

GLOBALISATION AND SOVEREIGNTY

by

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I want to begin by thanking the McGill Institute for the Study of Canada and Desmond Morton in his role in overseeing the Mallory Lecture. I am most honoured by the invitation to be part of this series but also a little wobbled by the waves of nostalgia as I remember my days as a junior lecturer and the awe we all accorded Jim Mallory as an outstanding and highly respected professor. When I studied economics in those good old days we were still living in the Oxbridge tradition of political economy, so I took classes in sociology and political science and never really recovered from the effect. I have remained outside the mainstream of the minimalist mathematized discipline and continued stubbornly to believe that politics and policy and social institutions and history really do matter. Part of what is embedded in my mind came from McGill and Jim Mallory. And for good or ill it shows up even in the title of my lecture: Globalisation and Sovereignty.

I. Introduction

There is a growing view, approaching conventional wisdom in some quarters, that the power of the nation state is being eroded by globalisation. Decades ago, in his book The End of Ideology, Daniel Bell asserted that the state was becoming too small to handle really big problems and too large to deal effectively with small ones. Perhaps his vision is now manifest. In any case there is little doubt that the accelerating pace of structural transformation of the global economy places increasing strain on the adaptive capacity and hence legitimacy of governments and international institutions. The basic problem of policy lag is now different by a quantum degree. There are two clocks ticking: the clock of accelerating interdependence and the clock of domestic and multilateral decision-making. And there is no sign of synchronization evident.

The first part of this lecture will deal with the effects of globalisation on “sovereignty”. But, as Bell notes, the nation state has proved increasingly ineffective in coping with the everyday problems of its citizens at the local level. One response to this crisis of legitimacy has been devolution. While I do not suggest any systemic linkage between globalisation and devolution -- except, perhaps, the challenge of adaptability -- the devolution trend is spreading both in Europe and, albeit in a different fashion, in the U.S. And, it hardly needs noting, in this country. Thus in the latter part of my talk on the implications of globalisation for Canada, I will briefly highlight some of the main issues in ongoing debate over the division of powers in this country.

II. Globalisation

The much-used word globalisation has never been defined (even though it first appeared in 1986). I prefer the term “deeper integration” which refers to the ongoing process of ever-tighter linkages among countries which has proceeded in stages since the end of World War II. The shallow integration of the early postwar decades was focused mainly on border barriers to trade flows. Reducing these barriers through successive rounds of GATT negotiations clearly involved some degree of constraint on governmental freedom of action but it was limited. Indeed, the original concept underlying the GATT was to maintain a balance between domestic priorities and international obligations.

Global integration began to intensify in the 1970's and 1980's when the liberalization of capital flows and deregulation of financial markets steadily eroded the scope for national monetary and fiscal policies. As the Asia crisis has confirmed, this erosion has been vastly magnified and has raised real questions not only about the benefits

and costs of financial flows but also the legitimacy of the International Monetary Fund (IMF).

By the end of the 1980's a new phase of interdependence had begun, led by a marked increase in foreign direct investment (FDI) primarily in capital- and technology-intensive sectors and services. With international rivalry intensifying, global integration of production is growing as firms use the new information and communication technologies (ICT) to improve their efficiency.

This third phase of integration was and is closely linked to the Information and Communication Technologies (ICT) revolution in (and technological changes in transportation, especially containerization) which made it cheaper and easier to manage far-flung and widely dispersed production networks. And within service industries, rapid developments in these technologies increased tradability and enabled firms to allocate portions of the production process to foreign affiliates. The result of this profound transformation is that the multinational enterprise (MNE) is today the main funnel for the three engines of growth: trade; capital; technology and the bidding war for FDI is ratcheting up.

Moreover, the full impact of the ICT revolution clearly has some distance to go and a fourth phase of global integration is now visible in the growth of electronic commerce. Reflective of the underlying movement in the technology trajectory from "hard" to "soft", and the growing importance of "network markets", especially telecommunications, this new world of cyberspace literally eliminates borders so that the term "domestic policy" could become an oxymoron! Be that as it may, the main issue for the subject at hand is that the steadily deepening integration of the global economy is in

effect creating a momentum to a global single market. Of course we may never arrive at that destination but the pressure for system convergence -- harmonisation of domestic policies and institutions and hence the erosion of national sovereignty -- will be fed by these autonomous economic and technological forces. And the trend to deeper integration has been reinforced by international economic policy in both multilateral and regional fora. This is best exemplified in the trade field with the creation of the first post-coldwar institution, the World Trade Organization (WTO).

