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## Feature of the Swiss Foreign Economic Policy Report 2018

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### International trade crisis and Switzerland's options for action

*International trade is facing an escalation of protectionist measures between the major trading powers. These sparked off a series of countermeasures and complaints to the WTO.*

*To some extent, these measures may have been motivated by negotiating tactics. The question remains, however, as to whether the danger of a serious departure from the WTO's multilateral global trading system is imminent.*

*These events in any case threaten to trigger a serious international trade - and hence also economic - crisis. Thus the continual process of liberalisation of international trade and expansion of multilateral commercial law that followed the establishment of the General Agreement on Tariffs and Trade in 1947 could be in jeopardy. Despite these frictions, the EU and Japan in particular are continuing to develop their free trade relations actively. In a counter-movement to recent events, they have concluded new bilateral and regional preferential agreements.*

*With its limited domestic market and very close international ties, Switzerland is much more dependent on international trade than other, larger economies. As a*

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*medium-sized economy, it has only limited scope for developing bargaining power by means of foreign trade policy measures. It is therefore more dependent on multilateral arrangements and on all the other parties complying with international commercial law. Consequently, Switzerland is also more vulnerable to any reorientation of the multilateral trading order.*

*This presents Swiss foreign trade policy with a number of different challenges. For Switzerland, it is vital that the WTO's multilateral trading system is maintained and further developed - and that it can play its part through negotiations. The multilateral trading system has to restrict the principle of "might makes right", it has to find answers to current trade-related issues - with regard to digitalisation, for example - and has to contribute to sustainable development. Switzerland for its part should avoid a situation in which its exporters are put at a disadvantage versus their competitors on major foreign markets because free trade agreements are outdated or non-existent. Tackling these issues calls for an expansion and deepening of existing free trade arrangements. To a large extent, however, the options open to Switzerland in the area of foreign trade policy also hinge on domestic policies. It needs to keep working on an economic-policy framework that will maintain and strengthen its already considerable ability to adapt to the constantly changing international environment.*

## **1.1 Development and significance of the rules-based international trading system since the 1930s**

Owing to the relatively small size of its domestic market, the Swiss economy is heavily dependent on international trade.

It is thus particularly reliant on the development of the rules-based multilateral trading system and until now has benefited from this system as a successful exporting nation. The rules underlying the multilateral trading system provide the legal security necessary for predictable foreign trade and protect the actors in international trade against harmful protectionist measures.

### **1.1.1 Development of the multilateral trading system and global tariff dismantling**

Today's multilateral trading system developed in stages after the Second World War. In 1947, based on experience gained from the disastrous effects of protectionism in the 1930s, 23 countries signed the General Agreement on Tariffs and Trade (GATT)<sup>1</sup>. Switzerland joined the GATT as a full member in 1966.

Based on the trading rules defined by it, the GATT constituted a successful negotiating platform. In eight rounds of negotiations between 1947 and 1994, import duties on industrial goods between participating states saw substantial reductions and

<sup>1</sup> General Agreement on Tariffs and Trade (SR 0.632.21).

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became binding under international law. Duties on agricultural goods and in other labour-intensive sectors, especially textiles, remained exempted for a long time. Only on conclusion of the Uruguay Round in 1994 these were integrated, together with other provisions, in the rules of the World Trade Organization (WTO), founded at that time<sup>2</sup>. Furthermore, customs duties in a number of developing countries were only made binding to a certain extent.

Thanks to these developments, along with regional free trade agreements (FTA) and autonomous liberalisations, the last few decades saw a substantial worldwide reduction in import duties. On average since 1990, the average level of import duties actually applied throughout the world has decreased continually from 14 per cent to just under five per cent today. Almost half of global trade is now conducted on a duty-free basis. Even the financial and economic crisis that began in 2008 did not bring about any retreat into tariff-based trade-policy measures.<sup>3</sup> Nowadays, only the trade in agricultural goods is still subject to significant import duties. In the non-agricultural sector, substantial import duties are only levied by certain developing and emerging countries, which use them not only to protect domestic industry but as a major source of government revenues.

### 1.1.2 Challenges post-2000

The founding of the WTO in 1994 came at a time when globalisation was gathering pace, with increasing differentiation of cross-border value chains.<sup>4</sup> The associated deepening of international trade relations reinforced the need for an international legal framework that increasingly incorporated regulations applicable beyond the border (e.g. product-related rules) and also encompassed services and investments. Moreover, the protection of intellectual property became increasingly important in the context of technology transfer.

