



**NAVIGATING NEW  
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NEXUS OF TRADE AND  
CLIMATE CHANGE:  
IMPLICATIONS AND  
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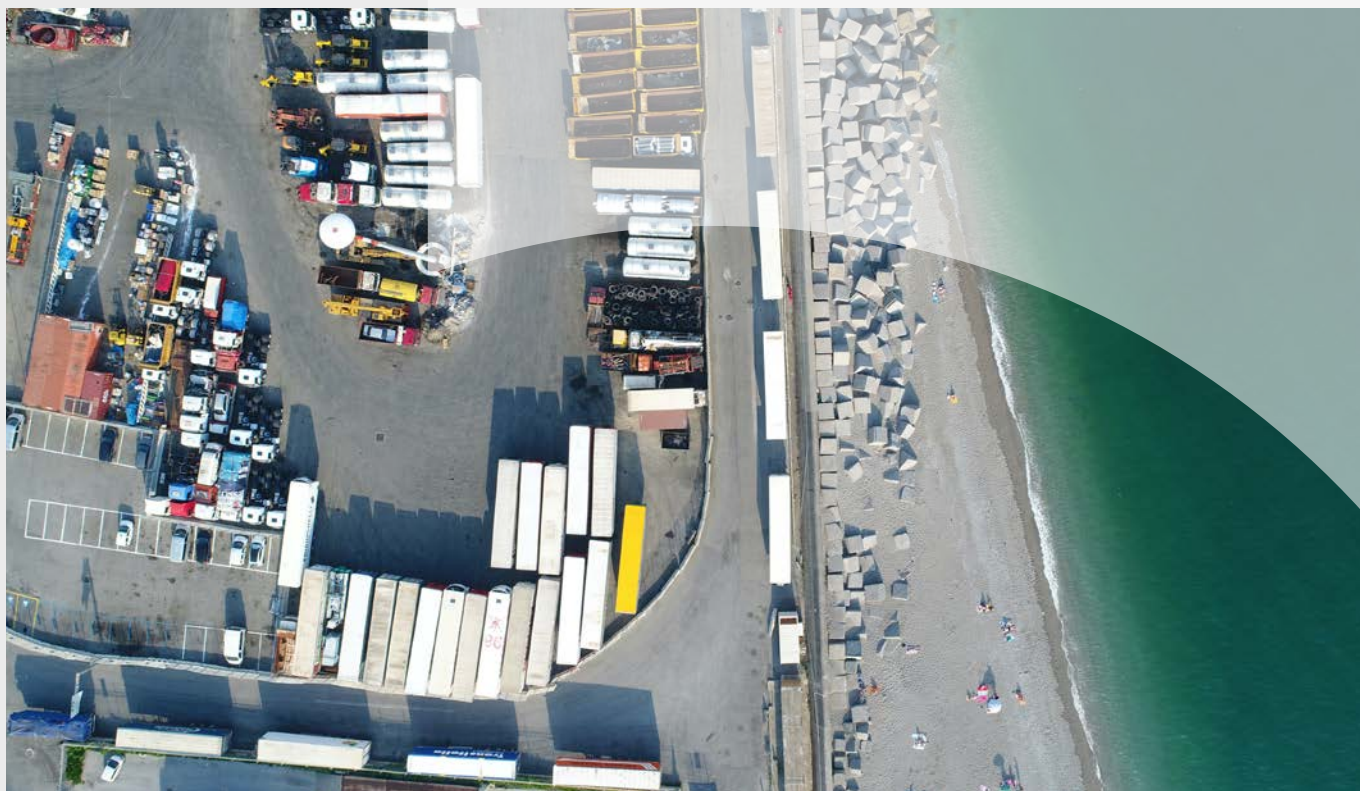
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# INTRODUCTION

