AUSTRALIA IN THE GLOBAL ECONOMY

2025

Tim Dixon • John O'Mahony

TOPIC 1

THE GLOBAL ECONOMY

SAMPLE PAGES

Focus

The focus of this study is the operation of the global economy and the impact of globalisation on individual economies.

Issues

Topic 1 economic issues questions can ask you to:

- Examine the effects of globalisation on economic growth and the quality of life, levels of unemployment, rates of inflation and external stability
- Assess the potential impact on the environment of continuing world economic development
- Investigate the global distribution of income and wealth
- Assess the consequences of an unequal distribution of global income and wealth
- Discuss the effects of protectionist policies on the global economy

Skills

Topic 1 skills questions can ask you to:

- Analyse statistics on trade and financial flows to determine the nature and extent of global interdependence
- Assess the impact on the global economy of international organisations and contemporary trading bloc agreements
- Evaluate the impact of development strategies used in a range of contemporary and hypothetical situations

Economics Stage 6 Syllabus 2009 extracts © NSW Education Standards Authority for and on behalf of the Crown in right of the State of New South Wales, 2009; reproduced by permission.

Topic 1

Introduction

This section (chapters 1 to 3) covers Year 12 Topic 1 *The Global Economy* and focuses on the structure of the global economy and the key features of globalisation. To understand the Australian economy we need to start with a global perspective. Topic 1 is critical to the rest of the course because it provides the overall perspective for when we later examine other topics such as Australian economic issues and policy.

Chapter 1 provides an overview of the global economy. It discusses the main components of the global economy – international trade, international flows of finance and investment, and the role of technology and people movements in strengthening links between individual economies. These links are highlighted with a review of international and regional business cycles.

Chapter 2 examines the main economic theory that underpins globalisation – the concept of free trade and the economic benefits that trade brings. Chapter 2 then examines the reasons for countries restricting trade and protecting their own industries, and how recent years have seen many international agreements to reduce barriers to trade. This chapter concludes with a look at the role of international organisations and government economic forums in managing the global economy.

Chapter 3 examines the divisions within the global economy. Understanding the gaps in the living standards between rich and poor nations is essential to an analysis of the global economy. This chapter looks at the distinction between economic growth and economic development. It discusses the main categories into which different economies are grouped and examines the global and domestic factors that contribute to inequality. Chapter 3 also discusses the impacts of globalisation on economic development.

Topic 1 concludes with case studies of Brazil and Indonesia. Understanding the impacts of globalisation on individual economies is an important complement to any analysis of globalisation at the global level and is a requirement of the Year 12 Economics Course.

Case Study **Brazil** is one of the four largest emerging economies in the world. Like Australia, Brazil is a major commodity exporter, but unlike Australia it has not opened up its economy fully to global forces, and it has had significant economic problems in the past decade. As a case study, Brazil highlights the opportunities and challenges of increased economic integration.

Case Study **Indonesia** is the largest emerging economy of South-East Asia – a region that experienced rapid industrialisation and improvements in economic development in recent decades. The increasing linkages between Indonesia and Australia make understanding the Indonesian economy especially valuable for future Australian economists.

The case studies may complement another country that you choose to study. You may decide to compare the impacts of globalisation on these two economies or you may choose to make either Brazil or Indonesia your case study in 2025.

SAMPLE PAGES

Introduction to the Global Economy

1

1.1 The global economy

1.2 Globalisation

1.3 The international and regional business cycles

1.1 The global economy

The study of economics has traditionally focused on how individual economies operate. While countries have always traded with each other, economic theories have generally assumed that economies operate separately from each other and that the structure and performance of economies is mainly the result of local developments and influences.

This way of looking at economics no longer describes the real world. Today we live in a **global economy** – where the economies of individual countries are linked to each other and changes in a single economy can have ripple effects on others. For many advanced and developing countries, the value of what they buy and sell from overseas is often greater than half of the value of the economy's annual output. When conditions in the global economy change, these changes can have an impact on the economies of far-flung countries almost immediately. The importance of global factors in driving economies has been starkly illustrated in the 2020s by the COVID-19 pandemic and the war in Ukraine. Both of these events resulted in global economic impacts on supply chains, production and prices.

In many respects there is nothing new in the fact that major economic developments can have impacts across the world. For example, the Great Depression of the late 1920s and 1930s had a global impact with many countries experiencing a severe economic downturn. On the other hand, economies are more closely integrated now than at any previous time. The linkages between economies are deeper and more far-reaching than ever before. There are few aspects of life that have not been affected by the waves of global influences washing across the world. This is especially the case in a smaller economy such as Australia, which has embraced the global economy and pursued policies to integrate its economy with those of its region and around the world.

In the past three decades, **globalisation** has become a dominant economic, political and social theme. Globalisation is the integration between different countries and economies and the increased impact of international influences on all aspects of life and economic activity. Unlike many previous times in world history when one major empire often dominated the relationships between economies, globalisation in recent decades has involved layers of influences in all directions. The United States is still the leading world economy, but its power is increasingly constrained by China and other major economies.

Globalisation refers to the integration between different countries and economies and the increased impact of international influences on all aspects of life and economic activity.

Globalisation is also a phenomenon with increasing impacts on national politics. Recent years have seen a backlash against globalisation in many countries. Numerous leaders (such as Donald Trump, who was President of the United States from 2017 to 2021) have come to power promising to strengthen their country against global economic forces. The COVID-19 pandemic added to public concerns about the impact of globalisation, as

SAMPLE PAGES

travel between countries accelerated the spread of the coronavirus, and countries ran short of medical supplies because of their reliance on global supply chains. Some economists describe the past decade as "slowbalisation" because of low growth in trade volumes, increased restrictions on trade and rising geopolitical tensions.

From an economic point of view, the major indicators of integration between economies include:

- international trade in goods and services
- international financial flows
- international investment flows and transnational corporations
- technology, transport and communication
- the movement of workers between countries.

There are many dimensions to globalisation and there are many statistics that can be used as measures of globalisation. For example, some indication of the extent of globalisation can be gained from examining the proportion of programming on television networks and streaming services that is made in Australia versus made overseas; or similarly, the proportion of the top social media influencers who are Australian versus from overseas. These would be classified as social or cultural indicators of globalisation. Each of these indicators provides an insight into the way in which economies are now linked to each other and reshaping the global economy.

Spaced full stops rather than ellipses?

"Globalization reached a record high in 2022 and remained close to that level in 2023. Given the widespread speculation about the "end" of globalization, this result might be unexpected for many . . . . How are such strong globalization numbers possible despite the very real rise of geopolitical tensions, wars, and protectionism?

. . .

First, we might be focusing too much on the largest countries and economies. Many see the U.S. and China interacting less, Europe and Russia decoupling, and the UK leaving the EU as signs of "the end" of globalization. The rate of growth in global trade and connectedness might have slowed, but it stays on a high level.

. . .

Then there is negativity bias. Bad news draws more attention than good news. Dramatic events like attacks on ships in the Red Sea, the Panama Canal's low water levels, or a giant container ship stuck in the Suez Canal generate loud headlines about "deglobalization." Meanwhile, there is little media coverage of all of the goods being delivered every day without a problem.

. . .

[Further], even with the U.S. and China reducing their ties, and Europe and Russia decoupling, the world economy is not breaking apart into rival geopolitical blocs. Many major economies strive for independent and flexible positions, resisting the separation of rival blocs.

. . .

[Also], contrary to many forecasts, globalization has not given way to regionalization. We also see a continued advance in corporate globalization."

– Tobias Meyer CEO, DHL Group
DHL Global Connectedness Report 2023

1.2 Globalisation

Trade in goods and services

Gross World Product (GWP) refers to the sum of total output of goods and services by all economies in the world over a period of time.

International trade in goods and services is an important indicator of globalisation because it is a measure of how goods and services produced in an economy are consumed in other economies around the world. The value of exports of goods and services has grown rapidly in recent decades, increasing from US$4.3 trillion (19 per cent of global output) in 1990 to US$30.7 trillion (29 per cent of global output) in 2023. The size of the **Gross World Product (GWP)** – the aggregate value of all goods and services produced worldwide each year in the global economy – is now 9 times its nominal level in 1980, but the volume of world trade has grown to over 13 times its 1980 level.

