GLOBALIZATION AFTER THE FINANCIAL CRISIS

JORDI CANALS

General Director of the IESE (University of Navarra), Professor of Economics and Business Administration at the IESE, and Doctor of Economic Sciences and Business Administration (University of Barcelona), Jordi Canals has received Honorary Masters and Doctoral Prizes. He was a Post-Doctoral Research Fellow at Harvard University, Visiting Scholar at the World Bank and International Monetary Fund, and Guest Scholar at The Brookings Institution (Washington, D.C.). As well as a Fulbright Scholar and founding member of the European Shadow Financial Regulatory Committee, member of the Commission to Foster Market Transparency and Security (Aldama Commission), and board member of the European Institute for Advanced Studies in Management (Brussels), the Graduate Management Admission Council (GMAC), the European Corporate Governance Institute, and EQUIS (European accreditation agency). He has published a variety of texts on economics, finance, corporate government, and business administration, including: En busca del equilibrio. Consejos de Administración y alta dirección en el gobierno de la empresa (Pearson, 2008), Managing Corporate Growth (Oxford University Press, 2000), Universal Banking: Theoretical Perspectives and International Comparisons (Oxford University Press, 1997), La internacionalización de la empresa (McGraw-Hill, 1994), and Competitive Strategies in European Banking (Oxford University Press, 1993).
INTRODUCTION

In the Richard T. Ely Lecture, “Globalization and its Challenges,” given at the annual meeting of the American Economic Association on January 3, 2003, Stanley Fischer ended his defense of globalization with the following words: “The pro-market pro-globalization approach is the worst economic policy, except for all the others that have been tried (Fischer 2003).”

Globalization as a social and economic phenomenon is nothing new. Historians speak of the first globalization, which took place between 1870 and 1914, and the second globalization, which stretches from the end of the Second World War to the present (Williamson 2002). The first globalization failed when war broke out in Europe in 1914. In light of the enthusiasm shown for the globalization process, Keynes (1919, 9–10) turned an admiring eye on the growing economic integration before the outbreak of the Great War, considering it positive and natural. He pointed out that “a person of that period considered this state of the world, an increasingly integrated economy, something normal, certain and permanent except in its possibility to improve. And any deviation from this tendency seemed aberrant, scandalous, and avoidable. The projects and politics of militarism and imperialism, of racial or cultural rivalries, of monopolies, restrictions, and exclusions that played the role of serpents in paradise were no more than distractions in the newspapers and they seemed to have no influence whatsoever on ordinary economic and social life, whose institutionalization seemed complete in practice.”

In other words, Keynes looked admiringly on the normalcy that surrounded the process of international economic integration. Following the First World War, however, he was surprised by the scant attention citizens in general and politicians in particular had paid in previous years to the possible effects that certain emerging social phenomena could have on globalization, including the possibility of stopping that process altogether.

Nowadays, almost a century after Keynes’s observations from 1919, and to the favorable interpretation of globalization offered, among others, by Wolf himself (2004) and Baghwati (2004). The first globalization failed because of a set of erroneous policies that led European nations into two world wars. The second globalization, however, runs the risk of failing due to the collapse of a deficiently regulated international financial system that has developed on the basis of free market, deregulation, and free capital flow between countries. Globalization does not depend solely on the financial system but in a modern economy the latter acts as a nervous system, so a dysfunctional financial system can lead to the collapse of much of the world’s economy, as we saw in the summer of 2007.

In the present article, we wish to reflect on a central question: will the financial crisis stop the globalization process, or at least change its rate? In other words, can the globalization process survive the consequences of the current financial crisis? Before we pose this question, let us begin with an earlier one: is globalization the principle or indirect cause of the financial crisis?

Before we go any farther, we should point out that economic globalization is only part of the broader social phenomenon of globalization. By economic globalization we mean the growing international integration of countries through commercial flows, capital flows, flows of direct investment, technology transfers, and
the movement of workers. Globalization also has social, human, cultural, and political dimensions beyond the strictly economical ones. In that sense, from a sociological perspective, Roberson (1992, 8) explains that globalization “refers both to the compression of the world and the intensification of consciousness of the world as a whole.” Guillén (2001, 236) defines “globalization as a process leading to greater interdependence and mutual awareness (reflexivity) among economic, political, and social units in the world, and among actors in general.” The weight of economic variables on globalization is considerable, but it is not the only one. In fact, protectionist policies and deficient international financial coordination following the First World War are what halted the process of economic globalization. It is also important to note that for the international economy and for business, globalization is not a finished process, but rather, a developing one. When some companies commit the error of thinking in terms of a completely globalized world, the number of mistaken decisions multiplies.1

It is interesting to observe that what is slowing globalization today is the financial crisis. Protectionism may also contribute to its deceleration, but it is worth remembering that the coordination of economic policies can contribute to the recovery of the world economy and to insuring that economic integration does not stop. Moreover, it is important to emphasize that economic globalization should not be considered a permanent state, but rather a fluid one, whose rate can accelerate or decelerate. Therefore, when we refer to the effects of the crisis on economic globalization, we must limit ourselves to reflecting on possible changes in the rate or manner in which this process occurs.

