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CHAPTER 21

International Political Economy

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In this chapter, you will gain understanding of the following;

- What is meant by IPE
- How the global economy has evolved over time
- Rival theoretical approaches
- The nature of the contemporary international political economy

Introductory box The 2008–13 global recession

'When America sneezes, the world catches a cold' is a famous adage used to highlight one of the major implications of today's interconnected, globalised world: the problems of the world's largest economy very rapidly become problems for everyone. The phrase itself originated in the wake of the 1929 Wall Street Crash in the USA, which led to the Great Depression, and subsequently to a world-wide recession. The maxim achieved prominence again in 2008 when the world experienced its worst downturn since the 1930s, sometimes referred to as the Great Recession.

The 2008 financial crisis was triggered by the collapse of the US housing market. US banks had been offering highly risky loans – subprime mortgages – to people who could not afford them, and when borrowers began to default in large numbers on their repayments, this sparked a major credit crunch in the banking system, and a drastic cut in lending. Yet this did not remain a purely American problem for long,

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with the ripple effects soon spreading right across the world. Trillions of dollars were wiped off the values of economies, and unemployment and poverty rates rose sharply. Even ten years after the recession began, many economies were still recovering from its effects in 2018 (Chen et al. 2019).

However, the global recession had not only a massive real-world impact, but also important lessons for International Political Economy as a discipline (Mosley and Singer 2009; Drezner and McNamara 2013). Indeed, Benjamin Cohen argues that the crisis was IPE's equivalent of International Relations' experience with the collapse of the Soviet Union nearly three decades before: both events not only signalled major 'systemic transformation[s]', but also were ones that scholars 'failed to see . . . coming' (2009: 437).

For Cohen, and many other critics, the global recession also appeared to reveal significant deficiencies with prevailing orthodoxies, not just with the specific lending practices of American banks. In particular, it seemed to show that untrammelled free markets, coupled with weak regulatory frameworks (as operated by both national governments and international financial bodies) were what had led to economic crisis. In other words, while the US subprime mortgage crisis was the *proximate* cause of the global recession, the *underlying* ones were structural and institutional, and both economic and political. As such, the Great Recession raised questions about the fundamental tenets that had long been dominant within political economy, those of free-market neoliberalism, that favoured only very 'light touch' economic regulation. In this way, we can see how real-world developments may strongly influence intellectual debates, and how we think about the relationships between markets, governments and wider society.

Introduction

International Political Economy (IPE), also known as Global Political Economy (GPE), is a sub-discipline of International Relations (IR) that originated in the 1970s (Cohen 2008). It was pioneered by American writers such as Robert Keohane and Joseph Nye (1977), and British writers like Susan Strange (1970). In simple terms, IPE is the study of how politics and economics interact at the global level.

In part, the emergence of IPE was due to the related political and economic crises of the period: major oil price rises that rocked the global economy, 'stagflation', and the seeming impotence of governments, even of the most powerful states, in the face of these problems. As a result, two important intellectual points became increasingly recognised. First, that the artificial separation of politics and economics that had developed within academia needed to be questioned; and second, similarly, that the traditional distinction drawn in IR between the domestic and the international also required challenge. Consequently, the 1970s witnessed not only a revival of Political Economy, the study of the intersection of politics and economics *within* a given state, but the creation of a newer discipline, IPE, to apply its insights to the *international* level.

In part, too, the rise of IPE can be explained in terms of globalisation. Few seriously dispute that the flow of people, ideas, goods and money across state borders has greatly intensified in modern times, with major implications for our understanding of both politics and economics. Prior to the 2008 crash, the volume of goods traded had risen more than 27 times from the levels of the late 1940s (WTO 2007). While there have been significant periods of growth in the internationalisation of economic activities before this current phase of globalisation, none have occurred so rapidly or to such an extent.

The study of IPE in academic circles, and appreciation of it in governmental circles, emerged from the 1970s as a number of key realisations became apparent which challenged previous assumptions about how to compartmentalise issues into the subjects of 'Economics', 'Politics' and 'International Relations':

- *Economic events in one state can have economic implications for others*: As illustrated in the opening case study, the global recession of 2008–13 originated in the collapse of the US housing market, but quickly spread throughout most of the world.
- *Political events in one state can have economic implications for others*: For example, the reunification of Germany in 1990 was a key factor in the collapse of the UK pound in 1992. The Bundesbank had to raise German

interest rates to pay for the absorption of their poorer Eastern neighbour, causing financial fluctuations in the European markets unused to such extravagance from the Continent's traditionally prudent economic leader. In what became known as 'Black Wednesday', on 16 September 1992, the British government was forced to withdraw the pound from the European Exchange Rate Mechanism (ERM) – a system of fixed exchange rates within the European Union – because it could not afford to support sterling remaining within it. The fall in the currency's value wiped billions of pounds from the UK stock market.

- *Economic events in one state can have political implications for others*: Increasingly, the performance of a domestic economy is as much dictated by international economic events as it is by how a government manages its fiscal (tax), monetary or industrial policy. Evidence for this can be found as far back as 1929 and the Wall Street stock market crash in the USA, which precipitated the world's worst-ever economic recession. This was then a contributory factor in the fall of many democratic governments, and the rise and spread of fascism and communism as alternative models of political and economic management.
- *Power in international relations can come from economic as well as military might*: (West) Germany and Japan rose again as world powers in the 1950s and 1960s not by rearming and invading neighbouring states, as they had done in the 1930s and 1940s, but by building their economies and trading their way to wealth and influence. Similarly, during the oil crises of the 1970s, states like Saudi Arabia, Iran and Iraq suddenly became much more influential players on the world stage because of their possession of the world's most important commodity, oil.
- *International political structures reflect economics*: Intergovernmental organisations set up to regulate the international economy after World War II, such as the International Monetary Fund, were from the start dominated in their decision-making by one country: the United States. The USA in 1947 accounted for around half of all economic production in the world, a level of superiority never seen before and never repeated since. As a consequence, these organisations were designed to further the US economic interest of promoting more trade opportunities and the political interest of propping up the capitalist world against the threat of communist expansion.
- *A short history of the international political economy*: Although it may not have been a recognised academic discipline before the 1970s, there was, of course, an 'international political economy' well before then. International trade has linked states together since ancient times and, from around the 16th century, the recognisably modern era of trade, diplomacy and an international system centred on nation-states began to take shape (Kindleberger 1996; Baten 2016; Amatori and Colli 2019). It is important to understand commercial exchanges in the modern era as being as much about politics as economics, as the world has become more interlinked with advances in transport and communications, and economic competition is structured around the political division of the world into sovereign states.

