

The global trade slowdown and the Transatlantic Trade and Investment Partnership (TTIP)

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Main takeaways

World trade loses momentum due to some cyclical factors (downturn in EMU and China), but also due to structural reasons such as the change of growth model in China, the diminished impulse from Global Value Chains (GVCs) or the lack of advances in reducing restrictions on trade

The major weight of goods and services flows and FDI between Europe and the US highlights that fostering market access and enhancing regulatory cooperation would have positive effects on bilateral and even on global trade

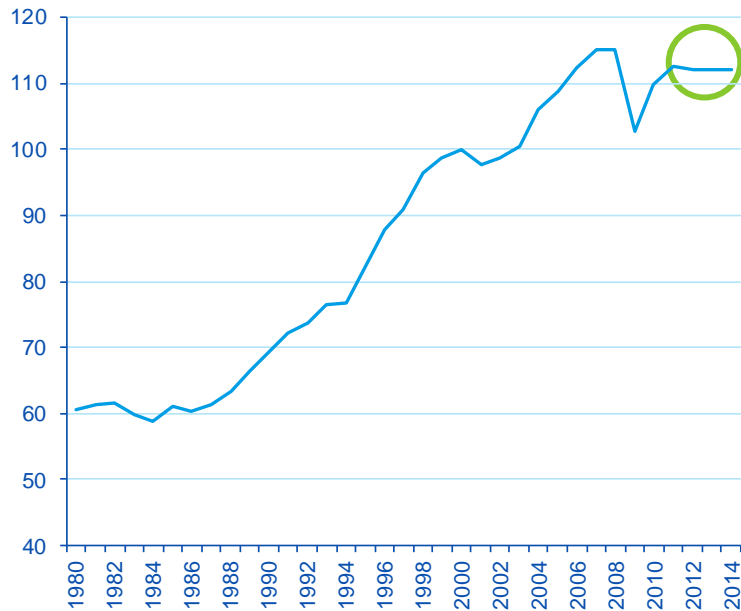
The Transatlantic Trade and Investment Partnership (TTIP) under negotiation between US and EU aims to ease market access, improving the regulatory cooperation between both areas and setting new rules to help firms in their strategies of export and foreign investment. If implemented successfully, TTIP could become a global framework to promote world trade links and to strengthen regulatory cooperation across the board

The elasticity of trade to economic activity has diminished since the impact of the 2008-09 crisis

World trade

Ratio (X+M)/GDP, goods and services, volume (1992=100)

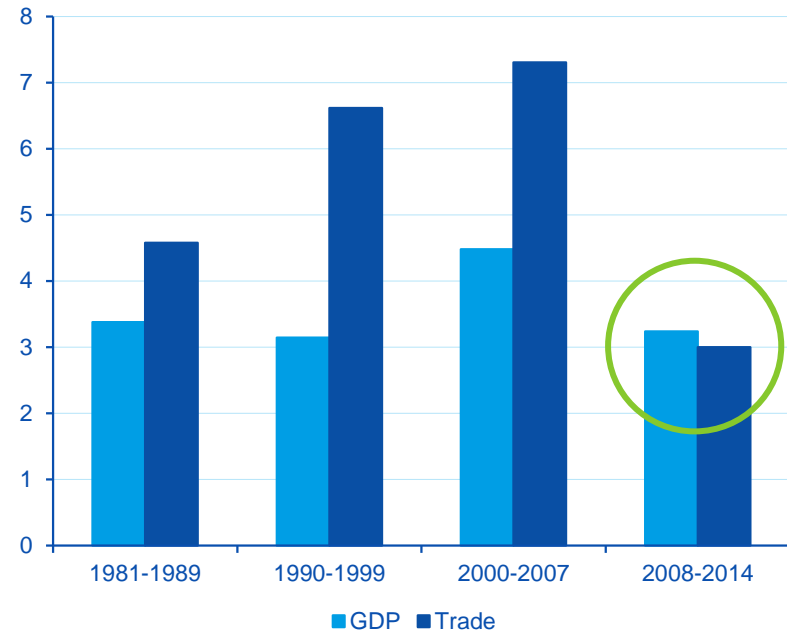
Source: BBVA Research, IMF



World GDP and trade

(average real growth in each period, %)

Source: BBVA Research, IMF



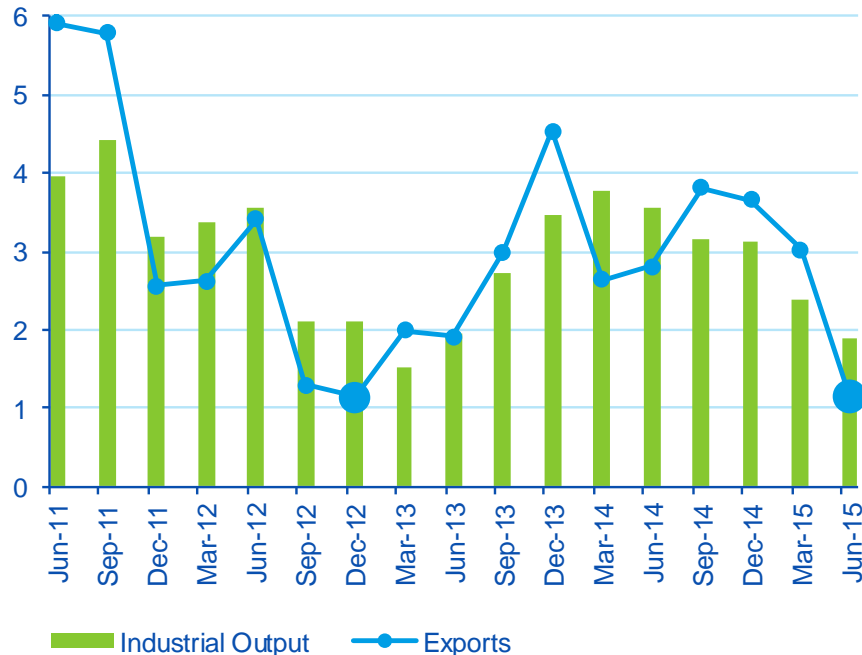
The combination of technological change, business innovation, policy reforms and China's re-integration into the world economy explained the remarkably high growth in global trade until 2007, exceeding the advanced rates registered by income

Recent data do not reveal a more favourable outlook. Are we witnessing a “new normal” in world trade?

