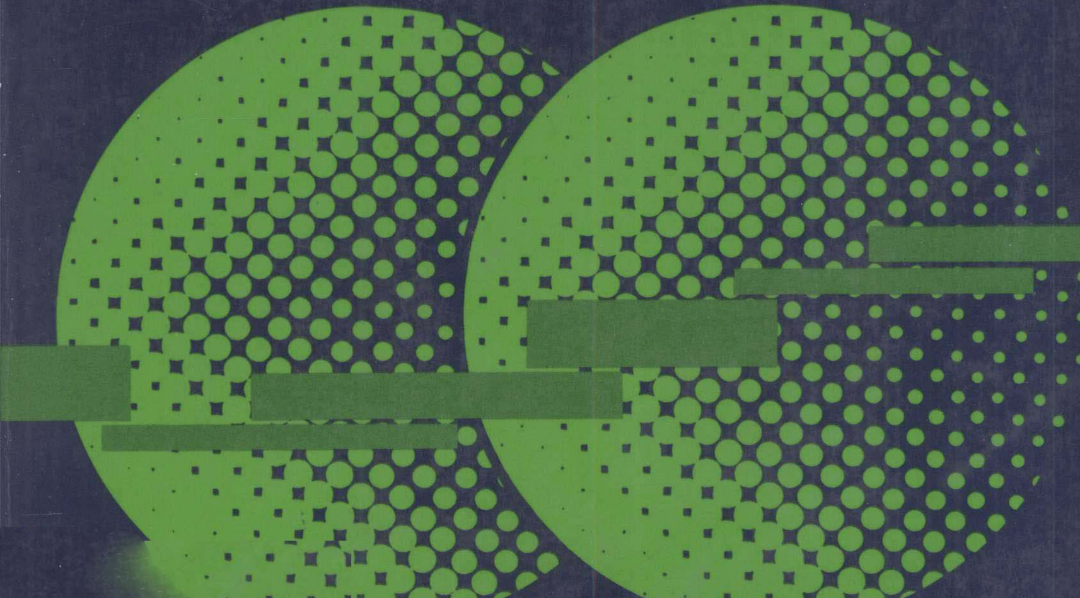
THIRD EDITION

The Politics of Global Economic Relations



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Third Edition

The Politics of Global Economic Relations

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Preface

The structure and analytical approach employed in the third edition of this work remain essentially unchanged since the first appearance of *The Politics of Global Economic Relations* in 1975. This framework has permitted us to discuss myriad changes in international economics that have occurred in the past eleven years. We have witnessed the dollar plunge uncontrollably and then ascend to unprecedented heights in relation to other major currencies and then fall again. Either occurrence poses staggering challenges to the American and global economies. The OPEC states acquired immense wealth and power in the 1970s only to face a collapse in oil prices that makes petroleum producers among the world's most precarious debt risks in the mid 1980s. U.S. trade deficits that were alarming enough to help precipitate the collapse of the Bretton Woods monetary system in 1971 pale in comparison with the trade deficits the United States carried with little sense of crisis a dozen years later. Multinational corporations, which many analysts in advanced industrial countries as well as less developed countries viewed as a threat to the viability of states and the state system in the 1970s, seem to have become an accepted part of the landscape in rich and poor states with diverse political and economic philosophies in the 1980s.

In this edition, as in the previous ones, we try to describe these and other developments as they have affected the politics of international economic relations. But more importantly, we attempt to provide students with the analytical tools to understand the forces underlying these changes. It is important for us to anticipate and comprehend the circumstances that could produce changes every bit as profound as these in the years ahead. We think this book continues to be a useful tool in this regard.

We wish to thank all the students and faculty who continue to find this volume relevant to their work. This is particularly gratifying in light of the greater knowledge about international economic interdependence that today's students bring with them into the classroom compared to their counterparts in the early 1970s.

