

The Vulnerability of Globalization

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I

The process of economic convergence that produced the widening of the west into a universal concept was facilitated by the movement across national frontiers of goods, capital, labor, ideas and technologies. In short it came about as a result of the phenomenon now widely referred to as "globalization". In periods when obstacles were raised to the movement of economic factors (and also ideas) - above all in the interwar period of the twentieth century - the process of convergence was halted and reversed. But convergence resumed for the Cold War "West" after 1948-9, and then - after the political and economic upheavals of 1989-91 - more or less universally. By the 1990s, as Russia, India, Mexico and Korea, with quite different trajectories for most of the past century and strong traditions of nationalist economic management, all became in an economic sense western. They accepted a mix of commitments: to the rule of law, to democracy as a way of setting rules, and to free interchange (the market) as a way of optimizing outcomes within a secure system of property rights.

The world had become "western". The new climate was neatly described in a famous exchange at a meeting on a U.S. battleship off the coast of Malta in December 1989 that is often held to mark the end of the Cold War. When U.S.

Secretary of State James Baker talked about Germany and "western values", Mikhail Gorbachev, the General Secretary of the Communist Party of the Soviet Union, asked why democracy and the market were "western" and whether they were not values which "belonged to the whole of humanity"?¹ The world established by political and market reforms continues to have a powerful appeal.

However bad security relations are between what can now really be called the opposed sides of the Atlantic, or whatever spats there are across the Pacific on the value of the renminbi and the yen, there is a frequent hope that the strength and complexity of the economic inter-relationship (a product of globalization) is so great as to offer a counterweight to the political tensions. Indeed the reason that both sides in modern conflicts feel that they can afford to be rhetorically carried away is a function of the sense of interdependence, and that a really bad outcome is not possible. The British Prime Minister Harold Macmillan for instance liked to tell President Kennedy that a "united Free World was more likely to be achieved through joint monetary and economic policies" than through political or military alliances.² Advanced democracies do not go to war with each other, as they have too much to lose.³ Mercury, the god of commerce, has managed to send Mars, the god of war, into exile. We feel very secure about this argument and its implications - maybe we feel too secure.

¹ Michael Gorbachev, *Gipfelgespräche: Geheime Protokolle aus meiner Amtszeit*, Berlin: Rowohlt, 1993, pp. 128-9.

² Cited in Alastair Horne, *Macmillan. Volume II, 1957-1986*, London: Macmillan, 1989, p. 284.

³ There is an extensive literature on the "democratic peace", taking up an idea originally propounded by Kant. See Michael Doyle, "Kant, Liberal Legacies and Foreign Affairs", *Philosophy and Public Affairs*, 12, 1983, pp. 205-35, 323-53; and "Liberalism and World Politics", *American Political Science Review*, 1986, pp. 1151-69. Also Bruce Russett, *Grasping the Democratic Peace: Principles for a Post-Cold War World*, Princeton: Princeton University Press, 1993..

There are periods in the past when greatly increasing prosperity attracted many commentators to similar arguments: in the mid-nineteenth century, before the Crimean war, or in the early twentieth century. In John Henry Newman's *Apologia pro vita sua* (1864), for instance, Newman uses the widely believed association between commerce and peace to reach a verdict on attempts at "expedients to arrest fierce wilful human nature in its onward course, and bring it into subjection": "ten years ago there was a hope that wars would cease for ever, under the influence of commercial enterprise and the reign of the useful and fine arts; but will anyone venture to say that there is any thing any where on this earth, which will afford a fulcrum to us, whereby to keep the earth from moving onwards?"⁴

What was the origin of the fallacy Newman detected? If it were true that economics determines the way political and security relations work, there would evidently be harmony between the major industrial countries. We would slide into a sort of Fukuyama *post-histoire*, a vision elaborated with power and clarity after 1989. This harmony is frequently evoked in the "globalization paradigm". Many people, particularly those connected with the business world, repeatedly emphasize that the world is closely connected, and that political boundaries and political arguments are irrelevant to business logic. For all the political friction since September 11 and the Iraq war, there have been increased flows of funds and investments, and the economic connectivity has become greater rather than less. Many people who think of themselves as living in a globalization mindset would like to operationalize this economic inter-connectedness, and make the fact of

⁴ (ed.) Wilfrid Ward, *Newman's Apologia pro vita sua*, London: Oxford University Press, 1913, pp. 336-7.

interdependent prosperity a building stone for better international relations.

Is globalization the only show in town? The major alternative to the "globalization" world view sees connectedness as producing unfair advantages, and international relations as based on exploitation. One convenient way of labeling this alternative is "imperialism", a word generally used with a critical intent. Labeling U.S. policy as "imperialism" became part of the standard rhetorical weaponry of an anti-American left in Europe and elsewhere, as well as of critical voices in the United States. The school of diplomatic history under William Appleman Williams strongly engaged in this approach.⁵ In the 1990s, the language of empire as a way of critiquing power, and especially American power, was revived: most influentially by the Italian philosopher of violent revolution from the 1970s, Toni Negri, who now became a guru for the anti-globalization left. After 9/11, and especially after the Iraq war, this world view produced a tremendous spate of books. In particular, the Roman analogy, which had already been floated after the Second World War, became very popular: critics saw the imperialization of the United States as an analogous process to the ending of the Roman Republic and its replacement by the Augustan empire.⁶

⁵ Notably in William Appleman Williams, *Empire as a way of life : an essay on the causes and character of America's present predicament, along with a few thoughts about an alternative*, New York : Oxford University Press, 1980.

⁶ The very generalized use of Empire and Imperialism as a way of understanding the modern world was presented in what became a cult book by Michael Hardt and Toni Negri, *Empire*, Cambridge Mass.: Harvard University Press, 2000. The recent books include: Chalmers Johnson, *The Sorrows of Empire: Militarism, Secrecy, and the End of the Republic*, New York: Metropolitan Books, 2004; Benjamin R. Barber, *Fear's Empire: War, Terrorism, and Democracy*, New York: Norton, 2003; Michael Mann, *Incoherent Empire*, New York: Verso, 2003; Emmanuel Todd, *After the*

Curiously, however, this mostly critical literature began to be supplemented by normative suggestions that the United States should want to behave like an Empire of the European past. At the conclusion of a stimulating survey of the story of the British empire, Niall Ferguson tried to draw "lessons for global power". The United States, he concluded, first of all "can do a great deal to impose its preferred values on less technologically advanced societies".⁷ The suggestion was that it would be drawn in through a series of interventions analogous to those of nineteenth century Britain, and would create a functioning imperial system without really willing or knowing it. (One famous phrase, coined by the great British historian J.R. Seeley, claims that the Victorian empire was put together in a fit of absence of mind). Michael Ignatieff, reflecting on the legacies of Bosnia and Rwanda, added an appeal for a dynamic human rights internationalism, which he termed "Empire Lite".⁸

Most figures actually associated with the U.S. administration did not like the idea of taking up Caesar's mantle or Victoria's tiara. But Vice-President and Lynne Cheney in 2003 sent out a Christmas card with a quotation from Benjamin Franklin: "And if a sparrow cannot fall to the ground without His notice, is it probable that an empire can rise without His aid?"⁹

The new discussion of imperialism as a model is quite perplexing. In particular, some committed institutional liberal internationalists such as John Ikenberry have pointed out that Empire Lite actually looks like old-

Empire: The Breakdown of the American Order, New York: Columbia University Press, 2003.

