Making trade sustainable impact assessment more relevant to trade negotiations

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Download the final report from the SIAMETHOD project website:

http://www.iddri.org/iddri/html/projet/sia_method/index2.htm

POLICY BRIEF

Making trade sustainable impact assessment (Trade SIAs) more relevant to trade negotiations

I. Introduction

1. Since the GATT agreement in the late 1940s the terrain for the negotiation of further trade liberalisation has been changed out of all recognition, both by world events and by the eight rounds of negotiation that have been successfully concluded. It is now far less obvious that there are significant further net gains to be equally achieved across countries from trade liberalisation. Certainly there are social forces well beyond traditional vested interests that now contest whether this is the case. Trade negotiators themselves seem less certain that trade liberalisation will help them achieve their national social, economic and political objectives. Trade negotiations in this new context have become becalmed.

2. In this new context, trade Sustainable Impact Assessments (Trade SIAs) are confronted to new challenges. Their value and effectiveness now go beyond the identification of and advocacy for flanking measures. Our research results show the need for Trade SIAs to go deeper into the motivations of the negotiations themselves to identify i) those areas in which progress towards liberalisation might be relatively uncontroversially made (where vested interests may be confronted or compensated, and provision may be made for short-term adjustment costs); ii) which areas may need special agreement or arrangements (for example, those externalities that require international cooperation to be effectively addressed); and iii) which areas are unlikely to be the subject of further liberalisation agreements (where strongly held collective preferences conflict with further liberalisation).

3. A main problem negotiating countries and Trade SIAs face altogether is that motivations to govern trade may widely differ across countries. Even though overcoming vested interest, addressing trade externalities and safeguarding collective preferences on trade-related sustainability issues constitute ascertained motives to govern trade today, considerable uncertainty prevails on the relative weight different countries confer to each. This uncertainty hampers trade negotiations in short term while

postponing the emergence of a global governance of trade as if sustainable development really mattered.

“Policy makers face a complex range of arbitrations which cannot be restricted to sustainable development “pillars”, and include arbitrations across sectors, across actors and also over time.”

4. The SIAMETHOD project explores the implications of this analysis for a number of the most contentious areas in trade negotiations, like commodities, investment, and services, correlating in each case, Trade SIAs outcomes with the three identified motives to govern trade.

II. Underlying assumptions for Trade SIAs extension

5. A retrospective analysis of Trade SIAs shows that they have been conceived to help policy makers maximise positive trade-offs across the three “pillars” of sustainability (economic, social, environmental) in the liberalisation process. But the new context described above faces policy makers with a complex range of arbitrations which cannot be restricted to sustainable development “pillars”, and include arbitrations across sectors, across actors and also over time.

6. We assume that policy makers’ arbitrage requires information on the distributive effects of trade liberalisation scenarios (across sectors, across actors and over time), as well as on the sustainable development impacts *valued* by the different countries involved in the trade negotiation process. This provides Trade SIA with an extended framework of analysis.

III. SIAMETHOD propositions

Proposition 1: Going beyond the protectionist bias

7. Existing Trade SIAs tend to assess the overall impact of trade liberalization on each of the three sustainable development pillars. We argue that an “overall impact”

ultimately depends on collective preferences, which depend on national income, culture, history, resources and endowments. The challenge for SIA is not only to show a particular state that the reform scenarios of its trade policies are sustainable or not, but also to help it understand that other states have different views on sustainability. To us, both views can be compatible with sustainability, depending on the relative priorities a society gives to each pillar of sustainable development. This implies that indicators should be designed not so much to be aggregated between societies as to be weighted by each society. This further suggests extending the contribution of SIAs to trade negotiations in order to increase reflexivity, meaning that each side should be provided a better understanding of the collective preferences of the other.

Proposition 2: Reducing uncertainty on dynamic effects

8. Most trade liberalization simulation models like computable general equilibrium (CGE) models do not account for welfare changes between two market equilibria. Their approach is basically comparative and static, wherein two situations are compared: before liberalization and after liberalization, with the assumption that all workers adjust to new prices. CGEs are therefore a source of misunderstanding. *Ex post* assessment of trade liberalisation impacts tends to list environmental and social impacts, but according to trade economists, these occur because they are in the transition period, that is, governments have not implemented the appropriate environmental policies to correct externalities (funded by liberalization welfare gains) and workers in fragile sectors have not yet changed job and region. These are the so-called adjustment costs. For most of trade economists, these costs are transitory. For governments, dealing with such costs lies at the core of their mandate.

