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Globalisation, Economic Interdependencies and Economic Crises

Ivo Mossig and Michael Lischka

Since the early 1990s, globalisation has become a major subject of research in the social sciences. However, its impact is contested in academic and public discourses and no clear, uniform or consistent concept of globalisation has been established so far (Jahn 2016). Common views concern the increase of global connections and interdependencies of ecological, social, political and economic systems. The intensification of worldwide social relations links distant places in a way that local events are affected by events occurring far away (Giddens 1991). In this chapter, we conceptualise globalisation as a process of intensification and expansion of multidimensional cross-border relations that are shaped by powerful actors, especially transnational corporations, political actors at the level of nation states and international organisations (Giese et al. 2011).

With regard to the following chapters, we focus on economic globalisation processes and economic interdependencies leading to increasing

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global integration of economic sectors and production systems. The aim of this introduction is presenting the causes and effects of economic globalisation. By analysing long-term data on trade, economic growth and foreign direct investments (FDI), we identify three different waves of economic globalisation separated by far-reaching emergencies such as wars and economic crises. Subsequently, we discuss specific causes and manifestations of economic globalisation and economic crises in each phase and briefly outline their impact on the dynamics of social policy.

1 Three Phases of Economic Globalisation and Economic Crises

According to international trade theories, economic trade has a positive effect on wealth. Due to differences in the technologies used and the structures of demand and supply of production factors, some countries have a relative price advantage in manufacturing certain products. Following the Heckscher–Ohlin model, countries specialise their production according to these price advantages. Through international trade in goods, trading partners can buy the required goods at the lowest possible price and sell their own products transnationally due to their own relative price advantages (Krugman et al. 2018).

International economic interdependencies are not a recent phenomenon, however. Throughout time, closed economies have barely existed. Already in ancient times, spices, fabrics or gold were traded. Nonetheless, economic historians disagree about what point in time an economic globalisation started. Some point to the discovery of America as the crucial turning point, others claim it only started at the beginning of the nineteenth century (O'Rourke and Williamson 2002). At least, there is a consensus that the extent of international interdependence changes over time and that different phases can be identified depending on the intensity of trade relations and respective economic philosophy (e.g. mercantilism, economic liberalism or protectionism), international conflicts, or economic crises (Giese et al. 2011). The available data allow an analysis from 1870 onwards and thus begins immediately before the establishment of the first transfer-oriented social security systems in the 1880s.

An important indicator of economic globalisation is the global trade of goods, notably the ratio of exports and the gross domestic product (GDP) (Dreher 2006). Figure 23.1 shows the non-linear growth of global exports since 1870. Different growth phases can be identified that are separated by significant economic slumps related to the two world wars and the Great Depression from 1929 onwards. More recently, the financial and economic crisis in 2007/2008 or worries about the economic development in China, the United States and Europe in 2015/2016 led to a decline in global exports (cf. Fig. 23.1). The inset in Fig. 23.1 is a magnification of the curve between 1870 and 1948 to show details of global trade in this period.

While trade increased in absolute terms, the comparison with global GDP proves that an increase in trade is associated with an intensification of economic interdependencies. For comparing these two indicators, annual growth rates were calculated (cf. Fig. 23.2). We use five-year moving averages to improve the identification of long-term developments and

