The State as a Key Driver of Economic Globalization
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Introduction

The period of economic globalization after the Second World War has been characterized by an increase in transnational trade, foreign direct investment (FDI) and a growth in transnational corporations’ activity. The globalization process of the economy has been intensified in terms of production and exchange due to technological changes, liberalization and deregulation allowing new forms of economic organization influencing the behavior of TNCs as a driving force of economic globalization. According to the hyper-globalization thesis, markets as a...
result have become fully integrated restricting national economic policy-making to “market-friendly policies” as the need to provide incentives to “footloose” TNCs to invest has caused a significant reduction in the state’s domestic capabilities. Despite these arguments, there appears no unambiguous evidence that economic globalization as the transnationalisation of production has caused the inevitable demise of the state in terms of capacity and autonomy. Skeptics of the hyper-globalization thesis emphasize that TNCs and their economic activity despite the technological improvements in communication and transportation remain concentrated in their home countries making them subjected to national control implying economic policy instruments stay effective. Furthermore, the volume of international trade during this period is unprecedented when compared to the level of international economic integration, primarily between industrializing Western states and their colonies, during the late 19th until early 20th century.

The role and power of the state are nonetheless changing but, given the importance of location and territoriality, remains an important actor. The decisions of TNCs are not solely driven by production costs but by a combination of factors, including the availability of skilled labor and infrastructure, contributing to a relationship between states and TNCs based on a complex distribution of benefits. Globalization is more than an

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economic process affecting prosperity as the geo-political and national contexts have to be taken into account and governments play a regulatory role. Furthermore, states can manipulate their economic performance as policies influence international competitiveness ensuing a globalizing economy depicted by an ‘uneven process rather than an end-state’. Trade, for example, remains concentrated among the industrialized states and increasingly involves newly industrialized countries. The international financial system dominated by transnational financial institutions, on the other hand, is far more globalized than trade or production given the high level of mobility of capital movements and financial transactions. This evolution did impose policy and regulatory constraints on states leading to a greater loss of monetary autonomy.

This research paper intends to identify the conditions under which states push, impose, shape, and resist the economic globalization of production and trade, and when they promote or discourage the transnationalisation of their home-based TNCs. The research question concerns the role of the state as a key driver of economic globalization, discussed in the second chapter, when pursuing its policy objectives while looking at the underlying logics and ideologies. The function and influence of TNCs are analyzed in chapter three while international organizations and trade arrangements are evaluated in the fourth chapter. A comparison between the United States (US), Japan and East-Asian countries in the fifth chapter illustrates these developments in practice.

Role of the State in Economic Globalization

There is no ‘single universal model’ for the interaction between economic globalization, states, and their political and social priorities. States can deploy a range of strategies to use the ‘opportunities offered by international markets’ caused by differences in competitive advantages determining a state’s willingness to participate in the international economy. A state’s

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economic power influences its policy options available in promoting international competitiveness, determining its vulnerability and ability to shield itself against the negative implications of economic globalization\(^\text{17}\). The level of integration in the international economy as a result has been uneven as FDI and TNCs have been concentrated in certain economic sectors and industrialized states\(^\text{18}\). This confirms the necessity of states to retain their capacity and abilities to pursue particular policy goals as ‘there appears to be a relationship between economic performance and political power’\(^\text{19}\).

As a consequence, it is useful to make a distinction between strong states and weak states when considering the impact of economic globalization. The strength and adaptability of a state are determined by its size, resources, geo-strategic advantages, and economic strength. From a realist perspective, strong states are able to shape the rules and institutions of the international economy according to their own interests. They control, to a certain degree, the pace and nature of their integration into the international markets by using protective barriers such as subsidies, import quotas, and tariffs to defend their strategic sectors and intellectual property rights. At the same time, they have the ability to penetrate the markets of other states where they have a competitive advantage leading to selective trade liberalization. To this category belong the industrialized states\(^\text{20}\) and newly industrialized countries\(^\text{21}\). Weak states, on the other hand, have little influence concerning the setting and enforcing of international rules. They have limited control over the extent they become integrated into the international economy to the point of “coercive liberalization” and “forced harmonization”\(^\text{22}\).

Strong states become identified as drivers of economic globalization by exploiting the opportunities of the international economy when they promote the transnationalisation strategies of their

\(^{22}\) To this group belong the G-7 countries which are the US, UK, France, Germany, Italy, Canada and Japan.

\(^{23}\) South Korea, Taiwan, Singapore and Malaysia.