III. The Policy Process of Deeper Integration:

(a) Role of the MNE's

The negotiations to launch the Uruguay Round negotiations took almost as long as the entire previous Round of negotiations of the 1970's, the Tokyo Round. The Americans had been trying to launch the negotiations since the early 1980's because of dissatisfaction with the results of the Tokyo Round and rising protectionist fury in Congress (mainly because of the overvalued dollar). After a number of near-failures, the Uruguay Round was launched in Punta del Este, Uruguay in September 1986 and formally concluded in Marrakesh, Morocco in April 1994, several years later than the target completion date originally announced. The extraordinary difficulty in both initiating and completing the Round stemmed essentially from two fundamental factors: the nearly insuperable problem of finishing the unfinished business of past negotiations, most of all agriculture; and the equally contentious issue of introducing quite new agenda items, notably trade in services and intellectual property and, though in a more limited way, investment. The Europeans blocked the launch to avoid coming to grips with their infamous Common Agricultural Policy (CAP) and a number of developing countries were

bitterly opposed to including non traditional issues such as services and intellectual property because they involved negotiation of domestic policies and institutions such as economic regulation and legal systems, alien to the GATT world of shallow integration and considered a direct challenge to national sovereignty. The inclusion of these issues was demanded by the Americans, who were world leaders in these areas, to correct the basic structural asymmetry of the original GATT.

Without a fundamental rebalancing of the GATT, it seems highly improbable that the American business community or politicians would have continued to support the multilateral system for much longer. The role of American multinationals in the ultimately successful launch of the Round was crucial. Confronted by failure to budge the E.U. and the hand-line developing countries and in an effort to increase pressure for a launch, the main U.S. private sector advisory committee sprang to action. In cooperation with other U.S. business groups it launched international initiatives in services and intellectual property and mobilized support in Europe and Japan and other countries such as Canada. Indeed the only instance of effective involvement by many foreign firms in the Geneva activities was due to American business leadership.

(b) Role of the INGO's

While the deeper integration agenda at present largely reflects the agenda of the MNE's, the International Non-governmental Organizations or INGO's are of increasing importance in the policy agenda and process. Virtually non-existent at the onset of the

century, they grew to over 500 by 1990 with most of the growth taking place after the Second World War. Since the onset of the 90's that growth has accelerated, so the INGO's are a relatively new but increasingly pervasive institutional phenomenon.

The INGO's are very diverse in nature but have certain characteristics in common. They are part of a much broader phenomenon now receiving increasing attention under the ill-defined term "civil society", to include all manner of non-governmental institutions or even informal group interactions from philanthropic bodies and professional societies to community sports clubs. A distinction is sometimes made between community-based associations organized around mutual social interests (bowling or charity), and mass membership organizations -- like the environmental, human rights, women's groups -- based on single interests and more akin to traditional lobbyists. These latter groups are, by definition, policy-oriented advocacy groups and thus more relevant in the context of this discussion.

INGO's are flourishing today in large part because of ICT which permits rapid and inexpensive global networking. And they are very skilled in dealing with the media, especially television. They can be termed "transformational coalitions" that are less concerned with traditional interest-group concerns like the division of the pie than with the recipe for making it, and thus their agenda is often at odds with the other players, governments and the MNE's. In a sense they are post-Enlightenment, linked less by a rule of reason than by a rule of morality or values.

The most prominent INGO's at present are the greens and their influence was already evident at the Marrakesh meeting which concluded the Uruguay Round in April 1994 and also established a Committee on Trade and Environment. It is no accident that

the green INGO's were the first to play a role in trade policy at the launch of the renewed multilateral rules-based trading system. In 1994 the implementation of the North American Free Trade Agreement (NAFTA) included specific environmental provisions: the first in trade history. And in 1994, the United Nations Rio Conference on Environment and Development (UNCED) has been described as a watershed event for non-governmental organizations by endorsing their role in international policy-making.