The present article is structured as follows: in the next section we will make some notes on the impact of globalization on the triggering and propagation of the financial crisis. Then we will analyze the effects of the financial crisis on the globalization process. Finally, we will offer some reflections on the impact of the crisis on the globalization of companies.

GLOBALIZATION AND THE UNLEASHING OF THE FINANCIAL CRISIS

One of the characteristics of the current financial crisis is that it has been worldwide right from the start. The crisis had been brewing for months, but an important outbreak began on August 9, 2007 when the American Home Mortgage Investment Co. announced its incapacity to meet its financial obligations with regard to funds guaranteed by “sub-prime” mortgages. A week later, it declared bankruptcy. The event was preceded in July 2007 by various warnings issued by credit rating agencies about the growing risk of financial assets guaranteed by mortgage instruments. In late July some agencies lowered the ratings of “sub-prime” mortgage bonds. The collapse of stock exchanges and capital markets was immediate. Liquidity suddenly became the financial system’s most coveted value. And yet, what seemed to be a problem originating in a very specific segment of the United States’ financial markets immediately became a global problem.

The United States’ strong foreign investment in recent years, fostered by economic growth, good investment opportunities, and a flexible legal regime, was directly driven by countries with an enormous balance of payments surplus, such as Germany and China. This increased the exposure of international investors to the risks of the US market. The imbalances were fed by the United States’ voracity, its shrinking internal saving rate was financed with foreign capital that led to an enormous current accounts deficit. International financial imbalances cushioned by a highly global financial system transformed a US financial crisis into a global one.

Consequently, financial integration among countries facilitated the rapid international transmission of the crisis.2 The United States’ financial necessities have driven financial innovation, capturing capital from all over the world. In particular, numerous financial entities from other countries that acquired US financial assets linked to sub-prime mortgages with the expectation of high profits have had to face an important drop in their market value as the effects of the crisis unfold. This obliges them to recognize their losses, restructure their balance, and limit credit growth. Those investors not only seek profits unavailable in their own countries—due in part to a lesser development of their financial systems (see Caballero, Fahri, and Gourinchas 2008)—they also seek a greater diversification of their investment portfolios. The safety that the United States offers international investors reinforced that tendency. Therefore, investments by banks and international insurance companies in financial products issued by American institutions have worsened the crisis’s international dimension.

The phenomenon of international financial investment reveals the flip side of financial glo-
The growing liberalization of foreign investment, especially China’s access to the World Trade Organization, have fostered a process of economic growth in China that rests on a very competitive industrial base and a slightly under-priced currency. China’s efficient manufacturing and logistic complex has driven the growth of industrial exports, making China the world’s largest factory. The growing liberalization of foreign investment in China has further strengthened this country’s role as a manufacturing base. Industrial outsourcing in the United States and Europe driven by the search for lower costs and greater productive efficiency have made it possible for China to achieve this power as an exporting country. And the fact that other countries have outsourced industrial enterprises to China and other emerging countries increases their need to import. Once again, growing economic interdependence underlies the foreign imbalances of countries that have also contributed to the triggering of the current financial crisis.

Voracious spending in the United States has been temporarily sated by the austerity and weak domestic demand of Germany and China. While economic globalization has allowed the United States to rapidly absorb the surplus savings of those countries, the crisis has brought out the fact that it is not possible to construct a stable global economy, nor a balanced globalization process, on the basis of such fundamental imbalances in the foreign accounts of the large economies.

Therefore, economic globalization has played a central role in the international transmission of the crisis. Until spring 2008, the disconnection of emerging economies, mainly China and India, was hypothesized, positing that they might be immune to declining economic activity in the United States and Europe. The reality, however, has been less flexible, and the crisis has also affected those countries, and even more so, other economies in Latin America, Africa, and Asia.

Various mechanisms have transmitted the crisis to those emerging countries. The first is the global liquidity crisis, which has also affected financial entities—some of which have high levels of debt in international markets—and investors in those countries. Suddenly, numerous banks found themselves with growing liquidity problems and losses in portfolios with investments in US financial assets. The liquidity problems rapidly led to credit restrictions and rising long-term interest rates, with the expected effects on consumption, investment, and economic activity.

