

## CRT Insights

### How do FTAs augment job-creating effects of trade? The answer is through Rules of Origin

-Ram Upendra Das

FTAs are important ways in which trade, especially exports can be made to generate higher levels of jobs. The issue assumes special significance due to a variety of reasons. First, due to concerns over jobless growth, the potential of trade contributing to job-creation is also underestimated. Secondly, it is not just underestimation of role of trade for employment-generation but also tremendous apprehension that trade is in fact employment-generating. Thirdly, recent times have witnessed a new narrative that trade is essentially employment-reducing – as manifested in an anti-trade sentiment in several important regions of the world. Finally, overall unemployment has remained a major developmental concern in both the developed and the developing worlds, alike.

This is the context in which trade-employment linkages assume greater importance. One of the primary lacunae in the above-outlined context is that trade is not viewed separately in terms of exports and imports. Both exports and imports can be employment-generating. Imports, however, could be employment-reducing as well if they displace domestic production in equal measure, which only highlights that the net effects of exports and imports of a country in terms of employment-generation needs to be calculated. On the other hand, it is worth-mentioning that imports create employment in the partner country. Employment generation is a need of the hour in every country and employment generation in the partner country can augur well for the exports of another country as they raise the purchasing power (demand levels) in the partner country.

FTAs can possibly provide an answer to augmenting the net effects of exports and imports, i.e. trade. This is possible if Rules of Origin provisions are formulated and implemented properly under any FTAs; rather than treating them as non-tariff barriers.

Rules of origin (ROO) are a set of instruments to determine the country in which the product is originated in the international trade flows. Within any FTA, origin-rules exist in order to prevent third countries (non-FTA partners) from taking advantage of the FTA concessions. Thus, one of the primary functions of rules of origin is to prevent trade deflection in FTAs when the different modalities of determining the origin of a product aim at substantial transformation in inputs.

However, what remains unappreciated is that these rules of origin and their modalities together facilitate and ensure value-addition in the country of manufacturing and play a developmental role through employment- generation effects when substantial transformation of inputs results in a distinct new output. This is brought about because value addition or substantial transformation in a manufacturing process allows firms to pay wages and salaries to labour, interest to capital, rent to land and profits to entrepreneurs. This means higher the value addition in manufacturing higher would be the potential to employ all factors of production and not just labour. Higher value addition is the avenue to reap higher profits to entrepreneurs. In short, rules of origin under FTAs can play a developmental role by having manufacturing-augmenting and employment-generating effects.

What is more, through regional cumulation and other innovative provisions, ROO can help create and strengthen Regional Value Chains (RVCs) as well!

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