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COVER NOTE

from: Secretary-General of the European Commission,
signed by Mr Jordi AYET PUIGARNAU, Director

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to: Mr Uwe CORSEPIUS, Secretary-General of the Council of the European
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Executive summary of the impact assessment on the future of the EU-US trade
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COMMISSION STAFF WORKING DOCUMENT

**EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT ON THE FUTURE OF
THE EU-US TRADE RELATIONS**

Accompanying the document

Recommendation for a Council Decision

**authorising the opening of negotiations on a comprehensive trade and investment
agreement, called the Transatlantic Trade and Investment Partnership, between the
European Union and the United States of America**

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INTRODUCTION

The EU and the US are the world's major global traders and investors. In fact, the EU is the largest economy in the world, representing 25.1% of world GDP and 17.0% of world trade and the US is the second largest economy accounting for 21.6% of world GDP and 13.4% of world trade.¹

However, the relative share of the bilateral relationship in the two economies' total trade has been in decline over the last decade. This relative decline is particularly sharp when looking at EU trade in goods. Between 2000 and 2011, while EU exports of goods to the world increased at an average annual growth rate of 7.6%, EU exports to the US only grew by 1%. As a result, the share of the US in total EU goods exports declined from 28.1% in 2000 to 16.9% in 2011.

Stakeholders complain about barriers to trade and investments that block economic potential in the transatlantic market place. Although transatlantic tariff barriers are comparatively low, tariffs still impose costs that are not negligible. The WTO estimates² average MFN tariffs of the US and the EU at 3.5% and 5.2% respectively, and both the US and the EU maintain “tariff peaks” in sectors of economic interest to the other partner.

More importantly, regulatory differences for goods and services act as impediments to trade and investment flows. In the context of sophisticated regulatory regimes, with very often similar aims, differences in approaches can result in significant additional burdens for EU and US businesses. According to the results of the public consultations that the Commission has conducted, this is particularly true for SMEs, which report lost opportunities in terms of jobs and growth. Economic analysis (Ecorys 2009) suggests that trade cost equivalents³ are usually higher than 10% (of equivalent duties) and above 20% for many sectors.

The access to the US public procurement market is another area where European firms report difficulties. The US has limited legally binding international commitments in this area, whether under the WTO Government Procurement Agreement (GPA) or in its bilateral FTAs.

¹ Source: World Bank's World Development Indicator, current prices:
<http://data.worldbank.org/indicator>.

² http://stat.wto.org/TariffProfiles/E27_e.htm; http://stat.wto.org/TariffProfiles/US_e.htm

³ The amount of additional cost burdens for trading across the Atlantic, compared to the domestic market.

Only 32% (€178bn)⁴ of the U.S. procurement market is open to EU businesses under the commitments recently agreed by the US in the framework of the GPA.

Given the huge volume of economic interaction and the vast respective market size of the EU and the US, trade and investments freed from such restrictive measures could potentially create big benefits for EU and US businesses and consumers, creating jobs and growth on both sides of the Atlantic.

OBJECTIVES FOR ENHANCING THE EU-US TRADE AND INVESTMENT RELATIONSHIP

Based on expert studies and public consultations, the Impact Assessment Report identifies the following specific operational objectives from a European perspective.

As regards **trade in goods** and related investment, we should aim at eliminating all tariffs, while considering options for the treatment of the most sensitive products. Duty elimination would be particularly significant for those sectors (e.g., processed agricultural products, textiles and clothing, leather and footwear, etc.) where tariffs still constitute a substantial barrier to trade. Even more importantly, we should aim at eliminating or reducing the trade cost of regulatory obstacles to trade.

To the extent that regulatory obstacles stem from legitimate, non-discriminatory and proportionate regulatory measures, and from unavoidable differences in the regulatory environment, we should aim to reduce divergences where possible. This should be applied to industrial and agricultural rulemaking and could be achieved by making use of a number of different methods, which are complementary, including the convergence of US standards with international standards, the harmonisation of standards and technical regulations between the US and the EU, and/or mutual recognition and equivalence of standards, technical regulations, audits and inspections. Since not all regulatory divergences can be eliminated in one go, we should envisage a "living agreement" that allows for progressively greater regulatory convergence over time against defined targets and deadlines. Furthermore, strengthened institutional mechanisms should be set up to enhance upstream regulatory cooperation.

With regard to **trade in services** and related investment, we should aim to bind the existing level of autonomous liberalisation and to "future-proof" such liberalisation by subjecting it to a ratchet which would capture any future new liberalisation. Furthermore, we should seek to achieve genuine new market access through an effective opening of key services sectors, such as transport. We should also address regulatory barriers through closer regulatory cooperation and by establishing common regulatory disciplines, thus ensuring more open competition and establishing a level playing field for EU industry in those services sectors where full access is restricted. In general, we should ensure the application of non-discrimination through unconditional national treatment.

