

»» TTIP – an opportunity for European SMEs

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The Transatlantic Trade and Investment Partnership (TTIP) currently under negotiation between the EU and the USA holds potential for growth. Small and medium-sized enterprises in particular could benefit from lower non-tariff trade barriers. Mutual recognition of technical standards, testing procedures or certification requirements would lower fixed market entry costs that affect small and medium-sized enterprises significantly more than large corporations.

The results of a 2014 survey by KfW Group of around 1,900 larger European and US SMEs has confirmed this.¹ Their approval of TTIP depends primarily on their own level of competitiveness. Financing difficulties and skills shortages, however, could severely reduce the benefits of a transatlantic free-trade agreement as well.

Some 1,100 SMEs in China, Russia, Brazil and Japan were also surveyed. While access to credit plays an important role there, too, enterprises in third countries are significantly less optimistic with regard to the impacts of TTIP. Trade diversion effects are likely to be a major reason.

Representatives of the EU and USA have been negotiating the Transatlantic Trade and Investment Partnership, or TTIP in short, between the two economic blocs since July 2013. A successful conclusion of the negotiations would create the world's biggest free-trade area. Together, the EU member states and the USA combine more than 50 % of global economic output. They represent roughly one third of global trade in goods and services and nearly 60 % of all foreign direct investment.²

Focus on eliminating technical and administrative trade barriers

One measure envisaged to facilitate trade between the USA and the EU member states is to reduce tariffs. However, as the weighted average tariff rates for exports from the EU to the USA are already at a very low level, at around 2.8 % in manufacturing and 2.6 % in agriculture, the effects expected in this area are rather low.³

Far more significant, in turn, is the intended reduction of non-tariff trade barriers. Under TTIP, the mutual recognition of technical standards is to be advanced and administrative hurdles are to be reduced. Necessary product adjustments, additional tests and double certification currently cause addi-

tional costs averaging 10 to 20 % of export value.⁴ Examples of non-tariff trade barriers include the difference in colour coding of power cables or power points in the EU and the USA,⁵ and the difference in quality control procedures for oysters which forces European exporters to have their goods tested twice.⁶

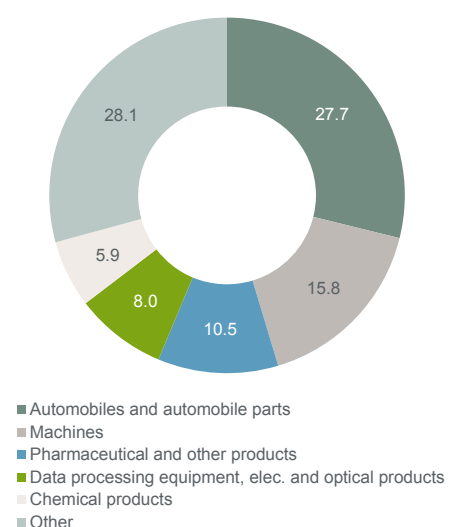
TTIP also aims to simplify access to public contracts in the respective partner country. The agreement also aims to set out social and ecological standards as well as provisions for improving investment security. The draft also includes a chapter on small and medium-sized enterprises that primarily deals with making information more readily accessible. For example, a website should make the conditions for entering the target country's market transparent for potential exporters.

USA and EU already have intensive trade relations

The USA and the EU are already their most important respective trading partners. In 2014, the 28 EU member states exported goods worth EUR 311 billion to the USA. This is equivalent to 18.3 % of the EU's total goods exports.⁷

Figure 1: Automobile industry represents the bulk of German exports to the USA

German exports to the USA by product groups.
Data for 2014 in EUR billions.



Source: Destatis

The USA recently overtook France as Germany's most important export destination. Germany exports almost EUR 96 billion worth of goods to the USA, almost one third of them from the automobile industry. Engineering, pharmaceuticals and electronics make up another third (Figure 1).