To some extent, the WTO took account of these developments. With regard to the trade in goods, multilateral agreements on technical trade barriers and subsidies were *inter alia* concluded which had previously been agreed plurilaterally, i.e. for only certain of the GATT members of the time. The multilateral *General Agreement on Trade in Services*, (GATS<sup>5</sup>) and the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (TRIPS<sup>6</sup>) were extended as well. However, the expansion and deepening of the multilateral rules on such subjects that go beyond tariff reductions (at the border) and internal regulations (behind the border) remained highly contentious.

<sup>2</sup> Agreement on the Establishment of the World Trade Organization (SR 0.632.20).

<sup>3</sup> World Integrated Trade Solution (WITS), [www.wits.worldbank.org](http://www.wits.worldbank.org).

<sup>4</sup> cf. "Strengthening Switzerland's competitiveness in global value chains" in the Federal Council's 2014 Foreign Economic Policy Report dated 14 January 2015 (BBl 2015 1457).

<sup>5</sup> SR 0.632.20, Annex 1B: General Agreement on Trade in Services (GATS).

<sup>6</sup> SR 0.632.20, Annex 1C: Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

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## Sluggish progress of WTO negotiations

The Doha Round of negotiations, launched in 2001 as a sequel to the Uruguay Round<sup>7</sup>, and the overall continued development of the WTO, which sought to focus in particular on the developing countries, was not brought to a conclusion even after many years of drawn-out negotiations. With hindsight, this failure may be attributed to various factors. The economic rise of key emerging countries, including China, posed increasingly serious hurdles to decision-making, as did the strong expansion of WTO membership. At the same time, the readiness of the economically advanced nations to enter into compromises decreased. This was partly because some developing countries had already autonomously dismantled their tariff barriers out of economic self-interest.

Many of the new and strengthened WTO members, moreover, have taken up a defensive position and are demanding far-reaching and global exemptions to development – referred to as “special and differentiated treatment” - for new agreements. Yet other countries are insisting on improved legal certainty in trade relations also with regard to developing countries, and are only willing to agree to exemptions if these are justified by the actual state of development of the countries concerned. Moreover, the financial and economic crisis of 2008 narrowed the trade policy space that many countries need in order to make the concessions required for successfully concluding the Doha Round. For the reasons mentioned, new market openings and agreements on new topics could be achieved more easily and quickly through bilateral or regional preferential FTAs.

## Trade protection measures

In past years, a number of WTO members continuously asserted their right to introduce trade defence measures to counter illicitly subsidised exports (“countervailing duties”) or to protect industries in the event of fast-growing, deleterious imports (“safeguard measures”). Anti-dumping duties are of prime importance in this context. In 2016 and 2017, 294 of these mechanisms were introduced, a high proportion of them by the USA and India. Most were aimed against imports from China.<sup>8</sup>

In many cases, the countries affected by the trade defence measures disputed the legality of these measures, even before the WTO's dispute settlement body. Due to general considerations, Switzerland did not impose any such measures. It is of the view that such mechanisms are at best only effective in the short term and that in the long term they damage the competitiveness of the country imposing them. Switzerland's economy is very deeply integrated in global value chains: if it were to impose trade defence measures itself, these would make the inputs more expensive for the products it exports and thus undermine its international competitiveness. Given the small size of its domestic market, the numerous companies with a high proportion of foreign sales would derive little benefit.

<sup>7</sup> Several WTO agreements dating from 1994 called for the negotiations to be continued, notably the Agricultural Agreement (Art. 20) and the GATS (Art. XIX:1).

<sup>8</sup> WTO Trade Report on G20 Trade Measures, 4 July 2018.

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## Non-tariff trade barriers

According to the WTO Secretariat<sup>9</sup>, there are signs that, with the dismantling of tariff barriers, the focus of protectionist policies has in some cases shifted towards non-tariff measures (NTM). These comprise all types of state-imposed measures not involving duties, including technical specifications (e.g. minimum standards for technical equipment relating to energy consumption) and subsidies (e.g. to promote certain locations) which influence the prices or quantities of internationally traded goods and services. Owing to their variety and their somewhat indirect impact on trade, these measures and their protectionist consequences are difficult to quantify.

