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## Cataracts of globalization and the economic diplomacy of small states

**Abstract:** This paper strives to briefly delineate the development of economic diplomacy vis-a-vis globalization and tendencies in the world politics and economy. It outlines the impact of globalization on economic diplomacy and defines fundamental trends of international development that could shape its overall functioning. Then, it determines the political and economic phenomena that affect and shape the economic diplomacy of smaller countries, influence its orientation and pose new challenges. The example of Denmark is considered as an effective and successful model on which Slovak economic diplomacy could be based. The authors attempt to outline appropriate pillars of economic diplomacy of smaller countries, while underlining the importance of systematic and timely information analysis.

**Keywords:** Economic Diplomacy; Globalization; Small Economy; New Challenges; Protectionism; Denmark; Slovakia

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### Проблеми глобалізації та економічна дипломатія малих держав

**Анотація.** Автори статті окреслюють розвиток економічної дипломатії та глобалізації, а також тенденції в світовій політиці й економіці. У роботі викладається вплив глобалізації на економічну дипломатію, визначаються основні тенденції міжнародного розвитку, які могли б формувати її функціонування. В роботі визначені політичні й економічні явища, які визначають форми економічної дипломатії малих країн, впливають на їх орієнтацію та висувають нові завдання. Приклад Данії вважається ефективною і успішною моделлю, на основі якої можна було б формувати Словацьку економічну дипломатію. У статті зроблено спробу систематизувати підходи до економічної дипломатії в малих країнах з урахуванням датського досвіду, підкресливши при цьому важливість регулярного та своєчасного аналізу інформації.

**Ключові слова:** економічна дипломатія; глобалізація; мала економіка; протекціонізм; Данія; Словаччина.

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### Проблемы глобализации и экономическая дипломатия малых государств

**Аннотация.** Авторы статьи обозначают развитие экономической дипломатии и глобализации, а также тенденции в мировой политике и экономике. В работе излагается влияние глобализации на экономическую дипломатию, определяются основные тенденции международного развития, которые могли бы формировать ее функционирование. В работе определены политические и экономические явления, которые определяют формы экономической дипломатии малых стран, влияют на их ориентацию и выдвигают новые задачи. Пример Дании считается эффективной и успешной моделью, на основе которой можно было бы формировать Словацкую экономическую дипломатию. В статье предпринята попытка систематизировать подходы к экономической дипломатии в малых странах с учетом датского опыта, подчеркнув при этом важность регулярного и своевременного анализа информации.

**Ключевые слова:** экономическая дипломатия; глобализация; малая экономика; протекционизм; Дания; Словакия.

### 1. Introduction

The roots of economic and trade diplomacy can be traced back to ancient times (Manning & Morris, 2005) [1]. Even then trade exceeded the confines of state institutions and continents. Trade and geographical discoveries prompted a need to create permanent representations, focused, inter alia, on information gathering, also in the area of the economy. «*The evolution of economic diplomacy ... is a result ... of the economic dimension of international relations*» (Toth & Horvathova, 2006) [2, 18].

Modern economic diplomacy started to form more saliently between the 19th and 20th centuries. The first wave of globalization was then at its peak and led to extensive changes (Toth & Horvathova, 2006) [2, 20-21]. However, the political and security agenda was of primary importance. That changed after

the Second World War when the role of international cooperation increased significantly. At the end of the 1970s, extensive economization of politics led by M. Thatcher and R. Reagan took place, inter alia, as a consequence of the inclusion of the Soviet economy in the global system (Gaidar, 2007) [3, 110]. Deregulation, liberalization and privatization became the three pillars of the neoliberal economy, and economic diplomacy began to acquire its current shape.

Free trade has strengthened as a result of the Iron Curtain's collapse. Changes caused by the growth of international trade and apprehensions of losses in trade and wealth mobilized the states. The position of the economy changed to the extent that for the states «*a defeat in the area of international division of labour could have repercussions in social and political aspects*

*tantamount to a military defeat in the past ... notwithstanding, states felt threatened by the possible complete loss of sovereignty»* (Stouracova, 2012) [4, 62].

