International Chamber of Commerce

The world business organization

Standing up for the global economy

Key facts, figures and arguments in support of globalization

International Chamber of Commerce

38, Cours Albert 1er, 75008 Paris, France

Telephone +33 1 49 53 28 28   Fax +33 1 49 53 28 59

Web Site www.iccwbo.org   E-mail icc@iccwbo.org

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Preface

By Maria Livanos Cattaui, Secretary General of ICC

Companies are in a unique position to observe and help shape today's global economy. They are at the heart of international trade and investment, engaging in business across borders and linking economies together into a more interconnected world.

The purpose of this report is to provide a business perspective on some of the main issues and concerns raised by globalization. Is it pushing governments to the sidelines? Is it a threat to jobs? Is it helping to overcome poverty, or creating more? How can the changes arising from globalization be managed?

This report is the result of a comprehensive review of existing research by international organizations, academic institutions, governments and informed commentators with the aim of better understanding the impact of globalization on people and national economies.

What it finds is that globalization has already brought unprecedented improvements in material welfare to billions of people. The evidence suggests that the global economy of today offers an unparalleled opportunity to raise living standards across the world.

That disparities between rich and poor are still too big is undeniable. But those who sincerely want to alleviate the poverty of millions in the developing world should focus on practical ways to harness the potential of globalization instead of making globalization a scapegoat.

There are two key elements I wish to highlight in this report as promising avenues in the quest for a more inclusive global economy: the vast potential for increased South-South trade and the key importance of good governance.

A more open world economy and more effective governments are by no means contradictory goals. More than ever, globalization requires the enforcement of the rule of law, the encouragement of innovation, the development of efficient infrastructure, the improvement of education and social programmes, and greater political and economic stability in order for countries to seize all the opportunities that the world economy can offer.

This report was prepared by Julian Kassum of ICC's international secretariat with the input and guidance of ICC's Corporate Economists Advisory Group (CEAG) for the ICC 35th World Congress, held 6-9 June 2004 in Marrakesh. An electronic version will be posted on ICC's website (www.iccwbo.org) and updated in light of new findings.

I take this opportunity to thank members of the CEAG – a group of 28 corporate economists from global companies and business organizations in more than 20 countries – and particularly the chairman, Donald Hepburn of Unilever, for this further example of their valued contribution of solid economic analysis to ICC's policy work.

ICC is pleased to offer this synthesis of research and analysis of globalization as a contribution from world business to the ongoing public debate about this much-misunderstood phenomenon.

What is globalization?

Globalization can be described as the increasing interdependence of the national economies of both advanced and developing countries. Such economic integration occurs when countries open themselves to expanding flows of trade, capital, labour and ideas with the rest of the world.

Globalization is not new, but it has changed

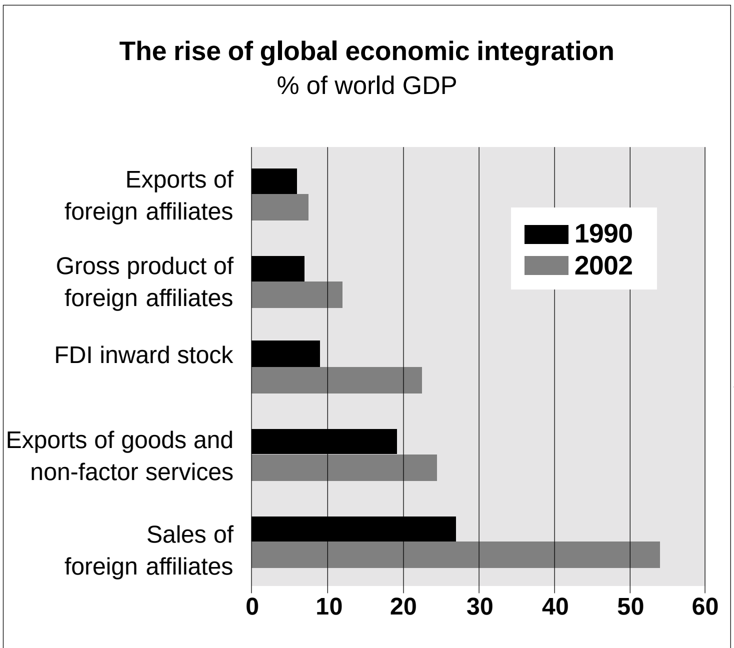
To a certain extent, the world economy was more globalized in the late 19th century than today. The period between 1870 and 1914 saw a boom in cross-border trade and capital flows, led by a sharp decline in transport and communications costs resulting from rapid technological advances. But there are a number of features that make today's globalization an unprecedented phenomenon in world economic history.

How has globalization changed?

1. The composition of trade has evolved dramatically since the mid-1980s

Today, over 70% of developing country exports are manufactures. In a country like Japan, over half of manufactured imports come from the developing world.

Industrialized and developing countries are now trading in competing products[2]. Traditionally, trading relations followed a well-established pattern: Western countries exported manufactures while the rest of the world exported primary commodities. Today, over 70% of developing country exports are manufactures. In a country like Japan, over half of manufactured imports come from the developing world[3]. Services, which have long been considered as "local", now account for an increasing share of world trade.The overall boom in world trade has largely accelerated economic growth of both developed and developing countries, giving rise to new regional economic powers.



Source: UNCTAD and OECD[1].

2. This shift in the composition of trade has come hand-in-hand with a global redistribution of production and employment

Many developing countries have become major suppliers of industrial goods, such as clothes, consumer electronics or metal products. Industrialized countries now enjoy sustained economic growth thanks to a dynamic services sector and increased levels of investment overseas. A new trend is currently taking shape, upheld by the information technology revolution, with a growing number of services jobs being "transferred" to developing countries. Multinational companies have largely contributed to these structural changes by locating their operations where the comparative advantages – proximity to markets, wage costs, know-how – are the greatest.

3. Market reforms and more open trade policies have been key in the emergence of today's globalization

Industrialized countries paved the way by engaging in eight successive rounds of trade liberalization under the General Agreement on Tariffs and Trade (GATT) during almost 50 years. From the 1970s on, developing countries started to deregulate their economies and to liberalize trade, placing more reliance on market forces to generate economic growth. With the end of the Cold War and major economic reforms in China, the pace of globalization has accelerated dramatically. Today, 148 countries are working together within the World Trade Organization (WTO) to further liberalize trade and investment, with a view to boost economic growth and raise living standards across the world.

Benefits and challenges

Countries that have successfully integrated into the global trading system are shown to enjoy faster growth, better living standards, easier access to capital and technology, higher productivity and lower prices than countries with closed economies. However, as with all great movements of change, transitional problems of adaptation arise. The economic changes brought by global economic integration can have profound social and cultural impacts on particular groups. The accelerating pace at which these changes are unfolding can be particularly disturbing. It is the responsibility of governments to ensure that such transformation is accompanied by socially-oriented measures that help people adapt, especially those who lose out from the initial phases of the process.

Benefits
Faster growth
Better living standards
Easier access to capital and technology
Higher productivity
Lower prices

Challenges
Transitional problems
Social impact
Cultural impact

Governments also need to better explain the rationale behind the global economy as a force for positive change. Using globalization as a scapegoat for domestic problems, or capitulating to narrow interests clothed in anti-globalization pressures, can only distract attention from the serious challenges that need to be addressed, and may even jeopardize the potential benefits that the global economy can bring. Contrary to a widely held belief, globalization is not irreversible. It has already been reversed in the past, with dramatic consequences for the world economy: the backlash against globalization between the two world wars coincided with the Great Depression. Another era of economic stagnation would hurt everyone, especially the world's poorest people.

