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## Tensions at the Economy-Environment Interface

As the preceding chapters make clear, serious environmental harms across APEC threaten to directly undercut the welfare gains achieved through economic growth (chapter 3). Furthermore, widespread uninternalized externalities, unmanaged common resources, and price-distorting and environmentally damaging government policies (all of which are responsible for serious environmental harm) undermine the efficient functioning of market forces and further reduce social welfare (chapter 4). Another important reason to address environmental issues arises from the range of tensions at the economy-environment interface that threaten to spill over into the economic realm and make countries back away from trade and investment liberalization—or, worse, erect new protectionist barriers. Given that the increasing openness of national economies has been central to the economic vitality of the Asia Pacific region, a retreat from further liberalization could leave many citizens in APEC’s developing nations in poverty and may, more broadly, derail economic progress across the region.

At stake is the political will to proceed with further economic integration. In many APEC countries, both developed and developing, the political forces in favor of trade liberalization face constant challenges from those who see expanded international trade as a threat to national sovereignty as well as to traditional economic structures and values. In the United States, in particular, majority support for new trade and investment initiatives cannot be taken for granted (Nader 1993; Perot 1993).

These tensions also endanger the delicate trade bargain between developed and developing countries.<sup>1</sup> The industrializing nations of APEC

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1. As Tay (1996, 193) notes, many (e.g., Khor 1992) in the developing world “believe [they] have paid too high a price for that bargain. They seek to re-open some of the past discussions, and to question the entire basis of international trade.”

have benefited enormously from their access to export markets, and they recognize the need to open their own markets in return. But many officials in the South fear economic domination from the larger and better established enterprises of the North; they are concerned about rising protectionism, especially in the form of hidden nontariff barriers, in the United States and their other export markets. Conversely, business and government leaders in APEC's developed nations recognize the significant opportunity represented by the large and growing markets of APEC's developing members. Thus, although they worry about a flood of cheap imports, they have been willing to promise to keep their markets open, minimize the use of trade disciplines, and work within the multilateral framework to resolve trade disputes, in return for the removal of the remaining substantial trade barriers in developing countries (and Japan) (Bergsten 1996).

Political support for further economic integration might be undercut by any one of a number of strains at the economy-environment interface. The central tensions include

- a conflict between developing-country desires for market access commitments, including guarantees that environmental standards will not be used to exclude their products, and developed-country insistence on maintaining regulatory sovereignty and the right to set their own environmental standards;
- disputes over the appropriateness of using trade measures to reinforce multilateral environmental agreements or of applying trade sanctions unilaterally to achieve extrajurisdictional environmental objectives;
- disagreement over the legitimacy of competitive advantages accruing to nations with lower environmental standards;
- controversy over the benefits of freer trade and economic growth more generally, with some environmentalists rejecting these goals as inevitably leading to more pollution and the depletion of scarce resources; and
- discomfort in some nations at the prospect of deepening economic relationships with countries whose behavior, including environmental performance, dips below what they regard as baseline standards.

These tensions are not new. They have, however, gained prominence as a result of deepening economic integration across APEC. The primary effect of integration—as many small and medium-sized economies have realized—is a considerable loss of autonomy over fiscal and monetary policy, as international markets impose external disciplines on economic policy (OECD 1997; Cooper 1994; Greider 1997). A similar loss of autonomy over environmental decisions occurs in the context of regional integration and globalization (K. Anderson 1995a; Rodrik 1997). Increasing

interdependence has also put new economic issues—competition and antitrust rules, tax codes, and environmental standards—at the top of foreign and trade policy agendas.

The increased scrutiny given to what have traditionally been “domestic” policies can be attributed to two factors. First, as barriers to trade are removed and international competition becomes more intense, differences in domestic policies become more significant in determining trade and investment flows and the pattern of industrial location (Lawrence, Bressand, and Ito 1996; Lawrence 1996; K. Anderson 1996). This competitiveness pressure explains complaints by organized labor about “social dumping” and by environmentalists about “eco-dumping,” and the demands that there be baseline standards for all participants in a free trade area to ensure “fair” trade (Bhagwati 1993a).

The second reason for increased scrutiny of domestic policies is that economic integration brings countries into closer contact with each other, creating a sense of community and giving rise to pressures for common standards that define the bounds of behavior for all those operating within (and benefiting from) that community (Esty 1996b, 638-48; Rodrik 1997, 29-44). Of course, it is often difficult to disentangle the source of demands to reduce social policy differentials. Most such demands arise because of both competitiveness concerns, which may in part be protectionist, and a sense that all members of a community should adhere to communitywide baselines of behavior.

