Chapter 6

Hypotheses for research

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The present chapter develops a number of research themes and hypotheses as a prelude to our country case studies. Our project is located in the debate on the effects of globalisation. We explore the agency and room of manoeuvre of nationally based states and 'producers' (companies and farmers) that respond to global and regional financial 'flows', 'webs' of transnational business organisations and regulations that prescribe standards, property rights and 'economic liberal' practices of trade and investment.

In the following discussion we firstly develop a number of hypotheses about the 'immediate effects' and general trends associated with processes of globalisation and regionalisation with regard to the accomplishment of industrial upgrading, a stable and reliable system of finance, environmental sustainability and a secure livelihood. Secondly, we develop hypotheses about the ability of local actors to adjust and modify these structural constraints. Finally we develop hypotheses about the effects of these processes relating to two main issues within the globalisation debate; whether globalisation promotes institutional convergence, and the role of globalisation in creating winners and losers between countries as well as within countries.

a) Global political regulation and local adjustment

While our discussion of global political regulation will cover more areas, the present discussion focuses on the role of the WTO, the World Bank and the IMF. In combination with the expanding number of bilateral and regional trade agreements, the WTO normally will be the agency with the strongest influence on local policy making and governance during normal periods in the kind of fast-growing middle-income countries that mainly – but not exclusively – are discussed in the present volume. Normally, these countries do not rely on assistance provided by the IMF and the World Bank, while they are heavily involved in foreign trade and vulnerable to rulings by the WTO. The main exception to this rule will be periods of major economic crisis, such as the 1997/98 Asian financial crisis, where also middle-income economies such as South Korea and Thailand had to rely on emergency credits under IMF control. However, once the economies revived the countries tended to shift to less "orthodox" policies, demonstrating the limited leverage of the IMF during normal times.

Global regulations are becoming increasingly penetrating. For instance, structural adjustment demands have been extended from issues of macroeconomic balance in the early 1980s to detailed guidelines for micro-level public and private sector policies and institutions. Similarly, the WTO framework has been extended to include intellectual property, trade-related investment, services and agriculture in addition to the traditional focus on merchandise trade. These new policy areas are creating juridical infrastructures, regulating international trade and investment, and are the result of economic and political pressure, especially from the United States.

The standards and policies of the global organisations are also becoming increasingly interlocked. For instance the World Bank and the IMF use the WTO's review of country performance through the Policy Review Mechanism (PRM) in their own evaluation of policy performances. Given this background of increasingly penetrating and interlocked forms of global regulation, we move on to our hypotheses.

a.1: Global regulation has a constraining impact on national development strategies. For instance, WTO regulations such as TRIPs and TRIMs are weakening import-substituting strategies and sector-based industrial policy programmes. Financial service liberalisation and conditionality demands from the IMF impede national strategies of capital control and promotion of domestic financial institutions. The WTO's agricultural regulations weaken small-scale and subsistence-oriented farming at the cost of large-scale agri-business.

a.2: Despite this constraining impact, global regulations are reconcilable with innovative strategies of adjustment and interpretation. For instance, while WTO rules impede subsidisation of import-substitution programmes to targeted sectors, they do not rule out publicly supported research and development networks with a certain degree of targeting of new sectors of production. Thus, industrial policies are as likely to be refashioned due to the impact of global rule making, as to be completely abandoned. The outcome (abandonment or refashioning of industrial policies) will to a large extent depend on local conditions and capabilities.

a.3: We argue that global regulations do not only reduce nation states' possibilities of undertaking interventionist policies, but also force them to improve regulatory capacities. In that respect the rules are enabling as well as constraining. However, an effective organisation is a key factor in responding to global rules, such as the WTO's sanitary and phyto sanitary regulation (SPS). If no actions are taken to increase capacities to coordinate and control compliance and assessing conformity to SPS and other rules, regulation will be left to market forces. This, we argue, will generate marginalisation of both countries and individual companies, as these are excluded from participation in core markets. Henceforth, both institutions and firms need sophisticated management, which cannot be taken for granted. However, we will also argue that countries that have the capacity to upgrade support institutions and individual firms to international SPS standards have the opportunity to link up to global value chains, gain original equipment manufacturing (OEM) status and by that increase the value added in their production.

