CHAPTER THREE

The Dynamics of the International Political Economy

THE MARKET system has become a major factor in shaping modern society; market competition and the responsiveness of economic actors to relative price changes propel society in the direction of increased specialization, greater efficiency, and (if liberal and Marxist predictions ultimately prove correct) the eventual economic unification of the globe. Marx observed that the market, or capitalist system, was a revolutionary departure in world history and also argued that traditional cultures and political boundaries would crumble in its path as it moved inexorably toward the full development and integration of the planet's productive capacities.[1]

Although the market system is driven largely by its own internal dynamics, the pace and direction of its forward movement are profoundly affected by external factors. The interaction of the market and environmental conditions account for much of the economic and political history of the modern world. Among the so-called exogenous variables that affect the operation of markets are the structure of society, the political framework at the domestic and the international levels, and the existing state of scientific theory and technological development, all of which constitute constraints and/or opportunities affecting the functioning of economic actors. However, the market itself affects and transforms external factors in important ways; it dissolves social structures, alters political relations, and stimulates both scientific and technological advance. An understanding of the ways in which market forces and external factors affect one another is essential to comprehension of the dynamics of the international political economy.

CONTEMPORARY THEORIES OF THE INTERNATIONAL POLITICAL ECONOMY

Three contemporary theories accounting for the emergence, expansion, and functioning of the international political economy have

[1] The *Communist Manifesto* is a paean to the productive and unifying power of international capitalism.

gained influence in recent years. The first, derived principally from economic liberalism, will be called the theory of the "dual" economy; it regards the evolution of the market as a response to the universal desire for increased efficiency and the maximization of wealth. The second, strongly influenced by Marxism, is best identified as the theory of the Modern World System (MWS); the world market is essentially a mechanism for the economic exploitation of the less developed countries by the advanced capitalist economies. The third, closely but not entirely associated with political realism, has become known as the theory of hegemonic stability; it interprets the rise and operation of the modern international economy in terms of successive liberal dominant powers.[2] Although these theories contradict one another in a number of particulars, they can also be considered complementary in other ways, and together they provide important insights into the reasons for the dynamics and functioning of the international political economy.

The Theory of the Dual Economy

The theory of the dual economy[3] (dualism) asserts that every economy, domestic and international, must be analyzed in terms of two relatively independent sectors: a modern, progressive sector characterized by a high level of productive efficiency and economic integration, and a traditional sector characterized by a backward mode of production and local self-sufficiency. The theory argues that the process of economic development involves the incorporation and transformation of the traditional sector into a modern sector through the modernization of economic, social, and political structures. Global integration of markets and institutions is the consequence of an inexorable movement of economic forces toward higher levels of economic efficiency and global interdependence. Individualism, economic rationality, and maximizing behavior drive out age-old values and social mores.

In this view, the rise of a market economy is the natural result of the unleashing of market forces. Human beings, in their natural tendency "to truck and barter," will expand their economic activity as external constraints are removed and opportunities unfold. Advances in communications and transportation, the development of efficient economic institutions, and the reduction of transactions costs (the costs of doing

[2] The expression, "the theory of hegemonic stability," was coined by Robert Keohane (1980). "Hegemony" comes from the Greek word for political leadership. In the opinion of some writers, however, it has a pejorative ring and they prefer the term *leadership* itself.

[3] Although the concept of the dual economy is as old as Adam Smith, Hicks (1969) is an excellent recent statement of the argument.

business) have led to the continuous displacement of traditional economies by modern ones. Dualism views the modern world economy as having evolved through the global expansion of the market mode of production and the incorporation of new areas into the international economy, rather than as having suddenly come into existence in the sixteenth century through an act of force by European capitalist states. The modern sector has displaced the backward sector gradually as more and more societies have adapted to the market mode of economic organization.

The primary forces at work in this process have been economic, organizational, and technological; they include innovation of new products and productive techniques, opening of new markets and sources of supply, and new means of organizing and managing economic activities (Schumpeter, 1950). The monetarization of economic life, the rise of cities, and advances in communications and transportation such as the telephone and the railroad have been particularly important; these developments have reduced the costs of economic transactions and thereby facilitated the expansion of individual markets and their integration into an evolving global economic interdependence. The process of economic evolution is driven by market competition and the price mechanism toward ever higher levels of productive efficiency and wealth maximization. Inefficient actors are forced to adjust their behavior and to innovate or else face economic extinction. The resulting expansion of markets, accumulation of capital and other factors of production, and innovation of new technologies and organizational forms have set the world on a course of continuous economic growth and global interdependence. Although this process of economic modernization may be affected in the short run by social and political developments, in the long run it is largely independent of these external influences; fundamentally, the creation of the modern world is a consequence of factors internal to the market.

The Theory of the Modern World System

The basic thesis of the Modern World System (MWS) position is that the history and operation of the international political economy can only be understood in terms of the "Modern World System," defined by one proponent as "a unit with a single division of labor and multiple cultural systems" (Wallerstein, 1974b, p. 390).[4] Each of the terms embedded in the name of this theory expresses a crucial aspect of this

[4] Paul Baran (1967), Emmanual Wallerstein (1974a), and Andre Gunder Frank (1969) are three of the most prominent theorists of the Modern World System.

conception of international history. "Modern" economic and political relations are believed to be fundamentally different from premodern antecedents. The "world" is a structural whole (although the term obviously does not include the entire globe) and is the appropriate unit and level of analysis. And the modern world must be understood as a "system" in which all the various parts of the structure are functionally and necessarily related, a system that operates in accordance with a set of economic laws. Proponents of the Modern World System position assert that the primary task for political economists is the analysis of the origins, structure, and functioning of this system.[5]

Although the advocates of this position are not necessarily Marxists and indeed some adherents deviate from classical Marxism in a number of important respects, the MWS theory is grounded in the Marxist conception of social reality (Michalet, 1982). First, the theory accepts the primacy of the economic sphere and the class struggle over political and group conflict as a determinant of human behavior. However, traditional Marxism focuses on the domestic class structure and struggle, and the Modern World System theory speaks of an international hierarchy and struggle of states and economic classes. Second, the analysis centers on capitalism as a global phenomenon; however, whereas traditional Marxism regards the international economy as producing development, albeit unevenly, and evolving toward global unity, the MWS theory assumes an already unified world economic system composed of a hierarchy of class-dominated states held together by economic forces and producing underdevelopment throughout the dependent periphery. Finally, this modern world economy is believed to be characterized by inherent contradictions and functions according to deterministic laws that govern its historical development, inevitable crises, and eventual demise. Traditional Marxism asserts that capitalism has a historic mission to develop the world, but MWS theorists argue that the world capitalist system underdevelops the less developed countries.

The Modern World System position is based upon the classic Marxist thesis that both the nation-state of the nationalists and the market of the liberals are derivative from underlying and more fundamental social and economic forces. Rather than being independent actors or variables, they are the consequences of a peculiar juncture of ideas, institutions, and material capabilities (Cox, 1981). State and market are the products of a particular historical epoch and are firmly embedded in a larger social matrix. The task of understanding the international

[5] Brewer (1980) is an excellent critique of this thinking.

political economy, therefore, is one of comprehending the nature and dynamics of this more basic reality of the Modern World System.

Although proponents differ with one another and the theory itself is rife with inconsistencies, the central argument is that the world economy contains a dominant core and a dependent periphery that interact and function as an integrated whole. Whereas dualism considers the advanced core and the traditional periphery to be loosely joined, if at all, in a beneficial relationship, the Modern World System theory views them as an integrated whole so that the same mechanisms that produce capital accumulation and development in the core produce economic and political underdevelopment in the periphery.[6]

In contrast to the emphasis of dualism on the tendency toward separation of core and periphery and especially on the economic isolation of large parts of the periphery, MWS theorists see core and periphery as closely connected. Modern and traditional sectors are functionally related; the latter is held back by its connections to the former. The theory of dualism is thus considered to be a myth designed to hide from the Third World the real source of its backwardness. In the words of Andre Gunder Frank, the integrated commercial networks of advanced and backward sectors necessarily lead to the "development of underdevelopment." The periphery is the source of the wealth of the core; the latter exploits and siphons off the resources of the former. According to Frank, economic development and economic underdevelopment are merely the opposite sides of the same coin:

> Thus the metropolis expropriates economic surplus from its satellites and appropriates it for its own economic development. The satellites remain underdeveloped for lack of access to their own surplus and as a consequence of the same polarization and exploitative contradictions which the metropolis introduces and maintains in the satellite's domestic economic structure (Frank, 1969, p. 9).

According to this position, the international economy functions to distort the economies of the Third World. The international division of labor imposes class and state structures on the periphery and dependent economies that prevent their economic development. External relations of the society rather than internal factors are believed responsible for economic underdevelopment and the creation of weak states.

[6] The core/periphery formulation goes back at least to the early nineteenth century in the writings of Johann Heinrich von Thünen (Giersch, 1984, p. 107) and remains the central idea in regional economics. It is ironic that although in its original formulation the core develops the periphery, this idea has been corrupted by contemporary radical thinkers. According to most of these writings, the core underdevelops the periphery.

Contrary to the dual economy model, the more that the world economy progresses, the more difficult it is for the periphery to develop and the greater is the revolutionary effort required to escape global market forces.

Different adherents of the MWS theory emphasize different aspects, explanations, and organizing principles. Undoubtedly the most systematic and influential statement of the position is that of Immanuel Wallerstein (1974a). According to his formulation, the pluralistic balance-of-power system of western Europe was the necessary prerequisite for the emergence of the Modern World System. Until the advent of the nation-state political system in early modern Europe, the international system was characterized by successive "world empires." Capital accumulation and productive investments in these premodern imperial systems and command economies were thwarted by the absorption of the economic surplus by parasitic bureaucracies. As the market was never able to escape political control, commerce and capitalism could not reach their full potential for producing wealth and transforming society. The substitution of the nation-state system for these premodern imperial economic and political systems permitted market forces to escape from political control. The market was thus freed to develop and transform the world economy according to its own internal logic.

Although this theory of the Modern World System asserts that a pluralistic state system was the primary prerequisite for the creation of the world economy, it considers the interaction of international trade and investment to be the fundamental mechanism for the perpetuation of its structural features. This structure, according to Wallerstein, is defined by a single capitalist world division of labor. The efficient global organization of production is characterized by an expanding regional specialization based on different methods of labor control. The world economy is an international structure of unequal states that maintains the international division of labor and is responsible for the accumulation of capital in the advanced capitalist states and for the cycle of backwardness and underdevelopment in the rest.

The major components in this international division of labor are three hierarchically ordered tiers of states, differentiated by the position they have been able to wrest for themselves in the market pecking order: the core, the semiperiphery, and the periphery. The core states tend to specialize in manufacturing, the periphery is relegated to the production of raw materials, and the semiperiphery is somewhere in between. These structural features of modern capitalism, it is argued, have remained essentially unchanged over centuries. In stating his agreement with Paul Baran (1967), one of the first exponents of the po-

sition, Andre Gunder Frank sums up the essence of the position: "It is capitalism, both world and national, which produced underdevelopment in the past and which still generates underdevelopment in the present" (quoted in Brewer, 1980, p. 158).

The most important feature said to characterize this Modern World System is that, functioning as an integrated whole, it extracts economic surplus and transfers wealth from the dependent periphery to imperial centers. The components of the system, their relations to one another, and their internal social and other characteristics are determined by the overall system. There can be "no such thing as 'national development' " independent of the function of the world system (Wallerstein, 1974b, p. 390). As Theda Skocpol has observed, "the only definite dynamics of Wallerstein's world capitalist system are market processes: commercial growth, worldwide recessions, and the spread of trade in necessities to new regions of the globe" (Skocpol, 1977, p. 1078).

The following statement captures the wholistic and functional nature of the system:

> The capitalist world system is divided into three tiers of states, those of the *core*, the *semi-periphery* and the *periphery*. The essential difference between these is in the strength of the state machine in different areas, and this, in turn, leads to transfers of surplus from the periphery to the core, which further strengthen the core states. State power is the central mechanism since "actors in the market" attempt to "avoid the normal operation of the market whenever it does not maximize their profit" by turning to the nation state to alter the terms of trade (Brewer, 1980, p. 165).

The original placement of a state in this inexorable international division of labor determines whether a state is "hard" or "soft." Whereas the former is able to resist external market forces, channel them to its own advantage, and can effectively manage its own economy, the latter is pliable, at the mercy of external market forces, and cannot control its own economic affairs. Thus, "soft" states and dependent economies are caught in a web of market forces from which escape is very difficult.[7]

In summary, according to Wallerstein, the modern system put into place by Western capitalism in the sixteenth and seventeenth centuries has not been altered in its essentials over the centuries. It is a system that tends to reproduce itself as the rich get richer and the poor get

[7] The concept of "hard" and "soft" or "strong" and "weak" states is a highly ambiguous one and deserves more analysis than it has so far received. I believe that the distinction can be misleading. Krasner (1978, ch. 3), Zolberg (1981), and Ikenberry (1986b) provide contrasting treatments of the subject.

poorer. Over the long term, however, it cannot escape the inevitable laws of the demise of the capitalist mode of production set forth by Marxist theory (Skocpol, 1977, p. 1078). As will be shown, this conception of the world economy has profoundly influenced many less developed countries and their demands for a New International Economic Order.

