Bottom Feeders

The "race to the bottom" in global labor and environmental standards has captivated journalists, politicians, and activists worldwide. Why does this myth persist? Because it is a useful scare tactic for multinational corporations and populist agitators peddling their policy wares.

BY DANIEL W. DREZNER NOVEMBER 19, 2009

The current debates over economic globalization have produced a seemingly simple and intuitive conclusion: Unfettered globalization triggers an unavoidable "race to the bottom" in labor and environmental standards around the world. The reduction of restrictions on trade and cross-border investment frees corporations to scour the globe for the country or region where they can earn the highest return. National policies such as strict labor laws or rigorous environmental protections lower profits by raising the costs of production. Multinational corporations will therefore engage in regulatory arbitrage, moving to countries with lax standards. Fearing a loss of their tax base, nation-states have little choice but to loosen their regulations to encourage foreign investment and avoid capital flight. The inevitable result: a Darwinian struggle for capital where all other values — including workers' rights and the environment — are sacrificed upon the altar of global commerce.

The fear of such a race to the bottom has helped forge an unlikely coalition of union leaders, environmentalists, and consumer groups; together, they have spearheaded significant public resistance to several recent international economic initiatives. These include the North American Free Trade Agreement (NAFTA), the abortive Multilateral Agreement on Investment (MAI), the 1999 World Trade Organization (WTO) talks in Seattle, China's admission into the WTO, and the African Growth and Opportunity Act that U.S. President Bill Clinton signed into law last May. In each instance, protestors argued that unless globalization is reversed or at least slowed, a race to the bottom is inevitable.

At the opposite end of the political spectrum, the rhetoric and goals may differ, but the underlying imagery remains the same. Pro-market politicians and multinational corporations also cultivate the idea of an unstoppable global race — except they do so in order to advance environmental deregulation and "flexible" labor legislation that otherwise would become ensnared in fractious political debates. Multinational corporations argue that the pressures of the global marketplace force them to relocate or outsource their production to lower-cost facilities in poor nations.

The race-to-the-bottom hypothesis appears logical. But it is wrong. Indeed, the lack of supporting evidence is startling. Essayists usually mention an anecdote or two about firms moving from an advanced to a developing economy and then, depending on their political stripes, extrapolate visions of healthy international competition or impending environmental doom. However, there is no indication that the reduction of controls on trade and capital flows has forced a generalized downgrading in labor or environmental conditions. If anything, the opposite has occurred.

Given this dearth of evidence, why does the race to the bottom persist in policy debates? Because the image is politically useful for both pro- and antiglobalization forces. Unfortunately, by perpetuating the belief in a nonexistent threat, all sides contribute to a misunderstanding of both the effects of globalization and how governments in developing and advanced economies should — or should not — respond.

RUNNING IN PLACE

If economic globalization really does trigger a race to the bottom in regulatory standards, two trends should be evident. First, countries that are more open to trade and investment should have fewer and less demanding regulations affecting corporate production costs. Once barriers to trade and investment are lowered, the logic goes, nation-states must eliminate burdensome regulations or risk massive capital flight. Over time, therefore, more open economies should display lower labor and environmental standards. Second, multinational corporations should flock to countries with the lowest regulatory standards. The core of the race-to-the-bottom hypothesis is that profit-maximizing firms will locate to places where the production costs are relatively low. Since any regulatory standard presumably raises these costs, corporations will seek out countries with the weakest possible standards.

These predicted trends are, in fact, nonexistent. Consider labor standards. There is no real evidence that economic openness leads to the degradation of workers. In fact, some evidence suggests that openness actually improves worker standards. A comprehensive 1996 study by the Organisation for Economic Co-operation and Development (OECD) found that "successfully sustained trade reforms" were linked to improvements in core labor standards, defined as nondiscrimination in the workplace, the right to unionize, and the prohibition of forced labor and exploitative child labor. This linkage occurs because multinationals often pay higher-than-average wages in developing countries in order to recruit better workers. Moreover, since corporations have learned to work efficiently under rigorous regulatory standards in their home countries, they favor improving standards in their foreign production sites in order to gain a competitive advantage over local competitors, who are not accustomed to operating under such conditions. A recent World Bank survey of 3,800 workers in 12 Nike factories in Thailand and Vietnam found that 72 percent of Thai workers were satisfied with their overall income levels, while a majority of Vietnamese workers preferred factory employment over lower-wage jobs in their country's agricultural sector.

