



Sustainable Development through Diversification:

Challenges and Potential for Developing
Economies

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Introduction

“To everything there is a season, and a time for every matter under heaven,” wrote the author of Ecclesiastes, a wisdom book of the Old Testament. This ancient wisdom reminds us that change is not only inevitable but necessary, and that there is a right time for everything. In the modern world, the time for sustainable economic diversification in developing economies is not only right but urgent. The global economy is in a state of flux, with the traditional powerhouses facing challenges from emerging economies, and the entire world grappling with the impact of climate change. Developing economies, which have long been dependent on a narrow range of sectors, often related to the extraction and export of natural resources, are particularly vulnerable to these changes. The need for economic diversification, therefore, is not just a matter of economic prudence, but of survival. However, the path to diversification is fraught with challenges, from the lack of necessary infrastructure and skilled workforce to political and financial constraints. However, it also presents numerous opportunities, from leveraging natural resources and technological advancements to forming global partnerships and developing sustainable tourism. This report aims to provide a comprehensive analysis of the challenges and opportunities in sustainable economic diversification in developing economies, with a view to providing actionable recommendations for policymakers, business leaders, and other stakeholders.



Sustainable development is the pathway to the future
we want for all. It offers a framework to generate
economic growth, achieve social justice, exercise
environmental stewardship and strengthen governance

Ban Ki-moon, (September, 2013)



Sustainable Development in a Changing World: Redefining Progress

The realization that we are living in a world that now demands considerable review of old ways of thinking and doing, as well as quick adaptation to the phenomenal changes occurring across the globe, is more pronounced than ever before. We can no longer afford to remain within the confines of rigid and hierarchical organizational structures. Nor can we afford to be casual about the unique challenges specific to countries, regions and ultimately, our world. Dialogue, collaboration, co-operation, and consistent progress towards the goals of Agenda 2030 are the need of the hour. There is a native American proverb that says “We do not inherit the earth from our ancestors; we borrow it from our children”. The World Commission on Environment and Development (1987) has defined sustainable development as “Ensuring the needs of the present generation without compromising the ability of future generations to meet their own needs”.

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WCED 1987

A steady transition towards sustainable development brings to the fore the important question of managing transitions in such a way that social, economic, and environmental goals can be met through a single concerted process (Vollenbroek, 2002) This is not easy and efforts in this regard can vary significantly, especially if comparisons are drawn between developed and developing countries. For example, how can we ensure food security for a growing population without degrading the natural resources and ecosystems that support it? How can we promote economic growth and social inclusion without increasing greenhouse gas emissions and climate risks? How can we foster peace and justice without violating human rights and democratic principles? These are some of the questions that require innovative solutions and collective action from all stakeholders. Cutting edge technology and expertise is presently based in developed countries. Developing countries are progressing towards Agenda 2030 at

varying rates and in many cases the gaps between countries with regard to sustainable development, are getting wider. As Albert Einstein once said, “We cannot solve our problems with the same thinking we used when we created them”. Therefore, we need to embrace new ways of thinking and doing that are more sustainable, resilient and inclusive. We need to learn from the best practices and experiences of different countries and regions that have made progress towards sustainable development. We need to engage in dialogue, collaboration and co-operation with diverse partners and stakeholders who share our vision and values. And we need to monitor and evaluate our actions and outcomes to ensure that we are on track to achieve the goals of Agenda 2030. It is therefore extremely important to provide and promote international support for effective capacity-building in developing countries, to speed up the process of sustainable development, innovation, and entrepreneurship.

New Technologies and the Emphasis on Green Economy

Aiming for economic development at the expense of social well-being, environmental hazards and disruptions of the eco-system is not an option. Hence it is extremely important for all countries, developing and developed, to formulate policies and instruments that address these themes. The Green Economy serves as an alternative pathway for growth and sustainable development—a pathway that not only takes into account the need for steady economic growth, but also focuses on the ecological and social aspects for a holistic improvement in people’s lives. Incremental innovations (greater material and energy efficiency in production processes) are important for the transition to a green economy. However, more radical technological innovation is inevitable . For instance, the substitution of fossil fuels in the transportation sector, as well as in steel and iron production, requires fundamental shifts in technology, way beyond incremental efficiency improvements (Söderholm, 2020). Introducing such radical shifts in technology is a greater challenge for developing countries because of capacity issues and resource constraints. This again underpins the importance of providing the necessary assistance to such countries by the more advanced economies of the world (Tadjoeddinb, 2020; Barbier, 2020).