The Theory of Hegemonic Stability

According to the theory of hegemonic stability as set forth initially by Charles Kindleberger (although he preferred the term "leadership" or "responsibility"), an open and liberal world economy requires the existence of a hegemonic or dominant power. In the words of Robert Keohane, the theory "holds that hegemonic structures of power, dominated by a single country, are most conducive to the development of strong international regimes whose rules are relatively precise and well obeyed. . . . the decline of hegemonic structures of power can be expected to presage a decline in the strength of corresponding international economic regimes" (Keohane, 1980, p. 132). The hegemonic power is both able and willing to establish and maintain the norms and rules of a liberal economic order, and with its decline the liberal economic order is greatly weakened.

The key word in the preceding paragraph is "liberal," that is, the theory relates to the existence of an international economy based on the precepts of the free market such as openness and nondiscrimination. The theory does not argue that an international economy would be unable to exist and function in the absence of hegemony. International economies obviously have always existed in one form or another. Rather, it argues that a particular type of international economic order, a liberal one, could not flourish and reach its full development other than in the presence of such a hegemonic power.

The mere existence of a hegemonic power, however, is not sufficient to ensure the development of a liberal international economy. In addition, the hegemon itself must be committed to the values of liberalism or, to use John Ruggie's language, its social purpose and domestic distribution of power must be favorably disposed toward a liberal international order (Ruggie, 1982, p. 382). The domestic economic structures of the hegemon and of other societies are obviously important determinants of the disposition of states toward a liberal international economy (Katzenstein, 1976). Hegemony without a liberal commitment to the market economy is more likely to lead to imperial systems and the imposition of political and economic restrictions on lesser powers, for example, the Soviet bloc today. And, finally, "a congruence of social purpose" in support of a liberal system must exist among the ma-

jor economic powers (Ruggie, 1982, p. 384). Other powerful states must also have an interest in the growth of market relations; the hegemon can encourage but cannot compel other powerful states to follow the rules of an open world economy. Thus, three prerequisites—hegemony, liberal ideology, and common interests—must exist for the emergence and expansion of the liberal market system. (These conditions are treated in greater detail in Gilpin, 1981, ch. 3.)

Hegemony or leadership is based on a general belief in its legitimacy at the same time that it is constrained by the need to maintain it; other states accept the rule of the hegemon because of its prestige and status in the international political system (Frohlich, Oppenheimer, and Young, 1971). A considerable degree of ideological consensus, or what Marxists following Antonio Gramsci would call "ideological hegemony," is required if the hegemon is to have the necessary support of other powerful states (Keohane, 1984a, pp. 44-45). If other states begin to regard the actions of the hegemon as self-serving and contrary to their own political and economic interests, the hegemonic system will be greatly weakened. It will also deteriorate if the citizenry of the hegemonic power believes that other states are cheating, or if the costs of leadership begin to exceed the perceived benefits. In such situations, powerful groups become less and less willing to subordinate their interests to the continuation of the systems.

Historically, the conjuncture of circumstances favorable to hegemonic leadership and the emergence of a liberal world economy has occurred only twice. The first was the era of the Pax Britannica that extended from the end of the Napoleonic Wars to the outbreak of the First World War. With the political triumph of the middle class, committed to the ideology of liberalism, Great Britain used its influence to usher in the age of free trade. The example of British economic success, the general acceptance of liberal ideals among the major economic powers, and the recognized benefits of trade encouraged states to negotiate tariff reductions and to open their borders to the world market (Kindleberger, 1978b, ch. 3). Similarly, the United States took the lead in promoting a liberal international economic order following the Second World War. The General Agreement on Tariffs and Trade (GATT) and the International Monetary Fund (IMF), embodying liberal principles, were established by the United States and its allies. American leadership was exercised subsequently in the reduction of trade barriers. During these eras of British and American preeminence the international market and global economic interdependence expanded.[8]

[8] A number of writers identify Holland in the seventeenth century as a hegemonic power, but the case is not a convincing one. Although Holland certainly was the leading

As formulated originally by Kindleberger and subsequently extended and modified by others, including this writer, the theory of hegemonic stability argues that an open market economy constitutes a collective or public good (Olson, 1965). Such a good "is one the consumption of which by an individual, household, or firm does not reduce the amount available for other potential consumers" (Kindleberger, 1981, p. 243). A road or a sidewalk is a prime example. However, because an individual can "consume" the good without paying for it, collective goods tend to be underprovided unless the interests of some actor cause it to assume a disportionate share of the costs or some agency (e.g., government) exists that can force consumers to pay for the good.

In the realm of international relations, a number of collective goods are said to exist. An open and liberal trading regime based on the Most-Favored Nation (MFN) principle of nondiscrimination and unconditional reciprocity—that is, a tariff concession made to one country must be extended to others—is an example of such a collective good.[9] Another frequently cited example is a stable international currency, because it facilitates commerce from which everyone can benefit. A third, and more debatable, collective good is the provision of international security (Jervis, 1982). Individual states, the argument runs, can enjoy these collective goods whether or not they contribute to the maintenance of the good.

According to the theory, the hegemon or leader has the responsibility to guarantee provision of the collective goods of an open trading system and stable currency. The theory assumes that a liberal economic system cannot be self-sustaining but must be maintained over the long term through the actions of the dominant economy. An open world economy is particularly threatened by the "free rider" problem, wherein cheaters benefit from the collective goods but refuse to pay their "fair" share toward providing it (Frey, 1984b, ch. 7). Also, particular states attempt to advance their interests at the expense of others, for example, by exploiting a monopolistic position. According to the theory of hegemonic stability, these temptations to cheat and exploit others too frequently overwhelm the liberal argument that a hegemon is unnecessary because trade is by definition of mutual benefit.

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economy, it did not exercise influence over the international system comparable to Great Britain in the nineteenth and the United States in the twentieth century. The seventeenth century, it should be recalled, was the height of the first mercantilist era.

[9] The term "unconditional reciprocity" means that concessions made to one member of the GATT are automatically available to all other members. Thus, it is very close to the Most-Favored Nation principle. "Conditional reciprocity," on the other hand, means that concessions are made only to those other parties who specifically reciprocate.

The hegemonic economy, according to the theory of hegemonic stability, performs several roles crucial to the operation of the world economy. It uses its influence to create international regimes defined simply as "principles, norms, rules, and decision-making procedures around which actor expectations converge in a given issue-area" (Krasner, 1982a, p. 185). The regime prescribes legitimate and proscribes illegitimate behavior in order to limit conflict, ensure equity, or facilitate agreement (Keohane, 1982a, p. 354). The hegemonic power must prevent cheating and free riding, enforce the rules of a liberal economy, and encourage others to share the costs of maintaining the system. The gold standard of the nineteenth century and the postwar Bretton Woods system are notable examples of an economic regime in which the hegemon establishes and enforces the rules of a liberal market regime and suppresses the ever-present tendencies toward economic nationalism.

As Kindleberger has argued, "for the world economy to be stable, it needs a stabilizer, some country that would undertake to provide a market for distress goods, a steady if not countercyclical flow of capital, and a rediscount mechanism for providing liquidity when the monetary system is frozen in panic" (Kindleberger, 1981, p. 247). The hegemon must also prevent states with monopoly power from exploiting others. It must also encourage states that at least initially would lose from free trade to remove their trade barriers (H. Johnson, 1976, pp. 17, 20).

Furthermore, in a world of flexible exchange rates and integrated capital markets, the hegemon "must also manage, in some degree, the structure of foreign-exchange rates and provide a degree of coordination of domestic monetary policies" (Kindleberger, 1981, p. 247). If there were no hegemonic power to create and manage international regimes, this theory suggests, the international economy would become unstable as liberalism and free trade gave way to the forces of economic nationalism.[10]

In addition, the growth and dynamism of the hegemonic power serve as an example of the benefits of the market system and perform as an engine of growth for the rest of the system; its imports stimulate the growth of other economies and its investments provide developing countries with the financing needed for growth. Through the process of technology transfer and knowledge diffusion, it also supplies developing economies with the technology and technical expertise required for

[10] Keohane (1984a) provides a critique of the reasoning that a hegemonic power is necessary for the creation and preservation of a liberal international economy.

their industrialization and economic development. This role of the hegemon in the global process of economic growth is a cement that helps hold the system together; when this growth declines, centrifugal forces increasingly manifest themselves.[11]

Although the two hegemons in the modern world have in turn been the dominant military state in the international system, they have radiated their influence largely through the exercise of economic power. The hegemon, in the words of Robert Keohane, "must have control over raw materials, control over sources of capital, control over markets, and competitive advantages in the production of highly valued goods" (Keohane, 1984a, p. 32). The hegemon is provided with the means of leadership over other economies through control of financial capital, particular technologies, and natural resources.

Thus, although hegemonic leadership benefits those economies able to take advantage of liberalized exchange, an interdependent world economy also creates external vulnerabilites and a nexus of power relations. As Hirschman (1945, p. 16) has written, the essence of economic power, or at least one form of it, is the capacity to interrupt commercial intercourse. The actual or threatened cutoff of trade, finance, or technology can be a potent means of leverage over other states. The ability of the hegemon to exercise its power through the mechanisms of economic interdependence contributes to its governance and management of the international market economy, but, as will be pointed out below, it also enables the hegemon to exploit its dominant position.[12]

The relatively large size of the hegemon's market is a source of considerable power and enables it to create an economic sphere of influence.[13] The hegemon can gain influence over other states by opening its market to "friendly" states or denying access to "unfriendly ones." Although the utility of economic sanctions tends to be greatly exaggerated, they are the foremost example of this power.[14] As will be discussed later, the United States has also extended its hegemonic power

[11] I am indebted to Robert Walker for this observation.

[12] The relationship of interdependence and power is a complex one. In part this is the case because "interdependence" has so many meanings. Cooper (1985, pp. 1196-1200) explores numerous aspects of this subject.

[13] The concept of an economic sphere of influence is an interesting but undeveloped one. It is found, for example, in the writings of Alfred Marshall. See Choucri (1980, p. 110) for a brief discussion of the subject.

[14] In recent years much has been written on economic sanctions and related topics. My own view that economic sanctions are of little utility is discussed in Gilpin (1984). David Baldwin (1985) and Hufbauer and Schott (1985) are the best and most extensive recent examinations of the subject.

considerably through the overseas expansion of its powerful multinational corporations.

The central role of the hegemon's currency in the international monetary system provides it with financial and monetary power. Both Great Britain in the nineteenth century and, to a much greater extent, the United States in the twentieth have used to their own advantage the right of seigniorage "which is the profit that comes to the seigneur, or sovereign power, from the issuance of money" (Kindleberger, 1981, p. 248). The United States has also employed its financial power to reward friends with access to capital markets and to punish enemies through the denial of access. Also, in the case of the United States, the financial perquisites of the hegemon have been crucial to its ability to maintain its dominant position and domestic prosperity into the 1980s.

The ultimate basis of the economic strength of the hegemon is the flexibility and mobility of its economy (Hawtrey, 1952). In the long term, economic power is neither the possession of particular monopolies and/or technologies nor economic self-sufficiency, but rather the capacity of the economy to transform itself and to respond to changes in the global economic environment, such as shifts in comparative advantage or price changes. The inflexibility of the British economy in the late nineteenth century in response to the rise of new industrial powers was an important cause of its decline (Lewis, 1978b, p. 133). Similarly, the difficulties experienced by the United States during the closing decades of the twentieth century in adjusting to profound shifts in the global location of industry and the revolution in the price of energy have undermined its power and international position.[15]

Although a favorable political environment is required for the release and development of market forces, the international market tends to operate according to a logic of its own. As noted above, economic competition and the price mechanism drive the market economy toward ever higher levels of productive efficiency, economic growth, and the integration of national markets. In time, the market produces profound shifts in the location of economic activities and affects the international redistribution of economic and industrial power. The unleashing of market forces transforms the political framework itself, undermines the hegemonic power, and creates a new political environment to which the world must eventually adjust. With the inevitable shift in the international distribution of economic and military power from the core to rising nations in the periphery and elsewhere, the capacity of the

[15] Kindleberger (1962, ch. 7) analyzes the problem of economic transformation and its importance for adjustment to economic change.

hegemon to maintain the system decreases. Capitalism and the market system thus tend to destroy the political foundations on which they must ultimately depend.

