

criticized for imposing identical prescriptions for economic development on all countries, regardless of what conditions prevail locally. Developing societies are expected to adopt the free market blueprint (sometimes called the 'Washington Consensus') – opening their economies up to foreign investment, financial de-regulation, reductions in government expenditure and budgetary deficits, the privatization of government-owned enterprises, the abolition of protection and subsidies, developing export orientated economies – or risk the withholding of much needed aid and finance. And because they are required to remove national controls on capital movements – which make it possible for states to reach their own conclusions about investment and spending priorities – the direction of their economic development is increasingly set by amorphous financial markets which act on profit opportunities rather than out of any consideration of national or community interest.

Arguments for free trade are still powerfully made on the grounds of economic efficiency and as the only way of integrating the developing world into the wider global economy. Protectionism within the North is said primarily to hurt the South by pricing their economies out of markets in the industrialized world, thus denying them the opportunity to modernize their economies.

For leading players, however, free trade is often non-reciprocal and an ideological weapon used to regulate the economic development of subordinate societies. Their rhetoric supporting the sanctity of market principles is rarely matched by their own economic behaviour. This tendency, together with fundamental changes to the structure of the world economy and the forms of international trade, casts some doubt on the extent to which liberals can explain the globalization of the world economy solely on their own terms.

Sovereignty and foreign investment

The enormous volumes of unregulated capital liberated by the collapse of the Bretton Woods system in the early 1970s, have transformed the relationships between states and markets. Credit (bonds and loans), investment (Foreign Direct Investment, or FDI) and money (foreign exchange) now flow more freely across the world than commodities. The resulting increase in the power of transnational capital and the diminution of national economic sovereignty is perhaps the most dramatic realization of liberal economic ideas (Strange 1996, 1998).

The relationship between a nation's economic prosperity and the world's money markets is decisive. Because most states are incapable of generating sufficient endogenous wealth to finance their economic development, governments need to provide domestic economic conditions

which will attract foreign investment into their countries. In a world where capital markets are globally linked and money can be electronically transferred around the world in microseconds, states are judged in terms of their comparative 'hospitality' to foreign capital: that is, they must offer the most attractive investment climates to relatively scarce supplies of money. This gives the foreign investment community significant leverage over policy settings and the course of a nation's economic development generally, and constitutes a diminution in the country's economic sovereignty.

The power of transnational finance capital in the modern period can scarcely be overestimated. The volume of foreign exchange trading in the major financial centres of the world, estimated at over \$US1.5 trillion per day, has come to dwarf international trade by at least sixty times. UN statistics suggest that the world's 100 largest TNCs, with assets of over \$US5 trillion, account for a third of the total FDI of their home states, giving them increasing influence over the economies of host countries.

The brokers on Wall Street and in Tokyo, the clients of the 'screen jockeys' in the foreign exchange rooms, and the auditors from credit ratings agencies such as Moody's and Standard & Poor's, now pass daily judgements on the management of individual economies, and signal to the world's financial community the comparative profit opportunities to be found in a particular country. Inappropriate interventionary policies by government can be quickly deterred or penalized with a (threatened) reduction in the nation's credit rating, a 'run' (sell off) on its currency or an investment 'strike'. The requirements of the international markets can be ignored only at a nation's economic peril. Not only have nation-states lost direct control over the value of their currencies and the movements of capital around the world, they can no longer determine the institutional settings in which capital markets operate. Neo-liberal financial commentators regard this development as a positive change, believing that on the question of allocating resources, markets rather than the governments know what is in peoples' best interests.

Finance markets, dominated by large banks and financial institutions, insurance companies, brokers and speculators, exist only to maximize their own wealth. There is no compelling reason for them to act in the interests of the poor, the homeless, the infirm or those who are deprived of their basic human rights by their own governments. States which cede economic sovereignty to these global players in the name of free trade and commerce therefore run the risk of elevating private commercial gain to the primary foreign policy objective of the state.

When the foreign investment community is freed from state barriers and controls, and able to choose the most profitable location for its capital, it has the effect of homogenizing the economic development of

nation-states across the globe. In what is effectively a 'bidding war' for much-needed infusions of capital, states are driven by the lowest common denominator effect to reduce their regulations, standards, wages and conditions, in order to appear attractive to the investor community. Priority is given to the drive for efficiency and profits. The threat of disinvestment becomes the stick for markets to wield over the heads of government. For liberals, this is a pleasing reversal of modern history which they see as a struggle for liberation from the clutches of arbitrary state power. Ironically, in many instances the key to attracting overseas investment is for the host government to provide the transnational investor with subsidies and protection from market forces. In some cases, this is the only way states can win and maintain the confidence of global markets.