⁷ Niall Ferguson, *Empire*, New York: Basic Books, 2003, p. 367.

⁸ Michael Ignatieff, *Empire lite : nation-building in Bosnia, Kosovo, and Afghanistan*, London : Vintage, 2003.

⁹ *Washington Post*, December 28, 2003.

fashioned liberal internationalism.¹⁰ What is new? The story of some of the human rights catastrophes of the 1990s, as well as of international terrorism, raises the obvious issue that there are many people who will go to considerable risks to undermine a liberal and tolerant international and national order. How, in the absence of a world government, can they be kept in line? Only by the application of force by the hegemon.

Many readers will feel that it is possible to see both the world views presented here at the same time: that in the spirit of *Empire Lite*, rules without enforcement are bound to be ignored, and enforcement without fixed rules is likely to be widely rejected as tyrannical. Therefore both rules and an enforcer (who is a state) are needed for stability and order. There is a well established literature, based on the work of Charles Kindleberger and Robert Gilpin, which suggests that the nineteenth century liberal order only worked because of the benign hegemon and that after 1945 the United States learnt this lesson.¹¹

This is not, however, how most of the world sees the process of making politics in an integrated world. Generally, the rules approach demands a participation in the formulation of the binding rules of a broad group of countries, views, and interests. Without such participation, the rules began to lack legitimacy (unless it is generally agreed that the rules stem from a divinely created natural law order). The more a generalized relativism guides our approach to rule making, the more we insist on process as the way of creating legitimacy. But

¹⁰ See his collective review of a recent collection of this literature G. John Ikenberry, "Illusions of Empire: Defining the New American Order", *Foreign Affairs*, March/April 2004.

¹¹ See Charles Kindleberger, *The world in depression, 1929-1939*, London: Allen Lane, 1973; Robert Gilpin, *The political economy of international relations*, Princeton: Princeton University Press, 1987.

these processes are actually deeply divisive in practice, and the most intractable tussles of recent years arise out of arguments about the rule making process in such institutions as the United Nations, the World Trade Organization, the International Monetary Fund, or the European Union. There is in each of these cases a sort of expectations trap.¹² International rule-making looks more crucial, so we have greater hopes about what international negotiation can produce. But the result is a compromise that is disappointing, and so there comes to be a substantial questioning of the legitimacy of the process.

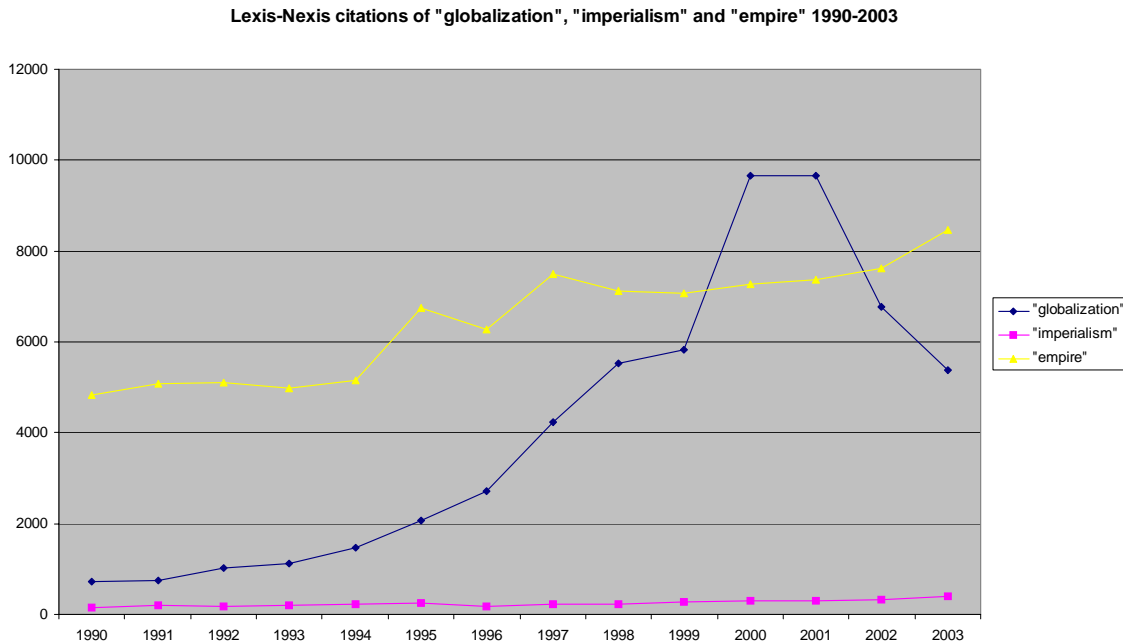
As a result, when our hopes of rules are disappointed, we react by seeing power in its full *Realpolitik* nakedness. *Realpolitik* overrides rules, or, as a rather old British pun had it, Britannia waives the rules in order to rule the waves.

The "imperialism" and the "globalization" models are overall interpretations of such power for their adherents that the other perspective simply disappears. The alternative is rejected as naive or ideological, as in Robert Kagan's juxtaposition of the Mars and Venus views of American and Europeans.¹³ As approaches, they are like the optical illusions made famous by Maurits Cornelius Escher, where squares either pop out of a page, or recede, but where the observer cannot be brought to see both phenomena at the same time. There is one perspective - or the other.

Since 2001, there has been a definite retreat of the "globalization" paradigm. It is evident in a survey of Lexis-Nexis citations of the word "globalization" in major world newspapers, which shows a distinct falling off after

¹² See for instance, Harold James, "From Grandmotherliness to Governance: The Development of IMF Conditionality", in *Finance and Development* December 1998.

2001. On the other hand, there are more references to "empire" and "imperialism".



II

The clash of these interpretative models shapes responses to the major international economic issues of the day. Any economic order depends on systems of rules to set a framework for contracts: this is true on the international level as it is in national affairs. Globalization depends on rules. Its critics see rules as an expression of power relations.

The major current debates concern the world trading system, the order of corporate governance, and the world monetary order. All of these domains have recently become highly contentious.

¹³ Robert Kagan, *Of paradise and power : America and Europe in the new*

First, the commercial system: In the "globalization" view of the world, trade wars are destructive and dangerous. Globalizers are relieved when states draw back from the brink of confrontation, as recently in the case of the U.S. steel tariffs dispute. They believe the rationale for international economic institutions such as the GATT or the WTO lies in the enforcing of rules and procedures that might prevent the escalation of self-destructive responses to domestic political pressures. The likelihood of a WTO ruling against the steel tariffs thus helped the United States to have a better policy, and give up on the unilateral imposition of the tariff.

