Globalisation and Sustainable Development

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Introduction

Globalisation can be thought of as a process in which business decisions, production processes, and markets gradually exhibit more “international” characteristics and less “national” ones. Globalisation implies a wide range of underlying structural reforms (e.g., business organisation, the public-private interface, and altered consumption patterns). Technology change is also important. Globalisation is a broader concept than economic growth—globalisation contributes to economic growth, but is only one of the contributors. Population change, natural resource endowments, and cultural traditions are other important drivers of growth (Jones 1998).

Globalisation also has both endogenous and exogenous components. To the extent that globalisation is fuelled by endogenous technological change (e.g., development of the Internet), it may indeed be beyond the power of governments to control. However, globalisation is also fuelled by exogenous policy decisions of government, such as trade and investment liberalisation. To some extent, therefore, governments can influence both the pace and the direction of the globalisation process.

Although there are many ways of defining sustainable development, one that has received broad support is: “Sustainable development [is]…‘development that lasts’—i.e., a path along which the maximisation of human well-being for today’s generation does not lead to declines in future well-being….H]uman well-being [includes] not only the satisfaction of economic needs, but also aspirations for a clean and healthy environment, and preferences in terms of social development. Types of capital that sustain well-being…include natural, human, and social capital.” Sustainable development therefore has three main components: environmental, social, and economic. It also clearly has important temporal dimensions (Pearce and Barbier 2000; OECD 2001a).

The OECD has recently proposed that an appropriate framework for achieving sustainable development contains four key elements (OECD 2001a; OECD 2001b).

- Make wider use of markets. There is significant scope for expanded use of market-based approaches to provide signals to internalise environmental and social externalities in an efficient manner. On

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b The opinions expressed in this paper are those of the authors alone, and do not necessarily reflect the views of either the OECD, the United Nations, or their member countries.
the environment side, this is likely to involve more use of environmental taxes, tradable permits, and subsidy reforms.

- **Strengthen decision-making processes.** Better policy co-ordination at all levels of government could improve the efficiency and effectiveness of policy interventions. Among other things, this implies the need to better integrate environmental and social policy needs into sectoral economic policies, as well as to improve transparency and democratic participation in policy design and implementation. It also implies stronger efforts to co-ordinate policy at the international level.

- **Harness science and technology.** Scientific progress and technological development are major forces underlying rising productivity and living standards. This suggests the need to provide a business environment in which suitable incentives exist for technological innovation or diffusion. Over the long term, this implies a strong role for government in basic research activities, leaving applied research largely to the private sector.

- **Manage links to the global economy.** The global economy embodies two policy areas of particular concern for sustainable development: (1) international trade and investment flows; and (2) the particular needs of developing countries as participants in global economic activity. One major implication of these issues for sustainable development policy is that trade and investment flows need to be as compatible as possible with society’s environmental and social policy objectives. Another is that achieving global sustainable development will not be possible without the active participation of developing countries.

For reasons of space, this paper focuses on only one element of the globalisation process—links between international trade/investment liberalisation and other elements of the sustainable development paradigm.

**Trade, investment, and sustainable development: opportunities and risks**

International trade and investment promote *economic* growth and competition. In so doing, they contribute directly to poverty reduction and enhance long-term development opportunities in poorer countries. They also stimulate technology development and diffusion, and promote the structural changes necessary to make more efficient use of natural and environmental resources. This benefits citizens through lower prices, greater product diversity, and increases in the purchasing power of their wages. In recent years, countries that have had more open trade and investment policies have achieved double the annual average growth rates of others, and have attracted a larger share of foreign direct investment (FDI) (OECD 1998).

Unfortunately, many of the poorest developing countries have not been able to benefit as much as other countries from the growth induced by openness to trade and investment. Market openness is therefore not sufficient to ensure economic growth; sound macro-economic policies, as well as institutional and social stability, are also required (Rodrik 1999; OECD 2001c).

The *environmental* consequences of trade and investment activities will broadly result from the expansion of economic output (scale effects), the reallocation of production and consumption activities,
both globally and between sectors (structural effects), and the stimulation of technological development and diffusion (technology effects).