D.H.B. and R.S.W.
March 1986

To
DAVID, JENNIFER, KIMBERLY, SCOTT, and CLAIRE

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1

Introduction

economic transactions and world politics

Since the early 1970s we have been undergoing a key transition in American foreign policy that in some respects is even more profound than the dramatic foreign policy moves made by the United States immediately following World War II. The Bretton Woods system, membership in the United Nations, the Truman Doctrine, Marshall aid, NATO, and the construction of a complex of alliance systems ringing the Communist world are commonly viewed as evidence of that turning point in United States history when we abandoned our tradition of isolationism (however different its face in different parts of the globe). Through these instruments the United States was seen as having moved into a series of multilateral commitments that saddled it with tremendous responsibilities abroad and circumscribed American freedom of action in ways that the United States had found unacceptable in the past. But the United States during the 1970s and 1980s has confronted a series of foreign economic challenges that are likely to result in even more constraints on its freedom of action than did the agreements in the 1940s.

As an isolationist, the United States could maximize freedom of action in its international relations (economic and political) by avoiding formal commitments; this was a basic theme, for example, in opposition to American membership in the League of Nations. Following World War II, when the United States did bind itself by numerous multilateral commitments in the economic and political spheres, it did so from a clearly preeminent position and, thus, was able in substantial measure to shape the various agreements to conform to American interests. The postwar multilateral agreements were typically of a sort that committed all member states to abide by specified global norms of behavior, which, while ensuring benefits for these countries, also underlined American preeminence. These commitments had the net effect of ensuring America's freedom of action in the globe rather than circumscribing it.

Now, however, the United States is in the process of having to reformulate its foreign economic and political relations to take into account new global realities. America has moved from virtual self-sufficiency in energy to extensive reliance on oil imports. Europe, through the creation of the Common Market, has transformed itself from a junior partner of America to a giant economic rival/partner. Japan's economic miracle and vigorous promotion of exports now threaten the vitality of key industries (such as automobiles, steel, and semiconductors) and hundreds of thousands of jobs in the United States. In numerous rapidly growing economic fields such as telecommunications, computers, ceramics, fiber optics, and biogenetics the Japanese are also threatening American supremacy in commercial applications of new process and product technologies. Newly industrializing countries in the Third World have assumed an important position in the vitality of America's trade and banking. The world's confidence in the dollar as the top international currency waxes and wanes in an era of flexible exchange rates. These and other developments have combined to produce an evolution toward a new global economic and political order in which American preeminence must either decline or be retained at substantially escalated domestic and international costs.

The political significance of global economic relations goes well beyond this contemporary transition in the international position of the United States. The increased sensitivity in economic interdependence among virtually all states compels us to assess the political implications of international economic transactions everywhere. Even if economic transactions between states have grown at a slower rate than have economic transactions within them,[1] the volume and speed with which economic resources can now be transferred between states places tremendous economic and political strains upon them. For example, modern communications and the management capabilities of giant international banks and corporations, which command assets greater than the gross national products of most states, allow massive capital transfers in response to disparities in the market conditions (interest rates, growth rates, wage levels, etc.) and the political milieus of various states.[2] Long-term investments by these economic actors and the movement of their liquid assets in international monetary markets can undermine domestic economic and politi-

[1]See K. Deutsch and A. Eckstein, "National Industrialization and the Declining Share of the International Economic Sector, 1890–1959," *World Politics*, 13, no. 2 (January 1961), 267–99; and K. Waltz, "The Myth of National Interdependence," in *The International Corporation*, ed. C. Kindleberger (Cambridge, Mass.: M.I.T. Press, 1970), p. 208.

[2]For an elaboration of the sensitivity of international economic interdependence and its substantive implications, see Richard Cooper, "Economic Interdependence and Foreign Policy in the Seventies," *World Politics*, 24, no. 2 (January 1972), 159–81. See also Chapter 7 of this book.

cal programs and produce severe conflicts between states. Indeed, some observers of these banks and corporations feel that they may ultimately undermine the contemporary nation-state system itself.[3]

Although international economic relations among private and public actors necessitate profound alterations in contemporary American foreign policy and in political relations among states everywhere, American students of international politics have until recently paid little attention to interrelationships between economic transactions and international politics. This situation must be remedied if we are to understand contemporary global politics and the transition of America's role in the world. A major obstacle to our understanding of these problems, however, was the poverty of conceptual frameworks with which to address systematically the various interrelationships between international political behavior and international economic behavior. It is important to ask why this was the case and what has been done to increase our analytical capabilities for examining these problems.

