UNIVERSIDAD DE CHILE
FAC. DE CIENCIAS FÍSICAS Y MATEMÁTICAS
Ingeniería Industrial

IN75A Analysis of the Global Economy

Patricio Meller

Magíster en Gestión para la Globalización

ECONOMIC RATIONALE OF GLOBALIZATION

1. Pre – GL $\Rightarrow$ Y close C: Geographic Clustering

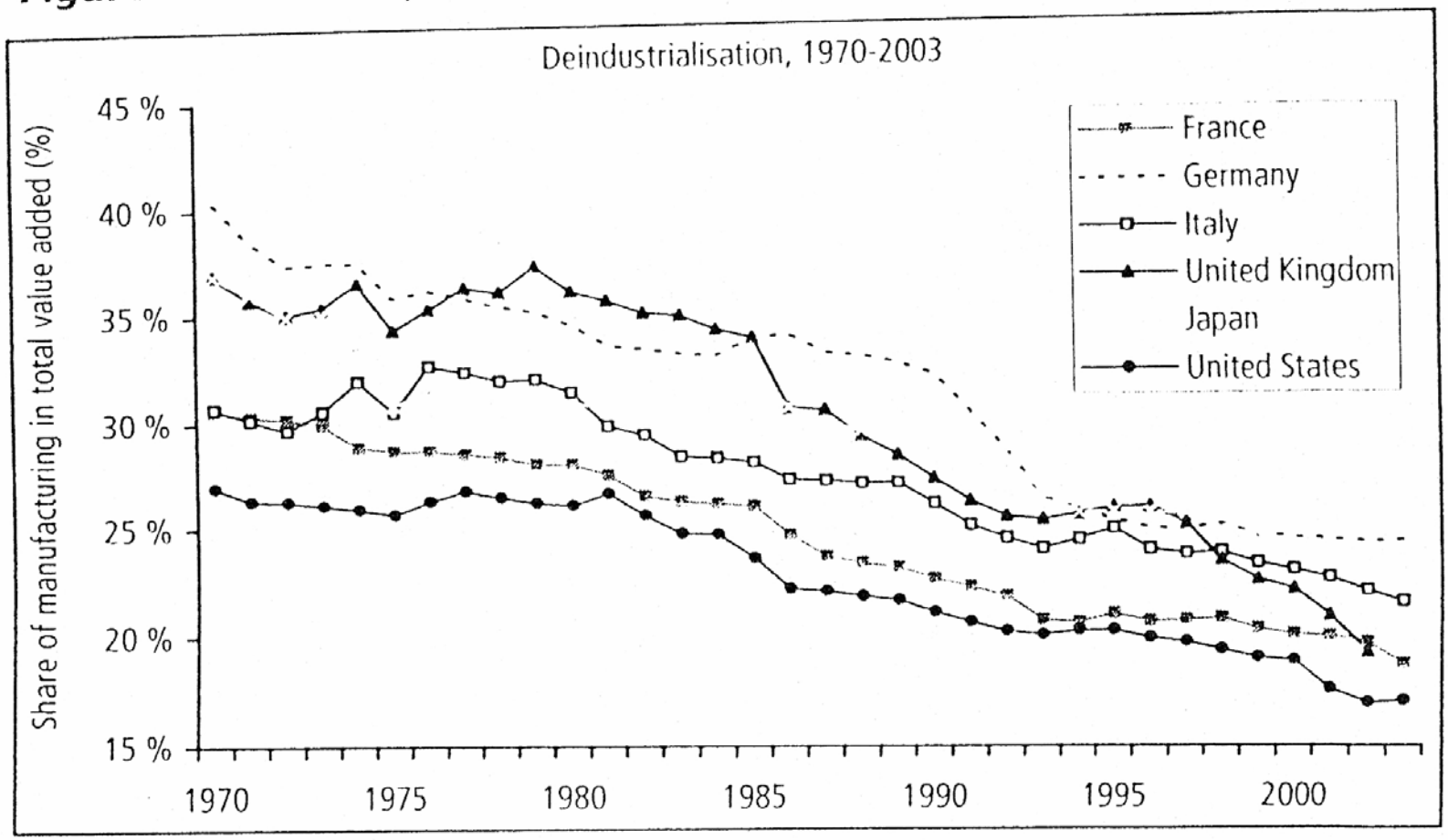
2. $\downarrow$ Cost moving goods/people/ideas: **GL1**
   $\Rightarrow$ Separation production/consumption

