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TTIP – Opportunities and Risks for Developing Countries

Contributions in International Journals and Think Tank Publications 2013–2014
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Since 2013 the European Union and the United States have been negotiating a Transatlantic Trade and Investment Partnership (TTIP). Such a deal would create the world's largest free market and impact significantly on developing countries and the world trade system. Numerous authors discuss the expected effects, with strongly diverging assumptions leading to very different findings. Supporters of TTIP hope for significant prosperity gains, opponents fear grave disruptions in labour markets and the world economy. Overall, there is great concern about negative net effects on third countries not involved in the talks.

As well as trade in goods, TTIP sets out to liberalise the service sector, create a positive climate for investment, and further open public procurement markets. During the past two years the planned agreement has triggered lively discussions and criticism. A number of published studies on TTIP work with strictly economic assumptions and econometric models. They produce concrete, quantified results that are valid only under the assumptions of the model in question. As a rule it is presupposed that the goals of the talks (such as abolishing all customs duties) will actually be achieved. The potential benefits of the agreement consequently tend to be overestimated.

Most of the contributions, however, steer away from a strict analytical framework. In some cases this is a deliberate choice, driven by a certain scepticism as to whether the formulated assumptions can actually produce viable pointers to real outcomes. These should be understood as political contributions, although depending on their standpoint they are sometimes also based on restrictive and in some cases even contradictory assumptions.

Trade and Social Welfare Effects in Third Countries

If TTIP comes into effect, the European Commission forecasts considerable additional growth for the European Union (€119 billion/year) and the United States (€95 billion/year). The trade volume of third

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countries would also increase, and their GDP could rise by almost €100 billion. So even countries not involved in the talks would profit from TTIP. In a study for the German Federal Ministry for Economic Affairs (**Felbermayr et al.**), Ifo-Institut predicts a long-term increase in global prosperity of 3.3 percent. Another study (**Felbermayr, Heid and Lehwald**) for Bertelsmann Stiftung considers two scenarios: firstly, liberalisation of all customs duties, and secondly an even deeper liberalisation encompassing a simplification of rules and standards and other steps. Although the authors find worldwide gains in the first scenario, the results vary widely between countries. Reciprocal tariff liberalisation by the United States and European Union (in other words, granting trade preferences within the planned free trade area) would toughen competition for third countries in the EU/US market where they remain subject to the usual tariffs. For this reason the big losers of a dismantling of tariffs are developing countries – in particular Ivory Coast and Guinea, but also Uganda, Tanzania and others – which would experience dramatic losses of market shares as their exports to Europe were displaced by competition from the United States. But there would also be winners profiting from indirect effects, such as Brazil, Kazakhstan and Indonesia. In the second scenario (deep liberalisation through TTIP), large aggregated gains would be expected, with mean global per capita income increasing by 3.27 percent. Losses in third countries would be distributed differently than in the first scenario: Traditional US trading partners such as Mexico, Canada, Chile, Australia, Japan and Israel would be the main losers. That, however, is based on the (unrealistic ceteris paribus) assumption that standards and regulations in the affected countries are not adapted to the new circumstances in the EU/US market. As a result the negative effects are probably overestimated.

In a study for the British Department for International Development, **Rollo et al.** investigate the effects of TTIP on low-income countries (in other words a much smaller group than those analysed in the aforementioned studies). Although they point to the problem of erosion of trade preferences for certain countries and products (fish, bananas, sugar), they argue that the overall danger of export losses is small for this group, because the European Union and the United States are already unable to compete with them in the areas where the highest tariffs apply (textiles, clothing, shoes). Although there would be a theoretical risk of trade diversion for Bangladesh, Pakistan and Cambodia, the authors assert that such effects are not to be expected. The reason for this finding might be that, given the sectors involved, the poorest countries are not competing directly with the European Union in the United States or vice versa. Even within the textile and clothing sectors, Bangladesh and the United States serve different segments of the European market. **Rollo et al.** foresee no grave consequences even for smaller low-income countries, because their exports to the European Union and the United States are dominated by raw materials or products with low customs duties, which would not be affected at all by TTIP.