World goods exports and industrial production

volume, YoY change, %

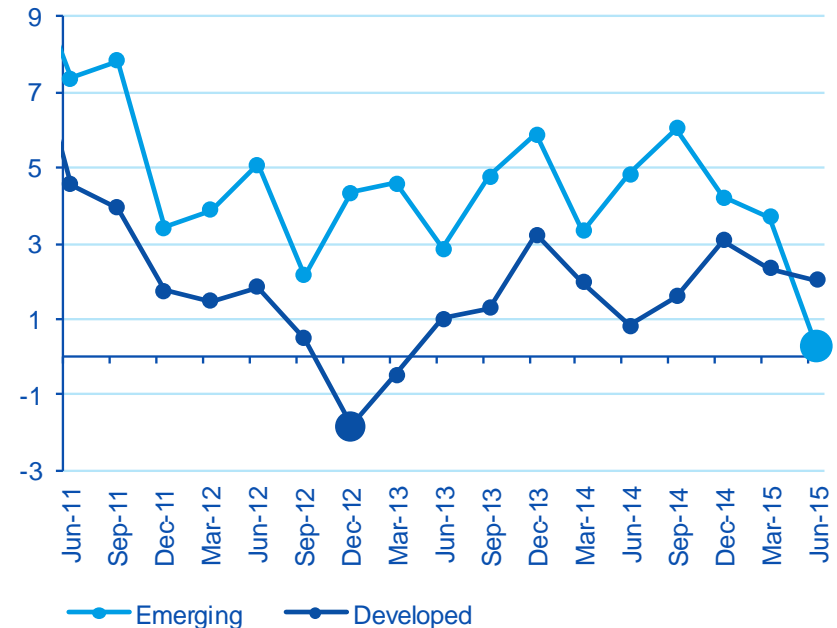
Source: BBVA Research, CPB



World goods exports: developed and emerging

volume, YoY change, %

Source: BBVA Research, CPB



China’s economic slowdown and its impact on Asian trade flows are key in the moderation of global trade, offset partially by the recovery in Developed Markets and, in particular, intra-EU trade

Factors behind the current slowdown are both cyclical and structural

Cyclical

- EMU's enduring slowdown
- China's trend deceleration
- Restrictions on trade financing after 2008

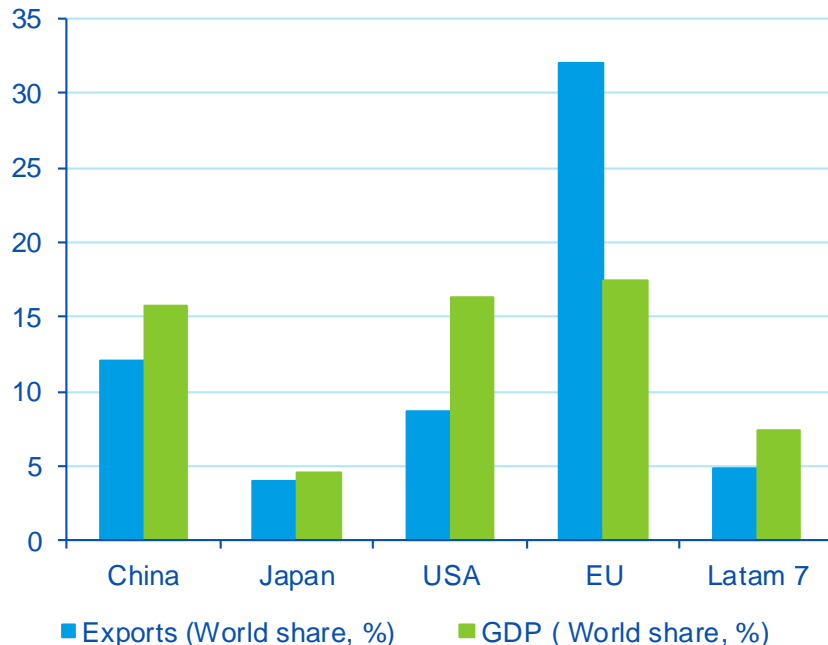
Structural

- China's productive structure change
- Trade-distorting policies
- Changes in Global Value Chains' production strategies

Regarding **cyclical factors**, the impact of EMU's long slowdown and China's downturn is remarkable

GDP and total exports, 2014

Source: BBVA Research, IMF



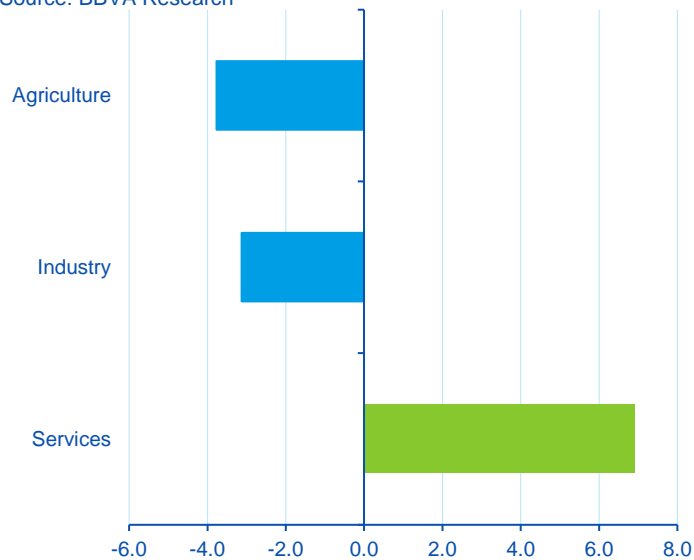
- The EU accounts for 17% of world GDP and 32% of exports of goods, with a significant relevance of intra-EU trade flows. China represents 16% of world GDP and 12% of exports
- Therefore, a slowdown in the economic growth of both areas causes downside pressures on global activity and trade

