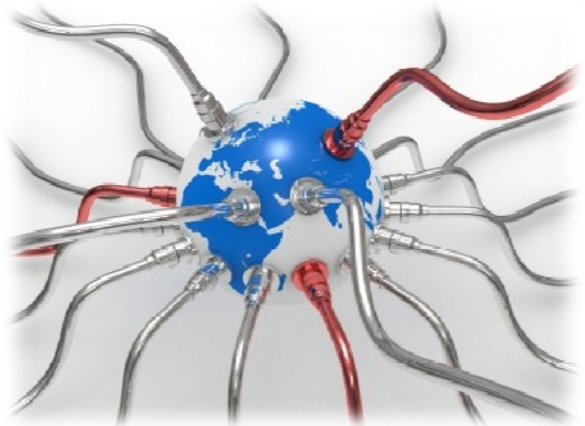


Economics from the Ground Up

A brief history of globalisation'

Early history of economic integration: the Silk Road

Economic interaction between distant groups of people, including trade, has always been a feature of human history. For example, many of the foods and materials we take for granted as part of our lives were once highly exotic, originally moved around the world as a result of trade. People's desire to acquire natural resources that were not indigenous to their region was often the motivation for developing networks for trade. One of the oldest and longest trading routes in history was the Silk Road, which stretched between the Roman Empire in the west and China in the east, and operated from the first millennium B.C. through to the middle of the second millennium C.E. It promoted a sharing of not only commodities, but also ideas, art and culture. This was a fascinating period of human history, and many things we now take for granted were introduced to western culture as the result of that period including silk, paper and gunpowder from China. There is evidence that prior to any European contact, indigenous Australians in northern Australia traded with peoples from nearby regions to the north.



Colonialism and mercantilism (1500s to late 19th century)

The colonisation of large parts of the world by the European great powers, namely Spain, England, Holland, Portugal, Germany and France, led to the development of a **mercantilist** model of economic integration. The rise of “mercantilism” saw European imperial, colonial nations like Britain, France, Germany, Spain and the Netherlands colonise areas of the globe – Africa, Asia, Oceania, North and South America. They extracted natural resources from those places, including wool, sugar, spices, tea, cotton and rubber, and then returned the commodities to the colonial power. The important thing was that these resources were not available in the colonial powers since commodities like sugar, cotton and tea could not be grown in Europe. In the European country, the commodities were converted into more sophisticated manufactures, using the labour and machinery of the thriving industrial economies in the European countries, and these were then consumed in the European nations and also exported back to the colonies, at much higher prices. This process was called “value-adding” and we see it at work in many countries still today, where cheap raw materials are imported and converted into more valuable, value-added manufactures such as clothing, footwear, steel or whitegoods. For example, during the mercantile period, the United Kingdom imported raw materials such as cotton from India at very low cost. They then processed this in factories, and exported the finished textiles back to India and other locations at much higher prices, generating enormous profits.

It is important to note that in some instances, this process was also supported by slave labour, as in the sugar plantations of the Caribbean, and the tobacco plantations of the Americas. The Europeans tried to

limit the colonized nations from creating industry for value-adding themselves, since this would create competition and bring down prices. Just like in the present period of globalisation, the development of technology, namely the steam engine in the mid-1700s, and subsequently the introduction of the steamship, allowed for faster transport, more efficient mechanised industry and increased trade around the globe.

Enormous economic benefits were gained for the colonial powers, but not for the colonised nations. If you know your history, you will be aware that the establishment of Australia as a European colony was part of this process. In 1901, Australia exported around 27% of its output, and almost 60% of that was to the United Kingdom. These days, Australia's exports make up only around 20% of GDP on average, and the UK only receives 5% of our exports.

Once again, many items we now take for granted were first introduced to European society during this period, including tomatoes, potatoes, and tobacco from the Americas, cotton, rubber, tea, sugar and spices from Asia.

