

# EU Open Strategic Autonomy in a Post-Covid World: An Italian Perspective on the Sustainability of Global Value Chains

by Fabrizio Botti, Cristina Castelli and Giulio Giangaspero



## ABSTRACT

The new EU trade strategy focusing on supply chains resilience and sustainability as a pillar of the European path towards open strategic autonomy raises concerns, especially with regard to the potential risks of encouraging protectionism and undermining international interdependence. According to recent evidence concerning Italy's role in international production networks, the restructuring of GVCs through reshoring processes does not seem to be neither efficient nor a priority for companies. Drawing on recent findings concerning the debate on economic interdependence and the resilience of global value chains, alternative trade policy options are recommended as possible applications of the EU open strategic autonomy in the pursuit of sustainable GVCs.

*Italy | European Union | Foreign trade | WTO*

**keywords**

## EU Open Strategic Autonomy in a Post-Covid World: An Italian Perspective on the Sustainability of Global Value Chains

by Fabrizio Botti, Cristina Castelli and Giulio Giangaspero\*

### Introduction

European strategic autonomy is an increasingly significant and controversial guiding concept for the European Union external and internal action. The term originated in the defence and security domains and gradually spread to other policy fields, including EU trade policy. It refers to the EU's ability to chart its own course in line with its interests and values at a time of new global challenges such as the twin transitions of climate change and digital transformation, together with geopolitical tensions threatening rule-based multilateral regimes.

In February 2021, through the issue of the 2021 Trade Policy Review, the European Commission launched a new trade strategy that explicitly supports the EU's open strategic autonomy according to three main directions: openness to trade and investment for economic recovery; responsibility for a greener and fairer world with the aim to strengthen value chains' sustainability and resilience; and assertiveness against unfair practices undermining the effectiveness of multilateral institutions.<sup>1</sup> In particular, the Commission aims to integrate EU trade policy into

<sup>1</sup> European Commission, *Trade Policy Review - An Open, Sustainable and Assertive Trade Policy* (COM/2021/66), 18 February 2021, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52021DC0066>.

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the new sustainable growth model defined by the Green Deal and the European Digital Strategy.

The resilience and sustainability of supply chains are deemed to be a pillar of the European path towards open strategic autonomy. Nonetheless, the new EU strategic framework raises concerns, especially with regard to the potential risks of encouraging protectionism and undermining international interdependence.<sup>2</sup> In view of supply shortages of medical products during the covid-19 pandemic and geopolitical tensions between China and the United States, the reconfiguration of global value chains (GVCs)<sup>3</sup> has been increasingly debated as an economic policy tool to secure the supply of critical products and establish strategic autonomy. Yet some of the key factors identified by the European Commission to ensure resilience (i.e. production and supply chain diversification, strategic stockpiling and dependency identification) are ambiguous and point to a trade-off between dependence on foreign supply and unilateralism.

The reconfiguration of GVCs through the “reshoring” of productive activities<sup>4</sup> is a highly controversial policy option available to Europeans to achieve economic resilience. For most governments, industrial policy is seen as a crucial instrument to enhance the domestic production capacity of critical/strategic goods, in order to be better prepared for future crises, as it is showed by increasing competition in the attraction of foreign investments. An in-depth comparative analysis of Italy’s role in international production networks shows the geography of GVCs in different sectors and allow to assess the relevance of a restrictive implementation of the strategic autonomy model to trade and investment policy, i.e. the restructuring of GVCs through reshoring processes.

Drawing on recent findings concerning the debate on economic interdependence and the resilience of global value chains, alternative trade policy options are explored as possible applications of the EU open strategic autonomy in the pursuit of resilient and sustainable GVCs.

<sup>2</sup> Nathalie Tocci, *European Strategic Autonomy: What It Is, Why We Need It, How to Achieve It*, Rome, Istituto Affari Internazionali, February 2021, <https://www.iai.it/en/node/12819>.

<sup>3</sup> GVC refers to production segmentation into activities and tasks carried out by multiple firms and workers in different countries. At each step in the production process (supply chain) across geographic spaces and firms (from the design to support services to the final consumer) value is added to the end product. Several distinctive traits of the contemporary globalisation process (liberalisation of trade and investment, lower transport costs, advances in ICT, and innovations in logistics) encourage companies to restructure their operations internationally through outsourcing and offshoring of activities.

<sup>4</sup> Reshoring (also termed backshoring, backsourcing) is “a voluntary corporate strategy regarding the home country’s partial or total relocation of (insourced or outsourced) production to serve the local, regional or global demands, making the phenomenon a strategic option for manufacturing firms in regards their international relocation activities”. See Eurofound, *Reshoring in Europe: Overview 2015–2018*, Luxembourg, Publications Office of the European Union, 2019, p. 8, <https://op.europa.eu/s/prah>.

## 1. Is the reconfiguration of GVCs a relevant application of European strategic autonomy? The case of Italy

The establishment of complex international production networks has experienced profound transformations since the mid-1990s, with increasing fragmentation of the production processes across different locations and actors. The expansion of global production via GVCs peaked before the 2008-2009 global financial crisis, with trade and cross-border investment flows starting to enter into a slow-growth rate trend relative to GDP, and production networks experiencing a gradual regionalisation. The increasing vulnerability of GVCs to global shocks such as the covid-19 pandemic, digital transformation, the weakening of rule-based international regimes and growing geopolitical tensions are likely to reinforce incentives to reconfigure GVCs and possibly encourage companies to make reshoring decisions.

