

Stan Kelly Lecture

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A call to arms - the threat of Green protectionism

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I have been asked to address the prospects for free trade. The context to the question is obvious. There is understandable concern that the greatest economic recession in 80 years may result in a regression away from a global economic order which has demonstrated how application of the principles of free trade has created the fastest rise in prosperity and the greatest reduction in poverty in human history.

There is no need to rehearse the statistics to this audience, although they warrant constant restatement in the wider public. Public opinion is fickle. People forget. Consider the problem of poverty. We can now say with confidence that poverty can be eradicated. We now know how to do it. Globalization has created the tools.

It is fashionable to oppose globalization, and protectionism

What did we do in the Western world, on the cusp of moment of supreme importance in human where, if we pushed on, developing open markets, poverty could have been despatched? We changed tack. Globalization is now widely derided by most undergraduates in most of the industrialized economies, including our own. Other things, including protection of the environment, are now seen as more important. The result is that the share of aid directly supporting economic growth in poor countries has halved in the last decade. Almost all leading NGOs, environmental and social, now deride free trade and globalization. Even NGO slogans have become oxymoronic. Oxfam's latest is "Stop Climate Poverty".

In these circles Free trade is inferentially depicted as morally inferior: "fair trade" is promoted as the alternative; with the deliberate implication that free trade is not fair. Most people who support the idea have no idea what free trade is, but have a series of value judgements about the unpleasant things it is supposed to do – allow cheap foreign goods to undercut products made at home, subject poor countries to competition from bigger, rich countries, oblige producers in small countries to compete in global markets and foster competition. The last is unacceptable to those who believe no activity or person should be rated against another; unless they are at the football, where very clearly not all "voices" should have equal weight.

Most people hold these views because they are fashionable, not because they reflect a coherent set of values. They will drink fair trade coffee and eat fair trade chocolate, but not advocate increases in tariffs. One thing economic liberals should take some heart from is that it is unfashionable argue for protection. When the co-editor of *Arena* argues for removal of parallel import restrictions on books, things have indeed changed.

Most of this same group will also not appreciate that there are those who propagate these ideas in a coherent political construct. From that view point, today's global economy is controlled by transnational corporations, many of whose turnover is larger than that of most economies, as if that is relevant, to which the only antidote is the institutionalization of "civil society". Its task is to monitor and "out" the excesses of these capitalist creations, by "Watching" them. That is why we have "Aid Watch", "Bank Watch" and so on.

The moral guardians are the likes of Naomi Klein and George Monbiot. Their case does not rest on the construct of their arguments: in Klein's case it is fashionable flirting with anti-consumerism, advancing the ideas using the marketing techniques of the consumer industry; and in Monbiot's it is delivery of Marxist and anarchist values through similar anti-consumerist diatribe.

One thing they do understand about free trade is Adam Smith's observation that it is the consumer who drives the formation of wealth through free trade.

Will the global crisis revive protectionism?

The fear of free traders is that we will see a reversion to protectionism as Governments struggle to minimize the growth-sapping impact of the global recession on their economies. They are right to be concerned.

As most economists know, resort to protectionism through imposition by the UN Congress in 1930 of the notorious Smoot-Hawley tariffs was the cause of the economic downturn which resulted in the Great Depression. US imports and exports fell by over 60 percent between 1929 and 1933. World trade fell by nearly two thirds.

The rise of competitiveness of Chinese enterprises and the pressure their cheaper products put on producers in the United States and the European Union has created ready political reasons for regulators in both of those advanced economies to use the excuse of current economic pressures to restrict imports.

The international community, if we choose to regard the collective declaration of leaders of the G8 and G20 at their Summit meetings as a measure of this, have disavowed resort to protectionism. The WTO and the World Bank are monitoring compliance with these undertakings and report an increase in trade barriers.

Yet when these are analysed, we find that most are applied within the rules of the WTO which permit "contingent" protection. They allow imposition of anti-dumping measures, measures to countervail the impact of subsidies, and measures to "safeguard" against the impact of surges of imports.

There are rules in the WTO to limit misuse of these measures. They are regularly invoked and excesses are ruled inviolate. While the increases of this contingent protection is an unhappy development, and will demonstrate something that has been clear for at least a decade – these rules need to be revised to further constrain their use; they also demonstrate that major economies are not seeking an overthrow of the global system of rules which regulate the free market, globalized economy.