Box 21.1 gives an overview of the evolution of the international economy in relation to the internationalisation of political ideas, in terms of changing beliefs about how governments should orientate themselves towards the rest of the world.

Box 21.1 Timeline of the international political economy

1500–1780: The Age of Mercantilism

The birth of modern capitalism: the major European powers began to accumulate large amounts of wealth in a competitive system based on self-interest and protectionism, and the exploitation of overseas' markets and resources.

1780–1850: The Industrial Revolution

Economic production began to shift from primarily small-scale and agrarian to large-scale manufacturing, in part as a result of new technological developments

1815–1873: The Age of Liberalism

1821 Great Britain adopts the gold standard (ties its currency to a set value in gold). This was intended to create greater certainty and confidence in the value of its currency

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1846	Repeal of the Corn Laws – landmark British Act of Parliament which reduced protectionism. The Corn Laws had used tariffs and other measures to protect British agriculture; their repeal represented a repudiation of mercantilism and the embrace of free-market liberalism
1860	Cobden–Chevalier Treaty – Franco-British agreement to free up bilateral trade
1866	Latin Monetary Union – short-lived currency union based on the French franc involving several South European states
1871	Germany adopts the gold standard
1873–1945: The Return of Mercantilism	
1873–96	The Long Depression
1929	The Wall Street Crash and the Great Depression – a massive, world-wide economic downturn. Many interpreted it as showing that unfettered free markets do not always produce the best results, leading to the revival of protectionist and interventionist economic policies
1930	Smoot–Hawley Act – highly protectionist law passed in the USA
1931	Collapse of the gold standard – fixing currencies to the value of gold proved too restrictive for many governments in the context of the Great Depression
1944: The Liberal International Economic Order	
1944	Bretton Woods Conference
1947	General Agreement on Tariffs and Trade (GATT) launched
1971	Collapse of the Bretton Woods monetary system
1971–74	Oil crisis
1989–91	Collapse of communism
1995	World Trade Organization (WTO) founded
1997–99	East Asian financial crisis
2008–13	Global recession following US subprime mortgage crisis
2020–21	Global recession following Covid-19 pandemic

The ages of mercantilism and classical liberalism: 1500–1945

From the 16th to 18th centuries, the economic policies of the great powers, and the overall economic system, are often described using the term 'mercantilism'. This means that governments during this era played strong roles in managing and regulating economies, to bolster the power of their own states, and to outdo their rivals – a form of economic nationalism. It involved trying to maximise exports and minimise imports, to boost national profits and weaken competitors. All of this was predicated on the belief that international economics is a 'zero sum game', in which there is a fixed amount of wealth in the world, so that for one country to increase its share must inevitably come at the expense of others. There was also a strong emphasis on possessing precious metals like gold and silver because these were seen as the physical embodiment of wealth and power.

At this time, international economic relations were also carried out within the context of colonialism. A small number of states controlled most of the world, both politically and economically. These states – including Britain, France, Spain, Portugal, the Netherlands and Turkey – constructed their own international economic systems in which they imported what they needed from their colonies, while also using those territories as markets for their surplus exports. Imperial powers traded with each other when necessary but, in general, saw other trading giants as commercial rivals, rather than partners. As such, they looked to beat each other to the acquisition of any remaining uncolonised territories while, at the same time, jealously guarding their own possessions from covetous rivals.

Mercantilism never disappeared, and persists today in less explicit forms. However, with the dawning of the Industrial Revolution and the Age of Enlightenment, for the first time it faced a rival philosophy: economic liberalism. In the 19th century, a significant precursor to contemporary globalisation took place, in which international trade grew dramatically, due to increases in both economic capacity and political willingness to engage in international commerce. A great leap in economic production occurred due to the emergence of new manufacturing industries and processes, allied to an intellectual shift in favour of seeing other states more as partners than rivals in the international economy.

This period, in which economic liberalism began to flourish and challenge the logic of mercantilism – by emphasising the mutual benefits of free trade over narrow self-interest and protectionism – was aided by the peace and diplomatic cooperation which marked the 19th- century 'Concert of Europe' era – a period that began in 1815 following the Napoleonic Wars, in which the major powers reached a broad consensus in terms of respecting one another's boundaries and spheres of influence. In other words, the *political* settlement that allowed for relative peace within Europe also facilitated the development of a new *economic* order, grounded in liberal principles.

However, this order started to unravel with the renewal of political conflicts in Europe, beginning with the Franco-Prussian War of 1870–71. A growth in nationalist ideologies coupled with an economic recession at the end of the 19th century saw governments look more inwardly again. As a result, there was a renewed focus by states on acquiring resources for themselves, through force if necessary, rather than seeing the benefits of free trade. Economic downturns invariably encourage governments to be more cautious about free trade and instead focus on holding on to what they have. This, added to a political reluctance to trade with countries deemed to be rivals, saw international trade slow down after the extended period of globalisation. Mercantilism thus came back to the fore in the late 19th and early 20th centuries, in the context of global military conflicts and extremist ideologies that emerged in this era.