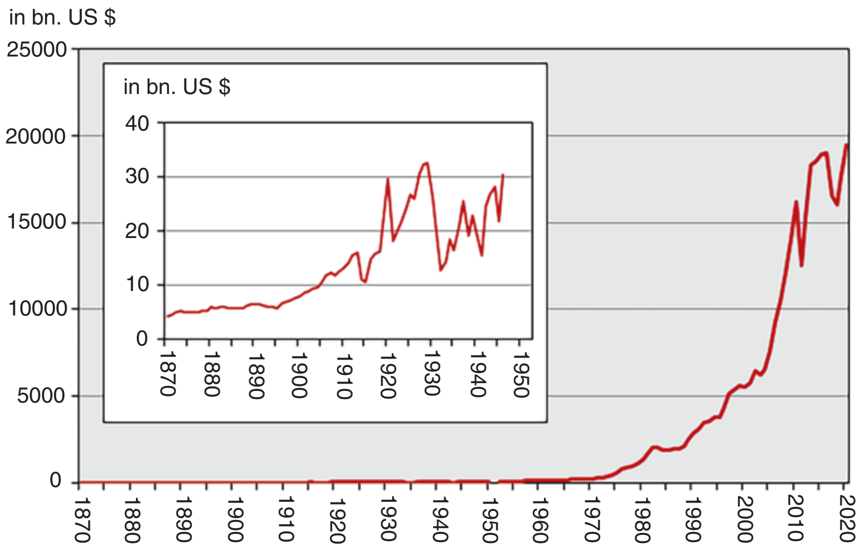

Fig. 23.1 Development of Global Exports 1870–2018. (Sources: Own calculations using data from http://correlatesofwar.org, https://unctadstat.unctad.org (accessed January 21, 2020))

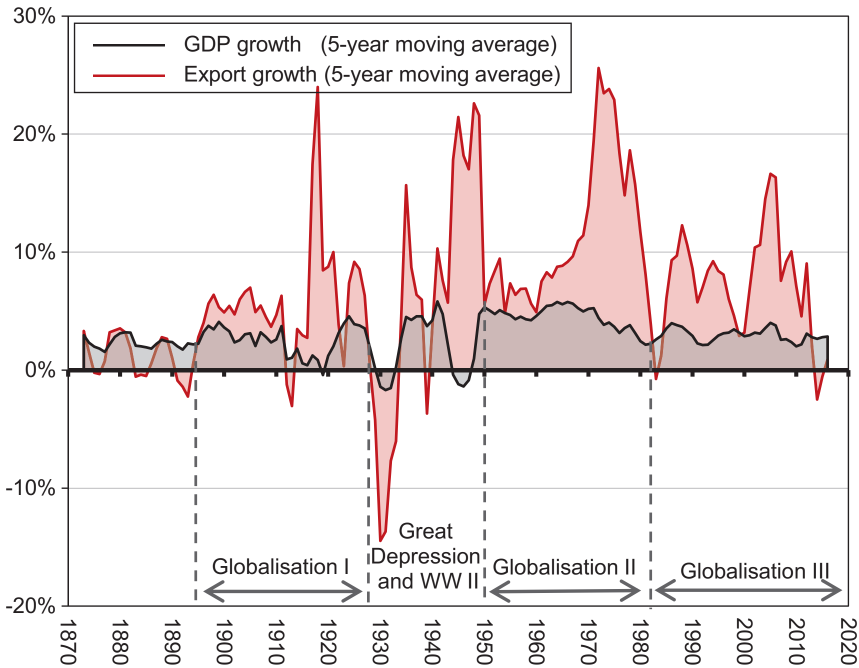

Fig. 23.2 Growth rates of global exports and economic growth measured by GDP 1870–2018 shown as five-year moving averages. (Sources: Own calculations using data from http://correlatesofwar.org, https://unctadstat.unctad.org (accessed January 21, 2020) http://www.ggdc.net/maddison/Maddison.htm, https://data.worldbank.org (accessed March 2, 2020))

to eliminate extreme short-term deviations. A phase of increasing global interdependence is evident when export growth rates exceed the growth rate of global GDP. Different phases of economic globalisation can be identified by intersections of both lines. Negative growth rates of GDP indicate global economic crises, which are often the starting point for interventions in social policy (Obinger 2019).

The average annual growth rate of global exports from 1870 to 2018 is 6.77 percent, while global GDP only increased 2.93 percent on average in this period. Overall, three waves of globalisation and one longer phase of economic crisis can be identified. During all waves, the average growth rate for exports exceeded the growth of GDP (cf. Table 23.1). In the following, we discuss particularities and causes for each phase as well as relevant effects regarding social policy.

Table 23.1 Average growth rates of global GDP and global exports for different time periods

	Entire period 1870–2018	Before globalisation I 1870–1895	Globalisation I 1896–1928	Great Depression 1929–1939	Globalisation II 1950–1980	Globalisation III 1981–2020
GDP, annual growth rate (%)	**2.93**	2.40	2.54	1.74	4.63	2.91
Exports, annual growth rate (%)	**6.77**	1.30	6.41	−0.51	12.63	6.56

