States, Politics, and Globalization: Why Institutions Still Matter

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It is almost impossible to open a newspaper today and not see a story about "globalization." Although the term means many things, scholars often use it to refer to sharp increases since the mid-1970s in trade, production, and capital flows across national borders due to tariff liberalization, reductions in capital controls, and dramatic improvements in telecommunications and transportation. Many of them argue that the pressures of globalization are forcing nation-states either to reduce taxes, spending, budget deficits, and regulatory control of their economies or to pay the consequences in terms of higher unemployment, rising interest rates, lower rates of economic growth, and the like. Politicians often invoke this argument to justify such policies, claiming that their hands are tied to do otherwise by the overwhelming pressures of globalization. States, it would seem, have become weakened significantly by globalization. In the vocabulary of state theory, they have lost much of their autonomy from the influences of capital and have experienced a decline in their capacities to manage their economies. These arguments also suggest that economic globalization is leading to a tribal convergence not only in policy, but also in the political and economic institutions of advanced capitalist countries. That is,
institutions create incentives for policymakers to maintain the status quo with regard to tax, welfare, regulatory, and other policies rather than succumb to the incentives for neoliberal reform that stem from globalization pressures. These criticisms constitute an institutional thesis with which I am largely sympathetic. However, I argue in this chapter that there is still some truth to the globalization thesis and that the truth needs to be more carefully distinguished from the fiction. Furthermore, although politics and political institutions do mediate how states and economic actors respond to global pressures when they occur, critics of the globalization thesis have not systematically specified the full range of mechanisms or processes by which this mediation occurs. This chapter does that and, as a result, fills an important gap in the literature.

The argument proceeds as follows. First, I review evidence that indicates that the extent of economic globalization has been exaggerated as have its effects, particularly the rise of neoliberal state policies. In other words, neither state autonomy nor state capacities, respectively, have been eroded nearly as much as the globalization thesis suggests. Second, I suggest briefly why the economic globalization thesis has been overstated and argue that some of the problem lies in the fact that its proponents neglect the importance of national political and institutional differences among countries. Third, I identify seven important mechanisms whereby states respond to globalization in important ways—all of which suggest that states are far from being incapacitated in the face of global economic pressure. Finally, I conclude with some reflections on whether the globalization thesis might eventually be vindicated and why it has remained such an accepted part of our political discourse despite its shortcomings.

HOW EXTENSIVE IS ECONOMIC GLOBALIZATION?

Central to the globalization thesis is the claim that international trade has expanded dramatically among the advanced capitalist countries during the last few decades. Indeed, figure 9.1 shows that since 1960 in the seventeen richest OECD countries, average exports and imports as a percentage of GDP, a standard measure of a national economy's openness to international trade, increased from 24 percent to 30 percent. Yet it is difficult to see this as an overwhelming force, particularly given the fact that between 1974 and 1993 these figures remained virtually constant. Instead, it appears that the increase in international trade occurred prior to 1973, at least insofar as the OECD is concerned. If we take a longer and more encompassing view, we find that although international trade increased substantially in absolute terms during the twentieth century, in relative terms it rose only slightly. In 1913, 13 percent of all world economic activity involved international trade—a figure that remained the century's high water mark until it was surpassed in the mid-1990s, reaching 17 percent in 1996. In other words, by the mid-1990s about 83 percent of the world's economic activity was still domestically based.

Two additional points about trade require brief mention. First, by 1995 roughly 97 percent of world trade was among the developed countries—the so-called triad region of North America, Western Europe, and Japan—and represented only a very slight increase since 1980. This may seem remarkable insofar as the emerging Asian economies contributed increasingly to international trade during this period, but this effect was offset by declines in trade from the Middle East, Africa, Eastern Europe, and the former Soviet Union. Second, there is significant variation across advanced countries in how open their economies are and, thus,
how vulnerable they might be to the pressures stemming from global trade. For example, between 1960 and 1994, exports and imports as a percentage of GDP increased in the Netherlands from 42 percent to 53 percent, in France from 14 percent to 22 percent, and in the United States from 3 percent to 11 percent. Of course, many of the smaller OECD economies have been much more open than the larger ones for a long time. This makes sense as the larger economies have much larger domestic markets within which their companies can operate, so there may be less incentive to tap international markets. The point is that these differences show little sign of change.

