

Evenett, Simon J.

## Article

# Must EU Trade Policy Be Entirely Reactive?

Aussenwirtschaft

## Provided in Cooperation with:

University of St.Gallen, School of Economics and Political Science, Swiss Institute for International Economics and Applied Economics Research

*Suggested Citation:* Evenett, Simon J. (2010) : Must EU Trade Policy Be Entirely Reactive?, Aussenwirtschaft, ISSN 0004-8216, Universität St.Gallen, Schweizerisches Institut für Aussenwirtschaft und Angewandte Wirtschaftsforschung (SIAW-HSG), St.Gallen, Vol. 65, Iss. 4, pp. 343-351

This Version is available at:

<https://hdl.handle.net/10419/231206>

## Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

## Terms of use:

*Documents in EconStor may be saved and copied for your personal and scholarly purposes.*

*You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.*

*If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.*

## **Must EU Trade Policy Be Entirely Reactive?\***

Simon J. Evenett

University of St. Gallen and CEPR

EU trade policy has accomplished little of substance during the past decade. This column identifies five reality checks that should be taken on board as the European Commission and the Member States reformulate their approach to commercial relations.

*JEL Codes:* F13

*Keywords:* EU trade policy, WTO, Political economy

### **Introduction**

The twenty-seven member states of the European Union pool their sovereignty on commercial policy matters, with the European Commission negotiating on their behalf. This institutional arrangement – representing over 10 trillion US dollars of spending power per annum and several trillion dollars of overseas investments – ought to confer upon EU negotiators substantial clout. Yet, the EU has closed few trade deals during the past ten years. This clout could not bring the Doha Round to conclusion. Nor have many regional trade agreement (RTA) negotiations been completed. Moreover, the benefits from the few accords that have been signed have fallen far short of initial expectations. No doubt the European Commission has blocked proposals counter to the EU's interests, but is the future of EU commercial policymaking to be entirely reactive?

Of course, some events cannot be anticipated and may call for a trade policy response. In this sense, some elements of EU trade policy must be reactive. Recent developments in North Africa – with their potential to change the direction of economic policy in hitherto dominated by ruling families and associated local and foreign associates – are a case in point. One cannot blame European trade policy officials for not anticipating these developments. It is, however, fair game to assess any changes in commercial policy motivated by such events.

The purpose of this article is to question several of the tenets of current EU trade policy. The discussion is organised around five reality checks precise-

---

\* An abridged version of this article was published on voxEU.org in September 2010 under the title “A Future Agenda for EU Trade Policy As if the Real World Really Mattered.”

ly because of the Alice-in-Wonderland character of much current EU trade policy. One consequence of over-selling the effects of enforceable trade agreements is that many parties want to influence EU trade policy. This has resulted in an unwieldy negotiating agenda, poor prioritisation, and diffusion of negotiating capital. More importantly, in a business where finding the basis of a deal with trading partners is central, the EU's priorities are increasingly out of line with the aspirations of the EU's trading partners, especially the larger emerging markets. Too many angels are trying to dance on the head of the pin that is EU trade policy.

### **Reality Check 1: With respect to the WTO “do no harm”**

We all love the WTO but we all know it is in serious trouble. Despite their public statements, Heads of Government are simply not prepared to make the trade-offs necessary to complete an economically meaningful Doha Round. No doubt a mouse could be produced if matters get so bad that we need a Doha Round deal to “save the system”.<sup>1</sup> But, by 2008, it became clear that everyone had learned that there was no basis for a deal.<sup>2</sup>

Thomas Schelling, the Nobel Prize-winning strategist, provides the best way of thinking about the Doha Round stalemate. Schelling showed that if one negotiator was given by its government a very restrictive negotiating mandate then, under some circumstances, other negotiating parties keen to conclude a deal would do so on the former's terms. But Schelling also pointed out that if many governments tied the hands of their negotiators then stalemate was possible.

The contemporary relevance of Schelling's insight can be found in the manner in which the European Council, the U.S. Congress, the Prime Minister and President of China, and the political forces in India have repeatedly shackled their respective trade negotiators on agricultural trade matters. Worse, the same “leaders” then issued disingenuous G20 Declarations calling on their negotiators to complete the Doha Round negotiations. This cynical device is at the heart of the Doha Round impasse and certain EU

1 At the time of writing, another tack is being taken by certain eminent trade experts. Namely, the Doha Round must be completed in so (i) acting as an insurance against protectionism, (ii) to make irreversible certain farm reforms, (iii) to create new market access and (iv) to reinforce the multilateral trading system, and (v) to ultimately allow the multilateral trading system to address matters of greater contemporary relevance. See: HIGH LEVEL TRADE EXPERTS GROUP (2011).

