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Transatlantic Free Trade Zone:  
A promising, but difficult venture

# Working Paper

## No. 161

### Transatlantic Free Trade Zone: A promising, but difficult venture

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## **TRANSATLANTIC FREE TRADE ZONE: A PROMISING, BUT DIFFICULT VENTURE**

At around 5%, global trade has been growing at an annual rate that is almost twice as fast as global economic output (+2.7% a year) over the past ten years. Exports have evidently shown much more dynamic development than domestic demand, i.e. consumption and investment. So we do not need to resort to economic theories in order to highlight the fact that the expansion in international trade has been one of the main drivers behind growing prosperity levels.

For a few years now, most of the world's industrialized nations have been grappling with anemic growth. On average, their real gross domestic product has shown growth of only 0.2% a year over the past five years, whereas the emerging markets have been clocking up growth of 5.0%. So it comes as no surprise that the industrialized nations struggling with weak growth are trying to up their contribution to world trade growth. Various strategies could be considered in this respect: measures to boost macroeconomic productivity, efforts to obtain free access to foreign markets or policies aimed at devaluing a country's own currency. The latter has become a hotly debated topic, branded "the currency war", in recent months, with some countries, and Japan in particular, being accused of using their monetary policy to actively promote devaluation.

So especially given this debate, the fact that policymakers are looking into other ways of boosting growth comes as a welcome development. The decision made by the EU and the US to enter into negotiations on a transatlantic trade and investment partnership is a key initiative within this context.

### **1. A bilateral agreement would now appear to be within reach**

In a concerted press statement<sup>1</sup>, US President Barack Obama, President of the European Council Herman Van Rompuy and President of the European Commission José Manuel Barroso announced, in mid-February, that they would soon be commencing negotiations on an extensive "transatlantic free trade and investment partnership". According to the presidential trio, the aim of this partnership is not only to stimulate transatlantic trade and mutual investment, but also to contribute to the development of global regulations to strengthen the multilateral trading system.<sup>2</sup>

The idea of a joint free trade agreement is not new. Rather, the announcement is the outcome of a political debate that has been ongoing since the mid-1990s. What is new, however, is the broad-based political support signaled by almost all EU governments and US Democrats and Republicans alike, as well as the specific time frame that has been set out.

Official talks on the EU-US free trade agreement, which would create a market with more than 800 million potential customers, are to be launched in connection with the G8 summit on 17/18 June in Lough Erne, Northern Ireland, the aim being to conclude them within a two-year period. First, the EU member states have to issue the Commission with a formal representation mandate, with the US Congress having to do the same for the

<sup>1</sup> See European Commission: "Statement from United States President Barack Obama, European Council President Herman Van Rompuy and European Commission President José Manuel Barroso", Memo, Brussels/Washington, February 13, 2013, [http://europa.eu/rapid/press-release\\_MEMO-13-94\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-94_en.htm).

<sup>2</sup> See European Commission: "European Union and United States to launch negotiations for a Transatlantic Trade and partnership", Memo, Brussels, February 13, 2013, [http://europa.eu/rapid/press-release\\_MEMO-13-95\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-95_en.htm).

American government. The second half of March is likely to see the Council make a decision on the draft negotiation guidelines to be submitted by the European Commission. The US administration, in turn, plans to send a notification to Congress triggering a 90-day layover period.

The planned bilateral agreement is backed up by the final report of a high-profile working group that was set up in November 2011 under the auspices of the United States Trade Representative Ron Kirk and the European Commissioner for Trade Karel De Gucht, and which was the force behind the start of the negotiations. The report outlines an extensive agreement covering a broad range of bilateral trade and investment issues.<sup>3</sup> Three trade policy strategies lie at the heart of the initiative:

- **Market access** by way of (a) the elimination of as many tariff trade barriers as possible (customs duties on industrial and agricultural products), (b) opening of the service sectors in line with other trade agreements, as well as in new sectors such as the transport industry, (c) achieving the highest possible levels of liberalization and investment protection and (d) free access to public-sector tenders (opening up access to government procurement markets)
- **Elimination of non-tariff trade barriers and gradual regulatory convergence** in respect of a more integrated transatlantic market: (a) coordination/mutual acceptance of standards and procedures in the sanitary and phytosanitary sectors, as well as in respect of technical trade barriers, based on the SPS/TBT Agreements of the World Trade Organization (WTO)<sup>4</sup>, (b) more consistent regulatory requirements in specific sectors (automotive, chemicals and pharmaceutical industry, other healthcare sectors such as medical appliances)<sup>5</sup>
- **Coordination of trade policy positions** in respect of the "Global Trade Challenges and Opportunities in the 21st century", which, according to the negotiation leaders, include protecting intellectual property, as well as the social and ecological aspects of trade. These are areas in which the US and the EU want to set examples of global rules. After all, these two regions are the most important trade and investment partners for many countries across the globe.<sup>6</sup>

Given that the duty rates are already relatively low, the expert group believes that the greatest benefit of the agreement would be that it would eradicate "trade barriers lurking behind the customs barriers".

## 2. The transatlantic trade network – an overview

The two heavyweights, the US and the European Union, which generate just shy of half of nominal global output (2012e: 48%) and contribute one third to the world's trade flows, are already closely intertwined in economic terms.

Accounting for just under 17% of extra-EU exports, the United States is the EU's primary trading partner. The country also makes up 11.1% of extra-EU imports, putting it in third place in the list of the old continent's main import partners (behind China and Russia). At the same time, the EU is the US' second most important import market (16.9%) and

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<sup>3</sup> See Final Report, High Level Working Group on Jobs and Growth, February 11, 2013, [http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc\\_150519.pdf](http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc_150519.pdf).

<sup>4</sup> SPS: Agreement on the Application of Sanitary and Phytosanitary Measures. TBT: Agreement on Technical Barriers to Trade.

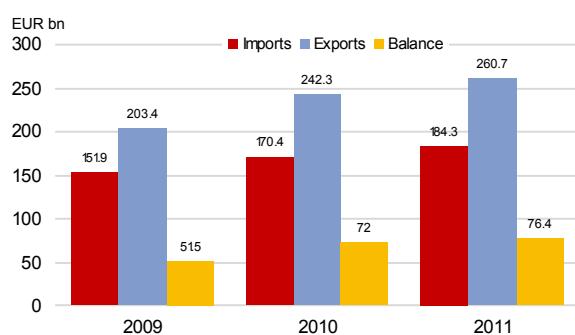
<sup>5</sup> For example, by extending the principle of the mutual recognition of standards or product tests.

<sup>6</sup> See <http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/countries/united-states/>.

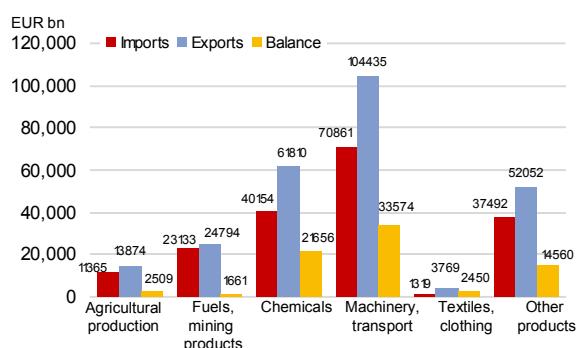
export market (18.5%) after Canada. In 2011, the 27 EU countries exported goods worth EUR 260.7bn across the Atlantic and imported a volume of goods worth EUR 184.3bn.<sup>7</sup> Machinery and transport equipment, chemicals, as well as fuels and mining products made up the lion's share of the trading volume, with only 5.6% of the exported, and 4.3% of the imported goods relating to agricultural products due to the level of protection surrounding these markets. Services exports and imports (leaving the public sector out of the equation) totaled EUR 143.9bn and EUR 138.4bn respectively in 2011. This means that 24.1% of the services exported to countries outside of the EU were destined for the United States, with 29% of services purchased from outside of the EU originating from the US.

