THIRD EDITION

INTERNATIONAL POLITICAL ECONOMY

PERSPECTIVES ON GLOBAL POWER AND WEALTH

JEFFRY A. FRIEDEN AND DAVID A. LAKE

INTERNATIONAL POLITICAL ECONOMY

PERSPECTIVES ON GLOBAL POWER AND WEALTH

THIRD EDITION

Jeffry A. Frieden
University of California, Los Angeles

David A. Lake
University of California, San Diego

St. Martin's Press New York

Executive editor: Don Reisman
Managing editor: Patricia Mansfield-Phelan
Project editor: Amy Horowitz
Production supervisor: Joe Ford
Art director: Sheree Goodman
Cover design: Jeannette Jacobs

Library of Congress Catalog Card Number: 94–65224

Manufactured in the United States of America.

9 8 7
f e d c

For information, write:
St. Martin's Press, Inc.
175 Fifth Avenue
New York, NY 10010

ISBN: 0–312–08418–8

INTERNATIONAL POLITICAL ECONOMY

PERSPECTIVES ON GLOBAL POWER AND WEALTH

THIRD EDITION

PREFACE

The readings in *International Political Economy: Perspectives on Global Power and Wealth* are primarily intended to introduce the study of international political economy to those with little or no prior knowledge of it. The book is designed for use in courses in international political economy, international relations, and international economics. The selections present both clear and identifiable theoretical arguments and important substantive material. Twenty-two of the thirty-three articles are new to this third edition of our book, and the theoretical approach has been revised substantially to reflect both changes in the real world and intellectual progress in the field of international political economy.

Although the selections can be used in any order, they are grouped in seven parts that reflect some of the more common organizing principles used in international political economy courses. Each part begins with an introduction by the editors that provides background information and highlights issues raised in the readings. Each reading is preceded by an abstract summarizing its specific arguments and contributions. The readings were edited to eliminate extraneous or dated information, and most footnotes were removed.

The introduction defines the study of international political economy, summarizes major analytic frameworks in the field, and identifies several current debates. In past editions, the introduction and readings were largely structured around three analytic perspectives: Realism, Marxism, and Liberalism. This framework is retained in this edition, but substantially downplayed. The field of international political economy has made significant progress over the past decade, and this division—while useful as a pedagogic device—has become increasingly obsolete. To capture the most important work and current debates in international political economy, we now highlight the analytic tensions between international and domestic explanations, on the one hand, and state- and society-centered explanations, on the other. These two dimensions create four distinct views, which we refer to as the international political, international economic, domestic statist, and domestic societal approaches. Part I presents examples of these different perspectives in international political economy. The readings in this part are intended to suggest the underlying logic and types of arguments used by proponents of each approach. Although they are representative of their respective schools, they do not necessarily capture the wide range of opinion within each approach.

Part II, which reviews the history of the international economy since the nineteenth century, provides the background and perspective necessary to understand the contemporary international political economy. The selections describe the major developments in the history of the modern international economy from a variety of different theoretical viewpoints.

The remainder of the book is devoted to the post-1945 international political economy. Separate sections on production, money and finance, and trade look at the principal broad issue areas associated with the politics of international economic relations. Part VI, wholly new to this edition, focuses on the particular political and economic problems of developing and formerly centrally planned economies. Finally, Part VII examines current problems in the politics of international economics.

The selections in this volume have been used successfully in our courses on international political economy at the University of California, Los Angeles, and the University of California, San Diego. In our own research, we approach the study of international political economy from very different perspectives. Yet, we find that this set of readings accommodates our individual approaches to the subject matter while simultaneously covering the major questions of the field.

