Trade Sustainability Impact Assessment in support of negotiations of DCFTAs between the EU and respectively Georgia and the Republic of Moldova

Draft Inception Report - Executive Summary

Client: European Commission - DG TRADE

Rotterdam, 6 February 2012
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Executive Summary

This is the executive summary of the Inception Report for the TSIA in support of negotiations of the Deep and Comprehensive FTA (DCFTA) between the EU and respectively Georgia and Moldova. According to the Terms of Reference (ToR, p. 12) ‘The Trade SIA should assess how the trade and trade-related provisions under negotiation could affect economic, social, and environmental issues in the EU and, respectively, in Georgia and Moldova (as well as in other relevant countries, in particular neighbouring developing countries). Furthermore, it should propose measures (trade or non-trade) to maximise the benefits of the FTAs and prevent or minimise potential negative impacts. It should also include a reference to the EU-Turkey Customs Union and assess the impact of each of the future FTAs on the Customs Union’s functioning.’ In line with this clear definition of what is expected of the study, we present here our approach and conceptual framework, quantitative methodological approach, consultation plans for Georgia and Moldova, studied sources (literature, tools, references) and a first preliminary screening of issues that are of importance for this study.

New elements in our approach and conceptual framework

The general approach is based on the TSIA Handbook (2006) of DG Trade and all its core elements are included. In addition to the methodology laid out in the Handbook, we have strengthened our approach for this TSIA in four ways, based on evolved insights and developments of what is (methodologically) possible.

First, we have significantly improved the way we have modelled services-related and other non-tariff measures. With the Steering Committee providing the draft text of the final EU-Ukraine agreement, we have ‘translated’ this (with some adjustments) into a scenario – at sector specific level – for how the EU-Georgia and EU-Moldova DCFTAs could come to look like. We have also included the potential for MFN spill-overs for Georgia and Moldova to other countries due to the DCFTA with the EU.

Second, the social and environmental quantitative analysis has been further sharpened and developed (without taking any rigour away from the economic impacts). This implies we use satellite account data and supplementary modelling techniques to look deeper into the social and environmental impacts of these DCFTAs, including the use of household surveys to obtain more disaggregated income distributional insights that could follow from the DCFTAs.

Third, the human rights impact assessment approach has been strengthened and added in line with the requirement of the ToR. Based on a crucial scoping analysis, the sectors and issues most linked to HR issues will be flagged and potential effects presented and interpreted.

Fourth, the consultation side of this study has been significantly strengthened compared to earlier (similar) studies and the Handbook. Firstly because of the fact that we present already in the Inception Report Consultation Plans for both Georgia and Moldova in order to prepare early, identify key stakeholders early and start the discussion early, and not when we envisage going to the TSIA workshops in those countries. Second, because of the use of online media that we aim to employ. This will happen mainly through an updated interactive section on the TSIA websites.
Quantitative methodological approach

Our quantitative approach consists of three elements. First, we will use a computable general equilibrium model (CGE model) to determine general equilibrium effects of the potential DCFTAs with Georgia and Moldova. Second, in addition to the CGE model, via complementary social and environmental quantitative impact analyses, we can strengthen the social and environmental quantitative outcomes in this study. Third, it is possible to employ a partial equilibrium tool to look deeper into (up to) two specific products for further analysis if needed.

Computable General Equilibrium model

The CGE model is a multi-sector multi-country dynamic CGE model, which is one of the most elaborate available at the moment. For the specific details we refer to the chapter, but some elements are worth mentioning as they are key to our approach. First, we single out 10 countries or country groupings, including the EU27, Georgia, Moldova, Turkey (to look at the DCFTA impacts on EU-Turkey Customs Union), Ukraine, Russia, Azerbaijan, Armenia, China, and Rest of World (ROW). Second, a scenario is built compared to a baseline (2010), based on anticipated changes in tariff lines, services related regulatory approximation and other types of regulatory approximation. Third, we calculate a short-run (static) set of results and a long-run (including dynamic investment effects) set of results. We will report the findings of the DDA in the baseline in the main report, while we will present the findings without DDA in the baseline in the Annexes;

Social and environmental quantitative analyses

In addition to the CGE modelling, which provides the general frame of effects, we emphasise social and environmental effects more strongly by adding quantitative analyses in these two fields, building on the GE outcomes, but going into more detail regarding the sustainability aspects. Social aspects focus on the effects of the DCFTA on consumption, prices for consumer goods and labour income effects (by employing additional literature sources, SPS measure information and household survey data). The environmental quantitative analysis focuses on effects on airborne emissions, greenhouse gasses and the effects of these on climate change and other external costs using default damage factors.