Booming trade (1870-1913)

Between 1870 and 1913 (just before the outbreak of World War 1), the increase in world trade as a share of world GDP was greater than at any time since then. World merchandise exports rose from about 5% to 12% of world domestic product. The mobility of commodities, capital and labour reached record levels with telegraphs and sea transport never being busier. As economic historian Niall Ferguson noted, people spoke euphorically of distance having been annihilated.

The closing down of globalisation: between the wars (1914-1944)

The outbreak of the World War I brought about a halt to the economic globalisation that had preceded it. The war itself disrupted trade, including sea transport. Then the advent of the Great Depression in 1929 contracted trade even further. For most large countries, foreign trade fell by between 50% and 70% during that time. Many countries reacted to the economic insecurity of the time by shoring up their tariff barriers and becoming more protectionist, thinking that might protect their own economies by encouraging local production rather than importing cheap imports from overseas countries with low inflation. For example, after 1931, the average rate of duties on imports to the USA jumped to 50%. Some economists have argued that the sharp decline in trade helped prolong the Great Depression, especially for countries that were highly dependent on foreign trade.



After the wars: re-opening the world economy (1944-1970s)

"The economic health of every country is a proper matter of concern to all its neighbors, near and far."
U.S. President Franklin D. Roosevelt, at the opening of Bretton Woods

Towards the end of the World War II, hundreds of representatives from the Allied nations met at a hotel in New Hampshire, at a conference that became known as *Bretton Woods*. Their goal was to develop a new set of regulations to govern the world financial system, and avoid the kind of global instability that had caused the Great Depression. Several key international institutions and agreements that still have enormous influence in the global economy were set up at that time: The World Bank (originally the International Bank for Reconstruction and Development) to help rebuild Europe, the General Agreement on Tariffs and Trade (GATT, the predecessor of the World Trade Organisation, designed to promote freeing up trade), and the International Monetary Fund (to provide a framework for international commerce). The role of these institutions in economic globalisation is discussed in more detail in section 12.10.

Many economists argue that the most recent, accelerating phase of economic globalisation can be traced back to the signing of the GATT, with its intention to end economic nationalism, free up trade between countries by removing tariffs, quotas and other barriers to free movement of commerce across international borders. The conference participants believed that this was the key to economic growth and global prosperity and stability. Over a period of around 25 years from 1948 to 1972, the a series of GATT rounds saw tariffs on trade in manufactures reduce from around 40% of their market value to less than 5% by 1993. During this time there was also rise in countries joining together to create free trade blocs and customs unions – groupings of countries that would trade with each other without tariffs or other trade protections, bringing several countries' markets into one. These included the European Economic Community which later became the European Union, and

At the time Australia was out of step with the global community, and maintained high tariff barriers until 1973. Australia in the post-war period was keen to develop our economy through replacing imports. By imposing high tariff barriers on imports, the idea was to avoid imports and manufacture products ourselves, rather than importing them.

Contemporary economic globalisation: the high tech age and a new era of globalisation (1970s to now)

Most economists agree that the new era of accelerated economic globalisation, and what is most often referred to as globalisation in common parlance, commenced in the early 1970s.

Globally, this era saw the rapid development of technologies that would facilitate the integration of global economies, such as in 1971 when the computer chip was invented. China began its economic reforms to open up its economy to the global market in the early 1980s. And in 1991, the



World Wide Web was introduced.

During the post-war period Australia had watched as countries around Asia – first Japan then Hong Kong, Taiwan, Korea and other places in Southeast Asia thrived as they opened up their economies.

In 1973, Australia joined the rest of the developed world in rapidly reducing its tariff barriers, after the share of exports in Australia's GDP had stalled during the protectionist period. This heralded the beginning of many major reforms to the Australian economy, which proceeded through the 1980s and 1990s to deregulation of many areas of the economy, privatise large numbers of government enterprises, remove subsidies from agriculture, and reduce tariffs to some of the lowest rates in the developed world. As will be discussed later, there are now only a small number of protected industries in Australia, with our maximum tariff rate on most imports being less than 5%.