Promoting the resilience and sustainability of supply chains is one of the pillars of the EU's plan to achieve open strategic autonomy. Despite the Commission's traditional emphasis on the rule-based trading system and on developing a cooperative system to facilitate access to critical supplies, European policy discussions have addressed the role of other potentially more assertive elements. The security of supply-related measures such as subsidies or tax incentives to companies for the local production of essential products and an investment screening mechanism might affect companies' decisions to relocate offshored production and, more generally, the reconfiguration of GVCs.<sup>5</sup>

How relevant are the processes of GVCs' shortening and restructuring in the pursuit of strategic autonomy? Given the current degree of specialisation and involvement in the international production network, what is the potential (if any) for reshoring? Empirical evidence on the case of Italy's role in international production networks compared to major international trade actors, and the resilience of corresponding supply chains are presented in sections 1.1 and 1.2.

### 1.1 Italy's participation to GVCs

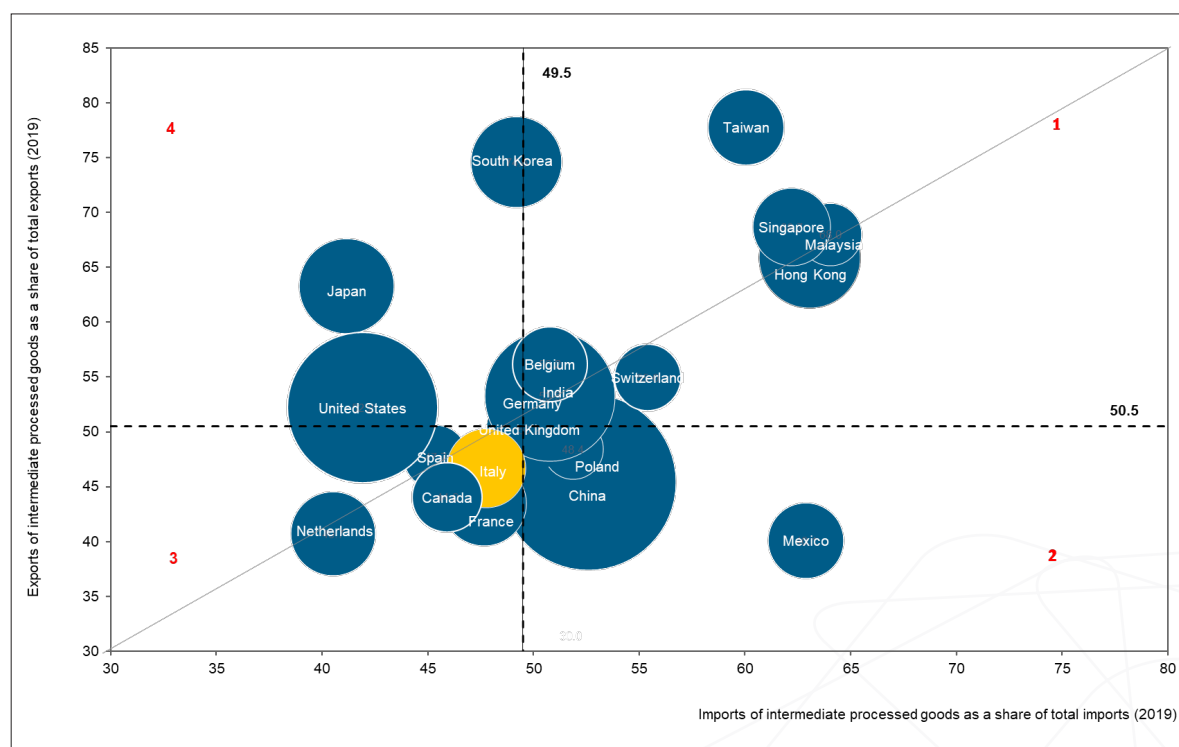
To describe Italy's involvement in international production networks, trade data on intermediate "processed" goods (parts and components without raw materials, as defined by UNCTAD<sup>6</sup>) can be used to show Italy's position among the twenty main

<sup>5</sup> The call for member states to set up and enforce a FDI screening mechanism under the FDI Screening Regulation in the security field, in European Commission, *Trade Policy Review*, cit.; the protection of Europe's strategic assets invoked in the Communication of 25 March 2020: European Commission, *Guidance to the Member States Concerning Foreign Direct Investment and Free Movement of Capital from Third Countries, and the Protection of Europe's Strategic Assets...* (C/2020/1981), 25 March 2020, [https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020XC0326\(03\)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020XC0326(03)).

<sup>6</sup> United Nations Conference on Trade and Development (UNCTAD), *Key Statistics and Trends in International Trade 2020. Trade Trends under the COVID-19 Pandemic*, Geneva, United Nations, January 2021, <https://unctad.org/webflyer/key-statistics-and-trends-international-trade-2020>;

trading countries and its relative specialisation in “upstream” or “downstream” production phases (over and under the bisector line, respectively; see Figure 1). We observe that Italy, like France and Spain, has a relatively lower participation rate in GVCs than Germany or Switzerland and several emerging Asian countries. As the share of processed intermediates in imports is larger than the share in exports, Italy appears to be slightly more specialised in downstream phases (assembling of final goods), holding a position similar to that of France. However, it has to be noted that there are wide differences across sectors and that in some cases – like other countries – Italy’s relative position has evolved since 2010.<sup>7</sup>

**Figure 1** | Trade in processed intermediate goods as a share of total trade in goods, by country



Note: The size of the bubble measures each country’s share of all reporting countries’ trade in intermediate processed goods in 2019, on total trade (imports+exports). The dotted lines refer to the total of reporting countries. Total trade excludes products not classified by the Broad Economic Category classification (BEC, Rev.4).