International trade law, for example, grants countries the right to impose health or environment policy measures in order to provide an adequate level of protection. However, such measures are also deployed for protectionist purposes. With this type of “disguised protectionism”, avoidable distortive side effects on trade are either intentionally or deliberately accepted. Moreover, in many cases – for instance when various countries pursue a similar goal with different sets of regulations – the very lack of any international coordination may generate high costs for trade. As complying with government regulations (such as the obligation to provide certificates of conformity) incurs expenses, small and medium-sized enterprises (SME) are put at a greater disadvantage by such regulatory costs than larger companies.<sup>10</sup>

### 1.1.3 The economic importance of international trade

In past decades technological advances, declining protectionism and the resulting closer integration of global value chains led to vigorous growth in global trade. On average, the global exchange of goods and services increased at about twice the rate of growth in global gross domestic product (GDP) between 1960 and the outbreak of the 2007 financial crisis.

Increasing international trade in past decades has contributed to economic growth throughout the world, in the developing countries particularly. According to information provided by the World Bank, the proportion of the world population living on less than USD 1.90 a day, adjusted for inflation and purchasing power, fell from around 35 per cent in 1990 to less than 11 per cent in 2013.<sup>11</sup> In developing countries, the incomes of the poorest section of the population are rising. That this increase in the incomes of the poorest 20 per cent of the population is closely connected with the liberalisation of trade policy is undisputed, and indeed this is confirmed by studies produced by the International Monetary Fund.<sup>12</sup>

In Switzerland too, exports rose by an average of 3.6 per cent a year between 1980 and 2017 – as against GDP growth of 1.7 per cent in the same period. Since 1980 the Swiss foreign trade ratio (the proportion of GDP accounted for by imports and

<sup>9</sup> WTO Staff Working Paper 2014-18: Trade Policy Substitution.

<sup>10</sup> cf. OECD (2018) Estimating Ad Valorem Equivalents of Non-Tariff Measures. OECD Trade Policy Papers, No. 2015.

<sup>11</sup> The World Bank – World Development Indicators, <http://datatopics.worldbank.org/sdgs/>.

<sup>12</sup> IMF, WBG, WTO (2017): Making Trade an Engine of Growth for All – The Case for Trade and for Policies to Facilitate Adjustment.

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exports of goods, not including gold or services) has risen from 69 per cent to 93.<sup>13</sup> This shows just how important foreign trade is to Switzerland. Not only large, often multinational companies in Switzerland are active internationally: so are two thirds of SMEs, it is estimated.<sup>14</sup> About three quarters of employees work for companies for which international trade is a relevant factor.<sup>15</sup>

Switzerland is thus far more closely integrated into international trade than other countries. The foreign trade ratio in 2016 was just 27 per cent in the USA and 59 per cent in the United Kingdom; even in Germany it was 84 per cent – well below the Swiss figure.<sup>16</sup> This has had a positive impact on Swiss living standards. According to a study by the Bertelsmann Foundation in Germany, Switzerland achieved the highest growth in per-capita income due to globalisation between 1990 and 2016 – thus benefiting to a disproportionate degree from the integration of global trade.<sup>17</sup>

Open borders intensify competition and accelerate structural change, most of which is technology-driven. Internationally active companies must remain especially competitive if they are to survive. This dynamic is reflected in the labour markets, which highlight the adjustment costs for the population; Basic and advanced training, specialisation, job flexibility. Ongoing structural change is also taking place in Switzerland, which so far has coped with it well. There has been a substantial increase in employment in Switzerland, and unemployment is permanently low. However – as in other countries – it is clear that structural change is primarily driven by population growth and technological advances, much less by foreign trade (“globalisation”).<sup>18</sup>

## 1.1.4 Sustainable development

Global governance for sustainable development has increased in importance since the turn of the century.<sup>19</sup> Corresponding efforts in the international arena culminated in 2015 in the adoption of the United Nations’ Agenda 2030 for sustainable development (*Sustainable Development Goals*, SDGs). Various objectives are directly relevant to international trade and investment policy. A major challenge remains the improvement of coherence and interfaces between international environmental and social regulatory frameworks on the one hand, and trade and investment on the other.

<sup>13</sup> GDP quarterly estimate 29.11.2018, goods and services, not including gold bars, other precious metals, coins, gems and precious stones, works of art and antiquities, SECO.

<sup>14</sup> Credit Suisse (2014): Success factors for Swiss SMEs – prospects and challenges in the export field.

<sup>15</sup> Statistik der Unternehmensstruktur (STATENT), Federal Statistical Office (FSO)

<sup>16</sup> Goods and services; The World Bank - World Development Indicators, [www.datatopics.worldbank.org](http://www.datatopics.worldbank.org). The corresponding foreign trade ratio for Switzerland, including non-monetary gold and valuables, is 120%.

<sup>17</sup> Bertelsmann Foundation (2018): 2018 Globalization Report – Who Benefits Most from Globalization?