By increasing the scale of economic activity, trade and investment liberalisation may place additional pressure on the environment. In countries where environmental policies are weak or poorly enforced, these pressures could lead to reduced environmental quality. In this sense, economic liberalisation may exacerbate existing weaknesses in environmental policy regimes.

On the other hand, when trade and investment liberalisation are combined with strong regulatory frameworks to protect the environment, they can have a beneficial effect on environmental conditions. Not only will adequate environmental policies protect against negative scale effects, they may also promote positive structural effects (e.g., improved use and management of environmental resources), as well as positive technology effects (e.g., wider diffusion of environmentally-friendly technologies). Furthermore, environmental policies themselves may also contribute to economic growth. For example, the Asian Development Bank estimates that the welfare costs to China associated with environmental damage could be equivalent to 10 percent of gross domestic product (GDP). Reversing these environmental costs would directly improve economic conditions.

FDI flows to a wide range of industries, companies, and countries—some of which are careful environmental stewards, some of which are not. However, the risk of FDI flowing toward countries with low environmental standards is rather small. Environmental costs are only one of a broad number of factors (including quality of infrastructure, access to inputs, wage costs, labour productivity, political risk, and the size and growth potential of markets) that investors take into account when making location decisions. The costs of adhering to environmental regulations are also a small part (2 to 3 percent on average) of total production costs for most firms (OECD 1998; Adams 1997; UNEP and IISS 2000), although in certain resource-intensive sectors these costs may be higher. Multinational enterprises generally seek consistent environmental standards and enforcement, rather than lax environmental rules (OECD 1997). The net result is that the risk of “pollution havens” associated with economic liberalisation is sometimes overstated.

The social effects of trade and investment liberalisation come essentially from two factors—effects on labour markets and effects on the equality of income distribution. Although foreign firms clearly create employment opportunities where they trade or invest, concerns are sometimes expressed about the quality of that employment. Especially where governments compete to attract FDI, the enforcement of national laws that promote core labour standards may suffer. However, there are also major constraints to a “race-to-the-bottom” logic in labour standards (OECD 2000). As is the case with most environmental policies, core labour standards are not important determinants of investment location decisions, suggesting that policy competition between governments in core labour standards is likely to be an unproductive policy over the long term (OECD 1998).

Nor is using trade measures to encourage respect for core labour standards likely to be very effective. For example, in some circumstances, a ban on child labour may actually worsen the economic condition of households and of the children living in them. Even though a ban on the import of goods that use child labour might succeed in driving the practice out of export industries, this may simply displace that
child labour towards more informal sectors of the economy. Broadly, OECD studies suggest that subsidies to help keep children in school is likely to be a more effective approach than trade interventions per se (OECD 2000).

The other social effect of trade and investment is on the distribution of income, both within and across nations, and on poverty reduction. Trade and investment have grown significantly in recent years, at the same time that the share of the world’s population experiencing extreme poverty has fallen dramatically (from 29 percent in 1990 to 24 percent in 1998 [World Bank 2000a]). That still leaves a total of more than one billion people in poverty, and there are still important regional variations around this average. Nevertheless, it is by no means appropriate to associate trade and investment liberalisation with rising levels of poverty.

It is true that the economic growth and increased welfare associated with market liberalisation are not always distributed equally among different groups in society. Liberalisation can lead to transitional disturbances in the markets in which the poor operate. If reform boosts the demand for labour-intensive products, it will also increase the demand for labour. Either wages or employment (or both) will then increase. Whether this increase will reduce poverty depends on whether the poor are strongly represented in the type of labour for which demand has risen (Ben-David et al. 1999). Policymakers thus need to complement policies stimulating economic growth with policies intended to broaden access to income opportunities.

**Policies to promote sustainable development in an integrating world economy**

In order to reap the full benefits (and to mitigate as far as possible any negative effects) of trade and investment liberalisation, it is important that the various goals of sustainable development—economic growth, environmental protection, and social development—be well integrated into national and international policy frameworks. This implies the need for effective and transparent government institutions, accountability, and a solid and consistent legal framework.