Analysts of international politics develop conceptual frameworks in order that they may better address what they perceive to be substantive problems of overriding importance. Almost without exception, American specialists in international politics for two decades following World War II saw the Cold War and the defense of the non-Communist world as the substantive focus of U.S. foreign relations. As a consequence, they relied heavily upon paradigms in which security and power relations among states were postulated as constituting the quintessence of world politics. The dominant paradigm (political realism) led to a focus upon states as sole or primary actors in world politics,[4] and except insofar as economic instruments (such as aid and trade) were employed directly in power struggles between states, the distribution of benefits from domestic and international economic relations were seen as lying outside the boundaries of international politics.[5] Within this analytical tradition, international economic transactions such as trade and monetary affairs were typically looked upon as essentially nonpolitical relationships. They were seen as being managed, in the non-Communist world at least, according to politically neutral, technical criteria and administered by functionally specific ("nonpolitical") international organizations such as the General Agreement on Tariffs and Trade and the International Monetary Fund. The study of such affairs was left to international economists, international lawyers, and students of international organizations—most of whom neglected to analyze the larger significance of such transactions (and of international economic organizations themselves) in world politics.

In short, until recently the conceptual frameworks used most frequently by American analysts of world politics tended to relegate economic relationships to the periphery of inquiry; the interrelationships between domestic

[3]See Frank Tannenbaum, "The Survival of the Fittest," *Columbia Journal of World Business*, 3, no. 2 (March–April, 1968), 13–20.

[4]See Hans Morgenthau, *Politics Among Nations*, 4th ed. (New York: Knopf, 1967).

[5]Ibid., pp. 25–26.

and international politics were not examined systematically; and actors other than states received scant attention in studies of international politics. Marxist analyses dealing explicitly with interests and relationships neglected in the dominant analytical tradition of American scholarship on international politics were virtually ignored. These are some important reasons accounting for the poverty of conceptualizing the politics of international economic relations.

However, developments over the past one and one-half decades have brought economic dimensions of world politics back into prominence. New conceptual orientations are fostering systematic analysis of the relationship between international economic and political behavior, in contrast to paradigms focusing exclusively on power and security aspects of world order. Economic security and stability have emerged alongside military security as top-priority foreign policy challenges for advanced industrial as well as developing states. Multinational corporate activities, instability of both the dollar and gold in international financial relations, supply interruptions and price escalations for critical resources such as oil and food, and import surges that displace local production and jobs as well as threaten to unleash trade wars are fueling domestic as well as international political disorders of profound importance. Indeed, in many respects these disorders affect the personal lives of individuals throughout the world more directly than do most forms of international diplomacy focused on maintaining military security.

These problem areas are now widely perceived as being highly salient in contemporary world politics and U.S. foreign policy. They cannot be analyzed adequately within the conceptual frameworks used most frequently in the past by American international politics specialists. In response to these developments, and as a result of logical theoretical evolution, considerable progress has been made in the international political economy subfield of international relations. We now have new conceptual schemes that admit to a much broader range of actors and processes integral to the study of world politics.[6] These frameworks of analysis permit us to address more systematically the relationships between international economic and political behavior.

As a consequence of this gradual evolution in substantive and conceptual focus, specialists in international politics have become much more cognizant of the economic dimensions of world politics. Nonetheless, no theory has emerged that specifies adequately the relationships existing among various actors and processes now viewed as integral to the study of world politics. No attempt will be made in this volume to provide such a general theory. Instead, our aim is to describe more richly and explain more adequately the political significance of various economic relationships by contrasting assumptional bases that

[6]See, particularly, Robert Keohane and Joseph Nye, *Power and Interdependence* (Boston: Little, Brown, 1977); Robert Keohane, *After Hegemony* (Princeton: Princeton University Press, 1984); Edward Morse, *Modernization and the Transformation of International Relations* (New York: Free Press, 1976); Robert Gilpin, *War and Change in World Politics* (Cambridge: Cambridge University Press, 1981); Peter Katzenstein, ed., *Between Power and Plenty* (Madison: University of Wisconsin Press, 1978); Stephen Krasner, ed. *International Regimes* (Ithaca: Cornell University Press, 1983); and Immanuel Wallerstein, *The Modern World System* (New York: Academic Press, 1976).

underlie alternative views of political and economic behavior. The chapters that follow examine the major substantive areas of trade, monetary relations, foreign investment, aid, technology transfers, alternative economic strategies for poor states, and the formulation of foreign economic policy in the United States. Each of these areas, and the interdependencies among them, will be described in terms of how they affect political relations among rich states as well as how they affect relations between rich and poor states. In addition, we will examine how various conceptual frameworks lead to alternative conclusions about which policies are most appropriate for resolving conflicts of interest among states and other actors.

