



The European Union's Sustainability Impact Assessment (SIA) Study of the Euro-Mediterranean Free Trade Area (EMFTA)

Sustainability Impact Assessment of the Euro-Mediterranean Free Trade Area

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Executive Summary

This report presents the results of a sustainability impact assessment (SIA) study undertaken for the European Commission to assess the economic, social and environmental impacts of the evolving Euro-Mediterranean Free Trade Area (EMFTA). It synthesises the findings of the previous stages of the study and presents overall conclusions and recommendations. The results are intended to provide information for the trade negotiations and for the development of parallel policy measures to enhance the beneficial impacts of the EMFTA and to avoid or mitigate adverse ones. The principal findings of the study are presented in this Executive Summary, together with recommendations for negotiators and policy-makers in the EU and Mediterranean Partner Countries (MPCs).

It should be noted that the recommendations made in this report represent the views of the consultants and should not be interpreted as being endorsed by the European Commission. They are intended to form a basis for discussion among stakeholders of the most appropriate means of incorporating the SIA findings into the future development of the Euro-Mediterranean Free Trade Area and the Euro-Mediterranean Partnership.

The SIA analyses the impacts of four components of a postulated EMFTA scenario, in comparison with a without EMFTA baseline scenario. These four components cover removal of tariff and non-tariff barriers for: industrial products; agriculture; services; and south-south trade liberalisation. Liberalisation of industrial products is as defined in the current Association Agreements between the EU and MPCs. For the other three components, the postulated scenario includes all the major issues covered by the ongoing negotiations. For industrial products, some of the impacts will already have occurred in those MPCs that have begun tariff reductions. This is taken into account in the assessment.

For all four components of the EMFTA scenario, significant impacts will be specific to the conditions in individual countries, and will vary in particular according to the level of existing tariff and non-tariff barriers and the proportion of EU trade in a country's total international trade. Impacts are also time dependent, with variations in both magnitude and direction between the short term, medium term and long term.

The assessment initially gives worst case indications of potential impacts, assuming that no mitigating actions are taken. It then proceeds to assess potential policy measures to mitigate adverse impacts or enhance beneficial ones.

Principal findings

Impacts in the EU

The economic impacts for the EU are expected to be beneficial overall for all four components of the EMFTA scenario, but small in terms of direct economic efficiency. Larger economic gains may occur in the longer term for services, and to some extent for industrial products, associated with investment effects. These cannot be forecast with certainty as they will be strongly dependent on individual investment decisions and other aspects of economic and development policy in both the EU and MPCs.

For agricultural liberalisation the economic benefits may be accompanied by significant adverse social impacts in local areas of the EU if not remedied by parallel mitigation

measures. These impacts are mainly restricted to rural areas of southern European countries, where the types of crops grown are similar to those produced in MPCs. In some areas the affected workers will include temporary migrants from MPCs, with a knock-on effect on social issues in MPCs.

Both positive and negative environmental effects in the EU are expected. Impacts on water resources, agricultural pollution and biodiversity are generally beneficial, while those on the agricultural value and amenity value of rural environments may be adverse.

Impacts in MPCs

In terms of direct effects on consumer welfare the economic impacts in MPCs are generally positive and larger than in the EU, although a small short term negative effect is possible in some countries. For industrial products, welfare is expected to rise by an average of about 0.8% of GDP, ranging from slightly less than zero in some countries up to about 2% of GDP in others. For agriculture and services the additional welfare gain averages about 0.5% for each, with a small additional impact from south-south liberalisation.

As in the EU, larger economic gains may occur in the longer term, but these are strongly dependent on domestic reforms and investment decisions. In particular there are large potential economic benefits from fuller regional integration, but to achieve them, other policy measures are needed in addition to south-south trade liberalisation and the EU-MPC trade agreements.

The study identifies some social impacts in MPCs that are beneficial in the short term as well as the long term, and others that may be significantly adverse unless effective mitigating action is taken. The potential impacts of greatest concern are:

- a significant rise in unemployment, particularly for liberalisation of EU-MPC trade in industrial products and agriculture, and to a lesser extent for services and south-south liberalisation;
- a fall in wage rates associated with increased unemployment;
- a significant loss in government revenues in some countries, with potential for consequent social impacts through reduced expenditure on health, education and social support programmes;
- greater vulnerability of poor households to fluctuations in world market prices for basic foods;
- adverse effects on the status, living standards and health of rural women, associated with accelerated conversion from traditional to commercial agriculture.

