



The Use of the EU's Free Trade Agreements

Exporter and Importer Utilization
of Preferential Tariffs

Produced in collaboration between
the National Board of Trade Sweden
and the United Nations Conference
on Trade and Development (UNCTAD)

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About the National Board of Trade

The National Board of Trade is a Swedish government agency responsible for issues relating to foreign trade, the EU Internal Market and to trade policy. Our mission is to promote open and free trade with transparent rules. The basis for this task, given to us by the Government, is that a smoothly functioning international trade and a further liberalised trade policy are in the interest of Sweden. To this end we strive for an efficient Internal Market, a liberalised common trade policy in the EU and an open and strong multilateral trading system, especially within the World Trade Organization (WTO).

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Preface

The issue of free trade negotiations has increasingly become the focus of the trade policy agenda. As such, it is increasingly important to base negotiating proposals and policy decisions on empirical data and objective facts. This report – prepared in collaboration between the National Board of Trade Sweden and the United Nations Conference on Trade and Development (UNCTAD) – constitutes a first effort to analyse the use of tariff preferences in free trade agreements from both parties and from both an exporter and importer perspective. The observations and findings are based on the EU's free trade agreements with a number of developed and developing countries. The EU is one of the principal negotiators of free trade agreements on a global level and one of the few free trade parties where data on preference utilization is – more or less – publicly available. The findings may, however, be relevant for all free trade agreements in force and under negotiation.

This report challenges some enduring myths on preference utilization in free trade agreements. For example, it is commonly believed that free trade agreements, in general, are not used to a high degree. Empirical data, on the other hand, as presented in this report, indicates that the EU's free trade agreements, in general, are used to a high degree and that border-related aspects of implementation of the free trade agreements in some cases might be more cumbersome than the provisions of the free trade agreements themselves. In addition, the report indicates that both the EU and partner countries – and both exporters and importers – are benefitting from the use of the EU's free trade agreements. However, there is still a great potential to increase the preference utilization in the EU's free trade agreements in the future.

The focus of this report is on the EU's free trade agreements, but – hopefully – at some moment in time, the analysis of the use of free trade agreements might be expanded to also cover other regions, as soon as data on preference utilization become available. Ideally, however, analyses of the utilization of preferences should be carried out by the free trade parties themselves with the objective to target 'pockets of underutilization' and facilitate the utilization of preferences by all – different sectors of the economy, and large and small companies alike. UNCTAD and the National Board of Trade Sweden hope that the report "The Use of the EU's Free Trade Agreements: Exporter and Importer Utilization of Preferential Tariffs" will inspire progress in the analysis of preference utilization of free trade agreements based on empirical evidence in the future.

Stockholm, January 2018



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Executive Summary

In the last few decades, there has been a proliferation of free trade agreements on a global level. The European Union (EU) is one of the most prolific negotiators in recent years. Even though the scope and depth vary across the free trade agreements, they all have the overarching purpose of reducing or removing tariffs and other obstacles to trade between the partner countries.

In reality, however, the reduction or removal of tariffs within a free trade agreement through so-called tariff preferences does not necessarily mean that all products can move freely across the borders. For example, parties of a free trade agreement have to comply with substantive and administrative requirements to prove the origin of the products in order to benefit from tariff reductions. However, companies may be unable to comply with these requirements. Instead of taking advantage of the tariff reduction, companies may have to pay the tariff that applies to other countries that are not part of the free trade agreement.

With this as a background, it is increasingly relevant to analyse to what extent companies in the EU and its partner countries actually use the existing free trade agreements in order to obtain tariff reductions for their products. In order to facilitate the analysis, this report presents data on the use of the possible tariff reductions for both parties of the EU's free trade agreements, and from both an exporter and importer perspective. The report also presents data on the values of exports and duty savings obtained by using the EU's free trade agreements – as well as the values of exports and duty costs paid by not using the EU's free trade agreements.