The "imperialism" model thinks that trade relations shape an unequal system of exchange and dominance, and that political force molds trade law and patterns of commerce. Aggressive trade policy is or can be used as an instrument of policy and can create new opportunities for the assertion of power and the development of economic muscle. The current trade order thus reflects the ability of the United States to impose its vision on the world, and other countries are compelled or cajoled into compliance by threats (for instance to use Super 301 of the 1988 Trade and Competitiveness Act) or promises (of better access to U.S. markets).

Second, corporate governance until very recently was thought to be strictly the domain of national governments and regulators. Over the past ten years, however, there has been a systematic attempt to engage international institutions in governance issues. This is partly because the legal framework of a modern economy is so complex that it would be needlessly complicated for national governments to work out all the rules required from scratch. In

world order, New York : Knopf, 2003.

practice, when many states adopted market economies in the aftermath of the collapse of communism, they almost invariably either took over the legal systems of the European Community/European Union or of the United States.¹⁴

There are also obvious overlaps to issues concerned with trade law, and to financial stability issues. In the wake of the 1997-8 Asia financial crisis, international institutions and the U.S. government focused much of their analysis on misgovernance or "crony capitalism" as responsible for the crises in Asian economies. According to this analysis, crony capitalism had led to a misinvestment in unproductive enterprises, and to moral hazard problems. International lenders and investors had chosen to lend by preference to borrowers who were politically well connected, and whose debts thus carried an implicit government guarantee. Any reform program thus required a dismantling of corrupt structures and the institution of accounting and oversight mechanisms to guarantee greater corporate transparency.

The most contentious issue in the Doha round of trade negotiations concerned rules for investment, which were often seen by developing countries as a way of producing one-sided benefits for industrial capital-exporting countries and interests. The tough position adopted by Japan and the E.U. on this issue (the so-called Singapore issue) was largely responsible for the breakdown of the Cancun ministerial meeting of the WTO.

In analyzing governance, it is hard to separate concern with overall rules from debates about self-interest: whether with the discussion of trade-related investment issues, or with the dismantling of crony capitalism. Critics pointed

¹⁴ See Joseph Weiler, "The Constitution of the Common Market Place: The Free Movement of Goods," in *The Evolution of EU Law*. P. P. Craig and G. de Búrca, eds. New York: Oxford University Press, 1999.

out that in practice improved transparency in domestic financial systems meant permitting market entry to large U.S. and E.U. institutions. American banks took dominant positions in Mexico and Korea, and Spanish banks in South America. After big corporate scandals emerged in the U.S. and other big industrial countries, much of the 1997-8 preaching to Asia looked outrageously hypocritical. Again, it could be portrayed easily as a mask for concrete interests and for the projection of power.

Third, the international monetary order: In the "globalization" interpretation, the operation of the international economy requires a stable system of monetary rules. The system may take a diversity of forms. The restoration of the world monetary order after the breakdown of the interwar era and the Second World War took place on the basis of fixed exchange rates and restrictions on capital mobility. Modern globalization has developed on the basis of flexible exchange rates between major industrial economies and capital mobility. But both these orders are internally consistent and robust.

The "imperialist" vision takes these rules and sees political advantage lurking behind them. Both the Bretton Woods system (the first postwar order of fixed exchange rates) and the modern international economy gave the United States an unfair position, or what General de Gaulle memorably termed an "exorbitant privilege". "No domain," the General explained to Alain Peyrefitte, "escapes from American imperialism. It takes all forms. The most insidious is that of the dollar."¹⁵ The dollar was the key currency of both systems, with the result that Americans could finance their civilian consumption and their military imperialism with "OPM": Other Peoples' Money. In Bretton

¹⁵ Alain Peyrefitte, *C'était de Gaulle*, Paris: Gallimard, 2002, p. 663.

Woods, the U.S. financed capital outflows and military expenditures through a build-up of claims on the U.S. dollar. De Gaulle and his successors complained, but they failed to shake the reserve role of the dollar. Thus the United States in the 1980s and 1990s and especially since 2000 has been able to finance very large current account deficits as other countries build up surplus positions.

The odd parallelism of the 1960s and the floating rates era leads those who are suspicious of the United States to spend considerable amounts of time and intellectual energy trying to devise new monetary orders, and institutions that might enable them to pull off something of the American trick. In particular, the long story of European monetary integration is permeated by what economic psychologists might term "dollar envy". Many European currencies - especially the influential case of the Deutschemerk - were devised so as to make the political use of the currency hard, in order to avoid some of the problems of the European past. The Deutschemerk carried with it a restrictive vision of what a currency should be, and this was transferred to the Euro. By contrast, the dollar seemed a "can do" currency, which could be harnessed by its political masters. The Werner Plan was drawn up as the Bretton Woods system started on its final crisis, the European Monetary System originated in part as a response to the perception that Jimmy Carter was abusing the world monetary system, and proponents of European Monetary Union in the 1990s sometimes (but not always) sounded an anti-American note.

There is a growing tendency, especially where corporate governance and monetary issues are concerned, to reinterpret the world in power political terms - to see through the imperialism lens rather than that of globalization. This tendency especially in Europe, however, marks a deep sense

of frustration about the geo-politics and geo-economics of the new post-Cold War era. In the 1960s, the highpoint of the Gaullist critique, Europe could mount not only an intellectual critique, but also a real challenge to the position of the United States and of the dollar. In the 2002, it cannot, and the real challenges and threats to the stability of the system come from elsewhere.

III

Such a survey of the rule-based vision of the world economy and its vicissitudes raises the question of how far and long the U.S. role in the system can continue, and of the extent to which it depends on the compliance and cooperation of others. The United States is unlike conventional historical empires in that its rule depends on cultural and above all economic influence rather than territorial domination. Indeed Dominic Lieven pointed out in his wide-ranging survey of *Empire* that the modern analogues of traditional empires are large ramshackle multi-ethnic states such as India or Indonesia (or even the European Union) rather than the United States.¹⁶

The world economy after the Second World War was rebuilt on the basis of systems of rules and complex institution-building.¹⁷ One way of thinking about the economic story is to regard rule-building in two critical areas as moving in different ways. During the interwar period, international discussions on international

¹⁶ Domic Lieven, *Empire*, Cambridge Mass.: Harvard University Press, 2000.

¹⁷ The classic account of the postwar order is by Richard Gardner, *Sterling-dollar diplomacy; the origins and the prospects of our international economic order*, New York, McGraw-Hill, 1969. See now G. John Ikenberry, *After victory : institutions, strategic restraint, and the rebuilding of order after major wars*, Princeton: Princeton University Press, 2001.

cooperation foundered because trade negotiators believed that while tariff reduction and quota elimination might be desirable, there was no point in discussions until a stable monetary system had been created. Without stable monetary order, the use of trade measures to stem the export of pernicious deflation could be justified as a desirable second-best measure. On the other hand, the monetary discussions foundered because of reluctance to make agreements while the vicious spiral of trade protection was still underway. During the Second World War, the U.S. made it clear that it was not prepared to negotiate on trade liberalization that it saw as necessary to postwar peace, and as a result, all the diplomacy concentrated on a framework of monetary rules (at Bretton Woods). Bretton Woods of course created institutions, the World Bank and the IMF, devised to implement the monetary order, but the intended third pillar (ITO: International Trade Organization) was left until after the War, and in practice was only realized in the 1990s.

