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Chapter 1

Introduction: Why Study EU Trade Policy?

From the creation of the European Economic Community (EEC) in 1958 until today, the member states of the European Union (EU) have crafted a common commercial policy. With this momentous decision embodied in the Treaty of Rome, within a few years they abolished tariffs and other barriers to trade between themselves, and they delegated the setting of external tariff levels and of rules regulating trade with the rest of the world to the supranational, European level. Member states thus granted the Union exclusive competence in the conduct of external trade policy. Along with only a few other policy fields, such as the regulation of the internal market, competition policy or monetary policy, trade policy is one of the outright most important exclusive competences of the EU. This makes the Union similar to a country in the realm of trade policymaking and international trade law.

Although EU trade policy has enjoyed this position of primordial importance in overall European policymaking for over six decades now, the trade policy of the EU has attracted much more attention in recent years, from both the public and scholars. The Doha Round negotiations in the World Trade Organization (WTO) have been facing a stalemate: new trading powers besides the United States, Japan, Canada and the EU – formerly known as the Quad – have entered the world stage, and the trade agenda has broadened, mobilizing more, and more diverse, stakeholders. Despite the rise of emerging economies like Brazil, India and particularly China, the EU's trade policy still matters in world politics because it remains the largest single market, trader and investor. Due to its sheer market size and its pivotal role in world trade, the EU is an economic and political powerhouse to be reckoned with by all other countries. Although the common commercial policy is the oldest and most integrated external policy of the EU, and a field in which the EU actually wields considerable power, it has – compared to EU foreign

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policy – not been the subject of many dedicated textbooks. This introductory chapter sets the scene by asking why countries trade, to what extent the EU is a trade power and what factors other than legal competence shape EU trade policy.

Why do countries trade?

One of the most standard economic explanations for why countries trade is because they expect gains from a favourable trade policy. Economies can gain by specializing in the sectors in which they have a comparative advantage – that is, activities in which they encounter lower opportunity costs (in terms of how much of a good country has to give up in order to release enough resources to produce more of another good). It can be efficient to specialize in a narrow range of activities so as to earn income to buy a wide range of goods and services from abroad. Comparative advantage can explain inter-industry trade between countries that are different in terms of technology or how they have been endowed with factors of production.

Countries can also gain from trade due to the existence of economies of scale in production – that is, when a larger amount of production can be achieved at a lower cost. Economies of scale can be found particularly in industries that have large fixed costs in production (e.g. chemicals, steel and automobiles). The larger the output, the more the costs of the equipment can be spread out among more units of the good. In the presence of economies of scale, specialization and trade can increase productive efficiency. Economies of scale can explain intra-industry trade between similar countries (e.g. trade of different types of cars between the EU and the United States).

Besides allocative gains, technical efficiency gains are considered one of the most desirable effects of trade liberalization because exposure to foreign competition can function as an incentive for technological progress and access to innovation. It is thus potentially beneficial to have a trade policy to reap such gains; to obtain market access for domestic exporters, low-cost inputs for importers and larger varieties of goods and services for consumers; or to protect domestic producers and consumers if necessary. The fundamental changes in global supply chains, where companies participate in dynamic worldwide networks involving people, information, processes and resources in the production, handling and distribution of materials and finished products or providing services to the customers, have made it less important where exports are officially

recorded compared to where value added is in fact created. Trade is thus more and more about adding value from research and design to manufacturing of components, logistics or other services. This has made the protection of intellectual property and investments abroad more essential. As companies become more dependent on the protection of their patented products or copyrights, their governments are more inclined to ensure this protection through international law. Similarly, companies may attach greater importance to the legal status of their investments abroad since global supply chains have become pivotal to their survival and success, incentivizing governments to enlarge the international legal framework. At the same time, public authorities are also likely to turn more to ensuring fair and equal access to other markets as well as other countries' public procurement and to defend their companies against unfair competition.

Why do EU member states trade under a common policy?

The EU has in the first place a common commercial policy because it was and is a customs union. This means that custom tariffs levied at the EU external borders are exactly the same, regardless of which member state they enter the territory of the EU through. The same basic principle applies to providers of foreign services that want to engage in business within the EU. The advantage of this internal unification and liberalization has been and still is that it is relatively easier for the EU to open up markets abroad for European exports and investments. Although the economies of the EU member states also compete with each other when it comes to promoting exports or attracting foreign investment, together the Union has much more bargaining leverage for defending the interests of EU companies and citizens. A customs union constituted an important step in the European project, and it ensured the closer economic and political integration of West Germany. In addition, this step created necessary revenue for the EU. Finally, the common commercial policy can flank and assist other EU policies, notably development cooperation and foreign policy (see also Buonanno and Nugent, 2013, pp. 251–254).

