Stiglitz on Globalization and Development, with an Eye to Keynes

DAVIDE GUALERZI*

Department of Economics, University of Pisa, Italy

ABSTRACT *In an influential recent book Joseph Stiglitz has laid out in a compelling story many of the issues central to the debate on globalization. Globalization has become a contentious issue because the economic policies advocated for and, at times, almost imposed upon developing countries by international organizations like the International Monetary Fund, the World Bank and the World Trade Organization are based on misconceptions about how market systems work. Market fundamentalism underlies the entire policy framework of the Washington Consensus. The limits of this approach are nowhere clearer than in the examples presented by developing and transition economies. Many policy missteps could have been avoided by adopting the main insights of traditional Keynesian theory, whose basic lessons remain valid, even if it has been largely excised from the IMF's recipe book. The results of twenty years of market fundamentalism make clear that globalization and development are distinct issues, and that the former does not necessarily entail the latter. To understand how they are connected we need to supplement macroeconomic analysis with studies of how international economic integration comes about.*

1. Introduction

A recent book by Joseph Stiglitz (2002a)[1] has become a central piece of the debate on globalization. The book is based on Stiglitz's experiences as chairman of President Clinton's Council of Economic Advisors from 1993 and then as chief economist for the World Bank from 1997 until he resigned in January 2000. He writes in his Preface that 'what I saw radically changed my views of both globalization and development…. I saw firsthand the devastating effects that globalization can have on developing countries, and especially the poor in these countries' (p. ix). The book discusses the major topics of the

* *Correspondence Address*: Department of Economics, University of Pisa, Via Ridolfi, 10, Pisa, Italy. E-mail: Gualerzi@ec.unipi.it

globalization debate in light of the facts of the last two decades, during which globalization imposed itself as *the* issue for the world economy. Stiglitz disputes the effectiveness of neo-liberal policies, contrasting theory and evidence in the strategies pursued by international institutions like the IMF and the World Bank. Stiglitz paints a disturbing picture of a policy framework inspired by an ideology of the market, rather than by a careful analysis of how markets operate.

2. Globalization and Global Institutions: The Washington Consensus

Indeed, 'the promise of Global Institutions', as the title of Chapter 1 reads, was never achieved. One of the reasons is that the proponents of globalization have been 'even more unbalanced' than the critics, who 'too often overlook its benefits'. To its proponents, 'globalization (which typically is associated with the acceptance of triumphant capitalism, American style) *is* progress; developing countries must accept it, if they are to grow and fight poverty effectively. But to many in the developing world, globalization has not brought the promised economic benefits' (p. 5). This is why, although it is 'a force that has brought so much good' (p. 4), it has become such a controversial issue.

This force is identified with the growth of world trade and the improved economic conditions it fostered in many countries. Export-led growth benefited Asia in particular, integrating it into a growing world market. But foreign aid is also part of the growing interconnectedness of the world economy and it has had beneficial effects. The problem is that this is only one part of the story. The list of shortcomings is long and includes episodes in Africa, Asia and Latin America.

[1] Except where indicated otherwise, all page numbers in what follows refer to this book.

A fundamental aspect of globalization is the creation of new institutions that have played a central role in shaping the rules of the game. Thus, 'to understand what went wrong' (p. 10) we have to look at three institutions: the International Monetary Fund, the World Bank and the World Trade Organization. These institutions emerged from the Bretton Woods agreements in the aftermath of the Second World War. Their purpose was to sustain the reconstruction effort and ensure postwar global economic stability. The IMF in particular 'was charged with preventing another world depression'. Though born out of Keynesian ideas, these institutions have embraced what Stiglitz labels 'market fundamentalism', following the political shift initiated in the US and the UK in the 1980s by Ronald Reagan and Margaret Thatcher. Indeed, 'Keynes would be rolling over in his grave were he to see what has happened to his child' (p. 13).

The experience of the 1990s was dismal for many economies: 'The IMF has made mistakes in all the areas it has been involved in: development, crisis management, and in the countries making the transition from communism to capitalism' (p. 18). Rather than controlling economic crises and fostering development the global institutions have made globalization an issue of conflict and confrontation. IMF structural adjustment policies were no remedy to crises and instead caused social unrest. They mainly benefited those who were already well off, while usually leaving unchanged or even worsening the conditions of the poor.