Nor is there anything to indicate in the politics of the world's major economies that that is in prospect. There is however a related apprehension. The WTO has now not been able to agree on a global strategy to reduce trade barriers for nearly a decade. Just at the point in time when we need a robust multilateral trading system, is the WTO at risk of losing its effectiveness and credibility?

Is the WTO in trouble?

Before the collapse of leading Western investment and banking companies, the conventional measure of the health of the global trading system was seeing progress made in the WTO towards securing a successful conclusion of the Doha Round. It is a measure or preparedness of the global community to liberalize further.

Yet there has been very little for decade. The Doha Round (which restarted in 2001 the Round of global negotiations to reduce trade barriers which failed in Seattle in 1999) has effectively been stalled since 2003 when the negotiations were adjourned at the WTO Ministerial meeting in Mexico.

On the other hand the failure to do this does not reflect a disposition to reverse liberalization. The implications of failure in the Doha Round have been overstated.

To a large extent, this has been caused by trade officials and ministers themselves. You hear it commonly said by them that a failure in the Doha Round would threaten the authority of the global trading system. This argument is made with the aim of putting pressure on members of the WTO to reach agreement, the assumption being that an agreement is within reach. The tactic is ineffective and the supposition is incorrect.

The grim truth is that the leading trading economies – the US and the EU – and the majority of WTO members – now a large number of small developing countries which are not major traders – as well as other major traders like India and Brazil – do not see any political gain in a conclusion of the Doha Round.

As a point of digression, in a rational world, those who favour liberalization would not support the package that could be constructed from what is currently on the table. It produces very little liberalization and, in some areas, strengthens illiberal concepts which should be diminished, not enhanced in the fabric and structure of the WTO's agreements.¹

As to the risk of diminution of the authority of the WTO, it is not good for its standing that this Round of negotiations has been stalled now for six years. This does not however diminish the authority importance of the capacity of the system to underpin an open, global trading economy.

Over the last decade, the WTO has made the most important contribution to that since the negotiation of the GATT and the formation of the WTO itself. It has provided a ready framework through which 20 former communist states have locked their economies into a liberal economic model. Seven more, including Russia are negotiating accession.

¹ For example there are several propositions in draft packages which would create stronger legal rights for developing countries not to apply key free trade principles.

More importantly, China joined the WTO and committed to the most ambitious program to liberalize its economy of any major economy when acceding to the system. Contemplate the distortions to trade that could have occurred had China reached its current position as one of the world's leading trading nations without operating within the constraints of the WTO system.

The systemic and economic gains from China's accession are much more important than what could be delivered even from a successful Doha Round and should be loudly trumpeted as one of the greatest successes of the GATT/WTO system.

A failure in the Doha Round will not deter those wanting accession from proceeding. China will not consider its right to use WTO disputes procedures to challenge trade bullying by the US or the EU weakened because the Doha Round may not be completed.

And the fundamental importance of the WTO system will be demonstrated when finally the global economy regains strength for its denying the global trading community (or maybe it is just the US Congress) the opportunity from making the same mistake that was made in 1930. Recall then there was on GATT or WTO.

With all that said there is something wrong with the way in which negotiations to reduce trade barriers work in the WTO. Why is it that most of the world's leading trading nations are entering bilateral and regional agreements to liberalize trade in products which they will not liberalize in the WTO? And why are they happy to negotiate removal of barriers to investment and even agree to commitments to strengthen competition policy when these subjects were removed from the Doha negotiating mandate and are now taboo?

It is clear that the political economy dynamic, the reciprocal exchange of concessions, which drove liberalization through the GATT and produced the Uruguay Round and its substantial overhaul of the GATT system of trade rules no longer works. Free trade theorists always disliked the idea that negotiations should rest on such reciprocity and regularly pan it for fostering mercantilism: one only liberalizes if others do. They were right to contend it was not as beneficial as unilateral liberalization. But it is a misreading to argue it dissuaded liberalization.

Governments which liberalize do so for domestic reasons. They used the GATT/WTO system to lock these commitments into international law, making them difficult to reverse, which incidentally is probably why those who dislike open economies seek to demonize the WTO as the icon of globalization.

