

## **EconoFact Chats: How Can Trade Contribute to Sustainability?**

**Joel Trachtman, The Fletcher School, Tufts University**

**Published on September 10th, 2023**

### **Michael Klein**

I'm Michael Klein, executive editor of EconoFact, a nonpartisan, web-based publication of the Fletcher School at Tufts University. At EconoFact, we bring key facts and incisive analysis to the national debate on economic and social policies, publishing work from leading economists across the country. You can learn more about us and see our work at [www.econofact.org](http://www.econofact.org).

### **Michael Klein**

The Washington Post economic columnist Catherine Rampell began a recent op-ed with the sentence, “Desperate political leaders of all stripes, Republican, Democratic, Communist, have found a common enemy: free trade.” While there was an increase in trade restrictions in the Trump administration, that the Biden administration has largely not reversed, and nationalists and populists in other countries have also pushed for more trade barriers, it is important to understand that international trade has never been unfettered. Trade policies are pursued for a range of reasons. A new report by leading trade experts entitled ‘Remaking Trade for a Sustainable Future’ recognizes that the multilateral trade system is at a critical juncture and it proposes policies to preserve open trade while also fostering a range of environmental, social, development, and economic goals. My guest on EconoFact chats today is one of the co-authors of that report, Professor Joel Trachtman. Joel is an internationally recognized expert on trade law, and I'm very glad to say, my colleague at the Fletcher School of Tufts University. Joel, welcome back to EconoFact Chats.

### **Joel Trachtman**

Thank you, Michael.

### **Michael Klein**

Joel, to introduce this topic, could you briefly recount the ways in which the trade policy of the world has evolved in the post-World War II era?

### **Joel Trachtman**

Okay, that's a big ask, but I'll try to do it really quickly. The 1947 General Agreement on Tariffs and Trade was a leftover from a plan to have a bigger, more, an institution with broader coverage that would have been part of the Bretton Woods institutions. After that, there were a number of rounds of tariff-reducing negotiations that were very successful over time in reducing worldwide tariffs, especially among wealthy countries. There was a round of de-colonization after 1947, and by 1964, that GATT system, General Agreement on Tariffs and Trade, sought to incorporate concerns of developing countries. By 1979, you started to see talk about non-tariff barriers,

regulatory barriers, product standards. Then we had the 1986 to 1994 Uruguay round, which included intellectual property and services. And on the first day of 1995, they formed the World Trade Organization, which is the organization charged with trade today. By 1999, there was the Seattle ministerial, where we sometimes call it the 'battle in Seattle,' where environmental protesters raised questions and concerns. And then in 2001, you had the Doha Development Agenda begin, and that's not really concluded. It's produced a few smaller things, but has been generally a failure. At the same time, China joined the World Trade Organization, and the rise of China has been a big challenge to this system. And in part, led up to what Catherine Rampell has spoken of, the scapegoating of China, and indirectly, or by virtue of that, the scapegoating of the trade system for the economic problems of the United States, that Trump began. And Biden, in order to maintain his electability, I think, has continued to scapegoat trade. At the same time, we've had the rise of these modern issues of e-commerce, of sustainability, and sustainable development, which is the focus of my work, and of security and weaponized interdependence in this area.

**Michael Klein**

So you mentioned sustainability as a focus of your work, and it's also a focus of your report. What are, more specifically, the sustainability goals that you discuss in your report?

**Joel Trachtman**

Well, there are two main categories, environmental sustainability and a kind of social sustainability, which really works out to be a kind of political sustainability. On the environmental side, we have a climate crisis, which I think everyone now sees in different kinds of events. And the goal there is net zero greenhouse gas by 2050. The G20 has asserted that goal. Biodiversity is being destroyed, and so we want to try to reduce that destruction. That's also a crisis. There are things that are less crises, like plastics pollution on sea and on land, and a goal of circular trade that supports all sorts of environmental benefits. And then on the social side, we have the important one, the politically salient one of labor protection. We have the goal of promoting micro, and small and medium enterprises, especially in developing countries, gender participation, and a traditional one of a social safety net. So the idea that in order to maintain the political support for trade, it's important to take care of those whose work is disrupted, to have a social safety net.

**Michael Klein**

So this is putting a lot on trade. And in the report, you and your co-authors identify natural linkages between trade and sustainable development goals, as well as constructed linkages. What do you and your team mean by these different types of linkages, and how is trade associated with these sustainable development goals?

**Joel Trachtman**

It's a great question. Trade can intensify certain types of production and consumption, and that alone can cause environmental degradation. Economic actors like firms and countries can seek competitive advantage by externalizing the costs of environmentally or socially harmful action, including international externalization like greenhouse gas emissions. And then similarly, they can provide subsidies that can have distortive effects and also adverse effects for sustainability through intensification of unsustainable production methods, especially in areas like agriculture and fishing. And the European Union has been particularly concerned in the greenhouse gas area that trade can cause leakage in response to national regulation, where production shifts to other locations with lower regulatory costs, and the associated environmental harms are simply shifted rather than actually reduced or eliminated. In addition, trade can put pressure on national environmental or labor regulation that imposes costs on domestic producers, and might competitively disadvantage them in the international marketplace. So there's a concern that trade can cause disruption of the social bargain in an importing country, and then that's a response to leakage and this related political pressure.

