Global Public Policy

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GOING GLOBAL

GIVEN THE widespread use of the term globalization, it is surprising how little we know about it. In most cases, it is asserted but never defined. Those who do describe it characterize it as a continuous increase or cross-border financial and economic activities leading to greater economic interdependence. Essentially, interdependence and globalization are used interchangeably. This creates a paradox: the same term that is understood as a mere quantitative rise in a trend going back to the 1960s is also used to refer to a fundamental qualitative change in the international system, predicting perhaps the end of the nation-state. If the former is true, there is little need for governments to reassess their role, or that of the institutions and principles that have governed the world economy since the end of World War 11, in view of globalization. If the latter holds, it becomes necessary to draw a distinction between economic interdependence and globalization, a distinction that provides a basis for reassessing the role of government and governance in an emerging global economy.

Unlike interdependence, which narrowed the distance between sovereign states and caused closer macroeconomic cooperation, globalization is a microeconomic phenomenon. Globalization represents the integration of a cross-national dimension into the very nature of the organizational structure and strategic behavior of individual companies. The cross-border movement of intangible capital, such as finance, technology, and information, allows companies to enhance their competitiveness.

While in the 1960s and 1970s foreign direct investment closely correlated with world output and trade, it expanded at an average of 16 percent annually between 1985 and 1995, compared with 2 percent and *7* percent, respectively, for output and trade. Most of this additional investment was concentrated in the countries of the Organization for Economic Cooperation and Development and a few developing countries and consisted of mergers and acquisitions in research and development-intensive industries. Controlling for the opening of both China and the former Soviet bloc, which attracted almost no investment before 1985, the share of foreign direct investment going to the developing world actually dropped. The pattern of corporate alliances and collaborative agreements confirms this picture. Such alliances have multiplied during the last decade, and close to go percent have occurred in OECD countries.

These changes have had qualitative implications for international trade, which increasingly is structured and restructured by foreign direct investment and international alliances. Today about 70 percent of world trade is intra-industry or intra-firm. Both are closely tied to global corporate strategies, and neither has much to do with the textbook case of comparative advantage. The mid-1980s advent of securitization transformed the financial world, facilitating global corporate strategies, giving foreign debtors and creditors access to domestic financial markets, and contributing to the skyrocketing growth of cross-border capital flows during the last decade. In particular, the market for derivative instruments has led to greater growth and volatility of international capital flows. In 1995 the combined annual value of global trade and foreign direct investment amounted to only six days of turnover on the global foreign exchange markets.

These data show that much of the past decade's international economic activity reflects the internal but cross-border restructuring of corporate activities. In many cases, corporations absorb foreign capital stock, enveloping economic activities that were once conducted on the open market. Alliances such as long-term supplier agreements and licensing and franchising contracts are also not fully exposed to market forces. Globalization is resulting in the emergence of a single integrated economy shaped by corporate networks and their financial relationships. Reliable data for intra-firm trade exist only for the

United States, but in 1944 this off-market trade accounted for approximately 40 percent of total U.S. trade. Governments continue to register these internal transfers not because they are traded but because they cross borders. Although the practice is widespread, equating globalization with the emergence of a global market economy can be misleading.

Interdependence was an important precursor of globalization. It led to the creation of international regimes like the General Agreement on Tariffs and Trade and the International Monetary Fund and it was an important causal factor in encouraging globalization. Like technological innovation, the deregulation and liberalization of cross-border economic activity fostered an environment that not only permitted but compelled companies to adopt global strategies. The public policy response by governments to increased interdependence cannot also be its consequence. Before considering policy responses to globalization, it is necessary to examine the challenges globalization presents to governments and how they differ from those of interdependence.

THREATENING DEMOCRACY

GLOBALIZATION CHALLENGES sovereignty, but so did interdependence. Neither interdependence nor globalization can challenge the legal sovereignty of a state - only other states can. If anything, these forces challenge the operational sovereignty of a government, that is, its ability to exercise sovereignty in the daily affairs of politics. Sovereignty has two dimensions, internal and external. The internal dimension is the relationship between the state and civil society. Following Max Weber, a government is internally sovereign if it enjoys a monopoly of the legitimate power over a range of social activities, including economic ones, within a given territory. That power is embodied in the domestic legal, administrative, and political structures that guide public policies. With respect to the economy, internal sovereignty takes effect when governments collect taxes or regulate private sector activities.