The main findings from the analysis are the following:

- About two-thirds of EU exports to partner countries use the free trade agreements whereas the corresponding number for partner country exports to the EU is as high as 90 percent. These numbers are, however, based on the value of exports and may not necessarily imply that most companies use the free trade agreements. This means that even though most trade in terms of value takes advantage of the tariff reductions, there might still be a large number of smaller companies that do not take full advantage of the benefits of free trade agreements. The import perspective mirrors the export perspective.
- The value of exports using the free trade agreements is higher for EU exporters than for partner country exporters – the net difference is 33 billion euro. However, the value of exports not using the free trade agreements is also considerably higher for the EU than for partner countries – the net difference is 60 billion euro. This amount is a lost opportunity or future potential for EU exporters.

- The value of duty savings by the partner country importers of using the free trade agreements is higher than the value of duty savings by the EU importers — the net difference is 1.5 billion euro. However, the absolute value of duty costs by partner country importers of using the free trade agreements is also considerably higher for the partner countries than for the EU — the net difference is 3.1 billion euro. This amount represents a lost opportunity or future potential for partner country importers
- The largest under-utilization of the EU's free trade agreements is found among EU exporters in their trade with Tunisia, Morocco, Egypt, Lebanon and Mexico. The one-sided under-utilization of the possibilities for tariff reduction in these free trade agreements account for about 40 percent of the total value of exports or duty costs of not using the EU's free trade agreements (or as much as 80 percent if only the medium-sized free trade agreements are considered). This one-sided under-utilization of the possibilities for tariff reduction is, accordingly, a large lost opportunity or future potential in the use of the EU's free trade agreements. This one-sided under-utilization of preferences might be border-related and in need of trade facilitation initiatives. The import perspective mirrors the export perspective.
- The duty savings obtained by using the EU's free trade agreements benefit both the EU and partner countries. The duty savings are on average about 6 percent of the import values for both parties of the EU's free trade agreements. This implies that both parties benefit from the use of the EU's free trade agreements to a fairly equal degree at a total level.

Even though the use of the possibilities of tariff reductions in the EU's free trade agreements is on average about 75 percent, it is important to identify possible pockets of low utilization at a more detailed level. The identification of possibly cumbersome provisions and their causes is an important step to improving the export and/or import performances of the EU and its partner countries, and the possibilities to actually benefit from tariff reduction in free trade agreements. These pockets of low utilization have to be identified in the individual free trade agreements and at an industry and/or product-specific level. It is also important to identify the main incentives or 'drivers' for using and/or obstacles for not using the EU's free trade agreements in order to provide more empirical facts for the understanding of the use of free trade agreements in reality. This will be the focus of future research by the National Board of Trade Sweden and UNCTAD.

This report aims to inspire future analysis of the use of free trade agreements by making data on their use more publicly available. The monitoring of the use of free trade agreements should preferably be an ongoing exercise in order to identify and analyse to what extent exporters and importers actually use them in their business decisions, in order to make the free trade agreements work for all.

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Introduction

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In reality, however, the reduction or removal of tariffs within a free trade agreement through so-called tariff preferences does not necessarily mean that all products can move freely across the borders. For example, parties of a free trade agreement have to prove the origin of the products in order to benefit from tariff reductions. The process of proving origin for products can in some cases be so demanding that companies, instead of

taking advantage of the tariff reduction, choose to pay the tariff that applies to other countries that not are part of the free trade agreement.

With this as a background, it is increasingly relevant to analyse to what extent companies in the EU and its partner countries actually use the existing free trade agreements in order to obtain tariff reductions for their products. In order to facilitate the analysis, this report presents data on the use of the possible tariff reductions for both parties of the EU's free trade agreements, and from both an exporter and importer perspective. The report also presents data on the values of exports and duty savings obtained by using the EU's free trade agreements – as well as the values of exports and duty costs paid by not using the EU's free trade agreements.

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