The rule-based monetary order disintegrated in stages between 1968 and 1973, and after that the IMF's functions changed very dramatically. Its major task turned out to be plugging market failures left by the newly invigorated capital markets: in practice a great deal of attempt at crisis prevention and a great deal of experience in crisis resolution.

A consensus gradually emerged for U.S. administrations that attempts at international monetary coordination were pointless and counter-productive: like the Bretton Woods order, they restrained monetary policy in a sub-optimal way and led to undesired outcomes. Thus the experience of the 1978 Bonn summit, or the 1985-87 negotiations and semi-agreements about appropriate exchange rates were generally

viewed as discrediting the idea of negotiating about exchange rates. The mantra of all administrations since the 1980s is that exchange rates are set by the market.

The postwar period produced a great expansion of trade that is fundamental to the story of increased prosperity. Trade became institutionally more regulated. The GATT generalized bilateral agreements, then produced general tariff reductions in the 1960s Kennedy round, and then became fully institutionalized as the WTO in 1996. Many observers are surprised by the apparent willingness of the U.S. to accept rules in this area at each stage of the development of a rule-based order. The story of trade opening can be read as a suspense drama, with a new twist to the narrative on almost every page. The GATT was a compromise. It achieved its biggest successes in the 1960s, largely at the cost of reducing its extent so as to exclude some of the most contentious trade items - textiles and agricultural products. By the 1970s, after the collapse of the Bretton Woods par value system, most writers agreed that the GATT was moribund. The Tokyo Round was protracted and spotty. In the mid-1980s, the leading experts concluded that the GATT was "in a state of breakdown". The ministerial meeting of 1982 had failed. The Uruguay Round looked doomed to failure as the United States and the European Community became locked in a politically complex struggle over agricultural pricing and subsidies. Even in 1993, on the eve of the final agreement of this Round, a major text produced by a GATT official had as its theme "the weakening of a multilateral approach to trade relations", "the creeping demise of GATT", and the fact that "the GATT's decline results from the accumulated actions of governments." But then came the astonishing extension of multilateral principles to intellectual property, trade-

related investment, and the creation of a more complete conflict resolutions procedure and the institutionalization of multilateralism in the World Trade Organization. At that time, the commentators were skeptically insisting that the United States would ignore the new institution, and instead continue a unilateral exercise of power through the application of Super 301. But when the first ruling came against the U.S., the U.S. accepted it. In 1998, everyone gave reasons why the financial services agreement could not be realized. Then, apparently unpredictably, at the last moment it came about. Rules still ruled.

In the earlier age of worries about globalization at the turn of the nineteenth century, a backlash began, which in the end produced restrictions on migration and high levels of trade protection. When national protection became the major priority of most countries, in the 1920s and 1930s, the world became both poorer and less safe. There was a vicious cycle, in which external forces were blamed for loss and disaster, and high levels of trade protection destroyed national prosperity.

Most countries have avoided this sort of backlash in the second half of the twentieth century, although their citizens had the same angst. The changing of employment patterns is a constant accompaniment of growth. In the early 1970s and again in the 1980s U.S. workers and producers were upset about the loss of jobs to Japan. Some of the most skilled jobs, in automobiles, were lost; household appliances like TVs were no longer made in the United States. On each occasion, the administration tried to respond to the job loss worries not by trade restrictions, but by exchange rate alterations that would make the U.S. products more competitive: first the end of the gold convertibility of the dollar in 1971, and then in

1985 the Plaza agreement to depreciate the dollar. Monetary and exchange rate policy initiatives offered a way of absorbing adjustment pain. The focus of trade discontent was shifted to the monetary arena in a way that helped to undermine the legitimacy of institutional ways of regulating the international financial system.

The use of monetary policy and exchange rate adjustment to deescalate trade conflict is harder today, since many of the countries whose products are entering the United States peg their own currencies to the dollar. Governments still feel that they need some response in an attempt to "feel the pain", and to show that they are doing something. Like the Bush administration they adopt tariffs that may then be over-ruled by the WTO. In this way they do nothing very harmful, but point out to the electorate that their hands are tied by international agreements and institutions. But this sort of action itself then produces a new kind of backlash, against the international institutions.

Trade problems are in fact routinely dealt with by shifting the emphasis to the monetary arena. The world has developed its institutional arrangements in the setting of globalization by making them harder in the trade arena and softer in the monetary one. In the future the offloading of adjustment problems to monetary policy will be more difficult (because of widespread Asian exchanger rate pegging) and the trade system will be in consequence more vulnerable.

Can the post-Bretton Woods order blow up in a manner analogous to that of the disintegration of Bretton Woods? This is the fundamental fear of those who think U.S. current account deficits unsustainable, and are worried about the way in which the United States attracts over an amazing three quarters of net international capital inflows (in

2002: 75.5 percent). There is an obvious contrast with British imperial experience, and the resilience of the British Empire owed a great deal to its long term current account surplus position from the mid-nineteenth century to the first world war. By contrast, Imperial Spain in its Golden Era in the sixteenth seventeenth centuries had permanent deficits, financed by the extraction of precious metals. It deindustrialized and lost the basis for pre-eminence.

There are two complementary ways of thinking about the balance of payments and hence of judging its sustainability. The first is that it is a reflection of the relative attraction of foreign assets for U.S. residents and of U.S. assets for those outside. The deficit is driven by the high demand for U.S. assets, and its sustainability depends on the continuance of this demand.

One apparently odd fact makes the deficits more sustainable: the yield on U.S. assets for foreigners, the price paid by the U.S. for its borrowing, is substantially lower than the yield for Americans on their foreign holdings. This reflects not miscalculation or stupidity on the part of foreign investors, but a calculation in which they buy security in return for lower yields. The primary attraction of the United States as a destination for capital movement is the unique depth of its markets (which generate a financial security) and the political and security position of the country. This is why inflows to the United States may increase after global security shocks (as they did after September 11).

The ability of the United States to finance its deficits depends on the continued perception that it is a high growth and high productivity economy and that it is politically and militarily secure. Conversely the security

of the United States depends on the continued inflow of capital, as a sudden adjustment would be unbearably painful and intolerable politically.