Globalization has already brought immense benefits to those people and countries that were able to participate in the process. Still, for a majority of least-developed countries, the integration into a fast-paced and competitive global economy is not an easy task. The challenge is to make the prosperity that flows from globalization available to the fifth of the world's population still living in deep poverty. To do this, the capacity needed in poor countries must be built so they can seize the opportunities offered by globalization. To quote Kofi Annan, Secretary-General of the United Nations: "I believe the poor are poor not because of too much globalization but because of too little"[4].

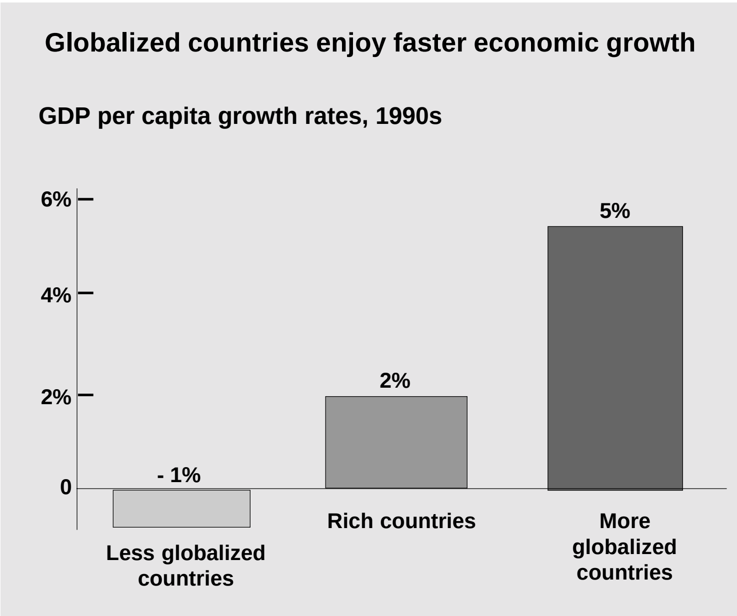
"I believe the poor are poor not because of too much globalization but because of too little" – Kofi Annan, Secretary-General of the United Nations.

[1] Table drawn from: Martin Wolf, *"Hopes are rising for sustained recovery"*, in *"The World: 2004"*, Financial Times, 21 January 2004
[2] Ajit K. Ghose, *"Jobs and incomes in a globalizing world"*, International Labour Organization, 2003
[3] World Trade Organization, *"Statistics on globalization"*, 2001
[4] Kofi Annan, Secretary-General of the United Nations, addressing the Millennium Forum on 22 May 2000

Do open economies grow faster?

Absolutely

The most spectacular increases in economic growth all involve simultaneous increases in both exports and imports. Individual case studies and cross-country analysis nearly all show that integration into the global trading system leads to faster economic growth and rapid poverty reduction. One study by Jeffrey Sachs and Andrew Warner[5], which has received particular attention, finds that open economies grow between 2% and 2.5% per year more rapidly than closed ones. David Dollar and Aart Kraay from the World Bank reach similar conclusions[6].



Source: David Dollar, *"Globalization, Investment Climate and Growth"*, World Bank, November 2003.

In the 1990s, the fastest growth in the world occurred in globalizing developing countries, home to about 3 billion people. With the long-term trend growth rate of the rich countries at around 2%, the fast-growing developing countries are gradually catching up. However, about 2 billion people live in countries not deeply involved in integration and with negative growth and increasing poverty.

Look at China and India

Openness to foreign trade and investment is a key element of a sound development strategy. China and India are good examples of developing countries that have achieved impressive growth rates and vast poverty reduction after opening their trade regimes in the 1980s and 1990s. In India, the poverty rate had barely changed between 1949 and 1978. As the economy opened up, growth reached an average of 6% annually and poverty was cut in half.

How does an open world economy promote growth?

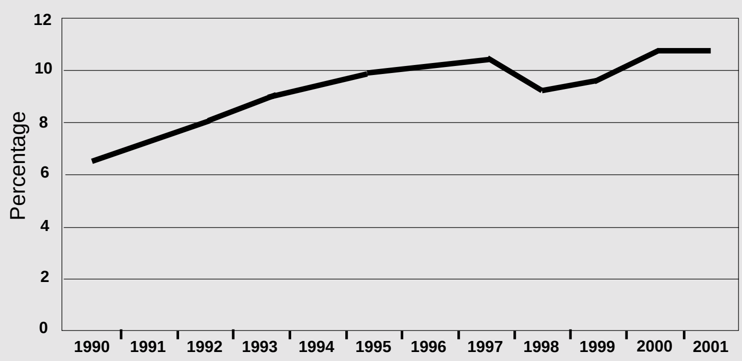
Openness promotes economic efficiency by allowing countries to specialize in what they do best rather than produce everything on their own. In an open world economy, countries tend to export what they produce efficiently and to import what they produce relatively less efficiently. This allows a more effective allocation of resources both *within* and *between* countries, thereby increasing the overall economic pie.

Exports create new opportunities for employment and investment, as companies sell their products to wider markets. Imports bring cheaper products to consumers and companies, including high-quality goods and services that were not available previously. Foreign investment in production creates jobs that employ local people, drives economic growth by contracting with local suppliers, and allows a significant transfer of technology and know-how from country to country. More generally, increased foreign competition provides a powerful incentive for domestic companies to innovate and to become more competitive.

Why is there still such a wide gap between rich and poor countries?

Through all these channels, globalization offers a unique opportunity for the developing world to boost economic growth and raise living standards. But developing countries have not yet exploited all the benefits that the global trading system can bring. One major reason is that industrialized countries continue to impose high tariffs and other trade barriers on labour-intensive products – such as textile, clothing or agricultural products – in which developing countries have a competitive advantage. Developing countries themselves tend to protect their own markets against each other. Despite a steady increase throughout the 1990s, South-South trade still represents a tiny share of world trade.

Share of South-South trade in world merchandise trade, 1990-2001



Source: WTO, International Trade Statistics.

How can developing countries close the gap?

The expansion of South-South trade would be a means for developing countries to reduce their dependence on markets of industrialized countries and to diversify their export base[7]. According to Oxfam, a 5% increase of the share of developing countries in world exports would generate US $350 billion – seven times as much as they receive in aid[8]. Overall, World Bank calculations show that dynamic gains from multilateral trade liberalization under the WTO Doha Development Agenda could amount to more than US $800 billion a year by 2015, with more than half accruing to developing countries.

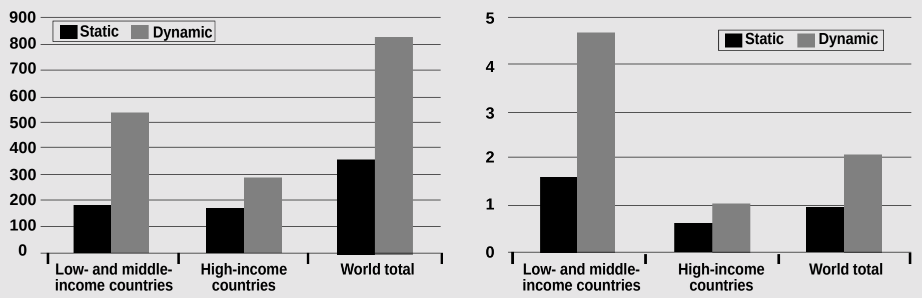
A 5% increase of the share of developing countries in world exports would generate US $350 billion – seven times as much as they receive in aid.