For developing countries, adequate national governance regimes may be particularly hard to achieve, due to the high costs likely to be associated with reforms, particularly in terms of the skills, knowledge, and competencies required. Participating in international arrangements aimed at sustainable development objectives may be even more difficult for these countries. Both problems suggest a need for improved capacity-building efforts in these countries.

National and international policy responses will each define the way in which individual countries interact with the global economy. For example, national environmental policies may affect trade and investment activities at the global level; conversely, international trade and investment arrangements in which a country participates may affect national environmental or social policies. Similarly, international environmental arrangements (e.g., multilateral environmental agreements) may affect international trade and investment activities, and vice versa. Some of the more important of these linkages are explored in the following sections.
National policies

The trade and investment effects associated with national policies that use economic instruments depend on the particular instrument involved—including its design and the market in which it operates. If these instruments are fundamentally discriminatory, they could negatively affect market access for foreign producers—for example, certain forms of economic support (subsidies) that are environmentally damaging (perhaps because they lead to excessive exploitation of environmental resources). These subsidies may also be trade distorting, insofar as they reduce the competitiveness of foreign products produced with the environmental resource being subsidised. Reform of these subsidies would therefore probably represent a “win-win” opportunity for sustainable development.

Prior assessment of the environmental impacts of specific projects (environmental impact assessment [EIA]) is required in virtually all OECD countries (OECD 1997). EIAs can help focus environmental policy on the effects of economic activities stimulated by trade and investment liberalisation. EIAs may also cover social impacts, such as disruptions caused by forced resettlements associated with large infrastructure projects (e.g., dams). When these assessment procedures are applied to forthcoming trade or investment agreements, they can help negotiators of those agreements better understand the probable effects of liberalisation. Many OECD countries are therefore already committed to undertaking environmental (sustainability) reviews of World Trade Organisation (WTO) and regional/bilateral trade agreements, in order to identify those trade measures most likely to exacerbate pressures, or areas where further liberalisation could yield additional benefits.

International economic integration, along with increased consumer concerns about the environmental and social impacts of what they buy, have intensified tensions between a narrow focus on the physical characteristics of products and a broader focus on the environmental externalities generated by production processes. To promote sustainable development, a wide range of national product policies are currently being used, such as eco-labelling, extended producer responsibility, and “green” public purchasing. Each of these policies may generate adverse impacts on international trade or investment activities, so each needs to be designed with care. For example, trade concerns may arise when eco-labels are applied in a manner that protects (even inadvertently) domestic producers to the detriment of foreign ones. In order for these policies to avoid becoming disguised market barriers, they need to be non-discriminatory, transparent, involve widespread consultation, and be non-protectionist in intent.

Generalised systems of preference (GSP) schemes provide preferential market access to particular developing countries and, in particular, market conditions. Two existing OECD-based schemes of this type also incorporate provisions requiring compliance with certain labour and environmental standards. For example, the GSP scheme of the European Union provides special access for products that have been produced in an environmentally sustainable way (e.g., tropical nuts and fruits, and tropical wood). Tariff reductions are also offered to countries that prove compliance with standards contained in the International Labour Organization (ILO) conventions. The use of unilateral trade measures to influence policies is politically sensitive. For example, some potential GSP beneficiaries have expressed opposition to the monitoring of social or environmental legislation in their territories, fearing that such
tools could be used for protectionist purposes. This underscores the importance of establishing strong consultative mechanisms with beneficiary countries.

**International policies**

Although *individual WTO agreements* do not aim directly at achieving environmental objectives, environmental considerations are included in some of them. For example, the Preamble of the Agreement establishing the WTO recognises that Parties should conduct their trade relations in a way that allows for the optimal use of the world’s resources, in accordance with the objective of sustainable development. The GATT also provides some exemptions from obligations, such as the national treatment and most-favoured nation principles, to allow measures necessary to protect human, animal, or plant life or health, or that relate to the conservation of exhaustible natural resources.

