Global outsourcing comes with environmental costs

Outsourcing may mean bigger profits for companies seeking cheaper ways to produce goods and services, but it's not all good news for the host countries.

For the countries in the South that welcome the factories of companies from the wealthier North, outsourcing comes with environmental costs.

The People's Republic of China, considered the world's factory, is an example. Since China joined the World Trade Organization in 2001, there has been an influx of companies moving their factories to the East Asian country. Attracted by the prospects of lower production costs and cheap labor, companies from the North outsourced production of garments, apparel, toys, footwear, tools, light machinery, electronics, and information technology products, among others, to China.

But producing huge amounts of such goods has damaged China's air, water, and soil, triggering deforestation, desertification, and global warming, while seriously endangering public health.The damage to China's environment was estimated at $230 billion in 2010, or 3.5% of the nation's gross domestic product—three times the damage in 2004.

India, another country that welcomes outsourcing, has also seen similar damage to its environment.Industrial pollution has caused acid rain, damaging buildings, degrading the environment, and reducing crop yields.Wheat fields near a power plant produced 49% less than those 22 kilometers away.

Other host countries face similar problems.Since the countries that welcome outsourcing are mostly developing countries whose primary goal is growing their economies, the environmental costs of outsourcing had been largely ignored.

Not anymore.

As more companies opt to outsource their production to developing countries, the resulting environmental damage has become too great for host countries to bear. About a decade and a half ago, major host countries, notably China, started passing environmental regulations.But these moves couldn't restore the environmental quality to World Health Organization standards.Environmental quality in China and its neighbors, including the Republic of Korea, Cambodia, India, the Lao People's Democratic Republic, Malaysia, and the Philippines, continues to deteriorate.

As host countries become more vigilant about the environment, the prices of outsourced goods and services for companies from the North have gone up.As a result, many firms from the North have adopted new strategies to counter the rising costs of outsourcing. Since the mid-2000s, Northern firms' outsourcing patterns have been changing. Instead of outsourcing their entire production overseas, some now opt to outsource just parts of it, while others now also rely on in-house resources to perform tasks previously outsourced overseas.

Countries in the South will need stronger regulation and international cooperation to make firms from the North fully account for the environmental costs of outsourcing.

This episode is based on research done for the Asian Development Bank Institute by Jai-Young Choi, professor at the Department of Economics and Finance, Lamar University, Texas; and Eden S. H. Yu, vice president and chair professor at the College of Business of Chu-Hai College of Higher Education in Tuen Mun, Hong Kong, China.

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