Source: Italian Trade Agency, *Italian Firms in International Production Networks. Executive Summary*, cit., p. 8.

previous reports, based on Broad Economic Classification (BEC).

<sup>7</sup> For example, in transportation means and electric machinery and appliances, Italy experienced a change in its relative specialisation between 2007 and 2019: in the former sector, Italy appeared to be slightly specialised in upward phases in 2007 and became more specialised downward in 2019; the opposite occurred in the latter sector; for further details see Italian Trade Agency, *Italian Firms in International Production Networks. Executive Summary*, Updated version, October 2020, <https://www.ice.it/it/sites/default/files/inline-files/EXEC%20SUMM%20agg%20ottobre%202020.pdf>.

Furthermore, indicators on trade in value added (VA) provide useful insights on the geographic origin of VA in exported goods.<sup>8</sup> For the main manufacturing sectors, Table 1 shows the share of foreign VA embodied in Italy's gross exports, deriving from imports of intermediate goods (so called *backward linkages*). Overall, foreign VA amounts to 28.2 per cent, while domestic VA reaches 71.8 per cent, with some differences across sectors. For example, food, beverages and tobacco, as well as textiles, apparel, leather and related products feature a relatively higher content of domestic VA (79.7 and 78.6 per cent, respectively); conversely, transport equipment shows the highest integration in GVCs (foreign VA is 33.5 per cent), followed by computer, electronic and electrical equipment (31 per cent).

**Table 1** | Origin of value added in Italian manufacturing gross exports, by geographic area and sector (percentage share)

	Textiles, apparel, leather and related products	Transport equipment	Chemicals and pharmaceutical products	Machinery and equipment	Computers, electronic and electrical equipment	Food products, beverages and tobacco	Manufacturing sector
<b>Domestic value added</b>	<b>78.6</b>	<b>66.5</b>	<b>69.7</b>	<b>72.1</b>	<b>69.0</b>	<b>79.7</b>	<b>71.8</b>
<b>Foreign value added, of which:</b>	<b>21.4</b>	<b>33.5</b>	<b>30.3</b>	<b>27.9</b>	<b>31.0</b>	<b>20.3</b>	<b>28.2</b>
EU (26)	8.2	18.0	12.7	13.3	14.5	9.9	12.4
Other European countries (*)	3.0	4.7	6.4	3.9	4.1	2.6	4.6
North America	1.2	2.5	2.3	2.1	2.3	1.5	2.0
East and South East Asia	4.8	4.7	2.3	4.4	5.9	1.9	3.7
South and Central America	0.5	0.5	0.4	0.7	0.8	0.8	0.7
Other countries	3.8	3.2	6.1	3.6	3.6	3.6	4.8
<b>Total value added</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
Value added from the region (Italy, EU26, other European countries)	89.8	89.1	88.8	89.3	87.6	92.2	88.8
EU26 share on foreign VA	38.1	53.7	41.9	47.8	46.7	48.5	44.0
EU26 and other European countries share on foreign VA	52.3	67.6	63.1	61.6	59.9	61.5	60.4

Note: (\*) Iceland, Norway, United Kingdom, Russian Federation, Switzerland, Turkey.

Source: Authors' calculations on OECD TiVA database, 2018, <http://oe.cd/tiva>.

<sup>8</sup> See OECD TiVA database, <http://oe.cd/tiva>.

In line with the economic literature,<sup>9</sup> Table 1 confirms that international production networks generally have a regional character and highlights Italy's integration with the EU and other countries of the European area. In regard to manufacturing exports, VA originates to a large extent from Italy, the EU (26) and some other European countries (88.8 per cent),<sup>10</sup> all of them (except Russia) linked to the EU by preferential trade agreements. The share is slightly lower in the computer, electronic and electrical sector (87.6 per cent), where Asian suppliers are more significantly involved.

Moreover, if we consider only EU members, we notice that the share of foreign VA is particularly high in transport equipment (53.7 per cent), in the food and beverage sector (48.5 per cent) and for machinery (47.8 per cent), while lower in the textile, apparel and leather products sector (38.1 per cent).

Trends highlighted by trade of processed intermediates and VA indicators appear to be substantially in line with the results of a multiple case study carried out by the Italian Trade Agency, involving interviews with representatives from 48 companies based in Italy (twenty lead firms in the electrical appliances and transport equipment sectors, and 28 suppliers).<sup>11</sup> Although not statistically representative, in-depth interviews can provide useful insights to complement statistical evidence: for example, the study confirms the relevance of procurement, as lead firms producing final goods coordinate complex networks of suppliers (which often rely on other suppliers too) and define themselves as "big assemblers" of parts and components. In both electrical appliances and transport equipment, inputs sourced externally represent approximately 50 per cent of turnover, around one third of which originates from other countries, and mainly from independent suppliers.

As to the geography of their production networks, lead companies confirmed that parts and components are sourced mainly in the European region. In the case of electrical appliances, Italy, the EU and other European countries account for 83.6 per cent, and 78 per cent in the case of transport equipment. Nonetheless, in these sectors quality and technology are important drivers for procurement, so that in several cases the geographic distance of a supplier does not represent a barrier. It is also worth noting that large companies (representing the majority of the lead firms interviewed) seem to be better organised for scouting and sourcing components from distant places, often having foreign affiliates to support them.

<sup>9</sup> Bart Los, Marcel P. Timmer and Gaaitzan L. de Vries, "How Global Are Global Value Chains? A New Approach to Measure International Fragmentation", in *Journal of Regional Science*, Vol. 55, No. 1 (January 2015), p. 66-92; Koen De Backer et al., "Reshoring: Myth or Reality?", in *OECD Science, Technology and Industry Policy Papers*, No. 27 (January 2016), <https://doi.org/10.1787/5jm56frbm38s-en>.

