

3

Will Terrorism Defeat Globalization?

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Globalization is the process of creating a common economic space. It is the result of a growing integration of hitherto relatively closed economies through the increasingly free movements of goods, capital, and labor. It is not a new process. It has usually been associated with the creation and maintenance of empires. The latter have been created in part to provide "order" in the economic space, by suppressing various threats to the productive and orderly ways of life of civilizations from various roving bandits, who today are called terrorists. An elaboration of these points will allow us to answer the question posed in the title of this paper.

One of the features of a closed economy is that goods and services do not enter international trade—they are non-traded. Their prices are set by domestic demand and supply. The efficiency gains which accrue from differences in the domestic and international prices of traded goods in an open economy cannot be obtained. These gains can be decomposed into the consumer gain, which allows consumers to obtain their consumption bundles at a lower cost, and the production gain, which arises from the specialization in domestic production on the basis of comparative advantage, allowing countries to use the more productive "technology" provided by international trade to raise their output from given resource endowments.

Goods can be non-traded because natural barriers raise transport costs, or because tariffs prohibit trade. In the millennial past when costs of communication and transport were very high, only high-valued non-bulky goods entered into long-distance trade. This trade was always threatened by pirates and bandits of every kind. They imposed a further cost in addition to natural barriers to trade. If the costs of piracy were high enough, trade would not have taken place. As happened when the Great Powers' attempts to control the bandits failed.

4. See William H. McNeill, *The Human Condition* (Princeton, NJ: Princeton University Press, 1980).

5. The distinction between the material and cosmological beliefs of a culture is outlined and discussed in D. Lal, *Unintended Consequences* (Cambridge, MA: MIT Press, 1998). The former are concerned with ways of making a living, the latter with, in Plato's words, "how one should live."

6. This implied a rise in per capita income based on the Smithian gains from trade. But it was bounded because the ancient agrarian economies depended upon a fixed factor of production—land. The Industrial Revolution converted these agrarian economies into mineral energy economies which were no longer bounded by land but could use the near unlimited stock of fossil fuels for energy. This unleashed modern economic growth which allows a sustainable and continuous rise in per capita income. These two forms of *intensive* (with rising per capita incomes) are to be distinguished from *extensive* growth (where output grows *pari passu* with population, leaving per capita income unchanged), which has been ubiquitous through human history. See D. Lal, *Unintended Consequences*.

7. Douglass North, "Sources of Productivity Change in Ocean Shipping, 1600–1850," *Journal of Political Economy*, no. 5 (1968).

8. The fatuity of this principle was noted by Dean Acheson in a speech at Amherst College on Dec. 9, 1964. He said this high-sounding moral principle of self-determination "has a doubtful moral history. He [Woodrow Wilson] used it against our enemies in the First World War to dismember the Austro-Hungarian and Ottoman Empires, with results which hardly inspire enthusiasm today. After the Second World War the doctrine was invoked against our friends in the dissolution of their colonial connections. . . . On the one occasion when the right of self-determination—then called secession—was invoked against our own government by the Confederate States of America, it was rejected with a good deal of bloodshed and moral fervor. Perhaps you will agree it was rightly rejected" (Acheson, "Ethics in International Relations Today," in D. L. Larson, ed., *The Puritan Ethic in U.S. Foreign Policy* [Princeton, NJ: Van Nostrand, 1966], 134–35).

9. The illegal drug trade was estimated to be about \$400 billion in 1997, compared with a value of legal world exports of \$5 trillion that is about 8 percent of the value of legal world trade. The profits from the trade are enormous. Thus, a kilogram of cocaine base sells for between \$650 and \$1000 in Bolivia or Peru. It can be processed into cocaine hydrochloride for export for between \$900 and \$1200, which sells for between \$13,000 and \$40,000 wholesale in the U.S. before reaching consumers at a retail price of between \$17,000 and \$172,000. Heroin from Burma begins its progress at \$70 per kg to the Burmese producer, to \$3000 after processing in Thailand, whence it is exported from Bangkok at \$6000–\$10,000. It sells wholesale in the U.S. for between \$90,000 and \$200,000, and at retail for nearly \$1 million (A. Krueger and C. Aturupane, "International Trade in 'Bads'," in H. Giersch, ed., *Merits and Limits of Markets* [Berlin: Springer, 1998]). The direct budgetary costs of enforcing the prohibition of drugs in the U.S. have been estimated to be over \$20 billion per annum. Yet the war shows no sign of succeeding. There is a strong case for legalization, while Krueger and Aturupane rightly contend that following the theory of trade and welfare, the correct policy is not to prevent production by the most efficient worldwide producer, but only to seek to tax or prohibit domestic consumption.

10. P. Navarro and A. Spencer, "September 11, 2001: Assessing the Costs of Terrorism," *The Milken Institute Review*.

11. See A. Krueger, "New York's Economic Resilience," *New York Times* (September 16, 2004).

12. See Deepak Lal, *In Praise of Empires* (New York: Palgrave, 2004).

13. See M. Doyle, *Empires* (Ithaca, NY: Cornell University Press, 1986).