“Long-term trade liberalisation’s gains are beyond policy-makers’ scope. Transition matters, but it is not currently taken into account by trade models”

9. Because most CGE conclusions are derived from the market equilibrium hypothesis they are built on, and particularly from the way dynamics is integrated, a careful interpretation of the simulation is absolutely necessary. Secondly, the current development of the dynamics model towards long-term gain simulation seems more a lure than an effective improvement of policy-makers’ decision-making tools. Long-term gains are beyond policy-makers’ scope. Transition matters, but it is not currently taken into account, with some exceptions outlined in the report. Dealing with adjustment costs within a CGE framework implies a

huge amount of innovation on the formalization of expectations and disequilibrium modeling.

Proposition 3: Reducing uncertainty on sector gains and losses

10. Product chain assessment is an emerging methodology for understanding the dynamics and impacts of global economic transformations. It helps to understand the transformation dynamics of product chains including their sustainability impacts. The underlying assumption of a globalised and liberalised world economy is that trade liberalisation agreements support fast changing transformation processes of product chains world-wide due to simplification of market access.

11. Integration of a product chain perspective into SIA is done by analysing the characteristics of the product chain ("mapping the chain"), the governance structure, material flows and social and environmental impacts. The report elaborates a methodological framework on how to carry out a product-chain based SIA. Promising methods at hand are profit analyses, actor analyses and governance (power distribution along the chain) analyses.

12. Trade SIAs should deliver comparable results between and within sectors and branches. Sustainability impact assessment in the field of international trade should hence bear two general perspectives in mind: the inter-sector perspective and the intra-sector perspective. The comparability of sustainability performances between sectors (inter-sector perspective) is straightforward for policy-makers when negotiating on trade policies, since assessment results give hints on which sectors, with appropriate flanking measures, to favour so as to improve *sectoral* sustainability. But because trade does not occur only across sectors but does also within sectors, the intra-sectoral sustainability benchmarking should be used in a complementary way to assess existing differences of sustainability impacts within a branch, considering geographically dispersed product-life-cycles analysis.

Proposition 4: Reduce uncertainty on gainers and losers

13. The impacts of trade openness on a wide array of social indicators must be disentangled at the household or individual level, for example assessing the consequences of changes in the relative demand for skilled labor through induced technical change, with imperfect access to markets (credit, labor, input, education). This cannot be done by investigating the macro-economic consequences of trade openness alone.

14. Methods must be implemented to further investigate at the household or individual level how the macro-economic changes interact with household or individual behaviour and welfare. Existing work reviewed show that available micro-modeling could increase our understanding of the micro determinants of growth and exports, and of the reactions of firms to trade openness. Such improvements make it possible in the long run to understand which variables drive factor demands and relative factor returns.

Proposition 5: Addressing commodities, services and investment specific issues

Commodities

15. The trade in primary commodities continues to have serious social and environmental impacts and implications which mean that it cannot be said with any degree of certainty that overall it makes a positive contribution to sustainable development. The many initiatives that have been established to try to mitigate these negative impacts, while welcome in themselves, have had mixed effects, and have certainly not solved the problems.

“We make a proposal for a new generation of Sustainable Commodity Agreements (SCAs)”

16. It is therefore not clear that further trade liberalisation in respect of commodities, under current conditions, will contribute positively to sustainable development. Trade negotiators therefore have rational reasons to be wary about further trade liberalisation in respect of commodities, and it may be that these reasons are contributing to the current difficulties in the trade negotiations.

17. We make a proposal for a new generation of Sustainable Commodity Agreements (SCAs), which draw on past experience, but go beyond it, and could provide a framework within which an expansion of trade in commodities did make an unequivocal positive contribution to sustainable development.

Services

18. Trade in services liberalisation effects have rarely been investigated with EIAs and extremely rarely with SIAs so far. This denies the importance of the growing trade in services, its relevance to world trade volumes and to domestic impacts.

“The the extend to which trade in services liberalisation can boost or hamper the development process (in the direction of the UN Millennium Goals) strongly depends on domestic regulatory capacities.”

19. The trade liberalisation effects are often supplemented or multiplied by domestic privatisation and deregulation policies which in many cases were in turn initialised or pushed by international organisations like the World Bank or the IMF. Further, trade in services liberalisation processes often touch sensitive issues like national infrastructure, supply of basic needs, national security - and thereby can interfere severely with domestic collective preferences. Trade SIAs should therefore investigate distributional effects very closely. Collective preferences might be assessed by actor network analyses, public opinion polls or even public referenda.