Another global factor alleged to be weakening states and precipitating policy convergence is the tendency for companies to shift their investments in production and marketing capacity to other countries. Indeed, figure 9.2 shows that foreign direct investment (FDI), that is, the money firms spend buying shares in foreign companies, building plants abroad, and merging with foreign firms, has increased sharply since 1985 and certainly much faster than trade. Of this, 75 percent of the total accumulated stock and 60 percent of the flow of FDI were concentrated in the three region regions. In other words, the vast bulk of FDI remained within the advanced capitalist countries. Despite the increase, however, FDI remained only a small fraction of total firm investment during this period. Even for firms in smaller, more open economies, which typically have the highest rates of FDI, this amounted to only about 20 percent of total firm investment. Given the fact that most investment remained in firms' home countries, one must wonder how much of an effect rising FDI really had on states. Furthermore, while it is true that companies can exert power over states to grant favorable tax treatment, trade protection, and the like when they are deciding where to invest internationally, once the decision is made the host country gains considerable power in future bargaining because it is often hard for firms to pull out once they have made their investments, so the threat of capital flight diminishes.

Perhaps the clearest indicator of increasing global economic activity is international portfolio investment, that is, foreign investment in equities, bonds, currencies, and the like, especially insofar as these investments are more liquid and potentially volatile than FDI. In fact, figure 9.3 shows that international portfolio investment grew much faster than FDI during the 1980s and early 1990s. In 1993, these investments were three times larger than FDI. Nevertheless, domestic investment remained the norm, at least insofar as stocks and bonds were concerned. Investors still preferred to keep almost all of their investments at home, even though the possibility for international investing increased as barriers to overseas participation were lifted. For example, foreign participation in stock markets increased during the 1980s but remained quite small. Foreign listings on the New York Stock Exchange increased from 2.5 percent to 5.4 percent of total listings; on the London Stock Exchange, from 13 percent to 22 percent; and on the Tokyo Stock Exchange, from 1 percent to 7 percent. Notably, even though the most dramatic increase in international listings occurred on the Tokyo exchange, the volume of trade in foreign securities there remained quite modest.

In sum, although the world economy has become more open, at least since World War II, it is less internationally integrated than often suggested by the globalization thesis. Domestic markets remain the location for most firms' production and capital investments as well as for global portfolio investment. Most international economic activity, notably...

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Footnotes:
3. Hirst and Thompson, Globalization, 63.
trade and FDI, is located among the advanced capitalist countries but even here there is considerable cross-national variation. Some aspects of economic activity have become more globally oriented than others. The point of all this is rather simple. Economic globalization has not been so extensive as to obliterate the autonomy of states from international economic forces. Because globalization is not as pervasive and ubiquitous as often assumed, it should not be surprising if its effects on state capacities are also less pronounced than often claimed.

WHAT EFFECTS HAS GLOBALIZATION HAD ON STATE POLICIES?

Many observers have bemoaned the fact that globalization has increased the possibility for capital to flee to countries where it can enjoy the most favorable investment conditions, notably low tax rates. In turn, these countries have claimed that this would cause states to compete in order to attract capital by lowering tax rates, thus precipitating a “race to the bottom,” the result of which would be an international convergence on relatively low tax rates. Generally speaking, this has not happened. Figure 9.4 reveals that taxes as a percentage of GDP increased steadily between 1960 and 1993 among OECD countries. The same is true specifically for taxes on business, where most of the increase stemmed from higher employers’ social security taxes although corporate income taxes increased slightly as well. There is also little evidence for a convergence in business taxes. For example, business taxes in the Scandinavian social democracies rose most dramatically, from about 4 percent to 10 percent of GDP between 1965 and 1995, while taxes in more neoliberal countries, such as the United States and Britain, increased from about 5 percent to 10 percent. If anything, movement has been away from convergence. Why? Some have argued that this occurred where in exchange for higher business taxes social democratic governments were more likely to increase spending on education, research and development, and the like. Because business benefited from this spending, it was willing to help pay for it through higher taxes. Others have noted that higher rates of taxation fund spending for programs that contribute to political stability—another collective good that business values and is
willing to help support, especially during a time when greater international market integration may threaten the economic security among broader segments of society. In sum, business may be willing to support policies whereby states socialize some of the risks that would otherwise prevent them from investing.12