## EU: Economic relations with United States

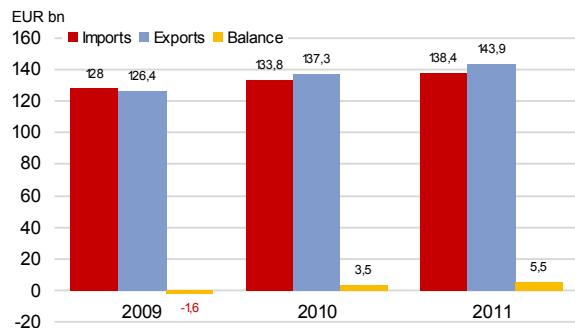
### Trade in goods



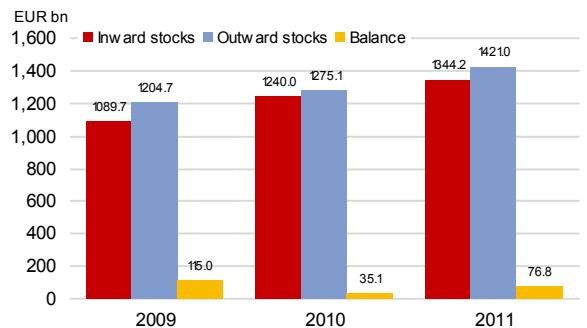
### Merchandise trade by products



### Commercial services



### Foreign direct investment



Sources: Eurostat, European Commission.

Investments on both sides of the Atlantic tallied up to almost EUR 2.8 trillion in total in 2011. According to information supplied by the European Commission, US companies invested three times as much in EU countries as they did in the entire Asian region. As far as the EU is concerned, direct investments in the United States are eight times higher than those made in India and China.<sup>8</sup> Last but not least, the significant share of inter-company trade at multinational companies is testimony to the fact that foreign direct investment is a key driver of transatlantic relations. Estimates suggest that inter-company trade accounts for around one-third of the total transatlantic trading volume.<sup>9</sup>

<sup>7</sup> See European Commission, Directorate-General for Trade Statistics, [http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc\\_111704.pdf](http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_111704.pdf).

<sup>8</sup> See <http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/countries/united-states/>.

<sup>9</sup> See ibid. More than 15 million employees work for European companies in the US or US companies in Europe. See European Commission: "Trade: a key source of growth and jobs for the EU", Commission

### 3. What trade restrictions apply?

**Customs policy:** Customs duties drive a wedge between the global market and domestic market price. According to the WTO, United States International Trade Commission (ITC) and the United Nations Conference on Trade and Development (UNCTAD), the EU's customs barriers, which average 5.2%, and those imposed by the US, averaging 3.5%, are relatively low.<sup>10</sup> The costs triggered by import duties are significant due to the substantial volume of trading flows across the Atlantic.

The customs duties levied on agricultural products in transatlantic trading exceed on average the customs duties imposed on non-agricultural products. US companies, for example, paid customs duties averaging 13.9% for agricultural exports to the European Community in 2010, while European agricultural exporters were faced with customs rates of 6.8% on average. The customs duties imposed on trading in non-agricultural products came in at 4.3% and 3.5% respectively.<sup>11</sup>

Far more significant are the much more opaque and selective **non-tariff trade barriers**.<sup>12</sup> Particularly due to the key role played by the regulation of product and factor markets on both sides of the Atlantic, inconsistent norms and product-specific standards hinder exporters in their access to the markets and increase transaction costs. According to the EU-US expert group, regulatory differences are responsible for additional costs that correspond to levies of more than 10%, or as much as 20% in some sectors.<sup>13</sup>

Different regulations apply both to the exchange of goods and to services products, such as insurance or financial products. Classic trade barriers in the exchange of goods include differences in how precise designation of origin information has to be, different provisions governing reporting obligations, threshold values and environmental requirements in the chemicals industry, diverging technical standards in the automotive industry and, last but not least, different labeling practices for genetically modified foods (agricultural sector). It is also questionable whether the independent regulatory authorities in the drug sector could readily accept European/US certification.<sup>14</sup>

Restrictions in the service sector range from tax discrimination to the application of certain accounting regulations (IFRS vs. US GAAP), differences in the implementation of the Basel II regulations for banks and diverging US regulations imposed by the Securities and Exchange Commission (SEC) on the financial services sector, to postal service monopolies for the communications sector.<sup>15</sup>

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contribution to the European Council of 7-8 February 2013, [http://ec.europa.eu/commission\\_2010-2014/president/news/archives/2013/02/pdf/20130205\\_2\\_en.pdf](http://ec.europa.eu/commission_2010-2014/president/news/archives/2013/02/pdf/20130205_2_en.pdf), p. 6.