The accelerating transition to a lower carbon economy, now well under way, is leading several of the developed country majors to introduce programmes and policies that amount to a significant departure from the trade policy playbook crafted during the era of hyperglobalisation. Although climate science is warning that we are still far from averting the threat of catastrophic climate change, there is much greater urgency and seriousness in parts of the developed world to drive a more decisive shift to lower carbon products and technologies. This is evident in efforts to give effect to ‘net zero’ commitments made in United Nations Framework Convention on Climate Change (UNFCCC) Conferences of the Parties (COPs). As part of these processes, two rather different measures with trade policy implications stand out – the European Union’s (EU) Carbon Border Adjustment Mechanism (CBAM) and the ‘green’ industries support sections of the United States’ Inflation Reduction Act (IRA). This paper will discuss some of the implications of these measures for developing countries and in particular for the efforts of African countries to address the long-recognised fundamental challenge of underdevelopment by reducing dependence on production and export of primary products through diversifying and moving to higher value-added production (industrialisation).

Trade liberalisation was one of the overriding and most important policy objectives promoted during the era of hyperglobalisation that began in the late 1980s. Along with privatisation, deregulation and adherence to prescribed macroeconomic policy ratios, the doctrine of neoliberalism that was at the heart of the then hegemonic Washington Consensus held that tariff reduction and removal was the indisputable pathway to integration in global value chains. This, in turn, was heralded as the royal road to prosperity available to all. Harvard economist Dani Rodrik characterised this doctrine as amounting to a reduction of development policy to trade liberalisation.<sup>1</sup> One of the mantras associated with this doctrine was that no other policy or programme could or should be ‘trade distorting’.

1 See, inter alia, Dani Rodrik, ‘The global governance of trade as if development really mattered’, report submitted to UNDP, July 2001, <https://digitallibrary.un.org>

In institutional practice, this doctrine underpinned the World Trade Organization's (WTO) de facto emergence as a 'super' multilateral organisation, progressively subsuming the mandates of other organisations (beginning with the World Intellectual Property Organization, WIPO, whose mandate was effectively subordinated to decisions of the WTO on Trade-Related Aspects of Intellectual Property Rights – TRIPS – issues). This occurred as a growing list of trade-related matters (from subsidies to localisation policies and technical standards) were all seen as needing to be 'disciplined' to make tariff concessions effective. Later, as the Doha Development Round stalled and developed countries began to pursue 'mega regionals' outside of the WTO (notably the Trans-Pacific Partnership and the never concluded Trans-Atlantic Trade and Investment Partnership), these so-called high-quality, twenty-first-century trade agreements included extensive commitments on a range of 'behind the border' regulatory matters – with the stated intention of ensuring 'regulatory neutrality' so that the ambitious trade liberalisation provided for in these agreements would not be 'diluted' by regulations on competition, investment and electronic commerce, among other things.

What now seems to be emerging is that this trend toward an ever more expansive agenda of trade liberalisation trumping all else is being halted and partially reversed as developed countries introduce 'protectionist' measures justified in the name of climate action. Of course, the trade liberalisation agenda was never absolute even for its most ardent proponents. Advanced industrialised countries pursued liberalisation more vigorously in industrial products (where they were more competitive, at least until the rise of China) than they did in agricultural products (where they were less competitive and fought to retain the right to deploy sizable subsidies and maintain significant tariff protection). This was hardly surprising. Heterodox economists and economic historians<sup>2</sup> have convincingly shown that the trade policy stances of today's advanced industrialised countries varied at different stages of their development and level of competitiveness in relation to their rivals. At an early stage of their industrialisation all of today's industrialised countries, without exception, nurtured, supported and indeed protected nascent industries, while overtures from competitors to open up their markets and adopt 'free trade' were rejected. Later, as they became more competitive and sought to increase exports of their now competitive products, the very same countries began promoting ideas of free trade, even to the point of denying others access to the very same policy tools they themselves used at an earlier stage of development – a phenomenon known as 'kicking away the ladder'.<sup>3</sup> Behind what some have termed the climate-justified 'new protectionism'<sup>4</sup> is the recovery of industrial policy by developed countries (led by the United States) in the midst of increasing competition and contestation over the mastery of low carbon products, technologies and 'solutions'. This follows similar competition and contestation over the 'big data' digital technologies of the so-called fourth industrial revolution. This competition/contestation has a number of dimensions. Immediately, it is taking place between companies and corporations over the development and marketing of lower carbon products and the growing imperative to demonstrate 'green credentials' in existing activities. This, however, is spilling over into increasing contestation between different countries and blocs in a world system shifting rapidly from the unipolar world order with its undisputed single hegemon that emerged from the Cold War and shaped the processes of hyperglobalisation to a world that is becoming more multipolar. More specifically, the rise of China as a major industrial power and competitor has been a major factor. China invested heavily in the development of both digital and low carbon products and technologies and as a result established an early lead in some areas. This has led to a growing identification by developed, western countries of the recovery and maintenance of mastery in these fields as a central objective not just of economic, but also of foreign and national security policy.