The case of export processing zones (EPZs) in developing economies underscores the spuriousness of the race-to-the-bottom argument. EPZs are areas established in order to attract foreign investment. Typically, governments entice investors into EPZs with infrastructure investment and duty-free imports and exports. There are more than 850 export processing zones worldwide, employing some 27 million workers; in some developing nations, like Mauritius, EPZs account for a majority of a country's exports. If there is a race to the bottom in labor standards, it should be particularly evident in EPZs.

There are a few countries, such as Bangladesh and Zimbabwe, that have attempted to preempt competitive pressures by exempting their EPZs from regulations covering labor standards. However, contrary to the race-to-the-bottom hypothesis, such policies have not compelled other countries to relax labor standards in their own EPZs. Indeed, several nations, including the Dominican Republic and the Philippines, actually reversed course in the mid-1990s and established labor standards in their EPZs when none previously existed. A 1998 International Labour Organization report found no evidence that countries with a strong trade-union presence suffered any loss of investment in their EPZs, while a 1997 World Bank study noted a strong positive correlation between higher occupational safety and health conditions and foreign investment in EPZs. Analysts also have found that wages in EPZs actually tend to exceed average wages elsewhere in the host country.

Similarly, openness to trade and investment does not lead to a race to the bottom in environmental conditions or regulations. Countries most open to outside investment — OECD nations — also have the most stringent environmental regulations. Even developing countries such as Malaysia, the Philippines, Thailand, Argentina, and Brazil have liberalized their foreign investment laws while simultaneously tightening environmental regulations. In Latin America, there is clear evidence that more protectionist countries, such as pre-NAFTA Mexico and Brazil under military rule, have been the biggest polluters. This finding is hardly surprising; the most protectionist economies in this century — the Warsaw Pact bloc — displayed the least concern for the environment. Privatization programs in these countries, which help attract foreign direct investment, have contributed to improved environmental performance as multinational corporations have transferred cleaner technologies from the developed world. In Brazil, for instance, the privatization of the petrochemicals sector in the early 1990s led to a greater acceptance of environmentally safe practices.

Race-to-the-bottom critics counter that stringent labor and environmental standards in developing economies are backed by purely nominal enforcement capabilities. Although it is difficult to quantify compliance and enforcement in developing economies, the emergence of watchdog groups — analogous to election observers and human rights organizations — that scrutinize the enforcement of national labor and environmental legislation is a positive development. The United States has recently pursued this strategy by bolstering the role of the International Labour Organization in monitoring core labor standards around the world. And even in the absence of uniform national enforcement, many multinational corporations have embraced self-monitoring programs for the environment — an effective complement to government regulations.

Perhaps most damaging to the race-to-the-bottom proponents, there is no evidence that corporations direct their investment to developing countries with lower labor or environmental standards. Indeed, the relationship between foreign direct investment (FDI) and labor standards is strongly positive. During the 1990s, an overwhelming majority of global FDI was directed toward advanced economies (which tend to have higher labor standards), not to poor nations. A similar story can be told with environmental standards. Comparing data on U.S. FDI in developed and developing countries reveals that pollution-intensive U.S. firms tend to invest in countries with stricter environmental standards.

Profit-maximizing corporations invest in countries with high labor and environmental standards not out of a sense of obligation, but for hard-nosed business reasons. Consumption has gone global along with production; many firms base their investment decisions not just on likely production costs but also on access to sizable markets. A 1994 survey by the U.S. Department of Commerce found that more than 60 percent of the production of U.S. corporate affiliates in developing countries was sold in the host country and less than 20 percent was exported back to the United States. In Mexico, which provides an ideal platform for reexporting to the United States, only 28 percent of production by U.S. affiliates made it back to the United States; more than two thirds was marketed in Mexico. The great fear of the race-to-the-bottom crowd — that U.S. multinationals will locate production facilities in developing countries, exploit local resources, and reexport back to the United States — has not materialized. In fact, that type of activity characterizes less than 4 percent of total U.S. investment abroad. The oft-cited cases of garment facilities based in poor nations and geared to consumers in advanced economies are the exception, not the rule. This exception is largely due to the low capital investment and importance of labor costs in the textiles sector.