A second transmission mechanism was the panic that gripped foreign investors in emerging countries during the spring and summer of 2008. That panic led to spectacular drops in those countries’ stock indexes. According to data from the BIS (2009), after good performance following the crisis in summer of 2007, the MSCI indicator of stock prices on emerging markets fell 28% in local currency between May and September 2008—even before the fall of Lehman Brothers. On the other hand, the S&P 500 index fell only 12% during the same period. Between September 15 and October 30, 2008, that same MSCI index fell another 40% (see BIP 2009). The realization that the possible disconnection of emerging economies had only been wishful thinking led to the withdrawal of funds from those countries’ markets, contributing to posterior drops in the process of financial assets, with the corresponding wealth effect and a considerable increase in uncertainty.

Consequently, the same circuits that had fostered economic and financial integration in recent years were now used by the investors that had driven that process to divest, and the market mechanisms that had transferred the effects of a crisis in the US financial market to the global market also traveled along those same circuits. Economic globalization cannot be considered the main cause of the current financial crisis, but it is true that greater international economic and financial integration have made the worldwide transmission of the crisis’s effects faster and more intense. What can be seen as the positive side of globalization in one context—international trade flows and investment in emerging countries—could, in a moment of panic, turn into an accelerator of financial crises, giving greater impetus to their international transmission and planetary impact.
the convenience of reducing the global level of debt by financial and non-financial companies with regard to total resources, the need to improve regulations and supervision, the suitability of mechanisms for managing risk or the convenience of economic incentives related to the volume of transactions and their short-term results. Moreover, doubts about the efficacy of the financial system have also been cast on the actual functioning of market economies and, indirectly, on the future of economic globalization. Are the words about globalization and the policies that promote them, which Fischer uttered at the end of his Richard T. Ely Lecture in January 2003, still valid today?

In the following pages, we will try to argue that the development of the globalization process can be stopped or shifted, although, as forms of economic organization go, the free-market economy continues to be the least-bad choice. Still, its functioning could clearly be improved, as the current crisis has shown. The market is not an absolute criterion and long-term progress depends not only on the existence of dynamic, free and open markets, but also on a prudent and efficient presence of the public sector, which is needed to correct negative spillovers generated by markets. Nevertheless, the economic globalization process has a somewhat different rationale than the market economy. When the free market is proposed beyond national borders, there are not only cultural and linguistic barriers, but also economic, political, and legal barriers to contend with, and some of them are of very considerable size. In that sense, the economic globalization process could stop because it is an option, a choice, and as such, it could be reversed by the policies adopted at each moment.

To examine this question, it might be useful to consider that in recent decades the economic globalization process has manifested mainly in a significant increase in trade and financial flows. At different moments, this process has been driven with differing strength and rates by four main motors: public policies, the expansion of international companies, the dominant values and ideas in public policies and society, and technology. Of these four, technology has not been directly affected by the economic crisis, so we will not consider it here, concentrating instead on public policies, dominant values, and companies. Below, we will analyze the leading external indicators of the globalization process, and will then analyze the three motors mentioned above.

EFFECTS OF THE CRISIS ON INTERNATIONAL ECONOMIC ACTIVITY

TRADE FLOWS

The economic deceleration caused by the recent implosion of the global financial system has led to an abrupt fall in international trade. Restrictions on credit to companies—including credit to companies’ circulating capital—have also made that drop even more intense. Moreover, this reduction in economic activity has provoked a significant excess in the capacity of some sectors of the economy and a consequent increase in unemployment. Over the last twelve months, the automotive industry in Europe and the United States has experienced the largest drop in sales in various decades. Other sectors, including steel or capital goods, have experienced equally serious drops.

Consequently, the financial crisis has not only prompted a global economic recession, it has also brought out some of the weaknesses and structural risks of economic globalization: greater dependence on international trade, greater exposure of domestic industry to excesses of capacity when economic activity drops abruptly, and indirectly, an incorrect but latent and manifest perception in the most advanced economies that globalization has weakened their countries due to outsourcing of industrial activities. Once again, the deindustrialization of countries like Great Britain is lamented when, in recent years, the shift to a tertiary economy had begun to seem natural and almost desirable.

Dropping demand and increased unemployment efficiently spur new calls for economic protectionism. Until now, the governments of countries with the greatest economic weight have resisted the temptations of protectionism rather well. But this battle can never be definitively won: the entire world’s prosperity, and especially that of the most needy countries, depends on the existence of open goods and services markets that allow them to export their products to the most advanced markets. Neither China nor Brazil, among others, would have been able to so significantly reduce poverty in the last twenty years had they not been able to freely enter the richest countries’ markets.