3. g take-off & geographic clustering
   - learning spillovers are localized geographically
   - spatial clustering of industry processes:
     - innovation - τ progress - g

4. 1st g take-off: Europe XIX – XX

5. 2nd g take-off: Japan – Asia XX
   generates de-industrialization in DC

Figure 1 Industry as share of GDP, large OECD nations, 1970–2003.



CHARACTERISTICS OF GL1

1. GL works at level of firms/sectors
2. Production stages - spatially clustered in a single factory
3. Spatial bundling: L, K, τ

   Big factories (vertical integration)
4. GL $\Rightarrow \uparrow$ trade $\Rightarrow \uparrow$ competition

   DC most competitive sectors: High τ, HK^+, K^+

   DC least competitive sectors: unskilled L intensive
5. Opposite situation for LDC
6. Policies for GL $\Rightarrow$ - upgrading skills of workers

   - $\uparrow$ HK
7. GL $\Rightarrow$ (DC) clear pictures

   losers: sectors (L^+)

   losers: workers (L^+)

CHARACTERISTICS OF GL2

1. Separation of production stages

2. Rationale for GL2: - ↑ DC / LDC Y_n/w gap
   - ↓ costs: TIC – air shipping
   Ex. Maquiladoras - U.S./Mexico; South-East Asia - Japan

3. Triangular Trade: Japan (Hi-tech, design)
   China (Production)
   U.S. (Consumption)

4. Task - previously considered non-tradable become traded –
   due to ↓ TIC costs. Ex. USA call centers move to India

5. GL trade now affects one stage of a firm

6. Implication - winners / losers of GL are not related to:
   sector / firm / skill HK ⇒ ∃ **unpredictability**

7. Policy Implication: ↑HK will not work
   Children: important to learn how to learn

8. Everything will become tradable?

Figure 6 The first and second unbundling schematically.

