

ORIGINAL ARTICLE



International trade and foreign direct investment: empirical testing of the trade–environment triangle

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ABSTRACT

The debate on growth and development has largely been argued during the seventies and eighties over the world. Subsequent to the eighties and nineties, the concern shifted towards the global environment through the emphasis on pollution and other forms of environmental degradation. Thereafter, the entire development debate has been revisited from the point of view of trade, development and the environment. The existing literature, however, is both incomplete and uncomplicated in as much as it does not relate these three vital dimensions of the trade–environment debate with each other. This paper attempts to verify empirically the triangle consisting of the Environmental Kuznets Curve (EKC), the Pollution Haven Hypothesis (PHH) and the type of economic development. EKC challenges the intuitive dichotomy between development and environment whereas PHH emphasises the implications of global foreign direct investment for the environment. The findings are in accordance with the new literature, which forms the basis of the trade, environment and economic development triangle at the global level.

KEYWORDS

Trade and environment; environment and development; global FDI; Environmental Kuznets Curve; Pollution Haven Hypothesis

1. Introduction

The world economy has undergone fundamental changes in the past few decades. What we are witnessing today is an era of trade openness, global economic interdependence and unprecedented competition. Countries from across the world are pushing for greater convergence, through further trade liberalisation and structural transformations, in the process producing many opportunities for businesses. An open trade regime is often propagated on the grounds of better resource allocations, productivity improvements, increased world output, better quality, and lower prices for consumers, so on. It has been believed and learnt from experience as well, that trade and investment liberalisation can stimulate economic growth and foster greater welfare. But the sustainability of such growth and welfare has been questioned on several occasions. At the heart of such sustainability concerns lies the complex and highly debated relationship of trade and environment. The implications of falling cross-border trade and investment barriers on environment are far too significant to ignore. With national economies merging and pressure on ecosystems mounting, this trade–environment interface is often characterised as a conflicting one, but the possibilities of conciliation between the two are also not ruled out.

Further, trade cannot be unrelated to development. There is an avowed relationship between economic development and international trade, which arises from the new strategies of economic development of the emerging 'newly industrialised economies'. Economic development strategies have come to be associated with trade strategies like Import Substituting Industrialization and Export Promoting Industrialization. In this context, the debate was about import substitution versus export promotion argument in the 1970s and 1980s. After the 1980s, particularly since the era of liberalisation and WTO (World Trade Organization), the debate shifted to free trade, because before this period, free trade was only in text books. It became a reality only with the emergence of WTO. In this context, the debate was restricted to trade and development aspects, till the nineties. In recent years, however, the realisation has dawned upon the world at large that the overarching issue is the environment. Issues like global warming, climate change and pollution have substantiated that this debate necessarily includes