Nevertheless, while trade flows parry the thrust of protectionism, commercial interdependence among countries can also help to more rapidly propagate economic recovery. Emerging countries are also major clients of companies in the most advanced countries. If the latter increase their
exports it will improve economic growth, the need to import capital goods or sophisticated intermediate goods and also investments in public infrastructure. All of these tendencies are good news for multinational corporations. Consequently, just as commercial interdependence has worsened the international repercussions of the crisis, it also means the possible recovery by the most relevant economic countries will have a more rapid effect on the world economy. We can thus see that, as a process, globalization can have a variety of effects on the world economy, and they are not always foreseeable or predetermined.

**CAPITAL FLOWS**
The impact of the financial crisis on capital flows has been direct, immediate and enormous. First, the liquidity problems that initially affected US banks and investors rapidly affected all countries belonging to the international economy. Liquidity problems quickly turned into credit restrictions, which especially affected those companies with the highest debt levels.

In spring 2008, a growing perception that liquidity problems could be long-lasting and could possibly turn into problems of solvency provoked a flight of capital from emerging markets to more developed economies. According to BIS data presented earlier, the MSCI indicator of share prices on emerging markets dropped 28% in local currency between May and September of 2008—even before the fall of Lehman Brothers—while the S&P 500 index fell only 12% over the same period. This may be because the unstoppable liquidity crisis of the first months of 2008 turned into a financial panic at the possible collapse of the world banking system, leading investors to opt for US Treasury debt rather than assets on emerging markets.

Direct investments in emerging countries also dropped drastically as a result of growing uncertainty about global demand and demand in the countries receiving those investments, as well as the credit restrictions of investment firms in their countries of origin and the fact that investments in emerging countries became less attractive with the changing economic scenario.

The recent restructuring of the banking sector, mainly in the United States and Great Britain, is provoking a greater concentration—as banks in crisis are absorbed by more solid banks—as well as a reduction in size of some of the major banks with international operations. In this case, two phenomena converge. First, strict indications by US financial regulators that banks in receipt of public recovery aid must improve the efficiency of their operations. And second, that in numerous banks, the restructuring of international operations is a clear field for improvement. In the case of European banks, such as those in England, Holland, and Germany, the smaller number of international operations is the result of an explicit decision by the top directors of those very banks to optimize the management of resources and reduce the degree of geographic diversification of their operations.

Underlying these decisions by banking institutions is the need to sell assets to reduce debt, the greater demands of capitalization, an awareness that some international operations have been characterized by deficient risk management, and the need to divest themselves of international operations that were not very efficient in some cases. This is an interesting phenomenon. We find that one of the most dynamically internationalizing sectors, banking, faces a drop in its international operations as a result of the financial crisis.

Moreover, the difficulty of regulating banks with international operations due to their greater complexity has led to public debate about whether it would be preferable for banks, as regulated institutions, to have a smaller geographic area of operations. Unless the debate on public policies in Europe changes radically, it seems unlikely that this debate will mark a turning point for international banking operations. Nevertheless, the fact that this debate has arisen is a clear indication of the degree to which the financial globalization process is now being questioned.

Finally, mergers and acquisitions—another important motor in the globalization process in recent years—have also dwindled as a result of the financial crisis. These corporate operations have an important cyclical component, so it is natural for them to diminish in parallel to economic deceleration. And yet, at this point in the economic cycle, the drop in the number and volume of such operations is related to the loss of attractiveness of certain key markets, poorer expectations of the stock market, general uncertainty about the future of globalization, and reduced credit facilities for undertaking acquisitions financed with debt.

Nevertheless, the financial crisis has also shown how important it is for the international financial system to have a high degree of integration. The enormous imbalances in the US budget and balance of payments have been financed with foreign savings, which would have been
more difficult just a few decades ago. Without China’s integration into the international economy, the United States would not have been able to support those deficits without substantially raising interest rates.

This is the second positive dimension of financial globalization worth noting: international capital flows have not completely disappeared during the financial crisis. As a result, the absence of liquidity in certain markets has not led to a generalized rise in interest rates.

And last, the crisis has revealed the enormous impact of public policies, particularly monetary policies applied by major central banks to combat the perverse effects of the financial crisis. A coordinated effort by central banks to inject liquidity, rein in the panic, and maintain nominal interest rates at a very low level has clearly kept the financial crisis from turning into a great depression. In that sense, the crisis has proven the efficiency of the circuits through which financial globalization runs, even when the imprudence of certain banks and the lack of regulation in keeping with the new realities could have provoked an even greater disaster. Likewise, central banks have shown that even when circumstances are very adverse—as they were in 2007 and 2008—the financial globalization process allowed adjustments that might have been more costly and less efficient in other circumstances.