Comprehensive trade liberalisation holds growth potential

Studies conclude that a free trade agreement could lead to a sharp increase in the volume of trade between the EU member states and the USA. This would spur on real income growth and the creation of new jobs in the USA as well as in the EU.⁸

In particular, Germany's exports to the USA could increase by an estimated 94 % in the long term. This way, TTIP could lead to real income increases of around 4.7 % in Germany. Simulations also show that a comprehensive transatlantic free trade agreement could create some 25,000 new jobs in Germany.⁹

TTIP holds opportunities for European SMEs

TTIP would not just benefit large corporations, however, as is often alleged. Small and medium-sized enterprises (SMEs) on both sides of the Atlantic could benefit from comprehensive trade liberalisation. Dismantling non-tariff trade barriers would primarily reduce fixed market entry costs, which weigh much more heavily on small enterprises than on large ones. Paying the high costs of product adaptation and certification is thus far not worthwhile for them because the sales volume they are able to achieve in the USA is comparatively low, other than for large corporations. Mutual recognition of standards would greatly simplify business for SMEs and make exporting goods and services to the USA profitable for them in the first place.¹⁰

This finding is not only corroborated by economic theory arguments. The results of a 2014 KfW Group survey among some 1,900 SMEs in Germany, France, Spain, Italy, the UK and the USA show that many of them have a positive view of TTIP.

Highest approval in Spain and the UK

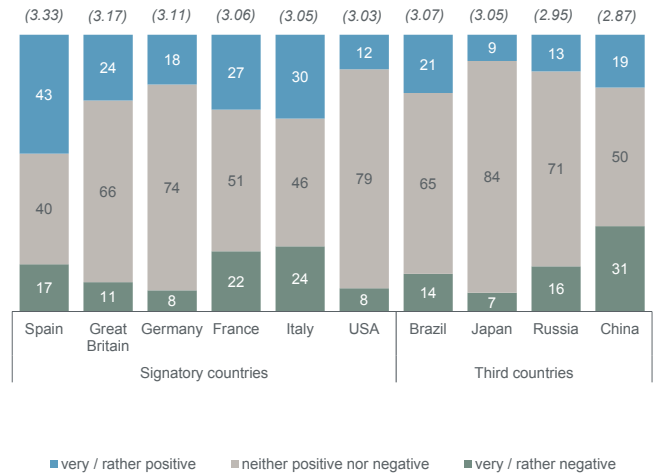
SMEs in Spain are particularly optimistic about TTIP. Forty-three per cent of them expect TTIP to have a positive impact on their business (Figure 2). Fewer than one fifth expect a transatlantic free-trade agreement to have negative consequences for their enterprise. This attitude also reflects the strong export growth which has recently supported the country's economic recovery.¹¹

The average verdict in the UK is also very optimistic. One quarter of all businesses with 30 to 500 employees expect positive effects (Figure 2). Only 11 % believe that an agreement could affect them negatively. The trade relations between the UK and the USA have traditionally been strong and the USA is by far the main export destination of UK producers. This may also explain why the estimated prosperity gains from a transatlantic trade partnership are higher in the

UK than in all other European Union member states. Real incomes here could rise by around 9.7 % in the long term as a result of a TTIP.¹²

Figure 2: Most SMEs are neutral towards TTIP

How will a free-trade agreement between the EU and the USA affect your business?



Note: The companies were asked what impact they expect a free-trade agreement between the EU in the USA to have on their business. Possible answers: (1) very negative; (2) rather negative; (3) neither positive nor negative; (4) rather positive; (5) very positive. The figure shows the weighted shares of all companies in a country that gave a particular response (in the bar graph) and the weighted mean of all companies (in brackets).

Source: KfW Competitiveness Indicator 2014

German SMEs are relaxed about TTIP

Of all European companies surveyed, German SMEs were the least euphoric. Only around 18 % of those surveyed expect TTIP to have positive or even very positive effects on their business (Figure 2). However, there are also significantly fewer pessimists. At 8 %, the share of companies that fear negative impacts from a transatlantic free-trade agreement is lower in Germany than in any other European country surveyed. The vast majority is calmly following the negotiations. Almost three quarters of German SMEs assume that TTIP will be of no relevance to their business.

In Germany, manufacturing companies are the most optimistic, with 29 % expecting TTIP to have positive effects on their business. This result is hardly surprising as Germany's manufacturing sector, which includes the automobile industry, engineering and chemicals, is particularly export-oriented. More than 91 % of the manufacturing SMEs surveyed were exporters.

Positions in France and Italy are more polarised

In France and Italy the share of SMEs in favour of TTIP is significantly higher than in Germany – but so is the share of SMEs that disapprove TTIP. Positive business effects are expected by 27 % of SMEs in France and 30 % in Italy (Figure 2). At the same time, 22 % of French SMEs and 24 % of Italian SMEs fear negative consequences of a free trade agreement.