Similarly, both positive and negative environmental impacts are expected in MPCs. The main potential adverse impacts that have been identified are:

- significant local impacts on water resources, soil fertility and biodiversity in areas of high existing stress;
- higher environmental stress in cities, resulting from declining rural employment and accelerated rural-urban migration;
- higher air pollution and coastal water pollution from greater international transport;
- higher waste generation from greater use of packaging materials.

Many of these potential impacts would occur primarily in the short or medium term, although this may be as long as ten to fifteen years over the full period of adjustment. Unless effective action is taken in the short term, some impacts may continue into the long term.

Global environmental effects

The assessment indicates an overall adverse impact on climate change and global biodiversity, arising primarily through the influence on greenhouse gas emissions of increased transport and changed consumption patterns in MPCs, and pressures for increased agricultural production in biologically sensitive areas in MPCs. These scale effects, which arise from increased trade and increased production and consumption, can in principle be countered by technology or regulatory effects. In itself, the EMFTA scenario that has been assessed does not include measures which will strengthen these positive effects sufficiently to counter the adverse ones. The study does however indicate an overall economic gain, part of which could be directed towards parallel actions to mitigate the expected impacts.

Impacts on the Millennium Development Goals

The SIA has implicitly evaluated the impacts of the postulated EMFTA scenario on the Millennium Development Goals (MDGs), through the core indicators that frame the SIA methodology. It shows that unless effective mitigating action is taken, there will be a small but significant adverse effect on Goals 1 (poverty), 2 (education) and 4 and 5 (health). Both positive and negative effects occur for Goal 7 (environment), while the impact on Goal 8 (global partnership) is positive. The potential adverse impacts arise primarily from a short term rise in unemployment and loss in tariff revenues, occurring mainly for liberalisation of industrial products, but with additional effects from the other components of the EMFTA scenario. Without effective mitigation, some of the short term effects may continue into the long term.

Recommendations for negotiators and policy-makers

The SIA study is not intended to make specific recommendations for the negotiating positions of the EU or MPCs. However, negotiators in all countries are urged to take account of the impacts discussed above, in developing their positions and throughout the ongoing negotiation process. In particular, they should note the potentially adverse effects on Millennium Development Goal 1 (extreme poverty and hunger), and the mixed effects on Millennium Development Goal 7 (environmental sustainability). Negotiators and policy makers are urged to satisfy themselves that measures such as those discussed below are being taken within the negotiations and alongside them, in sufficient degree to counter these potentially adverse effects.

Specific policy measures have been identified for actions which may be taken by the EC and MPC governments to mitigate adverse impacts and enhance beneficial ones. These are presented below in six categories:

- A. Trade-related measures
- B. Domestic policy in the EU
- C. Domestic policy in MPCs
- D. EU development assistance
- E. EU support for stronger global governance

F. Joint action to monitor the future evolution of EMFTA

Many of the recommended actions have been examined in more depth in the case studies undertaken during the SIA. These studies give examples of initiatives that have been taken to implement such actions, along with a discussion of their effectiveness and of related issues. Footnotes to the recommendations are presented in the main body of the report, to indicate aspects for which additional information can be found in the case studies.

A. Trade-related measures

Measures that may be taken within negotiated agreements include both the extent of liberalisation and the timing of implementation.

- A1. For *industrial goods*, the phasing of liberalisation may be adjusted to take account of the evolving conditions in individual MPCs, particularly in respect of the level of unemployment and the implementation of tax reforms to compensate for lower tariff revenues.
- A2. Similar flexibility in timing may be incorporated into agreements for *agriculture*, services and south-south liberalisation, and may be linked to the monitoring of actual conditions for key economic, social and environmental indicators.
- A3. For *agriculture*, special arrangements may be identified for those products for which large production changes are anticipated in either southern EU countries or MPCs. Such arrangements may be optimised by a thorough evaluation of the alternative options. This may for example take the form of collaborative research into the interacting impacts in both the EU and MPCs, including participatory evaluation on both sides of the Mediterranean of the alternative lifestyles of affected groups, and a fuller evaluation of the environmental issues. The options to be considered would include: continued protection for sensitive products; the removal of protection combined with programmes to support the multifunctional role of agriculture; phased transition from one to the other; and phased transition to full liberalisation. The timing of negotiations would need to be compatible with the availability of the research findings.
- A4. For *services*, special arrangements may be identified for those services for which strong regulation and/or government subsidies may be needed in order to avoid potentially adverse impacts. This may for example apply to distribution services (with potentially significant adverse impacts on small traders), environmental services (related to the availability and cost of supply to poor communities) and financial services (related to lenders' sensitivity to local cyclical pressures and gaps in the credit system). Such arrangements may for example include linking the timing of liberalisation to monitoring the implementation of the necessary regulatory reforms.
- A5. Similar arrangements may be incorporated into *south-south agreements*.
- A6. In negotiating these and other measures, negotiators are encouraged to note the specific effects discussed in the full SIA report, alongside the arguments presented by their counterparts in other countries.

