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EFFECTS OF GLOBALISATION ON DEVELOPING COUNTRIES: A CASE STUDY OF THE BALTIC STATES

Master's Thesis

IEVA BUMBURE

Supervisor: AHMET IZZET KARACAHISARLI

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Member Title, Name and SURNAME	----------------------------------

ABSTRACT

EFFECTS OF GLOBALISATION ON DEVELOPING COUNTRIES: A CASE STUDY OF THE BALTIC STATES

Ieva Bumbure

Master of Business Administration

Thesis Supervisor: Ahmet Izzet Karacahisarli

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This study examines positive and negative impacts of globalization on developing countries Estonia, Latvia and Lithuania, also known as the Baltic states, during the period of 1991-2012. In 1991, the Union of Soviet Socialist Republics formally ceased to exist. After regaining independence Baltic states begun process of shifting from a command economy to a market economy and implemented many difficult and complex market-oriented structural reforms. The effects of globalization in the Baltic states have been analysed from economic, political and social perspective, also considering recent history of these countries.

The empirical studies conclude that globalization has had both positive and negative impacts on Estonia, Latvia and Lithuania. The Baltic states have become more integrated in the world economy and globalization has contributed to the economic growth, however it has also imposed high social costs on Estonia, Latvia and Lithuania, which can have a negative effects in the future by creating a loss of human capital and pose serious economic and political challenges.

Keywords: Baltic States, Globalization, Economy, Financial Crisis, Social Exclusion

ÖZET

GELİŞEN ÜLKELER ÜZERİNDE KÜRESELLEŞMENİN ETKİLERİ: BALTİK ÜLKELERİ ÖRNEK ÇALIŞMASI

Ieva Bumbure

Master of Business Adiminstration

Tez Danışmanı: Ahmet Izzet Karacahisarli

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Bu çalışma 1991 – 2012 dönemi sırasında küreselleşmenin gelişmekte olan ve Baltik ülkeleri olarak da bilinen Estonya, Letonya, Litvanya üzerindeki negatif ve pozitif etkilerini incelemektedir. 1991 tarihinde Sovyet Sosyalist Cumhuriyetler Birliği resmen sona ermiş, bağımsızlığın tekrar kazanılmasından sonra Baltik ülkeleri kumanda ekonomisinden piyasa ekonomisine geçiş sürecini başlatmış ve birçok zor ve karmaşık piyasa odaklı yapısal reformlar uygulamaya konulmuştur. Baltık ülkelerindeki küreselleşme etkileri ekonomik, politik ve sosyal perspektifden incelenmiştir. Ayrıca bu ülkelerin geçmiş tarihleri göz önünde bulundurulmuştur.

Deneysel çalışmalar göstermiştir ki küreselleşmenin Estonya, Letonya ve Litvanya üzerinde hem pozitif hem de negatif etkileri olmuştur. Baltik ülkeleri dünya ekonomisi ile daha çok bütünleşmiş ve küreselleşme ekonomik büyümeye katkıda bulunmuştur. Ancak Aynı zamanda Estonya, Letonya ve Litvanya üzerinde yüksek sosyal maliyetler getirmiştir. Bundan dolayı negatif etki olarak gelecekte yetişmiş insan kaybı ciddi ekonomik ve siyasi sıkıntılar yaratabilir.

Anahtar Kelimeler: Baltik Ülkeleri, Küreselleşme, Ekonomi, Ekonomik Kriz, Sosyal Dışlanma

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ABBREVIATIONS

BOP	:	Balance of payments
CIA	:	Central Intelligence Agency
EU	:	European Union
FDI	:	Foreign direct investment
GDP	:	Gross domestic product
IMF	:	International Monetary Fund
MNE	:	Multinational enterprise
NATO	:	North Atlantic Treaty Organization
OECD	:	Organisation for Economic Co-operation and Development
USSR	:	Union of Soviet Socialist Republics
WB	:	World Bank
WTO	:	World Trade Organization

1. INTRODUCTION

1.1 BACKGROUND

This study is an attempt to understand positive and negative effects of global political, social and economic processes on developing countries Estonia, Latvia and Lithuania known also as the Baltic states, which are still trying to find their places in the highly interconnected and globalized world. The reason to choose these particular countries is that they are former Soviet Union countries which regained their independence only in 1991, but since then they have joined the European Union (EU), became new players of the global world and created relatively attractive conditions for foreign capital that ideally should positively influence the process of their integration with the global economy. Furthermore, it is essential to understand that the post Soviet economic and political transitions were not simply a matter of creating something new from scratch. These were about erasing outdated habits, perception, organization and governance styles that were harmful to the development of free market capitalism. However, adoption of capitalism paved the way for necessary improvements and provided people with much broader horizons and opportunities than they previously had. Baltic countries embraced free market capitalism since it was seen as a necessary liaison to the democratic government in achieving better standards of living. Historical preconditions and lack of rich natural resources have impacted the pace of their development and their ability to adjust to global challenges. Baltic states decided to take the road of opening their markets, liberating their economies and adopting democratic institutions to successfully function in the modern political system. However, the process was not as smooth as expected as the global crisis starting in 2007 hit very hard all three countries and harsh austerity measures had to be taken in order to cure the economies and return them to growth. The main goal of this thesis is to analyze how being under the social and economic conditions inherited from the Soviet legacy as well as from the geo-political reality, Estonia, Latvia and Lithuania have been affected by globalization and what positive and negative effects globalization has brought to these countries.

The analysis of this process is done through the lenses of globalization which will help to understand dynamics of development in the Baltic states. The purpose of this study is to extend the amount of knowledge and level of insight in the globalization process in Estonia, Latvia and Lithuania. The research will mainly focus on all three countries and compare and contrast the experience of each country. More specifically analysis will be done measuring three main dimensions of globalization: economic, social and political.

1.2 RESEARCH QUESTIONS

The overall objective of this research is to provide an empirical study into the impact of globalisation on three developing countries Estonia, Latvia and Lithuania and analyse positive and negative effects of globalization on their development. This is a major task and it looks both at positive and negative effects of globalization in Baltic states. To do this one will have to look at many different aspects of Estonia, Latvia and Lithuania and their development within the world. Furthermore, several questions are introduced considering the fact that globalization effects will be examined through economical, political, social and also cultural perspectives.

The first issue is related to the economic dimension of globalisation. What are the net flows of Foreign direct investment (FDI) and trade volumes in Estonia, Latvia and Lithuania and how has it developed during the time of liberalization? How is economy growing or shrinking in the Baltic states in terms of Gross domestic product (GDP) and GDP per capita? Dynamics of FDI since 1991, when Baltic states regained their independence and when the actual data begins, will be analyzed. This is an important indicator of globalization as globalization often starts with the opening up of domestic markets to the global economy. Hypothesis suggests that globalization in long-term promotes positive effect on growth of economies in the Baltic states.

In 2008-2009, all three countries were severely affected by the global financial crisis and as a result had to implement tough austerity measures. For this matter globalisation as contributor will be discussed and research on whether it was possible to decrease the negative effects of the global crisis on the economies of Baltic states and at what cost will be introduced. Hypothesis suggests that restoring national sovereignity and independence facilitated globalization processes in the Baltic states.

The third research issue is concerning the poverty and income inequalities in the Baltic countries. Do poor people benefit from globalization? Are rich getting richer and poor getting poorer? Is income inequality lower in other developing countries than in Estonia, Latvia and Lithuania? Changes in unemployment rate and correlation between unemployment and globalization tendencies will be studied. Hypothesis states that globalization has negative effects on poor people and has deepened income inequality.

The fourth research issue is regarding political effects of globalization. The political aspects of globalization are evidenced when governments create international rules and institutions to deal with issues such as trade, human rights, and the environment. How widely Estonia, Latvia and Lithuania have been involved in international organizations and international agreements? What are pros and cons of being part of the organizations that govern globalization as World Trade Organization (WTO), European Union (EU), World Bank (WB) and others? Countries can significantly benefit from being part of international organizations, however small countries like Estonia, Latvia and Lithuania might see some rules and conditions unfair comparing to other countries. Globalisation also enables to let governments consider more in thought when they are setting policies in their countries. And governments can absorb the experiences from other countries. On the other hand, globalization accelerates conflicts between countries and regions, which in turn leaves negative effect on the development of particular countries. Hypothesis suggests that becoming members of international organizations for small countries like Estonia, Latvia and Lithuania is indispensable step in order to have more economic power, trade opportunities and stronger voice in the international environment.

1.3 METHODOLOGY

This thesis aims to explain what are the effects of globalization to the development of Estonia, Latvia and Lithuania. The first objective is to define globalization and explain how globalization has evolved and developed through the centuries. Furthermore, important and commonly used terms such as economic, political and social globalization will be explained. The study approaches the research question primarily with an explanatory approach. An explanatory study is best suited because the paper aims to understand how the globalization has affected the economical, political and social development in Baltic countries. The goal of explanatory research is to go beyond the traditional descriptive designs of the positivist approach to provide meaning as well

as description. The purpose of explanatory research is broader than descriptive research; it is conducted to build theories and predict events. Objectives for explanatory research include explaining why some phenomenon occurred as well as interpreting a cause-and-effect relationship between two or more variables (McNabb 2008, p.100). In this thesis an analysis will be conducted of the effect of the globalization process on Baltic countries and how these countries have developed during the past few decades.
The research design has furthermore been of quantitative nature, using already existing research papers from organizations such as the UN, the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF). In the collection of quantitative data such as FDI rates, poverty rates and income distribution, The United Nations Conference on Trade and Development (UNCTAD) and the IMF websites have been helpful sources. The author aims to use secondary data as the main source of information. For this type of research approach the author believes that using secondary data is sufficient for answering the research questions. Most of the data has been collected through research and an extensive use of journal articles and reports from reliable sources.

1.4 SIGNIFICANCE OF THE STUDY

Despite the rich literature on the subject of globalisation, and more specifically, globalisation and developing countries, there is an absence of studies that have attempted to analyse the experience of individual developing countries (particularly, Estonia, Latvia and Lithuania) in order to understand whether the experience has been positive or negative. To a large extent the literature is general or focuses on specific issues, for example, exploring the potential environmental implications globalisation has had on a specific developing country, and therefore, does not explore overall effects of globalisation.
In summary, a contribution will be made to clear the gap to some extent in the current literature by providing a study of individual developing countries in order to understand positive and negative effects on these countries affected by globalisation.

2. LITERATURE REVIEW

2.1 DEFINING GLOBALIZATION

The proper meaning of globalization is a debatable issue and it can be different to different people and different disciplines. An extensive amount of research has been done within the field of describing globalization. According to a report from the OECD the term "globalization" refers to the dynamic and multidimensional process of economic integration within a country and can be explained by the fact that national resources are becoming more and more internationally mobile. Furthermore, globalization has for a long time been used to describe the increasing internationalization of financial markets and the different markets of goods and services. There are mainly three forces that are contributing to the process of globalization and these are the liberalization of capital movements, the opening of global markets to trade and investment, and the increasing use of information and communication technologies. Governments and international organizations have also played a very important role in the globalization of the world economy[1]. Same definition has been given by Martin Wolf who explains globalisation as the integration of economies through markets across frontiers, which is driven, in turn, by two forces: the reduction in the costs of transportation and communications and economic liberalization (Wolf 2005). The process of globalization is an international economic order which leads to the progressive integration of the world economy through pulling the barrier of trade, exchange rate and greater mobility of factors of production (Bhandari, Heshmati 2005, p.1). Joseph Stiglitz (2002, pp.9-10) states that "globalization is the closer integration of the countries and peoples of the world which has been brought about by the enormous reduction of costs of transportation and communication, and the breaking down of artificial barriers to the flow of goods, services, capital, knowledge, and (to a lesser) extent people across borders. Globalization has been accompanied by the creation of new institutions that have joined with existing ones to work across borders". Similar opinion has been expressed by Swedish journalist Thomas Larsson (2001), who in his book "The Race to the Top: The Real Story of Globalization", states that globalization

[1] OECD Handbook on Economic Globalization Indicators, 2005, http://www.oecd.org/science/sci-tech/oecdhandbookoneconomicglobalisationindicators.htm [accessed 10 February 2014]

“is the process of world shrinkage, of distances getting shorter, things moving closer. It pertains to the increasing ease with which somebody on one side of the world can interact, to mutual benefit, with somebody on the other side of the world”. Globalization refers to the fact that more people across large distances become connected in more and different ways.

No one will argue, that the irrevocable forces of globalization and regionalization have significantly reshaped the world economic landscape over the past quarter century. Globalization involves growing diffusion, expanding interdependence, more transnational institutions, and an emerging world culture and consciousness – all aspects of connectedness at the heart of globalization, all elements of the world society globalization is creating (Lechner, Boli 2008, p.2).

In fact, globalization is helping to give birth to an economy that is closer to the classic theoretical model of capitalism, under which rational individuals pursue their interests in the light of perfect information, relatively free from government and geographical obstacles. It is also helping to create a society that is closer to the model that liberal political theorists once imagined, in which power lies increasingly in the hands of individuals rather than governments, and in which people are free, within reasonable bounds, to pursue the good life wherever they find it (Micklethwait, Wooldridge 2008, p.17).

To sum up, globalisation describes a process by which national and regional economies, societies, and cultures have become integrated through the global network of trade, communication, immigration and transportation. “Globalisation” has become the buzzword of the last two decades. The sudden increase in the exchange of knowledge, trade and capital around the world, driven by technological innovation, from the Internet to shipping containers, thrust the term into the limelight.[2] In the more recent past, globalisation was often primarily focused on the economic side of the world, such as trade, foreign direct investment and international capital flows, more recently the term has been expanded to include a broader range of areas and activities such as culture, media, technology, socio-cultural, political, and even biological factors, e.g. climate change.

[2] http://www.economist.com/blogs/freeexchange/2013/09/economic-history-1 [accessed 13 December 2013]

The goal of this study is not to theorize about the nature of globalization or prove that it is in general a negative or positive phenomenon, but rather to analyze the impacts that arise from globalization on development of developing countries – countries that are still trying to define their place within the international political and economical system. The main goal of this thesis is to examine how Baltic states respond and adapt to the rapidly spreading conditions of globalism which is represented by integration into the world economy, eliminations of trade barriers, and extraordinary mobility of human capital, goods and services.

Based on this understanding of globalism this study will look at economic, social, political and cultural aspects of globalization and examine how these factors affect the overall development of Estonia, Latvia, Lithuania.

2.2 HISTORY OF GLOBALIZATION

The term globalisation is used to describe a recent period in international economic activity which started from the late 1980s. Nevertheless, globalization has been happening already for a long time. Many scholars point to sixteenth-century Europe as the original source of globalization. After all, the Europeans established worldwide trade connections on their own terms, brought their culture to different regions by settling vast areas, and defined the ways in which different peoples were to interact with each other. Economically and culturally, the modern world system already existed nearly five centuries ago (Lechner, Boli 2008, p.2). Some world historians attach globalization big bang's significance to 1492 (Christopher Colombus stumbles on the Americas in search of spices) and 1498 (Vasco da Gama makes an end run around Africa and snatches monopoly rents away from the Arab and Venetian spice traders). Such scholars are on the side of Adam Smith who believed that these were the two most important events in recorded history. Although Adam Smith himself never used the word, globalisation is a key theme in the "Wealth of Nations". His description of economic development has as its underlying principle the integration of markets over time. The process that Smith describes sounds rather like "globalisation", even if it was more limited in geographical area than what most people think of the term today.[3] Other

[3] When did globalisation start, 2013, Economist, http://www.economist.com/blogs/freeexchange/2013/09/economic-history-1 [accessed 17 December 2013]

world historians insist that globalization stretches back even earlier. There is a third view which argues that the world economy was fragmented and completely de-globalized before the 19th century. None of these three competing views has explicitly shown the difference between trade expansion driven by booming demand and supply within the trading economies (e.g., the underlying fundamental, population growth), and trade expansion driven by the integration of markets between trading economies (e.g., the central manifestation of globalization, commodity price convergence) (O'Rourke, K. H. & Williamson J.G., 2000). While Immanuel Wallerstein believes that "it was in the sixteenth century that there came to be a European world-economy based upon the capitalist mode of production", he also believes that several parts of the world (India, Russia, the Ottoman Empire and West Africa) only became incorporated into this world economy some time between 1750 and 1850, as the trade in luxury goods which had linked these regions to the core was replaced by trade in bulk goods (O'Rourke, K. H. & Williamson J.G., 2000, p.2).