The painfulness of adjustment will become apparent in considering the other way of thinking about the U.S. balance of payments position: a relationship between saving and investment in the U.S. As long as investment is high and saving is low, the gap is financed from abroad. Low levels of saving reflect a high commitment to consumption. Contrary to popular assumption particularly outside the U.S., this is not fundamentally the result of an addiction to outrageous forms of conspicuous consumption such as SUVs. (Though there are some odd statistics that seem to bear parts of this thesis out: Americans spend more on jewelry today than on shoes.) But expenditure on food and clothing as a proportion of income has fallen quite dramatically over recent decades, expenditure on housing remains more or less constant, and the big growth has been in spending on education and health. Many academic economists (who have an obvious interest as educators) would like to reclassify these as forms of investment in human capital, and it is probably true that the continued innovative capacity of the U.S. depends on quality education. We can also get much or at least some benefit by attracting highly educated people from other parts of the world; and the export of people trained in American universities is a vital part of Joseph Nye's idea of "soft power".¹⁸

Another element of the over-consumption theory arises out of the contemplation of the link between fiscal issues and the current account. Government spending on the military is a form of consumption, and in the Vietnam era,

¹⁸ Joseph S. Nye, *Soft power : the means to success in world politics*, New York : Public Affairs, 2004.

in the Reagan defense build-up, and in the post-2001 this was a current issue in international discussions of the stability of the monetary and financial order. In all these cases, the defense build-up went hand in hand with domestically-oriented fiscal expansion, to create the Great Society, or for Reagan and Bush2 to cut taxes. It is as if the U.S. could not gather the domestic support for defense or war without buying social content at home. De Gaulle's criticism of the U.S. seems a peculiarly timeless of the European view of each of these incidents: "The United States is not capable of balancing its budget. It allows itself to have enormous debts. Since the dollar is the reference currency everywhere, it can cause others to suffer the effects of its poor management. This is not acceptable. This cannot last."¹⁹

The "cannot last" issue is however the one that raises the link between the capacity to borrow and its dependence on continued economic dynamism. In the late nineteenth century era of open capital markets, inflows to high growth countries (such as the United States or Australia) were sustained over very long periods of time.

The question about sustainability then turns into one about the probability of continued growth rates that are higher than those of the rest of the industrialized world. For much of the 1990s foreign capital inflows reflected a foreign view that the peace dividend, fiscal prudence and technological dynamism represented an ideal environment. In the 2002, part of this environment clearly deteriorated. Growth rates are threatened by long term fiscal problems arising both out of military commitments and the burdens of

¹⁹ Peyrefitte, de Gaulle, p. 664. See also Francis J. Gavin, *Gold, dollars, and power : the politics of international monetary relations, 1958-1968*, Chapel Hill: University of North Carolina Press, 2004, p. 121.

ensuring social security for an ageing population: in this the United States shares (in a less extreme form) a problem that is also emerging in the ageing industrial societies of Europe and Japan.²⁰

Fiscal problems thus pose a long-term threat to the capacity of the United States to sustain growth and hence capital inflows.

The world economic environment is however clearly not made by the United States alone. The likelihood of bad effects coming from crises elsewhere is increased by increased financial turbulence and also by the deinstitutionalization of international monetary relations as discussed above. To go back to the immediate post-1945 vision, Bretton Woods aimed at establishing an institution (the IMF) to manage reserves. Now reserve positions held at the IMF play a minor role, and the major holders of reserves are national central banks, as they were before the Second World War.

On the other hand, explosive and contagious debt crises in the past have been in part reflection of the policy-mix in advanced industrial countries. In the early 1980s, or mid-1990s, high interest rates worldwide changed the debt dynamics and made previously tolerable levels of debt unsustainable and thus touched off creditor panics. In the modern scenario, the effects of expansive fiscal policies, not just in the U.S. but in many European countries, will be likely to result in real interest rate rises.

In this setting, the build-up of large claims on the U.S. - especially in the form of the massive reserve

²⁰ Lawrence Kotlikoff, Hans Fehr and Sabine Jokisch, "[The Developed World's Demographic Transition -- The Roles of Capital Flows, Immigration, and Policy](#)", mimeo, October 2003; Lawrence Kotlikoff and Niall Ferguson, "[Going Critical](#)", *The National Interest*, Fall 2003.

holdings of Asian central banks - as a potential danger. Asian reserves now account for over two thirds of the world's reserves, and Japan holds some \$650 bn. in U.S. (mostly Treasury) securities and China \$420 bn. Of the U.S. government debt, 37.3 percent is now held abroad, compared with 4.7 percent in 1965 when General de Gaulle believed that he needed to criticize U.S. dollar politics. The danger today probably lies less in the political instrumentalization of these reserves (such as would be represented by a de Gaulle-like conversion of dollars into something else, probably euros). There might be a certain political attraction of such an anti-American action at particular moments, but it would be enormously costly for those who undertake it since it would push down the value of the dollar assets very quickly and substantially. The risk is that these reserves are unlikely to be held perpetually for economic rather than political reasons. The world of liberalized capital movements that evolved in the 1990s has seen remarkable shifts and reversals of direction of capital flows. So the question arises what if Japan, or more probably China or (even more probably) India (which has also been recently accumulating reserves very rapidly) needs to use them?

This is an area where the costs of the de-institutionalization of the international monetary system may become apparent. In the 1990s, contagious financial crises were handled by big IMF-coordinated rescue operations. The big capital account crises of the 1990s involved much larger amounts of support relative to previous crises. Mexico in 1995 drew 688 percent of its quota, Korea in 1997-8 1939 percent, Argentina in 2001 800 percent, and Turkey in 2002 1330 percent. Before the 1990s, there had been an inclination to give too little in order to give

incentives to program countries to make adjustment and reforms. When the emphasis shifted to reassuring nervous markets in a capital account crisis, the priorities were reversed, and stabilizing the expectations of the markets would involve the assurance of so much support that speculators could not take a position against a country or currency and hope to succeed. This function had an analogy to the role of central banks in national economies as lenders of last resort, an analogy that was controversially drawn by the IMF's First Managing Director Stanley Fischer. The parallel is sometime made to the Colin Powell doctrine about military intervention: that it only makes sense if conducted with massive and overwhelming force.

The aftermath of the big bailouts in the 1990s is acutely controversial. The immediate criticism, which was probably overstated, was that it produced a moral hazard problem. In the view of Milton Friedman, for instance, the 1995 Mexican program produced the Asian crisis of 1997 because investors assumed a Fund guarantee. This may have been some part of investors' calculations, but they were fundamentally impressed by the idea of an "East Asian miracle" that they should buy into. There is an analogy with the development of the stock market boom in industrial countries in the late 1990s: some of it may have been driven by the idea that central banks (and in particular the Federal Reserve) would support a certain level of the market, but mostly it was driven by a vision of a "New Economy".

The real problem came from the size of the rescue operations, the strain that these brought for the IMF's resources, and the fact that as a result such operations could not be envisaged for a large number of countries simultaneously. This brought an element of intellectual

incoherence to the whole approach, that was particularly visible in the stance of the United States. Paul O'Neill as Treasury Secretary in the Bush administration repeatedly attacked the idea of "big bailouts" in principle, but then went on to advocate them very forcefully in particular cases, often in the face of resistance from other G-7 countries who wanted to interpret them as political opportunism.

There is a likelihood that as India and China continue to grow, and move toward the liberalization of the capital account, that there will be repeats of the abrupt reversals of capital movements that afflicted many or indeed most emerging markets. High growth is usually - as it was in the nineteenth century U.S., or in Korea since the 1960s - quite uneven and prone to sudden setbacks and crises of confidence. But the scale of potential reversals in India or China are so much greater than anything that the world dealt with in the 1990s that it is likely that the world financial system will become more vulnerable than at any time since 1945. The United States will be unable to isolate itself from this general financial volatility. Historically, eras of volatility have tended to tip the balance against globalization.

IV

The "globalization" view is not always popular, and seems to be subject to pendulum swings and backlashes. Some of the backlash stems from the political and social psychology inherent in globalization, and in particular in the resentments brought by changes in relative income and wealth.