B. Domestic policy in the EU

Adverse impacts within the EU occur primarily for agriculture.

- B1. Develop social policy and environmental policy for affected areas of southern EU countries in line with the findings of detailed research on *agricultural* reform, for example as developed for CAP reforms, extended to cover the specific impacts of EU-MPC liberalisation..

C. Domestic policy in MPCs

For all four components of the EMFTA scenario, action needs to be taken by MPCs to avoid or minimise significant adverse social and environmental impacts, and to enable the potential benefits to be realised.

- C1. Direct measures to help *industrial* companies increase their competitiveness against European companies, based on in-depth research into competitive strengths, weaknesses, opportunities and threats for key industrial sectors. Measures may for example include assistance to both large scale producers and SMEs to access appropriate information and funding for modernisation, schemes to facilitate the development of internal supply chains, mechanisms to strengthen the ability of producers to meet EU environmental, health and safety standards, and initiatives to strengthen the responsiveness of education and training systems to changing private sector needs.
- C2. Develop *national development strategies* in which sustainable agriculture and economically diversified rural development are fully integrated with urban development. Strategies should be based on further research into the social and economic capabilities of individual rural communities, particularly women and young people.
- C3. Measures to facilitate the transition to commercial *agriculture*, and to accommodate changes in the types of agricultural produce. These should be fully integrated with parallel measures to support the livelihoods of subsistence farmers and low income farm workers during the transition period. Facilitation measures such as land reforms, skills training and micro-credit schemes may be combined with temporary income support measures and initiatives to promote the development of rural industries and accelerate the creation of alternative sources of income in rural areas.
- C4. Measures to provide wider dissemination of information on *EU product standards* and other market access constraints and opportunities, and to facilitate certification to these standards.
- C5. The development of *integrated regional industrial and agricultural policies*, in order to take greater advantage of economies of scale within the region, and achieve greater synergy of development strategies.
- C6. The creation of *regional institutions* to undertake research into common issues of economic, social and environmental development, and contribute to the development of regional and national policy initiatives, such as developing a common system of rules of origin, and regional approaches to dismantling non-tariff barriers.
- C7. Cooperative investment in regional *transport and other infrastructure*.
- C8. Revised provisions for *food subsidies*, designed to buffer world price fluctuations.
- C9. Strengthened *environmental regulation*, particularly in relation to water resources, land use planning and controls, and protection of biological diversity.
- C10. Further research to identify those particular localities where *water stress* is already high and agricultural production rises are expected.
- C11. Assistance to large and small companies in *environmental management* and cleaner production systems.

- C12. Action to combat *climate change* and improve economic performance through the integration of energy efficiency and renewable energy initiatives into energy policy and related legal and institutional frameworks.
- C13. Promotion of environmentally sound *farming practices*.
- C14. Strengthening of environmental standards for *marine transport and commercial vehicles*.

D. EU development assistance

The development assistance programmes of the Barcelona process already address many of the issues in varying degrees. In order to counter the incremental effects of the EMFTA, these efforts need to be strengthened in particular areas.

