III. Key trade and development issues in the current global economic environment

84. The unprecedented pace, scope and scale of globalization described above have not only given rise to new realities but also sharpened or given urgency and renewed focus to some key trade and development issues. Facilitating the quantitative and qualitative integration of developing countries, and countries with economies in transition, into the international trading system requires that these key trade and development issues be identified and that, in the years ahead, their implications for development be assessed, and relevant policies and measures at both national and international levels be elaborated. This chapter will identify a number of such issues, including the new South and South–South trade, energy security, labour mobility, services, commodities, environment and climate change, and technology and innovation.

A. The emergence of the "new South"

85. North–South trade remains important, with the North providing the main markets and sources of imports, investment and technology for developing countries. Conversely, the South is now becoming a major source and destination market for the North, a fact that reflects growing interdependence. Furthermore, what is significant is that South–South trade, in terms of both quantity and quality, has emerged from the periphery of world trade towards becoming a more central and dynamic aspect. Integral to this transformational change has been the rise of the new South – a new breed of dynamically growing trading and investing countries with wide-ranging portfolios and global enterprises. Globalization now has a Southern face too. There has been a marked diversification of export-import baskets and improvement in terms of trade, including through increased complementarities and trade. South–South merchandise trade increased threefold from $577 billion in 1995 to $1.7 trillion in 2005; this raised the South–South share of world merchandise exports to 15 per cent in 2005, accounting for 46 per cent of those countries' merchandise trade. The manufacturing sector represented a large part of South–South trade, accounting for 42 per cent in 2005, but commodities are becoming dominant and services trade has begun to thrive.

86. Intraregional trade is the mainstay of South–South trade, but interregional trade has burgeoned, particularly since 2000. Intra-Asian South–South trade accounts for 80 per cent of the Asian region's South–South trade, but there has been a surge in Asia's trade with Africa and Latin America, driven largely by its demand for energy, food and industrial raw materials, and its exports of manufactures to other developing regions. While China is a main driver of South–South trade expansion (China–Africa merchandise trade totalled $55.5 billion in 2006), India, Brazil, South Africa and South-East Asian countries are also potential regional and interregional drivers.

87. The implications of this phenomenon for the drivers themselves, other developing countries and the rest of the world are manifold and evolving. The new South's ascent, capacity and persistent challenges require a realistic assessment and systematic monitoring, so that growth continues and in turn contributes to replication of further successes in those countries and the rest of the South. This can be better ensured with the emulation of the new South's best trade practices, including in supporting productive capacity, value addition, infrastructure-building

and linkages, and transfer of appropriate technologies. Institutional adaptation and innovation at national, regional and global levels are required in order to more effectively tap and realize the development potential of the South.

88. South–South trade is beginning to acquire a critical mass of its own. It will need continuous nurturing through appropriate trade and investment liberalization and facilitation and infrastructure agreements, financing arrangements, macroeconomic and regulatory policy coordination, and consultative mechanisms. Furthermore, the North can play a supportive role, including by providing preferential market access and South–South cumulation in rules of origin to build South–South production and trade chains. Already Northern enterprises have contributed to regional and interregional value and supply chains, and this should no doubt receive a further boost. Aid for Trade packages can be targeted to support South–South trade for a multiplier effect. Enhancement of the South's individual and collective purchasing power, productive capacity and demand growth is bound to be beneficial for all countries.

89. The promotion of South–South trade remains a desirable objective because of the market and investment opportunities that it offers to low-income developing countries. Systematic monitoring, research and analysis regarding South–South trade flows are essential in order to identify lessons and best practices that can contribute to replication of positive development experiences and sustain further development of such trade. One way in which UNCTAD could assist South–South interaction is through its research and analysis and by developing and strengthening a South–South trade information system. The continued servicing of the GSTP Agreement and its third round of negotiations by UNCTAD and the implementation of results remain central to UNCTAD's work on South–South trade. Furthermore, UNCTAD's support to institutional development for the South-South trade in commodities, services and manufactures and broader economic cooperation needs to be enhanced to meet the emerging need for institutional reforms.