Although both Great Britain and the United States accelerated their relative decline through their own actions, the hegemonic system is ultimately unstable (Kindleberger, 1981, p. 251). For internal and external reasons, the hegemonic power loses its will and its ability to manage the system. Domestic consumption (both public and private) and the costs of defending the system militarily rise relative to national savings and productive investment, as seen in the case of the United States (Oye et al., 1983, ch. 1). The hegemon grows weary and frustrated with the free riders and the fact that its economic partners are gaining more from liberalized trade than it is. More efficient, dynamic, and competitive economies rise that undercut the hegemon's international position and the economic surplus that had financed the costs of global hegemony (Gilpin, 1981). In time, the hegemon becomes less able and willing to manage and stabilize the economic system. Thus, an inherent contradiction exists in a liberal world economy: the operation of the market system transforms the economic structure and diffuses power, thereby undermining the political foundations of that structure.

The important and interesting question of how hegemonic decline can be inevitable, given the alleged overwhelming power of the hegemon, lies beyond the scope of this book. Suffice it to say that although all dominant powers must one day decline, they display great differences in their longevity. Venice may be said to have been the hegemonic economic power of the western Mediterranean for a millennium; British hegemony lasted over a century; and American hegemony was in decline after a brief three decades. (Some speculations on these matters are presented in Gilpin, 1981, ch. 4.)

As Kindleberger suggests (in part echoing Cooper's views discussed earlier), renewed economic stability requires either a new hegemon, an agreed-upon set of rules binding all (including the weakened hegemon), or continuous policy coordination among the reigning economic powers (Kindleberger, 1981, pp. 251-52). The declining hegemon may also seek, as did the Reagan Administration, to reassert its dominant economic and political position. If none of these options materializes, the liberal system begins to break down. Although no particular outcome is inevitable, the theory suggests that the world economy will be increasingly characterized by economic conflicts.

The extent of these conflicts depends upon the capacity of the hegemon to adjust to its decline. As the locus of economic growth and the leading sectors shift in new directions, can the hegemon develop new

competitive industries? Is it able to bring its political commitments and economic power back into balance? Can the hegemon and the rising economic powers cooperate to solve the problems that inevitably attend major economic transformations? The answers to these and other questions determine whether a liberal economic order can survive hegemonic decline.

Although the liberal international regimes associated with the declining hegemon may erode, other factors such as the force of inertia, the absence of an alternative, and the residue of common interests or social purposes among the dominant powers operate to maintain the system (Krasner, 1976, pp. 342-43). As Keohane (1984a) cogently argues, the norms of the regimes themselves inhibit proscribed behavior. Regimes are more easily maintained than created, as states learn their benefits (Haas, 1980). In Kindleberger's words, "regimes are more readily maintained than established since marginal costs are below average costs; as hegemonic periods come to an end with the waning of the leading country's economic vitality, new regimes needed to meet new problems are difficult to create. . . . it took [eighty years] to create and get functioning the World Health Organization despite the clear benefits to all countries from controlling the spread of disease. And it takes work to maintain regimes; in the absence of infusions of attention and money, they tend in the long run to decay" (Kindleberger, 1986, p. 8). And just as it is more costly to create than to maintain a regime, considerable costs must be incurred to bring down a regime. Thus, as has been pointed out, the nineteenth century trading and monetary regimes continued to survive long after British hegemony began its decline with the emergence of rival powers.

With the relative decline of the hegemon in international competitiveness and other measures of economic capabilities, however, the possibility increases that a financial crisis or some other calamity will occur that will cause a dramatic collapse of the system, particularly if a divergence of interests among the major powers takes place. For example, the financial panic of 1929 and the subsequent conflictual policies of the Great Powers utterly destroyed the economic regimes that had been revived after the First World War. Although a similar eventuality is highly unlikely in the contemporary world, one should not assume that the regimes created by American hegemonic leadership are somehow invulnerable.

The crucial role of the hegemon, Kindleberger points out, is that of crisis management and not simply the routine one of regime maintenance. If a liberal world economy is to survive, the hegemon must be able and willing to respond quickly to threats to the system. For ex-

ample, as Kindleberger has argued, the ability of Great Britain to be the "lender of last resort" substantially moderated the financial crises of 1825, 1836, 1847, 1866, and 1907; in contrast, its inability to play this crisis management role in 1929 and the unwillingness of the United States to take over this task of "lender of last resort" in the face of pyramiding bank failures was a major cause of the collapse of the international financial system and of the Great Depression (Kindleberger, 1986, pp. 8-9). In the final decades of the twentieth century the international economy confronts the dangers accompanying the relative decline of American hegemony. The international debt problem, the increase in trade protectionism, and other issues could trigger a crisis over which the United States and its economic partners could easily lose control. Such a failure of crisis management could once again bring down the liberal international economic order.

The Political Economy of Structural Change

Each of these three theories provides important insights into the dynamics of the international political economy. First, it is obvious that the historical context emphasized by the MWS position is crucial in the determination of economic and political change. As already noted, the market system and the nation-state are both products of modern society and of profound changes in human consciousness, productive technology, and social forces. It is equally obvious, however, that human beings have always organized themselves into what Ralf Dahrendorf (1959) has called "conflict groups," such as tribes, empires, and city-states. In the modern epoch, as the theory of hegemonic stability stresses, nation-states and the conflicts among them are the foremost manifestation of man's nature as a "political animal." Far from being mere creatures of economic and historical forces, states are independent actors in economic and political affairs.

It should also be equally obvious that the market and "economic man" have achieved an independent reality. Once having come into existence the modern market cannot be reduced to sociological forces. Although it is correct, as Karl Polanyi has written, that the important role of the market and economic laws in the modern world is the outcome of a peculiar set of historic circumstances, the market, like the modern state, has come to exercise a powerful influence over historical developments (Polanyi, 1957). The dynamics of the international political economy must be understood in terms of the interaction of state and market within their larger historical setting.

At some future date modern social science may unlock the secrets of

history and explain scientifically the interactions among social forces, political actors, and economic activities. Perhaps, as Marxists and proponents of the Modern World System theory both argue, state and market as well as other aspects of social life can be explained through the workings of historical laws. But our understanding of our own behavior is primitive indeed; rather than validated laws and theories we have conflicting perspectives and partial insights into these matters. With only a single historical example of a world dual economy or Modern World System, depending upon one's point of view, and two hegemonic systems, it is obviously impossible to prove or disprove any of these theories.

With this caveat in mind, the strengths and weaknesses of these three "theories" as means to explain and understand structural change will be discussed. My understanding of structural change and of the dynamics of the international political economy is derived from my evaluation of these theories.

By "structure," I mean simply "the parts of an economic whole which, over a period of time, appear relatively stable alongside the others" (Marchal, quoted in Hartwell, 1982, p. 102). These structures provide constraints and opportunities within which actors attempt to achieve their objectives. A major goal of states and powerful organizations is to change the structures themselves. These structures include social institutions, the distribution of property rights, the division of labor and location of economic activities, the organization of particular markets, and the norms or regimes governing economic affairs. The term "structural change" is defined as the alteration of these institutions and fundamental relationships. What, then, are the contributions of the three theories of the international political economy to our understanding of the nature of structures and structural change?

The liberal theory of the dual economy correctly stresses the important role of self-interest and the seemingly universal desire to maximize gains as driving forces in the evolution of the world economy. Whatever the underlying motive, be it greed or, as Adam Smith speculated, emulation, when constraints are removed and opportunities present themselves, human beings seek to engage in economic intercourse. The consequence of this drive to "truck and barter" is the steady erosion of traditional ways and the eventual creation of modernized economies.

In addition, relative prices and price changes play a powerful role in the dynamics of the international political economy. In the economist's universe of prices and quantities, any changes on the supply or the demand side of the economy or the innovation of new products and productive processes will cause responses throughout the system (Nelson

and Winter, 1982). For example, the profound impact of the increased cost of world energy on international economic and political affairs in the 1970s was an excellent example of the potency of a price change. The market does matter in determining the structure and dynamics of the international political economy.

Another strength of this theory is the central role that it gives to technological advances in the evolution of the international political economy. Improvements in communications and transportation that reduce the costs of conducting business have encouraged the integration of once isolated markets into an expanding global interdependence. From the innovation of oceangoing sailing ships to contemporary information-processing systems, technological advances have been an almost inexorable force for uniting the world economy.

The economist's method of comparative statics, however, is very limited as a tool for understanding structural change. It lacks any means of predicting and explaining the shifts in supply or demand that cause changes in relative prices. Economists also lack an explanation of technological change. Nor can they analyze in a systematic fashion the longer-term effects of such changes and innovations on economic, political, and social affairs. Economic theory treats as exogenous and tends to ignore the institutional, political, and historical framework (e.g., the distribution of power and property rights, reigning ideologies, and technological factors) within which the price mechanism works its effects. Thus, the dual economy theory tends to neglect the political and social environment that influences and channels the evolution of the market.

The basic problem is that economists lack a theory of economic change. In the words of Walter Rostow, "the most vital and fully articulated bodies of modern economic thought have been developed within Marshallian short-period assumptions; that is, the social and political framework for the economy, the state of the arts, and the levels of fixed capacity are assumed to given and, usually, fixed" (quoted in R. Cameron, 1982, p. 29). The basic assumption of their studies is the existence of equilibrium and, as one writer has put it, history is never about "equilibrium" (Hartwell, 1982, p. 92). Economists are not generally interested in structural change nor do they have the analytical apparatus to explore it in any depth.[16]

The emphasis of the theory of the Modern World System on "the historical structure of the world political economy" also makes a valuable

[16] North (1981) and Northrop (1947) provide contrasting evaluations of the possibility of developing an economic theory of structural change.

contribution to our understanding of the dynamics of the international political economy (Tooze, 1984, p. 13). The setting of ideas, technology, and social forces within which state and market operate creates opportunities and constraints on political and economic behavior. The state could not exist, in fact, without the supporting ideology of nationalism; nor could the market survive without liberalism. This theory, however, is flawed by its economic determinism and its static conception of the international political economy.

According to this theory, the international political economy must be viewed as an integrated structure of core and periphery. The primary nexus of this system is the hierarchical international division of labor, which determines the place of a society in the system. The structure of the world economy is responsible both for the external relations and the internal characteristics of individual societies. The essential structure of the Modern World System, this theory argues, was put into place in the sixteenth century and has not been substantially altered over the succeeding three centuries.

The argument that the pluralist European state system was a necessary condition for the rise of a market economy is an important insight.[17] Every state has a powerful disposition to attempt to gain control over economic activities and to make them serve its ends. The sufficient conditions for the rise of a world market economy, however, were the economic, institutional, and technological developments stressed by the dual economy theorists. One cannot, for example, reduce the development and subsequent evolution of science, which has so profoundly transformed the modern world, to the propositions advanced by supporters of the MWS theory. Nor can one account for the dynamics of the international system, as this position tends to do, solely in terms of the evolution of market forces.

Although the argument of the MWS theory that the world economy should be understood in hierarchical and structural terms is a necessary corrective to the emphasis of the dual economy theorists on an egalitarian and disaggregated market, it errs in several important particulars. First, although the economic structure does significantly influence the policies of powerful states, it is equally influenced by them. Second, the nexus among states is primarily political and strategic rather than

[17] The first writer to argue that a pluralistic state system was necessary for the rise of a global market economy appears to have been Jean Baechler (1971) and not Wallerstein (1974a). Whereas the latter employed this idea in a radical critique of capitalism, the approach of the former is a strong defense of capitalism. As noted elsewhere in this book, writers in political economy frequently employ the same basic ideas to justify very different intellectual and political positions.

economic, and political relations provide the framework for economic activities. Third, whether a state is "soft" or "hard" (for example, Argentina and Japan, respectively) is basically a function of internal social and political factors. Fourth, as the Japanese today and the Germans before them have proven, more than anything else it is the nature of the society and its policies that determine its position in the international division of labor. Fifth, the structure of the international market has changed dramatically over the past several centuries due to the evolution of the international division of labor and the changing position of economies in the system.

The argument that the structure of the world economy has been static is patently wrong. The market economy, as Marx pointed out, develops the world. It is an evolutionary system that over time has incorporated more and more of the world. The colonial empires of the early modern period integrated a very small fraction of Asia, Africa, and the New World into the so-called Modern World System; the largest segment of the world's periphery of traditional economies, as proponents of the dual economy thesis rightly point out, lay outside the system. Until the end of the nineteenth century, in fact, Europe remained relatively self-sufficient in food and raw materials. It could feed itself and possessed most of its required industrial raw materials, especially coal and iron (Dillard, 1967). Only with the second phase of the Industrial Revolution and the huge growth of population late in the century did the European core require commodity imports; these came, however, mainly from the "lands of recent settlement" in the temperate zones and a few tropical entrants into the system (Lewis, 1978a). What the MWS theorists call the periphery remained marginal until quite recently.