The shift from a Keynesian orientation, stressing 'market failures and the role for government in job creation' to the 'free market mantra of the 1980s' (p. 16) was part of a new Washington Consensus, involving the IMF, the World Bank and the US Treasury, as to the right policies for developing countries. But global institutions are not democratic in the most literal sense of the word; some countries hold a disproportionate share of power. These institutions are dominated not only by the Western powers, but by specific

constituencies, in particular by the commercial and financial communities. Thus, it is the representation of interests within the institutions that explains the sometimes enormous difference between the official advice and what developing countries saw as needed. Consequently globalization is now often met with disillusion and strong opposition.

'Globalization itself is neither good nor bad,' Stiglitz remind us, but it benefited those countries that embraced it on their own terms, as East Asia countries did. For others it was 'an unmitigated disaster' (p. 20). However, he argues that 'globalization can be reshaped' and if 'properly, fairly run ... there is a possibility that it will help create a new global economy in which growth is not only more sustainable and less volatile but the fruits of this growth are more equitably shared' (p. 22).

3. The Case for Development

The failure of global institutions is first and foremost evident in the fact that in developing countries throughout the world 'the gap between the rich and the poor' if anything 'has been growing' (p. 24). Neither the eradication of poverty through development, nor the fostering of development through trade, nor global macroeconomic stability in a new world order has been achieved.

Over and over again economic policies pulled from an abstract book of recipes were suggested and imposed with little consideration for the fact that they might be inappropriate and indeed extremely harmful in the early stages of economic development. A barely disguised colonial mentality persisted in the presupposition that the international institutions knew best. Economic policies based on a blind adherence to orthodoxy led development experts and policymakers to ignore reality. Nowhere was the clash clearer than in Ethiopia. There financial market liberalization was imposed as a condition for IMF assistance, when in fact the Ethiopian banking system—well designed for a largely rural

country—was highly efficient at providing credit to farmers. But ‘to the Fund, a liberalized financial system was an end in itself’ (p. 31). Detailed knowledge was generally thought to be unnecessary, because the IMF advice to developing countries, and the conditions that went with it, were based on a ‘one-size- fits- all’ approach.

To further illustrate the point, Stiglitz contrasts the failure in Ethiopia with Botswana’s success. In Botswana prudent and sensible economic policy was the result of a much better relationship with outside advisors and stemmed essentially from this government’s commitment to maintain political consensus and national unity around the development strategy. When faced with a crisis Botswana did not adhere to IMF prescriptions, and this appears nothing less than the continuation of a wise course of policy followed since independence. Democratic rule meant some income redistribution policies and investment in physical and human capital, with high primary school enrolment. Economic policy was marked by the pervasive role of government, pursuing macroeconomic stability and negotiating the exploitation of its main resource, diamonds, with foreign investors. State-owned enterprises, financial and non-financial, played a fundamental role in the success story.

But Botswana is a peculiar case. A country of only one and a half million people, in large part semi-desert, with about twice as many cows as people, it saw its bright star in the discovery of diamonds right after independence in 1966. The large consensus enjoyed by the Botswana Democratic Party was the condition for a stable democratic government that, directing the substantial revenues of the minerals policy to investment, promoted both growth and human development. One fundamental aspect of this consensus appears to be the creation of tribal land boards that oversaw land allocation without disrupting traditional land tenure arrangements.

4. The Pillars of the Washington Consensus

In Chapter 3 Stiglitz discusses more explicitly the principles guiding the policies of the global institutions. The three pillars of the Washington Consensus are '[f]iscal austerity, privatization, and market liberalization' and they dominated development policy in the final two decades of the twentieth century (p. 53). These guidelines emerged in response to the rampant inflation and huge deficits of the 1980s in Latin America. While they made 'considerable sense' for the purposes for which they were originally designed, they became 'ends in themselves, rather than means to more equitable and sustainable growth.' And they were fully inadequate to face the early stages of development or transition to the market economy.