**Michael Klein**

So you mentioned ways in which climate is affected by trade. What kind of policies do you advocate to slow or reverse climate change?

**Joel Trachtman**

Well, one way to reverse climate change obviously is to reduce greenhouse gases, that's the way I should say, and there the idea that makes the most sense is to impose a global greenhouse gas price to avoid that kind of leakage and to have kind of a coherent global policy. That of course raises questions about the way different countries can do that and who's responsible. One idea though is to try to make sure that as countries fight over these things, that they preserve trade to avoid greenhouse gas-based or carbon-based trade wars, and to allow fair border adjustments. As you know, the European Union has developed a carbon border adjustment mechanism that is designed to impose on imported goods, the kind of carbon pricing that they charge internally, and so in order to make that kind of system fair, we need to have a system for interoperability. So other methods of addressing climate change, like simply protecting your forests or like the United States Inflation Reduction Act system of subsidies can be given credit in that system. We also need agreed methods to calculate the embedded greenhouse gases in particular products, and finally we need fairness to rebate these carbon border adjustments to developing countries and to recognize this principle of common but differential responsibilities that we've accepted in the Paris Agreement under the United Nations Framework Convention on Climate Control, that it makes sense to have different ways of imposing burdens on developing countries compared to wealthy countries. In addition, we need to regulate fossil fuel subsidies, and discussions have begun at the World Trade Organization on that. We need to regulate agriculture and fishing subsidies that can have climate effects. We need to liberalize trade in green goods and services

and technology so that countries can cheaply import those things in order to achieve climate goals, and finally we need to agree on product standards for deforestation and other climate related issues. And then I think one thing we can do in terms of the constructed linkages is to link trade to climate action and to recognize the fact that wealthy countries have terms of trade power, and they can use that terms of trade power to establish conditions for trade, and those conditions may have to do with sustainability. So you may recall that the economist William Nordhaus from Yale proposed climate clubs to use trade power to punish non-adherence to climate reduction goals through special tariffs, and so that's the kind of thing that could be used to implement some of these ideas.

**Michael Klein**

So there's a lot to unpack with that. It's a very good comprehensive answer, Joel. First off, when you talk about goods that embed greenhouse gases, I guess a good example of that would be, for example, cement, right?

**Joel Trachtman**

Yes.

**Michael Klein**

Because the production of cement involves the use of a lot of energy and so on, correct?

**Joel Trachtman**

That's right.

**Michael Klein**

And also when you talk about the terms of trade effect, maybe for our listeners, that's when a country is big enough that it can, for example, restrict the supply of a good, and force up its price, and that's kind of like a monopoly power, right?

**Joel Trachtman**

Yes, and that's why wealthy countries can charge tariffs and benefit themselves by collecting those tariffs and causing the exporter to bear that cost. And similarly, I think terms of trade power can be used to cause exporters to change their climate policies, for example.

**Michael Klein**

So you talked about in your answer both tariffs and subsidies, and typically when you learn about this in kind of basic international trade, you learn about the distorting effects of tariffs and subsidies. But your report offers a framework for thinking about the trade-offs between the distortions introduced by tariffs and subsidies, which reduce economic efficiency, and the ways

in which these can be used to realize sustainability goals. Can you talk a little bit about that trade-off?

**Joel Trachtman**

Well, first of all, I think at least in the United States and maybe in some other places, industrial policy has experienced a bit of a resurgence in the United States in the Inflation Reduction Act and the CHIPS policy. But the trade system in the past has addressed subsidies by reducing the ability to externalize the effects of your subsidies by allowing foreign countries to charge countervailing duties, to absorb the subsidy that is put on a good, and also to prohibit certain kinds of subsidies or require certain kinds of subsidies to be removed. And that has all been based on the trade distorting effect. In our project, what we have done is try to raise the concern for the environmentally harmful effect that subsidies can have in areas like fossil fuels or agriculture or fisheries or some kinds of manufacturing, too, like steel or cement, as you've mentioned. And the idea is to recognize what seems very important to countries, which is to maintain their autonomy, their so-called right to regulate, but to constrain their ability to externalize harms to others. And here, both competitive harms, but also sustainability harms. And so there are good reasons for subsidies in market failures in the environmental area, and often environmental problems like climate change involve market failure. So it makes sense to have some subsidies there, and we want to make sure that the trade system is revised to permit those kinds of environmentally sound subsidies where their trade distorting effects are not excessively large. And on the other side, to prohibit subsidies that are harmful to sustainability or sustainable development, and especially where benefits in other areas are not very large. That requires a lot of evaluation and judgment, but we think it's important to be able to have good policy in this area.

