a specific kind of response to it.

Free trade One of the most popular policies advocated by economic liberals. In keeping with the *laissez-faire* notion that government intervention in the economy undermines efficiency and overall wealth, free trade removes protectionist measures (tariffs, quotas, etc.) that are designed to insulate domestic producers from international competition. It has been a major goal of most international trade institutions since 1947.

Functionalism A theory of regional integration predicting that when states establish central institutions to govern one economic sector (such as the steel industry), that will produce "positive spillovers" into other sectors, causing more central institutions to extend their authority over states' economic policies and deepen regional integration.

General Agreement on Tariffs and Trade (GATT) An international agreement in 1947 that became the basis of many rounds of international trade negotiations to reduce tariffs and trade barriers among its many member nations. At the end of the Uruguay Round in 1995, GATT, which contains the main rules governing trade in goods, was incorporated into the new World Trade Organization.

General Agreement on Trade in Services (GATS) One of the WTO agreements that came into force in 1995. It liberalizes the trade in services between WTO members and establishes rules members must follow in the treatment of foreign companies delivering services in insurance, telecommunications, banking, transport, and other sectors.

Genetically modified organisms (GMOs) Also labeled GMs. Living organisms that have had their genetic code altered for commercial or scientific gain. For example, a crop might be genetically modified to enhance desirable nutritional qualities. Critics of GMOs worry about the loss of native biodiversity, the accompanying shift to monoculture farming techniques, and a greater reliance on herbicides.

Glasnost Russian term for the policy initiated by Soviet Premier Mikhail Gorbachev in the late 1980s that opened up the Soviet state to political reform. It was meant to complement economic reform, or *Perestroika*.

Global governance Management of transnational problems. It encompasses the rules, institutions, and processes that shape international cooperation in specific issue areas such as climate change, environmental damage, and organized crime. The concept emphasizes that many different actors, including states, transnational corporations, nongovernmental organizations, and international institutions, cooperate through voluntary and flexible mechanisms to achieve common goals.

Global security structure (GSS) The global institutions and distribution of military power that determine which countries dominate global security policies and under what circumstances there is likely to be peace or conflict. The security structure is also profoundly shaped by the ideas states have about security, including their nuclear strategy, their understanding of their own purpose, who they consider to be friends or enemies, and their view of their national interests. During the Cold War the GSS was bipolar, but it became more multipolar by the 2000s. Today the GSS is more unstable with a more aggressive Russia, a rising China, and a United States under Trump that is less willing to shoulder international responsibilities.

Global value chains Gary Gereffi and Karina Fernandez-Stark define GVCs as "the full range of activities that firms and workers do to bring a product from its conception to its end use and beyond." Different firms in different countries are linked in a division of labor that leads to the production of final goods and services. In many GVCs Western firms deal with finance, basic research, design, product-branding, and marketing. LDCs want to move up the value chain from low-wage manufacturing to more profitable activities.

Globalization A process of global economic integration driven by economic liberal ideas and policies. Globalization also connotes increasing economic interdependence as well as the spread of Western (U.S.) cultural influence all over the world.

Good governance A government's conduct of public policies in a manner that is transparent, relatively free of corruption, respectful of popular wishes, and effective in promoting economic development. In normal usage, good governance does not necessarily require the presence of democratic political institutions.

Grameen Bank A pioneering microcredit bank founded in Bangladesh by Mohammad Yunus in 1976 and which has served as a model for other microcredit programs. This kind of bank is a popular mechanism for helping poor women in poor countries create small business enterprises.

Green Revolution Scientific and economic programs in the 1960s that increased food production in India, the Philippines, and other developing countries by introducing hybrid seeds, high-yielding varieties of wheat and rice, fertilizers, and modern farming techniques.

Grexit An abbreviation for "Greek exit," meaning a possible withdrawal of Greece from the Eurozone.

Guaranteed basic income An unconditional monthly income that the government provides to every adult citizen of the country and that is sufficient to pay for their basic necessities. A main goal of the basic income is to eliminate poverty and serve as a replacement for government welfare programs. Also called a universal basic income or a

guaranteed minimum income.

Gulf Cooperation Council (GCC) An economic and security alliance composed of Saudi Arabia, the United Arab Emirates, Kuwait, Oman, Bahrain, and Qatar. These six countries share a heavy reliance on foreign workers, who make up a significant proportion of their combined workforce.

Hard power A state's capacity to use military and economic assets to directly influence, persuade, or coerce other states. See *Soft power*.

Heavily indebted poor countries (HIPCs) A designation for some forty of the world's poorest countries—mostly in Africa—whose governments have run up relatively high levels of commercial and multilateral foreign debt.

Heavily Indebted Poor Countries (HIPCs) Initiative A multilateral initiative begun in 1996 (and expanded in 1999) to provide major debt relief to more than 30 poor countries, primarily in Africa. The IMF and the World Bank, along with official creditors, formally approved debt reduction while requiring countries to establish a track record of economic reforms and implement poverty reduction programs.

Hegemonic stability theory A theory positing that one country that is unusually rich and powerful dominates the entire international system for a length of time, during which it enforces rules that keep the system open to trade, with sound money, and at peace. While the hegemon benefits from this arrangement, it bears the costs of maintaining it.

Heterodox economic liberals Those who are broadly supportive of market-oriented economies but who believe that the state needs to intervene in important ways to preserve the competitive market and make it work more effectively for the majority of people in society. Many heterodox economic liberals are inspired by Keynes. They often stress the role of institutions and history in shaping economic outcomes.

Historical materialism The Marxist theory that social and political institutions are determined by the physical foundations of the economy.

Hot money Capital or investments that move from one country to another in search of short-term profits. Because hot money moves relatively quickly and frequently from one financial market to another, it can cause financial instability and significant changes in the value of some currencies.

Hydra effect A process in which a crackdown on an illegal commodity (e.g., drugs) in one area causes it to spread and multiply in a different area. For example, U.S. anti-drug efforts in Latin America caused drug production and trafficking to flourish in Mexico.

