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## Globalization, Trade, and Interdependence

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**Abstract:** During the course of the second half of the twentieth century, the world economy has become increasingly interdependent as a result of the economic liberalization measures that have been taken by many countries, and the bilateral and multilateral trade promotion and cooperation agreements that have been reached by a majority of trading partners around the world. However, the benefits from the growth in international trade, and economic cooperation and interdependence, have not been shared equally by all nations. Some have benefited more than others, and some have lagged behind due to their inability to compete in a broader and increasingly dynamic global market. This paper examines the impact of economic interdependence from the perspectives of different national groupings, particularly the developed and the least developed countries. One of the questions to be addressed is: What factors contribute to the differences among those nations in taking advantage of open trade and capital mobility? It is expected that this study would be of value to economic planners and to students of international trade and globalization.

**Keywords:** Globalization; Liberalization; Multinational corporations; Supply chains; Foreign direct investment (FDI).

### 1. Introduction

Economic interdependence and interconnectedness have a far reaching impact on economic stability and growth in many nations. As trade and investment barriers have come down during the course of the second half of the twentieth century, many countries started to have greater access to each other's markets. New opportunities for trade and net trade creation have emerged like never before in history (Tananyiwa and Hakuna, 2014). As a result, world trade has risen consistently over the last several decades to an unprecedented level, reaching \$19 trillion in 2014, according to the World Trade Organization (Higott, 2001); (World Trade Organization, 2016). The increase in trade has, in turn, led to growth in many trading partners' gross national products (GNP) and in their employment figures, and has encouraged foreign direct investment (FDI) flows, modernization of the foreign trade infrastructures including international shipping capacities, changes in styles of living due to the emergence of new industries and global brands, and, thus, more economic interdependence (OECD *et al.*, 2010). As evidenced by historic experience, Martin (2001) further stresses the strong link between trade and economic growth, stating that "most of the countries that have grown the fastest have done so with rapid increases in their participation in world trade" (p. 1).

Describing the extent of change in world trade, Higott (2001) indicates that "between 1959 and 1966 (for example) ...merchandise trade expanded 16-fold" (p. 131). The World Trade Organization (WTO) also reports that international trade has been rising at an average of eight per cent a year over the last several decades, thanks to continued economic growth and liberalization of trade and investment (p. 2). In regard to the globalization of finance, Daniels (2012) also observes that integration of the international financial system has even exceeded the rise in the flow of trade, stating that "money is (now) able to move across globalized regions quite fluidly" (p. 4).

Despite the growth in the overall flow of goods and cross-border financial transactions, however, some nations and regions have lagged behind the rest in their trade and in improving the quality of life of their citizens. The benefits from open trade have not in reality been shared equally or fairly among all world trading partners. Smaller, weaker, and poorly managed economies have been particularly vulnerable to imbalances in their trade and financial flows, declining terms of trade, and external shocks that have necessitated excessive reliance on foreign debts, and painful economic restructuring and austerity measures. As Daniels (2012) indicates, "most LDCs have seen little benefit from the globalization of the finance industry .... (as) the deep integration of the financial industry has occurred mostly with a persistent global triad: North America, Europe, and East Asia" (p. 3-4). Taking into account the economic and, particularly, trade conditions and differences among different nations, this paper examines the impact of open trade and interdependence from the perspectives of different groups of nations, mainly the developed and the least developed ones. A question to be addressed is: What makes some nations winners or losers in the current international trade and financial systems?

## 2. Pros and Cons of Economic Interdependence

Proponents of globalization point to the benefits that come with trade and financial interdependence, including the benefits from efficiencies that are obtained from economies of scale, specialization among trading partners, product standardization and the increased competition among trading partners. As [Surugiu and Camelia \(2015\)](#) explain, “interdependence is occurring due to the specialization of countries ... An example of such interdependence is found in the European Union with countries having a degree of specialization that is due to factors such as labor, capital, culture, etc.” (p. 133).

Supporters of globalization and the increased volume of trade and interdependence also associate trade with economic development. [Todaro and Stephen \(2009\)](#), for example, state that “trade can be an important stimulus to rapid economic growth. This can be amply demonstrated by the successful experiences of countries like China, ... Singapore, and South Korea” (p. 615). Those countries have transformed their economies by successfully implementing diversification and export-led growth strategies.

Despite the record of trade growth that is attributed to the lowering of trade barriers and the resulting growth in economic interdependence among major players in international trade, a barrage of criticism of globalization and open trade takes place at meetings of international financial institutions and whenever world leaders meet to assess the state of, and progress in, the world economy. Those critics bring attention to some direct and some collateral damage from open trade and the increased financial integration and interdependence, particularly in regard to the status and role played by large, highly integrated, and profit-driven multinational corporations. Some see the interconnectedness in the global trading system as a primary cause behind the fast spread of economic problems from one or a few nations to the rest, as the Great Recession of 2008-2009 has demonstrated. In that case, the financial crisis that began in the banking sector in United State spread globally and to other sectors within a short period of time, and “plunged the global economy into the deepest recession since the early 1980s” ([Hill and Thomas Hult, 2017](#)).