- The worse relative performance by trade in goods vs. services is partially due to the nature of the recent economic crisis.
- Industrial production continues to suffer the lagging recovery of investment at the global level whereas consumption is the main support of growth in key economies such as US or EMU

As structural factors, it is worth mentioning the ongoing change in China's productive structure

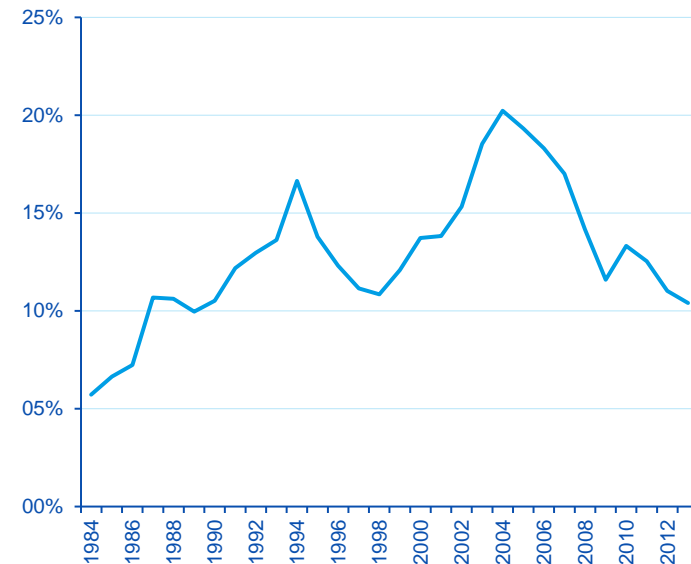
China: productive structure change (2004-14), %

Change of share in GDP (total by sector)
Source: BBVA Research



China: share of manufacturing imports in GDP, %

Source: BBVA Research



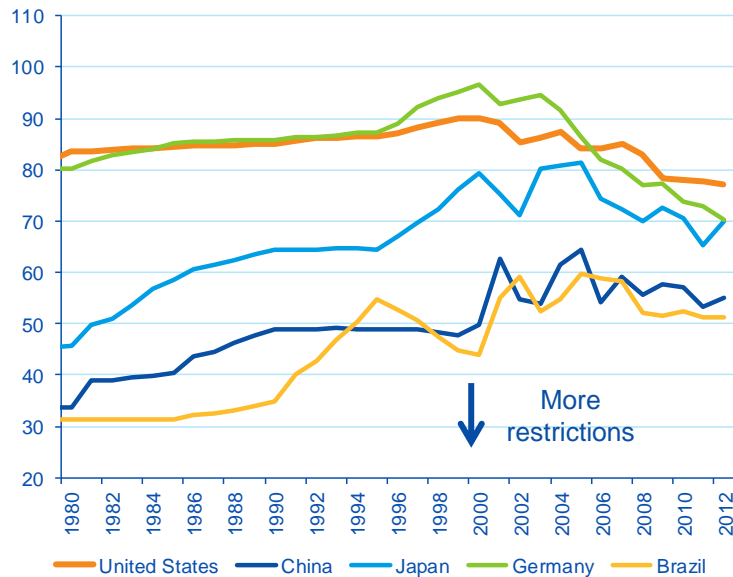
China has been trying to rebalance its economy towards domestic demand and away from an export-driven growth model. Increasing its currency's margin of fluctuation and making advances in the financial liberalisation process are two examples of this

The recent dynamism of activity in services, as opposed to industrial activity, and the continuing fall in the importance of manufacturing on GDP show that this rebalancing is on track

The impact of trade policies is not conclusive but, to say the least, they seem less supportive than before

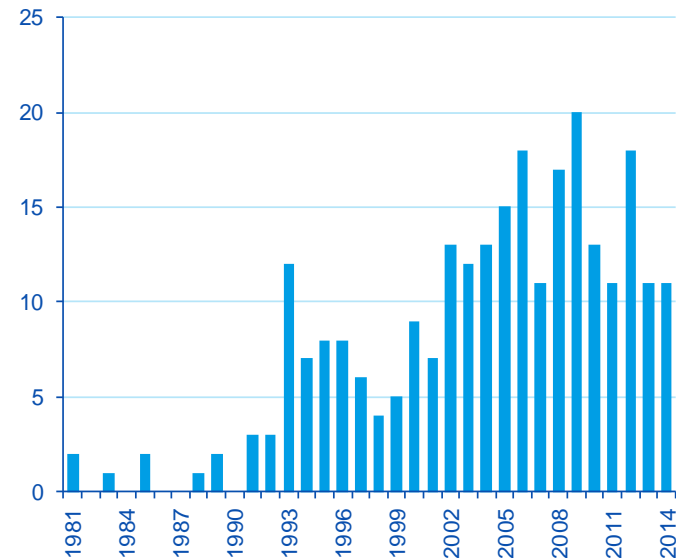
Economic Restriction Index

tariffs on imports, non-tariff barriers imposed on international flows and capital controls
 Source: BBVA Research, KOF Swiss Economic Institute



