

***University of Cassino***  
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**International Economics**  
**International Trade**  
**(International standards –  
lecture 8)**

***Piero Esposito***  
**University of Cassino**



# Introduction: the Standards

- Since the end of World War II, many of the formal barriers to trade have been removed.
- Conflicts remain over the standards of quality (of the product and of the production process), i.e.:
  - technical product standards,
  - health and safety standards,
  - labor standards,
  - environmental standards.
- Standards can be a barrier to trade, but it can also improve the quality of production and trade.
- They are particularly relevant in North-South trade

# Emissions embedded in traded goods and services

- 22% of CO<sub>2</sub> emissions stem from goods produced in other countries
- Examples:
  - UK -22% of domestic emission 1990-2014, -11% if imports are included
  - US +9% of domestic emissions 1990-214, +17% when trade is included
- <https://www.carbonbrief.org/mapped-worlds-largest-co2-importers-exporters>

# Setting the Standards in three ways

Most regional trade agreements and the WTO agreements practice a combination of:

- **Harmonization of standards:** Two or more countries adopt a common set of standards
- **Mutual recognition of standards:** Countries maintain their own standards, but accept the standards of others as valid and sufficient
- **Separate standards:** Countries maintain their own standards and refuse to recognize the standards of others



# Setting Standards: efficiency and costs

- There are no general rules to determine which approach is most efficient or fairest in all cases.
- Each of the three mechanisms has advantages and disadvantages
  - Harmonization of technical standards, for example, leads to a larger market and greater efficiency, but may also freeze inferior standards that may develop to superior ones.
- Higher standards or changing standards is usually costly.

# Concerns about the Standards

- However, differences in labor and environmental standards, in particular, have generated concerns.
  - **High-income** countries fear that laxer standards in other countries induce domestic firms to:
    - (1) adopt lower standards to remain internationally competitive;
    - (2) move to countries with lax standards.
  - Countries fear a **race to the bottom** – i.e. the adoption of the lowest level of standards possible in order to attract foreign firms.



# Spread of Labor Standards

The U.S. and many other countries today want labor and environmental standards included in future trade agreements. For example:

- U.S. trade agreements with Canada and Mexico (the North American Free Trade Agreement, NAFTA) address labor and the environment: each country must enforce its own standards or face monetary fines.

However, labor and environmental activists see fines as inadequate to enforce standards and to hinder the race to the bottom.

# Defining Labor Standards

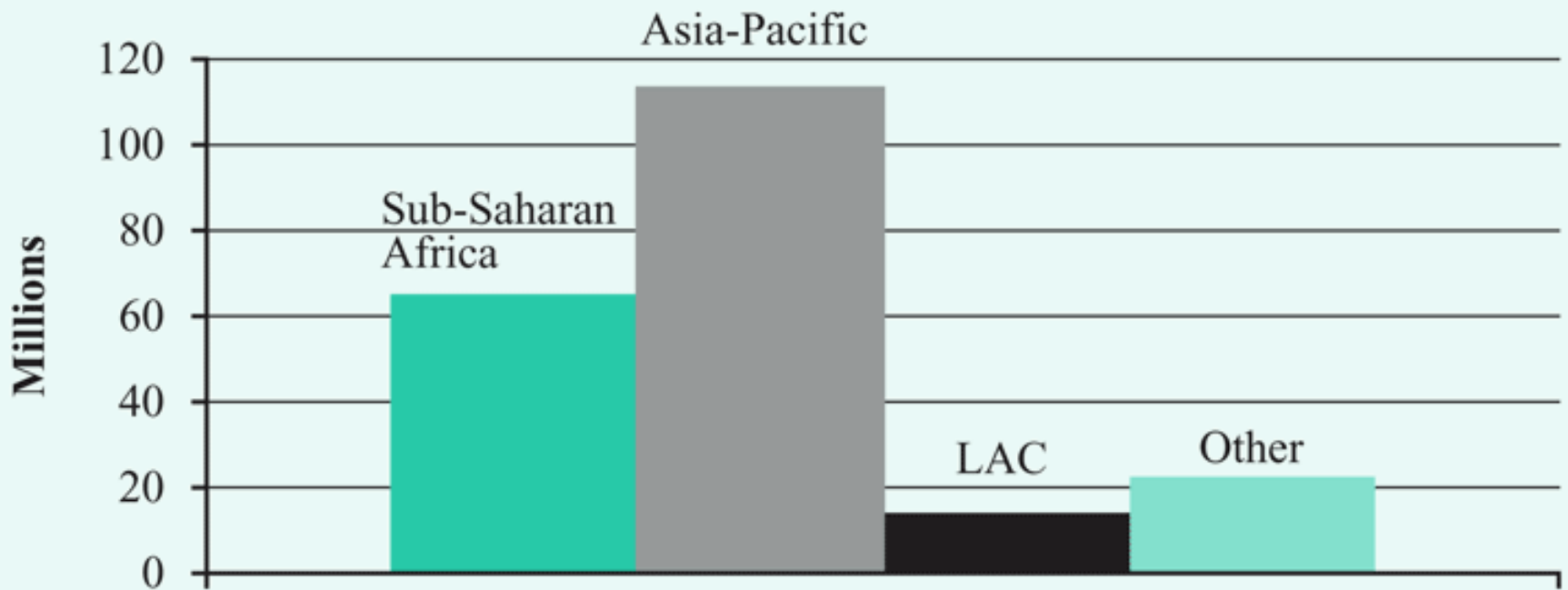
- The **International Labor Organization (ILO)** proposed five labor standards as basic rights (revised by OECD):
  1. Prohibition of forced labor
  2. Freedom of association
  3. The right to organize and bargain collectively
  4. An end to the exploitation of child labor
  5. Nondiscrimination in employment
- NB: **ILO** promotes social justice and human rights at the international level on work matters.