<sup>10</sup> Based on the availability in the TiVA database, we include Iceland, Norway, United Kingdom, Russian Federation, Switzerland and Turkey.

<sup>11</sup> Italian Trade Agency, *Le imprese italiane nelle reti produttive internazionali*, July 2018, <https://www.ice.it/it/node/5503>.

Moreover, the study highlights the importance of inter-firm coordination between lead firms and suppliers: in fact, in both sectors, the majority of sourced inputs are customised parts and components, where co-projecting and long-term relationships, based on trust, play a relevant role (in the case of electrical appliances, around 60 per cent of the inputs provided by suppliers are customised, and 74 per cent in the case of transport equipment). As GVC literature indicates,<sup>12</sup> forms of “explicit coordination” take place in international production networks between lead firms and independent suppliers. Therefore, the implicit cost of changing suppliers can be high, leading to a “stickiness” that helps to explain GVCs’ resilience during the covid-19 pandemic, the quick rebound of trade by the end of 2020 and the fact that, so far, a widespread reconfiguration of supply chains has not taken place.

### 1.2 Economic interdependence and GVCs resilience

The global reach of the covid-19 crisis has laid bare the degree of interconnectedness of the global economy and especially the role of international production networks. Accordingly, the debate on economic interdependence and the resilience of GVCs has gained momentum. In fact, supply chain disruptions occur from time to time, and can derive from very different causes. Some prominent examples are the earthquake in Japan (the one that provoked the Fukushima nuclear incident) and the floods in Thailand in 2011,<sup>13</sup> as well as the recent accident at the Suez Channel, where a huge container ship ran aground next to the canal, blocking trade traffic for days. Many scholars and observers who research the issue of fragmented production are asking whether involvement in international production networks contributes to mitigate increasing risks and growing uncertainty, which strategies should be adopted by firms to solve the trade-off between efficiency and stability and whether to pursue a reconfiguration of GVCs or focus on risk diversification, as well as what are the options for trade policy.<sup>14</sup>

Recent analysis and surveys of Italian firms provide evidence concerning the much-debated question about the resilience of international production networks. A first survey, carried out by the Bank of Italy in October 2020, shows that most

<sup>12</sup> See Timothy J. Sturgeon, *Global Value Chains and Economic Globalization. Towards a New Measurement Framework*, Report to Eurostat, May 2013, <https://ec.europa.eu/eurostat/documents/7828051/8076042/Sturgeon-report-Eurostat.pdf>.

<sup>13</sup> Masahiko Haraguchi and Upmanu Lall, “Flood Risks and Impacts: A Case Study of Thailand’s Floods in 2011 and Research Questions for Supply Chain Decision Making”, in *International Journal of Disaster Risk Reduction*, Vol. 14, Part 3 (December 2015), p. 256-272.

<sup>14</sup> See among others: Pol Antràs, “De-Globalisation? Global Value Chains in the Post-Covid-19 Age”, in *NBER Working Papers*, No. 28115 (November 2020), <https://www.nber.org/papers/w28115>; Alvaro Espitia et al., “Pandemic Trade. Covid-19, Remote Work and Global Value Chains”, in *World Bank Policy Research Working Papers*, No. 9508 (January 2021), <http://hdl.handle.net/10986/35023>; United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2020. International Production Beyond the Pandemic*, Geneva, United Nations, 2020, <https://unctad.org/webflyer/world-investment-report-2020>.



firms are not considering a reconfiguration of GVCs, that they did not radically change their choices about the location of their plants or of their foreign suppliers and, most importantly, that they are unlikely to change their strategy in future, despite substantial losses in turnover.<sup>15</sup> The survey also shows that Italian internationalised companies have dealt with the crisis better than those operating only in the internal market. This “sheltering” function of GVC participation is also highlighted in other research, based on the latest World Bank covid-19 surveys on Italy (carried out in June and in December 2020). As in the previous surveys, micro-level evidence shows that internationalisation has mitigated the contraction of firms’ sales, especially during the second wave of the pandemic.<sup>16</sup>

Moreover, in January 2021 the Italian National Statistics Institute (Istat) collected some relevant findings on firms’ procurement strategies, confirming the results of the previous research as firms declared that they had not changed their suppliers, and highlighting differences between small and medium-large firms. Larger companies showed an increased number of foreign suppliers, especially from the EU and China (which could be a sign of risk diversification), whereas smaller firms declared a decrease in foreign procurement and a shift towards domestic suppliers.<sup>17</sup> As is well known, firms bear high fixed costs related to foreign direct investments (FDIs) as well as “substitution costs” to change suppliers (especially the main ones), which are relevant especially for complex products. These costs could explain why firms adopted a “wait and see” attitude as a response to the pandemic shock.

These findings are in line with firms’ strategies outlined in the case study carried out by the Italian Trade Agency, which includes several medium to large lead firms. The initial drivers of productive internationalisation could indeed determine their current strategies, as most firms reported during the interviews that their foreign affiliates operate mainly on the local market and as “export platforms” for the region. Market access, proximity to clients, lower logistical costs, lower trade barriers have been mentioned as the main determinants for decision concerning involvement in GVCs, while cost factors were less relevant. It is likely that lead firms pursuing a market access strategy would not disinvest from large and dynamic markets (e.g. from Asian countries) and that, instead of reconfiguring their international production networks, they would probably prefer diversification and risk management. Moreover, consumer demand for sustainable products is growing, and regional production close to markets is a way of reducing logistics

<sup>15</sup> Giorgia Giovannetti et al., “Il ruolo delle catene globali del valore nella pandemia: effetti sulle imprese italiane”, in *Rivista di politica economica*, No. 2/2020, p. 77-99, [https://www.confindustria.it/home/centro-studi/rivista-di-politica-economica/dettaglio?doc=RPE\\_traiettorie\\_europee\\_2020\\_2](https://www.confindustria.it/home/centro-studi/rivista-di-politica-economica/dettaglio?doc=RPE_traiettorie_europee_2020_2).