A revival of cordial relations between the great powers, and of liberal thought, occurred in the 1920s, in the wake of the horrors of the Great War – this was the era of the League of Nations and attempts to rebuild more cooperative relations between the major powers. However, these efforts proved abortive, and a potential new era of economic and political globalisation came to a crashing halt with the onset of the worst-ever global recession – the Great Depression – which began in 1929 (Galbraith 1955; Kindleberger 1973). Illustrating the economic interconnectedness of the world well before the contemporary era of globalisation, the effects of the Wall Street Crash quickly reverberated around the world and saw a massive downturn in international trade. The sudden stock market collapse in the USA occurred due to the bursting of a 'speculative bubble' of stocks and shares that had become over-priced on the back of a domestic economic boom. This caused banks and businesses to collapse as the US economy shrunk by a third. The domestic crisis quickly internationalised as the US government responded in a mercantilist manner. Loans given to European allies indebted by the Great War were recalled and measures were enacted to cut imports in order to protect weakened US industries from being undercut by foreign competition. Between 1929 and 1933, the value of world trade fell from $35 billion to just $12 billion as states, such as many in Latin America, suddenly saw their main market for exports dry up. Many European states followed the example of the USA and put up barriers to trade.

The world came out of economic depression only as a result World War II, which prompted renewed growth and international trade, partly due to the enormous industrial production that war required in order to support the arms industry. Recognising that relying on World Wars to ensure economic growth was not a viable long-term strategy, leading capitalist states at the close of the war sought to take international political steps to ensure that another Great Depression, as well as another World War, would not happen again

The liberal international economic order: 1945–1990

At a 1944 Conference, held at Bretton Woods in the USA, the governments of the host country and the UK led discussions which created the institutional architecture of what would become known as the **Bretton Woods system** (Steil 2014). To support international capitalism against both another depression and the perceived

threat of communism, the attendees decided that intergovernmental organisations were needed to provide stability to the international economy and prevent governments lurching towards mercantilism when they experienced economic difficulties.

Hence, at the close of World War II, the present era of international political economy – often termed the liberal international economic order (LIEO) – was initiated. This was based upon the Bretton Woods system of two new institutions, created within the newly established UN system, and an international treaty:

- *The General Agreement on Tariffs and Trade* (GATT) – a treaty establishing a regime intended to promote international trade and prevent governments resorting to mercantilist measures.
- *The International Monetary Fund (IMF)* – an organisation based in the USA, which seeks to foster monetary cooperation, international trade and global financial stability. It offers loans to states that run into economic difficulties (see Box 21.2).
- *The International Bank for Reconstruction and Development (the World Bank)* – an organisation also based in the USA, which lends to governments in order to develop their economies.

Central to the General Agreement on Tariffs and Trade (GATT) was the resurrection of an old idea for facilitating trade which Britain had used in the 19th century: the **most favoured nation** principle. This principle involves an undertaking between two states that, in granting trade concessions to each other (e.g. mutually reducing tariffs on certain goods), they also agree not to grant even greater concessions to another state. For example, if State A and State B have a most favoured nation agreement, they are both then committed not to conclude a new deal with even greater concessions to States C or D, no matter how mutually beneficial it may be. The point of this principle is to give some order and openness to international trade, and to avoid an endless series of undercutting deals and the conflicts that would likely ensue.

Box 21.2 The IMF: key facts (2022)

Credit: Photo by AgnosticPreachersKid on Wikimedia Commons

Headquarters: Washington, DC (USA)

Members: 190
The vast majority are sovereign states as recognised by the UN, though a few are not – e.g. Kosovo. Equally, a small number of UN member states are not members of the IMF – e.g. Cuba and North Korea.

Head: Managing director – since 2019, Kristalina Georgieva (Bulgaria).

Key functions: provides a source of funding for governments in economic difficulties and facilitates free trade by creating monetary stability. Funding comes from member-states, using a formula based on the size of their economies (so that richer states pay more).

Decision-making: the Board of Governors is the highest decision-making body of the IMF, and is composed of one governor and one alternative governor appointed by each member. Daily business – including lending decisions – is conducted by an Executive Board consisting of 24 Executive Directors, with weighted voting rights based on members' relative economic strength. Eight states are represented individually on the Board. These are (with their % voting rights): USA (16.50%), Japan (6.14%), China (6.08%), Germany (5.31%), UK (4.03%), France (4.03%), Russia (2.62%) and Saudi Arabia (2.01%). The rest of the membership is organised into loose geographical groups that are represented by one of their members in turn, with their voting rights quotas combined.

Debate – for and against the IMF

Criticism	**Defence**
Unfairly dominated by the wealthiest states	*Those who pay the most money should decide where it goes*

As the figures above show, the world's richest states far outweigh the rest in voting rights allocated for decision making. Constitutional changes require an 85% 'supermajority' – giving the USA, even on its own, an effective veto. Defenders of the system argue that the imbalance is fair, since the weightings accord with how much money states contribute to the IMF's coffers. Yet critics contend that the system simply entrenches the global imbalance of power in the international economy.

Conditions for loans are too harsh	*Loans should be conditional*

The most prominent criticism of the IMF is that it attaches conditions to its loans that exacerbate problems, including poverty. It does this by insisting on the implementation of what are called structural adjustment programmes (SAPs), which are typically neoliberal in their requirements, including cuts to government spending, privatisation programmes and opening up economies to free trade. For example, critics claim that the IMF *worsened* the 2001 financial crisis in Argentina by insisting on the privatisation of state utilities, which saw unemployment rise as foreign firms bought up local industries. However, defenders of the IMF argue that not insisting on measures to ensure governments do not waste or embezzle funds, as has been known to happen, would be irresponsible. Supporters also point out that some states – such as the 'Asian Tigers' (e.g. South Korea) and post-communist transition states of Eastern Europe (e.g. Poland) – have successfully used IMF funds to kickstart rapid economic growth.

Secretive and politicised decision-making	*States need a global monetary facility, and some secrecy*

Supporters of the IMF argue that there is a clear need for a global organisation to promote financial stability and that, like governments, to be able to make effective decisions, some of its deliberations need to be in secret. Yet critics argue that a lack of transparency adds to concerns about poorer states losing out and being dominated by richer ones. In particular, there is a concern that lending decisions may be made using political, rather than strictly economic, criteria. For example, when the IMF refused to provide an emergency loan to Venezuela in 2020, which it requested to help deal with the Covid-19 pandemic, critics argued that this exposed the IMF's US bias: since the US government was heavily opposed to Venezuela's left-wing government at the time, the IMF was being political in siding with its largest donor, rather than responding to the desperate needs of the Venezuelan people (TRT World 2020).