Import quotas Limits that a government places on the quantity of a good that can be imported into its country. Quotas tend to drive up the price of a good while at the same time restricting competition.

Import-substitution industrialization (ISI) A popular economic development strategy in the 1950s, 1960s, and early 1970s that promoted domestic manufacturing by restricting imports of foreign products. Contrast this strategy with *Export-oriented growth*.

Inclusive wealth A composite measure of a country's economic and social progress that

includes the stock of manufactured capital, human capital, and natural capital. Considered by many to be a better measure than GDP of a country's true wealth and potential because it includes variables for economic output, natural resources, and a population's health and educational characteristics.

Industrial policies State-directed economic policies designed to guide business investment and development of particular industrial sectors. Such policies often include subsidies for businesses, trade protection, infrastructure spending, and promotion of innovation.

Infant industries New industries in any nation that are at a disadvantage relative to older, more efficient, foreign industries. Most mercantilists and even some economic liberals suggest that protective measures such as high tariffs on imports are justified until the newer industries are able to compete fairly with mature foreign industries.

Informal economy The parts of an economy that governments do not effectively regulate or tax. In less developed countries, many people work in the informal economy in small firms doing construction, selling food and everyday items on streets and in local markets, offering domestic services, and participating in illegal activities.

Information sovereignty A state's freedom from foreign interference in its control of the production and use of information within its borders, and a state's independent right to control flows of information (particularly digital flows) into and out of its territory.

Insourcing The process in which a corporation that had moved manufacturing overseas resumes manufacturing a product in its own factories in the country where it is headquartered. In other words, the corporation makes new investments and hires workers in its home country so that it no longer uses a contractor in a foreign country such as China to make or assemble a product.

Integration The process whereby states (usually in a geographic region) agree to unify or coordinate many economic, political, and social policies. Economic liberals tend to support integration because it enhances efficiency and productivity and generates trade.

Intellectual Property Rights (IPRs) Exclusive rights to control for a limited time the use of inventions, artistic works, and marks used in commerce. The most common IPRs are patents, copyrights, and trademarks.

Intergovernmental Panel on Climate Change (IPCC) An intergovernmental body established in 1988 by the UN Environmental Programme and the World Meteorological Association with a mandate to assess scientific information on climate change. Its periodic reports, written by scientists from around the world, are influential in shaping policy making and international negotiations on climate change.

Intergovernmentalism A realist theory of regional integration applied to Europe which stresses that national governments are the driving force in integration and will preserve their sovereign power but also create supranational institutions when their national interests converge. The theory predicts that national governments will pool sovereignty when it is an effective and efficient method of solving domestic problems.

Interlocking directorates When individuals sit on the board of directors of many

different corporations at the same time. They form business networks that can reduce competition in the economy, increase coordination between capital owners, and foster a sense of class interest among individuals at the global level.

Intermediate goods Parts, components, and other semi-finished inputs used in the production of final goods. Intermediate goods are bought by companies, not consumers. Globalization and outsourcing, among other factors, have made trade in intermediate goods the major share of all global trade.

Internally displaced people (IDPs) People who have been forced from their homes due to violence or natural disaster and who are still living within the borders of their own country.

International Monetary Fund (IMF) Created as part of the *Bretton Woods* system, the IMF is an organization of over 150 member states charged with stabilizing the international monetary system. The IMF makes loans to member states when they experience severe *current account deficits*. These loans are made subject to enactment of economic reforms, a practice called *conditionality*.

International political economy (IPE) The interdisciplinary social science that examines the relationships between states, markets, and societies in an international context. IPE seeks to understand how power is used in those relationships to affect the distribution of scarce resources.

Internet of Things (IoT) A network of devices such as smart phones, home appliances, and cars with sensors allowing them to connect to the Internet and share data with each other. The IoT is expected to increase the efficiency of government planning, commercial operations, and everyday consumer activities.

Investor-state dispute settlement An international arbitration mechanism through which corporations and investors can sue governments when they believe that their rights under a treaty have been violated. ISDS protects investors from discriminatory government practices and expropriation of assets. It is a component of many bilateral and multilateral investment treaties.

IPE structures Networks of actors and institutions that determine the rules governing production, trade, finance, security, and knowledge. According to Susan Strange, the rules of each structure confer power on certain actors and constrain the way states behave. The structures regulate the processes by which goods and services are produced and exchanged, and they shape flows of money, technology, and information between countries.

Irregular migrants Migrants who reside and work in a foreign country without the appropriate legal documents. These workers may have entered the country without permission or entered with a visa but then stayed on past the limits of that permission.

Islamic State Also called the Islamic State of Iraq and the Levant (ISIL) and the Islamic State of Iraq and Syria (ISIS). A brutal jihadist group that seized territory in Iraq and Syria in 2014 and declared a caliphate. Iraqi, Kurdish, and Western military forces forced ISIS out of major cities it controlled and largely crushed the group by the end of 2017.

Jihadist A term describing a fundamentalist Sunni Muslim ideology that espouses armed struggle against Western powers and perceived corrupt, un-Islamic governments. Jihadists groups seek to unite the Muslim community and establish government based on "true" Islamic principles.

Keynesian compromise A class compromise after World War II in which capitalists shared gains from growth and productivity with workers in the form of rising wages and benefits, while workers maintained social peace. Associated with this compromise was significant state regulation of international financial flows with the goals of preserving government fiscal autonomy and achieving full employment.

Keynesianism To be Keynesian is to be in agreement with the general thrust of the economic philosophy of John Maynard Keynes—to believe that there is a positive role for the state to play in domestic economic affairs (fighting unemployment and poverty, for example) and in international economic affairs (the kind of role conceived for the International Monetary Fund and the World Bank). Keynes's views were influenced by the catastrophe of World War I and the Great Depression of the interwar period. His ideas were reflected in the Bretton Woods institutions and have gained renewed attention due to the global economic crisis. Keynesianism advocates government stimulus spending during a recession to boost demand and employment.