The late twentieth century largely saw the victory of the globalizers: with the result that they became quite secure about the inherent strength and resilience of the system. The sort of analysis that was given by Joseph Schumpeter began to look very dated.²¹ From the perspective of the middle of the twentieth century, he had offered on the one hand a celebration of the creative achievements of a liberal capitalistic world order, but on the other the prognosis that the resentments generated would bring down the system. Anti-globalization protest in the 1990s, while widespread, was - as even its militants recognized - intellectually incoherent and diffuse. The more rational anti-globalization figures insisted that they wanted a better or more just globalization, a unification of people rather than of capitalistic interests. But both the pro-globalizers and the anti-globalizers were over-confident about the stability of the globally integrated economy.

One of the comfort blankets that modern people clutch is the idea that there was only ever one big simultaneous world depression, produced by such an odd confluence of causes as to be quite unique: the legacy of the First World War and of the financial settlement of reparations and war debt; the chaotic banking system of the largest economy of the world, the United States; and inexperience in handling monetary policy in a world that was still pining for metallic money. Since these circumstances were so unique, they can't occur again. Historians should say that this reasoning may be quite wrong.

A great deal of the historically informed literature on globalization makes the point that there were several previous eras of increased worldwide integration that came

²¹ Joseph A. Schumpeter, *Capitalism, socialism, and democracy*, New York: Harper & Brothers, 2nd edition 1947.

to a halt, and were reversed, with painful consequences. The most familiar precedent for modern globalization is that of the late nineteenth and early twentieth century, that ended definitively with the interwar Great Depression. But there were also earlier epochs of integration: the Roman empire, the economic rebound of the late fifteenth and early sixteenth centuries (the economic backdrop to the Renaissance), or the eighteenth century, in which improved technology and increased ease of communications opened the way to global empires (for Britain and France).

All of these previous globalization episodes ended, almost always with wars. Bad policies can obviously wreck individual economies in a whole range of different ways; but systemic collapse is a product of militarized conflict. Globalization as an economic phenomenon depends on the movement across state boundaries of goods, labor and capital. Security concerns produce heightened worries about all these kinds of mobility. Trade may create a dependence on imports that leads to strategic vulnerability, and one of the oldest arguments for agricultural protection was the need for autarkic self-sufficiency in case of attack. Labor flows may camouflage the movement of spies or saboteurs. Thus, for instance, First World War Britain was gripped by panic about the numbers of Germans employed in London restaurants. Finally, capital controls have often been justified on grounds of national security. One way of destabilizing politics was to try to promote financial panic, and restrictions on capital mobility might be a way of generating increased immunity to speculative attack.

There are obvious analogies in some of these past experiences to some of the threats to the economic order and to economic integration posed by the war on terror. Trade, financial flows, and labor movements are all vulnerable in

the post- September 11 world. After September 11, every part of the package that had previously produced such unprecedented economic growth in many countries - the increased flow of people, goods, and capital - now seem to contain obvious threats to security. Students and visitors from poor and especially from Islamic countries might be "sleeper" terrorists; or they might become radicalized through their experience of western liberalism, permissiveness, or the arbitrariness of the market economy. It soon became apparent that customs agencies scarcely controlled the shipment of goods any longer, and that explosives, or even ABC (atomic, biological, chemical) weapons might easily be smuggled. The free flow of capital, and complex bank transactions, might be used to launder money and to supply funding for terrorist operations.

It is natural and legitimate to suggest that all these areas should be subject to more intense controls in the face of security threats. But there is a danger of giving an absolute priority to the war against terrorism. Every sort of control also offers a possibility for abuse by people who want controls for other reasons: because skilled immigrant workers provide "unfair" competition, because too many goods are imported from cheap labor countries; or because capital movements are believed to be destabilizing, producing severe and contagious financial crises. A new debate about the security challenge offered the chance to present older demands for the protection of particular interests in a much more dramatic and compelling way. Protectionists of all sorts suddenly had a good story to tell about the harm done by international trade.

Is this the recurrent collapse of globalization and the phenomenon of war an accidental or coincidental linkage?

There are two major ways in which war undermines globalization. The first, most obvious (and the one that has been most studied), is simply the consequence of the cost of war considered in a broad sense: the problem of financing unproductive military activity, the disruption of commerce, the suspension of migration and the freezing of capital movements because of security priorities. The second is the way in which armed conflict, even when its scope is quite small, provokes the emergence of new issues that produce international disaccord that affects other areas of international interaction. In this way, war challenges assumptions about the global distribution of economic and political power.

The idea that war is costly and disrupts "normal commerce" is well understood in the classic literature of economics. Indeed, for those who experienced the wars of the American and French revolutions, how could it be otherwise? Adam Smith's first volume of the *Wealth of Nations* (1776) closes at the end of Book III with the reflection that "the ordinary revolutions of war and government easily dry up the sources of that wealth which arises from commerce alone."²² Such disruption arises most immediately and most obviously in the case of sustained and major conflict.

Most periods of modern conflict have been accompanied by inflationary war finance, and followed by sharp periods of deflation. The most obvious mechanism that made for postwar deflation is the effect of increased government expenditure on interest rates. An alternative way of thinking about this is as the destruction or wearing out of capital in wartime, and a consequently higher price of new

²² (ed.) Edwin Cannan, Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, Chicago: University of Chicago Press, 1976, I, p. 445.

capital. The rise in real long-term interest rates makes peacetime investment more expensive and depresses activity. This effect is enhanced if governments try to return to pre-war exchange rate systems with prices and wages that have been boosted and distorted by the high levels of wartime demand.

Almost all of the most dramatic historical episodes of sustained deflation followed in the aftermath of war. A sustained economic depression followed the American war of independence, and accentuated the initial anti-commercial bias of the politics of the new Republic. After the Congress of Vienna (1814-15) ended the Napoleonic wars, Europe had decades of deflation, in which industrial investment was costly and the bankruptcy of entrepreneurs frequent. The aftermath of the 1860s civil wars (or wars of unification) in Italy, Germany and the United States all included an immediate speculative bubble, and then the bursting of the bubble (after 1873), with stock market price collapses, bankruptcies and reduced investment. The First World War was also followed by a brief reconstruction boom in 1919, and then by a collapse in the major western economies in 1920-1; one decade later came the Great Depression.

Some of these classic effects in which war produces monetary instability are still very visible in the aftermath of the major international conflicts of the post-1945 era. Korea and Vietnam both produced inflationary surges, which initially reduced and then increased real interest rates, and which corresponded to investment surges and declines. The 1991 Gulf War no longer fits this pattern: both inflation and interest rates fell. It was followed by a brief recession, which is generally held by political analysts to have frustrated the reelection of President

George H.W. Bush in the 1992 election. The 1990s war was simply too small-scale and cheap to have a major macro-economic impact: and this holds true for 2003 too. If there is a threat, it arises out of long term developments in domestic spending which are characteristic of almost all industrial societies (see above).