Only few US SMEs expect to be affected by TTIP

Almost 80 % of US SMEs expect TTIP to be of no consequence to their business (Figure 2). Only 12 % of enterprises expect positive effects, fewer than in all other signatory countries. Similarly, however, only 8 % of SMEs expect negative consequences.

One possible explanation of this result is the comparatively lesser importance of small and medium-sized enterprises in the USA. The US economy and, in particular, export business is driven more strongly by large enterprises and corporations than in Europe. Domestic trade within the USA also plays a significantly bigger role than it does within the EU member states. Not even 4 % of enterprises with fewer than 500 employees are exporters and almost 60 % of exporting SMEs supply only a single foreign market, mostly Canada or Mexico. These countries are not only geographically close but, along with the USA, are members of the North American Free Agreement (NAFTA).¹³

In Germany, by contrast, almost 23 % of enterprises with fewer than 500 employees generated foreign sales in 2014. The share of SMEs that export to non-European countries alone is 8.4 %, more than twice as high as in the USA.¹⁴

SMEs in third countries are divided

The survey interviewed not only enterprises in Europe and the USA but also some 1,100 SMEs in Brazil, Russia, China and Japan, asking them how they expected a transatlantic free-trade agreement to affect their business.

The survey found that these enterprises are anything but neutral with regard to a TTIP, with the possible exception of Japan. Here, 84 % of SMEs expect neither positive nor negative effects (Figure 2).

Chinese SMEs are rather critical of TTIP

Chinese enterprises are largely critical of a trade partnership between the USA and the EU. Almost a third of all SMEs expect TTIP to have a negative impact on their business. In contrast, the share of enterprises expecting positive effects is rather low, at 19 % (Figure 2). Accordingly, the average assessment of possible impacts is at the lower margin of all countries surveyed, at 2.87 on a scale of 1 (very negative) to 5 (very positive). In Russia the share of enterprises that fear negative impacts is higher than the share of SMEs hoping to benefit from TTIP, too.

One reason for the rather pessimistic view adopted by SMEs in some third countries could be what is referred to as trade diversion effects. If trading costs are eliminated between the USA and Europe, enterprises in third countries become relatively less competitive than their counterparts in the free-trade area and they lose market share. Trade flows shift from exporters in third countries to exporters in the free-trade area. For example, with TTIP in force, a Chinese enterprise would have to continue paying tariffs on its exports to the EU and adjust the prices of its products and services accordingly, while its US competitor is exempt from those tariffs. As a

result, Chinese products would become less attractive for European importers.

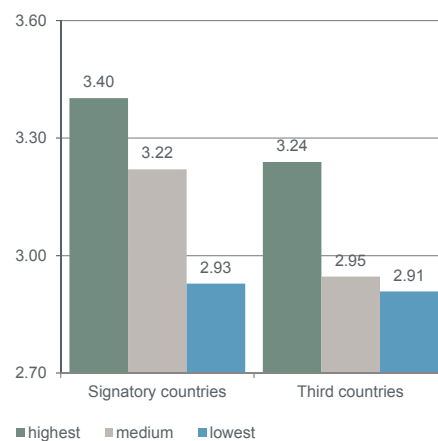
Brazilian SMEs could benefit from TTIP

TTIP could also generate income effects, however, that would benefit third countries. If a free-trade agreement leads to higher incomes and employment in the USA and Europe, as various studies forecast,¹⁵ it may also boost demand for goods or natural resources from third countries.

This may explain the mainly positive attitude of Brazilian SMEs towards a transatlantic free-trade agreement. Resources such as oil or iron ore and agricultural produce such as soya beans or coffee make up almost 40 % of Brazilian exports to the USA and the EU. They are used for production and consumption in the target countries and are difficult to replace with alternative products. Moreover, closer regulatory cooperation between the USA and the EU could benefit Brazilian enterprises if it leads to a reduction in the prices of imported goods such as machinery or equipment.¹⁶

Figure 3: TTIP losers concentrated among unproductive SMEs

Expected effects of a TTIP depending on enterprises' competitiveness



Note: The enterprises were asked what impact they expect a free-trade agreement between the EU in the USA to have on their business. Possible answers: (1) very negative; (2) rather negative; (3) neither positive nor negative; (4) rather positive; (5) very positive. The figure shows the weighted average across all enterprises depending on their competitiveness. An enterprise's competitiveness is derived from its self-assessment of price, quality, degree of innovation, reputation, delivery times, service as well as costs of personnel and materials. All enterprises within the upper tercile of the distribution of competitiveness within each country are considered to be enterprises with the highest level of competitiveness.

