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Time to re-think the EU trade policy

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As of 2017, the EU has 44 trade agreements in place with more than 60 countries across the globe. In addition, five accords have been finalised but are not yet being applied (with East African countries, Ecuador, Singapore, Vietnam and West Africa).

Notwithstanding the EU's comparative advantage in building trade relationships worldwide, the combination of competency issues between Brussels and Member States and rising discontent towards globalisation seriously risks undermining the Union's Common Commercial Policy.

Thus, in order to avoid a worst-case scenario of paralysis and increasing irrelevance, European institutions and Member States should amend the 2009 Treaty of Lisbon by reviewing the mixed approach. This move will strengthen the 2015 "Trade for All Strategy" and will lead to a more effective and functional common commercial policy.

Introduction

On 14 October 2015, the European Commission launched its new trade and investment strategy: Trade for All (EC, 2015). The relative success of this agenda, the recent reinforced commitments to speed trade talks up and the willingness to start negotiations with countries such as Australia, Chile and New Zealand have been hailed by European policymakers as a victory.

Yet, there is nothing to be complacent about. Current legal challenges, rising concerns about potential weakening of standards and the increasing discontent towards globalisation seriously risk undermining the EU's Common Commercial Policy (CCP). In fact, the combination of competency issues and growing dissatisfaction with 2nd generation comprehensive trade agreements might lead the EU trade strategy to a worst-case scenario of paralysis and increasing irrelevance.

The important legal case over the EU-Singapore FTA

The EU and Singapore completed the negotiations for a comprehensive free trade agreement (EUSFTA) on 17 October 2014. At the moment, the deal is still pending formal approval by the European Commission, agreement by the Council of Ministers and ratification by the European Parliament (EC, 2017). However, on 16 May 2017 the European Court of Justice (ECJ) delivered a final opinion on the deal, arguing that EUSFTA can only be concluded by the EU and the Member States acting jointly (Euractiv, 2017).

Singapore is the EU's 17th largest trading partner and for many EU exporters it is the main hub to serve the ASEAN region. ASEAN is a growing market of around 625 million people, with an annual real growth rate of 5.3% between 2007-2015, and attracted US$121 billion, or 7% of total global FDI inflows in 2015 (ASEAN, 2017).

The latest ECJ ruling will have a profound impact on EU trade policy. Specifically, the Court has decided that EUSFTA should be classified as a mixed agreement and not as an EU-only trade deal. As the Treaty of Lisbon explains, EU-only agreements require a simple ratification by the European Commission, the Council of the EU, and the European Parliament, which, in this case, acts on behalf of the 28 Member States. By contrast, mixed agreements require ratification by both EU institutions and Member States, creating a lengthy and unstable approval process. The recent EU-South Korea FTA and the EU-Canada deal provide clear evidence of this.

The ECJ decision can also be seen as bad news for both European institutions and the UK, which will soon intensify their Brexit talks to achieve a new comprehensive FTA. In fact, whilst it was already very difficult to imagine the EU and the UK reaching a good trade deal within the two-year negotiations window, it now seems even more difficult to do so. In effect, the latest ECJ ruling has simply underscored how weak and confusing the current EU's CCP is.

The EU-South Korea FTA was signed on 15 October 2009 and it has been provisionally applied since 1 July 2011. This treaty was the first 2nd generation comprehensive FTA the EU had never negotiated. On top of tariffs and duties elimination, the agreement included provisions for intellectual property, public procurement, competition, transparency of regulation and sustainable development as well as specific commitments against non-tariff obstacles on sectors such as automobiles, pharmaceuticals and electronics. However, due to its mixed nature, the ratification process was completed by all EU Member States only in late 2015, exactly six years after it was signed (Council of the EU, 2015).

The EU's trade policy is unfit for 21st century FTA

EU total trade in goods increased by 57% from 2005 to 2015 and services surged by 94%. The EU share in world trade (14.7% for trade in goods and 22.2% for trade in services in 2015 compared to 17.5% and 24.1% in 2005 respectively), declined due to the economic crisis and the growing importance of emerging economies (Wruuck, 2017).