<sup>18</sup> SECO (2017): Ursachen und Auswirkungen des Strukturwandels im Schweizer Arbeitsmarkt.

<sup>19</sup> cf. *Sustainability in foreign economic policy* in the 2009 Foreign Economic Policy Report of the Federal Council dated 13 January 2010 (BBl 2010 479).



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EU and Japan; among other things, this criticism is related to the persistently strong, or even growing role of the state in various sectors of the Chinese economy. At the same time, and despite advancing liberalisation, foreign direct investment in China remains subject to restrictions that are far from being transparent, while intellectual property enjoys little protection or in extreme cases is even subject to forced technology transfer.

### **1.2.1 Reversion to tariff-based trade protectionism**

The recent escalation was triggered by the new protective duties introduced by the USA at the beginning of the year under review. In addition to photovoltaic panels and washing machines, these apply to steel and aluminium products – justified by the USA in these last two categories on the grounds of the need to protect national security. Exports from Switzerland are affected by these measures, and so are exports from other countries – especially the EU – with inputs from Switzerland. The USA also introduced targeted duties on imports from China.

In response to this action by the USA, which to a certain degree may have also been tactically motivated by the prospect of new bilateral negotiations, a number of major trading partners – including China, the EU, Canada, Mexico and Turkey – immediately retaliated by introducing import duties on goods from the USA. Switzerland did not institute any countermeasures. In addition to such countermeasures, some trading partners introduced additional safeguard measures to protect their industries against goods flows that were liable to be redirected after protective duties had effectively excluded them from the vast US market. These safeguard measures have far-reaching implications, because they apply to imports from all countries of origin.

The safeguard measures taken by the EU in the steel sector in the year under review are particularly significant for Switzerland. In the period between 2013 and 2017, an average of 95 per cent of Swiss steel exports went to the EU. Since 19 July, imports to the EU exceeding the prescribed import quotas have been subject to duty of 25 per cent. Uncertainties about the future shape of EU safeguard measures have, since autumn, resulted in noticeable declines in sales. The additional duties imposed from mid-December even forced some of the Swiss companies affected to stop exporting to the EU altogether.

Under the terms of the WTO agreement on safeguards, those taken by the EU apply equally to all third countries. The EU exempted only certain developing countries and the EEA states from these safeguard measures. Switzerland intervened several times at various levels of the EU: invoking the 1972 bilateral FTA <sup>21</sup> (FTA 1972), it called for protective measures not to restrict bilateral trade. For its part, the EU justifies its decision not to exempt Switzerland from these measures on the basis that, unlike the EEA states, it is not part of the common market.

<sup>21</sup> Agreement of 22 July 1972 between the Swiss Confederation and the European Economic Community (SR 0.632.401).

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## 1.2.2 Counter-movements

The USA's protectionist rhetoric and the trade measures it subsequently implemented have been political stimuli in other countries for certain counter-movements. The EU, Japan and China in particular are stepping up their efforts to enhance the integration of international trade. The EU is working on the broad expansion and improvement of its already extensive FTAs, having recently concluded agreements with Vietnam, Canada and Japan. Negotiations with Mercosur (Argentina, Brazil, Paraguay and Uruguay) made good progress in the year under review. The existing agreements with partners such as Mexico and Chile are being modernised, and the EU has begun negotiations with Australia and New Zealand.

Japan has taken over the leading role in the revival of the *Trans-Pacific Partnership* (TPP) agreement following the USA's withdrawal from this regional FTA in 2017. The agreement, which now describes itself as a *Comprehensive and Progressive Trans-Pacific Partnership* (CPTPP), was signed by all eleven remaining contracting parties<sup>22</sup> on 8 March. The agreement basically permits all states to accede to it, and South Korea, Indonesia, the Philippines, Thailand and the United Kingdom<sup>23</sup> in particular are considering to do so. Against the backdrop of the current trade crisis, Switzerland is also carefully considering the possible benefits of accession. Switzerland already has FTAs with numerous members of the CPTPP<sup>24</sup> and is in negotiation with others<sup>25</sup>, so any negative effects on the Swiss economy to be expected from the establishment of the CPTPP would in any case be limited – even if Switzerland did not take part in it.

Another significant initiative is the *Regional Comprehensive Economic Partnership* (RCEP), led by China. In addition to China, this partnership also includes the member states of the *Association of Southeast Asian Nations* (ASEAN)<sup>26</sup> and its free trade partners Australia, India, Japan, New Zealand and South Korea.

