

# Enhancing the Contribution of Preferential Trade Agreements to Inclusive and Equitable Trade: Latin American cases



UNITED NATIONS

ECLAC

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# Selected countries

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- ▶ Three national seminars were held in the participating countries (Ecuador, Colombia and Jamaica)
- ▶ Technical assistance in 4 countries (Ecuador, Guatemala, Honduras and Jamaica)
- ▶ Desk studies in the cases of Colombia, Ecuador, Jamaica, Honduras and Guatemala.
- ▶ **Topics covered in Seminars:**
  - ▶ Summary of available empirical evidence on social and distributional effects of trade policy (poverty, inequality and employment)
  - ▶ Review of the evolution of trade policy at the country level with particular emphasis on trade liberalization efforts that were undertaken in the specific countries.
  - ▶ Roundtable of discussions on possible studies and needs.



# Consensus reached by participants in the Workshops

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## ► Five main issues with trade policy:

- 1.- Reduce transactional costs associated with multiple trade agreements;
  - 2.- Identify winning and / or losing sectors with the aim of maximizing the benefits of trade policy changes (FTAs, imposition of safeguards, quotas or other measures);
  - 3.- Make ex-post estimates of the effects of a trade policy applied in the past to see if there were winners or losers;
  - 4.- Introducing socio-economic dimensions in trade policy assessments: employment, poverty and income distribution;
  - 5.- Consider value chain analysis, productive integration, and possible effects on economic agents (SMEs)
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## ...in all cases

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- ▶ **Requests made to train officials and policymakers in order to learn about:**
    - ▶ Various databases (trade, tariff, NTMs, ...)
    - ▶ Trade indicators (diversification, similarity, intra-industrial index, comparative advantages, among others);
    - ▶ Methodologies to conduct trade policy assessments:
    - ▶ Econometric models: Time series, gravity model;
    - ▶ Partial and General Equilibrium Models (GEM);
    - ▶ Micro-simulations using household surveys to assess socioeconomic dimensions: poverty, employment and income distribution.
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# Case Studies in LAC Region

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- ▶ Capacity building courses for trade officials and policymakers
- ▶ **Concerns of governments:**
  - ▶ Socio-economic assessment of possible FTA between Ecuador and EU
  - ▶ Evaluation of a Trade Facility Program between Guatemala and Honduras
  - ▶ Evaluation of the economic and social impact of possible trade negotiations between Jamaica and Central America, Mexico and the countries of the Northern Caribbean
  - ▶ Desk Study for Colombia: impact on employment and wages at the firm level in Colombia as a result of a negative shock of broken diplomatic ties with Venezuela in 2008.



# Socioeconomic assessment of possible FTA between Ecuador and EU

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- ▶ Ecuador, a member of the Andean Community of Nations (CAN), had lagged behind Colombia and Peru which had signed a trade agreement with the European Union.
- ▶ At the end of 2016, Ecuador was going to lose the Generalized System of Preferences Plus from the EU (GSP+).
- ▶ **Methodology:** Computerized General Equilibrium Model (CGE) and also a Micro-simulation Model for social evaluation (employment, poverty and income distribution changes)
- ▶ **Basic Scenarios:** Loss of GSP+ and Signing of Agreement with the EU.
- ▶ Ecuador had the risk of losing competitiveness in a range of products in which it had comparative advantages (bananas, shrimp, tunas, flowers,...)



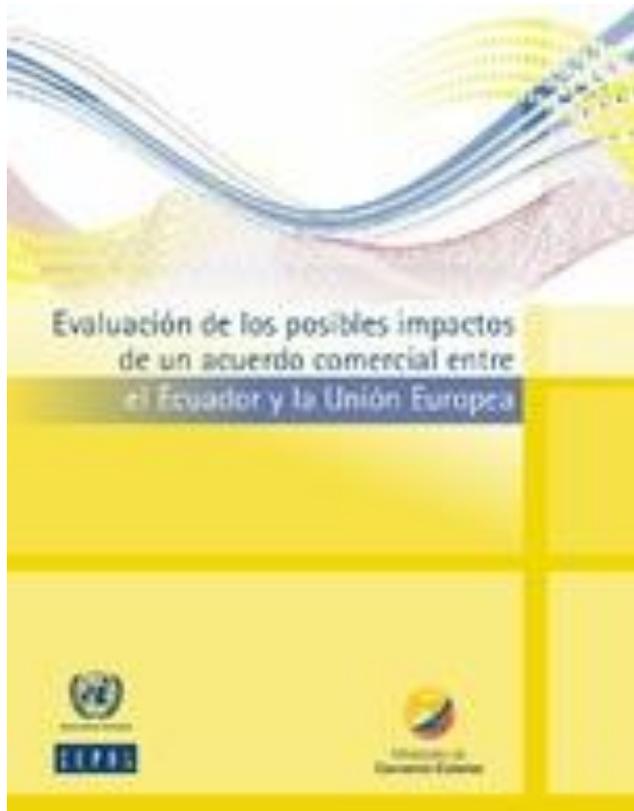
# Socioeconomic assessment of possible FTA between Ecuador and EU

