How to cooperate when the United States, EU and China have very different climate and trade policies

Chad P. Bown (PIIE) & Kimberly Clausing (PIIE & UCLA Law)
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The macroeconomic implications of climate action
Roadmap

• Starting Point
• Climate Change Policy in China, the United States, and the European Union
• Policy Spillovers and Frictions
• Unilateral and Bilateral Policy Evolution in Wake of IRA
• Lessons from the WTO
• Steps Forward for the EU, China, and the United States
Starting Point

- US, China, and EU: 60% of world economy and nearly half of world emissions
- Their climate policies are not aligned… on the contrary, divergent policies generate substantial frictions
- Easing trilateral frictions can help build a framework to facilitate climate change mitigation while reducing collateral damage to trading system
- It won’t be easy.

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>Share of Global Greenhouse Gas Emissions (%) in 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>China</td>
<td>26.4</td>
</tr>
<tr>
<td>2</td>
<td>United States</td>
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</tr>
<tr>
<td>3</td>
<td>India</td>
<td>7.1</td>
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<tr>
<td>4</td>
<td>European Union</td>
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<td>Russia</td>
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</tr>
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<td>Japan</td>
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</tr>
<tr>
<td>7</td>
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<td>20</td>
<td>Thailand</td>
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</table>
Climate Change Policy in China, the United States, and the European Union

- Some of the same tools are used, but the devil is in the details.

- Subsidies vary in scale, flexibility, and mechanisms.

- Pricing is only subnational in the United States and limited in China.
Policy Spillovers

1. Emissions Externalities (+ ambitious policy helps others)
2. Tradable Industry Competitiveness Spillovers (+/- if cost-imposing/reducing)
3. Learning/Scale Spillovers (+ ambitious policy helps others)
4. Upstream effects (depends on country, time period)
5. Downstream effects (+/-)
Unilateral and Bilateral Policy Evolution Post IRA

EU Response: some critiques, some possible policy shifts?

US Response: implementation decisions, coming political battles?

US/EU: mini-agreements; green steel deal? other tools?

US/China: conflicts; is this de-risking or de-coupling?

EU/China: pragmatism prevails (so far); is this de-risking?
Example of US implementation decision: IRA’s “leasing” work around for EVs may help.

Steps Forward, Focusing on the EU, China, and the United States

First, why these jurisdictions?

Key Principles:
1. Climate change paramount priority
2. Policy and system diversity inevitable => frictions inevitable
3. Gains from trade large and rules-based system of high value today
4. More policy alignment would be very helpful => nudge world in that direction

⇒ Return to reciprocity of GATT, driven by a common external threat (climate change)
⇒ Move to a (more) cooperative equilibrium
Lessons from the WTO and New Guardrails (1)

Current Subsidies Rules
- Prohibited (domestic content, export) v. Actionable (others)
- Role of remedies
- Current risks: possible IRA impacts, not suited to NMEs

Reforms
- Acknowledge role of subsidies but seek to minimize spillovers
- Make responses to subsidies legitimate and routine (w/ evidence, sunsets)
- Reject and dismantle national content provisions
Lessons from the WTO and New Guardrails (2)

Current Border Measure Rules

• Market Access Commitments, MFN
• National Treatment and Non-discrimination
• Current risks: EU CBAM may be challenged

Reforms

• Greenlight nondiscriminatory CBAMs
• Make explicit link between CBAMs and equivalent domestic cost-imposing policies
• Move toward greater policy alignment
Lessons from the WTO and New Guardrails (3)

Current Export Restriction Rules

- Limits on use of quantity restrictions (is the good “essential”?)
- No limits on equivalent export taxes (except China per WTO accession)
- Current risks: national security; trade weaponization due to monopsony power

Reforms

- Commit to no export restrictions on climate-related goods
- In turn, this helps limit impulse toward subsidies and discriminatory policy
Role of Dispute Settlement

Current Issues

- Dysfunctional (at present)
- *Slow*, limited (in general)
- Designed to prevent trade wars

Handling prior issues is a prerequisite to reform.

Cannot be done à la carte: All three guardrail issues need to be tackled jointly, as policies are interrelated.
Concluding Thoughts and Questions

• What about the rest of the world?

• Greater policy alignment makes this so much easier; how do we encourage that?

• Time is of the essence; how to best push forward climate cooperation?
  
  o Can we learn from the international tax agreement?

  o Are there ways to make more effective carrots? Sticks?

  o What are the best forums for action?
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Chad P. Bown
cbown@piie.com

Kimberly Clausing
clausing@law.ucla.edu