Finally, in respect of **public procurement** we should aim at improving EU firms' access to public procurement opportunities in the US, inter alia by: 1) increasing the coverage of federal procurement (e.g. additional procuring entities and removing Buy America conditions attached to federal funding); 2) broaden the coverage of the US sub-federal level both by increasing the number of states, as well as the coverage of those currently offered by the

⁴ European Commission estimates, based on the US Statistical reports to the GPA Secretariat, US Federal Procurement Data System (FPDS) reports and the US census.

GPA, leading to comprehensive coverage of utilities, and removal of the "Buy America(n)" provisions and achieving treatment equivalent to local suppliers; and 3) persuading the US to progressively eliminate trade barriers to cross-border procurement ("Buy America(n)" provisions and sectoral derogations, in particular on Mass-Transit and with respect to SMEs).

POLICY OPTIONS ANALYSED

Different policy options are analysed in the Impact Assessment Report:

- A. a baseline scenario which does not carry any substantial policy change and would allow envisaging modest progress focused on regulatory issues for goods under the Transatlantic Economic Council (TEC), the High Level Regulatory Cooperation Forum (HLRCF) and ongoing sectoral dialogues as the main platforms;
- B. "tariff-only", "services-only" or "procurement-only" agreements; and
- C. a comprehensive option that involves the negotiation of a comprehensive EU-US trade and investment agreement covering tariffs, regulatory barriers for goods, services, investment and government procurement simultaneously. Under this option, two scenarios are explored to provide for a possible range of outcomes: a "conservative" one and an "ambitious" one.

ECONOMIC IMPACT OF THE OPTIONS ANALYSED

A **tariff-only** agreement would provide overall benefits to the EU. In the political reality of negotiations, the most trade-restricting tariffs (those that have the biggest impact on bilateral trade) will be retained or phased out last. The tariff-only scenario therefore assumes a more conservative 98% elimination of all tariff lines, falling short of the goal of full duty elimination announced in the context of the High Level Working Group (HLWG). In reality, a 98% coverage might even be too high because "tariff-only" negotiations would give fewer possibilities for the EU and the US to trade-off concessions and benefits across all pillars such as services and procurement, where in particular the EU has strong interests (and which would require the biggest internal efforts on the US side). Based on these assumptions, under a **tariff-only** agreement, EU GDP would rise by 0.10% amounting to a yearly increase of national income of €15bn by 2027, compared to the baseline option. Given the importance of services in bilateral EU-US trade (€269bn, 2011) this option is analysed in addition to the tariff-only policy option. As would be the case for a tariff-only agreement, a **services-only** agreement would lack trade-off possibilities. Consequently, the estimate is based on a conservative set of assumptions. Under such assumptions, EU GDP would rise by 0.01% amounting to a yearly increase of national income of €2.5bn in 2027 compared to the baseline option.

After the political conclusion of the negotiations in December 2011, the GPA revised text and additional market access commitments were formally adopted by the GPA Parties on 30 March 2012, but are not yet implemented. Although part of the WTO framework, the GPA negotiations were de facto bilateral procurement-only negotiations. The U.S. expanded access to their central level entities, including some US Federal agencies, but the ultimate goal of the EU to substantially increase market access on the US sub-federal level could not be reached. Since the coverage and depth of the commitments of the US States could not be expanded, it is unlikely that much additional market access for EU business would be achievable under a

procurement-only scenario, without considering other potential trade-offs in non-procurement trade areas where the US, in particular States, might have offensive interests in the EU market. Consequently, the economic impact of a procurement-only agreement is limited. Based on the data base used for economic model, the EU GDP would rise by 0.02% on a yearly basis and lead to EU income gains of €3.6bn by 2027, compared to the baseline option.

Under the **option of a comprehensive trade and investment agreement** with conservative assumptions, including a 20% spillover effect, according to the model used, GDP would increase in the EU by 0.27% (in 2027, yearly basis) compared to the baseline option. The estimated gains in terms of national income for the EU amount to an increase of €48bn. Most of the gains from the regulatory cost reduction stem from purely bilateral liberalisation. Spillover effects have only a marginal influence on the results.⁵

Under the ambitious scenario, the model predicts GDP increases for the EU of 0.48% compared to the baseline option. For the EU, these estimated gains amount to an increase of national income by €86bn. The table below provides an overview of the impact of the different policy options.

