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HOW EU TRADE DEALS CAN INCREASE CLIMATE ACTION

DEVELOPING 'PROACTIVE' GREEN TRADE APPROACHES AFTER THE EU TSD REVIEW

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The EU is resuming its bilateral trade agenda, responding to increasing geopolitical and economic uncertainties. This comes after the EU reviewed its Trade and Sustainable Development (TSD) approach to its Free Trade Agreements (FTAs). While the TSD review recognises climate cooperation as a priority, upcoming political moments will test the EU's ability to develop a more 'proactive' approach to green trade. Success is important because the EU's future prosperity and security relies on trade partners also transitioning to a clean economy.

Summary

The EU is moving away from a 'defensive' understanding of climate policy in FTAs, towards a more 'proactive' stance. This change involves the EU not only seeking to safeguard its own domestic climate ambitions in the terms of its FTAs, but also using them to support its trade partners' climate transitions.

However, to develop this proactive approach effectively, the EU will need to break down siloes between its trade and climate diplomacy functions.

Upcoming EU priorities for this agenda include:

- > **Forests** – the EU could better incorporate **climate finance** into its approach, while supporting diplomatic goals such as the Forests and Climate Leaders Partnership, aiming to bring **Brazil** and others into the Partnership.
- > **Fossil fuel subsidies** – the EU should include provisions in future bilateral FTAs and support the multilateral Fossil Fuel Subsidy Reform process.



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- > **Coal phase-out** – the EU should use **export finance** and **investment facilitation** to accelerate the coal-to-clean transitions in priority countries such as **India, Indonesia, and Australia**.
 - > **Green industrial development** – the EU should use **capacity building, regulatory cooperation, and technology transfers** to support nascent green industries in partner countries, particularly where clear comparative advantages exist, such as with critical raw materials in **Chile**.

Introduction

Russia’s invasion of Ukraine has prompted the EU to resume its bilateral trade agenda, seeking increased trade diversification and international cooperation, as it also seeks to recover from the pandemic.

In this new context, the EU no longer views trade deals only as a means of achieving economic growth. Instead, the EU is starting to prioritise other objectives, such as increasing supply chain resilience, deepening cooperation with trusted partners, and securing access to materials and technologies that will be vital for achieving the objectives of the European Green Deal.

Prior to the Russian invasion of Ukraine in 2022, the 2019 European Commission deprioritised the EU’s bilateral trade agenda in favour of developing a range of autonomous trade instruments,¹ to enhance its assertiveness and defend its economic competitiveness. This shift to ‘open strategic autonomy’ was a response to the politics of 2016: President Trump’s ‘America first’ agenda, the rise of China, and a growing opposition to trade deals in the EU – most notably the Transatlantic Trade and Investment Partnership (TTIP).

To resume its bilateral trade agenda, the Commission first needed to ensure domestic support for it, including from key constituencies like environmental and labour groups. To this end, the Commission reviewed its so-called Trade and Sustainable Development (TSD) approach to its Free Trade Agreements (FTAs), to enhance its criteria on climate, environment, and workers’ rights.

¹ ECIPE, 2022, **The New Wave of Defensive Trade Policy Measures in the European Union** – These measures include: the Anti-Coercion Instrument (ACI), International Procurement Instrument (IPI), Carbon Border Adjustment Mechanism (CBAM), Foreign Subsidy Instrument (FSI), Corporate Sustainability Due Diligence (CSDDD), Level Playing Field Provisions in the EU-UK Trade and Cooperation Agreement (LPF), Enforcement Regulation (ER), and the Deforestation Initiative (DI)



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Background: the EU's TSD review

Policymakers in the European Parliament and Member States have received the Commission's TSD review positively.² Below, we summarise the TSD review, with a focus on the key climate-related outcomes. The review itself details 19 specific "Actions" for the Commission to take forward in its ongoing and upcoming trade negotiations, under a series of headings, which we have interpreted as Goals.

