

# PERSPECTIVE

RESEARCHERS AT ISEAS – YUSOF ISHAK INSTITUTE ANALYSE CURRENT EVENTS

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## **Trade and Environmental Disputes May Persist Despite Promising Leaders' Summit on Climate**

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The recent Leaders' Summit on Climate Change, organised by the Biden Administration, signalled the US return to the Paris Agreement after years of neglect. In this picture, US President Joe Biden delivers remarks during Day 2 of the virtual Leaders' Summit on Climate at the East Room of the White House on 23 April 2021 in Washington. Photo: Anna Moneymaker - Pool/Getty Images/AFP POOL/GETTY IMAGES NORTH AMERICA/Getty Images via AFP.

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**EXECUTIVE SUMMARY**

- The recent Leaders' Summit on Climate Change convened by the Biden Administration signalled the US' return and major powers' unwavering commitment to tackling climate change.
- Four of ten ASEAN leaders -- Indonesia, Singapore, The Philippines, and Vietnam — were invited to the summit and announced their newest goals and initiatives, which include renewable energy acceleration, decarbonisation practices, and pathways to net-zero emissions.
- One key emphasis shared by several ASEAN leaders' speeches is the principle of Common but Differentiated Responsibilities and Respective Capabilities (CBDR-RC) which recognises differentiated levels of economic development between states in response to climate change.
- Some ASEAN thought-leaders have recently expressed a growing concern about the Carbon Border Adjustment Mechanism (CBAM), introduced by the European Union (EU), functioning as trade protectionism or discrimination which could threaten the exports of developing countries.
- The themes and issues raised by some ASEAN leaders at the summit are a harbinger of climate negotiations to come. Can developed and developing countries find a balance between heightened climate ambition and the spirit of CBDR-RC?

**THE LEADERS' SUMMIT ON CLIMATE: AN INSIGHT**

The recent Leaders' Summit on Climate Change, organised by the Biden Administration, signalled the US' return to the Paris Agreement after years of neglect. The US and 40 world leaders restated their commitment and highlighted their countries' efforts to limit global warming to 1.5-degree Celsius, and most importantly, demanded more concrete actions from the United Nations Climate Change Conference (COP 26) to be held in November 2021 in Glasgow.

To observers, the summit showed a glimmer of hope that two major powers, the United States and China — despite their belligerent relationship in trade and strategic affairs — are approaching climate challenges with the same urgency. As major carbon emitters, both countries agreed to ramp up efforts to combat rising temperatures and strengthen international institutions in meeting this challenge.

In his opening remarks, President Biden spoke about economic opportunities from climate actions which include job creation, clean technology and infrastructure renewal. The US' climate plans also call for decarbonising the US power sector by 2035 and achieving net-zero emissions by 2050.

The Biden Administration recently introduced a US\$2 trillion plan to overhaul the country's infrastructure and boost the US economy's competitiveness. The plan emphasises the need to accelerate renewable energy adoption, provide ubiquitous charging stations for electric cars, and invest in public transportation. While Republicans and Democrats are still deeply divided on the matter, Biden's pragmatic and economically opportunistic approach to climate change exhibits a strategic bid to win bipartisan support.

President Xi Jinping, in much the same way, has reiterated China's commitment to green development. China has vowed a technological revolution, industrial transformation, and innovation to achieve carbon neutrality before 2060 — the country is to begin phasing down coal in the period of 2026-2030. Unlike the US, China has in recent years been looking to build a global coalition. On several occasions, Chinese leaders pledged their commitment to green initiatives to benefit all Belt and Road (BRI) partner countries. Chinese investment has brought capacity-building opportunities and technology transfers which are much needed for sustainable development in these developing countries.