Unsurprisingly, the increasingly significant departures from both the erstwhile neoliberal playbook and even established trade rules have been unilateral. Since their objective is to secure or maintain a partisan advantage against actual or potential competitors, they are being implemented with little consideration of their potential impact on developing countries – with overtures then of the phenomenon of 'kicking away the ladder'.

While having these broad features in common, the two main 'climate-justified' protectionist measures adopted to date – CBAM and the IRA – are different in content with somewhat different potential implications for developing countries in general, and Africa in particular. The remainder of the paper will look in more detail at these measures before suggesting some of the elements of a possible response.

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2 See Ha Joon Chang, *Kicking away the ladder*, Anthem Press, 2002; Erik Reinart, *How rich countries got rich...and why poor countries stay poor*, Carrol and Graf, 2007.

3 The term was coined by nineteenth-century German economist Friedrich List, and used as the title of Ha Joon Chang's book, cited above.

4 See Avantika Goswami, 'A new order of trade', *Down to Earth*, 16–28 February 2023, [https://cdn.downtoearth.org.in/pdf/20230222-dte-story\\_green\\_manufacturing\\_war.pdf](https://cdn.downtoearth.org.in/pdf/20230222-dte-story_green_manufacturing_war.pdf).



## THE EUROPEAN UNION'S CBAM

The CBAM<sup>5</sup> is ostensibly a measure to prevent 'carbon leakage' through trade by pegging the emissions content of imported products to levels set for domestic equivalents. Goods produced within the EU are subject to the European Trading System (ETS) – a cap-and-trade system that caps the total amount of overall emissions, lowers that cap over time, and sells the right to emit carbon at an increasing price. The CBAM aims to mirror and complement the ETS by creating what purports to be a measure intended to level the playing field between EU producers and exporters from third countries. In particular, once fully operational, EU importers will be required to buy CBAM certificates to cover the price difference between the carbon price that is paid in the country of production and the price of carbon allowances in the EU ETS. The carbon price of imports will be based on actual emissions as declared by importers where feasible. However, when actual emissions cannot be adequately determined by the authorised declarant, default values will be applied.

The CBAM system will be introduced in stages. It will begin in October 2023 with a requirement that importers of, initially, aluminium, cement, electricity, fertilisers, iron and steel report in detail on the carbon emissions involved in their production. This will be followed in 2026 with a requirement that CBAM certificates are purchased in respect of all imports of products in the designated list.

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<sup>5</sup> For accessible summaries, see World Economic Forum, 'CBAM: What you need to know about the new EU decarbonization incentive', December 2022, <https://www.weforum.org/agenda/2022/12/cbam-the-new-eu-decarbonization-incentive-and-what-you-need-to-know/>; African Climate Foundation, 'Implications for African countries of a Carbon Border Adjustment Mechanism in the EU', May 2023, [https://africanclimatefoundation.org/news\\_and\\_analysis/implications-for-african-countries-of-a-carbon-border-adjustment-mechanism-in-africa/](https://africanclimatefoundation.org/news_and_analysis/implications-for-african-countries-of-a-carbon-border-adjustment-mechanism-in-africa/); Deloitte, 'EU Carbon Border Adjustment Mechanism', <https://www2.deloitte.com/nl/nl/pages/tax/articles/eu-carbon-border-adjustment-mechanism-cbam.html>.