SAMPLE PAGES

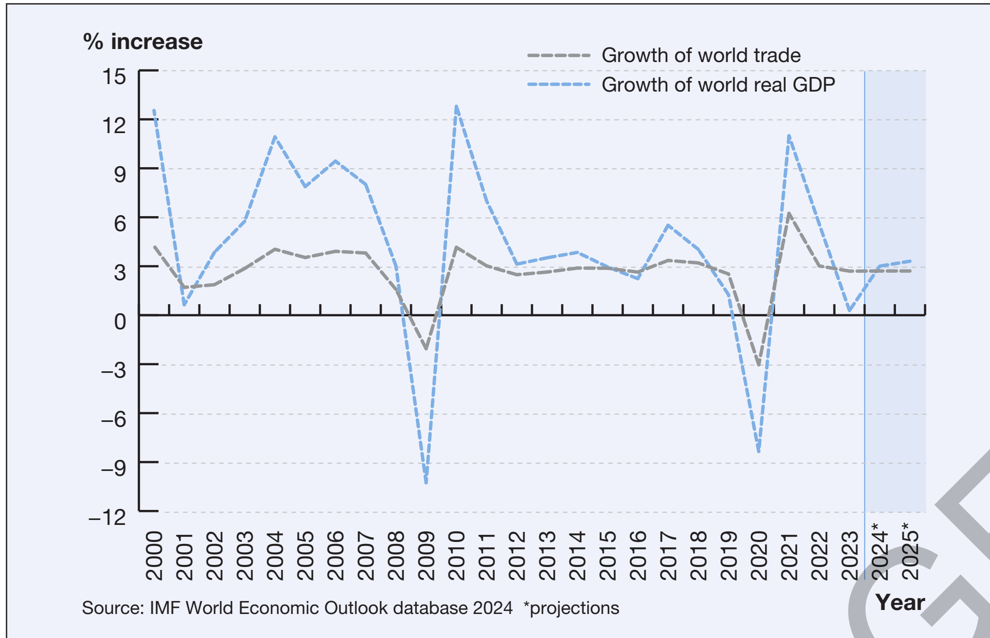


Figure 1.1 – Gross World Product and world trade

Annual growth in the value of trade has generally been around the same level as world economic growth since the global financial crisis. During economic downturns, such as in the early and late 2000s and in 2020, the growth of global trade has contracted faster than world economic output, highlighting the **greater volatility** of trade compared with the GWP. The impact of the COVID-19 pandemic on supply chains, tourism and international education led to a contraction in global trade of 7.8 per cent, followed by a strong rebound in 2021.

The high volume of global trade reflects the fact that economies do not produce all the items they need, or they do not produce them as efficiently as other economies, and have to import goods and services. Global trade grew strongly for decades because of new technology in transport and communications, which reduced the cost of moving goods between economies and providing services to customers in distant markets. Over the same period, governments have encouraged trade by removing barriers and joining international and regional trade groups such as the **World Trade Organization** (WTO), European Union (EU), and the Association of South-East Asian Nations (ASEAN). These developments have been a major force behind increasing global trade.

World Trade Organization (WTO) is an organisation of 164 member countries that implements and advances global trade agreements and resolves trade disputes between nations.

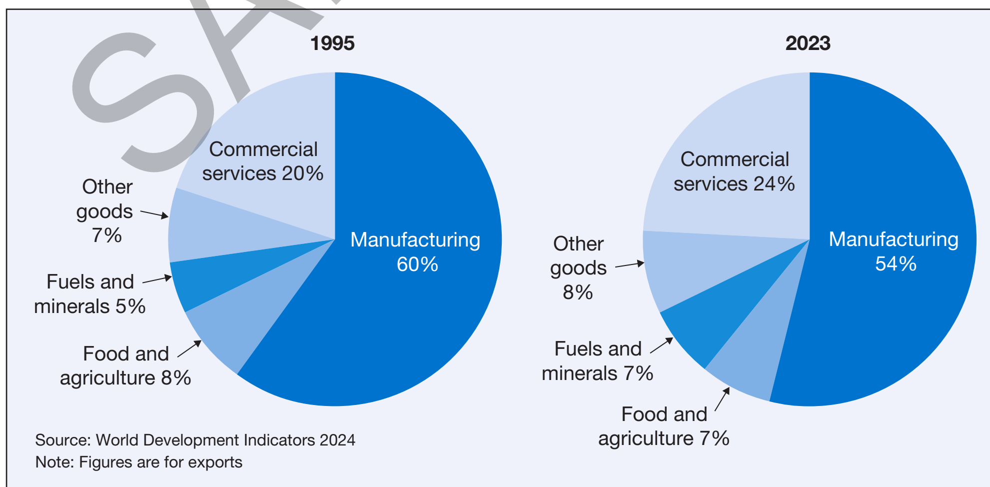
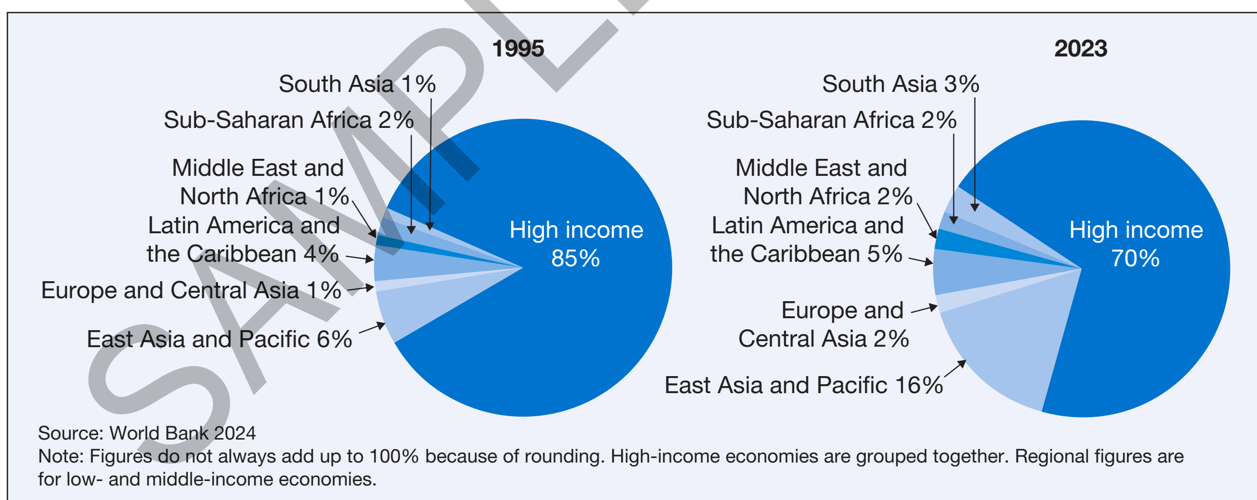


Figure 1.2 – Composition of global trade, 1995 and 2023

SAMPLE PAGES

The mix of what goods and services are traded, known as the **composition of trade,** can have an impact on individual economies. Figure 1.2 shows that global trade is dominated by manufactured goods, such as vehicles, clothing and electronic goods. However, high inflationary pressures have recently softened growth in merchandise trade, which declined by 1.2 per cent in 2023. Inflation has caused lower consumption of imported manufactured goods relative to services and reduced real incomes and consumption, particularly in the EU where energy price spikes have been more pronounced. Trade in services, such as finance and communication, is the fastest-growing category of trade and makes up around two-thirds of global output, but it currently makes up less than one-quarter of global exports. In particular, digitally-delivered exports are likely to be strong future drivers of global trade growth, already quadrupling in value since 2005 according to the WTO. Countries such as Australia should continue to benefit from the growth in services trade because countries with highly educated workforces are best positioned to compete in growing global markets for services. However, less-developed countries that lack the workforce and infrastructure to capitalise on growth in digital service exports may fall behind amidst this growth. Indeed, the least-developed countries currently account for less than half a per cent of total digitally-delivered service exports. Nevertheless, the COVID-19 pandemic resulted in a change in the composition of world trade, at least in the short term, with services sectors such as tourism and international education severely affected by travel restrictions. However, COVID-19 accelerated growth in digital service exports, expanding by 16 per cent in 2021.