Since corporations invest overseas to tap into new, large markets, host countries actually wield considerable power. They can use that power to resist deregulatory pressures. Multinational corporations have invested large sums in China despite formidable regulatory hurdles, a blatant disregard for copyright laws, high levels of corruption, and strict requirements for technology transfers. The prospect of 1 billion consumers will cause that kind of behavior among chief executive officers. Mexico has enhanced its environmental protection efforts while trying to attract investment. The result? Foreign direct investment around Mexico City has exploded, while the air quality has actually improved.

Multinational firms are also well aware of the growing link between public opinion and profits. Increasingly, citizens care about the conditions under which their products are manufactured — an environmental or labor mishap can cripple a corporation's brand name. Thus, foreign investors in Costa Rican bananas or Asian lumber insist on higher standards than the local government in order to cater to environmentally savvy European consumers. And PepsiCo pulled out of Myanmar in 1997 because it did not want to be linked to that country's repressive regime. To be sure, some multinational corporations are hardly paragons of labor or environmental virtue, as the perilous labor conditions at Royal Dutch Shell and Chevron's operations in Nigeria make clear. But in general, corporations understand that it is smart business to stay in the good graces of their customers.

The lack of evidence for a race to the bottom is not surprising when put in historical perspective. In the late 19th century, there was an enormous increase in flows of capital, goods, and labor among countries in the Atlantic basin. On several dimensions, such as labor mobility and investment flows, the degree of market integration 100 years ago is much greater than today. Despite claims made at the time that these trends would lead to a world ruled by social Darwinism, the United States and Europe created national regulatory standards for consumer safety, labor, and the environment and developed regional institutions (including a predecessor to the European Central Bank) to cope with the vicissitudes of financial markets. Indeed, globalization does not eliminate the ability of sovereign states to make independent regulatory decisions. Nor does globalization render governments impervious to the preferences of their own citizens. Even authoritarian countries are not immune to public pressure; the beginning of the end of the Soviet bloc saw environmental protests against rising levels of pollution. Governments, particularly in democratic countries, must respond not only to domestic and foreign firms but also to the wishes of citizens who prefer stricter regulatory standards.

THE SCAPEGOAT FACTORY

Of course, one can hardly dispute that developing countries often display deplorable environmental and labor standards and conditions, far below those in the world's advanced economies. But the evidence thus far indicates that globalization itself does not cause or aggravate this disparity. If anything, the opposite is true. So why do so many people seem to believe in a hypothesis that has yet to attract any evidence? Because the myth is politically convenient for all sides. Nongovernmental organizations (NGOs), corporations, politicians, and academics use the race to the bottom as an excuse to peddle their policy wares.

Opponents of globalization — including environmentalists, labor unions, and a multitude of NGOs — advance the myth of a race to the bottom to oppose further global market integration. The race to the bottom is a wonderful rallying tool for fundraising and coalition building and also serves as the perfect bogeyman, allowing these groups to use scare tactics derived from previous domestic policy campaigns against nuclear power and acid rain. Such strategies are consistent with a pattern of exaggerating dangers to capture the attention of the press and the public: Only by crying that the sky is falling can antiglobalization forces rouse complacent citizens. For example, Public Citizen, one of the most vocal NGOs on trade issues, has argued that steps toward economic liberalization will have devastating social effects. Its Web site notes that the Multilateral Agreement on Investment would have "hasten[ed] the 'race to the bottom,' wherein countries are pressured to lower living standards and weaken regulatory regimes in an effort to attract needed investment capital." Whatever shortcomings the MAI may have displayed, it demanded discerning criticism, not knee-jerk attacks based on spurious reasoning.

The race to the bottom also provides a useful scapegoat for larger trends that adversely affect specific interest groups, such as labor unions. A recent statement by Philip Jennings, general secretary of the Geneva-based Union Network International, which represents more than 900 unions in 140 countries, provides an apt example. "Globalization is not working for working people," Jennings declared in July 2000. "It needs a human face." Similarly, union leaders in the United States have argued that globalization and the race to the bottom are responsible for the 30-year stagnation in the median real wages and the growing income inequality in the United States. Such simplistic views disregard other key factors — particularly advances in technology and the subsequent demand for high-skilled labor — affecting wage and employment levels. If, as race-to-the-bottom proponents suggest, U.S. workers are being replaced by their counterparts in developing economies, then the 2.6 million employees laid off by manufacturing multinationals in the United States over the past three decades were replaced with a mere 300,000 workers hired in developing nations over the same period. In other words, Third World laborers would have to be nearly nine times as productive as those in the United States — hardly a persuasive proposition. In fact, the U.S. labor force displays the highest productivity levels in the world.