Know-thy-customer rules A principle of due diligence in banking whereby providers of financial services are expected to verify the identity and check the background of potential clients to determine if they are involved in money laundering or other criminal activities.

Kyoto Protocol A protocol (or set of informal procedures and norms, but not a formal treaty) agreed to in Kyoto, Japan in 1997 that established carbon emissions goals for all industrialized countries. In order to deal with the problem of global warming, states agreed to achieve these goals by 2012. While many states signed the agreement and implemented the protocol, the United States did not ratify it. China, India, and other emerging economies were not required to adhere to the agreement but encouraged to do so. The protocol officially came into effect in 2005.

Lacey Act A U.S. wildlife protection law first passed in 1900 and amended in 2008. Among other things, it prohibits the import, export, or interstate trade of certain endangered animals, trees, and plants.

Law of comparative advantage According to David Ricardo, the law holds that nations should produce and export those goods that they can produce relatively more efficiently (i.e., at lower opportunity cost) than other nations and import those items that other nations can produce relatively more efficiently. It is often cited as the foundation of free trade policy.

Levels of analysis The four levels of analysis are the individual, state/societal, interstate, and global levels. The levels-of-analysis concept was theoretically developed by the international relations scholar Kenneth Waltz to explain different sources of international conflict and war. Each level focuses on specific factors that shape relations between states and cause certain international outcomes.

Lifeboat ethics A controversial argument by Garrett Hardin that the rich countries constitute a lifeboat in a world with limited resources and should not let the developing world's poor onto the lifeboat. He opposed giving food aid to poor countries with rapidly growing populations because he believed it would only encourage unsustainable population growth that would put strains on the world's food, resources, and environment, ultimately bringing ruin to the rich countries.

Malevolent mercantilism Intentionally harmful economic policies that aim to weaken or defeat an enemy or potential enemy. Associated with Germany and Japan before World War II.

Managed float A system in which currency exchange rates are allowed to reflect market rates but are affected by occasional interventions by central banks.

Massive retaliation A U.S. nuclear strategy developed during the Eisenhower presidency in which the United States threatened to respond to a Soviet invasion of Europe with overwhelming nuclear strikes that would literally destroy the Soviet Union. This strategy of deterrence by brinksmanship was deemed to be flawed once it was clear that the United States was territorially vulnerable to Soviet nuclear retaliation.

Mercantilism A seventeenth-century ideology that made accumulation of gold and silver through regulated trade a major goal of the state. Today, it is a philosophy that justifies government regulation of a nation's economy and intervention in international economic relations in order to increase state power and security. Policies of import restriction and export promotion (to accumulate wealth at the expense of other countries) follow from this philosophy. See *Economic nationalism*.

Microcredit Small loans given to groups of low-income people (usually women) in less developed countries who share the risk of repaying the loans. Microcredit has been heralded for helping overcome poverty by putting money directly into the hands of those who actually need it, thus encouraging sustainable entrepreneurship and self-empowerment.

Middle-income trap A situation that many developing countries encounter after a period of rapid economic growth, when per-capita GDP stalls in the range of about $10,000 to $15,000 and it becomes increasingly difficult to close the development and technology gap with high-income countries.

Migrants People who are living in a country other than their country of birth. As the term is normally used in the media, it describes poor people who have voluntarily left their country in search of economic opportunities or desperate people who have fled their country seeking safety elsewhere.

Millennium Development Goals (MDGs) A United Nations–sponsored program launched in 2000 with backing from all UN members. It established specific goals for developing countries to achieve by 2015, including: the eradication of extreme hunger and poverty; attainment of universal primary education and gender equality; empowerment of women; reduction in child mortality; improvement of maternal health; and combating HIV/AIDS, malaria, and other diseases.

Modern world system (MWS) A theory based in part on Marxist-Leninist ideas. The MWS views economic development as conditioned by the relationship between the capitalist *core* and the less developed *periphery* nations. The historic mission of the core is to develop the periphery (often through the *semiperiphery*), but this development is exploitive in nature.

Most favored nation (MFN) A trade principle under the World Trade Organization stating that trade preferences (i.e., the most favorable trade treatment) that a WTO member extends to one country should be extended to all other countries equally.

Mujahideen A term meaning Islamic freedom fighters. It originally referred to those who in the 1980s resisted the Soviet Union in Afghanistan with the help of American weapons and training. This support was blamed as a source of "blowback," whereby these former U.S. surrogates formed terrorist organizations targeting Western interests.

Multidimensional Poverty Index (MPI) An index of poverty that factors in a country's standard of living, health conditions, and educational achievement. By using more measures than just income, the MPI is thought to give a more complete picture of conditions of deprivation in the world. Nearly 1.5 billion people suffer from multidimensional poverty.

Multinational corporation (MNC) An international business firm that engages in production, distribution, and marketing activities that cross national boundaries. The critical factor is that the firm has a tangible productive presence in several countries. See *Transnational corporation (TNC)*.

Multipolarity The condition of a security structure with more than two centers of power. President Nixon and Secretary of State Henry Kissinger promoted a multipolar security structure comprised of the United States, the Soviet Union, Japan, Europe, and the People's Republic of China in 1973. Contrast with *bipolarity*.

Muslim Brotherhood A Sunni Muslim organization established in Egypt in 1928 and which today has branches in many Arab countries that operate as political parties and offer social services to the poor. The Brotherhood is the main political opposition to the government in Egypt, Jordan, and the Palestinian Authority.

Mutually Assured Destruction (MAD) The Cold War strategy of the United States and the Soviet Union under which each had sufficient military power to destroy the other, even if in doing so it destroyed itself. MAD supposedly kept the peace between the two by ensuring that neither nation could realistically "win" a nuclear war.

Name-and-shame campaigns Campaigns by advocacy groups to bring negative international publicity to certain companies and countries to pressure them to change practices that are perceived to be illegal or unethical.

Nation A group of people bound together by a shared sense of history and culture. Members of a nation have common myths about their origins, make claims to a particular territory, and usually seek to govern themselves within that territory.