Some economists states that globalisation depends on technology and politics and that historically, technology has been the single most important force for opening up borders. In the 1800s it was the spread of the steamship and refrigerator, the expansion of railroads and the invention of the telegraph that gave a push to globalisation. In the 1980s and 1990s it was the shipping container, and more recently it has been the internet, allowing information and services to be exchanged in the blink of an eye (Almeida M., Barral W., Batson E. et al., 2013, pp.3-20).

The first transatlantic cable was laid in 1866. This, argues professor Kevin O'Rourke (2002, pp.74-76), was "the most important breakthrough of the last 200 years" for the capital markets. "No other innovation," he writes, "including the late nineteenth-century invention, the telephone, or its late twentieth-century equivalent, the Internet, has had comparable impact on the speed of information flows and capital market integration" (O'Rourke 2002, p.74-76).

When did globalization become sufficiently advanced that it started influencing overall living standards and income distribution, by influencing domestic factor prices and living standards changing and inducing the widespread reallocation of resources within national economies? Many studies shows that globalization was sufficiently advanced by the early 19th century and certainly not before. Therefore, large-scale globalization begun in the 19th century. And late 19th century is described as a period of intense globalization, when millions migrated, trade greatly expanded, and new norms and organizations came to govern international conduct (O'Rourke, K. H. & Williamson J.G., 2000, p.7).

To summarizing, in the last centuries trade and globalization have developed enormously. Globalized society offers a complex system of forces and factors that are bringing markets, cultures and people into increasingly higher proximity to one another.

2.3 ADVANTAGES OF GLOBALISATION

Globalization is often seen as global Westernization. On this point, there is substantial disagreement among many proponents and opponents. Those who take an upbeat view of globalization see it as marvelous contribution of Western civilization to the world. From the opposite perspective, Western dominance – sometimes seen as a continuation of Western imperalism – is the devil of the piece. In this view, contemporary capitalism, driven and led by greedy and grabby Western countries in Europe and North America, has established rules of trade and business relations that do not serve the interests of poorer people in the world (Sen 2008, pp.20-31). Actually, none of this is really true. Over thousands of years, globalization has contributed to the progress of the world through travel, trade, migration, spread of cultural influences, and dissemination of knowledge and understanding (including that of science and technology). These global interrelations have often been very productive in the advancement of different countries (Sen 2008, pp.20-31). And even despite of recent global financial crisis, almost all countries still embrace the principles of international trade and investment. They want to enjoy the benefits of globalisation, but as much as possible they now also want to insulate themselves from its downsides, be they volatile capital flows or surging imports (Almeida M., Barral W., Batson E. et al., 2013. pp.3-20).

Globalisation is proposed to have had a number of benefits on developing countries. Dollar and Kraay (2001, p.12) assert that where developing countries have been able to participate in globalisation, they have experienced higher growth rates than developed countries. Some of the benefits of globalisation to developing countries are based on arguments put forward by free-trade advocates in earlier periods, while others are driven by the specific trends evidenced during the more recent period of globalisation (Dollar, Kray 2001, p.12).

Globalisation has increased the FDI and multinational enterprise (MNE) activity for some developing countries, it has provided the dynamic benefits, such as access to capital, technology and managerial practices and production techniques. It also afforded the opportunity for some developing countries to increase manufacturing outputs, which form part of the critical path towards development. More generally, FDI and MNE activity have brought unemployed or unemployed resources into production and stimulated domestic demand through imports (Rodrik 2011, p.120).

Corporations can benefit from changes and differences between the economic regulations between the countries. For example, issues related to property rights, financial infrastructure, and corporate governance laws, the regulation of work practices, or issues regarding taxation and bureaucracy vary between such financial systems. By developing knowledge and links while exercising such regulations, companies develop experience and can often benefit from them (Elliot, Kar, Richardson 2007, pp.17-62).

Globalization has also very positive effects in putting restrictions on national governance and policies. National autonomy is often used to pursue bad governance and policies, as in North Korea and Burma (to take extreme examples). Exposure to international trade and factor movements, and participation in international cooperation and institutions tend to prevent government mismanagement. For instance, the creation of the European Monetary Union has placed much-needed discipline on bad national monetary and fiscal policies (Elliot, Kar, Richardson 2007, pp.17-62).

Although, all parts of the world are affected by globalization, full force of change is felt by a relatively small number of upper and middle income countries. Most economies are still only partially integrated into the global system. While this insulates them to a degree from the risk of turbulence associated with volatile short term capital flows it also prevents these countries from tapping the resources, energy and ideas inherent in globalization (Yusuf 2001, pp.4-5).

2.4 DISADVANTAGES OF GLOBALISATION

The degree to which countries have moved toward globalization varies widely. In both the industrialized and the developing countries skeptics question the benefits and losses, and in many cases there is considerable resistance to further integration. Much of the globalisation literature makes reference to the processes of globalisation being uneven and unequal (Stiglitz 2002, Robertson 2008, Rodrik 2008). The globalisation experience differs between developing and developed countries, and even amongst developing countries.

Disadvantages of globalization mainly concentrates on the social impact of globalization and its influence on the people's wealth, culture, values and traditions, as well as environment. Globalisation has been attacked by critics of free market economics, like the economists Joseph Stiglitz, Dani Rodrik and Ha-Joon Chang, for perpetuating inequality in the world rather than reducing it. Some agree that they may have a point. The IMF admitted in 2007 that inequality levels may have been increased by the introduction of new technology and the investment of foreign capital in developing countries. Others, in developed nations, distrust globalisation as well. They fear that it often allows employers to move jobs away to cheaper places.[4] The fact that employees can be more easily substituted for each other across national boundaries undermines what many conceive to be a postwar social bargain between employees and employers, under which the former would receive a steady increase in wages and benefits in return for labor peace. This is because employees now have to pay a larger share of the cost of improvements in work conditions and benefits, they have to incur greater instability in earnings and hours worked in response to shocks to labor demand or labor productivity and their bargaining power erodes so they receive lower wages and benefits whenever bargaining is an element in setting the terms of employment (Rodrik 2008, pp.241-246). Country's exposure to international trade, and to world markets more generally, affect the distribution of incomes within the country. Not surprisingly, the entry of many developing countries into the global world market in the last three decades coincides with changes in various measures of inequality in these countries

[4]When did globalisation start 2013, Economist http://www.economist.com/blogs/freeexchange/2013/09/economic-history-1 [accessed 17 December 2013]

(Goldberg, Pavcnik 2007, pp.1-4). What is more surprising is that the distributional changes went in the opposite direction from what the conventional wisdom suggests: while trade liberalization was expected to help the less skilled, who are presumed to be the relatively abundant factor in developing countries, there is overwhelming evidence that they are generally not made better off relative to workers with higher skill or education levels (Goldberg, P.K., Pavcnik, N. 2007., p.2) For some groups, the rising flow of trade and capital has heightened the sense of vulnerability. Blue and many white collar workers in industrialized countries fear being displaced by cheaper labor in developing countries. The volume and volatility of capital flows, has increased the risks of banking and currency crises as well as their costs. Production and trade is increasingly dominated by transnational corporations which use the options afforded by globalization to their own best advantage, and without much regard for the longer term development objectives of individual countries. There are also those who fear that an excessive focus on material progress threatens the sustainability of development and the cultural underpinnings of societies. The environment is being irreversibly degraded, and ‘cultural capital’ is being lost as the result of an incipient homogenization of tastes, beliefs, and cultural markers (Yusuf 2001, p.4).

Globalization has much to offer; but even as we defend it, we must also, without any contradiction, see the legitimacy of many questions that the antiglobalization protesters ask. There may be misdiagnosis about where the main problems lie (they do not lie in globalization, as such), but the ethical and human concerns that yield these questions call for serious reassessments of adequacy of the national and global institutional arrangements that characterize the contemporary world and shape globalized economic and social relations (Sen 2008, p.20-31).

2.5 MEASURING GLOBALIZATION

There are many different ways to measure globalization and the effects of it. Main measure often used for globalization is trade openness, which can be measured as exports and imports as a percentage of the GDP. However, trade openness can be influenced by location of a country and access to the sea, which is important to take into consideration.

Another measure of the impact of globalization is the FDI. There are several concepts to explain and measure FDI. The study of economists Drusilla K. Brown, Alan V.Deardorff and Robert M.Stern (2007, pp.279-329) shows that FDI often takes the form of acquisition of an existing facility, but most FDI into developing countries is "greenfield" investment – that is, newly constructed establishments which therefore add to the physical capital of the host country. They describe two types of FDI. The type intended to serve the host-country market and the type intended to produce for export. Obviously, there exists some FDI that serves both purposes, but if so, one purpose is usually dominant and the other incidental. In case of Baltic countries it can be assumed that FDI serves the host-countries considering that in overall, producing for export is not cost effective as these countries can not offer an advantage in form of cheaper inputs, higher-quality inputs, or both, such as labor or some natural resources. However, Estonia can qualify for offering higher quality inputs in information technologies and electronics (Brown, Deardorff, Stern 2007, pp.279-329).

Common way of measuring extent of a country's integration with the world is to split globalization into economic, political and social dimensions. Economic globalization measures the extent to which a country is exposed to foreign capital and trade with the world. Political globalization measures the degree of a country's political integration. For example, diplomatic relations with the rest of the world and international relations. Indicators on social globalization can be for example poverty, unemployment and income distribution.[5]

By looking at the economic, political and social dimensions, globalization effects on Estonia, Latvia and Lithuania will be analyzed. As for economic dimension, key measurements such as merchandise trade, exports of goods and services, FDI, GDP and GDP per capita will be researched. A review of political situation in the Baltic states will be made by looking at historical development in these countries since Soviet times as well as discussing the memberships in the IMF, World Trade Organization (WTO), EU, OECD and the North Atlantic Treaty Organization (NATO). Furthermore, poverty rates, unemployment rates and income distribution will be analyzed in order to understand how people's welfare has developed during the recent era of globalization.

[5] KOF Index of globalization, http://globalization.kof.ethz.ch/ [accessed 8 March 2014]

3. DATA AND METHOD

3.1 ECONOMIC ANALYSIS

3.1.1 Recent historical perspective and the USSR

As stated by Thomas L.Friedman (2006, p.9-10), second globalization era lasted roughly from 1800 to 2000. In the second half of this era globalization was powered by falling telecommunication costs – thanks to diffusion of the telegraph, telephones, the PC, satellites, fiber-optic cable, and the early version of the World Wide Web. During this era World saw the birth and maturation of a global economy, in the sense that there was enough movement of goods and information from continent to continent for there to be a global market, with global arbitrage in products and labor (Friedman 2006, p.9-10). Part of these technological achievements would not have been present in the Baltic states at the end of 20th century if not for the collapse of the USSR. Reason behind that is the Iron curtain which separated the USSR from non-communist areas in the Europe. It served as a barrier to understanding and the exchange of information and ideas from one country toward another. Rigid censorship and secrecy applied to all of the communication and activities over the borders, almost eliminating the possibility for the Soviet Union countries to benefit from globalization[6]. Integrated world markets help to ensure an optimal allocation of factors of production, and therefore help to maximize both aggregate world welfare and individual national welfare. By contrast, sealing off national borders fosters economic inefficiency, and has negative consequences for poverty alleviation and development prospects (J.Ravenhill 2008, p.67-95).

All three Baltic states played significant role in the economy of the USSR, however Latvia differed from Estonia and Lithuania in several regards. The country harbored larger and more important Soviet military installations than its neighbors. Riga, the capital of Latvia, has been a dominant city in the region for centuries, having attracted a large Russian population even before World War II. With its large and good ports, Latvia was the main transit country in the Baltics. Riga's large industrial enterprises, producing phones and microbuses, overshadowed those in the neighboring countries.

[6] Soviet Union, The Cold War, http://www.country-data.com/cgi-bin/query/r-12457.html [accessed 12 March 2014]

Because of its great strategic significance, Latvia was more tightly controlled by Moscow than its neighbors.[7]

In the USSR, Latvia, Lithuania and Estonia always stood apart. The Baltic republics boasted a higher standard of living than other parts of the country, and produced goods that set the standard for quality for the entire nation. But their citizens never sought to fully integrate into the country's multi-ethnic community. Rather they sought independence, first in their everyday lives, and then as nations.[8]

In 1991, the USSR formally ceased to exist. For some, particularly among the old generations, this was an unwelcome transformation. Communism was a great system for making people equally poor. In fact, there was no better system for that than communism. Capitalism made people unequally rich, and for some who were used to the plodding, limited, but secure Socialist lifestyle – where a job, a house, an education, and a pension were all guaranteed – the changes were deeply unsettling (Stiglitz 2002, p.220).

After dissolution of the Soviet Union new independent states chose different paths of development that were defined by historical and economic factors and shaped current conditions of those countries. One of the biggest local challenges that Baltic states have been facing after becoming independent was lack of an institutional mechanism and economic interdependence those states have inherited as a part of Soviet Union legacy. As Soviet republics, Estonia, Latvia and Lithuania depended on raw materials and energy mainly from Russia, while they were producing all the wrong goods. After independence, many of the former Soviet republics – and especially Russia – could purchase goods like the ones they had previously received from the Baltic states, cheaper or better quality elsewhere. As a result in the beginning of 1990s the Baltic states had one of the highest shares of industries with a negative value-added among the states of former Soviet Union (Norgaard, Johannsen 1999, p.145).

The thinkers of Enlightenment, such as Thomas Jefferson, Tom Paine, John Stuart Mill and Karl Marx never doubted that the future for every nation in the world was to accept some version of western institutions and values (Gray 2008, p.24). The former Soviet

[7] Latvia's post-Soviet transition, http://www.piie.com/publications/chapters_preview/6024/01iie6024.pdf [accessed 20 March 2014]

[8] Latvia's post-Soviet transition, http://www.piie.com/publications/chapters_preview/6024/01iie6024.pdf [accessed 20 March 2014]

Union embodied a rival Enlightenment Utopia, that of a universal civilization in which markets were replaced by central planning. The human costs of that defunct Utopia were incalculable. Totalitarianism, superiority of communism and centralized planning were main characteristics of the USSR. And at the close of the Soviet era Russia itself was in some ways further from modernity than it had been in late Tsarist times in 18th century (Friedman 2006, pp.51-55).

Following their renewed independence in the early 1990s, the Baltic countries showed impressive progress already after a decade of transition. They liberalized and opened their economies to the international market, and implemented a significant number of difficult and complex market-oriented structural reforms. The tremendous output fall of the early nineties reflected the great differences which existed before transition and the degree of restructuring required (Popov 2001, pp.7-8). Also the prospects of the EU enlargement stimulated convergence across the three countries by creating a common policy framework and goals. The Baltic states had to adopt the policies targeting to obtain the best possible allocations of resources and create the conditions for sustainable growth and improvement of living standards.