Developing countries could reap income gains of over $500 billion from full trade liberalization

(billions of 1997 dollars, additional income in 2015 compared with baseline)

– which implies up to a 5% boost in incomes.

(percent of baseline income in 2015)



Note: Static gains refer to the results holding productivity constant. Dynamic gains allow productivity to respond to sector-specific export-to-output ratios.

Source: World Bank model simulations.

Source: World Bank, *"Global Economic Prospects"*, 2002.

Is an open economy enough to raise living standards?

Openness to foreign trade and investment should not be seen as a guarantee of rising economic growth and living standards. Open trade policies will never make up for shortcomings in other areas. For a country to attract long-term and productive investment, some key conditions have to be met on the ground:

- **A stable political system** supported by a professional and accountable public service; an open and constructive attitude toward the private sector, both local and foreign; a predictable and transparent regulatory framework; and a respect for the rule of law and due process.
- **A sufficiently comprehensive, transparent and non-discriminatory legal framework** to operate modern commercial operations (including company law, bankruptcy law, competition law, protection of property rights including intellectual property), and free access to an impartial judicial system to redress wrongs and settle disputes.
- **Sound macro-economic, fiscal and monetary policies** (including currency stability and convertibility) sufficiently flexible to adapt to market signals, low inflation and moderate levels of personal and corporate taxation.
- **A dynamic economic base** supported by an expanding domestic market, growing demand and purchasing power, a healthy local private sector of suppliers, distributors and competitors, and efficient capital markets and financial services.
- **Rising standards of education, health care and social infrastructure** to encourage human resource development, an adequately educated and trained work force, and an efficient system of physical infrastructure, in particular in the key areas of transportation and communications.

It takes two days to start a business in Australia, but 168 days in Indonesia and 215 days in Congo.

A regulatory framework that encourages private enterprise is key to generating economic activity and job creation. One recent World Bank report shows that most poor countries tend to regulate their business excessively, thereby crowding out potential investors and entrepreneurs[9]. For example, it takes two days to start a business in Australia, but 168 days in Indonesia and 215 days in Congo. Excessive business regulation can have counter-productive effects: it protects those who may be able to circumvent cumbersome rules, but it makes life particularly difficult for small and medium-sized enterprises – the main engines of economic growth in most developing countries. In many parts of the world, good governance and domestic reform will be absolutely necessary to ensure a successful integration into the global economy.

[5] Jeffrey Sachs and Andrew Warner, *"Economic Reform and the Process of Global Integration"*, Brookings Papers on Economic Activity, 1995
[6] David Dollar and Aart Kraay, *"Trade, Growth and Poverty"*, World Bank Development Research Group, 2002
[7] World Trade Organization, "*World Trade Report 2003*", 2003
[8] Oxfam, *"Rigged rules and double standards"*, 2002
[9] World Bank, *"Doing Business in 2004"*, 2004

Why is agriculture attracting all the attention in the WTO trade negotiations?

It is vital to economies of the South, but a political taboo in the North

Agriculture is the major stumbling block that has led the current round of WTO trade negotiations to a deadlock. Most WTO member countries from the developing world are united in calling for a vast reform of agricultural markets, asking rich countries to allow more agricultural exports from developing countries into their markets by dismantling their protectionist and trade-distorting agricultural support programmes. But farm reform remains a “political taboo” in the EU, Japan and the US, where governments are facing intense social pressure from their farmers not to remove these support programmes, despite evidence that a more open trading system in agriculture would benefit many in both industrialized and developing countries.

In Morocco, for example, agriculture may account for only 14% of GDP, compared to 60% for services and 18% for manufactures, but it remains the largest employer with 44% of the workforce.

Three quarters of the world’s poorest people live in rural areas, with the majority making their living from agricultural production. Agriculture plays a vital role in the economies of developing countries, including those that are already well advanced in the industrialization process. In Morocco, for example, agriculture may account for only 14% of GDP, compared to 60% for services and 18% for manufactures, but it remains the largest employer with 44% of the workforce [10]. In least developed countries, farmers can represent up to three quarters of the workforce.

A healthy agricultural sector, which can secure strong revenues for its producers, is therefore critical to stimulate local economies and non-agricultural economic sectors. Research by the International Food Policy Research Institute shows that, in sub-Saharan Africa, each additional dollar of income from agriculture generates two to three dollars of growth in the overall economy [11]. In particular, agriculture offers great export opportunities for developing country farmers, especially for products in which they have a competitive advantage.

In sub-Saharan Africa, each additional dollar of income from agriculture generates two to three dollars of growth in the overall economy.

Poor farmers are suffering. Protectionism is to blame

Yet, over recent years, agriculture has been more a burden than a boon for poor countries. According to the United Nations Conference on Trade and Development (UNCTAD), the share of developing countries in world agriculture exports has slumped from 31.7% in 1970-1972 to 26.4% in 1998-1999. The least developed countries’ share dropped from 3.5% to 1.0% during the same period [12]. Meanwhile, dramatic falls in world prices of commodities such as milk, sugar and cotton have forced many developing country farmers out of business.

According to the Organisation for Economic Co-operation and Development (OECD), a major explanation lies in the US $318 billion that OECD governments spend every year to support their own farmers [13]. Protectionism in the North in the form of export subsidies, price-support mechanisms and other trade-distorting domestic support measures tend to destroy markets in the South as they lead to overproduction and drive down world prices to levels where farmers cannot compete. On top of this, many industrialized countries impose high tariff barriers against agricultural imports, protecting their farmers from more competitive producers in Asia, Africa or South America. More troubling, tariffs are even higher for processed food, discouraging developing countries from upgrading their food industry.

Consumers are taken for a ride

According to the OECD, Europeans pay twice the world price for beef and five times the price they should be paying for rice.

Ironically, industrialized countries do not benefit either from their own protectionism. Their citizens lose out on two counts: as taxpayers, by financing these costly subsidies, and as consumers, by paying higher prices for food. According to the OECD, Europeans pay twice the world price for beef and five times the price they should be paying for rice. The vast majority of farm support in industrialized countries goes to a minority of large agricultural producers rather than to small family farms. But these large-scale farmers carry considerable political weight in their countries and fiercely oppose any major reforms.

Major farm reform will require tough political decisions and careful follow-up

A rise of only 1% in Africa's share of world exports would amount to US $70 billion a year.

The World Bank estimates that the liberalization of agricultural trade (with a repeal of all rich-country trade barriers and subsidies to agriculture) would improve global welfare by about US $250 billion by 2015, of which almost US $150 billion would accrue to developing countries [14]. A rise of only 1% in Africa's share of world exports would amount to US $70 billion a year. These compelling figures leave no doubt that governments of developed countries must start now to prepare their domestic constituencies for major farm reforms in the near future. Not all forms of agricultural support will have to be eliminated. But price- and trade-distorting policies must be seriously reconsidered in light of their impact on the world's poor.

It is important, however, not to raise undue expectations of the benefits that a more open trading system for agriculture would bring to developing countries. These benefits will only materialize if developing countries use the gains from agricultural trade liberalization – higher incomes for their farmers, new export opportunities – to invest in productive activities, and to introduce domestic policy reforms in order to improve their competitiveness in agriculture and other sectors.

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[10] World Trade Organization, *"Trade Policy Review: Morocco"*, 2002

[11] Per Pinstrup-Andersen, Mattias Lundberg, and James L. Garrett, *"Foreign Assistance to Agriculture: a Win-Win Proposition"*, International Food Policy Research Institute, 1995

[12] United Nations Conference on Trade and Development, *"Agricultural Exports of Developing Countries: Unlocking Potential"*, 2001

[13] Organisation for Economic Cooperation and Development, *"Agricultural Policies in OECD Countries: Monitoring and Evaluation"*, 2003

[14] World Bank, *"Global Economic Prospects and the Developing Countries: Making Trade Work for the World's Poor"*, 2001

Is globalization destroying jobs in industrialized countries?

