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Globalization and inclusive development

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Executive summary

This note highlights some topical policy issues that could contribute to promoting a more inclusive, pro-poor process of globalization. The issues selected aim to take advantage of the window of opportunity that has opened up as a result of the last five years of unprecedented economic growth. The international community currently faces two broad challenges: first, the current growth trends need to be actively maintained, so as to allow an increasing number of developing countries to reap the benefits of globalization; and, second, there is a need to ensure that the process of globalization becomes more inclusive, so that it benefits countries and sectors of the population that have been left out. A number of issues that require policy attention are highlighted, including aspects relating to trade policy, regional integration, new and innovative financial mechanisms, building productive capacity, the global value-chain, the promises and perils of commodities, climate change and environmental concerns and opportunities, and the role of aid, including aid for trade.

I. Introduction: the promise of globalization

1. The world economy has experienced unprecedented growth in the past five years. This has allowed many developing countries to make significant economic progress, achieving on average 5–6 per cent growth. In 2006, only two of 132 developing countries recorded falling real income, compared to seven countries in the period 2000–2005 and 13 in the half decade before that. Millions of people have been lifted out of extreme poverty and many developing countries have also been able to make some progress towards achieving the Millennium Development Goals.

2. This dynamic growth in developing countries has been stimulated by an intensification of globalization in the form of trade and investment flows. Since 1995, world merchandise trade has been growing at an annual average rate of 7.5 per cent. A distinguishing feature in the emerging pattern of globalization is the increased role played by developing countries: real exports of developing economies nearly tripled between 1996 and 2006, while those from the G-7 rose by only 75 per cent. Asia clearly dominated the picture, with transition economies and Latin America coming in second, and Africa showing exactly the same increase as the G-7. In terms of imports, the expansion in different regions was much closer. Overall, the share of developing countries in global trade increased from 29 per cent in 1996 to 34 per cent in 2006.

3. A related development has been the sustained rise in South-South exchanges. For example, South-South merchandise trade is estimated to have expanded from US\$ 577 billion in 1995 to US\$ 1.7 trillion in 2005. This resulted in a concomitant increase in the South-South share of world merchandise exports to 15 per cent in 2005, compared to 11 per cent in 1995. During the last two decades, the shares of a number of emerging economies in international merchandise and services trade have grown considerably.

4. Another interesting feature of the current expansion is the boom in commodity demand and prices. Common factors responsible for the price increases include the rapid pace of industrialization in the South, especially in China, but also in India and other emerging developing countries, and increased demand for biofuels. The rise in commodity prices has generated surpluses for many commodity-producing developing countries and has led to significant and prolonged improvements in their terms of trade.

5. These developments have helped some countries make progress towards the Millennium Development Goals. As noted in the *Millennium Development Goals Report 2007*, worldwide the number of people in developing countries living on less than \$1 a day fell to 980 million in 2004, down from 1.25 billion in 1990. The proportion of people in extreme poverty fell from nearly a third to 19 per cent. Indeed, if current trends continue, most regions will achieve the goal of halving the proportion of people living in extreme poverty. There has also been progress towards many other goals, such as improving education, with primary-school enrolment growing from 80 per cent in 1991 to 88 per cent in 2004, most of this progress having been achieved since 1999. Not surprisingly, much of this progress is due to significant advances made by countries of the South and south-east Asian countries in recent years.

II. The qualification: the benefits of globalization have not yet reached all

6. Despite the impressive performance of developing countries as a whole in recent years, and the aggregate development progress achieved, many countries, in particular the least developed and other low-income economies, have not been able to benefit from the propitious environment. Despite the recovery in 2003–2007, the per capita growth rates in Africa (3 per cent on average) and the developing countries of America (3.5 per cent) were only half that in East and South Asia (6.3 per cent). Moreover, some countries have not been lifted to the same extent by the economic recovery and continue to rely on exports of low-value-added primary commodities. These countries have suffered from worsening terms of trade, highly volatile world prices and a decline in their share in world trade. For example, the export share of the 50 least developed countries (LDCs), fell from 2.5 per cent in 1960 to about 0.5 per cent in 1995, and has since hovered around this level, though the improvement in commodity prices helped raise their share to 0.8 per cent in 2006.

