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Translation of article published November 11, 2014
in the Danish daily news paper Information

New research study: TTIP will have adverse effects on GDP, exports and jobs

If you choose a macroeconomic model different from the one the EU Commission and the Danish government rely on when calculating the outcome of a Transatlantic Trade Agreement, you end up getting quite opposite results for the EU and Denmark, says the author of a new model-based macroeconomic study

According to a new study of the economic impact of the Transatlantic Treaty on Trade and Investment, the TTIP will lead to the dis-appearance of 600,000 jobs within the EU. Exactly the opposite of the European Commission's calculations, which - as seen in the left side of the illustration – states that the Trade agreement will create 15,000 jobs./

Sofie Holm Larsen / iBureauet.
Note: The above 600,000 was misquoted as 200,000 in the original article, and has been corrected by the translator

By Jørgen Steen Nielsen

A Transatlantic Treaty on Trade and Investment Partnership between the EU and USA will not increase GDP, exports or employment as claimed by the EU Commission, the Danish government and the Confederation of Danish Industry. On the contrary the so-called TTIP could lead to losses on all three accounts, especially in Northern European countries like Denmark.

This conclusion is reached in calculations of the consequences of TTIP presented in a recent research study by Jeronim Capaldo, economist and researcher at Tufts University, Massachusetts, USA, and staff member of the UN's International Labour Organization, ILO.

According to the working paper, titled *The Trans-Atlantic Trade and Investment Partnership: European Disintegration, Unemployment and Instability*, the Northern European countries will suffer export losses in the magnitude of two per cent of GDP, lower growth rates, a loss of more than 200,000 jobs, downward pressure on wages, and loss of revenue for the public coffers.

»TTIP appears to favour economic dis-integration, rather than integration, in Europe. At a minimum, this shows that official studies do not offer a solid basis for an informed decision on TTIP,« Jeronim Capaldo concludes.

The results conflict directly with reports from, among others, The European Commission (EC). The EC website states that a trade treaty with the United States can strengthen the EU economy with 120 billion Euros, giving an average EU family an annual gain of 545 Euros and create hundreds of thousands of European jobs. In a Danish context, the Confederation of Danish Industry claims that the agreement could increase Denmark's exports by 27 billion DKK (3,6 billion Euros), create 15,000 new jobs and lead to lower prices on many goods for the Danish consumers.

The ongoing negotiations between the EU Commission and the US Government started in the summer of 2013. The ambition is to reach an agreement that abolishes all or most of the remaining trade tariffs and - more importantly - harmonizes the European and US regulations and standards, in order to streamline trade and investments between the two regions and increase exports in both directions across the Atlantic.

The official reports about the economic and employment gains from the TTIP are based on studies using so-called computable general equilibrium models - CGE models - the same type of model as the Danish DREAM model used by the Economic Council. The most widely cited TTIP-study with the positive results is produced for the European Commission by the UK-based Centre for Economic Policy Research (CEPR).

The critique

Like several other economists Jeronim Capaldo criticizes the use of equilibrium models in the current context and thus also the CEPR study and its conclusions.

CGE models build on a wide range of assumptions, including a core assumption of 'full employment', in the sense that the market mechanism ensures that everyone who - as a consequence of a trade and investment treaty - loses their job in one industry are automatically absorbed and employed in other industries. When a TTIP deal with increased competition across the Atlantic slashes some companies or does away with them completely, the unemployed labour will quickly find new jobs in other companies benefiting from the trade liberalization.

»These models exclude, per definition, any negative effect on employment. The CGE models specify and assume an equilibrium for every market in the economy including the labour market: no part of the labour force can ever be idle or superfluous,« Jeronim Capaldo explains. Prior to his position at the ILO, Capaldo worked with modelling international trade at the United Nations' Department of Economic and Social Affairs (UNDESA). He has also worked with the UN Food and Agriculture Organization (FAO).

The mechanism which - according to the CGE models - ensures the equilibria is the change of prices, including wages: A trend toward higher unemployment will reduce wages, whereby the demand for labour increases and 'full employment' is restored.

»In practice, however, this "full employment" mechanism has rarely operated. In many cases, less competitive sectors have contracted quickly while more competitive ones have expanded slowly or insufficiently, leaving large numbers of workers unemployed.«

»One need only look at the experience of Europe in the last decade to see that full employment does not re-establish itself even if job seekers are willing to work informally and at relatively low pay,« states Capaldo.

He points to the experience from trade liberalizations in Latin America, where general equilibrium models predicted only positive effects, but in fact had several negative consequences for employment and the economy.