Effects in the Field of Standards

Technical, sanitary and phytosanitary standards are an important aspect of the planned agreement. When it comes to the effects of the mutual recognition or harmonisation of standards sought under TTIP, opinions diverge in some cases. According to certain studies (**Rollo et al., Bertelsmann Stiftung, Freytag et al., Berger et al.**) this field contains great potential for simplification and cost-saving that would benefit all countries. The reciprocal recognition of rules by European Union and United States could also be open to third countries. Their exports to these important markets would then only have to fulfil the standards of one market and they would no longer have to deal with different standards in the Euro-

pean Union and the United States. The same applies to harmonisation of standards, although these would initially incur adjustment costs because existing EU and US standards would have to be modified (**Rollo et al.**). In this connection **Freytag et al**. point to the centrality of conformity assessment systems which, they say, are necessary in order to profit from the advantages that arise. For conformity assessment, a recognised institution must confirm that the product in question meets the set criteria. This faces developing countries with great challenges, because they generally possess a less developed quality infrastructure and often lack such recognised institutions. **Rollo et al.** also mention the difficulties developing countries would find themselves exposed to if sanitary and phytosanitary standards were tightened in the course of a harmonisation between European Union and United States. This, they say, would affect numerous African countries including Ghana, Kenya, Nigeria, Burkina Faso and Burundi.

Falk and Unmüßig apply the opposite assumption in their contribution for Heinrich-Böll-Stiftung – namely, that TTIP would lower rather than raise standards – and conclude that this would ease market access for developing countries. But the Green Party's principled goal of raising standards would, they argue, have to be pursued at the multilateral level. **Jäcklein** in *tageszeitung* also emphasises the danger of TTIP watering down standards and fears that the EU will abandon its "precautionary principle" in favour of the legal remedies favoured in the United States. A press release from **Attac** speculates that "chlorinated chickens", hormone-fed pigs and GM maize could overrun the European market. Finally, **Wallach** (also in *tageszeitung*) points out that concerns about unsafe and unhealthy products flooding the domestic market exist in the United States too, in particular in relation to drug safety and toys (from the European Union). America fears the imported "salmonella chicken" just as much as Europe loses sleep over the "chlorinated chicken".

Effects on the Multilateral System

There are also contradictory views about the effects of TTIP on the multilateral system. As well as the aforementioned additional growth, **Felbermayr et al.** emphasise that less regulation is normally positive, also for the international system. But substantial gains in prosperity are, they say, only possible if trade barriers are dismantled – and that is inconceivable within the WTO framework. The multilateral approach is, they argue, therefore no alternative to a deep regional agreement – and this could actually benefit third countries. There is something to be said for this theory: reciprocal recognition and harmonisation of standards also ease market access for third countries. Simplified customs procedures and border controls (trade facilitation) also directly benefit exporters from other countries. The simplification of provisions relating to export of services (such as visa rules) can also be extended unproblematically to third countries, while improved transparency in public procurement benefits all bidders. The relative importance of the trade-restricting effects of such rules and standards has increased strongly in recent decades as customs duties have fallen globally. The chances that a free trade agreement addressing non-tariff trade barriers will benefit all have therefore risen.

Freytag et al. supply another argument why the conclusion of "mega-regionals" like TTIP should have advantageous effects on the world economy: partners not affected by the agreement are generally strongly integrated into international value chains. That means, they argue, that tariff reduction in a free trade area like TTIP no longer necessarily discriminates against third countries, because products exported from the European Union to the United States or vice versa also contain generally a high share of value from third countries.

Others suspect that TTIP will cause great harm to the world economic system. **Falk and Unmüßig** interpret the agreement (together with the TPPA) as an attempt to

establish a new world economic order under EU and US tutelage, and argue that lack of influence on TTIP pressurises emerging economies to step up their multilateral engagement. **Dieter** (Stiftung Wissenschaft und Politik) contests the assumption that TTIP could advance global rule-making on the grounds that the Chinese government will not accept rules from whose formulation it has been excluded. The assumption itself is unconvincing, he argues, because it ignores Beijing's growing weight and confidence.