What is thus commonly called 'trade policy' are those public policies that regulate the trans-border movement of goods and services. Generally, this concerns states, but in the case of the EU, this policymaking capacity is located entirely at the supranational, European level. The member states of the EU have liberalized trade in goods and services internally and established external tariffs for goods and uniform rules

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for the conduct of their trade policies towards the EU's trade partners. In comparison to most other public policy fields, like welfare state policies or the provision of public health, education, justice and policing, trade policy is one of the very few policy fields in which the EU has state-like competences – along with a monetary policy in the eurozone or a competition policy against anti-competitive behaviour by firms.

Trade policy has a direct impact on EU companies and citizens. Millions of European jobs depend on exports and on foreign direct investment (FDI). In a special 2010 Eurobarometer, 44 per cent of respondents across the EU said that they personally benefited from international trade, in particular by cheaper products and wider choice, whereas 39 per cent said that they did not benefit (European Commission, 2010c). Moreover, two-thirds (65 per cent) of Europeans thought that the EU was benefitting a lot from international trade. For the future, in light of the recent economic crisis, the creation of jobs in the EU was considered the most important priority for trade policy. Although trade is not directly associated with social and environmental standards, almost 40 per cent of respondents said that they were willing to pay more for goods and services that support certain values (*ibid.*).

Apart from this internal importance of trade policymaking for the member states, trade policy decisions of the EU have always been of considerable significance for its trading partners. The EU very much acts as any other state within the international trading system, and it 'speaks with one voice' to the outside world. Whether for developed countries, other regions, developing countries or least developed countries, EU decisions affect them due to the sheer size of the EU internal market.

The EU as a trade power

Table 1.1 compares the EU with other major established or emerging economies in the world, including the Quad and the BRICS countries (Brazil, Russia, India, China and South Africa): their relative shares of global domestic product (GDP), of trade in goods and services and of FDI inward and outward stocks.

China has in recent years started to bypass the EU and the United States in terms of its share of GDP and its share of trade in goods. Yet, the EU is still the biggest trader in services as well as the most important provider and host for FDI.

TABLE 1.1 *The EU in the World Economy (in per cent, 2016)*

	<i>Share in world GDP</i>	<i>Share of trade in goods</i>	<i>Share of trade in services</i>	<i>Share of FDI inward stocks 2015</i>	<i>Share of FDI outward stocks 2015</i>
EU-28	16.7	15.1	22.5	37.8	48.0
US	15.5	14.4	17.0	33.2	37.7
Canada	1.4	3.2	2.4	4.6	7.0
Japan	4.4	5.0	4.8	1.0	7.8
Brazil	2.6	1.3	1.3	2.9	1.1
Russia	3.2	1.9	1.7	1.5	1.6
India	7.2	2.5	4.0	1.7	0.9
China	17.8	14.8	9.0	7.2	6.3
South Africa	0.6	0.6	0.4	0.7	1.0
South Korea	1.6	3.6	2.8	1.1	1.8

Source: Based on European Commission (2017b, pp. 20, 30, 31, 68).

Table 1.2 ranks the 20 major trading partners of the EU in terms of export and imports of goods. When it comes to trade in services, the largest partners by far are the United States (27.2 per cent of EU exports and 31 per cent of EU imports in 2015), followed by neighbouring Switzerland and then China, China with a considerably lower share of 4.5 per cent in exports and 3.8 per cent in imports (European Commission, 2017b, p. 59). The transatlantic relationship is still crucial for the EU, although China has been catching up in its bilateral trade with the EU.

The EU is thus a trade power and of systemic importance for the world trading system. For example, the active support of the EU for the multilateral negotiations on trade liberalization from 1986 to 1994, at a time when the EU was completing its own internal market, was vital for the establishment of the WTO in 1995. The EU's longstanding relationship with some of the poorest developing countries, first and foremost the African, Caribbean and Pacific (ACP) states, has had a lasting impact on the global trade regime, as has its decision in 2001 to

6 *The Trade Policy of the European Union***TABLE 1.2** *The EU's Major Trading Partners: Trade in Goods (2016)*