The reciprocity driver worked in GATT in the late fifties and sixties when it was clearly in the interest of the major trading economies – in Europe and North America - to open their economies, the largest in the global economy, to each other. The economic benefits were clear. Increased trade and productivity provided a political retort to complaints that liberalization created increased imports.

The dynamic worked in the Uruguay Round negotiations in the late eighties. Asian and Latin American nations were in liberalizing mode and their economies were growing. It suited them to go along with the proposition from industrialized economies to liberalize services and strengthen protection of intellectual property (although this was not trade liberalization) in return for commitments from them to liberalize their agricultural and garments and textiles industries. France

demonstrated the political value of reciprocity. It argued to protesting farmers that French services industries would have new opportunities to expand into global markets.

The grand deal only half worked. Garments and textiles markets were liberalized and protection of intellectual property increased in the developing world. However liberalization of agricultural markets in industrialized economies and services in developing countries was limited.

Both services and agriculture remain highly protected. But there is not enough of a political gain to enough major economies for a broad political deal to be struck across those two sectors. Major developing economies – China and India - don't want liberalization of agriculture. Most developing countries also do not appreciate enough the economic gains from liberalizing services.

The natural dynamic for reciprocal liberalization now lies in trade in goods among developing economies - trade between China, Brazil and India and trade between them and other developing economies. However, the level of trade is probably not sufficiently large for reciprocal liberalization to acquire political appeal. As the largest trading nation among developing countries, it would be economically logical for China to define the reciprocal benefit. For the time being, signs are that trade policy in Beijing is being shaped by the politics of multilateralism not the economics of international trade.

It is widely assumed that if the US and the EU were to agree to liberalize their agriculture sectors, this may create the necessary dynamic for agreement in the Doha Round. This could not be tested until 2013 because the EU decided it would not review its agricultural subsidies until then. But it still might not be enough. China and India don't want to liberalize their agricultural sectors. And the claim the biggest gains would be achieved in developing countries if the EU and US liberalize is considerably overstated. Economically, the biggest beneficiaries would of course be the US and the EU. And the export gains would fall principally on those economies with the globally competitive agricultural sectors - Argentina, Australia, Brazil, Chile, New Zealand Thailand and Uruguay: not the poorest developing countries such as a Ruanda, Jamaica, Papua New Guinea or Chad.

At some point soon, WTO members will need to revise the procedures used in the WTO for trade liberalization. The current approach which aims for "big bang" trade liberalization where the goal is to achieve simultaneous liberalization in several sectors or areas through a linked set of commitments is now dysfunctional. For example, there is no rational reason why progress in services should be tied to progress in liberalizing trade in goods.²

It would be wholly rational no longer to aim for broad scale liberalization but to recognize the reality of liberalization. In key respects, it can be argued that the GATT and WTO have done their job. The rules for open global trade have been laid down, and in the case of the world's leading trading nations, reinforced by legal commitments. Compliance to those commitments is enforceable in what is possibly the only significant system of international governance.

² A key driver of competitiveness from opening services markets is contestability, not exposure to global prices of goods as it in the GATT system. While preferable for other reasons, it is not essential to open services markets on a non-discriminatory basis. And given that services markets by and large are considerably more protected than markets for goods, important gains can be achieved through liberalization of services alone.

It is open to all WTO members to use that system, to elect to lock into it, as Australia and New Zealand did, the result of determined efforts to open their economies. They did not do this because there was some deal offered by a trading partner to open its economy to their exports; they did it according to Adam Smith's observation – to derive the domestic benefit of international specialization in each economy.

Notwithstanding how processes of liberalization will work in the future, it is vitally important Governments emphasize publicly the political and economic importance of the GATT/WTO legal framework. They need to indicate it is of fundamental importance to preserve the fabric of the global trading system, whether or not the Doha Round reaches any conclusions, sooner or later.

The interests of those who understand the importance to their political goals of a decline in the effectiveness and importance of the WTO system also need to be heeded.

Guiding the Invisible Hand

I have suggested that we should not be concerned that the current economic crisis will produce a repeat of the protectionism following the great depression. This does not mean that we should regard the institution of free trade as safe from attack. It has only been a feature of the architecture of global affairs for 70 years.