The external dimension of sovereignty refers to relationships among states in the international system. These relationships are defined by the absence of a central authority. As Thomas Hobbes put it, anarchy is the rule of the international system. External economic sovereignty comes into play when, for example, countries collect tariffs and alter their exchange rates. Economic interdependence challenges this dimension of state sovereignty. Governments have responded by following the principles of liberal economic internationalism, endorsing the gradual reduction of their external economic sovereignty by lowering tariffs and capital controls.

Global corporate networks challenge a state's internal sovereignty by altering the relationship between the private and public sectors. By inducing corporations to fuse national markets, globalization creates an economic geography that subsumes multiple political geographies. A government no longer has a monopoly of the legitimate power over the territory within which corporations operate, as the rising incidence of regulatory and tax arbitrage attests. By no means does this imply private sector actors are always deliberately undermining internal sovereignty. Rather, they follow a different organizational logic than states, whose legitimacy derives from their ability to maintain boundaries. Markets, however, do not depend on the presence of boundaries. While globalization integrates markets, it fragments politics.

The threat to a government's ability to exercise internal sovereignty implies a threat to democracy. Although individuals may exercise their right to vote, the power of that vote in shaping public policy decreases along with a state's internal sovereignty. Persistent weakness in internal sovereignty will cast doubt on democratic institutions. It is an important factor in the declining trust in democratic institutions of governance and one to which governments must respond.

PUBLIC POLICY WITH BORDERS

POLICYMAKERS ARE likely to respond to challenges to internal sovereignty in two ways, variants on what is essentially an interventionist strategy. Defensive intervention relies on economic measures such as tariffs, non-tariff barriers, and capital controls, forcing companies to reorganize along national lines. If economic nationalism fails to arouse broad popular support, its political counterpart - territorial secession and partition - may do so. Alternatively, policymakers can intervene offensively with subsidies or competitive deregulation. Under these circumstances, states themselves become global competitors, seeking to entice corporations to set up shop within their territory. Among

OECD countries, subsidies grew 27 percent from 1989 to 1993 and competitive deregulation has become common among financial centers and, more recently, among national tax jurisdictions. The use of offensive intervention has increased as policymakers attempt to broaden the reach of internal sovereignty to match the economic reach of corporate networks. Two recent examples are the HelmsBurton Act and California's attempt to impose its unitary tax code on companies like Barclays and Colgate-Palmolive.

None of these responses bodes well for international relations. Protectionism by one country, irrespective of its intentions, leads to retaliation and jeopardizes the world economy. Subsidizing an industry to gain competitive advantage will not advance integration, but rather divert scarce public funds from important public policy goals. Competitive deregulation may not lead to disintegration, but it defeats the original purpose of the policy; a fully deregulated market further reduces a government's internal sovereignty. Extraterritoriality is no friend of deeper integration either. Other states will retaliate against a dictate. Finally, redefining political geography through partition only gives the appearance of greater control of policy. Partitioning a country focuses exclusively on the external dimension of sovereignty. In no way does it insulate governments from the challenges of globalization. If anything, it makes them more vulnerable.

All these responses emphasize territoriality as an ordering principle of international relations, a condition that integration has tried to overcome and that the end of the Cold War appeared to have secured. All are at odds with globalization and will succeed on1y if the achievements of interdependence are reversed. The popularity of these policies has increased considerably since the early 1960s. In many countries, political opportunists have taken advantage of the public's fear concerning the declining effectiveness of internal sovereignty. Unless policymakers find a better alternative, governments may be forced into these counterproductive measures to halt the loss of internal sovereignty and the further erosion of confidence in democratic institutions.

NEW PARTNERS

ANY ALTERNATIVE strategy must avoid the pitfalls of territoriality. Forming a global government is one response, but it is unrealistic. It would require states to abdicate their sovereignty not only in daily affairs but in a formal sense as well. A more promising strategy differentiates governance and government. Governance, a social function crucial for the operation of any market economy, does not have to be equated with government. Accordingly, global public policy uncouples governance from the nation-state and government.

To implement such a strategy, policymakers would delegate tasks to other actors and institutions that are in a better position to implement global public policies-not only to public sector agencies like the World Bank and the IMF, but also business, labor, and non-governmental organizations. These groups not only have a stake in the outcome and better information, but have a boundless range of activity. Such public-private partnerships would increase the legitimacy of global public policy and produce a more efficient and effective policy process. Whether grappling with global financial regulation, environmental protection, transnational law enforcement, the control of dual-use technology, or other issues, public-private partnerships could provide the foundation for global public policy.