The **direction of trade flows** has changed in recent decades, reflecting the changing importance of different economic regions. Between 1995 and 2023, high-income economies (concentrated in North America and Western Europe) saw their overall share of global trade fall from 85 per cent of exports to 70 per cent, as shown in figure 1.3. Over the same period, the fast-growing economies of East Asia and the Pacific region (which includes China, Indonesia and Vietnam) experienced the most rapid increase in trade, with their share of global trade surging from 6 per cent to 16 per cent.



Source: World Bank 2024
Note: Figures do not always add up to 100% because of rounding. High-income economies are grouped together. Regional figures are for low- and middle-income economies.

Figure 1.3 – Share of world's exports by region, 1995 and 2023

SAMPLE PAGES

Trends in the direction of trade can also have an impact on individual economies. For example, recent decades have witnessed strong growth in the Chinese economy, resulting in stronger trade relationships and inter-linkages in global supply chains. Countries such as Australia have prepared for stronger economic relations with China by encouraging students to learn Mandarin at school. At the same time, concerns about Australia being too reliant on exports to China, particularly given China's recent economic slowdown, are a factor in Australia's growing emphasis on expanding trade with India and other growing economies in the region.

reviewquestions

1. Explain TWO reasons for the increase in trade in goods and services in the global economy.
2. Describe trends in the composition and direction of trade flows in the global economy.
3. Discuss the impacts of changes in global trade flows on economies.

Financial flows

International finance now plays a leading role in the global economy. Because finance is crucial to so many aspects of how modern economies work, the globalisation of finance has had a major impact in terms of linking economies around the world. Finance is the most globalised sector of the world economy because money moves between countries more quickly than goods and services or people.

International financial flows expanded substantially following financial deregulation around the world, which in most countries occurred in the 1970s and 1980s. Controls on foreign currency markets, flows of foreign capital, banking interest rates and overseas investments in share markets were lifted. Technological change also played an important role. New technologies and global communications networks linked financial markets throughout the world, allowing events in major international markets such as New York, Tokyo, London and Hong Kong to produce immediate results.

While there is no single measure of international financial flows, all have shown a dramatic increase during the globalisation era. Figure 1.4 shows the growth of exchange-traded derivatives, which are a major instrument in global financial markets. The volume of financial flows fluctuates in response to global conditions. Sharp falls in financial flows have been followed by strong recoveries in 2008 (with the global financial crisis), 2013 (with the Eurozone crisis) and 2020 (with the COVID-19 pandemic).

SAMPLE PAGES

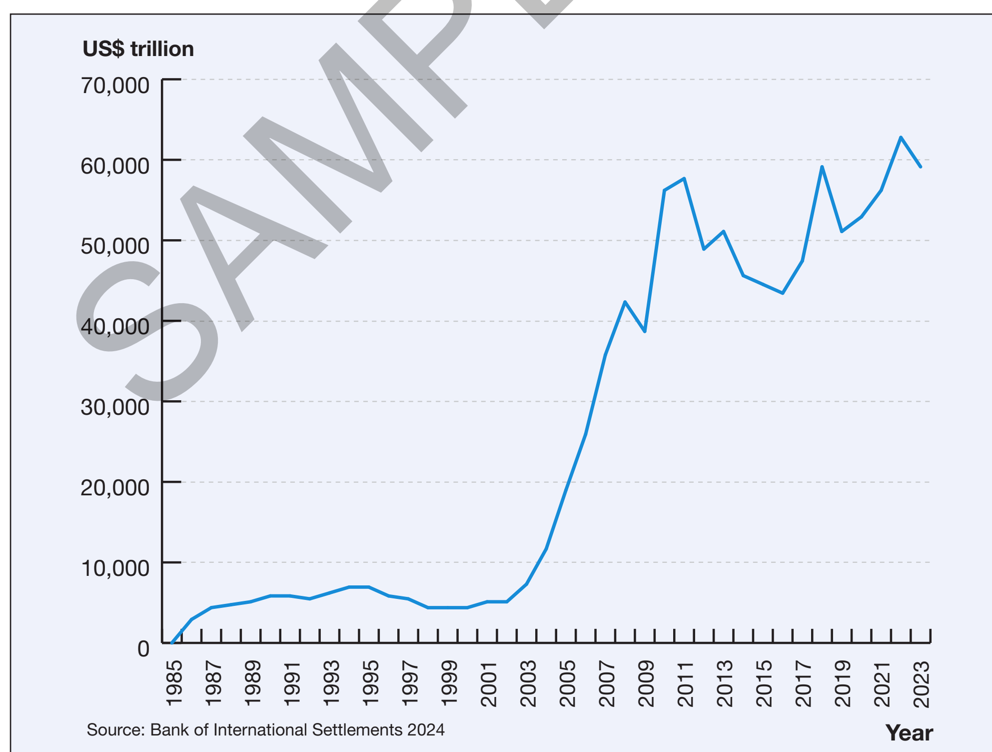


Figure 1.4 – The growth of global financial flows: exchange-traded derivatives

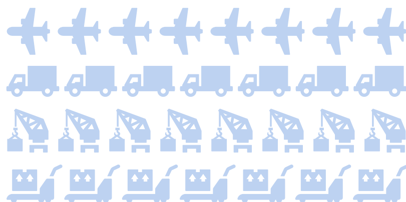
An important feature of international finance is **foreign exchange markets** (or forex markets), which are networks of buyers and sellers exchanging one currency for another in order to facilitate flows of finance between countries. Foreign exchange markets have experienced extraordinary growth in recent years, with annual turnover reaching US$58 trillion in 2011, 10 times its level of just 20 years earlier. Levels were lower in the 2010s and only reached new highs after the COVID-19 pandemic. The value of a currency is expressed in terms of another currency and is known as the **exchange rate** between two currencies. As will be discussed in chapter 5, most countries determine the value of their currency through the interaction of the forces of supply and demand in foreign exchange markets.

Speculators are investors who buy or sell financial assets with the aim of making profits from short-term price movements. They are often criticised for creating excessive volatility in financial markets.

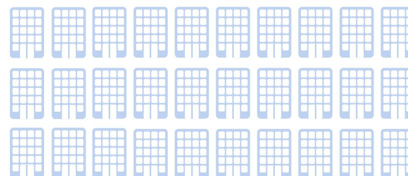
The main drivers of global financial flows are **speculators and currency traders** who shift billions of dollars in and out of financial markets worldwide to undertake short-term investments in financial assets. Based on data from the Bank for International Settlements' (BIS) Triennial Survey of foreign exchange transactions, only a small share is for "real" economic purposes such as trade and investment. The vast majority is for speculative purposes – to derive short-term profits from currency and asset price movements – or for technical purposes, such as hedging against future exchange rate movements and swapping funds between currencies. International investment banks and hedge funds, often based in the United States, are generally responsible for most of these transactions. The aim of these transactions is either to gain from short-term movements in asset prices – namely currency and share price fluctuations – and to generate profits, or to hedge against future movements and minimise the risk of losses.

SAMPLE PAGES

GLOBAL INVESTMENT
US$1.33 TRILLION
FOREIGN DIRECT INVESTMENT



GLOBAL COMPANIES
104 THOUSAND
TRANSNATIONAL CORPORATIONS



GLOBAL COMMUNICATIONS
5.4 BILLION
INTERNET USERS

GLOBAL LABOUR
169 MILLION
MIGRANT WORKERS

SOURCES: World Bank 2024, Bank for International Settlements 2024, International Telecommunications Union 2024, United Nations Conference on Trade and Development 2024, International Organization for Migration 2024. Note: Excludes migrants who have taken citizenship in their new country.

The main benefit of greater global financial flows is that they enable countries to obtain funds that are used to finance their domestic investment. In particular, investors in countries with low national savings levels would not otherwise be able to obtain the necessary finance to undertake large-scale business and investment projects if their economies were closed off to global financial flows. In this regard, global financial flows may enable a country to

achieve higher levels of investment (and therefore economic growth) than would otherwise have been possible if finance from overseas were not available.

