

May 9, 2005

## Globalization From the Business Viewpoint

John D. Sullivan, Ph.D.  
*Executive Director, CIPE*

Globalization has redefined the global system, as the old concept of First World, Second World, and Third World is no longer valid. New players have joined the global economy and will have significant influence on how it will develop in the coming years. From the business perspective, globalization is not about analyzing pros and cons, but about understanding its impact and properly responding to it. This response should be thought of as a rules-based system that is currently under construction. Development of these rules should not be left to governments – business has to be at the table where the decisions are made. If it fails to do so, the business community will end up living in a system of rules that it never built, but was created by someone else. And this is true for businesses regardless of industry or location, as the need to actively participate in the development of an international system of rules applies equally to businesses from developed and developing countries. In the end, for the private sector, globalization is about creating a business-friendly environment, both on a local level and globally.



published by the

**Center for International Private Enterprise**

an affiliate of the U.S. Chamber of Commerce

1155 Fifteenth Street NW • Suite 700 • Washington, DC 20005 • USA

ph: (202) 721-9200 • web: [www.cipe.org](http://www.cipe.org) • e-mail: [cipe@cipe.org](mailto:cipe@cipe.org)

## Introduction

Globalization has replaced the Cold War as the defining element of the international system. How one deals with globalization as a country, as a company, as a region will define much of what develops over the next 20 to 30 years.

There is an abundance of books and articles analyzing the impact of globalization. On the one side, there are plenty of arguments for the benefits of trade. On the other side, there is another series of books and articles saying that globalization will end the world as we know it. While it is easy to point out the benefits and the pitfalls, such an approach may be misleading. The reason is that because if you are for globalization, you try to present the best picture, and if you are against it, the picture you present is the complete opposite. But among these debates on the pros and cons of globalization one key issue often remains overlooked – what does one do about globalization and how does one deal with it? Similarly, globalization can be viewed in the framework described by Dominique Moisi of the French Institute of Foreign Relations, who said that discontent about globalization comes both from the fear of being absorbed into an artificial world culture, on the one hand, and the equal fear of being left out in an increasingly unequal world.

From the business perspective, the process of globalization entails a pressing need for the business community to understand its impact and to properly respond. Those companies that fail to do so risk being left on the sidelines. In fact, there is a growing gap between companies that choose to join the global economy and those that try to exclude themselves from it or lack the capability to join.

## The Changing Global Economy

The world has gone through tremendous changes in the past several decades. When the United Nations (U.N.) was founded, two-thirds of the current members of the U.N. did not even exist as countries. In that brief period since 1948, two-thirds of the countries in the world formed their governments, and since that time the planet's population grew from 2.5 billion people to 6.5 billion people, and it continues to grow.

The rapid growth of countries and economies is also evident in the increased growth in trade. Since the 1940s, world exports grew by a factor of ten, and a big part of this has been the growth of trade within multinational companies, i.e. within the global supply chain. As international capital flows are no longer dominated by government to government assistance and are rather defined by private sector investment flows, countries begin to realize the need to create a proper investment climate necessary to draw those multinational companies and trade with. Those that fail to create such a

**Table 1. Developing Countries:  
Top Destinations for FDI (in billion US \$)**

|                | 1995 | 1998 | 2002 |
|----------------|------|------|------|
| China          | 35.8 | 43.8 | 53   |
| Mexico         | 9.5  | 12.2 | 13.7 |
| Argentina      | 5    | 7.3  | 1    |
| Brazil         | 5.4  | 28.9 | 16.6 |
| Hungary        | 4.4  | 2    | 0.9  |
| Malaysia       | 4.1  | 3.7  | 3.2  |
| Poland         | 3.7  | 5.1  | 4.1  |
| Chile          | 3    | 4.8  | 1.6  |
| Thailand       | 2    | 7    | 1    |
| India          | 2.1  | 2.3  | 3.5  |
| Czech Republic | 2.6  | 3.7  | 9.4  |
| Peru           | 2    | 1.9  | 1.4  |
| Russia         | 2    | 2.7  | 2.4  |

*Source: United Nations Conference on Trade and Development (UNCTAD) World Investment Report [www.unctad.org](http://www.unctad.org)*

climate, risk being isolated from the global economy.