The ill-fated Multilateral Agreement on Investments (MAI) was a vivid illustration of just how far governments in the developed world have been prepared to follow liberal advice and surrender their discretionary economic power to the markets. In this case Organization for Economic Cooperation and Development (OECD) members were offering voluntarily to restrict their own ability to discriminate against foreign capital. The MAI is a reminder that, as with the establishment of national markets in the nineteenth century, globalization is not the result of the gradual and spontaneous emancipation of the economic sphere from government control. On the contrary, it has been the outcome of conscious and sometimes violent state intervention by advanced capitalist states. Just as domestically the labour market can be 'freed' only by legislative restrictions placed on trades unions, the creation of the post-war liberal trading regime and the de-regulation of the world's capital markets in the 1970s required deliberate acts by interventionary states.

During the current phase of globalization, national economic sovereignty has not so much been lost but either enthusiastically given away or begrudgingly surrendered. The state's capacity to direct the national economy has been deliberately and significantly undercut by the globalization of relations of production and exchange. Significant sovereign power has been ceded to bond holders, funds managers, currency traders, speculators, transnational banks and insurance companies – groups that by definition are democratically unaccountable in any national jurisdiction. In effect, the world economy has come to resemble the global strategic environment. It has become anarchic in character and, as a consequence, the competition for economic security is as intense as the search for strategic security.

Unsurprisingly, concern about a growing 'democratic deficit' has arisen within liberal political philosophy. David Held's (1995) advocacy of cosmopolitan democracy is seen as somewhat utopian by hard-nosed

realists, however it is a serious attempt to bring some of the forces of globalization under a degree of popular control. Proposals such as regional parliaments and the devolution of sovereign power to regional bodies, universal human rights benchmarks entrenched in domestic jurisdictions and monitored by international courts, radical reform of the United Nations and the promotion of a global civil society are serious suggestions for extending and modernizing democratic politics. The work of Held and his colleagues is an important reminder that as well as rendering significant economic change, globalization has important political challenges and implications which liberals cannot ignore (Held 1995; Archibugi and Held 1995; Archibugi 1998).

Non-state terrorism

Whether or not the current wave of Islamic militancy is the latest chapter in a long-standing revolt against the West, there can be little doubt that it represents a direct challenge to both the claim that liberal democracy is the universal destination for the species and the assumption that globalization is inexorable. However incoherent and unlikely it is as a political programme, Islamic terrorism is profoundly anti-secular and an opponent of liberal modernity (Gray 2004).

It therefore seems premature and misleading for liberals to claim that the emergence of Al-Qaeda and affiliated groups which perpetrate transnational terrorism constitutes a victory for the deterritorialization of world politics (Buzan 2003: 297, 303). Rather as David Harvey notes, 'the war on terror, swiftly followed by the prospect of war with Iraq ... [has] allowed the state to accumulate more power', a claim difficult to refute and one that poses an unexpected new challenge to liberals who believed that globalization was finally eroding the sovereign significance of the state (Harvey 2003: 17). The national security state has been revived.

The resuscitation of state power across the industrialized world after the 9/11 attacks has taken numerous forms, including new restrictions on civil liberties, greater powers of surveillance and detention, increased military spending and the expansion of intelligence services. The threats posed by Islamic terror and the dangers of Weapons of Mass Destruction (WMD) have also been met by an increase in state intervention around the world, in particular by US-led coalitions acting in Afghanistan and Iraq. With each subsequent terrorist assault, states which consider themselves innocent victims have been emboldened to interfere in each others' internal affairs – even pre-emptively.

Pre-emption, the disarmament of states alleged to possess WMD, regime change, humanitarianism and the spread of democracy have all been invoked as public justifications for these interventions, although

critics have pointed to traditional geo-strategic rationales beneath the surface. Many states, such as China, Israel and Russia, have also used the cover provided by the 'war against terror' to settle domestic scores with secessionists, dissidents and those resisting their territorial occupations. Others seem to be victims of 'blowback', reaping disastrous and unintended consequences from earlier foreign policy actions. Regardless of what the true motives of these interventions are, the irony of socially conservative, economically neo-liberal governments expanding the reach and size of government should not be lost on anyone (Johnson 2002).

The return of the overarching state is perhaps an unsurprising response to community calls for protection from non-state terrorism. When citizens of a state require emergency medical relief, as many victims of the Bali bombings did in October 2002, there is little point appealing to market forces for help. Nor can those responsible for attacks such as the Beslan school atrocity in September 2004 be hunted down, disarmed and prosecuted by privately owned TNCs. Even if the state is no longer prepared to insulate its citizens from the vicissitudes of the world economy, it is still expected to secure them from the threat of terrorism. Only the state can meet these and many other challenges such as 'border protection' and transnational crime. There are no market-based solutions to the dangers posed by what seems to be the latest chapter in the revolt against the West.

Since the end of the Cold War, realists such as Kenneth Waltz have argued that in the absence of effective countervailing pressures, the United States is likely to become increasingly unilateral in seeking to secure its foreign policy interests, and in so doing rely on military power to realize its vision of a new world order. The 'war against terror' has seemingly changed little in this regard. If anything, these events have enhanced a trend which some liberals had either believed or hoped had passed into history.