National champions Key domestic companies or industries that a government nurtures

for long-term development through subsidies, trade protection, and other forms of support. Although some national champions become globally competitive, they tend to reduce competition in their home economy.

National treatment An important principle in the GATT, GATS, and TRIPS agreements that requires a country to treat imported products and services—once they have passed through customs—no less favorably than similar domestically produced goods and services. In other words, internal taxes, regulations, and requirements should not discriminate against imported goods in favor of local goods.

Neoconservatives (neocons) The term applies to those today who have a conservative economic outlook. The term "neocons" is also associated with defense policy officials in the George W. Bush administration who held a unilateralist outlook that included the use of force whenever the United States felt it necessary or justified.

Neoimperialism An element of the structuralist perspective on capitalism. *Core* nations exploit the periphery through the finance, production, and trade structures. While classical imperialism employed force to achieve its ends, neoimperialism emphasizes the use of nonmilitary tools to dominate weaker states. Although neoimperialists selectively intervene militarily in certain countries, they mostly focus on spreading liberal economic ideals and institutions around the world.

Neoliberalism An economic philosophy that advocates market deregulation, privatization of government enterprises, minimal government intervention, and open international markets. U.S. president Ronald Reagan and UK prime minister Margaret Thatcher popularized neoliberalism in the 1980s and implemented policies derived from it.

Neomercantilism A version of mercantilism that evolved in the post-World War II period. Rather than focusing simply on producing trade surpluses, neomercantilism today promotes a wide variety of protectionist trade, finance, and development policies to generate national wealth and enhance national security. Neomercantilist states work closely with their domestic private sector to advance national interests in an intensely competitive international economy.

Neorealism An international relations theory that asserts that in an anarchical international system, states are compelled to behave in predictable ways as they seek to insure their own survival and security.

New constitutionalism A broad movement to remove sensitive economic issues from democratic political control and to place their governance in the hands of independent bodies or the private sector. The new constitutionalism is also entrenched through international economic agreements that "lock in" economic policies and rules that privilege corporations and capitalists.

New International Economic Order (NIEO) A radical agenda for reforming international economic governance put forward by developing countries in the mid-1970s. Its proposals included greater regulation of transnational corporations, improving developing countries' terms of trade, and redistributing more wealth and technology from rich to poor countries.

Nondiscrimination A fundamental principle of international trade under World Trade Organization rules stating that countries should not discriminate between their trading partners or treat imported goods and services any less favorably than domestically produced ones.

Nongovernmental organizations (NGOs) National and international voluntary organizations that have played an increasingly bigger role in the global political economy since the end of the Cold War. Many NGOs provide services that states cannot or will not. Others promote particular values and norms such as protection of human rights. Examples of NGOs include Greenpeace, Human Rights Watch, the Red Cross, and Doctors Without Borders.

Nontariff barriers (NTBs) Government-instituted measures (other than tariffs) that restrict imports, often for the purpose of protectionism. NTBs include health and safety standards, domestic content legislation, licensing and labeling requirements, voluntary export restraints, and foreign exchange controls. Such measures often make it difficult for imported goods to be marketed and raise their price.

Norm antipreneurs A term coined by Alan Bloomfield to refer to groups that defend existing global norms against change by norm entrepreneurs. Antipreneurs often (though not always) try to disrupt the adoption of new norms that weaken state sovereignty and progressive norms that pertain to social and human rights.

Norm cascade A process whereby a significant number of states rapidly adopt and conform to a new norm, in part because each state wants to be identified as a responsible, legitimate international stakeholder.

Norm entrepreneurs Groups and individuals that call attention to particular international issues and seek to persuade states to adopt new norms regarding the appropriate ways to govern those issues.

Norms Standards of appropriate behavior for a political actor based on that actor's identity. Norms are generally beliefs shared by a group of actors that guide them to act morally towards a particular issue. For example, the prohibition on deliberately killing civilians in wartime is an international norm.

North American Free Trade Agreement (NAFTA) A free trade agreement between the United States, Canada, and Mexico that took effect in 1994. When fully implemented by 2005, NAFTA eliminated tariffs and quotas on most goods traded among the three countries. The treaty remains controversial; scholars disagree about how much it has benefited its members, and President Trump has insisted on renegotiating it to protect U.S. jobs and reduce the U.S. trade deficit with Mexico.

North Atlantic Treaty Organization (NATO) A military alliance established in 1949 between North American and European countries to defend against potential aggression by the Soviet Union. Today the members of this collective security organization include the United States, Canada, Turkey, and most countries in the European Union. Since the end of the Cold War it has conducted missions in the former Yugoslavia, Kosovo, Libya, and Afghanistan. Tensions between NATO and Russia rose sharply after Russia invaded and

annexed Crimea in 2014.

North—South The relationship between developed, industrialized countries (the North) and less developed countries (the South). This concept is often associated with core-periphery analysis but can also be simply a descriptive device.

Nuclear taboo A widely shared reluctance by states since World War II to use nuclear weapons, significantly due to the moral restraint of public opinion and the efforts of a worldwide antinuclear weapons movement to stigmatize use as unthinkable and immoral.

Odious debt Foreign debts incurred by a former corrupt regime that leave the new government owing tremendous sums of money to banks and investors, often stifling development efforts. Many experts argue that these debts should be considered illegitimate and should be forgiven for the poorest of nations.

Offshoring When a company moves its production or business function from one country to another. The company still controls the activities it moves to a subsidiary or affiliate in another country. In contrast, outsourcing involves transferring production to a third party or contractor in another country.

Oil for Food Program A UN program imposed on Iraq after the Persian Gulf War (1990–1991) that allowed the country to sell some of its oil in international markets in exchange for income to buy imported food and emergency aid supplies. The controversial program was plagued with corruption and blamed for causing many Iraqis to die from malnutrition and disease.

Oligarchs A small group of people who attempt to control a government for their own benefit. In Russia, the term applies to men who became wealthy in the 1990s as a result of corrupt privatization programs and to billionaires today with close ties to Putin and whose wealth comes from monopolistic businesses or illegal activities.

