THE MAI AND THE WORLD ECONOMY

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INTRODUCTION

A dizzying array of new international institutions have emerged to forge a new international economic order: the powerful World Trade Organization (WTO) has replaced the General Agreement on Tariffs and Trade (GATT); the North American Free Trade Agreement (NAFTA), the European Union (EU), and the Asian Pacific Economic Cooperation group (APEC) mark the formation of new regions of accumulation; and Western hemispheric and even trans-Atlantic free trade loom on the horizon.

The current efforts to construct a liberalized world economy, at times coordinated and at others ad hoc, stand in a long line of such efforts that can be traced back to the early period of merchant capitalism. The arguments of neo-liberals in favour of globalization date back to Adam Smith, who argued that mutual exchange between countries allows an international specialization in the division of labour in areas of comparative advantage that raises the general welfare of both (although a range of dubious assumptions, including full employment and perfect competition, are necessary for the results to hold). The neo-liberal thinkers who dominate the World Bank continue to assert that "the liberalization of trade and investment laws around the world has contributed to an enormous increase in the volume of world trade and foreign direct and portfolio investment, whose impact on the welfare of participants has been considerable and for the better."[1]

The case for free trade has been for a reduction in tariffs to reallocate factors of production to more 'efficient' uses within a national economic space. The internationalization of economic activity is also defended today in terms of "more efficient" international financial activities. The freeing of currency trading, the lifting of restrictions on capital movements, the proliferation of off-shore credit sources, and the deregulation of national banking laws are all defended as adding to 'efficient' global capital allocation and balancing risk in an 'integrated' world economy. The International Monetary Fund's (IMF) policies of liberalization of balance of payments transactions and the Bank of International Settlements' (BIS) defense of international banking and advocacy of lower reserve requirements have been central to the processes of financial internationalization.

Free trade advocates have come to defend the international mobility of investment in production, on the grounds of market 'efficiency,' favouring the global reallocation of production as if the world constituted a *single* market. The investor-protection and national treatment clauses of NAFTA are an example of the neo-liberal defense of this side of internationalization.

The Multilateral Agreement on Investment (MAI) is a further effort to liberalize investment in the world economy which expands the investment provisions won in NAFTA and seeks to generalize them to the world economy as a whole through a WTO-like treaty process.[2] The preamble in the draft MAI promises that investor protections "will contribute to the efficient utilization of economic resources, the creation of employment opportunities and the improvement of living standards."[3] In this view, the MAI is an engine of growth which will contribute to the elimination of international economic inequality and raise incomes.

The MAI proposes to protect not just foreign direct investment (FDI), but also financial internationalization in an all-encompassing definition of investment as "every kind of asset owned or controlled, directly or indirectly, by an investor," including intellectual property rights, a range of legal claims, and seemingly all private property forms.[4] FDI has usually been differentiated from short-term capital flows and defined as the internationalization of capital via transnational corporations (TNCs) investing in new plants or engaging in merger and acquisitions outside their home country.

TNCs are increasingly active in the internationalization of services, from financial services to producer and marketing services. In other words, TNCs are national firms operating across national boundaries.

Portfolio capital may be invested for the long-term in acquisition of foreign securities (without control over the management of the company), although the structure of secondary markets and the strategies of institutional investors have certainly made them less so. Financial flows internationalizing production also take the form of direct investment diversifying production sites of a common process across national boundaries and linking different processes in production networks that span several countries.

Internationalization of production has been a response to stagnant output and cost conditions in the corporate search for a 'spatial fix' to increase profits. The volatility due to international costs, currency and interest rate movements has provided further impetus to diversify production sites. This aspect of internationalization, it needs to be stressed, has not produced a global production system outside of national states and indifferent to local production conditions.

There are distinct geographical and temporal limits to the mobility of fixed capital. Foreign investment in productive activity is internalized within the host country, in linkages to the rest of the economy, and to the constellation of political power, even as it redefines national political autonomy and shifts a larger portion of economic activity outward.

In this essay, we note that the expansion of the capitalist world system has seen successive phases of liberalization and integration, contraction and disintegration. It is necessary, in assessing liberalization measures like the MAI, to avoid "confusing the effects of continuing stagnation in the world capitalist economy with the auguries of a transformation of the global capitalist order."[5]

Alongside 'cooperation and growing interdependence' between countries, we also see the 'chaos' and 'sources of tensions between the leading capitalist powers' that Magdoff warned about.

Contrary to the claims made for globalization, the internationalization of capitalism has frequently brought periods in which inequality and instability have increased rather than lessened. Indeed, as more resources have been thrown into export-oriented economic strategies by all countries adopting trade liberalization at the same time that domestic demand is being curtailed, the world economy is more and more reproducing conditions of 'competitive austerity'. The neo-liberal project of globalization cemented in the MAI contributes to an unstable and polarizing world economy and impedes democratic capacities to establish alternative distributional systems that support egalitarian economic outcomes.

1. National Economies in a World System

Capitalism is inherently an expansionary productive system. Social and political institutions, not least military force, have been crucial to providing the labour force, resources and organized coercion necessary for this expansion within nation-states.[6] The expansion of trade and the export of capital across boundaries, under the state system, is a logical extension of the internal expansion within states.[7]

The institutionalized regimes of the world economy structure the flows of capital and commodities connecting national spaces, of value formation, combining the development of national economies within an evolving international division of labour.

The international expansion of capital, whether via trade, portfolio investment, or foreign direct investment, has always occurred within the patterns and structures established by international regimes, which historically have been organized under the leadership of a hegemonic political power and encompass trade, the international monetary system, the international credit system (including a loan enforcement and repayment regime), and the security regime.[8] The evolution of these regimes establish distinct phases of world order, which facilitate and constrain the national and international expansion of capital in different ways.

In any given period, the construction of a trade and investment regime faces the task of orchestrating the expansion of national capitalisms growing at different rates and occupying different niches within the world economy. The world economy does not consist of spontaneously complementary national economies. Rather, the world economy amounts to 'a world configuration' between different national economies within a historically and geographically variable international division of labour). As Lipietz points out, globalization as a process of universalizing capitalist exchange relations has not effaced the problem of world order:
"...the world economy has not (yet?) developed beyond this implicit level of organization. No institutional form regulating world demand has been possible. No supra-national authority to control money supply has been created. The complementarities and antagonisms that exist between national economies remain unstable, constituting little more than partial and random *configurations*."[9]

The integration of national sites of production into the world of circulation always produces tensions and potential contradictions, setting up tensions between national modes of economic regulation and the international conjuncture.