While purchase of CBAM certificates is not strictly a tariff, it will as a financial levy on imports have a similar effect. Moreover, as it depends both on the extent to which the carbon content of the import exceeds the norm established in the EU cap-and-trade system and the ETS auction price (itself partly determined by where the cap is set), the exact incidence cannot be predicted with any certainty at this time. Nor can the rate and pace at which the system is expanded beyond imports in the initial list (which is clearly seen as eventually covering all imports). Proposals to exclude Least Developed Countries (LDCs) or apply the CBAM differentially to developing countries were rejected by the European Parliament, meaning the arrangement will apply to developed, developing and LDC country products alike.<sup>6</sup>

A study commissioned by the African Climate Foundation measured the potential impact based on different scenarios for ETS carbon price per tonne and product coverage. It found that even in the ‘lightest’ scenario with the most limited impact, ‘Africa’s economy will be negatively affected by the CBAM with exports to the EU declining by 4% in total, that Africa will be worse affected than any of the other major economies analysed...that even at €40 per tonne, the CBAM will raise EU import tariff revenue substantially, but have little impact on global CO<sub>2</sub> emissions.’ With a higher carbon price and more extensive product coverage, Africa’s exports to the EU would decrease by 5.75%, ‘with Africa’s GDP falling by 1.12% (almost twice the initial scenario of a partial CBAM and a lower carbon cost)’.<sup>7</sup> With the impact unevenly distributed among individual countries, some would be affected by more than these averages. These include Mozambique (an LDC), one of whose most important exports is smelted aluminium. According to the Center for Global Development, the CBAM levies on its aluminium exports could reduce its GDP by 1.5%.<sup>8</sup>

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6 See African Climate Foundation, *op. cit.* p. 7.

7 *Ibid.*, pp. 13 and 23.

8 Cited in World Economic Forum, *op. cit.*





## THE UNITED STATES' IRA

The IRA of 2022<sup>9</sup> is a US federal law with several sections and chapters dealing with subjects ranging from measures to combat prescription drug price gouging to the imposition of a minimum tax rate for large companies (to combat tax avoidance) and to strengthen the Internal Revenue Service.

It also includes, more importantly for present purposes, a section authorising US\$391 billion in federal funding to support climate-related measures, including incentives for manufacturers of clean energy equipment and new energy vehicles. A tax incentive is also provided for consumers who buy electric vehicles with prescribed percentages of components manufactured in the USA.

To put this into context, the IRA climate-related funding is almost equivalent to the GDP of Africa's largest economies – Nigeria, Egypt or South Africa – and more than the annual expenditure proposed under the next multi-year Farm Bill (around \$143 billion).<sup>10</sup> This points both to the 'deep pockets' of the US and the scale of state support for low carbon industries envisaged by the US administration.

The tax credit for consumers buying electric vehicles with locally manufactured components appears at face value to be incompatible with the WTO's Trade Related Investment Measures (TRIMs), whose 'illustrative list' of prohibited measures includes imposing such 'local content' requirements on private sector transactions. Following a threat by the EU to mount a challenge in the WTO, the two sides agreed to 'immediately begin negotiations on a targeted critical minerals agreement' to ensure that minerals extracted or processed in the EU would count for clean vehicle tax credits under the IRA.<sup>11</sup> This would amount to an unprecedented arrangement in which localisation requirements implemented by one WTO member would be extended to cover inputs from selected other WTO members as well.

The EU also announced on its own Green Deal Industrial Plan.<sup>12</sup> This includes an accelerated allocation of €225 billion for loans and €20 billion in grants to support EU green tech companies. The EU further signalled its intention to establish a European Sovereignty Fund, to table a Net Zero Industry Act prescribing targets to be reached by 2030, and to develop internal rules as well as work with allies to counter what it considers unfair subsidies by others.