**EFFECTS OF THE CRISIS ON THE MOTORS OF GLOBALIZATION**

**PUBLIC POLICIES**

As we emphasized above, the financial crisis has raised numerous questions about the future of the economic globalization process. That crisis has undermined the foundations on which the world economy has been developing in recent decades, foundations that essentially supported free and open markets, the liberalization of international commerce and capital flows, deregulation, and reduction of the public sector’s weight in the economy. At the base of this hypothesis is a set of convictions about public policies necessary to guarantee the proper functioning of an economy.

The first of these convictions is that deregulated markets function better than regulated markets except in certain cases, such as monopolies. The second is that financial markets tend towards efficiency, which signifies that share prices adequately reflect all available information on companies. The third is that, in the face of the free-market/regulation dilemma, the dominant paradigm has been that of less regulation and more market, and this has been especially true in financial markets.

Reflection on these criteria in the context of the current crisis also leads to a reconsideration of the public sector’s role in a market economy. This is neither the time nor place for a reconsideration of what have generally been correct decisions aimed at limiting or eliminating the public sector’s participation in mercantile companies, reducing tax pressures—especially those that tax economic activity—and improving the efficiency of public spending. Nor is this the place to defend a greater presence of the public sector in countries’ GNPs, other than the discrentional spending considered prudent to revive economic activity in times of crisis. Still, it is clear that the deregulation movement of the 1980s and 1990s coincided with a regression in the state’s role in economic activity to such a degree that two phenomena were mistaken for each other: less activity by the public sector and less regulation. Experience shows that the first, less presence by the public sector, has generally been a good one. The decision toward less regulation, however, has been ill advised in some cases, principally in the financial sector.

One of the main effects of the financial crisis is the reconsideration of those basic aspects of market economies and of the need for greater regulation of financial activity. This phenomenon will have some consequences on globalization. The first is that a re-regulation of the financial sector will make international expansion by banks more difficult and will generally limit, and increase the cost of, international capital flows. The second is that in a period of lesser economic growth a greater presence of the public sector as a regulatory agent of the financial sector could lead it to intervene in other areas of the economy beyond those needed to guarantee desirable levels of social protection. The US Government’s intervention to rescue the automotive sector in the United States is a clear example of these new realities. The return of state regulation could have implications for greater economic protectionism, which could include the shameless defense of so-called national champions in strategic sectors. This would be bad news for the proper functioning of economies and would have a negative impact on globalization.

**DOMINANT VALUES AND IDEAS**

In recent decades, partially as a result of the ideas described in the previous section, which
have inspired economic policies in numerous countries, another opinion has become widespread: the idea that specific aspects of social life—or of society as a whole—should behave in a manner similar to the marketplace, with the corresponding incentives. This idea reached its peak in the moments of greatest growth during the 1990s and reappeared in the present decade before the summer of 2007. With this notion, a sensible approach—the idea that the organization of economic activity in competitive markets is generally the most efficient solution—has been transformed into the argument that social life should be centered on the market. Logically, the financial crisis has brought out the weak functioning of certain markets—especially financial markets—and has revealed the need for reasonable regulation. It has also debunked the myth that society mirrors the market.

As Nobel prizewinner, Amartya Sen, recently pointed out in reference to Adam Smith (see Sen 2009), “it was in his first book, The Theory of Moral Sentiments, published exactly 250 years ago, that he extensively investigated the role of non-profit values. While stating that ‘prudence’ was ‘of all virtues that which is most helpful to individuals,’ Smith went on to argue that ‘humanity, justice, generosity, and public spirit, are the qualities most useful to others.’” Sen adds: “It is often overlooked that Smith did not take the pure market mechanism to be a free-standing performer of excellence, nor did he take the profit motive to be all that is needed.” In conclusion, Sen observes that all this should not lead us to reject the market, but rather to understand the limits of the market itself. In other words, the market has limits. Moreover, there are other personal and social realities for which the market offers no reasonable explanation.

Closely related to the previous hypothesis about the market’s role in the economy and in society is the fact that the search for one’s own benefit or interest has become a basic principle of economic and corporate organization—not to mention its presence in society as a whole—and that search has been accompanied by an abandonment of the quest for the common weal. The satisfaction of personal objectives and interests has been particularly eloquent in financial institutions, especially investment banks and collective investment institutions, some of which have disappeared with the financial crisis. The pursuit of self-interest at any cost, sometimes driven by greed, has corroded the personal integrity of many individuals and has endangered both the continuity of many organizations, and the market economy’s stability and acceptance as a social referent. The current financial crisis has provoked a wave of distrust of the market that is not logical, just as there is nothing reasonable about how, until very recently, the market economy was praised as a successful paradigm.

