

Sustainability Impact Assessment in Support of the Negotiations for the Modernisation of the Trade Part of the Association Agreement with Chile

Inception Report

20 July 2018

EXECUTIVE SUMMARY

This Trade Sustainability Impact Assessment (SIA) supports the negotiations to modernise the trade pillar of the existing EU-Chile Association Agreement¹ (hereinafter EU-Chile FTA or Agreement) between the two partners; evaluates the impact of removing or reducing remaining barriers to trade and investment flows; and analyses the likely economic, social, human rights and environmental impacts of a modernised EU-Chile FTA. This inception report reviews the methodology and processes envisaged for carrying out these assessments and summarizes the preliminary desk research undertaken following the kick-off meeting on 26 April 2018 with the Commission's Inter-service Steering Group (ISG) following this study. The final report of this study will present the findings and develop recommendations to maximise the benefits of the modernised Agreement and prevent or minimise potential negative impacts.

Trade and Macroeconomic Impacts

The SIA drives off the simulated trade and economic impacts of the modernised EU-Chile Agreement conducted in the ex-ante study.² On the basis of these simulations, based on the assumed stronger liberalisation in Chile the modernised FTA will impact mainly on EU exports to Chile, boosting these by between EUR 2 to 4 billion or about 10-20%, while having only small impacts on Chilean exports to the EU. These trade impacts produce positive but modest economic welfare impacts in both the EU and Chile, with the gains greater in percentage terms in Chile given its relatively small size compared to the EU. In sectoral terms, the EU makes gains mainly in industrial goods exports (machinery and automotive) while Chile makes gains mostly in agricultural exports (led by beverages and tobacco, vegetables, fruits and nuts, other food products and oilseeds, vegetable oils and fats). Services impacts are positive but small.

¹ http://eur-lex.europa.eu/resource.html?uri=cellar:f83a503c-fa20-4b3a-9535-f1074175eaf0.0004.02/DOC_2&format=PDF.

² http://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155758.pdf.

The generally small scale of trade effects under the modernised Agreement translates into small impacts on production. The impact on Chile at the sectoral level is larger in percentage terms than in the EU; however, the larger impacts are positive and the largest negative impacts are in relatively small sectors of the economy, implying minimal adjustment difficulties. Gains are concentrated in SME-intensive sectors, suggesting favourable impacts on this regard. Overall, the impact of the modernised Agreement is modest in economic terms, with real GDP gains of about 0.001% to 0.002% in the EU and 0.09% to 0.175% in Chile, with welfare gains of EUR 269 million to 712 million in the EU and EUR 369 million to 529 million in Chile. The small size of these economic impacts implies modest impacts on third countries and on the EU's Outermost Regions.³

Sustainability Issues: Preliminary Scan

From a purely **economic** perspective, the modernisation of the EU-Chile FTA does not raise sustainability concerns in terms of the scale of the impacts and adjustment pressures, either at the aggregate economy level or at the sectoral level. The impact for the EU would not be palpably felt; in Chile, the impact would be noticeable for the most affected sectors – with output in dairy products, and vegetables, fruits and nuts expanding most, and contracting most in machinery and motor vehicles, according to the CGE simulations – but would similarly be of a scale that would raise minimal concerns from a sustainability perspective. Given their small size, the quantifiable economic impacts have small implications for environmental, employment and other socio-economic impacts. These preliminary conclusions do not prejudge the outcome of the qualitative analysis that goes beyond the CGE model-based review.

As regards potential **social** impacts, the SIA will review likely impacts of the modernised FTA on employment and wage levels, prices, and welfare. Qualitative assessments will focus on job quality, freedom of association and the right to collective bargaining as well as social dialogue as a prerequisite for an enhanced protection of workers' rights. The baseline analysis indicates that, despite progress, gender gaps remain and are particularly significant in Chile. Accordingly, the analysis will pay particular attention to the impact of the modernised FTA on women. Based on the preliminary findings, job quality is an issue in sectors which are likely to be affected by the modernised Agreement and are proposed for a more detailed analysis, including hotels and restaurants, and trade. These sectors are characterised by high levels of informality, low wages, low rates of vocational training, low presence of trade unions, high levels of sub-contracting and accidents at work, relatively long working hours, and occurrence of child labour. At the same time, they are important for women in their roles as employees and entrepreneurs (e.g. 64% of women-led enterprises in Chile are concentrated in these two sectors; in the EU, women entrepreneurs account for 39% of hotel and restaurant businesses, and 33% of trade businesses). Mining and construction are important for men, as employees and entrepreneurs, with mining being the leading sector in Chile for value chain development and foreign investment, with positive impacts in terms of high wages, demand for skilled workers, and high health and safety work standards.

As regards **human rights**, two issues – gender discrimination and the rights of indigenous peoples – are indicated as particularly linked to international trade in the ex-ante study. Preliminary analysis suggests that sensitivities also exist with respect to, inter alia, the right to water and consequently the right to health and right to a clean environment, as well as certain aspects related to the right to an adequate standard of living (particularly affecting vulnerable groups of the population and the poor), migrants' rights, and discrimination based on the social status. It cannot be excluded that some of these issues could be related to international trade and, therefore, based on this preliminary screening exercise, they might be impacted by the modernisation of the EU-Chile FTA. The potential

³ The nine EU's Outermost Regions consist of six French overseas territories (French Guiana, Guadeloupe, Martinique, Mayotte, Réunion and Saint Martin), two Portuguese autonomous regions (the Azores and Madeira) and one Spanish autonomous community (the Canary Islands).

for impacts will be assessed accordingly, taking into account the extensive work program between the EU and Chile on human rights.