[Spence \(2011\)](#) indicates that interconnectedness that results from globalization can not only affect entire countries, but also “some subgroups within... countries, including the advanced economies” (p. 41). It has long been recognized also that getting into a state of dependence on the foreign trade sector of the economy (importing and exporting) as the primary source of strategic and basic societal needs, of national revenues, and of jobs, can have serious adverse economic and foreign policy implications. This has been the case with smaller and weaker economies throughout history, but has become more so, with the sharp increase in the volume and variety of products traded at present and in recent history.

## 3. Perspective of Developed Economies

It is generally realized that the economically advanced countries have been the main beneficiaries of globalization and of interdependence. As their economies recovered from the devastating effect of *WWII*, *International* trade between them grew faster than their trade with developing countries, whose low incomes did not allow them to import many things and whose exports were mainly commodities and primary goods (although developing economies are now an important destination of developed countries exports of high technology and other products) ([Balassa, 1984](#)). Since the world’s largest western economies were the initiators and primary promoters of the current wave of globalization, and along with the international financial and trade institutions they have created, they have been the main force in setting trade and finance liberalization rules, while the rest of the nations of the world have remained as rule- takers, and many of them are still trying to economically catch up with them. However, many of those advanced economies have not been able to completely, and forever, avoid some of the unintended negative consequences of the mobility of resources, and shifting production and trade patterns; and some of them have remained protective of some of their economic sectors, like the agricultural sector, by subsidizing domestic producers and limiting agricultural imports to lessen competition for their agricultural products ([Balassa, 1984](#)).

The loss of some manufacturing jobs in some developed countries due to capital mobility, offshoring and the movement of some manufacturing plants by multinational corporations to low- wage countries has become a political issue in those countries. Thus, some labor unions and political leaders in the United States and the United Kingdom, for example, have started to call for slowing down the pace of globalization or, at least, managing it better. Some nationalists in those countries have even been calling for economic de-globalization because they associate the loss of some jobs and manufacturing capacities to the way globalization and interdependence have been managed, but not necessarily to globalization or interdependence per se. [Stiglitz \(2013\)](#), for example, argues that, “the problem ... is not that globalization is bad or wrong, but that governments are managing it poorly – largely for the benefit of special interests” (p. xiii). He emphasizes, for example, that by allowing labor bargaining power to erode, some workers in countries like the United States have become victims of globalization and interdependence and capital mobility ([Stiglitz, 2013](#)). He and others also blame governments for, under the banner of globalization, have been allowing multinational corporations to unconditionally move capital and manufacturing facilities whenever they found that to be in their interest, without regard to the community’s economic damage and the employment issues they leave behind ([Stiglitz, 2013](#)).

[Spence \(2011\)](#) also observes that employment in the post-industrial societies, like the United States, has increased in the non-tradable sector both due to the growth of that sector and its relative immobility, as compared to the tradable sector that has lost some jobs due to the relocation of plants and the changes in manufacturing

technologies. He further observes that “the employment structure of the United States economy has been shifting ...except for the upper end of the value-added chain.... (Hence) incomes are (now) high, and rising, for the highly educated people at the upper end of the tradable sector, but they are diminishing at the lower end” (p. 30, 32, and 35). Implied by these observations is that some jobs and some manufacturing activities have been moving from some of the advanced economies to some developing, newly industrialized and emerging economies; and with those movements, changes in trade volumes and patterns as well as levels of interdependence continually take place.

#### **4. Perspective of the Least Developed Countries**

Some developing countries have benefited in varying degrees from interdependence. However, some have been hurt from the lowering of their trade barriers, and the liberal opening of their markets to imports without an equal or, close to equal, increase in their exports. The oil exporting countries, for example, have benefited substantially from the need for their oil by the hundreds of non-oil producing nations, all around the world. They have also benefited from the inflow of the FDI that has allowed them to export such a strategic commodity. Regarding what has happened in some other successful developing countries, (Goldberg, 2007) points to the benefits they are realizing from adjusting their economies in order to produce intermediate products and establish labor intensive industries with domestic and/or foreign capital and know-how. However, not all developing countries, particularly the least developed among them, have been successful in doing so.