In truth, the modern world system in its present form did not really come into existence until the decades immediately preceding the First World War, when the dominant industrial economies emerged. The same countries that were important prior to the First World War were still the core economies in the post-1945 period. Most of the lands that Wallerstein and others would later assign to the periphery have been largely ignored by traders and investors until relatively recently (except for slaves and precious metals). The contemporary international division of labor between the industrialized Northern core and the nonindustrialized Southern periphery actually took shape in the closing decades of the last century. As Arthur Lewis (1978a) has shown, the modern world system is less than a hundred years old.

Contrary to the views of the MWS theorists, the modern world system was a consequence of the development of the North rather than the

cause of its development. It has been the rapid development of the core and its need for food and raw materials that has led to the integration of the periphery into the system and the subsequent growth of those peripheral economies that could take advantage of this fact. As one Marxist economist has argued, modern capitalist economies have not been dependent upon exploitation of the periphery for their development, and the growth of the capitalist economies was due to the achievement of internal efficiency (Brewer, 1980, pp. 170-71). The Northern core has served as an engine of growth for the South throughout this history. The world economy diffuses rather than concentrates wealth.

Although it is appropriate to view the worldeconomy as a hierarchical structure or system composed of core and periphery, it should be noted that the geographic locus of the core and the global distribution of economic activities have shifted continuously over the past three centuries, from the Mediterranean to the North Atlantic and, in our own age, toward the Pacific. The emergence of new industrial powers in Asia and Latin America is transforming the international division of labor and has resulted in profound changes in the leadership and nature of the international political economy.[18] Providing a better understanding of the causes and consequences of this dynamic process is a major challenge.

One strength of the theory of hegemonic stability is its focus on the role of the nation-state system and that of international political relations in the organization and management of the world economy. Although the MWS theory is obviously correct that the modern nation-state is ultimately the product of historical forces, the nation-state and its actions cannot simply be reduced to economic forces. Once the nation-state exists, it behaves in accordance with the logic of the competitive state system.

The theory of hegemonic stability begins with recognition of the intensely competitive nature of international relations. The modern nation-state is first and foremost a war-making machine that is the product of the exigencies of group survival in the condition of international anarchy. The security and political interests of states are primary and determine the international context within which economic forces must operate. The expansion and success of the market in integrating modern economic life could not have occurred without the favorable political environment provided by the liberal hegemonic power.

[18] Braudel (1979) develops this important theme of the shifting locus of the core of the international political economy.

Since its original formulation by Kindleberger, the theory of hegemonic stability has been subjected to intense criticism, some of which has been warranted, revealing its limitations. Others, however, have grossly misinterpreted the theory. There is confusion about its nature, about its actual content, and especially about the significance of hegemonic decline for the continuation of a liberal international regime. My position follows.

The phrase, "the theory of hegemonic stability," was formulated originally by Robert Keohane to refer to the ideas of a rather diverse group of scholars regarding the relationship of a dominant economy and a liberal international system (Keohane, 1980). Unfortunately, this expression implied a much more unified, systematic, and deterministic "theory" than was intended by its proponents; thereby, many of its subsequent opponents were easily misled. (It is noteworthy that Keohane himself, a critic of the theory, is frequently identified as one of its major proponents.)

The theory of hegemonic stability in its simplest form argues that the existence of a hegemonic or dominant liberal power is a necessary (albeit not a sufficient) condition for the full development of a world market economy. Contrary to the overly simplistic characterization of the theory by some critics as deterministic, the theory holds that the hegemonic political structure is permissive, but does not determine either the nature of commercial policy or the content of economic transactions (Gilpin, 1981, pp. 129-30). Commercial policy is determined primarily by domestic coalitions and interests, or what Ruggie has called "social purpose" (1982, pp. 382, 404), and economic transactions mainly by economic variables. Thus, although a pluralist and nonhegemonic system like that of the seventeenth and eighteenth centuries obviously does facilitate the growth of the world market, in the absence of a hegemon, mercantilistic competition and nationalistic policies tended to predominate. It was only after the Napoleonic Wars and the emergence of Great Britain as a liberal hegemonic power that the world entered the liberal era of free trade.

There are several versions of the theory of hegemonic stability that differ importantly from one another. My own views have changed in response to criticism by other scholars and my own reflections on the subject. Although it is not possible to examine all the issues raised by the theory itself and by its critics here, several points important to the argument of this book need to be examined.

One issue is whether it is possible to refer to "international collective goods," or whether they are merely private goods masked as public ones. Some argue that the trade and monetary regimes are not true col-

lective goods because the number of beneficiaries is so small. The definition of a "public good" requires "indivisibility" and "nonappropriability." Some critics assert that international collective goods cannot meet these two requirements (i.e., "indivisibility"—in which the consumption of the good by one does not preclude consumption by another, or "nonappropriability"—in which no one can be denied access to the good). These same critics note that the requirements could be easily violated if, for example, the consumption of the good by one actor precludes its consumption by another, and if particular actors can be denied access to the good. Further, some point out that international actors can and do provide the goods for themselves through bargaining, mutual cooperation, and the punishment of cheaters. Therefore, some writers assert that the appropriate model for the international economy is that of a Prisoner's Dilemma or collective action problem in which individual nations cooperate and bargain to achieve their economic objectives (Conybeare, 1985).

These criticisms have merit and do weaken the collective goods argument supporting the need for a hegemon. The number of beneficiaries is sufficiently small (at least among the major economies) to facilitate cooperation and enable them to provide for themselves; it should be noted, however, that as the number of states has expanded and power has shifted toward Japan and the less developed countries in recent decades, trade and monetary cooperation have become more difficult to maintain and the free-rider problem has worsened. Also, it is true that very few *pure* collective goods actually exist in the international realm. Almost every so-called international collective good exists only with respect to a particular constituency. But this criticism can be applied to virtually every collective good. An individual may consider almost any good to be a private good; a sidewalk, which is the classic example of a collective good, is after all accessible only to those individuals actually admitted to the country. The rich may benefit the most from the police, but the poor can benefit as well. Similarly, the General Agreement on Tariffs and Trade (GATT) and the International Monetary Fund (IMF) are public goods only for their members, but a trade war or unstable monetary system would harm everyone. Even the Soviet Union can and does take advantage of a stable international monetary system.

Other critics maintain that the hegemon can exploit its position, and the theory of hegemonic stability itself is said to have a normative content. It can be used to defend the role of the hegemon as not only necessary but also beneficial (Snidal, 1985, p. 582). That is, these critics assert that the theory can be used and in fact is used to support and ra-

tionalize American imperialism and domination of other countries. Proponents of the theory of hegemonic stability, however, are fully aware that the hegemon can exploit its position for its own nationalistic ends. Kindleberger himself has been one of the most severe critics of American economic behavior in recent years, and I second these criticisms.[19]

My position is that a hegemon is necessary to the existence of a liberal international economy. Whether such an economy is conceived as a collective good or a private good shared by a particular group of states, historical experience suggests that, in the absence of a dominant liberal power, international economic cooperation has been extremely difficult to attain or sustain and conflict has been the norm. As John Condliffe (1950, p. 219) has written, referring to the liberal system of the nineteenth century, "leadership in establishing the rule of law lay . . . as it always lies, in the hands of the great trading nations." British power and interest tried to maintain an open and integrated world economy throughout much of the century, but as British power waned, so did the fortunes of the liberal world economy. With the outbreak of the First World War, the liberal world economy collapsed. Following the war, efforts to revive the liberal system broke down as economic nationalism, "beggar-my-neighbor" policies, and imperialistic rivalries spread. Protectionism and economic nationalism are once again threatening the liberal international economic order with the relative decline of American power.

It is valid to probe the motivations that the hegemon may have to create and sustain a liberal international economy. Proponents of the theory posit motives ranging from cosmopolitan to enlightened self-interest (Krasner, 1982a, pp. 198-99). For example, whereas Kindleberger tends to view the hegemon as motivated by cosmopolitan economic goals, I believe that the United States has been motivated more by enlightened self-interest and security objectives. The United States has assumed leadership responsibilities because it has been in its economic, political, and even ideological interest to do so, or at least it has believed this to be the case. To secure these long-term interests the United States has been willing to pay the short-term and additional costs of supporting the international economic and political system.

[19] Americans tend to argue that the United States made economic concessions to achieve political goals; West Europeans more frequently take the opposite view. Many believe, for example, that the United States exploited its postwar technological monopolies. Although there is some basis for the European position, the United States certainly has been constrained by its allies from taking even greater advantage than it has of its dominant economic position.

However, because of the free-rider problem, the hegemon does tend to pay far more than its share of the costs of maintaining the public good over the long run (Olson and Zeckhauser, 1966). In addition, economic benefits to other states may be disproportionately favorable because of the larger size of the hegemon's market. The hegemonic country as a whole (in contrast to particularistic interests) can lose economically through the opening of its market (Conybeare, 1985, p. 74). Indeed, during much of the postwar era the United States has created and maintained an international economy advantageous, perhaps disproportionately so, to other countries.

The hegemon, however, can and may exploit its position so that it "exerts power to produce a result more favorable to it than if that power had not been exerted" (Kindleberger, 1981, p. 245). It can become coercive and attempt to improve its own position through the use of optimum tariffs, currency manipulation, or other interferences in economic relations (Young, 1982). As John Conybeare has argued, "the first best policy for the hegemon is to apply optimal trade restrictions" and thereby improve its terms of trade (Conybeare, 1985, p. 74). This argument assumes that the maximization of economic gain is the highest priority of the hegemon. The possibilities of retaliation and of negative effects on relations with friendly states and political allies and the ideological commitment to liberalism inhibit the hegemon's use of this strategy. Yet the hegemon is increasingly tempted to take advantage of its position as its power declines, as has occurred with the United States in the 1980s.

Throughout most of the nineteenth century, the British followed the path of self-restraint and frequently even took actions contrary to their own economic interests. Indeed, one might even argue that the British were excessively bound by their liberal ideology and consequently suffered economically. They could have taken a number of interventionist measures to arrest or at least slow their economic decline (Stein, 1984). It was only in the 1930s and in response to the Great Depression that they began to subordinate their liberal internationalism to more narrowly nationalistic goals.

When the United States launched the Bretton Woods system of fixed exchange rates, implemented the Marshall Plan, and took the lead in the GATT negotiations on trade liberalization, it acted in enlightened self-interest. The United States as well as other countries gained through the lowering of trade and other economic barriers. At least into the mid-1960s and following the implementation of the Kennedy Round of tariff reductions, the United States undoubtedly gained substantially from liberalization because of its technological mo-

nopolies and strong competitive position in world markets. At the same time, it should be recalled, in the interest of alliance solidarity, the United States for most of tbe postwar period tolerated European and Japanese discrimination against its exports.

The United States had ideological, political, and strategic motives to seek a liberal world economy; it desired to promote its values abroad, to create a secure international order, and to strengthen political ties with its allies. For two decades following the Second World War, the United States, largely for political and security reasons, subordinated many of its parochial economic interests to the economic well-being of its alliance partners. With certain notable exceptions, such as the economic containment of the Soviet bloc or demanding national treatment for American multinational corporations, in the early postwar years the United States eschewed the temptation to exercise its political and economic power for nationalistic ends. Indeed, the United States created an international economy of which others could take full advantage.

In the late 1960s, however, the United States began to pursue economic policies that were more self-centered and were increasingly denounced by foreign critics (Strange, 1985c, p. 256). Beginning with the escalation of the war in Vietnam and continuing in the Reagan Administration, with its massive budget deficit, the United States exploited its hegemonic position in ways that released inflationary forces and contributed to global economic instability. Although other countries can certainly be faulted for equally self-serving behavior, the American hegemon undermined its own legitimacy and the acceptance of its rule when it failed to fulfill what others considered to be its leadership responsibilities. By the 1980s, the United States was pursuing protectionist, macroeconomic, and other policies that could be identified as appropriate to what Conybeare has called "a predatory hegemon" (Conybeare, 1985, p. 406). With its relative decline, the United States began to shift from a benevolent to a predatory hegemon, a change that will be discussed in Chapter Ten.

Although the hegemonic system does provide some collective goods for some states, it also contains characteristics of the classic Prisoner's Dilemma, that is, states may have an incentive to cooperate, but they also have an incentive to cheat and thereby increase their relative gain (Conybeare, 1984). As the hegemon declines, these latent conflictual elements come increasingly to the fore; as they do, the Prisoner's Dilemma model, rather than the collective goods model, becomes an applicable description of the system. Controversies arise over the fact that a nation may have access to foreign markets without reciprocation or

that it may pursue macroeconomic policies that put other countries at a disadvantage. Bilateralism, discriminatory policies, and economic nationalism begin to supplant liberalism.