Sources: Own calculations; data sources see Fig. 23.2

2 The First Wave of Globalisation from 1895 to the Great Depression

The first phase of globalisation stretches from 1895 to 1928. The Great War was a significant break in the growth rates of GDP and exports, although the high growth rates of the following years compensated for this decrease. According to the Heckscher–Ohlin model, price differences and the associated country-specific specialisations made trade over long distances lucrative, despite the associated transport costs. Decreasing freight rates in the nineteenth century had a favourable effect in this first phase. Through the expansion of railways and inland waterways hinterland connections improved, providing access to remote production sites and sales markets. In North America it was primarily farmers who benefited, while in Europe it was industrial companies. Compared to previous trade relations, price differences no longer remained stable—commodity price convergence rather indicated an increasing integration of the markets. Therefore, the argument of relative price differences causing foreign trade lost its validity. Instead, producers now faced the challenge to achieve productivity improvements, especially through technological innovations, in order to maintain competitiveness in global markets (O’Rourke and Williamson 2002; Torp 2005). The concomitant economic and social transformations in the course of rapid industrialisation created social needs that explain why states adopted social policies during this phase. Large differences between states regarding the timing and form of introduction still demand in-depth explanations (Obinger and Petersen 2019).

3 The Great Depression and World War II

The period between the Great Depression and World War II was a significant break. Caused by the New York stock market crash in October 1929, the global economy collapsed. In 1932, global exports were at a mere 40 percent of their 1929 level, while global GDP shrank more than 4 percent per annum. Industries in many countries demanded protectionist measures to support domestic producers. Adhering to the belief that exports create jobs while imports destroy them, governments subsidised exports and imposed high import restrictions. This economic policy—known as "beggar-thy-neighbour"—tried to shift the burden of the economic crisis onto other countries, triggering a cycle of competitive market foreclosure (Weintraub 2007). A change in economic policy only came with the Roosevelt administration which supported a stronger liberalisation of global trade and signed numerous bilateral trade agreements (Giese et al. 2011). Although the global growth rates of GDP and exports stabilised in the second half of the 1930s, they were still far below the long-term average over the period from 1929 to 1939 (cf. Table 23.1).

The industrial crash caused by the Great Depression led to mass unemployment and catastrophic living conditions. In some countries such as Sweden, New Zealand and the United States this situation prompted welfare state expansion. This is exemplified by the U.S. Social Security Act which was enacted in 1935 as part of the New Deal. By contrast, the right-wing autocracies in Europe responded with austerity and welfare state retrenchment. This bifurcated development in social policy demonstrates that governments might respond very differently to similar economic problems (Obinger and Petersen 2019).

4 The Second Wave of Globalisation after World War II Until 1980

Already during World War II, the United States and its Western allies developed plans for a new economic order. The 1944 Bretton Woods conference, in which forty-four states participated, was a landmark event. Key decisions were the establishment of the International Monetary Fund (IMF) and the World Bank (Tetzlaff 1996) as well as the system of fixed exchange rates linked to the US dollar. The dollar was tied to government gold balances to prevent states from devaluing their currencies in crises (e.g. the Great Depression) in order to gain advantages in foreign trade. In 1971, the United States revoked its guarantee to exchange US dollars for gold, leading to the collapse of the Bretton Woods system. In 1973, the exchange rates for the most important currencies were liberalised. On the other hand, the General Agreement on Tariffs and Trade (GATT), which came into force in 1948 and was replaced by the World Trade Organization (WTO) in 1995, boosted the rapid growth of global trade. In eight rounds of negotiations, trade tariffs were reduced from an average of 40 percent in 1947 to below 5 percent in 1994 (Giese et al. 2011).

The liberalisation of markets for goods and services led to a massive increase in global trade (cf. Fig. 23.1). In particular, from the 1960s onwards, the annual growth rates of exports were significantly higher than the global growth rates of GDP (cf. Fig. 23.2). Overall, from 1950 to 1980 exports grew by an average of 12.63 percent per year, while GDP grew "only" by 4.63 percent per year (cf. Table 23.1). However, not all parts of the world were equally embedded in international trade. Rather, there was a communist bloc under Soviet leadership, united in the Council for Mutual Economic Assistance (Comecon), and the group of the capitalist-oriented Western nations. The latter, also known as the Triad, consisted of North America, Western Europe and the Asia-Pacific economic area, often dominated by Japan (Dicken 2007). However, during the second wave of globalisation, large parts of the world population did not live in either of these two blocs but in countries of the Global South which were far less integrated into global trade activities. A genuinely worldwide economic integration, as the term globalisation suggests, did not take place during this phase.