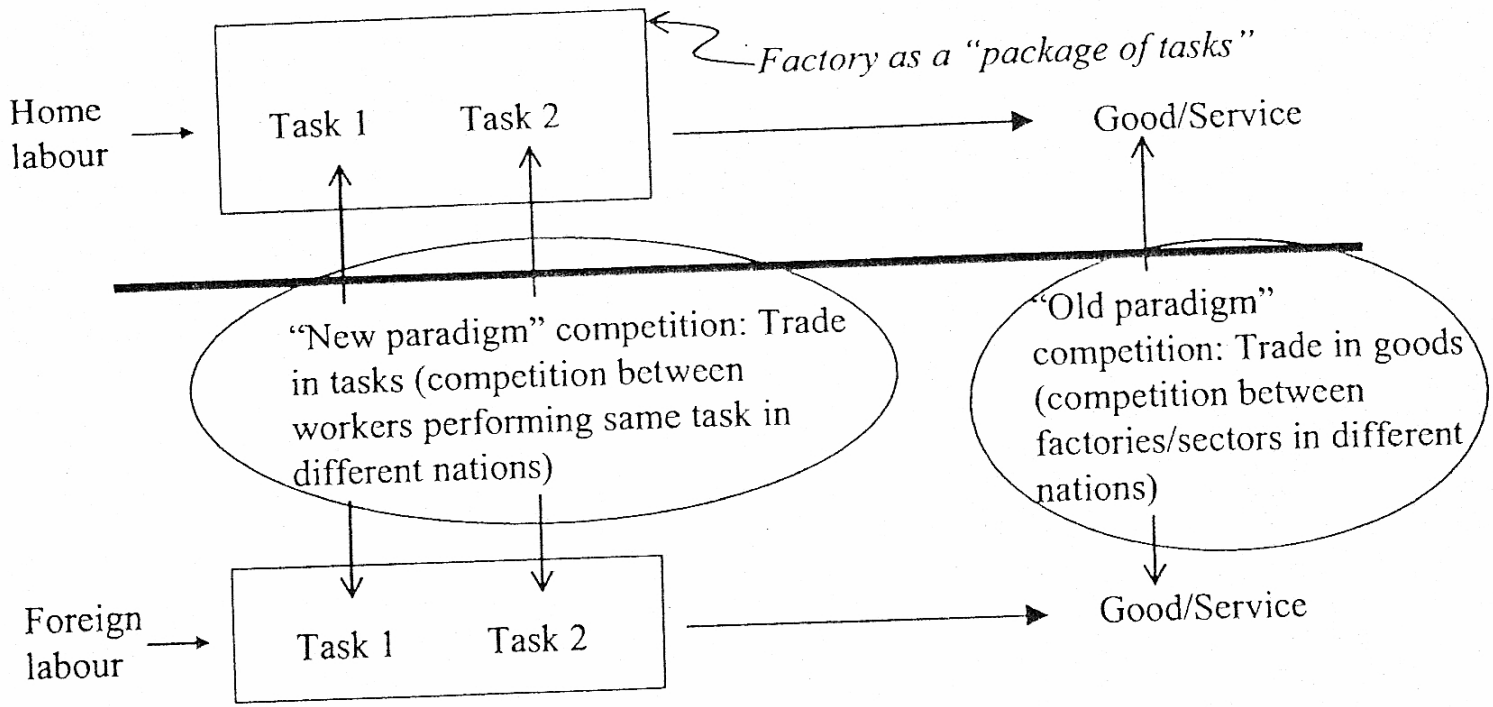
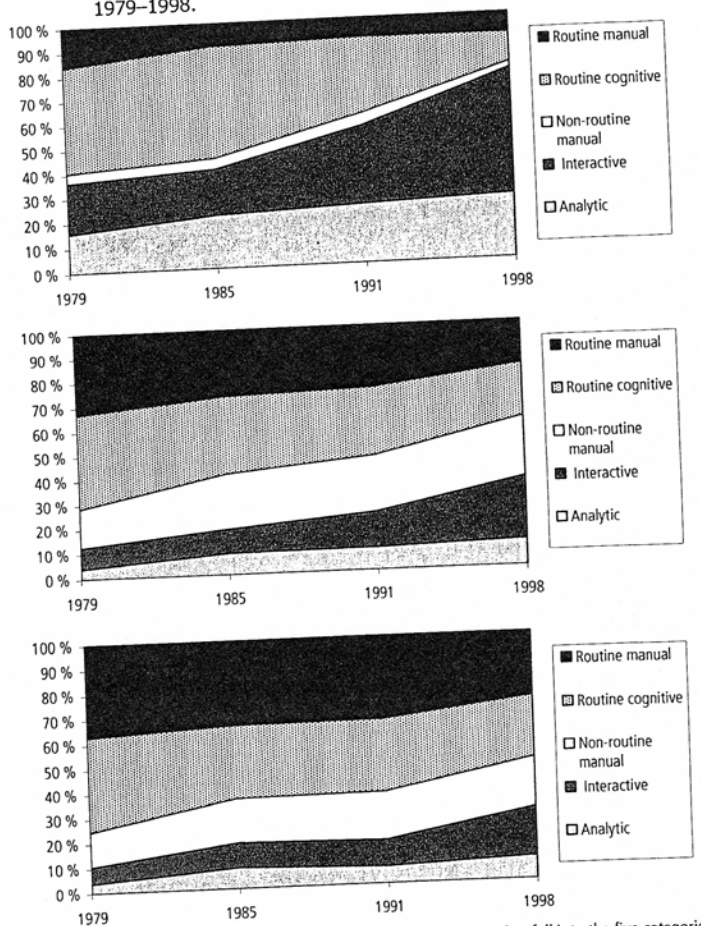


Figure 4 Share of tasks by type for high-skilled (top), medium-skilled (middle) and low-skilled (bottom) workers in West Germany 1979–1998.



Note: the numbers show the share of all the tasks an employee performs that fall into the five categories of tasks, so apart from rounding issues, each row sums to 100. The survey behind this did not ask employees about the amount of time they spent on each task.

Source: Spitz (2004). Table 6.