90. A major feature of the new South is the emergence of developing countries as significant sources of investment. In absolute terms, outward FDI flows from developing countries increased – from an annual average of $65 billion in the 1990s to $120 billion in 2005. A small number of home countries are responsible for a large share of these FDI outflows, but companies from more and more countries see the need to explore investment opportunities abroad to defend or build a competitive position. The value of the stock of FDI from developing and transition economies was estimated at $1.4 trillion in 2005, or 13 per cent of the world total. As recently as 1990, only six developing and transition economies reported outward FDI stocks of more than $5 billion; by 2005, that threshold had been exceeded by 25 developing and transition economies.

91. This has given rise to the emergence of developing country TNCs. Southern TNCs invest proportionally more in developing countries than do their developed-country counterparts. FDI can assist host developing countries in a number of ways, including adding to financial resources and productive capacity, supporting export activity, creating employment and transferring technology. This assists the continuing burgeoning of developing economies and South-South cooperation. FDI by developing-country TNCs can result in proportionally greater gains where their competitive strengths, motives and strategies differ from developed-country TNCs. For example, they are more likely to establish greenfield operations, they more

commonly use standardized, non-proprietary technology, and the technological gap between local firms and their affiliates is narrower than the gap with affiliates established by developed-country TNCs. All this augurs well for South-South development cooperation, with the aim of maximizing gains and avoiding pitfalls.

B. Energy security

92. Energy is one of the most important drivers of economic development, especially in the context of increasing globalization, trade growth and the digital revolution. However, access to energy varies dramatically between countries and regions. For example, two billion people in developing countries lack access to electricity and need to be taken out of this energy poverty. Energy demand and uses by developing countries are growing exponentially owing to population growth and economic requirements for building infrastructure, including transport, productive capacity in agriculture and manufacturing, and trade competitiveness. By 2030, developing countries will account for almost half of total energy demand. The International Energy Agency estimates that satisfying global demand requires a cumulative investment in energy-supply infrastructure of more than $20 trillion over the period 2005–2030, with at least half this amount being directed to developing countries.

93. Owing to rapid increases in world consumption and geopolitical upheavals, the past few years have witnessed wide fluctuations in oil prices, which reached a record high in the summer of 2006 at $70 a barrel. One obvious effect of this is higher oil import bills. It has also had a greater impact on oil-importing middle-income developing countries, where industrialization has led to greater dependence on oil imports.

94. For oil-exporting countries, the main challenge is to invest the surpluses prudently in order to ensure income for future generations and to ensure that the revenue flow does not cause real exchange rate appreciation, weaken competitiveness or lead to overdependence on a single sector. Local participation in both upstream and downstream activities needs to be increased. The impact on oil-importing countries tends to be a greater absorption of export revenues through rising import bills, higher transportation costs and inflation rates, and reduced GDP growth, trade competitiveness and resources for anti-poverty programmes. Oil-importing developing countries, especially LDCs, need to adopt measures that mitigate the effects of oil price peaks through appropriate arrangements and need to be supported by developing partners through appropriate stabilization/compensatory finance funding mechanisms.

95. Diversifying into renewable energy sources is an imperative at national, regional and global levels for economic and environmental sustainability. Awareness of this has pushed energy security and rebalancing of energy mixes high up the trade and development policy agenda of all countries and of the corporate sector. At the global level, the imperatives for creative solutions through R&D and coalitions of energy users and producers for efficient use of energy and renewable energy sources cannot be overemphasized. Increasing adoption of energy efficiency standards will affect production and processing methods in traded goods and services, thus impacting on the trade competitiveness and productive capacities of developing countries. Sustainable energy mixes best suited to each country’s situation and strategic and development-conducive energy portfolios are needed.

96. Among the products emerging from the search for a new economic model based on low-carbon emissions are biofuels. The biofuels sector has experienced considerable development over the past decade. To ensure that biofuels production and use yield positive environmental and development results, Governments have to develop appropriate strategies on issues such as whether biofuel production is intended for transportation or for broader energy replacement, land requirements and which conversion technology is desirable. The economic and environmental impacts, the compatibility of biofuels with existing fuel delivery/use infrastructures and competing uses for biomass also have to be assessed. Country-based assessments (such as those undertaken by UNCTAD in Guatemala and the jatropha plantation development in Ghana) will help countries to better engage with biofuels and assist them in setting up the required domestic frameworks. For biofuels to make a major contribution to development, it is important that the comparative advantage of the South in this area be recognized and given scope, and that the South be involved in standard-setting.