7. In addition, many countries, especially the least developed countries and lower- and middle-income developing and transition countries, have been unable to translate growth effectively into poverty reduction and broader human development. For example, despite its recent recovery, the proportion of people living in extreme poverty in sub-Saharan Africa (which includes 34 of the 50 LDCs), remains very high, decreasing only from 46.8 per cent in 1990 to 41.1 per cent in 2004. Given the rapid population growth, this has meant that the number of people living on less than \$1 a day has actually been increasing, and is only now beginning to level off. Even in some of the faster-growing developing economies, some segments of the population continue to be excluded from the benefits. Poverty has been increasing in western Asia, for example, and continues to fall only slowly in Latin America and the Caribbean.

8. One of the disconcerting consequences of the new wave of globalization is therefore the rise of inequality, both within and between countries, be they developed or developing. Today, the richest 2 per cent of the world's adult population owns more than half of global household wealth. The bottom half, in contrast, barely owns 1 per cent.¹

9. The international community now faces two broad challenges. First, the current growth trends need to be actively maintained, so as to allow a growing number of developing countries to reap the benefits of globalization. This means addressing potential downside risks such as global imbalances, disturbances in financial markets, further increases in energy prices and the slow development of alternative technologies, and the potential reversal of commodity prices. Second, there is a crucial need to ensure that the current process of globalization becomes more inclusive. While economic growth has touched more economies than ever before, many developing countries continue to be left out. Also, even in countries that have benefited as a whole, there are communities or sectors of the population that have not been included.

10. This note is concerned with this second challenge. In concrete terms, promoting inclusive development requires the reduction of poverty, unemployment and underemployment; bringing lagging countries into global knowledge systems and global value-chains; and ensuring that marginalized communities have access to housing, health, education and other social services,

¹ See "Inclusive globalization" in the United Nations Development Programme's *Annual Report 2007*.

are able to exercise their civic, civil and political rights and are able to expand their “capacities and capabilities”.²

III. Policy response: much more can be done to promote inclusive and pro-poor globalization

11. This section identifies some of the main policy areas that need to be addressed in order to make the globalization process more inclusive. There is evidence to suggest, especially in Africa and LDCs, that the recent trends in global growth have not generated the level of employment that will help reduce poverty. The International Labour Organization (ILO) estimates that worldwide unemployment stands at about 200 million people, rising to one third of the global workforce if the definition is broadened to include those who are underemployed.³ The problem of jobless growth in commodity-dependent economies, for example, requires policy attention. In other areas, unemployment or underemployment is more related to falling productivity, or lack of productive capacity. In LDCs, for example, where the labour force is expected to increase significantly over the next few years,⁴ falling farm size and increasing population growth is making it harder for agricultural workers to make a living. Low levels of investment and innovation in agriculture fuel a vicious cycle of poverty, prompting rural dwellers to look for work in the urban and non-agricultural sector, where there are, however, very few employment opportunities.

12. Moreover, what is ultimately desired is not just employment per se, but rather employment that pays sufficiently well and that allows people to enjoy more fulfilling lives. The following broad policy areas are therefore worth considering.

A. Access is important, but trade policy must increasingly address other issues

13. Further liberalization of trade in goods and services through the Doha round offers an important opportunity to allow more countries to benefit from trade. If it delivers on its “development agenda”, the round may begin to correct existing imbalances in the trading regime. Agriculture continues to be the linchpin of the negotiations, but as many middle-income countries have already become producers and exporters of manufactured goods, the Doha round must also result in significantly enhanced and additional real market access for developing countries’ exports in these sectors.

14. Other important areas for discussion include the need to liberalize trade in services, including the Mode 4 movement of natural persons. This would have a very large and positive impact in developing countries, in part because of the sheer size of the services economy. It has been estimated, for example, that welfare gains from liberalizing the movement of workers could amount to US\$ 156 billion a year if developed countries increased their quota for the entry of workers from developing countries by 3 per cent. Another study has projected annual gains of some US\$ 200 billion if a temporary work visa scheme was adopted multilaterally.

² Sen, Amartya (2000), *Development as Freedom*, New York: Knopf.

³ Sachs, Ignacy, “Inclusive development strategy in an era of globalization”, ILO Working Paper No. 35, Geneva, May 2004, p. 4.