<i>EU exports to ... (in per cent)</i>		<i>EU imports from ... (in per cent)</i>	
1. United States	20.8	1. China	20.2
2. China	9.7	2. United States	14.5
3. Switzerland	8.2	3. Switzerland	7.1
4. Turkey	4.5	4. Russia	7.0
5. Russia	4.1	5. Turkey	3.9
6. Japan	3.3	6. Japan	3.9
7. Norway	2.8	7. Norway	3.7
8. United Arab Emirates	2.6	8. South Korea	2.4
9. South Korea	2.6	9. India	2.3
10. India	2.2	10. Vietnam	1.9
11. Canada	2.0	11. Brazil	1.7
12. Hong Kong	2.0	12. Canada	1.7
13. Mexico	1.9	13. Taiwan	1.5
14. Saudi Arabia	1.9	14. South Africa	1.3
15. Australia	1.9	15. Malaysia	1.3
16. Singapore	1.8	16. Thailand	1.2
17. Brazil	1.8	17. Mexico	1.2
18. South Africa	1.3	18. Singapore	1.1
19. Israel	1.2	19. Saudi Arabia	1.1
20. Morocco	1.2	20. Hong Kong	1.1

Source: Based on European Commission (2017b, p. 58).

grant duty- and quota-free access for all goods (except arms) coming from the least developed countries. The EU is a champion of the rules-based multilateral trading system, and it was a pace setter in the late 1990s for the WTO's first trade round. Only when it became evident that the Doha Round, launched in 2001, would not deliver the expected results in a reasonable period of time did the EU revert to engaging in an extensive and growing network of bilateral preferential trade agreements. To take another example, the EU's decision in 2013 to impose

so-called anti-dumping measures against heavily subsidized and under-priced solar panels manufactured in China affected the structure of the world market for this good, and it shaped Europe's relationship with the new commercial powerhouse of the world, which had joined the WTO in 2001.

Furthermore, the significance of the EU's common commercial policy becomes eminently clear when considering how very recent developments in world politics have been crucially intertwined with questions of trade policy. For instance, since 2013, the EU had been engaged in bilateral trade and investment agreement negotiations with the United States. With the arrival in office of the new US Administration under President Trump in January 2017, however, these bilateral negotiations were put on ice. As a first act in trade policy, the US President withdrew the United States from the Trans-Pacific Partnership signed in 2016. The announcement that the United States may deviate from its free trade policy and support of the WTO poses serious challenges to EU trade policy.

In times of internal and external crises, open markets often come under (protectionist) pressure. The EU has in recent years been facing multidimensional challenges. First of all, the EU had to deal with economic and financial challenges as a result of the banking and ensuing sovereign debt and eurozone crises that hit Europe since 2008. Second, the EU faced a governance crisis in the wake of what was often referred to as a 'refugee or migration crisis' during 2014–2015, when hundreds of thousands of asylum seekers from Syria and other conflict countries as well as irregular migrants arrived in the EU and at its borders. Third, protests against deep and comprehensive free trade agreements and a wave of right-wing populism and increased Euroscepticism have been on the rise in many EU member states, undermining European solidarity and common policies. A major fracture in this regard was the decision by referendum in June 2016 that the United Kingdom, one of the largest and most important EU member states with regard to international trade, would leave the EU. 'Brexit' means that the United Kingdom will forsake its free access to the European internal market and will become subject to some of the restrictions that many other countries face when they want to trade with the EU. After agreeing on the terms of withdrawal, the United Kingdom and the EU will have to negotiate a new trade relationship, and the EU's relative position in the world economy will weaken.

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Questions of trade policymaking are of course embedded in the broader framework of the EU's external policies in the field of development, environmental cooperation, security and human rights, to name but some of the most important ones. In contrast to EU trade policy, though, these policy fields are governed by another set of decision-making rules. Nevertheless, the scope of what is commonly called 'trade policy' or 'commercial policy' has gradually been widened to cover a vast array of policy measures on regulatory affairs. This gradual expansion of the remit of trade policy was primarily driven by the requirement to start coordinating standards such as those on public health or environment, the standardization of customs valuation methods, the gradual integration of trade in services into international economic agreements, the growing importance of intellectual property rules, rules of origin or public procurement, attempts to limit ruinous subsidy races and many more regulatory matters. Since the 1980s, these issues have taken centre stage in the multilateral negotiations taking place within the framework of the General Agreement on Tariffs and Trade (GATT)/WTO.