In the last three to five years, China and India have both had economic growth rates of historic importance. They have emerged as dominant players in the world economy. The old concept of thinking in terms of the First World, the Second World, and the Third World is gone. It is no longer relevant. Brazil is poised to be another player at that same level, and other countries, such as Mexico, are not too far behind.

There has also been a huge shift in the patterns of foreign direct investment. A little over a decade ago, very little investment went to Russia or the countries of Central and Eastern Europe. Today they are big and important players in the world economy, especially countries in Central and Eastern Europe who have recently joined the European Union (E.U.). Also, the United States is no longer the dominant recipient of foreign investment, as China has recently surpassed the United States as the world's largest recipient of foreign direct investment.

Another factor in this emerging story of globalization is the evolution of Europe, which has changed fundamentally in the last seven years. One of the major changes is that there are ten new countries that recently joined the E.U.; but another factor is the decline in economic status of France and Germany. Not so long ago, a story in the Financial Times, the world's business newspaper, said that Chinese engineers working for Siemens developed a new cell phone technology.

This was not engineered in Germany; rather it was engineered by world-class Chinese engineers who are creating innovative engineering products in China. This is a tremendous change for Germany, and unless they can find a way to remain competitive, they will begin to see the outsourcing not just of manufacturing jobs, but of innovation. In fact, the rise of China as one of the global economic leaders is changing the structure of most world economies, not just Germany, in ways that are very difficult to foresee.

What does this mean for business? For business, globalization as a process of change, the speeding up of transactions and the flow of funds, is not new. It has been there in the past – the globalization of the early 1900s was interrupted first by the Great Depression and by World War II, then there was a brief spurt in the 1970s, and an increasing process in recent years.

But the real story is not increasing trade and flows of funds and money – it is the development of an international system of rules. It's a system of rules that governs today's global economy which the business community must help shape. If it fails to do so, the business community will end up living in a system of rules that it never built, but was created

by someone else. And this is true for businesses regardless of industry or location – the need to actively participate in the development of an international system of rules applies equally to businesses from developed and developing countries.

### The Drivers of Change

This process of developing an international system of rules has several different drivers. The first driver is the shaping of the international trade system, where of fundamental importance are free trade agreements, both regional and international. To illustrate the trends in trade, it is helpful to look at exports as a percentage of world output – in 1870, exports as a percentage of world output accounted for about five percent, in 1996, by comparison, the number had grown to 24 percent, and today it's probably closer to 28 percent. More importantly, not just exports of goods, but exports of services have also grown, as barriers to trade have significantly declined in many developing countries during the last several decades.

The second major driver is financial flows, not just foreign direct investment, but remittances and other sources of global capital flows. In terms of foreign direct investment,

**Table 2. Economic Globalization Indicators**

|                              | Trade in Goods<br>(% of GDP) |      | Gross Private Capital<br>Flows (% of GDP) |      | Gross Foreign Direct Invest-<br>ment (% of GDP) |      |
|------------------------------|------------------------------|------|---|------|---|------|
|                              | 1990                         | 2001 | 1990                                      | 2001 | 1990  | 2001 |
| <b>Income</b>                |                              |      |   |      |   |      |
| Low Income                   | 27.4                         | 39.8 | 3.0                                       | 5.1  | 0.5   | 1.7  |
| Middle Income                | 35.5                         | 50.8 | 6.8                                       | 12.2 | 1.0   | 4.3  |
| High Income                  | 32.3                         | 37.9 | 23.6                                      | 23.6 | 3.0   | 5.3  |
| <b>Regions</b>               |                              |      |   |      |   |      |
| East Asia/ Pacific           | 47.0                         | 61.0 | 5.0                                       | 11.1 | 1.7   | 4.6  |
| CEE Europe/<br>Central Asia  | --                           | 65.9 | --  | 13.2 | --  | 3.9  |
| Latin America/<br>Caribbean  | 23.3                         | 37.6 | 7.9                                       | 12.1 | 0.9   | 4.4  |
| Middle East/<br>North Africa | 48.1                         | 45.4 | 6.2                                       | 9.7  | 0.8   | 1.3  |
| South Asia                   | 16.5                         | 23.4 | 1.4                                       | 3.2  | 0.1   | 0.6  |
| Sub-Saharan Africa           | 42.3                         | 56.0 | 5.1                                       | 17.0 | 1.0   | 8.1  |
| European Union               | 44.9                         | 56.3 | 14.1                                      | 49.3 | 2.9   | 14.8 |