Overall, GATT proved hugely successful in liberalising international trade. In the 1950s and 1960s, the process of continually reducing tariffs helped stimulate very high rates of world trade growth: approximately 8 per cent a year on average (WTO 2015: 17). There were limits to its effectiveness – for example, GATT allowed states that formed trading blocs to be exempted from the most favoured nation principle (that is, they could give greater concessions to their trade bloc partners than to their most favoured nations). Over time, as bodies like the European Community/European Union have become more significant, this has raised questions about whether or not they increase or decrease the amount of international trade. Some see trade blocs as a positive development for liberalisation, since they clearly increase free trade among members, and may be stepping stones towards global free trade. However, others voice concern that trade blocs are detrimental to international free trade since they produce 'trade diversion', increasing trade among their own members at the expense of trading with the rest of the world.

Another mechanism devised at Bretton Woods to lend stability to the post-war global economy involved reviving another scheme from the 19th century – the gold standard – though strengthened through the creation of the IMF to support its operation. Unlike in the past, the system worked not by states tying the values of their currencies directly to the value of gold, but to the value of the US dollar (gold was still pivotal to the system, since the dollar was tied to the price of this precious metal). This created a system of fixed exchange rates, with the dollar becoming the unofficial 'currency' of the capitalist world (though not, of course, the communist one). This gave the international monetary system much greater stability, but also gave the USA enormous advantages in controlling the all-important dollar, and meant that it did not have to worry about exchange rates or balancing its own books.

The US economy and global capitalism thrived in the immediate post-war decades, but it all came unstuck in the 1970s. The age of seemingly endless economic growth came to an abrupt halt amid the global economic recession that began at the beginning of the decade. A sudden rise in oil prices, instigated by the Organization of the Petroleum Exporting Countries (OPEC), allied to the spiralling costs of the Vietnam War, led to the US budget deficit (the amount that spending exceeds tax revenue) growing so large that bondholders and other governments began to lose faith in the dollar holding its value in relation to gold. US President Richard Nixon was forced to end the international convertibility of the dollar to gold in 1971. The system of fixed exchange rates was eventually abandoned and the capitalist world entered a new era of floating exchange rates, which persists to this day – though some countries do continue to peg the value of their currencies to the dollar, or other powerful currencies.

In any case, the world economy survived this shift, and the USA remained the dominant economy of the free world for the remainder of the Cold War. Moreover, while the Bretton Woods system of fixed exchange rates may have 'collapsed' in the 1970s, many of its key institutions survived, including the IMF and the World Bank.

The post-Cold War era: 1990–present

The beginning of the 1990s witnessed a major transformation in the international political economy, with the collapse of communist states in the Soviet Union and Eastern Europe. This event not only appeared to economic liberals to vindicate their belief in the superiority of free-market capitalism over state-run 'communism', but also had major impacts on the global economy. In 1990, the total population of the Eastern bloc was over 400 million people and, despite years of economic stagnation, it had a combined gross domestic product (GDP) of over $3 trillion (CIA 1991). The opening up of these formerly closed states meant a massive influx of new 'consumers' into the global marketplace, and access to their industries and natural resources for foreign investors.

However, despite the optimism – even triumphalism – of many economic liberals at the start of the 1990s, the process of transition from communism to capitalism was longer and harder than many anticipated. Many former communist states (including Russia) experienced a decade of deep recession, with inflation, high unemployment and falling living standards (Roaf et al. 2014). For most living in these states, it was not until the 21st century that any of the economic benefits of capitalist transformation began to be experienced.

In tandem with the fall of communism, the post-Cold War era has seen a massive acceleration of globalisation. In terms of international trade, this has grown in value more than eight-fold: from $3.5 trillion in 1990 to $28.5 trillion in 2021 (UNCTAD 2022: 2). Driving this growth has been a range of political, economic and technological factors. In terms of technology, the rise of the internet and digital communications

technologies have been highly significant. However, so have been moves towards regional trading blocs which increase trade among members (see Chapter 18) and global efforts to lower trade barriers. An important part of this process was the founding of the World Trade Organization (WTO) in 1995. The WTO absorbed the GATT Treaty and regime and added to it measures committing its members not to violate the rules, together with mechanisms to enforce decisions. Hence, the WTO became widely referred to as 'GATT with teeth'. It is discussed in Box 21.3.

Box 21.3 The WTO: key facts (2022)

Headquarters: Geneva (Switzerland)

Members: 164
As well as full members, there are 25 observer states – e.g. Ethiopia and Iran. Only a very small number of states are neither – e.g. Kosovo and Eritrea.

Head: Director-General – since 2021, Ngozi Okonjo-Iweala (Nigeria).

Key functions: implementing the General Agreement on Tariffs and Trade (GATT), resolving trade disputes and promoting free trade.

Decision making: overall steering is by a biannual WTO Ministerial meeting of all member states. Regular decisions are taken by the General Council (which also meets in the guise of the Trade Policy Review Council or the Dispute Settlement Body). All decisions are by 'consensus' – that is, they need to be accepted by all member states.

Debate – for and against the WTO

Criticism	**Defence**
Dominated by the Global North	***Decisions are consensual***

A prominent criticism of the WTO is that it is a vehicle for hegemony, allowing the states of the Global North to dominate those of the Global South, by compelling them to open up their economies, providing the North with new markets and cheap labour. In defence, it can be pointed out that the WTO's decision-making structure is egalitarian since, with no majority or weighted voting (unlike the IMF), any state is free to block proposals of which it disapproves. In addition, many WTO decisions have ended restrictive trade practices in powerful Global North states. Critics respond by observing that consensus, far from empowering the weak, actually reinforces hegemony, since the large WTO delegations of the Global North states, having coordinated their own positions in caucus meetings outside of the formal decision-making structure, are able to put pressure on the smaller delegations of Global South ones and stifle opposition.