Number of new regional trade agreements

Source: BBVA Research, WTO



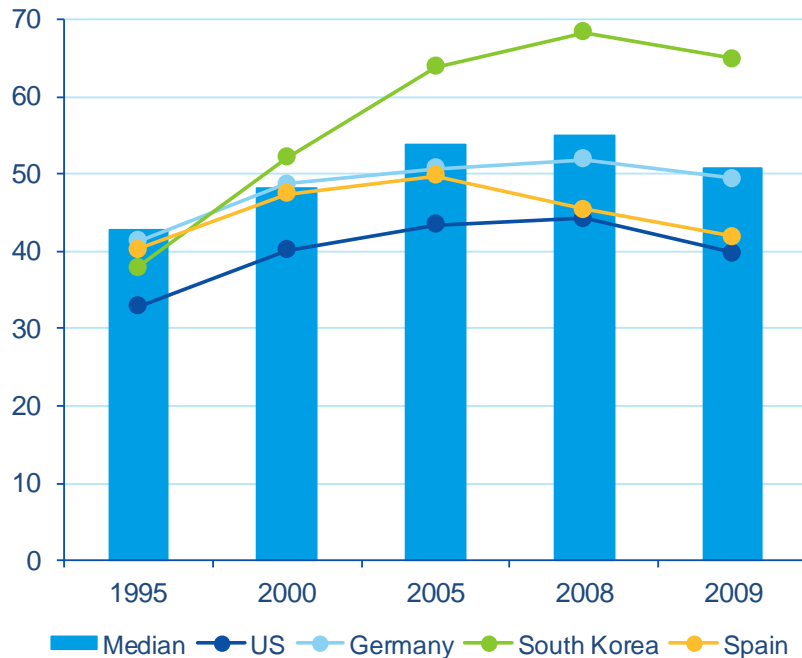
- There is no consensus regarding the size of the impact of heightened protectionism/lower rhythm of liberalisation on the current trade slowdown ...
- ... although the slight increase in the Economic Restriction Index for the most important economies and the lower dynamism in terms of regional trade agreements could suggest some impact on certain countries/sectors

All in all, there could be a reduction in the importance of Global Value Chains of goods and services

Participation in Global Value Chains (import content of exports)

Imports used as inputs in exports plus exports used as other exports by another country

Source: OECD (2015), Import content of exports (indicator)



Trade flows are recorded on a gross value basis, including the value of the intermediate inputs. From a value-added perspective, this implies that there is double-counting, exaggerating the size of trade flows

The spread of GVC has been a key factor behind the rapid growth of global trade relative to income in the 90s and the first half of the 00s. The ICT revolution favoured the fragmentation of production across geographies, reshaping global production chains into “factory” and “headquarter” economies

In the coming years, there may be a move away from highly fragmented, globe-spanning supply chains towards a greater reliance on regional production networks, since the variations in wages and technological advances between emerging and developed countries are converging

However, additional improvements in coordination technology that imply lower costs of geographical unbundling could mitigate this pattern, mainly among countries with greater per capita income (firm excellence is as relevant as wage gaps)

In sum...

World trade dynamics have changed since the impact of the financial crisis, growing slightly less than GDP and the recent data do not show a more favorable outlook

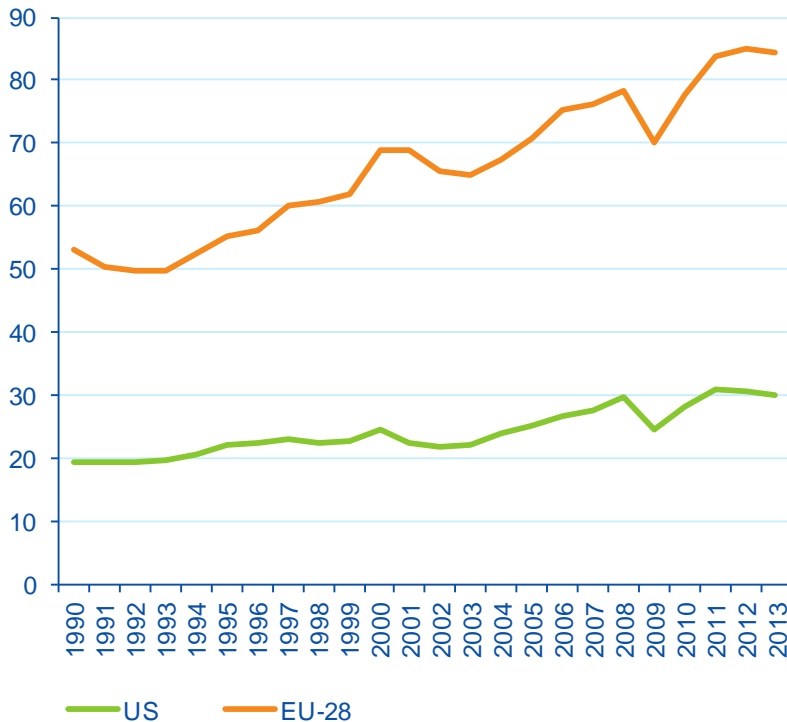
Cyclical factors (downturn in EMU and China) but also more structural elements such as the change of growth model in China, the potential impact of higher economic restrictions in some countries or the lower impulse from GVCs are behind the recent evolution of global trade

Global stimulus policies should contribute to reverse this trend. Then, the Transatlantic Trade and Investment Partnership (TTIP) between US and EU could become a global framework to promote world trade links and the economic growth and to strengthen regulatory cooperation across the board

US and EU account for 40% of world merchandise trade and almost 60% of services exports. The fall in both shares of world flows is explained by the rise of Asia

Trade openness

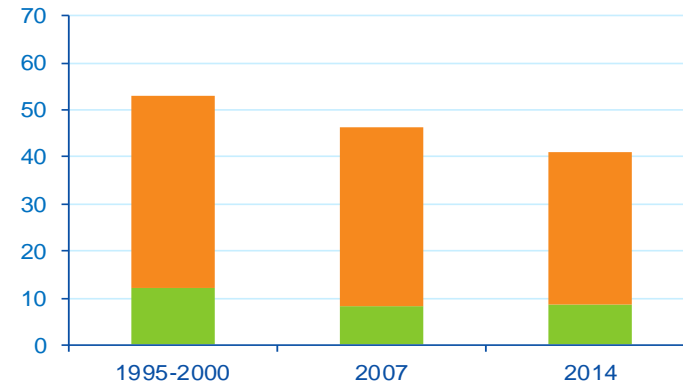
Exports and imports of goods and services on GDP, %
Source: BBVA Research, UNCTAD and IMF