Similarly, other major economies are adopting the premise of green transformation to revive their economies after the Covid-19 crisis. The European Green deal, an ambitious plan to make Europe carbon neutral by 2050, is one example. President Macron of France has suggested an overhaul of the global financial system, bringing together sovereign funds, asset managers, and private equity firms to integrate climate risks in the investment calculation. Likewise, Chancellor Merkel of Germany has reiterated the need to establish a robust market system to stymie carbon emissions. As one of the global leaders on climate action, Germany has been fairly successful in implementing carbon pricing. Early this year, it introduced a €25 (US\$30) per ton carbon tax on the transport and heating sectors.<sup>1</sup>

**CONTENTIOUS ISSUES**

Four of ten ASEAN member states—Indonesia, Singapore, the Philippines, and Vietnam—were invited to the summit, where they announced their newest goals and initiatives. President Joko Widodo announced that Indonesia is piloting a net zero emissions development project called the Indonesia Green Industrial Park, and that it will rehabilitate 620,000 hectares of mangroves up to 2024. Philippine Secretary of Finance, Carlos G. Dominguez III, shared that The Philippines' first NDC had just been submitted. Prime Minister Lee Hsien Loong announced the Singapore Green Plan 2030, a living plan with climate and sustainability targets across sectors such as energy, green finance, transport, waste and adaptation. He also shared that Singapore will quadruple its solar energy production by 2025. President Nguyen Xuan Phuc highlighted new targets of increasing the share of renewables in the primary energy supply by 20% by 2030 and 30% by 2045, and reducing greenhouse gas intensity by nearly 15% and methane emissions from agriculture by 10%.

One key emphasis shared by several ASEAN leaders' speeches is the principle of Common but Differentiated Responsibilities and Respective Capabilities (CBDR-RC), which acknowledges that the non-polluters of yesterday should not bear the cost of climate consequences today. Often brought up by developing countries to call for assistance in achieving their climate goals, this sentiment was echoed at the summit by Indonesia, The Philippines and Vietnam, as well as China.

In particular, President Xi Jinping used this principle to discourage developed countries from enacting green trade barriers, and instead called for them to support developing countries in finance, technology and capacity building to help transition to low carbon-development. President Joko Widodo approached the same topic from the angle of multilateralism, warning that applying trade barriers under the pretext of environmental issues would undermine a real global partnership. These arguments highlight a growing concern about green trade barriers threatening exports from developing countries where environmental regulations may be less stringent, and are perceived as trade protectionism by developed countries.

In March 2021, the European Parliament backed a Carbon Border Adjustment Mechanism (CBAM) proposal, which, if implemented, would impose a carbon price on certain carbon-intensive imports into the European Union (EU), including cement, steel, aluminium, oil refining, paper, glass, chemicals, and fertilisers, whether embedded in intermediate or final products.<sup>2</sup> The CBAM is applied to extend the geographical reach of EU's carbon price in order to more accurately reflect the carbon content of imports.<sup>3</sup> This mechanism aims to mitigate longstanding concerns about carbon leakage or the relocation of emissions from the EU to non-EU countries due to the high carbon price imposed within the EU. Without such a mechanism, a reduction in overall global emission is impossible to achieve.

Some critical points have been emerging against the CBAM proposal, however, chief of which being the unfair impact it will have on developing countries' exports. If such a law is imposed to all imports currently covered by the EU's Emission Trading System, up to US\$16 billion of exports from developing country to the EU could face an additional charge, thus making them less competitive in the EU market.<sup>4</sup> This could undermine the principle of CBDR-RC embraced by the Paris Agreement that forms the basis of agreement that

developing countries should not share the same burden as those of the rich. Under such a principle, the global community has acknowledged that rich countries must bear the cost of climate change, as they have historically contributed a larger share of carbon emissions.

Further, there is concern about the technical aspects of the carbon tax on imported goods. Currently, the EU favours limited implementation on some carbon-intensive goods. However, drawing distinctions between targeted and non-targeted sectors is extremely challenging since the supply chain of goods production has now become highly complex. Companies tend to object to disclosing location details of their supply chains, often considering these to be trade secrets.<sup>5</sup> Companies could also re-route their products from countries that impose carbon tariffs over to unregulated markets.<sup>6</sup> Calculating the total carbon content of a certain good will also be a huge challenge. For instance, a car might be made of components from many countries with different climate and energy policies.<sup>7</sup> To be sure, more robust rule of origins control in a Free Trade Agreement (FTA) would help importers determine the country of origin and carbon content of a product.

Likewise, the implementation of the CBAM is politically costly for the EU. Some countries have raised concerns over the CBAM to the World Trade Organisation (WTO), particularly on how the EU may use the mechanism as a revenue raising tool and to favour their domestic resources rather than as a means of addressing climate change.<sup>8</sup>

## **WHERE DOES ASEAN STAND?**

Generally, the EU's CBAM is viewed by its global counterparts as a protectionist and unilateral approach to trade and environmental protection. EU officials have however frequently affirmed that such an approach is necessary and that the absence of climate actions by other countries could derail the decarbonisation progress made so far by the EU.