Unpredictability – High Risk Society

A. <u>Black Perceptions</u>

1. Economic insecurity - fact or life for: - every worker
   - every firm
2. Government – abandoning its traditional role
   as ultimate guarantor of security: firms / workers
3. No one can assume that today's job will still $\exists$ five years from now
4. Few parents can guarantee their children's future

B. <u>Why is the present world $\neq$ from the past?</u>

1. High uncertainty & unrestricted competition $\Rightarrow \downarrow \neq$ real economy & MK
   Rules governing Wall St. - now will apply to entire economy
2. Implication - Taking chances is now essential
   Low risk strategy $\Rightarrow$ mediocrity & stagnation
3. Factors generating high risk in GL:
   Trade, τ, corporate restructuring, deregulation
4. These four factors generate destructive creation
   & generate the high risk society.

Historical Perspective

1. Old View: High g $\Rightarrow$ goods news for all T_j

   Low g $\Rightarrow$ bad news & more uncertainty

2. In the past - when insecurity / uncertainty were present **solution was: g**

3. Now - GL2 - same factors generating g generate uncertainty

   High g & high uncertainty come together

4. In the high risk society:

   No product, no skill, no innovation is unique

   Ex. Indian Software producing engineers

   DC have affiliates in LDC

Figure 2-1

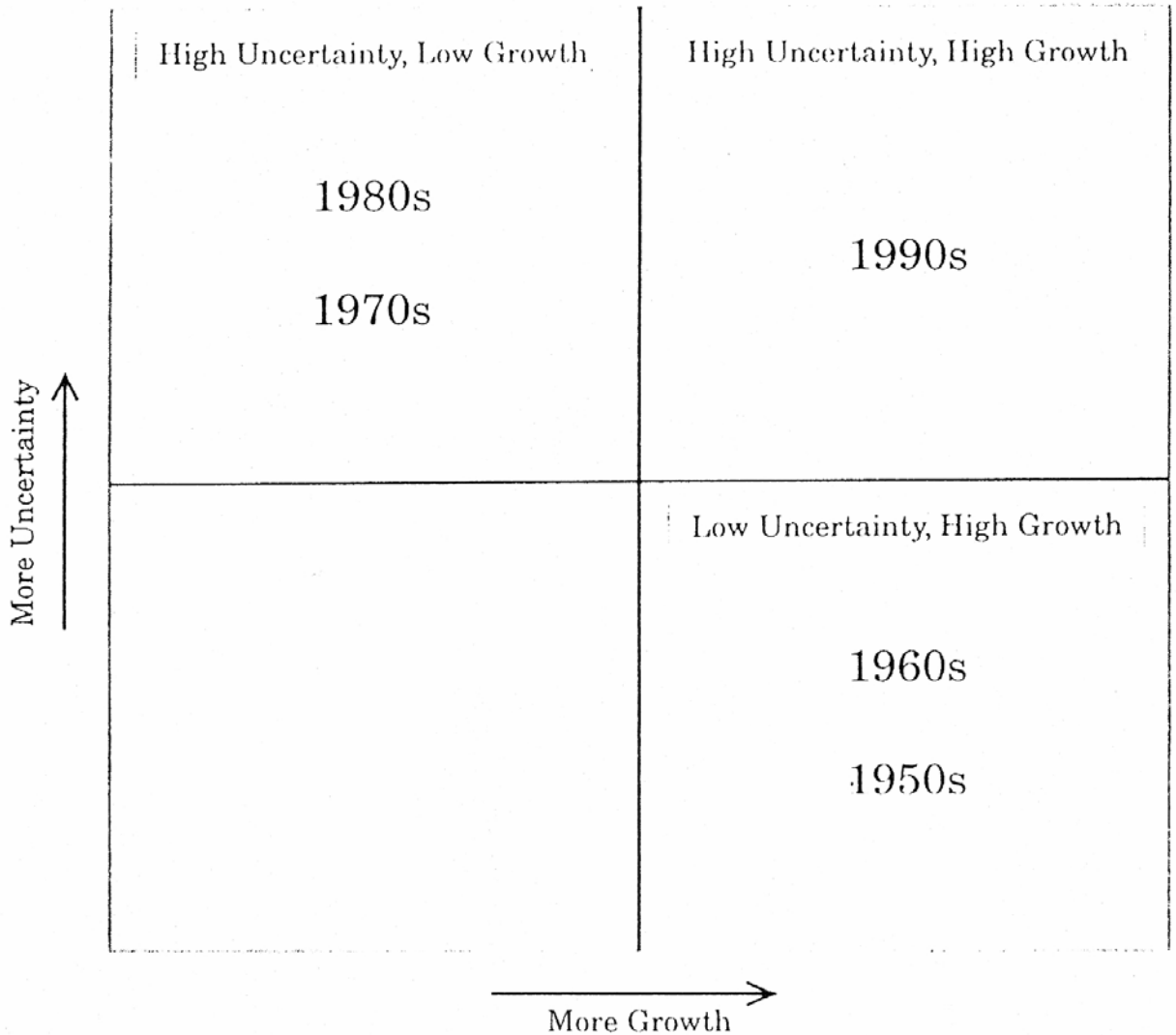
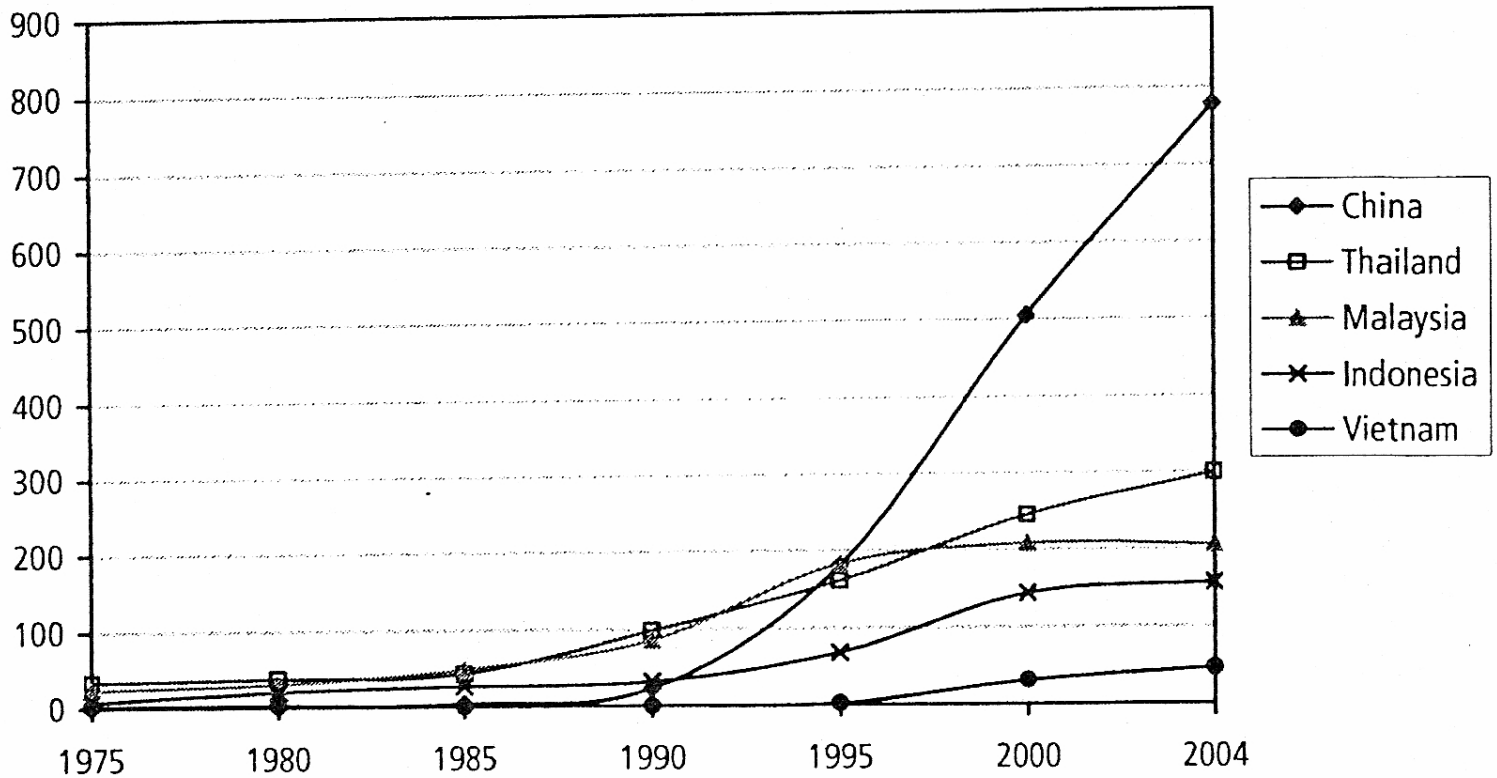

