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THE TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP: WHY DOES IT MATTER?

What is being proposed?

On 13 February 2013 the United States and the European Union announced their intention to launch negotiations on a "high standard" Transatlantic Trade and Investment Partnership (TTIP). The stated goal is to expand bilateral trade and investment between them, creating an economic stimulus from the resulting structural reform and giving a boost to growth and jobs. The prospective partners have also said that they aim to "contribute to the development of global rules that can strengthen the multilateral trading system."

The stated priorities for negotiation include the removal of remaining tariffs, lowering barriers to investment, liberalising public procurement markets, and aligning rules and technical product standards.

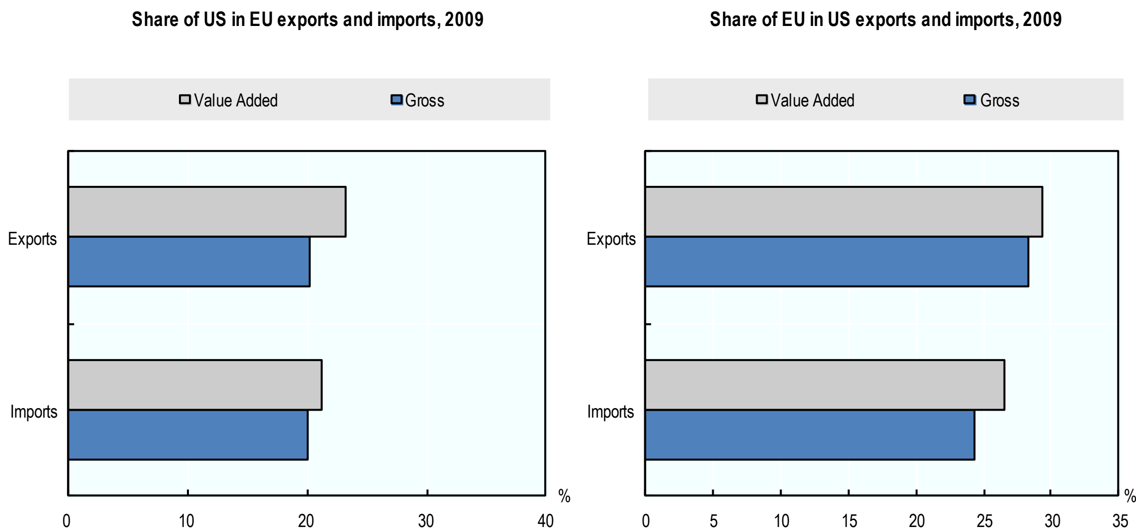
Why is this proposal attracting attention – even *before negotiations start?*

If successfully concluded, this would be the most significant bilateral Free Trade Agreement (FTA) to date, covering approximately 50% of global output, almost 30% of world merchandise trade (including intra-EU trade, but excluding services trade), and 20% of global foreign direct investment.

The United States and the European Union are each other's primary investment and trade partners. In 2012, 63% of US FDI went to the European Union and 44% of FDI inflows to the United States originated from the European Union. Bilateral investment flows between the United States and European Union generated a fifth of all international merger and acquisition (M&A) activity. The US accounts for 20% of EU exports and 20% of EU imports (excluding intra-EU trade), while the European Union accounts for 28% of US exports and 24% of US imports.

Measured in value added terms transatlantic trade flows are even more important than when measured in gross terms. The United States receives 23% of total EU exports and provides 21% of EU imports on a value added basis, while the European Union accounts for 29% of US exports and 27% of US imports (Figure 1). In other words, the United States is by far the most important destination of EU value-added and the United States is by far the largest supplier of value-added in EU imports.