**Michael Klein**

Another point that you and your co-authors raise in the report is one of standards, product standards. So these product standards can help realize sustainability goals, but as you point out, there's a potential tension because they can also hurt developing countries that would find adhering to these standards prohibitively expensive. And there's this other issue of whether standards apply to products or to the way that the products are made. And so this then raises a different standards issue, labor standards. How do you think these tensions could be resolved?

**Joel Trachtman**

Well, they're difficult, and it's a hard question to answer. Standards are everywhere in modern production of goods and services. And as you say, we have new standards that relate to the way goods are produced. And of course, goods are produced in the exporting countries. So those standards are a way for the importing country to reach out and try to regulate the way goods are produced in the exporting country. And the reasons they do that, for example, in the area of climate change is because those foreign standards, those lax climate standards in foreign

countries, have adverse effects across borders. Now, standards have proliferated. There are a lot of these sustainability standards, and there are two main types. There are private standards developed by industry associations and by private consumer groups. And there are governmental required standards, mandated standards. And in the WTO system, once international standards are made by, for example, the International Organization for Standardization, countries have to base their national standards on those international standards. So in our report, in order to reduce inefficient diversity of standards, and also in order to make sure that those standards are not excessively burdensome for developing countries or small producers, we recommend making more international standards in the sustainability area with a more inclusive process that is attentive to the needs and capabilities of developing country producers. So some areas in which sustainable development standards are needed are greenhouse gas measurement, as I mentioned before, deforestation, biodiversity, fishing and marine products, core labor rights, and circular commerce is very much standard dependent. And the broad area, which is an area that might present some opportunities for developing countries of digital commerce, is also very standard dependent on things like privacy and competition. So the tensions with developing countries and protection for marginal producers can only be addressed through, I think, an inclusive process that recognizes their capabilities and needs and provides technical and financial support for transitional periods during which they adapt to those new standards.

### **Michael Klein**

So this discussion of standards raises a broader issue, Joel, an argument that today's poorer countries are being hampered in their development through trade rules that today's rich countries didn't have to follow as they grew wealthier, like rules on labor or environmental standards. How does your report address these issues?

### **Joel Trachtman**

It's another difficult issue. Developing countries believe it's unfair to require them to expend scarce resources or forgo development to address the climate problems which are caused by the stock of greenhouse gases, mostly produced by wealthy countries over time and by their production over time and their consumption today. But the problem is that the poorer countries are often the most vulnerable to climate change. And so while arguments about fairness are rarely persuasive in this context, developing countries need to use their bargaining leverage and they have advantages in solar energy and in having younger workforces, that may allow them to attract investment and to grow. So our project suggests ways to promote that kind of investment in developing countries to use these advantages for development. It's too late for developing countries to follow a low environmental protection path to development, especially for these global environmental issues like climate change and biodiversity destruction. And so other paths have to be found.

**Michael Klein**

So you talked about sort of the self-interest of developing countries, but this brings us to the issue of the enforcement mechanism for realizing these goals. Within a country, of course, there's a judicial system that people need to adhere to otherwise they're going to face fines or even imprisonment. But international enforcement mechanisms aren't as robust and countries could just opt out or refuse to comply. And I guess it would be likely to do so if they think the cost of complying greatly exceeds the benefits of staying within the multilateral trade system. So how do you and your co-authors think about the enforcement of the kinds of policies that you're talking about? Is it something beyond enlightened self-interest?

**Joel Trachtman**

It's tough to make new rules. And in this sustainability area, we need to make new rules in this international system where each country's consent is required. And in a sense, if they've consented to these rules, we hope that they will comply with them. But the first question is how to get them to consent. And here we need to release, we need to adapt, and develop different forms of reciprocity, different forms of bargains, different forms of cross-functional bargains. And we also need cross-functional leadership in this network of international organizations that have different mandates, like the United Nations Environment Program or the WTO or the IMF. And these organizations want to protect their own turfs and their own goals. So in order to enforce these new rules, we need to use that reciprocity. We'll need the same types of things that cause states to enter into the rules in the first place, that transactional reciprocity in which commitments are reliable because the threat of retaliation through withdrawal of reciprocal commitments is credible. But the good news is that many of these sustainable development dimensions can be understood as helpful to all. So strong incentives for compliance may not really be needed. We just need to get off the mark and get to work to establish these ideas as legal rules and norms that countries will follow.

**Michael Klein**

Well, Joel, I know that you and your co-authors have been working hard on this report for more than two years and that you'll be presenting it to policymakers throughout this autumn and into next year. And I hope your work receives the attention it deserves and has an impact on trade policy. So thanks very much for joining me today to discuss this very important work.

**Joel Trachtman**

It's my pleasure, Michael. Thank you for having me.

**Michael Klein**

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