

## THE NEW GLOBAL ECONOMIC ENVIRONMENT

Suna Oksay\*  
M.Serhan Oksay\*\*

### *Abstract*

*Globalization has emerged as an unavoidable process. Its impact upon different levels create different results. Therefore, the effects of globalization on the world, on countries, on industries, and on firms must be examined separately. The principal worldwide effect of globalization is the increase in the volume of world trade. Its effects on countries have become apparent through the process of deregulation and the elimination of obstacles to trade, etc. At the industrial level, it creates factors such as the rapid development of technology and the realization of production through industries in different countries. Lastly, its principal effect on firms is the creation of a medium of competition whose intensity increases rapidly. For example, during the next two years, the 10 largest firms of today shall be completely replaced by others. Developing technology, practices of deregulation, regional powers and changing individual preferences shall constitute the dynamics of change.*

We live in an increasingly global world. Globalization as "an irreversible process, not an option"<sup>1</sup>. It is a positive force, but it is also blind and therefore needs to be carefully harnessed.

Globalization therefore should be examined thoroughly on different levels: At the Worldwide Level; At the Level Of a Specific Country; At the Level Of a Specific Industry; At the Level Of a Specific Company.

\* Associate Prof. Dr., Marmara University

\*\* Assistant Prof. Dr., Kadir Has University

### **1. At the worldwide level;**

Globalization refers to the growing interdependence among countries as reflected in increasing cross-border flow of goods, services, capital & know-how. Between 1989 and 1996, cross-border trade in goods and services grew at an average annual rate of 6.2% almost twice as fast as the average annual growth rate of 3.2% in the world's GDP during the same period.<sup>2</sup>

A prominent feature of the ongoing global economic change is that the developing countries are active participants as both agents and beneficiaries of the change. Countries best placed to benefit from the new opportunities offered by globalization are those that are successfully transforming their policies and structures to support outward oriented growth. Some of the poorest countries are the least integrated internationally. Finding ways to accelerate their integration into the new global economy is a special challenge.

Globalization demands greater responsibilities from all countries, that for developing countries, integration into a globalize and highly competitive world economy entails many new challenges. These involve:<sup>3</sup>

- creating and sustaining a sound macroeconomic framework and an appropriately open, favorable and stable environment for trade and investment flows
- building economic and social infrastructures and institutions
- creating social safety nets
- undertaking sustained efforts to enhance the efficiency and flexibility of their economies through continuous human resource development as well as more effective, participatory and accountable governance.

### **2. At the level of a specific country**

Globalization refers to the extent of the interlinkages between a country's economy and the rest of the world. Not all countries are equally integrated into the global economy. Some key indicators used to measure the global integration of any country's economy are exports and imports as a ratio of GDP, inward and outward flows of foreign direct investment (Inflows of foreign direct investment are likely to exceed \$1,000 billion in 1996 compared with 1995's figure of \$865 billion.<sup>1</sup> This compares with only \$58

billion as recently as 1982. Foreign direct investment (FDI) is being driven by cross-border mergers and acquisitions, including the purchase by foreign investors of privatized state-owned enterprises and royalty payments associated with technology transfer<sup>5</sup>. The increasing global economic role and integration of developing countries also implies growing economic feedback from developing to industrial countries, making the links between them increasingly more important in both directions. For example, about 1/5 of industrial country exports went to developing countries in the late 80s. Today this share has risen to 1/3 and it appears likely to exceed that by the end of the next decade.

Nowadays, data<sup>6</sup> shows that developing countries which are the most open to trade are the ones catching up with rich countries.

Introducing the report, WTO Director-General Mike Moore said: "This report confirms that, although trade alone may not be enough to eradicate poverty, it is essential if poor people are to have any hope of a brighter future." The WTO Director-General noted as an example that South Korea was as poor as Ghana 30 years ago. Thanks to trade-led growth it is as rich as Portugal today, he said. In general, living standards in developing countries are not catching up with those in developed countries. But some developing countries are catching up - the ones that are most open to trade.<sup>7</sup>

The study concludes that "trade liberalization is generally a strongly positive contributor to poverty alleviation - it allows people to exploit their productive potential, assists economic growth, curtails arbitrary policy interventions and helps to insulate against shocks."

Referring in a speech given in London to the study's findings equating economic convergence with openness to trade, Mr Moore said "This is particularly good news for China. The liberalization that joining the WTO requires will give another big boost to Chinese living standards."

Mr. Moore conceded that, in the short term, some people do lose out from globalization. As trade barriers fall, foreign competition forces domestic firms to specialize in what they do best, rather than making goods that can be more efficiently produced elsewhere.

He suggested that the hardship of such people should be eased with welfare benefits and job retraining, not by putting a halt to globalization. "The

temporary losses of a few should not prevent a country from reaping the much bigger - and permanent gains - from free trade.