2 Recall the “nothing is agreed until everything is agreed” negotiating rule employed during the Doha Round. Such a rule makes a nonsense of claiming that 80% (say) of the negotiation is complete.

member states bear their share of the blame. Without a substantial offer to reform agricultural support policies, it is difficult to see what the EU can do to revive the WTO's negotiating function (and indeed whether such an offer would be enough).

The failure to conclude the Doha Round isn't the only drain on the credibility of the WTO and the rules-based trading system. Poor choices of dispute settlement cases are too. It appears that some are so besotted with the "power" of multilateral trade rules that they actually believe that governments will be cowed sufficiently by losing WTO disputes that they will bring themselves back into compliance with those rules. The threat of sanctions may affect the incentives to come back into compliance, but that is no guarantee that compliance will occur. In some disputes the commercial interests at stake are so big that compliance is unlikely and the magnitude of sanctions so large that their imposition would significantly disrupt the trade.<sup>3</sup>

The foolishness of bringing the EU-US disputes over subsidies to wide-bodied aircraft to the WTO has been compounded by a recent case to bring a case against China on export taxes for a provision which it alone is legally bound to in its accession protocol. The latter dispute is likely to backfire, allowing the Chinese to highlight the inequities of the WTO accession process and the asymmetries in WTO rules. Moreover, a "victory" here for the plaintiffs will be pyrrhic – for it will only encourage Beijing to retaliate against the commercial interests of the plaintiffs, taking advantage of the fact that WTO accords do not cover every way to harm foreign commercial interests. Of course, the rules don't allow for the loser in a case to retaliate but expecting every government to have respect for the rules is the kind of naivety that a EU trade policy grounded in realism would avoid.

As a vehicle for advancing Europe's commercial interests in the larger emerging markets, the above considerations imply that limits of what the WTO dispute settlement system can deliver have been reached. Bringing highly controversial cases will invite retaliation against EU commercial interests from vengeful losers and will only discredit the DSU system in the eyes of developing country WTO members. Case selection should be handled very careful: "do no harm" being the operative principle. If necessary,

---

3 Worse, in some very significant cases the impression is given that WTO Dispute Settlement is being followed only to alter the "threat points" in a negotiation that will ultimately begin and conclude before any final determinations are issued by the WTO's Appellate Body. One is not naïve enough to suppose that legal systems are not used strategically; the realisation that they are, however, does not necessarily cover either the parties or legal systems involved in glory.

the European Commission and Member States should find some other way to induce foreign governments to change their behaviour.

So what should the stance of the EU towards the WTO be? Of course, the EU is not going to disavow the multilateral trading system. Diplomatic niceties dictate that the EU state that preserving the WTO and finishing the Doha Round are “priorities”. Realistically, though, EU expectations for what the WTO can deliver should be lowered significantly. Some will reject this assessment, arguing that it demonstrates the need for a WTO reform agenda. Perhaps the niceties require EU support for a WTO reform agenda but proponents should think hard about what the Doha Round negotiations and the reaction to the global economic crisis really reveal about certain governments’ willingness to be further bound in legally binding accords and whether those accords can be effectively enforced through WTO dispute settlement. The success of any WTO reform agenda ultimately turns on the latter two considerations.

### **Reality Check 2: RTAs and EPAs are a sideshow**

In its *Global Europe* Communication in 2006 the European Commission committed itself to negotiating a new tranche of Regional Trading Agreements (RTAs) and to completing the Economic Partnership Agreements (EPAs). Far less here has been accomplished than was anticipated at the time. The biggest deal, the RTA with Korea, was supposed to go well beyond the terms of the US-Korea RTA, an objective that no one mentions any more. Meanwhile, the RTA negotiations with India, Mercosur, and the GCC countries proceed slowly. The EPA process remains a public relations embarrassment, made worse by less than judicious interventions from certain EU member states.