Perhaps the most misunderstood and controversial aspect of the theory of hegemonic stability is the significance of the decline of the hegemon for the continued openness of the international economy. The theory is not, as critics charge, deterministic. What it says about openness and closure is that "a hegemonic distribution of potential economic power is likely to result in an open trading structure" (Krasner, 1976, p. 318), and "the tendency toward breakdown or fragmentation of the system greatly increases with the relative decline of the [hegemon]" (Gilpin, 1975, p. 73). This obviously does not preclude continued international cooperation in a period "after hegemony" (to use Keohane's phrase [1984a]), *provided* that the interests and social purposes of the major economic powers are congruent (Ruggie, 1982, p. 384). The theory does not say that international cooperation is impossible in the absence of hegemony. To quote Kindleberger, the author of the theory, some countries might "take on the task of providing leadership together, thus adding to legitimacy, sharing the burdens, and reducing the danger that leadership is regarded cynically as a cloak for domination and exploitation" (1981, p. 252). What the theory does say is that this scenario is unlikely and that, with the decline of the hegemon, the preservation of a liberal international regime (with emphasis on the term *liberal*) will be much more difficult.

The theory of hegemonic stability (at least in its more crude forms) has tended to overemphasize the role of the state and of political factors in the existence and operation of the international market economy. It has underemphasized the importance of motivating ideologies and domestic factors, of social forces and technological developments, and of the market itself in determining outcomes.[20] Whether its proponents ever intended it to be or not, critics have assessed and criticized it as a general theory of international political economy (Lake, 1984). They have correctly noted its limited scope, its inability to demonstrate a close asssociation between power and outcome, and its failure to predict when and how the hegemon will act in particular instances (Keohane, 1984a, ch. 3).

I consider the theory to be a necessary corrective to the complete focus on economic factors of the dual economy and Modern World System theories. The hegemonic stability theory sets forth the political

[20] I am endebted to Joanne Gowa for first making me aware of this significant limitation of the theory of hegemonic stability.

conditions for the existence of a liberal international economic order and the idea that the rise and decline of the hegemon is an important determinant of structural change. It thus contributes one element to an understanding of the dynamics of the international political economy.

The Mechanisms of Structural Change

Religious passions, social institutions, and material conditions (resources and technology) motivate people and create the constraints and opportunities for human action, as Max Weber, Karl Polanyi, and others have taught us. In the modern West, the ideologies of secularism, liberalism, and nationalism, the spread of democratic societies, and the continuing industrial revolution have led to the emergence of the market and the nation-state as the primary means of organizing economic and political life. Yet, as Marxists and other critics of capitalism properly remind us, these social forms are the product of particular historical forces that may one day pass from the scene. The spread of socialist ideas, the growing importance of non-Western and nonliberal societies, and technological developments could undermine either or both of these institutions. Nevertheless, market and state are well entrenched in the present period and will continue to be the most dynamic factors in contemporary society into the foreseeable future.

Within the historical setting of constraints and opportunities, state and market interact to create the structure of the international political economy, that is, those relatively enduring aspects of the world economy that include the international division of labor, the network of trade, and the international monetary and financial system as well as rules or regimes governing these economic activities. These structures tend to reflect both the power of actors and the operation of market forces.

Throughout history these structures have been created following the great or hegemonic wars, which have determined the international hierarchy. As Wallerstein, Braudel, and others have noted, prior to the era of the nation-state, imperial structures or "world empires" tended to characterize international economic and political relations. In the modern world, the structures of the international political economy have been the consequence primarily of the actions of successive hegemonic nation-states. These core economies—Great Britain in the nineteenth century and the United States in the twentieth—have used their military and economic power to establish liberal international market economies (Gilpin, 1981).

Although reflecting the interests of dominant economies, these suc-

cessive economic and political structures have also provided opportunities for the growth and expansion of other economies. As time passes, changes in the social environment, in the distribution of economic and military power, and in the interests of economic actors undermine the foundations of the structure; actors who would benefit from changes attempt to reform the old structure or create a new one by altering the trading, monetary, and other aspects of the international economy and of its governing rules. The economic actors who would lose from changes, including the declining hegemon, resist such demands or attempt to alter the structure to benefit themselves. This inevitable conflict between rising and declining powers is eventually resolved either through a resort to force or through peaceful adjustments that result in a new or reformed structure that reflects the changed array of national interests and the distribution of military and economic power.

Underlying the mechanism of structural change is the fact that although the market system does promote the economic and political development of the world, it does not do so evenly. Indeed, the process of economic growth is uneven in several respects. The growth rate varies considerably from one region of the globe to another, and the primary locus of growth shifts from one country and region to another. Various sectors of an economy also grow at different rates, and the high-growth sector shifts, in time, from less to more technically advanced industries; leading, trailing, and declining economic sectors exist in every economy. Furthermore, the rate of economic growth is uneven over time; it fluctuates from periods of slow to rapid growth. These three fundamental tendencies in any growing economy undermine the existing structure of the international political economy and create challenges that must be met if the economy is to remain stable.

Uneven Growth among National Economies

Every economy is a hierarchical structure composed of a dominant core (or cores) and a dependent periphery.[21] Whether it is a city, region, or country, the core is the growth pole of the economy, drawing resources (food, raw materials, and labor) from the periphery and supplying goods, services, and markets to the periphery. The core expands and incorporates an ever-greater periphery into the economic system as industry and other economic activities grow. Although there are wide-ranging variations of this expanding interdependent relationship, the division of labor between dynamic core and dependent periphery is a universal characteristic of every economy (Friedmann, 1972).

[21] The following paragraphs have been adapted from Gilpin (1975).

This process of growth has two opposed consequences for the distribution of wealth, power, and economic activities within the economy. On the one hand, what Gunnar Myrdal has called the "backwash" and Albert Hirschman the "polarization" effect takes place: capital, industry, and economic activity tend to concentrate in the core. On the other hand, in opposition to this agglomeration effect, there is a tendency for a "spread" (Myrdal) or "trickling-down" (Hirschman) effect to take place; that is, wealth and economic activities diffuse from the center or growth pole to the periphery and distribute themselves at new nodal points in the system.[22] As David Hume was undoubtedly the first to note and as later economists have stressed, a powerful tendency exists for industry to migrate toward cheaper pools of labor and natural resources.[23]

The opposing tendencies of concentration and spread are of little consequence in the liberal model of political economy. Furthermore, due to the absence of political or other boundaries within domestic societies, these opposed tendencies are not of crucial significance within domestic societies. Despite the possibility of temporary dislocations, the movement of labor and capital between core and periphery within a domestic society tends to produce an economic and political equilibrium as labor moves freely from the periphery to the core and capital from the core to the periphery, thereby equalizing wages and rates of return. In the international realm, however, where political boundaries divide core and periphery and restrict the free movement of labor and capital, the process of concentration and spread has profound political implications. It releases powerful forces of economic nationalism, first in the periphery and perhaps subsequently in the core.

The initial advantage of the core over the periphery is its technical and organizational superiority, and this advantage underlies the division of labor between the advanced industries of the core and the low-technology and raw material producers of the periphery. Because of its lead in innovation and its industrial superiority, the center tends to enjoy favorable terms of trade with its economic partners. The greater efficiency and consequently higher rates of profit and capital accumulation are the most important reasons for the rapid economic growth and the concentration of wealth and power in the core. In the short term, therefore, and in the absence of political resistance by peripheral states,

[22] This discussion is derived from the writings of Hirschman (1958) and Myrdal (1971) on the spatial aspects of economic growth.

[23] On the historic tendency of industry to spread geographically, see H. Johnson (1968). The reference to Hume comes from an essay by Lewis (1957, p. 582). Those observations are directly counter, of course, to the views of dependency theory.

the polarization effects at the core tend to predominate over spread effects to the periphery.

Over the longer term, however, the rate of growth in the core tends to slow and the location of economic activities tends to diffuse to new growth centers in the periphery. For a variety of reasons, such as the increasing cost of labor and declining marginal returns on investment, the core begins to lose its dynamism and competitive advantage. Simultaneously industry spreads from the core to the periphery through the mechanisms of trade, investment, and the transfer of technology. In this process of diffusion, the periphery enjoys the "advantages of backwardness": lower labor costs, the most modernized plants, and expanding investment opportunities (Gerschenkron, 1962). As a consequence, newly industrializing cores in the former periphery eventually displace the old core as the growth poles of the system.

As a number of writers have observed, the growth and evolution of the market system is to a considerable extent a frontier phenomenon.[24] Economic growth is promoted through the discovery of new sources of food and raw materials and the development of new markets at the frontier or periphery of the system. In previously untapped regions, profits and monopoly rents tend to be higher than in already developed regions. Furthermore, technological advance and other forms of innovation frequently function, for example, with novel modes of transportation or communications, to open up the economic frontier through the reduction of transaction costs. As traditional Marxists in particular have appreciated, this continual expansion into peripheral frontiers gives new vigor to capitalism at the same time that it develops the frontiers and creates new economic competitors.

The diffusion of economic activities and the growth process, however, does not take place evenly throughout all of the periphery. The distribution of raw materials, the existence of entrepreneurial skills, and the networks of communications as well as the policies of governments and other factors favor one area over another. Nations commence their development at different times and grow at different rates, and spread takes place unevenly in the form of new concentrations of economic power and wealth (Hawtrey, 1952, p. 70). In time, what was an undifferentiated part of the periphery becomes a growth pole in its own right and may even become a center for the further diffusion of economic growth.

[24] Economic growth as a frontier phenomenon is a frequent theme in historical writings and is closely related to the expansionist tendency of a market system. See, for example, the many writings of William McNeill on historical patterns. Di Tella (1982) presents a systematic analysis of this subject.

This process of uneven growth among national economies in a liberal world economy results in an increasing economic and political differentiation of states and creates an international hierarchy of wealth, power, and dependency relations among emergent core economies and periphery economies dependent upon the former for the major sources of their growth. Powerful nationalistic reactions are stimulated as new centers of economic growth arise and other economies decline. Individual states and economic interests attempt to counter and channel the operation of economic forces.

In effect, economic nationalism arises in the periphery as a protective measure against those market forces that first concentrate wealth and then divide the international economy into advanced core and dependent periphery. Economic nationalism reflects the desire of the periphery to possess and control an independent industrial core in which wealth, attractive careers, and power are located. Its objective is to transform the international division of labor through industrialization and to transform the peripheral nation into a relatively independent industrial core. As industrialism spreads to the periphery and creates new sources of competition, the core may become protectionist in an attempt to slow or arrest its industrial decline.

Because of the initial industrial superiority and competitive advantages of the core, the later the industrialization of the periphery the greater the effort necessary to develop viable industries and to break into world markets. There is a corresponding need for a strong national authority or "hard state" to offset the market forces that tend to concentrate wealth, economic activity, and power in the core. Although the spread of growth, as well as the concentration of wealth, can be explained in large part by market forces, the existence of some centralized political authority or strong state that can counteract the economic power of existing centers and the centralizing tendency of market forces is a necessary condition for spread to take place at the rate desired by the periphery.

Once set upon the course of industrialization, however, the late industrializers enjoy the "advantages of backwardness" mentioned earlier, which eventually enable them to surpass the rate of growth of the industrial leader. Utilizing the most advanced and efficient techniques and lessons learned by the more advanced economies, the late starters catch up with and may, in fact, overtake the industrial leaders, in time shifting the center of world industrial power and, of course, the international balance of military power.

As world industry and economic activities spread to rising centers of economic power in the periphery, the original core (or cores) comes un-

der increasing competitive pressures. With relatively high wage rates and increasingly inefficient industries, its exports are displaced in world markets by those of lower-cost foreign producers. Decreasingly competitive industries begin to lose the domestic market, thereby unleashing within the declining core economy itself powerful forces of economic protectionism to defend threatened industries and the economy's position within the system. Liberalism gives way to nationalistic policies, and protectionism spreads throughout the international system. As a consequence the liberal world economy threatens to fragment into competing economic nations or regional blocs.

The process of uneven growth described here may be characterized as follows: During the early phase of an interdependent world economy, polarization effects predominate over spread effects. Over time, however, due to the growth of efficiency in the periphery and to increasing diseconomies in the core, spread overtakes polarization. Certain peripheral economies grow and industrialize at a more rapid rate than the core. As this happens, the competition between rising peripheral economies and declining core economies intensifies, thereby threatening the stability of the liberal economic system.

The Rise and Decline of Leading Sectors

Another characteristic of economic growth is that various sectors of the economy grow at different rates; the process of economic growth is an unbalanced one. In every economy, whether regional, national, or international, there are leading or rapidly expanding sectors that pace and drive the rest of the economy, relatively stagnant sectors that exist in a state of overall equilibrium, and declining sectors, former growth sectors that have become brakes on the rest of the economy. A market economy evolves through successive structural changes produced by what Joseph Schumpeter called a process of "creative destruction" (Schumpeter, 1950).