The opponents of the GATT and its successor were what is it is handy to describe a "protectionist interests". Historically we have described them as interest groups seeking to maximize their economic interests by protecting markets from more competitive interests. These have been companies dominant in the sectors in which they trade and which are not globally competitive and labour organizations concerned to optimize the economic benefits to their members in areas usually enjoying the same protection.

There is another threat lurking which has a deeper and longer genesis, although its modern manifestation is considered a contemporary event.

It is little acknowledged that "An Inconvenient Truth" was a book as well as a film and that it was based on a book Al Gore wrote in 1991 entitled "Earth in the Balance". When published it was widely parodied in right wing media in the US, but among the many elements which reveal what created Al Gore's world view was a statement that when it came to the environment "the invisible hand needed guiding".

It is intriguing how often an innate understanding of important ideas is reflected in what people say, even if they do not realize it. It is clear from his books, that Gore is not an economic liberal.

Stated simply, Gore was saying that free market forces could not be relied upon protect the environment. He was however reflecting a profounder point. There is not enough support in communities for taking action to protect the environment in the way in which Gore and other Greens would find acceptable to create a market in which environmental goods would be priced as sufficiently valuable.

The willingness of a community to buy a product was what generated wealth. In a society with no or few restraints on how people used that wealth, Smith's invisible hand guided the actions which

distributed the benefits. The only driver of exchange was the value the buyer placed on the good. Smith famously derided those who considered that trading durable goods like British-made metal products for consumables like French wine was an activity that reduced national wealth.

So if the community at large did not consider the protection of the environment was sufficiently important to give value to products and services which did so, which Gore evidently understood, what was the appropriate strategy to take to protect the environment, however defined?

The strategy is to exercise political pressure on governments to direct resources to protect the environment. If it is considered a public good, the decision about how much resource is directed to that activity is, in a democracy, ultimately determined at the ballot box.

Environmental groups are not unique in acting this way. Smith warned us what happens when powerful businesses get together. Was his ghost a fly on the wall at the Five Nations Hotel in Richmond? They have also demonstrated disposition to secure economic protection from Government through laws and rules which deny the community the full option to determine the value of their product in the market place.

Some will protest at this comparison. But the economic result, the distortion of the allocation of resources, is that same. Smith's point was that if people invested in things that would yield them the highest return, the economic welfare of the entire society would be raised. Protectionism restricted that choice. Actions by governments to direct financial resources and investment resources to less productive activities will have a similar economic effect.

The erosion of the right of the community to determine the value of environmental goods and services considered necessary to tackle global warming has been egregiously disregarded in the way in which most Western Governments, including Australia have developed their climate change strategies.

This was first reflected in the negotiation of the Kyoto Protocol. The UN Framework Convention, of which the Kyoto Protocol is a subsidiary instrument, makes no mention of using binding caps or targets to reduce emissions. When negotiations began on the Kyoto Protocol, and the call for caps was one of the first demands, little attention was paid in economic agencies in Western Governments – it was largely left to environmental agencies.

As the Protocol took shape and the implications were grasped of the magnitude of the task of capping emissions principally from the combustion of fossil fuels for something so fundamentally important to economic growth as generation of energy, attention was focussed on the most politically expedient and economically efficient way to reduce emissions.

Emissions trading quickly became the favored idea. Governments liked it because it offered a stream of revenue that was not formal tax which could be utilized to help meet the costs of reducing emissions. This was despite the fact the system had only been used once before and that was to distribute the cost of measures to cap emissions of two gases in the United States.

Green groups leapt with alacrity to the idea they were supporting a “market mechanism”. They have become specialists in saying they like market mechanisms, when they don’t.³ This brings us to the most stupendous feature of the current global fixation in the Western world with global warming.

Leaders of most of the world’s leading western economies are supporting imposition in their national economies of a command and control tool which would have the effect of subjecting all economic activity in each economy to substantial government regulation. Many Governments would not have experienced such a tool since the abolition of wartime rationing or, in the case of the transition economies, since the more recent communist era.

Only the President of the Czech Republic, Vaclav Klaus appears to have grasped the point, in public anyway.

“The advocates of global warming alarmism ask for an almost unprecedented expansion of government intrusion, of government intervention into our lives and of government control over us.”