Undermining state sovereignty	***Restraining governments is in the global public interest***

Critics have also voiced fears that the WTO is fundamentally undemocratic, since its rules often overturn popular domestic laws. Perhaps the chief grievance of the whole anti-globalisation movement is the view that a *democratic deficit* has emerged, in which global rules are being codified and enforced by a secretive and unaccountable body serving the interests of big business and over which ordinary people have no real influence. Defenders of the WTO, and globalisation in general, contend that freeing up trade is in the common human interest and, if we want to reap the benefits of this collective good, we need to have a global body powerful enough to stop governments acting in their own, rather than their citizens', best interests.

Puts profit before people	***The WTO is about trade – it is up to governments to protect their citizens from exploitation***

Related to the previous two concerns, critics fear that the power of the WTO has served to undermine the security of workers in poorer states and damaged the environment the world over. Freer cross-border trade has led to a 'race to the bottom', in which multinational corporations from rich states take the opportunity to exploit low wages and lax safety standards in poor states, so that an exploitative global division of labour emerges. In defence, it is often suggested that the WTO cannot be held responsible for governments which fail to enact domestic laws to protect their own citizens.

However, despite unprecedented international political efforts to liberalise international trade, the contemporary global economic system is far from being entirely free, and government recourse to mercantilist measures is still regularly seen. It is important to note, though, that developing countries are the ones that tend to impose the highest tariffs – the 'top ten' states for tariff levels include Bermuda, Gambia, Fiji and Chad (World Bank 2022). Their justification for this is that they need protectionist measures to shield their more fragile, developing industries from competition from the lower-priced goods that wealthier states can produce.

Credit: Photo by Steve Kaiser on Wikimedia Commons

This highlights the fact that, even after the end of communism, the tenets of economic liberalism do not go unchallenged. Another clear sign of this is the controversy and political activism that has surrounded the WTO ever since it was founded. For example, when the WTO met in Seattle in 1999, a series of large-scale protests occurred on the city's streets, which included confrontations with the police and violence directed against businesses. This is sometimes interpreted as the beginning of the 'anti-globalisation' movement, a disparate alliance of groups, active around the world, that view globalisation and free trade as mechanisms for extending the dominance of wealthy states over poorer ones, and for riding roughshod over human rights in the name of economic progress. In other words, far from everyone accepts the liberal international economic order.

These challenges from social movements within civil society are not the only ones to the existing global economic order. Another is from the changing balance of power in the world, both politically and economically (Pieterse 2017; Westra 2019). In IPE, attention focuses on emerging market economies (EMEs) – those that have travelled some distance down the road of economic development, and become increasingly integrated in the global economy, but have not yet achieved the full status of being considered 'developed'. Among those states considered to be EMEs are what is sometimes called the E7: Brazil, China, India, Indonesia, Mexico, Russia and Turkey. The label of E7 is deliberately designed to contrast with that of the G7, the alliance of the most powerful developed states, to show how the locus of power in the world may be shifting.

Many EMEs have enjoyed astonishing levels of economic growth over the last few decades, often more than two or three times greater than those of established developed states. Although the sizes of EMEs' populations (and thus labour forces) have not changed dramatically, their productivity has. Indeed, EMEs have become the major growth engines of the global economy. One study predicts that by 2050, the E7 economies may increase their share of world GDP to almost 50 per cent (PwC 2017).

China's economy is already the second largest in the world (in terms of nominal GDP): as of April 2022, its GDP was $19.91 trillion, compared to the USA's $25.35 trillion (IMF 2022). On current projections, China will likely be the largest economy by the end of the decade. Furthermore, China appears to be taking on a significant role in global economic development. Its Belt and Road Initiative (BRI), launched in 2013, involves China spending billions of dollars on infrastructure building and economic integration projects in more than 70 countries (for example, Malaysia, Nigeria and Greece), strengthening connections between Asia, Africa and Europe (Jie and Wallace 2021). In this way, it hopes to build an interdependent market for China's benefit, and bolster its global position (especially vis-à-vis the USA). However, while many of the countries receiving Chinese support may well benefit from the initiative, gaining much needed infrastructure investment, it does not come without potential downsides. Critics have accused China of engaging in 'debt trap diplomacy' – financing infrastructure projects through loans that it knows recipient countries will be unable to repay, and then using their debt to gain leverage over them. As such, China may be accused of acting in a neo-colonial fashion – demonstrating that this is not necessarily the sole preserve of Western states.

Next, it will be useful to examine some of the major approaches to the study of international political economy.

Major approaches to IPE

Traditionally, three main approaches to IPE are identified. Two of these we have already encountered – mercantilism and economic liberalism; the third is Marxism. This section will begin by exploring these three perspectives, before giving an overview of more recent theoretical developments.

Mercantilism

As already seen, mercantilism is the earliest approach to political economy of the three main ones, achieving dominance in the early modern period of the 16th to 18th centuries. Even if the label itself is rarely used any longer by modern economists or politicians, its principles have continued to be espoused by contemporary thinkers and policy-makers.

Mercantilist thinking exhibits certain core tenets (Magnusson 2015; Horrocks 2017). One of these is *self-sufficiency*. Mercantilists tend to share with realists pessimistic assumptions about human nature and state behaviour: the world is anarchic, and other states can rarely be fully trusted, since their general orientation is to be inward-looking and self-serving. This leads mercantilists to believe that states should focus on hoarding and protecting what they have, and reduce reliance on other states as much as possible.

An extreme manifestation of self-sufficiency is the policy known as autarky, which is the pursuit of total self-reliance. This might be relatively straightforward for states blessed with all the natural resources they might need, but for most this is a far from easily realisable goal. Attempts at achieving total self-reliance in the modern age have typically been associated with states driven by ultra-nationalist and imperialist ideologies: those that have no qualms about taking whatever resources they require from other states, to allow them to be 'self-sufficient'. Thus, the global conquests of the major imperialist powers, the rise of fascism and Nazism, and Iraq's expansionist activities of the 1980s and 1990s can all be seen in this context. In the 21st century, the global recession of 2008–13 discussed at the start of this chapter helped revive mercantilist thinking again. Since total self-reliance is generally not a realistic prospect anymore (if it ever was), Mercantilist-informed strategies today aim, instead, for the accumulation of as many resources as possible, together with policies to shield domestic industries from competition.