Underlying this phenomenon of uneven sectoral growth in the modern world is the law of industrial growth and retardation or what will subsequently be called the "product cycle."[25] First described by Simon Kuznets (1930), the pattern of development of significant industrial innovation follows an S or logistics curve. The initial period is one of rapid economic growth characterized by quantitative increases in output and qualitative improvements in the basic technology; secondary

[25] On the law of industrial growth or retardation, see Kuznets (1930, ch. 1). This idea is basic to the concept of product cycle. Much of the argument in this section centers on this concept.

and tertiary industries are spun off and radiate growth throughout the economy. In time, however, the growth impulse of the innovation flags and the industry recedes as a generator of high rates of profit, wages, and employment. Eventually, the industry declines and is displaced by rapidly expanding industries beginning their ascent of the curve. Rising and declining industrial technologies characterize the dynamic economy and significantly affect its politics (Kurth, 1979).

Since the Industrial Revolution, the major cause of economic growth has been a series of technological innovations that have provided new opportunities for investment and economic expansion. A new product, a more efficient industrial process, or a novel mode of transportation constitutes a powerful stimulus to a particular sector of the economy. In time, however, the expansion of these "epochal" innovations, to use Kuznets's term, begins to dwindle, causing a decline in the marginal return on investment and its displacement by other new and expanding sectors (Kuznets, 1966, p. 5).

The history of the world economy over the last two hundred years is one of successive leading economic sectors. These rising and declining areas of economic activity have been responsible for the process of economic growth; they define the various phases of the continuing industrial revolution and they reshape the political landscape as well. Technical breakthroughs in steam power, iron metallurgy, and textiles propelled economic growth and resulted in the industrial preeminence of Great Britain. Subsequently, the development of the railroad and the opening of new lands in America and elsewhere in the "lands of recent settlement" provided the great stimulus to investment and growth. In the latter part of the nineteenth and into the twentieth century, new methods of industrial organization and the science-based technologies of steel, electricity, and chemicals led the process of growth, especially in the two emergent industrial powers, Germany and the United States. In the middle of the twentieth century and during the era of American hegemony, consumer durables, the automobile, and petroleum-based industries paced the world economy. In the last decades of this century, the new technologies of electronics, computers, and communications and the so-called service sectors are bringing important changes in the structure of the international economic and political system.

In the liberal model of an economy, this process of uneven sectoral growth and structural change takes place relatively smoothly. In such an economy, sectors on the steep part of the curve grow at a rapid rate and absorb the productive resources (labor, capital, and land) that are released from the declining sectors of the economy. Others are at the top of the curve, ceasing to be sources of continued growth. Still other

sectors are on the downward slope of the curve, declining and releasing resources that can feed the expanding sectors of the economy. Although disaggregate growth among various sectors is uneven, in the aggregate the economy continues to grow and thus ensures a steady rate of employment, profits, and economic welfare.

In the real world, however, this process of uneven sectoral growth and structural change is far from smooth. Intense conflict over resources and markets usually exists between expanding and declining sectors. Labor and capital in declining sectors resist being displaced by labor and capital in expanding sectors and become proponents of protectionism and nationalist policies. Political conflict ensues between declining and rising sectors over the control of economic policy. This political tension is especially acute when the expanding sector is located in one nation and the declining sector is located in another. In a world of nation-states and political boundaries, capital and especially labor cannot migrate easily from declining to rising sectors to find new employment. As a consequence, interstate conflicts arise as individual states seek either to promote their expanding industries or to protect their declining ones.

A major objective of states in the modern world is to be the locus of the growing sectors of the international economy. States aspire to be the source of technological innovation and to acquire industrial superiority over other societies. The possession of a technological monopoly in the expanding sectors of the world economy enables a state to extract "technological rents" from other economies in the system. In the language of contemporary economics, every state, rightly or wrongly, wants to be as close as possible to the innovative end of "the product cycle" where, it is believed, the highest "value added" is located.[26]

As Schumpeter argued in *The Theory of Economic Development*, profits and high rates of return on investment are due to the existence of monopoly (Schumpeter, 1961). In a system of perfect competition, profit would not exist. Monopoly profits tend to be highest in the expanding sectors of the economy before an initial technological advantage diffuses to economic competitors. Smith's observation that every businessman aspires to be a monopolist and enjoy monopoly profits or rents can also be applied to states. For this reason, interstate competition for growth and high value-added sectors is a major aspect of the

[26] Dixit (1985, pp. 22-23) is a good discussion of the concept of "value added" or super-profit and its utility.

dynamics of the international political economy. One of its fundamental issues is the global location of these activities.

Although these tendencies have always existed, they have become more intense and significant due to an increased rate of technological diffusion and resulting changes in comparative advantage. In this more dynamic world, leading economic sectors are destroyed with increasing rapidity, forcing painful adjustment costs on capital and labor. When this process of economic change and adjustment takes place across national boundaries, as has happened with the remarkable rise of Japanese competition in the late twentieth century, the phasing out of declining industries and creating of new growth sectors have powerful political effects.

Long-Term Variations of Economic Growth

Economic growth has been truly remarkable throughout the long-term history of the world economy in the modern age. A prolonged and massive increase in aggregate wealth per capita has taken place over several centuries. As liberals point out, the world economy has followed an upward linear growth path. This process, however, has been uneven over time just as it has been uneven with respect to regions of the world and economic sectors. This phenomenon of cyclical economic growth also has significant political effects.

The fact of uneven rates of economic growth is not a matter of serious dispute among economists. Business cycle theorists have identified a number of cyclical patterns, such as the Kitchin (about three years), the Juglar (nine or so), and (more debatable) the Kuznets (approximately twenty years).[27] Economists differ regarding the causes and dynamics of these cyclical phenomena, for example, the types of shocks that cause the economic system to depart from its equilibrium growth path and the factors that account for subsequent failure to adjust quickly and thereby to return to a state of equilibrium growth. Economists also disagree about the susceptibility of business cycles to control through fiscal or monetary policy.

A more controversial and significant problem for the world economy is the alleged existence of long cycles of economic expansion and contraction. First given international prominence by the Soviet economist N. D. Kondratieff in the 1920s and subsequently incorporated into the business cycle theories of Joseph Schumpeter and others, these "long waves" or "Kondratieff" cycles are said to be of approximately fifty years' duration. Relegated to the intellectual scrapheap by liberal econ-

[27] Lewis (1978b, p. 19) summarizes the different types of economic cycles.

omists and an embarrassment to most Marxists, the theory of long waves of economic growth and stagnation refuses to go away.[28]

According to the long-wave hypothesis, these upward and downward swings are an inherent feature of the operation of the world economy. The theory argues that the world has experienced several Kondratieff cycles since the Industrial Revolution of the late eighteenth century. From 1788 to 1815, there was an expansionary phase of economic growth and rising prices, which was followed by contraction and falling prices from 1815 to 1843. The period from 1843 to 1873 was one of expansion but, following the major depression of 1873, slower yet substantial growth and falling prices characterized the world economy until 1897. Another expansionary phase then began; it continued until the economic collapse of the Great Depression. The recovery that commenced in the late 1930s and 1940s led to the unprecedented expansion of the late 1950s and 1960s. Since 1973, economic contraction and, until the 1980s, rising prices have characterized the world economy. Kondratieff cycle theorists view the history of the world economy as one of periodic crests and troughs with the separation between one crest and the next lasting approximately fifty years.

Although Kondratieff himself associated the outbreak of major wars with economic upswings, a number of contemporary social theorists have gone further and posited a determinant and systematic linkage between such long-term economic cycles and what they identify as cycles of great wars and world political leadership.[29] Although this is an intriguing idea, the causal relationship has not been adequately demonstrated. At least, however, as the theory of hegemonic stability suggests, the existence of a "liberal" world political leader does facilitate the stability and growth of the world economy and, furthermore, the economic health of the hegemon and of the world economy more generally are no doubt closely related. (See discussion below.) For the moment, however, with the existence of "long waves" themselves in dispute, these still bolder theories connecting economic and political cycles should be regarded with some reserve.[30]

Although few economists would deny that the world economy has experienced alternating long periods of rapid growth and of relatively

[28] The revival of this theory in the 1970s led to a number of writings by Marxist and other scholars. Van Duijn (1983) provides an extensive discussion of the theory. By the mid-1980s, with economic recovery, the theory had once again receded into the background.

[29] Modelski (1978) is a systemic discussion of the relationship of long waves and political development.

[30] See Levy (1985) and Gilpin (1986) for an evaluation of this theory.

slow (or no) growth, most would dispute the interpretation that these ups and downs represent a regularized and cyclical phenomenon (Maddison, 1982, p. 72). Skeptics point out that there are too few occurrences of major upswings and downswings to establish the existence of a cycle; or, to put it another way, there are insufficient points on the curve to support any generalizations. More important, in the absence of an identifiable mechanism to explain successive periods of expansion and contraction, one must assume that they are due to random events; that is to say, what appears to be a wavelike characteristic inherent in or endogenous to the process of economic growth is really due to a variety of exogenous political and other developments. Finally, insofar as any pattern can be said to exist, it is primarily a price phenomenon in which the upswings and downswings represent rising and falling prices that may or may not affect the level of real phenomena, for example, levels of employment or aggregate output.

Yet even the skeptics believe that certain conclusions may be valid regarding these alleged long waves. They agree that the world economy has experienced a series of alternating periods of rising and of falling prices for reasons that are not well understood. They also acknowledge that periods of rising prices tend to be associated with rapid economic expansion and those of falling prices, with economic contraction. They note, however, that even during the latter times, the general trend has been continuing, although reduced, growth. Thus, although the evidence does not confirm the hypothesis of a fifty-year Kondratieff cycle, it does support the existence of alternating periods of rising and falling prices and of changing rates of economic growth.

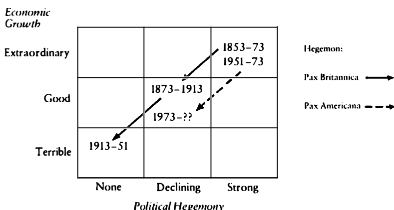
Even though long waves may be merely price phenomena, which are unrelated to "real" phenomena, rising and falling price levels can and do have a profound impact on both domestic and international society. Prolonged periods of inflation and deflation redistribute income among social classes and can trigger social and political discontent. Changes in relative prices also alter the terms of trade between industrial and agricultural products. For example, the falling prices from 1873 to 1897 that brought hard times to many farmers, workers, and particular industries stimulated economic nationalism and a global retreat from free trade. Due to the high level of global economic interdependence and the vulnerability of domestic economies to change in the world economy, such vicissitudes transmit shocks throughout the system and cause profound economic and political dislocations.

Further, several of the economic troughs have in fact represented a profound slowing, at least momentarily, of the engine of economic growth. Although it is perhaps only a coincidence that these alternating

crests and troughs have occurred approximately fifty years apart, it is important to recognize that in the three major recessions over the past century—post-1873, the Great Depression of the 1930s, and again beginning in 1973—there have been significant consequences for international relations. The recession of 1873 undoubtedly was a factor in the subsequent rapid spread of economic nationalism, commercial rivalries, and imperialistic conflict. The Great Depression with its spawning of Hitler and other dictators, was a major factor leading to the Second World War. And the slowing of economic growth in the late twentieth century has again strained global political relations. In short, the transmission of these recessions as well as other untoward economic dislocations throughout the interdependent world economy has caused individual countries to retreat into economic isolation in order to protect themselves and has also stimulated nationalistic antagonisms.

The periodization of these long swings in economic activity is a disputable enterprise at best, given the paucity of reliable data. One of the most noteworthy and helpful charting efforts is that of Arthur Lewis. Lewis has calculated that over the past century and a half, the world economy has experienced several alternating periods of extraordinary growth, good growth, and terrible growth (Lewis, 1984, p. 15). (See Fig. 1.) There have been two periods of extraordinary growth (1853-1873 and 1951-1973); two periods of good growth (1873-1913 and

FIGURE 1
Economic Growth and Political Hegemony



SOURCE: Adapted from W. Arthur Lewis, *The Rate of Growth of the World Economy* (Taipei: The Institute of Economics, Academia Sinica, 1984), p. 15.

1973-present); and one period of terrible growth (1913-1951), in an era that included two world wars and a severe depression. These periods are very interesting from the perspective of the theory of hegemonic stability. (See McKeown, 1983, for another view.)

Although the causal connections are unclear and debatable, it is worth noting that the periods of extraordinary growth coincided with the eras of British and American economic and political hegemony and that the periods of slower but still good growth paralleled the decline of these hegemonies. The period of terrible growth was the interregnum between these two eras of hegemonic leadership. Whatever the causal relationships, a strong association certainly exists between relative rates of global economic growth and the global political structure.

As Lewis points out, the periods of extraordinary growth have three important characteristics. First, these are catching-up periods in which other countries adopt those technological innovations within the leading sectors of economic growth that have been pioneered by the more advanced countries. For example, during the 1853-1873 period of rapid growth, continental Europe, the United States, and Japan adopted the technologies that Britain had innovated during the first phase of the Industrial Revolution: textiles, iron smelting, railroads, and the steamship. In the next rapid-growth period, Europe and Japan led the world in economic growth by adopting technologies developed by the United States during the interwar period: automobiles, electricity, consumer durables, synthetic fibers, telephones, and aircraft. Indeed, the "Americanization" of Europe and Japan and their conversion to mass consumer societies were major factors in the postwar period of rapid growth.