*Source: World Bank 2003 World Development Indicators*

Table 3. FDI Inflows (in million US \$)

|                                   | 1990           |             | 2000             |             | 2002           |             |
|-----------------------------------|----------------|-------------|------------------|-------------|----------------|-------------|
|                                   | Amount         | % of Global | Amount           | % of Global | Amount         | % of Global |
| <b>Developing Countries</b>       | <b>36,959</b>  | <b>17.7</b> | <b>246,057</b>   | <b>18</b>   | <b>162,145</b> | <b>25</b>   |
| Africa                            | 2,430          | 1.2         | 8,849            | 0.6         | 10,998         | 1.7         |
| America                           | 9,701          | 4.7         | 95,358           | 6.8         | 56,019         | 8.6         |
| Asia                              | 24,264         | 11.7        | 142,091          | 10.2        | 94,989         | 14.5        |
| <b>Central and Eastern Europe</b> | <b>640</b>     | <b>0.3</b>  | <b>26,373</b>    | <b>1.9</b>  | <b>28,709</b>  | <b>4.4</b>  |
| <b>Developed Countries</b>        | <b>171,076</b> | <b>82</b>   | <b>1,120,528</b> | <b>80</b>   | <b>460,334</b> | <b>70.6</b> |
| North America                     | 56,004         | 27          | 380,764          | 27          | 50,625         | 7.8         |
| Europe                            | 103,363        | 49.5        | 709,877          | 51          | 384,391        | 59          |
| Others                            | 11,708         | 5.6         | 29,887           | 2           | 25,319         | 3.9         |

Source: UNCTAD "2004 Development and Globalization: Facts and Figures"

in 1990, foreign direct investment flows to emerging markets were about \$25 billion per year. Last year, they totaled \$135 billion, although they are on a decline since topping \$180 billion in 1999. There are a lot of spirals in foreign investment flows, including portfolio investment, equity investment, debt, lending, and bonds. In such an environment, one of the major challenges for the international system is how to create a framework to smooth out the uncertainty. For businesses in developing countries it's about creating a framework that will lock in foreign investment once it is acquired. It is about making sure that it doesn't become fight-and-flight capital, flowing in and flowing back out.

The third driver is the expanding process of communications. The discrepancy between developed and developing countries in terms of mobile phone use is astounding. In high-income countries, six people out of ten use mobile phones, while in low and middle-income countries less than one person out of ten uses it. In the coming years, countries like China and India will become the biggest markets for mobile technology.

The fourth driver, closely related to the third, is the growth of technology. For example, in the market penetration of personal computers, high-income countries are far ahead of low- and middle-income countries – with 416 out of 1,000 people having access to personal computers there compared to only 21 out of 1,000 in the developing world. This is a large gap that clearly needs to be bridged, and much of this gap has to do with increasing educational opportunities as well as connectedness. Similarly, there is a gap in the use

of the Internet as well, and it is very important because, in today's world, if one can't communicate and can't use technology, one ends up feeling isolated.

And the final driver, of course, is population mobility. The flow of human capital from developing to developed markets has been increasing and is expected to grow further in the coming years. This is true not only for low-skilled workers, but also for workers with high skills and advanced education. Workers are able to take advantage of better opportunities in other markets, and doing so is becoming easier as the global system evolves.

### Rules-Based System is Under Construction

Underlying this process of globalization is the development of a knowledge system – the knowledge of how the rules work and how the international trading system functions. This is an integral part of today's international market economy of which you're either part of or you're locked out of. The decisive factor that allows countries and businesses to stay in the global economy as well as reap the benefits of such membership is whether they play by the rules and actively participate in shaping them or refuse to do so.