"After all, the interests of candle makers were not allowed to stop the introduction of electricity. Nor are governments scrambling to stop the internet cutting out middlemen." The WTO Director-General said.

### **3. At the level of a specific industry**

Globalization refers to the degree to which a company's competitive position within that industry in one country is interdependent with that in another country. The more global an industry, the greater is the advantage that it can derive from leveraging technology, manufacturing prowess, brand names and/or capital across countries. Globalized industries tend to be dominated by the same set of global companies. The athletic foot ware industry for example is dominated by: Nike, Reebok & Adidas. Key indicators of the globalization of an industry are the extent of cross-border trade within the industry as a ratio of total worldwide production; the extent of cross-border investment as a ratio of total capital invested in the industry and the proportion of industry revenue accounted for by companies that compete in all major regions.

### **4. At the level of a specific company**

Globalization refers to the extent to which a company has expanded its revenue and asset base across countries and engages in cross-border flows of capital, goods and know-how across subsidiaries. Toyota is a good example of a highly globalized company. At the end of 1995, one-third of its output came from wholly or partially owned affiliates in 25 foreign countries spread over the Americas, Europe & Asia. Furthermore it exported 38% of its domestic production to foreign markets.<sup>8</sup> Key indicators of the globalization of a company are international dispersion of sales revenues and asset base, intra-firm trade in intermediate and finished goods, and intra-firm flows of technology.

According to Karl Sauvant, UNCTAD's World Investment Report's chief author: "A global marketplace for firms is emerging. Companies are being bought and sold across borders on an unprecedented scale."

The integration leading to deeper forms of economic landscape is not the same as it was 20 years ago nor is the pace of global economic change expected to slacken in the next 20 years. On the contrary change is likely to accelerate. To understand the pace of change it would be enough to look at the change within two years at the top 10 companies of FT500<sup>9</sup> (Table). You may note that six of the top 10 are next new entrants. The top ten companies will completely change in the 10 years.

If Globalization is so fast, what fuels it? Trade and foreign direct investment are major engines of growth in developed and developing countries alike.<sup>10</sup> Trade and investment-induced market

**Table**  
**The Change Within Two Years**  
**at the Top 10 Companies of FT500**

Rank 2000	Rank 1998	Company
1	1	Microsoft
2	2	General Electric
3		NTT Mobile Communications
4	19	Cisco Systems
5	9	Wall-Mart Stores
6	7	Intel
7	11	NTT
8		Exxon Mobil
9	21	Lucent Technologies
10	27	Deutsche Telecom

Source: World Investment Report, UNCTAD, 2000

Integration has led to deeper forms of economic interdependence among nations, as a growing number of developing and former centrally-planned economies have become more closely linked to the global economy.

The case for open markets rests on solid foundations. One of these is the fact that when individuals and companies engage in specialization and exchange, a country will exploit its comparative advantage. It will devote its

natural, human, industrial and financial resources to their highest and best uses. This will provide gains to firms and consumers alike.

In sum, the case for opening markets to investment is as compelling as it is for trade. More open economies enjoy higher rates of private investment, which is a major determinant of economic growth.

Some statistics<sup>11</sup>:

- The volume of world merchandise trade is 16 times greater today than it was in 1950, reflecting the dismantling of import and export barriers.  
OECD "Opening markets matter: The benefits of trade and investment liberalisation"
- A study of OECD countries found that each \$1.00 of outward foreign direct investment was associated with \$2.00 of additional exports and a trade surplus of \$1.70.  
OECD "Opening markets matter: The benefits of trade and investment liberalisation"

The internationalisation of services will likely lead to the next stage of economic globalisation. Services are internationalising rapidly. In both trade and foreign direct investment, services are the fastest-growing component. Services comprise a wide array of economic activity. The main thrusts of the services revolution are the knowledge-based services and the growing tradeability of services.

It is the knowledge-based services (such as professional and technical services, information technology services, banking and insurance, modern health care, and education) that constitute the dynamic edge of the services economy today. An important driving force behind the internationalisation of services is the expansion of electronic networks and the new possibilities for trade in long-distance services associated with these networks.

Progress in information technology is making it increasingly possible to unbundle the production and consumption of information-intensive service activities. The introduction of new products (such as financial derivatives)

and expansion of access to market information (such as computer reservation systems for airlines) have been greatly facilitated by information technology.

International trade in services is, of course, not a new phenomenon: transportation, travel, and insurance have long been important traded activities. What is new is the rapid expansion of international service transactions over the past decade or so and the advent of new modes of supply, as in the case of services transmitted over electronic networks.