Globalization is also said to trigger a convergent race to the bottom in government spending. Lower taxes mean that governments will eventually have to reduce expenditures in order to maintain some semblance of fiscal responsibility, or pay the price through higher interest rates and inflation. But OECD social expenditures increased between 1960 and the early 1990s, although the rate of increase declined since 1980 (see fig. 9.4). The globalization thesis also suggests that capital is supposed to move in search of not only cheap labor, but also a lower social wage, including social security, unemployment benefits, and various transfer payments, the costs of which business helps cover through taxes. Thus, even if overall government expenditures remain steady or even rise, we should at least see states cutting these social programs in order to attract investment and mitigate capital flight. Instead, Figure 9.5 shows that OECD social welfare transfers increased from 1960 to 1997, and figure 9.6 indicates that, although countries that often had social democratic governments spent more than their Christian democratic or liberal counterparts, the trend held for all three types of governments at least through 1986, the most recent year for which I have data. But were these countries punished for their fiscal behavior? First, budget deficits in most OECD countries increased during the early 1990s, and where they did, countries tended to incur slightly higher real long-term interest rates, as globalization theorists predict. Still, it is important to note that governments with higher levels of spending were no more likely to experience increased deficits than countries with lower levels of spending.13 Second, the OECD also tended toward lower, not higher, rates of inflation.14 Third, there is little evidence that higher levels of spending, taxation, or budget deficits caused capital to flee to other countries.15 Fourth, there is much evidence that higher taxing or spending, typical for social democratic and Christian democratic governments, undermined economic growth.16 Fifth, the literature is unclear regarding whether social democratic and Christian democratic governments are any more prone to unemployment than neoliberal ones, although it does appear that disinvestment causes unemployment to increase.17 In sum, the evidence is again far from overwhelming in its sup-

12 Carret, Partisan Politics: Carret, “Global Markets.”
13 See Linda Scott, The Myth of the Powerless State (Ithaca: Cornell University Press, 1994). It is not to say that Scandinavian firms were completely enthralled with all forms of state spending. Indeed, in Sweden there was a strong backlash against many welfare state policies that business believed had sparked inflation. See Mark M. Blinder, “The Transformation of the Swedish Model: Economic Ideas, Distributional Conflict and Institutional Change,” ms., Department of Political Science, Johns Hopkins University, 1999. However, these were likely to be Swedish programs rather than those that benefited business directly, such as business subsidies that increased during the 1980s and early 1990s. See Kenworthy, “Globalization,” 63. However, in some countries, such as Denmark, business has actually been quite supportive of social programs. See Elke Svenje and Carsten Jo Martin, “Employer’s and the Welfare State: The Political Economic Organization of Firms and Social Policy in Contemporary Capitalist Democracies,” Comparative Political Studies 34, 8(2001): 889–925.
14 It is worth noting that within the OECD the country that has undertaken the most dramatic reduction in social spending has been the United States, the most closed economy (except for Japan) in terms of trade and, thus, the country for which globalization theorists might have been least likely to expect such cuts. See Fuglesang, The Architectures of Markets, chap. 9.
15 Carret, Partisan Politics, chap. 6.
17 Carret, “Global Markets.”
1971 a tendency for governments to grant their central banks more autonomy to set interest rates and regulate the money supply in order to better control inflation and defend currencies in the face of increasingly mobile international capital and currency speculation—a trend that has removed monetary policy from national politics and led to generally more austere monetary policy. However, this appears to have been matched with important changes in bankruptcy law whereby governments eventually recognized that stringent monetary policy increased the possibilities of recession, business failure, and unemployment, so, out of concern for the political ramifications, many governments revised their bankruptcy laws to facilitate corporate reorganization rather than liquidation. In other words, neoliberal deregulation in monetary policy was counterbalanced with non-neoliberal deregulation in bankruptcy policy.

Moreover, initial efforts to deregulate many economies turned out quite differently in the end. Often reforms were implemented by policymakers and bureaucrats who struggled over the specifics of reform and managed to shape them according to their institutionally and organizationally defined interests. The Japanese telecommunications industry is a good example. According to Steven Vogel, the Japanese had long believed in a strong managerial role for government in the economy, and, as a result, the state had developed institutional capacities to structure markets and guide industrial development. But in 1980, motivated in part by the example of U.S. deregulation a decade earlier, the legislature started to talk about liberalizing the use of telephone lines, and in 1984 it privatized the national telecommunications carrier, Nippon Telegraph and Telephone Public Corporation (NTT). Neoliberal deregulation appeared to have arrived. However, the Ministry of Posts and Telecommunications used this as an opportunity to enhance its role as protector and promoter of the industry and thus reassert the state’s control over the industry albeit in a new form. Previously, the ministry enjoyed only limited supervisory control over NTT, but as privatization proceeded it played a key role helping to craft legislation that left it with extensive capacities to regulate prices and the introduction of new services—a maneuver that elevated it to a position of power and prominence among Japan’s state ministries, including the mighty Ministry of International Trade and Industry. Reform ended up conforming less to some neoliberal ideal and more to the institutional tractions (cognitive, normal...

