Benefits of EU international trade agreements

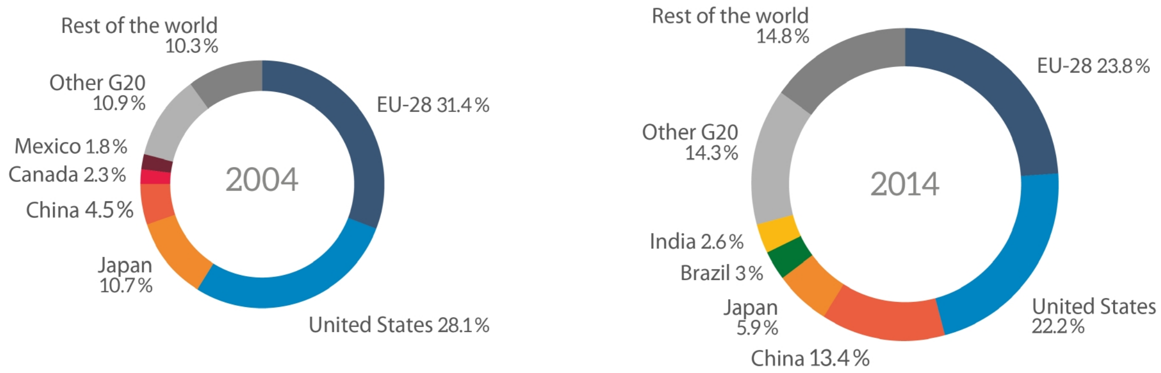
- **31 million jobs in the EU depend on external trade**
- **EU consumers gain about €600 a year due to increased choice in goods**
- **Finalising current free trade agreement negotiations could increase EU GDP by €250 billion**

EU international trade policy

Trade is the EU's most important link to the world beyond its borders. In force since the 1957 Treaty of Rome, the transition to a common EU trade policy was completed in 1968. It is the EU's oldest instrument influencing the bloc's foreign relations. Today, Article 207 of the Treaty on the Functioning of the European Union (TFEU) establishes the common trade policy as an exclusive EU competence.[1] Following the procedure under that legal basis the EU negotiates, concludes and implements trade agreements. Currently, the EU is negotiating and up-dating Free Trade Agreements (FTAs) with 19 countries[2] and 2 sub-regional blocs, namely the Association of Southeast Asian Nations (ASEAN) and the Southern Common Market of South American countries (*Mercado Común de Sur*: Mercosur).

Within the EU's latest trade strategy – the 2015 'Trade for All – Towards a more responsible trade and investment strategy', FTAs are considered instruments that contribute to the EU's objective of generating jobs and growth. About 31 million jobs in Europe depend, directly or indirectly, on the EU and its Member States' ability to trade. In other words, EU external trade concerns almost one in every seven jobs in Europe. In France, for example, over 2.2 million jobs rely on French exports outside the EU. Around 90 % of future global growth is expected to be generated outside Europe's borders. Figures show that the EU share of world GDP has slowly decreased in recent years (see graph below). Against this background, the EU needs to seize trade opportunities beyond its borders in order to gain higher levels of growth in Europe.

EU share of world GDP



Source: Eurostat.

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Crucially, the EU is committed not only to use its common trade policy to generate growth and jobs in Europe, but also to support countries worldwide to achieve sustainable development through trade. For instance, the EU has opened its markets fully to imports from the world's poorest countries, and assists in building infrastructures and the skills needed to trade successfully. EU imports from developing countries are worth €860 billion a year. Moreover, EU trade policy is designed to promote European principles and values in the world. These include good governance, environmental protection, human and labour rights, health and consumer protection, and protection of cultural diversity. Various third-country governments have requested the EU intensify dialogues on trade.

In its July 2016 resolution on a forward-looking and innovative future strategy for trade and investment, the European Parliament recognises that EU 'trade policy is of utmost geopolitical and economic importance for Europe to shape globalisation, to strengthen international standards and to increase access to foreign markets'.

New generation of EU free trade agreements – three examples

Responding to today's greater international economic complexity, the EU has moved from classical FTAs focused on tariff cuts and trade in goods to a new generation of FTAs. These aim to open up new markets and to initially include services, public procurement, investments, and regulatory cooperation. In addition, their aim is to foster sustainable development similar to the 17 Sustainable Development Goals (SDGs) agreed at United Nations level in 2015. The EU's new generation of FTAs include the three following examples:

EU-South Korea Free Trade Agreement

The EU-South Korea Free Trade Agreement was the first of the new generation of EU FTAs, and has contributed to boosting trade between the EU and South Korea. Provisionally applied since July 2011 (and formally in force since December 2015), it has helped EU exports to South Korea increase by around 55 % since 2011. As the EU's ninth largest export destination for goods, South-Korea belongs in the top ten of EU export markets. Conversely, the EU is South Korea's third largest export market. In 2016, EU exports to South Korea, mainly machinery and appliances, transport equipment and chemical products, amounted to €44.5 billion. EU imports from South Korea reached €41.4 billion in 2016, mainly consisting of machinery and appliances, transport and plastics. In May 2017, the European Parliament adopted a resolution welcoming the fact that the Agreement has led to a significant growth in trade between the EU and South Korea.

Development of EU-South Korea trade

Source: Eurostat.