3.1.2 Enablers of globalization

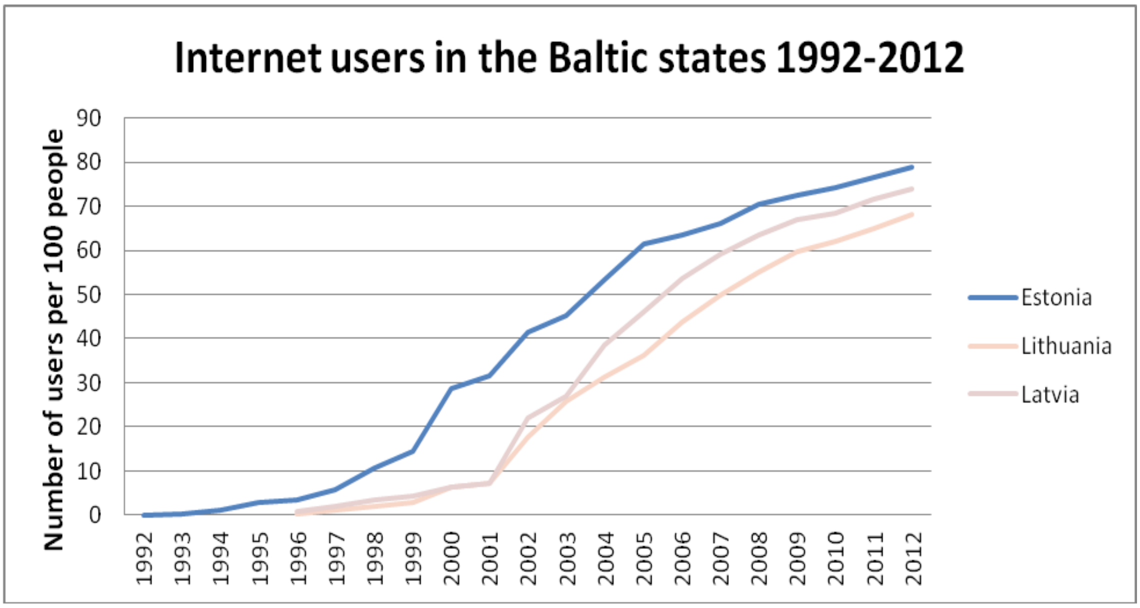
Enablers are factors that have changed within the international economy to allow an increased level of integration or greater flows between countries. Some of these factors have represented reduction in barriers to international activities that have previously existed. Broadly, the factors that have enabled globalization encompass technology and innovation, also improvements in transportation and communication. The Internet and cellular phones are increasing the flow of information, improving productivity and efficiency, and opening up new markets and new kinds of business all across the economy. Also there is evidence that improving mobile internet access helps economies too.[9]

In the global economy, access to broadband has become as essential to individual and community economic prosperity as electricity and roads. From rural to urban areas and

[9] What is the impact of mobile telephony on economic growth?, 2012, Deloitte http://www.gsma.com/publicpolicy/wp-content/uploads/2012/11/gsma-deloitte-impact-mobile-telephony-economic-growth.pdf?_ga=1.230414556.1377408786.1395849811 [accessed 26 March 2014]

everywhere in between, all people stand to benefit economically from the Internet network. In addition to the obvious beneficial effects on productivity, Internet access has socio-economic effects, including acquisition of knowledge and skills that are required for jobs and education. High speed connections accelerate business development by providing new opportunities for innovation, expansion, and e-commerce[10].

Figure 3.1: Internet users in the Baltic states 1992-2012



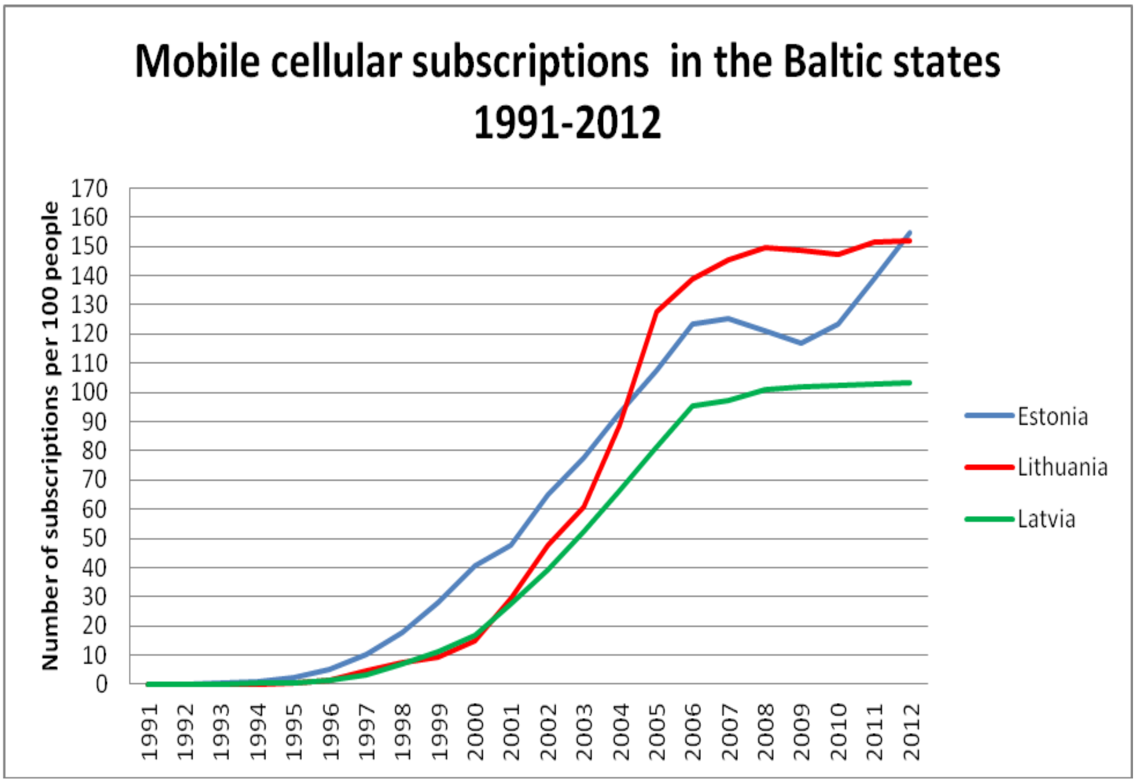
Source: World Bank, Internet users (per 100 people), http://data.worldbank.org/indicator/IT.NET.USER.P2/countries?display=default [accessed 22 March 2014]

The internet extended beyond borders of the United States of America to Europe in 1990. That time only small part of the people in the Baltic states were using electronic mailbox. As shown in Figure 3.1 the Internet in Estonia begun to widespread in 1992, but in Latvia and Lithuania only four years later in 1996. Initial statistics show that less than one person per 100 people was using the Internet. The Internet in Latvia and Lithuania began to experience significant growth in 2001 but in Estonia already in 1999. However, still the Internet at home was not common in the Baltic states, and many people did not use it at all; those who did instead accessed it in public areas or through their place of work, as high subscription prices for using the Internet at home remained a barrier. But by 2008 access prices fell followed by increase in numbers of

[10] What is the impact of mobile telephony on economic growth?, 2012, Deloitte http://www.gsma.com/publicpolicy/wp-content/uploads/2012/11/gsma-deloitte-impact-mobile-telephony-economic-growth.pdf?_ga=1.230414556.1377408786.1395849811 [accessed 26 March 2014]

the Internet users. In 2012, there were 79 Internet users per every 100 people in Estonia, 68 in Lithuania and 74 in Latvia. By 2013, Latvia had one of the fastest internet speeds in Europe. Neighboring Lithuania and Estonia also perform relatively well.

Figure 3.2: Mobile cellular subscriptions in the Baltic states 1991-2012



Source: World Bank, Mobile cellular subscriptions (per 100 people), http://data.worldbank.org/indicator/IT.CEL.SETS.P2 [accessed 26 March 2014]

In Europe, first mobile cellular phones were used in Nordic countries in the beginning of 1980s (Beise 2001, p.138). As shown in Figure 3.2 among the Baltic countries Estonia was the first to introduce cellular network in 1991 followed by Latvia and Lithuania in 1992; in all three countries there were less than one mobile cellular subscription per 100 people. Meantime, the EU had 6.37 mobile cellular subscriptions per 100 people. Mobile cellular subscriptions in the Baltic states significantly increased from 1996 onwards. In 2012, numbers of subscriptions in Estonia and Lithuania were very close, 154 and 151, respectively, while in Latvia there were 103 subscriptions per 100 people.

Technology is important to bring about globalization and it could not have occurred in its absence. Without modern communication infrastructures in particular, a worldwide economy would not be possible (McGrew 2008, 2008, p.77-314). Writers refer to the transformation in communications and transport technologies and the way in which this has “shrunk the globe”. For the Baltic states global technological achievements have played a significant role as these countries were isolated from the rest of the world for a long years. Improvements in transportation and communication have reduced perceptions of time and distance. More specifically, transportation innovations have lowered the cost of transport services and decreased the time necessary to move products, while developments in communication have resulted in improvements to consumer markets, for example, through providing an understanding of alternatives, and have promoted knowledge sharing.

3.1.3 Trade with world

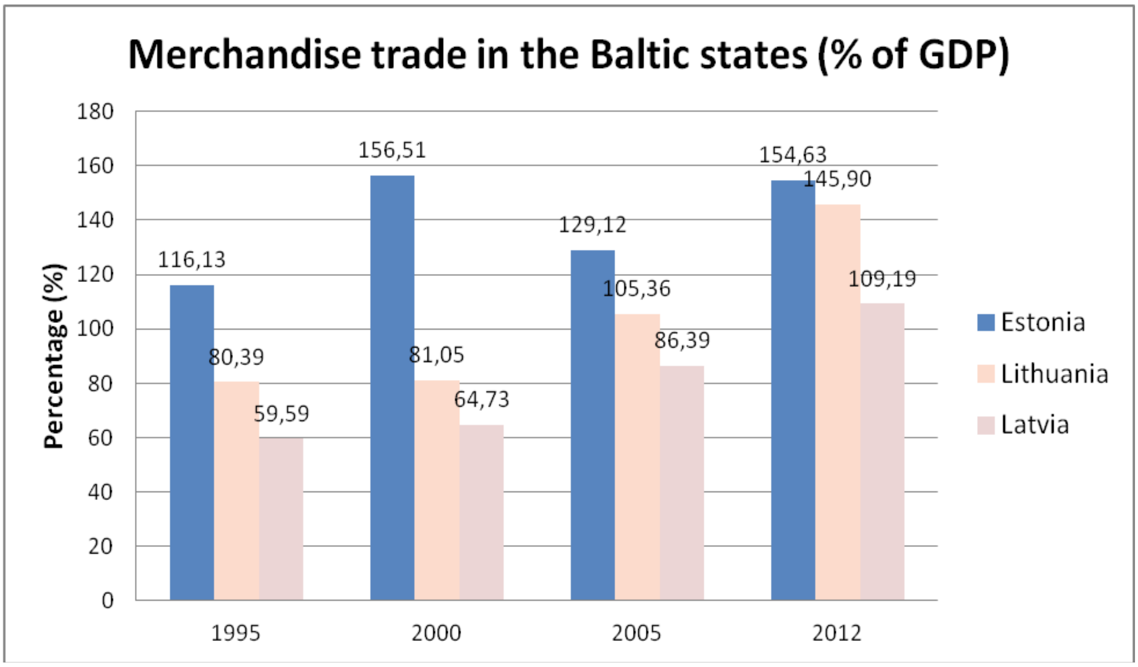
A spectacular achievement of all three post-communist countries was the instant adoption of current account convertibility, which applied to tourist traffic and foreign trade allowing residents to make and receive trade-related payments, and capital account convertibility freedom to convert local financial assets into foreign financial assets and vice versa at market determined rates of exchange. Estonia was the first post-communist country to opt for full convertibility in 1994, which greatly facilitated foreign trade liberalization.[11]

Multiple international agreements reinforced trade liberalization. Adopting free trade policies led to dramatic geographical and sectoral shifts in the pattern of Baltic trade. In 1990s, globalization and trade liberalization strongly interacted with inter-sectoral adjustment and economic restructuring. Employment and revealed comparative advantages decreased in most heavy or capital-intensive industries, such as machinery, textile fabrics or electronics, whereas the light industry and sectors in line with Baltic resource endowments, such as wood and wood manufacturers and clothing had re-surfaced. It is worth noting that new industries that have been emerging in terms of trade specialization, such as telecommunication equipment or furniture, are largely connected with foreign direct investments. Experience of the Baltic states is a powerful practical expression of the law of comparative advantage, and demonstrates how resilient its effects have been to fifty years of central planning(Haraldsdottir, Thorarensen 2007, pp.19-31).

[11] Latvia’s post-Soviet transition, http://www.piie.com/publications/chapters_preview/6024/01iie6024.pdf [accessed 27 March 2014]

Trade (both imports and exports) is vital to any successful modern economy. In the long run trade is crucial for the competitiveness of the Baltic states' economies. By International competition forces the countries to focus on areas of comparative advantage. This helps to ensure that lacking skills and resources are deployed where they are most productive. Estonia, Latvia and Lithuania are small countries both by population and territory and they tend to be more trade-dependent than larger countries.

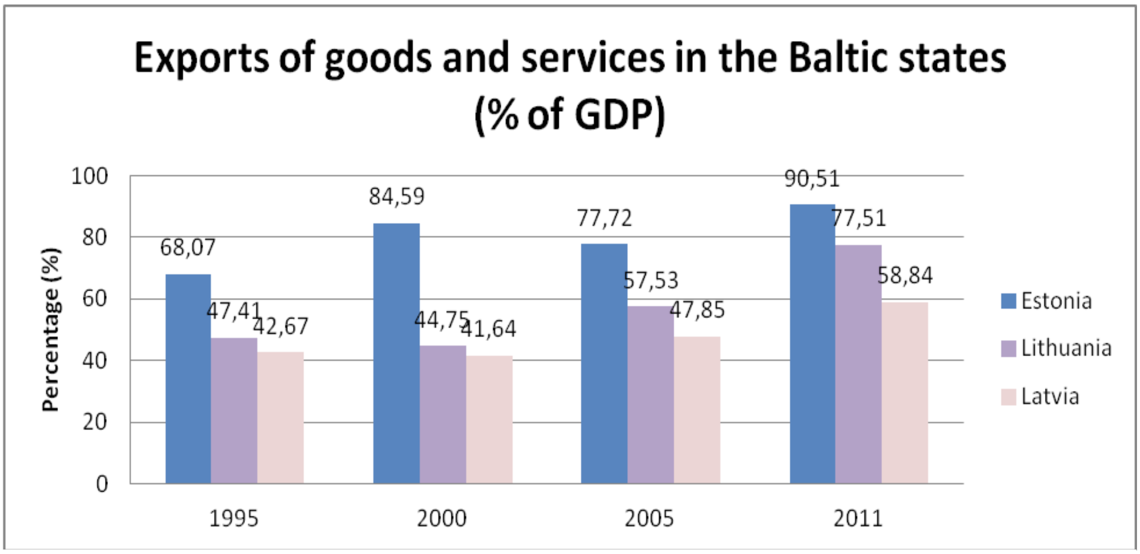
Figure 3.3: Merchandise trade in the Baltic states (% of GDP)



Source: World Bank, Merchandise trade (percentage of GDP), http://data.worldbank.org/indicator/TG.VAL.TOTL.GD.ZS [accessed 27 March 2014]

The trade-to-GDP-ratio measures a country's 'openness' or 'integration' in the world economy. It is often called the 'trade openness ratio'. As shown in Figure 3.3 Estonia's trade to GDP ratio was 154.63 percent in 2012, up from 116.13 percent in 1995. Latvia's trade to GDP ratio was 109.19 percent in 2012, up from 59.59 percent in 1995. But Lithuania's trade to GDP ratio was 145.9 percent in 2012, up from 80.39 percent in 1995. These countries import and export more than they produce meaning that international trade plays high importance for these countries. They are more dependent than other larger countries due to their small size and population. They need to import more goods than larger countries in order to satisfy domestic demand.