## 1.3 Conclusions for Switzerland's foreign economic policy

Securing access to foreign markets with minimum discrimination and maximum legal certainty has always been a central pillar of the Federal Council's foreign trade strategy, and it remains so today.<sup>27</sup> This market access is under threat from the currently beleaguered multilateral trading system and the danger of the further escalation of trade disputes. Such an escalation and the erosion of the rules-based

<sup>22</sup> Australia, Brunei Darussalam, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam.

<sup>23</sup> See the British government's *White Paper* of July 2018, margin note 159.

<sup>24</sup> Chile, Japan, Canada, Mexico, Peru, Singapore.

<sup>25</sup> Malaysia, Vietnam.

<sup>26</sup> Brunei Darussalam, Indonesia, Cambodia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, Vietnam.

<sup>27</sup> See the Reports of the Federal Council on Foreign Economic Policy 2004, 2005 and 2011 (BBl 2005 1089, BBl 2006 1665 and BBl 2012 827).

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multilateral trading system would affect Switzerland much more severely than trading partners with large internal markets, such as the USA, China and the EU.<sup>28</sup>

The challenges for Switzerland thus include the safeguarding of Swiss interests in the multilateral and bilateral contexts, as well as the continued development of the domestic economic environment. The central concern here is to strengthen Switzerland's already impressive ability to adapt to a changing environment and its scope for action in the sphere of foreign trade policy.

### **1.3.1 Safeguarding and reform of the multilateral trading system**

Switzerland has a vital interest in ensuring that the legal framework of the multilateral trading system is respected, and that the trade barriers recently put in place are dismantled in conformity with the rules. This is the only way of maintaining the integrity of the multilateral trading system, and of extending it with new reforms and further liberalisation.

Owing to its limited trading power, it is not generally in Switzerland's interest – as mentioned earlier – to combat trade measures taken by other countries with direct countermeasures. That would merely escalate the trade dispute, while doing nothing to rectify the causes of the problem. Moreover, it would expose Switzerland to accusations of infringing WTO rules, thus making it vulnerable to attack. On top of that, retaliatory measures could weaken Switzerland's competitiveness by increasing the prices of inputs and consumer goods.

One possibility open to Switzerland is to assert its existing rights with the WTO's Dispute Settlement Body. In fact, it has already initiated proceedings against the US duties on steel and aluminium (see section 3.1). As in the past, Switzerland only chooses this path in the event of clear breaches of rules, and after having exhausted diplomatic and trade-policy options for resolving the dispute amicably. This makes it all the more important to Switzerland for this central function of the WTO to be maintained.

#### **Current approaches to the reform of the WTO**

The WTO will become more relevant to international trade policy if its members succeed in further developing existing agreements, and especially incorporating new topics in them. The first steps in this direction have already been taken. At the WTO's eleventh Ministerial Conference in Buenos Aires in 2017, members in varied combinations – and at very different levels of development – approved plurilateral initiatives involving some WTO members on a variety of subjects (see table 7.1.1). Work on these began during the year under review. Switzerland is convinced that plurilateral agreements that jointly cover a critical mass of the global trade affected can function as an important catalyst, paving the way towards subsequent multilateralisation. This happened in GATT negotiation rounds with analo-

<sup>28</sup> Conseil d'analyse économique (2018): Avis de tempête sur le commerce international, [www.cae-eco.fr](http://www.cae-eco.fr).

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gous mechanisms that were subsequently multilateralised under the aegis of the WTO, thus making an important contribution to the continued development of the multilateral trading system. Switzerland thus continues to actively support these processes.

One central obstacle to the conclusion of new agreements is the question of the extent to which the different stages of economic development reached by various WTO members are taken into account. There is no longer a consensus in favour of the previous practice of across-the-board exemption provisions for countries classified as developing simply because they self-identify as such. The approach devised in the course of the multilateral WTO agreement on trade facilitation and originally instigated by Switzerland, in which varying levels of development are accounted for on a differentiated basis, could be the way forward. From the Swiss viewpoint, suitable solutions must be found for individual cases in future negotiations that make individual allowance for countries' development levels and the opportunities that trade policy afford them.

A consensus on common rules for 164 countries is required in multilateral negotiations. As an acknowledged supporter of the multilateral trading system ("*friend of the system*"), Switzerland will do everything it can to ensure that the role of the WTO is strengthened – not least in order to overcome this crisis. It is actively involved in a reform process initiated by Canada (cf. section 3.1).