- D1. Promotion of collaborative research among all MPCs into the cost-effectiveness of past measures and potential future ones to enhance the competitiveness of MPC *industrial* companies. Provision of technical and financial assistance for such measures, in a manner that is tailored to address specific local issues in individual MPCs, and which supports strategies and initiatives that are nationally driven with national long-term funding.
- D2. Assistance based on the experience of EU countries in developing efficient *tax systems* which replace the lost tariff revenues.
- D3. Support for incorporating *carbon taxes* into tax reforms.
- D4. Detailed research into the social and environmental impacts of *agricultural* liberalisation in MPCs and southern EU countries.
- D5. Where EU support is targeted at economic development in either urban or rural areas, this support should be designed in such a way as to promote measures which link rural development to urban development within an overall *national development strategy*.
- D6. Tailor and where necessary extend existing EU programmes on water issues to support MPC institutions in conducting further research to identify those particular localities where *water stress* is already high and production rises are expected.
- D7. Assistance with schemes providing wider dissemination of information on *EU product standards* and other market access constraints and opportunities.
- D8. Targeting of continued support for stronger *environmental management* towards measures that are particularly relevant to EMFTA impacts. This may for example include strengthening institutional capacity for integrated economic, social and environmental planning, and integrated urban-rural and industrial-agricultural planning.
- D9. If MPCs choose to wholly or partially privatise water services and other *environmental services*, assistance based on experience in EU countries may be provided in developing the necessary frameworks for regulating the industry and subsidising poorer sections of the community.
- D10. Assistance with strengthening institutional capacity for the use of *environmental economics* techniques in development planning.
- D11. *Coordination of all EU support* within the Barcelona process towards common sustainable development objectives, through, for example, inter-agency screening of programme proposals against the priority actions defined in the Mediterranean Strategy for Sustainable Development (MSSD).
- D12. Support for *further development of the MSSD*, taking account of continuing research into the economic, social and environmental impacts of greater regional integration,

such that it may be formally adopted as the overarching regional strategy for development.

D13. Review *Country Action Plans* in the EU Neighbourhood Policy to ensure that the specific recommendations of the SIA study are appropriately incorporated.

E. EU support for stronger global governance

- E1. Reinforce efforts to strengthen Multilateral Environmental Agreements (MEA) and associated governance mechanisms which effectively address *climate change* and declining *global biological diversity*, including the Framework Convention on Climate Change, the Convention on Biological Diversity and the Convention to Combat Desertification. Impacts in these areas would otherwise deteriorate incrementally under the EMFTA scenario that has been assessed.
- E2. Strengthen mechanisms to co-ordinate the implementation of MEAs at Mediterranean regional level.

F. Joint action to monitor the future evolution of EMFTA

- F1. Establish a mechanism for monitoring, reporting and disseminating information on the future evolution of the EMFTA and its impacts on sustainable development, as a formal component of the Euro-Mediterranean Partnership and the Barcelona process.
- F2. Establish a formal relationship between the joint EC-MPC bodies responsible for monitoring Action Plans under the Neighbourhood Policy, and the regional body appointed to supervise the EMFTA monitoring mechanism.

Overall conclusions of the SIA study

Six broad conclusions are drawn:

1. In parallel with other strategic measures at the national and regional level the Euro-Mediterranean Free Trade Area is capable of making a major contribution to achieving the objectives of the Euro-Mediterranean Partnership and hence to the sustainable development of the region.
2. Implementation of the EMFTA on its own will make only a small contribution to the economic objectives of the EMP, and needs to be accompanied by appropriate parallel measures if significant adverse social and environmental impacts are to be avoided at the local, regional and global level.
3. The parallel measures that are necessary to enhance the beneficial effects of the EMFTA and to avoid significant adverse impacts include actions both at the regional level and nationally in each of the partner countries.
4. In order for the EMFTA to make its full potential contribution to the sustainable development of the region, the Euro-Mediterranean Partnership itself needs to be re-invigorated and re-directed towards clearly defined economic, social and environmental goals for each of the partner countries and for the region as a whole. This reinforces a similar regional need arising from the challenges of addressing climate change, economic globalisation, regional migration and the Millennium Development Goals.

5. The monitoring mechanism proposed for the EMFTA may be used as a framework for addressing all of these challenges.
6. Any such re-invigoration of the Euro-Mediterranean Partnership should be based on a strategic review of its objectives and of the interactions between the EMFTA and the other components of the Barcelona Process in contributing to those objectives.

Further consultation

The results of the SIA will contribute to refining the EU's position in the ongoing negotiations and in the design of its development assistance programmes. They are also expected to be taken into account by policy-makers in the Mediterranean Partner Countries. Comments and suggestions on all aspects of this consultation draft of the SIA report will be greatly appreciated. They should be sent to the project email address:

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