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“Globalization and Sustainability” by Kevin P. Gallagher

Globalization is fast becoming a fact of life - too fast for many people to accept. It is transforming trade, finance, employment, migration, technology, communications, the environment, social systems, ways of living, cultures, and patterns of governance. The main features of the current phase of globalization that are discussed in this section are the accelerated integration of the world's economies through the liberalization of trade and investment regimes; the adoption of structural adjustment programs for many of the less developed countries; and the diminishing role of the state in developed and developing economies alike.

At the global level the 1990s witnessed a new round of negotiation under the General Agreement on Tariffs and Trade (GATT) that resulted in the creation of the World Trade Organization (WTO). At the regional level, free trade and investment agreements were initiated in Europe, Asia, Africa, Latin America, and North America. Also during that time, many structural adjustment programs were adopted in the developing world. While the pace of globalization appears to be increasing, a growing number of scholars and activists, some of whom are represented in this section, are making the case that the current form of globalization is not compatible with sustainable development.

THEORY AND REALITY

Economic arguments for trade liberalization are based on David Ricardo's theory of comparative advantage. Ricardo argued that different countries with different technologies, customs and resources will have different costs to produce the same product. If each country produces and exports the goods for which it has comparatively lower costs, then all parties will benefit. The mutual benefits from trade are said to include greater efficiency in production and higher world-wide rates of consumption. In this model, some groups may lose as a result of trade. However, the net national gains are predicted to exceed losses.

The effects of comparative advantage on factors of production are dealt with in the "Heckscher-Ohlin" model. This economic model assumes a framework in which all countries have perfectly competitive economies and can make the same diversified mix of products, with perfect factor mobility between industries. In this framework, the Stolper-Samuelson theorem predicts that international trade increases the prices of products in which a country has a comparative advantage. This in turn has similar effects on the country's demand for, and prices

of, factors of production: demand and prices rise for those factors in which the country is relatively abundant.

Under this theory, free trade would lead rich countries to specialize in capital- and skill-intensive products, while poor countries would specialize in unskilled-labor-intensive products. As a result, wages would rise for skilled workers in rich countries, and for unskilled workers in poor countries. Conversely, in this simple model, trade should cause employment and wages to fall for unskilled labor in rich countries, and for skilled labor in poor countries.

Criticisms of this model are of two sorts. One approach is based on analysis of the costs to the “losers” in liberalized trade, the other on the model's assumptions. The former criticism was addressed in Volumes 4 and 5 in this series. Those volumes covered the ongoing debate over to what extent trade liberalization is responsible for job losses and inequality in the developed and developing world alike. This volume examines the latter criticism: what happens when key assumptions in trade theory break down?

Externalities such as pollution and resource depletion are assumed not to exist in conventional trade models. Since externalities are, in fact, pervasive, trade liberalization can have unintended consequences: nations with lower environmental standards could gain a comparative advantage in “dirty” production, relative to nations with higher standards. This could create an incentive to lower environmental regulation worldwide, an effect that is sometimes referred to as the “race to the bottom.” (Daly, 1991).

A separate problem is that trade theory assumes that every country is capable of moving into any industry in which it could potentially obtain a comparative advantage. Some countries are at a stage of development where they do not yet have the networks of infrastructure, suppliers, etc. that would allow them to develop the export industries necessary to accrue full benefits from trade. In such cases, the optimal solution may be to protect industries temporarily until a certain level of development is achieved. Import substitution, a development strategy based on protection of key industries from trade pressures, has long been out of favor with economists; recently, however, it has received a new and at least partially sympathetic hearing (Burton, 1998).

RACE TO THE BOTTOM OR CLIMB TO THE TOP?

While there are a growing number of analysts who share the view that the underpinnings of trade policy do not reflect the goals of sustainability, there is a wide range of opinion regarding the impact of globalization. Some see global economic integration as a crisis for environment, labor, and community, others see it as opportunity.

Paul Streeten argues that for globalization to be successful markets have to rest on a framework that enables their energies to flourish and to be used for socially and ecologically sustainable development. However, the reduced power of national governments combined with the spread of worldwide free markets (and technological innovation) without a corresponding authority to regulate them makes achieving sustainability close to impossible. Streeten points out that, while globalization has helped to achieve significant improvement in human

development, it has also contributed to increased impoverishment, inequality, insecurity, and a weakening of institutions and social systems.

From an economic perspective, **Herman Daly** argues that there is clearly a conflict between free trade and a national policy of internalizing external costs. To take the simple case of trade between two nations, if one nation implements policies which internalize environmental and social costs, and enters into trade with a nation that does not, the latter nation can enjoy a comparative advantage in goods that incur high amounts of such costs. Those nations that enjoy such a comparative advantage will become “havens” for industries that are highly polluting or that have unfair labor practices in the world economy.