Legal certainty – maximised by final, legally binding rulings – is in the interests of the Swiss economy. To this end, the present blockade of the WTO's appellate body must be lifted so that final rulings can continue to be delivered. The WTO's dispute resolution procedure also features prominently in the discussions regarding the reform of the Organization. The enforcement of law by means of final rulings is one of its greatest achievements. In this context, Switzerland continues to do all it can to keep political influence on the administration of justice to a minimum in future.

Transparency is also an important factor in improving the enforcement of existing law. With its regular reviews of trade policy, the WTO already has an effective mechanism for the creation of transparency with regard to developments in the trade policies of individual members. Action is needed with regard to notification obligations, which at present are not always met satisfactorily. Switzerland is committed to ensuring that members improve compliance with them.

### **1.3.2 Safeguarding and expansion of the bilateral path with the EU**

The EU remains Switzerland's most important trading partner by far – though despite continuing growth in bilateral trade volume, the EU's share of Switzerland's foreign trade has declined in the last ten years as new markets opened up. Even so, some 53 per cent of Swiss visible exports went to the EU in 2017 – and the EU accounted for as much as 72 per cent of its visible imports. The EU is also Switzerland's most important partner in the trade in services, with 47 per cent of exports and 50 per cent of imports.

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Unhindered access to the EU's internal market for goods and services, and to that of the United Kingdom after it leaves the EU, is crucially important to the Swiss economy (see section 2). If the multilateral trading system emerges from the crisis described above in a weakened state and multilateral trading rules are less effective in securing market access abroad than they are now, it will be even more important to safeguard and expand the bilateral path in the area of market access to the EU – a partner with whom Switzerland shares similar positions and views, and not only in matters of trade policy.

### **1.3.3 Expanding and deepening the network of preferential trade agreements**

Preferential trade agreements (free trade agreements, FTAs) improve market access in partner states, and they are also designed to prevent Swiss exporters from being at a political disadvantage where they are in particular competition with exporters in the EU. The present dynamic of the EU in its free trade negotiations also requires a greater commitment from Switzerland in order to avoid discrimination of Swiss companies abroad. Switzerland already has a broad network of FTAs: 30 of them, with 40 partners<sup>29</sup> outside the EU and the European Free Trade Association (EFTA). This network is being constantly expanded, while existing FTAs are being extended and modernised (see sections 3 and 7.1.2).

The existing network of FTAs with partners outside the EU/EFTA gives Swiss companies preferential access to markets with about 2.4 billion consumers and a total GDP of around USD 27 trillion.<sup>30</sup> Exports of goods from Switzerland to these countries in 2017 accounted for 23 per cent of total exports.<sup>31</sup> The most commercially important country with which Switzerland has no FTA yet is the USA. Although developments in international trade policy are hard to foresee at present, there may well be new opportunities to conclude FTAs – with the USA, for example, Switzerland's second-most-important trading partner after the EU. Exploratory discussions about possible negotiations are currently under way.

But modern FTAs go beyond the elimination or reduction of customs duties on the trade in goods, covering other important fields as well. The subjects of greatest concern to Switzerland are the establishment of rules for the delivery of services (financial services in particular), access to public procurement procedures, the protection of intellectual property and improved coherence between trade and sustainable development. Where older agreements have only rudimentary provisions – or none at all – in these areas, Switzerland works for appropriate additions.

It is also important to ensure that the agreements apply in practice to all economic operators, especially SMEs. In this connection the design and – if necessary – the review of the rules of origin should be mentioned. One example: Switzerland is

<sup>29</sup> See State Secretariat for Economic Affairs (2018). <https://www.seco.admin.ch> > Foreign Trade and Economic Cooperation > Economic\_Cooperation > Free Trade Agreements > List of Free Trade Agreements of Switzerland

<sup>30</sup> 2017 figures, World Bank.

<sup>31</sup> Swiss Impex, Federal Customs Administration (FCA).

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calling for the modernisation of the Regional Convention on pan-Euro-Mediterranean preferential rules of origin<sup>32</sup> (the PEM Convention), which harmonises the rules of origin in the entire free trade area of the EU, the EFTA, the western Balkans and the Mediterranean. In free trade relations outside Europe, Switzerland is striving for greater simplification and harmonisation of the complex rules of origin within the various FTAs as well as for the more flexible cumulative application of FTAs.