However, changes in global financial flows can also have significant negative economic impacts. Speculative behaviour can create significant volatility in foreign exchange markets and domestic financial markets. This is because speculators are often accused of acting with a herd mentality, meaning that once an upward or downward trend in asset prices is established it tends to continue. Speculative activity has been blamed for large currency falls and financial crises in several countries over the past decade, including Britain in 2016, Türkiye in 2021 and repeatedly in Argentina. As discussed further in chapter 2, the **International Monetary Fund (IMF)** is responsible for the overall stability of the global financial system. One of its roles is to stabilise individual economies experiencing currency crises or financial turmoil, in order to prevent flow-on effects to other economies.

International Monetary Fund (IMF) is an international agency that consists of 190 members and oversees the stability of the global financial system. The major functions of the IMF are to ensure stability of exchange rates, exchange rate adjustment and convertibility.

reviewquestions

1. Account for the trends in international financial flows during the globalisation era.
2. Examine the role of speculators and currency traders in global financial markets.
3. Discuss the impact of global financial flows on economies.

Investment and transnational corporations

Another indicator of globalisation is the rapid growth of investment between countries over the past two decades. Since the 1980s, the global economy has witnessed rapid growth in movements of capital. While there are similarities in the growth of global finance and global investment, the two concepts can be distinguished by describing the shorter-term, speculative shifts of money as *finance*, and the longer-term flows of money to buy or establish businesses as *investments*.

One measure of the globalisation of investment is the expansion of **foreign direct investment (FDI)**, which involves the movements of funds that are directly invested in economic activity or in the purchase of companies. Reforms in developed and developing countries led to a surge in FDI flows from the 1980s onwards. Figure 1.5 demonstrates the dramatic increase in FDI flows over the past three decades. FDI flows are strongly influenced by the level of economic activity. The global recession in the late 2000s reduced FDI flows sharply, but they gradually recovered and the 2010s decade saw sustained high levels of FDI. The COVID-19 pandemic caused another sharp downturn in FDI flows in 2020, with UNCTAD recording a fall to under US$1 trillion for the first time in almost two decades, but this was a brief downturn, with FDI flows recovering quickly the following year. Uncertain economic conditions and greater geopolitical uncertainty have been factors reducing the growth of global FDI in recent years.

Foreign direct investment (FDI) refers to the movement of funds between economies for the purpose of establishing a new company or buying a substantial proportion of shares in an existing company (10 per cent or more). FDI is generally considered to be a long-term investment and the investor normally intends to play a role in the management of the business.

FDI flows have traditionally favoured developed nations. With greater industrial capacity and larger consumer markets, economies in Europe, North America and Japan were the natural destination for foreign investment during the globalisation decades of the 1990s and most of the 2000s. But this dominance has changed, with the share of FDI destined for developing and other economies significantly exceeding the developed world's share since 2020. The majority of FDI inflows to developing countries flow to economies in Asia. Of the US$867 billion inflows to developing countries in 2023, US$513 billion went to economies in East and South-East Asia (including US$163 billion to China, and US$28 billion to India). The increase in FDI inflows to developing countries since 2020 reflected stronger returns on FDI, relative to the returns on investment in developed countries.

SAMPLE PAGES

Developing economies have also become a major source of investment funds in the global economy. In 2023 these economies contibuted 30 per cent of global FDI funds, compared to around 12 per cent in the mid-2000s.

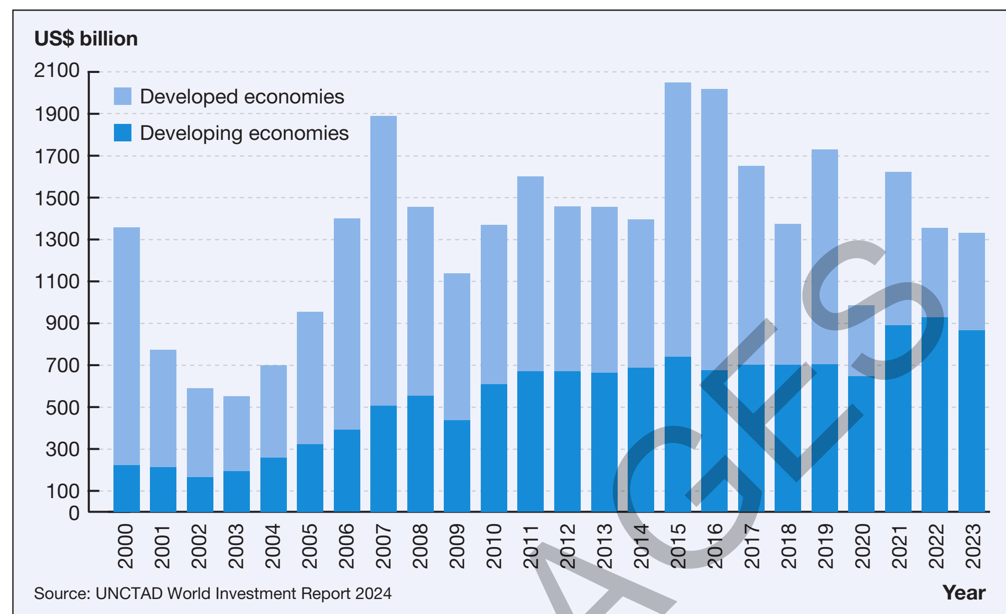


Figure 1.5 – Total world FDI inflows

Transnational corporations (TNCs) play a vital role in global investment flows and account for roughly 80 per cent of global trade, according to the World Bank. The largest 100 TNCs employ over 20 million people and own nearly US$21 trillion in assets – half of which are held outside the host country. Often, they will have production facilities in countries around the world, sourcing inputs from some countries, doing most of the manufacturing in another country, and doing other packaging and marketing tasks in another country.

As TNCs such as Apple, Amazon and Tesla establish or expand production facilities in a country, they bring foreign investment, new technologies, skills and knowledge. Because of the capital and job opportunities they bring, governments often encourage TNCs to set up in their country through supportive policies like subsidies or tax concessions. Since the early 1990s, the number of TNCs has grown from 37,000 to 104,000, and the number of affiliates to TNCs has grown from 170,000 to over 1,116,000. Foreign affiliates of TNCs employ around 80 million people globally.

TNCs in digital industries have experienced particularly rapid growth due to increased adoption of digital solutions during the pandemic. Twenty of the top 100 TNCs were technology and telecommunications businesses, according to UNCTAD's World Investment Report 2024. As TNCs continue to increase in both volume and significance, there has been an associated increase in cross-border cartels between large corporations, which reduces competition in economies and disadvantages local consumers. Global fines for cartels across major economies totalled US$1.4 billion in 2023 according to the Global Cartel Enforcement Report. However, many cartel arrangements are never uncovered by regulators, and fines are unlikely to fully capture the true cost of harm caused by cartels. Further, 26 countries imposed a global minimum tax on TNCs in 2023, leading to major restructuring and reduced FDI.

A significant cause of the growth of international investment is the increased level of international mergers and takeovers. During recent decades, there has been a spate of mergers between some of the world's largest corporations – most recently between technology companies Salesforce and Slack, pharmaceutical companies AstraZeneca and Alexion Pharmaceuticals, and media companies Walt Disney Company and 21st Century

SAMPLE PAGES

Fox. These mergers have seen the formation of companies worth hundreds of billions of dollars and reduced the number of truly global companies in different product markets. The peak year for cross-border mergers and acquisitions (M&As) was 2007, when US$1 trillion of mergers took place, as shown in figure 1.6. International M&As typically move in line with changes in global economic conditions – investment falls when economic growth is lower. In 2023, M&As fell 46 per cent to US$378 billion because of weaker economic conditions and low investor confidence.