*Box 1. Summary of the EU's TSD review with specific "Goals" and "Actions"*³

Summary of the EU's TSD review

Goal 1: A comprehensive TSD approach anchored in multilateral agreements and cooperation

- > Action 1: step up engagement to ensure Paris Agreement compliance
- > Action 2: Provide support for reform and capacity building through technical and financial assistance
- > Action 3: facilitating dialogue, including on EU autonomous measures

Goal 2: Country-specific implementation

- > Action 4: apply tailored approaches, supported by impact assessments identifying country-specific sustainability priorities
- > Action 5: negotiate detailed and time-bound roadmaps with milestones for cooperation

Goal 3: Mainstreaming sustainability throughout trade agreements

- > Action 6: negotiate market access for environmental goods and services, prioritising renewables, and investment and access to raw materials
- > Action 7: support these negotiations with impact assessments

Goal 4: Collective monitoring of the implementation of TSD commitments

Goal 5: Reinforcing the role of civil society

Goal 6: More assertive enforcement, including through trade sanctions

- > Action 19: extend state-to-state dispute settlement to the TSD chapter and the possibility of trade sanctions in cases that may "materially defeat the object and purpose of the Paris Agreement"

² European Parliament, 2022, [Resolution on the outcome of the Commission's review of the 15-point action plan on trade and sustainable development](#)

³ European Commission, 2022, [The power of trade partnerships: together for green and just economic growth](#)



The EU’s TSD review: towards ‘proactive’ green trade

The EU’s TSD review has progressed the EU’s trade and climate agenda in two ways: Firstly, by starting a shift from mainly defensive to more proactive ways of incorporating climate objectives into its approach to trade. Secondly, moving away from approaching sustainability only within the FTA text towards a greater recognition that other policies play an important role in its bilateral trade and climate relations.

Below, in Table 1, we take the objectives listed in the TSD review, as summarised in Box 1, and assess their progress within our own conceptual framework – we use a colour code to assess those areas where the Commission’s thinking is most and least developed.

Table 1. Conceptual framework of EU TSD approaches

	Defensive TSD approaches	Proactive TSD approaches
FTA-specific activities	Paris Agreement compliance and non-regression, ‘right to regulate’ provisions	Liberalising environmental goods and services, investment and access to critical raw materials, impact assessments, cooperation on green subsidies and public procurement
FTA-adjacent activities	EU autonomous measures: e.g. EU Carbon Border Adjustment Mechanism, Deforestation Regulation, Due Diligence Directive	EU climate diplomacy goals: supported by technical and financial assistance, capacity building, supply chain management, investment facilitation, export finance, regulatory cooperation, green industrial development
<p>▶ Goals most developed by TSD review, reflected in subsequent EU positions</p> <p>▶ Goals developed by the TSD review, yet to see developed in practice</p> <p>▶ Goals called for in the TSD review, but unclear EU strategy to deliver</p>		



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Paris Agreement compliance, non-regression and ‘right to regulate’ provisions, and the EU’s autonomous measures, are defensive trade policy tools. This is because objectives like non-regression, addressing carbon leakage, competitiveness, and supply chain standards, primarily aim to safeguard the EU’s own domestic climate policy from trade risks rather than supporting the policies of its trade partners.

In contrast, objectives like liberalising environmental goods and services, facilitating investment and access to critical raw materials, and supporting progress on the EU’s climate diplomacy goals, are more proactive goals. They have the potential to maximise trade and climate benefits not only for the EU but also for its trade partners, and as a result, have a greater global impact.

The European Green Deal and the long-standing political demands from the European Parliament and others to enhance the EU’s trade and climate approaches is enabling the EU’s shift from a defensive to a more proactive way of thinking. As are contemporary geopolitics: the EU’s post-pandemic response, along with Russia’s invasion of Ukraine, is leading the EU to intervene more in supply chains, further diversify its trade relations, and deepen its cooperation with key partners. This more ambitious proactive green trade agenda has the potential to drive global climate action forward.

Implementation: upcoming EU FTAs

Institutional capacity is another factor that can explain why the EU has developed certain TSD approaches more than others. The EU’s trade officials are naturally more familiar with FTA-specific considerations and the EU’s autonomous trade instruments, whereas they are less familiar with the EU’s climate diplomacy goals.