High Uncertainty, Low Growth
1980s
1970s
High Uncertainty, High Growth
1990s
Low Uncertainty, High Growth
1960s
1950s
More Uncertainty
More Growth

Figure 5 Placement of Japanese automobile and electronics plants in East Asia, 1975–2004.



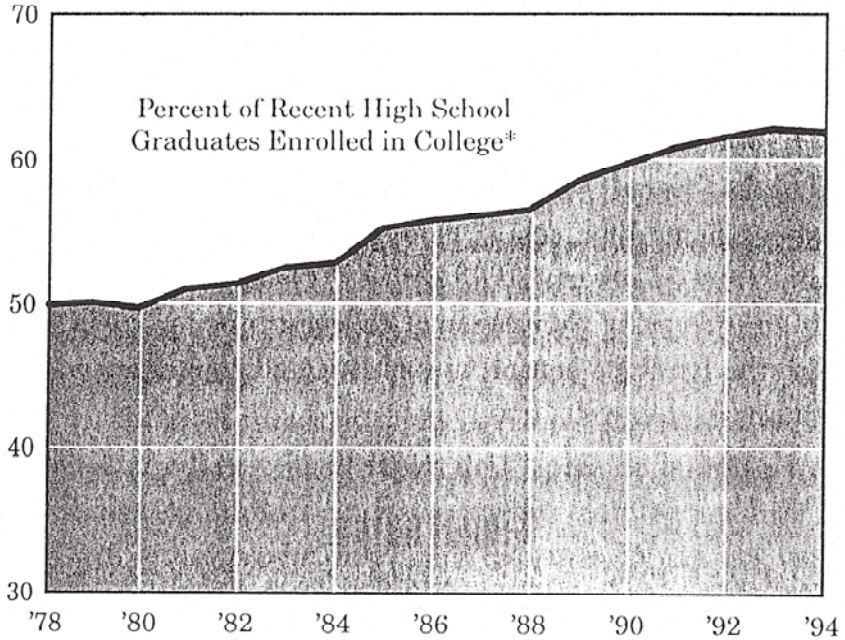
Source: Baldwin (2006), Figure 2.

Behavior in a High Risk Society (M_K)

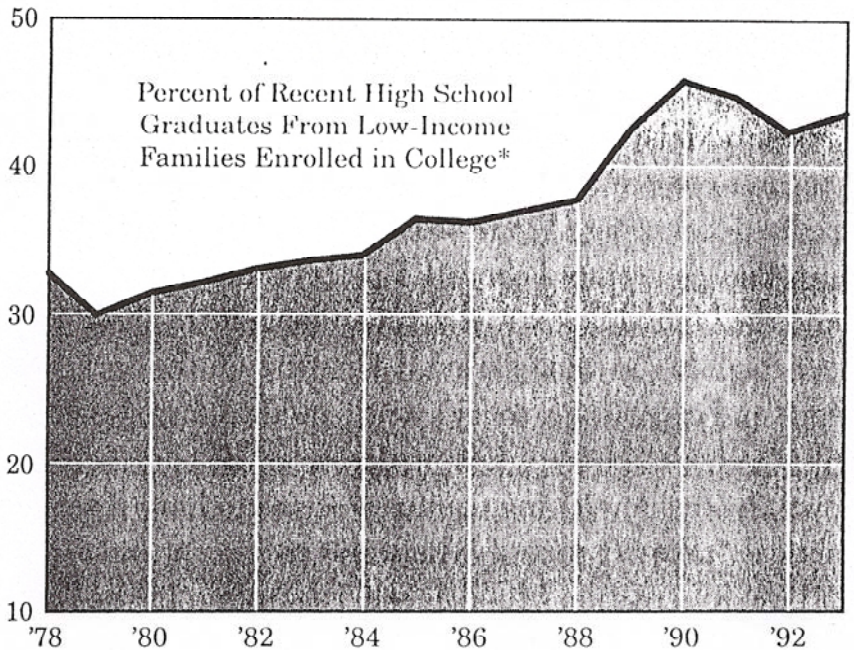
1. Rapid reaction to profit opportunities
   - IF is the key input - Use new IF quick
   - $\exists$ rapid imitation of new products
     good ideas, new products are copied quicker than before
2. $\exists$ risk - return trade-off
   In M_K - risk associated with I - it is as important as r
   High (low) risk I $\Leftrightarrow$ High (low) r
3. $\exists$ risk-r trade off $\Rightarrow$ you know what you can (cannot) control
4. Payment of high r - for high risk: Not possible to pick winners/losers
   No one knows in t_0 – winner in t_1
5. Perfect M_K are unpredictable – not due to lack IF
   M_K are unpredictable because everyone has same IF
   No one has lasting competitive advantage
   Value of new IF quickly disappears

