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World Economy?

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## **IS REGIONALISM AN INCREASING FEATURE OF THE WORLD ECONOMY?\***

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**ABSTRACT:** Measuring the importance of regionalism in international trade is desirable but difficult. The number of regional trade agreements (RTAs) reported to the WTO or the proportion of world trade which is between countries in a RTA are frequently cited as evidence that regionalism is growing at an accelerating rate. This paper questions whether RTAs really are as important as the headline numbers suggest, or whether they just occupy an excessively large part of policymakers' and economic journalists' time. The main contributions are to analyse the number of RTAs and the share of world trade criteria in order to show why both are meaningless measures of the extent of regionalism in the current world economy. The impact of RTAs on world trade is difficult to assess because some of the most important RTAs go beyond trade to deep integration measures, while a large number of RTAs are either not implemented or have very limited coverage. The tendency towards extreme outcomes (ie. economic union or negligible economic effects) explains why, despite the apparent proliferation of RTAs, regionalism has not posed a serious challenge to the world economy as the multilateral trading system has over the last sixty years gone from strength to strength.

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## **Is Regionalism an Increasing Feature of the World Economy?**

“Regional Trade Agreements (RTAs) are a major and perhaps irreversible feature of the multilateral trading system” is the opening sentence of a Working Paper (Crawford and Fiorentino, 2005), which appears on the same WTO webpage as a dramatic graph showing the increasing number of RTAs reported since the early 1990s.<sup>1</sup> As of June 2005, 312 RTAs had been notified to the GATT/WTO, and 196 of these were in the decade after the establishment of the WTO in January 1995. Numbers like these are so frequently reported that it has become a stylized fact of the world trading system that regionalism is growing at an accelerating rate.<sup>2</sup> The aim of this paper is to question whether RTAs really are as important as the headline numbers suggest, or do they just occupy an excessively large part of policymakers’ and economic journalists’ time?

### **1. Historical Introduction**

The cornerstone of the General Agreement on Tariffs and Trade (GATT) and hence of the WTO is the nondiscrimination principle embodied in unconditional most-favoured nation treatment. Yet, since 1947 the principle has seemed under recurring threat, most especially in three waves of discriminatory trade policies.<sup>3</sup>

In the 1950s six western European countries began a process of economic integration that led to establishment of a customs union in the 1960s, which through contagion and imitation effects led to other RTAs. Seven other European countries formed the European Free Trade Association (EFTA) in 1960. The six EU members used preferential trading agreements to encourage future members and as a substitute for traditional foreign policy instruments.<sup>4</sup> Developing countries in Africa, the Caribbean and Latin America signed many RTAs, which were to varying degrees modelled on the EU. The Generalized System of Preferences (GSP) in 1971

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<sup>1</sup> The Appendix contains a list of RTAs notified to the WTO up to 1<sup>st</sup>. March 2006, and a graph of the cumulative number of notifications similar to that on the WTO webpage.

<sup>2</sup> They are highlighted in, for example, a flagship publication of the World Bank (2005) and are mentioned in passing in many papers as though they prove the case for burgeoning regionalism without needing comment. A paper by a Canadian government-funded think-tank, entitled “The Rush to Regionalism”, states that “regionalism in trade and investment agreements has been on a steep rise since the early 1990s” (IISD, 2004, 2). In these studies, and in the academic literature, the *font et origo* of the belief that RTAs are important and proliferating is the WTO website.

<sup>3</sup> The various RTAs are described and analysed more fully in Pomfret (2001; 2006).

<sup>4</sup> In this paper EU is used to refer to the European Union and its predecessor organizations.

legitimized extension of tariff preferences for developing countries. In the event, however, only the EU itself had any significant effect in terms of the impact of preferential trade policies on trade flows. The majority of the original EFTA members eventually joined the EU, while other RTAs from the 1960s were weakly implemented and eventually collapsed. Preferential access to rich countries' markets proved to be a feeble instrument for promoting developing countries' exports, because the preferential tariffs under GSP schemes were unilateral and tended to be revoked if they seriously impacted on trade flows.