C. Mobility and development: Labour integration

97. There are unprecedented and increasing opportunities for labour integration and mobility in the context of trade- and investment-led globalization. This is due to several factors, including growing complementarities between developed and developing countries with respect to demographics and labour force (e.g. an ageing population in developed countries versus a young one in developing countries, skill shortages in developed countries and surpluses in developing countries at all skill levels in key sectors); innovations in transport, telecommunications and ICT which allow easy access to cost-quality competitive labour anywhere in the world (e.g. the outsourcing of business services); the growth of new labour-intensive sectors such as nursing- home and health-care services; and productivity and wage differentials between developed and developing countries.

98. With these push and pull factors and the obvious benefits and costs of migration for sending and receiving countries, the challenge is to ensure that there is "gain" rather than "drain" from migration for all as a result of liberalizing the movement of people. The socio-economic benefits to the sending countries include the inflow of remittances and foreign exchange; and the return of skilled workers, which may increase local human capital stock, as well as transfer of skills and links to foreign networks (brain gain and circulation). Remittances have received much attention from sending countries as they are seen as a stable source of development finance.

99. There is a need for more conscious raising of awareness in both developed and developing countries of the actual costs and benefits of labour integration, together with a sustained dialogue between labour and global enterprises. This would include an economy-wide analysis of labour requirements sectorally, both domestic and foreign, and in the short to medium term in order to determine the best policy mix with respect to migration. International cooperation for a better managed migration policy would certainly be useful, including devising rules and regulations on employment and labour, visas, human resource development, structural adjustment policies and social safety nets. Policies could be geared towards better managing movements through regulated entry of temporary workers rather than outright prohibition leading to illegal migration and attendant problems. A meaningful

outcome to the Doha negotiations on Mode 4 would provide an important avenue for facilitating legal temporary movement of persons to supply services.

100. One way of assuaging public opinion in receiving countries and ensuring mutual benefits for both sending and receiving countries is to ensure temporariness of stay. This can include actions such as taxing employers, or requiring them to post bonds for every migrant recruited, or targeted incentives for migrants to return to their home country at the end of the contract, including through refunding their social security and pension contributions. Sending countries need to make maximum use of benefits from remittances and returning migrants; assist in the reintegration of returning migrant workers and stimulate investments; put in place the appropriate infrastructure and incentives; and invest in building the human capital base to mitigate possible negative effects of the movement of highly skilled workers.

101. UNCTAD, together with other international organizations in the Global Migration Group (GMG), will play its part by clarifying issues that lie at the interface of trade, migration and globalization for development in order to better equip policymakers everywhere and to shape public opinion in favour of a greater understanding of the true balance of benefits accruing from labour market integration. UNCTAD believes in the premise that it is a win-win situation for countries that are the origin of labour movements and those that are the destination of such movements, and for the global economy as a whole, if integration is managed by all concerned in an enlightened and cooperative spirit, with pragmatism, realism and a global strategic vision, and without political or cultural prejudice.

D. Services: The new trade and development frontier

102. Services contribute to economic growth and development through the creation of a competitive economy, providing new jobs, enhancing universal access to essential services and stimulating trade. Services sectors provide the backbone of an integrated and effective economy nationally, regionally and globally. An improved services economy improves performance in merchandise trade as the increased sophistication and availability of producer services enhance international competitiveness in exports of primary and manufactured goods. The informal services sector is also an important aspect of the services economy in developing countries. With globalization, the potential for developing countries to expand and diversify their economies through increased services development and trade has increased immensely. Today, services account for over 70 per cent of employment in developed countries and about 35 per cent in developing countries. World services trade has nearly tripled to reach $2.4 trillion, while the FDI inward stock has quadrupled to nearly $10 trillion in the wake of globalized production of goods and services It is widely acknowledged that increased services trade can generate development gains that cannot be achieved through a narrow focus on exports of primary commodities and manufactures alone.

103. Developing countries’ performance in services trade in recent years has been exceptional. Since 1990, services exports from developing countries have grown at an average annual rate of 8 per cent compared with 6 per cent for developed countries. Accordingly, their share of world services exports has climbed to 24 per cent. However, at present the services trade of developing countries is dominated by only a few of those countries. Asian countries account for 75 per cent of all

developing countries' services trade. Africa and Latin America and the Caribbean accounted for 10 per cent and 15 per cent respectively. The top 15 developing country services exporters account for 80 per cent of all developing country services exports. An increasing number of countries are successful in exporting services such as tourism, transport, construction, audiovisual, computer and information services, and business and professional services, particularly through Modes 1 and Mode 4. South–South trade in services is also expanding, and within this trade regional trade agreements play an important role.

