

# Trade and global climate-policy

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*In terms of new emissions reductions, little materialised at the climate-change negotiations in Durban in November. This column argues that trade policy could widen the range of jointly beneficial potential outcomes and in this sense be a potential facilitator of an agreed global climate regime. Moreover, trade provides a mechanism for achieving an internalisation outcome for the global externality that climate change represents.*

Unsurprisingly, little materialised at the UN Framework Convention on Climate Change (UNFCCC) negotiations in Durban in terms of new emissions reductions (see Bosetti and Frankel 2011), and the commitments made in Copenhagen in 2009 under the Copenhagen Accord will largely define the regime for the immediate period going forward from 2012 to 2017 along with financial transfers in the climate fund, but with no formal role for trade policy.

Trade can potentially play a key role in both negotiating and operating a post-Kyoto global climate-policy regime. However, trade policy linked to climate-policy commitments lurks in the background as the UNFCCC process likely moves forward.

## Climate bargaining and trade policy

As an addition to the bargaining set for a global climate negotiation, trade in principle widens the range of jointly beneficial potential outcomes and can in this sense be a potential facilitator of an agreed global climate regime. But the reverse is also true, that in a linked climate-trade-financed global policy coordination structure that goes well beyond what was envisioned at Bretton Woods, climate now added to the global policy bargaining set also offers the prospect of potentially stronger trade disciplines (and even beyond WTO disciplines being negotiated). Furthermore, trade policy can as well be an instrument for the implementation of a global climate regime, since trade provides a mechanism for achieving an internalisation outcome for the global externality that climate change represents, and that provides a potentially more efficient outcome and also helps meet distributional objectives. In short, trade added to the emerging post-2012 climate regime can both expand the bargaining set for both (effectively linked) negotiations, and additionally provide an instrument for the implementation of an agreed outcome. This added linkage has not been successfully exploited in the UNFCCC post-2012 negotiation (as in the WTO Uruguay Round which expanded the trade bargaining set by adding intellectual property and services). There may be pessimism going forward as to whether any significant outcome post-Durban multilateral emissions reduction can emerge, even before trade policy is added to the negotiation, but both the UNFCCC and the Copenhagen accords remain in place, even if the latter is weak discipline.

## What trade cannot do for climate negotiations

It is also useful to acknowledge what trade cannot do for a global climate-policy outcome. First, trade offers nothing that will help resolve the property-rights issue of who has rights to do what, and who should be compensated by whom and by how much for actions that follow aiming to internalise the global externality that climate change represents. But at the same time property rights remain the critical (if not the central) issue for the developing countries in a global climate negotiation since they both assert historical responsibility for emissions of individual countries (and especially developed countries) and hence in emissions reduction, and also seek preferential treatment under the Common but Differential Responsibilities doctrine enshrined in the 1994 UNFCCC. In the classical development of externality literature, Pigou (1932) argued for the use of internalising Pigouvian taxes. Later, Coase (1960) argued that once rights to do what are assigned (by courts) bargaining will achieve internalisation, and if achieved in this way, Pigouvian taxes will only worsen outcomes. Relative to this discussion, climate stands as a trans-border global externality over which courts have no jurisdiction to award rights, and hence power and political process determine implicit property-rights outcomes. Trade cannot help directly in this process of internalisation, but will potentially play a role in the exercise of transnational power via threatened or actual trade measures if proposals for cooperation made towards others are not met.

Trade also cannot assist to any significant degree in providing the compensation (in cash or in kind) that will be needed for full developing-country participation in global emissions reduction arrangements. The size of compensation needed for developing countries, discussed in Copenhagen, would seem to be too large to be met by a special accommodation in trade policies in developed countries towards developing country exports.

## Trade as a second-best climate-policy instrument

As an instrument for achieving internalisation of the global externality that climate implies, trade policy remains only a second-best instrument. The first best internalisation mechanism is full global carbon pricing (achievable with an equivalent carbon tax). Trade policy comes into the picture if such a mechanism is unachievable due to non-participation by a subset of countries, and/or differentiated commitment levels by countries in terms of implied joint global emissions reduction under global projection of national commitments. Trade policy will inevitably distort production and consumption of goods both internally and will do so globally, but these costs may be justified by the benefits of the higher emissions reduction achieved in their absence.

The unilateral commitments that have been made by both developed and developing countries, both during the run up to Copenhagen and since, suggests that as far as a commitment period beyond 2020 (or even 2030) is concerned additional commitments needed to achieve an outcome jointly acceptable to all countries and consistent with IPCC (or as proposed by G20 leaders) temperature-change targets may be modest. If this is the case, the extra work that trade would need to contribute to a globally agreeable outcome could be less than some suppose. Put differently, trade can perhaps be considered in its potential role in climate negotiations in terms of what may be needed to be added to any future multilateral negotiating process to take it over a threshold starting from sizeable unilateral commitments, rather than from a de novo zero commitment initial situation.

## References

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