The EU's Common Commercial Policy (CCP) has evolved over the years and the 2009 Treaty of Lisbon has de facto strengthened the EU's powers on trade, notably in services, some aspects of intellectual property rights and foreign direct investment. However, whilst article 207 of the Lisbon Treaty makes FDI an exclusive EU competence, it still remains too ambiguous when it comes to other forms of investment (e.g. portfolio investment). That is why, in order to clarify the situation, in October 2014 the Commission requested the opinion of the European Court of Justice on the competence of the EU to sign and conclude the deal with Singapore (EC, 2014).

Thus, in light of the latest ECJ decision and the ongoing Brexit negotiations (Webb, 2017), a number of structural weaknesses have re-emerged. In fact, the legal question of competency undermines not only the credibility of the Union to stipulate commercial treaties with third countries in a relatively short period of time, but it has also enabled anti-trade groups to gain ground and to capitalise on people's fears, such as a lack of European institutions' democratic mandate and a lack of transparency (Wruuck, 2017).

As Kleinmann and Kübek (2016) write, the recent Wallonia saga exemplifies well the risks of paralysis and increasing irrelevance for the EU trade policy. On the one hand, the fact that a constituency of 3.5 million inhabitants was able to credibly threaten to block a treaty supported by the political representatives of 500 million EU citizens has reinforced existing incentives for political blackmail, rent-seeking behaviour, and, eventually, political paralysis of EU multi-level economic governance. On the other hand, it highlighted how, despite European policymakers' rhetoric, the EU Common Commercial Policy is unable and unfit to effectively deal effectively with 21st century comprehensive FTAs.

If the EC and the remaining 27 Member States are not able to re-think and reform EU trade policy, the Union might sooner or later lose its ability to act in a policy area where it has a strong comparative advantage compared to other rich and open economies, such as the United States. As of today, in fact, the EU is the top trading partner for 80 countries. By comparison the US is the top trading partner for a little over 20 countries (European Commission, 2014).

Trade makes European countries better off

Compared to 1995, the export-supported employment increased in almost all Member States. The Member States with the strongest increases in relative terms between 1995 and 2011 were Luxembourg (296%), Ireland (187%), Malta (147%), Greece (126%), Spain (126%) and Austria (121%) (EC, 2015).

Contrary to conventional wisdom, trade makes the EU richer and more prosperous. According to a study by the European Commission (2015), between 1995 and 2011, EU jobs supported by exports to the rest of the world increased by 67%, to reach 31.1 million. This means that in only 16 years, trade has been the major cause of the creation of some extra 12.5 million jobs.

Moreover, as standard economic theory suggests, trade agreements do increase trade among nations. For example, recent studies by Khol (2014) and Handley and Limao (2015) find evidence that deeper and more comprehensive agreements tend to be more effective and that credible preferential trade agreements can increase trade even if applied barriers are already low.

A good example of the benefits derived from 2nd generation trade agreements comes from the EU-South Korea deal, the first comprehensive FTA signed by the Union. Although only provisionally applied from July 2011 to October 2015, EU exports to South Korea have increased by 55% in the fourth year of FTA implementation, compared to the 12-month period before the FTA took effect. In particular, EU exports of fully liberalised goods increased by 57% and those partially liberalised by 70%. At the same time, imports of fully and partially liberalised goods from South Korea increased by 35% and 64%, respectively (EC, 2017).

Conclusion

Following the latest ECJ's decision, European policymakers have a great opportunity to re-think the Union's trade policy. The timing could not be more propitious, too. Current negotiations with the UK, recent difficulties in ratifying 2nd generation comprehensive agreements and the increasing discontent towards globalisation do pose a significant challenge for EU trade policy. As suggested by the latest White Paper on the future of Europe (scenarios 4 and 5) (EC, 2017), Member States should quickly move towards an EU-only trade policy. This will mean transforming the current CCP into a proper, more effective, more functional trade strategy.

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