<sup>16</sup> Simona Giglioli et al., “The Resilience of Global Value Chains during the Covid-19 Pandemic: The Case of Italy”, in *Economia italiana*, No. 1/2021, p. 73-123, [https://economaiitaliana.org/wp-content/uploads/2021/06/EI\\_2021\\_1\\_04\\_S\\_Giglioli-et-al.pdf](https://economaiitaliana.org/wp-content/uploads/2021/06/EI_2021_1_04_S_Giglioli-et-al.pdf).

<sup>17</sup> Istat, *Rapporto sulla competitività dei settori produttivi. Edizione 2021*, April 2021, <https://www.istat.it/it/archivio/255558>.

costs and carbon footprints.<sup>18</sup>

According to a recent report published by McKinsey, the economic case for making large-scale changes in a company's physical location appears to be limited given the interconnected nature of GVCs, and firms may build up diversification and supply chain resilience in different ways.<sup>19</sup> These include strengthening risk management capabilities, building redundancy in supplier and transport networks, creating the capacity to flex production across sites and holding more inventory. Similarly, the Organisation for Economic Co-operation and Development (OECD) underscores the critical role of the private sector in managing supply chains risks, because such firms have experience in managing a wide range of risks and shocks along the supply chain, as well as the importance for governments to cooperate proactively with the private sector, in order to promote resilience.<sup>20</sup>

Lastly, from a macroeconomic point of view, a simulation carried out by the OECD in 2021 using the CGE Metro model offers interesting insights.<sup>21</sup> Results shows that a generalised relocation of production, aiming to reduce GVCs' involvement, is unlikely to result in increased certainty or stability of supply for at least two main reasons. First, as not all stages of production can be undertaken in the home country, trade in intermediate inputs and raw materials continues to play an important role in domestic production. Second, while reshored production may have fewer transmission channels, when a shock does occur firms in the domestic economy are vulnerable anyway due to a lack of external adjustment channels. The OECD shows that this can lead to increased instability, negatively affecting trade, prices and household incomes, and adding further GDP losses to the economic slowdown caused by the pandemic.<sup>22</sup> Overall, a shift to a "localised regime" is estimated to decrease welfare and global real GDP by more than 5 per cent on average, with significant reductions in economic activity across all regions and countries, and most pronounced in regions that currently rely largely on trade and GVCs.

<sup>18</sup> Koen De Backer et al., "Reshoring: Myth or Reality?", cit.

<sup>19</sup> Susan Lund et al., *Risk, Resilience, and Rebalancing in Global Value Chains*, McKinsey Global Institute, August 2020, <https://www.mckinsey.com/business-functions/operations/our-insights/risk-resilience-and-rebalancing-in-global-value-chains>.

<sup>20</sup> Organisation for Economic Cooperation and Development (OECD), "COVID-19 and Global Value Chains: Policy Options to Build More Resilient Production Networks", in *OECD Policy Responses to Coronavirus (COVID-19)*, 3 June 2020, <https://doi.org/10.1787/04934ef4-en>; OECD, *Fostering Economic Resilience in a World of Open and Integrated Markets. Risks, Vulnerabilities and Areas for Policy Action*, Report prepared for the 2021 UK Presidency of the G7, March 2021, <https://www.oecd.org/newsroom/OECD-G7-Report-Fostering-Economic-Resilience-in-a-World-of-Open-and-Integrated-Markets.pdf>; Sébastien Miroudot, "Resilience versus Robustness in Global Value Chains: Some Policy Implications", in Richard Baldwin and Simon Evenett (eds), *COVID-19 and Trade Policy: Why Turning Inward Won't Work*, London, CEPR Press, 2020, p. 117-130, <https://voxeu.org/node/65536>.

<sup>21</sup> OECD, *Shocks, Risks and Global Value Chains: Insights from the OECD METRO Model*, June 2020, <https://www.oecd.org/trade/documents/shocks-risks-gvc-insights-oecd-metro-model.pdf>.

<sup>22</sup> OECD, *Fostering Economic Resilience in a World of Open and Integrated Markets*, cit.

## 2. The role of trade policy in enhancing GVC resilience and sustainability in a strategic autonomy framework

The review of recent available evidence concerning Italy's role in international production networks and economic interdependence and resilience of related GVC documented Italy's significant integration in already regionalized production networks. Moreover, firms involved in corresponding GVCs appear to have dealt better with the crisis than domestic firms, making the reorganisation of international networks a less relevant and efficient policy option for European policymakers in search of open strategic autonomy. Explored evidence showed the need to keep markets open and facilitate cross-border investments. Therefore, there is wide scope for trade policy to support GVC resilience and sustainability, tackling border and "behind the border" issues, at all decision levels: national, bilateral, regional, plurilateral and multilateral. In particular, open plurilateral initiatives, although representing a second-best option, could achieve some progress among like-minded states, allowing for progress in several fields, while negotiations over the reform of the multilateral trading system continue within the World Trade Organisation (WTO).