- ▶ The social cost of not signing the agreement was about 5% of the country's GDP (From 2015 to 2020)
- ▶ The total tariffs the country faced would increase from 7.7 to 16%, and more in the case of some products (fishing and fresh flowers);
- ▶ From the social point of view, major losses in the banana sector, with 1.5 million jobs at risk.
- ▶ Signing the agreement would recover Ecuador's competitiveness vis-à-vis Colombia, Peru and Central American countries.

	With Agreement (%)	Without the agreement (%)	Net effect (A-B) (%)
Changes in GDP	0.10	-0.20	0.3
Changes in bilateral Xs to EU	1.6	-3.7	5.3

# Project results of the assessment of Ecuador-EU FTA

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- ▶ Impact assessment discussion at a very high level (President and Ministers)
- ▶ The country signed the agreement considering some advising
  - ▶ Protection of SMEs in the government procurement
  - ▶ Special and differential treatment

## **CAPACITY BUILDING**

- ▶ 2 National training courses (Trade Minister, Foreign Affairs Minister, servants, Export Promotion Agency)
    - ▶ Quito
    - ▶ Guayaquil
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# Evaluation of a Trade Facility Program between Guatemala and Honduras

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- ▶ Guatemala and Honduras requested assistance to evaluate the possible impacts of deepening their Customs Union.
- ▶ Countries decided to harmonize customs union to facilitate trade.
- ▶ Policymakers asked: What is the effect of deepening the Customs Union and implementing a Trade Facilitation Program?
- ▶ Not only economic effects but also socio-economic effects (employment, poverty and income distribution)
- ▶ **Methodology:** Gravity model to calculate costs associated with trade facilitation; CGE (macro), Micro-simulation (social) and trade analysis of custom microdata (by firms and HS) to identify value chains and the participation of SMEs.
- ▶ **Scenarios:** Reduction of tariff equivalent calculated (EAV) by 60% in best possible scenario. In a less optimistic scenario, the reduction considered was 30% of EAV.



# Evaluation of a Trade Facility Program between Guatemala and Honduras

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- ▶ Deepening unified customs territories of Guatemala and Honduras would boost production and trade in both countries and also increase tax collection.
- ▶ From a social point of view, deepening the customs union encourages job creation and promotes the reduction of poverty and indigence.
- ▶ Comparatively, economic effects appear more visible than social effects. The results are more auspicious in the case of the ambitious scenerios.
- ▶ The results of the study were useful in the policy discussions that led to the plan becoming a reality.
- ▶ In June 26 of this year, the Presidents began the process by opening of three integrated border crossings.



# Project results of the Assessment of Trade Facility Program between Guatemala and Honduras

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- ▶ Discussion at a very high level (Minister's meetings between both countries and the SIECA Secretary)
  - ▶ In June 28 the Presidents of Honduras and Guatemala opening three integrated border crossings
  - ▶ Trade Facilitation borders
  - ▶ Common territory of 221 Km<sup>2</sup>
  - ▶ 52% of total Central America territory



# Evaluation of the economic and social impacts of potential FTAs between Jamaica and Central America, Mexico, and North Caribbean countries

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- ▶ **Methodology:** CGE (macro), Micro-simulation (social) and trade analysis of trade indicators to evaluate potential products demanded by the selected countries.
- ▶ Results show that the greatest effects occur when Jamaica signs trade agreements with Mexico and Central America in which case GDP increases by 0.01% and 0.02% respectively, with slight increases in private investment and consumption.
- ▶ The FTA, which has comparatively greater increases in trade flows, mainly exports, is the one with the countries of Central America, a region with which Jamaica would have a greater density of bilateral trade.