As noted, and should be stressed, the influence of the INGO's as exemplified by the environmental groups, has been greatly enhanced by the ICT revolution, both through agile and skilled use of the media (especially television) and the low cost and global span of communication linkages such as e-mail. The environmental message is especially attractive to a younger generation searching for a moral cause and also (as the recent successful attack on the Multilateral Agreement on Investment (MAI) at the OECD demonstrated) as a rallying point for a wide range of groups opposed to globalisation. But there is a growing North-South divide on many environmental issues -- especially in the realm of trade. Since the most powerful INGO's are based in the OECD countries, and especially in the English-speaking countries, it's becoming less clear how "universal" their messages really are. For this and other reasons, indigenous INGO's are proliferating in some Latin American and Asian countries while Western INGO's are focusing more on Southern environmental problems. In some countries this has earned them the name "eco-imperialists."

To conclude this survey of the growing role of the transnational actors in the global economy I think it's useful to underline two points. First the process of deepening integration is ongoing and in this process the role of the MNE's and INGO's is evolving in

a very rapid and arguably unpredictable fashion. But the second point also needs scoring: inherent in the process is the erosion of sovereignty. But -- and it's a big "but" -- the sovereign state is the only player at the policy table in the intergovernmental institutions (at least so far). In a sense, these institutions were created after World War II as fora for pooling sovereignty. In the trade arena the result was the rules-based trading system, first under GATT and now, fifty years later, in the WTO. Let me then conclude this part of my lecture with a brief look at the mandate and capabilities of this new institution.

(c) Deeper Integration and the WTO

With the shift of policy focus inside the border, the Uruguay Round launched the first small step on the long and difficult path to a rules-based regime for a single global market and the WTO was created to provide the institutional infrastructure for this extraordinary undertaking. But there is growing concern about the capability of the WTO to handle the new agenda which will go well beyond the Uruguay Round. The WTO secretariat is minimal and lacks the highly qualified experts able to undertake policy analytic research as in the other international institutions. Equally serious, the WTO has no executive committee which can provide a forum for policy discussion. Yet the issues the WTO must deal with are fundamental to determining the trade-off between domestic and international objectives and the crucial issue of the state-market frontier. Moreover, in addition to the complexity and contentiousness of the issues, the size and disparate interests of the membership greatly adds to the difficulty of achieving consensus. Further, while the Uruguay Round demonstrated the power of the MNE's in the policy-making process, the role of the INGO's in this process and in the WTO itself has become a major - and highly contentious issue.

I have made a number of suggestions for WTO reform in various publications so won't take the time to review them here. What I want to underline in this lecture is the importance of Canada's role in the evolution of the trading system. In the Uruguay Round, by forming coalitions with other middle powers, that role was very significant in determining the agenda and facilitating the negotiations. Indeed, the WTO was a Canadian proposal, ultimately supported by the Europeans as a safeguard against American unilateralism.

But devising an effective Canadian strategy will face far greater problems today. First of all because the steadily deepening integration of the world economy has generated a backlash against globalization or unleashed "globaphobia". The debate between proponents and opponents of globalization has been going on for several years but recently (perhaps as a sign of millennial angst?) has assumed near-religious overtones. Is globalization Nirvana or Armageddon? The defenders are most trade policy experts and the business community. The main opposition to globalization includes a diverse array of advocacy NGO's, politicians at both extremes of the political spectrum, and a growing legion of nationalists both in Europe and in this country.

Obviously for thoughtful analysts, globalization is neither Nirvana nor Armageddon. The compelling arguments for deepening integration of the world economy are economic. Consumers would be able to buy the best products at the lowest prices anywhere and everywhere. The gains stem not only from the static, once-and-for-all efficiency gains from eliminating barriers and impediments to trade and investment but also, and more importantly, from dynamic efficiencies which increase growth and create new jobs as global competition forced firms to restructure, network, and innovate.

“Global” growth increases; “global” consumers benefit; but the distributional effects of these gains, the distribution of winners and losers both among and within countries, affects the immobile factors of production, land (or the environment) and all but the most highly skilled and educated labour of the nation state. It is, indeed the alleged effects of globalization on labour markets (rising unemployment in Europe and widening income disparities in the U.S. and, to a lesser extent, in Canada) as well as on the environment, culture, social values, etc. which has aroused much of the recent attack on globalization.

Even this brief survey of the globalization debate suggests that to maintain the ongoing momentum to deeper integration of the world economy will not be easy. Yet, I would argue that the genie is out of the bottle. The trend may be slowed but, barring a catastrophe like the 1930’s, not reversed. The dynamic benefits which derive from the increased flows of trade, investment and technology greatly outweigh the structural costs in the view of the most powerful countries, specifically the U.S. and the E.U., and it is they who determine the direction of global policy.