9 For summaries and source of figures cited, see Goswami, op. cit.; White House, 'Inflation Reduction Act Guidebook', <https://www.whitehouse.gov/cleanenergy/inflation-reduction-act-guidebook/>; 'Inflation Reduction Act of 2022', [https://en.wikipedia.org/wiki/Inflation\\_Reduction\\_Act](https://en.wikipedia.org/wiki/Inflation_Reduction_Act).

10 Figures from US Department of Agriculture, *FY 2022 Budget Summary*.

11 'United States, EU agree to start talks on critical minerals amid trade tensions', 11 March 2023, <https://www.reuters.com>.

12 Reuters, 'Factbox: What's in the EU's green industrial plan?', 16 March 2023, <https://www.reuters.com/business/sustainable-business/whats-eus-green-industrial-plan-2023-03-16/>.



## ASSESSMENT AND A WAY FORWARD FOR AFRICA

Both the CBAM and the IRA are indications of the seriousness with which powerful industrialised countries are approaching the development and roll out of lower carbon products and technologies. In the face of a perceived or actual lag behind China, this has now led to a partial but significant unilateral shift from the ‘free trade trumps all else’ mantra they themselves promoted during the era of hyperglobalisation. The EU and the US (the authors of CBAM and the IRA, respectively) are in competition with each other. More significantly, both are competing with China, which has been an early mover and consequently has a technological lead in at least some areas. This competition has now morphed into inter-bloc contestation with a growing foreign and security policy dimension.

The CBAM and the IRA both represent departures from the spirit, and likely too the letter, of several WTO rules and provisions. The fact that these measures have been implanted unilaterally means that little consideration has been given to their impact on developing countries, which have also not been consulted in designing them.

Addressing Africa’s deep-seated developmental challenges has long been identified as depending on reducing its dependence on production and export of primary products and moving to higher value- added production (through industrialising). This applies equally in the current accelerating transition to a lower carbon economy. Thus, while opportunities have been identified for Africa to supply mineral products that will be used in green technologies or to use its abundant sunlight as a potential competitive advantage in producing green hydrogen, it is also important that the continent deploys active industrial policy to promote higher value-added opportunities. These exist across existing manufacturing. For example, the shift to sustainable fibres and relative nearshoring in clothing and textile value chains creates a historic opportunity for building stronger sustainable African textile value chains.



But there are also opportunities that must be seized for Africa to produce value-added products in new green technology areas. These would include production of wind tower and solar energy components, fuel cells and fuel-cell-driven public transport and underground mining vehicles as well as renewable energy provision, particularly in areas not connected to existing electricity grids. The roll out of the African Continental Free Trade Area (AfCFTA) is also increasingly recognised as potentially contributing to the creation of regional value chains by providing a larger continental market capable of underpinning deeper industrialisation than would be possible in either national states or even regional economic communities.

At the same time, the existing multilateral trading system has long been seen as problematic for African development. It has delivered uneven and unequal outcomes, subordinated issues of importance for the continent's development (like agriculture) to the priorities and whims of the developed world, seen the principles of Special and Differential Treatment (fundamental to the bargain leading many developing countries to join) inconsistently applied and under increasing challenge from richer countries, while many existing and proposed rules have been recognised as constraining the policy space needed to support development.

The above, in my view, needs to shape an African approach to the issues raised by the CBAM and the IRA. The CBAM is a direct barrier to market access, with the same effect as a tariff on products subject to it. Meeting the same carbon standards as those of EU-based companies will require large additional investments and this alone would amount to pushing African countries, including LDCs, way beyond the nationally determined contributions they have tabled at UNFCCC COPs (most of which, in any case, were conditional on receipt of as yet non-existent climate funding). It is thus a measure that undermines the principles of both 'less than full reciprocity' and 'common but differentiated responsibility', supposed to underpin multilateral trade rules and climate-related commitments respectively.

Moreover, research cited earlier points to huge disproportionality in its application to a continent that is among the least responsible for greenhouse gas emissions, but among those most effected by climate change. The gains in emissions reduction are small, compared to the loss of export earnings and incomes in any of the scenarios. As such, CBAM is a measure that, in my view, needs to be rejected, opposed and challenged in any way or forum possible. Developing a strategy for this is doubly urgent in view of its propensity to be replicated in several other jurisdictions.