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Figure 9.6. Average OECD social welfare payments. “Social welfare payments” include social security, consumption payments (in-kind benefits such as health and education), and transfer payments (cash benefits such as income support and unemployment benefits). Source: Adapted from John Stephens, Evelyn Huber, and Leonard Kyri, “The Welfare State in Hard Times,” in Kirscheit et al., eds., Continuity and Change.

There is also always the possibility that national governments will invoke trade sanctions when they perceive that other countries are engaged in "unfair" economic practices. For years the United States refused to extend most-favored nation status to China in order to force the Chinese to change their labor and human rights policies, and the United States is now considering trade sanctions against the Japanese for hunting whales. As these examples illustrate, one very important reason why the forces of globalization ebb and flow is that states actually have some control over them. Rather than suffering the consequences of globalization, states may actively contribute to globalization itself. Indeed, T. V. Paul argues in chapter 5 in this volume that the advanced capitalist states in general and the United States in particular have contributed to the rise of globalization in many ways.

Second, the globalization thesis neglects the importance of institutional legacies and how they mediate international pressures with important effects. Vogel has shown that differences in normative and cognitive understandings among policymakers and state bureaucrats led to important variations in the manner in which regulatory reforms were implemented in Britain, Japan, and several other advanced capitalist countries. More formal institutional arrangements also mediated how these reforms proceeded. He explains that because Britain's constitution tends to concentrate policy control in the executive branch, Margaret Thatcher had an easier time pursuing a more draconian deregulatory program than Ronald Reagan did in the United States, where constitutional provisions fragmented control between Congress and the executive branch, thus muting reform. For similar reasons, neoliberal tax cuts were more sustained in Britain during the 1980s than in the United States, where the deep cuts advocated by the president and passed by Congress in 1981 were partially restored a year later after various interest groups, including some members of the business community, who enjoyed relatively easy institutional access to policymakers, convinced them that the cuts had triggered budget deficit problems. Indeed, political-institutional factors continued to reinforce differences in national economic experiences.


See especially Sotschel et al., "Convergence."

Vogel, *Challenge*, 181.
tax policies and the amount of revenues states collected throughout the OECD. Finally, national politics exert similar effects. For example, once established, social programs tend to develop constituencies over time who will defend them if they come under siege. In the United States, when social security became a budget-cutting target during the 1980s, the American Association of Retired Persons, one of the most powerful lobbying organizations in Washington, successfully repelled the attack. The effort to cut old-age pensions was more successful in Britain because the pension system was more fragmented institutionally, consisting of both universal flat-rate and means-tested components, so opposition to retrenchment was divided. Similarly, labor unions, which have been organized differently throughout Europe and developed different collective identities, reacted in unique ways to the efforts of employers and governments to shift labor-management relations in a neoliberal direction due to globalization pressures. Swedish unions, for instance, focused their attention, albeit unsuccessfully, on defending the central wage bargain; German unions sought to protect wages and the length of the work week; Italian unions struggled to preserve cost-of-living increases; and U.S. unions wanted to control benefits from shop-floor or relations. The degree to which unions were successful varied in each case, but labor politics played a key role in shaping whether globalization resulted in neoliberalism or not. Of course, as Brad Smith notes in chapter 10 in this volume, states were also culpable in all of this insofar as they helped shape and sustain various industrial relations systems.

Lastly, even though some members of the business community sought neoliberal responses to the pressures of globalization, others did not. German employers associations were deeply divided about dismantling co-determination practices. In particular, large firms wanted to preserve neocorporatist wage bargaining in order to keep wage conflicts out of the cooperative shop-floor relations they had historically kept with workers and that they believed were crucial for maintaining the kind of flexibility in production that was still required to compete internationally. So far they have managed to defend against the neoliberal alternatives that small and medium-sized firms have advocated. On the same note, during the last thirty years when employers were organized collectively, such as through national employers associations, they tended to support, not attack, social spending programs in the OECD countries. This was probably because they saw these policies as contributing to human capital development, helping to cultivate trust with workers and the general public, and facilitating a well-functioning economy in other ways.