In order to improve risk management, trade policy should help firms diversify their suppliers and build up redundancies. It is important to keep tariffs on intermediate goods at a low level and reduce non-tariff barriers, given that these measures are cumulative when production inputs are traded across borders (which can occur multiple times).

Since the mid-1990s, overall tariffs on imported intermediates have been well below duties applied on consumer goods. However, due to recent international tensions, since 2018 trade-restrictive measures (in the form of higher tariffs) have targeted especially intermediate goods.<sup>23</sup> This implies higher production costs for lead firms assembling final products, or additional expenses for searching new suppliers, and leads to a decrease in firms' competitiveness on both domestic and foreign markets.<sup>24</sup> Accordingly, within the EU, it is important to support actions to smoothen trade tensions with the United States and other countries, ensuring that higher duties do not affect trade, especially in intermediate goods.

In regard to non-tariff barriers, an important step for trade facilitation would be to move towards a harmonisation of the rules of origin (RoO).<sup>25</sup> So far, under the WTO

<sup>23</sup> Gene M. Grossmann and Elhanan Helpman, *When Tariffs Disrupt Global Supply Chains*, Princeton, Princeton University Department of Economics, Center for Economic Policy Studies, January 2021, <https://scholar.harvard.edu/helpman/node/661696>.

<sup>24</sup> Sébastien Miroudot, Dorothée Rouzet and Francesca Spinelli, "Trade Policy Implications of Global Value Chains. Case Studies", in *OECD Trade Policy Papers*, No. 161 (2013), <https://doi.org/10.1787/5k3tpt2t0zs1-en>; Cecilia Bellora and Lionel Fontagné, "Shooting Oneself in the Foot? Trade War and Global Value Chains", in *CEPII Working Papers*, No. 2019-18 (December 2019), <http://www.cepii.fr/CEPII/en/publications/wp/abstract.asp?NoDoc=12417>.

<sup>25</sup> Rules of origin represent the criteria needed to determine the national source of a product, due

agreement,<sup>26</sup> harmonisation of non-preferential RoO has not progressed farther than some progress in enhancing notification and transparency procedures. On the other hand, RoO adopted in preferential agreements are often complex, non-transparent and inconsistent,<sup>27</sup> which can represent – due to the huge number of existing trade agreements – a burden for firms involved in international trade.<sup>28</sup> Some progress was made at the 2015 WTO Ministerial Conference, but the improvements reached so far aim at facilitating market access for developing countries only.

The EU could take steps to enhance *harmonisation of both preferential and non-preferential rules*, in order to converge towards core principles. According to some observers, international cooperation to reduce trade-impeding effects could be more feasible than is often assumed, as over time some rules have been simplified and there is a partial convergence.<sup>29</sup> A plurilateral initiative could therefore represent an important step to lower transactions costs, facilitating supplier diversification and risk management, aiming to expand membership and, eventually, multilateralise the agreement.

Furthermore, in a world of fragmented production processes, diversification of suppliers can be increased by promoting the harmonisation of technical standards and the mutual recognition of conformity assessments so as to remove unnecessary regulatory divergence. Reducing technical barriers to trade in intermediate goods is a relevant issue for example in the automotive, aerospace and electronic sectors. Lead firms sourcing intermediates require specific standards, and suppliers from different countries may struggle with burdensome certification procedures in trading with new clients.

Besides improving transparency, as required by the WTO,<sup>30</sup> *regulatory cooperation* within international institutions (such as ISO, IEC or CEN, CENELEC at the

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to the fact that duties and restrictions in several cases depend upon the source of imports. Rules of origin can be non-preferential, applying in the absence of any preferential trade preference, or preferential, the latter being found usually in bilateral and regional trade agreements.

<sup>26</sup> Agreement on Rules of Origin, [https://www.wto.org/english/docs\\_e/legal\\_e/22-roo\\_e.htm](https://www.wto.org/english/docs_e/legal_e/22-roo_e.htm).

<sup>27</sup> Simon Lacey, "Multilateral Disciplines on Preferential Rules of Origin: How Far Are We from Squaring the Circle?", in *Global Trade and Customs Journal*, Vol. 7, No. 11/12 (November 2012), p. 473-492.

<sup>28</sup> It may be noted that, in response to the covid-19 pandemic, some countries have taken steps to temporarily ease rules of origin requirements to ensure that essential goods can enter the markets more rapidly.

<sup>29</sup> Bernard Hoekman and Stefano Inama, "Harmonization of Rules of Origin: An Agenda for Plurilateral Cooperation?", in *East Asian Economic Review*, Vol. 22, No. 1 (March 2018), p. 3-28, <https://dx.doi.org/10.11644/KIEP.EAER.2018.22.1.336>.

<sup>30</sup> Transparency is a cornerstone of the WTO Technical Barriers to Trade (TBT) Agreement. See WTO website: *Transparency Toolkit*, [https://www.wto.org/english/tratop\\_e/tbt\\_e/tbt\\_transparency\\_toolkit\\_e.htm](https://www.wto.org/english/tratop_e/tbt_e/tbt_transparency_toolkit_e.htm).