David Dollar made helpful suggestions on the editors' introductions, as did Ronald A. Francisco, and the following reviewers for St. Martin's Press: Stephen Anderson, University of Wisconsin at Madison; Thomas J. Bellows, University of Texas at San Antonio; Richard Ganzel, University of Nevada; Lowell Gustafson, Villanova University; Anne R. Hornsby, Spelman College; Charles K. Kennedy, Wake Forest University; Robert McIntire, Millikin University; Elizabeth Norville, Lewis and Clark College; Frances H. O'Neal, University of Alabama; John G. Speer, University of Houston; and Scot A. Stradley, University of North Dakota. For this edition, Don Reisman and Mary Hugh Lester of St. Martin's Press helped us shepherd the project through the publication process; Risa Brooks, Barbara Butterton, Bart Fischer, and Roland Stephen provided research and editorial assistance. Finally, we want to thank our respective spouses, Anabela Costa and Wendy K. Lake, for their encouragement.

Jeffry A. Frieden
David A. Lake

CONTENTS

Introduction

INTERNATIONAL POLITICS AND INTERNATIONAL ECONOMICS

Over the past twenty-five years, the study of international political economy has undergone a remarkable resurgence. Virtually nonexistent before 1970 as a field of study, international political economy is now a popular area of specialization for both undergraduates and graduate students, as well as the source of much innovative and influential work by modern social scientists. The revival of international political economy after nearly forty years of dormancy has enriched both social science and public debate, and promises to continue to do both.

International political economy is the study of the interplay of economics and politics in the world arena. In the most general sense, the economy can be defined as the system of producing, distributing, and using wealth; politics is the set of institutions and rules by which social and economic interactions are governed. *Political economy* has a variety of meanings. For some, it refers primarily to the study of the political basis of economic actions, the ways in which government policies affect market operations. For others, the principal preoccupation is the economic basis of political action, the ways in which economic forces mold government policies. The two focuses are in a sense complementary, for politics and markets are in a constant state of mutual interaction.

It should come as no surprise to inhabitants of capitalist societies that markets exist and are governed by certain fundamental laws that operate more or less independently of the will of firms and individuals. Any shopkeeper knows that an attempt to raise the price of a readily available and standardized product—a pencil, for example—above that charged by nearby and competing shopkeepers will very rapidly cause customers to stop buying pencils at the higher price. Unless the shopkeeper wants to be left with piles of unsold pencils, he or she will have to bring the price back into line with "what the market will bear." The shopkeeper will have learned a microcosmic lesson in what economists call the market-clearing equilibrium point, the price at which the number of goods supplied equals the number demanded, or the point at which supply and demand curves intersect.

At the base of all modern economics is the general assertion that, within certain carefully specified parameters, markets operate in and of themselves to maintain balance between supply and demand. Other things being equal, if the supply of a good increases far beyond the demand for it, the good's price will be driven down until demand rises to meet supply, supply falls to meet demand, and the market-clearing equilibrium is restored. By the same token, if demand exceeds supply, the good's price will rise, thus causing demand to decline and supply to increase until the two are in balance.

If the international and domestic economies functioned like perfectly competitive markets, they would be relatively easy to describe and comprehend. Fortunately or unfortunately, however, the freely functioning market is only a highly stylized or abstract picture that is rarely reproduced in the real world. A variety of factors influence the workings of domestic and international markets in ways that a focus on purely economic forces does not fully capture. Consumer tastes can change—how large is the American market for spats or sarsaparilla today?—as can the technology needed to make products more cheaply, or even to make entirely new goods that displace others (stick shifts for horsewhips, calculators for slide rules). Producers, sellers, or buyers of goods can band together to try to raise or lower prices unilaterally, as the Organization of Petroleum Exporting Countries (OPEC) did with petroleum in 1974 and 1979. And governments can act, consciously or inadvertently, to alter patterns of consumption, supply, demand, prices, and virtually all other economic variables.

It is this last fact, political "interference" with economic trends, that is the most visible, and probably the most important, reason to go beyond market-based, purely economic explanations of social behavior. Indeed, many market-oriented economists are continually surprised by the ability of governments, or of powerful groups pressuring governments, to contravene economic tendencies. When OPEC first raised oil prices in December 1973, some market-minded pundits, and even a few naive economists, predicted that such naked manipulation of the forces of supply and demand could last only a matter of months. What has emerged from the past twenty years' experience with oil prices is that they are a function of both market forces and the ability of OPEC's member states to organize concerted intervention in the oil market.