There are limits to the possibilities of bilateral and plurilateral free trade policy, however, as a growing number of agreements – and consequently of rules and regulations – increases complexity for economic operators. Switzerland's freedom of movement to conclude new FTAs and modernise existing agreements is limited in particular by the fact that many of its current negotiating partners have offensive interests in the area of agriculture that are virtually impossible for Switzerland to acquiesce to at present.<sup>33</sup> Negotiation partners make concessions in areas important to Switzerland conditional on Swiss concessions on market access for agricultural produce. Whereas Switzerland has hardly adjusted its practice in relation to market access for agricultural produce, the agricultural policies of many other countries – especially in the EU – have undergone further development and liberalisation.

The EU is now in a position to conclude FTAs with partners with significant offensive agricultural interests. It has much greater freedom of action than Switzerland. Japan has also taken the internal policy steps necessary to enable it to continue to conclude FTAs. Under the CPTPP, for example, Japan has been able to make far-reaching concessions. Both parties to the comprehensive economic and trade agreement between the EU and Canada (CETA) have eliminated over 90 per cent of their agricultural duties. Switzerland's restrictive agriculture policy means that its objective of concluding FTAs at least as comprehensive as those of its most important competitors cannot at present be achieved. Modernisation negotiations with Mexico and Canada, for example, have been blocked for over a year, while the EU has successfully concluded its negotiations with the same two partners.

Besides modernising existing FTAs and negotiating new ones with various partners in Asia, Switzerland's current efforts concentrate particularly on concluding negotiations with the Mercosur states. At present the Mercosur states import goods from Switzerland to the value of CHF 2.8 billion<sup>34</sup>, making them important target markets for Swiss exporters. Mercosur duties on Swiss exports are high: seven per cent on average, but ranging as high as 35 per cent. There is also considerable potential for discrimination vis-à-vis the EU. An FTA with this partner would give Swiss business improved access to a large market with a growing middle class. The EU is currently in the closing stages of its negotiations with Mercosur.

<sup>32</sup> SR **0.946.31**

<sup>33</sup> cf. section 5.1 (free trade agreements and agriculture) in the 2017 Foreign Economic Policy Report of the Federal Council dated 10 January 2018 (BBl **2018** 821).

<sup>34</sup> Not including gold bars or other precious metals, coins, gems and precious stones, works of art or antiquities.

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### 1.3.4 The economic policy framework in Switzerland

To ensure that Switzerland remains a competitive place to do business and all strata of the population are to be able to share in the prosperity brought by international trade, an appropriate economic policy framework is necessary – not least in areas such as education, the labour market and the fiscal and social systems. The important contribution that international trade makes to growth poses political challenges, especially if the effects of structural change appear concentrated at certain times or in certain regions. In the last few years, some sectors and regions in economically advanced countries, in particular the USA, have suffered substantial job losses.

Technological advances, digitalisation among them, will continue to contribute to this constant structural change. However, isolationism is not an appropriate response to this sort of economic policy challenge. Globalisation is a comprehensive development: besides intensifying economic relations through trade, it also increases the political, cultural and social networking of societies. These trends cannot be stopped without causing enormous costs.

Many different policy areas have major effects on business location quality.<sup>35</sup> A good policy environment strengthening the competitiveness of companies in Switzerland has to be ensured. This includes, for example, fiscal and competition policy and alleviating the administrative burden on companies. Structural change must be accompanied at a political level in order to help cushioning adjustment costs. Central factors here are the structure of the labour market and the high quality of the education system.

#### **Unilateral reduction of industrial customs duties and simplification of customs procedures**

The decision of the Federal Council to prepare a proposal for the unilateral reduction of customs duties on imported industrial goods is highly significant for foreign trade. The increasing integration of global value chains means that competitive companies are now heavily dependent on imported inputs. Other economies with strong international networks – Singapore, New Zealand, Canada, Norway and Iceland, for example – have also begun to reduce their import duties unilaterally. This will reduce the prices of imported goods, thus combating the effects of “high-price Switzerland”. Not only will consumers benefit, but the economy too will benefit from cheaper foreign inputs and from the reduced administrative burden on companies. A unilateral reduction of duties on industrial products will underline Switzerland’s commitment to a liberal world trade order. The Federal Council opened a hearing on the necessary legal adjustments on 7 December, and the proposal will subsequently be submitted to Parliament.

New technological developments have created great potential for increasing the efficiency of cross-border freight traffic. By 2026, the FCA’s DaziT<sup>36</sup> transfor-

<sup>35</sup> See “Switzerland as a business location – an appraisal and central contributing factors” in the 2015 Foreign Economic Policy Report of the Federal Council dated 13 January 2016 (BBl 2016 817).