Trade-related layoffs represent a small fraction of unemployment

Globalization is often blamed for “exporting jobs” to countries where labour is cheaper, creating job insecurity for workers in rich countries. The recent waves of layoffs and factory closures in the US, Europe and Japan have aroused widespread concern over the domestic consequences of increased competition from cheap imports and production relocation in low-cost developing countries. Low-skilled manufacturing workers were long seen to be the hardest hit, but fears are now growing that white-collar staff may also lose their jobs as a result of competition from developing countries.

Global economic integration does indeed make it easier for companies to shift or expand operations in countries where market conditions are most attractive. That is, however, a far cry from arguing that globalization is a key cause of job losses.

Strictly speaking, international trade can explain only about 20% of the increased inequality between high- and low-skilled workers in either wage or employment terms[15]. In the same way, production relocation accounts for only a small proportion of the jobs constantly being created and destroyed in industrialized countries. According to the French Ministry of Economy, only 4% of France’s foreign direct investment is likely to be related to production relocation. In the US, the Bureau of Labor Statistics estimates that trade-related layoffs represented a mere 0.6% of total unemployment at their peak in 2001[16].

Only 4% of France’s foreign direct investment is likely to be related to production relocation.

Technology is having a far more dramatic effect on jobs

Technology, not trade, is the chief explanation for the decline in manufacturing employment in industrialized countries. Automation and the information technology revolution have boosted productivity over the last 20 years, reducing demand for low-skilled labour. Fewer workers are now needed to produce the same amount of output. In France, for instance, 1.5 million manufacturing jobs have disappeared since 1978, but manufacturing was able to keep its share of GDP unchanged – at roughly 20%[17].

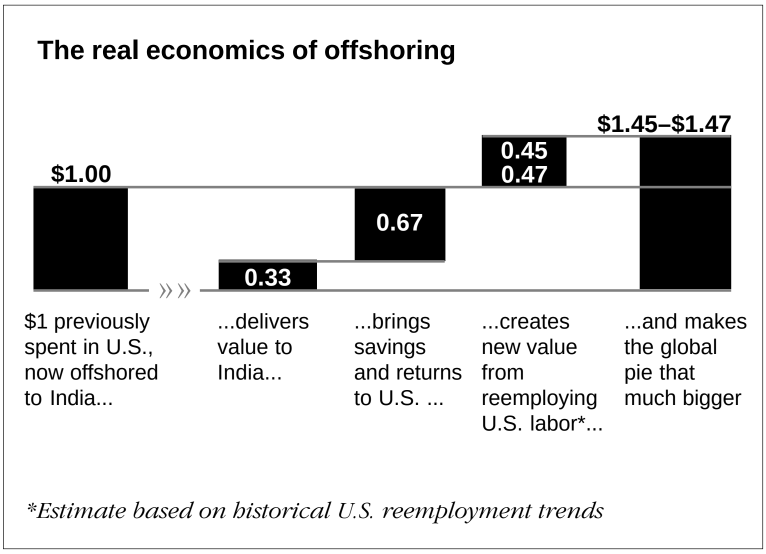
Manufacturing in industrialized countries is not losing its competitive edge. It is shifting to higher value-added products, such as airplanes, fiber-optic equipment or luxury goods. In the process, companies create better-paid jobs with better working conditions. In parallel, manufacturing companies are devoting greater resources to tasks that are upstream (e.g., conception) and downstream (e.g., marketing) of the production process, thus creating millions of new jobs for the educated workforce of industrialized countries.

Manufacturing in industrialized countries is not losing its competitive edge. It is shifting to higher value-added products.

A similar pattern is now occurring in the services industry, with a growing number of operations being relocated to low-cost countries. The communication revolution is allowing companies in industrialized countries to move back-office activities –

such as handling customer-service hotlines or processing payments – to developing countries. Some companies are even starting to outsource skill-intensive activities – such as research or software programming – to countries like India and Malaysia.

Many high-skilled workers, particularly in the US, fear that jobs in information technologies (IT) and services will now disappear just as manufacturing jobs did. In a study for the Institute for International Economics, Catherine L. Mann offers a much more optimistic perspective: “Frequently cited projections indicate that millions of jobs will be lost to offshore workers. What these projections ignore is that the globalization of software and IT services, in conjunction with the diffusion of IT to new sectors and businesses, will yield even stronger job demand in the US for IT-proficient workers” [18].



Source: McKinsey Global Institute.

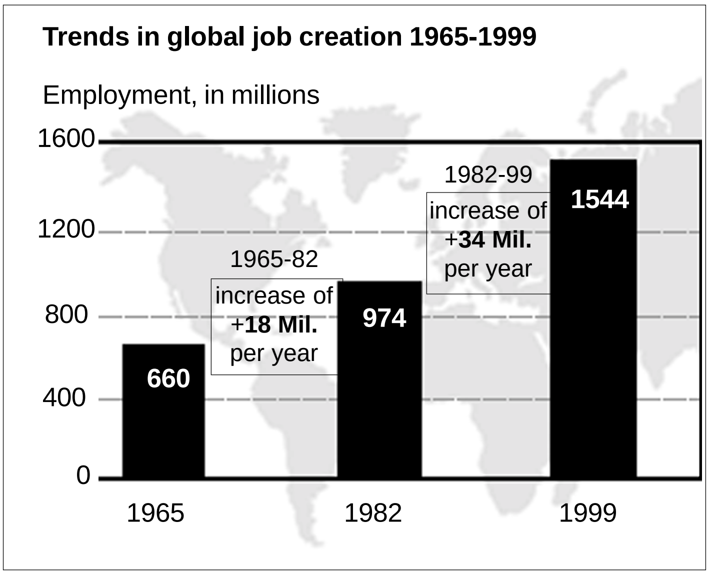
According to Ms Mann, the global integration of IT software and services will lead to a decline in the prices of software and services, thus promoting further diffusion of IT use in more companies and more sectors. This will result in a new wave of productivity growth, generating faster economic growth and more employment: in the US, the Bureau of Labor Statistics predicts the net creation of 22 million new jobs over the next decade, mostly in business services, health care, social services, transportation and communications. In particular, demand for computer-support specialists and software engineers is expected to double between 2000 and 2010.

How to manage shifting employment patterns

In a dynamic economy, jobs are continuously lost and created. Trade expansion and increased business activity over the last 20 years have substantially accelerated the pace of job creation across the world. Between 1982 and 1999, 34 million jobs were created [19] on average every year in manufacturing and services worldwide, more than double the number of jobs created between 1965 and 1982 [20]. Thanks to productivity gains – made possible by technological innovations and the global integration of production – industrialized countries have been able to enjoy sustained economic growth and to create new jobs at a pace which allows most advanced economies to operate at or close to full employment.

Much resistance to the changes that technological progress and competition – both internal and external – bring about stems from a widespread belief in what economists call the “lump of labour fallacy”. This is the flawed notion that there is a fixed amount of work with a fixed amount of jobs. It is a notion that flies in the face of economic theory and practical experience: countries generate more or fewer jobs depending on factors such as the cost of employment, the prevalence of an entrepreneurial culture and the regulatory environment. Belief in the “lump of labour fallacy” is a recipe for economic stagnation and isolationism.