To digress briefly, not only can domestic interests help preserve corporatist and other institutionalized forms of bargaining, they may sometimes create pressure to expand or build these institutions anew. For instance, Brendan O'Leary in chapter 2 in this volume suggests that domestic conflicts over nationalism may lead to the development of consociational bargaining. The implication is that this and other sorts of domestic pressure may act as a countervailing to whatever global pressures there may be to move away from such institutions.

Certainly the relationship between institutional legacies and politics is an important one insofar as national-level institutions help organize politics and thus the degree to which political opposition emerges and prevents neoliberal reforms from proceeding when proponents of the globalization thesis advocate them. As a result, neglecting these political-institutional effects obscures the mechanisms that determine how national actors respond to the pressures of globalization when they arise or are otherwise invoked. But can we be more specific about what these mechanisms are?

SEVEN MECHANISMS THAT MEDIATE THE EFFECTS OF GLOBALIZATION

Several scholars on both the left and right have argued that nations are increasingly incapacitated or hollowed out as a result of their inability to cope with the globalization of economic activity and, thus, are forced to pursue neoliberal policies. Others have disagreed. How:

- Swank and Martin, "Employers."
- Crozier and Streake, eds., Political Economy of Modern Capitalism, Jespers, "Future".
- Other, "Roads, Race, Work of Nations."
- Peter L. Hall, "Organized Market Economies and Unemployment in Europe: Is It
ever the evidence suggests that states respond to shifting international economic pressures in various ways that often prevent them from being incoordinated by neoliberal currents. To begin with, states can block pressures for neoliberalism for long periods of time. Scandinavia is a case in point where states have persistently maintained high levels of business taxation and government spending. Others have shown that states with strong unions and social democratic governments have held out against the neoliberal juggernaut, sometimes even managing to strengthen traditional social democratic policies as they provide the security and stability businesses seek in the face of rising international economic competition and risk. Of course, the ability of states to block pressures for neoliberalism is not restricted to the OECD. A cogent argument can be made that the institutions of the Soviet command economy buffered the Soviet Union from the vicissitudes of the international economy for decades. Notably, the state monopoly on foreign trade and the administrative command system of central planning long protected key industries, such as energy, from fluctuations in international prices. Even after several of the largest energy companies were privatized after the fall of the communist regime, high-ranking state officials retained control over the post-Soviet energy sector, continued to block neoliberal reforms and the development of efficient energy markets, and perpetuated much of the centralized, bureaucratic management of the Soviet era, including its institutional legacy of inefficiency and corruption. Indeed, political and institutional legacies die hard, and as a result, may block neoliberal reform even when it may be desirable.

States can also translate neoliberalism into their own long-standing institutions without abandoning them entirely. In Denmark, pressures of international competition led policymakers to search for ways to incorporate neoliberal principles into traditional Danish institutions where economic policy was the product of elaborate negotiations between the state and private actors. Rather than abandoning industrial policy

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Vogl, P. Markets.

See Francesco Dentu, Emerging Europe: Nation States within the Common Market (Albany State University of New York Press, 1999). Scholars have noted that the same sort of multinational economic relations that occur in the global diffusion of neoliberalism in the post-Maastricht era is inextricably linked to the identity and economic policies of nation states. See Yaron Soysal, Limits of Citizenship (Chicago: University of Chicago Press, 1994).

international pressure, political elites do not automatically respond with neoliberalism; political and institutional arrangements help determine whether neoliberalism proceeds or retreats. Sometimes even if states choose not to reverse neoliberal reform, they may compensate for it in other ways. This is essentially what occurred when states eased bankruptcy law and made corporate reorganization a more likely option than liquidation when it became clear that relinquishing control over monetary policy to central banks increased business failures. Compensation may be at work elsewhere as well. Scholars often point to the comparatively low rate of unemployment in the United States during the 1990s as evidence of how successful a country can be if it accepts neoliberal reforms. Indeed, the United States did initiate several such reforms during the 1980s, notably tight monetary policy but they led to two recessions before unemployment dropped to historic lows in the mid-1990s. Meanwhile, however, rates of incarceration skyrocketed, increasing 300 percent since 1980, reaching rates five to six times greater than in Western Europe and, as a result, lowering unemployment statistics significantly by reducing the pool of available labor in the first place. This should not be surprising because those more likely to be jailed in the United States were also those most likely to be unemployed during economic downturns, that is, poor, uneducated, or of color. In effect, incarceration served as an insidious form of labor-market policy and was, therefore, a major deviation from neoliberalism, that compensated albeit unintentionally for the otherwise deleterious effects of neoliberalism.