In the corporate world, the maximization of market value for shareholders—a new criterion that has replaced the notion of maximum profit—has become the central paradigm of business management, even when, for top management, maximization is neither an operative criterion nor the result of decisions they can make. Clearly, in this case we tended to replace a real market of clients, products, people, efficiency, and economic results with a market based on expectations—the stock market—under the hypothesis that the prices in the latter would reflect all available information. It has finally become a widespread criterion that payment of top management should be determined in terms of company results, and more specifically, in terms of the company’s market value. Payment of top management is a complex challenge, but that challenge turns into nonsense when the referential indicators are short-term rather than long-term results. Short-term results generate perverse incentives to take risks with the expectation of high short-term returns, without any concern for the company in the long term.

The answer to the market’s failure to explain certain human and social realities is to return it to its rightful place—the world of economic transactions—and to recognize that in both the personal and social spheres there are numerous dimensions and areas in which market logic is insufficient. Neither a stable economic system nor human society can rest on foundations of self-interest. If they did, the social edifice would suffer from considerable structural weakness. It is necessary to combine a legitimate interest in one’s own affairs with a necessary interest in the legitimate wellbeing of others. That alone will guarantee a peaceful and enriching human coexistence for all. At the same time, there is also need for an explicit defense of the common weal, which represents the ideals of social life—freedom, a sense of justice, peace, human development—that make it possible for each person to grow. In Sen’s words, authentic development consists of offering people and societies the necessary means to construct a destiny in keeping with their expectations and desires.

Therefore, it is not a matter of limiting the proper functioning of the market in economic
NEITHER A STABLE ECONOMIC SYSTEM NOR HUMAN SOCIETY CAN REST ON FOUNDATIONS OF SELF-INTEREST. IF THEY DID, THE SOCIAL EDIFICE WOULD SUFFER FROM CONSIDERABLE STRUCTURAL WEAKNESS.

life, rather, its true meaning must be found in the area of economic transactions, where its operation is efficient for the development of people and society. At the same time, even in this setting there is sometimes need for adequate regulation of the market. The financial crisis has made it uncomfortably clear that the lack of good regulation in specific areas of financial activity has permitted the unleashing of a crisis of brutal proportions. A more efficient and active regulator might have been able to limit the damage that has been caused by certain credit investment operations and specific opaque and non-liquid assets.

The current financial crisis could help return economic globalization to its proper place—the economy—an area of human activity that must be subject to politics, which must in turn be subject to ethics, as we find in the classical ideal formulated by Aristotle (see Aristotle 1996 and 2002). That is the notion that has been present in the most brilliant periods of Western society. Politics must be oriented towards the quest for the common weal, an ethical value superior to that of individual interests or those of certain lobbies. At the same time, economics should combine its specific and distinctive areas of competence—the quest for efficiency in the organization of economic activity—without seeking to apply the idea of the market to all areas of social life. That idea considers the market an efficient mechanism for organizing a large part of society’s economic transactions, but, as Pope Benedict XVI observed, economic activity cannot resolve all social problems simply by applying the logic of commerce; to be efficient, it must pursue the common good, which transcends personal interest. In the final analysis, the market economy needs ethics in order to function in a sustainable fashion.

Similarly, globalization offers indubitable advantages in the quest for economic efficiency, including access to markets in the most advanced countries for products from emerging nations, as has been shown by the industrialization of China and Brazil. Still, the logic of globalization cannot limit itself to merely economic reasoning, much less to what some have called enlightened self-interest (an expression coined by Alexis de Tocqueville), which would be something like a humanized version of the self-interest that Adam Smith describes as the motive for a merchant’s actions.

As we discussed above, Smith himself never admitted that personal benefit should be the only motive for an individual’s behavior, or that the market could be the only manner of organizing social life. Limiting globalization to its economic dimensions and justifying it in the name of benign self-interest is simply unreasonable. Self-interest as the dominant criterion is a sign of selfishness and a manifestation of injustice. Basing international relations on a concept of globalization rooted in benign egoism—one that generates mistrust because it is seen as a rather unjust model lacking in sensitivity to the needs of others—clearly constitutes a danger for the peaceful development of nations and for human coexistence.

In that sense, the crisis is a magnificent opportunity to reflect on how fitting it may be to base economic integration processes on noble human values that foster cooperation among people and nations. Economic efficiency as a manifestation of professional excellence is one of those human values, but a leading role should also be played by the humanization of relations among people, justice, magnanimity, and the search for the common good, among others.

INTERNATIONAL CORPORATE EXPANSION

International corporations have been important drivers of the economic globalization process, along with technology and public policies to promote international trade. The international expansion of contemporary companies has provided the second globalization of the economy with deeper roots than the previous attempt before the First World War. What impact has the financial crisis had on international corporations and, indirectly, on globalization? The crisis has put a brake on the expansion plans of many companies, but in the minds of many directors internationalization is a central element in the twenty-first-century economy.