Operation Car Wash (*Operação to Lava Jato*) A massive Brazilian corruption scandal and criminal investigation that has resulted in the prosecution of dozens of politicians, public officials, and businesspeople since 2014 on charges including bribery, embezzlement, and money laundering.

Ordoliberalism A variation of economic liberalism popular in Germany that stresses the importance of competition and personal freedom. Because ordoliberals do not believe that markets are self-regulating, they stress that the state must establish and enforce rules and laws that keep the market operating efficiently and free from control by special interests.

Organization of Petroleum Exporting Countries (OPEC) An organization of nations formed in 1960 to advance the interests of Third World oil exporters. Since 1973 OPEC members have coordinated production levels in order to reach and maintain targeted international oil prices.

Orthodox Economic Liberals A group of people who rigidly adhere to economic liberal ideas, values, and policy prescriptions. Most agree that instead of the state, "open" and "free" markets should be allowed to determine socio-political outcomes whenever possible. They also tend to model economic behavior on the assumption of individual rationality.

Outsourcing When a firm transfers part (or all) of the production of a good or service to a company in another country. By hiring a foreign company to perform tasks that used to be done internally, a corporation can often cut costs and raise profits. Many economic liberals believe that outsourcing creates economic efficiency and ultimately lowers prices for consumers. Outsourcing causes domestic jobs to be lost to foreign suppliers.

Paradox of thrift During a recession, if one individual saves more income, rationally speaking, that individual may be more financially secure. If everyone does this, however, the combined actions can reduce overall demand in the economy, cause companies to reduce output, and deepen the recession, thus making everyone less secure economically. The paradox of thrift, then, is an example of the potential problems of an unregulated economy. Keynes supported an active role for the state in the economy to help overcome this problem.

Paris Agreement An agreement reached by 195 countries in 2015 to combat climate change. Among other things, signatories aim to keep temperatures from rising more than 2 degrees Celsius above pre-industrial levels and reach the peak of global carbon emissions soon followed by rapid reductions. Countries can decide themselves how to implement their emissions reductions goals. In 2017 President Trump announced that the United States would withdraw from the agreement.

Patents Government-granted exclusive rights to make, use, or sell an invention for a period usually of twenty years (counted from the date of filing a patent application). Patents are designed to encourage research and innovation; many companies argue that without them they would be unable to capture all of the benefits of their R&D expenditures.

Peak oil The controversial idea that the world's production of oil will reach a maximum level, after which it will gradually decline to zero. Experts disagree on when that will happen and what the impacts on oil prices and society will be when global production starts to go down.

Perestroika Russian term for economic restructuring and economic reform implemented in the Soviet Union in the mid-1980s.

Periphery The nonindustrialized countries of the modern world system that produce mostly agricultural goods and natural resources. Modern world system theory hypothesizes that peripheral states (e.g., developing countries) are usually made worse off as a result of interaction with core states.

Peshmerga A term for Kurdish fighters who constitute the military forces of the autonomous Kurdish Regional Government in northern Iraq.

Petrodollar recycling Since 1973, the system whereby oil exporters recirculate their oil revenues through the global financial system by importing goods, purchasing foreign financial assets, or parking revenues in foreign banks (which then lend money to governments and private borrowers).

Philanthrocapitalism A form of philanthropy in which extremely wealthy businesspeople

fund programs in developing countries that have specific goals and clearly measurable outcomes and that sometimes are profit-generating. Philanthrocapitalists often claim to be more efficient and effective than development NGOs and governments. They often apply big data, technology, and business practices in the battle against major social problems such as disease, poverty, and poor education.

Positive-sum game Any interaction between actors that makes all participants simultaneously better off. See *Zero-sum game*.

Precariat A term coined by Guy Standing to describe a new class of workers with insecure jobs, few job benefits, high debt, and no meaningful occupational identity.

Primitive accumulation A Marxist concept that is hypothesized to be at the root of capitalism's initial development. The process is one of coercive or violent seizure of assets (particularly land) owned or used regularly by others.

Problematization A process by which states and advocacy groups use discourse to construct something as a political problem that requires some kind of coordinated, international response.

Procurement Government purchasing of goods and services from private companies. Mercantilists believe that governments should always try to purchase from domestic firms, not foreign ones, and use procurement to help domestic firms gain from economies of scale and become more innovative.

Profit paradox When law enforcement tries to ban an item for which there is high demand (e.g., drugs), the reduction in supply drives up prices in the short term, but this bolsters profits for those willing to illegally supply the item, thus encouraging others to enter the illegal business. Thus, the temporary reduction in supply is reversed as criminals find ways around the ban.

Proletariat In Marxist analysis, the class of workers who do not own capital and who are wage earners exploited by the bourgeoisie.

Protectionism State policies such as import tariffs, non-tariff barriers, and import quotas that restrict trade in order to benefit (protect) domestic producers.

Public goods Goods or services that, once provided, benefit everyone simultaneously but cannot be denied selectively to one person or state. A lighthouse and national security are classic examples of domestic public goods. A stable international currency and reduced carbon emissions are examples of international public goods.

Quantitative easing (QE) Central banks such as the U.S. Federal Reserve and the Bank of England engage in quantitative easing by electronically creating new money which is used to buy government bonds, mortgage securities, and other assets in the hopes of lowering interest rates so that private companies make new investments and private banks make more loans. The Federal Reserve engaged in three rounds of QE between 2008 and 2014.

Realism A theory in international relations emphasizing that states seek to acquire more power in order to enhance their security. The national interest is a determinant of state

behavior. In the view of realists, states, like individuals, tend to act in their own self-interest.

Reciprocity A traditional principle of the World Trade Organization system whereby trading partners mutually reduce trade barriers. The idea is that when a country offers trade concessions to other countries, they should reciprocate with similar concessions.

Red line In a warning in August 2012 to Syrian President Bashar al-Assad, President Obama said that if Syria used chemical weapons or moved them around, that would cross a "red line" causing Obama to change his "calculus" and lead to "enormous consequences." When Syria did attack civilians with sarin gas in 2013, Obama almost ordered military strikes on Syria before agreeing to a Russian proposal to peacefully remove all chemical weapons from Syrian territory.