EU RTA policy runs into two constraints. First, EU negotiating objectives are far too diffuse, ranging from traditional tariff considerations to new behind-the-border rules to “sustainable development” and a plethora of other non-economic goals. The latter are often wrapped up in patronising language about promoting European values. Second, some of the RTA partners are large enough that they too have demands, demands which the EU probably cannot deliver. (Indian demands for visas being a case in point.) Both factors have eroded, if not eliminated, the basis of the deal in many negotiations. In fact, the EU negotiating package seems best suited for other industrialised countries that have either defensive agricultural interests (Korea)

or are willing to forgo their offensive agricultural interests (Canada). The problem is that there aren't many such countries left for the EU to negotiate RTAs with! As far as the large emerging markets are concerned, little should be expected.

Overall, unless there is a substantial streamlining of EU negotiating demands and occasionally a willingness to make serious concessions to negotiating partners, the EU's RTA and EPA negotiations will remain a side-show. These negotiations may afford opportunities for experimentation but there aren't enough deals in the works to dramatically scale up any innovative provisions.

### **Reality Check 3: Follow the money**

Whatever "grand bargain" the EU has offered trading partners in recent years, there haven't been many takers. The EU would be better advised to go back to the drawing board and identify those matters for which there are substantial supportive constituencies at home as well as in negotiating partners. Such an approach would likely streamline EU trade negotiating priorities as well as focus more attention on whether the really is a sufficient basis for a deal, however codified.

Recent developments in the world economy suggest that this approach might be not only timely but also likely to garner the support of leading lights in the corporate sector. First, a growing number of multinationals are headquartered in emerging markets<sup>4</sup> and run into the same regulatory obstacles and malfeasance abroad as Western multinationals. The recent global economic crisis has exposed much murky protectionism against foreign commercial interests, both developing and industrialised countries. Second, participation in international supply chains requires substantial cooperation between collaborating firms, who are likely to see commercial obstacles in the same light. A trade policy agenda based on extending national treatment principles further into domestic regulations, greater transparency, stronger consultation mechanisms, requirements on scientific and evidence-based decision making by regulators, rights of review for the regulated, and encouragement to adopt common standards or at least, mutual

---

4 The 2010 version of the World Investment Report notes that there are over 20,000 transnational corporations headquartered outside of industrialised countries, approximately 28 percent of the world total. See Internet: [http://www.unctad.org/en/docs/wir2010ch1\\_en.pdf](http://www.unctad.org/en/docs/wir2010ch1_en.pdf) (as of March 1, 2011).

recognition of standards would benefit this growing and substantial corporate constituency.

However, there should be no illusions about how far reaching this agenda could be. The European Commission and its Member States would have to be prepared, in some instances, to alter their domestic regulatory structures. Something-for-nothing won't work as a negotiating tactic here; the list of failed transatlantic initiatives over the past decade indicates precisely what happens when each negotiating party won't contemplate reforming its own regulatory institutions. Undoubtedly the EU would face demands for visas (so that foreign companies can better operate their supply chains in Europe), changes to competition law enforcement (especially as it relates to mergers) etc. Of course, European negotiators would be entitled to advance searching demands of their own. Still, the point remains, the EU will have to determine internally how far it is prepared to go down each of these paths.

That many of the areas of greatest interest to internationally-active business are seen as sensitive in policymaking terms suggests that initiatives here will almost certainly start off as cooperative, non-binding accords. (Given the failings of the multilateral trading system and the limited scope for negotiating RTAs mentioned earlier, binding enforceable approaches offer little realistic prospect of success, at least in the short run.) These accords could be sectoral in nature or could be bundled together in a "Business Compact" or some such package. There is no reason why such accords must initially be brought within the ambit of the WTO, even though this is a desirable long term goal.

Rest assured a "follow the money" approach would run into opposition from the very non-governmental organisations who have done so much to load on to European trade policy objectives for which there are few takers in the rest of the world. The miserable record of EU RTA negotiations should amply demonstrate the limits of EU commercial policy as an instrument for social reforms.<sup>5</sup> Perhaps the day will come when foreign governments are more receptive to such reforms, in the meantime these EU demands either result in rejection or subterfuge on the part of EU trade negotiators. Criticising the non-governmental organisations, however, misses one very important point. Namely, that EU commercial policy priorities are set by national governments and it has been the very cravenness of

---

5 The issue at hand are not the reforms sought but whether they should be linked to trade negotiations and agreements.

many northern European governments towards their non-governmental organisations that has led to this sorry state of affairs. The reward for internal cowardice has been external deadlock.