<sup>10</sup> See WTO, ITC and UNCTAD: "World Tariff Profiles 2012", 2012, pp. 76 and 170, [http://www.wto.org/english/research/publications\\_e/world\\_tariff\\_profiles12\\_e.htm](http://www.wto.org/english/research/publications_e/world_tariff_profiles12_e.htm).

<sup>11</sup> See ibid. Figures are non-trade weighted customs rates.

<sup>12</sup> These basically include not only quantity and price-related restrictions "on the border" (e.g. import quotas), but in particular also trade barriers "after the border", i.e. administrative restrictions and economic policy measures that cause trade restrictions as a sort of side effect (e.g. labeling requirements, structural and regional subsidies).

<sup>13</sup> European Commission: "European Union and United States to launch negotiations for a Transatlantic Trade and partnership", Memo, Brussels, February 13, 2013, [http://europa.eu/rapid/press-release\\_MEMO-13-95\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-95_en.htm).

<sup>14</sup> See Thomas Ludwig: "Woran der transatlantische Handel krankt" (the weak points of transatlantic trade), Handelsblatt no. 32, February 14, 2013, pp. 8 et seq.

<sup>15</sup> See Berden, Dr. Koen et al. (2009): "Non-Tariff Measures in EU-US Trade and Investment – An Economic Analysis", ECORYS Nederland BV, Client: European Commission, Directorate-General for Trade, [http://trade.ec.europa.eu/doclib/docs/2009/december/tradoc\\_145613.pdf](http://trade.ec.europa.eu/doclib/docs/2009/december/tradoc_145613.pdf). In the US, the US Postal Service has a monopoly on certain postal services.

The sectors hit particularly hard by non-tariff barriers according to a study commissioned by the European Commission's Directorate General for Trade<sup>16</sup> include, from an EU perspective, on a "trade restrictiveness index" scale of 0-100, the aerospace sector (56), engineering (51), medical technology (49), the cosmetics industry (48), chemicals and biotechnology and the food and drinks industry (46 in each case). The lowest non-tariff barriers apply to the pharmaceuticals sector (24), the wood and paper industry (30) and the service sectors of information and communication technology (24) and financial services and insurance companies (30 each).

#### 4. How a free trade agreement filters through

A free trade agreement has two effects: it creates and diverts trade. Trade is created if a product that is manufactured domestically is replaced by an imported product because the reduction in customs duties makes it cheaper than the product that is manufactured domestically. The reduction in customs duties results in lower prices and prosperity gains due to more efficient production. A second possible effect, however, is trade diversion. Trade is diverted when a member of the trade agreement opts not to import a product from a non-member country with efficient production, but from a member country with less efficient production, because the abolition of the customs duties favors the less efficient producer. Shifting production from an efficient producer to a less efficient one constitutes a reduction in prosperity.<sup>17</sup> So in principle, a trade agreement could reduce prosperity if the trade diversion effect outweighs the trade creation effect. This risk applies in particular to bilateral trade agreements that abolish high customs duties.<sup>18</sup>

If a free trade agreement is concluded, it is important to determine which goods originate from the partner country and which do not. Rules of origin are the terms and conditions that define a product's country of origin. Often, they set a minimum proportion of the product value that has to be produced in the country in question. Renowned economists like Jagdish Bhagwati and Anne O. Krueger have been particularly critical of the rules of origin in free trade agreements.<sup>19</sup> Restrictive origin definitions can also end up diverting trade. By way of example, higher requirements regarding the domestic share of a product can squeeze out more efficient producers from other countries.<sup>20</sup> So rules of origin can be abused for protectionist purposes.

Another problem with free trade agreements is that they violate a fundamental principle of internal trade, the "most favored nation" clause, which says that the trade advantages granted to one WTO member state must also be granted to all of the other WTO member states. A free trade agreement gives the products of the parties to that agreement preferential treatment over the products of countries that are not party to the agreement but may be WTO member states. The agreements of the WTO itself, however, grant members of free trade areas exceptions from the "most favored nation" clause, provided that they meet certain requirements. Nevertheless, one of the objections frequently leveled against free trade agreements is that they weaken the fundamental framework of

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<sup>16</sup> See *ibid.*

<sup>17</sup> See Cooper, William H.: "Free Trade Agreements: Impacts on U.S. Trade and Implications for U.S. Trade Policy", Congressional Research Service, June 18, 2012.