When the fine print of the Shergold Report and the Garnaut Report, and no doubt whatever plan is finally adopted by the Senate, is combed through, proposals are to be found for creation of super regulators who, in one way or another, will be responsible for ensuring the cap is achieved. It is the regulatory consequence of what Klaus perceived.

Yet this has featured little in domestic discussion to date. Regrettably, much of the professional neoclassical economic community in Australia has until only recently devoted its attention to ensuring the market has an optimum influence in trading of permits and that the system distributes the cost as efficiently as possible. Belatedly there has been a limited debate on whether or not a carbon tax would be preferable to a ‘cap and trade’ system for abating emissions. Little is made of the broader implications of using a cap at all.

The decision to plump for cap and trade has, as was predicted, lead to a rent-seeking feeding frenzy. It is no good for the liberal economists who plumped for cap and trade to complain this is because their advice that no exclusions be permitted in the allocation of permits was set aside. Their failure was a failure in the trade of economic advising on public policy; a failure to assess carefully the practicability of implementing a cap and trade system; and the failure to assess the validity of the supposition which was an integral part of the idea, that a global system, as envisaged in the Kyoto

³ It has become commonplace for some environmental groups, WWF in particular, to appropriate the language of market mechanisms when advancing distinctly non-market propositions. For example, WWF contentions that the “market” should be used to restore the environmental health of the Murray Darling river system by creation of tradeable water rights became questionable when it insisted the flows necessary to secure the environmental health of the system had to be determined by the Government and not be available for trading (to a level decreed by WWF as necessary). In the market model the Government would compete with other users to purchase the rights required to secure the environmental flow.

Protocol, was practicable. It would be easier to create a single global currency. And no thinks that is feasible.⁴

And what result is in prospect? My colleague, Jeff Rae, well known many of you, has observed that the cap and trade system amounts to nationalization of all CO2 emissions and that he expects it to be as successful as all previous efforts at nationalization.

We should also be under no illusion that the transgression of the basic principles of open market economics in climate change policy is fully appreciated in Canberra. The need to use such regulatory tools is justified on the grounds that the declared failure so far to halt emissions of greenhouse gases is now cited as the "greatest market failure in economic history".

"Market failure" is cited regularly in discussions about the economics of environmental measures. It is argued that it is a 'market failure' that the environmental services provided by those who tend forests in developing countries are not properly remunerated. This is sophistry. The people in those economies understand very well the value of that forest land, particularly when it is converted for growing cash crops.

Markets fail when transaction costs are too high. This is usually not obviated when Governments intervene. Transaction costs in Government are invariably higher and the intervention usually produces a worse result.

Adam Smith reminds us that the market is the community of consumers. Have they failed to appreciate the value of efforts to reduce levels of greenhouse gases in the atmosphere? They haven't been asked yet, either about the cost or the reliability of the supply of power; but the Government is about test their opinion as it institutes measures that will hike the cost of electricity or, if it prevaricates for too long, deters investment as well in new power generating capacity. I think it is fair bet the consumers will not like it.

What has this got to do with the prospects for a resurgence of protectionism? The quote from Klaus provides an obvious clue.

⁴ This paper is not about what strategies are appropriate for national action on climate change. However given the highly charged nature of the debate, I will state what I consider would be appropriate. Governments are required to respond to a clear public desire to take action. Given the considerable uncertainties, including important gaps in data, about nature and impact of global warming, I do not consider policies which will reduce the economic welfare of society are warranted. In this respect, the most productive path to follow would be for government to support research on technologies which will contribute to improvements in efficiencies in generation of energy, increases in carbon sinks, and management of the polluting impacts. This funding should be available to all industries and sectors and not specified as assisting to preserve the competitiveness of any Australian industry. If it is inevitable that an effort is made to provide some sort of price signal on carbon, a carbon tax should be used. No effort should be made to design that to reduce the impact on the capacity of producers to trade. The reality is that in the foreseeable future, there will be no international regulatory governance of measures to reduce emissions. Measures should be designed as national schemes. Any adverse impacts on the capacity of any Australian industry to compete globally should be fully absorbed as a cost to the economy. No measures which raise challenges to the fundamentals of the WTO multilateral trading system should be contemplated.