Partial equilibrium modelling

In order to be able to look deeper into product specifics if needed, we can employ the SMART partial equilibrium model. The advantage of this model is that it allows for analysis at a much more disaggregated product level. The choice of the specific products can be made later, depending on where it is most interesting to analyse further. One could think of wine or walnuts, for example, given the DCFTAs with Georgia and Moldova. The SMART model is based on the World Integrated Trade Solution (WITS), software developed by the World Bank in close consultation with major international organisations. It includes trade figures, tariff data and non-tariff measures data of various sources.

In-depth analysis of detailed issues

The quantitative approach (CGE and social/environmental modelling) provides the starting point for a more detailed analysis of specific issues and aspects related to the DCFTA negotiations that jump out.
Often, in addition to the modelling outcomes, detailed analyses that take into account Georgian, Moldovan or EU specifics need to be added to understand what is truly going on. That is why – in line with the ToR - we will employ a screening/scoping analysis together with subsequent Causal Chain Analysis to structure our analysis around the largest and most important impacts we envisage, coming up with useful detailed insights, as well as flanking, enhancing and/or mitigating policy measures. It is in this stage, where we separate clearly the economic, social, environmental and human rights qualitative impacts that could result from these DCFTAs.

**Selection criteria for in-depth analysis**

Based on four criteria (see table below) we aim to select sectors and horizontal issues that matter most and focus this study in the right direction to be of direct relevance to the negotiations. Using these criteria and by supplementary partial equilibrium analysis (see above), we will be able to have a more specific selection of the key sectors affected by the DCFTA. In addition, the final selection of the sectors for the EU, Georgia and the Republic of Moldova will be done in close consultation with civil society and the Steering Committee.

<table>
<thead>
<tr>
<th>Number</th>
<th>Criterion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Criterion 1</td>
<td>Initial importance for economy (GDP, employment, trade shares)</td>
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<tr>
<td>Criterion 2</td>
<td>Economic impact from DCFTA</td>
</tr>
<tr>
<td>Criterion 3</td>
<td>Social / environmental importance / impact</td>
</tr>
<tr>
<td>Criterion 4</td>
<td>Stakeholder issues of special importance</td>
</tr>
</tbody>
</table>

**In-depth analysis using Causal Chain Analysis**

Once the selection has been done, we will conduct a detailed assessment using Causal Chain Analysis of – for example – the following issues for the sectors concerned:

- Identification and analysis of the NTMs hindering trade and investment;
- Effects on Small and Medium Enterprises (SMEs) specifically the potential effects of the DCFTA on their competitiveness and on Georgian and Moldovan policies regarding export promotion and competition policy;
- Cross-sectoral effects for these selected sectors;
- Sectoral economic, social and environmental consequences from the DCFTA.

The Causal Chain Analysis framework that we employ is presented in the figure below. This figure is slightly adapted from Chart 3 of the TSIA Handbook (p. 35).

An illustration of our approach is presented in the table above where the effect of five horizontal issues on n different sector is categorized according to level of intensity.
Causal Chain Analysis: from trade measure to impact on sustainable development

Policy influence (for phase 3)
- Mitigating or enhancing measures
  - Influence exogenous factors
  - Negotiate different level of FTA
  - Different effect on trade measures (endogenous variables)
  - Influence SWOT to have different change from baseline to initial economic impact
  - Influence effect of initial economic impact on production systems
  - Influence specific SWOTs to have different effects of production systems of the three types of impacts
  - Influence three types of impact on sustainable development

Exogenous Factors:
- Structural change
- Pre-existing economic, social, environmental & legal framework
- Political factors
- Infrastructure
- Knowledge & development
- Non-EU market access

Endogenous Factors:
- Trade (in goods and services)
- Technical barriers to trade and SPS
- Capital movement & payments
- Competition
- Intellectual property rights
- Trade facilitation, customs and RoI
- Trade and sustainable development
- Energy
- Labour standards
- Environmental standards

Baseline Economic, Social and Environmental Conditions

Initial Economic Impact
Initial Social Impact (Human Rights)
Initial Environmental Impact
Socioeconomic and Environmental System
Economic Impact
Social Impact (Human Rights)
Environmental Impact
Sustainable Development

Cross-cutting issue analysis
In addition to the detailed sector-specific analysis, cross-cutting issues for the overall economy will be analysed. Cross-cutting issues such as public procurement, establishment and investment, labour mobility or trade facilitation have an effect in the overall economy but selected goods and services can be disproportionately affected.