Privatization of course is preached on the assumption that it will lead to greater efficiency, as state-run economic activities and firms pass into the hands of private entrepreneurs. However, it would be a mistake to assume that markets arise quickly, and the private sector can be slow to take over activities that were previously done by the state. But in the 'narrow ideological perspective [of the IMF and the World Bank] privatization was to be pursued rapidly' (p. 54). This may enhance monopoly power, and it greatly increases social costs. Instead, privatization must be part of a larger policy design where 'Timing (and sequencing) is everything' (p. 57). A striking symptom of the failure of privatization is corruption. Privatization was supposed to eliminate 'rent seeking' on the part of government officials, either in the form of bribes or of cronyism. In reality it became a channel for corruption, to the point of being referred to as 'briberization' (p. 58). This is not surprising, since the same corrupt government officials were in charge of the privatization of state enterprises.

Liberalization means the removal of the obstacles to the market, in particular, trade barriers and government interference in financial and capital markets. While the potentially

disastrous consequences of excessive financial and capital markets liberalization are now recognized, the dismantling of trade barriers still enjoys almost undisputed support. But trade liberalization has proven beneficial only to countries, like those of East Asia, that pursued it 'slowly and in a sequenced way' (p. 60). It had negative consequences when no steps were taken to counteract the impact on employment and wages. Moreover trade liberalization is marred by an 'unfair trade agenda', in which developing countries are told to open up their markets, most recently to the trade of services, while they are cut off from access to rich countries' markets, which were and are protected. But countries in Latin America that have followed the IMF and World Bank recommendations, especially those concerning the liberalization of the trade in services, have experienced the disastrous results of that policy.

The theoretical foundations for liberalization are considerably weaker, observes Stiglitz, when it comes to financial markets. In this case liberalization implies the abandonment of regulation in the domestic market and allowing penetration by powerful foreign financial institutions. This, it is argued, is necessary to attract capital. But the case of China, a recipient of significant capital inflows starting in the 1990s, suggests that to be untrue. It is also argued that capital market liberalization would promote stability, a claim Stiglitz derides as 'laughable in light of the financial crisis that began in 1997' (p. 67). The IMF and the World Bank have been stressing bank stability, when in fact the displacement of local banks by foreign banks is one of the most destructive features of financial market liberalization. Here the case of Argentina is particularly instructive. Argentina's downward spiral started precisely because of the lack of finance for local business just when the system needed desperately to get back on its feet.

5. The Role of Foreign Investment

Stiglitz notes that 'Foreign investment is not one of the three main pillars of the Washington Consensus, but it is a key part of the new globalization. … Privatization, liberalization and macrostability are supposed to create the business climate attracting investment, including from abroad' (p. 67). But here again, what needs to be told is a story in which more efficient production methods, and therefore lower prices, destroy local producers. And when competition has been replaced by monopoly power there is nothing to prevent prices from rising. Furthermore, foreign investment can easily extort privileges from local government officials through bribery—all the more so when what is at stake is free access of foreign companies to the exploitation of natural resources. Often, then, 'foreign investment comes only at the price of undermining democratic processes' (p. 72). However, the more fundamental issue concerns economic development as such. Foreign investment in a mine, for example, contributes little to the process of development. It may help to create a 'dual economy, where there are pockets of wealth', but a dual economy is not a developed economy. Development requires nothing less than 'a transformation of society' that is well beyond what foreign capital inflows can finance. Hence, 'by unnecessarily corroding the very fabric of society' IMF policies have set back the development agenda (p. 76).

In the success stories of Asia, foreign investment either played no role (Japan and Korea) or it did so because it was kept in check (Singapore, Malaysia and China). And when it did play a role, that was not because of the provision of capital, as the conventional wisdom suggests, or because of the contribution of entrepreneurship, but mainly through the improved access 'to markets and new technology'. In fact, the success of the East Asian economies was the result of growth combined with some policy for social equality. That raises another fundamental issue. Stiglitz argues that, despite some illustrious proponents, inequality is not good or even necessary for growth.

6. Theory and Facts

The secret of the 'East Asian Miracle'[2] is that those countries were successful because they did not follow the IMF advice. It was again the impact of the IMF policies, especially the 'excessively rapid financial and capital markets liberalization', that caused and then exacerbated the downturn set in motion in 1997 by a run of currency speculation. Similarly when the crisis erupted in Russia, the advice—borrowing more in US dollars, despite an already heavy debt burden—eventually precipitated a devaluation crisis in 1998.