Critics of such an approach will correctly question the wisdom of placing private and public interests under the direction of the same institution, charging that the public's interest is likely to be neglected. The limited experience with mixing public and private regulation at the national level supports these skeptics. But rather than abandoning global public policy, the current shortcomings of mixed regulation should be addressed. First, greater transparency is necessary. Strict principles of disclosure and guaranteed access for interested parties would raise public confidence. Second, corporations must facilitate public-private partnerships by improving their own internal control and management structures. Independent audits and incentives that discourage excessive risk are examples. The better these controls, the lower the risk of market failure and the need for outside regulation. Those with doubts about public-private partnerships and global public policy should consider the danger of the alternatives.

KEEPING UP WITH THE TIMES

GIVEN THE still limited reach of globalization, international relations remains characterized by the coexistence of interdependence and globalization, cutting across countries and industries. Globalization dominates relationships between advanced industrial countries. The increasing focus on non-tariff barriers ranging from financial regulation to health, environmental, and safety standards is a telling example. Interdependence remains the rule for industrializing countries. External sovereignty and territorial interests remain important factors in determining their foreign policy. In North-South relations, the coexistence of interdependence and globalization is reflected in the changing mandate of international organizations such as the World Trade Organization, which no longer focuses exclusively on free trade but has been pressed by the industrialized countries to pursue free trade with an eye to environmental protection and minimum labor standards. The dynamics of interdependence and globalization also coexist in individual economic sectors, such as financial services. At the same time that industrialized countries, through the IMF, the WTO, and the OECD, are encouraging developing nations to deregulate and liberalize their financial markets, they are attempting to establish global public policies that can respond to the consequences of the deregulation and liberalization of their own financial services industries.

The coexistence of interdependence and globalization is not yet reflected in the world's approach to a growing number of transnational policy issues. At a minimum, the institutions of interdependence, such as the IMF, and of globalization, such as the Joint Forum, which brings together regulators from the banking, securities, and insurance industries, should cooperate much more closely. In many cases, policy efforts to promote interdependence and global public policy may best be located under one roof. A united effort would help avoid bureaucratic overlap and turf fights between international institutions and permit a more integrated approach to developing economies' dual challenge of national liberalization and global public policy.

As for the security ramifications of the now largely interdependent and rapidly globalizing world, it will no longer suffice for the architects of international security to view international relations along traditional lines. The coexistence of interdependence and globalization places new demands on international security. Combining external and internal sovereignty in a constructive way will be a significant challenge. Whereas external sovereignty depends on the ability to exclude, internal sovereignty depends on the ability to include.

The shifting demands on international security will also transform the domestic politics of security policy. The challenges emanating from globalization do not usually threaten a country's overall security or territorial integrity. The threats are diffuse and seldom directed at an entire country, often challenging specific groups and in some cases individuals. These threats come from global networks of non-state actors in domains as diverse as communication, finance, technology, and transport. Anticipating and measuring them will be difficult, as will mustering support for collective national responses to them. Policy coalitions to counter these new threats will transcend national boundaries, calling into question the very concept of national security.

As globalization reaches more countries, international institutions charged with security management will have to expand their ability to handle issues of internal sovereignty. The debate over the future of NATO is a case in point. Opponents of NATO enlargement focus on external sovereignty, emphasizing the policy's territorial consequences. Proponents stress internal sovereignty, recasting the alliance's mission as the promotion of democracy and civil society. Given the political bias in favor of enlargement, whether or not NATO should be enlarged may be the wrong question. The real question is whether NATO members are prepared to choose the right mix of external and internal sovereignty, one that reflects the changing composition of European and global security demands and engages Russia.

The need for inclusiveness extends beyond NATO enlargement. The data on foreign direct investment and corporate alliances demonstrate that large parts of the world economy remain excluded from globalization. With internal sovereignty becoming an issue of international relations, this suggests a strategic vision that places the international financial institutions, such as the IMF and the World Bank, and regional development organizations at the center of future international security. The World Bank has already begun to shift its attention to aspects of internal sovereignty, including good governance, poverty reduction, and conflict prevention, and it should continue in that direction. The IMF has begun to focus on such matters as global financial system regulation, money laundering, tax collection, and corruption. By drawing attention to the economic consequences of excessive military spending, both institutions have questioned a country's requirements for the preservation of external sovereignty when basic elements of internal sovereignty can no longer be financed. Five decades ago these institutions were given the mandate to manage growing interdependence. Their future lies in the management of globalization and global public policy. Without adjustments, the institutions will not be in a position to pursue this new mandate, let alone rationalize their continued existence.