Investment capital itself embodies this tension between the local and the global. As a stock of capital, investment must be rooted in local production relations to produce a surplus; as a flow, investment capital seeks to overcome all fixed relations and barriers to its circulation and realization. National and international investment regimes, from local zoning restrictions to national foreign investment review agencies and international agreements on investment measures, link local accumulation with the world of capital circulation.

The relationship between the international regime and national economic development has had different consequences for democratic capacities to pursue egalitarian goals at different times. The struggle to *constrain* (and even to disengage from) the market and impose social priorities on its workings has historically been most effective at the national level, primarily because the political and institutional means to control capital have been developed most strongly at the level of the nation-state.

Capitalist development has always required the visible hand of the state to counteract its crisis tendencies, and labour movements and other groups have historically organized at this level to attempt to contain, and even reverse, what Polanyi identified as the tendency of the self-regulating capitalist market to 'disembed' the economy from the social protections of non-market relations.[10] In reaction to the fact that capital has always been better able to command social space, labour movements seeking to constrain market processes and counteract competition have directed their energies at trying to 'anchor' capital within national and local spaces.[11]

Democratic struggles over egalitarian objectives to direct economic activity where it is needed or to redistribute income, have benefited from international regimes that regulate and constrain trade and capital mobility, permitting the imposition of social and political controls on the market. Liberal international regimes, conversely, have historically weakened domestic constraints on the market to serve domestic welfare goals. During historical phases in which the international regimes facilitating the world expansion of capital undermine the national regulation of capitalism, the effects have often been stagnation, increasing polarization, and insecurity.

The key question raised by the MAI is whether, in the context of a liberalizing international financial and trading order, the expansion of FDI in the 1980s and 1990s is a force for growth, stability and growing equality in the world economy, or whether it promises to do little to rectify mounting imbalances and instability. What is the relation between the growth and liberalization of international investment (globalization) and the dismal state of the world economy today (stagnation, polarization and instability)?

Globalization in Historical Perspective

The present period of liberalized portfolio and direct investment flows is commonly compared with the period between 1870 and 1913, which also witnessed the growth of large-scale international flows of both short-term and long-term (primarily portfolio) capital.[12] During this period, the world economy reached levels of openness unmatched until the 1970s; trade and output grew steadily, though somewhat more slowly than portfolio capital flows, which also outstripped FDI growth.[13] In the quarter-century after 1880, however, with the spread of tariff barriers among the late-industrializing economies of North America and beyond, FDI began to take on added importance. Technological advances in transportation, communications and storage promoted the internationalization of production, as did the transformation of business organization, which permitted firms to develop greater coordination and efficiency over an expanded scale. In the industrialized and industrializing world, a substantial proportion of FDI went into manufacturing; in the Third World, primary production was the principal outlet for direct investment flows from abroad (Canada, of course, being a case of both).

The period spanning the late 19th and early 20th centuries saw many states that today belong to the advanced industrialized world successfully 'catch-up' to the leading capitalist economies, and it is therefore pointed to as evidence of the "convergence effects" of a regime of free trade and capital flows. However, the context and nature of economic development in the earlier period was very different from the laissez-faire environment of today.

In the late 19th century, late-follower countries everywhere contended with the challenge of capital shortages, imported technology, and infant industries which necessitated a role for barriers to trade and state involvement in the development process.[14] Despite free flows of capital and trade among a number of regions, the world economy could still be characterized as strongly protectionist; FDI and portfolio investment assisting the industrialization of late-followers after 1880 increasingly needed to jump tariff walls, as the example of U.S. companies entering into Canada suggests.

Unlike the present, the context for expansion at the turn of the century was one of active state involvement in the mobilization and allocation of capital required for the large-scale infrastructural projects of industrialization. Moreover, in the colonial possessions of the South, where the pattern was more consistently liberalized trade with the imperial powers, de-industrialization and declining shares of world manufacturing resulted. If the world economy is considered as a whole, global investment flows prior to World War I did not produce international convergence. Rather, the period is remembered as marking an historical divide between the industrialized world and the non-industrialized world—the classic 'age of imperialism'—from which time world inequalities widened considerably.[15]

The international monetary regime increasingly adopted after 1880—the classical "gold standard" under British hegemony—was as much a barrier to employment and income equality as a force for stable growth. Under the inflexible rules of the gold standard, the imperative of balancing international accounts displaced the objectives of employment and stable incomes. By forcing deficit countries to adjust via deflation, the gold standard placed the burden of external adjustment on working-class incomes and the unemployed, the social consequences of which were only offset by large-scale migration from Europe to the New World.

In the wake of World War I, the reconstructed gold exchange standard was more clearly a destabilizing force in the world economy. Amidst the trade dislocations of post-war reconstruction and the global imbalances of the 1920s, the return to gold forced deflationary adjustment onto the weaker economies. The 'beggar-thy-neighbour' tariff spiral was the result—and not the cause—of the structural imbalances in the world economy. With world economic collapse, adherence to gold impeded reflation and spread deflationary pressures around the world. Only with a break from the gold standard, the imposition of exchange controls, and the shift to divergent development strategies and managed trade were states

TABLE 1

INDICATORS OF ECONOMIC PERFORMANCE IN THE G7 COUNTRIES
UNDER VARIOUS INTERNATIONAL MONETARY REGIMES

	Gold Standard		Bretton Woods				Floating Rates	
	1881-1913		1946-58		1959-1970		1974-1989	
Indicator	Mean	Variation	Mean	Variation	Mean	Variation	Mean	Variat.
Real Growth Per Capita	1.5	2.5	4.3	0.5	4.5	0.4	2.2	1.1
Inflation	1.0	3.4	3.9	1.5	3.9	0.5	7.2	0.5
Real Long-te term Interest Rate	3.5	0.7	2.0	2.0	2.7	0.4	2.7	1.6
Change in Real Exchange Rate	0.9	0.9	5.8	1.5	2.0	1.0	8.2	0.8

Source: UNCTAD, Trade and Development Report, 1997, p.79.

able to take steps to expand and cope with the high unemployment and social crisis of the Great Depression.[16]

The Bretton Woods System

Capitalist expansion in the post-war period mainly took the form of a deepening of national markets. To be sure, trade expanded internationally (mostly conducted within the industrialized core), as did flows of FDI, from an initially low level. In particular, American investment abroad grew rapidly. On the whole, however, investment was largely confined to national spaces, and growth was centred around the deepening of national markets.[17] While foreign investment grew at a rapid pace, faster than output or trade, among the industrialized economies it remained a minor share of GNP.