The second globalisation wave coincided with the so-called Golden Age of the Western welfare state. Immediately after World War II, there was an immense need for social protection to counter the enormous consequences of the war. Many Western countries increased social benefits and extended social protection to larger segments of the population which, along with demographic ageing, caused a disproportionately high increase in social spending vis-à-vis economic growth. Cameron (1978) demonstrated for eighteen Western countries that differences in the expansion of the public economy can be attributed to the varying degrees of integration in global trade between 1960 and 1975. Since small open economies are vulnerable to fluctuations in world markets, they expand the public (welfare) sector to mitigate the risks associated with their high trade dependency. The disproportionate expansion of the welfare state in smaller countries such as Belgium, the Netherlands or the Scandinavian countries can therefore be explained by their economic openness. This argument lies at the heart of the "compensation hypothesis" (Rieger and Leibfried 2003; Starke and Tosun 2019).

However, economic interdependencies also shaped social policies in non-Organisation for Economic Co-operation and Development (OECD) countries. From the 1940s onwards, many Latin American states for example pursued a strategy of import-substituting industrialisation. Social policies were designed for the industrial workforce, specifically in the areas of education and health. The agricultural sector received little attention or was not included at all. This gave rise to increasing inequalities. Financial problems, cyclical downswings and inflationary policies favouring exports contributed to a lack of investment in social infrastructure and to the decline of the population's living standards. Consequently, such strategies came to a halt in the 1980s (Cortés 2009).

5 The Third Wave of Globalisation Since the 1980s

The third wave of globalisation from the 1980s onward is defined by an increasing international division of labour and the massive restructuring of production processes and organisational structures of transnational enterprises (Dicken 2007). In the second wave of globalisation, economic growth was based in particular on productivity increases through Taylorist mass production. In order to realise economies of scale, as many production steps as possible were concentrated at a central production site, from which the finished products were exported to global sales markets. This production method, also known as Fordism, fell into crisis in the 1970s. It started with the oil crises, but these external shocks cannot explain the far-reaching changes. On the contrary, it became clear that the possibilities for increasing productivity through economies of scale had reached their limits. Furthermore, consumer habits changed so that standardised mass products less and less met the demand and more flexible production systems had to be established (Bathelt 1994). Searching for new ways to reduce costs, the largely integrated production process was split up in order to relocate parts of the production to cheaper locations. Differences in labour costs played a central role in this process. In contrast to the second wave, economic integration was less driven by trade than by the establishment of global production networks of transnational companies (Henderson et al. 2002) and the accompanying integration of financial markets. The rapid growth of foreign direct investments as a driving force of the third wave of globalisation illustrates this point. FDI stocks and flows are a suitable indicator of the progressive expansion of the international division of labour and the relocation of formerly domestic jobs to foreign production sites (Giese et al. 2011).

Figure 23.3 shows the development of outward FDI flows compared to global exports and GDP. The values were indexed in relation to the base year 1970 (index 1970 = 100). Obviously, the FDI volume has grown faster than global exports and GDP since the mid-1980s and has significantly and massively increased since the early 2000s (cf. Fig. 23.3).

Technological improvements enabled the establishment of global production networks. The development of programmable computer-integrated machines replaced the rigid principles of Fordist mass production with flexible forms of production. New time-space-shrinking technologies were essential prerequisites for effectively organising production processes across production sites. They allowed the transfer of larger amounts of information at ever-lower prices and over ever-shorter time (now in real time). New transport technologies facilitated savings in terms of costs and time. And increasing digitalisation allowed for new