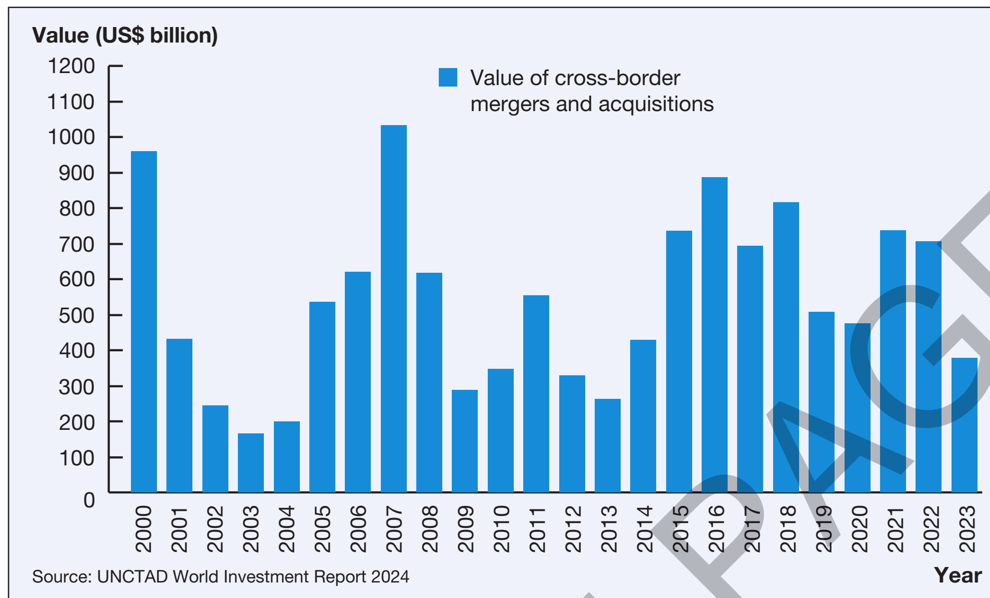


Figure 1.6 – Cross-border mergers and acquisitions

In overall terms, most investment in economies around the world still comes from domestic sources. FDI typically accounts for less than 20 per cent of total investment, meaning that over 80 per cent of investment still comes from within national economies.

reviewquestions

1. Distinguish between global financial flows and global investment flows.
2. Outline trends in the growth and direction of FDI flows.
3. Explain the role that TNCs play in global investment flows.

Technology, transport and communication

Technology plays a central role in globalisation. In part, this is because technological developments facilitate the integration of economies. Consider the following examples:

- Developments in freight technology, such as the use of micro warehouses nearer customers to improve "last mile" logistics and increased use of blockchain technology to simplify tracking and facilitate greater trade in goods. The WTO has estimated that the digitisation of trade has the potential to cut trade costs by 6 per cent.
- Cheaper and more reliable international communication through high-speed broadband allows for the provision of commercial services to customers around the world. A 2023 OECD study estimated that digital connectivity is having a three times larger impact on reducing trade costs today than in 1995. The proportion of the global population using the internet increased from 7 per cent in 2000 to 67 per cent in 2023.

SAMPLE PAGES

- In finance and investment, technology plays a key role in facilitating globalisation through secure, high-speed networks that allow money to move around the world in a fraction of a second. UNCTAD's World Investment Report 2024 found that countries are increasingly using dedicated online portals to encourage foreign investment, by providing information to investors, or by streamlining the business registration process.
- Smartphones and mobile internet access are fundamentally changing the structure of many industries, from retail and transport sectors to education, leisure and professional services. Technology is causing disruptive change to the structures of many of these industries as huge populations embrace online technologies. The number of mobile phone subscriptions is now over 8 billion, which is roughly equal to the number of people in the world.
- Advances in transportation, such as longer nonstop flights and high-speed rail networks, allow greater labour mobility between economies and increased accessibility to tourism and travel for consumers.

SOCIAL MEDIA AND GLOBALISATION

Social media platforms have accelerated globalisation at many levels. By creating new online communities, social media platforms such as Facebook, Instagram, TikTok, YouTube and X (formerly Twitter) connect individuals on an unprecedented scale. Of all internet users, over 90 per cent are active on social media. Facebook, for example, claims around 3 billion members.

As well as accelerating the globalisation of cultures, social media platforms have major economic impacts. Social media is central to marketing consumer products and services. Firms may use professional networks such as LinkedIn to source the best talent from global labour markets. Google Chief Economist Hal Varian has even suggested that word-search data for terms like *unemployment benefits* and *holidays* could be used to predict trends in consumer confidence and economic conditions.

Social media platforms are also worth vast sums. Elon Musk bought Twitter for US$44 billion in 2022. Google earned over US$300 billion in 2023, mostly from advertising revenue. Apple Inc. became the world's first trillion-dollar company by selling the phones, tablets and laptops through which people access social media. Social media platforms can rise and fall quickly (TikTok, for example, launched globally in 2017 and had over 4 billion downloads by 2024), but they are reshaping the economics of many sectors beyond media and telecommunications.

Technology is one of the strongest drivers of globalisation because it allows integration at a depth unthinkable in previous decades and centuries. OECD research in 2023 found that a 1 per cent increase in bilateral digital connectivity increases both domestic trade (2.1 per cent) and international trade (1.5 per cent). Economies that adapt to new technologies rapidly also tend to be the economies that are most closely integrated with other economies in their region or around the world. The COVID-19 pandemic also highlighted the disparity in access to technologies between countries, a phenomenon known as the "digital divide". Countries where digital technology use was high (such as Israel, the Netherlands and Australia) were better able to cope with the physical lockdowns necessary to prevent the spread of the virus by continuing normal activities through digital marketplaces, virtual meetings and online learning.

Another way that technology influences globalisation is as a driver of growth in trade and investment. For the leading technology innovators and exporters, technology represents a major trade opportunity. The United States earns substantial export revenues from its global leadership in many areas of new technologies. This reflects the geographical distribution of the top 100 digital TNCs' headquarters, with 59 per cent in the United States. Other countries rely on importing technology from a small group of developed economies with the hope that, over time, as they adopt new technologies, they can become innovators and develop their own technology exports as countries such as India, South Korea and Israel have done in recent years. Trade, therefore, spreads new technologies. Because innovation is an ongoing process, the leading country can often retain its technological superiority for a long period of time.

Business corporations that play a leading role in developing new technologies will often move directly into overseas markets in order to sell their products and services direct to local buyers. For example, leading information and communications technology corporations such as Google, Salesforce and Broadcom all have extensive global operations. These corporations bring extensive know-how into a new market and will often invest substantially in the new countries that they enter, particularly in education and training. In this way technology drives increased foreign investment. This is particularly apparent for

SAMPLE PAGES

digital TNCs, which have less reliance on physical assets. The 20 largest technology and telecommunications TNCs launched almost 3500 greenfield projects around the world in the decade to 2023, according to UNCTAD's World Investment Report 2024.

The internet provides a communications backbone that links businesses, individuals and nations in the global economy. This not only allows greater communication within and between firms but also reduces business costs that have in the past been a barrier to integration between economies. The World Information Technology and Services Alliance (WITSA) has estimated that the global marketplace for information and communications technology is worth almost US$5 trillion. The surge in worldwide internet usage to over five billion users highlights the rapid spread of technologies across countries in recent years and the increasingly interconnected nature of the global economy. COVID-19 accelerated this trend, with international internet traffic roughly doubling in 2020. At the same time, as online information flows have become more globalised, regulations have been required to mitigate cybersecurity attacks, which by 2027 are expected to cost the global economy a staggering US$24 trillion a year. Figure 1.7 shows the number of internet users in selected countries.

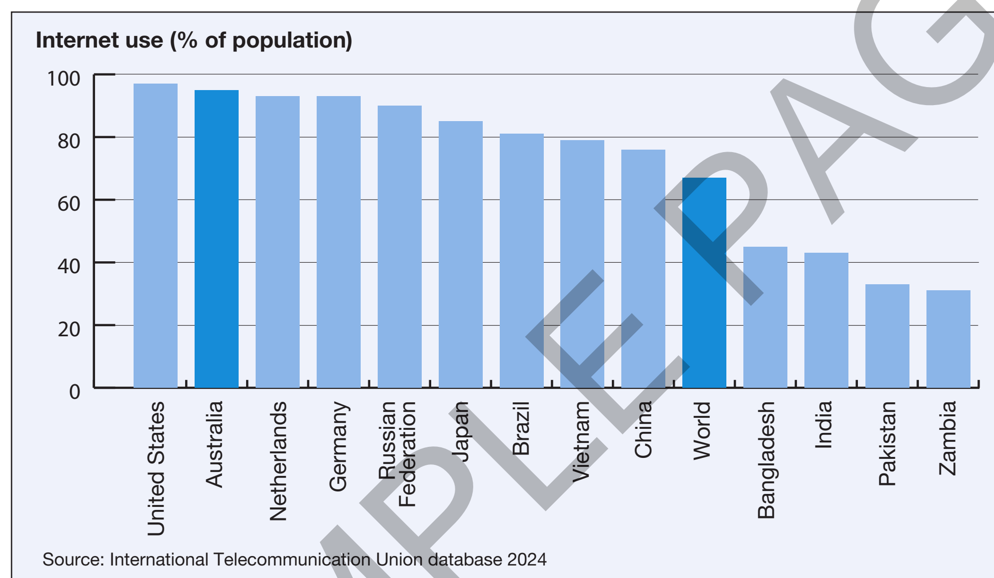


Figure 1.7 – Internet users in selected countries

International division of labour and migration

Labour markets differ from markets for goods and services, finance and investment, in that they are far less internationalised. While money can move around the world in fractions of a second, goods and services can move in days and investments can be made in weeks, people do not move jobs quite as freely. In fact, in recent years, the industrialised world has become more restrictive about immigration of people from poorer countries.