# Ambiguities of Labor Standards

- The five standards are widely agreed upon, but also ambiguous: what is meant by “exploitation”?
- Several labor standards are contentious, e.g.:
  - universal minimum wage level,
  - limits on the number of work hours,
  - workplace health and safety.
- Low-income countries are reluctant to pay much higher minimum wages: higher wages would reduce firm profits, and result in closing down of production and a rise in unemployment

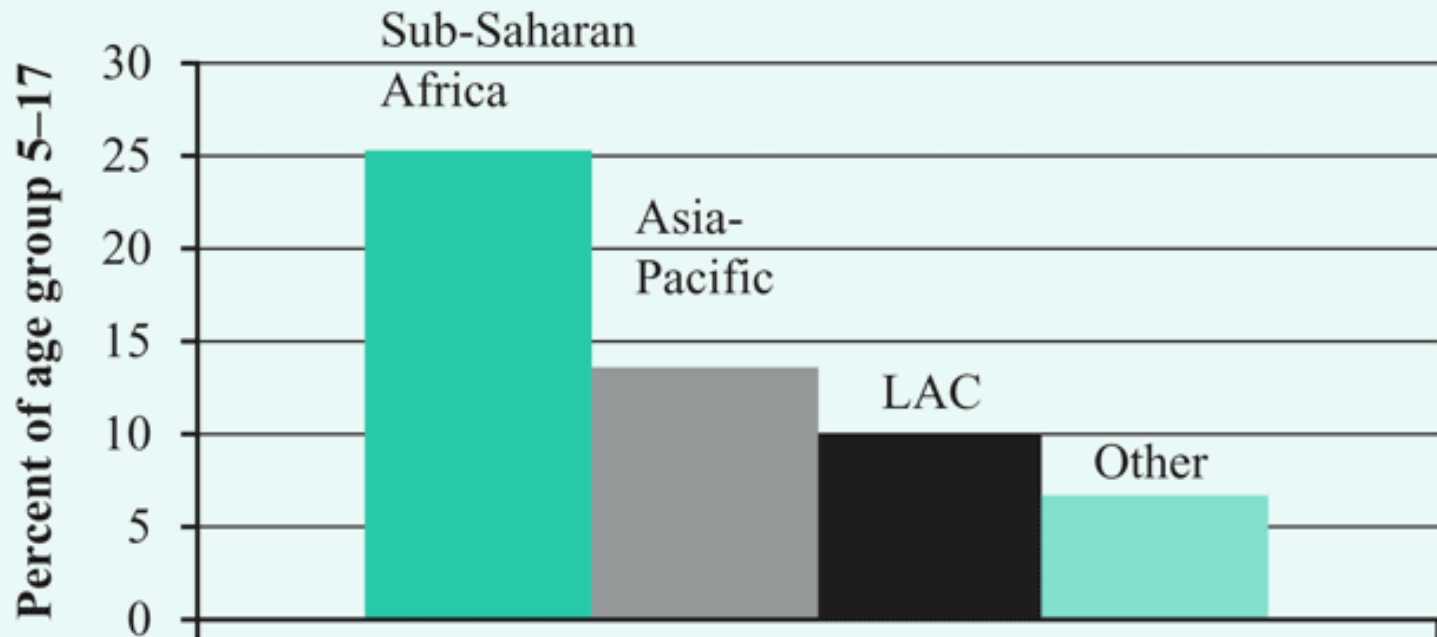
# Child Labor, 5-17 Age Group, 2008



Asia has the most child labor, followed by sub-Saharan Africa. LAC is Latin America and the Caribbean.

Source: International Labour Office, *Accelerating the Action against Child Labour* (2010).

# Percent of Children Working, 5-17 Age Group, 2008



Sub-Saharan Africa has the highest proportion of children working, followed by the Asia-Pacific region.