For other countries the main benefit of globalization is the diffusion of technology or, more broadly, of knowledge. Knowledge is the basic source of productivity growth and thus of rising living standards. This maxim is starkly evident in the poverty of the weakly integrated countries, especially in Africa.

But productivity is only part of the story. Mid-sized countries such as Canada have strongly supported the multilateral rules-based system for one simple reason: the alternative is a system based on power. It would not be in our interest to fight a losing battle against deepening integration. Our strategy should be to encourage a meaningful debate on the basic issue of international rules and domestic sovereignty. In terms of our

own country our strategy should be to minimize the costs and maximize the benefits of globalisation. But that requires getting our own house in order which brings me to the question of the “other trend”, i.e. devolution.

IV. The Devolutionary Trend

Canada, if not the most decentralized federation in the world, is close to that title. None the less, as is clear from recent developments including, but not only, the social union arrangements, further devolution is in process. In part this is due to a phenomenon apparent in all the advanced industrialized countries, i.e. the redesign of the postwar welfare state. In a sense, one could argue that the process of devolution in Canada was launched by Federal fiscal policy. But that’s another story.

While health and social security have been the high-profile issues in the current debate about the division of powers between the Federal and Provincial governments, neither the press nor the politicians have mentioned Canada’s international role. Yet think how many times you see or hear the word globalization each day! A devolution of responsibility in one set of policies -- largely related to role of government in social policies -- is quite compatible with an expansion of Federal power in another set related to international issues and, I would argue, issues where there may be interprovincial spillover such as the environment or labour market policies.

As is clear from the description of the new WTO mandate, trade policy is not trade policy anymore. WTO negotiations now or will in the future cover many policies which are either under provincial or joint federal-provincial jurisdiction. These include services, government procurement, investment regulations, environment and food regulations, and perhaps labour market regulations. There must be an effective federal-provincial

coordinating mechanism to ensure that a policy strategy can be devised and that WTO rules, once established, are enforceable. Indeed this issue is important not only for Canada but also other Federal states (such as the U.S.) and the E.U. itself. So Canada should get its own act together and then play a facilitating role in achieving a broader multilateral consensus.

Another, arguably more fundamental issue, concerns the growing global competition for investment. Since foreign investment is a major source not only of capital but of knowledge, the locational decisions of the MNE's can be of great importance, especially to middle-sized countries. Indeed there is an ongoing bidding war of tax and other fiscal incentives which is highly distortionary and should be an urgent priority for any future negotiations on investment in the WTO. (A similar phenomenon is apparent among provinces in Canada, by the way, and has not yet been tackled effectively).

But my main point on locational investment relates to domestic policies and the devolution issue. In the long-run the locational attractiveness of any country is far more important than any fiscal incentive. The essence of locational advantage today is the knowledge infrastructure -- the quality of education and training and of R & D. Yet this knowledge infrastructure in Canada has never been viewed in terms of a national priority. The knowledge sectors are either Provincial -- education and now training -- or joint, as in the case of R & D. The acquisition of knowledge requires a significant knowledge base to start with in order to tap multiple sources of information. For example, the price of entry into a joint R & D agreement for any company is a strategic asset and that involves a rich knowledge base. The knowledge base rests on human resources, scientific, technical and skilled. To them that hath shall be given ---. Of course, the opposite is also true: vicious

circles can develop. The costs of bad policies will be correspondingly higher than in the past.

Despite all this, in Canada no federal-provincial coordinating mechanisms exist and no national strategy exists. Indeed, just as an example, in a world where knowledge is the key asset and technological change has created the need for lifelong learning, the Federal government has transferred all training functions to the Provinces. This has been done at a time when markets for highly skilled labour are no longer local or national but global and Canada is not only competing for investment but arguably more vulnerable to brain drain than any other country in the world because of our location. So, as in the case of “trade” policy and devolution there is a need to update the debate now confined to outworn notions of a division of powers based on the past. Devolution in some areas can be both effective and efficient. But a redefinition of the Federal role and the establishment of meaningful coordinating mechanisms is essential if Canada is to minimize the losses and maximize the benefits of a globalising world.

Finally, the other lesson to be learned from the dramatic and accelerating changes in the global economy is that there is an enormous comparative advantage in a governance system which is flexible and can adapt to or anticipate change. So, again, the concept of devolution per se is simplistic. Whatever the decision on a given division of powers today, it's likely to need some adaptation in the future and the time between now and the future is shrinking.