For a variety of reasons, the crisis has led to a drop in activity for many international companies. The first is the economic recession in many countries, which has caused reduced sales, especially in the capital goods and infrastructure sectors, but also in the automotive, telecommunications, computing, and consumer-electronics sectors. This recession is particularly intense in some countries and regions, especially certain countries in Eastern Europe and Latin America. The second reason is the credit restriction that has affected all companies in general, and particularly those whose investment projects have the highest perceived risk, which is the case with international operations.

The third reason is the growing importance that the location of a corporation’s headquarters
The positive performance of the major Spanish various markets; and a greater proximity to the Spain, in particular, periodically experiences financial services in its economy and the loss final consumer. And yet, in some, the crisis has ing capacity and innovation—that disconnection can have a limiting effect on the latter—and the disinterest on the part of youth in technical-tries of a disconnection between manufactur-ation and innovation—that disconnection can have a limiting effect on the latter—and the disinterest on the part of youth in technical-scientific university studies. Great Britain would be an example, given the growing importance of financial services in its economy and the loss of industrial sectors there over the last two decades. In fact, this attitude is a very real obstacle when preparing the new generations of company directors and highly qualified professionals.

Nevertheless, the financial crisis has also revealed some positive aspects of corporate internationalization, which could encourage this process in the future when the global economic situation improves. The first of these is that international corporations tend to systematically seek out efficiency when buying, producing or selling on various markets. The second is the greater diversification of the risk effect—both market and financial risks—especially in companies with balanced portfolios in various regions.

The positive performance of the major Spanish banks or of Telefónica during the financial crisis—especially when comparing their evolution with that of other companies in the same sector in other countries—is very eloquent in that respect. The third are the opportunities for future growth. International expansion is a never-ending process. Presence in emerging markets that have best weathered the crisis, such as China, India, and Brazil, has been a lifesaver for numerous European companies and will continue to be so in the future.

The fourth dimension is that the crisis has brought out the importance of diversity among management teams, and internationalization contributes to this. The presence of top management from other countries in which a company has a significant presence is a guarantee not only of greater understanding of the local market and its relevant circumstances, but also of a greater capacity to foresee the future in that country.

The success of international corporations that have done especially well in certain emerging markets, such as Novartis, PepsiCo, and Unilever, among others, cannot be separated from the fact that they have a very notable international diversity in their top management teams.

The fifth dimension is that the crisis has revealed the value of efforts to achieve information transparency and good government in many international corporations. Much of the intensity of the crisis has been due to many people’s distrust of the value of companies. The financial crisis has hit all kinds of companies, but, since the bubble burst, those companies with the clearest approach to corporate government have shown a tendency to recover more rapidly. The case of US and British banks is a clear example. Those institutions that have been slow to admit their losses, adjust their management teams, or modify obsolete models of economic compensation have been hardest hit by the mistrust of their shareholders and the market. On the other hand, those banks that have shown the greatest maturity in their mechanisms of corporate government and have been capable of clearly informing their investors as to the reality of their situation and the logic behind their strategic decisions have been least damaged by the crisis.

To summarize, the financial crisis has had a negative short-term impact on international corporations, although for the time being we do not have evidence to determine whether that impact has been greater or smaller than on more local companies. Logically, this impact has a negative effect on the globalization process because companies have been the fundamental driving forces in this process.

Still, we should also point out that the financial crisis has brought out some of the strengths...
of international corporations compared to those with a more domestic profile. It is clear that a company’s potential for globalization cannot be evaluated on the basis of how strongly it is affected by a gigantic financial crisis of the sort that only occurs every few decades. And yet, the impact of this crisis on international corporations at the root of economic globalization has brought out some of the advantages to this kind of company. Their strengths are also a relative guarantee that globalization may slow during the crisis, but it is not condemned to stop altogether.

SOME REFLECTIONS ON THE FUTURE OF CORPORATE GLOBALIZATION

In the corporate field it is worthwhile reconsidering two critical questions that have been at the base of the values and ideas underlying the globalization phenomenon in recent years. The first is the notion of the company itself. A company is a mercantile entity. As such, economic theory has posited the company’s goal as the maximization of profits or, in a more recent version of this goal, the maximization of value for stockholders. As this is an unwieldy and diffuse goal, in practice it has been transformed into the maximization of short-term value.  

Still, above and beyond the legal reality, a company is essentially a human group that seeks to satisfy the needs of its clients through the efficient production and distribution of goods and services, and in that process, a company must generate economic profits, as well as offering opportunities for its employees’ professional development. That may seem like a more complex version of the concept of a company but the experience of legendary companies and the testimony of their founders shows that in many companies profit is not the principal motive. Such companies do generate profits, but they are the result of a process, not its essence.