Key themes for sustainable development and innovation include renewable energy, oceans and blue economy, disaster risk reduction, circular economy, water and sanitation and the promotion and support of micro, small and medium-sized enterprises. The shift to frontier technologies like Green Hydrogen, Electric vehicles, Biomass and Bio Fuels, Wind energy, Big Data, Nanotechnology, Block Chain, and Internet of Things is happening fast and if the developing countries do not adapt quickly to a fast-changing world, the gap between the developing and developed countries will get wider (Ahmed, 2018). This, of course is against the spirit of the Sustainable Development Goals and the second principle “Leave No one Behind”.

Partnerships between developed and developing countries to level out the playing field are as important as regional alliances to take advantage of global value chains and share knowledge and success stories. The developing countries will have to place a lot of emphasis on environmentally appropriate technologies, development of the required infrastructure, open and adaptive political and administrative systems, decentralized decision-making, minimal environmental degradation, greater justice and social equity, adequate financial resources and open economic systems (Lawrence, 1997).

Investment & Innovation

Investment can be perceived as a concept that entails looking ‘within’ and looking outside, at the national level. Quite literally, every country has to invest in whatever gives it a competitive advantage, be it natural resources, technology, or people. From the economic perspective, making the business climate investment friendly for domestic as well as foreign investors is critical for development. The real challenge is that no country or region can do this independently of the influence from the rest of the world. Climate change alone requires global solutions, which in turn necessitate collaborative ventures and concerted efforts.

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Innovation is a critical factor in growth, that steers businesses towards excellence, guaranteeing a competitive advantage, increasing environmental efficiency, and tipping the scales in favor of raising the social capital essential for future developments (Giudice, 2019). Developing countries need to focus

especially on encouraging innovation through providing skills and facilities to the youth for establishing start-ups and MSMEs.

Developing countries face a plethora of challenges when it comes to innovation, such as low investment in research and development, weak intellectual property protection, poor quality of education and human capital, limited access to finance and markets, and inadequate infrastructure and institutions (Naqvi, 2011). These challenges hinder the potential to become a knowledge-based economy that can produce and export innovative goods and services that are aligned with the Sustainable Development Goals. To overcome these challenges, it is imperative to increase spending on R&D, strengthen legal and institutional frameworks for innovation, improve the quality and relevance of education and training, promote a culture of innovation and creativity among the youth, foster linkages and collaboration among different actors in the innovation ecosystem, leverage digital technologies and platforms, and build capacity for monitoring, evaluation and learning from innovation initiatives and outcomes. These actions will help to narrow the gap with other countries in terms of innovation performance and achieve sustainable development and diversification.

<i>Action Area</i>	<i>Strategies and Steps</i>
Investment in R&D and Innovation	- Increase public and private investment in sectors aligned with the SDGs. - Focus on sectors with high potential for social and environmental impact.
<i>Intellectual Property Rights</i>	- Strengthen the legal and institutional framework for IP rights. - Enhance enforcement and awareness of IP protection among innovators and entrepreneurs.
<i>Education and Training</i>	- Improve the quality and relevance of education at all levels. - Develop skills and competencies for innovation and entrepreneurship.
<i>Youth Engagement</i>	- Promote a culture of innovation and creativity among the youth. - Provide opportunities and support for youth to pursue their ideas and ventures.

*Collaborative
Ecosystem*

- Foster linkages among universities, research institutes, industry, government, civil society, and international partners.

*Digital
Technologies*

- Leverage digital platforms to facilitate access to information, knowledge, finance, and markets.

*Monitoring and
Evaluation*

- Build capacity for monitoring, evaluation, and learning from innovation initiatives.
- Share best practices and lessons learned with other countries.

Global Value Chains for Sustainable Development

Global Value Chains (GVCs) can be extremely significant for greening the global economy. From the lens of sustainability, the value in these chains now goes beyond the economic aspect and includes the social and environmental dimensions also. GVCs depend on global interdependence and interconnection, and this interconnection requires added focus on sustainability so that the dividends of growth are reaped not only by the developed countries but by the developing countries as well.