Figure 3.4: Exports of goods and services in the Baltic states (% of GDP) [12]



Source: World Bank, Exports of goods and services (percentage of GDP), http://data.worldbank.org/indicator/NE.EXP.GNFS.ZS [accessed 26 March 2014]

Exports of goods and services in the Baltic states has consistently increased since regaining independence, particularly after accession to the EU. As shown in Figure 3.4, in Estonia in 2011 the value of total exports compared to 1995 increased by 22 percent, in Latvia - by 16 percent and in Lithuania – by 30 percent. In 2012, main trade partners of Estonia were EU27[13] (57.5 percent), Russian Federation (17.5 percent), United States (6.5 percent), Norway (3.0 percent) and Ukraine (1.3 percent). Latvia was mainly trading with EU27 (68.8 percent), Russian Federation (11.4 percent), Norway (2.6 percent), Algeria (2.1 percent) and Belarus (1.8 percent) and Lithuania with EU27 (60.5 percent), Russian Federation (18.9 percent), Belarus (4.6 percent), Ukraine (3.6 percent) and Norway (2.0 percent).[14] Being EU member states and having common trade framework, Baltic countries trade most with EU27 countries.

The share of Estonian, Latvian and Lithuanian export in world trade in 1996 was 0.04 percent, 0.03 percent and 0.06 percent, respectively (Misztal 2013, p.27). However, in

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[12] Note: Exports of goods and services represent the value of all goods and other market services provided to the rest of the world. They include the value of merchandise, freight, insurance, transport, travel, royalties, license fees, and other services, such as communication, construction, financial, information, business, personal, and government services. They exclude compensation of employees and investment income and transfer payments.

[13] Note: EU27 member states are Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom.

[14] WTO Trade Profiles 2013, http://www.wto.org/english/res_e/booksp_e/trade_profiles13_e.pdf [accessed 27 March 2014]

2012 it was 0.09 percent, 0.08 percent and 0.16 percent, accordingly. The share of Estonian, Latvian and Lithuanian import in world trade in 1996 was 0.04 percent, 0.03 percent and 0.06 percent, respectively. But in 2012 Estonian share was 0.10 percent, Lithuanian – 0.19 percent and Lithuanian – 0.17 percent (WTO Trade Profiles 2013). This data shows that Baltic countries in more and more degree get involved in international trade. And it is visible both on the export side, as well as on the import side. It essentially shows growing international competitive position of these countries.

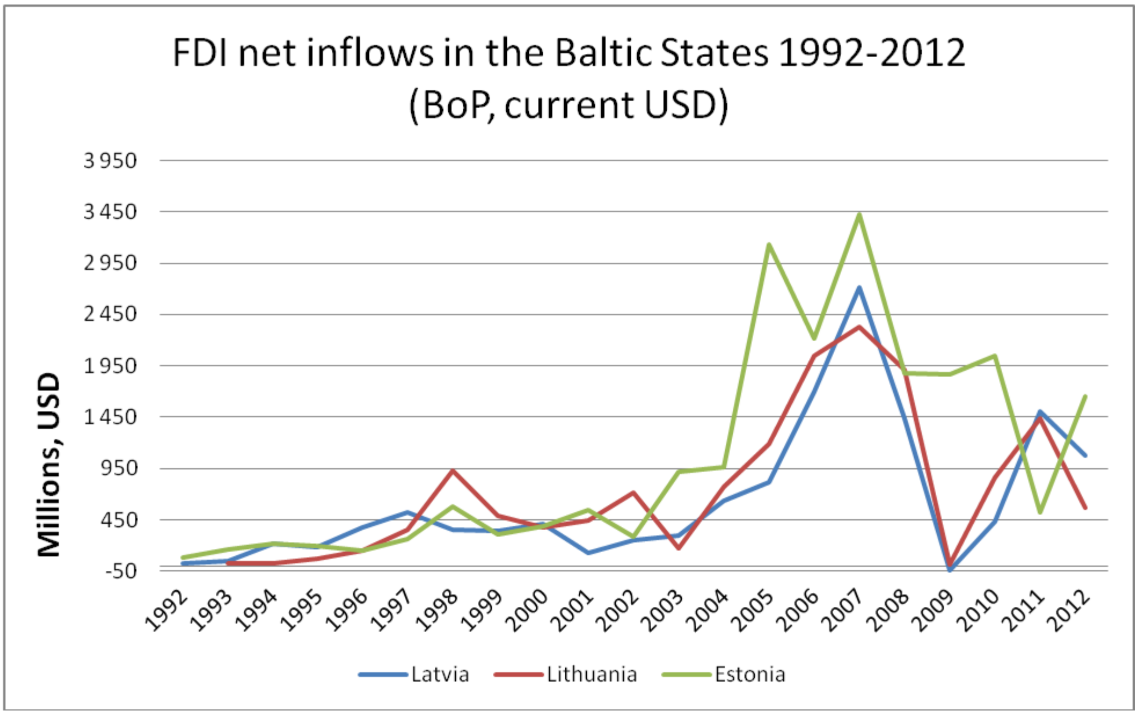
3.1.4 Foreign direct investment

Central planning in the USSR meant having more than 90 percent of production under direct state control (IMF, et al. 1991). Gosplan (State Planning Committee) formulated all import and export plans, coordinated the allocation of investment and other resources, and had final authority over all decisions concerning foreign trade, including trade levels and commodity composition. As a result of foreign trade policy, foreign direct investment had a minor role as the USSR historically had pursued a policy of self-sufficiency (Hirsch 2005, pp.231-240).

Since 1970s flows of FDI worldwide have not only become more geographically diffuse, but also much more intense. Recent years have witnessed a significant change in the pattern of inward and outward FDI flows – with almost doubling of the share accounted for by developing economies (Mcgrew 2008, p.290). This trend has also positively affected the Baltic states in terms of FDI flows.

Since EU accession in May 2004 and the resultant increase in investors' confidence, FDI flowed steadily into the financial intermediation, manufacturing, and real estate sectors of the Baltic economies with a significant share originating from Sweden, Finland, and Denmark (Obiora, 2009, p.4), however it continued until global financial crisis in 2008. As shown in Figure 3.5 sharp decline in FDI net flows occurred during 2009-2011 as a result of the global financial crisis. This also represents negative immediate impact of globalization on domestic economies during a global downturn.

Figure 3.5: FDI net inflows in the Baltic states 1992-2012 (BoP, current USD)



Source: World Bank, Foreign direct investment, net inflows (BoP, current USD), http://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD [accessed 01 March 2014]

FDI in Estonia has steadily been increasing since the country gained its independence from the Soviet Union. As shown in Figure 3.5 FDI net inflows have increased from 82.3 million USD in 1992 to 1648.5 million USD in 2012. Estonia's main sources of comparative advantage since the start of transition is proximity to the Nordic markets, location between Eastern and Western Europe, competitive cost structure and high-skilled labor force[15]. Because of full-scale liberalization and successful privatization Estonia has been able to attract FDI beyond the absorption level despite of its small market mostly by serving as headquarters for many Nordic MNEs. The country's geographical position and decisiveness of its government has placed Estonia as one of the best improved EU members and its growth prospects for the future are good. Also, important to note that Estonia was receiving FDI earlier than other two Baltic countries as it was more attractive for foreign investors due to early market reforms.

Latvia's location has been main reason for attracting FDI in the country. Latvia provides a good market base for the whole Baltic region, a well-functioning transit and logistics point for the East and a favorable manufacturing location. As shown in Figure 3.5, FDI

[15] Invest in Estonia, Estonian Investment Agency, http://www.investinestonia.com/en/ [accessed 03 April 2014]

net inflows have significantly increased from 29.4 million USD in 1991 to 1076.3 million USD in 2012.

Lower FDI net flows in Latvia during some periods can be explained by the fact that Latvia is scoring worse in international rankings of economic freedom, corruption and credit rating. Its institutions are also more unmanageable, more prone to corruption and are sometimes more hesitant in supporting FDI (Hunya, 2004).

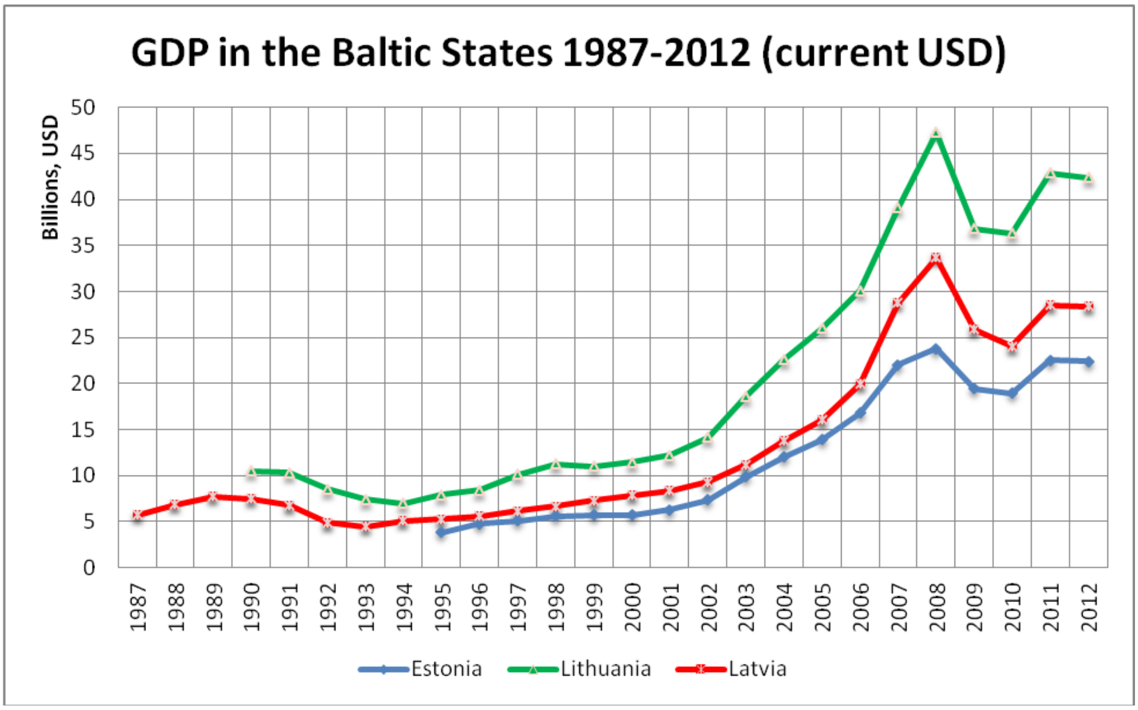
Location of Lithuania also makes the country significant logistically, both by sea and ground. In Lithuania, mainly manufacturing and energy sectors are attracting FDI. Lithuania has several other attractive features. The country has legislation to promote and protect foreign investments and network of Free Economic Zones set up at the main transport and industrial centres in Klaipeda and Kaunas. FDI net flows have increased from 30.18 million USD in 1992 to 574 million USD in 2012 as shown in Figure 3.5.

Empirical evidence from broad-based country studies suggests that FDI has a positive impact on economic growth, restructuring and competitiveness – both directly through transfer of capital and knowledge to foreign-owned companies and indirectly through spillovers to the domestic sector (Hunya, 2004). Baltic states have been building their economies largely on the Soviet infrastructure. Although the process from moving towards a free market economy has been economically complex with many concerns and uncertainties, the Baltic countries have managed to strengthen their economies, attract FDI and see the benefits of economic globalization.

3.1.5 Gross domestic product

Economic progress in a country is traditionally measured by GDP. From a strictly numerical perspective, GDP provides an easy-to-follow indicator of economic health. The GDP in Latvia was worth 28.37 billion USD in 2012, in Lithuania – 42.25 billion USD and in Estonia – 21.85 billion USD. GDP volume has risen significantly comparing to the first data entries (according to the World Bank, statistics of Latvia available since 1987, Lithuania – 1990 and Estonia – 1995) and has increased for 22.65 billion USD in Latvia, for 31.83 billion USD in Lithuania and for 18.61 billion USD in Estonia as shown in Figure 3.6.

Figure 3.6: GDP in the Baltic states 1987-2012 (current USD)



Source: World Bank, GDP (current USD), http://data.worldbank.org/indicator/NY.GDP.MKTP.CD [accessed 27 February 2014]

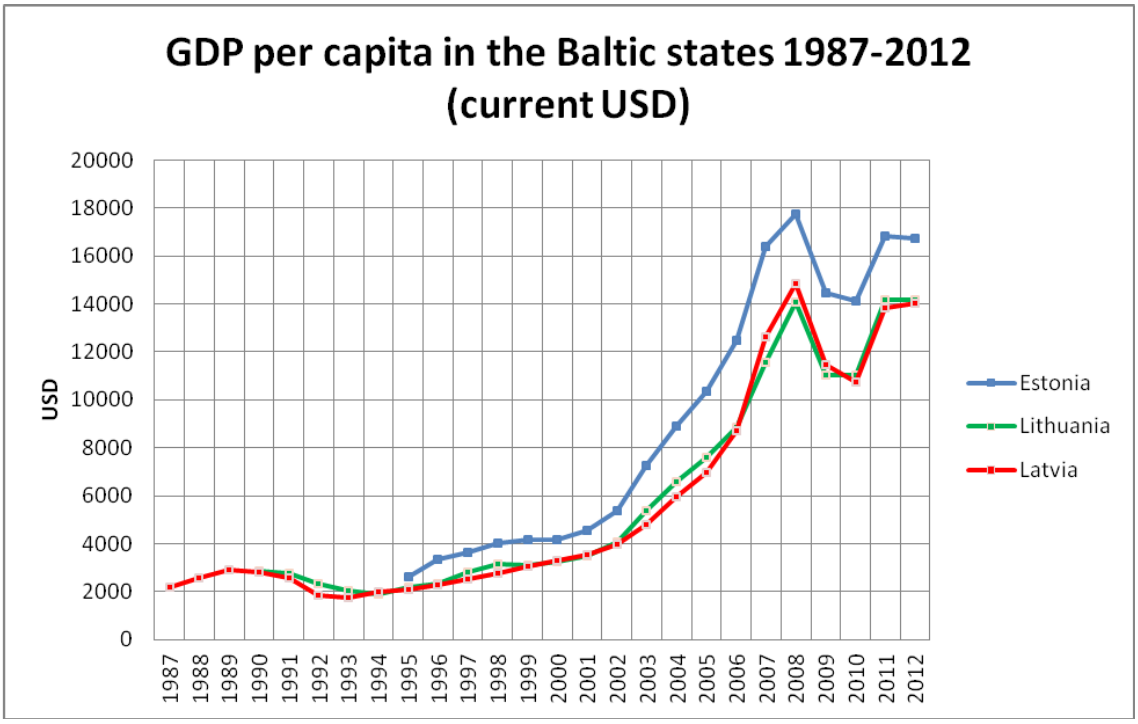
In 1991, when the Baltic states left the Soviet Union, the Soviet economy was collapsing in every sense: GDP was approaching free fall; the Soviet budget deficit was about 31 percent of GDP; prices were skyrocketing, but even so shortages prevailed as prices were still state controlled; and no foreign currency reserves were on hand, which disrupted most trade.[16] Baltic states had to establish a functioning economies. Reform package was based on liberalization of prices and trade, macroeconomic stabilization and privatization. Without deliberation the Baltic states embraced globalization and pursued free-market radicalism which was the only path these countries could take in order to develop a competitive economy. As Estonia, Latvia and Lithuania reformed and integrated with the world market, they begun to see the benefits from globalization.

[16] The Post Soviet Transition, http://www.piie.com/publications/chapters_preview/6024/01iie6024.pdf [accessed 02 March 2014]

3.1.6 Gross domestic product per capita

GDP per capita reflects changes in total well being of the population. The growth in real GDP per capita indicates the pace of income growth per head of the population. As a single composite indicator it is a powerful summary indicator of economic development. It does not directly measure sustainable development but it is a very important measure for the economic and developmental aspects of sustainable development. [17]

Figure 3.7: GDP per capita in the Baltic states 1987-2012 (current USD)



Source: World Bank, GDP per capita (current USD), http://data.worldbank.org/indicator/NY.GDP.PCAP.CD [accessed 28 March 2014]

As shown in Figure 3.7 the common trend of GDP per capita in Estonia, Latvia and Lithuania indicates growth in a steady pace until 2009. Economic growth within the EU suffered from 2008 global financial and economic crisis. A severe recession in most countries in 2009 was followed by a partial recovery in 2010, when also the Baltic states begun their economic recovery. In 2010, the three Baltic states had all of their population living in regions with an average GDP per inhabitant below 75 percent of the

[17] Gross Domestic Product, United Nations Statistics Division, http://www.un.org/esa/sustdev/natlinfo/indicators/methodology_sheets/econ_development/gdp_percapita.pdf [accessed 29 March 2014]

EU-27 average.[18] In 2012, in Estonia GDP per capita compared to 1995 increased by 14 088 USD, in Latvia GDP per capita compared to 1987 increased by 11 832 USD and Lithuanian GDP per capita compared to 1990 increased by 11 342 USD.