a. 4: Global regulations may be ignored to a greater or smaller extent. The authority of global governance organisations is restricted, their demands are sometimes contradictory, difficult to operationalise and open for negotiations. The conditionality organisations in particular may also sometimes ignore defiance of their demands for political reasons.

a.5: Global regulations are likely to have a bifurcating national impact, creating winners and losers. WTO rules on intellectual property may for instance favour large enterprises with the capacity to establish strategic alliances with TNCs, while going against smaller enterprises that rely on copying which is ruled out by the new rules. Similarly, agri- and aquacultural export producers may benefit from international market access through the WTO, while small producers loose domestic markets or are incorporated into global webs of production in a less favourable way in the process. We do however contend that the extent of bifurcation resulting from global regulations will vary, depending on local conditions.

b) Global webs and local adjustments

'Global economic webs' refer to the functional integration and transnational organisation of production and services through corporations. Global firms are involved in international operations in intricate ways, some of which take the form of equity-based intra-firm control, while others are inter-firm and based on a variety of non-equity based forms of co-ordination and control. The terms global production networks, global value chains or global webs refer to this mixture of governance forms. It should be observed that foreign investments and non-equity based extension of manufacturing and services are concentrated in a growing but still limited number of developing countries. However, most of countries dealt with in this book actually belong to the emerging economies in which linkages to global (and regional) production network play an increasing role.

In this volume we are investigating how the activities of transnational economic actors impact upon socio-economic development in developing countries. More precisely, we are concerned with the following issue: under what conditions can we expect TNCs and global traders to play a developmental role and under what conditions that is not the case.

b.1: We contend that the potential for building linkages between TNCs and local firms and institutions differs according to TNC strategies. Such strategies, in turn, vary according to country of origin (e.g. United States vs. Japan), market focus (e.g. domestic vs. export markets), ownership structure (e.g. wholly vs. partly owned subsidiaries) and sector (e.g. electronics vs. chemicals).

b.2: We hypothesise that TNCs and global traders generally have an increasing interest in upgrading a few selected partner companies in developing countries but that they have little to offer to the many enterprises which are weak in the sense that they are not able to live up to the higher and stricter requirements concerning price, quality, flexibility and delivery. Therefore, if left to the 'market forces', global webs and global opening tend to 'upgrade the few and marginalise the many'.

b.3: We hypothesise that with regard to the potential for building domestic capabilities, the core competence strategies of TNC provide opportunities as well as constraints. The local business community may be increasingly able to acquire knowledge and capabilities in the fields of human resource management, quality management, process control, logistics etc. This learning may take a direct form (such as technical assistance or training) or may take the indirect form of spillovers from day-to-day business transaction. At the same time customer firms will be increasingly protective of their core knowledge and competences (product technology, design, marketing and branding).

b.4: As for the agricultural and aquacultural system, our focus is on the impact of globalisation and adjustment to globalisation in terms of sustainability and livelihood of the rural population as well as economic adjustment. We contend that the new kinds of global webs of agricultural/aquacultural production are likely to integrate small primary producers in an unfavourable way into the global economy, unless they are checked by pro-producer government regulations and local organisations. WTO regulations further complicate successful adjustment, which require the legal ability and commitment to small-producers interests on the side of the government. In addition, political and social protection must go along with policies to upgrade agri-/aquaculture by the government or agri-/aquacultural associations, for instance through infrastructure development and research. Successful adjustment will then to a large extent hinge on a strong institutionalised commitment to small producers within the political regime.

b.5: The ability of business organisations and companies to adjust to the global webs varies considerably. The likely outcome depends on the strategic intent, strength and flexibility of enterprises (as well as the policy environment).

b.6: States may play a crucial role in two ways. Partly, by improving the attractiveness of their countries to foreign investors/buyers. Though that attractiveness in this context is mainly generated by broader societal conditions - such as the actual and potential size of the market; the factor and resource endowment of the country; the relative price structure, including the price and availability of relevantly qualified labour; the basic infrastructure and communication system; and basic attitudes to work; etc. - these conditions, particularly in a longer-term perspective, may be influenced by state interventions. Partly, the state plays a crucial role through interventions that aim at ensuring an appropriate selection of TNC investments and operations in keeping with national development priorities; at increasing net benefits from on-going TNC activities by inducing established investors to upgrade their products, processes and functions; and at developing local capabilities and absorptive capacities, so that the local firms can take advantage of the links with foreign investors and with global value chains more broadly.