These facts, Stiglitz concludes, makes it clear that decision-making was inherently biased, dominated by ideology and politics, as opposed to ideas and frank discussion. He speaks of a strange world of bureaucracy and politics (p. 25) intruding and actually preventing clear thinking and prescriptions based on evidence and facts. Sensible as this is, one wonders whether direct experience and specific knowledge are the only ways to understand complex phenomena. Preference for a case-by-case approach may be appropriate, but should we discard theory altogether? When economists turn into politicians they seem to forget their training, the attitude and the mindset of the scientist, as they also forget what they learnt. Or perhaps what they learnt is the problem.

Stiglitz's answer is that much of the problem lies with market fundamentalism and with ignorance. The latter can only be partially solved. Indeed, not even a large institution like the IMF can have firsthand knowledge of the countries it assists. This almost inevitable shortcoming would then strongly recommend a prudent attitude and a willingness to listen to economists operating on the ground. Instead international

[2] Stiglitz (p. 91) explains that 'The East Asian Miracle' is the title of a World Bank report commissioned in the 1990s under pressure from Japan and 'after the Japanese had offered to pay for it.'

institutions favored a 'good-for-all' approach, as if there were indeed a solid theoretical basis for the strategies they advocated. That outlook guided the uncompromising and rigid posture taken towards countries who sought advice and assistance.

But the theoretical basis rested on the notion that markets are perfect and rapidly lead to desirable outcomes. Economists should know, argues Stiglitz, that markets are *not* perfect and that when it comes to issues like equality, employment and environmental degradation, government intervention is needed. Common sense alone would suggest avoiding rigid ideological views in policy design. Similarly, pacing, prudence and good relationships with local governments and economic advisors are virtues in themselves. All of this can be distinguished from questions that concern theoretical views. Ultimately the claim to a superior understanding was based on an erroneous notion of how markets operate.

As is well known Stiglitz has his own views on how markets work. In the book he recalls the body of theoretical work he has in large part helped to shape, concerning market imperfections and the economics of information (see Stiglitz, 2002b). But then again, weren't the economists of the IMF and the World Bank trained in good western universities, exposed to the best economic thinking?[3] Weren't they exposed to the debate within the profession and to the imperfect markets approach? What did they learn, anyway? There is something missing here.

Politics may get in the way of good economic advice. But it also appears that the economists who advise developing countries are indeed too much immersed in their own

[3] Stiglitz seems to think that this is indeed one of the problems: 'Unfortunately, too often the training of macroeconomists does not prepare them well for the problems they have to confront in developing countries. In some of the universities from which the IMF hires regularly, the core curricula involve models in which there is never any unemployment' (pp. 34–35).

discipline and often have an almost blind trust in their specialized knowledge, to the point of ignoring well-known caveats about market imperfections. This is the most plausible explanation of what is otherwise incomprehensible. In these circumstances a good, 'secular' politician, outside the religion of economics, might have easily foreseen the undesirable consequences of market fundamentalism. Politics should have saved economists from their mistakes.

The problem is that one particular brand of economic theory has become the cornerstone of an ideology and of a political coalition. The advocates of the Washington Consensus favored a brand of theory that suited a certain policy. This cast a considerably different light on the relationship between theory and policy. That economists in the international institutions were prisoners of a misconception of the market is only part of the story. The good-for-all approach was consistent with a certain policy, couched in terms of a strategy for development in the era of globalization.

7. Keynesian Economics

Information asymmetry is the hallmark of New Keynesian theory, but the general thrust of Stiglitz's book enhances just as much the status of old Keynesian theory. Keynes's message permeates the book.

Stiglitz believes the IMF is too pessimistic about the usefulness of government intervention, just as it is far too optimistic view of the market. But none of the pillars of the Washington Consensus would do anything for economic development if not accompanied by appropriate regulation. And the key to macroeconomic policy is the solid, old fashioned Keynesian advice: treat unemployment as an evil that must be kept in check because it is

socially disruptive and because the market will not spontaneously move to full employment. Pursuing economic efficiency requires that the operation of the market to be tempered and regulated by government. And the long-run benefits of particular policies seldom justify the short-run economic distress they inflict. Stiglitz reminds us of the group of economists assembled in the 1970s by Hollis Chenery to work with the World Bank to study ‘how market failed in developing countries and what governments could do to improve markets and reduce poverty’ (p. 13). Finding the appropriate balance between government and markets is precisely the opposite of the neo-liberal reinvention of laissez faire. Over the past three decades, however, Keynes’s analysis has been replaced by a return to Pre-Keynesian positions; fiscal austerity is advocated in the face of economic downturns. Stiglitz has repeatedly, and at times with self-critical inflections, identified this as the core issue.