Such “pollution havens” are commonly expected to be concentrated in developing nations. The U.S.- Mexico border region is often cited as an example of how trade liberalization between a developed and developing nation leads to unsatisfactory levels of highly polluting industries with unfair labor practices in the developing country. This in turn affects the social welfare of the developed country and the world economy as a whole (Public Citizen/RMALC, 1996). However, the bulk of the economics literature has found that trade is only one of a multitude of factors that influence the relative concentrations of dirty industries in the world economy (Jaffe et al, 1995; Mani and Wheeler, 1999; Goodstein, 2000).

James Boyce shows how liberalization can also undercut more sustainable practices in developing countries by forcing them to import goods from developed countries that have not internalized the negative externalities associated with those goods. This notion is illustrated in the context of genetic diversity. Genetic diversity in crop plants is essential for long term world food security. Such diversity is sustained “in the field” by poor farmers in developing countries. Agricultural imports from developed countries that do not include the internalization of externalities in their prices can displace local production in centers of genetic diversity. Such a displacement can threaten both rural livelihoods and the continued maintenance of genetic diversity. Boyce’s article shows how the North American Free Trade Agreement (NAFTA) has impacted Mexican maize farming in this manner.

The empirical story on labor and social standards, extensively covered in the previous two volumes in this series, is mixed. While the debate is interesting and illuminating, it is difficult to come to a decisive yes-or-no resolution. There is a strong case for trade effects as one of the important causes of the declining prospects for low-skilled labor in developed countries, but also a strong case for the view that other effects must be of equal or greater importance. Perhaps the most surprising conclusion is the difficulty of precisely defining and measuring the effects of trade, and the extent to which the evaluation of these effects rests on a series of subtle technical judgments (Ackerman, 1998). One effect that is difficult to pick up in empirical analysis is the use by employers of the threat of moving overseas as a means to win concessions from workers, even when no actual movement of jobs occurs (Belman and Lee, 1992). A more recent article by **James Crotty, Gerald Epstein, and Patricia Kelly** calls this the “magnification effect,” and adds that such employers are buttressed by stagnant wages and contractionary monetary policies that keep aggregate demand low, increasing the need for communities to bid to attract employment.

Although much of this discussion has focused on ways in which nations can derive comparative advantage through economic and institutional means that are harmful to society and the environment, there are also a number of scholars who focus on how comparative advantage can be associated with positive externalities that will result in a “climb to the top” rather than a race to the bottom. These analysts contend that the globalization process, especially in the realm of private capital flows, can be harnessed to achieve sustainable development. Since 1990 Foreign Direct Investment (FDI) has increased from 44 billion dollars in 1990 to over 650 billion dollars in 1998, while official development assistance continued to hover at close to 50 billion dollars (UNCTAD, 2000). Private capital flows that are moving to areas where they will enjoy a new comparative advantage often originate from developed countries where environmental and social standards are more stringent. Thus, it is argued, these practices can be transferred to the developing countries where these firms will now concentrate, therefore improving the prospects for sustainable development in the developing world. This more positive view of trade impacts is presented in the article by **Esty and Gentry**, summarized here (see also Gentry, 1996).

A well-known advocate of this view is businessman Stephan Schmidheiny, who cites the Mexican privatization of its steel industry as an example of environmental progress through privatization. Altos Hornos de Mexico (AHMSA), the largest Mexican steel plant, was sold to a group of Dutch and Mexican investors in 1991. The Dutch investor supplied international and European environmental certification of its manufacturing standards and installed a state of the art environmental management system (Schmidheiny, 1998). This approach has promise but falls far short of being the key to sustainable development. Of all FDI flows in 1998 - 657 billion dollars, - only 25 percent was located in the developing world. Moreover, three nations, China, Mexico, and Brazil receive almost half of the developing world's share (UNCTAD, 2000). What about the rest of the developing world that receives relatively little private capital? Moreover, massive capital flows to the developing countries are not a sustained guarantee; such flows have proven to be erratic and volatile over time. In addition to receiving relatively little investment, most developing countries are minor players in the trade picture as well. Although the value of world trade tripled from 1980 to 1997, the least developed countries only imported and exported one-sixteenth of all imports and exports in 1997.¹ (World Bank, 2000).

Dharam Ghai, director of the United Nations Research Institute for Social Development (UNRISD) adds that, in addition to the effects of global integration on the environment, working conditions, and job creation, it is also altering patterns of leisure and consumption activity, that the world is creating a mixed pattern of inclusion and exclusion. Ghai argues that as images of wealth and leisure are widely disseminated by global media, the life chances of many are becoming more and more restricted and marginalized. One of the most obvious responses by those threatened with exclusion or marginalization is to migrate, whether within countries or abroad. Migration can be a process both of integration and of division. For the affluent and educated migrants, life chances are often improved. Larger-scale migration by poor people, in contrast, can sometimes mean greater impoverishment and a disruption of existing forms of social organization in both sending and receiving regions. Herman Daly and John Cobb, have similarly argued that these economic integration is undermining communities on both sides of the comparative advantage divide (Daly and Cobb, 1994) .

REASSESSING STRUCTURAL ADJUSTMENT

Structural adjustment programs are the policy instrument that is most frequently relied on to bring the developing world into the world economy. SAPs are often applauded for achieving their desired macro-economic changes. From a sustainability perspective the question is: at what cost?