Hermisson (Heinrich-Böll-Stiftung) formulates the central question as: "Do we want to join in actively shaping globalisation – or withdraw into national or regional spaces?" He concludes: "Isolationism in Europe is not only an economic illusion, but a politically dangerous undertaking." Green Party demands, he believes, should not be restricted to simply stopping TTIP.

Freytag et al. point out that TTIP could potentially lead to diversion of investment, with investors outside the free trade area gaining an incentive to invest within it in order to avoid the tariffs of the expanded transatlantic market. Such a diversion could, they argue, also reduce the flow of investment to developing countries.

There is disagreement over the question of who might benefit most from TTIP. **Felbermayr et al.** argue that reducing non-tariff trade barriers would be most helpful to smaller and middle-sized businesses, whereas the biggest firms – which already export to the United States – would remain largely unaffected. The **World Development Movement,** on the other hand, asserts that TTIP is about multinational corporations exploiting a global trade and investment framework to further expand their power. The predicted benefits for the world economy are exaggerated, it says, and even where they arose they would not benefit ordinary people.

Investor-State Dispute Settlement

The main object of criticism is investor-state dispute settlement (ISDS). As **Bréville and Bulard** explain in *tageszeitung*, more than three thousand bilateral and free trade area agreements worldwide protect foreign companies from the consequences of state decisions (in the form of laws, regulations and norms) that could impair their investment. Here the last word is not with national regulators and local courts, but supranational arbitration courts that to date, the authors assert, have mainly penalised countries in the Global South. Three of the four complaints heard before the International Centre for Settlement of Investment Disputes (ICSID) were lodged by the United States and the European Union. "Of the 244 cases decided by the end of 2012, 42 percent ended with a win for the state, 31 percent with a win for the investor and 27 percent with a compromise," report **Bréville and Bulard**. Most of the lawyers and arbitrators involved in investor-state dispute settlement, they say, come from a group of about twenty (mostly US-based) law firms. But their examples demonstrate that today complaints may also be lodged against the governments of industrialised countries – Vattenfall v. Federal Republic of Germany over the nuclear shutdown being a case in point.

The most problematic aspect of ISDS is that different rules apply to domestic and foreign investors (**Langhammer, Verbraucherzentrale Bundesverband, Eberhardt**), as it permits foreign businesses to take the German government to the court of arbitration, while domestic businesses are obliged follow German legal channels. **Langhammer** underlines the importance of reforming investment protection agreements such that supranational arbitration courts can only be called where foreign investors are recognisably disadvantaged vis-à-vis domestic counterparts. **Verbraucherzentrale Bundesverband** also criticises this "reverse discrimination" and calls for the investment protection chapter to be dropped from TTIP.

Eberhardt is not alone in warning that ISDS narrows the policy space of democratically elected governments. **Attac** demands that banks and corporations be given no new rights to take states to private arbitration courts, in order to prevent them subverting democratic political decisions.

The fact that most complaints to date have been lodged by corporations from the United States and the European Union supports the suspicion of critics that the transatlantic free trade agreement is now supposed to cement this system firmly into place as the global model. This supposition gains credence from a statement by EU Trade Commissioner **De Gucht** in Berlin (as reported by **Greive** in the *Welt*) that it would be problematic to omit the investment protection clauses from TTIP because that would complicate other trade talks, for example with China.

The period of public consultation granted by the European Commission in the spring opened the possibility to introduce positions on investor-state dispute settlement into the European discussion process. Hopefully the passionate debates of recent months will enhance transparency and aid substantive clarification. **Bundesverband der Deutschen Industrie** (BDI), which argues for robust investment protection, nonetheless wishes to use the TTIP talks to push for reforms: protection of the government's right to regulate, greater transparency in ISDS cases, narrow definition of central terms like "indirect expropriation", establishment of an appeals procedure, and protection from inadmissible complaints. That way, the BDI argues, TTIP could become the "gold standard" for other investment protection agreements. To **Eberhardt**, on the other hand, these would represent only minor modifications to the existing mechanism and would be unsuited to addressing the central problems. She argues for future investment protection agreements to do without arbitration systems. Also, she argues, agreements must place binding social and ecological obligations on investors.