Asymmetric information theory shows that market failures are pervasive and involve more than involuntary unemployment. In other words, the invisible hand is invisible because it does not exist. This calls market fundamentalism into question, but is it sufficient to address an old problem, underdevelopment, in a new context, globalization? For instance, does it satisfactorily explain why markets would fail either to arise or to work properly in developing countries?

8. The Economists’ Consensus

Before broadening the perspective, it is useful to consider a fundamental idea that the analysis of globalization has taken from economic theory. The ultimate argument for globalization is the idea that the free operation of the market is the indispensable condition for improving living conditions and economic performance. Inequality is an unfortunate, but passing, circumstance. There is an economists’ consensus that needs to be addressed.

Stiglitz explains how trade liberalization can be turned from a sensible premise into a dismal, or at best an ambiguous, policy prescription. In fact most of the time it resulted in job loss and greater inequality, casting a negative light on the world trade agreements framework. Yet, the theoretical foundation of trade liberalization, comparative advantage, is hardly questioned by economists.

The basic premise of the competitive model is that factor mobility is a condition for efficient allocation. But mobility is constrained by the existence of national borders, via the barriers created by culture and institutions. Thus, efficiency can be improved by the mobility of goods. Free trade will then move in that direction by exploiting (relative) comparative advantage via specialization of the national economies. In this perspective, globalization is no more than a step in the process of the integration of world economies driven by the search for greater efficiency. In other words, there is nothing 'qualitatively' different under the sun. The process sped up as a consequence of the liberalization of the movement of factors and goods, with a spectacular integration of financial markets and increasing flows of foreign investment. Since the movement of factors would tend to equalize their rewards, it would be in everybody best economic interest to adhere as much as possible to the free market. Any obstacle to this process, however much camouflaged by appeals to the national interest, is likely to reflect instead the rent-seeking agenda of special interests. In any case, it will result in less efficiency and thus ultimately in a reduction of production and welfare.

These propositions re-establish the competitive model as the point of reference for any policy aimed at fostering growth and development. Thus, it is especially necessary to challenge the 'indisputable' premise that free trade and unimpeded factor mobility necessarily lead to greater efficiency, and consequently to greater welfare, if economic thinking is to be rescued from the ideology of globalization. In other words, it must be

recognized that the theory of comparative advantage can lead at times to disastrous 'specialization' in the developing economies, exposing them to the negative effects of fluctuations of prices in world markets, while creating the basis for a dependency on the imports of manufacturing goods.

Critics of globalization have focused on the lack of equity in the sharing of the advantages brought about by greater integration. But the question posed here is not one of fairness, which is usually circumvented by the insistence that the economist ought not to make value judgments. Even if the unequal distribution of benefits is kept off the table, globalization exposes a more fundamental problem: the limits of the ability of free trade and factor mobility to achieve efficiency improvement. It is the adherence to the basic economic model of competitive markets that reproduces the drive toward policies that have not had the expected results. But the 'indisputable' claims emerge from the very core of economic thinking, not from any small minority within the profession. In fact, reasserting the market as the main mechanism of allocation and the driving force in the expansion of global output has helped to wipe out many of the basic principles of Keynesian economics.

Globalization, or rather the way the argument in favor of globalization is made, is only an extension of the same principle, which asserts itself in changing technological and institutional conditions. Technology facilitates movements of capital and labor, not to mention information. At the same time globalization as a set of policies is defined by the transition to a form of regulation that increasingly shifts power from the national state to the technocratic governance of international institutions. Yet the failures of globalization suggest precisely that trade and the movement of factors of production, do not lead to more even development and are even less a cure for poverty.