Similarly, even when states lose some capacities they may be able to build new ones. For instance, Christopher Hood argues in chapter 8, this volume that although increased international capital mobility may pose problems for the capacity of states to extract revenue by traditional means, states may develop new capacities, such as leasing state assets, shifting tax burdens to domestic industries, and imposing new taxes on the Internet economy. Furthermore, Gregorres Ekiert shows in chapter 11 that an important way the postcommunist Polish state coped with pressures for neoliberalism was to build new state capacities by shifting power to the prime minister, creating a professional civil service, it creating the number of public sector employees, and raising—not lowering—the level of revenue extraction and social expenditures.

Much of the preceding discussion draws attention to the important ways in which institutions affect how states deal with the pressures of globalization. Indeed, warnings about the neoliberal juggernaut are exaggerated in part because they neglect the stickiness or path-dependence
of institutional legacies. However, states can also utilize quite self-consciously existing institutional arrangements to cope with these pressures. In this sense institutions “enable” political elites by affording them unique opportunities for action. Peter Hall has argued that advanced capitalist political economies assume a variety of institutional forms, each with its own “comparative institutional advantages” when it comes to dealing with increased international economic competition. For instance, so-called liberal market economies (LME), such as the United States, are adept institutionally at rapidly moving capital, labor, and other resources among firms and across sectors, thus facilitating radical and successful product innovation, as has been the case in biotechnology, computers, and software. Among other things, this is because labor unions are weak, corporate managers enjoy unilateral decision-making power, and capital markets favor shareholder interests and short-term profitability. On the other hand, organized market economies (OME), including Germany and some of the smaller West European countries, are better situated institutionally for maintaining high product quality, flexible production, and more incremental kinds of innovation in industries like machine tools. This is because unions are strong and under labor market agreements are guaranteed a role in cooperative decision making with managers and finance capital takes a more long-term view of profitability because stakeholders rather than shareholder interests receive top priority.

Hall’s point is that in addition to cutting costs to cope with globalization, countries can compete effectively by utilizing their comparative institutional advantages. Indeed, this is precisely why some German industrialists have fought to preserve rather than scrap co-determination and corporatist wage bargaining, and why Scandinavian capitalism may have been willing to continue paying high taxes for substantial government spending. Certainly in the area of technology development, perhaps one of the most important issues as global competition is concerned, differences in institutional arrangements offer policymakers both advantages and disadvantages upon which they can capitalize if they recognize them. Whether they recognize them and react effectively is another question, particularly insofar as the ideology of globalism and neoliberalism is so pervasive. In any case, these sorts of institutional differences are another important reason why there has been no more convergence toward the neoliberal norm.

This discussion underscores one final, but very important institutional mechanism: institutions play a key role in actors’ preference formation and may do so in ways that do not support neoliberalism. Two examples will suffice. First, as noted above, one reason why German firms persist in defending the institutions of social partnership is that they perceive that it is in their interests to do so. However, this was not always the case. Indeed, it was only after the government enacted co-determination legislation over the objections of business and firms were forced to live with it for awhile that they began to appreciate the benefits such institutions might afford them—the sort of efficiencies often neglected in neoliberal rhetoric. Second, one reason why central employer associations tend to support social spending is that associations see the potential benefits and try to educate their members about them, thereby transforming members’ perceptions of their interests. Of course, sometimes institutions affect preferences in surprising ways. Minxin Pei argues in chapter 12 in this volume that decentralizing state capacities may create incentives that undermine political and economic efficiency—an outcome quite the opposite from that predicted by neoliberalism. He shows that in China the decentralization of revenue ex

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tration created principle-agent problems that precipitated tax evasion, corruption, and thus revenue loss for the state.

CONCLUSION

I have argued that nationally specific institutions mediate the degree to which the pressures of globalization result in an erosion of state capacities within the advanced capitalist world and that there are seven mechanisms that are responsible for this mediation. Some of these mechanisms are well known in the literature, but some are not. In particular, relatively little attention has been paid to how bits and pieces of the neoliberal model are translated into local contexts or how states compensate for neoliberal reforms in one policy area with non-neoliberal reform in another. We would do well to specify more clearly the processes involved. For instance, it would be useful to know why some parts of the neoliberal model are selected for translation while others are not, and how these decisions are made. Similarly, one wonders how decisions are made whereby policy adjustments are made in one area to compensate for those made in others, or whether compensatory actions are more unintentional than deliberate.