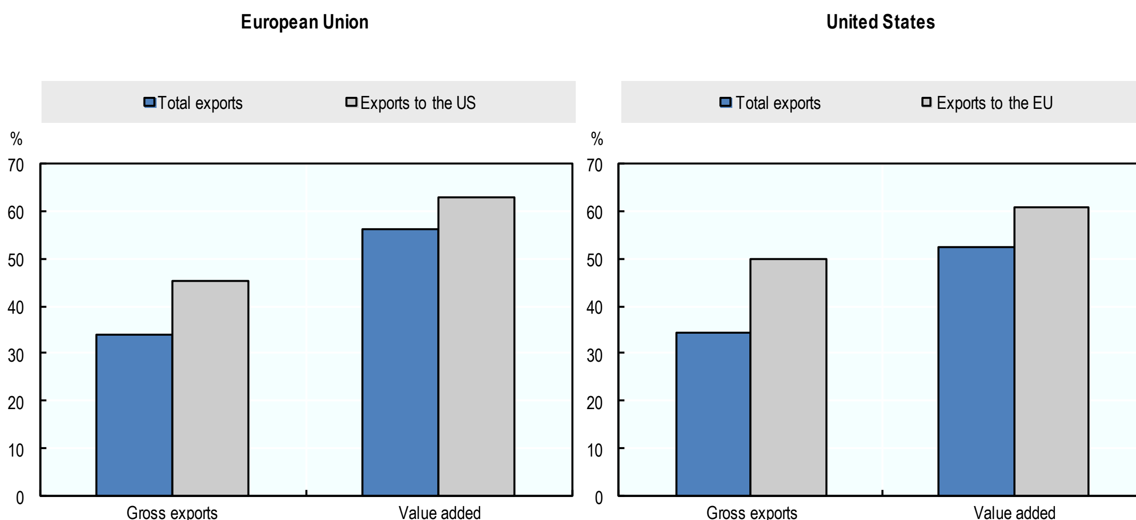
Figure 1. Partner shares in gross and value added terms, as a percentage of total exports and imports, 2009



Measuring trade in value added also reveals the hitherto underestimated importance of services which, on a gross basis, represent about one-third of EU and US total exports (Figure 2). The services share in value-added exports of the United States jumps to 52% and that of the European Union to 56%. In the United Kingdom, France and Spain the share of services is even higher. Moreover, the share of services in value-added trade is higher in trade between the European Union and the United States than it is with other trading partners: 63% of EU bilateral exports and 61% of US bilateral exports.

This argues in favour of an ambitious agenda, consistent with the aims expressed by the parties in February, going behind the border and cutting unnecessary costs wherever they occur along the value chain. Non tariff measures that regulate the production and trade of goods and services should be central to this effort.

Figure 2. Services as a share of gross exports and value added exports, 2009



What are the potential benefits?

The answer depends entirely on the level of ambition actually achieved.

- On tariffs, the goal is to get as close as possible to the removal of remaining duties on agricultural and industrial goods, although it has already been agreed that the most sensitive products will receive “special treatment.”
- In services and investment, the ambition is to go at least as far as in existing US and EU trade agreements. In addition, services liberalisation will be sought in new sectors such as transport. Importantly, services negotiations are planned to address sub-federal levels of government.
- On government procurement, the goal is to achieve further market opening at all levels of government.
- There is a high level of ambition to reduce non-tariff barriers by removing measures that create unnecessary costs and delays for trade, for example by introducing mutual recognition of standards and procedures. The negotiations are expected to address regulatory compatibility in sectors such as chemicals, automotive, pharmaceuticals, health and medical appliances.
- The negotiations are expected to address divergences in intellectual property rights regimes.
- In agriculture there is potential for very real gains, for the FTA parties and for others, if current forms of protection were to be lowered or removed.
- Social and environmental aspects of trade will also be addressed based on what is already developed in existing trade agreements of the two parties.

Given that traditional trade barriers are already low between the United States and the European Union, existing studies suggest that most of the benefits from an eventual agreement will come from easing behind the border impediments to trade and investment. For example, substantial benefits would be reaped if public procurement both in the United States and the European Union were opened, at all levels of government. Fiscal savings from reductions in the cost of procurement would be expected, even in the very short term.

An earlier OECD study estimated that potential welfare gains to the European Union and the United States could be as large as 3 – 3.5% of GDP. Other studies estimate gains ranging from 0.5 to 3.5% of annual GDP, while one study even puts these gains at as high as 13% for the United States and 5% for the European Union. With both economies facing a long term need for fiscal consolidation alongside persistently high unemployment, these gains are considerable, all the more so because no additional spending or borrowing will be needed to achieve them.

None of these estimates capture the potential dynamic effects of trade and investment liberalisation and resulting productivity growth, which are notoriously difficult to estimate accurately. Many commentators believe that these are, in fact, the most important potential gains but they have not been captured in any of the studies done so far.