# **Evaluation of the economic and social impacts of potential FTAs between Jamaica and Central America, Mexico, and North Caribbean countries**

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- ▶ Opening Jamaica to Central America, Mexico, and the countries of the North Caribbean produces small but negative changes in the level of household expenditures due to the increase in prices of some products (eg. food) which are not compensated by the decrease in prices of other products (in particular textiles).
- ▶ The prevalence of this increase may translate into a loss of well-being in households in particular in the first quintiles if they are not accompanied by similar increases in income as a result of the agreement itself, an aspect that is not analyzed in this study because of the limitations in the existing information.
- ▶ The study is under consideration by the government of Jamaica. We sent it for their comments on July 7th.



# Impact on employment and wages at the firm level in Colombia as a result of a negative shock of broken diplomatic ties with Venezuela in 2008.

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- ▶ The people of the Colombian Statistic Agency (DANE) requested that a dataset which combines the Manufacturing survey with trade data (production and exports by firms) be applied.
- ▶ The analysis focused on the impact on employment and wages at the firm level after the closure of diplomatic relation with Venezuela in 2008.
- ▶ **Methodology:** A difference-in-differences event model with an analysis of the evolution of the same sample of firms before and after broken diplomatic ties between Colombia and Venezuela.



## **Impact on employment and wages at the firm level in Colombia as a result of a negative shock of broken diplomatic ties with Venezuela in 2008.**

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- ▶ The study finds heterogeneous effect, with strong negative impacts of the trade shock for firms with a strong presence in the Venezuelan market.
  - ▶ The firms with a diversified product structure and a wide range of destinations were not affected.
  - ▶ There is a temporary increase in the probability of death of the affected firms two years after the shock and a skill-upgrading effect in those companies that responded to a closing of the Venezuelan market with an increase in sales to the United States.
  - ▶ **For firms that were more diversified by product and destination, export structure allowed them to avoid negative social effects.**
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# How do we address inclusivity in our technical assistance?

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- ▶ Consider vulnerable sectors through an ex-ante evaluation method that takes into account employment and consumption.
- ▶ We do this by analyzing household surveys as well as income and expenditure surveys.
- ▶ **We make the countries aware of the need to have this information.**
- ▶ **Taking decisions in trade and social policies is not something that can be done in a vacuum.**
- ▶ A broad economic study identifies macroeconomic and sectoral effects. With these results, and through the use of micro-simulation techniques, we determine which sectors are more or less affected after possible changes in policies (winners and losers).



# Inclusivity in terms of outcome

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- ▶ With the information of winners and losers each government manages their own sensitive areas
- ▶ Calculation of possible compensation is made
- ▶ Dialogue with relevant sectors to assess the possibilities of implementing complementary policies
- ▶ Design specific instruments:
  - ▶ Economic compensation in extreme cases;
  - ▶ Technical assistance;
  - ▶ Exclusion of sectors and
  - ▶ Longer timeframes for tariff reductions in local sectors.



# Excluded countries

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- ▶ Excluded countries are usually left at a disadvantage
- ▶ They lose competitiveness in the face of preferences obtained by third parties who sign trade agreements, e.g. the case of Colombia and Peru gaining better conditions in the European Union and United States
- ▶ Another way to lose is due to trade diversion. Granting preferences to third parties may harm partners without agreements.
- ▶ An indirect way to lose is to give preferences and low tariffs to similar but better quality products. The risk there is raising the costs for economic agents.



# Lessons Learned

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- ▶ A trade agreement is not the panacea or solution to all the structural problems facing an economy
- ▶ Trade benefits from open trade are not evenly distributed
- ▶ Not everybody wins within a country
- ▶ There are winning sectors and losing sectors
- ▶ The great challenge of public policy is to balance the imbalances
  
- ▶ **Inclusiveness is critical. One method for inclusion is adopting complementary policies**



# Complementary policies matter and are crucial for vulnerable sectors

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- ▶ Trade openness depends on a number of factors beyond free trade
- ▶ A trade agreement is not the panacea or solution to all the structural problems facing an economy
- ▶ For these reasons, complementary trade policies that allow low-income persons to benefit from trade are key:
  - ▶ Investment in human capital
  - ▶ Investment in infrastructure
  - ▶ Policies to support macroeconomic stability
  - ▶ Access to credit and technical assistance for producers, especially agricultural producers
  - ▶ Labor market reforms: create institutions that promote labor mobility
  - ▶ Mitigation policies to help low-income persons that are negatively affected by trade: transfers, subsidies, etc,



# Enhancing the Contribution of Preferential Trade Agreements to Inclusive and Equitable Trade: Latin American cases

*Thank you*



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