The founding members of the EEC were also early contracting parties to the 1947 GATT, and soon after the completion of the customs union, the EEC de facto acquired member status (see Box 1.1 and Chapter 5). The 1994 WTO Agreement (Art. XI) stipulates that all contracting parties to GATT and the European Communities become founding members of the WTO. EU membership of the WTO is possible because any customs territory having full autonomy in the conduct of its trade policies can join the organization. In a nutshell, the WTO is an international organization operating a system of trade rules guaranteeing the stability and predictability of tariff levels granted on a non-discriminatory basis, a forum for negotiating further trade liberalization agreements and an institution to settle trade disputes at the global level.

The gradual expansion of international cooperation in the area of trade and the negotiation of new regulatory agreements on trade-related topics constituted one of the major developments to which the EU contributed and to which EU trade policy had to adapt over time. While being an important member of the WTO, the EU in parallel has been engaging in the conclusion of bilateral and/or regional trade agreements, in turn creating new challenges to EU trade policy (see Chapter 7).

This book deliberately refrains from the formulation of broad sweeping statements of what the EU *should* do, nor does it engage in the formulation of bold predictions of how the EU is likely to act *in the future*. Rather, this book intends to explain how the institutions and

**Box 1.1 Global multilateral trade regime:
GATT/WTO**

Next to the creation of the World Bank for Reconstruction and Development and the International Monetary Fund for international monetary cooperation, the United States of America and the United Kingdom rallied countries around their initiative to create a third international institution for trade. Over 50 countries participated in negotiations to create an International Trade Organization (ITO) as a specialized agency of the United Nations. An ambitious ITO Charter was agreed in 1948, but ratification proved impossible in some national legislatures, especially in the US Congress. However, the GATT, signed in 1947, was already provisionally applied. This agreement then provided the rules for much of world trade for almost 50 years, and member states used the GATT forum to reduce tariffs step by step in most economic sectors, in a series of multilateral negotiations known as ‘trade rounds’. The economic recessions in the 1970s drove many governments to devise other forms of protection for sensitive sectors. By the end of the Cold War, tariff liberalization in international trade in goods had become very substantial, yet new forms of non-tariff barriers – large-scale negotiated exceptions for developing countries and for some economic sectors, notably textiles and agriculture – had come to characterize the global trade regime. On the other hand, trade in services and international investment had expanded with the globalization of the world economy. These developments contributed to member states’ willingness to reinforce the multilateral trading system. The GATT Uruguay Round, which lasted from 1986 to 1994, led to the creation of the WTO. Whereas GATT had dealt with trade only in goods, the WTO agreements also covered trade in services, trade-related intellectual property rights and investment measures. Moreover, the organization acquired more clout through the reinforcement of its dispute settlement procedures.

Source: Based on WTO website.

decision-making processes are organized and how this setup fosters particular policy outcomes at the detriment of others. On the broadest level, perhaps the most important characteristic of European trade policymaking is that it is governed by super-majorities. All key decisions, as well as non-decisions, come about only when there is qualified majority

or even consensus support from the 28 (soon 27) governments of the EU member states, an absolute majority in the European Parliament and often also the approval of national parliaments. The consensual or super-majoritarian nature of EU decision-making, and of trade policy-making in particular, often bewilders observers alleging that it is elitist, bureaucratic, protectionist, insufficiently transparent or too neoliberal. However, this book contends that none of these allegations really do justice to EU trade policymaking, since consensual political systems are in the first place characterized by a great deal of stability, making them prone to conservatism and the continuation of policies that were in place before. Consensual political systems generate their policy effects in a structural fashion, reproducing certain policy practices over a long period of time and allowing for gradual changes only when these gain support from a wide variety of actors.

Given that trade policy touches on many legal, economic and political questions, this textbook takes a rather pluridisciplinary approach. In the study of EU trade policy, lawyers tend to focus on the competence allocation between the EU and its member states; economists on the economic benefits of trade and their distribution; political scientists on the competition of interest groups and their access to policymakers; and international relations specialists on the role of the EU as a global player. Each of these perspectives makes a contribution to understanding EU trade policy.

Beyond the distribution of legal competences, which will be set out in Chapter 2, many other factors have an impact on the contents of EU trade policy. Economic and societal stakeholders, developments in other policy fields, trade policies of non-EU states and international political developments all play a role in shaping decisions.

Shaping the contents of EU trade policy

This section deals briefly and in a cursory manner with some major elements that influence the contents of the common commercial policy. Each of them will be elaborated in greater detail in the subsequent chapters.

Aggregating preferences

In pluralist societies the preferences of the negotiator usually reflect the aggregation of different domestic constituencies mediated through domestic and European institutions (see Chapter 4). For the conclusion of trade

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