The international regime provided a framework supportive of the unprecedented growth of the post-war boom, partly through default from the collapse of trade in the inter-war period and the needs of reconstruction, and partly through restrictions on the mobility of short-term capital flows and currency trading from countries facing large debts and minimal foreign exchange reserves.

The institutional framework established at the 1944 Bretton Woods conference was designed with the memory of the instabilities and inflexibilities of the inter-war system in mind, and was meant to achieve a system of international integration permitting flexible adjustment that would not come at the expense of employment and welfare goals.

The Bretton Woods institutions established the foundations for a new world economic regime, reconstructed under American political and economic hegemony, and committed to the reconstruction of the European and Japanese economies within the capitalist world, the restoration of currency convertibility, and the formation of a free trading world order in which trade and international capital flows would be subordinate to domestic job growth programs and welfare programs. The deflationary bias of the gold standard was replaced by the flexible and expansionary regime of national currencies pegged to the American dollar, which was in turn exchangeable for gold.

Over the post-war period, the liberalization of the flow of goods interacted virtuously with growth, employment, and rising incomes: both trade and output expanded at unprecedented rates, and the world economy moved from an initially low level of international openness towards a more open trading environment at a faster pace than prior to World War I.[18] Approximately 80% of all tariffs were eliminated in less than 15 years after the establishment of GATT, and colonial markets were opened up to the penetration of foreign, especially American, capital.[19] Despite the commitment to, and growth of, a liberal world economy, however, world trade remained fragmented, uneven, and subject to controls. Most of the socialist bloc remained disengaged, and Japan and other capitalist economies retained controls over the creation and flow of credit in the interests of national industrial strategies. Capital controls and planned credit allocation systems kept finance centred on national spaces, subordinated to the imperatives of reconstruction and domestic-economy-centred growth, and permitting fiscal and monetary policy to be utilized to support domestic welfare goals.[20]

Moreover, private international lending took a back-seat to official lending from the World Bank and the other international financial institutions channelling direct investment to the developing world. Only by the end of the 1960s did private international lending regain its pre-war importance.[21] FDI grew steadily and substantially, especially U.S. TNCs, but this activity remained small relative to output and was often subject to government screening and monitoring.

As world economic integration proceeded, however, the contradiction between growing trade imbalances and the international monetary system helped undermine the post-war institutional order. The reconstruction of the devastated economies of Europe and Asia, and world liquidity, relied on the United States running persistent balance of payment deficits, financed by the export of American currency.

In the 1960s and 1970s, unregulated capital markets made possible speculative attacks on weak currencies that helped undermine the Bretton Woods system. The integration and rapid reconstruction of the European economies and the return to convertibility of the European currencies set the stage for sharpened international competition in the form of a 'non-American challenge' as European states and firms, in particular, used their growing dollar reserves to purchase foreign assets as well as invest in new plants.

A corresponding accelerated expansion of direct investment from American TNCs followed, reproducing the imperialist rivalry of the early part of the century.[22] With the offshore accumulation of U.S. dollars, American banks began to pressure for deregulation in order to compete in Eurocurrency markets, setting in train pressures for the competitive deregulation of financial markets.[23] Speculative flows soon created accumulated pressures on the system of fixed exchange rates, sparking the United States to suspend parity with gold in 1971, a process that eventually broke the fixed exchange rate regime and ended the Bretton Woods system by 1973.

After Bretton Woods

The demise of the Bretton Woods system ushered in a period of economic internationalization of trade, financial flows and currency and banking deregulation, equally a period of stagnation, mounting instability, and growing income inequality. Intensified international restructuring and a dramatic growth of the world stock of FDI have coincided with a significant slowdown in growth. Output growth across the OECD after 1974 fell to an annual average of 2.9% for the years 1973-1989, having averaged 4.8% between 1960 and 1973.[24]

Similarly, after the stock of business capital grew at an annual average of 5.3% between 1965 and 1973, it fell to 3.2% yearly growth in 1982, and manufacturing accumulation especially has fallen off.[25] The 1980s expansion failed to restore private invest-

TABLE 2

GROWTH OF REAL GDP, 1966-95
(PERCENTAGES, ANNUAL AVERAGES)

	1966-73	1974-80	1981-90	1991-93	1994	1995
World total	5.1	3.4	3.2	1.2	2.9	2.8
OECD countries	4.8	2.9	3.1	1.2	2.9	2.4
Transition countries	7.0	5.1	1.8	-12.5	-8.4	-2.5
Eastern and Central Europe	6.9	6.1	2.1	-9.0	-7.5	-0.7
Former Soviet Union	7.1	1.1	1.0	-15.5	-12.6	-4.0
Developing countries	6.9	5.0	3.3	4.6	4.6	4.9
East Asia	7.9	6.8	7.6	8.7	9.3	9.2
China	8.5	6.3	9.9	12.3	12.2	10.2
South Asia	3.7	4.0	5.7	3.2	4.7	5.5
Sub-Saharan Africa	4.7	3.4	1.7	0.6	2.2	3.8
Latin America/Caribbean	6.4	4.8	1.7	3.2	3.9	0.9
Middle East/North Africa	8.5	4.7	0.2	3.4	0.3	2.5

Source: ILO, World Employment 1996/97, p. 3.

ment to post-war 'Golden Age' rates, despite the apparent restoration of favourable conditions for investment and profits in the 1980s.[26]

Amidst slower growth, the liberalization of financial markets and the growth of enormous pools of highly-mobile short-term financial capital, uncoupled from output, trade and productive investment, have been a major force behind the destabilization of the international monetary system. In the 1990s, the world's financial markets are integrated on an unprecedented scale; short-term capital movements have grown to the point where turnover in currency markets now dwarfs the value of trade, or for that matter, the combined official reserves of the world's governments. In the 1990s, daily foreign exchange trading is estimated at over US$1 trillion, 50 times the value of daily trade volumes, with no sign that the pace of growth is likely to slacken.[27]

Relative stagnation in manufacturing has sparked a shift of capital out of long-term productive investment and into financial speculation, encouraged by the adoption of floating exchange rates and the removal of capital controls which had separated national financial markets. Financial liberalization has been permitted by the same technological developments—computer and information technology networks—that have enabled the global coordination of production and distribution by transnational corporations. However, the movement in the direction of liberalization is not a consequence of technology, but was driven by states.