Overview of economic impacts of analysed options

Options analysed	GDP (quantity index), % change	National income, bn euros
Tariff-only agreement		
European Union	0.10	15.376
Services-only agreement		
European Union	0.01	2.540
Procurement-only agreement		
European Union	0.02	3.360
Comprehensive trade and investment agreement (conservative scenario)		
European Union	0.27	48.385
Comprehensive trade and investment agreement (ambitious scenario)		
European Union	0.48	86.453

ANALYSIS OF THE ENVIRONMENTAL IMPACT⁶

We analysed the possible impact of a reduction in trade barriers between the EU and the US on the environment. Impact on climate change is measured as changes in global CO₂

⁵ A sensitivity analysis undertaken shows that a hypothetically assumed spillover of 10% is predicted to lead to GDP increases of 0.25%.

⁶ It has to be noted that in line with the WTO rules, the EU usually includes general exceptions in its trade agreements with respect to the environment and public health, which can legally override the trade obligations. The EU and the US will therefore keep its "policy space" with regards to these matters.

emissions. The negligible trade effects expected from the baseline option will have correspondingly negligible effects on the environmental dimension. Tariff-only, services-only or procurement-only agreements options can realistically be assumed to have limited negative impacts on the environmental dimension. In fact, as a consequence of reduced production in third countries, the tariff-only option will lead to a decrease in CO2 emissions by 0.02%.

Even under the most trade enhancing policy option, the impact on global emissions is limited (11m tonnes CO2, 0.07% of the current annual rate compared to the baseline in the most ambitious scenario). The main changes are expected in the US (3.9m tons) and the EU (3.6m tons), due to growth in these economies, and China (4.3m tons) through enhanced sourcing. Other parts of the world see either a rise or a dampening of their emissions, but impacts are limited.

An estimation of the natural-resources-use-intensity based on the sector input-output relations predicts only a minimal increase (0.01%) of the intensity.⁷

THE SOCIAL IMPACT

In line with the limited or negligible expected economic impact of separate agreements in individual areas, a tariffs-only agreement could be expected to have a positive impact on skilled and non-skilled wages in the EU, but significantly below those of a comprehensive trade and investment agreement (0.12% compared to between 0.30% and 0.50% under the comprehensive option). At the same time, services-only or procurement-only agreements would, in isolation from an agreement in other areas, provide only negligible benefits in terms of wages.

In the comprehensive scenario, the EU would benefit from increases in wages of skilled and unskilled workers. Wages of unskilled workers are expected to rise in the EU, between 0.30% (conservative scenario) and 0.51% (ambitious scenario), compared to the baseline scenario. The wages of skilled workers are expected to rise in the EU, between 0.29% (conservative scenario) and 0.50% (ambitious scenario). Hence, the expected benefits are very similar for skilled and unskilled workers, but it is noteworthy that contrary to the usual perceptions, also unskilled workers derive a positive income dividend in terms of higher wages.⁸

PREFERRED POLICY OPTION

There is a clear-cut case for the EU to enter into negotiations of an ambitious and comprehensive trade and investment agreement.

As outlined in the analysis of the Impact Assessment Report and in line with the different expert studies,⁹ most of the economic gains can be obtained from the reduction of Non-Tariff Measures. A higher reduction of NTMs facilitates more economic growth and thus leads to larger welfare gains and the creation of more business and job opportunities, including for

⁷ In the model used, the natural resource use intensity depends on the input-output relations between the different sectors and to the extent that this leads to changes in the size of the agriculture, forestry and fisheries sectors. An increase of agriculture, forestry and fisheries sectors leads to more intense natural resource use, a decrease of these sectors would lead to a less intense use of natural resources.

⁸ This can be explained by the strong output growth in sectors that are engaged in physical production activities such as the car sector (strong growth in the EU) or the other machinery sector (strong growth in the US).

⁹ Ecorys 2009 and CEPR 2013.

SMEs. Accordingly, the ambitious scenario performs better when weighed against the criteria of effectiveness, efficiency and coherence and it creates more benefits with regards to the simplification of administrative burdens.

As a result of an ambitious EU-US trade and investment agreement, all regions of the world will see welfare gains in terms of increased national income. These global welfare gains, if used for environmentally friendly purposes, should easily allow for the compensation of possible limited negative effects on the environment.

While it is clear that some countries and regions will benefit more in relative economic terms, if trade barriers are dismantled bilaterally, an ambitious trade and investment agreement between the EU and the US is expected to raise total world income by €238bn of which €86bn are expected to materialise in third countries. Such an initiative can reasonably be described as substantially supporting the world economy.