[18] Eurostat regional yearbook 2013, http://epp.eurostat.ec.europa.eu/portal/page/portal/product_details/publication?p_product_code=KS-HA-13-001 [accessed 28 March 2014]

3.2 POLITICAL ANALYSIS

International co-operation can help to address three typical problems associated with the process of global integration: a temptation to free ride, and inhibiting fear and a need to find meeting points in situations where collaboration will produce differing costs and benefits to governments (Aggarval, Dupont 2008, p.67-95). In practice, the benefits of globalization cannot always be realized by states pursuing independent policies; co-operative action is required. A country's need for international co-operation depends on its socio-political structure as well as on the structure and flexibility of its economy (Cavanagh, Mander 2002, p.31-32).

Estonia, Latvia and Lithuania are members of the main important international organizations. IMF, WTO, EU and NATO are considered to be some of the more important ones. Estonia is also a member of the OECD. By looking into countries' participation and role within these international organizations an analysis of how globalization has affected Latvia politically will be conducted in this section.

3.2.1 IMF and global financial crisis 2007-2009

Globalization of the world economy has increased the relevance of the international financial institutions as key arbiters of economic policy, the guardians of macroeconomic stability, and the leading resources for knowledge and technical advice on development issues. The IMF is one of the most powerful institutions on Earth - yet few know how it works. In particular, the IMF and the WB has played a central role in stemming financial crises and aiding in the economic transition of the post-communist countries of Eastern Europe and the former Soviet Union. The IMF and WB is at the center of the major economic developments and the key institutional gatekeepers for countries that desire full participation in the global economy (Erikson 2003, p.151). All three Baltic countries became members of the IMF and also the World Bank in 1992.

The dissolution of the Soviet Union in 1991 enabled the IMF to become a (nearly) universal institution as the memberships increased rapidly. The IMF played a central role in helping the countries of the former Soviet bloc transition from central planning to market-driven economies.[19] The challenges facing the economies of the former Soviet Union and the other Communist bloc nations in transition were daunting: they had to move from one price system – the distorted price system that prevailed under communism – to a market price system; they had to create markets and institutional infrastructure that underlies it; and they had to privatize all the property which previously had belonged to the state and they had to create new enterprises to help redeploy the resources that had been previously so inefficiently used (Stiglitz 2002, p.140). This kind of economic transformation had never before been attempted, and sometimes the process was less than smooth. The sheer size of the task, historic nature of the transition, and complexity of the economic issues involved, forced the IMF to dramatically reorient their thinking towards the challenges facing transition economies. In December 1991, the IMF created a new area department called European II to work exclusively with the Baltic States and former members of the USSR (Erikson 2003, p.15).

Important part of the cooperation between the IMF and the Baltic states was through technical assistance, concentrated in the fiscal, financial, statistical and legal areas. Technical assistance was provided through staff visits from headquarters as well as advisors placed in the respective capitals. It was coordinated with other providers, such as the World Bank and the EU, and bilateral assistance, in particular by the United States and EU countries (Knobl, Kaas 2003, p.5). Finally, with EU accession approaching, cooperation had switched into a "surveillance mode". Surveillance of members' policies was carried out through regular consultations with all members. The IMF staff visited Estonia, Latvia and Lithuania, usually annually, to discuss the economic outlook and policies. The staff reported to the IMF Executive Board, where the consultation is concluded in a discussion of the reports. Later summary of discussion is communicated to the countries. Followed by all three Baltic countries, publishing staff reports as well as the summary of the Board discussion by placing them on the IMF's website became a common practice (Knobl, Kaas 2003, p.5).

The IMF staff assisted in formulating economic policy programs that were supported financially by the IMF in the form of stand-by arrangements and the use of the structural transformation facility. The main elements of the policy were tight monetary

[19] Societal change for Eastern Europe and Asian Upheavel (1990-2004), IMF, http://www.imf.org/external/about/histcomm.htm [accessed 30 March 2014]

and fiscal policies aimed at bringing down inflation, and structural measures aimed at institution building and rationalization of economic incentives. By the end of the decade, most economies in transition had successfully graduated to market economy status after several years of intense reforms. From the end of March 2003, all three Baltic countries moved from cooperation with the Fund in the form of formal arrangements to a surveillance mode concentrated on consultations, a development that testifies to the progress these countries have made since joining the IMF. It should also be considered as the normal form of cooperation for countries that are approaching accession to the EU (Knöbl, Haas 2003, p.7).

During the transition period, the IMF membership for the Baltic countries facilitated access to funds from regional development organizations and provided an important signal to foreign investors that seek a stable economic climate (Erikson 2003, p.151).

In 2009, with cumulative output declines of 20–25 percent from their peak levels, Estonia, Latvia and Lithuania were more severely affected by the turmoil in global trade and financial markets than any other region in the world. They experienced a collapse of credit and demand, and a dramatic swing in the current account, yet an outright banking crisis was avoided. At the same time, unemployment surged and earnings fell, highlighting the high social cost imposed by the crisis and subsequent adjustment (Purfield, Rosenberg 2010, p.3).

Therefore, the Baltic states had no choice but to implement fiscal consolidation that was unprecedented by historical and international standards. In Latvia, IMF-led lending package included across-the-board reductions in current and non-EU financed capital budgets (the reductions were particularly deep, with, for example, the education and health ministry budgets being reduced by one-half and one-third) and the phasing-in of structural reforms to ensure a more sustainable reduction in spending to affordable levels. In December 2008, Latvia signed an agreement with the IMF, the EU and a number of neighbouring countries, which agreed to make 7.5 billion euro available to Latvia. (Purfield, Rosenberg 2010, pp.14-22). Estonia and Lithuania avoided bailout and recovered without the financial support from the IMF.

Austerity policies have subsequently become the subject of heated debates in academic and policy-oriented circles. Proponents argue that austerity restored stability and confidence and facilitated an internal devaluation that restored competitiveness, thus forming the basis for a quick return to growth. Critics point to the social costs of

subdued income levels and continued high unemployment five years after the outbreak of the crisis and argue that exchange rate depreciation and expansionary fiscal policies would have been beneficial (Staehr 2013, p.301).
Many believe that globalization is driven by a set of rules and self-interested institutions and that the policies are not designed to benefit them but to benefit rich industrial countries and their global corporations (Cavanagh, Mander 2002, p.31-32), however one needs to admit that international financial institutions are undeniably vital actors in managing the global economy and promoting economic development (Erikson 2003, p.151).

3.2.2 World Trade Organization

In the first decade of their independencies Lithuania, Latvia and Estonia became signatories of the General Agreement to Tariff and Trade (GATT) and after ratifying the WTO arrangements, became members of the WTO. On October 14, 1998, Latvia became the first Baltic state that joined the WTO, followed by Estonia on November 13, 1999 and Lithuania on May 31, 2001[20]. There was WTO working party established and extensive negotiations carried out in each country before joining the WTO. The countries had to agree to bring their economic and trade regimes into conformity with the WTO rules and obligations in all areas, agreeing to follow the same global rules governing imports, exports and foreign investments that most countries in the world were following.[21]
In 1990s, from the perspective of the Baltic states WTO represented a powerful attraction for countries in transition and they treated WTO membership as a "stamp of approval" of their policies and the admission into the international community – a feat quite important for the countries that have been isolated from world markets for more than 50 years (Bachetta, Drabek 2002, p.2). Reason for that - governments often faces a "credibility gap" in trying to convince foreign and domestic investors and the rest of the business community about their commitments to particular policies. By framing the countries' concessions into legal commitments, the WTO Membership provides

[20] Members and Observers, WTO, http://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm [accessed April 15 2014]
[21] Accessions, WTO, http://www.wto.org/english/thewto_e/acc_e/acc_e.htm [accessed April 2014]

powerful guarantees of governments' policy directions. It is particularly important and present in the case of Estonia, Latvia and Lithuania due to their history of central planning and political instability (Bachetta, Drabek 2002, p.10). The WTO membership gives stability and reliability to these countries for trade partners and investors. The Baltic states trade with the third countries has become more liberal, transparent and predictable, while Lithuania, Latvia and Estonia – more attractive to foreign investment.
The WTO has 159 members by April, 2014, however there are ongoing negotiations with other countries to join the organization. The WTO derives most of the income for its annual budget from contributions by its members. These are established according to a formula based on their share of international trade. In 2013, Estonian contribution to the WTO budget was 0.09 percent, Latvian contribution – 0.08 percent and Lithuanian – 0.14 percent.[22] The WTO is usually described as a "member-driven" organization, meaning that the members and not the WTO secretariat are mainly responsible for setting the agenda and carrying out the functions of the organization. One of the important tasks of the WTO is to monitor and research the trade policies of the members. The organization consists mainly of a set of rules intended to promote trade between member countries, and in particular to provide for non-discrimination in trading relations (Ravenhill 2008, p.162).

Small countries like Estonia, Latvia and Lithuania cannot significantly affect global economic and political processes, therefore it is advantageous to be a part of the WTO, thereby gaining greater influence in various processes and disputes that may arise with trade issues. It is beneficial for all three Baltic countries that their main foreign trade partners like Russian Federation, Ukraine, Norway, and Belarus are also members of the WTO and committed to ensure the predictability of trade regime and reduce restrictions on import and export. Also it is ensured that goods manufactured by Estonia, Latvia and Lithuania do not meet discrimination in export markets (customs tariffs, subsidies, standards and other trade regulations) by other WTO members. However, inequalities exist between such multi-shaped member states which sometimes result in violation of trade rules and discrimination of smaller countries.

It can be noted that the EU is regulating much more aspects of economic life of the Baltic countries than the WTO, since it regulates in a much more detailed way than the

[22] WTO Trade profiles, 2013, http://www.wto.org/english/res_e/booksp_e/trade_profiles13_e.pdf [accessed 1 April 2014]

WTO. And the European Commission — the EU’s executive arm — represents and speaks for all EU member States at almost all WTO meetings[23].

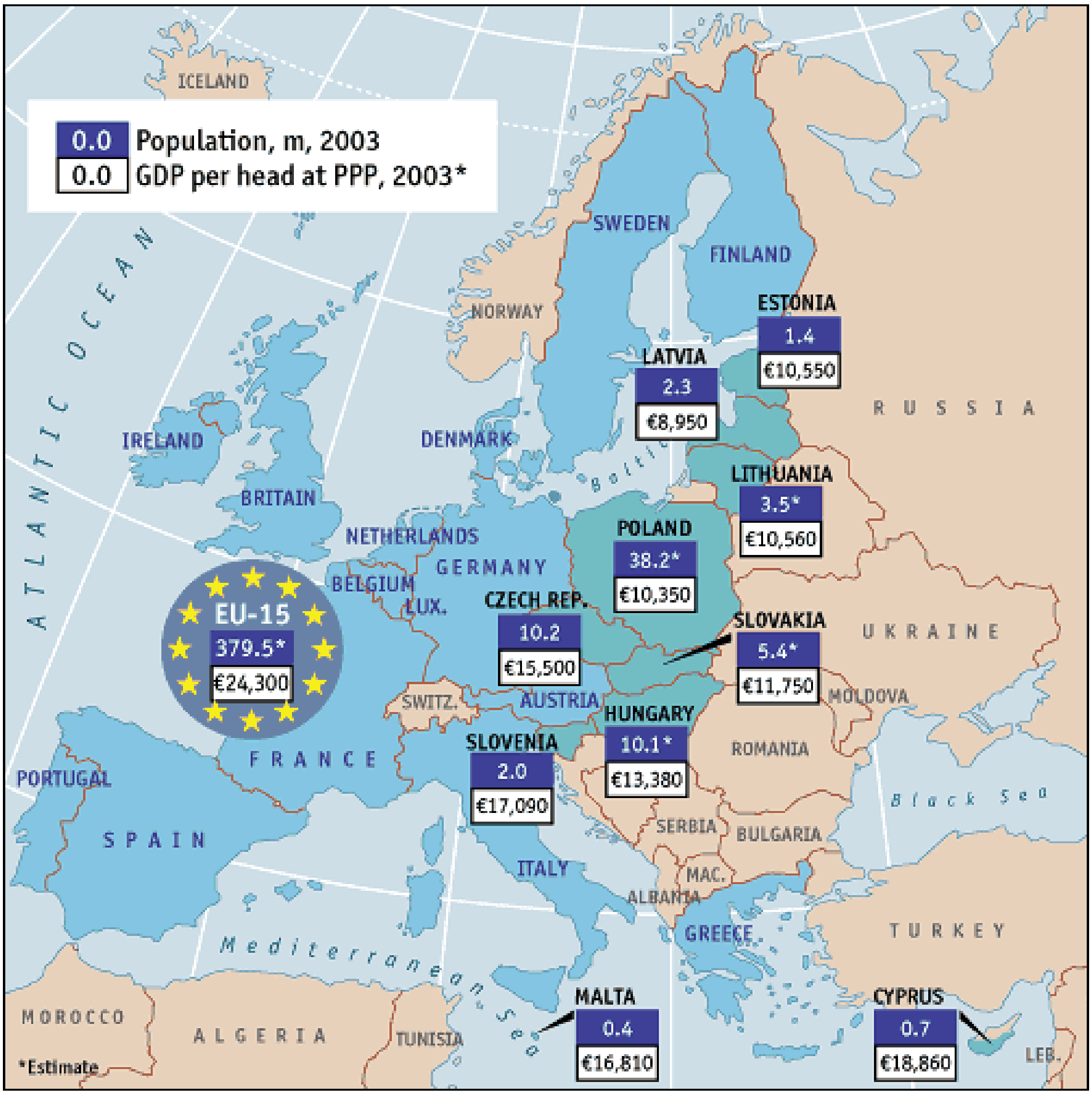
3.2.3 European Union

What began as a purely economic union after II World War has evolved into an organization spanning policy areas, from development aid to environment. The EU is the regional organization which has the most palpable effect on every EU citizen in everyday life. Thanks to the abolition of border controls between EU countries, people can travel freely throughout most of the continent. And it's become much easier to live and work abroad in Europe. The single or “internal” market is the EU's main economic engine, enabling most goods, services, money and people to move freely. The core values of the EU are human dignity, freedom, democracy, equality, the rule of law and respect for human rights.[24]

In 2004, Estonia, Latvia and Lithuania became member states of the EU. All three countries made huge efforts to reform their economic legislation in the framework of their integration in the EU. The EU is based on the rule of law: everything that it does is founded on treaties, voluntarily and democratically agreed by all member countries. These binding agreements set out the EU's goals in its many areas of activity. However, in a lot of cases, unanimity of the member states is not required, which implies that the member states can be bound by rules to which they did not agree. EU regulations also have a direct effect and have supremacy over national legislation and EU case law is binding upon the member states. In addition, the standards set by the EU automatically incorporate part of the rules and the main principles of the WTO.