One explanation of the changing effects of war in very recent times is obvious: the cost of each war for the major superpower has been falling since the middle of the twentieth century. In 2002 dollars, the Second World War cost the United States \$4,700 bn., Korea \$400 bn., Vietnam \$572 bn., the 1991 Gulf War \$80 bn., and the actual fighting in the Iraq war of 2003 (as opposed to the post-occupation insurgency, which is bound to be much more expensive) cost little over \$20 bn.²³ It would consequently be appropriate to expect a diminution of the purely fiscal impact of wars, and consequently of their deflationary legacy.

If we just take a naïve approach to the demand and supply for military action, falling costs should suggest increased demand and a new likelihood of the use of force to effect regime change. The less a war costs, and the fewer the casualties, both military and civilian, the more likely it becomes. The declining willingness of advanced industrial societies to use force in the second half of the twentieth century, which has been noted by many observers from Edward Luttwak to Jeremy Black,²⁴ and is sometimes attributed to the much larger political impact of casualty figures, is thus not likely to be a permanent phenomenon.

²³ Figures from "In Perspective: America's Conflicts", *New York Times*, April 20, 2003, p. B16.

²⁴ Edward Luttwak, "Toward Post-Heroic Warfare: The Obsolescence of Total War", *Foreign Affairs*, 74/3, May/June 1995; Jeremy Black, *Why wars happen*, London : Reaktion Books, 1998; Jeremy Black, *Warfare and the Western World 1882-1975*, Bloomington, IN : Indiana University Press, 2002.

Countries such as France, Britain and the United States actually showed a surprising willingness to take casualties, and to respond to calls for the need for the maintenance of order in remote parts of the world. As long as there is a clear technical military superiority, cases for a morally and politically appropriate use of force will continue to be quite powerful.

Adam Smith made a similar point about some of the wars of the eighteenth century. The combination of technology, which made war between advanced and backward countries less costly for the advanced country, and new methods of spreading the financial burden of war through the sale of debt instruments, was making war more likely. "In great empires the people who live in the capital, and in the provinces remote from the scene of action, feel, many of them, scarce any inconveniency from the war; but enjoy, at their ease, the amusement of reading in the newspapers the exploits of their own fleets and armies." ²⁵

The same conclusion can be reached by a less cynical route. During the Cold War and the period of superpower tensions, wars were held in check by a widespread realization that the cost of their escalation would be too high. But since the end of the Cold War, there has been a proliferation of international as well as of threatening domestic conflicts as states break up. Hence the need for intervention.

Some commentators have jumped already to the conclusion that it is wrong simply to think about the cost of military conflict, and that in particular the growing expense and political embarrassment of post-conflict Iraq precludes another such conflict. This reasoning is fallacious, because similar situations are highly likely to recur. We

²⁵ Smith, *Wealth of Nations*, II, pp. 455-6.

are internationally sensitive to human rights issues; and also to the potential of bad governments to destabilize whole regions. Both concerns are realistic, and I would add creditable. They will necessarily lead to military engagements in sometimes expected and sometimes unexpected places. Moreover, it is possible to envisage more attention being paid in advance to the management of post-conflict situations in a manner which in the Iraq case was made impossible by the rush of events.

V

Wars also lead to questions about the legitimacy rules that are essential in guiding economic interaction, both internationally and also domestically. All wars, big or small, produce new problems and divisions. There has been a spillover from security concerns to economics. The most obvious type arises out of the financial legacies of wars and debates about reparations and war debts. Such debates poisoned the international economy in the 1920s (as Keynes predicted in *The Economic Consequences of the Peace*). They are presently recurring in the fierce debate about whether and how and what kind of pre-war Saddam debt should be forgiven in order to help Iraq in reconstruction.

One tradition of thinking about wars (and especially of the smaller scale wars of the classical late nineteenth century era of globalization) suggests that they have economic origins, and that they are fought - especially in eras of globalization - because of a wish to control a greater share of global resources. This is familiar to historians and social scientists as the Hobson-Hilferding-

Lenin interpretation of imperialism.²⁶ It is largely wrong as an explanation of the origins of the wars, but very powerful in understanding the political response to them.

This paradox arises because of other effects of eras of globalization. New opportunities to create new wealth mean radical changes in distributions. Large and apparently illegitimate increases in fortune provoke resentments and a populist reaction. There are clear historical precedents to the current worldwide wave of reaction against and rejection of what is now perceived as U.S. style capitalism.

Martin Luther's protest against the universalism of the Renaissance world took the form of a protest against the "luxury" of long-distance and foreign trade: "But foreign trade, which brings from Calcutta and India and such places wares like costly silks, articles of gold and spices - which minister only to ostentation but serve no useful purpose, and which drain away the money of land and people - would not be permitted if we had proper government and princes."

27

The eighteenth century, in which both the French and the British East India Companies unfolded their activities to the full, spanning continents, qualifies by most measures as an era of globalization. The protests that the East India Companies excited, because of their global reach, and because of their use of low wage labor for some part of their production, have a very modern tone. Adam Smith showed how the activities of the East India Company in

²⁶ The canonical texts are: J.A. Hobson, *Imperialism: A Study*, New York: J. Pott, 1902; Rudolf Hilferding, *Das Finanzkapital*, Vienna, 1910; V.I. Lenin, *Imperialism: The Highest Stage of Capitalism*, (1916), new translation New York: International Publishers, 1939. For analyses, see David Fieldhouse, "Imperialism: An Historical revision", *Economic History Review*, 14, 1961; and Wolfgang J. Mommsen, *Imperialismstheorien*, Göttingen: Vandenhoeck und Ruprecht, 1977.

²⁷ Martin Luther, "Trade and Usury" in (ed.) Walther Brandt, *Luther's Works Vol. 45: The Christian in Society*, Philadelphia: Muhlenberg Press, 1962, pp. 245-6.

Bengal had reduced incomes and induced widespread famine.²⁸ Here were unaccountable companies, distributing luxury products which were unnecessary and which were believed by many Christian ministers to be morally pernicious. Smith concluded that: "Such exclusive companies... are nuisances in every respect; always more or less inconvenient to the countries in which they are established, and destructive to those which have the misfortune to fall under their government."²⁹ The history of the United States began with an anti-globalization revolt directed against a particular company, not the British monarchy: the dumping of tea in Boston harbor was a protest not just against taxes but against the business practices of the East India Company.

In the mother country, the outcry over the East India Company focused increasingly on what was then called "exorbitance": the disproportionate remuneration of corporate executives. Warren Hastings, the Governor General, was eventually impeached in public trial by the British parliament. In 1777 his pay had been £10,000, but he had sent home precisely this amount, and in 1778 he sent £45,000 back home to England.³⁰

The same sort of debates were repeated in the globalization phase of the late nineteenth century, where they were linked with a critique of imperialist war. The model of the imperialist war that the British liberal Hobson, and the Marxists who adapted his explanation, had in mind was the relatively short, non-total, war that characterized the era of high globalization. The Spanish-American war (1898) brought the United States into the

²⁸ See Emma Rothschild, *Economic Sentiments: Adam Smith, Condorcet and the Enlightenment*, Cambridge Mass.: Harvard University Press, 2001, pp. 27, 32, 73.