<sup>18</sup> See Langhorst, Christina: "Die bilateralen Handelsabkommen der Europäischen Union" (the bilateral trade agreements of the European Union), Konrad-Adenauer Foundation, KAS-Neuerscheinungen, issue 45, October 2007.

<sup>19</sup> See Bhagwati, Jagdish: "The Wind of the Hundred Days: How Washington Mismanaged Globalization.", The MIT Press, Cambridge, MA., 2000. p.240-245; Krueger, Anne O.: "Free Trade Agreements As Protectionist Devices: Rules of Origin", in James R. Melvin, James C. Moore and Raymond Riezman (eds.), *Trade, Theory and Econometrics: Essays in Honor of John C. Chipman*. Routledge Press. New York, 1999, pp.91-101.

<sup>20</sup> See Langhorst, 2007, p.5.

WTO regulations. The general Doha Round ground to a halt. It is argued that it has virtually no chances of success with far more than 300 bilateral trade agreements in place.

### Multilateral trade liberalization grinds to a halt

The economic crisis of 2008/09, in particular, has brought moves to liberalize trading at multilateral level to a standstill. The World Trade Organization (WTO) drafts its agreements in negotiation rounds based on the “single undertaking” principle, namely a consensus on all of the issues being negotiated. The aim of the Doha Round, which has been ongoing since 2001, is to open up the markets further and include less developed countries more in the global trade system. With negotiations in deadlock and only very sluggish progress being made, the idea of making progress outside of the multilateral framework has become a more attractive prospect. Since the WTO was set up in 1995, the number of regional and bilateral free trade agreements has been rising steadily. At the start of the year, there were 546 regional free trade agreements, 354 of which are in force (start of 2012: 511 regional free trade agreements, 319 in force).<sup>21</sup>

Another concern given the large number of free trade agreements is that their extensive regulation will increase the transaction costs that apply in international goods trading even more.

But in spite of all of the concerns, it is important not to underestimate the advantages of free trade agreements. Trade creation and diversion are only the direct effects, often referred to as static effects, of free trade agreements. It is important to distinguish these from the long-term dynamic effects:<sup>22</sup>

- More efficient production, because the abolition of customs barriers fuels competition among producers.
- Economies of scale for production, because a larger market for many products allows production volumes to be upped.
- More foreign investment by companies from countries that are not party to the agreement, because these companies also want to benefit from the favorable trade agreements.

All in all, the creation of a free-trade area can certainly be seen as a sort of structural reform that fosters innovation and productivity. What is more, free-trade agreements are no longer just about doing away with customs duties. Particularly for companies with international operations, adherence to different product standards from country to country is a significant cost factor. A substantial portion of global goods exchange now takes place on an intra-group basis.<sup>23</sup> As a result, harmonizing product standards is now an important factor in free trade agreements.

<sup>21</sup> See [http://www.wto.org/english/tratop\\_e/region\\_e/region\\_e.htm](http://www.wto.org/english/tratop_e/region_e/region_e.htm). The high number is also due to the fact that agreements governing goods and services are counted separately. See Andreas Freytag: “Ist die multilaterale Handelsordnung überholt?” (is the multilateral trade structure an outdated concept), in: Ludwig-Erhard-Stiftung, Orientierungen zur Wirtschafts- und Gesellschaftspolitik, no. 134, December 2012, p. 42.

<sup>22</sup> See Cooper 2012, pp.10/11.

<sup>23</sup> See Szigetvari, Andras: “EU erwartet Schub durch Freihandelsabkommen” (EU expects boost from free-trade agreements), Der Standard, February 13, 2013.

As far as the planned transatlantic free trade agreement is concerned, there is another aspect: any trade-diverting effects are likely to be fairly minimal, because the customs duties between the US and the EU are already relatively low. Abolishing non-tariff trade barriers, i.e. varying standards and rules and regulations on the markets, insofar as possible will be far more crucial in determining the success of a transatlantic agreement.

A transatlantic free trade agreement will probably not mean that the Doha Round is over for good either. Rather, it is more likely that the size of the resulting free trade area will have something of a ripple effect. Other countries will adjust to reflect the rules imposed by this free trade area and will prove more active, and willing to compromise, when it comes to putting global free trade regulations in place than they have been in the past. So the Doha Round could certainly be revived as a result of these very regulations.