20. The case studies show that the extend to which trade in services liberalisation can boost or hamper the development process (in the direction of the UN Millennium Goals) strongly depends on domestic regulatory capacities. Trade SIAs on trade in services should therefore include an evaluation of domestic governance structures towards the services sector and assess the regulatory capabilities of relevant authorities.

21. Without good governance and a well-sequenced process, “weak” countries might easily find themselves worse off and may realise aggravated domestic economic, environmental and social problems. Further, developing countries will not be satisfied with a mere reference to potential global gains stemming from

trade in services liberalisation and growth. Explicit support and transfer mechanisms must be developed and implemented before and alongside the liberalisation process - and not only promised. Trade SIAs may point out critical aspects (as for example insufficient regulatory capabilities), helping to identify focal points for preparatory support and flanking measures.

Investment

22. It is highly context-dependent the extent to which the conclusion of an investment agreement actually leads to an increase in foreign direct investment, and whether such investment translates into sustainable development benefits. Therefore an SIA for an investment agreement should first and foremost look at the factors defining the overall investment climate of a potential host country, notably the status of its economic and institutional development.

23. Quantifying the effects of investment liberalisation appears even more difficult than for trade liberalisation, due to the nature of the regulatory changes involved as well as data constraints. While economic modelling may provide at least some indicative figures for economic variables, it is doubtful whether attempts to quantify the implications on social and environmental indicators will lead to any meaningful results.

“Rather than predicting a specific outcome of investment liberalisation, a sustainability assessment should focus on what conditions need to be met in order to ensure additional investment will occur and render sustainable development benefits.”

24. Rather than predicting a specific outcome of investment liberalisation, a sustainability assessment should focus on what conditions need to be met in order to ensure additional investment will occur and render sustainable development benefits. And rather than exploring one overall ‘with agreement’ scenario, it may be appropriate to develop more differentiated partial ‘with measures’ scenarios.

25. Investment SIAs should duly take into account those aspects that have proven to be the most contentious ones in the debates on investment agreements, namely, concerns over national sovereignty and regulatory capacity, and the adequate balance of investor rights and responsibilities.

Proposition 6: Make participation both a means and an end

26. Currently, the objectives of public participation are frequently not clearly stated. Objectives need to be clarified to guide the selection of appropriate participation methods and to reduce the potential for false or exaggerated expectations and resulting disillusionment with public participation (and possibly the whole SIA process). In the face of limited resources and capacities for public participation it may often be necessary to give priority to some objectives over others.

“The objectives of public participation need to be clarified to guide the selection of appropriate participation methods and to reduce the potential for false or exaggerated expectations”

27. Public participation in SIAs currently occurs more or less ad hoc in the sense that there are relatively few institutionalised links between participation in different SIA. This has negative effects on the effectiveness and efficiency of public participation. Increased efforts at network building and the formation of a permanent SIA advisory committee could help to build bridges among the various participation exercises.

28. Capacity building measures should be an integral part of public participation in SIAs, in particular if the effects or trade agreements concern developing countries with weak civil societies.

29. Transparency is a crucial aspect of public participation in SIAs. Transparency requires that information is provided through adequate media and in suitable formats, while confidentiality must be kept at a minimum (perhaps with the help of the advisory committee). The selection of stakeholders who participate in SIAs as well as the incorporation of their input into the SIA must be transparent and documented.

30. Public participation may strengthen the credibility of SIAs and, consequently, the

link to trade negotiations if it is systematically incorporated in the analysis of issues that tend to block progress in the negotiations. This applies in particular to issues associated with cultural or normative concerns that are difficult to quantify and monetise and would likely require the increased use of deliberative methods of public participation in addition to current practices.

IV Conclusion

Between the too-limiting assumptions of trade SIAs over the variables of political choice scattered throughout economic, environmental and social effects on the one hand, and the political economy approach on the other, wherein all preferences should be conveyed through organised lobbies competing for public support, a bridge has to be built. Bridging these two strands of expertise and literature would lead to integrating more political economy into trade SIAs, meaning focusing more on gainers and losers, and, conversely, opening up our understanding of the political economy of trade negotiations through the integration of non-market impact variables that have been explored by trade SIAs. To help do so, SIAMETHOD propositions explore the possible extension of Trade SIAs to controversial sectors or “issue areas”, while correlating them with different governments’ motives to engage in trade liberalisation or protection. Further research on remaining issues which can help further develop the SIAMETHOD approach, and a testing on real negotiation cases, constitute the logical next steps of our analysis.

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