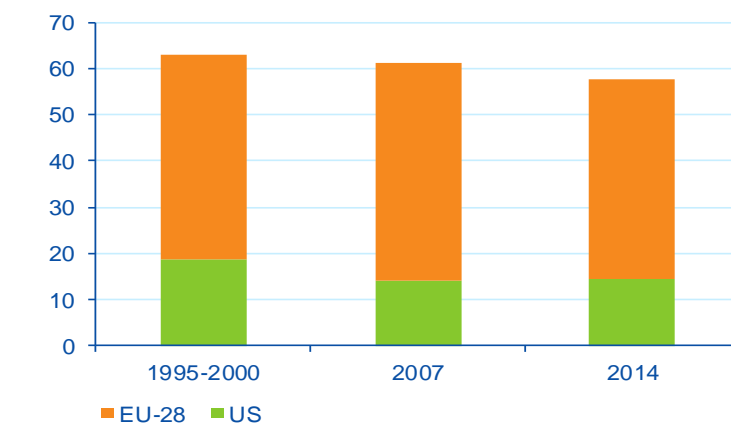
Shares of exports on total world, %

Source: BBVA Research, UNCTAD

Goods



Services

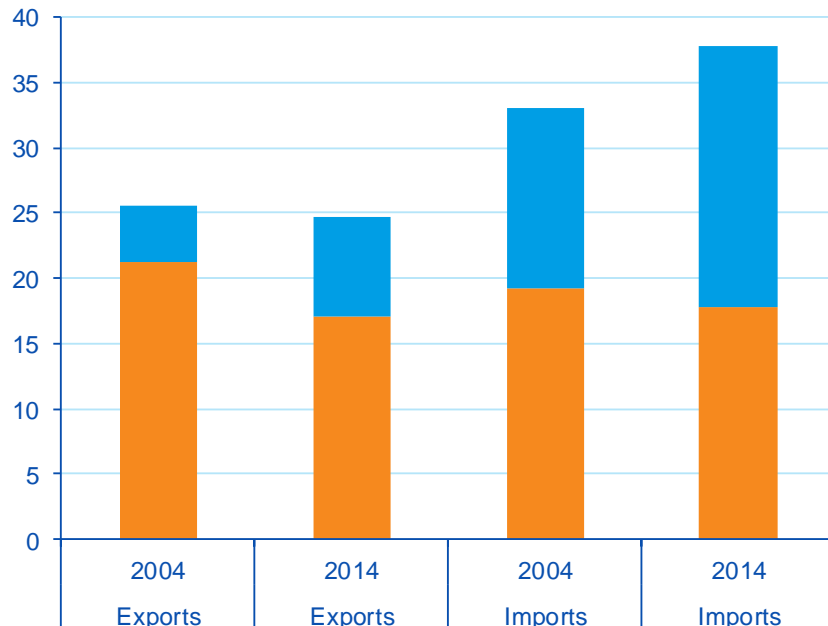


Commercial ties between the US and EU are among the deepest in the world, especially in the trade of merchandise goods, despite Asian competition

US: trade of goods by partner

Share of total (pp)

Source: BBVA Research, Bureau of Labor Statistics

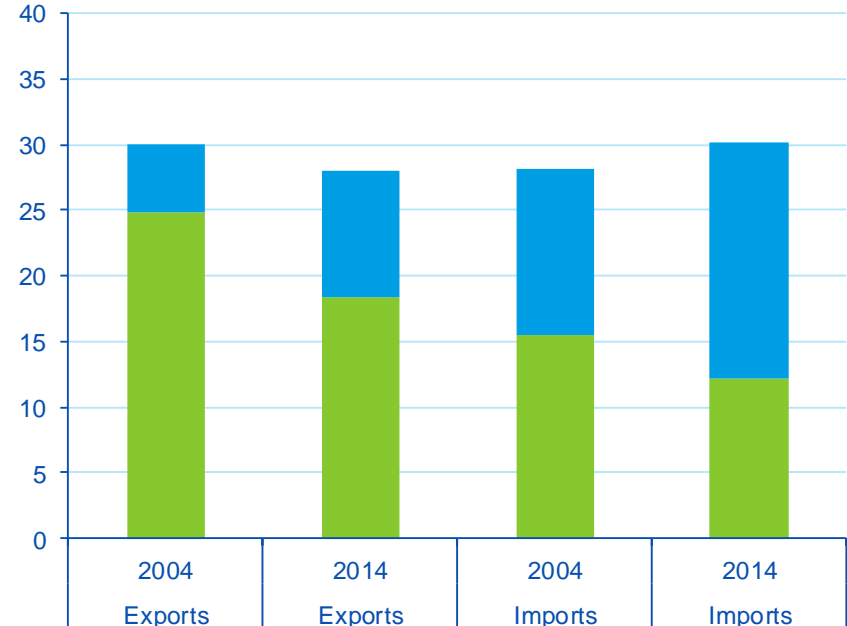


■ EU ■ China

EU-28: trade of goods by partner

(excluding intra-trade) share of total (pp)

Source: BBVA Research, EUROSTAT



■ US ■ China

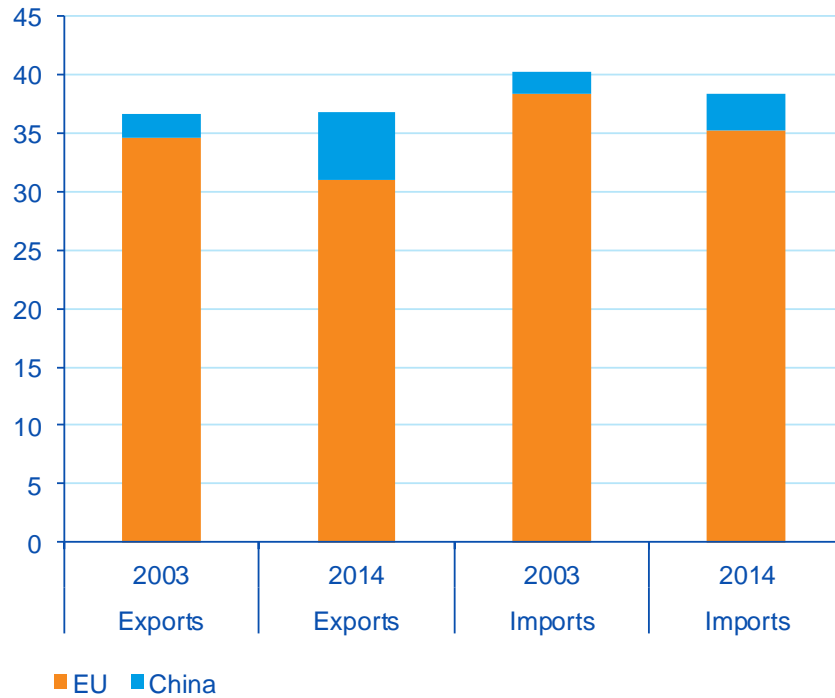
The trade complementarity index for merchandise goods, released by UNCTAD, records the value of 0.71 in 2013, in line with the last decade's average (higher value of index, higher degree of similarity between the structure of exports/imports of US and EU)