As the EU starts to consider more proactive and FTA-adjacent priorities in its approach to trade, it will become more necessary for the EU to break down silos between its trade and its climate diplomacy functions. This is within the EU institutions, as well as in better coordination with the Member States, where the EU’s climate diplomacy capacity traditionally sits.

The next major tests for the EU’s new TSD approach will be several highly political bilateral trade moments. They will focus mostly on two key regions: Latin America and the Indo-Pacific. These regions are key geostrategic areas for the EU, as they are critical balancing actors, with growing economic potential,



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and mostly like-minded democracies. The most significant agreements will be with:

- > **Chile** – the negotiated text was finalised in December 2022. The agreement will facilitate EU investments in Chile’s mining sector but risks limiting Chile’s capacity to use its mineral reserves to upscale its nascent green industries. Through the forthcoming update to the agreement’s TSD chapter, the EU should avoid viewing access to Chile’s reserves of critical raw materials as an offensive interest but rather as an opportunity to facilitate Chile’s green industrial growth and support its climate ambitions.
- > **Mercosur** – in 2019, after 20 years of negotiations, the EU reached an agreement in principle for an FTA with the Mercosur trade bloc. Concerns about the environmental sustainability of the deal have long blocked prospects for the European Parliament’s approval of the deal. Following the TSD review, the EU is hoping to agree an additional ‘sustainability instrument’ with Mercosur to allay domestic EU concerns.⁴ However, the recent change of President in Brazil may yet lead to more profound demands such as reopening negotiations.
- > **Australia** – negotiations are underway for an EU-Australia FTA, possibly aiming for conclusion in 2023. The new government in Australia has improved its climate commitments, lifting a major hurdle in the negotiations. Proactive priorities, beyond Paris Agreement commitments, include accelerating Australia’s coal-to-clean transition through increased European investment, and cooperation on the sustainable production and trade of critical raw materials.
- > **India, Indonesia** – negotiations are ongoing for FTAs with India and Indonesia. Both are major emerging economies with high carbon intensities. Decoupling their economic growth from climate and environmental impacts is a high global priority. Both countries are large coal power consumers and host important forested areas. Alongside these priorities, the EU can help establish Just Energy Transition Partnerships (JETPs) with both countries.

⁴ EPC, 2021, ‘**Mixed’ feelings about the EU–Mercosur deal: How to leverage it for sustainable development** – models include: a joint interpretation or declaration; a binding additional protocol; a non-binding joint roadmap; pre-signature or ratification commitments; unilateral statements or declarations – or a combination of these. The precise legal instrument is less important than the political offer the EU can make, along with real-world sustainability impacts. Hence, our suggested areas of focus below



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Below, in Table 2 we summarise the EU's upcoming FTAs, and offer suggestions of climate issues that the EU should prioritise inside and adjacent to each:

Table 2. Upcoming EU FTAs and suggested TSD priorities

EU trade partner	Status	Potential TSD priorities
New Zealand	Concluded	Carbon pricing Fossil fuel subsidy reform Regulatory cooperation Methane emissions
Chile	Negotiations ended, pending political approval	Critical raw materials Green industry Renewable energy Research and innovation
Mexico	Negotiations ended, pending political approval	Renewable energy Fossil fuel subsidy reform Regulatory cooperation Research and innovation
Mercosur	Negotiations ended, pending additional 'sustainability instrument'	Forest protection Renewable energy Fossil fuel subsidy reform Research and innovation
Australia	Negotiations ongoing	Coal-to-clean Critical raw materials Research and innovation Methane emissions
Indonesia	Negotiations ongoing	Coal-to-clean Forest protection Biofuels Research, innovation, and technology cooperation
India	Negotiations ongoing	Coal-to-clean Green industry Research, innovation, and technology cooperation



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Proactive approaches: aligning the EU's trade and climate diplomacy goals

For the EU to deliver on its climate goals through cooperation with trade partners, it needs to develop a proactive agenda tailored to each partner, combining both FTA-specific and adjacent initiatives.

Policy options include **climate finance**, **export finance**, **regulatory cooperation**, **capacity building**, and **technology transfer**. The most impactful policy options will vary depending on partners' specific climate challenges and opportunities. By adopting a thematic focus, EU policymakers can better understand how to match trade policy options with the EU's established climate diplomacy goals.