It is clear that trade in commercial services has grown faster than trade in merchandise over the past decade. As is the case in trade, services are the most dynamic component of Foreign Direct Investment (FDI) flows. To maximize the benefits from the internationalization of services, adopting a liberal trade and investment regime will be essential. Industrial countries also stand to gain from increased financial integration with developing countries. Increased foreign direct investment allows firms in industrial countries to reap the benefits of specialization in production and distribution on a global scale. In portfolio investment, emerging markets provide an outlet offering higher returns and risk diversification for the savings of the aging populations of industrial countries.

International Chamber of Commerce (ICC) 's interest in the services sector reflects the economic interests of its members in more than 130 developing and industrialized countries around the globe and the importance they attach to obtaining freer access to markets worldwide. Services are coming to dominate the economic activities of countries at virtually every stage of development, making services trade liberalization a necessity for the integration of the world economy.

In the high-income industrialized economies, the value added by services generally exceeds 60 per cent of total output; for example, 70 per cent in Australia, 71 per cent in France, 60 per cent in Japan, 72 per cent in the United States. In many emerging markets, services account for half or more of economic output; 55 per cent in the Czech Republic, 59 per cent in Hungary, 54 per cent in Poland. The same applies to many advanced developing or newly industrialized economies, such as Argentina, Brazil, Korea, Malaysia, Mexico and Thailand.<sup>12</sup>

In many developing economies as well, the service sector is the single largest contributor to economic output, ahead of either agriculture or

industry. Even allowing for the fact that governments are major service providers (education, healthcare, sanitation, etc.), the commercial market for services is huge and growing in virtually every country. And the trend is clear: as national economies develop and incomes rise, the commercial service sector accounts for an ever larger share of GDP.

Services promise a quantum leap in world prosperity through the "information revolution." Modern, state-of-the-art information technology services are critical to improving productivity and maintaining the competitiveness of industries and economies throughout the world. Importantly, these capabilities are not geographically constrained by endowments of many of the traditional factors of production, but depend upon human resources, education, intellectual capital and electronic infrastructure. Hence, it is vital to build up skilled human resources and electronic infrastructure in developing countries in order to enable them to partake in the benefits of the knowledge economy.

ICC's support for services trade liberalization is consistent with its long-standing support for open trade and investment. Freer trade in services enables countries to better enjoy the benefits of globalization and improves economic efficiency just as freer trade in goods does. It contributes to job creation, higher incomes, more consumer choice, downward pressure on inflation, and a better quality of life. Imports of services and foreign investment in services production stimulate the competition that improves the efficiency of domestic service industries. They add to the overall availability of services and to the variety from which individual and corporate consumers can choose. And they contribute to technological advancement. In short, freer trade leads to more, better and lower-cost services.

More, better and lower cost services are important because services are the "enablers" that permit economies to function and prosper. Some form essential infrastructure - transport, communications, finance, information, capital markets, for example, cannot function efficiently without abundant, high-quality information that can be quickly and frequently communicated. Other services are critical to the success of manufacturing and agriculture.

For some manufacturers, services provide a large second source of revenues and contribute significantly to company growth and job creation. For all manufacturers, services are essential to their success. For example, while

manufacturing is at the core of the automobile industry, it is clear that this manufacturing centre must be surrounded by highly developed service functions if the industry is to be successful. These include: an extensive dealership network for distribution; highly developed financial services to finance dealer inventory and sales; readily available maintenance and repair services to protect the consumer's investment.

Moreover, the manufacturing process and the business of running manufacturing industries are infused with services functions from beginning to end: research and development, inventory management and control, transport, marketing, advertising, insurance, and "backroom" functions, such as accounting and legal services. Similar observations can be made of agriculture, where success also depends upon research and development, finance, insurance, storage, transport, distribution, marketing, and a host of technical services. The point is that modern and efficient services play an essential role in improving the performance of other sectors and of the economy as a whole.

Liberalization of trade in services is an important means to encourage the continued rapid expansion of foreign direct investment, to integrate national economies more effectively and to reduce income and other disparities among countries. Since services production and consumption normally are proximate and simultaneous, services trade usually entails a significant transfer of technology and know-how from country to country. This is critical, especially for developing and emerging markets, which can acquire state-of-the-art skills relatively quickly and inexpensively through trade - at least in comparison with the time and expense that would be required to develop them *de novo*.

These state-of-the-art skills are essential, in turn, to building and maintaining the international competitiveness of other sectors. But services trade is not one-way, only from developed to developing nations. In fact, industrialized countries realize important economic welfare gains from the import of services such as data processing, software design and implementation from developing countries. Developing economies have significant hard currency earnings from exporting tourism and labour, as well. And there is substantial scope for expanding services flows in both directions.