Figure 3-5

A Flood of Human Capital: More Young People Are Going to College...



...Including From Poorer Families

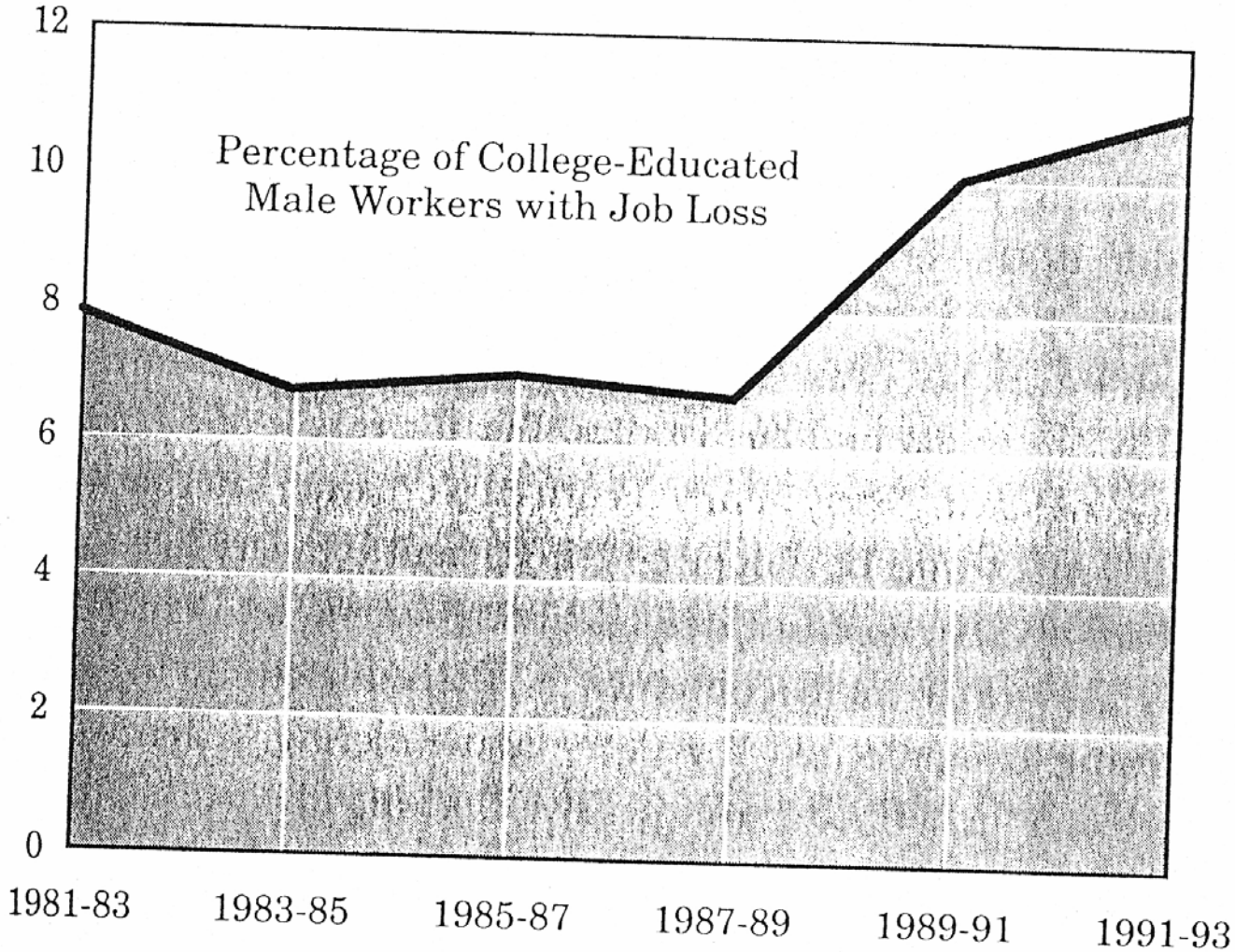


*Three-year moving average

Data: Education Dept.; Bureau of Labor Statistics

Figure 3-1

More Insecurity for the College-Educated



Data: Henry Farber, Princeton University; Bureau of Labor Statistics

6. In M_K – do not trust experts or historical patterns

   History repeat itself in M_K, but in an infinitely surprising variety of ways

7. IF is always useful

   Private IF - has value – but short advantage

   Public IF - built in into risk-r trade-off

Uncertainty in GL Trade

1. ↑ trade is >0 for a country
2. However, costs of uncertainty could outweigh potentials gains from trade

   Ex. ∃ 50 people

   Each one gets US$1.000

   Except for one - chosen at random - who will have to pay US$20.000

   The class wins US$29.000 - but one person loses US$20.000

   If each person - agrees to give US$408, the loser could be compensated

   Analogy to a country

3. USA (K^+) - what would be more convenient for X:

   a) - Consumer electronics - K_+

   - Movies - L_+

   b) Moreover - Hollywood film production much more expensive than India/France

   c) What are Hollywood advantages?

Table 5-1

A Hierarchy of Trade Risks

GOODS-PRODUCING INDUSTRIES		
Manufacturing (except printing and publishing)	Wide open to trade	HIGH TRADE-RELATED RISKS, HIGH TRADE-RELATED RETURNS
Agriculture		
Mining		
INFORMATION-ORIENTED INDUSTRIES		
Printing and publishing		
Communications		
Finance (except real estate)		
Business services		
Entertainment	Rising exposure to trade	
Legal services		
Consulting, architectural and engineering services		
Higher education		