If a regulatory control of a large part of economic activity in any national economy is to be erected, any process of exchange which rests on the precepts of open markets, and free trade is the leading processes in the global economy, will conflict with it. This was belatedly recognized by environmental groups in the early nineties when GATT dispute panels ruled that restrictions on trade of products because the environmental impact of how they were produced were not permissible under GATT rules.

Pressure for Environmental Trade Barriers

Environmental groups recognized that trade coercion was a useful tool to enforce environmental goals two decades ago and began to insert trade controls in environmental treaties.⁵ WWF and Greenpeace have lobbied for amendments to WTO Agreements to permit use of such trade barriers. The EU was sympathetic to the general principle so the core of the idea is part of the mandate for the Doha Round negotiations. It provides for consideration of the impact of the intersection of obligations between WTO agreements and multilateral environmental agreements.

The EU has not forced this issue in the Doha Round negotiations. (Pascal Lamy when EU Commissioner for Trade conceded at the WTO Ministerial meeting in Mexico in 2003 that the EU was isolated on this stand in the WTO). However there is a formal EU Directive which requires any measure adopted by the European Commission to take fully into account the environmental dimension. This impels any European Commissioner for Trade to act sympathetically. One result is that, as a matter of course, the EU or environmental officials in leading EU member states will no longer accept provisions in multilateral treaties which expressly protect the rights of parties have acquired through accession to provision of WTO agreements.⁶

Furthermore, the number of environmental regulations which prospectively put the EU in breach of the requirement in the GATT that they not discriminate in trade among trading partners is steadily increasing over time. The most notorious until recently were EU trade restrictions on imports of products containing Genetically Modified Organism.⁷ The EU also has measures providing for restrictions on chemicals according to EU rules about how dangerous they are, imports of electrical and electronic products according to provisions made for recycling those products, as well as restrictions on substances according to levels of toxicity in them which exceed considerably recognized international standards.

⁵ The Convention on International Trade in Endangered Species (CITES), the Convention on the Control of Transboundary Movements of Hazardous Waste (the Basle Convention), and on the Biosafety Protocol to the Convention on Biological Diversity (the Cartagena Protocol)

⁶ In the negotiation of the Biosafety Protocol to the Convention on Biological Diversity, EU Environment Ministers refused to include such a formulation. There is only a weak preambular reference. NGO's which lobbied for this Protocol made clear that a key aim was to weaken the provisions of the GATT which limited the extent to which parties were permitted to use regulations to protect health and safety to restrict trade.

⁷ The US has persistently and successfully challenged the EU trade restrictions on imports of GMOs on the grounds they fail to demonstrate that they are scientifically-based, as required in WTO Agreements.

Environmental groups have agitated for some time in Europe that carbon tariffs be imposed on countries that do not match EU policies to mitigate emissions of greenhouse gases. President Sarkozy when President of the European Council warned China that it faced such measures unless it acted to reduce emission of greenhouse gases. The US Congress has provisions in the Waxman-Markey Bill that would impose such restrictions on China.

Action on these measures are largely on hold until negotiations in the UNFCCC process move to the point where there is some certainty about what global arrangements will be agreed. Trade officials in the large economies have traditionally sought to avert trade wars. The current fragility of the global economy would enhance that sensitivity.

Major trading nations however are less solicitous when it comes to smaller trading partners. The EU has adopted the first climate change trade barrier. The EU Renewable Energy Directive restricts imports of biofuels and will require biofuel imports from countries where it is produced from forest lands to abide by EU rules on forestry. The measure is already under scrutiny in the WTO and several developing country producers of oil seeds have indicated they will challenge the measures under WTO disputes processes.

This measure is the result of a campaign largely emanating from Europe to use trade measures to pressure developing countries with tropical forest reserves to cease deforestation. It also serves the interest of European environmentalists to ensure that climate change abatement strategies work principally by reducing generation of emissions by consumption of fossil fuel and not by building new sinks to absorb emissions.

The EU is also threatening to restrict trade with these countries unless they legislate to impose regulations which will verify the legality of timber products when traded. As well, amendments to the Lacey Act (which outlaws purchase and including import of flora and for a which it is illegal to acquire in other jurisdictions) are designed to restrict the import of illegally logged timber by requiring the purchaser to satisfy themselves the product was legally supplied.