In the trade of services segment the ties are nearer than in goods trade

US: trade of services by partner

Share of total (pp)

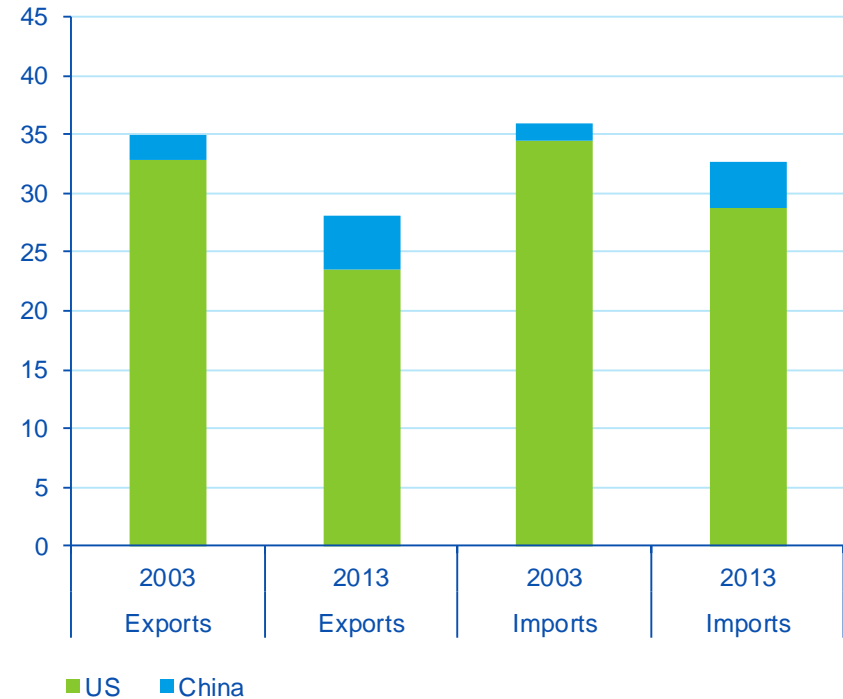
Source: BBVA Research, Bureau of Labor Statistics



EU-28: trade of services by partner

(excluding intra-trade) Share of total (pp)

Source: BBVA Research, EUROSTAT

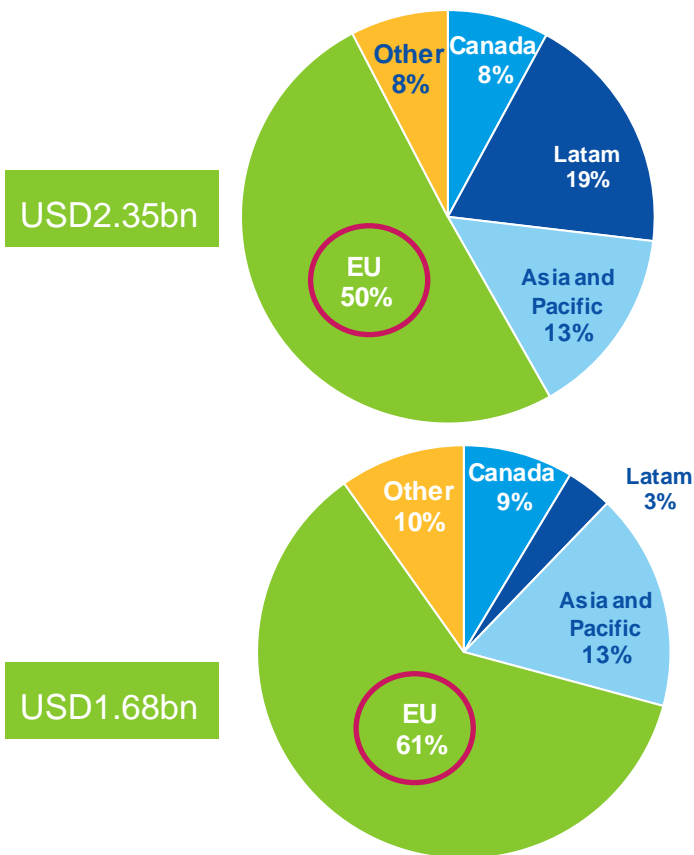


In terms of Foreign Direct Investment, the link between the two areas is even closer