The WTO Ministerial Declaration, adopted at Doha in November 2001, also made clear the mutual interests of globalisation and sustainable development: “We are convinced that the aims of upholding and safeguarding an open and non-discriminatory multilateral trading system, and acting for the protection of the environment and the promotion of sustainable development, can and must be mutually supportive.” For the first time, Ministers explicitly included environmental matters on the WTO negotiating agenda, focusing in particular on: (1) the relationship between WTO rules and trade obligations set out in multilateral environmental agreements (MEAs), including procedures for information exchange; and (2) reduction of tariff and non-tariff barriers to trade in environmental goods and services. They also asked the WTO Committee on Trade and Environment to examine issues related to the effects of environmental measures on market access (especially for developing countries), the environmental dimensions of trade-related intellectual property rights, and eco-labelling.

Nor do *international investment agreements* necessarily interfere with effective policies to promote sustainable development. For example, the core non-discrimination principle of most investment agreements calls on host governments to treat foreign investors no less favourably than domestic investors (national treatment) and no less favourably than other foreign investors (most-favoured nation). This principle provides ample scope for the non-discriminatory exercise of national regulatory powers of government, including those in the environment and social policy fields. The Monterrey Consensus also notes that a “universal, rules-based, open, non-discriminatory, and equitable multilateral trading system, as well as meaningful trade liberalisation, can substantially stimulate development worldwide...” and that “[l]iberalisation is an important element in the sustainable development strategy of a country.”

Trade and investment may interact with environmental concerns in the implementation of *multilateral environmental agreements* (OECD 1999). Of the approximately 200 MEAs currently in force, about 20 contain trade measures, ranging from bans on trade in endangered species and labelling of internationally traded living modified organisms, to prior approval procedures for hazardous chemicals and transboundary movements of wastes. Some MEAs explicitly recognise the need for coherence of environmental protection objectives with trade and investment objectives. For example, the Protocol on Biosafety and the Convention on the Prior Informed Consent Procedure for Certain Hazardous

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1 See www.wto.org/dohaministerialdeclaration (paragraph 6).
Chemicals both contain text calling for trade and environmental policies to be mutually supportive, with a view towards achieving sustainable development. Hypothetical situations can be envisaged wherein a country might not be able to meet both its obligations under the WTO and under an MEA. This possibility has elicited questions as to which agreement would take precedence in the event of conflict. This uncertainty is reflected in some recently adopted MEAs (such as the Protocol on Biosafety). So far, however, trade measures in MEAs have not been challenged in the WTO.

*International financial institutions and multilateral development banks* are increasingly incorporating social and environmental criteria into their lending policies and practices, and have put procedures in place to assess the impacts of their activities. For example, the International Finance Corporation (IFC), an arm of the World Bank Group, has a policy that all its operations should be carried out in an environmentally and socially responsible way. To this end, it has set up environmental, social, and disclosure policies for all projects, as well as obligations to adhere to international standards, and to comply with host country regulations. Some projects—such as those involving forced or child labour, illegal activities, trade in certain wildlife and wildlife products—are excluded altogether from IFC financing.

The way in which *multinational enterprises* behave is also important for sustainable development. OECD countries have launched several initiatives to promote responsible corporate behaviour in line with the sustainable development agenda. Among these instruments are the OECD Principles of Corporate Governance, the OECD Guidelines for Multinational Enterprises, and the OECD Bribery Convention.

For example, the OECD Guidelines for Multinational Enterprises provide a government-backed set of principles for corporate behaviour and help to level the playing field between competitors in the international marketplace. Recent revisions to the guidelines resulted in clauses dealing explicitly with disclosure and transparency (to encourage social and environmental accountability), employment (covering internationally recognised core labour standards), and environment (encouraging multinational enterprises to raise their environmental performance through improved internal environmental management and better contingency planning).