Mercantilists' view of international economics is, therefore, that it is fundamentally competitive, not cooperative. Mercantilists reject the notion that international trade leads to everybody benefiting in the long run – in other words, it is not a 'win–win' system, but a 'win–lose' one. For example, if a country imports cheap food from abroad this may be beneficial for consumers and the exporting country, but is likely to undermine the domestic agriculture industry. This being the case, states should pursue 'beggar thy neighbour' policies, pursuing ones that benefit themselves and disadvantage others, to ensure that they are among the winners (and their rivals among the losers) of the global economy.

Flowing from these beliefs – in self-sufficiency, the fiercely competitive nature of the international economy and that not everyone can be a 'winner' – it is unsurprising that mercantilists believe that governments *should* adopt strongly activist roles, to protect the interests of their state and citizens. As such, governments should be active both in supporting their own domestic industries and in hindering those of other states. One of the most common ways of doing this is by enacting policies of protectionism, designed to insulate domestic industries from foreign competition. The most common protectionist strategies are outlined in Box 21.4.

Box 21.4 Forms of protectionism

Protectionist policies that a state may pursue include the following:

- *Tariffs* – placing a form of tax on imports
- *Currency devaluations* – lowering the value of one's own currency, to make exports cheaper and imports more expensive
- *Quotas* – allowing imports only up to a certain amount
- *Export subsidies* – providing monetary support to exporters, to help them sell their goods and services abroad more cheaply
- *Domestic subsidies* – providing monetary support to domestic industries, so that they compete against foreign imports
- '*Red tape*' – using bureaucratic regulations to hamper foreign competition; e.g. by insisting on stringent product standards

The progression of the liberal international economic order has been marked by political efforts to reduce or outlaw governments' recourse to these various measures.

Economic liberalism

Economic liberalism emerged in the era of industrialisation and the Enlightenment towards the end of the 18th century, as a branch of the wider political and philosophical liberal movement that had swept through Western Europe and North America (see Chapter 7). The approach is underpinned by the core liberal tenet that people are 'naturally' inclined to cooperate with each other, and can be trusted to control their own destinies without the need for highly interventionist governments to prevent chaos and disorder.

Among the major liberal thinkers of the 18th and 19th centuries who sought to apply the logic of liberalism to the economic sphere were Adam Smith (see Box 21.5) and David Ricardo. Economic liberals share a number of beliefs and principles that distinguish their perspective from that of mercantilism (Smith 2013; Parvini 2021).

Box 21.5 Adam Smith (1723–90)

Credit: Photo by scotlandstudycentre on Pixabay

An 18th-century Scottish philosopher turned economist, Adam Smith is widely viewed as the father of economic liberalism and, possibly, of the discipline of Economics itself. Smith's landmark work, *The Wealth of Nations* (1776), developed an economic rationale for why free trade is positive and, ultimately, to the advantage of all. He reasoned that markets free from government interference are more likely to achieve mutually beneficial cooperation through an efficient division of labour. A well-known illustration used in his book concerns the manufacture of pins. Ten people making pins in which they cooperate – by dividing up the tasks involved in the pins' production and each specialising in one task – will make more pins than ten people working independently. In the competitive and selfish arena of international commerce, the less efficient method operates to the detriment of everyone. *The Wealth of Nations* greatly influenced British policy-makers and also the founding fathers of the United States of America (who declared their country's independence the same year that Smith's book was published).

Perhaps most fundamental, economic liberals believe in free markets and free trade. In the long run, they argue, a free economy benefits everyone who participates – in other words, it is a 'win–win' system. Consequently, they reject mercantilists' preference for activist government, instead favouring minimal government involvement in the economy. In terms of international trade, businesses should not be restricted in exporting their goods, while imports from abroad should not be limited by protectionist measures.

Adam Smith explained the benefits of the free market via the metaphor of the 'invisible hand'. As he wrote in *The Wealth of Nations*: 'It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own self-interest' (Smith 1776/1991: 8). His point is that a free-market economy does not require conscious direction – by, for example, the government – to produce its benefits. Instead, it happens 'spontaneously' by the cumulative process of individuals simply following their self-interests. We all ultimately benefit from this because we all get to enjoy the fruits of everyone else's labour.

Government interference in the economy simply distorts the workings of the free market, and makes it function less efficiently. For example, protectionist governments, reluctant to allow imports into their country for fear of exposing their domestic industries to cheaper competition, reduce the overall volume of international trade and thereby make everyone poorer. As a consequence, citizens have to pay more than they otherwise would for goods that were traded on the open world market, and lose out from the restriction that is placed on the overall amount of money that might be generated from free trade. Ironically, economic liberals argue, self-serving governments, though operating in the name of protecting their own citizens, actually end up disadvantaging them.

An English protégé of Adam Smith, David Ricardo, built on Smith's work by developing a further rebuttal to mercantilist approaches in the theory of *comparative advantage*. This theory provides an economic rationale for why free trade produces benefits for *all* states. The theory's starting point is the observation that different states are able to produce goods at different prices – for reasons such as climate, access to natural resources or the skills of workers. Consequently, a state may have a comparative advantage if it is able to produce goods more cheaply than its competitors – this does not mean that the latter *cannot* necessarily produce them, but that they cannot do so as *cheaply*. Everyone benefits from free trade because consumers can buy goods from wherever they are cheapest to produce.

For example, imagine a simple scenario in which State A can produce mobile phones more cheaply than State B, while State B can produce bananas more cheaply than State A. According to the theory of comparative advantage, both would benefit from each specialising in producing the goods they can more cheaply, and then freely trading with the other. In this way, consumers in both states get both mobile phones and bananas at the cheapest possible prices. If, by contrast, States A and B adopted protectionist, mercantilist polices, it *might* be possible for each to become self-sufficient in mobile phones and bananas – for example, even very cold countries *can* grow bananas, in expensive-to-heat greenhouses – but consumers would have to pay more overall as a result.