As the third largest trading partner and one of the largest exporters of machinery and transport equipment, agricultural products, and textile and clothing to the EU, ASEAN is generally not expected to favour such a mechanism. Yet, a recent survey report on the Perception of the Planned EU Carbon Border Adjustment Mechanism in Asia Pacific from Konrad Adenauer Stiftung captures nuanced perceptions among three ASEAN member states thought-leaders; Indonesia, Singapore, and Thailand.<sup>9</sup>

The survey report highlights that Indonesia, for instance, fears that the CBAM would damage its palm oil sector as the European Commission labels palm oil as high-risk commodity based on the indirect land use changes that result from its production. On the other hand, because Indonesia has not yet established its carbon pricing mechanism, the CBAM could be a trigger for Indonesia to adopt more ambitious climate policies. Experts also suggest that such a mechanism could become acceptable to Jakarta if the revenue generated from the CBAM is used to help Indonesia develop its decarbonisation pathway.

It should be noted though, that smoother environment-related trading interactions are possible. Experts cite the case of EU-Indonesia cooperation on certified timber. The EU, acknowledging Indonesia's particular challenges, provides assistance in capacity building and developing monitoring systems for its timber exports. This allows Indonesia to adhere to the EU's regulations and upgrade its own national timber legality assurance system. In this case, close understanding and support not only help avoid disputes, but also assist

Indonesia in improving the robustness of its own environmental framework. Experts thus recommend a similar approach for implementing the CBAM and other environmental trade mechanisms that still manages to maintain good trade relations and empower Indonesia to heighten its climate ambitions.

Thailand, despite concerns over the technical aspects of the implementation and the potential disadvantage these hold for developing countries, views the CBAM as a positive step in mitigating change climate impact. The country is in the process of developing its compulsory emissions trading scheme, and the CBAM could in that context encourage businesses to enhance their decarbonisation efforts and meet the country's climate pledges.

Singapore, meanwhile, expresses little concern about the CBAM as long as it complies with international rules and agreements. Singaporean experts suggest that the EU could start with small steps, for instance, only taxing heavy polluting industries before gradually moving towards other industries.

Indonesia and Malaysia – two of the most vocal opponents of the CBAM in ASEAN – recently protested against the EU's 2018 decision to ban palm oil imports for biofuel claiming how the industry contributes to deforestation, peatland degradation and resulting emissions. The Indonesian government claimed that it was a protectionist move to favour European rapeseed.<sup>10</sup> Both initiated WTO dispute complaints against the EU in 2019 and 2021 respectively, claiming that the EU's measures violated international trade agreements. The two cases are being heard, even as the EU and Indonesia continue to negotiate a free trade agreement. Similarly, at the second Seoul Summit of Partnering with Green Growth and the Global Goals 2030, Prime Minister Hun Sen of Cambodia called for a commitment to globalisation through multilateralism and international trade openness as a means for strengthening climate actions.<sup>11</sup>

Earlier this year, ASEAN and the EU initiated the first joint group meeting on palm oil.<sup>12</sup> Indonesia's Foreign Affairs Deputy Minister, Mahendra Siregar asserted Indonesia's willingness to improve sustainability practices in the palm oil industry, citing Indonesia's moratorium on new logging and plantation permits which successfully dwindled deforestation by 75% within the 2019-2020 period. At the same time, Indonesia demanded a fairer and transparent assessment from the EU.<sup>13</sup> Other vegetable oils such as rapeseed and soya plantations cultivated in the EU also contribute to pollution on soils, rivers and seas due to the use of pesticide. Mahendra also noted that another ASEAN country, The Philippines, had also expressed concerns about coconut oil being increasingly rejected by the EU market. These environmental trade regulations and disputes are likely to be a source of climate conundrum of the future.

## **CONCLUSION**

The issues raised by leaders at the Summit are a harbinger of climate negotiations to come. Whether developed and developing countries can find a balance between heightened climate ambition and the spirit of CBDR-RC bears monitoring, especially for developing Southeast Asian countries that are vulnerable to environmental trade regulations.