Somewhat less dramatic are the everyday operations of local and national governments that affect prices, production, profits, wages, and almost all other aspects of the economy. Wage, price, and rent controls; taxation; incentives and subsidies; tariffs; and government spending all serve to mold modern economies and the functioning of markets themselves. Who could understand the suburbanization of the United States after World War II without taking into account government tax incentives to home mortgage-holders, government-financed highway construction, and politically driven patterns of local educational expenditures? How many

American (or Japanese or European) farmers would be left if agricultural subsidies were eliminated? How many Americans would have college educations were it not for public universities and government scholarships? Who could explain the proliferation of nonprofit groups in the United States without knowing the tax incentives given to charitable donations?

In these instances, and many more, political pressure groups, politicians, and government bureaucrats have at least as much effect on economic outcomes as do the fundamental laws of the marketplace. Social scientists, especially political scientists, have spent decades trying to understand how these political pressures interact to produce government policy. Many of the results provide as elegant and stylized a view of politics as the economics profession has developed of markets. As in economics, however, social science models of political behavior are little more than didactic devices whose accuracy depends on a wide variety of unpredictable factors, including underlying economic trends. If an economist would be foolish to dismiss the possibilities of intergovernmental producers' cartels (such as OPEC) out of hand, a political scientist would be foolish not to realize that the economic realities of modern international commodity markets ensure that successful producers' cartels will be few and far between.

It is thus no surprise that political economy is far from new. Indeed, until a century ago, virtually all thinkers concerned with understanding human society wrote about political economy. For individuals as diverse as Adam Smith, John Stuart Mill, and Karl Marx, the economy was eminently political and politics was obviously tied to economic phenomena. Few scholars before 1900 would have taken seriously any attempt to describe and analyze politics and economics separately.

Around the turn of the century, however, professional studies of economics and politics became more and more divorced from one another. Economic investigation began to focus on understanding more fully the operation of specific markets and their interaction; the development of new mathematical techniques permitted the formalization of, for example, laws of supply and demand. By the time of World War I, an economics profession per se was in existence, and its attention was focused on understanding the operation of economic activities in and of themselves. At the same time, other scholars were looking increasingly at the political realm in isolation from the economy. The rise of modern representative political institutions, mass political parties, more politically informed populations, and modern bureaucracies all seemed to justify the study of politics as an activity that had a logic of its own.

With the exception of a few isolated individuals and an upsurge of interest during the politically and economically troubled years of the Great Depression, the twentieth century saw an increasing separation of the study of economics and politics. Economists developed ever more elaborate and sophisticated models of how economies work. Similarly, other social scientists spun out ever more complex theories of political development and activity.

The resurgence of political economy since 1970 has had two interrelated sources. The first was dissatisfaction among academics with the gap between abstract models of political and economic behavior, on the one hand, and the actual behavior of polities and economies, on the other. Theory became more ethereal and seemed less realistic. Many scholars began to question the intellectual justifications for a strict analytic division between politics and economics. Second, as the stability and prosperity of the first twenty-five postwar years started to disintegrate in the early 1970s, economic issues became politicized, and political systems became increasingly preoccupied with economic affairs. In August 1971, Richard Nixon ended the gold–dollar standard that had formed the basis for postwar monetary relations; two and a half years later, OPEC, a previously little-known group, succeeded in substantially raising the price of oil. In 1974 and 1975, the industrial nations of Western Europe, North America, and Japan fell into the first worldwide economic recession since the 1930s; unemployment and inflation were soon widespread realities and explosive political issues. In the world arena, the underdeveloped countries—most of them recently independent—burst onto center stage as the Third World, demanding a fairer division of global wealth and power. If in the 1950s and 1960s economic growth was taken for granted and politics occupied itself with other matters, in the 1970s and 1980s economic stagnation fed political strife while political conflict exacerbated economic uncertainty.