The UN model

In recognition of the simplified assumptions in CGE models about a market that ensures an equilibrium, UNDESA has developed the Global Policy Model (GPM), based on economic research at Cambridge University. The model is used by - among others - the UN Agency for Trade and Development (UNCTAD), and is also the basis of Jeronim Capaldo's analysis of the consequences of a TTIP agreement between the EU and the USA.

»The UN model was developed in order to avoid the shortcomings of the general equilibrium models. It assumes neither full employment nor perfect price flexibility. That is, the model does not assume that changes in prices and wages stemming from a trade agreement automatically fix all imbalances in the system, including restoring full employment,« Capaldo explains.

Instead the UN model attaches central importance to the level of effective demand: If, for example, an industry in a country or in a group of countries loses sales due to stronger competition following a trade treaty, then the dismissal of employees will reduce the purchasing power of the employees laid off and thus reduce the demand in the economy. Lower demand can lead to further layoffs in other industries, and further declines in demand, with negative consequences for the economy in general. In sectors where a trade agreement leads to a higher revenue, more jobs and increased demand, the mechanism is the opposite.

»Using the UN model is appropriate for large projects such as the TTIP, where the impact on employment is a key issue,« says the American economist.

In his GPM analysis of the consequences for the European economy and employment of a Transatlantic Treaty, Jeronim Capaldo ends up with the conclusion that »seeking a higher trade volume is not a sustainable growth strategy for the EU«.

The negative consequences
As far as Europe is concerned the concrete results of his analysis differ dramatically from those based on general equilibrium models and presented by the EU Commission, the Danish government and the Confederation of Danish Industry:

TTIP would lead to losses in terms of net exports after a decade, compared to the baseline “no-TTIP” scenario. Northern European economies would suffer the largest losses (2.07% of GDP) followed by France (1.9%), Germany (1.14%) and United Kingdom (0.95%).

TTIP would lead to net losses in terms of GDP, again with Northern Europe suffering the largest reduction: -0.50%.

TTIP would lead to the loss of approximately 600,000 jobs in the EU, of which 223,000 in Northern European countries, and besides to a loss of labour income of 4,800 Euros per worker.

TTIP would lead to a loss of government revenue in all EU countries, with France suffering the largest loss, thus pushing up government deficits as a percentage of GDP.

As a consequence, TTIP would lead to higher financial instability as well.

The analysis predicts – as does the European Commission's CEPR study – a growth in total trade between TTIP countries. When Capaldo's study nevertheless points to a negative outcome for the EU, this is partly because the increased trade with the United States leads to less internal trade within the EU.

»The biggest losers will be those in the EU who trade mostly internally between EU countries and do not export much to the United States - or those who import a lot from the US. According to the model the Northern European countries will be affected by this, « says Jeronim Capaldo.

At the same time the TTIP will put extra pressure on countries that treat their workers well in terms of pay, etc., because these countries will find themselves in fiercer competition with the US and with other economies with low production costs stemming from low wages.

Increased unemployment and falling wages will reduce demand and send the economy into a downward spiral and increase the pressure on the public coffers.

»In the current context of austerity, high unemployment and low growth, increasing the pressure on labour incomes would further harm economic activity«, the research paper concludes, adding that an already fragile EU in a transatlantic single market will be even more vulnerable to a possible crisis in the USA, than in 2007-2008 when the financial crisis was unleashed in the United States.

Uncertainties in every model

- *Some economists say that models of the UN-type are able to provide the best predictions in the short term, while CGE models are better for long term predictions - because the market in the long term will overcome imbalances. Isn't that a fair description?*

»No, I do not think so. And I do not find it useful to base policy decisions on an equilibrium model that comforts you by predicting we shall reach an equilibrium eventually – when in real life I can see that the disequilibrium actually continues. In reality there are countries out there that have been struggling with high unemployment for 15-30 years.«

- *The CEPR analysis presented by the EU Commission has been criticized for stating very precise figures for growth, employment, etc., when it is well known that these are based on lots of assumptions and there is much uncertainty in the calculations. Doesn't this go for your calculations, too?*

»Absolutely. There is no doubt that the precision you can achieve is quite limited. I do not present these calculations claiming they are absolutely true - although I think they are more reasonable - but only to show that a different set of assumptions can lead to dramatically different results concerning the effect of a TTIP agreement. «

The Danish news paper's website

Link to the article in Danish

Link to Jeronim Capaldo's research paper at Tufts University