The battle for economic power and hegemony is led by research and development teams and marketing and supplying armies. The competition transcends to hyper-competition - the battle for markets, rents and profits. National governments are often incapable of systematically and realistically influencing the global economic events and developments (Adrian, 2013) [5, 59].

## 2. Brief Literature Review

Globalization prompts strong interconnections between economic and foreign policies. Together with the increasing «Europeanization» of competences in business policies, the research discourse of the meaning and model of economic diplomacy intensified in small countries in theory and practice. The topic is relevant, but hardly new; the issue of economic diplomacy in a globalized world is dealt with in numerous publications of Slovak and foreign authors.

On the Slovak side, the works of Lysak (2005) [6], Pajtinaka (2007) [7], Toth & Horvathova (2006) [2] deserve particular attention. The global context of economic diplomacy is researched by P. Stanek (2001; 2005) [8-9]. Czech works from the conference on *Economic diplomacy* in Prague in April 2013 provide a significant contribution to discussion together with the works of J. Stouracova (2012; 2013) [4; 10]. The topic also resonates in works by foreign authors. Relations between the world economy and small states were outlined by P. J. Katzenstein (2003) [11]. The basis for comparison was laid by M. Kostecki and O. Naray (2007) [12] in the model of value-creating activity of economic diplomacy.

However, several issues still remain open; in particular, what is the main goal of economic diplomacy in relation to economic growth and jobs, and towards innovation accelerating in the times of globalization, challenges of the Internet and social networks.

## 3. The purpose

The contribution stresses the importance of economic diplomacy for small states in the changing world of globalization and interdependence. The authors seek to identify an effective model of economic diplomacy functioning in a small country in a global environment. The analysis of ways and means of how to adapt to this environment by small countries is the focal point of the contribution. It explores the possibilities of applying the model of Danish economic diplomacy as a successful small Western European country to the conditions of the open European market.

After the financial crisis, new challenges and opportunities have emerged in the field of economic diplomacy with new actors entering the scene. Viewed from the perspective of effective public spending, especially for small economies, it is important to consider and utilize the experiences of comparable successful countries in the area of economic diplomacy.

## 4. Results

### 4.1 Globalization and its influence and role in economic diplomacy

In the current mutual economic inter-state dependence «*economic diplomacy is gaining in importance*» (Bayne & Woolcock, 2011) [13, 3-4]. Following the financial crises, the researchers even stipulate that «*diplomacy must be determined by economics*» (Robejsek, 2001) [14]. Thus, economic diplomacy constitutes a significant and often the most decisive part of the activities of foreign policy. Economic diplomacy makes approximately 60% of the work of Slovak diplomats abroad (Internal material of the Slovak MFA, 2010) [15].

A well-set up system of economic diplomacy can contribute to the increase of bilateral trade by 6-10% (Van Veenstra, Yakop & van Bergeijk, 2010) [16, 6]. The overall development, especially in smaller countries, is influenced by the globalized and integrating external environment. Quick adaptation to the dynamics of such changes is important to them.

It is possible to concur that «*globalization has its economic, political, social, sociological, and psychological dimensions. It is not just a phenomenon of Earth getting smaller [...]; but also the reflection of the combination of numerous explosive social, political and other risks*» (Stanek, 2005) [9, 9]. Globalization is «*considered to be the key factor in further development of the world economy*» (Stanek, 2001) [8, 15].

Globalization is increasingly characterized by discontinuity, emergence of powerful, unpredictable changes and by the exceptional pace at which new technologies spread around. «*Economic performance may invite policy-makers into mistaking strategy with economy, which lowers their susceptibility to the political, cultural, social and spiritual impacts of the enormous changes inflicted by the contemporary modern technologies*». One of the greatest risks of expanding global processes is the fact that «*economic and technological inventions overtake the options of contemporary politics*» (Kissinger, 2002) [17, 23-24].

Globalization affects practically all areas of the state, whose functions had developed in accordance with J. M. Keynes' liberalization until the 1970s (Johnson, Moggridge & Robinson, 1992) [18]. The main turnover was imposed by R&D and new industrial revolutions (Rifkin, 2011 [19]; Bloem, et al., 2014 [20]).