[23] The European Union and the WTO, http://www.wto.org/english/thewto_e/countries_e/european_communities_e.htm [accessed 24 April 2014]
[24] How the EU works? http://europa.eu/about-eu/index_en.htm [accessed 24 April 2014]

Figure 3.8: Enlargement of the EU in 2004



Source: A May day milestone, 2004, Economist, http://www.economist.com/node/2628203 [acessed 2 April 2014]

As shown in Figure 3.8 the Baltic states economically were lagging behind the other EU candidate countries in 2003. Among them, Latvia had the lowest GDP per head based on purchasing-power-parity (PPP) equal to 8 950 EUR, while GDP per head at PPP of Slovenia, Malta and Cyprus was almost double. Estonia and Lithuania did not have significantly higher rates than Latvia. It can be explained by recent historical events and transition period in the Baltic states. Joining the EU, along with global events and developments helped the Baltic states to achieve higher GDP per head based on PPP by

2013: 16 492 EUR (22 731 USD) in Estonia, 14 064 EUR (19 385 USD) in Latvia and 16 533 EUR (22 787 USD) in Lithuania.[25]

EU funding and grants are very essential for economies and overall development of the Baltic states. Through period from 2000 to 2006 about 7 billion euro was allocated to the Baltic states. The aim of the Instrument of Pre-Accession Assistance is to enhance the efficiency and coherence of aid by means of a single framework in order to strengthen institutional capacity, cross-border cooperation, economic and social development and rural development. In addition, EU structural funds and Cohesion fund aim to reduce regional disparities in terms of income, wealth and opportunities. Europe's poorer regions receive most of the support, but all European regions are eligible for funding under the policy's various funds and programmes. For planning period 2007-2013 EU structural funds and Cohesion fund allocation in Lithuania was 6.9 billion EUR, in Latvia 4.6 billion EUR and in Estonia 3.45 billion EUR.[26] EU financing is targeted to cover areas like education, health, consumer protection, environmental protection, science and innovations and others. Although implementation of these funds is within the member states' competence, the EU provides the necessary directions and guidelines for qualification of projects.

All EU member states are part of Economic and Monetary Union and coordinate their economic policy-making to support the economic aims of the EU. However, a number of Member States have taken a step further by replacing their national currencies with the single currency – the euro. In fact, the EU member states (except Denmark and the United Kingdom) are obliged to join the eurozone. Currently 18 EU countries have adopted the euro as their currency. Estonia joined the euro area on January 1, 2011 and Latvia on January 1, 2014. Lithuania’s national target is set to join the euro zone on January 1, 2015. EU member states have to meet certain criteria in order to adapt the euro. The economic entry criteria are intended to ensure economic convergence – they are known as the “convergence criteria”[27]. Also Estonia and Latvia ensured price

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[25] World Economic Outlook Database, IMF, https://www.imf.org/external/pubs/ft/weo/2013/01/weodata/download.aspx [accessed 2 April 2014]

[26] Working for regions, EU regional policy 2013, http://ec.europa.eu/regional_policy/sources/docgener/presenta/working2008/work_en.pdf [accessed 2 April 2014]

[27] Euro area member states, http://www.eurozone.europa.eu/euro-area/euro-area-member-states/ [accessed 2 April 2014]

stability, soundness and sustainability of public finances, as well as exchange-rate stability to become part of the eurozone.

3.2.4 Organization for Economic Co-operation and Development

The OECD was officially born on 30 September 1961. Other countries joined in, starting with Japan in 1964. Today, 34 OECD member countries worldwide regularly turn to one another to identify problems, discuss and analyze them, and promote policies to solve them. Dani Rodrik (2011) states that "the OECD is a rich-country club established in 1961 that has enormous agenda-setting and legitimizing powers even though it exercises no formal sanctions".

In May 2007, OECD countries agreed to invite Estonia to open discussions for membership of the OECD. The accession procedure is complex and usually long, as it involves a series of examinations to assess a country's ability to meet OECD standards in a wide range of policy areas. Accession to the organization follows an invitation from the OECD Members, after they have reached a political consensus.[28] On December 9 2010, Estonia became a member, once necessary formalities, including parliamentary approval, were completed. Estonia is the first former Soviet republic to join the OECD.

The Estonian fiscal position is much better than in many OECD countries, the country stands out for having a rather lean government sector and the authorities are striving for efficient use of existing resources.[29]

Also Lithuania and Latvia have target to strengthen their global positions by becoming a members of the OECD. Review of situation and decision on Lithuania's membership will be taken in 2015.[30] The country is strengthening its relationship with the OECD to arrive to the 2015 benchmark in good shape.

The OECD has also set out a path for Latvia's accession to the organization, reinforcing a commitment to extend its global membership. The OECD opened accession discussions with Latvia in 2013. By February 2014 the country has elaborated the Initial Memorandum setting out Latvia's position on some 250 OECD legal instruments. This

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[28] OECD enlargement, http://www.mfa.gov.lv/en/policy/economic/oecd/OECD-enlargement/[accessed 4 April 2014]

[29] Estonia and OECD, http://www.oecd.org/estonia/estoniaandtheoecd.htm [accessed 2 April 2014]

[30] Lithuania and OECD, http://www.oecd.org/countries/lithuania/president-of-lithuania-mrs-dalia-grybauskait.htm [accessed 4 April 2014]

will allow the launch of the technical reviews in OECD committees examining Latvia's legislation, policy and practice to assess its alignment with OECD standards and best practices.[31]

The Baltic states sees membership in the OECD as an opportunity for further enhancing structural reforms, implementing social and economic policies, improving services to its citizens and learning from on-going reforms in other countries. Also, it is regarded strategically important due to the opportunities of participation in the global economic agenda and share of experience and best practices.

3.2.5 North Atlantic Treaty Organization

Within the NATO, twenty-eight members contribute to promoting security and stability through diplomatic, political and military means. They are committed to the principle of collective defence, which means that an attack against one member or more is considered as an attack against all. NATO also develops partnerships with non-NATO countries and is involved in crisis management operations and missions.[32] All three Baltic states are also members of NATO since 2004 and they are the only former Soviet republics that have joined this intergovernmental military organization. Estonia, Latvia and Lithuania had to make a lot of efforts in order to be granted the NATO membership. They were less qualified than other countries and their aspirations for NATO enjoyed less political support in the West. West worried about strong Russian opposition to Baltic NATO membership. Others worried whether the Baltic states could be defended given their exposed situation. However, the Baltic states were tirelessly pressing the Administration on how it intended to handle the Baltic issue in connection with the NATO enlargement. Baltic countries were admitted because of their willingness and commitment to do whatever it takes to be granted membership and the emerging strategic partnership between Russia and the USA (Urbelis 2003).

Estonia is home to the NATO Cooperative Cyber Defence Centre of Excellence (CCD COE). The other two Baltic states are listed as Contributing Nations, providing

[31] Latvia takes first step in accession discussions with OECD, OECD, http://www.oecd.org/countries/latvia/latvia-takes-first-step-in-accession-discussions-with-oecd.htm [accessed 4 April 2014]

[32] What is NATO?, NATO, http://www.nato.int/nato-welcome/index.html [accessed 5 April 2014]

personnel and finances to the CCD COE. However, whereas Lithuania and Estonia participate in no further COEs other than the CCD COE, Latvia also participates in the work of the Civil-Military Cooperation COE in Netherlands.[33] Baltic countries have also been militarily engaging in wars in Iraq, Afghanistan and Balkans.

[33] Keeping the Baltic Balance: Participation in NATO Centres of Excellence, 2012, http://www.lai.lv/en/blogs/keeping-the-baltic-balance-participation-in-nato-c/ [accessed 5 April 2014]

3.3 SOCIAL ANALYSIS

Apart from the political and economic aspects of globalisation, it is no less important and interesting to consider the relationship between social policy and globalisation, and social aspects of globalisation. The social dimension of globalization refers to the impact of globalization on the life and work of people, on their families and their societies. Concerns and issues are often raised about the impact of globalization on employment, working conditions, income and social protection. The social dimension of globalization also includes security, culture and identity. These will however, not be assessed as measurements in this paper.

There are no doubts that globalization brings potential for development and wealth creation. But there are many different views and perceptions among people as they are concerned about its social impact. Some argue that the present model of globalization has created problems such as unemployment, inequality and poverty (Stiglitz, Rodrik), while others argue that globalization helps to reduce these issues (Friedman, Dollar, Kray).While some people benefit from the waves of globalization, others suffer from it. These problems predated globalization of course, but it is clear that for globalization to be politically and economically sustainable, it must contribute to their reduction. Hence, the goal of globalization is what meets the needs of all people (International Labour Organization).

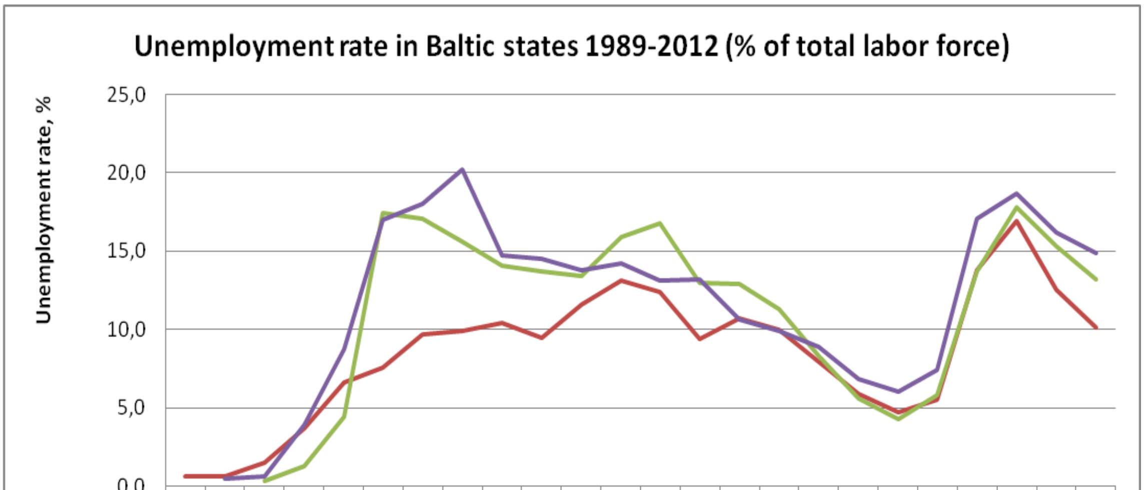
Concerns about increasing income inequalities in the world have become more and more widespread over the past 20 years. In the pre-globalisation period, the autonomy of managing national economies gave states the option to determine their own destiny. But liberalisation of the economy at the macro level leads to increasing inequality between and within countries, growth of poverty and increased level of vulnerability of people due to social risks (crime, unemployment)[34]. We have to acknowledge that Estonia, Latvia and Lithuania cannot succeed alone in the globalizing world, but it depends on what is happening in other countries, especially in those of the EU. All this applies to the social dimension of the globalization as well.

[34] Are we growing unequal?, OECD, p.1-2, http://www.oecd.org/els/soc/41494435.pdf [accessed 14 April 2014]

3.3.1 Unemployment tendencies

During the transition the large-scale employment shifts took place in the Baltic States. After regaining the independence the activity as well as employment rates fell dramatically in the Baltic States and the unemployment started to increase. While the largest increase in the unemployment in Estonia and Lithuania took place in 1991-1992, in Latvia the sharp increase in unemployment rates continued also in 1993-94 (see Figure 3.9). The unemployment continued increasing in 1995 as a result of the banking crisis, when several commercial banks went bankrupt and depositors lost all of their money. Small companies were affected by the banking crisis the most, and people working there were not always provided with social guarantees by their employers allowing them to receive an unemployment benefit. All of these events happening as a result of transition to market economies which is a by product of creeping globalisation, in an era when the labour markets in the Baltic states were static.

Figure 3.9: Unemployment rate in Baltic states 1989-2012 (% of total labor force)



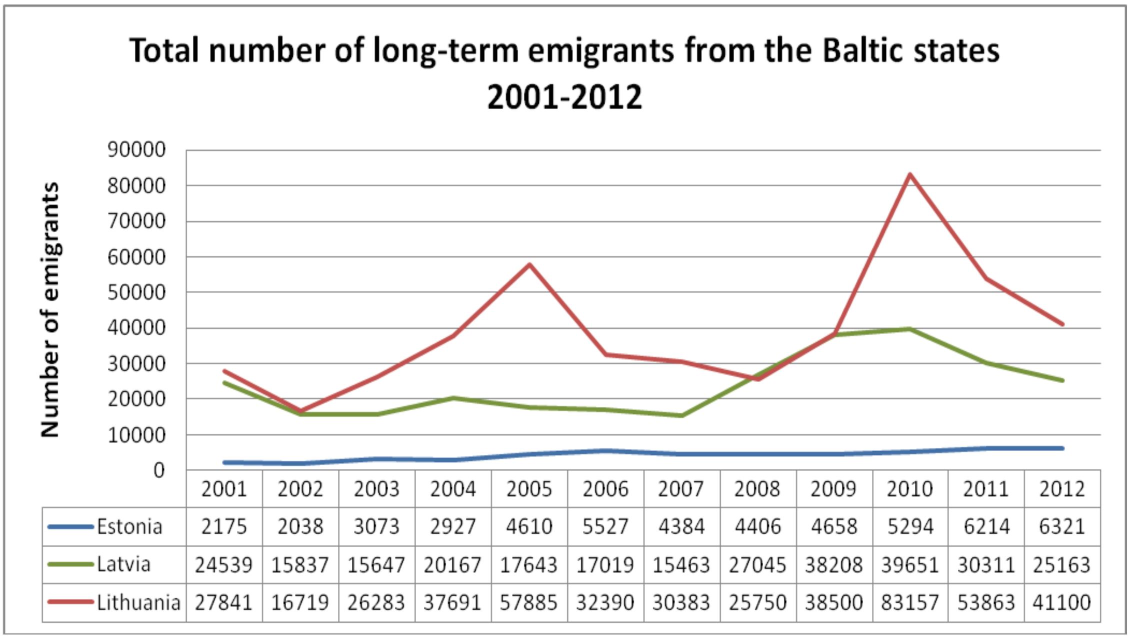
	89	90	91	92	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08	09	10	11	12
Estonia	0,6	0,6	1,5	3,7	6,6	7,6	9,7	9,9	10,4	9,5	11,6	13,1	12,4	9,4	10,7	10,0	7,9	5,9	4,7	5,5	13,8	16,9	12,5	10,1
Lithuania			0,3	1,3	4,4	17,4	17,1	15,6	14,1	13,7	13,4	15,9	16,8	13,0	12,9	11,3	8,3	5,6	4,3	5,8	13,7	17,8	15,3	13,2
Latvia		0,5	0,6	3,9	8,7	17,0	18,0	20,2	14,7	14,5	13,8	14,2	13,1	13,2	10,6	9,9	8,9	6,8	6,0	7,4	17,1	18,7	16,2	14,9

Source: World Bank, Unemployment, total (percentage of total labor force), http://data.worldbank.org/indicator/SL.UEM.TOTL.ZS [accessed 6 April 2014]

During the transition period in Estonia the unemployment rates were lower compared to other two Baltic States, indicating the relatively higher success of the reforms done during the transition process and the higher labour market flexibility, including the occupational mobility. In contrast, Latvia around the middle of 1990s evidenced by far the biggest unemployment in the Baltic countries, unemployment reaching to 20.2 percent in 1996 (see Figure 3.9).

In the beginning of the transition process labour force decreased mainly due to the emigration by the Russian-speaking population to Russia and to a smaller extent due to the increase in inactivity as a result of the introducing pre-retirement schemes (Room, Viilmann 2003). At the same time the unemployment started to increase from zero level since during Soviet time the unemployment was basically non-existent. It should be noted that the official statistics may not fully adequately reflect the actual situation since a lot of unemployment was „hidden”. In 2000, in the Baltic states the economic boom started showing the highest growth rates in the Europe and unemployment rates begun to fall reaching extremely low levels in 2006-2007. During 2008-2010 unemployment was increasing in all three Baltic states as a consequence of the global economic crisis and recession in these countries. As the economies begun to recover in 2010, also the unemployment begun to decrease in the Baltic states.