Source: International Labour Office, *Accelerating the Action against Child Labour* (2010).

# Labor Standards and Trade

- The major source of disagreements between the economists for free trade and labor activists is over the use of trade barriers to enforce labor standards
- Should one country use trade barriers to pressure another country into altering its labor standards?

# Problems with Labor Standards

1. **Effectiveness:** (a) only large countries or coalitions of countries can use trade barriers successfully to enforce standards, since small countries do not have a large enough impact on global demand;  
(b) use of sanctions could be counterproductive for boosting working conditions: improved enforcement in the target country may cause producers to shift to the unregulated and uninspected **informal economy**.

# Problems with Labor Standards (cont.)

## 2. **Hazy Borderline between Protectionism and**

**Concern:** special interests sometimes use the issue of foreign labor standards in order to attain their real goal, protection against foreign competition.

- Producers in a high-income country with scarcity of cheap, unskilled labor may seek sanctions against a low-income country in order to counter the competition posed by the low-income country producers with abundant supplies of cheap labor.

# Problems with Labor Standards (cont.)

3. **The Specific Content of Labor Standards:** there is no international agreement on the specific content of labor standards
  - Justifying the specific goal of sanctions to the international community is difficult; may lead to conflict in international economic relations
4. **The Potential to Set Off a Trade War:** use of sanctions is discriminatory and infraction of WTO
  - Sanctions may cause retaliation from the targeted country, further hurting international trade rules.




# Evidence on Low Standards as a Predatory Practice

Low standards are generally not effective mechanism to enhance competitiveness and to attract foreign investment.

There is very little evidence that countries that reduce labor standards succeed in obtaining a comparative advantage in a new line of production.

Low labor standards are correlated with unskilled, illiterate labor force, lack of economic development (poor telecommunications, schools, and sanitation).





# Trade and the Environment: Transboundary and Non- Transboundary Effects


- There is considerable overlap in the debates on labor and environmental standards.
- However, a further argument in favor of environmental standards is that pollution has **transboundary effects**.

# Trade and Transboundary Environmental Problems

**Transboundary** environmental impacts happen when one country's pollution spills over into a second country

For example, a shared watershed is polluted by an upstream user, or industrial production in one country creates acid rain in another country.

Transboundary environmental impacts can occur as the result of similar activities in many countries, leading to global impacts such as global warming.



# Claims of the proponents of trade barriers to enforce environmental standards

1. Without adequate enforcement of standards, countries engage in an **environmental race to the bottom** to boost industrial competitiveness
2. Lack of enforcement of standards in developing countries induce dirty rich country industries to “export pollution” and thus create **pollution havens**


# Pollution Havens

- Do **pollution havens** attract foreign firms?
  - Some dirty industries did move in the 1970s from high-income countries to low-income ones
  - However, there is no evidence that any country competes successfully for investment on the basis of lax environmental standards
  - As a result, individual firms cannot move to escape the environmental regulations of a high-standards country



# Alternatives to Trade Measures

- Currently, it is impossible to predict how, or even if, trade rules might eventually change to accommodate labor and environmental standards
- As long as there are large income gaps between rich and poor countries, it seems unlikely that differences in standards will disappear



# How to enjoy the benefits from world trade while resolving the conflicts over standards?

- There are three ways of enforcing sanctions without hurting international trade
  - Labels for Exports
  - Requiring home country standards
  - Increasing international negotiations
- Let's examine the usefulness of each of these in detail...

# Labels for Exports

- **Labeling:** A certification process producing a label attached on an exported good to indicate to consumers that the good was produced under humane and environmentally sound conditions
  - The method is already in place in some instances: Cambodian textile exports to the U.S., coffee imports, etc.
  - Problems: (1) Many countries resist labeling as an infringement of their sovereignty and (2) consumers must be convinced the label provides accurate information

# Requiring Home Country Standards

- High-standard countries can require their firms to follow home country standards when operating abroad
  - Pros: impedes the race to the bottom; avoids the problem of high-income countries' dictating standards
  - Cons: addresses only firms of high-standard countries; low-country producers are not affected; a high-standard country firm may outsource production to a low-standard country producer



# Increasing International Negotiations

- Using either existing international organizations or creating new agreements and organizations
  - ILO could be given a greater role and start, for example, publicizing lack of compliance with labor standard
  - The WTO is not an environmental organization; however, the WTO maintains an environmental database that reports all environmental agreements with potential trade impacts and that have been reported to the WTO.
  - As of 2012, there were 569 reported environmental agreements in the WTO.



# The pollution vs development dilemma

- The relationship between trade and growth is shaped like an inverted U:
  - as per capita incomes rise from low levels pollution increases,
  - beyond a certain threshold, further increases in income tend to diminish pollution (Environmental Kuzents Curve Hypothesis).