The paradigm of diminishing the role of the state in the economy has changed as a result of the 2008 global financial crisis. In the most liberal countries governments have begun interventions in the financial sector. The crisis strengthened the sovereignty of the state and curbed the autonomy of market and financial elites. Countries, which did not exercise control of their financial system, were exposed to the negative impacts of measures deployed by other states. This has also affected economic processes in the EU.

The changes invoke a need for new perception and role of economic diplomacy. New quality of economic diplomacy and configurations of its management are key parts of foreign policy.

### 4.2 The pillars of future international developments

The creation of a balance between the established and emerging powers constitutes a complex process. A fragmentation of the globalized world appears unavoidable (Neumann, 2008) [21, 70-89]. The EU is going through one of its most challenging times due to migrants, Brexit, Grexit, disparities within the European Monetary Union (EMU) and growth in number of EU members. Some EU member states are lagging behind in *high-tech* and reforms. The incompatibility is growing between the powerful 500-million-inhabitants-market and its weak political and military influence. Nevertheless, the EU is the world's largest trade block; it generates 25% of the global GDP and constitutes 27% of the world's trade in services, while contributing around 41% to the world's FDI [22].

The US will continue to be the main economic, political and military power (Lieber, 2012) [23]. China and India have become the engines of the world growth. They will, however, lag behind in the area of per capita income for several decades (Hu, Yan & Wei, 2014) [24]. The world's ten largest economies in 2024 should be as follows: the US, China, Japan, India, Germany, Brazil, the UK, France, Russia and Korea (Centre for Economics and Business Research, 2015) [25].

The Pricewaterhouse Coopers forecast estimates that the US would drop from the top position; Germany and the UK would remain the only two European countries in the top ten list (Tlapa, 2013) [26, 27]. The playground of the global economy would move into South-East Asia, Africa and Latin America.

The shift of the economic power from the West to the East (Looney, 2014) [27, 503] has been given by several factors. Beside the economic growth of the East (Global Outlook Summary, 2016) [28], the burning-out of the West and last but not least the growing co-operation of the emerging economies (BRICS) contribute to that tendency (Svihlikova, 2013) [29, 48].

China, Russia, the GCC countries and African states are not following the Western liberal model. Instead, they use state capitalism as a tool for managing their economies. The crisis consolidated the notion of larger state control and mistrust in unregulated markets. This means, inter alia, a growth of protectionism. Chinese foreign direct investments (FDI) are increasing in the developing world. The FDIs result in the creation of new alliances between industrializing and developing countries. The Chinese model might become an attractive option for authoritarians.

The conflict in Ukraine has put the world back into a modified Cold War. Russia is looking for its old/new position of domination. The West needs Russia to be part of the global integration and security and vice versa. Inter-regional tensions may divide the West; the EU and the US might have increasingly di-

vergent economic and monetary priorities. The agreement on transatlantic trade and investment partnership (TTIP) should be perceived in this context (Lipkova, 2013) [30, 34-47].

The international system appears to be more multipolar, heterogeneous and unstable. There are efforts by new, stronger actors to search for another balance. We might witness a disorderly world, with alternating leaderships in many regions. Thus, «*the world has switched to the multi-civilization, multi-polar system which is diverse and multidimensional by its nature*» (Soskin & Matviychuk-Soskina, 2014) [31, 4].

#### 4.3 Economic Diplomacy and its importance for smaller countries

The above mentioned development may increase the pressure to strengthen the performance and results of economic diplomacy, especially in countries with small or medium economic potential. «*The ability of small countries to adapt to economic change will determine their success and ability to remain competitive in the global market*» (Katzenstein, 2003) [12, 21].

The ability of smaller countries and their influence largely depends on their economic potential and performance. The financial crisis and demographics sharpen the competition in new markets. For smaller countries it is particularly important to have the ability to quickly analyse the impact of international events and define the strategic direction of their economies.

New trends should be reflected in smaller countries. They must be able to react pre-emptively. Digits of economic growth are ceasing to be their main ambition. Competitiveness, amplified by R&D, comes to the fore. This also poses challenges for economic diplomacy. Its core role is not only to create conditions for co-operation and growth, but also to support job creation. There are three key conditions for the effectiveness of economic diplomacy:

1) Effective cooperation of partner government institutions in the process of managing and implementing economic diplomacy;

2) Strong emphasis put on the well-functioning agency for promotion of exports and FDI inflow, as well as financial and insurance institutions;

3) Quality and professional network of representative offices abroad, which serve as service points for entrepreneurs (Stouracova, 2013) [11, 9-10].