European level<sup>31</sup>) could be intensified, with a focus on sustainability standards.<sup>32</sup> The convergence of standards and certification requirements is usually performed through preferential trade agreements, or by means of specific treaties on the mutual recognition of conformity assessment: as for RoO, there is enough room for harmonisation and, furthermore, to promote sustainability standards also through plurilateral initiatives.<sup>33</sup>

*Facilitating international trade in services* is another relevant issue to improve GVC resilience as, according to the OECD, over 30 per cent of the value added contained in exported manufacturing goods is related to services.<sup>34</sup> Depending on the organisational strategies of lead firms, services (regarding business functions such as ICT, R&D, marketing, logistics, distribution) have to be sourced in other countries. Given that trade in services is mainly affected by “behind the border” barriers,<sup>35</sup> Italy among other European countries could assess and remove some regulatory obstacles and, if needed, enhance regulatory transparency.<sup>36</sup>

At the supranational level, the EU should promote the resumption of the Trade in Services Agreement negotiations (TiSA).<sup>37</sup> Meetings started at a plurilateral level in 2013 with a view to achieve further liberalisation in services’ trade and, ultimately, upgrade the 1995 GATS. However, the negotiations were halted in 2016. European countries could support a new round, with the aim of focusing on social and sustainability priorities, in line with the principles outlined in the EU Open Strategic Autonomy. Moreover, as trade in services is often regulated by

<sup>31</sup> The International Organization for Standardisation (ISO) is an independent, non-governmental international organisation with a membership of 165 national standards bodies. The International Electrotechnical Commission (IEC) is an international standards organisation that prepares and publishes international standards for all electrical, electronic and related technologies. The European Committee for Standardization (CEN), is an association that brings together the national standardisation bodies of 34 European countries. The European Committee for Electrotechnical Standardization (CENELEC) is responsible for standardisation in the electrotechnical engineering field.

<sup>32</sup> For details on sustainability standards see: Archana Negi, Jorge Antonio Pérez-Pineda and Johannes Blankenbach (eds), *Sustainability Standards and Global Governance*, Singapore, Springer, 2020, <https://link.springer.com/chapter/10.1007/978-981-15-3473-7>.

<sup>33</sup> Plurilateral cooperation can range from developing mutual processes to harmonise regulations in existing bilateral arrangements, to replacing some or all bilateral arrangements with a plurilateral treaty.

<sup>34</sup> OECD, *Fostering Economic Resilience in a World of Open and Integrated Markets*, cit.

<sup>35</sup> Joseph Francois and Bernard Hoekman (eds), *Behind-the-Border Policies. Assessing and Addressing Non-Tariff Measures*, Cambridge, Cambridge University Press, 2019.

<sup>36</sup> In fact, according to the OECD Services Trade Restrictiveness Index, Italy ranks 31st among OECD countries. For more details regarding the STRI indicator see the OECD.Stat website: <https://stats.oecd.org/Index.aspx?DataSetCode=STRI>.

<sup>37</sup> The Trade in Services Agreement (TiSA) was a proposed international trade treaty between 23 parties, including the European Union, United Kingdom and the United States, aiming at liberalising trade of services. Until November 2016, 21 rounds of negotiation took place and negotiations were said to have been at an advanced stage, although an agreement did not materialise. See European Parliament, *Legislative Train Schedule: Plurilateral Trade in Services Agreement (TiSA)*, as of 24 June 2021, [https://www.europarl.europa.eu/legislative-train/theme-a-balanced-and-progressive-trade-policy-to-harness-globalisation/file-trade-in-services-agreement-\(tisa\)](https://www.europarl.europa.eu/legislative-train/theme-a-balanced-and-progressive-trade-policy-to-harness-globalisation/file-trade-in-services-agreement-(tisa)).

preferential agreements, European values could be promoted during the current negotiations with third countries, taking sustainability goals into consideration as well.<sup>38</sup>

*Fostering digitalisation.* It is a widespread assumption that internet-based and digital technologies have a positive impact on firms' performance and internationalisation. This finding dramatically emerged during the pandemic, as digital technologies have in most cases allowed firms to continue parts of their production through the use of smart or remote working.<sup>39</sup> Furthermore, digital technologies facilitated the adjustment of transport and logistics services to extra-demands from e-commerce, in particular through platforms that keep B2B (business-to-business) and B2C (business-to-consumer) commercial transactions running smoothly.<sup>40</sup>

However, internet and e-business technologies have a positive impact on internationalisation only if and when they are embedded within process and organisational innovations and when investments in digital skills have been made both by firms and institutions.<sup>41</sup> Therefore, the EU Commission should promote investments in digital infrastructure, mainly the expansion of broadband in many areas of bloc and the transition to the cloud, as well as strengthening the adoption of cybersecurity measures and enhancing human capital in the public and private sectors.

The widespread and fast adoption of digital technologies also creates a number of challenges and risks to both public and private actors, exposing firms, households and governments to attacks on digital security and critical infrastructure. These risks, associated with the protection of privacy, intellectual property rights and data governance, may be better – and sometimes *only* – addressed through international cooperation, as well as the setting or the development of updated international technology and regulatory norms, regulations and standards. To this end, the EU should support the UN Secretary General's Roadmap on Digital Cooperation.

As far as trade policy is concerned, Italy and the EU should also back the adoption of a plurilateral treaty on e-commerce, which would also be helpful from the perspective of harmonising regulations within free trade agreements (FTAs), often containing WTO+ provisions. WTO negotiations on this issue started

<sup>38</sup> For an update see on EU trade agreements see the European Commission website: *Negotiations and Agreements*, <https://europa.eu/!kf38dv>.

<sup>39</sup> OECD, "Tracking and Tracing COVID: Protecting Privacy and Data while Using Apps and Biometrics", in *OECD Policy Responses to Coronavirus (COVID-19)*, 23 April 2020, <https://doi.org/10.1787/8f394636-en>.

<sup>40</sup> OECD, "The OECD Digital Government Policy Framework", in *OECD Public Governance Policy Papers*, No. 2 (October 2020), <https://doi.org/10.1787/f64fed2a-en>.