Ending deforestation

With the EU seeking to conclude trade agreements with **Mercosur** and **Indonesia**, it is seeking closer ties with two of the three largest rainforest nations (Brazil, DRC, and Indonesia).⁵ Elsewhere on the EU's trade priorities list, **India** and **Mexico** also host large areas of rainforest.

Ending deforestation will be vital to avert the climate crisis. This was recognised at COP26, when 145 countries, covering 90% of the world's forests, promised to halt and reverse forest loss by 2030, supported by \$12bn of **climate finance** from twelve donor countries. If achieved, this effort would deliver 10% of the global climate mitigation needed by 2030 to deliver on the Paris Agreement.⁶

It is estimated that EU consumption causes 10% of global deforestation.⁷ To tackle this issue, the European Commission has proposed a regulation that will require companies to undertake due diligence assessments of deforestation in their supply chains. This proposal will increase compliance costs for EU partners, particularly smallholders, and there is a risk of disengagement and trade diversion.⁸ To remedy this, the EU must come forward with a proactive agenda to support its trade partners, combining various tools that are available, including **regulatory cooperation** and offers of **capacity building**.

⁵ Within Mercosur, Argentina, Paraguay, and Uruguay are also important rainforest countries

⁶ COP26 Presidency, 2022, [World Leaders Launch Forests and Climate Leaders' Partnership](#)

⁷ European Parliament, 2022, [Deal on new law to ensure products causing deforestation are not sold in the EU](#)

⁸ Fair Trade Advocacy, 2022, [50 CSOs call upon the Commission to evaluate the needs of smallholders and local communities to adapt to EU Deforestation Regulation](#)



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These efforts should also be situated within the efforts already underway as part of the multilateral climate agenda. At COP27, the COP26 Presidency launched the Forests and Climate Leaders' Partnership (FCLP) as a long-term delivery mechanism for the 2030 forest loss pledge. The FCLP has proposed several priority work strands and the EU could take a leading role on some of them.⁹ While the EU supported the Partnership at COP27, particularly with additional climate finance from Germany, other European donor countries should step up their support. The EU could leverage its trade negotiations with Mercosur to bring Brazil and other priority countries into the FCLP.

Fossil fuel subsidies

In the Glasgow Climate Pact agreed at COP26, countries agreed for the first time in a full multilateral setting to accelerate efforts to phase-out fossil fuel subsidies.¹⁰ In parallel, at the WTO, the **New Zealand**-led Friends of Fossil Fuel Subsidy Reform (FFSR) initiative has increased in momentum, with the EU among others joining in a fresh wave of commitment. At the multilateral level, the EU should continue to prioritise the FFSR initiative and consider it as a potential delivery mechanism for the Glasgow Climate Pact.

Bilaterally, for the first time in an EU trade agreement, the EU-New Zealand FTA contains a dedicated provision for fossil fuel subsidy reform.¹¹ Going forward, the EU should seek to replicate similar provisions in future FTAs.

Coal phase-out

Coal is the most polluting fossil fuel. According to the International Energy Agency, unabated coal power generation needs to be phased out urgently – by 2030 in the OECD and by 2040 in non-OECD countries – if the world is to get on track to achieving carbon neutrality by mid-century.¹²

The EU is seeking to conclude trade agreements with some of the most coal-intensive economies globally, including **India**, **Indonesia**, and **Australia**. The EU needs to urgently deploy stronger trade incentives to quicken the coal-to-clean

⁹ Climate Home, 2022, **As Glasgow forest pledge turns to action, most signatories drop out** – the action areas are: international collaboration on sustainable land use economy and supply chains, mobilising public finance, shifting private finance, supporting indigenous peoples' and local community initiatives, strengthening and scaling carbon markets for forests, and building international partnerships and incentives to preserve high-integrity forests

¹⁰ UNFCCC, 2021, **Glasgow Climate Pact**

¹¹ European Commission, 2022, **EU–New Zealand Trade Agreement**

¹² International Energy Agency, 2022, **World Energy Outlook 2022: Outlook for solid fuels**



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transition in these and other countries. Its focus on securing market access for renewables through its upcoming FTAs, as stated in the TSD review, will help lower barriers for the uptake of renewables in partner countries.