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national firms. Economic globalization can be used by strong states as a form of “soft power” when pursuing geo-political objectives using ‘competitive and coercive political and economic tactics’. Furthermore, strong states, are in the position to reverse national policies, impose restriction on FDI flows, and abandon international arrangements when these no longer appear in their interests. From a more constructivist perspective, strong states’ interests are influenced by the social structures of interaction when generating and forming “universal” ideas and beliefs concerning the international rules.

**Relationship Between the State and Transnational Corporations**

TNCs are both cause and effect of economic globalization and will often pressure for trade liberalization according to their own interests, however, an issue that occurs is how employment, exports, technology, and profits are affected by their foreign activities. The objectives of the TNCs and states as a consequence can diverge or even be conflicting. Especially unskilled and low-skilled workers from industrialized states might be negatively affected due to substitution by low-wage laborers from developing countries. In this case, there could be a rise in the relative demand for high-skilled workers in the home country of the TNCs implying, in Gramscian terms, the existence of a “historical bloc” compromising the interests of both capital and high-skilled labor. As a result, it is important to take into account the relationship between the interests of TNCs and governments as there appears to be no universal relationship between these international actors.

According to mercantilist arguments, TNCs are considered as instruments for the strong states’ economic expansion and their foreign policy objectives. This has been enhanced by shared interests as the gains of the transnationalisation of production have primarily been going to

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23 Weiss, “Globalization and the Myth of the Powerless State”.  
29 O’Brien and Williams, Global Political Economy; Intriligator, “Globalization of the World Economy”  
31 Robert Keohane and Van Doom Ooms, “The Multinational Enterprise and World Political Economy” International Organization 26 (1972); Lipset, “Home and Host Country Effects of FDI”. 


industrialized states. These overlapping interests between states and TNCs in the process of economic globalization constitute a ‘complementary profit and power maximization strategy’. States have more specifically been using home-based TNCs to exert and increase their power and influence in other states. Despite the fact that TNCs operate in multiple countries, they often have a particular state considered as their “country of origin” where they retain most of their assets, production, sales, employment and R&D activities. The country of origin benefits of TNCs, and FDI depend on the characteristics of a small number of industrialized states that function as home countries.

Strong states, while keeping ‘high value-added activities’, research and development activities’ in their own countries, have pressed for the opening of developing states their economies in order to repatriate profits back to the home country. Not only access to emerging markets has been facilitated but TNCs will also try to invest in ‘profitable, high-income markets’ and states with ‘better skills and production conditions’.

As a result, industrialized states have cooperated with TNCs and engaged in trade liberalization when this was deemed to be in their own advantage. This implies that TNCs are regarded as creators of wealth within the international political economy which increases the importance for states to collaborate with them in order to achieve ‘economic, political and social goals’ under the ‘expectation that profits made abroad will be repatriated back to the country of origin’. This is evident as TNCs have been supported by their home countries in terms of R&D funding, intellectual property rights and market protection in order to create comparative advantages for reasons of ‘national interest and political strategy’.

Industrialized states have been essential in creating the necessary conditions for...
the transnationalisation of production and the general implementation of economic globalization yet, in the case of conflicting interests, they have the capacity to restrict the activities of TNCs42.

**Relationship among the State, International Organizations, and Trade Agreements**

National governments have established international organizations in order to regulate the international economy43. From a realist perspective, international organizations are reflecting the interests of the industrialized states in the globalizing markets44. The strong states have designed and established international organization and trade agreements supportive of economic globalization and can use these as political instruments to ‘shape international economic decision-making and policy in their interests’ such as influencing access to markets45. After the Second World War, the Bretton-Woods institutions such as the International Monetary Fund (IMF), the World Bank and later the World Trade Organization (WTO) have contributed to the reconstruction of an international economy characterized by ‘liberal market-orientated global capitalism’ due to the influence of the industrialized states46. Developing countries have been pressured into the liberalization of their economies as economic globalization has been implemented upon them by the Bretton-Woods institutions using conditionality to force these countries to commit to trade liberalization and deregulation47.

International trade has been regulated through rounds of the General Agreement on Tariffs and Trade (GATT) negotiations as industrialized states reduced their tariff barriers during the 1960s. A structural break, however, came in the 1970s when previous efforts of trade liberalization were undone because of renewed protectionism in the form of non-tariff barriers during the oil crisis. These imposed trade restrictions, intended to ‘keep out the new competitive imports from successful developing countries’, violated the principle of non-discrimination and proved that the GATT was unable to restrain the industrialized states48. International agreements on trade and investment such as the OECD's Multilateral Agreement on Investment, the GATT's Uruguay Round on Trade-Related Investment Measures, Trade-Related Intellectual Property Measures and General Agreement on Trade-in-


44 Woods, “International Political Economy in an Age of Globalization”.


Services, and the Multi-Fiber Arrangement present a combination of economic liberalization and protectionism in favor of TNCs linked to the industrialized states\textsuperscript{49}.