As the economy goes global and new technologies are introduced, new business opportunities create jobs that did not exist before. Job losses to Chinese competition may be a reality. But new jobs created by growing Chinese demand as a result of China's rapid economic growth are also a reality. China's imports have risen by 70% since it joined the World Trade Organization in 2001, making it the world's third largest importing country and the fastest growing export market for EU, US and Japanese companies[21].



Source: Hauser and Oberhänsli in *WTO News*; St Gallen University, February 2002; based on data from ILO and Eurostat.

Globalization is not a major cause of unemployment in developed countries. Yet some individuals and local economies may lose their jobs as a result of the micro-economic process of production relocation. While resisting protectionist pressures, governments must focus their efforts on providing adequate safety nets for those displaced workers, such as unemployment insurance, job search assistance and training programmes. But perhaps the greatest challenge for governments is to ensure that their education systems provide their young citizens with the skills needed for the new jobs that are continuously being created.

15 Jean-Marie Cardebat and Eric Maurin, *"Mondialisation, innovation et emploi"*, Note de l'Institut Français des Relations Internationales n°49, 2003

16 Bureau of Labor Statistics, *"Extended Mass Layoffs"*, 2003

17 Délégation à l'Aménagement du Territoire et à l'Action Régionale, *"La France, puissance industrielle"*, 2004

18 Catherine L. Mann, *"Globalization of IT Services and White Collar Jobs: The Next Wave of Productivity Growth"*, Institute for International Economics, 2003

19 These were net jobs (jobs created less those that disappeared over the same period)

20 Herbert Oberhänsli and Oscar Véra, "Globalization: Concerns and Opportunities for the People in the Developing World", 2003. See www.humanglobalization.org

21 Nicholas R. Lardy, "Do China's Abusive Labor Practices Encourage Outsourcing and Drive Down American Wages?", Institute for International Economics, Testimony before the Senate Democratic Policy Committee Hearing, 2004

Does globalization encourage a "race to the bottom" in social and environmental standards?

No. It has the opposite effect

In an open world economy, countries compete with each other to attract the investment flows they need to create jobs and economic growth. In this context, governments have to create the best possible conditions for businesses to flourish and to maintain investor confidence. For critics of globalization, the inevitable result is global competition among governments – especially in poor regions – to reduce social and environmental standards, as companies seek to establish their operations in countries with the lowest tax rates, the weakest labour laws and the fewest pollution controls. In reality, there is no evidence of such a "race to the bottom" – quite the contrary.

Shunning poor working conditions

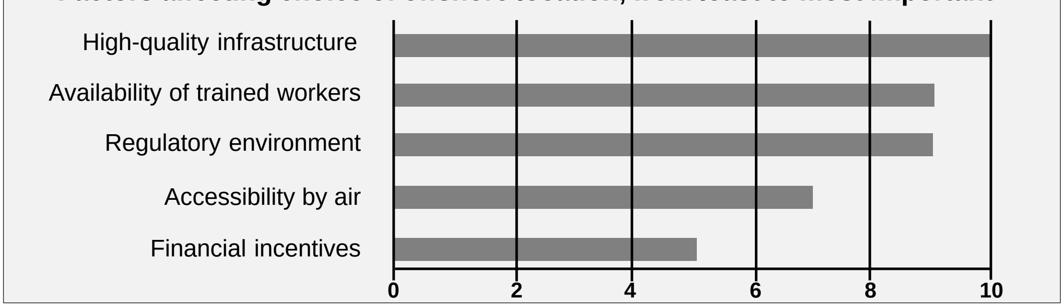
Companies are not necessarily attracted to countries with low wages and weak environmental protection. In the late 1990s, 80% of US foreign investment was in rich countries such as Canada, Germany, France and Japan, where social and environmental standards are high[22]. Nearly all the rest was in advanced developing countries such as Singapore, Mexico and South Korea, which also have high standards. One of the reasons why companies shun countries with poor working conditions is that low labour standards generally reflect low productivity, which implies a high unit cost of labour[23].

One of the reasons why companies shun countries with poor working conditions is that low labour standards generally reflect low productivity, which implies a high unit cost of labour.

Favouring responsible public spending

Nor do companies flock to countries with the lowest tax levels. Good physical and social infrastructure, rising standards of education, and macroeconomic stability are important considerations when companies make decisions about investment location. All of these require adequate levels of public spending. In effect, OECD countries have actually increased their average tax take from 32.1% of GDP in 1980 to 37.3% in 1999[24]. Taken individually, these countries vary considerably in the way they tax their citizens and companies. In other words, governments still have considerable latitude to pursue fiscal policies as they see fit.

Factors affecting choice of offshore location, from least to most important



Source: 2002 McKinsey survey of 30 executives at companies using outsourced labour in India.

Doubling wages in developing countries

Far from encouraging a “race to the bottom”, openness to foreign trade and investment actually helps countries to improve their social and environmental records. Research by the OECD and the Institute for International Economics shows that foreign affiliates of international companies pay about double the local manufacturing wage in least developed countries. According to a recent report by McKinsey Global Institute, foreign producers in the Chinese auto industry offer unskilled line workers more than twice the going rate for unskilled manufacturing jobs. Wages in India’s business-process-outsourcing sector are 50% to 100% higher than those in other white-collar sectors requiring similar skills[25].

Average wage paid by foreign affiliates and average domestic manufacturing wage, by host-country income, 1994

	All countries	High-income	Middle-income	Low-income
Average wage paid by foreign affiliates *(thousands of US dollars)*	15.1	32.4	9.5	3.4
Average domestic manufacturing wage *(thousands of US dollars)*	9.9	22.6	5.4	1.7
Ratio	1.5	1.4	1.8	2.0

Source: Edward M. Graham, Institute for International Economics.

Promoting environment-friendly practices

Similarly, foreign-owned plants in developing countries tend to be less polluting than domestic plants[26]. When multinational companies invest in different countries, it is cheaper for them to apply the same environmental policy everywhere and to use the same environment-friendly production methods, which often happen to be more productive. Using high standards also helps companies to maintain a good reputation, avoid clean-up costs and anticipate upward regulatory changes.

Boosting economic growth

Indeed, citizens are more likely to demand a cleaner environment and better working conditions as the economy grows and incomes rise, while governments and companies have greater means to finance improvements in social and environmental standards. According to a study by Alan Krueger and Gene Grossman, pollution levels start to fall when average per capita income reaches US $8,000[27]. Consumers can afford to pay for cars that pollute less, while companies can introduce clean technologies that use fewer resources. Significant improvements in air quality were registered in major urban areas in Brazil, China and Mexico throughout the 1990s[28].

Pollution levels start to fall when average per capita income reaches US $8,000.

Why trade sanctions would backfire

In many countries, progress can be desperately slow. This has led some in industrialized countries to call for trade sanctions against developing countries that fail to abide by given social and environmental standards. In practice, however, such measures would seriously undermine efforts made by developing countries to improve their social and environmental practices.

Imposing new barriers against imports from developing countries would directly hurt their export-oriented sectors, possibly displacing workers to inward-oriented sectors, where wages and working conditions are generally much less favourable. And it would inevitably depress their overall growth prospects – without a doubt the most decisive factor for raising social and environmental standards.

It is important to keep in mind that all countries come from different starting points in terms of social standards. In a speech to the World Economic Forum, former Mexican President Ernesto Zedillo pointed out that workers in trade-related activities often found that their new job was a significant improvement over their prior occupation in agriculture or in the informal sector of the economy. In many cases, these jobs are just a step toward better opportunities. In the final analysis, it is progress that matters the most when considering the standards of a given country.