The IRA and similar measures in other developed countries, however, in my view pose a different kind of challenge. Through the IRA, the US is deploying industrial policy on a scale and in a way that it has not done in the recent past. Some of its departures (like the localisation requirement on its tax credits and the extension of these to selected third parties) are in violation of the spirit, if not the letter, of TRIMs. The problem for the developing world is that this is being done unilaterally, without any suggestion that it is a generalised pathway that others could or should follow.

Trying to contain this unilateralism via WTO challenges or rules changes would not be in Africa's interest, in my view. A ruling or new 'transparency' requirement, even if it were accepted and implemented by the USA (which looks in no mood to do so), would set precedents of general application that would almost certainly apply more broadly and probably end up further reducing our own policy space. Moreover, while the immediate target in the politico-security contestation underpinning this move is China, we should not forget that the broader objective, outlined in several US policy statements, is to contain any other developing country or 'emerging economy' from contesting US or western domination in key strategic sectors.

Rather, we should, in my view, use this shift away from the erstwhile narrative of 'free trade trumps all else' to intensify calls for a Global Green New Deal to guide the transition to a lower carbon economy and also shape a new inclusive and developmental form of multilateralism. It is worth recalling that while one of the first calls for a Global Green New Deal (that by the United Nations Environment Programme in 2009<sup>13</sup>) focused on quantitative targets for public investments in green infrastructure, coupled with resource transfers to the developing world,

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13 United Nations Environment Programme, 'Global Green New Deal: Policy Brief March 2009', <https://www.unep.org/resources/report/global-green-new-deal-policy-brief-march-2009>.

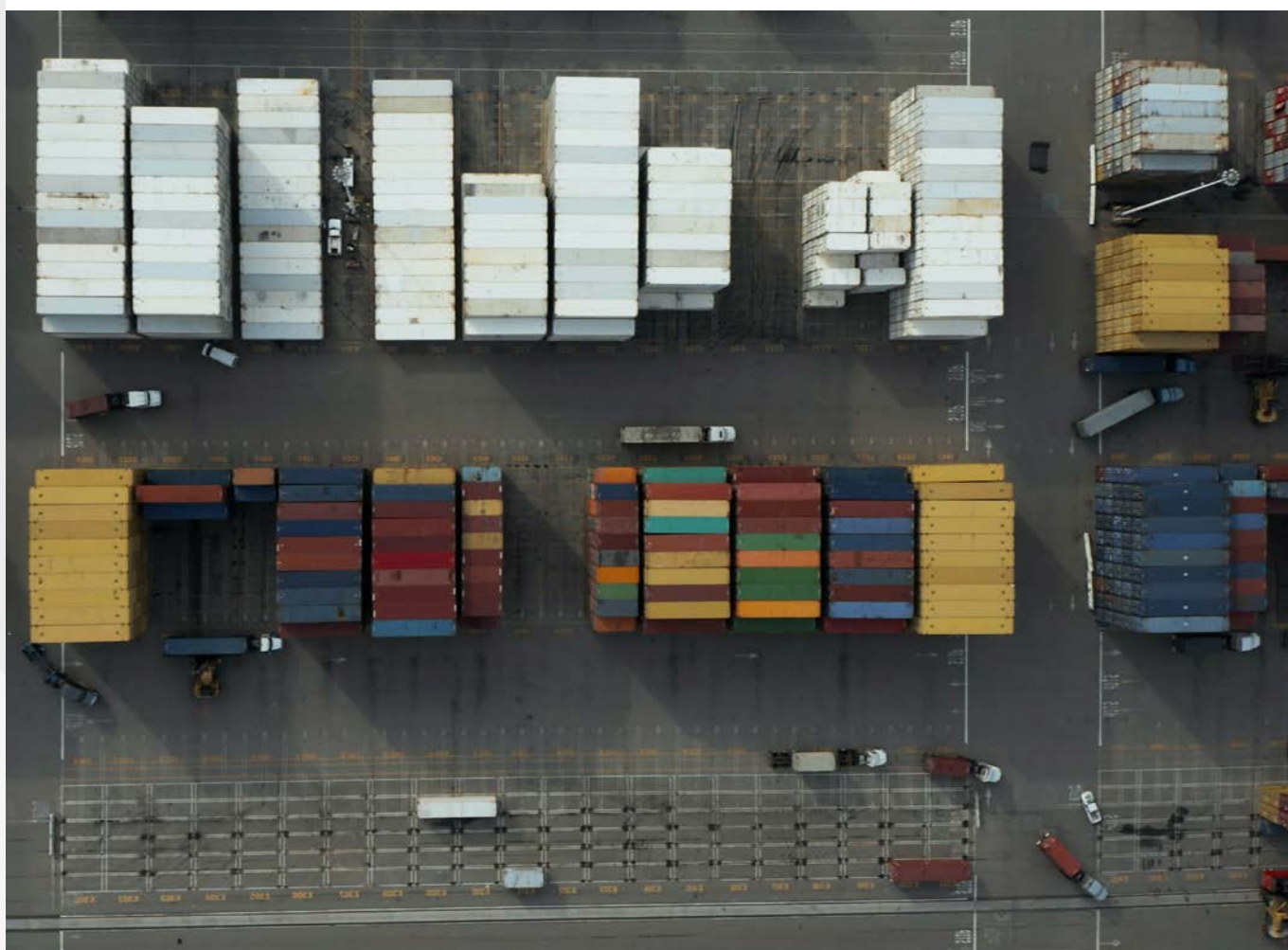
that by the United Nations Conference on Trade and Development (UNCTAD),<sup>14</sup> which followed a reality where bank bailouts dwarfed any kind of green projects, called for significant transformative policy shifts to underpin an inclusive and developmental green transition: a move away from austerity; strong caring public investment programmes; a new global financial architecture to release more funding for development; a revisiting of global trade and other rules to enlarge policy space, among other things.