#### **Reality Check 4: Develop a cooperative relationship with China**

While “Follow the money” ought to raise the profile giving to tackling murky protectionism, it will also help identify the trading partners where the gains from doing so are greatest. The substantial EU corporate investments in China are a case in point. In 2010 complaints from European business associations, and from the few business persons willing to stick their head above the parapet, about Chinese domestic policies intensified. The sheer size of the Chinese economy, plus its expected growth path, marks it out for particular attention in the years ahead.

How the European Commission best represents EU corporate interests should reflect the lessons of the past. The limits of WTO dispute settlement have already been mentioned. The incomplete nature of the WTO’s rules in many areas of government policy are open invitation to Beijing to retaliate against any punitive European measures. Sticks, it seems, won’t work. Carrots might. The language of partnerships is easy to use but, ultimately, there may be no alternative.

For example, establishing parallel review processes for industrial policies in the EU and in China, whereby the costs and benefits of existing measures are enumerated and lost distortive alternatives identified in a technocratic process, might be more effective in changing minds than sabre-rattling. Establishing common norms for regulatory policies that embody non-discrimination principles is another alternative, backed up with monitoring, reporting, and rights of review for aggrieved parties. A growing set of collaborative projects of commercial interest should be devised and added to over time, serving as constant reminder of the benefits of sustaining cooperation over discrimination. There will undoubtedly be bumps in the road, better than than risking one’s credibility with empty threats about sanctions.



### **Reality Check 5: Can EU trade policy afford another decade of failure?**

The preceding reality checks imply that the priority given to the different challenges facing EU policymakers needs to evolve. These challenges will require a change in emphasis as far as fora, subject matter, and instruments are concerned. A major shift in mindset is probably needed – the current approach is a recipe for continued stalemate and limited benefits for the European Union.

Twenty-first century trade policymaking needs to rediscover its roots, namely, seeking pragmatic solutions to first-order commercial problems. Developments in international corporate strategy and the murky protectionism revealed during the recent global economic downturn point to a national treatment-based and transparency agenda that could be of interest to the EU, the United States, Japan, and the large emerging markets.

Pursuing this agenda will require a new consensus among Member States concerning the negotiating room for manoeuvre for the European Commission, and therefore acceptance that key regulatory policies may have to change in response to trading partners' demands. Talk of propagating European regulatory models abroad should be replaced with a willingness to create a level playing field for twenty-first century business. This will mean taking on vested interests, often the regulators themselves.

Finally, failure to update EU trade policy risks much more than losing commercial opportunities. Should internal division lead to further stalemate and few additional commercial benefits, then surely some medium and larger pro-trade Member States will begin to question the basis of another deal; namely, what are they getting in return for pooling their sovereignty on commercial policy matters? These Member States are entitled to ask what alternatives are available to them if current arrangements do not deliver. Much more is at stake than most European policymakers probably realise.

## **References**

HIGH LEVEL TRADE EXPERTS GROUP (2011), *The Doha Round: Setting a Deadline, Defining A Deal*, Interim Report, January.

**Autoren – Authors****Prof. Simon J. Evenett, Ph.D.**

University of St. Gallen  
Swiss Institute for International Economics  
and Applied Economic Research (SIAW)  
Bodanstrasse 8  
CH-9000 St. Gallen  
Switzerland  
*simon.evenett@unisg.ch*

**Asier Minondo**

Deusto Business School  
Paseo de Mundaiz 50  
20012 San Sebastián  
Spain  
*aminondo@deusto.es*

**Henning Klodt**

Institut für Weltwirtschaft Kiel  
Hindenburgufer 66  
D-24105 Kiel  
Germany  
*Henning.Klodt@ifw-Kiel.de*

**Matthias Baumgarten**

University of Warwick  
c/o Hearsall Lane 147  
CV5 6HG Coventry  
United Kingdom  
*M.Baumgarten@warwick.ac.uk*

**Prof. Dr. Heinz-Dieter Smeets**

Universität Düsseldorf  
Lehrstuhl für Volkswirtschaftslehre,  
insbes. Internationale Wirtschaftsbeziehungen  
Universitätsstraße 1, Geb. 23.31  
D-40225 Düsseldorf  
Germany  
*smeetsd@uni-duesseldorf.de*

Reproduced with permission of the copyright owner. Further reproduction prohibited without permission.