The structural adjustment programs (SAPs) that have been prescribed by the International Monetary Fund (IMF) and the World Bank have the stated goals of achieving higher output growth and rising real incomes in the developing world. Structural adjustment policies have sought to bring developing countries into the world economy by adopting a development strategy based on: the promotion of export-oriented growth; the privatization of state-owned industry; the elimination of barriers to international trade and investment flows; the reduction of the role of the state as an economic agent; and the deregulation of domestic labor markets.

Even the harshest critics of SAPs acknowledge that it is erroneous to think that developing nations can develop in the context of hyperinflation, ballooning deficits, and extreme poverty (MacEwan, 2000). Macro-economic stability is a key ingredient for sustainability. From a macroeconomic point of view, there is little doubt that adjustment programs are having some positive effects. In most cases per capita GDP, agricultural exports, and revenues from extractive industries are all on the rise, while budget deficits and inflation have been brought under control. But this is not the whole picture. In two comprehensive book length studies, authors **Lance Taylor** and **Ute Peiper**, and **David Reed**, show that the social and environmental costs of these programs, may outweigh the short-term economic benefits. Taylor and Peiper's work, while including a chapter on environmental impacts, highlight the social impacts of SAPs. Specifically, they focus on the effects of SAPs on poverty and inequality, gender relations, and education and human health.

SAPs can create significant distributional conflicts and worsen inequality. Where this has occurred they have run a strong risk of failing. In cases like Turkey and Mexico, these authors found that the beneficiaries of SAP reform have been households in the top twenty percent of the income distribution, while the losers were people in the bottom eighty percent. Such ramifications have provoked extreme political backlash. The result has been corruption, accelerating inflation exacerbated by distributional conflict, high interest rates, and overvalued exchange rates -all problems that economic integration is supposed to overcome.

Taylor and Peiper conclude that people feel the effects of these programs in practically every aspect of their lives: food price increases, declines in family incomes, and reductions in public expenditures on social and health services. These changes directly affect women's role as principal homemakers. The degree to which women's productive roles are affected by SAPs is partly governed by existing social rules and gender roles, as well as by the process of class differentiation. Other studies have concluded that SAPs leave women at a clear disadvantage, and, because they don't own necessary factors of production, they are often the 'spectators' of SAPs rather than participants (Haddad et al, 1995).

While some analysts argue that it is still too early and too difficult to fully assess the environmental impacts of SAPs, David Reed's work draws on case studies of SAP experience in Cameroon, Mali, Tanzania, Zambia, El Salvador, Jamaica, Venezuela, Pakistan, and Vietnam . While Reed acknowledges that the short term economic problems were often solved in these countries, environmental problems were often, though not always, exacerbated. Most of the benefits of SAPs accrued to wealthy, outward-oriented producers and merchants, commercial farmers, and investors in extractive industries. The heaviest costs of SAPs have been borne by small rural farmers, workers in the informal sector, urban consumers, redundant government employees, and women.

Reed's study shows that in countries with large extractive sectors, output growth and employment benefits have resulted from structural adjustment, but these benefits have been accompanied by a dismantling of government capacity to manage and regulate those industries so as to minimize environmental costs. In Tanzania, Zambia, and Venezuela, such policy failures are generating highly damaging environmental impacts. The failure to couple internal and external adjustment with adequate regulatory reform and institutional strengthening is generating high revenue and employment on the one hand and higher environmental costs to be absorbed in the future on the other.

Reed's study also points out that there are a number of impacts on the environment that are clearly positive. In some cases, exchange rate reforms have led to a shift away from "erosive" to "nonerosive" crops, and price corrections have created new agricultural incentives that have stimulated expansion and diversification of tradeable crops and other commodities. These are positive effects in that they increase relative returns to the agricultural sector and raise the incomes of some farmers, thus encouraging on-farm investment.

Theodore Panayotou argues that since environmental improvement has not been the aim of SAPs, it is not fair to use an environmental measuring rod to assess such policies. However, he notes that to the extent that SAPs lead to natural resource depletion or environmental damage beyond the economic optimum, they are defective in economic terms by failing to meet their own objectives. Panayotou argues that SAPs should treat the natural resource base in the same way that man made capital is treated (Panayotou, 1996).

CONCLUSION

While Esty and Gentry have shown how globalization can promote sustainability, the other authors in this section demonstrate significant ways in which globalization in its current form is unsustainable. However, they also note that we are faced with many choices as to how to globalize the world economy. Many of those choices can promote sustainability, but not all of them can be addressed on the global level. A sustainable global economy will require the efforts of many different actors. These include corporations, local and national communities, as well as global institutions. In the sections that follow, we will focus on roles that these actors can play in shaping a sustainable systems at the local, national, and global level.

Notes

1. “Least developed” refers to “low income” countries as classified by the World Bank, and include countries like Nigeria, Vietnam, Nicaragua, Armenia, and Mali. Middle Income countries, ranging from Mexico, the Czech Republic, and South Africa, to Egypt, Bolivia, Indonesia, and the Russian Federation, only imported or exported one fifth of total imports and exports.