The campaign about illegal logging appears to have been developed and the nature of the problem deliberately magnified as part of a global strategy to halt deforestation.

The extent of concern about climate change demonstrates the increased public support in Western economies for action to protect the environment. There are three reasons to suppose that environmental groups like WWF and Greenpeace will continue to campaign to alter the WTO to allow environmental trade restrictions to be used.

The first is to remove from the threat of WTO challenge the capacity of institutions in the larger economies (the European Commission and Parliament and the US Congress) to threaten trade sanctions against others unless they comply with policies preferred by these Green organizations.

The second is to weave into the formidable dispute settlement processes of the WTO the right to use such measures. For all the criticisms that are made of the WTO, there is very deep respect for the effectiveness of the WTO machinery. No other system of international regulation is as effective.

Finally, there is an ideological desire to diminish the role the WTO plays in buttressing the multilateral trading system. There is a strong disposition among environmental NGOs to weaken the

free trade values of the WTO. Virtually all, large, global NGOs oppose globalization.⁸ Each time there is a major global conference on development, the leading NGOs typically ally to advance positions which advance anti-globalization positions. The result is that the WTO has now replaced the World Bank as the demonized global economic institution.⁹

A fundamental Challenge?

The response to the “Global Financial Crisis” demonstrates that the general commitment of the major economies to maintain the structure and laws and rules of the multilateral trading system remains robust. However it is clear that there is a strong policy trend in industrialized economies to elevate environmental policies over others and to use a heavier regulatory hand to implement them.

The proposal to create a global cap and trade system to alter the comparative advantage of economies in a uniform way by regulating production of energy to meet climate change goals clashes fundamentally the philosophy of the WTO system that members may not restrict trade in a manner which restricts their capacity to prosper on the basis of their perceived comparative advantage.

It is central to Green philosophy that protection of the environment should be the overriding interest in public policy. This is increasingly featuring in the international policy of the EU and its members.

Some foresee a clash between two competing systems of international obligations. Others opine there is more support for climate change than free trade in public opinion, suggesting that parallel action be taken in the WTO and the UNFCCC negotiations to ensure this no conflict.

The great clash is improbable. There will not be a global climate change agreement which will erect a global system to regulate emissions any time in the foreseeable future. The greatest weakness in most of the debate and propositions about how to develop global strategies to manage climate change is disregard of the fact we do have not supranational governmental institutions. A global system to trade emissions requires such a model. It would be easier to develop a world currency than to create a regulated global system of cap and trade. It is therefore unrealistic, if not incompetent, to argue for approaches to climate change which rest on that assumption.¹⁰

⁸ As well as the Green groups, Oxfam, most of the UK based development NGOs, Medecins sans Frontiers, Consumers International actively oppose free trade and advance strategies for relying on the public sector rather than the private sector to deliver services, such as health and education. What is not fully appreciated is how much WWF played a leading role in fostering the anti-globalization sentiment against the WTO over the last decade.

⁹ A key reason is that on environmental policy, and particularly forestry, World Bank policy has been effectively captured by the WWF. Other NGOs have now so influenced the safeguards policy conditions the Bank sets for loans that major companies, particularly in the extractive industries, will actively avoid funding from the Bank or the International Finance Corporation. The Bank is increasingly becoming a vehicle to deliver NGO anti-globalization policies through lending to developing countries.

¹⁰ In this respect, then, the reality is that a global agreement on climate change will be only as good as the political consensus among the leading economies. That is the turn factor which is central to what can be negotiated, not any assertion that the urgency or gravity of the situation is what should shape what can be done.

Nevertheless, national measures to increase the cost of power will affect the competitiveness of industries and have already generated pressure for carbon tariffs.

Vigilance is required

The challenge is to ensure the integrity of the multilateral trading system is not diminished. And, over the next quarter century, to ensure that it is not subordinated in international public policy to the intrusion of a directed regulatory hand which is supposedly necessary to protect the environment. What should be done?

Climate change policy is the leading vehicle through which the challenge of Green protectionism will be made. This has to be priority area for attention.

Free market economists must insist that Government ensures that the necessary information be made available to enable consumers to make informed decisions about what is the most appropriate climate change strategy for Australia.

Democracy is not enough to enable consumers collectively to decide what value to attach to an environment activity. They need information about the measure and the cost.