The race-to-the-bottom myth also helps pro-globalization forces sell deregulatory policies that may result in short-term economic pain. But rather than take the responsibility of pushing for deregulation directly, advocates invoke globalization as an excuse. It does not matter whether one favors deregulation or not; globalization will punish those who fail to deregulate, so there is little choice in the matter. For example, Pacific Telesis (now part of sbc Communications) used globalization as an excuse for cutbacks and layoffs in its San Francisco offices and to lobby Washington for deregulation. Unocal has argued that because of the competitive pressures of globalization, it should not be forced by U.S. sanctions to pull out of Myanmar.

Politicians also exploit the need to compete in the global marketplace and the myth of a race to the bottom as excuses to support policies that would otherwise trigger fierce public debate. State governments in the United States have often claimed that widespread deregulation must occur in order to attract capital. Meanwhile, European politicians trotted out the specter of globalization to justify the Maastricht criteria, a series of stringent economic prerequisites for a European monetary union. It was a clever tactic; governments across the European Union were able to push through deregulation and painful spending cuts without an overwhelming electoral backlash.

Perhaps the most potent reason for deploying the race-to-the-bottom myth is the psychological effect it has on individuals. By depicting a world without choices, the race to the bottom taps into the primal fear of a loss of control. Governments and citizens appear powerless in a world dominated by faceless, passionless capital flows. This perceived lack of control prompts unease for the same reason that many people prefer driving a car to flying in an airplane even though the latter is safer: Even if driving is riskier, at least we are behind the steering wheel.

A DURABLE MYTH

In his 1996 book *Jihad vs. McWorld*, Benjamin Barber warned that, by empowering owners of capital and disenfranchising voters, globalization would threaten democratic practices. Democracy may indeed be at risk, but not for the reasons Barber suggested. Globalization itself will not necessarily weaken democracy, but the rhetoric surrounding globalization may have that effect. If protestors persist in the indiscriminate trashing of multilateral institutions, they will only undermine the legitimacy of the mechanisms that democratic governments have established to deal with the very problems that concern them. And if enough leaders claim that globalization is an unstoppable trend demanding specific and formulaic policy responses, ordinary citizens will lose interest in a wide range of policy debates, believing their outcomes to be foregone conclusions determined by economic forces beyond their comprehension and control.

Can the race-to-the-bottom myth be debunk- ed? In time, perhaps. As facts continue to contradict fiction, the claim will become untenable, much as the notion of Japan's global economic superiority died down by the mid-1990s. Ironically, some of the strongest voices speaking against the race-to-the-bottom myth emanate from the very developing countries that antiglobalization forces purport to defend. In a speech before the World Economic Forum in January 2000, Mexican President Ernesto Zedillo charged that antitrade activists wanted to save developing countries. . . from development. Even in Malaysia, where Prime Minister Mahathir Mohamad has become notorious for his diatribes against currency traders and global capitalism, the Federation of Malaysian Manufacturers recently stated that globalization and liberalization should be viewed "with an open mind and [in] an objective and rational manner." And economist Jagdish Bhagwati of Columbia University is spearheading the Academic Consortium on International Trade, a group of academic economists and lawyers arguing that the antisweatshop campaigns currently underway at several U.S. universities will only "worsen the collective welfare of the very workers in poor countries who are supposed to be helped."

Unfortunately, bad economics is often the cornerstone of good politics. The belief in a race to the bottom has helped cement an unwieldy coalition of interests and has enhanced the influence of antiglobalization activists both inside the corridors of power and in the mind of public opinion. Myths persist because they are useful; there is little incentive to abandon the race to the bottom now, even though there is no evidence to support it.

For those who wish to deepen the process of globalization, however, the implications are troubling. Historically, bouts of protectionism have occurred primarily during global economic downturns. But the rhetoric of a race to the bottom has gained adherents during a time of relative prosperity. If the current era has produced so many challenges for continued economic openness, what will happen when the economy hits the next speed bump? The image of a race to the bottom will likely endure in global policy debates well into the new century.

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