104. However, the potential of services sector development and services trade is yet to be fully realized by many developing countries, especially in sub-Saharan Africa and LDCs. LDCs continue to be marginalized from international flows of services, with their share in world services exports being about 0.8 per cent. Also, most services in the informal sector are not tradable, a fact that reduces the ability to benefit from trade-led globalization. Positively integrating those countries into the services economy and trade and ensuring that they derive development gains remain a major development challenge. The Doha Round of negotiations on services offers an important avenue for liberalizing services trade in a development-friendly manner and from the perspective of developing countries, specifically through "meaningful" commitments in sectors and modes of export interest to them.

105. At the same time, for services liberalization to generate pro-development outcomes, the proper pacing and sequencing of reform and liberalization are crucial. Establishing regulatory and institutional frameworks that work well and are sound is a precondition for opening up services markets particularly essential services where universal access is vital. In developing countries, regulatory systems are still at an emerging stage, and this poses challenges for policymakers. Hence, there is a need for policy space for countries to go through the trial and error process, which allows them to identify the best policy in the light of their particular economic, social and developmental needs.

E. Commodities: Sustaining the new growth trend

106. A majority of developing countries are dependent on the commodity sector as the largest source of revenue and employment for the population and the principal source of external finance (foreign exchange) for development. Some 94 developing countries still derive more than 50 per cent of their export earnings from primary commodities. In addition, the commodity sector is beset by problems related to the workings of the international trading system. Persistent supply/demand imbalances in world commodity markets have been due, in varying degrees across commodities, partly to trade-distorting domestic support and export subsidies in certain industrialized countries. This not only displaces developing country exporters on world markets but also reduces world prices (e.g. cotton). Another factor has been pressures on low-income commodity-producing countries to increase export volumes, even in the face of declining world prices, so as to expand or maintain the level of foreign exchange earnings and thereby sustain debt servicing and import capacity.

107. Since 2002 there has been a "commodity boom", with international commodity prices showing a strong upward trend after their sharp fall from 1995–1997 to 2002. The rise in prices has been driven by the boom in metal and mineral prices, which have increased by 191 per cent, and crude oil prices, which have risen by 140 per

cent. Increases for agricultural raw materials and tropical beverages taken as groups averaged 58 per cent and 45 per cent, respectively. Common factors responsible for the price increases include the strong growth in the import demand of developing countries owing to the rapid pace of industrialization, especially in China but also in India and other emerging developing countries; the increased production of biofuels; and emerging supply constraints in some commodity markets. Notwithstanding the recent upward trends, the increases in commodity prices have not been large enough in some cases to offset the severe declines in prices suffered in the past. Expressed in current United States dollars, non-fuel commodity prices are still lower than they were in the early 1980s. In real terms, by the end of 2005 commodity prices were still about 30 per cent lower than the average for the period 1975–1985. Furthermore, low-income commodity-dependent developing countries continue to face difficulties in retaining international market shares.

108. Nevertheless, with prospects of better prices and stable demand growth for a considerable period of time, perhaps as much as 10 years, commodity-dependent developing countries may be able to generate sufficient finance to invest in their development and poverty reduction programmes. Their success in basing development on commodity production and trade will depend on both the international environment and their ability to undertake, alone or jointly, the necessary institutional changes.

109. Harnessing the present boom in commodity prices for development is an urgent matter for developing countries and the international community. It requires substantial investment in infrastructure and supply-side capacity-building. The AidforTrade initiative could play a critical role in supporting improvements in the competitiveness of traditional commodity sectors, vertical and horizontal diversification in commodity-dependent countries and the mitigation of the short-term impact of commodity “shocks” at the national level, including through the financing of safety net programmes for small and resource-poor producers seriously affected by commodity market instability.

110. It is also vital that issues relating to commodities be urgently and adequately addressed at the multilateral level. The Conference on the Global Initiative on Commodities, the first UNCTAD XII preparatory event, held in Brasilia from 7 to 11 May 2007, responded to this urgency by relaunching the commodities agenda from a poverty reduction and development perspective. The Global Commodity Initiative and its outcome represents the basis for an action agenda for a global commodity partnership strategy.

