›riented high-tech sector
es to Portugal.
l? The question can't be
ıe phenomenon. People
ʒ world inequalities, usu-
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up a country, or regions
tence economy. An area
›n world markets is very
al change.
s do other forms of eco-
purely economic means,
› the world market-place
ɜ economic globalisation,
misplaced tactic for rich
ɜcessary strategy at some
.e, Malaysia was correct to
ital from the country. But
lp the development of the
varring trade blocs.
. the beginning have con-
›n-state. Are nation-states,
are they becoming largely
›tates are indeed still pow-
the world. Yet at the same
: eyes. National economic
ıportantly, nations have to
›olitics are becoming obso-
say that, following the dis-
ıave enemies. Who are the
in Kosovo didn't pit nation
.erritorial nationalism and a

ı enemies, a massive shift in
ı comments could be made.
ɜar the same as they used to
ıt inside have become quite
mily, work, tradition, nature,
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s happening not only in the
They are what I call "shell
›me inadequate to the tasks

ɾ gather weight, they are cre-
global cosmopolitan society.

We are the first generation to live in this society, whose contours we can as yet only dimly see. It is shaking up our existing ways of life, no matter where we happen to be. This is not—at least at the moment—a global order driven by collective human will. Instead, it is emerging in an anarchic, haphazard fashion, carried along by a mixture of influences.

It is not settled or secure, but fraught with anxieties, as well as scarred by deep divisions. Many of us feel in the grip of forces over which we have no power. Can we reimpose our will upon them? I believe we can. The powerlessness we experience is not a sign of personal failings, but reflects the incapacities of our institutions. We need to reconstruct those we have, or create new ones. For globalisation is not incidental to our lives today. It is a shift in our very life circumstances. It is the way we now live.

2

Opening Scene

The World Is Ten Years Old

THOMAS L. FRIEDMAN

It's aggravating—we have nothing to do with Russia or Asia. We're just a little domestic business trying to grow, but we're being prevented because of the way those governments run their countries.

—DOUGLAS HANSON
CEO OF ROCKY MOUNTAIN INTERNET, INC.,
SPEAKING TO *THE WALL STREET JOURNAL* AFTER THE 1998 MARKET MELTDOWN FORCED HIM TO POSTPONE A $175 MILLION JUNK BOND ISSUE

On the morning of December 8, 1997, the government of Thailand announced that it was closing 56 of the country's 58 top finance houses. Almost overnight, these private banks had been bankrupted by the crash of the Thai currency, the baht. The finance houses had borrowed heavily in U.S. dollars and lent those dollars out to Thai businesses for the building of hotels, office blocks, luxury apartments and factories. The

Thai government was
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As Russia's economy continued to slide in early 1998, the Russians had to raise the interest rate on their ruble bonds from 20 to 50 to 70 percent to keep attracting the foreigners. The hedge funds and foreign banks kept buying them, figuring that even if the Russian government couldn't pay them back, the IMF would step in, bail out Russia and the foreigners would get their money back. Some hedge funds and foreign banks not only continued to put their own money into Russia, but they went out and borrowed even more money, at 5 percent, and then bought Russian T-bills with it that paid 20 or 30 percent. As Grandma would say, "Such a deal!" But as Grandma would also say, "If it sounds too good to be true, it usually is!"

And it was. The Asian-triggered slump in oil prices made it harder and harder for the Russian government to pay the interest and principal on its T-bills. And with the IMF under pressure to make loans to rescue Thailand, Korea and Indonesia, it resisted any proposals for putting more cash into Russia—unless the Russians first fulfilled their promises to reform their economy, starting with getting their biggest businesses and banks to pay some taxes. On August 17, 1998, the Russian economic house of cards came tumbling down, dealing the markets a double whammy: Russia both devalued and unilaterally defaulted on its government bonds, without giving any warning to its creditors or arranging any workout agreement. The hedge funds, banks and investment banks that were invested in Russia began piling up massive losses, and those that had borrowed money to magnify their bets in the Kremlin casino were threatened with bankruptcy.