Source: KfW Competitiveness Indicator 2014

Enterprise's competitiveness determines benefit of TTIP

From an economic perspective, free trade should be rated positively. Division of labour, specialisation, reallocation of resources to more productive enterprises and improved exploitation of scale effects increase overall economic productivity and real incomes. However, not all economic agents benefit equally from gains in prosperity. This also applies to SMEs, as the findings of the survey have shown.

Whether an enterprise is among the winners of TTIP de-

depends primarily on its own competitiveness. More competitive¹⁷ enterprises benefit more strongly from a transatlantic free-trade agreement. A small number of them are already active on target markets on the other side of the Atlantic and will be able to further expand their foreign sales and profits when tariffs are lowered. For some others a reduction in non-tariff trade barriers will make entering the market on the other side of the Atlantic worthwhile in the first place.

Less productive enterprises, on the other hand, will not be able to sell their products or services abroad at a profit even if the cost of entering the market is low. Worse still, these enterprises will feel all the more the competitive pressure from the new exporters on the other side of the Atlantic.

Figure 4: Successful exporters see biggest opportunities in TTIP

Expected effects of a TTIP depending on export status



Note: The enterprises were asked what impact they expect a free-trade agreement between the EU in the USA to have on their business. Possible answers: (1) very negative; (2) rather negative; (3) neither positive nor negative; (4) rather positive; (5) very positive. The figure shows the weighted average across all enterprises as a function of their export status. The individual countries are weighted equally.

Source: KfW Competitiveness Indicator 2014

Especially the less competitive SMEs stand to lose

The findings of our survey support these considerations. On average, SMEs that regard themselves as more competitive have significantly more positive expectations with regard to a TTIP (Figure 3). European and US enterprises in the upper third of the distribution tend to give a transatlantic free-trade agreement positive marks, averaging 3.40 points. SMEs in signatory countries with moderate competitiveness are somewhat less optimistic (3.22 points). Finally, SMEs whose competitiveness is in the bottom third tend to rate TTIP rather negatively (2.93 points). The picture looks similar in third countries where additional demand from the USA and Europe would primarily benefit those enterprises that are particularly competitive on world markets.

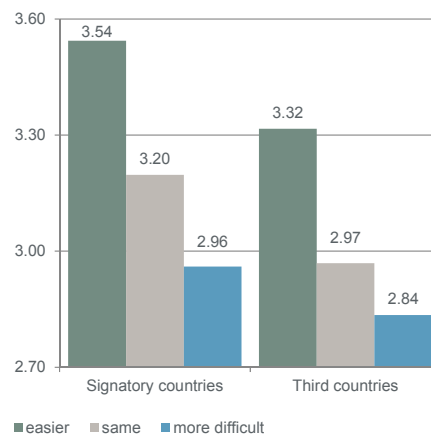
Successful exporters see biggest opportunities in TTIP

A glance at SMEs' export activities confirms this assumption,

too. It is primarily SMEs which are already exporting successfully and wish to further expand their overseas presence that hope for positive effects from a transatlantic free-trade agreement (Figure 4). They are likely to be more competitive, not only at international level. As lower trade barriers enable them to tap into new markets, they are also able to use existing networks, established distribution channels and employees with export experience. This is true of exporters in the US and in Europe (3.42 points), as well as exporting enterprises in third countries, even though the latter generally expect somewhat lower market opportunities from TTIP (3.15 points). Less successful exporters and SMEs that have not yet gained any export experience, on the other hand, do not expect a transatlantic free trade agreement to have any positive impacts on their business.

Figure 5: Access to credit determines benefit of TTIP

Expected effects of a TTIP depending on the development of access to credit



Note: The companies were asked what impact they expect a free-trade agreement between the EU in the USA to have on their business. Possible answers: (1) very negative; (2) rather negative; (3) neither positive nor negative; (4) rather positive; (5) very positive. The figure shows the weighted average across all enterprises depending how their access to credit changed in the past 12 months. The individual countries are weighted equally.