TABLE 3

CROSS-BORDER TRANSACTIONS IN BONDS AND EQUITIES, 1975-1996
(PERCENTAGE OF GDP)

	1975	1980	1985	1989	1990	1991	1992	1993	1994	1995	1996
United States	4	9	35	101	89	96	107	129	131	135	164
Japan	2	8	62	156	119	92	72	78	60	65	84
Germany	5	7	33	66	57	55	85	171	159	172	200
France	..	5	21	52	54	79	122	187	201	180	227
Italy	1	1	4	18	27	60	92	192	207	253	468
Canada	3	10	27	55	64	81	113	153	212	194	258

Source: Bank for International Settlements, Annual Report, 1997, p. 79.

The shift to floating exchange rates, together with the liberalization of capital movements, has created the opportunity for speculative activity, bringing with it exchange rate volatility and an uncoupling of currency values and output and trade performance. A quarter of a century after the end of fixed exchange rates, the vast majority of short-term capital movements are unrelated to the state of production and trade in individual economies, and currency values offer little or no indication of the balance of trade or current account.[28]

The fact that the American dollar has remained the international currency standard despite stagnant productivity, chronic trade deficits and a massive world surplus of dollars is a particularly glaring example of this.

This development has made a mockery of neo-liberal assurances that moving from a system of fixed exchange rates to a floating system would result in greater national policy autonomy. The deregulation and international integration of national financial markets has increased the ability of capital to constrain domestic monetary policy. Speculative short-term capital movements have forced governments to direct energies towards stabilizing the external balance. This stabilization increasingly comes, as in the gold standard period, in the form of the competitive austerity of deflation and cuts in working class living standards.

Ad hoc attempts to coordinate exchange rate policy among the G-7 have ensued. Indeed, emergency world economic summitry to battle payments crises is a constant feature of the world configuration today, though the currency crises in Italy and the U.K. in 1992, in Mexico in 1994, and East Asia in 1997-98 underline the volatility generated by unregulated short-term capital movements.

Despite fears of a revival of protectionism amidst a stagnant world economy, the international trade regime continues to be liberalized; a proliferation of bilateral, regional and multilateral trade liberalization agreements now pursue the 'deep integration' of national economies through the removal of non-tariff barriers and the harmonization of trade-related legislation.[29] The GATT rounds have moved beyond trade in manufactures, to provisions around agriculture, intellectual property and trade-related investment measures (TRIMs).

Under the stewardship of the WTO, which replaced the GATT in January 1995, service-sector activity has become the focus of trade liberalization efforts, as trade in services has doubled over the last 10 years to reach US$1 trillion per annum, representing over 20% of total trade.[30] Most recently, the Uruguay Round concluded under the WTO with an agreement committing member states to liberalize their markets in financial services, an astounding leap of faith amidst the currency turmoil, banking crises and debt problems plaguing all zones of the world.[31]

TABLE 4

IMPORTS AND EXPORTS OF GOODS, 1970-1993
(PERCENTAGE OF GDP)

	Imports of Goods					Exports of Goods				
	1970	1980	1985	1990	1993	1970	1980	1985	1990	1993
United States	4.0	9.2	8.9	9.3	9.5	4.2	7.9	5.1	6.7	6.8
Japan	9.3	13.3	9.6	7.9	5.7	9.5	12.2	13.1	9.8	8.6
Germany	16.2	22.9	25.3	22.2	17.9	18.5	23.6	29.4	25.9	19.9
France	13.2	20.2	20.4	19.4	16.0	12.4	16.7	18.5	17.5	16.4
Italy	13.9	21.8	20.8	16.2	14.6	12.3	17.4	18.5	15.5	17.1
United Kingdom	17.4	21.9	23.7	22.9	22.4	15.5	21.2	21.9	18.8	18.2
Canada	15.3	21.8	21.7	20.2	23.6	19.0	23.8	24.5	20.8	24.5
OECD Average	21.1	26.9	27.6	25.1	23.0	17.7	22.8	26.0	23.5	23.4

Source: OECD, OECD Economies at a Glance: Structural Indicators (Paris: OECD, 1996), p. 63.

Since the mid-1980s and the slowdown in world output growth, foreign direct investment has replaced trade as the principal form of international capitalist expansion. Global sales of foreign affiliates since 1987 have climbed faster than exports, as the extension of production facilities to foreign markets has allowed the exploitation of economies of scale unavailable from the continued penetration of markets through exports.[32] Between 1982 and 1994, the world's stock of FDI increased by a factor of four, doubling its share of world GDP to 9%, and growing twice as fast as gross fixed capital formation between 1986 and 1995.[33] Much of the growth of FDI has taken the form of cross-border mergers and acquisitions, rather than new investment.

Alongside this concentration and centralization of FDI, the share of intra-firm trade in total trade flows has also risen, while the internationalization of services, and especially business and financial services, has driven much of the growth of FDI. An ever-growing share of output, trade and investment is organized by TNCs, as integrated international production links national economies more closely.

TABLE 5

VALUE OF THE GROSS PRODUCT OF FOREIGN AFFILIATES AND THEIR SHARE IN GDP BY REGION (BILLIONS OF DOLLARS AND PERCENTAGE)

	Gross Product of Foreign Affiliates			Gross Product of Foreign Affiliates as percentage of GDP		
Region	1982	1990	1994	1982	1990	1994
World	553	1 383	1 557	5.2	6.7	6.0
Developed Countries	403	1 098	1 099	5.1	6.7	5.4
Western Europe	179	607	610	6.0	8.7	7.9
European Union	164	570	568	5.7	8.6	7.7
Other Western Europe	15	37	43	9.9	10.7	11.0
North America	177	407	392	5.1	6.7	5.2
Other Developed Countries	47	84	97	3.4	2.4	1.9
Developing Countries	150	283	445	6.0	7.0	9.1
Africa	15	28	32	4.4	7.4	8.8
Latin America/Caribbean	59	101	162	7.6	9.3	10.3
Asia	74	151	248	5.6	5.9	8.6
West Asia	30	39	36	6.7	4.0	6.7
South, East & South-East Asia	44	112	211	5.0	7.0	9.0
Central and Eastern Europe	0.1	2.3	12.6	0.1	1.1	2.3

Source: UNCTAD, World Investment Report 1997, p. 267.