Refugees People who have fled their country of origin because of natural disaster, fear of persecution, or violence. International organizations such as the United Nations Office of the High Commissioner for Refugees assist refugees and help them relocate to a place where they can safely reside until they are willing to return to their home country.

Regime A set of rules, norms, institutions, and decision-making procedures that conditions actor expectations and behavior regarding a global issue. Regime also refers to the people in power who comprise the government of any nation-state.

Regional trade agreements (RTAs) Agreements between states in a geographic area to reduce trade barriers between them. RTAs are often easier to form than global trade agreements because there are fewer interests to reconcile. Some economic liberals oppose RTAs, especially if they violate the WTO nondiscrimination principle or cause trade diversion.

Remittances Payments made by migrant workers to family or friends in their country of origin. Some experts believe that these transfers of money help alleviate poverty and spur economic growth in developing countries.

Renewable energy Energy derived from sources that can be replenished, including biomass, hydropower, geothermal, wind, and solar.

Rentier state A state that derives a large proportion of its revenue from taxes on oil and gas exports. In the cases of Iran, Iraq, Libya, Algeria, and Gulf Cooperation Council states, oil and gas rents relieve the government of having to heavily tax its citizens.

Rent seeking Efforts to achieve personal gain by creating artificial scarcity rather than by producing efficiently. Many corrupt activities can be viewed as examples of rent-seeking. Powerful lobbying groups seek rents from the government in the form of subsidies, favorable tax treatment, and special rules that allow them to extract money from others in the economy without necessarily increasing economic growth and productivity.

Reprimarization The process whereby a country that had significantly diversified its exports during industrialization reverts to being a large exporter of primary commodities such as minerals, hydrocarbons, and agricultural raw materials. Latin America has experienced some reprimarization due to boosting commodities exports to China.

Research and development (R&D) Activities leading to the development of new technologies, products, and innovative processes. R&D occurs in government-funded research institutions, universities, and private companies and is important for a country's scientific advancement and improvements to its existing products and processes.

Reserve currency A currency that is held by a nation's central bank in its foreign exchange reserves. The U.S. dollar is the world's most common reserve currency, and many international transactions and commodities are priced in U.S. dollars.

Responsibilization A process under neoliberalism in which the state transfers responsibility for tasks once performed by individuals. These individuals have to cultivate their own human capital, become self-reliant, and bear economic risks. Responsibilization goes along with the dismantling of the welfare state and the reduction of collective social support.

Restriction-opportunity dilemma A situation in which efforts to ban goods in high demand (e.g., drugs or guns) are often counterproductive because they make the black market provision of the goods more profitable.

Rogue states States that are regarded as threats to world peace or that often refuse to cooperate with other states. Iran, Syria, and North Korea are often cited as examples. These states also regularly violate well-established international norms related to nuclear proliferation, human rights, and other issues. Many states place sanctions on rogue states.

Scaling The process of turning a new technology into a product design, creating a prototype, and building a factory and hiring workers to manufacture the product. Some argue that a company should scale up in its own home country rather than outsource production if it wants to maintain a long-term innovative lead over competitors in foreign countries.

Secrecy jurisdictions Countries and territories such as Switzerland, the British Virgin Islands, and the Bahamas with strong banking privacy laws and rules that allow companies to register without declaring their real beneficial owners.

Securities These are certificates traded in a market that give a purchaser the right of ownership over assets or the right to earn interest from the underlying assets. Securities are traded in a market. Bonds are a type of security whereby a government or a private company promises to repay the buyer of the bond's principal plus interest at a specified time in the future. Mortgage-backed securities are bought by investors who are promised a return from the securities' underlying mortgages. Essentially, buyers of securities are lending money to issuers who promise to repay the buyers (with interest) in the future.

Securitization A process in which state elites use discourse to construct an issue as a security threat that then justifies the use of extraordinary and sometimes undemocratic measures in response to the threat.

Security community Some constructivists and realists assert that seemingly hostile rivals sometimes cooperate with one another because they have a shared understanding that they are part of a "security community"—a group of people or states with a sense of common

moral standards and a certain level of mutual trust. A good example is the Organization for Security and Cooperation in Europe (OSCE), which was set up in the mid-1970s as a process by which the Cold War antagonists could cooperate on security matters in Europe.

Security dilemma According to realists, a situation wherein one state's effort to protect itself or enhance its defensive capabilities is viewed as threatening by another state.

Semiperiphery An intermediate zone between the *core* and *periphery*. South Korea and Taiwan might be considered part of the semiperiphery today in *modern world system* theory. The semiperipheral states are typically industrializing and expanding their urban manufacturing zones, but they lack economic and political power at the international level.

Siloviki Powerful political allies of Russian president Putin who have backgrounds in the secret police, intelligence services, and law enforcement agencies.

Single European Act (SEA) The 1985 agreement by European Community members to advance to the next stage of integration: a union. The SEA came into effect in 1987. In policy terms, it meant extensive coordination of monetary policy, investment regulations, services, migration, labor, and foreign policy. It also created new rules and powers for European Community institutions.

Single Market In 1986 the members of the European Community passed the Single European Act that created a single market with a customs union and freedom of movement of labor and capital. This act led to passage of the Treaty of Maastricht in 1993 and creation of the European Union (EU), along with other steps to further integrate the members of the European community. See *SEA* and the *Treaty of Maastricht*.

Social entrepreneurship A profit-oriented activity designed to also serve a pressing social need of the poor. Social entrepreneurs often seek innovative solutions to old problems, try to create and deliver new low-cost products and services in poor communities, and place faith in market-based mechanisms.

Socially responsible investing Voluntary efforts by investors to avoid certain types of companies and countries that they perceive to be socially or environmentally unethical, such as those involved in land expropriation, human rights abuses, or unsustainable environmental practices.