Multinational Enterprises (MNEs) can play a very important role in this regard. They can help to promote social and environmental standards. Substandard labor and environmental conditions can be remediated by MNEs in global supply chain factories, which can then trickle down the chain. The introduction of private regulation that is targeted to regulate social and environmental issues across GVCs independently, in recent times, has been a welcome trend. MNEs have de facto assumed the role of the new regulatory actors that can facilitate and support sustainable development beyond state regulations (Brandl, 2021).

The global economy has entered a new mega-cycle characterized by value chain disruptions, resource competition, and climate change. These challenges require manufacturers to rethink and redesign their operations strategies instead of making incremental adjustments. In one of its latest white papers, the WEF identifies five trends

that will dominate the transformation of global value chains in the next decade (World Economic Forum, 2023):

From global to globally connected multi-local value chains: Manufacturers will move towards multiple connected but highly localized value chains that rely on local suppliers and customers, served by manufacturing “in the region, for the region”.

From “doing” digital to “being” digital across end-to-end operations: Manufacturers will adopt data analytics and automation technology to manage the complexity and cost increases in multi-local value chains, as well as to enhance their performance, resilience, and sustainability.

From economies of scale to economies of skill: Manufacturers will lose some of the benefits of large-scale production due to localization and diversification. To compensate for this, they will focus on developing specialized skills and competencies that can be recruited globally, trained internally, and deployed flexibly.

From regulatory compliance to innovative sustainability: Manufacturers will integrate sustainability into their localized operations as a way to meet the increasing expectations and regulations from customers, governments, and society. They will also use sustainability as a source of innovation and differentiation in the market.

From cost-driven to customer-value-driven: Manufacturers will shift from competing on cost to competing on customer value. They will tailor their products and services to the specific needs and preferences of local customers, as well as offer solutions that address social and environmental challenges.

Today, multinationals have a great responsibility for promoting sustainable value chains through the careful utilization of scarce resources like environment and labor. Policies designed to include global value chains will have to look beyond national frontiers to ensure the realization of the sustainable development goals and a future that leaves no one behind. The global interconnectivity of the entire value chain has to be taken into consideration.

Capacity Building through JVs and Skill Development

Capacity building projects and programs must integrate the three pillars of sustainable development – economic, social and environmental. Developing countries especially need to review their institutional structures and align public sector management practices and policies with Agenda 2030. International development partners can play a pivotal role in enhancing organizational capacity by providing technical assistance for skill development, training programs, and the adoption and adaptation of international best practices to the local environment. It is also important for developing countries to learn from each other's successes and encourage knowledge sharing at regional levels. There is a realization that environmental, social and economic stresses are interdependent, posing a collective threat to present and future generations (Smith, 1993; Artur Gudmanian, 2020). This renders it crucial to have a multi-stakeholder approach and regional partnerships. Discussions at international symposia for sharing knowledge and ideas to come up with synergistic solutions for building capacity through changing attitudes, modifying policies, upgrading human resource, and redesigning institutional frameworks, are crucial.

Capacity building needs have to be tailored to the local environment and must focus on creating a skilled workforce, adopting the latest technologies, and creating effective organizations committed to sustainable innovation and building partnerships. Capacity building through joint ventures and skill development can aid developing economies in accessing new markets, technologies, and capabilities while enhancing human capital, innovation, and competitiveness. Despite the significant challenges being faced by developing economies such as aligning interests and expectations, managing conflicts and governance issues, and ensuring the quality and relevance of learning – adopting best practices and learning from successful cases across the globe, can be fruitful. For instance, in 2019, the African Development Bank initiated the Coding for Employment Program in collaboration with notable partners like the Rockefeller Foundation and Microsoft, aiming to foster digital skills and employment opportunities in the ICT sector across 54 African countries. Following this, in 2020, Siemens Energy and Bentley Systems formed Siemens Bentley Systems GmbH to enhance the efficiency and sustainability of power plants through integrated solutions leveraging both companies' expertise.

Moreover, in 2021, the World Bank sanctioned a \$200 million project to bolster vocational education and training in select Indian states, targeting improved employability and earnings for graduates. These initiatives underscore the potential of joint ventures and skill development in fostering sustainable economic diversification in developing economies. However, they also emphasize the imperative of adept management, coordination, and evaluation to align these initiatives with the strategic aspirations and necessities of the involved nations.