Without attempting to force all analyses of global economic relations into one or the other of the following schools of thought, the major clash in description, explanation, prediction, and policy prescription relating to these problems appears to be between those analysts and decision makers subscribing to the assumptions of classical liberal economic thought and those subscribing to the assumptions of what Americans refer to as radical thought. The classical liberal economic approach is evident in the works of numerous analysts[7] as well as in the basic contemporary foreign economic policy orientations of the United States and other governments of advanced industrial societies in the West. They are evident as well in the policy orientations of key international economic institutions such as the General Agreement on Tariffs and Trade, the International Monetary Fund, and the International Bank for Reconstruction and Development. Examples of radical thought can be found in the works of Cold War revisionists, analysts of contemporary American imperialism, neo-Marxian political economists, and *dependencia* theories of Latin American relations in a capitalist international system.[8]

Although there are many differences of opinion among the statesmen and scholars within each of these two general schools of thought, there are

[7]Harry Johnson, *Economic Policies Toward Less Developed Countries* (Washington, D.C.: The Brookings Institution, 1967); "The Link that Chains," *Foreign Policy*, No. 8 (Fall 1972), 113–19; and "The Multinational Corporations as an Agency of Economic Development: Some Explanatory Observations," in *The Widening Gap*, ed. Barbara Ward (New York: Columbia University Press, 1971), pp. 242–52. See also, Richard Cooper, *The Economics of Interdependence* (New York: McGraw-Hill, 1968); Leland Yeager, with David Tuerck, *Foreign Trade and U.S. Policy* (New York: Praeger, 1976); and Robert Lawrence, *Can America Compete?* (Washington, D.C.: The Brookings Institution, 1984).

[8]William Appleman Williams, *The Tragedy of American Diplomacy* (New York: Dell, 1959); David Horowitz, *The Free World Colossus* (New York: Hill and Wang, 1971); Gabriel Kolko, *The Limits of Power* (New York: Harper & Row, 1972); Harry Magdoff, *The Age of Imperialism* (New York: Monthly Review Press, 1969); Susanne Bodenheimer, "Dependency and Imperialism: The Roots of Latin American Underdevelopment," in *Readings in U.S. Imperialism*, ed. K. T. Fann and D. C. Hodges (Boston: Porter Sargent, 1971), pp. 155–82; André Gunder-Frank, "Sociology of Development and Underdevelopment of Sociology," in *Dependence and Underdevelopment*, eds. J. Cockcroft, A. G. Frank, and D. Johnson (Garden City, N.Y.: Doubleday, 1972), pp. 321–98; Johan Galtung, "A Structural Theory of Imperialism," *Journal of Peace Research*, 8, no. 2 (1971), 81–117; Fernando Cardoso, with Enzo Faletto, *Dependency and Development in Latin America* (Berkeley: University of California Press, 1979); Arghiri Emmanuel, *Unequal Exchange: A Study of the Imperialism of Trade* (New York: Monthly Review Press, 1972); Samir Amin, *Accumulation on a World Scale: A Critique of the Theory of Development*, 2 vols. (New York: Monthly Review Press, 1974); and Immanuel Wallerstein, *The Modern World System* (New York: Academic Press, 1976).

nevertheless certain basic assumptions that are shared widely by the adherents of each school; these assumptions distinguish clearly the two orientations. In particular, there are important differences between the two schools' basic assessments of the primary values underlying actions taken by decision makers on behalf of states, the distribution of benefits from international economic relations, the degree and patterns of conflict inherent in international economic relations, and the location of the major obstacles to the achievement of national economic aspirations. The central tenets of these two analytical traditions are summarized in Table 1-1.