The potential for a degree of economic dislocation from expanded trade in services. But this is no different from the dislocation caused by trade in

goods and is likely to be substantially less than that caused by advancing technology. Dealing with these dislocations requires vibrant economies and effective adjustment policies, such as targeted income support and training programmes. Preventing or impeding the exchange of modern, cost-effective services would, in fact, contribute to even greater dislocations as other sectors are denied competitive inputs and become increasingly obsolete.

Further reductions in barriers to trade in services through multilateral negotiations will result in immense economic gains. These gains will benefit both importing and exporting countries, in the industrialized and the developing world.

The increased competition that is driving globalisation will always produce both winners and losers. It is therefore not surprising that some managers see current trends as a great threat while others view them as a challenge and an opportunity.

Four forces are behind the increase in global competition:

- changing customer expectations and preferences
- technological change
- de-regulation
- and regional forces

**Consumer expectations of quality:** service and price are higher than ever and still increasing. At the same time, future consumer preferences are becoming extremely difficult to predict. For example, the massive consumer acceptance of the Internet has been a surprise even to companies such as Microsoft. Few firms predicted the enormous success of mobile telephones but those few who did have profited enormously. Those companies that truly understand and can predict changing end-user needs are likely to be the winners in the future.

**Technological change:** The prime example of an industry affected by massive technological change is the personal computer industry. More powerful PC's are introduced every month. At the same time prices are falling. However, the effect of these changes is not limited to the PC industry. New information technology allows many companies to run their

business in a way that was impossible yesterday and at a fraction of the price. In almost every case, new technology will either reduce the entry barriers to an industry or create new substitute products and services. ' For example, start-up companies such as Amazon.com have revolutionised the global book retailing industry by exploiting the Internet. They provide outstanding customer value - the best prices, and the best book selection - while avoiding the expensive infrastructure of other retailers. Global Competitiveness Banking and insurance products are routinely sold and marketed on the Internet. In addition to the direct selling of these products, the Internet makes global pricing information much more transparent. Consumers can very easily consult the net before they decide what they will buy and where they will make their purchase.

**Deregulation:** Excessive regulation has long been an entry barrier in many industries. In recent years, the global trend - with the notable exception of environmental regulation- has been towards deregulation and less government intervention. In newly deregulated industries, such as telecommunications and utilities, competition has increased dramatically. The ultimate winner has been the consumer, who has benefited from better service and more choice at a lower cost.

**Regional forces:** There are huge regional differences in cost structure and growth rates in the world. At the same time, politically motivated regional trade blocks such as the European Union are being formed. Until the recent financial crisis, most global growth seemed certain to happen in Asia. Now the situation is not so clear. Flexible companies will view these trends as opportunities rather than threats and find ways to profit from change. There are two lessons we can learn from successful companies: They will exploit changing end-user needs & technologies.

Most people now accept that globalization is here to stay. The issue now is what form it should take, and what are its economic rules and its political guidelines and constraints<sup>13</sup>. Similarly, proponents of globalization have changed their tune - conceding that a global economy will not automatically lead to rising prosperity for everyone.

"The question now often asked by free-traders is how to take care of the victims of globalization without endangering the gains from enhanced competition and economic efficiency"<sup>14</sup>. The issues now being worked on by the world's financial leaders include such priorities as how to ensure better standards of governance, including greater accountability and

'transparency' and less corruption, both for corporations and financial institutions and for national governments.

The consequence is that global capitalism and private enterprise are going to become even more firmly entrenched as the 'best practices' of the industrial countries are spread around the world - not least because investors will demand the highest standards of accounting and corporate and governmental disclosure.

### Endnotes

<sup>1</sup> UN Secretary General Kofi Annan description.

<sup>2</sup> "As Business Goes Global", Financial Times, Global Business, Part One of Ten, May 1998

<sup>3</sup> UN Secretary General's report, 1998

<sup>4</sup> The United Nations Conference on Trade and Development reports, 1997.

<sup>5</sup> World Investment Report, UNCTAD,2000

<sup>6</sup> The World trade Organization report, 1996

<sup>7</sup> The study by Dan Ben-David of Tel Aviv University and Alan Winters of Sussex University, 1996

<sup>8</sup> "Creating the Global Organization", Financial Times, Global Business, Part Four of Ten, August 1998

<sup>9</sup> "Gaining Global Competitiveness", Financial Times, Global Business, June 2000

<sup>10</sup> World Investment Report, UNCTAD,2000

<sup>11</sup> "Strengthening the multilateral system" OECD study, 1996

<sup>12</sup> "Annual Report", International Chamber of Commerce (ICC), December 1998

<sup>13</sup> Reginald Dale, The International Herald Tribune, 20 February 1998

<sup>14</sup> Reginald Dale, The International Herald Tribune, 20 February 1998