**Case Studies**

The international economy is concentrated in and between three major economic regions which are ‘Japan and the newly industrialized countries of East-Asia, Western Europe and North America’\textsuperscript{50}. It is in these “Triad” economies that the ‘most powerful TNCs are headquartered’\textsuperscript{51}. The transnationalisation of production after the Second World War was first driven by TNCs from the US while in the 1960s European and Japanese TNCs were expanding their overseas activities and the East-Asian newly industrialized states followed in the 1990s\textsuperscript{52}. Using the theoretical determinants of economic globalization developed in this paper, a comparison between the US and strong Asian states such as Japan and the newly industrialized East-Asian economies is made.

\textsuperscript{51} Gill, “European Governance and New Constitutionalism”, 7.
\textsuperscript{52} O’Brien and Williams, *Global Political Economy*; Perraton et al., “Economic Activity in the Globalizing World”.

**United States**

Neo-liberal thinking, linking individual freedoms to market freedom, has been a dominant ideology in the US influencing its foreign policy\textsuperscript{53}. The US, engaged in a geo-political rivalry with the Soviet Union during the Cold War, has been a key driver of economic globalization pushing for the international economy to be opened up to trade\textsuperscript{54}. During the 1950s, TNCs were primarily headquartered in the US complementing its general dominance of the international economy\textsuperscript{55}. US-based TNCs, striving to expand their export markets, lobbied the American government to secure reciprocal tariff reductions during the GATT negotiation rounds in the 1950s and 1960s\textsuperscript{56}. This geographical expansion of US-based TNCs has been related to the foreign policy agenda and international political dominance of the US as hegemon\textsuperscript{57}. As a result, the US government has helped its TNCs gain competitive advantages and has occasionally engaged in the active support of firms operating in the European and Japanese economies\textsuperscript{58}. An example includes the controversial aid to its semiconductor industry confronted with severe competition from Japanese TNCs in the 1980s\textsuperscript{59}. Outward FDI from the US and US-based TNCs have created additional sources of foreign profits through direct investment during the 1950s in the

\textsuperscript{53} Harvey, A Brief History of Neoliberalism.
\textsuperscript{54} Agnew, "Putting Politics into Economic Geography".
\textsuperscript{55} Mitchell, “Nature and Government of the Global Economy”.
\textsuperscript{56} Agnew, "Putting Politics into Economic Geography".
\textsuperscript{57} Pauly and Reich, “National Structures and Multinational Corporate Behavior”.
\textsuperscript{58} Holton, *Globalization and the Nation-State*.
\textsuperscript{59} Yeung, “Capital, State and Space”.
advanced manufacturing industries of Western Europe and since the late 1980s in East-Asian and Eastern European markets.

A Marxist interpretation of the transnationalisation of US-based firms focuses on the complementarily between the interests of the dominant capitalist class having ownership in TNCs searching for additional sources of profits and the objectives of the US related to its foreign policy and “American imperialism” at the expense of developing countries. The impact of transnationalisation of US-based firms on employment indicates there is some empirical evidence of a 'shift toward more capital-intensive and skill-intensive production in the US, as labor-intensive, and particularly unskilled labor-intensive production has been allocated to affiliates in developing countries'.

There are examples of conflicting interests between the US government and its home-based TNCs leading the US government to intervene in its activities through the use of the “Trading with the Enemy Act” or by issuing economic sanctions against countries such as Cuba and Iraq. The US has also come into conflict with other industrialized states in the 1970s because of the implementation of an international political and economic framework benefitting US-based TNCs. The Bretton-Woods system, according to hegemonic stability theory, has been dominated by the US as a necessary precondition in the setting up of a liberal system of free trade while allowing the US to extend its economic power into political leverage on the international level. The dominance of the US is visible in the IMF as it is the only country with veto power. This became more evident with the way it managed the East-Asia crisis of 1997-1998 by preventing countries from defaulting against US-based banks through an IMF intervention. The Marshall Plan and NATO for example have also been instrumental in creating the political conditions allowing for US-led economic globalization. The WTO is another international organization that has reflected US interests through its rules, policies and protocols concerning tariff regulation and trade liberalization. The US managed to get concessions from developing countries while at the same time ignoring sanctions and being non-compliant with unfavorable WTO directives or rulings from disputes.
Japan and East-Asia