Adherents of classical liberal economic thought tend to see the focus of states' economic policies as the maximization of economic growth and efficiency. The basic value determining policy choice in regard to economic issues before the state should be the optimal allocation of resources for national growth in the context of a global economy that operates in accordance with the norms of liberal economic principles. Success or failure is usually stated in terms of aggregate measures of economic performance such as the level and growth of GNP, trade, investment, per capita income, and so forth.

In this context, global as well as national economic growth and efficiency dictate that all states open themselves to foreign goods and capital and that they specialize in the production of those goods in which they possess a comparative advantage. Existing international economic relationships are viewed as mutually beneficial, even if the distribution of benefits among states is not completely symmetrical.

To the extent that existing international relationships do not enhance growth and the efficient allocation of resources, this view blames the unwillingness of decision makers within states to pursue rational liberal economic policies. In other words, to the extent that the global economy as a whole, and individual states' policies, conform to classical liberal economic principles, *all* states' growth and economic efficiency will be maximized. Of course, world production will be maximized also.

Inherent in this positive-sum view of international economic relationships is minimal conflict of interest between states. For the adherents of classical liberal economic thought, policy prescription is universalist: no basic differentiation is made among policy prescriptions appropriate for different types of national actors (large or small, rich or poor). The formal rules of behavior in international economic relations, and the policies of international economic institutions enforcing these rules, are seen as politically neutral among all states.

Liberal economic analysts are prone to see a world composed of sovereign, autonomous states enjoying equal economic opportunity (though not equality of economic condition) in an open international system. All states are understood to possess considerable autonomy and decisional latitude in critical choices about their domestic and foreign economic policies. Resource allocation in economic exchange within and between states should be determined principally by market mechanisms. To the extent that market mechanisms generate socially unacceptable inequalities, the state's function is to ameliorate

TABLE 1-1 Central Tenets of Liberal Economic and Radical Thought

BASIC PREMISE	LIBERAL ECONOMIC THOUGHT	RADICAL THOUGHT
1. Primary value being pursued by states	Maximum aggregate economic growth in national and global economies	Maximum national economic growth consistent with capacity for national self-determination and with equitable distribution of income within and between states
2. Distribution of benefits from global economic relations conducted according to liberal principles	Mutual benefit if not symmetrical distribution; positive-sum	Clearly asymmetrical distribution in favor of rich states; zero-sum
3. Degree of conflict *inherent* in global economic relations conducted according to liberal principles	Minimal; tendency toward equilibrium	Very great; tendency toward disequilibrium and recurrent crises.
4. Persistent cleavages *inherent* in global economic relations conducted in accordance with liberal principles	None	Cleavages between rich states and poor states; cleavages between industrial-financial elites and labor within all capitalist economies
5. Major obstacle to achievement of national economic aspirations	Irrational state policies	Capitalist rules of behavior governing international economic relations
6. Overall result of activities of international economic institutions	Provision of infrastructure advantageous to all states in conduct of international economic relations	Provision of infrastructure for perpetuating dominance by rich, Western states
7. Characterization of existing international political system	Sovereign, autonomous states with considerable decisional latitude on economic policies	Hierarchically organized system of dominant and subordinate states; autonomy and meaningful decisional latitude on economic policy for dominant states only
8. Preferred means of resource allocation	Market mechanisms	State-administered terms of exchange
9. Relationship between economics and politics	Economics should be separated from politics	Economics determine politics

them through redistribution programs. States should be very wary of intruding on market mechanisms, for they are the key to efficiency for all economic transactions, in the view of liberal analysts.

The assumptional bases of radical thought are vastly different from those underlying the liberals' world view. Although growth and economic efficiency are seen as priority goals of states, national self-determination and equitable income distribution are just as crucial. Indeed, these last two goals would be ranked above economic growth by most radicals if, in the short run, the choice had to be made. The radical analyst tends to see income equality and the capacity for economic and political self-determination among poor states, at least, as incompatible with integration into the existing global economy, which operates in accordance with the norms of classical liberal economic thought. A poor state's open acceptance of foreign goods and capital, along with its specialization in the production of those goods in which it enjoys a comparative advantage, is felt to generate a form of international economic relations in which unequal economic units are afforded equal access to, and compete for, markets and resources around the globe.