Effects of cross-cutting issues for different sectors (example only)

<table>
<thead>
<tr>
<th></th>
<th>Public Procurement</th>
<th>Establishment and investment</th>
<th>Labour mobility</th>
<th>Trade facilitation</th>
<th>Etc.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sector 1</td>
<td>√√√</td>
<td>√</td>
<td>√</td>
<td>√√</td>
<td>√</td>
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<tr>
<td>Sector 2</td>
<td>√</td>
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<td>√√√</td>
<td>√</td>
<td>√√√</td>
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<tr>
<td>Sector 3</td>
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<td>√</td>
<td>√√√</td>
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<tr>
<td>Overall economy</td>
<td>√√</td>
<td>√√</td>
<td>√</td>
<td>√</td>
<td>√</td>
</tr>
</tbody>
</table>

Note: √= slightly affected; √√= directly affected; √√√= greatly affected
Consultation plan and stakeholders

We present a consultation plan and lists of relevant stakeholders as well as an overview of upcoming events that may be relevant for this study and/or the DCFTA process in general. For Georgia and Moldova, we have kept these processes separately, while keeping the approach and structure the same. For this part, we work together intensively with the local representations of CASE and we are in close coordination with the EC delegations in the two respective countries. The main elements of the consultation plan are the following – carried out for each of the two countries (Georgia and Moldova) separately.

First we have identified a preliminary list of the main relevant stakeholders, with the help of our local partners and local experts, the Steering Committee, the EC Delegations and own research (presented in Annex A).

Second, mapping the civil society landscape in Georgia, we find that there is a limited culture of consultation, especially outside government, and that they have very little impact on society, but also that – given the large number of civil society organisations (CSOs) – there is much scope for consultations, and that the Georgian government is increasingly opening up to cooperation with CSOs. There are also some peculiarities with respect to the different civil society actors that we elaborate upon shortly in this report, including the fact that many CSOs represent middle class, while there is an underrepresentation of less affluent groups as well as ethnic minorities.

Third, looking at the civil society landscape in Moldova, we find that also in this country there is a limited culture of consultations with and influence of CSOs. A process to accommodate and involve civil society has been underway since 2008 (Civil Society Development Strategy for 2008-2011). Also, the Moldovan government (Ministry of Economy) has set up the DCFTA Task Force, in which various NGOs participate, and active participation (for Moldovan standards) took place between government representatives and civil society, throughout 2011. The participation and inclusion of the Transnistrian stakeholders in particular and region in general is a major issue of concern however, requiring specific attention, the more since NGO activity in Transnistria is considered very weak.

Fourth, from these consultation mappings in the two countries, we distil the major risks to the stakeholder engagement plan. These relate to lack of participation of CSOs due to unawareness, political sensitivity, and/or lack of capacity. These also relate to the fact that certain stakeholders may be underrepresented due to the CSO structure in the countries, or because of other reasons (e.g. Abkhazia, South Ossetia in Georgia and Transnistria in Moldova).

Fifth, consultation activities will consist of electronic consultation and documentation (www.tsia.ecorys.com/moldova and www.tsia.ecorys.com/georgia), public meetings, TSIA Workshops in Georgia and Moldova (flanked by face-to-face meetings), and attendance of other relevant conferences, workshops, meetings, etc. relevant to this study.

Preliminary screening on key sustainability issues (criterion 4)

Even though the formal screening and extensive scoping can only take place after the modelling and in coordination with the key stakeholders, especially civil society representatives, we feel that – for an early focus of the study – a preliminary screening of sustainability issues – to be kept in mind
from then onwards – is important in this TSIA. Some of our core sustainability findings from exploratory conversations with key stakeholders and CSOs are the following. First, the importance of regulatory approximation is high in light of already significant tariff-related market access for Georgia and Moldova. Second, implementation issues regarding SPS, TBT, IPR and Competition are going to be important for the de facto benefits that may result from these DCFTAs, the more when also looking at spill-over effects beyond the EU-Moldova and EU-Georgia. Third, implementation issues regarding specific environmental and social topics like human rights issues, like the implementation progress on ILO Conventions or implementation of international fisheries agreements. Fourth, certain product specific issues that are important to keep in mind and analyse further. This could include the products of wine, textiles, fisheries for example.

From this preliminary screening, we already draw (preliminary) conclusions; conclusions that have already in part been worked out in this Inception Report. First, detailed sector-level modelling of TRQs, NTM reductions and services liberalisation (asymmetric across sectors) is needed. Second, specific additional analysis on expected impacts in the field of social, environmental and human rights issues is needed. Third, Phase 2 should keep in mind potential impacts, among others from working on regulatory approximation (mainly TBT and SPS) that cannot be captured (entirely) by the quantitative modelling. For example, the existence of informal rules in the Georgian or Moldovan societies, the presence of a parallel informal labour force, or the existence of bribery practices – that are not captured by the model but could influence the specific outcomes of regulatory approximation. Fourth, ensuring a balanced input in the consultation process from several stakeholders (e.g. for Moldova: including from Transnistrian stakeholders) should be sought.

Conclusions

We believe that this Inception Report that presents our more detailed approach, combined with the management structure and team expertise we have put in place provides the cornerstone for successfully carrying out this study. We also believe that at any time, we need to be aware of the potential risks that may come looking around the corner. Having carried out this type of studies before, we are, however, confident we will succeed.