Nevertheless, more people than ever before are moving to different countries to take advantage of the better work opportunities that other countries offer. The UN estimates that there are 281 million international migrants, or around 3.6 per cent of the global population. The International Labour Organisation (ILO) estimates that around 169 million people (around 2 per cent of the world's population) are migrant workers. Labour migration into Organisation for Economic Co-operation and Development (OECD) member countries fell because of reduced job opportunities following the global financial crisis, gradually recovering during the 2010s.

The number of migrants has continued to grow despite the impacts of COVID-19, reflecting both "push" factors (such as people leaving their country because of conflict and violence) and "pull" factors (the demand for workers in many countries). The net

SAMPLE PAGES

migration statistics in figure 1.8 show that with rare exceptions, the number of people on the move across the world remains low relative to country population sizes. In 2024, 6.5 million Ukrainians were displaced because of war.

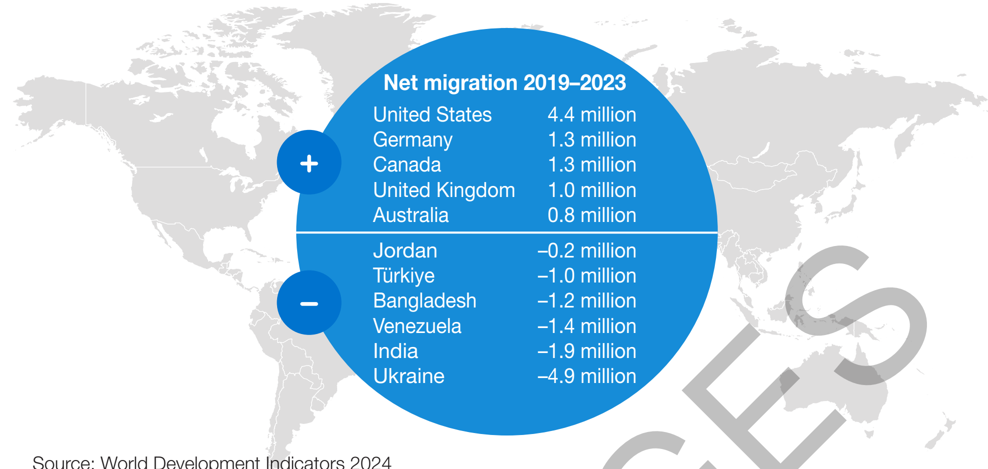


Figure 1.8 – Net migration by region and country (over past five years)

The movement of labour between economies appears to be concentrated at the top and bottom ends of the labour market. At the top end, highly skilled workers are attracted to larger, higher-income economies, with Europe and the United States experiencing the greatest inflow of migrant workers because of the higher pay and better job opportunities available in these countries. The ILO estimates that two-thirds of international migrant workers have moved to high-income economies. Smaller advanced economies, such as Australia and New Zealand, suffer from a "brain drain" of some of their most talented and skilled workers, who are attracted to other countries by greater rewards. In effect, there is a global market for the most highly skilled labour. This is reflected in the fact that the services sector has been the highest employer of migrant workers.

At the bottom end of the labour market, low-skilled labour is also in demand in advanced economies where it may be difficult to attract sufficient people born locally to do certain types of work. Jobs that only require basic skills (and perhaps do not require advanced language skills) are often filled by migrants. In the United States migrants are predominantly from Latin America; in European countries migrants are mainly from Eastern Europe and Africa; in richer Asian countries migrants are mainly from lower-income economies in the region. Low-skilled labour migrants often remit their earnings from countries with higher wages back to their families at home. Economies received remittances from overseas of US$790 billion in 2022, with India, Mexico and the Philippines the main destinations.

International division of labour is how the tasks in the production process are allocated to different people in different countries around the world.

These trends in migration reflect an **international division of labour** whereby people move to the jobs where their skills are needed while the globalisation of the labour market is increasing but there are still significant barriers to working in other countries. These barriers include immigration restrictions, language, cultural factors and incompatible educational and professional qualifications. Most people would prefer to stay in the country of their birth, where their family and friends live, and where they are most familiar with the language and culture. Against this preference, domestic instability and geopolitical turmoil may force people to flee their countries, with the UNHCR estimating that 110 million people were forcibly displaced by mid-2023. Nine-in-10 of these people come from low- and middle-income countries. The impact of conflict on overall migration is reflected in the top migration corridors as of 2024, including Syria–Türkiye and Ukraine–Russia in the top three.

The international division of labour is also evident from another aspect of the world economy – the shift of businesses between economies, rather than the shift of people. Just

SAMPLE PAGES

BRAIN DRAIN OR BRAIN GAIN?

Around 169 million people worldwide have migrated because of work. The proportion of these "economic migrants" who are highly skilled heavily outnumbers those who are low-skilled in almost all countries. In some countries, like Haiti and Jamaica, more than 80 per cent of the skilled labour force has moved overseas. Not even high-income countries are immune to the brain-drain problem, with Hong Kong and Ireland losing between one-third to one-half of their college graduates.

Brain drains have traditionally been perceived as a negative outcome for an economy in terms of both development and welfare. High levels of skilled labour emigration increase the technological gap between developed and developing countries as human capital flows towards more advanced economies and the source country may experience shortages of skilled workers. For example, health systems in developing countries can suffer when qualified doctors and nurses move to high-income economies where they are in demand.

On the other hand, economies experiencing outwards migration can benefit from remittance inflows, interconnected business networks and increased sharing of technological developments. The World Health Organisation (**WHO**) and the EU recently launched a project focused on the migration of health workers: From Brain Drain to Brain Gain. The program aims to manage and improve the flow of health workers from developing economies in Sub-Saharan Africa and Asia to maintain health standards and ensure that source countries retain some ability to deal with potential medical crises.

Sources: IZA World of Labor, WHO Health Workforce Alliance and the Health Workforce Department

SAMPLE PAGES

as people may move countries in search of the best job opportunities, corporations shift production between economies in search of the most efficient and cost-effective labour. In a globalised business environment, many producers operate what is called a global supply chain (or global value chain), with production facilities in several countries. The process called "offshoring" allows companies to shift production between countries to reduce costs. In 2022, research by the IMF found evidence that global supply chains had operated successfully during the COVID-19 pandemic, with less-affected countries able to supply goods when other countries were harder hit. Nevertheless, in many countries governments have taken steps since the COVID-19 pandemic to reduce their reliance on global supply chains and promote "onshoring" of essential industries. Recent years have also seen services functions such as IT support, data management and accounting move to more competitive locations to reduce costs, partly because of the rise of remote working. A 2023 survey by the Federal Reserve Bank of Atlanta showed 7.3 per cent of US executives were offshoring more jobs due to remote work.

The international division of labour reflects the economic concept of "comparative advantage" that is discussed in chapter 2. This theory states that economies should specialise in the production of the goods or services that they can produce at the lowest opportunity cost. Developing economies have a large population of workers with only basic labour skills and education levels, giving them a comparative advantage in labour-intensive manufacturing. Advanced economies have generally shifted away from labour-intensive manufacturing to focus on specialised service aspects of the economy that use more highly skilled workers who are in greater supply in advanced economies.

reviewquestions

1. Explain the role of innovations in technology, communications and transport in driving the process of globalisation.
2. Outline key trends in migration in recent years.
3. Explain how migration and offshoring reflect an international division of labour between different economies.