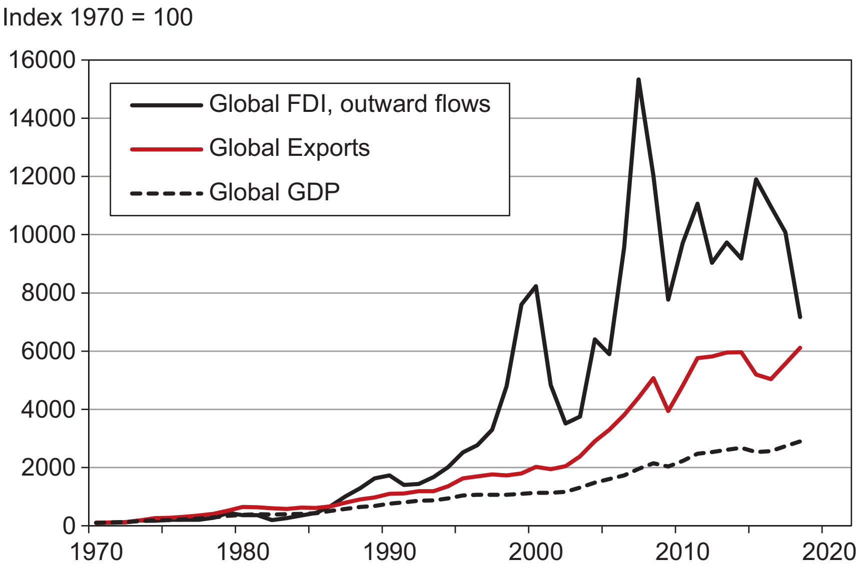

Fig. 23.3 Development of Foreign Direct Investments (FDI, outward flows), Exports and GDP 1970–2018. (Source: Own calculation using data from https://unctadstat.unctad.org (accessed March 10, 2020) https://data.worldbank.org (accessed March 10, 2020))

logistical concepts with the precise tracking of cargos and their coordination with production processes (Dicken 2007; Giese et al. 2011).

However, the third wave of globalisation is also characterised by other landmark events. First, the collapse of the Soviet Union and the "Eastern Bloc" and the subsequent integration of these states into the capitalistic global economy occurred. Second, there was the rise of China as a new economic power. And third was the recurrence of severe economic crises—such as the financial and economic crisis of 2007/2008 or the bursting of the dot-com bubble in March 2000—quickly leading to global disruptions due to increasing economic interdependence. It is apparent that the COVID-19 pandemic will massively reshape economic interdependencies. Already at the beginning of the crisis, a noticeable transformation or even a significant reduction of previous globalisation structures has become visible, with consequences for prosperity and welfare that are inestimable as yet.

As a result of these upheavals, the impact of globalisation on social legislation has been discussed more intensively but also more controversially. While the compensation thesis argued that a high degree of integration into the global economy leads to an expansion of the welfare state, the efficiency thesis—its antipode—postulates that increasing world market integration goes hand in hand with a dismantling of the welfare state. According to an "economic logic of globalization" (Swank 2010), economic openness pushes states into a global competition for the lowest wages, lowest production costs, as well as lowest tax rates and regulations. In this view, for succeeding in this competition, welfare state retrenchment by lowering social standards and social contributions seems inevitable in Western democracies. On the other hand, the gains in prosperity that are currently being achieved in the catching up countries offer the opportunity to expand social policy.

6 Conclusion and Outlook on the Chapters of This Section

Using long time data on the development of global economic growth, trade and foreign direct investments, we distinguished different phases of economic globalisation and identified episodes of deep economic crises. Besides the Great Depression as a long-lasting global economic crisis, three waves of globalisation can be identified, which markedly differ in terms of causes and manifestations alongside different phases of social policy development.

The term globalisation suggests an economic integration covering the whole world. Yet, for many countries of the Global South this has not happened (yet). The centres of power and control, represented by the headquarters of large transnational corporations or by the centres of the global financial sector, are still located in the Global North (Giese et al. 2011). Nevertheless, studies on Global Production Networks (GPN) show how the Global South is integrated into the chains of global value creation, thereby reproducing global inequalities and rendering it difficult to alter these conditions. When analysing global social policy, the GPN approach seems promising, since it takes nation states and transnational enterprises into account, but also other relevant actors like consumers, workforces or NGOs that actively shape the economic globalisation process and social policies in the countries of the Global South (Mossig and Düpont 2020).

The different phases and waves of economic globalisation represent the background for the following eight chapters examining key aspects of the effects of economic interdependence and economic crises on the introduction and design of social policies.

In Chap. 24, Nils Düpont, Ivo Mossig und Michael Lischka focus on the third wave of globalisation. It is less shaped by trade relations, but rather by the establishment of global production networks and capital market integration. Inspecting the ratio of inward to outward FDI stocks, they show that FDIs do not have a uniform impact on welfare efforts. Instead, it makes a difference whether a country is a net recipient or sender. Rather lending support for the "compensation hypothesis", their short history also shows that we may witness a renaissance of functional and institutional explanations with a time-shifted evolution of less developed countries and their road to welfare—fuelled by inward FDIs.