## 5. Possible impact of the planned agreement on growth

The estimated impact on EU growth ranges from 0.01% to 0.5% depending on the model used, the underlying assumptions and the time horizon applied.

An “extensive and ambitious” agreement in the form of reduced non-tariff trade restrictions between the two economic areas could translate into GDP growth of 0.5% for the EU and 0.4% for the US by 2027. This would correspond to additional income totaling EUR 86bn for the EU economy and EUR 65bn for the US economy. This is the conclusion reached by the high-level EU-US working group on the basis of an estimate commissioned by the Directorate General for Trade.<sup>24</sup>

The Commission's analysis focuses not only on demand-based effects resulting from increased extra-EU exports, but also supply-side effects in the form of longer-term productivity gains due to trade integration.<sup>25</sup> Increased foreign investment, also from companies from non-member states, are not mentioned explicitly. The exports of EU member states to the US would receive a boost to the tune of 1.4% (EUR 29.4bn) according to the calculations. A model simulation performed on behalf of the Dutch Ministry of Finance in 2009 covering the period leading up to 2020 produces the same result in the short term. In the long term, taking more efficient capital allocation into account, it expects to see additional export growth of 1.6% for the 26 EU member states (excluding the Netherlands). The US would receive much more of a boost (+5.6% and 5.7% respectively),<sup>26</sup> which could help balance out the current negative US balance of trade with the EU. Furthermore, empirical analysis for EU member states show that opening up an economy (measured as the ratio of imports to output) by 1% results in an average increase in labor productivity to the tune of 0.6%.<sup>27</sup>

Trade-induced productivity increases also play a key role in a study published in 2010 by the European Centre for International Political Economy (ECIPE), which, unlike the Commission's survey, looks into the complete abolition of tariff trade barriers. While, according to the ECIPE, the static GDP impact of the complete abolition of customs would only be 0.01% for the EU and 0.15% for the US, the economic output of the EU is likely to be

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<sup>24</sup> See European Commission: “European Union and United States to launch negotiations for a Transatlantic Trade and partnership”, Memo, Brussels, February 13, 2013, [http://europa.eu/rapid/press-release\\_MEMO-13-95\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-95_en.htm).

<sup>25</sup> See European Commission: “External Sources of Growth”, Commission Staff Working Document, 2012, [http://trade.ec.europa.eu/doclib/docs/2012/july/tradoc\\_149807.pdf](http://trade.ec.europa.eu/doclib/docs/2012/july/tradoc_149807.pdf), p. 19.

<sup>26</sup> See Berden, Dr. Koen et al.: “The impact of Free Trade Agreements in the OECD”, ECORYS Macro & Sector Policies, Client: Ministry of Economic Affairs, the Netherlands, 2009, pp. 58 et seq. Estimations based on a Computable General Equilibrium (CGE) Multi-region Trade Model.

<sup>27</sup> See European Commission: “Raising productivity growth: key messages from the European Competitiveness Report”, October 31, 2007.

0.32-0.47% higher, and the economic output of the United States 0.99-1.33% higher, in 2015 due to dynamic effects – in the form of labor productivity increases of 2-3.5% (cumulative) in the period from 2010 and 2015 and a 3% (cumulative) reduction in transaction costs.<sup>28</sup> So as argued above, the greatest growth impetus is likely to come from long-term dynamic effects.

30 million employees in the EU work in export-oriented sectors. The ratio of employment that is reliant on exports to employment as a whole varies within the EU, depending on the economic structure, from less than 4% in Portugal and Greece to more than 10% in Malta, Ireland, Finland und Luxembourg. Sousa et al. (2012) estimate that EUR 1bn in extra exports would translate, on average, into 15,000 extra jobs in the EU.<sup>29</sup> This means that the bilateral transatlantic agreement, which accounts for an additional export volume of EUR 29.4bn, could create 441,000 new jobs within the EU. At the same time, the structural changes triggered by the agreement can be expected to result in job losses in less competitive sectors.