Least developed countries, like some of the countries in Sub-Saharan Africa, have been facing major problems in their efforts to diversify their economies and fully participate in, and benefit from, the changes in the global trading system. Many of them lack the capabilities required even to exploit their natural resources to the fullest possible extent. Most of them frequently lack the capital and the infrastructure that can accelerate their industrialization, and allows them to have a competitive advantage in the global market. Ironically, some of those nations suffer from a brain drain problem because many of their better educated youths seek employment in the more developed economies (Collier *et al.*, 2004). Furthermore, the conditions imposed by aid-givers, make it difficult for them to take effective measures to protect their infant industries and their small modern industrial sectors (Balassa, 1984). In addition, not all developing countries have had the ability to attract enough export-boosting foreign investment to earn enough foreign exchange to finance their imports of capital and consumer goods. Thus, from the perspective of the least developed countries, opening their markets does not necessarily lead to net benefits in their trade balances, and to success in economic diversification and industrial development. After looking into different countries' successes and failures under alternative trade policies, and the arguments of trade optimists and trade pessimists, Todaro and Stephen (2009) have concluded that “the success of export promotion since the 1990s varies widely from region to region and from country to country....The current consensus leans toward an eclectic view (toward open trade policies) ....What works for one may not work for another” (p. 641).

#### **5. Trade and Interdependence at the Regional level**

Along with the globalization process that led to a great deal of economic interdependence, several geographic regions have established free trade zones, free trade areas, common markets, and other forms of regional trade regimes, with varying degrees of success. Those include the European Union (EU) that has 27 nations, and the North American Free Trade Agreement (NAFTA) that includes the United States, Canada, and Mexico. Understandably, one main objective behind establishing these regional groupings is increasing trade and investment flows among member states and, in some cases, with other (non-member) nations. Such agreements also help in combining operations in multiple markets to attain greater economies of scale within the region, creating regional supply chains, promoting the efficient use of resources (through rationalization and specialization), and advancing the sharing of the costs and benefits from adopting the latest technological advances. Thus, regional groupings are supposed to ultimately help in increasing the flow of goods and services through economic cooperation and interdependence at the regional level or within a limited, but a multi-nation, geographic area. As Tananyiwa and Hakuna (2014) also observe, regional geographic groupings can help weaker economies, like those of many Sub-Saharan African countries, that have been marginalized due to their inability to compete globally, to be individually more competitive at the regional level (Tananyiwa and Hakuna, 2014). Ghemawat (2007) also argues that regional agreements help in taking advantage physical proximity, which facilitates the movement of finished and intermediate goods as well as in maximizing benefits from cultural continuity.

#### **6. Trade and Interdependence Arguments and Counter-Arguments**

Mercantilism was the predominant economic philosophy in Europe until Adam Smith published his famous book, the *Wealth of Nations* in 1776, in which he called for trade liberalization, greater division of labor among trading partners (i.e. specialization in what each nation can produce most efficiently or more efficiently than others), and having less governmental interference in the economy; thus, allowing market forces to determine what to produce and what not to produce. As opposed to Adam Smith's advocacy of free trade, mercantilists saw trade as a zero-sum game in which the gains of one nation, obtained through exports, constitute an equal loss to the importing nation that has to pay for the imported goods. Present day free traders and globalists disagree with such perception of trade. They see trade as a non-zero-sum game because traders can benefit, and create win-win outcomes from the two-way flow of trade. Hence, interdependence can help, rather than hurt trading partners, and imports can have

multiple benefits, as exports do. In the international market, many individual nations can end up with net gains in their economies, at least, from the importation of strategic commodities, of items in short supply in the domestic market, of required raw materials, and of intermediate goods that are needed for further processing or assembly. Some of those imports can eventually generate more exports. In addition, consumers may also benefit from the increased competition that often leads to lower prices and improvements in product quality.

## 7. Conclusion

Lowering trade and investment barriers over the last several decades has created a state of economic interdependence among nation-states. Such interdependence has had positive and negative outcomes. It has led to fast growth in world trade, lower consumer prices, more efficient use of factors of production due to their increased mobility, and higher standards of living, among other positive outcomes. In the meantime, critics deplore the fast spread of economic crises and problems, the increase in income inequality within and among nations, the sharp rise of foreign debt, and the negative impact of imports on some local/domestic manufacturers and their workers. Some nations lower their trade barriers but don't have enough products to export in order to earn enough foreign exchange to pay for them; thus, incurring chronic trade and payments imbalances. However, the redistribution of trade and manufacturing among nations and continents has helped some developing countries (including China) to raise their per capita incomes and lift millions of their citizens out of extreme poverty (Over 600 million in China alone between 1979 and 2014, according to the World Bank).

This study reaffirms the mixed record of economic interdependence. It shows that the impact of liberalization of trade and investment has been uneven as some nations have benefited more than others. In the meantime, some nations and sub-national groups and economic sectors have been winners and some have turned into losers. It should be mentioned as well that multinational corporations have been among the winners since the lowering of trade and investment barriers has created new opportunities for them for greater vertical and horizontal integration, for growth in revenues, and for higher returns on their investment despite the frequently repeated criticism of their economic power and influence, and their continually growing share of the world's output.

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