For both intellectual and practical reasons, then, social scientists began seeking, once more, to understand how politics and economics interact in modern society. As interest in political economy grew, a series of fundamental questions were posed, and a broad variety of contending approaches arose.

To be sure, today's political economists have not simply reproduced the studies of earlier (and perhaps neglected) generations of political economists. The professionalization of both economics and political science has led to major advances in both fields, and scholars now understand both economic and political phenomena far better than they did a generation ago. It is on this improved basis that the new political economy is being constructed, albeit with some long-standing issues in mind.

Just as in the real world, where politicians must pay close attention to economic trends and economic actors must keep track of political tendencies, those who would understand the political process must take the economy into account and vice versa. A much richer picture of social processes emerges from an integrated understanding of both political and economic affairs than from the isolated study of politics and economics as separate realms. This much is by now hardly controversial; it is in application that disagreements arise. Government actions may color economic trends, but these actions themselves may simply reflect the pressures of economic interest groups. Economic interest groups may be central in determining government policy, yet the political system—democratic or totalitarian, two-party or multiparty, parliamentary or presidential—may crucially color the outlooks and influence of economic interests. In the attempt to arrive at an integrated view of how politics and economics interact, we must disentangle economic and political causes and effects. In this effort, different scholars have different approaches, with different implications for the resulting view of the world.

CONTENDING PERSPECTIVES ON INTERNATIONAL POLITICAL ECONOMY

All analysts of the international political economy are faced with the daunting task of understanding the interaction of many disparate forces. It is possible to simplify many such factors so that they can be arrayed on two dimensions. These two dimensions also capture many of the theoretical disagreements that characterize scholarship on the politics of international economic relations. One set of disagreements has to do with the relationship between the international and domestic political economies; another set concerns the relationship between the state and social forces.

The first dimension of interest concerns the degree to which the causes of international political and economic trends are to be found at the domestic or international level. All observers agree that in a complex world, both global and national forces are important. But different analysts place different emphases on the importance of one or the other. Some focus on how international forces tend to overpower domestic interests; others emphasize the degree to which national concerns override global considerations.

It should surprise no one that American tariff policy, Japanese international financial goals, and South Korean development strategies are important in the world's political economy. Disagreements arise, however, over how best to explain the sources of the foreign economic policies of individual nations, or of nation-states in general. At one end of the spectrum, some scholars believe that national foreign economic policies are essentially determined by the global environment. The actual room for national maneuver of even the most powerful of states, these scholars believe, is limited by characteristics inherent in the international system. At the other end of the spectrum are scholars who see foreign economic policies primarily as the outgrowth of national, domestic-level political and economic processes. For them, the international system exists only as a jumble of independent nation-states, each with its own political and economic peculiarities.

The international-domestic division is at the base of many debates within international political economy, as in the world at large. While some argue, for example, that the cause of Third World poverty is in the unequal global economic order, others blame domestic politics and economics in developing nations. Many see multinational corporations as powerful independent forces in the world—whether for good or for evil—while others see international firms as extensions of their home countries. For some, global geopolitical relations among nations dominate the impulses that arise from their domestic social orders.

The distinction between the two approaches can be seen quite clearly, for example, in explanations of trade policy. To take a specific instance, starting in the early 1980s the United States and many European governments imposed restrictions on the import of Japanese automobiles. The form of the controls varied widely: the United States and Japanese governments negotiated "voluntary" export restraints that Japanese producers agreed to abide by, while in some European countries quantitative quotas were imposed unilaterally. Concerned about stiff

Japanese competition that was reducing profits and employment, European and North American automakers and the trade unions that represent their employees provided key support for these policies.

From this example, one clear analytic conclusion would be that domestic political and economic pressures—the electoral importance of the regions where auto industries are concentrated; the economic centrality of the sector to the European and North American economies; government concern about the broad national ramifications of the auto industry; and the political clout of the autoworkers' unions—led to important foreign economic measures: the restriction of Japanese automobile imports. Indeed, many scholars saw the restrictions as confirmation of the primacy of domestic concerns in the making of foreign economic policy.