Multinational enterprises have also attempted to respond to public concerns about sustainable development by issuing their own codes of conduct. Several such codes now exist in the areas of environmental management, human rights, labour standards, the fight against corruption, consumer protection, information disclosure, competition, and science and technology. Environmental performance reporting is also used by an increasing number of firms to report the results of their efforts to the public. A range of international efforts is currently underway to ensure that the type and quality of these reports are consistent across firms (e.g., the Global Reporting Initiative).

Sustainable development is, of course, as much an objective for *developing and transition economies* as it is for OECD countries. However, the policy challenge facing these two groups is quite different. Not only are problems of poverty, population growth, food insecurity, desertification, and HIV/AIDS significantly larger in developing countries, they must attack these problems with much weaker institutions and much lower levels of resources than OECD countries generally have at their disposal.
From a global perspective, it is essential that OECD countries engage actively with developing countries in the search for sustainable development. Environmental, social, and economic issues can no longer be easily divided into “domestic” and “international” spheres. Risks of social disintegration and exclusion affect all countries, as do opportunities to benefit from participation in a growing global economic system. Technologies, capital, and know-how only flow to countries where the fundamental conditions are present to attract and effectively use these flows; many developing countries have not yet managed to establish the policy and institutional frameworks needed to attract them. There is therefore some risk of a “two-track” world developing, where some countries or regions progress while others fall behind.

For many developing countries, there will be important trade-offs between national priorities (e.g., reducing poverty) and protecting global public goods (e.g., the global environment). Developing effective burden-sharing arrangements that reflect “common but differentiated responsibilities” should play an important role in reconciling these trade-offs. There is considerable scope for “win-win” synergies that simultaneously achieve both local and international goals. For example, efforts to improve health by reducing air pollution can also contribute to economic development by reducing the number of workdays lost to illness. Development co-operation has an important role to play in helping developing countries exploit these synergies, mainly by helping to build up their capacities to participate in the global economy.

Conclusion

International trade and capital flows contribute to long-term economic growth and development, and provide a solid foundation for achieving environmental and social goals. When trade and investment policies and environmental and social policies are mutually supportive, the contribution of each to sustainable development is enhanced. OECD countries should reinforce this coherence, both in their domestic arrangements and in international negotiations. To grow in a way that is environmentally and socially sustainable, developing countries need improved access to OECD markets and active support from OECD countries for their capacity-building efforts.

The following concrete steps are suggested for reconciling the trade and investment elements of the global economy with the broader goal of sustainable development (OECD 2001b).

- **Strengthen coherence among trade, investment, environmental, and social policies by:**
  - reforming domestic policies that are both trade-distorting and environmentally-damaging;
  - assessing the environmental and social impacts of trade and investment liberalisation and of incentive measures aimed at attracting foreign direct investment, and developing or refining suitable methodologies to this end;
  - developing practical approaches for ensuring that trade and investment disciplines and environmental and social policy instruments remain mutually supportive; and
  - encouraging the use of environmental and social codes of conduct in the private sector; providing a supportive regulatory and institutional framework for private sector activity; and
promoting awareness and effective implementation of OECD instruments dealing with multinational enterprises, corporate governance, and bribery.

- **Support opportunities and capacities for developing countries to grow in a way that reinforces environmental protection and social development by:**
  - increasing market access for developing countries, especially in sectors where sustainable development is likely to benefit most from economic liberalisation;
  - reviewing economic and environmental policies from the perspective of the goal of poverty reduction;
  - promoting implementation of the international development goals reflected in the OECD's Development Assistance Committee (DAC) report "Shaping the 21st Century: The Contribution of Development Co-operation." In working toward these goals, most OECD countries are guided by the widely accepted target of 0.7 percent of GNP as an appropriate objective for official development assistance (ODA) levels;
  - continuing to help the poorest countries improve their capacity to participate in the sustainable development of the global economy. This includes establishing the policy and institutional frameworks needed to attract private capital flows to those countries, while minimising adverse environmental or social impacts associated with such flows, and providing appropriate support for technology co-operation; and
  - where development co-operation resources are used to support the provision of global public goods (e.g., climate change), focusing on those activities that have clear local benefits, and which also generate ancillary benefits at the regional and global levels.

**References**