In addition to the economic rationale for free trade, economic liberalism, in line with liberal political thought more broadly, argues that there are political gains to be had from supporting this perspective. Most notably, there is 'democratic peace theory', which argues that peace is created by the global spread of liberal democracy, because democracies do not go to war with each other (see Chapter 7). However, in parallel to this is the argument that states that are heavily interdependent in trade and commerce are unlikely to go to war with each other, either. This is sometimes called capitalist peace theory (Gartzke 2007). There may, therefore, be strong political motives for embracing free trade as much as economic ones.

Marxist approaches

Marxist approaches to IR more broadly are explored in Chapter 8. Here we shall focus on Marxist views of political economy.

Despite their differences, both mercantilism and economic liberalism share the belief that the purpose of theorising about political economy is to understand how the international system works and

to offer prescriptions to policy-makers that will ensure its perpetuation. By contrast, Marxism – while also seeking to understand the system – aims to do much more than this. As Marx wrote, 'Philosophers have hitherto only *interpreted* the world in various ways; the point is to *change* it' (1845/2002). In other words, understanding the system – capitalism – is not an end in itself; the whole purpose is to better understand how to transform and transcend it (through revolution). It is important to note in this context that Marx's best-known contribution to economics, *Capital*, has as its subtitle, *A Critique of Political Economy* (1867/1995). Marx did not see himself as offering just another theory of political economy, but as arguing for the overthrow of both the capitalist system and what he saw as its theoretical handmaiden.

Marx's writings engage heavily with classical economists like Smith and Ricardo. Consequently, some of the same elements are to be found in his work. For example, a cornerstone of Marx's thought is the labour theory of value; that is, the belief that the value of a commodity is determined by the labour time invested in it. Marx did not originate this theory (both Smith and Ricardo also subscribed to it), but he used it in a very different way than earlier writers. For Marx, a commodity requires a certain amount of labour time to produce, the average time of the averagely skilled worker, which he calls *socially necessary labour time*. However, when employed by capitalists, workers contribute an extra amount of labour, which Marx calls *surplus labour*, to add value to commodities, which he calls *surplus value*. This surplus value is the source of capitalists' profits. A crucial implication, therefore, is that profits are not – as mainstream economists argue – rewards for capitalists' entrepreneurialism, but derived from the extra labour workers have to perform above what is socially necessary. As such, capitalism is a system that does not pay workers the full value of their labour, with capitalists always seeking to extract as much surplus value from them as possible by keeping wages low.

This is a somewhat simplified account. As Marx fully recognised, many other factors – including political and social ones – come into play to explain actual prices and wages, not least the relative power of workers versus capitalists at any given time. When trade unions are strong, for example, they may be able to achieve higher wages for their members than at times when they are weak. However, Marx's understanding that capitalism is a system that, by its very nature, is centred on a continual class conflict between workers and capitalists, remains fundamental to his thought.

In the 20th century, later Marxists developed Marx's ideas, including to take into account the increasingly interconnected nature of the global economy. Notably, later Marxists have taken the analysis that Marx developed largely to explain how capitalism works *within* nation-states, and applied it to the international level. For example, some of the most famous passages in *Capital* concern the iniquities of the 19th-century British factory system, which forced British workers (including children) to labour long hours in dangerous conditions for British capitalists. Today, Marxist writers instead often focus on the exploitative nature of relations between capitalists in one state and workers in another. Thus, in relation to 'sweatshops' in developing countries – in which workers may be forced to endure similarly harsh working conditions to those of Victorian factory workers – even though these may be located in non-Western states, profits still often flow back to Western capitalists. Capitalism may have become much more globalised, but its inner dynamics remain the same.

In terms of how Marxists have sought to theorise the evolution of global capitalism, Lenin – writing in the early decades of the 20th century – argued that imperialism was the next (indeed, highest) stage in capitalism's development since Marx's time. He identified trends such as the growth of monopolies within capitalism and the increased reliance by the major Western powers on exploiting overseas colonies (Lenin 1917/1963). Later Marxists have continued to focus on new developments (Fine and Saad-Filho 2012). This includes the creation of global financial institutions like the IMF and World Bank, and the role Marxists see these as playing in furthering the interests of the most advanced capitalist states that created them. Similarly, there are the continuing political and economic imbalances between developed and developing states even after decolonisation occurred following World War II. Although developing states may have achieved formal political independence, Marxists see them as remaining highly dependent economically, both on wealthy states and transnational corporations.

Modern developments

IPE has become a diverse and multifaceted field, in which writers draw from many different traditions – including realism, liberalism, Marxism and more. To illustrate some of its more recent concerns, we will attend to three further approaches and theories: dependency theory, hegemonic stability theory and open economy politics.

Dependency theory emerged in the 1960s, as a critique of the then dominant paradigm of modernisation theory (Frank 1967; Dos Santos 1970). The latter posits that all societies pass through essentially the same stages of development, moving from 'primitive', subsistence-level economies eventually to become wealthy, industrial states. While some states may have passed through these stages much more quickly – Western ones – states in the rest of the world need only to follow the same path, embracing liberal political and economic models, and they will eventually 'catch up'. Dependency theory arose first in Latin America to explain why underdevelopment in fact appeared to be a *persistent* feature of many non-Western societies, and why universal progress and prosperity did *not* appear to be just around the corner. The reason, theorists argue, is because developed Western states have (deliberately) kept non-Western ones in a state of dependency. The world is divided into a 'core' of wealthy states, which exploit the labour and resources of the rest, which are consigned to the 'periphery'. It is this which explains why underdevelopment is not simply a temporary condition for developing states, but a permanent feature that keeps most of the world trapped in poverty and underdevelopment.