The Marxist historian Eric Hobsbawm has observed that 'the basic element to understanding the present situation is that 9/11 did not threaten the US. It was a terrible human tragedy which humiliated the US, but in no sense was it any weaker after those attacks. Three, four or five attacks will not change the position of the US or its relative power in the world' (Hobsbawm 2002).

This view is similar to Waltz's claim that the problem of terrorism does not challenge the continuities of international politics. 'Although terrorists can be terribly bothersome', says Waltz, 'they hardly pose threats to the fabric of a society or the security of the state ... Terrorism does not change the first basic fact of international politics – the gross imbalance of world power' in favour of the United States. 'Instead, the effect of September 11 has been to enhance American power and extend

its military presence in the world' (Waltz 2002: 348–53). So much for the end of the nation-state.

Realists in the United States also led the intellectual opposition to Washington's attack on Iraq in March 2003, arguing that Saddam Hussein had been successfully contained, that he was prevented from using his WMD against the West because of the likely consequences to him and that for similar reasons he couldn't risk passing these weapons – if he in fact possessed them – to groups such as Al-Qaeda. As during the Second Cold War, realists found themselves in the unusual position of being at the limits of respectable dissent in debates over the Iraq war as a consequence of the influence of the misnamed neo-conservatives, whose muscular liberalism underwrote the administration of George W. Bush (Mearsheimer and Walt 2002).

Conclusion

At the beginning of this chapter, it was argued that liberalism was an 'inside-out' approach to international relations, because liberals favour a world in which the endogenous determines the exogenous. Their challenge is to extend the legitimacy of domestic political arrangements found within democratic states to the relationships between all nation-states. To put it another way, liberals believe that democratic society, in which civil liberties are protected and market relations prevail, can have an international analogue in the form of a peaceful global order. The domestic free market has its counterpart in the open, globalized world economy. Parliamentary debate and accountability is reproduced in international fora such as the United Nations. And the legal protection of civil rights within liberal democracies is extended to the promotion of human rights across the world. With the collapse of Communism as an alternative political and economic order, the potential for continuity between the domestic and the international became greater than in any previous period.

Fukuyama had reason to be optimistic. The spread of liberal democracies and the zone of peace was an encouraging development, as is the realization by states that trade and commerce is more closely correlated with economic success than territorial conquest. The number of governments enjoying civilian rather than military rule is increasing, and there are signs that ethical considerations and ideas of human justice have a permanent place on the diplomatic agenda. The collapse of Marxism as a legitimate alternative political order removes a substantial barrier to the spread of liberal democracies, and there can be little doubt that the great powers are now much less inclined to use force to resolve their

political differences with each other. It appears that liberal democracies are in the process of constructing a separate peace.

The globalization of the world economy means that there are few obstacles to international trade. Liberals want to remove the influence of the state in commercial relations between businesses and individuals, and the decline of national economic sovereignty is an indication that the corrupting influence of the state is rapidly diminishing. TNCs and capital markets wield significant influence over the shape of the world economy, in the process homogenizing the political economies of every member state of the international community.

Globalization has undermined the nation-state in other ways that have pleased liberals. The capacity of each state to direct the political loyalties of its citizens has been weakened by an increasing popular awareness of the problems faced by the entire human species. The state cannot prevent its citizens turning to a range of sub-national and transnational agents to secure their political identities and promote their political objectives. Sovereignty is no longer an automatic protection against external interference called 'humanitarian intervention'. And decision making on a range of environmental, economic and security questions has become internationalized, rendering national administration often much less important than transnational political cooperation.

Despite these important changes, there are also counter-trends which can be identified. Realists would argue that liberals such as Ohmae are premature in announcing the demise of the nation-state. They would remind the enthusiasts for globalization that as a preferred form of political community, the nation-state still has no serious rival. There are currently over 200 nation-states in the world asserting their political independence.

Realists cite a number of important powers retained by the state despite globalization, including monopoly control of the weapons of war and their legitimate use, and the sole right to tax its citizens. They would argue that only the nation-state can still command the political allegiances of its citizens or adjudicate in disputes between them. And it is still only the nation-state which has the exclusive authority to bind the whole community to international law.

They would question the extent to which globalization today is an unprecedented phenomenon, citing the nineteenth century as period when similar levels of economic interdependence existed. They would also point to the growing number of states which reject the argument that Western modernity is universally valid or that political development always terminates at liberal-capitalist democracy. More recently realists have highlighted the expanding power and reach of the state as a result of the latest wave of anti-Western Islamic militancy – a significant reversal for liberals

who anticipated the imminent decline of the nation-state in modern life. Islamism is a direct challenge to liberal assumptions about economics and politics terminating at a liberal capitalist consensus.

Unpredictable challenges of this kind have left liberalism on the back foot, questioning whether the linear path to improving the human condition is as straight and as inexorable as they thought only a few short years ago.