Policies and Institutional Reforms

Policies and institutional reforms are the actions taken by governments and other actors to improve the rules, norms, and practices that shape the economic activities and outcomes of a country. They can influence the incentives, opportunities, and capabilities of economic agents to diversify their production and trade, as well as to enhance their productivity, innovation, and competitiveness (Chiu, 2011). Policies and institutional reforms can also affect the environmental and social impacts of economic diversification, such as greenhouse gas emissions, resource use, pollution, waste generation, income distribution, employment creation, and human development (Jin Zhao, 2021) .

To support sustainable economic diversification, a multifaceted approach encompassing various policy spheres is essential. Macroeconomic policies, including fiscal and monetary measures, lay the groundwork for economic stability and foster a nurturing environment for diversification by channeling investments into pivotal areas such as infrastructure and research (Basyal, 2023). Trade policies, on the other hand, focus on external economic relations, facilitating diversification through the enhancement of trade competitiveness and regional cooperation (Allen Dennis, 2011; Gnanngnon, 2019). Industrial policies aim to revitalize the economic structure by nurturing new sectors and fostering innovation, while environmental policies prioritize sustainability through regulations that mitigate adverse environmental impacts. Lastly, social policies are designed to ensure the inclusiveness of economic growth, emphasizing labor rights and social security to foster a society where economic diversification translates into holistic development.

Building on the foundation of well-rounded policies and institutional reforms, several developing economies have carved out success stories in sustainable economic

diversification. Taking a leaf from Chile's book, we find a nation steering away from fossil fuels to embrace a renewable energy sector, a transformation buttressed by a robust regulatory framework and the fostering of public-private collaborations (Shahriyar Nasirov, 2018). This green shift not only enhanced energy security but also spurred job creation, with research indicating a higher job generation per unit of energy through green sources (Shahriyar Nasirov, 2021). Another developing economy, Malaysia, has championed digitalization, evolving into a frontrunner in the digital economy landscape of Southeast Asia (Lam Quynh Trang Tran, 2022). The nation's shift from a manufacturing and commodities-centric economy has been facilitated through strategic moves such as the inception of Digital Trade Free Zones, the establishment of a digital economy agency, and significant investments in digital infrastructure and skill development (Ismail, 2018). These orchestrated efforts in policy reform and institutional restructuring have not only fortified Malaysia's economic resilience but also elevated its competitive stance on the global stage. Both narratives underscore the transformative power of targeted policies in nurturing sectors that are sustainable and equipped to meet the demands of the modern economy.

Conclusion

At the recent G20 summit, the European Commission President Ursula von der Leyen urged the world to work together to tackle the global challenges and opportunities that we face. She said:

"We are living in a time of unprecedented challenges and opportunities. We need to work together to address the global issues that affect us all...we need to build bridges, not walls, between continents and civilizations. We need to invest in the future, not the past, of our economies and societies..."

These words resonate with the need for economic diversification in a changing world as emphasized in this paper. Today, we need to explore new avenues of growth and prosperity, not only for ourselves, but for our planet and its inhabitants. We need to draw lessons from the past, but also look ahead to the future, using new technologies and innovations to create a green and inclusive economy. This calls for a new mindset, the mindset of the Earth's kin, one that is open to collaboration and cooperation across

borders and sectors. We need to foster a culture of innovation and creativity, that values the potential and contribution of our young generation, and that harnesses the power and opportunities of the digital age. We need to transform our development model into one that is sustainable in every sense of the word. Investment and innovation are key drivers of this transformation. They can help us create new opportunities and solutions for the challenges we face. They can also ensure that the benefits of growth are shared by all. We need to recognize the importance of greenifying the global value chains and in this process hold multinational enterprises accountable for their impact on the environment and society.

Now is the moment to spring into action, not to remain in a state of anticipation. It is the juncture to broaden the horizons of our economies, steering clear of over-reliance on singular, lucrative sectors. This is the time to combine ancient wisdom with modern innovation. It is the opportune time to lay the foundations for a future that stands robust, grounded in fairness and brimming with opportunities for all, transcending self-centered pursuits. This is the pivotal moment to forge a transformative imprint on the global tapestry, reaching beyond the borders of our individual nations.

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