Chapter 1
The Effect of Globalization on Economic Growth: Evidence From Emerging Economies

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ABSTRACT

Globalization has gathered great momentum over the past four decades and it has led to important changes in the economic, political, and cultural dynamics of countries. It is theoretically expected that globalization stimulates economic growth by leading institutional reforms, opening economies to global markets, direct and indirect foreign investments, and technology transfers. Therefore, it is crucial for emerging economies to increase economic growth. This study investigates the impact of globalization on economic growth for the panel of emerging economies by conducting second generation panel data techniques. For this purpose, employing annual data spanning from 1970 to 2014, the effects of overall KOF globalization index and three dimensions of globalization on economic growth are estimated via CUP-FM and CUP-BC estimators. Results show that overall the KOF globalization index, economic, and social dimensions of globalization have positive influence on economic growth while the effect of political dimension on economic growth is negative.

INTRODUCTION

As a known and comprehensive definition, globalization is a statement that can be simply defined as interaction and integration among people who lives anywhere in the world, and, who has different culture and ethnicity. So, it has crucial effects on all of life’s occasions with respect to economic, political and cultural aspects. In this regard, it refers to the growing interdependence and increasing integration among countries resulting from the increasing integration of trade, finance, consumption preferences, policies, life styles and ideas in one global marketplace (Soubbotina & Sheram, 2000).

The main contributing mechanism for globalization is economic motives that try to maximize welfare. Other types of globalization are byproducts of economic globalization. Hence, many international
institutions have been founded to increase economic cooperation in the wake of World War II, such as the World Bank (WB), International Monetary Fund (IMF), The Organization for Economic Co-operation and Development (OECD), European Union (EU), World Trade Organization (WTO), General Agreement on Tariffs and Trade (GATT). Much as these foundations have contributed to increase globalization, it has acquired huge dimension in parallel with increasing communication and transportation tools through technological advancement over past a few decades. Otherwise, “globalization could not have happened without extensive innovations in transport, communications, and data processing” (Ardalan, 2017).

Liberalization is a complimentary factor of this integration process as well. When considered from this point of view, it is evaluated as a process of becoming same of goods and capital market around the world in which legal limitations for foreign trade and investment are repealed (Gurgul & Lach, 2014). In this manner, economies become closer and more interrelated (Heshmati & Lee, 2010) and also interdependent. In this case, two accelerating factors of globalization are technological progress and liberalization (Soubbotina & Sheram, 2000).

Dreher (2006) deduces that economic growth is promoted through globalization by exemplifying with more globalized countries’ growth process. In his example, it is clear that globalized countries show a higher growth performance while growth performance is negligible in less globalized ones. According to Mishkin (2009), globalization stimulates economic growth by leading to institutional reforms in emerging economies and advanced ones contribute to this process by opening of their markets to goods and services from them. Institutional reforms have also been crucial to explain growth differences among countries and many seminal papers stress the importance of institutions in economic growth process (Acemoglu, Johnson, & Robinson, 2004, 2001; Easterly & Levine, 2001, 2003; Hall & Jones, 1999; Rodrik, Subramanian, & Trebbi, 2004).

Thus, numerous empirical studies focus on investigating the effect of globalization on the economic variables. However, most of the literature in this field suffer from insufficiency in terms of globalization measurement since they employ just a single variable and ignore policies such as restrictions, tariffs, quotas and so on. Additionally, as claimed by Rodriguez and Rodrik (2000), using only one specific data in order to capture the effects of globalization is not reliable. Also, the effects of globalization may be overestimated owing to the use of inappropriate indicators (Pekarskiene & Susniene, 2014). Additionally, most studies ignore cross-sectional dependence in panel data models. However, cross-sectional dependence problem, if exists, may lead biasedness, inconsistency or inefficiency in panel data estimations (Sarafidis & Wansbeek, 2010, 2012).

Contrary to prevailing literature, employing second generation panel data techniques that consider cross-sectional dependence, this study aims to investigate the impact of globalization on economic growth for the panel of emerging economies since globalization has vital importance, especially, for this kind of countries’ growth process (Gurgul & Lach, 2014). Another important point of this chapter is that it includes three dimensions of globalization into the panel data analyses to capture the effects of economic, social and political globalization. To the best of our knowledge, this is the first study analyzing emerging economies classified by Standard & Poor’s, as well as using second generation panel data estimators such as CUP-FM and CUP-BC. The remainder of the study is organized as follows: the next section explains background of globalization in economic growth process and reviews the literature. Then, data, model, and methodologies are introduced in section 3. Empirical applications and estimation results are presented in section 4. Finally, the study is concluded.
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