TABLE 6

INWARD AND OUTWARD FDI STOCK BY REGION, 1980-1995
(PERCENTAGE OF GROSS DOMESTIC PRODUCT)

Region	1980	1985	1990	1995
World				
inward	4.6	6.4	8.3	10.1
outward	4.9	5.9	8.1	9.9
Developed Countries				
inward	4.8	6.0	8.3	9.1
outward	6.5	7.5	9.8	11.5
Developing Countries				
inward	4.3	8.1	8.7	15.4
outward	0.5	1.0	1.8	4.5

Source: UNCTAD, World Investment Report 1997, annex table B.6

TABLE 7

INWARD AND OUTWARD FDI FLOWS
AS A PERCENTAGE OF GROSS FIXED CAPITAL FORMATION,
BY REGION AND ECONOMY, 1985-1995 (PERCENTAGE)

Region/economy	1985-1990 (annual average)	1991	1992	1993	1994	1995
World						
inward	5.4	3.1	3.3	4.4	4.5	5.2
outward	6	3.9	3.8	4.8	4.7	5.6
Developed Countries						
inward	5.5	3.2	3.2	3.7	3.5	4.4
outward	8	5.3	4.8	5.4	5.1	6.3
Developing Countries						
inward	8	4.4	5.1	6.6	8	8.2
outward	3.5	0.9	2.2	3.1	3.6	4

Source: UNCTAD, World Investment Report 1997, annex table B.5.

Table 8

Cross-Border Merger and Acquisition Purchases, 1990-1996
(millions of dollars)

Region	1990	1991	1992	1993	1994	1995	1996
World	159 959	85 279	121 894	162 344	196 367	237 184	274 611
Developed countries	152 201	79 900	99 168	134 895	163 010	212 084	239 139
European Union	90 967	50 537	50 017	74 770	75 333	98 725	114 316
North America	26 234	15 690	26 361	44 655	52 042	80 386	87 496
Developing countries	7 548	5 199	22 319	26 858	32 365	24 464	32 827

Source: UNCTAD, World Investment Report 1997, p. 358.

While most FDI originates in the industrialized countries of the North, in the 1990s a growing share has been directed at the developing world, increasingly in manufacturing and services. The privatization of state industry in the South, and the opening up of national infrastructure to direct foreign involvement has presented opportunities for FDI originating in the North.[34] A number of newly-industrializing economies account for the majority of inward investment; countries traditionally closed to foreign penetration, such as China and India, have grown in importance as sites for foreign direct investment.

The increasing role of transnational corporations in reshaping and integrating production systems on a global basis is behind much of the increase in FDI flows. But control in the form of product ownership (in the form of patents) rather than equity ownership have allowed corporations to control production and marketing (practices that the MAI would enhance). The influence and control of TNCs over the growth and integration of international production and marketing extends beyond what is indicated by FDI indicators and other measures of capital ownership:

> *...by differentiating their machinery, processes, and product, transnational corporations can preserve supply, servicing, and maintenance linkages.... Many of the ventures of transnational corporations therefore no longer include much or all equity: joint ventures, management agreements and service contracts, licensing and franchise arrangements, production-sharing agreements, and subcontracting can all replace equity.*[35]

Profits on foreign direct investments may thus be complemented or substituted for by interest, royalties, management costs, and service charges, so that the scale of TNC influence is underrepresented if FDI figures are considered alone.

The pattern of trade and investment flows is producing regional economic integration in the shape of continental trading blocs. Integration via trade and investment is occurring to its greatest extent between member states of the European Union, and between Canada and the United States. TNCs operating at a European or North American level make use of different national labour markets, capital markets and technological networks to coordinate a continental intra-industry division of labour.[36]

Regionally-operating firms can take advantage of resource and wage differentials between production sites to reshape the intra-firm division of labour. "Firms are increasingly able to divide the production process into different stages and locate them according to comparative advantage—'slicing up the value chain'—thus increasing trade in inputs and semi-finished manufactures."[37] Even within blocs, TNCs are still reliant on home-base support, economically and politically, and competition between nationally-based transnational firms has in many respects intensified.

Despite increasing regional integration, trade and investment flows between blocs remain substantial. Capitalist rivalry via internationalization has by no means disappeared.[38] Capitalist competition is most visibly taking the form of imperialist rivalry at the margins of the world economy—for example, in the struggle for advantage in the newly-integrating regions like Cuba and Iran, in the newly-privatized state sectors of telecommunications and infrastructure in the South, in the often-criminal scramble over the division of assets and markets in the 'transition economies' of Eastern Europe, and in the struggle to pry open East Asian markets to Western buyouts and joint ventures with the aid of IMF adjustment packages.

Competitive Austerity and Economic Instability

Balance of payments equilibrium in capitalist economies crucially depends upon unit labour costs at the prevailing exchange rate. Any country that can combine new techniques with relatively cheap labour will gain competitive advantage and increased production. All countries cannot run a surplus. Trade can turn nasty, as some countries run into balance of payments problems and stagnation.

Trade deficits require financing in the hope that borrowing to get in balance will later generate the surpluses to pay off loans. To do so requires that investments build up competitive capacity and not be used to finance consumption. More importantly, surplus countries must later go into deficit so that foreign exchange may be earned for repayment of loans and interest. This typically depends in deficit countries upon some mixture of devaluation and deflation in an attempt to reduce imports while increasing exports.

These policies, however, raise their own problems. Deflation reduces demand and creates unemployment, while devaluation destabilizes investment although industrial capacity must be developed to meet import substitution and export demands. The more widespread are payments imbalances between countries, the less likely the adjustment process can work for any single country without damaging its economy. The repeated failures of structural adjustment polices for developing countries have all too clearly shown this.