<sup>36</sup> [www.dazit.admin.ch](http://www.dazit.admin.ch)

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mation programme will modernise and digitalise all customs and revenue collection processes, thus making cross-border movement even simpler and faster. This requires the wholesale replacement of the FCA's IT systems. The objective is to enable customs formalities to be dealt with anywhere and at any time. In particular, this will reduce the burden on business by reducing the (regulatory) costs of customs clearance while at the same time making checks more effective.

### **Avoiding technical trade barriers**

The Federal Council is anxious to counter technical trade barriers in order to minimise the costs they give rise to. Such trade barriers include, for example, product regulations that differ from those of the trading partner or for which supplementary recognition processes exist. One measure taken by Switzerland to avoid technical trade barriers is its introduction of the *Cassis de Dijon* principle. This principle applies to products that are legally authorised for sale in an EU or EEA state and can thus be freely sold throughout the EU internal market. The principle makes it harder for new Swiss regulations to include unjustified deviations from EU/EEA regulations, thus inhibiting the creation of new technical trade barriers. The Federal Council can enact exemptions from the *Cassis de Dijon* principle in order to protect overriding public interests. These exemptions are reviewed periodically.

A further mechanism for the avoidance of technical trade barriers exists in international agreements on the recognition of tests, conformity assessments, registrations and approvals. An agreement was recently negotiated with South Korea, for example, on the mutual reliance on inspection results in the field of Good Manufacturing Practice (GMP) for medicines. This simplifies the mutual trade in medicines, and reduces costs and delivery times for the Swiss pharmaceutical industry. Switzerland has also reached equivalence agreements with a number of states<sup>37</sup> for organic products. The mutual recognition of rules for organic agriculture, the processing and labelling of organic products and the relevant control systems encourages trade in organic products.

Proposals have been forward in Switzerland increasingly in recent years for the implementation of trade-policy measures relating to goods imports to achieve legitimate political sustainability objectives. The Federal Council will continue to call for voluntary standards devised in consultation with the private sector and other relevant players, and for more sustainable forms of production in countries of origin. New measures must in any case be targeted and designed with as little trade-distorting effects as possible.

### **Agricultural policy reform**

Reforms in the Swiss farming sector need to be continued in order to increase the country's capacity to take action on trade policy. Agricultural trade has a high priority in multilateral WTO discussions with most members, including the USA – as it does in the current free trade negotiations (e.g. EFTA/Mercosur). In the context of agricultural policy from 2022<sup>38</sup> (AP22+) the Federal Council will put proposals to

<sup>37</sup> EU, Japan, Canada and the USA.

<sup>38</sup> [www.blw.admin.ch](http://www.blw.admin.ch) > Politik > Agrarpolitik > AP22 plus

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parliament for amendments to the present agricultural policy instruments, relating *inter alia* to direct payments.

AP22+ is intended to bring about targeted improvements in the domestic framework conditions, enabling the agriculture and food industry to make advances in the operational, market and environmental areas. As well as reducing its ecological footprint and pursuing other objectives, it is also intended to make Swiss agricultural production more internationally competitive.

## **1.4 Summary**

The multilateral trading system is in its deepest crisis since the WTO was founded in 1994.

The escalation of trade measures is a heavy burden on international trade, and it constitutes a grave threat to continued growth in the global economy. More than ever, international trade policy and Switzerland's foreign economic policy face an uncertain future.

It is still possible, however, that this crisis will take a positive turn and become the starting point for a relaxation of the accumulated trade-policy tensions and for a renewal of the multilateral trading system.

In any possible scenario, it is up to Switzerland to defend the interests of its economy. As it depends on the rules-based multilateral trading system, Switzerland is committed to maintaining and strengthening it with reforms. It thus supports the WTO reform agenda launched by Canada with a small group of like-minded WTO members. The annual informal WTO ministerial meeting on the fringes of the WEF in Davos on 25 January 2019 will be devoted to these challenges. Political and legal answers to open questions are required, for example in the area of digitalisation and sustainable development. Negotiations on individual subjects with some WTO members (known as plurilateral negotiations) may be able to act as an important catalyst here.

If the erosion of the multilateral system continues and trade-policy blocks emerge because of regional preferential agreements, Switzerland will have to take prompt action to counteract discrimination and ensure that Switzerland as a business location remains integrated in global value chains. To this end, Switzerland will provide legal certainty in foreign trade by negotiating and concluding new preferential agreements and the deepening of existing agreements as broadly as possible.

In terms of domestic economic policy, Switzerland relatively well positioned to meet the new challenges. Even so, further reforms are to be implemented so that its capacity to take action on foreign trade policy in order to defend its interests is ensured.