²⁹ Smith, *Wealth of Nations*, II, p. 158.

³⁰ Lucy S. Sutherland, *The East India Company in eighteenth-century politics*, Westport, CT. : Hyperion Press, 1979.

international system. It was, unlike the sustained conflicts earlier in the nineteenth century, a very unequal conflict between the world's fastest growing and largest industrial economy, and a very backward European imperial power. 274,000 U.S. soldiers were deployed, but only 379 killed. It was soon followed by another unequal conflict, the British conquest of the Boers.

Both these unequal wars were acutely controversial in domestic politics and could be interpreted as "land grabs", demands for resources that were scarce: sugar from the Caribbean, and diamonds (from the Kimberley field) and gold in southern Africa. At first the wars produced electorally successful nationalism, with the 1900 British "khaki election" producing a large Conservative and imperialist vote, and a surge of popularity for Roosevelt, who had been the hero of the 1898 war. Then there was a backlash, in which critics pointed out associations between war and personal gains of a small group of corrupt businessmen and financiers.

In Britain, Leo Chiozza Money denounced the corruption of finance. The Liberals made much of the hypocrisy of the British government's denunciation of the racial discrimination of the Boers while encouraging a massive Chinese immigration to provide labor for the development of southern Africa. They won a stunning electoral victory in 1906. The mood turned against the financiers who had bought the election of President McKinley in 1896. Roosevelt himself began to denounce "certain malefactors of great wealth" who had appropriated many of the gains produced by public action. Populists presented war and corporate scandal as going hand in hand.

These wars also made international relations significantly more tense. The Boer War was one of the quite

decisive moments in the growing breach between Britain and Germany, with the German Kaiser publicly supporting the Boers. The small conflicts thus set the stage for bigger and more global clashes, in which arguments over the distribution of spoils worsen the international climate.

At these moments, the different sides begin to see the way they do business in a contrasting way, that is quite at odds with the one world approach of the "globalization paradigm". To stay with the pre-First World War example, prominent Germans began to attack the hypocritical "commercialism" of the British hegemon. They depicted themselves as the bearer of a more heroic and more noble sort of society, in which "heroes" rather than "traders" set the tone. Those who developed this distinction, notably the economist Werner Sombart, went on to argue that German businessmen too shared in this heroic quality, because they went about business in a different way and would sacrifice short term profit for long term communal and national interest.

In order to make business conform more to a supposedly superior national model, more control is needed. There are obvious parallels in recent times to the way in which reactions against market capitalism target ethnic or religious minorities who are held to have positions of unfair or undue influence. Amy Chua has recently produced a bestseller documenting the backlashes against what she calls "market dominant ethno-national minorities": Chinese in much of Asia, Indian in southern Africa, Lebanese in West Africa, Jewish in former Soviet Republics.³¹ In none of these cases is it likely that attacks on the minority and the looting and despoliation of the minority will lead to anything

³¹ Amy Chua, *World on fire : how exporting free market democracy breeds ethnic hatred and global instability*, New York: Doubleday, 2003.

except poverty and disruption. Violent ethno-nationalism is a powerful and highly economically disruptive force, and is characteristic of periods of reaction against the globalization paradigm.

The political tensions of today go hand in hand with a revived discussion of contrasting national models of capitalism, and a new degree of skepticism about the "Anglo-Saxon model". The new mood can be linked to wider economic and political concerns. In part the European sensibility is the product of anxiety about the viability of small firms in an era of global competition. In part too, Europeans are naturally worried about the dismantling of the welfare state, and about the costs of their ageing population and the consequences of their low birth rates. This debate produces defensive images of an order that needs to be protected, and hostile visions of the outside world and its ethos. Enron has become a rallying cry of the anti-globalization movement. Business figures in Europe who tried to present themselves as advocates of an American style capitalism or of "shareholder value" such as Thomas Middelhoff or Ron Sommer or Jean-Marie Messier were now excoriated as incompetent or corrupt (which in many cases, needless to say they were). European executives were put on trial for agreeing to supposedly excessive compensation packages.

It is important to note that the attempts to formulate new visions of nationally distinctive and anti-global capitalisms are not just a product of anti-American reactions to perceptions of American capitalism bending the rules. The increased concern within the United States with increasing control and regulation - manifested notably in the 2002 Sarbanes-Oxley Act - is a part of the same reaction. But as with other initiatives, the United States

seeks to universalize the new approach, so that companies from other countries are obliged to accept the new U.S. regulatory approach if they wish to continue to do business in the United States.

* * *

The capacity of relatively small conflicts to destroy large elements of international agreement and to promote new visions of national distinctiveness obviously is a familiar theme in 2004. But it is not a new one. The danger of escalating conflict disrupting globalization has historical precedents that go back much further than the world of late nineteenth century globalization, when tensions coming out of the new imperialism led to the First World War. Two remarkable and contrasting books were published in 1776, the year of the signing of the American declaration of independence.

The first volume of Edward Gibbon's classic study of *The Decline and Fall of the Roman Empire* was (by chance) published at the same time as Adam Smith's *Wealth of Nations* to work out a completely new basis for democracy and participation in a world which in his eyes lacked consensus and community. Gibbon's advice and Smith's concern about war destroying commerce looks immediately relevant today, and quite alarming. Both Smith and Gibbon were thinking, in the wake of the humiliation of a global British commercial and military system, about the problems of what might be termed a reverse of globalization.

Gibbon begins with praise for the peaceful character of the Emperor Augustus, and of Roman realism and multilateralism: "Inclined to peace by his temper and situation, it was easy for him to discover that Rome, in her

present exalted situation, had much less to hope than to fear from the chance of arms; and that, in the prosecution of remote wars, the undertaking became every day more difficult, the event more doubtful, the possession more precarious, and less beneficial." This is a fine description of the attractions and perils of economic prosperity. However much the Emperor Augustus realized the pointlessness of distant wars, he actually did not have much choice. The wars were created out of the instability that inevitably swirls around success, or at least around successful imperial systems. Rome might have basked in consumer prosperity, but was sucked into and ultimately destroyed by a world of conflict. Gibbon even gave a neat account of the north European response to Roman power: "The forests and morasses of Germany were filled with a hardy race of barbarians who ... though, on the first attack, they seemed to yield to the weight of Roman power, they soon, by a signal act of despair, regained their independence, and reminded Augustus of the vicissitude of fortune."³² The "globalization thesis" turned into the vision of imperialism that needed to be rebuffed and fought.

There are many signs that we are at the beginning of a new era, in which the "globalization thesis" is being rolled back once more. In the new world, differences become important. Business leaders focus on the way they have "traditionally" done business. Individuals see risks coming from the outside rather than opportunities. Citizens detect corruption. Countries are willing to fight trade and currency wars, and to resist external interventions in corporate affairs. Political leaders focus on redesigning the trading and monetary system in order to alter the

³² Edward Gibbon, *The Decline and Fall of the Roman Empire*, New York: Modern Library edition (n.d.), pp. 1-2.

balance of political and economic power. In this world, conflict tends to escalate, and destroys the basis of prosperity and international order. Its inhabitants think about Mars, nor Mercury.