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[23] Arjit Ghose, *"Jobs and incomes in a globalizing world"*, International Labour Organization, 2003
[24] Organisation for Economic Co-operation and Development, *"Measuring globalisation: the role of multinationals in OECD economies*", 1999
[25] Diana Farrell, Jaana K. Remes and Heiner Schulz*, "The truth about foreign direct investment in emerging markerts"*, McKinsey Global Institute, 2004
[26] Glen Dowell, Stuart Hart and Bernard Yeung, *"Do Corporate Global Environmental Standards Create or Destroy Market Value?"*, Management Science, Vol 46, pp 1059–1074, 2000
[27] Gene Grossman and Alan B. Krueger, *"Economic Growth and the Environment"*, NBER working paper 4634, Quarterly Journal of Economics, vol. 110, pp 353–378, 1995
[28] Wheeler, *"Racing to the Bottom? Foreign Investment and Air Pollution in Developing Countries"*, World Bank, 2002

Is globalization widening the gap between rich and poor?

No. The gap has narrowed during the last two decades

It is often claimed that the gap between rich and poor has been widening over recent decades and that the living conditions of the poor have deteriorated as a result of globalization. A recurrent figure, drawn from the 1999 Human Development Report of the United Nations Development Programme (UNDP), gives an alarming account: "Gaps in income between the poorest and richest people and countries have continued to widen. In 1960 the 20% of the world's people in the richest countries had 30 times the income of the poorest 20% – in 1997, 74 times as much".

Correcting the record

New research disproves such claims and sheds a much more favourable light on the contribution of global economic integration to incomes and income distribution. In a study for the National Bureau of Economic Research, Xavier Sala-i-Martin points out that the UNDP report computed its poverty ratios by simply comparing unadjusted incomes, thus ignoring the fact that the cost of living is lower in developing countries[29]. Once adjusted for purchasing power parity, the poverty ratio of the richest 20% to the poorest 20% has actually started to diminish over the last two decades, according to Sala-i-Martin. "Rather than rising from 20 to 74, the ratio increases from 11.3 in 1960 to 15.9 in 1980, but then declines slowly to 15.09 in 1998".

Analyzing inequality between individuals – rather than between countries – provides a different picture of the actual trends in income distribution across the world.

Many economists have also identified another important shortcoming in the methodology used in the UNDP report. It considers each country as a point of comparison regardless of its population size. It thereby gives equal weight to China and any much smaller African country, while in reality China's population is twice that of all 35 African countries put together. Analyzing inequality between individuals – rather than between countries – provides a different picture of the actual trends in income distribution across the world.

Massive poverty reduction

Using nine different indexes to measure income distribution between individuals, Sala-i-Martin shows that there has been a substantial narrowing of the gap between rich and poor during the last two decades. Other studies by Surjit Bhalla[30] and Arne Melchior[31] reach similar conclusions. This decline in global inequalities is mainly the result of massive poverty reduction in countries such as India and China, which account for 38% of the world's population, and other large developing countries. Bhalla estimates that the proportion of people in the world living on less than a dollar a day has fallen from 30% in 1987 to 13.1% in 2000. In Asia, more than 650 million people were lifted out of deep poverty between 1970 and 2000.

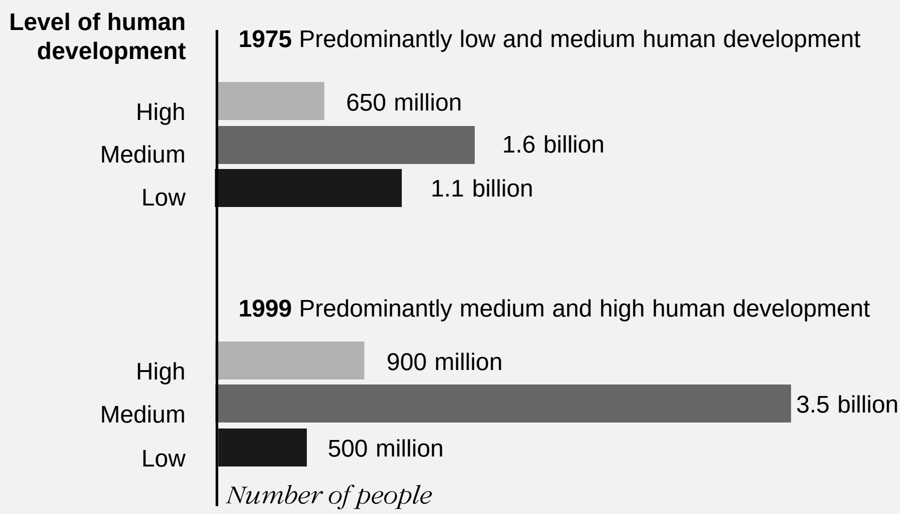
The proportion of people in the world living on less than a dollar a day has fallen from 30% in 1987 to 13.1% in 2000, according to estimates by the Institute for International Economics.

Quality of life

The number of undernourished people in the world has been reduced from 920 million in 1970 to 810 million today.

When measuring poverty, it is important to take into account living standards and not just incomes. Here again, the evidence is that, overall, quality of life has improved in the developing world. According to the Australian Department of Foreign Affairs and Trade, the number of undernourished people in the world has been reduced from 920 million in 1970 to 810 million today. A World Bank study says that school enrolments in Uganda doubled during the 1990s. In a report for the Brookings Institution Global Inequality Group, Gary Burtless shows that life expectancy has been rising almost everywhere in the world and that as a result "world inequality in the distribution of expected life spans has declined"[32].

Trends in living standards, according to human development indicators



Note: Data refer only to countries for which data are available for both 1975 and 1999.

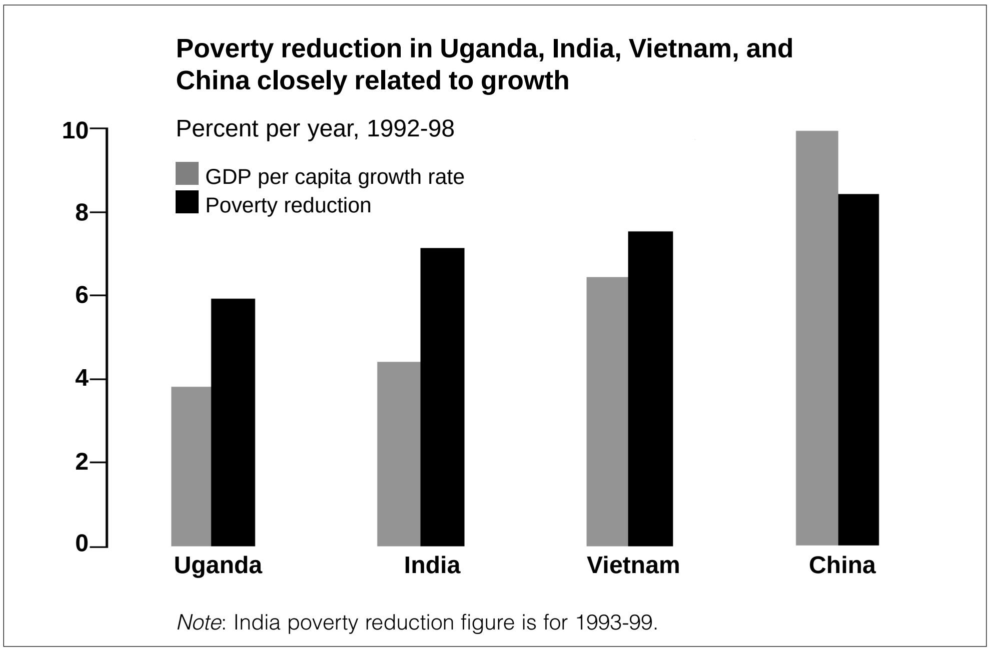
Source: Human Development Index, UNDP; *"Human Development Report 2001"*.