1.3 The international and regional business cycles

Business cycle refers to fluctuations in the level of economic growth due to either domestic or international factors.

Gross Domestic Product (GDP) is the total market value of all final goods and services produced in an economy over a period of time.

International business cycle refers to fluctuations in the level of economic activity in the global economy over time.

The level of economic activity in individual economies is never constant (that is, never in a state of equilibrium). Economic growth usually moves in cycles – in other words, instead of sustaining a steady rate of growth from year to year, most economies go through periods of above-average growth that then lead into periods of below-average growth. These ups and downs of the **business cycle** (that is, the general level of economic activity) are caused by changes in the level of aggregate supply and demand. This is shown in figure 1.9, which also shows that economies usually experience an overall trend of growth in output (measured by increases in **Gross Domestic Product**).

Just as individual economies experience stronger and weaker periods of economic growth, so too does the global economy. This ebb and flow of world economic growth is known as the **international business cycle**, which refers to the changes in the level of economic activity in the global economy over time. Although the levels of economic growth each year often differ greatly between countries, for most countries economic growth is stronger when the rest of the world is growing strongly, and weaker when other countries are experiencing a downturn. The extent of synchronisation of economic growth levels across individual economies is highlighted by the global recession resulting from the COVID-19 pandemic. Even countries where the pandemic was less severe still suffered immense economic damage, in part because of the flow-on effects of the recession in other countries.

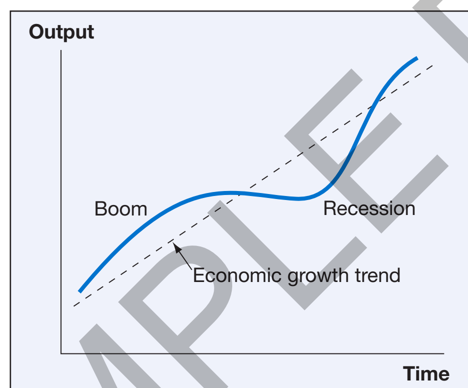


Figure 1.9 – The business cycle

Figure 1.10 highlights the strong relationship between the economic growth performances of the world's major economies. The United States, the Euro area economies, Japan and Australia all experienced a long period of moderate growth during the 2000s, followed by a sharp collapse in growth after 2008. Each of these advanced economies experienced slower rates of growth during the 2010s before the severe impact of the COVID-19 recession in 2020, followed by recovery.

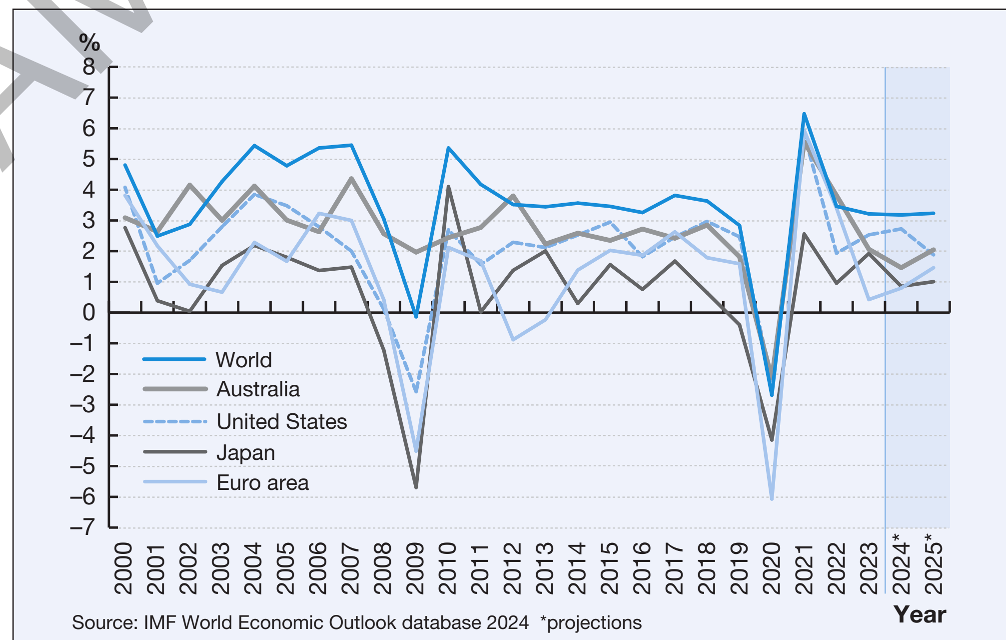


Figure 1.10 – Economic growth performance of major economies

SAMPLE PAGES

The world economy rebounded strongly from the pandemic in 2021 with 6.4 per cent growth in output, before growth rates stabilised at around pre-pandemic levels from 2022 at around 3 per cent. Emerging and developing economies outperformed the advanced economies in 2023, with 4.3 per cent and 1.6 per cent growth in GDP, respectively.

As a small open economy, the Australian economy is particularly affected by economic growth rates overseas. Research by the Reserve Bank of Australia (RBA) has found that 63 per cent of changes in the level of output in Australia can be explained by the changes in interest rates, growth levels and inflation rates in the Group of Seven (G7) largest industrialised countries. This means that for Australia, domestic factors have half as much influence as international factors on economic growth in any given year.

The transmission of economic conditions from one country to another is made more immediate by the increased integration of economies during the globalisation era:

- **Trade flows**: If there is a boom or recession in one country, this will affect its demand for goods and services from other nations. The level of growth in an economy will have significant flow-on effects on the economic activity of its trading partners.
- **Investment flows**: Economic conditions in one country will affect whether businesses in that country will invest in new operations in other countries, affecting their economic growth. For example, Brazil's weak economic performance in the past decade has meant that it has invested less in other economies. On four occasions since 2015, its annual FDI outflows have been negative.
- **Transnational corporations**: TNCs are an increasingly important means by which global upturns and downturns are spread throughout the global economy. For example, following reductions in the headcounts of major US technology companies Microsoft, Amazon, Google and Meta, in 2023 Australian technology company Atlassian also reduced its total staff by around 5 per cent.
- **Financial flows**: Short-term financial flows also play an important role in transmitting the international business cycle. A 2019 Reserve Bank Bulletin identified that Australia has benefited from being open to global capital markets, but that the financial integration of advanced economies exposes the Australian economy to shifts in their financial conditions.
- **Financial market and confidence**: Consumer confidence and the "animal spirits" of investors are constantly influenced by conditions in other countries. This is highlighted by the strong correlation between movements in share prices of the world's major stock exchanges – that is, they tend to go up and down at the same time. Events that threaten global stability – such as an increased risk of war, sovereign debt default or the collapse of a major business – can spark an immediate downturn in share values. This effect was seen in 2023 when the collapse of Silicon Valley Bank in the US and Credit Suisse in Switzerland sparked fears of another banking sector crisis, and prompted debate about regulation adequacy.
- **Global interest-rate levels**: Monetary policy conditions in individual economies are strongly influenced by interest-rate changes in other countries. If higher economic growth makes it necessary for the central bank to increase interest rates in the United States, this places pressure on central banks in other economies to follow suit. Inflationary pressures across the world in 2022 saw central banks raising interest rates. The Reserve Bank of Australia followed suit, with interest rate rises in 2022 and 2023.
- **Commodity prices**: The prices of key commodities such as energy, minerals and agricultural products are set by global markets. Their prices, in turn, influence the levels of inflation, investment, employment, growth and other features of the international business cycle. Historically, changes in oil prices have had major impacts on international growth (with lower prices boosting growth overall).

SAMPLE PAGES

In 2022, global sanctions against Russia, the world's second-largest supplier of oil, resulted in the largest global energy price increases in half a century, following contractions to worldwide supply. As a result, the World Bank estimated global trade would reduce by 1 per cent, causing global growth to be revised downwards by 0.7 per cent.