Moreover, there is a competitive incentive for other countries to match devaluation and austerity to avoid large losses. Liberalization of trade and financial flows cannot be justified on the basis of actual remedies, but by the religious faith that capital and exchange markets are always efficient and *in the long run it will all work out.*

Structural imbalances have characterized capitalism for some time now. In the post-war period, the U.S. supplied dollar liquidity to the world through capital exports to finance trade imbalances. This continued until the dollar became unsustainable as the hub currency and Bretton Woods collapsed in the early 1970s.

Since the late 1970s, the IMF and the World Bank have promoted financial liberalization as the mechanism to finance trade adjustments and have used foreign exchange markets to impose market imperatives on national economies. Yet trade imbalances and debt loads have not cleared. Many countries, especially in Africa, have pushed the effort to meet external obligations and to increase exports to desperate levels of poverty and environmental destruction. The Asian economies, which but a few months before they became enveloped in economic crisis were being touted as the model and locomotive of economic advance, now potentially face the same dire consequences.

The lesson that flexible rates had the capacity to destabilize national economies moved the world economy to more managed rates after the Plaza and Louvre Accords of the 1980s. Through the 1990s, fears of inflation and external instability have imposed a quasi-fixed exchange rate system. This is especially so for the U.S., where capital inflows have again raised the value of the U.S. dollar out-of-synch with its trade position: yet currency devaluation (or even the U.S. bringing its trade balance under control) would potentially throw the world economy into enormous turmoil.

Hence adjustment of trade imbalances has increasingly had to fall entirely on what the IMF calls expenditure reductions and more flexible labour markets—austerity and unemployment. The trade imbalances, however, remain and it is becoming quite un-clear, even to those favourable to this approach, how they can be corrected and financial obligations be met without politically unpalatable measures.

Regional and national policies for competitiveness through high-technology have everyone trying to export more, while cutting wages and social expenditures, under the discipline of portfolio and direct investment financial flows. This has established an international configuration of intense structural conflict—the interdependence and rivalry of national states, the stagnation and instabilities of the economic system.

Liberalization of international economic activities has neither been smooth nor soundly based. It has occurred in a context of deepening stagnation, redistribution of productive activity from the domestic to the traded sector dominated by TNCs, and the growth of hyper-active international financial markets. Against the one-sided accounts of globalization generated by the World Bank, the International Labour Organization's recent survey of world labour conditions concludes that "the world employment situation remains grim...there has been growing concern over the social exclusion that is breeding."[39] Far from being unique, the recent turmoil in Asia shows just how unstable world capitalism is.

2. CONTRASTING PERSPECTIVES ON GLOBALIZATION OF INVESTMENT

The imbalances and precariousness of the world economy have kept discussion of reform front and centre. It is notable that further expansion of the world market has been persistently invoked as a solution to both payments imbalances and national income and employment problems. FDI figures prominently in these discussions.

Neo-liberalism, Direct Investment and the MAI

Liberalization of investment flows is defended by neo-liberals on a number of specific grounds, over and above the invocation of the imperatives of globalization. A treaty to protect the gains from open investment flows is being pursued as a necessary institutional support to market processes that are seen as too often subject to capricious actions by states (even if these states are acting through constitutional means and democratic mandates).

The fundamental argument, of course, is that market allocations of investment are inherently efficient and that lifting barriers to investment flows will increase competition, and thus efficiency and innovation. Performance requirements, protections for home industry, incentives and the like that distort the 'efficient' allocation of capital, as much within states as between them, should be dismantled.

Free markets, rather than state planners, allocate resources best via price signals free of the distortions of regulation and screening of foreign investment (or other short-term capital flows). Foreign direct investment, freed from distortions and barriers, allows industrial rationalization so that higher-productivity, more competitive firms will prevail and 'best-practice' technologies spread.

Liberalizing and deepening international capital markets, it is argued, would also be *equalizing* internationally insofar as protected investment flows encourage and permit private lenders in the mature economies of the North, where savings exceed investment opportunities and investments face declining returns, to lend to the savings-constrained economies of the South or the emerging markets of the transition economies of Europe and Asia, just beginning to develop and promising higher returns on investments.[40]Profit incentives would therefore direct flows of portfolio and direct investment from the mature economies of the rich world to newly industrializing states and emerging markets, and thereby contribute to global convergence of incomes through market processes.

These alleged gains from trade and specialization should, in their turn, be *stabilizing* of the world payments system in the long-term. There is an additional, more immediate reason to favour investment liberalization. The debt burden and the instability of short-term financial flows has made it less than prudent for countries, it is argued, to rely on private bank lending for financial requirements.

External financing to support the domestic growth process, and to strengthen long-term economic capacities to innovate and trade, is better in the form of direct investment that lengthens the payments period and, in an open trading system, would earn foreign exchange.

Thus, neo-liberal proponents conclude: "An MAI would provide a better institutional structure with which to reflect the interrelated and complementary nature of investment, trade, services, intellectual property, standards setting, competition policy and related 'domestic' policies, all of which have become key determinants in the international contestability of markets."[41]

The argument for FDI is really the contention that unimpeded market forces offer direct benefits to host countries. TNCs are the source of technical and social progress in a globalized world. This result, of course, depends upon the absence of market failures such as externalities, research and development spread effects, non-monopolistic market structures, linked investments, and so on. All of these types of technological and institutional capacity-building have depended upon industrial policy-making, especially the political capacity to enforce TNC performance requirements and to review and even prohibit market access.

There is even less guarantee that the investment that does take place will be of the type that addresses any kind of social and democratic prioritizing of needs. Only in the idealized view of TNCs, legitimate shepherds of the development process, can the limitations that an MAI imposes be justified.

There are few grounds for claims about the global allocational efficiency of liberalized investment flows. Instead of capital flowing into long-term productive investment in the South, the debt crisis of the early 1980s combined with monetarism and tax cuts in the North to produce capital flight out of long-term lending to the South to finance consumption and the upwards redistribution of wealth in the developed countries of the North. Such misallocation is in fact a more common feature of deregulated markets than neoclassical economists concede, as investors' 'herd instincts' can lead flows to become cumulative rather than stabilizing.

