



Staying Open for Business: Environmental Competitiveness and Trade

The role of environment policies and practices in global trade has increased dramatically over the past decade or so. In the early 1990's issues related to environmental sovereignty, including cross-border movement of hazardous materials, unchecked use of harmful pesticides, and managing effects of mobile waste streams, figured significantly in the debate over the North America Free Trade Agreement. Establishment of the World Trade Organization (WTO) in 1995 created a platform that went far beyond the predecessor global trade agreements (GATT) for taking environmental and social consequences of trade into account in the course of trade negotiations.

More recent U.S. trade agreements, such as the Central America Free Trade Agreement (CAFTA) and the Morocco, Jordan, and Chile bilateral free trade agreements, now pay greater attention to worker health and safety and reducing implicit subsidies from unsustainable extraction and pollution. These agreements place a larger burden than their predecessors on public agencies to establish and enforce environmental regulations that secure a sustainable a foundation for economic growth and international trade. The agreements also call for traders and producers to assess and continually improve their own environmental and social impacts using third party audit and certification schemes to more exacting standards.

The European Union has similarly included environment features in their trade agreements and implementing policies. Anti-dumping rules increasingly look at the environmental costs of production and restrict member countries from pricing trade goods "below cost." Complementary EU directives restrict countries trading within and into the EU from supporting pollution or other "environmental subsidies" and require them to enforce the "polluter pays" principle. Other EU directives now require member countries to encourage utilities and industries to include the real costs of water, energy, and pollution in their pricing.

As part of the evolution in environment policies and practices in global trade **USAID has taken a leadership role** more so than previously on behalf of the U.S. Government in shaping and implementing those policies and in promoting complementary policies in developing country trading partners. For example, an interagency group in which USAID played a prominent role negotiated the Environmental Cooperation Agreement (ECA) with Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua. The ECA spells out priority areas and means of cooperating on environmental protection and management in the context of CAFTA. Key elements of the ECA include those in which USAID historically provided leadership, such as:

- strengthening each country's environmental management system capacity
- promoting voluntary market incentives for environmental protection
- creating effective public-private conservation partnerships

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- improving management of migratory or endangered species
- exchanging information on implementation of multilateral agreements
- promoting best practices in environmental management
- facilitating clean production technology development and transfer
- actively promoting environmentally beneficial goods and services
- improving public participation in environmental decision making
- exchanging ideas and experiences in environmental review practices

The role of governments in trade has traditionally been to ensure that agriculture products and agriculture economies do not pose risks to human, animal, and plant health. Declines in tariff barriers and the dramatic acceleration in international trade in agricultural goods have outstripped public inspection capability. Instead, **new demands are being placed on exporters through a steadily expanding array of private international standards.** Examples of such standards are ISO 14001 (environmental management), HACCP (food safety), EurepGAP (farm certification for food safety, environmental protection, and workplace safety), Green Globe 21 (environmentally sustainable travel and tourism), FSC (sustainable forest management), and IFOAM (organic farm production). Through standards like these the private sector has stepped in to address trade issues related to sanitary and phytosanitary conditions, worker welfare, product safety and environmental responsibility in the production process where government capacity and international agreements could not.

The proliferation of bilateral and multilateral environmental agreements, more effective national environmental regulatory regimes, and private product and production performance standards in a context of globalizing supply chains and markets have vast repercussions on international trade.

First, on the supply side they create a fiercely competitive environment that encourages firms to pay close attention to water and energy consumption, waste generation and management, and worker health and safety. Inefficient use of water, energy, and other inputs result in costs that can undermine a firm's competitiveness. Fees and fines associated with waste management practices cost money, open the door for corruption, and can risk business closures. Rejection by supply chain buyers or retail customers of contaminated, mislabeled, or improperly packaged products can be very costly. Competitive exporters have to operate in a manner that is sustainable, fair, safe, and environmentally well-managed in order to succeed and thrive. They must understand and apply best production practices and standards as a matter of business.

Second, on the demand side they give greater power to discriminating consumers, and as a result consumers play an increasing role in competitiveness and enforcement of de facto environmental regulations. Surging demand for organic foods and beverages; increasing consumer attention to food safety, nutrition, packaging, and production conditions; and purchasing preferences for 'ecofriendly' products and production processes highlight changing consumer interests. The proliferation of environmental and related safety requirements through treaties, regulations, private certification schemes, and labeling allow producers to differentiate their products in the marketplace in response to the demands of various market segments.

Third, they encourage a more expansive approach to corporate risk management.