However, to truly upscale renewables, the EU must put forward additional support schemes that facilitate green investments abroad. For instance, the EU's **Global Gateway** initiative could boost investments in core infrastructure like power grids. Other complementary tools include international **climate finance** investments, particularly when the efforts of several donor countries are combined to form Just Energy Transition Partnerships (JETPs). The South Africa JETP, brokered at COP26, has since acted as a model that others like Indonesia and Vietnam have replicated. India is also often considered a priority country for a JETP.¹³ Lastly, the EU should consider using **export finance**, in particular coordinating Member States' export credit agencies, to target financial support in favour of the coal-to-clean transition in partner countries.

Industrial decarbonisation

Industry and manufacturing are responsible for 45% of global energy-related emissions.¹⁴ An ambitious EU green trade agenda should seek to accelerate industrial decarbonisation by cooperating with trade partners. Proactive engagement would help develop growth markets for the EU's clean economy abroad, while also helping to remedy issues arising from the EU's autonomous measures, including risks of trade diversion and pushback from key partner countries such as **India**.

In its current approach to trade – most notably through the Carbon Border Adjustment Mechanism (CBAM) – the EU takes a largely defensive attitude towards industrial decarbonisation, aiming to protect EU industries from the risk of carbon leakage and unfair competition. However, these same policies can also be deployed proactively to foster green industrial transitions abroad. For instance, CBAM revenues could be used to support green industries abroad through **climate finance** and **capacity building**. Increased overseas demand for green products could also help address some of the competitiveness concerns for EU exports raised by the CBAM.

¹³ Politico, 2022, **G7 offered Vietnam and Indonesia \$15B to drop coal**

¹⁴ International Energy Agency, 2022, **Achieving Net Zero Heavy Industry Sectors in G7 Members** – this accounts for both direct emissions caused during the industrial processes (approx. 9 Gt of CO₂eq) as well as indirect emissions from electricity and imported heat generation (approx. 8 Gt of CO₂eq), according to the. Energy-related emissions represent almost two thirds of global greenhouse gas emissions



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The TSD review has made market access for environmental goods and services a key priority of new FTAs. To build on these objectives, the EU can better leverage its single market to boost industrial decarbonisation abroad through regulatory dialogues and Mutual Recognition Agreements aimed at lowering non-tariff barriers for imports. Outside of FTAs, the European Commission, working with the Member States, could foster joint off-take agreements for green industrial products, such as those being developed by Germany and the Netherlands for green hydrogen.¹⁵

There are a range of further tools that the EU could develop to enhance its proactive support of green industries abroad. These include cooperation on **research and innovation, technology transfers, sustainable investment facilitation** schemes, common green **public procurement** initiatives, and shared principles for **green subsidies**. Such initiatives have the most potential where partners benefit from clear comparative advantages, such as the critical raw materials reserves in **Chile** or **Australia**.

Conclusions

The EU has significantly improved the climate criteria of its FTAs through the TSD review. In the review, the EU has started to move towards a more proactive understanding of trade and climate policy, beyond seeing climate primarily as a defensive issue in its trade deals. Moreover, through the review, the EU has started not only to consider the climate criteria specific to its FTAs, but also how FTA-adjacent political and diplomatic goals can be brought into its approach.

However, it will be necessary for the EU to break down silos between its trade and its climate diplomacy functions – within the EU Institutions and in coordination with the Member States – if it is to effectively incorporate these climate goals into its new approach to trade.

These goals could include combating deforestation, reforming fossil fuel subsidies, and investing in trade partners' coal-to-clean and green industrial development. These are established EU climate diplomacy priorities that a new approach to trade can significantly support.

¹⁵ H2Global Stiftung, 2022, [The H2Global Mechanism](#)



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About E3G

E3G is an independent climate change think tank with a global outlook. We work on the frontier of the climate landscape, tackling the barriers and advancing the solutions to a safe climate. Our goal is to translate climate politics, economics and policies into action.

E3G builds broad-based coalitions to deliver a safe climate, working closely with like-minded partners in government, politics, civil society, science, the media, public interest foundations and elsewhere to leverage change.

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