Soft power The ability to influence international affairs and persuade other states through such intangible factors as culture, values, ideology, and institutions. Soft power does not rely on threats or coercion. It is less direct than *hard power* but sometimes more effective.

Sovereign wealth funds (SWFs) Large investment funds owned by states with large balance-of-payments surpluses. The funds are invested in stocks, bonds, real estate, and other assets around the world. While many states reinvest SWF returns for future generations, others use returns to pay pensions or fund social programs.

Sovereignty The ability and right to exercise supreme authority in a polity. For realist-mercantilists, sovereignty also refers to a state's freedom from control by an outside power.

Special and differential treatment Provisions in the WTO agreements that give developing countries exemptions from certain trade rules or let them delay implementing

certain WTO obligations. Provisions also give the poorest countries preferential access to markets in developed countries and technical assistance from rich countries.

Speculation An investment in a foreign currency based on a belief that the currency will either appreciate or depreciate. Speculators have different ways of betting against a rise or decline in a currency; if they bet correctly, they can earn a profit by buying or selling the currency before and then after it changes in value. Currency speculation is common in foreign exchange markets, but at times it can precipitate a financial crisis in a country.

Spiral model A constructivist model that explains five stages through which a state moves to internalize an international norm. Initially a state violates the norm, then denies the validity of the norm, then rhetorically acknowledges the norm's validity, then begins to act in conformity with the norm, and finally adopts the norm in its own laws and habitually behaves in conformity with the norm.

State A legal entity that monopolizes the legitimate use of force in a given territory. The state consists of all branches of government, the bureaucracy, the military, and associated institutions. It exercises sovereignty within its territorial borders.

Strategic resources Resources such as oil, natural gas, rare earth minerals, and food that are vital to an economy and its major industries. States seek to control these resources or guarantee their uninterrupted supply because the resources have important consequences for national security. Most nations fear becoming overly dependent on others for the resources they lack.

Strategic trade policies State efforts to purposefully create comparative advantages for domestic industries such as steel, aircraft, semiconductors, and high tech. These efforts typically involve state subsidies for companies to innovate, export more, gain economies of scale, and achieve greater production efficiency than foreign competitors. Strategic trade practices are often associated with state industrial policies—that is, intervention in the economy to promote specific patterns of industrial development.

Structural Adjustment Programs (SAPs) Economic austerity policies and free-market reforms in less developed countries intended to establish a foundation for future economic growth. The International Monetary Fund and the World Bank often force developing countries to adopt SAPs as a condition for receiving loans and other financial assistance.

Structuralism An IPE perspective rooted in Marxist thought that focuses on how dominant economic structures shape the political order and relationships between different classes. It emphasizes the conflictual and exploitative relationships between the *bourgeoisie* and *proletariat*, the *core* and *periphery*, and the *North* and *South*. Capitalism is the dominant economic structure that determines class interests and produces inequality within and between nation-states. Much debate exists as to whether and how structural conditions can be changed.

Subprime mortgage loans Home loans made by banks in the United States to customers who did not have to meet the higher standards for loans as they did before the mid-1990s. Easier terms such as little evidence of the ability to pay or lower credit scores greatly increased the number of people who "qualified" for home loans. For many experts,

subprime mortgages directly contributed to the global economic crisis and manifest some of the worst traits of the U.S. style of capitalism.

Sustainable development A pattern of economic development that is consistent with the goal of nondegradation of the environment. To implement this form of development requires politically difficult tradeoffs between economic growth and environmental protection.

Sustainable Development Goals A United Nations-sponsored agenda launched in 2015 that is a successor to the Millennium Development Goals. It repeats many goals for developing countries over the period lasting to 2030, such as ending extreme poverty, and adds new goals for all countries such as promoting sustainable consumption and production, reducing inequality, combating climate change, and protecting the environment.

Tax havens Countries and territories that have strong banking privacy laws, low corporate tax rates, and relatively light corporate regulations. These sovereign jurisdictions attract tax evaders who wish to hide their earnings from their home government or avoid inquiries into the (often illegal) sources of their income.

Tax inversion When a large corporation in a country with a relatively high tax rate sells itself to (or buys) a smaller company in a country with a lower tax rate and then reincorporates in the low tax country. The inversion effectively transfers the corporation's headquarters and tax home to another country in order to lower taxes.

Toxic securities Packages of investments such as risky subprime mortgages in the United States that were "bundled" and sold to investors all over the world.

Trade in Services Agreement (TiSA) A proposed trade agreement being negotiated between the European Union, the United States, and 21 other WTO members to reduce barriers to trade in services such as banking, insurance, e-commerce, and telecommunications. A number of countries hope that the provisions of TiSA will eventually be incorporated into a revised GATS agreement. Negotiations were put on hold in 2017.

Trademarks Signs or symbols (including logos and names) registered by a company to identify its goods and services. Protection for trademarks is usually granted for ten years and is renewable. Examples of trademarks include the Nike swoosh, the brand name Kleenex, and MGM's lion's roar. Large companies usually register their trademarks in all the countries where they do significant business.

Traditional Knowledge The accumulated knowledge of indigenous or local communities as it relates to such things as plants, plant uses, agriculture, land use, folklore, and spiritual matters. Having developed and preserved this knowledge, indigenous peoples and other communities seek greater control over it, such as the ability to require outsiders to seek permission to use the knowledge and to share any benefits derived from its use.

Tragedy of the commons A term coined by Garrett Hardin to describe situations in which human nature, rationality, and political freedoms drive individuals to overuse

communal resources. Hardin recommends strong government action to limit population growth to save the earth's resources.

Transatlantic Trade and Investment Partnership (TTIP) A trade agreement that the European Union and the United States began negotiating in 2013. The goal of the proposed agreement is to increase economic growth in both parties by eliminating most tariffs, harmonizing regulations, and liberalizing investment procedures. Negotiations stalled after the British referendum on leaving the EU and after the election of President Trump.

Transfer pricing A practice in which subsidiaries of the same corporation in different countries trade goods and services at artificial prices, i.e., prices that are much higher or lower than the normal market prices. Through transfer pricing, corporations essentially shift profits and losses between their subsidiaries in order to lower their overall global taxes.