As step towards such an eventual end goal, the IRA suggests the immediate urgent pursuit of two specific policy goals. The first would be to cite the USA's overt use of localisation to immediately insist on developing countries' right to implement local content requirements in ways adapted to their own realities and requirements. These should be designed carefully as part of broader industrial policies, and applied not just at national level, but also increasingly as part of programmes to build regional value chains as envisaged within the AfCFTA.

The other area susceptible to short-term action and campaigning is that of technology transfer. We need to campaign for recognition that the transition to a lower carbon economy is part of a (not yet sufficient) response to a global emergency – the threat of catastrophic climate change. Green technologies need, accordingly, to gain recognition as needing to be produced and developed in multiple locations, with a status more akin to global public goods than products providing opportunities for the reaping of huge monopoly profits buttressed by intellectual property regimes that have moved way beyond providing rewards for innovation. This would suggest, specifically, a campaign for a change in TRIPS rules, similar to that launched by India and South Africa around Covid vaccines, but targeting more significant and substantial outcomes than achieved in that campaign.

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14 United Nations Conference on Trade and Development, *Trade and Development Report 2017*, pp. xiii–xiv, 152–164.



# ACRONYMS

<b>AfCFTA</b>	African Continental Free Trade Area
<b>CBAM</b>	Carbon Border Adjustment Mechanism
<b>COP</b>	Conference of the Parties
<b>ETS</b>	European Trading System
<b>EU</b>	European Union
<b>GDP</b>	Gross Domestic Product
<b>IRA</b>	Inflation Reduction Act (United States)
<b>LDC</b>	Least Developed Country
<b>TRIMs</b>	Trade Related Investment Measures
<b>TRIPS</b>	Trade-Related Aspects of Intellectual Property Rights
<b>UNCTAD</b>	United Nations Conference on Trade and Development
<b>UNDP</b>	United Nations Development Programme
<b>UNFCCC</b>	United Nations Framework Convention on Climate Change
<b>US</b>	United States
<b>WIPO</b>	World Intellectual Property Organization
<b>WTO</b>	World Trade Organization



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