All in all, the estimates regarding the growth effects of a transatlantic pact appear to be cautious based on the given assumptions, particularly in the long term. It is, however, difficult to use quantitative methods to fully cover all effects of a change in an overall structural framework, such as the abolition of non-tariff trading barriers. This means that the long-term productivity and innovation impetus of greater competition is likely to be underestimated.

## 6. Final evaluation

The US and the EU have set themselves an ambitious target with an extensive trade and investment agreement. There is no doubt that this sort of agreement has to go further than merely taking the "conventional" route of abolishing customs duties. We believe that, as well as abolishing the remaining customs duties, the agreement should focus on the following:

- Making rules of origin as unrestrictive and straightforward as possible.
- Breaking down market entry barriers in the service sectors.
- Getting ride of the trade barriers lurking "behind" the customs borders, i.e. in particular the mutual recognition and, where possible, harmonization of technical product standards and regulatory convergence with a fixed timeframe.
- Opening up procurement at all state levels.
- Not excluding tricky sectors, probably including the agricultural and financial services sectors, from the negotiations.

The negotiating partners are aiming to have the agreement signed and sealed within a two-year period. We believe that this is extremely ambitious given the complexity of the matter. First of all, the regulatory differences that have separated the EU and the US over the past few years are likely to become more pronounced, if anything. Second, even within the US, regulations vary from federal state to federal state, with the differences in

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<sup>28</sup> See Bauer, Matthias und Frederik Erixon: "A Transatlantic Zero Agreement: Estimating the Gains from Transatlantic Free Trade in Goods", ECIPE Occasional Paper, No. 4/2010, [http://www.ecipe.org/media/publication\\_pdfs/a-transatlantic-zero-agreement-estimating-the-gains-from-transatlantic-free-trade-in-goods.pdf](http://www.ecipe.org/media/publication_pdfs/a-transatlantic-zero-agreement-estimating-the-gains-from-transatlantic-free-trade-in-goods.pdf). The multi-region CGE Model also serves as a model.

<sup>29</sup> Sousa, N. et al: "Extra-EU exports and employment", DG TRADE Chief Economist Note, No 2, 2012.

regulations bound to be even more pronounced from EU country to EU country. A whole series of step-by-step plans is likely to be necessary to integrate the two trade areas.

Willingness to compromise is an absolute must on both sides if the negotiations are to reach a successful conclusion. Given the political pressure for action as a result of the weak growth in the two economic areas, however, both parties are likely to remain keen to compromise. The scope for stimulating growth using monetary policy and fiscal policy has now been exhausted in full. Trade policy that promotes growth offers a way out of this political dilemma.

The mutual recognition of safety standards is a pragmatic way of avoiding the double cost of laborious product tests at companies with international operations in the future. Both the EU and the US, however, will have to give up on at least some of the positions they have clung to in the past. In the agricultural sector, for example, the EU will have to become more open, while the US will be unable to cling forever to the argument that agreements on issues relating to financial market supervision and regulation are not possible due to the autonomous nature of its supervisory authorities.

Particularly in the financial sector, we believe that there is a genuine need to make real progress in terms of consistent regulation. Attempts at G20 level to create a more uniform framework on the financial markets have not proved a success so far. The US and the EU have not even managed to put uniform rules and regulations in place in the field of accounting. What is more, the EU is still a place where individual countries or groups of countries have opted to “go it alone” in the field of financial market regulation, as the example of the tax on financial transactions shows. We will only achieve greater financial market stability if the big economic regions start to toe the same line.

These assessments are, as always, subject to the disclaimer provided below.

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Together with its customers and sales partners, Allianz is one of the strongest financial communities. Around 78 million private and corporate customers rely on Allianz's knowledge, global reach, capital strength and solidity to help them make the most of financial opportunities and to avoid and safeguard themselves against risks.

In 2012, around 144,000 employees in over 70 countries achieved total revenue of 106.4 billion euros and an operating profit of 9.5 billion euros. Benefits for our customers reached 89.2 billion euros.

This business success with insurance, asset management and assistance services is based increasingly on customer demand for crisis-proof financial solutions for an aging society and the challenges of climate change. Transparency and integrity are key components of sustainable corporate governance at Allianz SE.

## **CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.

Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events) (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the Euro/U.S. Dollar exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

## **NO DUTY TO UPDATE**

The company assumes no obligation to update any information or forward-looking statement contained herein, save for any information required to be disclosed by law.