EU-Canada Comprehensive Economic Trade Agreement (CETA)

The EU and Canada negotiated CETA between 2007 and 2014. The agreement was signed at the EU-Canada Summit in October 2016 and is currently undergoing ratification by the EU Member States and Canada. In February 2017, the European Parliament approved the agreement, which aims at boosting trade in goods, services and investment between both trading partners. The EU already exports a wide range of products to Canada. In 2016, EU exports to Canada amounted to €35.2 billion, whereas imports from Canada totalled €29 billion. CETA promises to make this trade between the EU and Canada easier and cheaper. According to the Commission, CETA provides various further benefits, such as lower prices and a wider choice for European consumers, allowing EU firms to bid for Canadian public contracts, and helping Europe's food and drinks producers based in rural communities.[3]

EU-Peru, Columbia and Ecuador Trade Agreement

Signed in June 2012, the trade agreement between the EU and Colombia has been applied provisionally since 2013 (its application to trade with Peru began in March 2013, and with Colombia in August 2013). Based on progressive and shared liberalisation, according to provisions of the World Trade Organization (WTO), the agreement has contributed to easing trade between the EU and the two Andean countries. In 2016, EU exports to Peru and Colombia together amounted to €9 billion, whereas EU imports from both countries totalled €10.3 billion. In July 2014, negotiations for Ecuador's accession to the agreement were concluded. In that form, the agreement is applied provisionally since January 2017. A 2016 study by the European Commission assessing the economic impact of the trade agreement between the EU and Ecuador estimates that the agreement will increase EU exports to Ecuador by around 42 % and exports from Ecuador to the EU by around 30 %.[4]

Economic, social and political challenges of free trade agreements

The rise in FTAs accompanies increased trading relations with countries with different living and production standards. This results in challenges for the EU, such as imperfect competition conditions, social dumping, and balancing EU trade policy with European values, as well as the aim of incorporating the SDGs into FTAs.

Increasing trade openness leads to a higher degree of competition,[5] implying that firms in EU Member States and third-country firms compete with each other. Except in the case of protectionist measures, the less productive companies exit the market.

Concerns regarding employment that result from FTAs could be especially valid in industrial, low-skilled jobs. This is due to the increase of economic vulnerability in some sectors, caused by higher import competition. Characterised by a predominance of low-skilled jobs, the main vulnerable EU sectors are textiles, clothing, footwear and leather, basic metals and fabricated metal products, and miscellaneous manufacturing industries.[6] To the contrary, service sectors and luxury manufactured products should face very low investment competition. Workers in service sectors are particularly less likely to see an increase in international competition jeopardise their jobs.

While growth generated by FTAs increases public budgets that could be invested in climate protection, they can also minimise the quality of goods, consumer and health protection, and social and environmental standards, because of lower norms. Against this background, a major challenge for the EU in implementing its trade policy is in balancing European economic interest and European values.[7] This also concerns the firm integration of the UN's 17 SDGs into the EU's common trade policy.

Benefits of EU trade to consumers

The academic literature highlights three main benefits from trade, of which two directly and one indirectly contribute to benefit European consumers and their welfare:

1. Decrease in prices for the same range of goods (direct);
2. Increase in the variety of products (direct);
3. Increase in the growth rate (indirect).

The increased competition engendered by FTAs decreases the price of goods, as new and larger imports incentivise EU firms to adjust their price policy and make their production more efficient and thus less costly. For example, they can invest more in research and development (R&D). Therefore, the creation of FTAs could in certain cases **raise consumer purchasing power**.[8] Furthermore, FTAs can help to break monopolies, also leading to a decrease in product prices.

The larger variety of products available in the EU is due to increased trade flows. This benefit of trade gives consumers the opportunity to choose from a larger pool of quantitative and qualitative factors for the same sort of goods. On these grounds, the economic gain for the average EU consumer is in the range of €600 per year in the EU.

The FTAs that are currently under negotiation can, according the European Commission's estimates, increase EU GDP by more than 2 %, a sum equivalent to **€250 billion annually**.[9] This represents the size of the Danish economy. Such a boost in growth is mainly driven through an increased search for innovation because of greater economic competition. The innovation process is accelerated, with higher investments in capital and in R&D, and also increased diffusion of technology. Resting on the endogenous growth theory, which proposes that investment in capital, knowledge and innovation foster growth with significant positive side effects, higher trade flows due to FTAs foster not only growth but, as a consequence of growth, lead to an **increased level in living standards for EU citizens**.[10]

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[1] In May 2017, however, the Court of Justice of the EU issued its opinion in the case of the EU-Singapore trade deal. The Court's view was that, with respect to non-direct foreign investment, (ii) investor-state dispute settlement (ISDS), and (iii) state-to-state dispute settlement relating to provisions regarding portfolio and ISDS, fall under shared competence with the EU Member States. For further information, see Puccio, L., CJEU Opinion on the EU-Singapore Agreement, EPRS, European Parliament, May 2017.

[2] The negotiations with the USA on the Transatlantic Trade and Investment Partnership (TIPP) are effectively on hold.

[3] European Commission, The Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada. The benefits of CETA, 2016.

[4] European Commission, Assessing the economic impact of the Trade Agreement between the European Union and Ecuador, 2016.

[5] Helpman, E. and Krugman, P. R., *Market Structure and Foreign Trade*, Cambridge, MIT Press, 1985.

[6] Jansen, M., International trade and the position of European low-skilled labour, WTO-Working Paper, 2000.

[7] Rudloff, B. and Laurer, M., The EU as global trade and investment actor - The times are a-changin, SWP-Working Paper, 2017.

[8] Mark-ups generally fall with import competition. However, it is not clear whether the phenomenon is due to elimination of the market power or the creation of negative profits. See Tybout, J. R., Plant- and Firm-level evidence on new trade theories, NBER-Working Paper, 2001.

[9] European Commission, How Trade Policy and Regional Trade Agreements Support and Strengthen EU Economic Performance, 2015, p. 7.

[10] Romer, P. M., 'The Origins of Endogenous Growth', in: *The Journal of Economic Perspectives*, 8 (1994) 1, pp. 3-22.

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