Trade between the United States and the European Union is to a large extent of an intra-industry and intra-firm nature, suggesting that one effect of TTIP is more likely to be changes within existing value chains rather than re-location of whole industries (which would be more typical of an FTA between countries engaging in more inter-industry trade). This already high degree of market integration argues for an aggressive "problem solving" approach to remove all unnecessary and costly bottlenecks to trade and investment.

The resulting reductions in costs will, of course, benefit businesses and generate growth and employment in the United States and the European Union. But more efficient regulatory regimes in the United States and European Union, by their very nature, are not discriminatory and could also benefit trading partners who are not direct parties to any eventual agreement.

The overall benefits, then, are likely to be both larger and more widely distributed than the purely bilateral actions would suggest.

Is TTIP good or bad for the multilateral trading system?

The United States and European Union do not only have an important bilateral relationship, they are principal export, import and investment destinations and sources for many third countries. An ambitious agreement could conceivably become the "gold standard" for deep and comprehensive global trade and investment integration. Negotiations between these two major players at similar levels of development arguably have the potential to address a wider range of sensitive issues than the stalled WTO negotiations. In this respect an ambitious agreement could be a building block for future multilateral initiatives, in much the same way as today there is interest in multilateralising "WTO-plus" provisions of existing RTAs. On the other hand, an agreement that offers little new trade and investment liberalisation, at and behind the border, would merely add one more to the hundreds of bilateral and regional arrangements that already exist.

Transparency will also be a key element in ensuring TTIP contributes to rather than detracts from an effective, rules-based multilateral trading system. Given that regulatory matters are expected to be at the heart of any eventual agreement, transparency in the way regulations are made and implemented will allow other countries, not party to the agreement, to consider whether and how to "opt-in". Some regulatory measures, such as improved border procedures and more effective anti-corruption provisions, are non-discriminatory by nature and offer benefits far beyond the borders of the European Union and United States themselves.

An eventual agreement could also be made open to other participants willing and able to agree to the provisions. In the investment field, the United States and the European Union are already bound by the MFN obligation under the OECD Codes of Liberalisation: any liberalisation measures which result from TTIP should be extended to other adherents to the Codes.

Extending mutual recognition of standards to third countries, with which either the United States or European Union has already reached a comparable agreement, is another possible way of ensuring that the benefits of TTIP are extended more globally.

TTIP, and other bilateral and plurilateral arrangements, are clearly a second best option to multilateral trade and investment opening. But as a practical matter, when progress is stalled multilaterally, governments can and will pursue other avenues. As an equally practical matter, these second best options can be supportive of an effective multilateral trading system if they are ambitious, break new ground in sensitive areas, keep participation as open as possible, and are amenable to multilateralisation.

Realistically, can such a “high standard” agreement be achieved?

This remains to be seen of course. The February announcement by the United States and the European Union was appropriately ambitious, focusing on the remaining impediments to trade and investment both at and beyond their borders. At the same time, there was explicit recognition of sensitive and often long-standing areas of difference. Mutually acceptable solutions in some areas may remain elusive in the short term, but innovative approaches to improving international regulatory collaboration, from mutual recognition agreements to joint consultative bodies, could mitigate differences over time.

What next?

Even while work continues in preparation of the WTO 9th Ministerial Meeting in Bali in December, discussions continue on a growing number of large RTAs and plurilateral arrangements, in Asia and Latin America as well as in the United States and Europe. Every effort must be made to ensure that bilateral and regional arrangements become “building blocks, rather than stumbling blocks” to the multilateral trading system and to the central role of the WTO.

OECD is committed to supporting, on the basis of objective analysis, all efforts to build a well functioning, transparent and rules-based, multilateral trading system. Trade and investment liberalisation are essential - and thus far significantly under-exploited — elements of effective structural policy reforms that would contribute much needed economic stimulus to the global economy.

Further OECD analysis will draw upon the recently published trade in value added (TiVA) database, a pending regulatory database covering all major services sectors and services providers, measures of support and protection in agriculture, indicators of trade facilitation measures, structural reform priorities identified in the *Going for Growth* initiative, and pending new product market regulation indicators. The aim is to provide further insights on practical actions that governments could take to ensure that trade and investment opening contributes to strong, sustainable and balanced growth. The more that trade policy and appropriate accompanying measures can trigger desirable structural reforms, the larger will be the benefits for growth and employment.

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