This requires updating the model and its actors. The complex functioning of a government, its links and cooperation with the private sector should be adapted to the new external and domestic demands. The emphasis on education, knowledge-based economy and technological advances can boost the power and status of a small state more than territorial gains.

#### 4.4 Some features of the Danish model and possibilities for its application in Slovakia

Slovakia and Denmark are subjects for examining the adaptation of the small countries to the globalization. In both countries, joining the EU and NATO caused transfers of some political, security and other agendas from capitals to Brussels. The core diplomatic networks of both countries have started to focus on economic, export and investment, public and cultural diplomacy. The high openness of the economies and the low absorptive capacities of the domestic markets create a need to search for business opportunities abroad.

Significant differences between Slovakia and Denmark exist in the area of public spendings, the tax system, and labour market. The Danish economy is based on the Nordic model of welfare state. The Danish companies almost exclusively play the dominant role in exports.

The GDP of Denmark reached approximately \$264,269 million in 2015; the country enjoys a prestigious AAA rating (Gross domestic product, 2016) [32]. Its relatively small and open economy has a high standard of living and an extensive welfare state system. It maintains a long-term balance of payments surplus and is a net exporter of food and energy with a low net foreign debt. Denmark is not a member of the Eurozone, the Danish kroner (DKK) is tied to a fixed exchange rate to EURO in the extent of +/- 2.25% (Bohac, 2015) [33].

Based also on the SWOT analysis, Denmark's economic outlooks are positive for the long-term perspective. Denmark

managed to overcome various obstacles for economic diplomacy, eliminated errors and went through processes, which Slovakia is currently undergoing. Therefore, it can serve as a good model. Comparison the economic diplomacies of Slovakia and Denmark could serve as a basis for enhancement of the current Slovak model of economic diplomacy. The strongly integrated, effective and successful Danish model demonstrates some common denominators with the Slovak one. With respect to the geographical size and population, Denmark is a comparable country to Slovakia. Long-term work of the author in the field of economic diplomacy, including the devising in Slovakia and tenure as the Slovak Ambassador to Denmark offer appropriate predispositions and capacities for this procedure (Bohac, 2015) [34].

#### 4.5 The specifics of Slovak economic diplomacy

Slovakia, which is keen to accelerate its transition towards a knowledge-based economy, is very similar to Denmark in the 1970s-1980s.

Slovakia's trade balance in 2015 reached EUR 3.303 billion in goods and services. Total exports grew by 4.9% year-on-year to EUR 67.865 billion, while total imports increased by 7.6% to EUR 64.562 billion. The growth was supported by exports of cars and electronic goods. More than 50% of Slovak export was realised by international companies (TASR, 2015) [35]; (Spectator staff, 2016) [36]; corporations are supplemented by half a million of Slovak SMEs - the pillars of the Slovak economy. In 2014, the SMEs created 70.7% of jobs and contributed 61.2% to the creation of added value (Analysis, n.d.) [37]; (Situation, 2016) [38].

Slovakia is dependent on exports. EU-28 international trade in goods with the rest of the world (the sum of extra-EU exports and imports) was valued at EUR 3,517 billion in 2015. Both imports and exports increased in comparison with 2014, but this increase was larger for exports (EUR 88 billion), than for imports (EUR 35 billion). As a result, the EU-28's trade surplus increased from EUR 11 billion in 2014 to EUR 64 billion in 2015. (Eurostat, 2016) [39]. The focus on exports to the European Economic Area (EEA) deepens Slovak sensitivity to its economic fluctuation. Slovakia should, therefore, gradually overcome the orientation to the car industry and diversify its export potential into new, non-traditional and less saturated markets outside the EEA. Such trends can be observed not only in Denmark, but also in other comparable countries, e.g. the Czech Republic, Switzerland, Sweden, etc.