It is an indictment of both sides of politics that neither considered it a duty to provide information to citizens about this issue which would enable them to make an informed judgement about what is the appropriate response for Australia. Lack of sound independent analysis of the implications of climate change policy is one of the greatest shortcomings in current policy formulation.¹¹

This raises the disturbing possibility that we are seeing in Canberra a drift away from the framework of sound policy-making which was such an essential feature of the reforms of the Hawke/Keating era and which, by and large, was followed in the Howard era.

Stan Kelly laid the basis for the legacy we have today which is the Productivity Commission. It was an essential part of that process of sound policy making. It is a standing criticism in the scientific community that no independent analyses of the impact of global warming on Australia have been undertaken.¹² Gladly, we are starting to hear calls for the Productivity Commission to analyse the economic impacts of strategies under consideration to reduce emissions.

Free market economists must engage in shaping policies to improve the environment to demonstrate alternatives to protect and manage the environment which do not require a priori managed intervention by regulatory authorities

The same standards of good practice and efficiency which shape regulation of trade and production should be applied to regulation of the environment.

¹¹ Another is the indecent haste with which the policy has been assembled and implemented. It is likely to produce several significant failures as a consequence.

¹² In contrast, an independent analysis and public review of all aspects of Australian forestry was undertaken in the Hawke/Keating era before the National Forest Strategy was developed.

We are familiar with them – reduce executive discretion in regulation, establish external and fixed standards, use tools that reduce pollution as close a possible to the point of pollution, apply the principles of proportionality of impact to the problem, aim to create a light hand; and give space to the private sector to deliver results and don't unnecessarily or gratuitously constrain it.

Yet, with the exception of the Productivity Commission which has excellent capacity in this respect, little attention has been paid to the need to argue for more efficient regulatory models for managing environmental effects. The fecklessness with people who toy with Life Cycle Analysis as a concept for regulating environmental impacts, instead of limiting its use to measuring environment impacts, is dismaying.

It is incumbent on us all to contend that the exchange of goods and services among nations should not be conducted on any other basis than the precepts of free trade. Greens and radical environmentalists will argue that protection of the environment is a morally superior activity. There is no intrinsic reason why these two great public policy interests should be in conflict.

In every case an environmental trade barrier has been proposed, it is either to defray the domestic cost of the action (by imposing a trade barrier on competing imports); or it is an action of coercion (by limiting access to markets) to advance a policy goal that others do not themselves accept.

This is not to say we cannot negotiate international agreements on the environment. We can. But they must be governed by political common sense and respect for national sovereignty.¹³

Free market economists should be absolute in insisting that Government accept that once the fundamentals of a global system based on free trade are compromised, the moral imperative of organizing economic activity and commerce in a way that raises the living standards of people is lost.

The reference point is the preservation of the integrity of the multilateral trading system.

It is also essential to contend that the cost of climate change mitigation measures has to be fully absorbed by each economy, in the same way societies should absorb the full cost of measures to protect industries, if they accept that there should be protection, and not try to defray the cost onto trading partners by imposition of trade barriers.

These are strange times. The quality of public policy deliberation on climate change is at a nadir. Vigilance is required. The welfare of the people is at stake.

¹³ There is a standard model for treaty making which is the only one upon which global agreements to alter common conditions can work. Parties agree on the nature of the problem and they agree on common measures to apply in their national jurisdictions. For example the nations of the Eastern Tropical Pacific region have negotiated an agreement whereby each party commits to apply common laws in their national jurisdiction to require nationally flagged tuna fishing boats to adopt fishing procedures that minimize the incidental killing of dolphin while netting tuna. This contrasts with earlier actions by the US Congress to ban imports of tuna from other nations in that region unless their tuna fishing fleets applied the same methods to reduce incidental kill of dolphin that the US Congress had legislated as compulsory for US registered tuna fishing fleets. This was an exercise of trade coercion by the US. It also transgressed the national sovereignty of its trading partners and meant the US was discriminating in the treatment of imports of tuna between one country and another. GATT disputes panels ruled against the US measure. However environmental groups prefer the trade sanctions route. Not doubt is it quicker and can be more effective, but it is uncivilized and ironic. In the area of terrorism or settlement of disputes among nations, many of these activists would argue that large powers should not throw their weight around.

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