At COP26, the world will observe the US' return to its leadership role in international climate negotiations, the effects of net-zero commitments from major economies, and a new

urgency for a green recovery from the COVID-19 pandemic. Much has changed since 2019, while the clock keeps ticking for the environment.

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<sup>1</sup> DW, “Merkel Pushes for Carbon Pricing ‘worldwide’ at Final Climate Conference,” *DW.COM*, May 6, 2021, <https://www.dw.com/en/merkel-pushes-for-carbon-pricing-worldwide-at-final-climate-conference/a-57451959>.

<sup>2</sup> European Parliament, “Towards a WTO-Compatible EU Carbon Border Adjustment Mechanism,” 02 2021, [https://www.europarl.europa.eu/doceo/document/A-9-2021-0019\\_EN.html](https://www.europarl.europa.eu/doceo/document/A-9-2021-0019_EN.html).

<sup>3</sup> M. Mehling and R. Ritz, “Going beyond Default Intensities in an EU Carbon Border Adjustment Mechanism,” *Cambridge Working Papers in Economics*, Cambridge Working Papers in Economics (Faculty of Economics, University of Cambridge, September 16, 2020), <https://ideas.repec.org/p/cam/camdae/2087.html>.

<sup>4</sup> Sam Lowe, “The EU’s Carbon Border Adjustment Mechanism: How to Make It Work for Developing Countries” (Centre for European Reform, April 22, 2021), <https://www.cer.eu/publications/archive/policy-brief/2021/eus-carbon-border-adjustment-mechanism-how-make-it-work>.

<sup>5</sup> Ben McWilliams and Georg Zachmann, “A European Carbon Border Tax- Much Pain, Little Gain,” *Policy Contributions*, Policy Contributions (Bruegel, March 2020), <https://ideas.repec.org/p/bre/polcon/35218.html>.

<sup>6</sup> McWilliams and Zachmann.

<sup>7</sup> The editorial board, “EU’s Carbon Border Tax Plan Is Risky but Needed,” *Financial Times*, January 29, 2020, <https://www.ft.com/content/28bbb54c-41b5-11ea-a047-eae9bd51ceba>.

<sup>8</sup> Lowe, “The EU’s Carbon Border Adjustment Mechanism.” and WTO, “Brexit, EU’s Carbon Border Adjustment Mechanism Take Centre Stage at Market Access Committee,” accessed June 1, 2021, [https://www.wto.org/english/news\\_e/news20\\_e/mark\\_16nov20\\_e.htm](https://www.wto.org/english/news_e/news20_e/mark_16nov20_e.htm).

<sup>9</sup> Konrad Adenauer Stiftung, “Perception of the Planned EU Carbon Border Adjustment Mechanism in Asia Pacific — An Expert Survey” (Konrad Adenauer Stiftung, March 2021), <https://www.kas.de/en/web/recap/single-title/-/content/perception-of-the-planned-eu-carbon-border-adjustment-mechanism-in-asia-pacific-an-expert-survey>.

<sup>10</sup> Verdinand Robertua, “ENVIRONMENTAL DIPLOMACY: CASE STUDY OF THE EU-INDONESIA PALM OIL DISPUTE,” July 10, 2019.

<sup>11</sup> Xinhua, “Cambodian PM Renews Call for Freer Int’l Trades, Adherence to Multilateralism,” accessed June 6, 2021, [http://www.xinhuanet.com/english/asiapacific/2021-06/01/c\\_139982475.htm](http://www.xinhuanet.com/english/asiapacific/2021-06/01/c_139982475.htm).

<sup>12</sup> ASEAN, “First Meeting of the Joint Working Group on Palm Oil between the European Union and Relevant ASEAN Member Countries,” ASEAN | ONE VISION ONE IDENTITY ONE COMMUNITY, February 1, 2021, <https://asean.org/first-meeting-joint-working-group-palm-oil-european-union-relevant-asean-member-countries/>.

<sup>13</sup> Jayanty Nada Shofa, “Asean Leads by Example in Sustainable Vegetable Oil: Indonesia,” *Jakarta Globe*, accessed June 1, 2021, <https://jakartaglobe.id/business/asean-leads-by-example-in-sustainable-vegetable-oil-indonesia>.

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