<sup>41</sup> See Ernesto Cassetta et al., "The Relationship Between Digital Technologies and Internationalisation. Evidence from Italian SMEs", in *Industry and Innovation*, Vol. 27, No. 4 (2020), p. 311-339.

in 2017 and, although the distance between countries' positions was wide, a consolidated text emerged in December 2020 and talks are progressing. Even if the final legal framework remains to be defined, this agreement has the potential to produce a reduction in trade barriers to e-commerce. Furthermore, as multilateral negotiations on digital trade will need to be complemented by bilateral and/or regional agreements to deliver significant improvements in market access, there will be several opportunities for the EU to choose strategic regional or single-state partners with whom to try to deepen e-trade liberalisation.<sup>42</sup>

*Preferential trade agreements* can play an important role in setting standards for protecting the environment and human rights, promoting European values and affirming the EU's assertiveness and strategic autonomy. Overall, only some trade agreements address current environmental standards and labour standards, although recent treaties increasingly encompass specific chapters, or refer to international treaties (e.g. to the International Labour Organisation Conventions).<sup>43</sup> For example, the EU has been including labour and environmental standards in its "new generation" free trade agreements since the FTA concluded with South Korea in 2011. However, according to some observers and scholars, there is room to improve the effectiveness of trade agreements regulations: sustainability and social standards could be tightened up, the administration of private complaints about infringements could be improved and the dispute settlement mechanism strengthened, as it is considered weaker than in other areas. Moreover, FTAs should include sanctions in cases of non-compliance.<sup>44</sup>

Therefore, during the current trade negotiations with third countries, the EU could support more stringent provisions on sustainability and labour rights.<sup>45</sup> In addition, it could promote the resumption of the plurilateral negotiations for an Environmental Goods and Services Agreement (EGSA, initiated by 46 WTO members in 2014, came to a halt at the end of 2016), in order to liberalise tariffs for a list of environment-related goods, as well as non-tariff barriers in related services.

<sup>42</sup> Gary Clyde Hufbauer and Zhiyao (Lucy) Lu, "Global E-Commerce Talks Stumble on Data Issues, Privacy, and More", in *PIIE Policy Briefs*, No. 19-14 (October 2019), <https://www.piie.com/node/14027>.

<sup>43</sup> For a comprehensive overview of the ILO resources and conventions on the labour dimension of FTAs, see the ILO website: *Free Trade Agreements and Labour Rights*, <https://www.ilo.org/global/standards/information-resources-and-publications/free-trade-agreements-and-labour-rights/lang--en>.

<sup>44</sup> Marco Bronckers and Giovanni Gruni, "Retooling the Sustainability Standards in EU Free Trade Agreements", in *Journal of International Economic Law*, Vol. 24, No. 1 (March 2021), p. 25-51, <https://doi.org/10.1093/jiel/jgab007>.

<sup>45</sup> This seems to be the position of the EU in the case of the EU–Mercosur FTA and of the EU–China investment treaty (CAI), both concluded "in principle" and not yet ratified; in the case of Mercosur there are concerns on environment protection in Brazil, while CAI is currently on hold due to the controversy on human rights and mutual sanctions.

## Conclusions

The European Commission recently launched a strategic framework for the EU trade policy in the coming five years in support of the open strategic autonomy model, with the promotion of supply chains resilience and sustainability at its core.

While the Commission's reaffirmed its traditional support to multilateral cooperation, trade policy support to EU's geopolitical goals may entail a more assertive approach against unfair trade practices. Correspondingly, European policy discussions have also addressed the issue of the reconfiguration of GVCs and the role of restrictive policy options such as the relocation of manufacturing and supporting process back to the company's country of origin. Furthermore, increasing vulnerability of GVCs to global shocks as showed by the covid-19 pandemic, digital transformation, the crisis of the liberal international order and growing geopolitical tensions will likely reinforce incentives for the reconfiguration of GVCs and possibly reshoring decisions by companies.

How relevant are the processes of GVCs' shortening and restructuring in the pursuit of a European strategic autonomy? Given the current degree of specialisation and participation in international production networks, what are the potential (if any) for reshoring? We have tried to answer this question by exploring recent empirical evidence on the role of Italy in international production networks and the resilience of corresponding supply chains and recommending some alternative trade policy options for the possible implementation of the EU open strategic autonomy model in the search of resilient and sustainable international production.

According to recent available evidence concerning Italy's role in international production networks and, the reorganisation of international production networks does not seem to be neither efficient nor a priority for companies. Moreover, a review of economic literature on economic interdependence and resilience of global value chains during the pandemic showed that companies participating in GVCs appear to have dealt better with the crisis vis-à-vis purely domestic firms. The more restrictive policy orientation towards the reorganisation of international networks such as reshoring seems therefore a less relevant and efficient option for European policymakers in search of open strategic autonomy.

This implies from a European policy-making point of view that it is necessary to promote markets openness and facilitate cross-border investments, as actually reaffirmed in the new EU Commission 2021 Trade Policy Review. Therefore, there is a large scope for the EU trade policy to support GVC resilience and sustainability, through the reduction of tariffs on intermediate goods and non-tariff barriers (i.e. rules of origin, technical standards, and conformity assessment). More specifically, in the framework of a recommended regulatory cooperation at supranational level on environmental sustainability standards, the EU should take the initiative to enhance harmonisation of both preferential and non-preferential rules. Plurilateral initiatives may help build consensus and progress on specific fields, while the





reform of multilateral trading system is debated.

Especially preferential trade agreements may allow to promote European values in the spirit of a renewed EU's assertiveness and strategic autonomy, by setting standards for protecting the environment and human rights.

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