This global system is under construction – and that construction is incredibly important for business. Unfortunately, governments have a tendency not to want to listen too much to the views of businesspeople. Instead, decisions are made on the higher level as business is left to deal with decisions rather than participate in making them. And

**Table 4. Mobile Phones per Capita (# of mobile phones per 1,000 people)**

| High Income   | 609 | Low and Middle Income | 53  |
|---------------|-----|-----------------------|-----|
| United States | 451 | Brazil                | 167 |
| Sweden        | 790 | Russia                | 38  |
| Finland       | 778 | Venezuela             | 263 |
| Canada        | 362 | Argentina             | 193 |
| Australia     | 576 | Turkey                | 302 |
| Singapore     | 724 | Romania               | 172 |
| UK            | 770 | China (Mainland)      | 110 |
| Germany       | 682 | Indonesia             | 31  |
| Japan         | 588 | India                 | 6   |

*Source: International Telecommunication Union Development Report 2002 and 2003 World Bank World Development Indicators. Data are for 2001.*

this is true of developed countries as well, although in the developing world the problem is more pervasive. Therefore, one of the things that business has to do is fight for a seat at that table where decisions are made.

And the table is not located in one place – rather, it has many different centers, because there's no central command-and-control operation in this global system. The World Trade Organization, of course, is one the dominant factors in trade, although the increasing numbers of regional free trade agreements have become very important as well.

Another place where these rules are being shaped, that many business people often ignore, is the International Monetary Fund. Another location for global capital that is incredibly important is the Basel Commission on Banking Supervision of the Bank for International Settlements. The rules adopted there affect not just banks in Europe and the United States, they are also going to affect access to capital for companies in many developed and developing countries. It is vital that such rules be brought up and businesses start dealing with them.

The World Bank, of course, is another location where the rules are shaped. The International Labor Organization is also becoming more active and is trying to become a more prominent location for setting these rules and standards. The Organisation for Economic Co-operation and Development (OECD) has developed a number of standards that are very important. And then, finally, there are a whole series of international standards that have been developed – such as quality standards like ISO 9000 and environmental standards

like ISO 14000. These standards are incredibly important and will become more important in the future.

In the past decade and a half we've moved from a world dominated by the so-called "Washington Consensus" that John Williamson identified in the late 1980s, which looked at issues like fiscal discipline, tax reform, and exchange rates, to the world of macroeconomic policy. In this world of macroeconomic policy property rights, good governance, market entry, the rule of law, and access to information require a great deal of attention. Addressing these issues is vital, as developing markets seek a seat at the table of globalization and want to become involved, not left out, as Dominique Moisi said. For the business community this comes back to how to create good, stable, democratic governance – governance that is very important for the business community because businesses with such governance can then be heard in this process of creating a rules-based economy.

There are a series of guidelines for foreign direct investment that presents a slightly different checklist than John Williamson's famous Washington Consensus. It includes a number of issues – political stability, market access, the quality of the labor force, tax rates and incentives, and barriers to entry – but in the end it comes down to creating a stable and predictable economic environment where rules are fair and thoroughly enforced. In countries where the business environment is weak and where the informal sector is large there is a lot of work to do to create a market system that will allow businesses to take advantage of the globalization process.

**Table 5. Computers per Capita (# of computers per 1,000 people)**

| High Income   | 416.3 | Low and Middle Income | 21.6 |
|---------------|-------|-----------------------|------|
| United States | 739   | Brazil                | 83   |
| Sweden        | 687   | Russia                | 77   |
| Finland       | 662   | Venezuela             | 76   |
| Canada        | 647   | Argentina             | 68   |
| Australia     | 630   | Turkey                | 52   |
| Singapore     | 596   | Romania               | 44   |
| UK            | 526   | China (Mainland)      | 27   |
| Germany       | 480   | Indonesia             | 13   |
| Japan         | 477   | India                 | 9    |

*Source: IMD World Competitiveness Yearbook 2003, International Telecommunication Union Development Report 2002, and 2003 World Bank World Development Indicators. Data are for 2001 and 2002.*

**Table 6. Internet Users (# of users per 10,000 people)**

| Developed     |       | Developing       |       |
|---------------|-------|------------------|-------|
| United States | 5,513 | Brazil           | 822   |
| Sweden        | 5,730 | Russia           | 409   |
| Finland       | 5,089 | Venezuela        | 505   |
| Canada        | 5,128 | Argentina        | 1,120 |
| Australia     | 4,817 | Turkey           | 805   |
| Singapore     | 5,043 | Romania          | 1,905 |
| UK            | 4,230 | China (Mainland) | 632   |
| Germany       | 4,726 | Indonesia        | 377   |
| Japan         | 4,448 | India            | 174   |

*Source: IMD World Competitiveness Yearbook 2003, International Telecommunication Union Development Report 2002, and 2003 World Bank World Development Indicators. Data are for 2001 and 2002.*

Contrary to some opinion, this international architecture actually does have a structure. And the structure can be found within the IMF under Reports on Standards and Codes (ROSC). There are 12 standards under construction, and they all very much affect the way in which business is conducted.