The scrutiny given to behind-the-border policies is heightened in APEC, where values are diverse and policy differentials are wide, creating the potential for significant acrimony. Globalization and regionalization have thus unleashed forces upon APEC’s members that have created an increasing interest in each other’s domestic environmental policies and in how these policies are used directly or indirectly to influence the environmental behavior of other countries. This interest is unlikely to subside as integration deepens (OECD 1997).

## Market Access and the “New Protectionism”

An important tension in APEC arises from the competing demands of its less- and more-developed members: the former seek guaranteed access to developed-country markets, while the latter want to be able to set their own health and environmental standards at whatever level of risk they independently deem appropriate (OECD 1996; Arden-Clarke 1993).<sup>2</sup> The

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2. A second dimension of concern about market access and protectionism involves private-sector rather than government behavior. In particular, tensions may arise if voluntary eco-labeling schemes or environmental management certification systems (such as ISO 14000) become default environmental product and process standards either because consumers come to expect products to carry eco-labels, or because companies require their suppliers

belief among some countries, notably Indonesia and Malaysia, that they are reducing their trade and investment barriers faster than they would otherwise choose to compounds the strain. These countries accept the faster pace of liberalization on the basis that the United States and Japan will ensure continuing and improved market access and thus greater export opportunities. Developed countries, while aware of this concern, are faced with domestic demands that environmental standards not be weakened in the name of market access.

A stronger version of the concern about market access is the fear in developing countries that environmental standards might be a guise for protectionism.<sup>3</sup> In a number of countries, including the United States, some environmental interests have been “captured” by, or have colluded with, domestic industries seeking to operate in less-than-open markets (Crowley and Findlay 1996; Low and Safadi 1992; Oxley 1993; Palmeter 1993; Van Grastek 1992). Wariness about coalitions of the “green and greedy” (Oye and Maxwell 1994) is not unfounded. In a number of cases, industrialists and environmentalists have proposed higher domestic environmental standards, countervailing duties, or import restrictions on goods and services produced in countries where process standards are less strict than those at home.

The difficulty in these cases lies in separating legitimate environmental objectives from overly stringent health and environmental standards that are designed to protect industry. In January 1997, for example, the Australian government decided to retain its ban on imports of uncooked Canadian salmon even though a draft inquiry had found that such imports did not put Australian salmon stocks at risk of contamination. The decision no doubt turned, in part, on pressure from the Australian salmon industry (André Dua, *The Australian*, 13 January 1997). Cases such as these exemplify the tension between market access and environmental standards that looms large as a source of potential friction within APEC. APEC countries thus need—and APEC is well positioned to provide—a procedure by which they can ascertain whether health and environmental standards are based on a sound scientific inquiry, appropriately designed to reflect community preferences, and well tailored to address the ecological or public health challenge, or whether they are a product of protectionist influence.<sup>4</sup>

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to have ISO 14000 certification. These concerns may sharpen if the standards adopted are perceived to be biased, inappropriate, or otherwise flawed—no matter that they are voluntary and private-sector driven. (For a discussion of ISO 14000 in the APEC context, see Roht-Arriaza [1996].)

3. Developed countries are by no means the only nations with standards that raise such concerns. South Korea, for example, has effectively used health (or “sanitary and phytosanitary”) standards to prevent agrifood products from entering its domestic market (Smithers and Dua 1994).

4. Esty (1994a, 117-27) spells out an environmental “legitimacy” test, designed to separate bona fide environmental policies from those motivated by protectionism.

## Trade Measures as “Sticks”

Many developing countries are uncomfortable with the use of trade measures to achieve environmental goals (Hudec 1996). They fear that the use of trade policy as a “stick” will be arbitrary and almost always wielded by the strong against the weak.<sup>5</sup> In particular, they object to the use of trade restrictions to enforce multilateral environmental agreements (MEAs).<sup>6</sup>

But even more upsetting to developing countries has been the unilateral use of punitive trade measures—in particular, import bans—by the United States to achieve extraterritorial environmental objectives. The US ban on imports of Mexican tuna caught using purse seine nets, which also killed dolphins, stands out as a celebrated case in point.<sup>7</sup> More recently, the United States raised the ire of Thailand and Malaysia by banning imports of shrimp caught using fishing techniques that threaten endangered sea turtles.<sup>8</sup> While the United States is attempting to negotiate a resolution with the aggrieved parties, Thailand has decided to go ahead with a complaint it filed at the WTO.<sup>9</sup>

Developing-country anxieties are shared by many free trade advocates, who worry that the use of trade measures to advance environmental goals will weigh down an already fragile trading system (Bhagwati 1993b).