Japanese outward FDI increased significantly in the 1980s as a strategy of ‘acquiring global economies of scale, access to international technology and getting a foothold in the markets’ of the other industrialized states, and was later followed by East-Asian newly industrialized states in the 1990s. Japan as a strong state has been able to integrate into the international economy on its own terms and for its own economic interests. It has resisted the forced implementation of foreign and international standards and refused to give up its protectionist policies, denying access to strategic sectors, during several years of WTO negotiations. TNCs from the newly industrialized states have proven to be highly competitive players in the international economy for the past three decades in specific industries where they have gained competitive advantages as industrial policy remains an important part of economic governance. Strong states in this region have, for strategic economic reasons, played an active role in driving the transnationalization process of its home-based TNCs by providing national firms moving abroad with ‘developmental infrastructure, inducements and government-business relations’ and establishing state-owned TNCs.

Important to keep in mind are the “evolutionary dynamics” in the success of these East-Asian countries and the changing role of TNCs as drivers of economic globalization. In the early phase of this process, from the 1950s until the 1970s, we can speak of a mercantilist tendency as these “developmental states” used industrial policies to help with the successful industrialization and transnationalization of their “national champions” and (former) state-owned enterprises. The use of an active industrial policy is “anti-neo-liberal” and contradicts the American approach of economic liberalization. But since the 1980s and 1990s, these firms have increasingly gained more autonomy as the strategic partnership these firms had with their home states has shifted towards other firms further integrating the East-Asian economies into the international economy. But in the aftermath of the 1997-1998 East-Asian crisis there have been ‘aggressive attempts to globalize these economies from outside’ due to the conditionality imposed by the IMF.

73 Yeung, “Drivers of Globalization”.
75 Yeung, “Drivers of Globalization”.
76 Sassen, “Making the Global Economy Run”, 411.
Conclusion

In the process of economic globalization, increasing the volume of transnational production, trade and investment, the state has remained a key player in the international economy. The hypothesis presented in this paper is that the state has played an active role in promoting and facilitating economic globalization by creating the necessary conditions to reach its political and economic goals. This implies that economic globalization and further integration into the international economy is a political choice and project driven by states and interest groups. An important elaboration of this argument is that the competitiveness of an economy and the general impact of economic globalization depend on the capacity of the state for political intervention in order to regulate international organizations and influence the development of competitive advantages of their home-based TNCs. Strong states have made selective economic globalization possible by implementing the liberalization in certain sectors of the international economy where they have competitive home-based TNC's in order to gain access to the markets of other states.

States have colluded with private economic actors engaged in global economic activity or intervened by obstructing and overriding their actions when these conflicted with national interests of profit accumulation, employment and foreign policy objectives. The most important private economic actors are the home-based TNCs as agents of economic globalization. The level of power a state has relative to TNCs depends on the possible exit options although the balance of power has been shifting in favor of the TNCs due to growing intra-firm trade. Strong states also promote and regulate economic globalization through international organizations and trade agreements, offering a certain degree of international economic governance, in an attempt to privilege home-based TNCs.

The neo-liberal belief of the US in the advantages of trade liberalization and its institutionalization into various international organizations has been a driving force of the economic globalization process after the Second World War and can be regarded as an

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80 Castells, “The Global Economy”;
83 Kobrin, “Sovereignty@Bay”; Intriligator, “Globalization of the World Economy”.

instrument of soft geo-politics in order to gain or strengthen its hegemonic power and stability. The American approach to economic globalization can be considered as one strategy among many as Japan and the newly industrialized states of East-Asia have followed a more mercantilist attitude by using industrial policies.

The conclusion of this paper is in line with realist and mercantilist assumptions of an international economy structured by the capacity of a number of strong states and home-based TNCs which can be considered as instruments for foreign policy and creators of national wealth. Yet there are also elements of liberal theory present given the importance of markets, competitive advantages, and complementarities between economic and political interests and aspects of Marxists theory due to the role played by a capital-owning class with interests in the economic performance of home-based TNCs.

When looking to future developments, there are relatively new forms of state participation in the international economy emerging including government-created “sovereign wealth funds” investing (trade) surpluses abroad which could be used for economic and political objectives. In terms of participants, an emerging economic power such as Russia with a ‘small and powerful oligarchy’ has become increasingly integrated into the international economy since its admission to the G-7 and the WTO adopting a strategy of ‘economic liberalism and authoritarian nationalism’ indicating states can use new and different strategies to secure a place in the international economy.

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