

Empirical Project 5: Trade and the Environment

A big concern for many anti-globalization forces is the potentially harmful effects of trade on the environment. A related concern for firms in developed countries is their loss in competitiveness because they face stricter regulations. This short article in the Financial Times in Nov. 24, 2006 (p. 1) touches on some of these issues:

Europe is damaging its competitiveness by moving faster than the rest of the world to tackle climate change, the European Union's industry commissioner has warned.

In a letter seen by the Financial Times, Gunter Verheugen says: "We have to recognise that . . . our environmental leadership could significantly undermine the international competitiveness of part of Europe's energy-intensive industries and worsen global environmental performance by redirecting production to parts of the world with lower environmental standards."

His comments are understood to be aimed in particular at the economic threat from China, India and other Asian nations.

The industry commissioner wrote to Jose Manuel Barroso, president of the European Commission, calling for special exemptions for such sectors to state aid rules and backing the introduction of a levy on imports from developed countries that have yet to implement the Kyoto treaty, which has been floated in Brussels.

However, he also believes that European business could benefit if the market-friendly emissions trading scheme is extended to cars and airlines by encouraging it to invest in new technology and reducing emissions in the developing world.

His distress call reflects the increasing priority Mr Barroso is putting on green issues since the publication of the Stern report by the UK and the US debate sparked by Al Gore, the former vice-president. Brussels is set next week to reject several of its members' emissions trading plans for the 2008-12 period as too weak.

ASSIGNMENT: Address the following points with data analysis, media quotes, and /or other evidence to back up your answers. As with all of these assignments, make sure to appropriately document your sources of information.

A) Explain how stricter environmental regulations can be a source of comparative disadvantage for a country. Which types of products would it impact the most. Relate this to Ricardian trade theory we have discussed in class.

B) On the flip side, environmental regulations may spur a country's firms to develop new products and technologies that consumers will demand in the future. Explain how this would affect comparative advantage and trade of goods.

C) There are other ways in which globalization can affect trade and the environment. What is the "Pollution Haven Hypothesis"? (A search on Google will pull up plenty of references to this. If this hypothesis is correct, will trade benefit or harm the environment? Does the evidence to date support this hypothesis?

D) What is the environmental Kuznets curve and what does this have to say about the relationship

between a country's income and pollution? Relate this to trade which theoretically raises country's overall welfare/income.

E) Are there other ways in which trade can affect the environment? Think about deforestation, but also think about less-developed countries access to inexpensive technologies that control pollution. Can we say that trade between countries leads to greater environmental damage on net?

RESTRICTIONS: Can have a maximum of three students handing in a joint project. Report cannot be longer than 4 pages of text (double-spaced) with an extra page allowed for charts and graphs.