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5. These fears are not groundless. Trade sanctions often appear to be somewhat arbitrarily imposed by powerful nations on weaker ones. US sanctions against Taiwan (but not the more egregious violator China) for failing to control trade in rhinoceros horns and tiger bones as required by international endangered species protection agreements provide one example of this phenomenon. The failure of Austria’s attempt to label and tax timber from unsustainably managed plantations and forests in the face of threatened retaliation by ASEAN countries provides further evidence that power, more often than principle, drives the use of trade measures.

6. The reluctance of developing countries to submit to trade disciplines in MEAs may reflect, in some cases, the absence of any serious intention by the signatories of adhering to the commitments they have made. Alternatively, among some countries the aversion to using trade measures in support of environmental goals may derive from a fear that they will have trouble meeting the goals set.

7. Two GATT dispute resolution determinations concluded that the US measure violated trade rules. In separate “tuna-dolphin” decisions (one in a case brought by Mexico and the other by the European Union), GATT “panels” concluded that the US tuna ban violated GATT’s Article III national treatment requirement, and that while Articles XX(b) and (g) were designed to protect human or animal life and exhaustible natural resources, parties could not take advantage of these exceptions to justify “extrajurisdictional” actions (Esty 1994a, 268-69).

8. Trade bans such as this have dramatic economic impacts. Thai shrimp exports are forecast to fall to 40 billion baht in 1997, down from 51 billion in 1995 (*Bangkok Post*, 26 June 1997).

9. Thailand has been joined in its action by Malaysia, India, and Pakistan (*Bangkok Post*, 26 March 1997). ASEAN, furthermore, recently decided not to sign an agreement with the United States to protect sea turtles, choosing instead to sign their own protection pact (*Bangkok Post*, 14 March 1997).

Why, they ask, must the trade regime do the bidding of environmental policy? Shouldn't pollution control and resource management aims be pursued with environmental policy tools?

Many environmentalists fear the opposite result. In particular, they worry that new trade agreements might impose disciplines on the use of trade measures employed to promote participation and compliance with international environmental agreements. They see economic integration and market access commitments as a backdoor mechanism by which trade goals will be positioned ahead of environmental ones. While other tools are available to affect environmental policy choices in other countries,<sup>10</sup> environmental advocates believe that the alternatives will be ineffective (e.g., eco-labeling) or, in practice, unavailable (e.g., resources for education or funding to induce compliance).

In contrast, trade measures, or the threat thereof, have been demonstrably successful. Both China and India hinted that they might not sign the Montreal Protocol, but each ultimately joined the worldwide effort to protect the ozone layer when spurred by the prospect of curbs on their trade (as well as the promise of funding to support the acquisition of CFC substitutes) (Brack 1996). Similarly, Taiwan, facing sanctions from the United States for failing to uphold the Convention on International Trade in Endangered Species (CITES) controls on trafficking in rhinoceros horns and tiger bones, dramatically improved its endangered species protection program (*Los Angeles Times*, 19 March 1995). In addition to supporting the use of trade provisions in MEAs, many NGOs advocate the use of unilaterally imposed trade sanctions.<sup>11</sup>

In the absence of a dispute mediation procedure that defines the legitimacy of, and boundaries for, trade measures aimed at changing the environmental behavior of other countries, APEC's economic vision remains constantly at risk. Aggrieved parties—either those subject to sanctions or those who feel that a trading partner is failing to uphold environmental obligations—may walk away from their trade commitments or the liberalization process more generally.

## Competitiveness and “Race Toward the Bottom” Concerns

Many American industries complain that stringent US environmental standards place them at an unfair competitive disadvantage vis-a-vis companies operating in countries with lax environmental standards. They

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10. Esty (1994a, 132) provides a comprehensive list of possible tools.

11. Charnovitz (1993, 50), for example, observes: “treaties do not appear like magic spirits. . . . Thus, those arguing that unilateral action is inappropriate have the burden of demonstrating the feasibility of [alternatives].”

demand a “level playing field” (Cooper 1994; S. Richardson 1992; Charnovitz 1995). Environmental advocates, in turn, worry that these competitiveness fears will trigger a regulatory “race toward the bottom” as countries seek to attract new industrial activity to their jurisdiction or prevent domestic industries from migrating to countries with lower environmental standards (“pollution havens”) by “lowering” their environmental standards.