Domestic factors

Income distribution in a given country primarily depends on domestic factors such as economic policy choices and redistribution mechanisms.

The purpose here is not to give a picture that is rosier than reality. Many countries have suffered from increased marginalization and have been unable to reduce poverty over the last two decades. More than 40% of Africans live on less than a dollar a day, a proportion that has been steadily increasing in the continent as a whole since the 1970s. Conflict and bad governance persist in holding many African countries back from economic progress.

Inequalities have also increased *within* several countries with high levels of growth. For example, rapid economic growth in China has widened the gap between rural and urban areas. But as a World Bank report points out, "if this increase of inequality in China has been the price of growth, it has paid off in terms of massive reduction of poverty". In fact, income distribution in a given country primarily depends on domestic factors such as economic policy choices and redistribution mechanisms.



Source: World Bank, *"Globalization, Growth and Poverty"*, 2002.

[29] Xavier Sala-i-Martin, *"The Disturbing "Rise" of Global Income Inequality"*, National Bureau of Economic Research, Working Paper 8904, 2002 and *"The World Distribution of Income (estimated from individual country distributions)"*, National Bureau of Economic Research, Working Paper 8933, 2002

[30] Surjit Bhalla, *"Imagine There's No Country: Poverty, Inequality and Growth in the Era of Globalisation"*, Institute for International Economics, 2002

[31] Arne Melchior, *"Global Income Inequality. Beliefs, facts and unresolved issues"*, World Economics, Vol. 2, No 3, July-September 2001

[32] Gary Burtless, *"Is the Global Gap between Rich and Poor Getting Wider?"*, The Brookings Institution, June 2002

Is globalization a threat to cultural diversity?

Yes and no

Globalization is both a factor for standardization and force for increased cultural diversity.

Undoubtedly, global economic integration has induced a certain degree of cultural homogeneity across nations, as illustrated by the increasing number of indistinguishable shopping centres around the world and the growing popularity of universal brands. Many lament such rampant uniformity – understandably so. But the danger is to forget that globalization is a multi-faceted process. Paradoxical as it may seem, globalization is both a factor for standardization and force for increased cultural diversity.

Increasing cultural exchange

By making more products and services available across continents, globalization has increased and diversified the supply of culture in most countries. Trade in cultural goods has grown exponentially over the last 20 years. Between 1980 and 1998, annual world trade of printed matter, literature, music, visual arts, cinema, photography, radio, television, games and sporting goods surged from US $95,340 million to US $387,927 million[33]. For consumers, this means greater choice, cheaper access to culture and increased exposure to new ideas.

Source: "Study on International Flows of Cultural Goods between 1980-1998", UNESCO, 2000.

For consumers, there is greater choice, cheaper access to culture and increased exposure to new ideas.

A recent poll by the Pew Institute shows that, in many developing countries, roughly nine out of 10 people feel there has been greater availability of foreign popular culture over recent years: Ukraine (94%), Lebanon (92%), Vietnam (92%), Indonesia (90%) Nigeria (89%) and Senegal (88%)[34]. There is concern, however, that this trend might also reflect greater hegemony of Western culture and values over the rest of the world. Much attention has also been drawn to the emergence of universally sold "global products" – some of them have now become symbols of globalization – and the irresistible spread of Western lifestyle.

Putting things in perspective reveals that there is no such cultural takeover. In Asia, three quarters of the music market is locally produced. Coca-Cola accounts for less than two of the 64 fluid ounces that the typical person drinks a day. For every McDonald's outlet in the UK, there are six Indian restaurants [35] . While greater exposure to Western culture in the non-Western world is a fact, the ability of people to adapt should not be underestimated. An interesting counter-current is underway, with people in different parts of the world defending their local cultures and at the same time seeking to diffuse them more broadly.

In Asia, three quarters of the music market is locally produced.

In other words, globalization can energize local identities. As G. Pascal Zachary, a senior writer at the Wall Street Journal, observes: "More people in more parts of the world are expressing their distinct social and cultural traditions than at any time since the dawn of European colonialism 500 years ago" [36]. The emergence of international news channels in Arabic (and soon in French) is a notable manifestation of this trend toward the global diffusion of local and national cultures.

The emergence of international news channels in Arabic (and soon in French) is a notable manifestation of this trend toward the global diffusion of local and national cultures.

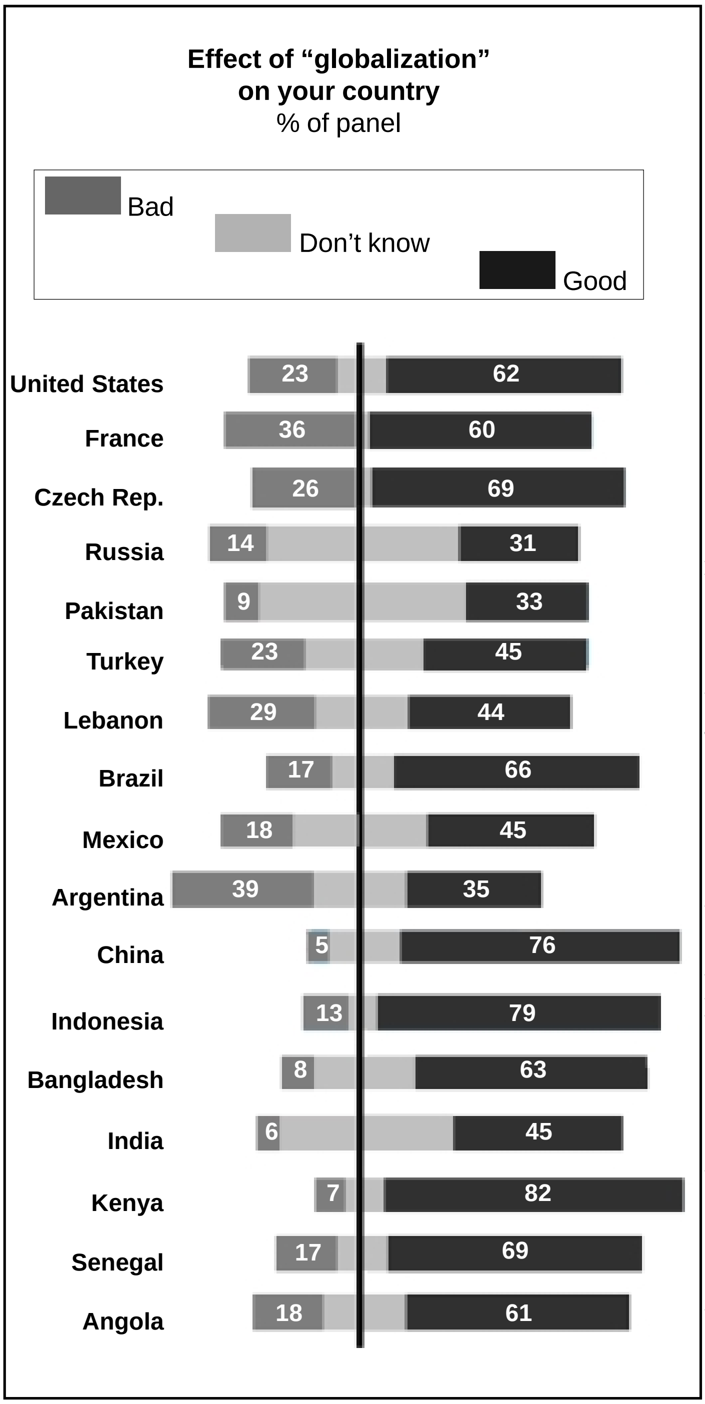
In this sense, globalization is a powerful force for increasing cultural exchanges and mutual understanding. The multiplication of ethnic restaurants in Western cities is an example of how globalization offers unprecedented choice. By promoting the intermingling of people and cultures, globalization exposes all parties to new ways of thinking and new ideas. During the period between 1942 and 1961, there was only one Nobel prize winner in literature who did not come from Europe or the US. Between 1962 and1981, there were already four from other regions. Between 1982 and 2001 there were eight [37].