Dependency theory is often rooted in Marxist thinking, though not all adherents are Marxists. It has, too, been subjected to much criticism. Economic liberals tend to argue that it is not the global political and economic system that holds countries back from developing, but domestic factors (such as corruption) and a failure fully to embrace global free trade – the solution, in simple terms, is *more* capitalism, not less. Other critics argue that the two-fold division of the world into a core and a periphery oversimplifies: while some states may be seemingly stuck in cycles of poverty and underdevelopment, this is far from true of all non-Western ones. For example, states like China and India (which for centuries existed under British colonial rule) have enjoyed very high levels of economic growth in recent decades (even if their citizens have not all benefited equally). More broadly, a crucial 'tipping point' was reached in 2008, when states classified as developing first accounted for over half the world's GDP – and their share has continued to grow since (OECD 2019). In other words, economic development *is* possible in historically underdeveloped and exploited states, even in a global capitalist system.

A very different theory within IPE is **hegemonic stability theory**. In IPE, a hegemon is a state with sufficient power and motivation to dominate international affairs in ways that allow it to create rules and institutions to further its interests. Hegemonic stability theory posits that the international system is more likely to be stable when there is a single, dominant hegemon. For example, Charles Kindleberger, a key theorist who argues in this vein, contends that a vital reason behind the economic and political crises of the inter-war years – culminating in the Great Depression and the rise of fascism – was that there was not a dominant hegemon to provide leadership and stability (Kindleberger 1973). The major European powers were too weakened by World War I, and the USA appeared reluctant to take on the mantle, retreating into isolationism.

However, hegemonic stability theory has also been challenged, not least because it seems to offer a justification for great-power domination of the global system. Furthermore, Keohane argues that it *is* possible to have international stability in the absence of a single hegemon, through multilateral cooperation (Keohane 1984). Keohane, a leading originator of liberal institutionalism – whose adherents believe in the creation of multilateral international institutions based on liberal principles as the best way to create global stability – thus challenges the assumptions of both hegemonic stability theory and neo-realism.

Open economy politics is a paradigm that emerged in the 1990s and has since become an influential approach in explaining why states adopt particular economic policies – for example, choosing between protectionist or free trade policies. As David Lake explains, the approach has three main elements (Lake 2009). First, it focuses on the *interests* of actors, both individuals and groups. For example, it asks who benefits and who loses from the adoption of particular economic policies. The former

will lobby for them, while the latter will lobby against them. Second, it analyses the roles of *domestic institutions*, including those of government, in both executive and legislative branches. Institutions aggregate conflicting societal interests and shape the bargaining over policies that takes place between different groups. Third, it looks at *international bargaining*. When the different interests *within* states have completed a process of negotiation, a 'national' economic policy will have emerged – but this will then often require bargaining with *other* states. As domestically, this may involve doing so within institutions, but this time international ones, potentially resulting in new treaties and agreements. Taken '[t]ogether, interests, institutions, and international bargaining explain the choice of policies by countries and the outcomes experienced by the world economy' (Lake 2009: 230).

As this all suggests, open economy politics is a more 'grounded', empirically focused approach than some of the others discussed, and may more readily lend itself to concrete research programmes than theories that focus on higher-level, system-wide analyses. However, it has also been criticised. For one, there is the extent to which it reflects reality – do individuals always have clearly defined interests, and are institutions always effective in mediating between them? Furthermore, as an approach, it implicitly accepts the basic features of the liberal international economic order, the system of free trade that operates within the framework created after World War II. To critics of free-market capitalism, while open economy politics may explain why particular economic policies are adopted, it offers little in the way of any critical perspective on the system itself.

Conclusion

This chapter has shown that the global economic system has gone through various phases over the last half a millennium – at different times, different states have dominated, as have different political and economic philosophies. Within IPE, there are also varying perspectives on how to understand these developments.

We may, perhaps, be living in another transitional period, with the liberal order that has dominated the international political economy since the close of World War II facing significant challenges, especially with the rise of non-liberal states like China. While China has undoubtedly embraced capitalism and international trade in the 21st century, this does not mean that it has also embraced liberalism. Politically, China remains a one-party, authoritarian state; and economically, it operates highly statist, interventionist policies. In all probability, the power and influence of this non-liberal capitalist power will continue to grow in future, including within international institutions like the IMF. However, this does not necessarily mean a complete upending of the liberal order is imminent. Whether or not this happens depends not only on the power and resilience of the world's major liberal states in defending it, but on which model of economic development the rest of the world chooses to follow.

Resource section

Questions

1. Contrast mercantilist and economic liberal theories of international political economy and consider which approach is most apparent in the contemporary world.
2. Are Marxists right to see capitalism as an exploitive system that benefits the few over the many?
3. Which of dependency theory, hegemonic stability theory and open economy politics do you find the most compelling?
4. Is China likely soon to eclipse the USA as the dominant state in the international system? What are the implications for the international political economy if it does?

Recommended reading

Best, J., Hay, C., LeBaron, G. and Mügge, D. (2021) 'Seeing and not-seeing like a political economist: the historicity of contemporary political economy and its blind spots', *New Political Economy*, 26(2): 217–228.

Reflects on the nature and history of IPE in terms of its 'blind spots': those aspects that have been neglected and marginalised, including racial and gender dimensions.

Boettke, P and Powell, B. (2021) 'The political economy of the COVID-19 pandemic', *Southern Economic Journal*, 87(4): 1090–1106.

A useful example of how the insights of IPE can be applied to contemporary issues, this article analyses the Covid-19 pandemic from the standpoint of political economy.

Phillips, N. (2017) 'Power and inequality in the global political economy', *International Affairs*, 93(2): 429–444.

This article examines the major drivers of socio-economic inequality in the global political economy.

Online resources

Brookings Institution – Global Economy and Development – www.brookings.edu/program/global-economy-and-development/

European Centre for Political Economy – https://ecipe.org/

International Monetary Fund – www.imf.org/en/Home

OECD – Global Economy – www.oecd.org/coronavirus/en/themes/global-economy

World Bank – www.worldbank.org/en/home

World Economic Forum – www.weforum.org/

World Trade Organization – www.wto.org/