One of these standards is corporate governance. It was very gratifying to see that when the OECD held their meeting in Paris to review their global standard this year, a number of private sector experts from developing countries were asked to help with the revision. It signified the evolution of global standards that is taking place today as developing countries are given an opportunity to participate in the creation of those standards. Five years ago, seven years ago, when that standard on corporate governance was developed, there were no emerging market countries asked to participate.

This is a very important part of this new international standard and it is a very important part of this emerging structure of globalization. If countries like Colombia succeed in developing corporate governance principles and standards that serve the interests of their local business community, all to the better. If countries don't do that, what's going to happen is that the IMF, the World Bank, the OECD, this international architecture of organizations will show up, work with local governments and business will wake up one day and find that it has to adhere to standards it never helped shape. From the point of view of business people it's better that they define themselves through active participation in reform.

Another big part of these international standards – regarding fiscal transparency, anti-money-laundering, and market integrity – comes back to the famous words, “anti-corruption.” In recent years, Business Principles for Countering Bribery (BPCB), developed by Transparency International, and the addition of the 10th Anti-Corruption Principle to the U.N. Global Compact have been important steps in developing these standards. The private sector now recognizes its role in combating corruption, and internal mechanisms are becoming just as important as external ones.

The defining characteristic of Latin America has been the gap between the rich and the poor – the income disparity. As business people, we really have to go back and take another look at Hernando De Soto's work on the informal sector. If we look at the steps and stages for barriers to market entry, it is evident that countries with these barriers, where business people are locked out and cannot get into the economy, run a terrible risk of having only very small parts of their economies linked into the global marketplace. And as we look at the WTO taking effect, as we look at trade agreements taking effect, the end of the Multi-Fiber Agreement, what are the new sources of economic growth for countries? How do you attract these foreign direct investors? How do you attract your own domestic investors?

Improving the business marketplace not just for firms in the formal sector but also for the informal sector, whether individuals choose to leave the informal sector and come to work for companies, whether they choose to create new companies and growth companies in the market, that's where we're going to see emerging markets develop the kind of healthy market economies that will increasingly attract and demand the investment opportunities that we all look for.

---

*John D. Sullivan has been Executive Director of the Center for International Private Enterprise (CIPE), an affiliate of the U.S. Chamber of Commerce, since 1991. In 1983, he was associate director of the bipartisan Democracy Program that created the National Endowment for Democracy that supports CIPE. Once the Endowment was established, John returned to the Chamber to help create the Center for International Private Enterprise (CIPE) where he served as program director. From 1977 to 1982, he worked at the U.S. Chamber of Commerce's Public Affairs Department and Special Project Division. In 1976, Mr. Sullivan joined the President Ford Election Committee in the research department on campaign strategy, polling, and market research. Prior to this he worked with the Institute for Economic Research and the Office of Minority Business Enterprise (U.S. Department of Commerce) in Los Angeles on projects to stimulate small and minority enterprise.*

*Mr. Sullivan has a Ph.D. in international relations from the University of Pittsburgh, and is the author of a number of articles and publications on the transition to democracy in Central and Eastern Europe, corporate governance, and market-oriented democratic development.*

*The Center for International Private Enterprise grants permission to reprint, translate, and/or publish original articles from its Economic Reform Feature Service provided that (1) proper attribution is given to the original author and to CIPE and (2) CIPE is notified where the article is placed and a copy is provided to CIPE's Washington office via mail, e-mail, or fax.*

*The Center for International Private Enterprise is a non-profit affiliate of the U.S. Chamber of Commerce and one of the four core institutes of the National Endowment for Democracy. CIPE has supported more than 800 local initiatives in over 90 developing countries, involving the private sector in policy advocacy and institutional reform, improving governance, and building understanding of market-based democratic systems. CIPE programs are also supported through the United States Agency for International Development.*