Transnational advocacy networks (TANs) International networks of activist groups that attempt to convince states to accept principled ideas and norms about appropriate political behavior towards issues such as migration, refugees, and human rights.

Transnational agribusiness corporations (TNACs) Also termed agribusinesses. Agribusinesses operate the world over in a variety of activities such as production, processing, and marketing of commodities and food. They are often accused of exploiting labor and unduly influencing political-economic conditions in countries they invest in.

Transnational capitalist class (TCC) The owners and managers of transnational corporations and financial institutions. Sociologist Leslie Sklair includes fractions of the state bureaucracy, the technical elite, and the media in the TCC, which spread a discourse of globalization and consumerism.

Transnational corporation (TNC) A large business that has affiliates and subsidiaries in regional or global markets and whose assets, production, and sales therefore extend beyond any one nation-state. The key characteristic of a TNC is a high level of foreign direct investment in multiple countries. See *multinational corporation*.

Trans-Pacific Partnership Agreement (TPP) A regional trade agreement signed by the United States, Japan, Australia, Brunei, Malaysia, Vietnam, New Zealand, Singapore, Canada, Chile, Mexico, and Peru in 2016. The agreement would have reduced or eliminated many tariffs on goods traded between the countries and strengthened intellectual property rights. After President Trump withdrew the United States from the TPP in early 2017, the remaining members began negotiating a similar agreement without the United States.

Treaty of Maastricht This treaty creating the *European Union* was ratified by members of the European Community in 1993. It signified agreement to move to a more advanced stage of economic integration and create more supranational political institutions and policies. It set a framework for eventually creating a monetary union.

Triple helix Describes a close, collaborative relationship between universities, private industries, and government designed to increase knowledge sharing, technological

innovation, commercialization of new products, and regional economic development.

TRIPS (Agreement on Trade-Related Aspects of Intellectual Property Rights) An agreement within the WTO that requires countries to provide minimum standards of protection for copyrights, patents, trademarks, and other forms of intellectual property.

Troika A group composed of representatives from the European Commission, the European Central Bank, and the International Monetary Fund that has administered financial bailouts for economically troubled Eurozone countries such as Greece and Ireland. When negotiating the terms of a rescue plan with a debtor country, the group typically requires the country's government to impose austerity measures and other painful economic reforms in exchange for receiving billions of euros to help pay back creditors.

Unipolar An international security structure in which only one state has overwhelming military and economic power.

United Nations Conference on Trade and Development (UNCTAD) Created in 1964, UNCTAD is a UN General Assembly institution that reflects the interests of developing nations on trade and development issues. Meeting every four years, it frequently counters the perspectives of the IMF, the World Bank, the WTO, and the Organisation of Economic Co-operation and Development (OECD).

United Nations Framework Convention on Climate Change (UNFCCC) An environmental treaty signed at the 1992 Earth Summit and later modified, resulting in the Kyoto Protocol.

United Nations High Commissioner for Refugees (UNHCR) A UN agency with a staff of more than 10,000 that provides emergency assistance and protection to millions of displaced people around the world—including refugees, asylum seekers, and internally displaced people—and helps them return home or resettle in another country.

Unmanned aerial vehicles (UAVs) The formal name for drones—small, remotely controlled aircraft that the United States has used extensively in Afghanistan, Pakistan, Iraq, Syria, and Yemen to conduct aerial surveillance and target terrorists with missiles. Many other countries have surveillance UAVs, and Russia, China, Iran, and Israel build their own missile-firing drones.

Uruguay Round Negotiations from 1986–1994 among the members of the General Agreement on Tariffs and Trade that focused on reducing trade barriers on manufactured goods, services, and agricultural commodities. It culminated in the creation of the World Trade Organization.

Vertically integrated A term describing a firm that owns its entire supply chain. A vertically integrated firm produces some of its raw materials, does its own manufacturing, and often controls wholesaling and retailing of its products.

Voluntary export restraints (VERs) Agreements that limit the quantity of a good that one country can export to another. Importers ask exporters to "voluntarily" set limits on the numbers of exports, backed by an implied threat of economic sanctions or some form of retaliation if the exporter does not comply with the importer's request. Also called

voluntary export agreements (VEAs).

Warsaw Pact Formally called the Warsaw Treaty Organization. A political and military alliance between the Soviet Union and seven of its allies in Eastern and Central Europe. Formed in 1955, the Pact was a counterbalance to NATO that also helped the Soviet Union solidify its control over communist countries in Eastern Europe.

Washington Consensus The neoliberal viewpoint, often evidenced in the recommendations of the U.S. Treasury Department, the World Bank, and the International Monetary Fund in the 1980s and 1990s, that less developed countries should adopt policies to reduce inflation, lower government budget deficits, privatize state enterprises, and deregulate markets.

Weapons of mass destruction (WMD) Technologically sophisticated weapons such as nuclear, chemical, and biological weapons that have the potential to indiscriminately kill large numbers of people.

White Helmets A common name for the Syrian Civil Defense, a large group of volunteer rescue workers who work in rebel-held areas of Syria, saving civilians in buildings that have been bombed and tending to people injured during fighting.

World Bank Officially called the World Bank Group. An international financial institution created by the Bretton Woods agreements in 1944. Today it makes low-interest loans and gives grants to less developed countries to stimulate economic development.

World Health Organization (WHO) A UN agency established in 1946 that directs and coordinates international public health initiatives, often in partnership with governments, NGOs, and private foundations. It also monitors global health trends and provides expertise to governments to help achieve national health objectives.

World Trade Organization (WTO) A multilateral organization created at the end of the Uruguay Round of trade negotiations in 1995. The WTO administers trade agreements such as GATT, GATS, and TRIPS, serves as a forum for new multilateral trade negotiations, and resolves trade disputes between countries.

Zero-sum game An interaction whereby gains by one party create equal losses for others. The concept plays a major role in the realist-mercantilist perspective.

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