9. Alternative Approaches

The criticism of comparative advantage is the basis of alternative theories of development. It has highlighted issues of unequal exchange, deterioration of the terms of trade, and the limits of export-led growth. Theoretical alternatives do exist, as well as a well developed critique. As Shaikh observes:

> the doctrine of comparative costs … is so familiar that it has come to be seen as a truism. Most often, this is presented in the form of the proposition that a 'nation' would always stand to gain from trade if it were to export some portion of the goods it could produce comparatively more cheaply at home, in exchange for those it could get comparatively more cheaply abroad. … But a normative proposition such as this has little value unless it can be shown that free trade among market economies actually operated this way. (Shaikh, 2003, p. 4)

In fact, he continues, each of the main propositions of standard trade theory have been 'widely criticized for its theoretical and empirical deficiencies.' Free trade does what it is supposed to do—it benefits the most advanced countries and firms.

This emerges quite clearly once we examine how the actual process of economic integration comes about. Accordingly, in the rest of this essay I will reconsider the literature on foreign investment and large corporations that came before the catchword 'globalization' gained prominence. Foreign investment directs attention to the motivation and actual dynamics of the process of economic integration, defining what theory should be analyzing. The economists' consensus is quick to point out that the movement of goods is the other side of the movement of factors. Thus, foreign investment is simply the result of factor mobility pursuing that equalization of returns, a process familiar since the work of Ricardo. This proposition can be taken either as an 'undisputable' way to bring us back to the competitive model, or as providing the necessary link between the heated discussion on trade and the analysis of development strategies.

Although there has been a boom of foreign investment in the past decade and a half, the topic is not much prominent in the debate on globalization. Foreign Direct Investment, according to United Nations data, have gone from $US23.7 billion in 1990 to $US119.4 billion in 1997; the tripling in FDI that occurred from 1970 to 1980 and the more than doubling that occurred from 1980 to 1990 pale in comparison to this recent increase. It also well known that labor cost differentials are an important motivation for these investment flows. The size of these differentials is nevertheless striking.[4] This in itself would suggest where to look for the causes of poverty in the developing countries. But wage differentials do not tell the entire story.

In a famous study of direct foreign investment Stephen Hymer (1976) distinguishes between two kinds of international capital movements, direct investment and portfolio investment. The distinction ultimately depends on control. If the investor controls the enterprise then we speak of direct investment, otherwise of portfolio investment.[5] Hymer notes that a well-developed theory based on interest rates differentials exists for portfolio investment. Risk, uncertainty and barriers to capital movements complicate the story, but the basic principle is simple. That principle does not, however, explain direct investment. Hymer shows that actual direct investment behavior is inconsistent with the predictions based on interest rates differentials and has certain quite definite characteristics. Above all the interest rate theory does not explain control, though 'If we wish to explain direct investment, we must explain control' (ibid., p. 23). Investors want control over a foreign

[4] In 1997 the major recipient of FDI was China with almost a third of the total. According to The World Development Report (1995), the hourly labor costs in the textile industry were 0.36 dollars in China and 0.56 in India, as compared to 20.50 dollars in Germany and 11.61 in the US.

[5] Admittedly it is difficult to define rigorously control, and 'the dividing line between some control and no control is arbitrary.' (p.1)

enterprise 'in order to remove competition between that enterprises and enterprises in other countries. Or the control is desired in order to appropriate fully the returns on certain skills and abilities' (ibid., p .25). Ultimately, 'The motivation for the investment is not the higher interest abroad but the profits that are derived from controlling the foreign enterprise' (p. 26).

So market control and differences in abilities to operate in a particular industry explain direct investment, which in turn is the key to the international operations of the firm. The theory of international operations is part of the theory of the firm. It concerns the fact that different nations have different governments, laws, language and economic rules. Direct investment operates to overcome this lack of integration. Indeed:

> This lack of integration can be quite important. It provides a good deal of the interest in the subject of international operations, especially since it may be fast disappearing. In recent years, there has been a great increase of communication between nations, and we may be watching the integration of the world economy or at least the economic integration of broader areas than in the past. The increased international operations may be the result of this, and they may also play their part in furthering integration, just as the emergence of the national firm allegedly did in countries like the United States. (ibid., p. 28)

For the economists' consensus, national differences are barriers to competition that should simply be removed. Barriers to entry are a familiar and important topic within the field of industrial organization. They might apply to firms of different nationality. But the fundamental point is that treating barriers simply as an obstacle to competition removes the entire problem of economic integration, which is the real object of investigation. Thus, Hymer's argument clarifies that the point is precisely to explain how integration comes about, rather than assuming it as if it were an immanent trait of the competitive model. The

very reason for direct investment is the existence of national differences, and these create a need for control. The difference of perspective could not be starker.