Developing countries, for their part, see the call for “fair” trade as protectionist, as well as intruding on their national sovereignty (Haas 1993). They object to being held to standards they perceive to be too strict given their level of development, environmental preferences, endowments, and assimilative capacity.<sup>12</sup> Differences in environmental standards are part of comparative advantage, they argue. Moreover, such differences are what make gains from trade possible.

Who is right? Most empirical studies seem to suggest that competitiveness and productivity suffer little from stringent regulations (Kalt 1988; J. Richardson 1993; Repetto 1995), and there is little evidence of industrial flight to countries with lower environmental standards (Dean 1992; Low and Yeats 1992; Jaffe et al. 1995; Eskeland and Harrison 1997). Yet politicians do fear the effects of regulation on competitiveness, and there is ample anecdotal evidence to support their conclusions (Esty 1994a, 21-23). Moreover, some recent analyses (Han and Braden 1997; van Beers and van den Bergh 1997) conclude that strict environmental regulation *will* affect competitiveness. Low standards in some jurisdictions might thus engender a welfare-reducing race toward the bottom.<sup>13</sup>

The empirical data must furthermore be taken with a grain of salt. Races toward the bottom are often difficult to spot because jurisdictions rarely lower environmental standards or remove environmental regulations that are already on the books. Instead, competitiveness concerns create a “political drag” (Esty 1994a) on environmental policymaking.<sup>14</sup>

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12. Where differences in standards legitimately reflect points of comparative advantage, they need not be—indeed, should not be—“leveled.” But in other circumstances, variations in standards may reflect not natural advantages but rather artificial ones akin to manipulated exchange rates. In such cases, policy intervention is justified to avoid triggering a competitiveness-driven race toward the bottom in environmental regulation. We unpack the call for “level playing fields” and the related demand that trade be “fair” in greater detail in chapter 7.

13. Some observers (e.g., Revesz 1992) argue that “regulatory competition” actually improves welfare, since competitiveness pressures force governments to operate more efficiently. But Esty (1996b) has shown that the market for industrial location in which jurisdictions compete is far from perfect and thus will often deliver inefficient and welfare-reducing outcomes.

14. A good example of the effect of political drag, or what Zarsky and Hunter (1997) call being “stuck in the mud,” is the European Union’s failed attempts to implement a carbon tax because of the fear that its members’ competitiveness would suffer if the United States did not follow suit (Esty 1994a).

Governments relax their enforcement of existing standards (Barron and Cottrell 1996), quietly promise to turn a blind eye to environmental harms, or choose not to raise standards. In each of these instances, empirical studies face the nearly impossible task of measuring something that does not happen.

In any case, the political reality of concerns over competitiveness cannot be denied. No issue retained more bite throughout the NAFTA approval process (Esty 1994b; Abbott 1995). If the current US debate over the extension of fast-track negotiating authority and the accession of Chile to NAFTA are any guide, the environmental competitiveness issue appears to have intensified (Richard Gephardt, letter to Democrat congressional colleagues, 26 February 1996).<sup>15</sup>

Resolving the tension between competitiveness concerns and fears on the part of developing countries that environmental standards will be inappropriately imposed on them will require a carefully structured bargain. APEC is ideally situated, as we argue in chapter 9, to provide the policy coordination required to manage this tension while at the same time facilitating the expansion of trade and investment.

## Resource Depletion and Pollution Caused by Trade-Led Growth

Some environmentalists see economic integration as a step in the wrong direction. They fear that trade and investment liberalization promotes economic growth, which leads inexorably to more pollution and the unsustainable consumption of resources (K. Anderson 1993). In particular, environmentalists who adhere to the “Club of Rome” or “limits to growth” worldview, which emphasizes population expansion and the likelihood of resource shortages (Meadows 1972), see all economic growth as harmful (Alker and Haas 1993; Andersson, Folke, and Nyström 1995). For them, there can be no reconciliation with free traders. Trade means growth, and growth means inevitable and irreversible environmental despoliation.<sup>16</sup>

Fortunately, the theories forecasting limits to growth have been shown to be largely overblown.<sup>17</sup> Real-world experience suggests that, in fact,

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15. In NAFTA, the conflict of unfair competitive advantage versus legitimate comparative advantage was ultimately resolved through an “Environmental Side Agreement,” a commitment by all parties to enforce their own standards more vigorously—a precedent that may be useful for APEC.