The communication revolution also plays a vital role in promoting cultural enrichment and raising political awareness in general. Individual access to the Internet means that governments, even less democratic ones, have to abandon their monopoly on the flow of information. The globalization of communication is indeed providing many people with more freedom than they previously enjoyed.

33 United Nations Education, Scientific and Cultural Organization, "*Study on International Flows of Cultural Goods*, 1980-98", 2000
34 The Pew Research Center, *"Pew Global Attitudes Project: Views of a Changing World"*, 2003
35 Philippe Legrain, *"Open World:/ The Truth About Globalisation"*, 2002
36 G. Pascal Zachary, *"Get over it"*, in Foreign Policy, pp 62-63, September-October 2000
37 Herbert Oberhänsli and Oscar Vera, *"Globalization: Concerns and Opportunities for the People in the Developing World"*, 2003
38 Table drawn from: Tyler Cowen, *"Modern mix: a cultural blend"*, Forbes Global, 2003

How do people in different parts of the world view globalization?

The majority say it is "a good thing"



Source: The Pew Research Center, *"Pew Global Attitudes Project: Views of a Changing World"*, 2003.

Polls conducted to sound out public opinion on globalization concur: an overwhelming majority of people almost everywhere think globalization is good for them and their country. Some of the findings are particularly telling:

- A survey of 25,000 citizens across 25 countries –14 of them in the developing world – shows that close to 75% believe globalization improves their lives and those of their families [39].

- According to another worldwide survey, support for globalization is strongest in Nigeria (90%), South Korea (84%) and Kenya (82%), followed closely by Indonesia (79%), Vietnam (79%) and China (76%). In South Africa and Uganda, four out of 10 even see globalization as a *very* good thing [40].

- In North America and Western Europe, most people also have a positive view of globalization, but opposition is stronger than in the developing world. In the European Union, 63% say they are in favour of globalization, 29% against [41].

- In France, six out of 10 think globalization is good for their country, while 36% have a negative opinion – the largest percentage among wealthy countries.

- Globalization is more popular among the young. In France, 72% of those below 30 years of age say globalization is a good thing, compared to 58% of respondents older than 50. More than 60% of young Peruvians view globalization favourably, compared with only a third of those their parents' age.

- In a recent survey conducted in the US, two thirds of respondents agreed with the following statement: "I favour free trade, and I believe it is necessary for the government to have programs to help workers who lose their jobs". Only 18% advocated free trade in the absence of such help [42].

- In sub-Saharan Africa, 75% of households think it is a good thing that multinational companies are investing in their countries.

- Nearly six out of 10 Nigerians (58%) and majorities in Vietnam (55%), Pakistan (55%) and Uganda (53%) say that the growth of trade and business has been *very* good for themselves and their families.

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[39] Environics International/World Economic Forum, *"Global Public Opinion on Globalization"*, 2002
[40] The Pew Research Center, *"Pew Global Attitudes Project: Views of a Changing World"*, 2003
[41] Eurobarometer/European Commission, *"Globalisation"*, 2003
[42] Program on International Policy Attitudes, *"Americans on Globalization: A Study of U.S. Public Attitudes"*, March 2000

Suggested reading

In "*Jobs and incomes in a globalizing world*" (2003), Ajit K. Ghose from the International Labour Organization finds many of the public concerns about globalization – notably its impact on jobs, income distribution and labour standards – to be unfounded.

Philippe Legrain offers a humorous and thought-provoking analysis of globalization in "*Open World:/ The Truth about Globalisation*" (2002). In a similar vein, Jagdish Bhagwati's "*In Defense of Globalization*" (2004) takes on globalization's critics and makes the case for the global economy, using vivid examples and sharp arguments.

A new website by Herbert Oberhänsli and Oscar H. Vera, *www.humanglobalization.org* provides a useful source of information on globalization, with numerous statistics and case studies on the positive contribution of globalization to raising living standards in developing countries.

In "*Globalization: Fads, Fictions and Facts*" (2003), Tim O'Neill analyses the institutional and social manifestations of globalization on domestic economies. He argues that the extent of global economic integration has been over-stated and that resulting constraints on economic and social policy are far smaller than is often argued.

The World Bank's "*Global Economic Prospects 2004*" focuses on the potential benefits for developing countries of a successful Doha round of multilateral trade negotiations. In its "*World Trade Report 2003*", the World Trade Organization examines recent developments in trade and trade policy, with a particular focus on South-South trade. "*Rigged Rules and Double Standards: Trade, Globalisation and the Fight Against Poverty*" (2002) by Oxfam shows that trade barriers imposed by rich countries on poor countries may well be the major obstacle to massive poverty reduction.

In February 2004, the International Labour Organization released "*A Fair Globalization: Creating Opportunities for All*". This report was prepared by the World Commission on the Social Dimension of Globalization, a panel of political leaders, economists, professors and representatives of business, labour and civil society from across the world. While recognizing that globalization's "potential for good is immense", the report calls for an "urgent rethink" of current policies and institutions of global governance.

In a new book entitled *"Why Globalization Works"*, Financial Times columnist Martin Wolf argues that the political fragmentation of the world into almost 200 independent sovereign states – many of which are very badly governed ('failed states') – constitutes a huge obstacle to reducing poverty and inequality through the spread of globalization.

The Center for Strategic & International Studies recently launched *www.globalization101.org,* a student's guide to globalization, with useful issue briefs and news analyses.

The International Chamber of Commerce

ICC is the world business organization, the only representative body that speaks with authority on behalf of enterprises from all sectors in every part of the world.

ICC promotes an open international trade and investment system and the market economy. Its conviction that trade is a powerful force for peace and prosperity dates from the organization's origins early in the 20th century. The small group of far-sighted business leaders who founded ICC called themselves "the merchants of peace".

Because its member companies and associations are themselves engaged in international business, ICC has unrivalled authority in making rules that govern the conduct of business across borders. Although these rules are voluntary, they are observed in countless thousands of transactions every day and have become part of the fabric of international trade.

ICC also provides essential services, foremost among them the ICC International Court of Arbitration, the world's leading arbitral institution.

Within a year of the creation of the United Nations, ICC was granted consultative status at the highest level with the UN and its specialized agencies.

Business leaders and experts drawn from the ICC membership establish the business stance on broad issues of trade and investment policy as well as on vital technical and sectoral subjects. These include financial services, information technologies, telecommunications, marketing ethics, the environment, transportation, competition law and intellectual property, among others.

ICC was founded in 1919. Today it groups thousands of member companies and associations from over 130 countries. National committees in the world's major capitals coordinate with their membership to address the concerns of the business community and to convey to their governments the business views formulated by ICC.

ICC
International Chamber of Commerce
38, Cours Albert 1er, 75008 Paris, France
Telephone +33 1 49 53 28 28   Fax +33 1 49 53 28 59
Web Site www.iccwbo.org   E-mail icc@iccwbo.org