⁴ See *The Least Developed Countries Report 2006* (UNCTAD/LDC/2006).

15. Policy attention should also be directed to the increasing application of non-tariff barriers, both as instruments of protection and for regulating trade. The nature of the non-tariff barriers most often applied has changed: measures intended to protect local consumers have increased, while measures meant to protect local producers have declined. In many developed countries, regulatory policy now focuses on protection of the environment, public health and safety, and often includes higher standards for the domestic market than existing international standards. These regulations may help promote higher prices for exporters from developing countries, but they may also open avenues for protectionist abuse and also entail greater compliance costs than would otherwise be the case. Some domestic subsidies that are currently allowed may have distorting effects on trade.

B. Regional integration as a stepping stone to markets and multilateral alliances

16. In addition to further liberalization of trade in the multilateral system, further progress can also be achieved through strategic regional integration. South-South investment and trade is emerging as a major new force in the world economy, with potentially far-reaching implications. For example, South-South agreements can achieve rapid boosts in production, consumption and trade at the regional level, as well as helping to underpin the position of developing countries in South-North agreements.⁵ Other promising areas which may require policy attention at the regional level include trade and transit facilitation, transport infrastructure, investment projects in energy and water supplies, projects in industrial development and research and development, and shortcomings in the international financial system. These initiatives are often too costly and risky for an individual developing country but may be viable if several countries pool their resources.

C. Developing new and innovative financial mechanisms

17. In addition to seeking ways to boost the benefits of foreign direct investment, policy attention needs to be directed to uncovering innovative and new financial mechanisms to help mobilize domestic and global resources. These include improving access to capital for small enterprises and the poor by reducing the costs of asymmetric information and by mainstreaming products such as micro-insurance and microfinance. There is a need for continued exploration of other new instruments that can potentially boost the pool of finance, including from new capital-surplus countries. The growth of some forms of South-South investment may help to bring about a more inclusive globalization, while more information is needed on the implications of increased portfolio investment to developing countries.

18. Ensuring that developing countries participate more equally in global credit markets is another area where a strategic policy approach is needed. The cost of capital in global markets is typically much lower than the costs that are charged to developing-country entrepreneurs. Policy attention needs to be paid to the search for new mechanisms to improve market information and to reduce the high transaction costs that can create barriers to viable business plans.

19. Another issue for discussion is the potential for a global monitoring and coordinating mechanism to reduce the likelihood and costs of financial crises caused by systemic vulnerabilities in the global financial markets. These can have particularly devastating effects on the poor, who lack financial resilience.

⁵ See *Trade and Development Report, 2007* (UNCTAD/TDR/2007).

D. Building productive capacity

20. In order to participate fully in the global economy, developing countries must first have productive capacity and become more competitive. In part, this is an issue of the natural resources with which a country is endowed, but increasingly in the modern global economy it is also a question of created advantages relating to infrastructure, human capital, skills, resources and knowledge. The crucial lack of adequate transport, telecommunications and energy infrastructure in many developing countries requires a range of policy responses including public-private partnerships, foreign direct investment and domestic resource mobilization.⁶ One of the challenges for improving inclusion is that mechanisms to recoup the costs of investment in essential infrastructure and utilities can be disproportionately damaging to the poor, so that new approaches for financing and service provision may be required.

21. Skills development and training is another important ingredient to help create a more inclusive global economy. Both in the agricultural and non-agricultural sectors, policy attention is needed to help introduce new productive techniques, investment in innovation and research and development, better entrepreneurial skills, and management and marketing training. The extent to which skills and technology can be boosted through mechanisms such as foreign direct investment, global knowledge partnerships, public-private initiatives and even migration policy, is yet to be fully addressed by developed and developing countries.

E. Creating synergies through the global value-chain

22. There can be important synergies between modern, large-scale enterprises (often producing for export) and local, small-scale enterprises, but these will not always occur automatically and may need to be directly addressed through industrial policy. This is most apparent in some of the newly dynamic economic sectors such as tourism. It is not always obvious to local communities how they can fit effectively into the global value-chain. However, some service sectors, particularly those with long and cross-cutting production processes, offer many possibilities for domestic enterprises to participate more fully if the enabling policies are in place. Promoting beneficial linkages through procurement and employment may require proactive public policies in addition to the adoption of corporate social responsibility policies and practices by enterprises and industrial organizations.