Figure 3.10: Total number of long-term emigrants from the Baltic states 2001-2012



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Estonia	2175	2038	3073	2927	4610	5527	4384	4406	4658	5294	6214	6321
Latvia	24539	15837	15647	20167	17643	17019	15463	27045	38208	39651	30311	25163
Lithuania	27841	16719	26283	37691	57885	32390	30383	25750	38500	83157	53863	41100

Source: Eurostat, Total number of long-term emigrants, http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=0&language=en&pcode=tps00177 [accessed 6 April 2014]

Restoring the independence in 1991 led to major changes in population composition and increasing emigration, which resulted in considerable depopulation in the three Baltic states. Steady economic growth in the Baltic states at the turn of the 21st century caused emigration to decline. However, as Estonia, Latvia and Lithuania joined the EU in 2004, people found it much easier to find a job and move abroad, therefore some part of the unemployed people left their home country and took opportunity to find a job within the EU. The outflow of population reflected in high negative emigration rates and results in considerable depopulation. Very rapid growth following EU accession caused emigration rates to drop slightly. However, since 2008 emigration rates rose yet again due to the global economic crisis. While emigration increased sharply in Lithuania and Latvia since 2009, the outward flow was considerably lighter in Estonia, where the economic crisis was relatively milder and the recovery comparatively faster. Emigration destinations vary according to economic opportunities, legal barriers and geographic and linguistic proximity. Finland is the most popular country of destination among emigrants from Estonia. Latvian and Lithuanian emigrants go to the United Kingdom, Ireland, Sweden, Norway and Germany.[35]

Emigration from the Baltic states (Estonia, Latvia and Lithuania) has rapidly increased over the past years, a phenomenon that has accelerated dramatically since the three countries joined the EU. Mostly young and skilled emigrants are leaving the countries and these outflows exacerbate a demographic situation in which Baltic countries face a rapidly ageing population and receive few immigrants themselves. Emigrants are sometimes seen as a key resource to support long-term growth in their countries of origin, not only providing remittances but contributing to development through investment, exchange, and intensification of networks[36], however high outflow of population is reflected in very high negative net migration rates and results in considerable depopulation and poses serious economic and political challenges over the long run.

3.3.2 Income inequality

Income inequality is important because of the link with education and health – and hence the capacity to live a longer and more productive life. An additional concern,

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[35] Coping with Emigration in Baltic and East European Countries, 2013, OECD http://www.keepeek.com/Digital-Asset-Management/oecd/social-issues-migration-health/coping-with-emigration-in-baltic-and-east-european-countries_9789264204928-en#page1 [accessed April 12 2014]

[36] Coping with Emigration in Baltic and East European Countries, OECD, http://www.keepeek.com/Digital-Asset-Management/oecd/social-issues-migration-health/coping-with-emigration-in-baltic-and-east-european-countries_9789264204928-en#page1 [accessed April 12 2014]

especially relevant to the transition process, is that greater inequality and poverty may not only harm individual lives, but may damage national prospects by reducing economic growth. There are many complex causes of income inequality. Certainly, globalization and technological change have led to greater competition for lower-skilled workers, while giving well-educated, higher-skilled workers increased leverage. Changes to tax rates, including favorable treatment for capital gains, also plays role, as well as globalization is associated with larger income gaps between top executives and the rest of the work force within the same company (Rodrik 2008, pp.241-247).

Table 3.1: Gini index in the Baltic states

	Estonia	Latvia	Lithuania
1989	28	26	26
1999	37	32	34
2010	31.3	35.2	35.5

Source: CIA World Factbook, Gini index, https://www.cia.gov/library/publications/the-world-factbook/fields/2172.html [accessed 8 April 2014]

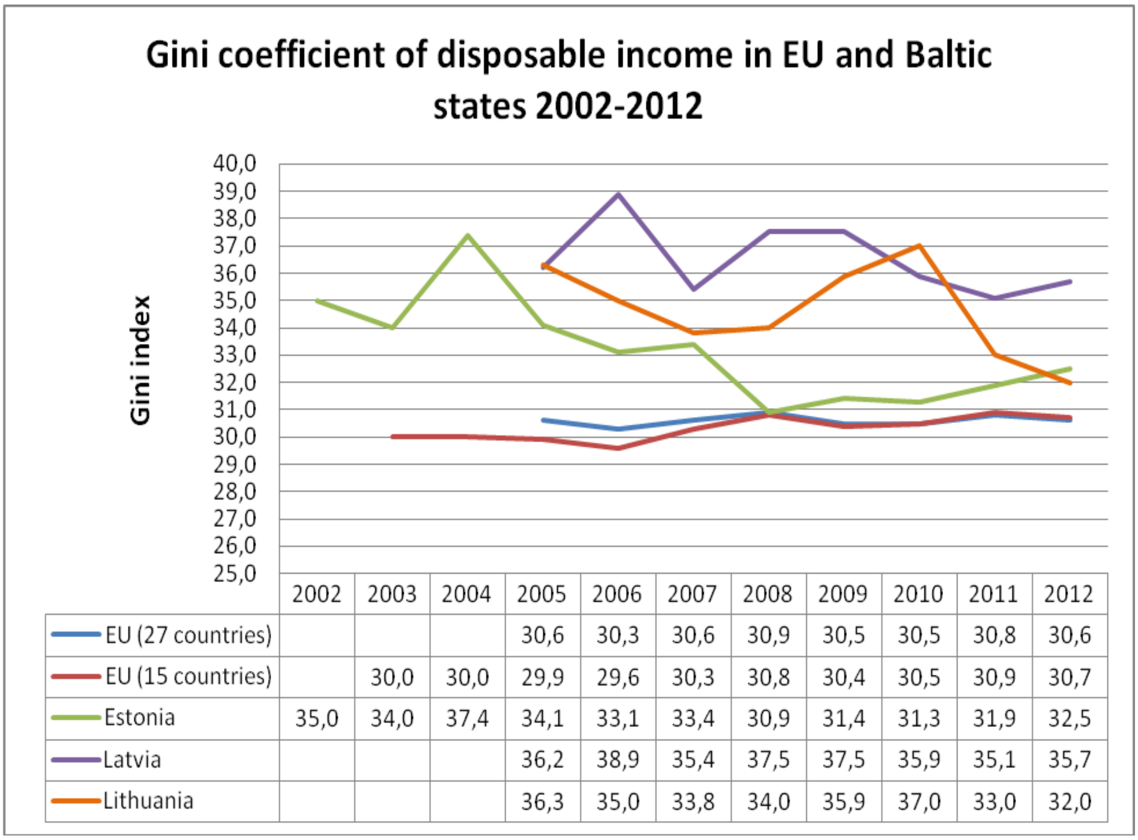
Gini index measures the degree of inequality in the distribution of family income in a country. The more nearly equal a country's income distribution, the lower its Gini index[37]. In order to compare Gini index of 1989 with more recent data, the CIA statistical information is used. Differences in income between households in the communist period were small compared to those in market economies (see Figure 3.11), meaning that the move from a planned system to a market system resulted in large increases in these differences. In Estonia, Latvia and Lithuania inequality has increased and income became more unequally distributed comparing the statistics of 1989 and 1999. In Estonia, it jumped from 28 to 37. The rapid increase in income inequality can be partly explained by the growing differentiation of wages according to education and other individual qualifications. In Latvia, Gini index of 26 in 1989 increased to 32 in 1999 and in Lithuania, it increased from 26 to 34, respectively. In following decade, Gini index continued to rise in Lithuania and Latvia, however it decreased in Estonia.

Main reason for inequality in the 1990s was lack of economic reform that was accompanied by a variety of factors that widen differences in incomes. UNICEF report "A decade of transition" (2001, p.10-11) states that in the Baltic states income became

[37] Distribution of family income – Gini index, CIA, https://www.cia.gov/library/publications/the-world-factbook/fields/2172.html [accessed 20 April 2014]

more unequally distributed due to the following reasons: huge falls in the share of wages in total income; growing importance of informal incomes; large reductions in government expenditure due to an inability to collect (or an unwillingness to reform) sufficient taxes; failure to stabilize the macro economy, notably to control inflation; capture of business and government, and outright corruption.

Figure 3.11: Gini coefficient of disposable income in EU and Baltic states 2002-2012



	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
EU (27 countries)				30,6	30,3	30,6	30,9	30,5	30,5	30,8	30,6
EU (15 countries)		30,0	30,0	29,9	29,6	30,3	30,8	30,4	30,5	30,9	30,7
Estonia	35,0	34,0	37,4	34,1	33,1	33,4	30,9	31,4	31,3	31,9	32,5
Latvia				36,2	38,9	35,4	37,5	37,5	35,9	35,1	35,7
Lithuania				36,3	35,0	33,8	34,0	35,9	37,0	33,0	32,0

Source: Eurostat, Gini coefficient (number), http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&language=en&pcode=tessi190 [accessed 8 April 2014]

Gini index of Estonia, Latvia and Lithuania is higher than on average in EU27 and EU15 during the period 2002-2012 (see Figure 3.11). Part of the explanation of comparably high income inequality in the Baltic States during the reference period is related to the tax and transfer policies. Baltic countries have higher inequality than other EU countries because of the smaller role of direct taxes and public transfers in redistributing incomes within these countries (Zaidi 2009, p.14). The overall trend shows that inequality has decreased in all Baltic countries comparing 2005 and 2012, however the decrease is not very significant and has been fluctuating during period

2002-2012 due to the global financial crisis and economic recession. On average, Estonia is the most equal of all the Baltic countries and Latvia – the most unequal. Inequality in Estonia was decreasing until 2008 when it reached level of the EU and Gini index of 30.9, however from 2008 onwards when the Baltic States experienced deep recession the Gini coefficient increased in Estonia and also Lithuania. In 2008 and 2009, Gini index in Latvia was 37.5 but has fallen by two points by 2012.

Income inequality in the EU countries is in general quite low compared to other countries in the world in large part due to the strong redistributive roles of their national tax and benefit systems, however Latvia, Lithuania, and Estonia have fairly high income inequality, at least when compared to other EU countries. Main reasons behind it are greater wage differences, higher unemployment rates, building-up of wage arrears, reduced public spending on transfers, as well as rapid inflation during the dynamic period of 1990-2012. However, income inequality in the Baltic states is still much lower than in most other countries in the world.

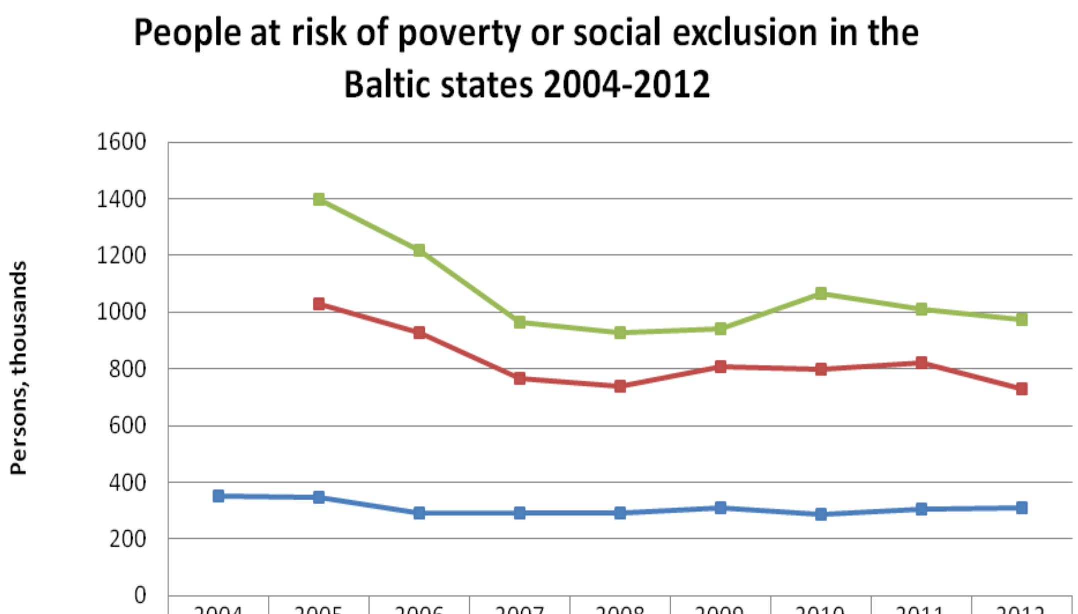
Inequality is dysfunctional and it slows economic growth, results in health and social problems and generates political instability, therefore it is a big concern in all countries to reduce income inequality while boosting the economy.

3.3.3 Europe 2020 indicators

Europe 2020 is the EU's ten-year growth and jobs strategy that was launched in 2010. Five headline targets have been set for the EU to achieve by the end of 2020. These cover employment; research and development; climate/energy; education; social inclusion and poverty reduction.[38] Europe 2020 is closely tied to social developments in the Europe and promotes social inclusion, in particular through the reduction of poverty, by aiming to lift at least 20 million people out of the risk of poverty and social exclusion. Latvia and Lithuania stand out among the EU countries with particularly high share of population in the risk of poverty and social exclusion (see Figure 3.12).

[38] Europe 2020 in a nutshell, EU, http://ec.europa.eu/europe2020/europe-2020-in-a-nutshell/index_en.htm [accessed 9 April 2014]

Figure 3.12: People at risk of poverty or social exclusion in the Baltic states[39]



	2004	2005	2006	2007	2008	2009	2010	2011	2012
Estonia	352	347	293	293	291	312	289	307	311
Latvia		1027	927	765	740	808	798	821	731
Lithuania		1400	1217	967	928	943	1068	1011	975

Source: Eurostat, People at risk of poverty or social exclusion, http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=t2020_50&plugin=1 [accessed 9 April 2014]

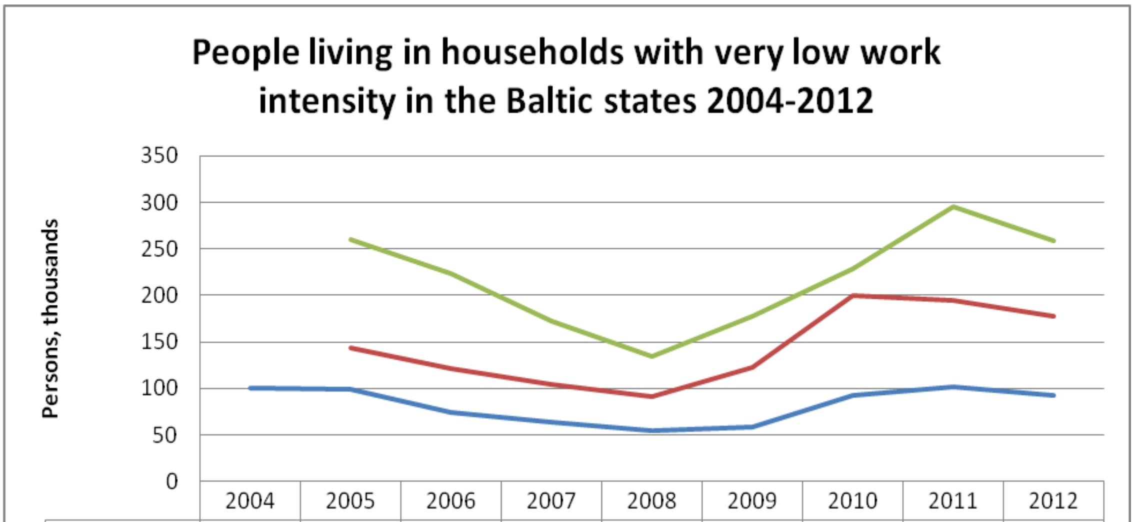
Period of economic development and growth of welfare (2000-2007) resulted in improvements in living conditions, material, social and physical security and higher satisfaction of life (Trumm 2010; p.44-49). The substantial decline in the number of persons at risk of poverty or social exclusion (see Figure 3.12) indicates that the economic growth impacted positively those social groups whose standard of living was the lowest. Global economic crisis (since 2008) resulted in high unemployment rates and increase in risk of poverty or social exclusion. In 2012, Estonia's population is 1.339 million with 311 thousand people at risk of social exclusion, Latvia's population is 2.025 million with 731 thousand people at risk of social exclusion and Lithuania's

[39] Note:This indicator corresponds to the sum of persons who are: at risk of poverty or severely materially deprived or living in households with very low work intensity. Persons are only counted once even if they are present in several sub-indicators. At risk-of-poverty are persons with disposable income below the risk-of-poverty threshold, which is set at 60 % of the national median disposable income (after social transfers). Severely materially deprived persons have living conditions severely constrained by a lack of resources, they experience at least 4 out of 9 following deprivations items: cannot afford i) to pay rent or utility bills, ii) keep home adequately warm, iii) face unexpected expenses, iv) eat meat, fish or a protein equivalent every second day, v) a week holiday away from home, vi) a car, vii) a washing machine, viii) a colour TV, or ix) a telephone. People living in households with very low work intensity are those aged 0-59 living in households where the adults (aged 18-59) work less than 20% of their total work potential during the past year.

population is 2.986 million with 975 thousands people at risk of social exclusion. Around one third of Lithuania's population is at risk of poverty or social exclusion since they live in households with very low work intensity or are materially deprived. As the European Commission notes, the causes of such developments have not received the required policy attention. According to the recent Statistics Estonia study "Poverty in Estonia" (2010), the increase in unemployment has been the main contributor to increasing poverty and a good education is an important presumption for the prevention of poverty.