A concept of companies in which the role of self-interest is appropriate and balanced with the overall interests of the organization, and of society, insures that a company will better respond to its underlying human reality, will better adapt to the challenges posed by crises and changes, and will be able to move confidently into the future. Moreover, this concept includes the idea that when a company acts as a driving force for globalization its role will be that of an institution seeking the common good of the societies in which it operates, and not only economic profit from its activities there. One part of the criticism directed at economic globalization has been motivated by the supposed lack of solidarity of some multinational corporations in economically less-favored countries. In terms of short-term economic results, the difference between these two concepts of a company may not be so great. But over the long term, the notion we are proposing here has the enormous advantage of greater respect for the nature of things and an emphasis on the idea that profit should not be the only dominant value in society.

This concept also implies a set of demands that must be met if companies are to continue to be the driving force in the economic globalization process. These demands are related to corporate government and, very specifically, to a company’s sense of mission and the responsibilities and tasks of its organs of government, specifically, its board of directors and top management.

In fact, one of the dominant corporate values in recent decades has been to view the board of directors and president as agents’ with powers delegated by stockholders in order to achieve the objectives set out by the latter, either directly, or through the expectations of financial analysts. Those objectives were based on the theory of efficient financial markets and related to the maximization of short-term value for shareholders. In order to align those agents with the shareholders’ objectives, it was proposed that executives be paid according to results or performance (“pay for performance”). Once again, the idea of performance was most frequently associated with the creation of short-term value.

This notion of the company has created perverse incentives for boards of directors and top management who, driven by greed, have ended up making decisions leading to short-term benefits even when they might have a negative impact on the company in the long term. The collapse of some investment banks in 2008, as well as of other companies in a variety of sectors, is a clear example of the lack of common sense and the irrationality of such behavior from the standpoint of the company as a whole and of society.

Companies can be stable motors for the economic globalization process to the degree that their top executives make decisions based on the projection and success of the company in the long term, rather than on personal interest. That is the only way that a company can become an institution worthy of respect for its economic efficiency, its capacity to create a positive referent for clients, suppliers and other competitors, and its positive impact on society as a whole.

5 Davies (2009) systematically shows how the theory of efficient markets and the objective of maximization of value for shareholders eventually conquered the corporate world beginning in the 1980s.

6 A more complete discussion of this idea of the company can be found in Building respected companies, Canals (2010). J.M. Rosanas (2009) presents the basis of an alternative to the neoclassical model of companies.

7 The term “agent” comes from what is known as “agency theory,” which seeks to explain the concept and goals of a company based on the delegation of powers by an owner or “principal” to an “agent.” A formulation of agency theory can be found in Jensen and Meckling (1976).
Of course the problems posed by the current financial crisis cannot be resolved with ethical criteria alone. It is also necessary to apply professional criteria to both the design of economic policies and the direction and management of companies themselves. Still, without ethics, even the best policies will be useless and the globalization process will not move forward, crushing the possibilities for improvement that this process can offer when the participants fostering it are driven not only by self-interest, but also by the interest of others and the common weal of society.

SOME FINAL REFLECTIONS

The economic globalization of recent years cannot be considered directly responsible for the financial crisis we are currently experiencing, but it has contributed to the acceleration of its international propagation. Still, just as the crisis has affected many countries that are scarcely involved in the process of financial innovation developed in the United States, the mechanisms of propagation can act in a positive direction when economic recuperation strengthens in the leading economies.

On the other hand, the financial crisis has led to a significant slowdown in the economic globalization process, partially through a drop in commercial and financial flows among countries. In particular, the liquidity crisis and a greater aversion to risk have led to capital flight from emerging markets towards more mature ones.

The crisis has also provoked a drop in international corporate activity, as companies reevaluate investment plans, debt decisions, projects for penetrating other markets and international investment portfolios and business.

Nevertheless, the greatest impact of the financial crisis may be on public policies that directly or indirectly affect globalization. Especially if governments cede to protectionist pressures, defending their own countries’ companies in detriment to companies from other nations.

An especially positive variable that the current financial crisis presents in the analysis of economic globalization is an examination of the values and suppositions that form the foundations on which the process of worldwide economic integration has advanced in recent years. Specifically, the primacy of criteria of efficiency and economic results over other criteria and variables. Economic efficiency, freedom, solid institutions, and a sense of fairness and justice are essential conditions for economic and social prosperity. Communism collapsed in the late 1980s because it met none of those requisites. Until now, the free-market economy has met some of them reasonably well, but nothing guarantees its existence if it does not manage to combine efficiency with achievements that are reasonable in terms of justice and fairness. And the future success of the globalization process does not depend so much on technology or the economies of scale that companies might develop, as on the public policies and values that societies develop with regard to that process. As Williamson pointed out (1998, 70), “Yet history does supply that warning: if a globalization backlash can be found in our past, it may reappear in our future.”