Herbert Obinger and Carina Schmitt (Chap. 25) tell the story of the introduction and spread of unemployment compensation schemes across the globe until 1950. In the first half of the twentieth century, the adoption of unemployment compensation was limited to less than thirty economically developed countries. Even today only ca. 50 percent of countries in the world have adopted this programme. Still, their short history is a story of warfare and economic crisis as driving forces creating tremendous social needs but also opening a (short) window of opportunity for the introduction and reform of unemployment insurance.

Examining the period of the Great Depression (1929–1939), Heiner Fechner shows in Chap. 26 that the global economic crisis represented a turning point for labour regulations in the colonies of European imperial powers in sub-Saharan Africa preparing the ground for major reforms in colonial labour legislation after World War II. Tracing the main features of labour-related legislation, he draws a nuanced picture of how the Great Depression marked the end of the era of post-slavery labour "market-making", characterised by a move away from forced labour, first steps towards protection of employees as well as a more generalised move towards collective labour relations and worker protection.

Similarly exploring the period of the Great Depression, Simon Gerard-Iglesias' short story on Argentina illustrates how trade interdependence affects social legislation (Chap. 27). Labour regulation was perceived as a disadvantage in international competition. Before the Great Depression, Argentina's economy had rendered much of its wealth from the export of agricultural products. The fear of economic backlash from other countries ultimately led to the inclusion of agricultural work as one of the last sectors into social protection schemes in Argentina.

Cornelius Torp (Chap. 28) focuses on pension policy in Britain and Germany after World War II. He demonstrates how mutual influences shaped British and German pension policy ever since. The modus operandi, however, constantly changed during the period under study. Until the 1970s, pension policies were characterised by bilateral knowledge transfers. Immediately after World War II, German politicians saw the British welfare state as a role model, while a few years later the Labour Party's pension plan was influenced by the German income-based pension system. In recent decades, transnational interdependencies gained importance as a factor of influence, increasingly replacing the bilateral character. Multilateral and supranational discourses as well as transfer patterns have gained ground, not least due to the influence of international organisations such as the World Bank and the EU.

Johanna Kuhlmann and Frank Nullmeyer (Chap. 29) explore the connection between expansive social policies in the field of old-age provision and the economic strategies of South Korea and Malaysia. In the two countries, contribution-based pension systems—a social insurance scheme in South Korea, and a provident fund in Malaysia—were established and expanded over the years with large sums of money being accumulated in the systems for paying out pensions. However, in both countries these capital stocks have been used not only for social policy but also for economic purposes, such as investments in large companies or infrastructure. The pension systems are thus part of both countries' export-oriented economies, and the expansion of social policy is supported by their governments for economic reasons.

Focusing on the socio-economic effects of crises, Magnus Brosig and Karl Hinrichs take the EU as an example in Chap. 30 to show the extent to which the global economic crisis of 2007/2008 affected national and supranational budgets and subsequently triggered reforms of the pension systems in the three most severely affected EU countries. Their story shows that the consequences of the crisis and the reforms depend on the design of the national pension system. Overall, the pension reforms implemented in the years since 2008 have often made the systems financially more sustainable, but jeopardised their adequacy and social sustainability in terms of legitimacy and acceptance. While recent reforms in a number of countries have led to short-term improvements, they were directly aimed at current or soon-to-be pensioners rather than at ensuring pension benefits that reliably prevent poverty and maintain decent living standards for younger cohorts at and during retirement.

Finally, Martín Cortina Escudero's short history (Chap. 31) tells a story about the interdependence of immigration and trade in Argentina for two phases of economic development, 1880–1929 and the period after 1929. During the first phase, integration into the world market led to an orientation toward an export-oriented economy specialised in agricultural products, accompanied by immigration of European workers. At that time, social policies focused on early retirement funds for powerful professional groups within the agricultural export economy. After the Great Depression of the 1930s, Argentina undertook a rapid process of industrialisation causing internal rural–urban migration and the formation of a working class. Global trade and integration into the international division of labour impeded a comprehensive social security system. Still, bilateral trade and protectionist measures encouraged industrialisation which in turn strengthened the working class and led to the construction of Argentina's modern welfare state.

As diverse as their approaches and foci are, all authors nonetheless tell a story of how social policy development and dynamics are linked and interwoven with (phases of) economic globalisation and crises.

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