b.7: There are considerable variations in the capacities of state agencies to design such policies and implement them according to the broader development strategies. Concerning the between-country differences, we expect a clear differentiation between strong developmental states, intermediate states and weak states. Concerning differentiation along the stages of the policy process, we suggest that the autonomy of policy elites and state autonomy in a broader sense are more limited at the implementation stage and that it is often severely limited at the impact stage (in the sense that intended effects cannot be brought about by state action). We suggest the following critical prerequisites for achieving and enhancing state capacities, particularly in relation to industrial development but also to some extent concerning environment management: a) developmental commitment among political elites; b) insulation of the bureaucracy that allows bureaucrats to implement policies in accordance with rules and in keeping with politically established priorities; c) a high-quality civil service with competence to formulate and implement economic policies; d) institutionalised government-business co-operation where policies are not simply imposed by politicians and bureaucrats but where policies are formulated and implemented as part of regular and extensive consultation and co-ordination with organised business and other key economic groupings.

b.8: In relation to the issue of convergence or non-convergence, we argue that global production networks are complemented by regional as well as national production networks in Asia. These local and regional networks are more relational in character and may show considerable resilience against the homogenising forces in the global webs. This does not rule out that manufacturers, traders and bankers increasingly have to adjust to Anglo-Saxon ways of doing business (professional management, lending based on collateral, increased use of written contracts etc.). However we contend that a major change of local and regional networks towards non-relational forms is unlikely.

c) Financial flows and local adjustment

While 'global economic webs' refer to the functional integration of production and services, we use the term global flows to denote the strong growth in international financial movements. Due to their lack of experience with financial regulation of swiftly growing financial markets emerging economies are highly vulnerable to financial instability. Unregulated international financial inflows and outflows may induce financial boom and bust patterns of great damage also to the 'real economy'. Prudent regulation of the national financial system and cross-border capital movements is therefore a main priority. Here the government and regulatory government agencies will be the main agents.

c.1: We contend that prudent financial regulation requires some form of regulation or 'sand in the gear' to contain short-term capital inflows, i.e. some form of formal or informal control on capital inflows. 'Governance reforms' of domestic financial institutions, including strict enforcements of reserve requirements may also be important to prudent financial management, but we propose that this does not suffice without restrictions on inbound short-term capital movements.

c.2: We emphasise the importance of state autonomy with regard to effective financial regulation. In the previous section we argued that institutionalised co-operation between government and business is a main condition for successful government policies in relation to international webs of production and services. In contrast, we contend that a relatively high degree of insulation of regulatory government agencies such as central banks from political interference by business interests and other lobby interest groups is vital for financial stabilisation. Autonomy of regulatory agencies must go along with a strong institutionalised commitment to financial stability and firm support of these policies from the political leadership. A strong commitment to financial stability within the polity becomes all the more important because there is a strong international pressure for financial deregulation from organisations of global governance and powerful First World states. These 'external' parties frequently ally with 'domestic' parties within and outside the state in favour of financial liberalisation, for instance ministries of finance and 'internationalist' business organisations.

c.3: We are sceptical about the 'globalist' argument that reliance on foreign sources of credit translates into convergence of policies and institutions with regard to capital account deregulation, domestic financial liberalisation, corporate governance (shareholder value capitalism) and relations government – business – financial institutions. According to these arguments investor perceptions shaped by 'international' (read American) credit rating agencies promote convergence as financial liberalisation is undertaken in order to attract foreign flows. We do contend that reliance on foreign credit indeed may promote liberalisation of cross-border capital flows and the financial system. However, these liberalisation processes are likely to vary in terms of their timing, form and re-regulation to such an extent that convergence is unlikely. Furthermore we contend that micro-level convergence of corporate governance standards and relations government–business–financial institutions are even less likely.

c.4: The converging impact during financial crises may be stronger than during normal conditions as regulatory authorities then may attempt to ensure capital inflows and demonstrate credibility by 'tying their hands' through foreign investment liberalisation. However, we would maintain that financial crises are unlikely to promote micro level convergence of corporate governance and relations government–business–financial institutions.