The benefits of such international economic relations between rich and poor states are distributed asymmetrically, in favor of the rich. This continued asymmetry in the distribution of benefits forms a basically exploitative relationship between dominant and dependent states that is seen by adherents of radical thought as the explanation for the existence and the widening of the gap between rich and poor countries. Hence, in a fundamental sense the major obstacle to the achievement of the national aspirations of poor states (most states in the world) is seen to be the nature of the international economic system itself, rather than the policies of individual poor states. Even if a poor state does formulate economic policy in accordance with classical liberal economic thought, the asymmetrical distribution of benefits in its international economic relations will condemn it to perpetual poverty, foreign penetration, and continued dependence upon rich states.

Clearly great conflicts of interest between states are inherent in this basically zero-sum view of international economic relations. Policy prescription is not universalist. Policies appropriate for rich states in the center of the global economy are not appropriate for poor states in the periphery. Classical liberal economic thought is viewed by radical thinkers as compatible with the interests of rich states but not with those of poor states. The existing international economic system is not politically neutral, as the classical liberal economists argue. The policies of all the key international economic institutions and the distribution of benefits from most public and private economic transactions inherently favor rich states, ensuring their dominance in global economic and political relations.

Radical economic analysts visualize a hierarchically organized world with dependent, subordinate states relegated to the periphery of the international economy dominated by the leading capitalist states. Only the latter possess autonomy in critical choices about their domestic and foreign economic policies. States in the periphery of the global economy must accept their place in an international division of labor imposed upon them by the leading capitalist states. Market mechanisms allocating resources in international and domestic economic exchange reinforce political, social, and economic inequalities that radical analysts find abhorrent. They seek an active role for the state in managing markets to introduce a greater measure of equity in domestic and foreign economic relations.

Quite obviously, the analysts and decision makers who employ these alternative sets of primary assumptions will differ greatly in their assessment of, say, multinational corporations and in their prescriptions for the treatment of multinationals by nations, acting individually and in concert. The profound cleavage in their basic premises leads adherents of the two schools of thought to talk past each other in analyzing specific economic issues, such as multinational corporations. To the classical liberal, for example, foreign investment appears mutually beneficial; to the radical, it is exploitative. Analysts from both schools seldom examine the appropriateness of the different assumptional bases from which their perceptions and policy prescriptions flow. In the absence of this examination, political conflict over economic issues is exacerbated. The typical analyst or decision maker within each school of thought simply sees no necessity to question seriously the assumptions underlying one's own stance on the issue and continues to propose policies that are seen as harmful in their incidence or intent by adherents of the other analytical tradition.

The clash between these two schools of thought not only has important substantive implications for international relations; it also affords an opportunity to analyze the political implications of various dimensions of global economic relations. In the following chapters, we will refer frequently to these alternative perspectives, and we will develop them more fully in specific contexts.

Despite the centrality of the liberal-radical "dialogue" in international diplomacy and political economic analysis, it is by no means sufficient in itself to address all aspects of such a complex subject matter. For example, mercantilist thought also enjoys considerable prominence in examining contemporary political economic behavior.[9] Mercantilists see politics as determining economics. Economic relations are to be understood in terms of competition for the distribution of wealth and power among states, as distinct from the individual and global welfare maximization stressed by liberal economists or the class competition emphasized by radical economists. They view liberal economic policies as a function of the distribution of power in the international system and the position of a nation's industries in the global division of labor—thus, a liberal international economic order is most likely to emerge when hegemonial

[9]Notable examples include Robert Gilpin, *U.S. Power and the Multinational Corporation* (New York: Basic Books, 1975) and *War and Change in World Politics* (Cambridge: Cambridge University Press, 1981); Stephen Krasner, *Defending the National Interest* (Princeton: Princeton University Press, 1978) and "State Power and the Structure of International Trade," *World Politics*, 28, no. 2 (April 1976), 317–47; John Zysman and Stephen Cohen, *The Mercantilist Challenge to the Liberal International Trade Order*, Study Prepared for the Joint Economic Committee, 97th Cong., 2nd Sess., Dec. 1982.