Global capital flows have recently produced disastrous flights of short-term and long-term capital in Mexico and East Asia. These forms of 'investor uncertainty' go far deeper than the risks of 'expropriation' or 'discrimination' that MAI advocates warn. The source of investor uncertainty lies in the asymmetries in the world economy that have massively increased the risk (the rational basis for the irrational growth in hedge markets, and so on) and severed any strict relation between capital flows and allocative efficiency. FDI raises these risks by committing in the long term a significant portion of the payments balance to capital outflows through eventual profit repatriation. Thus, FDI may well add to present destabilizing elements in the world economy.

The second claim that liberalization will be equalizing historically only holds for the advanced industrial countries and fails to explain the persistence of world inequalities.

More recently, the growth of FDI and liberalization of FDI flows have coincided with increasing global inequality, including greater impoverishment of the poorest. According to UNCTAD, the richest 20% of the world's population increased its share of world income from 69% in 1965 to 83% in 1990.[42] Per capita income among the richest quintile averaged 31 times that of the poorest; by 1990 it had reached a factor of 60.

The growing inequality during this period of liberalisization extends to inequalities *between* countries and *within* rich and poor countries, as well. When one considers that 98% of world FDI comes from TNCs based in 23 OECD countries, and is in fact reinvested in this zone, there is good reason to be skeptical about the equalizing tendencies of financial liberalization, including that of the MAI.

The 'deep integration' proposed by MAI investment liberalization is, finally, likely to be destabilizing. The interaction between trade balances, national demand conditions and increasing economies of scale from investment in advanced technologies reinforces patterns of relative economic strength and weakness. The persistent world inequalities stem from this tendency, as "existing

TABLE 9

INCOME INEQUALITY SINCE 1970 BY REGION

		Gini Coefficient in per cent			Ratio of Richest Quintile to Poorest		
Region	Number of Countries	1970-1979	1980-1989	1990-1994	1979-1979	1980-1989	1990-1994
Developed Market-Economy Countries	12	31.60	32.02	32.78	5.59	5.56	6.02
Transition Economies							
Eastern Europe	4	22.34	22.94	27.85	3.09	3.13	4.05
Russian Federation			26.40	30.53			5.08
China			31.51	36.20		4.74	6.10
Developing Countries							
Latin America	10	49.86	51.39		14.46	15.58	
East Asia	7	41.08	40.98		8.29	8.20	
Sub-Saharan Africa	10			44.64			9.52
North Africa	4			38.03			6.57
South Asia	2	31.06	31.73	31.28	4.56	4.71	4.63

Source: UNCTAD, Trade and Development Report, 1997, p. 108.

advantages are reinforced and the resulting spatial distribution of economic activity is likely to exhibit strong divergences, leading to increasing inequalities within and between regions."[43]

The tendency is the reverse for deficit countries which are compelled to adjust by deflating and use their price advantage in a liberal trading environment to export their way to economic advance. But, with slow output growth, global overcapacity and the fact that the richest and largest economy in the world capable of absorbing imports must also begin running a surplus to pay off the largest buildup in sovereign debt ever make this a precarious proposition. The threat to transmit deflation around the world is now an active concern, even among the backers of liberalization.[44]

As under the gold standard, deregulated capital flows and bond rating agencies are the anonymous disciplinary agents enforcing deflationary regulation of economic policy. Investment liberalization encourages the vicious interaction of austerity and polarization: it strengthens the capacity of firms to invest internationally and, through competition to capture investment, to engage in competitive bargaining over taxes and wages (a process well understood by the architects of post-war order capital controls).[45]

This also explains why lower wage countries in the South, with lower labour and environmental standards, are seeking to avoid having their 'competitive advantages' prohibited by the inclusion of labour and environmental standards in the WTO or the MAI. By casting a 'chill' on government reflationary or redistributive interventions, the MAI would further enforce the fiscal austerity and monetary tightening of the past decade around competition for investment. Indeed, as external financing in the form of private financial flows continues to account for a significant proportion of capital formation and to claim a larger portion of payments balances, the liberalization of investment flows will carry potentially greater consequences as national and economies become more and more dependent on an uncertain and competitive international situation. By entrenching investor rights and fully deregulating short-term and long-term flows, the MAI makes the world economy more unstable and uncertain.

Open-Economy Social Democracy

The failures of neo-liberalism have led many to become skeptical of the panacea of globalization. However, confusion around what medium and long-term alternatives there might be to global neo-liberalism is equally pervasive. Just as Keynes observed in 1933, there is a growing feeling today that—

> *...decadent international but individualistic capitalism...is not a success. It is not intelligent, it is not beautiful, it is not just, it is not virtuous—and it doesn't deliver the goods. In short, we dislike it and we are beginning to despise it. But when we wonder what to put in its place, we are extremely perplexed.*[46]

Opposition to neo-liberal globalization is certainly building everywhere. But what might replace it remains an exacting question.

For one strand of left critics, globalization represents a 'world market of opportunities' in which domestic prosperity and international capital mobility are mutually reinforcing. Hirst and Thompson, for example, argue that "free trade, in combination with the management of investment, offers the best prospect for promoting growth through fairer redistribution."[47] Investment regulations such as the UN *Draft Code of Conduct on TNCs*, which epitomize an outdated era in which TNCs were viewed as "exploiters and a threat to national economic autonomy," need to be replaced by a regulatory regime able to realize mutual gains from global capital mobility. Such an accord "would avoid 'beggar-my-neighbour' policies, first by governments in terms of their competitive attempts to attract FDI, and second by firms in their attempts to try to play one country off against another."[48]

In addition to setting out the property rights of TNCs, such an agreement would protect labour rights and working conditions, and "recognize the rights of government to defend certain of their legitimate national functions in respect to the economy— support for R&D, defence considerations, balance of payments issues, etc."[49]

Precisely because the tendency of international investment to exacerbate inequalities within and between regions threatens to undermine growth, Kozul-Wright similarly argues that "the full benefits of international integration require a complementary and robust framework of social agreements and constraints—including strong nation states—to resolve problems generated in production and to manage distributional conflicts."[50]

Above all else, this 'open-economy social democracy' viewpoint is concerned to preserve governance functions that facilitate accumulation within legislative frameworks of minimal social provision. It devotes little attention to strengthening the ability of democratic authorities to constrain capital, a view that they would no doubt charge with anachronistic "hostility" and "antagonism" towards TNCs, as if capitalist agencies had suddenly become merely efficient organizations of social progress apart from the economic stagnation and social inequalities that have been growing.[51]

In this strategy, there is no conception of conflicting interests that involve power and struggle between the objectives of private accumulation and of democratic provision for social need. The revisionist naiveté of such arguments is alarming in a period where capital mobility and threats of capital strikes are regularly being invoked to overturn redistributional policies. The capacity to determine social priorities is being displaced, through trade liberalization in general and investor-protection proposals like the MAI in particular, from democratic deliberation and coordination of economic activities to the ability of the state to supply profit-enhancing inducements to capitalists, national and foreign, to invest and hopefully to then be taxed. But why floors on these inducements should not be eroded by mobile capital—especially as states compete to provide competitive investment locales, if there are no direct constraints placed on capital—is left unexplained. This is ultimately the view that there are forms of 'progressive competitiveness' where social partnerships can be struck between workers and capitalists, national and foreign, that advance a general interest apart from class divisions.