F. Environment, climate change and development: The challenges ahead

111. Any attempt to promote sustained development and reduce poverty must take the natural environment into consideration, as it is the poor who are most dependent on the natural environment to meet their daily food, health, livelihood and shelter needs. Therefore, the environment qualifies as an important global public good, and the interface between the environment, on the one hand, and trade and development, on the other hand, is a central component of the globalization process. There is in particular a general recognition that increased trade flows that result from globalization have to be accompanied by environmental sustainability and poverty reduction in order to truly achieve sustainable development. Environmental impact

is perceived as an increasingly important factor of production that directly bears on production costs, competitiveness and opportunities in international trade.

112. The trade, environment and sustainable development nexus in the context of globalization renders policy coherence and an enabling environment essential for developing countries to effectively and proactively respond to the challenges and opportunities of climate change and biodiversity, environmental requirements and market access, increasing material efficiency and lowering the pollution intensity of production for export, profiting from export opportunities in environmentally preferable products, and avoiding the tacit import of old/second-hand/prohibited goods into developing countries.

113. Climate change is a crucial factor of globalization that currently poses one of the greatest risks to environmental, social and economic development in both the developed and developing countries; it is having profound and irreversible direct and indirect effects that threaten to reverse decades of development efforts. Increasing emissions of greenhouse gases such as carbon dioxide and methane are causing changes in the global climate systems, with adverse impacts on developing countries and related significant economic costs if no remedial actions are taken. The impacts of climate change are inequitable. Poor countries are hit the hardest and earliest, and yet they account for only a relatively small share of total greenhouse gas emissions. Sectors that are crucial for the livelihood of the poor in developing countries such as agriculture, fisheries, industry, energy and transport are very sensitive to climate change. The introduction of climate response measures through the emerging carbon market and the Kyoto Protocol has trade and development implications, as it affects economic sectors such as transportation, energy use, electricity generation, agriculture and forestry.

114. One persistent environment-related problem, which has direct implications for trade and development, concerns the new environmental, health and food-safety requirements (EHFSRs) on the access of developing country products to key export markets. New EHFSRs are becoming more stringent, frequent, complex and interrelated. This poses serious challenges, but also provides opportunities for export competitiveness as well as sustainable production and consumption methods at national level. There is also a trend towards privatization of many EHFSRs and thus a related tacit alliance between mandatory and voluntary private-sector-set requirements. Governments establish product characteristics and product-related processes and production methods (PPMs), and the private sector follows up by imposing specific non-product-related PPMs to meet the product characteristics. Private standards are widely believed to be outside WTO disciplines, and thus pose challenges in terms of justifiability, transparency, discrimination and equivalence.

115. The new private-sector-architectured supply-chain requirements tend to marginalize smaller countries and producers. This contradicts pro-poor development strategies and disconnects those most in need of trading opportunities, in particular small farmers. On the positive side, growing consumer demand for environmentally preferable products presents new opportunities for those producers and countries that can produce in more energy-efficient and environmentally friendly ways – and can effectively communicate this fact to consumers. An example is the rapid expansion of organic agriculture markets, with global growth rates of over 12 per cent in the last few decades, compared with overall agriculture market growth. Generally, there is heightened interest in environmentally preferable products,

services and production methods since these are the strategic markets of the future. Equally important has been biotrade, providing impetus to this emerging market. Developing countries need to identify and exploit the market niches and opportunities open to them.

G. Technology and innovation for trade and competitiveness

116. New technologies are a key enabler of globalization. Two features in particular have emerged as burning issues for development. One is that ICTs play a critical role in the fragmentation of the global value-added chain and in shifting parts of production to different geographical locations. This feature has now been extended to the service industry and the delocalization to lower-cost markets. By using ICTs, firms are able to exchange knowledge and information online from anywhere in the world, communicate just-in-time with clients and suppliers, and deliver services efficiently and promptly. Developing countries are increasing their participation in global ICT goods trade. The other feature is that rapidly growing containerization of international seaborne trade has led to technological advances in cargo-handling equipment, the extensive application of IT-based management systems, and transport organization processes in seaports and inland freight terminals. A number of developing countries have anticipated trends in transport services and technologies and speedily adapted to changing requirements. However, problems remain to be solved in the many low-income and vulnerable countries, especially LDCs and LLDCs, where basic transport infrastructure is in urgent need of improvement and where more advanced logistics services and networks can be put in place only with international support.