People living in households with very low work intensity have been recognised as one of the most challenging groups in terms of social cohesion within the EU. They are often dependent on social transfers and have difficulties in accessing basic goods and services. They are at great risk of permanently losing the link to the labour market, falling into poverty and becoming socially excluded. As a result, the number of 'people living in households with very low work intensity' is a component of the Europe 2020 strategy.

Figure 3.13: People living in households with very low work intensity in the Baltic states 2004-2012[40]



	2004	2005	2006	2007	2008	2009	2010	2011	2012
Estonia	101	99	74	64	55	58	92	102	93
Latvia		143	121	104	91	122	200	195	178
Lithuania		260	223	172	135	178	229	296	259

Source: Eurostat, People living in households with very low work intensity, http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=t2020_51&plugin=1 [accessed 9 April 2014]

[40] Note: People living in households with very low work intensity are people aged 0-59 living in households where the adults work less than 20% of their total work potential during the past year.

In Estonia, Latvia and Lithuania share of people in jobless or very low-work intensity households decreased during the period of economic growth from 2005 to 2007 and started to increase in 2008 as all three countries were hit by economic crisis (see Figure 3.13). In particular, the share of people living in households with very low work intensity increased in 2010 compared to 2008 in all Baltic countries. In 2012 compared to 2008, number of people living in households with very low work intensity increased by 38 thousands in Estonia, by 87 thousands in Latvia and by 124 thousands in Estonia. It almost doubled in all three countries. One of the main reasons for the increase in in-work poverty (i.e. those people working but living under the poverty threshold) is low labour market participation of all household members. Those who work on part-time or temporary contracts are more likely to experience joblessness and poverty as stated in European Commission issue paper “Jobless households – the link between employment and poverty”.

4. FINDINGS

After the collapse of the USSR in 1991, Estonia, Latvia and Lithuania regained their independence and begun the process of shifting from centrally planned economies to market economies. Baltic states went through a hard transition process by liberalizing and opening their economies to the international markets, and implementing complex market-oriented structural reforms. In the beginning of 21st century, the Internet and mobile cellular phones significantly increased the flow of information, improved productivity and efficiency and provided new opportunities for the businesses in the Baltic states. Trade openness ratio shows that Estonia, Latvia and Lithuania were more integrated in the world economy in 2012 compared to 1995 Estonia's trade-to-GDP ratio was 154.63 percent in 2012, up from 116.13 percent in 1995. Latvia's trade-to-GDP ratio was 109.19 percent in 2012, up from 59.59 percent in 1995. And Lithuania's trade-to-GDP ratio was 145.9 percent in 2012, up from 80.39 percent in 1995. Exports of goods and services have consistently increased since regaining the independence, especially after EU accession in 2004. In 2011, in Estonia the value of total exports compared to 1995 increased by 22 percent, in Latvia - by 16 percent and in Lithuania – by 30 percent. After joining the EU and resultant increase in investors' confidence, FDI flowed steadily into the financial intermediation, manufacturing, and real estate sectors, however it continued until the global financial crisis in 2008. Sharp decline in FDI during the period of 2007-2009 as a result of global financial crisis represents the negative immediate impact of globalization on domestic economies during a global downturn. From 1992 to 2012, increase in FDI net inflows was 1556.2 million USD in Estonia, 1046.9 million USD in Latvia and 543.82 million USD in Lithuania. During last two decades there has been also an increase in GDP and GDP per capita volumes showing economic progress in the Baltic States. In 2012, GDP in Estonia has increased by 18.61 billion USD compared to 1995, in Latvia GDP has increased by 22.65 billion compared to 1987 and in Lithuania it has increased by 31.83 billion USD compared to 1990. The common trend of GDP per capita in Estonia, Latvia and Lithuania indicates growth in steady pace until 2008 when it started to suffer from the global financial crisis. In 2010, three Baltic states had all of their population living in regions with an average GDP per inhabitant 75 percent below the EU-27 average. However, the same year they started to recover from the crisis. In 2012, in Estonia GDP per capita increased by 14 088 USD compared to 1995, in Latvia GDP per capita increased by 11 832 USD compared to 1987 and Lithuanian GDP per capita increased by 11 342 USD compared to 1990.

In 2009, Estonia, Latvia and Lithuania were severely affected by the turmoil in global trade and financial markets with cumulative output declines of 20-25 percent from their peak levels. They experienced a collapse of credit and demand, and a dramatic swing in the current account. At the same time, unemployment surged and earnings fell, highlighting the high social cost imposed by the crisis. All Baltic countries had to implement sizeable fiscal consolidation that was unprecedented by historical and international standards. In Latvia, IMF-led lending package included reductions in current and non-EU financed capital budgets and the phasing-in of structural reforms. Estonia and Lithuania avoided bailout and recovered without the financial support from the IMF. There are both supporters and critics to austerity policies implemented by the IMF in these countries in order to recover from the crisis. Supporters believe that they form the basis for quick return to growth, but critics point to social costs of subdued income levels and unemployment.

Estonia, Latvia and Lithuania are members of the main important international organizations: IMF, WTO, EU, NATO and OECD. All three Baltic countries became members of the IMF and also the WB in 1992. During the 1990s, IMF helped these countries in transition process from central planning to market-driven economies and also provided an important signal to foreign investors who were seeking for new markets and stable economic climate. During the global crisis, IMF was helping Baltic countries to overcome the economic recession in the region.

Latvia joined the WTO in 1998, Estonia in 1999 and Lithuania in 2001. From the perspective of the Baltic states, WTO membership is seen as a “stamp of approval” of their policies and the admission into the international community. Especially, as these countries were isolated from world markets for more than 50 years. The WTO membership implies that goods manufactured by Estonia, Latvia and Lithuania do not meet discrimination in export markets by other WTO members while the countries have become more attractive to foreign investment.

In 2004, Estonia, Latvia and Lithuania became member states of the EU, organization which has the most palpable effect on every EU citizen in everyday life. Travelling, living, studying and working abroad have become much easier within the EU borders. All three countries made huge efforts to reform their economic legislation in the framework of their integration to the EU. The EU is based on the rule of law: everything that it does is found on treaties, voluntarily and democratically agreed by all member countries. However, in many cases, unanimity of the member states are not required, which implies that the member states can be bound by rules to which they did not agree. The Baltic countries receive financial support from EU structural funds and Cohesion fund aimed to reduce regional disparities in terms of income, wealth and opportunities. As EU member states Estonia, Latvia and Lithuania are obliged to replace their national currencies with the euro and in order to do that EU member states have to meet certain requirements, including inflation rate, government budget deficit, debt-to-GDP ratio. Estonia adopted euro in 2011 and Latvia in 2014. Lithuania's national target is set to join the euro zone in 2015.

In 2007, the OECD countries agreed to invite Estonia to open discussions for membership of the OECD. In 2010, the goal was achieved and Estonia became the first former Soviet republic to join the OECD. Estonian authorities are striving for efficient use of existing resources and country's fiscal position is better that in many other OECD. Also Latvia and Lithuania have target to strengthen their global positions by becoming members of the OECD countries. The Baltic states see membership of the OECD as a matter of strategic importance due to the opportunities of participation in the global economic agenda and share the experience and best practices. The OECD opened accession discussions with Latvia in 2013. But review of situation and decision on Lithuania's membership will be taken in 2015.

Since 2004 the Baltic states are also members of NATO comprising of total 28 countries and they are the only former Soviet republics that have joined this intergovernmental military organization. Initially, they were not accepted to the NATO as they were less qualified than other countries and their aspirations for the NATO enjoyed less political support in the West. However, Baltic countries were admitted because of their willingness and commitment to do whatever it takes to be granted membership and the emerging strategic partnership between Russia and the USA.

Disadvantages of globalization mainly concentrate on the social impact side, particularly affecting employment, income inequality and increasing poverty. After regaining independence the activity as well as employment rates fell dramatically in the Baltic states and the unemployment started to increase. During the transition process unemployment rates in Estonia were lower compared to Latvia and Lithuania, indicating the relatively higher success of the reforms, higher labour market flexibility, including occupational mobility. In the middle of 1990s, unemployment rate in Latvia reached 20.2 percent, while in Lithuania 15.6 percent and in Estonia 9.9 percent. In the beginning of 2000s, the economic boom in the Baltic countries started, showing the highest growth rates in the Europe and consequently unemployment rates begun to fall reaching extremely low levels in 2006-2007. During 2008-2010 unemployment was increasing in all three Baltic countries as a consequence of the global financial crisis and following recession. In 2010, unemployment in Latvia reached 18.7 percent, in Lithuania 17.8 percent and in Estonia 16.9 percent. As a result of economic crisis and EU's open borders, the emigration increased sharply in Lithuania and Latvia from 2009 onwards, however the outward flow was considerably lighter in Estonia, where the economic crisis was relatively milder and the recovery comparatively faster. In 2010, because of the long-term emigrants, population of Lithuania was reduced by 83 175, population of Latvia was reduced by 39 651 and population of Estonia was reduced by 6 214, however unofficial data might be more unsettling and alarming.

Differences in the income between households in the communist period were small compared to those in market economies, meaning that the move from planned system to market system resulted in large increases in these differences. Gini index trends shows that in Estonia, Latvia and Lithuania income has become more unequally distributed comparing the statistics of 1989 and 2012. In Latvia, Gini index increased from 26 in 1989 to 35.7 in 2012. In Lithuania, Gini index of 26 in 1989 increased to 32 in 2012. In Estonia, Gini index of 28 in 1989 increased to 32.5 in 2012. Important to note that in the Baltic states higher income inequality is seen during the crisis and recession and it gets lower when economy is growing and living conditions rise. Income inequality in EU countries is in general quite low compared to other countries in the world in large part due to strong redistributive roles of their national tax and benefit systems, however Estonia, Latvia and Lithuania have fairly high income inequality, at least when compared to other EU countries. Main reasons behind growing income inequality during the dynamic period of 1990-2012 in the Baltic states were greater wage differences, high unemployment rates, outright corruption, high share of informal incomes and failure to stabilize economy and control inflation.

Latvia and Lithuania stand out among the EU countries with particularly high share of population in the risk of poverty and social exclusion. In the beginning of 2000s, the

Baltic states experienced period of economic development and growth of welfare. It positively affected those social groups whose standards of living were the lowest. As a result of global economic crisis number of unemployed people increased during 2008-2010 leading to increase in risk of poverty and social exclusion. In 2012, the number of people at risk of poverty has decreased in the Baltic states, however it is still high considering the total population of these countries. In 2012, Estonia's population was 1.339 million with 311 thousand people at risk of social exclusion, Latvia's population was 2.025 million with 731 thousand people at risk of social exclusion and Lithuania's population was 2.986 million with 975 thousand people at risk of social exclusion. The increase in unemployment has been the main contributor to increasing poverty and a good education is an important presumption for the prevention of poverty.

In Estonia, Latvia and Lithuania share of people in jobless or very low-work intensity households decreased during the period of economic growth from 2005-2007 and begun to increase in 2008 as all three countries were hit by the economic crisis. In 2012 comparing to 2008, number of people living in households with very low work intensity increased by 38 thousands in Estonia, by 87 thousands in Latvia and by 124 thousands in Estonia. These people are often dependent on social transfers and have difficulties in accessing basic goods and services. As a result, EU ten-year growth and jobs strategy Europe 2020 sets targets to reduce the poverty by aiming to lift at least 20 million people out of the risk of poverty and social exclusion by 2020.

5. DISCUSSION AND CONCLUSIONS

This study is an attempt to analyze how being under the social and economic conditions inherited from the Soviet legacy as well as from the geo-political reality, Estonia, Latvia and Lithuania have been affected by globalization and what positive and negative effects globalization has brought to these countries.

In the beginning of 1990s after collapse of the USSR the Baltic states shifted from communism to capitalism, but capitalism does not come with a unique model ensuring economic stability and prosperity. Aiming to achieve economic growth and integration in the world economy, Baltic states liberalised and opened their economies to the international market, and implemented a significant number of difficult and complex market-oriented structural reforms. Process of transition was not easy and smooth merely because of fifty years of central planning within the USSR, but restoring national sovereignty and independence facilitated economic development and globalization processes and set the Baltic States towards Westernization. Furthermore, participation in regional and international organizations fostered global integration and allowed Baltic States to benefit from globalization on a larger scale. Estonia, Latvia and Lithuania work towards increased power within the international organizations IMF, WTO, EU, NATO and OECD, which have also positive effects in putting restrictions on national governance and policies as the Baltic States have to comply with the conditions and rules of particular organizations. Estonia being also a member state of the OECD is showing relatively better results in the economy due to its early commitment to pro-market reforms, sound policies and close ties with Nordic countries.

The study shows that globalization has brought both positive and negative effects to the Baltic States. Although globalization has contributed to the economic growth in long-term, it has also imposed high social costs on these countries. While economic indicators such as FDI, international trade, GDP and GDP per capita reflect positive progress implying that the economies are growing and living conditions are improving, on the other hand, unemployment, income inequality and people at risk of poverty or social exclusion in these countries endured a negative trend. Globalization and technological change have led to greater competition for lower-skilled workers, while giving well-educated workers increased leverage. It also means that capitalism and increased globalization nowadays bring demand for skilled labour - a determinant for further growth.

Deep economic recession during the period of 2007-2009 as a result of global crisis represents the negative immediate impact of globalization on domestic economies during a global downturn. Latvia in particular suffered Europe's worst recession. However, the EU membership changed the balance of costs and benefits compared to going it alone. Also, the right of free movement of labour within the EU allowed many Estonian, Latvian and Lithuanian workers to emigrate, serving as a safety valve for an economy under pressure. However, high outflow of population can result in considerable depopulation and pose serious economic and political challenges over the long run. Therefore, the Baltic states, especially Latvia and Lithuania, have to work on better economic and social conditions and target return policies for emigrants in order to promote returning to country of origin. Emerging scarcity of labour in the future would be unlikely to be offset by a sharp rise in immigration or fertility, so it will be more important to enhance the existing human capital and to ensure that it is productively employed.

With the world becoming more and more global and the Baltic states being more exposed to events in world markets, the future can be challenging and it is therefore important that the right economic, political and social policies are introduced in these countries. Economic growth requires a pragmatic government willing to do whatever it takes to energize the private sector. It requires using markets and globalization strategically to diversify the domestic economies. It is also clear that for globalization to be politically and economically sustainable, it must contribute to reduction of unemployment, inequality and poverty.

It can also be acknowledged that the Baltic States cannot succeed alone in the globalizing world, but they depend on what is happening in other countries, especially in those of the EU. Globalization is a tremendously positive force, but only if the Baltic States are able to properly manage it to work for them rather than against them. A thin layer of international rules that leaves substantial room for manoeuvre by national governments is a better globalization. The countries must assume responsibility for their well-being themselves and safeguard benefits of a globalization while explicitly recognizing national diversity and needs. The Baltic states need smart globalization, not maximum globalization.

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