Source: KfW Competitiveness Indicator 2014

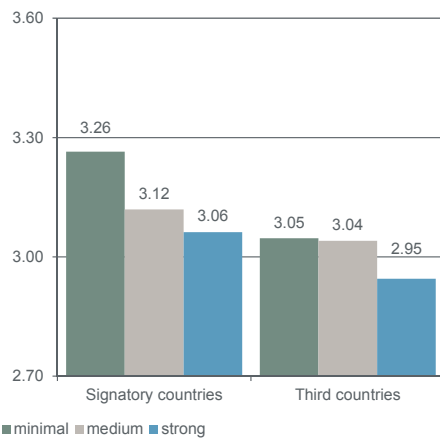
SMEs need access to capital and skilled labour to take advantage of TTIP

In addition to productivity, access to production factors such as capital and skilled workers is crucial to business success. SMEs whose access to credit became easier in the 12 months before the survey rate a transatlantic trade partnership significantly more positively than SMEs whose access to credit became more difficult (Figure 5). This correlation exists even when enterprises' competitiveness is controlled in multivariate analyses.

Even within a free-trade area, tapping into new foreign markets involves costs that an enterprise must pay long before generating foreign revenues. Good access to credit gives a business the room for manoeuvre it needs. Exporters with better financing possibilities can expand their activities on the other side of the Atlantic more quickly, secure bigger market shares and benefit directly from the trade creation effects of TTIP.

Figure 6: SMEs need skilled workers to take advantage of TTIP

Expected effects of a TTIP depending on the degree of skills shortage



Note: The companies were asked what impact they expect a free-trade agreement between the EU in the USA to have on their business. Possible answers: (1) very negative; (2) rather negative; (3) neither positive nor negative; (4) rather positive; (5) very positive. The figure shows the weighted average across all enterprises depending on the extent to which an enterprise is suffering from skills shortages. The individual countries are weighted equally.

Source: KfW Competitiveness Indicator 2014

Skills shortage reduces benefits from TTIP

A very similar correlation exists between expectations regarding TTIP and access to skilled workers. The less an enterprise regards itself as being affected by a skills shortage, the more optimistic it is about a TTIP (Figure 6). This applies to the signatory states in particular. They specialise more in technology-oriented and skill-intensive sectors than third countries such as China, Russia or Brazil, which tend to have a comparative advantage in the production of labour-intensive goods or in the extraction of natural resources instead. For this reason, the availability of skilled workers is much more important for export success and hence the ben-

efit of a transatlantic free-trade agreement in the USA and the EU.

Conclusion

TTIP holds many opportunities for SMEs in Europe and the USA. It will mainly benefit the more competitive small and medium-sized enterprises, by lowering tariff and non-tariff trade barriers and thus allowing them to tap into new markets. An important prerequisite, however, will be access to capital and skilled workers. Financing opportunities have to be created for enterprises particularly in the EU member states where the impacts of the European financial and economic crisis can still be felt. But even in Germany the skills shortage will have to be addressed with targeted measures, such as investment in education and the recruitment of foreign skilled workers. At the same time, more investment will be needed to improve the international competitiveness of small and medium-sized enterprises so that as many as possible will be able to benefit from TTIP and to cope with increased competition from abroad.

For the close of the negotiations, however, it will not only be crucial that SMEs in Germany and Europe support a transatlantic free-trade agreement. Without approval from the population, it is doubtful that TTIP will subsequently be ratified by the European Parliament or the national parliaments¹⁸. Disapproval is widespread in Germany in particular. The protests in Berlin with more than 150,000 participants in October 2015 were not the only manifestation of their negative attitude. In an autumn 2015 Eurobarometer survey, 59% of Germans were against the free trade agreement. Only in Austria was the disapproval rate higher, at 70%. The negotiators need to take a number of concerns seriously, from the fear of deteriorating environmental and social standards to the still unsettled question of the role of investment courts. Moreover, our analyses provide no grounds for dismissing the concerns of several non-governmental organisations that TTIP may negatively impact on some third countries¹⁹. ■

¹ The survey of enterprises on the impact of TTIP was conducted as part of the KfW Competitiveness Indicator 2014. It covered enterprises with 30 to 500 employees from the manufacturing industry, the retail and wholesale sector, the construction industry and the services sector. For details on the sample, methodology and contents of the survey see Abel-Koch, J. and J. Gerstenberger (2014): KfW Competitiveness Indicator 2014 – Tables and Methods, KfW Research, Frankfurt am Main.

² See Diekmann, B. (2013): Transatlantische Handels- und Investitionspartnerschaft: Chance und Herausforderung in der internationalen Handelspolitik (*Transatlantic Trade and Investment Partnership: an opportunity and a challenge for international trade policy*), in: ifo Schnelldienst 6/2013, pp. 7–10, in German.