A more common Left critique is far less naive about the obstacles that TNCs pose to social priorities that conflict with the logic of the market, and some of the power issues at stake. An alternative investment treaty to the MAI is needed, it is argued, that protects redistributional goals against the deterioration of public goods and the environment from commodification and social dumping. The alternative, possibly fashioned around the 1974 UN Charter of Economic Rights and Duties of States, would begin by recognizing and protecting the sovereign right of states to regulate investment in the 'national interest'.[52]

Explicitly raising performance requirements for corporations around employment, labour adjustment, and the environment would be complemented by a tighter competition policy that restricted corporate concentration (especially via foreign acquisitions of Canadian companies) and speculative activity. Although often ambiguous on this point, some form of international agreement on capital controls and profit repatriation is also often sought, as for example in the endorsation of the Tobin Tax on currency trading. This perspective is clear, if not always forthright enough about where contemporary social democracy is placed, in the political opposition and mobilization necessary to install these provisions into any multilateral investment agreement.

This critique has a number of limitations, however. Strategically, social forces attempting to rein in capital are better placed to be effective organizing on national and local levels rather than the international level, where the political base to mobilize pressure for constraints on capital are stronger. Politics remain principally national rather than supranational, and, without strong national bases of support, the scope for re-regulating capital at the international level, and forming a wider and necessary internationalist politics, is limited.

In the absence of national and local movements, side agreements on environmental and labour standards contained in international trade deals will remain marginal and weak protection against the imperatives of capitalist competition and economic internationalization, if the NAFTA side-agreements are at all indicative.[53]

International solidarity and pressure for regulation is a crucial and effective part of confronting globalization. But it is most effectively organized as stemming from strong national and local efforts to control and shape market processes. Local communities and nation-states have historically permitted workers the means, through struggle and political mobilization, to impose social and political controls on the logic of capitalist accumulation, thereby improving working conditions and extending some limited measure of democracy into the economic sphere.[54] As Bienefeld has noted,

> *...history has demonstrated the importance of the nation state as the one arena within which it has occasionally been possible to harness and channel the explosive but volatile and potentially de-*

structive power of the market...The absence of a plausible global alternative implies that national controls over capital must remain the most important immediate object of struggle.[55]

International effectiveness is therefore a reflection of the balance of social forces within local and national bases. Only until significant opposition is mounted in a significant number of local and national settings can the balance of power be shifted.[56]

However, allowing capital mobility and international competitiveness to determine the value-formation process, while imposing performance requirements on transnationals and limits on the downward levelling of competition, contains a more basic contradiction. To begin with, the internationalization of production has provided the ammunition for the attack on national controls on capital. With capital mobility preserved, domestic welfare goals such as employment and redistribution can be met only to the extent competitiveness is secured.

Yet floors placed under competition by international agreements will always be at risk in a world of massive inequalities and labour surpluses. Burdened by debt or plagued with faltering competitiveness, it will always be in the interest of some countries to exploit their 'comparative advantage' of surplus labour or lax environmental protection. Insofar as the imperative of competitiveness and rapid export-led growth is preserved, so is the incentive for states to remove restrictions on competition, precisely in the interests of employment and income.

The *threat* of mobility of investment is frequently sufficient to extract concessions from defensive workers and unions, leaving aside the actual capacity of firms to shift production activity. Facilitating the expansion of production on an international scale preserves the external orientation of national economies, maintains the dependence of national economies on private decision-making, and sustains the terrain of operation from which capital can whipsaw governments and labour forces.

3. Beyond the MAI

After two decades of freer markets and policies, neo-liberal globalization continues to strip away the limited stabilizing and redistributive structures of state regulation built up over the post-war period, without constructing any stable institutional order in its place. This threatens to reinforce and aggravate the relationship between greater inequality, slower growth, and financial instability. Far from being inevitable or desirable, therefore, global neoliberalism is looking increasingly *unsustainable* economically, socially, and environmentally.

The deep-seated contradictions of the present volatile and polarized world economy point to the need to encompass opposition to the MAI within a broader strategy of confronting globalism. The ability to impose performance requirements on TNCs will be of limited value in reversing the downward pressures of globalization if they must be restricted to measures promoting competitiveness; labour standards enshrined at the international level will be weak if states and firms—and workers themselves—are under constant pressure to ignore them.

Entrenching property and mobility rights for corporations undermines labour and other groups, not by weakening the state, but by diminishing the political space from which to impose democratic priorities on capital. Globalization, even in the shape of the MAI, is not so much a threat to <u>state</u> sovereignty as it is to <u>popular</u> sovereignty in the form of substantive capacities to democratically coordinate economic activities and enforce egalitarian measures. For this reason, the restructuring of the state in response to the internationalization of capital, the problem of envisaging and pursuing a more democratic state is more pressing than ever, if we are to break the impasse of seeking international guarantees for regulatory powers that political éltes and capitalist classes are doing their utmost to rid themselves of.

Expanding the scale of democracy will require reimposing controls on capital, redirecting production, re-establishing the credibility of public ownership, reversing the polarization of work and income, and fashioning institutions and industrial strategies to develop workers' skills and democratic capabilities.

At present, it is difficult to envisage institutions existing at the international level that might be capable of subordinating capitalist power to democratic decision-making apart from strong local and national movements.[57] The construction of these institutions is daunting. Yet market liberalization measures like the MAI that continue to strengthen unaccountable private power have placed the building of democratic institutions adequate to a more egalitarian and sustainable society more firmly on the agenda.

ENDNOTES

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