International supply chains now favor efficient and more dependable production facilities and discriminate against those with environmental and labor liabilities. Spurred on by international NGOs, internet publicity, community activism, and consequent attention during trade negotiations many companies carefully manage their reputational, and ultimately their financial risk exposure. Lax regulatory environments and frequent infractions are simply not acceptable to many international corporate buyers. Other effects on a company's stockholders, insurers, and lenders have also helped elevate corporate responsibility issues to the level of bottom-line concerns. Under the new conditions of international trade corporations can easily shift their sourcing over vast distances. This means that the environmental policies of developing countries are critical to helping their enterprises begin to access international markets through the supply chains of major corporations.

Global environmental requirements, whether arising from multilateral or bilateral agreements, from the regulations of markets such as the EU, or from private international standards, need to be recognized not as creating trade barriers or costs, but as creating opportunities for expanding sustainable trade. **Three strategic areas for environmental policy reform** must figure prominently in any developing country's effort to take advantage of these opportunities.

1. Improve capacity to meet international commitments

Developing countries often see a conflict between their interest in increasing their international sales and their commitments under multilateral environmental agreements, such as the Biodiversity Convention, the Convention on International Trade in Endangered Species, and the Convention on Persistent Organic Pollutants. USAID has a long record of providing support to developing countries to meet their international commitments principally by (a) helping to establish a framework of laws and implementing policies for agencies charged with implementing these conventions; and (b) assisting the financial and commercial actors to better understand and incorporate these commitments into business practices. Most often this support is provided through the following activities:

- project support for developing and implementing national environmental action plans and strengthening regulatory agencies responsible for conducting environmental reviews of public and private investments
- routinely conducting biodiversity and tropical forestry assessments of USAID strategic plans in order to identify the current state of natural resources and the extent to which USAID's program may address constraints and opportunities
- establishing or supporting clean production centers, environmental loan funds, and related activities that work to make businesses aware of government requirements and to support technical and management options for reducing pollution and improving enterprise competitiveness

2. Expand participation in environmental governance

Although most countries now have framework environmental laws, many have not yet developed implementing guidelines or institutional capacity to implement environmental policies. Moreover, many countries have not yet established standardized environmental review protocols that can serve as a basis for partnerships with communities and other stakeholders. Public participation in

impact identification and mitigation, public review and disclosure of environmental assessments, and methods to help civil societies voice environmental concerns have steadily become more important in trade and environment discussions. Accepted international environmental assessment protocols, such as those formulated by the International Association of Impact Assessment, call for routine and meaningful public involvement in assessing public and private sector projects. Methods that have been used to increase public involvement in environmental governance include:

- strengthening the role of the judiciary (judges, prosecutors, regulators) by increasing their awareness and accelerating advocacy for incentive-based reforms together with effective prosecution of polluters and resource looters
- increasing the role of journalists and independent media channels and strengthening global and regional networks for environmental compliance
- conducting participatory appraisals, community mapping, and needs assessments at appropriate levels to better design interventions and develop publicly supported roadmaps for required changes in policies and devolution
- deploying environmental management systems in public utilities, municipal operations, and private industries that improve communication with, and participation of, communities and local civic groups

3. Establish environmentally friendly trade and investment policies

Project financing can play an important role in stimulating trade and achieving environmentally sustainable development. The international finance community has begun to adopt provisions that include direct attention to sustainable use of natural resources, foster adoption of clean production and pollution prevention technologies, and are mindful of worker health and safety. This is particularly true with multinational companies and their suppliers that trade internationally.

More than 30 of the World's largest investment banks and multilateral facilities such as the Citigroup, Credit Suisse, World Bank, the International Finance Corporation and the U.S. Millennium Challenge Corporation screen their investments using a common set of guidelines commonly known as the "Equator Principles". Adherence to these principles means that investors and their clients will benchmark, document, and improve their environment and social performance. The principles describe required independent environmental and social review procedures and reporting guidelines, and prohibit lending for projects where the borrower will not commit to environmentally responsible construction and operation of the project. USAID missions can also use DCA, pooled financing, and other financing assistance activities in this way.

The respective roles of regulatory and trade agencies, industry and financial underwriters, and independent standard-setting and certification bodies are driving deep and irreversible changes in trade regimes. No longer satisfied with traditional or "one-off" environmental assessments conducted during project design, many multinational value chains now employ risk assessment and routine environmental audits to ensure conformance with market standards and compliance with applicable laws and conventions, and to minimize risk of environment-related liabilities. Environmental competitiveness requires regular management review, capturing and reporting costs and benefits, and punctual deployment of corrective actions. Policies that encourage this behavior in enterprises also promote good business practice and expanded participation in international trade.