Yet, analysts who search for the causes of national foreign economic policies in the international, rather than the domestic, arena, could also find support in the auto import restrictions. After all, the policies responded to the rise of Japan as a major manufacturer and exporter of automobiles, a fact that had little to do with the domestic scene in the United States and Europe. Many North American and European industries have lost competitive ground to rapidly growing overseas manufacturers, a process that is complex in origin but clearly one of worldwide proportions. Some have argued that trade policies are a function of realities inherent in the international system, such as the existence of a leading, hegemonic power and the eventual decline of that state (see Krasner, Reading 1). In this view, the decline of American power set the stage for a proliferation of barriers to trade.

The internationally minded scholar might also argue that it is important to understand why the European and American measures took the relatively mild form they did, simply limiting the Japanese to established (and often very appreciable) shares of the markets. If the measures had been adopted solely to respond to the distress of local auto industries, the logical step would have been to exclude foreign cars from the markets in question. Yet, the position of Europe and the United States in the global economic and political system—including everything from world finance to international military alliances—dictated that European and North American policymakers not pursue overly hostile policies toward the Japanese.

More generally, scholars have explained long-term changes in trade policy in very different ways. During the period between World Wars I and II, and especially in the 1930s, almost all European nations and the United States were highly protectionist. Since World War II, on the other hand, the North American and Western European markets have been opened gradually to one another and to the rest of the world.

Scholars whose theoretical bent is international point out that domestic politics in Europe and the United States have not changed enough during this period to explain such a radical shift. But the role of the United States and Western Europe in the international political and economic system has indeed been different from what it was during the 1930s: after 1945, North American and Western European countries were united in an American-led military and economic alliance against the Soviet Union. Some internationally oriented analysts argue that the causes of postwar foreign economic policies in North America and Western Europe can be found in the international geopolitical positions of these regions—the increase in American power, the decline of Europe, the Soviet challenge, and the rise of the Atlantic Alliance. Others point to broad technological and economic developments, such as dramatic improvements in telecommunications and transportation, that have altered governments' incentives to protect or open their economies.

Scholars who support domestic-level explanations take the opposite tack. For them, the postwar system was itself largely a creation of the United States and the major Western European powers. To cite the modern international political economy as a source of American or British foreign economic policy, these scholars argue, is to put the cart before the horse, since it was the United States and its allies that created the institutions—the Marshall Plan, the Bretton Woods agreement, the European Community—of today's international political economy. We must therefore search for the true roots of the shift in trade policy in North America and Western Europe within these nations.

The example of trade policy demonstrates that serious scholars can arrive at strikingly different analytic conclusions on the basis of the same information. For some, domestic political and economic pressures caused the adoption of auto import restrictions. For others, geopolitical, economic, or technological trends in the international environment explain the same action.

The second dimension along which analysts differ in their interpretation of trends in the international political economy has to do with the relative importance of politicians and political institutions, on the one hand, and private social actors, on the other. The interaction between state and society—between national governments and the social forces they represent, rule, or ignore—is indeed another dividing line within the field of international political economy. In the study of the politics of the world economy, questions continually arise about the relative importance of independent government action and institutions versus a variety of societal pressures on the policy-making process.

The role of the state is at the center of all political science; international political economy is no exception. Foreign economic policy is made, of course, by foreign economic policymakers; this much is trivial. But just as scholars debate the relative importance of overseas and domestic determinants of foreign economic policies, so too do they disagree over whether policymakers represent a logic of their own, or reflect domestic lobbies and interest groups. According to one view, the state is relatively insulated or autonomous from the multitude of social, political, and economic pressures that emanate from society. The most that pluralistic interest groups can produce is a confused cacophony of complaints and demands, but coherent national policy comes from the conscious actions of national leaders and those who occupy positions of political power and from the institutions in which they operate. The state, in this view, molds society, and foreign economic policy is one part of this larger mold.

The opposing school of thought asserts that policymakers are little more than the transmitters of underlying societal demands. At best, the political system can organize and regularize these demands, but the state is essentially a tool in the