The **Economist** (10 October 2014), also argues that reform should go further. It cites the World Trade Organisation, where only states can bring complaints, as a good example, because firms must first convince their governments that trade rules have been breached. The proceedings are run like trials, open to public scrutiny, and subject to appeal. The **Economist** concludes "Firms need protection; but so does the right of governments to pursue reasonable policies."

Bréville and Bulard point out that as it stands presently, only developing countries are affected by any negative consequences of investment protection, such as demands for compensation and the associated erosion of government power to enforce social, ecological and consumer protection rules. If TTIP is signed, however, European governments and the US Administration would also have to fear action: another reason why the proposals for the TTIP investment chapter are likely to be intensely scrutinised and in certain aspects – in comparison to existing agreements – revised. The heated discussion over the TTIP investment chapter and a possible agreement between European Union und United States on revised and additional formulations could also lead to stronger questioning of provisions in existing investment protection agreements with developing countries.

Recommendations for Developing Countries

How can developing countries ensure that they derive the greatest possible benefit from the emergent transatlantic agreement? **Felbermayr, Heid and Lehwald** emphasise that if a comprehensive agreement is concluded, additional economic growth in the European Union and the United States will generate enough wealth to compensate any losers. At the same time they hope that TTIP will inject new momentum into the WTO trade talks and increase the willingness of developing countries and

emerging economies to make concessions in the Doha Development Round. The idea is that these countries will be interested in global liberalisation to ameliorate the negative consequences of TTIP. According to the **Felbermayr, Heid and Lehwald** the industrialised countries should also be willing to compromise (at the multilateral level) because a major deepening of economic relations between the United States and the EU would generate the required resources. Adjustment processes required by global liberalisation would then be easier to finance.

Rollo et al. recommend that low-income countries demand compensation for possible losses, backed up by the following measures: 1) expansion of non-reciprocal trade preferences (this would largely affect the United States because the EU already grants free market access to the least developed countries); 2) exclusion of their most important products from TTIP; 3) reciprocal recognition for third countries on sanitary and phytosanitary standards; and 4) support for adaptation to higher standards through development cooperation. They also advise these countries, 5) to improve the competitiveness and flexibility of their own economies in order to cope better with externally-driven change. As such, they underline the importance of internal reforms and "good governance". The developing countries could also direct their energies towards a success of the multilateral trade talks, which would bring, **Rollo et al.** argue, greater long-term benefit than lobbying for compensation of the side-effects of TTIP.

In order to better assess the effects of TTIP on developing countries, more country-level analyses at would be useful. These could operate using more concrete assumptions, such as which specific customs duties would probably be included in a TTIP liberalisation and how this might affect the competitive situation of a country's export products in the EU/US market. They could also investigate which technical, sanitary and phytosanitary standards affect the export products of a particular developing country in the TTIP market and to what extent that country's quality infrastructure would be in a position to respond to changes in these standards. Only on the basis of such country analyses will developing countries be able to draw specific conclusions for their own positioning and preventive policy.

The effects of TTIP on developing countries will depend on what is actually agreed between European Union und United States. The difficult start to the negotiations suggests that there is unlikely to be a sweeping abolition of tariffs between the EU and the United States, and the two sides are far apart on many aspects of standards. To that extent the assumptions of the discussed studies are unrealistic and the findings of their calculations overoptimistic – not to mention that the original schedule for completing the talks by 2015 appears utopian. This also corresponds with the assessment of the former EU Trade Commissioner, now WTO Director-General **Pascal Lamy**, who said that the opponents of TTIP could sleep soundly because it would be many years before it was concluded. One might add that the agitation is overblown anyway, because the outcome of the talks will lie somewhere in the middle and the real-world effects will certainly remain moderate. Nonetheless, the studies examined here contain meaningful pointers to possible consequences of an agreement and direct attention to areas where TTIP could have critical consequences for individual countries.

Nor will the often overstated assumptions of the more political contributions turn out true. But they do reveal concerns associated with the agreement, above all in civil society, cast a light on aspects that give grounds for deeper investigation, and supply negotiators with important ideas for their positioning as the negotiations progress. The current public discussion could bring the results closer to societal preferences than is usual in cases with less strong public interest. The debate could also contribute to particular arguments being weighed very carefully. In all likelihood this will improve the quality of the outcome.

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