US: FDI outward/inward stock

% total, 2013

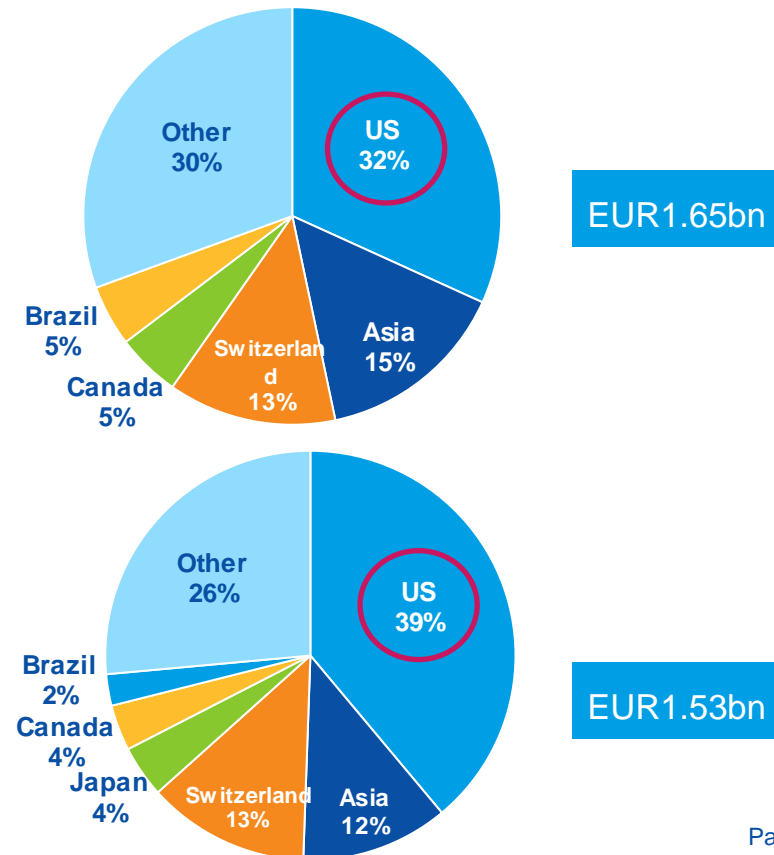
Source: BBVA Research, Bureau of Labor Statistics



EU-27: FDI outward/inward stock

% total excluding extra EU, 2012

Source: BBVA Research, EUROSTAT



Transatlantic Trade and Investment Partnership (TTIP): how would it work?

Pillars

Contents (negotiations started in July 2013)

Market access

better access to the US
/
EU market as other
trade deals

- Trade in goods and customs duties: cut or scrap customs taxes on goods that we export to each other
- Services: make it easier to sell services and investment in US/EU
- Public procurement: let EU/US firms bid for US/EU public contracts
- Rules of origin: agree rules that determine where a product is from

Regulatory cooperation

cutting red tape and
costs - without cutting
corners

- Regulatory coherence: agree ways to co-operate to set new rules
- Technical barriers to trade (TBT): cut the cost of complying with each other's standards
- Food safety and animal and plant health (SPS): ensure food, animal and plant imports are safe, while cutting unnecessary red tape
- Cut the cost of meeting US/EU rules that differ from those of the EU/US

New rules to help EU/US firms

making it easier and
fairer to export, import
and invest

- Smaller companies as target of TTIP
- Access energy and raw materials
- Protect intellectual property – the research and ideas behind new products
- Save time and money on paperwork at customs

Prospects and challenges ahead for TTIP

- TTIP should become a **global framework** to promote world trade links and to strengthen regulatory cooperation across the board.
- It should also be a **stimulating factor for other Atlantic area countries (Canada and Mexico, for example) and emerging economies with close trade links with US and EU** if it goes further in cutting the barriers to trade. Other countries could support the Treaty and access it (for example, after TTIP, Japan decided to sign the Trans-Pacific Partnership, TPP).
- As the **main challenges ahead**, it is worth pointing out the following:
 - **the role of Asian countries** (in particular, China) in the development of TTIP, taking into account their growing weight in trade and investment relations with US and EU
 - **the treatment of agricultural tariffs**
 - **full reduction of barriers to investment**
 - **potential inclusion of new rules for the treatment of financial services**

Main takeaways

World trade loses momentum due to some cyclical factors (downturn in EMU and China), but also due to structural reasons such as the change of growth model in China, the diminished impulse from Global Value Chains (GVCs) or the lack of advances in reducing restrictions on trade

The major weight of goods and services flows and FDI between Europe and the US highlights that fostering market access and enhancing regulatory cooperation would have positive effects on bilateral and even on global trade

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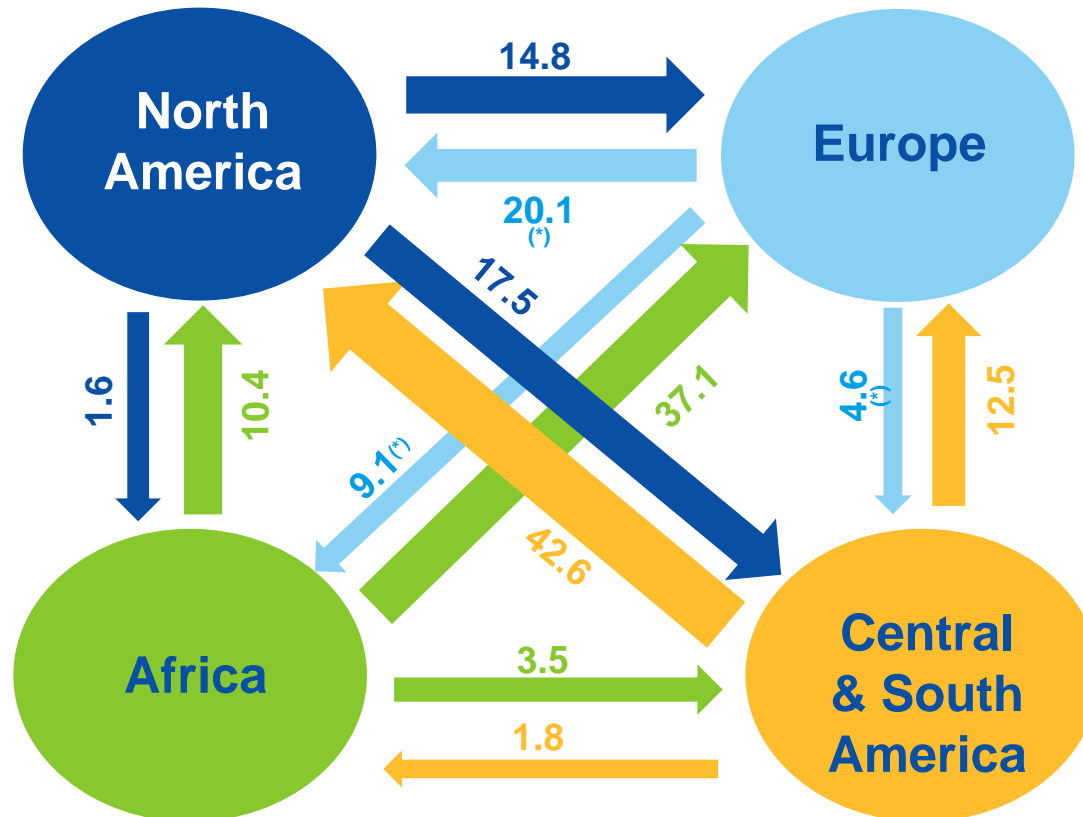
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Annex: the relevance of merchandise trade in the Atlantic area