As regards **environmental** impacts, preliminary analysis indicates environmental impacts will be modest given the scale of the economic impacts. Some environmental impacts are anticipated in terms of greenhouse gas emissions, with good prospects for reduction based on scope for energy efficiency and reduced pollution through bilateral trade and investment in general and for transportation in particular. Other areas that emerge as likely to require attention from a sustainability perspective given the likelihood of expanded agricultural output in Chile include land use, pressures on biodiversity and ecosystems, and water consumption.

Sector Deep Dives

According to a prioritisation exercise, the following six sectors are proposed to be selected for a detailed sector analysis. This selection constitutes a good mix of sectors employing mainly men (i.e. extractive sectors and construction) and those important for women (i.e. trade and tourism).

Construction: This sector has a high prevalence of SMEs, features some social and labour issues provisions on investment and public procurement, and is likely to be impacted by a modernised Agreement through provisions on investment and public procurement.

Communication and business services: This sector is projected to feel fairly significant impacts under a modernised Agreement, and features a number of issues, including intellectual property and digital linkage (future of work).

Mining: Although tariffs were fully liberalised already under the existing Agreement (including the downstream sectors), this sector is highly important for Chile in terms of export revenues, value chain participation, and linkages to other sectors within Chile (including services, equipment maintenance, engineering, and R&D). It also features environmental, social, human rights and governance sustainability issues.

Tourism and hospitality services and wholesale and retail trade. These two sectors are particularly important from a labour and gender perspective – both in terms of entrepreneurship and employment – and raise a number of social issues, such as a high degree of informality, child labour, etc. Furthermore, environmental issues are important for the tourism sector due to the use of protected areas as tourist destinations.

Dairy: This is one of the few sectors still protected by Chile and thus potentially impacted significantly by liberalised trade, and is a sensitive sector.

A number of other sectors have been rated at medium priority and are also candidates for the sectoral analysis. These include vegetables, fruits and nuts, forestry, wood and paper, fishery, and transport services. The final selection will be made following discussions with the Commission's ISG.

Case Studies

The following potential studies have been identified following a selection process considering the economic importance and/or prominence of issues in the political discourse, the anticipated impact of the modernised FTA, and initial consultations with experts and stakeholders:

1. **Olive oil:** this is a sector strongly developing in Chile, has potential economic impacts and raises some sustainability issues.
2. **Lithium batteries value chain:** Chile is the EU's main supplier of lithium, which is an important input for the EU automotive industry (development of car batteries).

3. **Renewable energy:** Chile is one of the largest markets for renewable energy in South America and EU equipment and energy companies play an important role.
4. **Labour rights:** Potential case studies could focus on **gender**, including women-led MSMEs, and **job quality** (e.g. precarious work in sub-contracting, seasonal workers and migrant workers, health and safety at work; demand for skilled workers).
5. **Effects on rural communities.** Trade impacts in a number of sectors, in particular forestry and agriculture, are likely to affect rural communities. It therefore seems warranted to provide a summary of these effects in one case study.
6. **Competition (notably mergers and acquisitions):** issues may arise from the modernised Agreement provisions on competition and investment.
7. **Subsidies and state aid:** issues related to transparency, good governance, level playing field, and market access.

Additional case studies could be considered for:

- Specific products within sectors (such as salmon farming within the fisheries sector);
- Value chains of agricultural or industrial products;
- Effect of the modernised Agreement on cooperatives.

Finally, a number of cross-cutting issues, such as effects on SMEs, gender issues and, potentially, migration issues, will be treated horizontally in the study but may also merit separate case studies. The draft interim report will therefore revisit the case study selection and propose, if appropriate, additional case study topics.

Consultation Plan

The consultations as planned feature five components:

- Pillar 1: Digital engagement with key stakeholders: website and other channels, and dissemination and discussion of (draft) results.
- Pillar 2: Interviews, meetings and surveys with key stakeholders, and dissemination of (draft) results.
- Pillar 3: Civil society dialogue (CSD) meetings in the EU.
- Pillar 4: SIA Workshop in Chile, flanking meetings and interviews.
- Pillar 5: Meetings with EC officials.

An initial database of stakeholders has been prepared during the inception phase based on the following sources and activities:

- For EU stakeholders, a review of past SIA reports and meetings, as well as of lists of participation in recent CSD meetings held on EU-Latin American trade (in particular, EU-Mexico and EU-Mercosur) has been undertaken;
- For Chilean stakeholders, invitation lists for recent workshops held in the context of reviewing the existing Association Agreement and preparing for its modernisation have been used as a starting point;
- Additional stakeholders have been identified through alternative networks, such as the UN Global Compact – in particular to strengthen the business link of the SIA – as well as the study team’s own network of partners, which is particularly well developed in Chile as a result of Vincular’s ongoing work on CSR issues.

Additional stakeholders will continue to be identified as the study work progresses; in particular, this will include stakeholders relevant for the sector and case studies being undertaken.