³ See Felbermayr, G., Larch, M., Flach, L., Yalcin, E. and S. Benz (2013): Dimensionen und Auswirkungen eines Freihandelsabkommens zwischen der EU und den USA (*Dimensions and impacts of a free trade agreement between the EU and the USA*), in German.

⁴ See Federal Ministry for Economic Affairs and Energy (2015): Transatlantische Handels- und Investitionspartnerschaft (TTIP) zwischen der EU und den USA (*Transatlantic Trade and Investment Partnership (TTIP) between the EU and the USA*), in German.

⁵ See European Commission (2015): Inside TTIP.

⁶ See European Commission (2015): Transatlantic Trade and Investment Partnership: The Opportunities for Small and Medium-sized Enterprises.

⁷ See European Commission (2015): European Union, Trade in Goods with USA.

⁸ See Francois, J., Manchin, M., Norberg, H., Pindyuk, O. and P. Tomberger (2013): Reducing Trans-Atlantic Barriers to Trade and Investment – An Economic Assessment, Final Project Report, CEPR and Felbermayr, G., Larch, M., Flach, L., Yalcin, E. and S. Benz (2013): Dimensionen und Auswirkungen eines Freihandelsabkommens zwischen der EU und den USA (*Dimensions and impacts of a free trade agreement between the EU and the USA*), in German.

⁹ See *ibidem*.

¹⁰ A survey conducted by the Ifo Institute among business associations in Germany confirms this. They indicated that non-tariff trade barriers, particularly quality specifications, administrative hurdles and special labelling requirements, hamper exports to the USA significantly more than tariffs. With respect to quality requirements, they estimate that 84% of the related costs are fixed costs. The fixed cost share of administrative hurdles is 51%, and for labelling requirements it is still a high 35%. See *ibidem*.

¹¹ See also Ott-Laubach, P. (2015): Spain: political uncertainty overshadows good economic outlook, Economics in Brief No. 98, KfW Research, Frankfurt am Main.

¹² See Felbermayr, G., Larch, M., Flach, L., Yalcin, E. and S. Benz (2013): Dimensionen und Auswirkungen eines Freihandelsabkommens zwischen der EU und den USA (*Dimensions and impacts of a free trade agreement between the EU and the USA*), in German.

¹³ United States International Trade Commission (2010): Small and Medium-Sized Enterprises: U.S. and EU Export Activities, and Barriers and Opportunities Experienced by U.S. Firms.

¹⁴ This is the result of an evaluation of data collected by the KfW SME Panel for the year 2014. See Schwartz, M. (2015): KfW SME Panel 2015 – With growing confidence, German SMEs are starting to invest again, KfW Research, Frankfurt am Main, for the conception and methodology of this data record.

¹⁵ See Francois, J., Manchin, M., Norberg, H., Pindyuk, O. and P. Tomberger (2013): Reducing Trans-Atlantic Barriers to Trade and Investment – An Economic Assessment, Final Project Report, CEPR, and Felbermayr, G., Larch, M., Flach, L., Yalcin, E. and S. Benz (2013): Dimensionen und Auswirkungen eines Freihandelsabkommens zwischen der EU und den USA (*Dimensions and impacts of a free trade agreement between the EU and the USA*), In German.

¹⁶ See Felbermayr, G., Kohler, W., Aichele, R., Klee, G. and E. Yalcin (2015): Mögliche Auswirkungen der Transatlantischen Handels- und Investitionspartnerschaft (TTIP) auf Entwicklungs- und Schwellenländer (*Possible impacts of The Transatlantic Trade and Investment Partnership (TTIP) on developing and emerging countries*), In German.

¹⁷ An enterprise's competitiveness can be broadly defined as its ability to successfully sell products or services on markets. The price plays a crucial role in this regard, but so do factors such as quality, service or delivery times.

¹⁸ If TTIP is classified as an EU-only agreement it can be signed by the Council of the European Union and would require approval only by the European Parliament. If, on the other hand, it is considered a 'mixed agreement' that covers issues for which the EU does not have exclusive competence, it would have to be approved at least in part by the national parliaments of the EU member states. As TTIP contains very comprehensive regulations it is very likely to be classified as a mixed agreement.

¹⁹ See Raschen, M. (2015): TTIP from the perspective of developing and emerging countries, Economics in Brief No. 78, KfW Research, Frankfurt am Main.