Merchandise trade flows in the Atlantic area, 2013
Exports of goods of each area/country by partner, % of total

Source: BBVA Research, UNCTAD

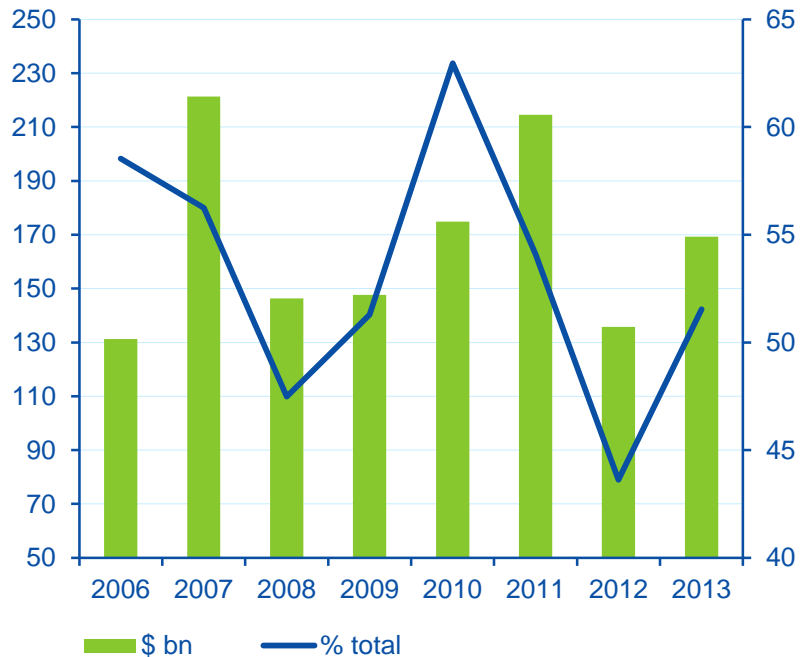


(*) % excluding intra-Europe trade

Annex: The EU attracted 50% of total US FDI outflows in 2013 and concentrated 25% of its own FDI outflows to the US (2012)

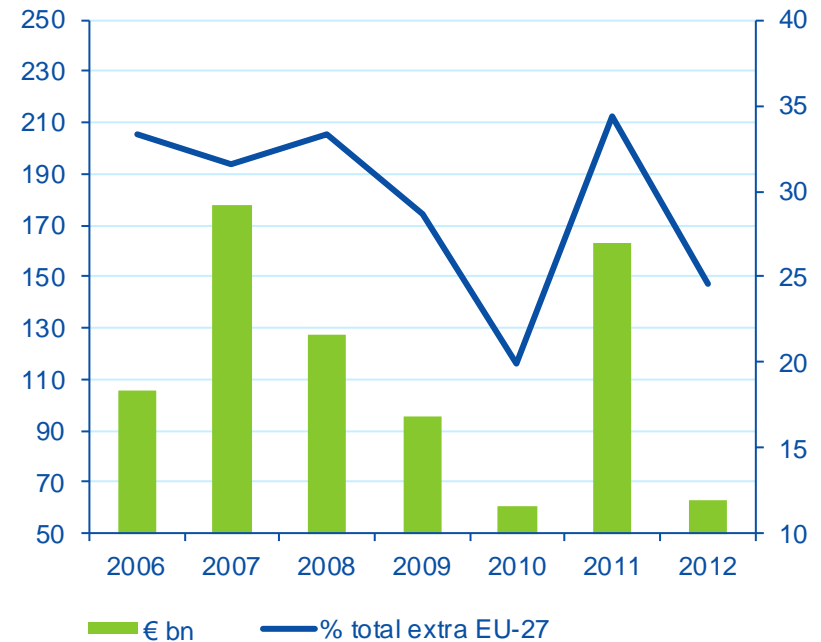
US: FDI outward flows to EU

Source: BBVA Research, Bureau of Labor Statistics



EU-27: FDI outward flows to US

Source: BBVA Research, Bureau of Labor Statistics



Annex: Current state of negotiations: 10th Round (July 2015, Brussels)

Pillars

Market access

- An important milestone was reached and both sides exchanged revised services offers
- Tariffs and public procurement were not addressed, although they remain essential elements of the negotiations

Regulatory cooperation

- Discussions on pharmaceuticals between the US Food and Drug Administration (FDA) and the EU pharmaceutical regulators continue to make good progress
- The EU and the US have now introduced compatible regulations leading to a single development programme for biosimilar medicines

New rules to help EU/US firms

- They have made good progress on competition, customs and trade facilitation, and state to state dispute settlement.
- They have also made significant progress on SMEs

Annex: Current state of negotiations: 10th Round (July 2015, Brussels)

Political context

At their last meeting in June, the leaders of the G7 gave the EU and US their clear endorsement to intensify their discussions on TTIP and to identify the way forward in all areas

On 8 July, the European Parliament gave strong support to the negotiations, underlining that only a comprehensive, balanced and ambitious agreement would get the support of the European Parliament

The US Congress adopted the Trade Promotion Authority Bill in June, which provides additional political impetus and support to trade negotiations