A second aspect of this phenomenon of alternating periods of slow and rapid growth is that the catching-up periods are preceded by slack periods and the accumulation of a scientific and technological backlog. In the words of A. C. Pigou, "there is evidence that in slack periods technical devices and improvements accumulate in the sphere of knowledge, but are not exploited till times improve" (quoted in G. Clark, 1937, p. 39). The initial period of extraordinary growth followed an era of famine, social unrest, and revolution in the 1840s, an era that depressed investment. The next period followed a series of disasters; two devastating world wars and a great depression were responsible for both a pent-up demand and a large supply of unexploited technologies and investment opportunities that led to postwar economic growth throughout the world.

A third feature of these periods of extraordinary growth is that they are characterized by a movement toward free trade under the leadership of the hegemonic economy. Preceding the surges of world trade

have been periods of rapid industrialization. The repeal of the Corn Laws in 1846 witnessed British launching of an era of free trade that lasted until the revival of economic nationalism in the 1870s. Due largely to American policy initiatives, international trade expanded even more rapidly than domestic economies during the 1950s and 1960s. The two periods of growing interdependence among national economies appear to have been triggered by increasing prosperity. Economic growth undoubtedly encourages the expansion of interdependence as much or more than interdependence fosters economic growth, but the relationship between growth and interdependence is obviously cyclical.

Eventually, the completion of the catching-up process and the slowing of the global rate of economic growth stimulate forces of economic nationalism, so that economic interdependence is then challenged by increasing trade protectionism. Although particular individual countries will continue to enjoy rapid rates of economic growth, as did Germany and the United States in the latter part of the nineteenth century and as do Japan and certain other economies in the 1980s, the global rate of growth declines until new sources of economic growth and a new economic leader emerge. The era of extraordinary economic growth that ended with the decline of British hegemony in the latter part of the nineteenth century was not renewed until new sources of growth emerged at the time of American hegemony in the 1950s.

In summary, although a regularized, systemic, and cyclical pattern of expansion and contraction may not exist, the modern world economy has in fact undergone a traumatic experience approximately every fifty years and has experienced alternating periods of rapid and slow growth. These massive swings up and down have affected mainly the price level; in some cases, however, they have entailed significant changes in economic output and in the rate of unemployment. Moreover, these erratic economic shifts have been global phenomena. Originating in the core economies, their effects have been transmitted through the market mechanism and the nexus of economic interdependence to the extremities of the planet, shattering individual economies and setting one economy against another as each nation has tried to protect itself against destructive economic forces. The periods of expansion and contraction have also been associated with profound shifts in the structure of the international economic and political system.

Several prominent and contending theories have been set forth to explain these alternating periods of rapid and slow growth.[31] Each can be supported with certain facts, but none of them is flawless. However,

[31] Hansen (1964) is a thorough discussion of these theories.

since they do illuminate the dynamics of the international market system, some will be evaluated in the following paragraphs. (Because the Marxist theory of capitalist crisis has been evaluated earlier, it will not be discussed here.)[32]

One theory of economic swings is that they are closely associated with major wars. Although a number of versions of this theory exist, one of the most important is that long waves are caused by the preparation for and the aftermath of great wars. According to this view, the long periods of rising prices and economic expansion are caused by large governmental expenditures associated with preparation for war. Then, following the war, the curtailment of war expenditures and the difficult adjustments to the reduced Keynesian stimulus of the war brings on a period of economic contraction. Thus, "long waves" are intimately related to the fiscal stimulus associated with the great or hegemonic wars of modern history.

Evidence for this theory is inconclusive and contradictory. The first "long wave" of economic expansion (1788-1815) and the subsequent contraction (1815-1843) were undoubtedly a consequence of the Napoleonic Wars; war expenditures and peacetime adjustments were key to the economic fortunes of these periods. War expenditures particularly stimulated development of those technological innovations associated with the Industrial Revolution, and overexpansion of industry during the wars followed by the postwar decrease in stimulus brought on the recession phase of the cycle. However, during most of the nineteenth century and the first part of this century, the connection between war expenditures and economic activities was less strong. War preparations once again were a stimulus after 1936. The period of expansion immediately following the Second World War was unrelated to military expenditures. The Korean War provided some stimulus, as did the Vietnam War, which was followed by contraction and high inflation. On balance, one can conclude that preparations for war can exert a Keynesian or demand stimulus, provided that growth and investment opportunities exist in exploitable technological innovations or newly available resources; further, long wars usually do cause serious economic problems in their aftermath. It is very difficult, however, to establish the existence of any necessary and systemic connections between war and economic activity.

A second theory of long waves (applicable primarily to the nineteenth century) associates the waves with changes in the effective supply of the monetary gold stock and the increasing volume of trade. For-

[32] Joshua Goldstein (1985) reviews the major theories of capitalist crisis.

tuitous discoveries of gold such as the California strikes of the 1840s gave a monetary stimulus to the economy, and the increase in the gold supply from the mid-nineteenth century to 1913 is said to have led to a rise in the price level and an era of economic expansionism. This line of reasoning, however, is very difficult to support; at best, gold served as an economic stimulant because of favorable "real" factors such as existing investment opportunities and favorable terms of trade for developed economies. From this perspective expansionary American monetary policy in the postwar era has been a major factor in the high rate of economic growth.

A third theory argues that the movement of agricultural and commodity prices is primarily responsible for long waves. Food shortages, for example, increase inflationary pressures whereas food surpluses are deflationary.[33] The period from 1873 to 1896 was one of agricultural depression; this was followed by an era of agricultural prosperity (1896-1920) and subsequently by further difficulties in the 1920s and the 1930s. The stagflation of the 1970s was certainly triggered and aggravated by the rapid rise in food and energy prices. Surpluses and shortages in supply do dramatically affect the terms of trade between commodity and industrial sectors. As will be argued below, supply constraints greatly limited growth in the 1970s. On the other hand, in the mid-1980s the drop in oil prices and overcapacity in most commodities were associated with global recession.

From the perspective of this book the most interesting theories focus on capital investment and technological innovation. One theory argues that long cycles arise from massive overinvestment in and depreciation of capital goods such as railroads and factories, and another attributes them to the clustering of major innovations in particular sectors at particular times (Joshua Goldstein, 1985). Although these theories are very closely related in that innovations stimulate investment, the second will be emphasized here.

According to a theory formulated by Knut Wicksell, Joseph Schumpeter, and others, economic cycles are caused by the relative abundance or scarcity of investment opportunities. Periods of economic expansion are due to development of technological and other innovations as well as discovery of new resources that provide the basis for the growth of real investment. During such expansive periods the pace of technological advance and the diffusion of innovations to developing economies is greater than usual. Thus periods of expansionism are caused by an

[33] Rostow (1978) discusses the relationship of commodity prices and economic swings.

explosion of revolutionary new technologies and investment opportunities that sweep through and transform the entire world economy.

When investment possibilities resulting from revolutionary technological breakthroughs or discoveries of new resources are exhausted, the rate of real investment and economic growth slows, thereby ushering in an era of reduced growth. Although economic growth slows, real income usually continues to rise due to the higher levels of productivity reached in the buoyant period and to continuing marginal technological improvements. During this less active period, investment declines but general economic advance continues, although at a slower pace. The post-1973 period is characteristic of this phenomenon.

Underlying this theory is the assumption that major technological innovations tend to cluster in time as well as in space. Although technological advance in general is incremental and continuous over time, this theory holds that the revolutionary innovations that accelerate the pace of economic growth and propel the economy in novel directions are clustered. For example, the innovation of the automobile and the consequent need to build highways spurred investments in steel, petroleum, cement, and other areas. The shape of cities, the industrial base of the economy, and the landscape itself were transformed. It is such a clustering tendency of revolutionary technologies and their secondary effects throughout the economy that are said to produce the great upswings of the world economy and the successive restructuring of economic activities.

According to this theory, therefore, the first period of economic expansion (1788-1815) was the result of the Industrial Revolution and its revolutionary technologies in textiles, coal, and iron. The subsequent era of hard times (1815-1843) was one of readjustment while these technologies were incorporated into the economic system. The second period of expansionism (1843-1873) was alleged to be based on what Schumpeter called the "railroadization of the world" and the opening of new lands, especially in North America.[34] This was followed by the sharp decline of the last part of the century (1873-1897). Then a new clustering of innovations in the electrical, chemical, and automobile industries ushered in the good times of the years prior to the First World War (1897-1913). The electrification and motorization of the Western world resumed in the 1920s, only to be stopped short by the Great Depression. Following the Second World War, the electrical, chemical, and automobile industries were joined by electronics, aviation, and others to feed the investment boom of the 1950s and 1960s. The ex-

[34] This discussion is based in part on Schumpeter's writings.

haustion of growth possibilities in these technologies and the increased cost of energy are believed to be partially responsible for the drop in the growth rate in the 1970s.

In addition to the fact that technological innovations tend to cluster during particular periods, they tend to occur within particular economies. The innovative technologies of the Industrial Revolution and the first upswing—textile, steam, and iron—were located principally in Great Britain. The railroad and the mechanization of production that fed the second upswing were developed primarily in Great Britain, France, and Germany. By the time of the third upswing the front runners in the technologies of electricity, chemicals, and automobiles were Germany and the United States. In the upswing following the Second World War, the United States has been joined by Japan. If this pattern of rising and declining national leadership in technological innovation continues, Japan should be the next locus of revolutionary technological breakthrough.

The clustering of technological innovation in time and space helps explain both the uneven growth among nations and the rise and decline of hegemonic powers. The innovative hegemon becomes the core of the international economy and, as the most efficient and competitive economy, has a powerful incentive to encourage and maintain the rules of a liberal open world economy. As it loses its inventiveness, the declining hegemon is unable to maintain an open world and may even retreat into trade protectionism. For a time, the declining center (or centers) of growth is unable to sustain the momentum of the world economy and the rising center is unable or reluctant to assume this responsibility. Periods of slowing rates of growth appear to be associated with the shift from one set of leading industrial sectors and centers of economic growth to another and with the transition from one hegemonic leader to the next.

This technological theory of business cycles has a certain plausibility and may indeed explain much about changing price levels and uneven growth. However, as Nathan Rosenberg and Claudio R. Frischtak (1983) have argued, this theory presents several serious problems. In the first place, proponents of the theory do not have a satisfactory explanation of why revolutionary technologies appear to cluster, especially every fifty years or so. Second, the theory does not adequately connect the process of technological innovation, diffusion, and investment to the "long wave" phenomenon. Third, even if major technological breakthroughs do tend to cluster, it has not yet been demonstrated that these innovations do in fact exercise a measurable impact on the total economy. For Rosenberg and most economists, therefore, the ap-

parent clustering of major innovations and the phenomenon of uneven growth constitute historical accidents determined by random events, accidents that in themselves cannot explain the experience of economic growth.

The absence of a satisfactory explanation of the phenomenon of technological innovation and its importance for uneven growth, however, does not lessen its significance. Whatever the cause may be, the growth of the world economy has proceeded as if long waves of rapid and slow growth do in fact exist. There have been alternating periods of rising and falling prices as well as eras of extraordinary growth and deep recessions during recent centuries. Economic dislocations have been global in character and have been followed by profound economic, social, and political disturbances. So, although little is known about the nature and causes of technological and other types of innovation, it is known that a strong tendency for innovations to cluster in space and time does exist. The major innovations that stimulate the growth of the dominant economy and subsequently carry the world economy into an expansionary phase tend to take place in particular national economies and at particular times. This clustering phenomenon helps account for the rise of the dominant economy and its crucial role as an engine of growth in the larger world economy. In time, however, the impetus provided by this burst of innovation recedes and the rate of world economic growth slows. The revival of economic growth appears to require a novel cluster of innovations and, it would appear, a new dominant economy to lead the world economy.

In a truly liberal world economy, the inevitable shifts in the locus of innovation underlying the process of uneven growth would proceed with little difficulty. Centers of innovation would rise and decline depending solely upon considerations of relative efficiency and comparative advantage. As old centers declined, they would release their underutilized resources of capital and labor to the rising centers of economic growth. The rising centers would in turn be receptive to absorbing such surplus capital and labor. Investment capital and unemployed workers would be free to migrate from declining to rising national centers of innovation and economic growth.

In the real world of nation-states and political boundaries, the transition from one center of innovation and growth to another is anything but smooth. It is highly conflictual as declining states and economic sectors resist the forces of technological change, and rising states and economic sectors try to break down trade and other barriers. Since capital and especially labor are unable to move freely throughout the system, structural rigidities prevent easy adjustment to emergent economic

reality. Inefficiencies, bottlenecks, and restrictions slow the rate of adjustment and economic growth.