On the face of it, the collapse of the Russian economy should not have had much impact on the global system. Russia's economy was smaller than that of the Netherlands. But the system was now more global than ever, and just as crude oil prices were the transmission mechanism from Southeast Asia to Russia, the hedge funds—the huge unregulated pools of private capital that scour the globe for the best investments—were the transmission mechanism from Russia to all the other emerging markets in the world, particularly Brazil. The hedge funds and other trading firms, having racked up huge losses in Russia, some of which were magnified 50 times by using borrowed money, suddenly had to raise cash to pay back their bankers. They had to sell anything that was liquid. So they started selling assets in financially sound countries to compensate for their losses in bad ones. Brazil, for instance, which had been doing a lot of the right things in the eyes of the global markets and the IMF, suddenly saw all its stocks and bonds being sold by panicky investors. Brazil had to raise its interest rates as high as 40 percent to try to hold capital inside the country. Variations on this scenario were played out throughout the world's emerging markets, as investors fled for safety. They cashed in their Brazilian, Korean, Egyptian, Israeli and Mexican bonds and stocks, and put the money either under their mattresses or into the safest U.S. bonds they could find. So the declines in Brazil and the other emerging markets became the transmission mechanism that triggered a herdlike stampede into U.S. Treasury bonds. This, in turn, sharply drove up the value of U.S. T-bonds, drove down the interest that the U.S. government had to offer on them to attract investors and

finance houses all thought they were safe because the Thai government was committed to keeping the Thai baht at a fixed rate against the dollar. But when the government failed to do so, in the wake of massive global speculation against the baht—triggered by a dawning awareness that the Thai economy was not as strong as previously believed—the Thai currency plummeted by 30 percent. This meant that businesses that had borrowed dollars had to come up with roughly one-third more Thai baht to pay back each $1 of loans. Many businesses couldn't pay the finance houses back, many finance houses couldn't repay their foreign lenders and the whole system went into gridlock, putting 20,000 white-collar employees out of work. The next day, I happened to be driving to an appointment in Bangkok down Asoke Street, Thailand's equivalent of Wall Street, where most of the bankrupt finance houses were located. As we slowly passed each one of these fallen firms, my cabdriver pointed them out, pronouncing at each one: "Dead! . . . dead! . . . dead! . . . dead! . . . dead!"

I did not know it at the time—no one did—but these Thai investment houses were the first dominoes in what would prove to be the first global financial crisis of the new era of globalization—the era that followed the Cold War. The Thai crisis triggered a general flight of capital out of virtually all the Southeast Asian emerging markets, driving down the value of currencies in South Korea, Malaysia and Indonesia. Both global and local investors started scrutinizing these economies more closely, found them wanting, and either moved their cash out to safer havens or demanded higher interest rates to compensate for the higher risk. It wasn't long before one of the most popular sweatshirts around Bangkok was emblazoned with the words "Former Rich."

Within a few months, the Southeast Asian recession began to have an effect on commodity prices around the world. Asia had been an important engine for worldwide economic growth—an engine that consumed huge amounts of raw materials. When that engine started to sputter, the prices of gold, copper, aluminum and, most important, crude oil all started to fall. This fall in worldwide commodity prices turned out to be the mechanism for transmitting the Southeast Asian crisis to Russia. Russia at the time was minding its own business, trying, with the help of the IMF, to climb out of its own self-made economic morass onto a stable growth track. The problem with Russia, though, was that too many of its factories couldn't make anything of value. In fact, much of what they made was considered "negative value added." That is, a tractor made by a Russian factory was so bad it was actually worth more as scrap metal, or just raw iron ore, than it was as a finished, Russian-made tractor. On top of it all, those Russian factories that were making products that could be sold abroad were paying few, if any, taxes to the government, so the Kremlin was chronically short of cash.

Without much of an economy to rely on for revenues, the Russian government had become heavily dependent on taxes from crude oil and other commodity exports to fund its operating budget. It had also become dependent on foreign borrowers, whose money Russia lured by offering ridiculous rates of interest on various Russian government-issued bonds.