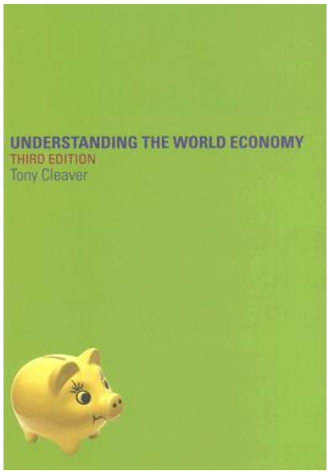

Title: Understanding The World Economy (Third Edition)

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The major theme of this book may be described as that of economic injustice, i.e., unequal distribution of global incomes. One basic assumption which permeates Tony Cleaver's analysis is that normative economic problems exist in both command and market economies and solving these problems – getting the mix right between how far markets should be left to themselves and how far central authorities should intervene – is the business of political economy of each and every country.

The end of the twentieth century has seen a marked shift in the world away from extensive government intervention toward decentralized markets as a means of solving problems of economic organization. This change has been most revolutionary in the case of the former Soviet Union and Eastern Europe, but it has also occurred on mainland China and has been a feature of deregulating and privatising governments all round the globe from South America to East Asia. There are very few countries which have not felt the impact of this shift in economic philosophy.

Cleaver is convinced, however, that there is no one mixed economy solution that is ideal for all communities, nor for one country for all time. The blend of government, corporate or consumer sovereignty; state or self-interest; planning and prices; public or private ownership; monopoly or competition must be kept continually under review by governments and individuals so as to maximise efficiency gains and guard against abuses.

What do market economies need to grow healthily? In Cleaver's opinion they require the following: an infrastructure of secure property rights, enforced without favor; an environment where risks are calculable and not dependent on government diktat. Growth requires innovation; innovation requires resources to move freely to efficient employments; rates of return will signal efficient investment opportunities only where competition rules – that is, where medium and large businesses can compete. Lastly, in a global marketplace, countries will attract limitless funds from abroad providing international as well as domestic investors are free from predation.

This book, however, suggests that the success or failure of the transition process is not dependent on foreign influence. Instead, it lies within the grasp of the peoples of Eastern Europe, the former Soviet empire and China – and particularly it rests in the hands of their political leaders. In particular, the author thinks that the future of Russia is crucial. If its deep-rooted structural problems are successfully addressed it will drag itself up and bring most of the continent with it. If it does not, its future will be bleak and its instability will continue to threaten its neighboring countries.

Cleaver suggests that unemployment is the creation of modern, Western society. Its causes are manifold: there are both macro- and microeconomic factors at work. For sufficient new jobs to be created sophisticated, integrated economies must continually evolve. Because there are social and private costs and benefits involved, governments, employers and employees all need to be involved in sharing the responsibility for new training and employment programs.

Considering free trade and regional agreements, the author argues that the principle of comparative advantage provides for substantial benefits in trade, but market economies must be flexible enough to respond to the changing dynamics of international commerce. In less developed countries in particular, where the geographical spread of the modern market sector may be limited and entrepreneurial resources may be scarce, governments need to work with business to design the appropriate policies in order to establish the institutions, the infrastructure, the preconditions necessary to secure economic development for all.

Freeing up trade between partner countries brings increasing economic benefits and such results may fuel arguments for even closer integration. This is indeed the case of the European Union. In the most mature economies of Europe the gains from trade have so overcome the historical rivalry between these countries that further economic integration has been pursued along the spectrum from free trade areas through customs unions to a common market.

Experience from other parts of the world suggests that one reaction of those left outside a common market is to set up rival trading blocs. For instance, a desire to emulate the EU's success and a fear of losing out in competition have fuelled the growth of other regional associations such as NAFTA, the Association of South East Asian Nations and others. The great danger here, however, is that world trade may become dominated by a few, large, rival groups, and – in an atmosphere of mutual distrust – common external tariffs may be easier to erect than to negotiate a general reduction in protection. If this occurs, then world trade may become greatly distorted over time. The author thinks that the potential for much trade diversion exists, rather than trade creation, but this is an outcome which would benefit no one and is a matter of concern that ought to be in the minds of all governments attempting to set up trade deals.

Referring to the European Union, Cleaver states that the community as a whole is not an optimum currency area. The striking economic diversity of European nations implies that, for some members of the Euro, the costs of joining the union are much greater than for others. In 1999, 12 countries of Europe took the plunge to link their currencies together but three that did not have since grown faster. It may be that the strains of monetary and economic integration have inhibited the advance of the brave 12 and in the future they will grow all the faster as they reap the rewards of this sacrifice but, in the author's opinion, to date there is no persuasive evidence to support this view.

Tony Cleaver is Euro-sceptic. According to him, the existing Euro members thought it imperative to swap monetary independence for a single unit of exchange in the new millennium but, whatever the historical, political and social arguments involved, there are economic costs – expressed in terms of recession and slower growth for those countries that have had greater difficulty in squeezing their economies into the 'one-size-fits-all' shape.

From the economics of the Euro, Cleaver takes his analysis to the economics of oil, one of the very important 21st century products. Oil production in the new millennium is affected by political instability in the Middle East and internal political instability in Russia. For decades, spare capacity in Saudi Arabia has enabled this country to act as the central bank of oil – opening or closing the taps to match supplies to changing world demand – but the stereotypical condition of oversupply had led to underinvestment such that in 2005, most producers were pumping furiously in order to keep up with surging oil demand. Prices are likely to stay high until more capacity eventually comes onstream and then there may be another price slump.

In the Russian Federation and neighboring states such as Azerbaijan, Kazakhstan and others, there are large known reserves that are waiting to be got out, but the political risk is high, much capital needs to be replaced and upgraded, and the distances to Western markets are great. Although there is much production potential, the author thinks that the unpredictable arm of government dictates how this potential is to be exploited, deters the application of Western technology and contributes to the uncertainty regarding the future.

Despite the volatility of the world economic environment, national governments are not completely powerless. Cleaver argues that wise domestic policies and sound internal investment are still the best bet for development. The Asian dragons, for instance, do not provide unqualified support for neoclassical economics. Indeed, the direction of strong government has been much in evidence there.

This book shows that economic development is not something that can be left to laissez-faire. Sensitive management of a growing economy is necessary – firstly, in parenting infant industries; secondly, in providing effective public infrastructure; and, thirdly, in policing fair and competitive goods and financial markets. Resources are allocated between various employments and between a country's present and future needs according to the prices which rule. It is on this issue ultimately that a successful and flexible market economy is built.

Tony Cleaver advocates economics that is environmentally friendly. In his view the possibility of doing irreversible environmental damage indicates the need for extreme caution. The premium for external costs that needs to be appended to many market prices may well be high.

The biggest practical problem this raises is finding the political will to implement these costs in the market prices we must all pay. If this is difficult enough in one country, the problem is far greater where environmental costs are spread across many nations – as in the case of global climate change, for example. Voluntary international cooperation is necessary here with the signing of a treaty on limiting greenhouse gas emissions. But even if vastly different countries' evaluations of the situation could be brought into agreement there is always the temptation for an individual nation to free-ride. Tony Cleaver advocates the need for a political way forward to confront the economics of the environment. One thing is certain: if we do not pay the full price of plundering our natural inheritance today, future generations will.