For now it should be clear that globalization's success depends on North-South transfers of capital, tangible and intangible alike. In 1990, 44 percent of all long-term financial flows to developing countries came from private sources, the remainder being public financial flows. By 1996, the share of private financial flows had increased to 86 percent. The bulk of North-South transfers will continue to come from the private sector. But if global public policy is to succeed, it requires public funds. Without this assistance, developing countries will not be able to participate too. Renewed calls for development assistance may seem vain, given the difficulty rationalizing foreign aid after the Cold War. But resource transfers to promote global public policy are neither foreign nor aid, but an investment that provides returns to all.

TOWARD A GLOBAL PUBLIC POLICY

INTERNATIONAL RELATIONS is at a crossroads. The interventionist strategies outlined above should not be dismissed as politically ill-fitting. Such strategies are increasingly popular, as seen in the last French election, the Iran-Libya Sanctions Act, and Quebec's attempt at secession. Consequently, external sovereignty will once again come to dominate relations between states, ultimately increasing the risk of territorial conflict.

The alternative scenario, global public policy, does not contest internal sovereignty as an organizing principle, but it does contest its territoriality. It demands political leadership and institutional change, both of which are in short supply. It also requires the willingness of private and non-governmental actors, especially in the global corporate community, to cooperate closely and share responsibility in implementing public policy while ensuring democratic principles.

The world economy consists of a growing number of global corporate networks. The current state of global governance, however, resembles at best a cross-national policy patchwork, conspicuous for its missing links and unnecessary overlaps. If global public policy is to be an alternative to interventionism, governments must ensure that these patchworks evolve into networks of governance. Their first step should be to commission a global governance audit that would map global obligations and responsibilities along different dimensions, including functional, financial, institutional, and structural. The New York-based Center on International Cooperation has recently initiated an effort along those lines.

The next step would be to fill the most important gaps identified in each policy area. National bureaucracies, not just the top leadership, need to establish permanent channels of communication on cross-border economic activity. The recent failures of financial regulation evidenced in the case of Barings and Daiwa Banks confirm the need for such networking, but it must go far beyond the domain of global financial markets. Policymakers should meet periodically to share experiences and techniques. Greater cooperation between international institutions would prevent unnecessary duplication of activities and an agreed-on division of labor on global governance could contain turf fights that have erupted in recent years. The December 1996 agreement on collaboration between the IMF and WTO is a welcome start. But as the World Bank's experience in the former Yugoslavia has shown, the exchange information and coordination of activities must extend to humanitarian and security organizations, such as NATO and the Organization for Security and Cooperation in Europe, which are also confronted with the challenges of eroding internal sovereignty.

Finally, while multi-government networks are a precondition for global public policy, they are by no means the only one. Unless governments and international organizations create and use cross-national structures of public interest, global public policy cannot emerge. In policy areas such as environmental protection, humanitarian assistance, and financial regulation, support for such structures has grown. But too often this support came as a hasty reaction to a crisis and not as part of a well-executed strategy. Cross-national social networks will signal the foundation of a global civil society and be vital to the legitimacy and accountability of global public policy.

Probing further into the future, including the future of the nation-state itself, one must recognize that globalization has ended the nation-state's monopoly over internal sovereignty, which was formerly guaranteed by territory. Outsourcing anarchy to the international system, as Hobbes did, will no longer guarantee internal sovereignty at home. This change deprives external sovereignty of its functional value.

The nation-state as an externally sovereign actor in the international system will become a thing of the past. But this will only happen if internal sovereignty is realized through global public policy. This requires political elites to dissociate themselves to some degree from territory and create more dynamic and responsive institutions of governance. Anarchy is no longer just the outcome of, but also the cause for state interests in the international system. Whether and how long this evolving hybrid is called a nation-state should be of little concern. The administration of sovereignty has changed many times over the centuries; the nation-state is a relatively recent form of governance and it has no claim to perpetuity. While the territorial state may eventually become redundant, the principles and values that govern democracies should not. Steps should be taken now to support the notion of global public policy so that society will be better equipped to respond to the demands of globalization.

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