With regard to the above mentioned, and based on the achievements and experiences of the author, it is possible to put forward several key pillars of the orientation of economies of smaller states, such as Slovakia, and the related role of economic diplomacy as follows:

- economic growth and employment;
- knowledge-based society, investments growth, start-ups;
- green economy and new sources of energy;
- state branding;
- support of FDI;
- effective functioning of agencies for export support.

Modern economic diplomacy works upon the supposition that it is capable of identifying sectors in which its country can achieve leadership and excellence, in which it can gradually become global. This does not mean only «*the export promotion*», but also «*development promotion*» and, if possible, the search for «*win-win*» solutions (Dub, 2013) [40, 17-20].

#### 5. Conclusions

The economic diplomacy of small countries must be able to distinguish between irrelevant and pertinent information, which can affect the development, trends and investment opportunities. One of the key tasks is collection and selection of information leading to a gain of political or economic influence or advantages. Wealth itself is not a key instrument of power; it is strategic gathering and processing of information and its real-time transfer to relevant addressees.

The evaluation of successes and failures of diplomacy is moving towards the economic domains. It is especially valid in cases of middle-sized and small countries with open and export-oriented economies, susceptible to global changes and crises. The global economic slowdown has put pressure on the achieve-



ments, accountability and functioning of economic diplomacy and all its components.

It is, therefore, necessary to design the strategic orientation of economies to exceed the duration of one parliamentary term. Instruments of smaller economies must be configured in this way, including in the area of economic diplomacy. The emphasis of economic diplomacy should be put on the functionality, effectiveness, added value, growth impulses, investments and jobs.

The foreign policy battle is shifting towards the areas of the economy, science, research, innovation, IT, modern technologies etc. The whole system of economic diplomacy must be adapted to the core trajectories of global development. It must adapt its analytical-information capability, because the world has become an IT society and IT technologies facilitate real-time information sharing. Quality and real added value of information is also significant.

In the 21<sup>st</sup> century, an economy of Slovak parameters can be sustained only by long-term economic state policies with a clear vision. It should advance and support an environment enabling growth and productivity. It should also search for added value in appropriate models for Slovak companies and attract private capital prone to invest in the Slovak ability to innovate.

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Tab. 1: SWOT analysis of Danish economy in 2015

Strengths	Weaknesses
1. High political and economic stability; the world's 2 <sup>nd</sup> most peaceful country	1. High tax rates
2. Quality infrastructure and services	2. High prices
3. The highest level of flexibility of labour market in the world	3. Relatively small domestic market
4. Best business environment in Europe	4. Fluctuating number of highly-qualified labour
5. High effectiveness of institutions	5. Low degree of investments in new projects
6. Highly-qualified and motivated labour	6. Low degree of risk capital
7. Open, excellent and attractive research system with linkages between research, business and intellectual assets	7. Few large companies acting as engines for growth and innovation
8. Innovations among the world's greatest	8. Economic stagnation in the last few years
9. Key competences in the clusters of clean-tech, ICT, natural sciences, design, sustainable energy and seamanship	9. The majority of leading research is in very limited areas; not all possessing the capabilities to secure «critical mass»
10. One of the lowest corruption in the world	10. Low mobility between research and business environment
Opportunities	Threats
1. Highly-absorbent market for goods with high purchasing power parity	1. Large global competition
2. EU membership and complex international integration	2. Too many small companies with low level of disposable income
3. Flexible structure of industry with a large segment of SMEs	3. High prices
4. Clear priorities of economic policies	4. Low level of government investments
5. Willingness to adapt to changes in industry; demand after flexible solutions in SMEs	5. Global recession
6. Good infrastructure for R&D, innovations	6. Scientific and technological challenges
7. Strengthening of international cooperation; creation of partnerships with world's leading technological corporations; combination of creative domestic abilities with high technologies of foreign partners	7. Outsourcing of the production abroad with growing tendencies
8. Ability to attract highly-qualified labour	8. Lack of qualified labour
9. Public sector as the engine for the participation in tenders	9. Commercially successful foreign companies
10. Gate into Scandinavia	10. Competition in the eastern markets and the countries of Central and Eastern Europe

Source: (Bohac, 2015) [33]