In 1995 the WTO replaced the GATT and it had an expanded role. During this period there was also the establishment of many new trading blocs including APEC, NAFTA, CER with New Zealand, MERCOSUR and the consolidation of the EU with a shared currency. During all this time, the output of multinational corporations was growing as a share of global production. Along with globalisation came controversy, and in December 1999 one of the earliest major anti-globalisation protests took place – the Battle for Seattle at the WTO meeting in Seattle, USA. These developments have all meant that the current phase of globalisation signifies an altogether unique era of intense truly 'global' globalisation.



As was explained in Chapter 10, reducing tariffs changes the relative prices of imports, making them relatively cheaper. This means consumers are more likely to be prepared to purchase imported goods and services at lower prices, encouraging the globalisation of business through the use of comparative advantage whereby goods are produced more cheaply in one country and imported into another. There is a clear, inverse relationship between tariff rates and levels of global trade – as average world tariffs fell, the amount of world trade grew, and this rising trade is a key component of economic globalisation.

The WTO calculated that world trade in goods and services grew on average by 7.8% annually between 2000 and 2009. Table 1 provides a picture of the rapid increase in trading volumes during the period of accelerated globalisation. Note how world trade peaked in 2008, before dropping back in 2009 during the GFC. It is also worth noting that it took ten years between 1980 and 1990 for the value of global trade to double, while the eight years from 2000 to 2008 saw trade increase one and a half times, indicating a rapid increase in the rate of growth in trade between those two periods.

Table 1: Total trade in goods and commercial services, selected years 1980-2009

| Year | 1980 | 1990 | 1995 | 2000 | 2008 | 2009 |
|----------------------|------|------|------|------|-------|-------|
| Value (US\$ billion) | 2313 | 4209 | 6224 | 7856 | 19554 | 15471 |

Source of data: World Trade Organization, 2010

Globalisation post-GFC (GFC and financial deregulation)

If there is one symbolic effect of globalisation that we cannot miss, it is the GFC and its reverberations around the globe. It is believed by many economists, and majority of the general population, that the GFC was such an enormous event and has had such a significant and enduring effect largely because of globalisation. They cite the close integration of the global economy and financial systems, and the emphasis on a free market approach to economics with increased deregulation and reduced government control of national economies as central to the crisis itself. They point to the fact that the collapse of the American housing market and instability in its financial system could result in the collapse of the Icelandic banking system and the destruction of the Irish economy.

The reverberations of the crisis, which started in 2007, continue to roll around the world like a never-ending tidal wave. It used to be said that when America sneezes, Australia catches a cold. Why? Because it was believed that Australia's economy was highly reliant on the health of the US economy because of the close trading links between the two nations. Perhaps a better descriptor now would be that if the any one major economy sneezes, the globe catches pneumonia! The GFC has seen a major slowdown in almost every economy across the globe. The global powerhouse China has experienced slowing rates of economic growth, while the United States has endured a long economic recession with rising unemployment. Fears have been expressed that high unemployment and increasing sovereign debt crises among governments in Europe may lead to not only a slowing of global demand but a rise in protectionism as countries lose interest in reducing barriers to trade.

Review Questions

- 1. Explain how globalisation can be considered to be a phenomenon that has extended over a long period of human history.**
- 2. Create an annotated timeline of the history of economic globalisation.**
- 3. Explain the main reason why globalisation slowed down during the period from the start of the First World War until after the end of the Second World War.**
- 4. Explain the main goals of the key global organisations that were founded after the end of the World War II.**
- 5. Explain how the recent experience of globalisation is fundamentally different to earlier periods of increased economic integration.**
- 6. Describe what happened to the value of global trade between 1980 and 2009.**