Nonconventional retailing (catalog, home shopping, Internet)		
SERVICE-ORIENTED INDUSTRIES		
Utilities and transportation (except communication)	Insulated from trade	LOW TRADE-RELATED RISKS, LOW TRADE-RELATED RETURNS
Retail and wholesale trade (except as listed above)		
Real estate		
Health care		
Elementary and secondary education		
Hotels		
Personal services (such as beauty parlors)		
Other services		

Table 4-1

Strategies for the High-Risk Society

HIGH-RISK, HIGH-RETURN STRATEGIES	LOW-RISK, LOW-RETURN STRATEGIES
WORKERS	
Take a job exposed to the global marketplace	Take a job insulated from foreign competition
Take a job in a high-tech industry	Take a job in a low-tech industry
Earn advanced degree	Stop with a college education
Work as a consultant or a sub-contractor	Find salaried employment
Work for a reengineered company	Work for a stable company
Start a business with employees	Start a business without employees
Invest retirement funds in the stock market	Invest retirement funds in money market or bond funds
COMPANIES	
Expand into global markets	Focus on protected domestic markets
Be an early adopter of new technology	Wait until new technologies are well established
Reengineer to improve productivity and cut costs	Maintain organizational stability
Adopt workplace reforms	Keep traditional forms of workplace organization
Enter a deregulated industry	Stay away from the turmoil of deregulation
COUNTRIES	
Adopt a free-trade policy	Preserve protectionism
Open the door to immigration	Keep tight limits on immigration
Initiate deregulation and privatization	Continue the traditional regulation
Allow recessions to run their course	Use fiscal and monetary policy to smooth out the business cycle