16. This view is embraced by both developed- and developing-country NGOs (Eder 1996, 117).

17. At the opposite end of the spectrum are a new generation of environmental optimists who see few environmental problems as either real or ultimately threatening (Easterbrook 1995).

the environmental effect of economic growth can be either negative or positive (OECD 1994). Whether economic growth is sustainable turns in large measure on whether the scale effect of expanded activity (which leads to increased pollution and consumption of resources) overwhelms (1) the income effect of growth (which provides more resources for investment in environmental protection and creates a wealthier public that demands greater attention to environmental quality); (2) the technology effect (which occurs as countries get richer, invest in research and development, and acquire newer, less-polluting plants and equipment); and (3) the industrial evolution effect (which arises as nations develop and their economic base evolves toward a cleaner high-tech and services-based economy).

Most environmentalists today accept the view that development can be sustainable. The “sustainable development” paradigm holds that economic growth can be environmentally beneficial if policymakers ensure that pollution control efforts advance in tandem with expanded production and consumption, and some portion of the material gains from growth are devoted to environmental protection. But despite the potential for good that many environmentalists see in economic growth, many fear that the world’s current growth trajectory is unsustainable, especially in APEC.<sup>18</sup>

The demands of environmentalists for a course correction have elicited a strong response from countries in the developing South. Malaysia, Indonesia, Singapore, and others argue that they have a fundamental right to development. For support, they point to Article 8 of the Stockholm Declaration, which says that “economic and social development . . . are necessary for the improvement of the quality of life,” and Principle 3 of the 1992 Rio Declaration, which recognizes the “right to development.”<sup>19</sup> The leaders of APEC’s industrializing economies resent what they see as attempts by the industrial North—and especially environmentalists, whom they regard as “eco-imperialists”—to retard their economic development and their progress toward prosperity. They are backed by an influential group of domestic politicians, advisers, academics, business leaders, and journalists who, armed with the confidence provided by recent economic success, have been forthright in expressing their views. Nevertheless, most officials accept the model of sustainable development. And many of APEC’s developing countries have, in fact, strengthened their domestic environmental regimes in the last decade to reflect their commitment to sustainability.

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18. This view has been forcefully articulated at the People’s Summits in Osaka and Manila, held in parallel with the Leaders’ Summits.

19. The United States took a “reservation” on this point at the Rio Earth Summit and thus rejects the notion of any right to development.

But the agreement of most environmental NGOs and most developing countries on sustainable development as the goal—despite the more strident views on either side—does not diminish the seriousness of the tension outlined above. Because environmental groups in the United States represent such an important swing constituency in trade debates, their views cannot be ignored (Esty 1997b). Without an effort to address this tension, US participation in future trade liberalization agreements cannot be guaranteed—with potentially dire global consequences.

## **Discomfort with the Policy Choices of Trading Partners**

Citizens in APEC's developed countries are increasingly expressing discomfort with the environmental policy choices of certain other countries—an unease that grows as economic integration makes these countries more important trading partners or competitors. This discomfort has received its strongest expression in the United States, where people ask whether they really want cheap imports if the goods are produced under conditions that they consider morally unacceptable. Should they accept Thai shrimp, the harvesting of which causes the death of endangered sea turtles? And do they want Chinese toys made in factories that expose workers to toxic chemicals, dramatically increasing the workers' risk of developing cancer?

Such questioning of the moral content of trade, however, raises serious concerns in the developing world, where countries strongly believe that social policy should not be dictated to them. National sovereignty, they assert, is the cornerstone of international relations.

As we discuss in the chapters that follow, economic integration to some extent creates a sense of community that, in turn, gives citizens a basis for demanding that others with whom they are dealing meet shared, community-determined environmental values. As the sense of community grows over time, and as the level of economic interaction broadens and deepens, the scope of the demands that citizens feel free to impose on each other may also expand. This process of parallel social integration will not always be smooth, but it will be necessary if countries wish to deepen their economic ties. It will test the developing-country expectation that "domestic" environmental policy should be immune to external pressures, a belief that misunderstands the imperatives of deepening economic integration. And it will challenge the developed-nation view that their moral preferences should be accepted by others. In sum, in the absence of a political foundation to undergird the push for economic integration, the fundamental mission of APEC—trade and investment liberalization—may grind to a halt.

## Conclusion

Each of the above tensions—relating to market access, the use of trade measures, competitiveness concerns, the effect of trade-led growth on the environment, and unease with trading partners' social choices—is serious. And each has the potential, if not carefully managed by APEC, to cause countries to back away from their commitment to freer trade or, less likely, to quit the international trading regime altogether. The missed opportunity to achieve social welfare gains would be a high price to pay for inattention to environmental issues, particularly when the tensions are plainly apparent and, as we argue in chapter 6, APEC is well positioned to respond.