Much of the literature advocating an institutional critique of the globalization thesis focuses on how the formal aspects of institutions, such as the arrangement of bureaucratic and regulatory agencies, are important in all of this. Much less attention has been devoted to how the normative and cognitive aspects of political institutions come into play. This is surprising because there is a substantial literature arguing that a common set of normative prescriptions and cognitive assumptions have diffused among nation-states and are exerting pressure for convergence in political practices (see note 3 above). I support the idea that nationally specific normative and cognitive factors are important but suggest, following others in this volume who recognize how persistent and powerful national identities can be, that normative and cognitive factors also operate in ways that contribute to the resilience of national policy differences despite globalization pressures. In this regard, I see less convergence in norms and cognition across countries than those who adopt the strict diffusion perspective. Indeed, I have provided examples above, such as the adoption of neoliberal reforms in Japan, which indicate how important these factors may be. Certainly one reason why the Danes decentralized, rather than jettisoned, their corporatist policy-making institutions was that these institutions have become so much a part of Danish political culture and so taken-for-granted at the

appropriate way of conducting policy making that it was virtually unthinkable for Danish policymakers to fully dismantle them.¹⁰

Let me raise three last issues by way of conclusion. First, the identification of these mechanisms is important because it helps explain why state capacities have not been eroded to the extent of the globalization thesis predicts. Many states remain quite capable of taxing, spending, and regulating economic activity within their borders. Indeed, when the circumstances that states face change, they are often flexible enough to transform their instruments and activities in ways that preserve their strength. Of course, this is not to say that states will necessarily act in ways that benefit their economies. Institutional legacies and politics are a double-edged sword. Thanks to them, political elites may mislead situations, make mistakes, or simply respond too slowly (or too rapidly) to situations in ways that cause more harm than good.¹¹ In the long run, this may even contribute to their own incapacitation and hollowing out if their tax base crumbles, inflation rises, productivity lags, unemployment grows, and political turmoil and electoral backlash ensues. However, the point is that none of this is as inevitable as the globalization thesis suggests, precisely because institutions and politics matter in the ways suggested earlier.
grams, and other far more institutionally specific factors because they see them as being more important for their competitive success than cheap labor inputs. The computer and software industries are especially pertinent examples." (2) It assumes that the financial markets and multinational firms care about the same thing when deciding where to invest when, in fact, the former are concerned principally with government budget deficits rather than levels of spending, taxing, and regulation per se, and the latter do not appear especially obsessed with any of this. (3) It assumes that states are passive recipients of globalization pressures when, in reality, they are often able to wield significant power over them. (4) It assumes that states are unwilling to suffer the costs of whatever punishments the financial markets and firms dispense when, as it turns out, they may be willing to tolerate some castigation, at least insofar as interest rates are concerned, if it makes them to ensure the economic security of the citizenry. To the extent that these assumptions remain flawed, there is good reason to suspect that neoliberal convergence is not likely and that states will retain considerable capacities for managing their economies no matter how long we wait.

Finally, if the evidence favoring the globalization thesis is so flimsy, why does it continue to attract so much attention and be taken for granted as the truth? This is a complicated question, well beyond the scope of this chapter, but a few thoughts are in order. The idea of globalization has been used by conservatives to create an ideological climate that suggests that government interventions are futile and could even hurt national economic competitiveness. Some leftists have also accepted the globalization thesis and used it as justification for various socialist projects. Furthermore, arguments about globalization are simple so they appeal to policymakers as well as business leaders some justification for making decisions that are unpopular with the general public. Indeed, in 1993 the Clinton administration invoked the pressures of globalization to legitimize painful spending cuts that it claimed were necessary to reduce federal budget deficits. Of course, the globalization thesis also provides scholars with exciting subject matter that sells books. The point is that the globalization thesis is politically and perhaps intellectually expedient; not only does it constitute a cognitive paradigm that constrains how people view the world, but it can be used as a frame for legitimizing a variety of activities and interests. Until we think more carefully about the relationships between international economic activity and national-level institutions and politics, its power will remain unchecked.