Instead of an easy transition from one industrial leader to another and a phasing out of dying industries, periods of structural change tend to be characterized by intense nationalistic competition. The newly industrializing countries, following in the footsteps of their predecessors, adopt the latest technologies and eventually challenge previous leaders in world markets; the old try to maintain their position and preserve their threatened industries. Consequently, the resistance to adjustment in the declining industrial sectors gives rise to intense trade protectionism. In the rising industries, potential technological leaders scramble for dominant positions, and trade rivalries become fierce. As Michael Beenstock has pointed out, these phenomena are symptomatic of the transition from one structure of global economic relations to its successor (Beenstock, 1983). In the late nineteenth century, in the 1920s, and again in the 1980s, transitions from one global industrial structure to another have been characterized by intensive commercial conflict. Structural crises of this type appear to be an inherent feature of the modern world political economy.

Over the past two centuries, technological innovation, population growth, and the development of new territories and associated resources have propelled the growth of the market economies. They have provided investment opportunities that have led to continuing capital accumulation. This growth of the Western economies has, on balance, stimulated growth in the less developed economies. The socialist economies have benefited through trade and adapting Western innovated technologies to their own development needs; few novel technologies have in fact originated in the Soviet Union and its bloc. When such factors as technological innovations, demographic growth, and discovery of new resources have coincided, the world has experienced the growth spurts of the mid-nineteenth and twentieth centuries. When one factor or another has been deficient, the engine of growth has slowed in the Western economies and subsequently throughout the entire globe. This process of uneven growth has provided much of the dynamics of modern history.

Structural Change and Economic Conflict

The process of uneven growth and structural change is accompanied by intermittent periods of economic cooperation and conflict. The history of the world economy has been one of vibrant eras of liberalism, openness, and free trade followed by eras of stagnation, protectionism, and

nationalist conflicts. Although the theories associated with the political economy of trade and protection are helpful, those theories that stress interest groups and other domestic factors are only partial explanations.[35] In addition, it is necessary to consider structural change at the international level. A recent formulation, originally set forth by Gautam Sen and extended here, may provide insight into the process by which structural change causes economic conflict (Sen, 1984).

According to this theory, all states want to possess modern industries because of the linkages among industry and overall economic development, the goal of economic self-sufficiency and political autonomy, and the fact that industrialism is the basis of military power and hence of national independence. This nationalist desire for industrial power leads states to promote industrialization based on the importation of foreign technologies. The less developed economy attempts to acquire the most advanced technology from the hegemonic power and from other highly developed economies. As Marx noted, "the country that is more developed industrially only shows, to the less developed, the image of its own future" (quoted in Sen, 1984, p. 15). The follower has the great advantage, moreover, of being able to skip economic stages and to overtake the industrial leader.

The political consequences of this diffusion of comparative advantages and of the rise of new industrial powers are powerfully affected by the speed at which the changes take place and how long is required for the rising challenger to take a significant share of world markets. The shorter the period, the greater will be the adjustment problem imposed on other states and the greater the resistance of domestic interests. Rapid shifts in comparative advantage give rise to intense economic conflicts between rising and declining economies.

In the modern world, four nations have captured substantial shares of international trade in manufacturing in relatively brief periods. The first was Great Britain after the Napoleonic Wars and continuing late into the nineteenth century. The second was Germany between 1890 and 1913, and the third was the United States, also beginning in 1890 and greatly accelerating in the twentieth century. The contemporary era is witnessing the spectacular rise of Japan as a trading power (Lewis, 1957, p. 579). The resultant impact of the export drives and the dislocations caused to other economies have generated strong resistance and deep resentment.

As Lewis points out, the process of diffusion was well understood by David Hume in the mid-eighteenth century: "Manufactures gradually

[35] See R. Baldwin (1984b, ch. 12) for a good summary of this literature.

shift their places, leaving those countries and provinces which they have already enriched, and flying to others, whither they are allured by the cheapness of provisions and labour" (quoted in Lewis, 1957, p. 582). Then technological imitation and the creation of similar industrial structures lead to a global overcapacity in particular sectors and trade conflict.[36]

Although advanced countries trade with one another more than with nonindustrialized countries, the creation of highly homogeneous industrial structures can cause commercial conflict in a number of manufacturing sectors. This is a recurrent feature of the world economy.[37] In Sen's words, "the reproduction of similar structures of production introduces a secular tendency towards the creation of surplus capacity in substantial areas of manufacturing since internal and external economies of scale compel a level of production which most countries cannot sustain through domestic consumption alone" (Sen, 1984, p. 158).

Initially, the less developed economy pursues nationalist policies in order to protect its infant industries and overcome the advantages possessed by the earlier industrializers. Eventually, it must attempt to break into world markets to achieve efficient economies of scale and to obtain foreign currency to finance imports of required resources and capital goods (Sen, 1984, pp. 157-58). To the extent that this industrialization is successful, the developing economy, with its lower wage structure, undercuts the industrial position of the more advanced economies. The resulting generation of surplus industrial capacity in the world economy is intimately related to the process of the relative industrial decline of the hegemon, intensified trade competition, and the possible onset of a global economic crisis.[38]

The problem posed for the hegemon by the spread of industrialization was recognized by the early nineteenth-century British critics of free trade who argued that other nations, as they industrialized, would close their markets to British goods and become Britain's competitors in world markets. Since the spread of industrialism would mean the inevitable decline of British industry and power, these critics said that the diffusion of British technology should be prevented (Gilpin, 1975, pp. 74-75). This argument, which can be labeled the Torrens thesis after

[36] Beenstock (1983) presents an interesting theory of these recurrent global economic crises.

[37] Akamatsu (1961), Hicks (1969), and Lewis (1957), among others, make this argument.

[38] Contrary to the view of Peter Cowhey and Edward Long (1983) that the theory of hegemonic stability and the theory of surplus capacity are alternative interpretations of economic crisis, they are really complementary explanations.

Robert Torrens, its foremost proponent, held that "as the several nations of the world advance in wealth and population, the commercial intercourse between them must gradually become less important and beneficial" (Torrens, 1821, p. 288). This idea has been revived in more recent times as the "law of diminishing trade."[19]

The weakness of the Torrens thesis is that it takes into account only the negative consequences for trade of the spread of industry. It neglects the fact that the diffusion of industry from advanced to developing economies has opposed effects (Hirschman, 1952, pp. 270-71). On the one hand, the spread is market-destroying as the newly industrializing countries become able to meet their own needs and eventually appear as competitors in world markets. On the other hand, the spread on industry is market-creating as the newly industrializing countries import capital goods from the advanced countries and, with increasing wealth, their total demand increases for both domestic and imported products. The overall growth in global wealth and volume of trade will thus be generally beneficial for all countries (League of Nations, 1945).

Whether the trade-destroying or trade-creating effects of the spread of industrialism will predominate in a particular situation depends upon a number of specific factors: the flexibility of the older industrial centers and their capacity to adjust to more advanced industries and exports, the nature and extent of protectionism, and the rates of economic growth in developed and less developed economies. These factors determine whether the hegemon and other advanced countries will try to protect their threatened industries or will transform their economies to the new international economic realities.

The paradox of this situation is that the hegemon, and other advanced economies for that matter, must run faster and faster to maintain their economic position. They must continually adjust their economic structures and shift resources out of declining sectors into new ones. For a society this poses what one author has called the "clash between progress and security" (Fisher, 1935). A powerful temptation exists to elect the latter. In the 1930s, this refusal to adjust was a major cause of the severity and longevity of the Great Depression.

The response of the threatened hegemonic power and other declining economies to shifts in the location of industry is therefore a crucial factor in determining whether economic conflict or adjustment takes place

[19] The "law of diminishing trade" is a recurring theme in the literature. Actually the opposite is the case, provided that political circumstances are favorable to the expansion of trading relations. Technological advances, especially in transportation and communication, have in fact made more types of goods and services tradeable and have thereby increased international economic interdependence.

(Ikenberry, 1985). One possibility is for the hegemon to protect itself and shift the costs of adjustment to other economies, as President Nixon did when he devalued the dollar in August 1971 (Gowa, 1983). Another possibility is to adjust to the structural changes and shift resources to more efficient and competitive industries. The third, of course, is to do nothing or very little; this was essentially the choice taken by Great Britain when its hegemony was threatened in the latter decades of the nineteenth century. In *Growth and Fluctuations, 1870-1913*, Arthur Lewis demonstrates how "Britain was caught in a set of ideological traps. All the strategies available to her were blocked off in one way or another" (1978b, p. 133). As a result of this inaction, the British failed to arrest their economic decline.[40]

Economic theory suggests that a powerful incentive exists for the hegemon to pursue a protectionist strategy. In traditional trade theory, for example, the economic monopolies enjoyed by a reigning hegemon mean that all factors of production benefit from free trade. This tends to create a national consensus in favor of economic liberalism. According to the Stolper-Samuelson theorem, however, once that monopoly is broken, the scarce factor loses; within the hegemonic power, labor is the scarce factor and it therefore becomes highly protectionist (Helpman, 1984, p. 362). Yet in the case of Great Britain, labor was never powerful enough to impose its will on trade policies. Moreover, British capital continued to benefit through foreign investment and used its powerful influence against economic protectionism. In the case of the declining American hegemon, the crucial choices have not been made as of late 1986.

The process of uneven growth poses the problem of economic adjustment, or what Kindleberger (1962, ch. 7) calls "the capacity to transform." The preferred strategy for the hegemon and the system as a whole is to transfer resources out of declining into more efficient and competitive industries that would promote continued economic growth and thus reduce the cost of economic adjustment; in this way growth and adjustment reinforce one another in a virtuous cycle. Failure to adjust reduces the rate of economic growth and makes the cost of eventual adjustment that much higher. With low rates of economic growth and capital investment, the economy enters a vicious cycle of decline, as occurred with Great Britain in the closing decades of this century.

Although economic adjustment to global shifts in comparative ad-

[40] This is the theme of Mancur Olson's (1982) impressive study of the rise and decline of modern nations.

vantage is the wisest choice for an economy, the adjustment problem has become far more difficult than in the past. The increased number of economic players and more rapid shifts in comparative advantage have greatly increased the attendant costs; the astounding pace set for the rest of the world by Japan's rapid movement up the technological ladder imposes immense costs on other economies. The rise of the welfare state and government intervention in the economy have greatly increased the ability of powerful interests to resist paying the adjustment costs, and the role of the market as a facilitator of economic adjustment has been weakened by the shift in the balance of power away from the market toward the state, business, and organized labor (Olson, 1982). And the slowed rate of global economic growth itself makes adjustment more difficult; with a smaller economic pie, there are more losers. These obstacles to economic adjustment threaten the world economy with the possibility of slow growth and failure to adjust that could deteriorate into economic warfare.

Conclusion

The evolution of the world economy and the accompanying structural change involves three developments. The first is the shift in the locus of economic activities from one region to another. The second is the rise and decline of economic sectors. And the third is the increasing integration of national economies and the consequent impact of external forces on domestic well-being. All three, associated with the process of uneven growth, impinge significantly on the interests of states and powerful groups and suggest important questions concerning the political effects of a world market economy that were mentioned in Chapter One and will be addressed further in succeeding chapters.

The first issue raised by the process of uneven growth is that of political leadership and international cooperation. A stable and growing economy requires political leadership, yet the process of growth tends to undermine such leadership. For stability and growth to continue, some new basis of leadership or international cooperation must be found.

The second issue is the relationship of economic and political change. The process of uneven economic growth causes major structural changes in the world economy, which pose a major political problem of adjustment for individual nations; resources must be transferred from declining to expanding industries as the geographic locus of economic growth and the leading sectors shift. Economic adjustment, however, entails significant gains and losses for different individuals,

groups, and nations and thus gives rise to intense political conflict. The failure, especially on the part of the hegemon, to adjust, transform its economy, and make this transition to new economic activities contributes to economic instability and the spread of economic nationalism.

The third issue raised by the growth process is its effects on the development, decline, and welfare of individual nations. A dynamic and expanding international economy leads to an increasing interdependence of national economies at the same time that states intervene in their own economies to control the process of economic growth. They may be motivated to accelerate development, arrest decline, or protect domestic welfare. Whatever the motivation, this interventionism leads to a clash between the desire for domestic autonomy and the benefits of international norms. A stable world economy requires that mechanisms exist that permit national management of the economy consistent with the norms and requirements of a liberal international economy.

The structural changes that have occurred in the postwar world economy and their implications for the liberal international economic order will be analyzed in later chapters. What are the prospects for pluralist leadership and economic cooperation? Can the United States and other powers successfully adjust to the profound shifts that are occurring in the global locus and nature of economic activities? How can the clash between domestic autonomy and international norms be resolved? Among the most important determinants of the answers to these questions will be the continued efficiency and stability of the world monetary system, which is the subject of Chapter Four.