Hymer's discussion points to a refocusing of the globalization research agenda. One of the main aims for the positive part of the analysis should be to understand how firms' international operations changed in the new competitive environment after twenty years of technological, regulatory and institutional change. This new focus should provide the ground for an analysis of globalization beyond Stiglitz's discontent.

One enthusiastic supporter of globalization, Kenichi Ohmae (1990), has outlined the logic of these changes in global markets. First of all, he argues, there are very few global products. There are instead global market segments, which are still mostly centered in one country. Second, serving these markets locally requires devoting attention to customers and their demands. Third, the recuperation of high fixed costs requires a larger market. The costs of developing and marketing successful ideas have gone through the roof, so R&D is also now a fixed cost, as is maintaining a trademark and a distribution network. This pushes firms to aim for production on a world scale. And world-scale production goes hand-in-hand with market segmentation at the global level.

More than a decade earlier, Raymond Vernon of Harvard Business School had suggested that world-scale production was appropriate only for standardized products suited to a homogenous world demand. He reached this conclusion by focusing on the rise of new world-scale producers in Europe and Japan competing with US companies that had previously held undisputable primacy (Vernon, 1979).Vernon's theory of international investment took that for granted and focused instead on the relationship between industrialized economies and developing countries (Vernon, 1966). He argues that what determine foreign investment are not costs in the narrow sense of the word, but considerations about innovation, scale economies, uncertainties and lack of information.

Consequently, international investment can be modeled on the product cycle. In the first phase, that of innovation, efforts are concentrated on the national market, with foreign markets being served from this home base. In the phase of maturity and large-scale production, the problem arises of serving foreign markets with local plants. When the product is fully standardized this strategy becomes most attractive and may imply an inversion of trade flows, re-importing the product into the home market.

10. Concluding Remarks

What is most interesting about the approaches to foreign investment and the logic of global markets discussed in the previous section is that they contribute to an understanding of the way economies actually integrate and therefore explain how a global economy emerges. They are theories, to be sure, but theories of a kind quite distinct from the celebration of the competitive model that appears to have led to the policies criticized by Stiglitz. They add something rather conspicuously absent from the current debate on globalization: the notion of a competitive struggle fought by means of investment strategies and local market penetration.

They also reach beyond Keynesian theory, old and new. What is needed is not a demise of theory, but rather appropriate theorizing on the crucial issues for development; such an effort would provide a necessary complement to Stiglitz's critical perspective on macroeconomic and structural adjustments policies. In particular, it can help to address the need for governance based on a different view of globalization.

Stiglitz does an excellent job at raising some fundamental questions. He sends a clear message: if globalization has to be considered an essential and unavoidable

characteristic of the future development of capitalism it must be governed by a more pragmatic and realistic approach to markets. Especially when dealing with developing countries, issues of redistribution, equality and justice will have to take a prominent role. Stiglitz concludes his book by making the case for a sweeping reform of international institutions, explicitly redefining their goals, as against the quiet and half-hearted redefinition the IMF is now attempting. He suggests reforming the IMF and the global financial system; the World Bank and development assistance policy; the WTO and the trade agenda. Perhaps the most disturbing indication of the present state of things is that, despite the success of the book and the broad circulation of Stiglitz's critique of globalization, not much debate on these reform proposals has taken place.

References

Hymer, S. (1976) *The International Operations of National Firms: A study of direct foreign investment* (MIT Press: Cambridge).

Ohmae, K. (1990) *The Borderless World: Power and Strategy in the Interlinked Economy* (New York: HarperCollins).

Shaikh A. (2003) Globalization and the myth of free trade, Conference on Globalization and the Myths of Free Trade, New School University [http://homepage.newschool.edu/ ~AShaikh/globalizationmyths.pdf].

Stiglitz, J. (2002a) *Globalization and its Discontents* (New York: Norton).

Stiglitz, J. (2002b) Information and the change in the paradigm of economics, *American Economic Review*, 92, pp. 460–501.

Vernon, R. (1966) International investment and international trade in the product cycle, *Quarterly Journal of Economics*, 80, pp. 190–207.

Vernon, R. (1979) The product cycle hypothesis in a new international environment, *Oxford Bulletin of Economics and Statistics*, 41, pp. 255–267.