F. The promises and perils of commodities

23. Commodity-dependent economies are historically more likely to be excluded from the benefits of globalization than economies with a more diversified resource base. Out of 144 developing countries, 86 depend on commodities for more than half of their export earnings. In the past, falling and highly volatile prices for key commodities have made this dependence particularly problematic, but today the current boom in commodity prices created by new demand in the emerging economies has opened up new opportunities for commodity-rich countries.⁷ Policy issues that are attracting the attention of the international community include: the need to find new approaches to investment that are more advantageous to host countries; how to improve the transparency and accountability of international revenue payments in the sector; and the related need for recipient Governments to use their

⁶ See *Economic Development in Africa: Reclaiming Policy Space* (UNCTAD/ALDC/AFRICA/2007).

⁷ See *World Investment Report 2007* (UNCTAD/WIR/2007).

revenues wisely and in ways that lead to a more equitable distribution to the poor. Moreover, commodity-dependent countries are looking for ways to diversify more into upstream and downstream activities related to the commodities sector, such as distribution and higher value-added processing activities; in addition to diversifying beyond the commodities sector.

G. Climate change and environmental concerns and opportunities

24. Growing concerns about climate change, biodiversity and the environment are being reflected in a number of policy measures aimed at developing and developed countries alike. There may be a re-thinking of industrial policy, with particular implications for developing countries, for example, whether the traditional trajectory from agriculture through manufacturing to the services economy needs to be followed slavishly, or whether they can leapfrog to a cleaner and greener diversified economy. In other areas, the search for new cleaner technologies can have positive implications for developing countries, if, for example, increased research and development leads to approaches or tools that reduce the costs of providing infrastructure services for remote or distant communities. Other opportunities that are opened up also require a positive policy response from many developing countries, in gearing up to the high certification standards required in organic agriculture, for example; or in enhancing their branding and marketing of high-value biodiverse products.

H. Aid must be more inclusive

25. In recent years, donor countries have been increasingly focusing their official development assistance on emergency aid and social services such as education and health. Recent UNCTAD research argues that these important contributions need to be supplemented by a more strategic approach that recognizes that long-term sustainability requires donor investment in productive capacities, including knowledge, science and technology, and enterprise development.⁸

26. One example on the global radar screen – aid for trade – could be a promising approach for pro-poor and more inclusive economic development. Despite the increase in market-access opportunities, the participation in global markets of many developing countries can be hampered by supply constraints or lack of infrastructure. Aid-for-trade could help to address these problems. The pledges offered by the leaders of developed countries now need to be realized, once an appropriate framework for identifying and implementing the most effective policy levers has been agreed.

27. Policy attention needs to be directed to finding the most critical areas where the resources generated through aid-for-trade could be most effectively deployed. Assessment at the level of individual countries and sectors is needed in order to identify and prioritize the most important areas where aid, rather than private investment, is most appropriate. It is likely that these will be characterized by aspects of public goods, transaction costs, asymmetric information, risk and uncertainty. Transport costs, for example are an increasingly important element in competitiveness. Landlocked countries experience transport costs as a barrier that can be three times as large as the tariff barriers they face in developed countries; but even countries with good port and harbour facilities may face a disproportionately heavy cost in meeting stricter international safety and security standards. Capital requirements are often too high for the Governments of developing countries, and the public-good

⁸ See *The Least Developed Countries Report 2006* (UNCTAD/LDC/2006).

aspects of much infrastructure are such that the market alone is unlikely to provide what is needed. Another important area where aid-for-trade is likely to be effective concerns the financing of research and development: an activity that can be critical if LDCs are to increase innovation, productivity and value-added in agricultural and other sectors. Even in developed countries, research and development is costly, risky and characterized by uncertainty, and is frequently funded in part, if not in full, by public rather than private investment.

IV. Conclusion

28. This paper has highlighted some topical policy issues that could contribute to promoting a more inclusive, pro-poor process of globalization by taking advantage of the window of opportunity that has opened up as a result of the last five years of unprecedented economic growth. A more measured and coherent approach is needed to ensure that the benefits generated by globalization are more widely shared, and so can help to reduce the gap between those who have benefited and those for whom the benefits have not yet been forthcoming.