- **International organisations**: International forums such as the Group of Twenty (G20) or Group of Seven (G7) economies can play an important role in influencing global economic activity. Discussions of global economic conditions at summit meetings mean that the G20 or G7 can act as the unofficial forum for coordinating global macroeconomic policy, especially during periods of economic uncertainty. These meetings can also resolve tensions between countries that threaten the economic outlook.

FACTORS THAT *STRENGTHEN* THE INTERNATIONAL BUSINESS CYCLE

- Trade flows
- Investment flows and investor sentiment
- Transnational corporations
- Financial flows
- Technology
- Global interest rates
- Commodity prices
- International organisations

FACTORS THAT *WEAKEN* THE INTERNATIONAL BUSINESS CYCLE

- Domestic interest rates
- Government fiscal policies
- Other domestic economic policies
- Exchange rates
- Structural factors
- Regional factors

Nevertheless, it is important to note that despite these linkages between economies, the pattern and the pace of economic growth differ between countries. Even countries that are at similar stages of economic development, such as the United States and European economies, experience differing levels of economic growth. Despite the global linkages previously described, many of the factors that influence the business cycle reflect distinctive national conditions:

- **Interest rates** have a significant impact on the level of economic activity, and interest rates differ between countries (or regions, in the case of European countries that share a common interest-rate policy). Higher interest rates will dampen economic activity while lower interest rates will stimulate economic activity.
- A government's economic policy decisions can influence their economic growth rate. For example, the UK's decision to leave the EU in 2016 reduced the rate of economic growth as investor confidence in Britain's economy fell. **Fiscal policies** also have a significant effect on the level of economic growth in the short to medium term. If a government in one country raises taxes while the government in another country cuts its taxes, economic growth is likely to move in opposite directions in those two countries.
- **Exchange rates** differ between countries and impact the level of trade competitiveness and confidence within economies. In turn, these factors will influence the level of economic growth. The BIS has noted that exchange rates are having an increased impact on domestic economies, particularly in the past decade as government policy has less ability to target economic shocks.
- **Structural factors** differ between economies. For example, countries have different levels of resilience in their financial systems; different levels of innovation and takeup of new technologies; different attitudes towards consumption and savings; different population growth rates and age distribution; different methods of regulating labour markets, educating and training employees and regulating businesses. These structural factors influence the competitiveness of economies and their level of growth.
- **Regional factors** between economies differ. Some economies are closely integrated with their neighbours and are therefore very influenced by the economic performance of their major trading partners. Research by Colombian academics found that regional business cycles in emerging markets experience different levels of synchronisation depending on factors such as the productive structure and trade integration of the country. For example, whilst Mexico has a high level of synchronisation with North America, economic conditions from nearby Latin American countries have a lower impact on Mexico's activity due to less trade integration.

In summary, there is an international business cycle and when there is a substantial economic downturn, such as in the mid-1970s, the early 1990s, the late 2000s and

SAMPLE PAGES

early 2020s, this downturn is shared across almost all countries. However, the factors influencing individual economies differ and the level of world economic growth is one of several factors that influence economic conditions.

Regional business cycles

Similar to the international business cycle, the term **regional business cycle** refers to the changes in economic activity in a particular region. In the same way that countries' activity can be affected by global changes, they can also be affected by regional changes. While changes in the US economy will have ripple effects around the world, they can have more pronounced impacts on the nearby economies of Canada and Mexico, which are most closely integrated with the US economy. Likewise, many of the 27 economies of the **EU** are influenced by activity levels in Europe's largest economies, Germany and France.

Regional business cycles are the fluctuations in the level of economic activity in a geographical region of the global economy over time.

In the **East Asian region**, economic conditions are dominated by the influences of China and Japan – the world's second- and third-largest economies. While the regional business cycle in Asia has been weaker than in other regions, it has strengthened in recent years because of increased integration between Asian economies. On the other hand, as growth rates in China and Japan slowed down in recent years, the region continued to experience stable growth due to moderate upswings elsewhere in the region.

Other regions around the world have a higher proportion of developing or low-income countries, and they tend to be less regionally integrated. In **Sub-Saharan Africa**, for example, many economies such as Chad, Uganda and Sierra Leone are dependent on high-income economies for more than 80 per cent of their exports, and are therefore as likely to be influenced by conditions in the world economy as they are by neighbouring African economies. In the **South Asia and Latin American regions**, regionally dominant economies such as India and Brazil respectively play a key role alongside influences from outside the immediate region.

While regional business cycles tend to be dominated by the largest and most globalised economies, it is also important to recognise the complexity of conditions at the regional level. In the early 2010s, economic conditions in European economies were weakened by financial turmoil in the relatively small economy of Greece. A financial crisis in Argentina and the severe impact of COVID-19 in Brazil weakened economies in **Latin America** in 2020. The war in Ukraine in 2022 reduced growth, trade and economic policy across **Europe and Central Asia**. In 2024, the UN Development Program estimated that the Israel-Gaza war had cost neighbouring economies Egypt, Lebanon and Jordan US$10 billion GDP because of refugee flows and the decline in trade and tourism. In this way, smaller economies can affect the performance of regional economies indirectly, even if they are not dominant economies.

Clearly, regional business cycles can be quite different from patterns in global economic activity, with some regions performing more strongly than others and fluctuating more independently from other regions. However, regional cycles are also part of the phenomenon of globalisation because they result from increased cross-border integration. These business cycles of different regions interact in complex ways to influence the level of economic activity around the world.

SAMPLE PAGES

reviewquestions

1. Define the terms *international business cycle* and *regional business cycle*.
2. Using the example of a specific economy, discuss the extent to which this economy's performance has reflected economic growth trends globally and in its region.
3. Outline the factors that strengthen and weaken the relationship between the economic cycles of individual economies.

chapter summary

1. **Globalisation** refers to the integration between different countries and economies, leading to the increased impact of international influences on all aspects of life and economic activity.

2. The **global economy** is a way of describing the activities of all the economies of the world as a whole, reflecting the fact that they are now increasingly linked together into one larger economic system.

3. The **Gross World Product** is the sum of the total output of goods and services produced by all economies in the world over a given period of time.

4. The growth of **world trade** is an important indicator of the extent of globalisation. During the period of rapid globalisation in the decades to 2010, trade grew at a much faster rate than world economic growth. In the 2010s, trade grew at close to the same level as overall economic growth.

5. The pattern and direction of world trade has changed to reflect the increasing importance of advanced technology and services and the growth of the Asia Pacific region.

6. The process of globalisation has occurred most rapidly in global finance which faces few barriers and is driven mostly by speculative activity (that is, investors seeking to make short-term profits out of fluctuations in exchange rates, interest rates and other financial indicators).

7. **Foreign direct investment (FDI)** is the injection of funds into an economy to establish a new business or purchase an existing business. FDI flows are driven by **transnational corporations (TNCs)** and often involve the transfer of technological innovations between economies.

8. **Technology, transport and communication** have driven increased economic integration by facilitating linkages between businesses individuals and nations in the global economy.

9. Globalisation has also contributed to the **international division of labour** in part because of the migration of workers to countries where jobs are plentiful or better paid, and also because of the shift of business between economies in search of the most efficient and cost-effective labour.

10. The concept of **international and regional business cycles** refers to the extent to which economies tend to experience a similar pattern of boom, downturn and recovery at similar times. Although the shape and the length of the business cycle differs from one economy to the next, the level of economic growth between different economies is closely related, and recessions and booms tend to occur around similar times.

SAMPLE PAGES

chapter review

1. Explain what is meant by *globalisation*, using recent trends to illustrate your answer.
2. "Just as the COVID-19 pandemic spread fast because of the contagious nature of the coronavirus, the COVID-19 recession spread fast because of the connected nature of the global economy." Discuss what this statement is saying about the global economy in the 2020s.
3. Describe the role of trade flows in globalisation.
4. Summarise recent changes in the direction and composition of international trade in goods and services.
5. Explain how technology drives growth in the trade of goods and services.
6. Explain the difference between *investment flows* and *financial flows*.
7. Outline the role of foreign-exchange markets in international financial flows.
8. Discuss the role played by transnational corporations (TNCs) in globalisation.
9. Discuss the impact of globalisation on the international division of labour.
10. Explain how changes in the level of economic growth in one economy can impact on economic growth in other economies.

SAMPLE PAGES