A second wave of regionalism was initiated by the United States' departures from the GATT non-discrimination principle in the first half of the 1980s and peaked with the 1993 North American Free Trade Agreement (NAFTA). The 1980s and early 1990s may be seen as a wave because the western hemisphere developments coincided with the 1983 Closer Economic Relations (CER) agreement between Australia and New Zealand, and the deepening (through the 1992 project for completing the internal market) and widening (to 15 members in 1995) of the EU. There were also some new or extended RTAs in South America (Mercosur), South Asia (SAFTA), West Asia (ECO), Southeast Asia (AFTA) and Africa (many).

In both of these waves, however, apart from the obvious and important developments in European economic integration and NAFTA, it turned out that discriminatory trade policies posed less of a threat to the global trading system than observers like Patterson (1966) or Pomfret (1988) feared. Completion of the Kennedy Round in the 1960s and of the Uruguay Round in 1994 was much more significant for the global trading system than were the contemporaneous waves of regionalism. By 1995 with the establishment of the WTO there existed a body of world trade law centred on the nondiscrimination principle, strengthened dispute resolution mechanisms, and low bound tariffs in the major economies for all goods outside agriculture.

In the early 2000s, a third wave of discriminatory trade policies can be observed. This time it is led by East Asia, partly stimulated by a perception that the global economic institutions let the region down in the 1997 Asian Crisis and partly by the increase of China's economic power.<sup>5</sup> The collapse of the 1999 WTO meetings in Seattle and the diminishing significance of APEC further stimulated new

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<sup>5</sup> The Severe Acute Respiratory Syndrome (SARS) outbreak in 2003 and then the December 2004 tsunami reinforced the impression of inadequate regional institutions in Asia.

approaches to trade liberalization in the Asia-Pacific region. Bilateral negotiations were begun in 1999 by Japan with Singapore, and plurilateral negotiations were initiated between China and ASEAN. Singapore, South Korea, and Thailand all embarked on bilateral agreements. In their embracing of bilateral agreements, the Asian countries were joined by the USA, which negotiated bilateral trade pacts with friendly countries such as Jordan, Morocco and Australia. As is obvious from these examples, although the third wave is often seen as a recrudescence of regionalism, many of the bilaterals are not regional.<sup>6</sup> Further evidence of increased regionalism in the early 2000s is seen in the expansion of the EU to 25 members in 2004, although this is clearly a different development to the new bilaterals.

In sum, a recurring paradox since 1947 has been between the commitment to MFN treatment by GATT/WTO members and the proliferation of RTAs. Regionalism has twice appeared as a terminal threat to the GATT system, but multilateralism emerged stronger than ever after the Kennedy and Uruguay Rounds. A third cycle is in progress, and again the literature on regionalism is flourishing despite the apparent strength of the WTO system. One difficulty with assessing the extent of the threat that RTAs pose for the multilateral trading system is that the importance of regionalism is difficult to measure.

## **2. Counting RTAs**

Many commentators cite the large number of RTAs notified to the WTO as evidence of the growth and significance of regionalism. From this perspective, because the number of RTAs notified to the WTO reached an all-time high in the early 2000s, regionalism was more prevalent than ever. Crawford and Fiorentino (2005) in their survey of RTAs state that “Between January 2004 and February 2005 alone, 43 RTAs have been notified to the WTO, making this the most prolific RTA period in recorded history”.

These counts include notifications under GATT Article XXIV, GATS Article V, and the Enabling Clause, as well as accessions to existing RTAs. They undercount

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<sup>6</sup> When Thailand under Thaksin, for example, embarked on a policy of negotiating bilateral trade agreements, it began with Bahrain and Australia before moving on to the USA and Japan; this pattern is weakening Thailand’s regional trading arrangements by eroding preferential treatment negotiated within ASEAN. South Korea’s experimentation with bilaterals started with Chile and New Zealand, willing collocutors, but hardly regional neighbours and never likely to generate large bilateral trade flows.

the total number of RTAs, because some RTAs under negotiation have not yet been notified to the WTO and others are among non-WTO members. On the other hand, the cumulative WTO counts overstate the current situation because they do not exclude abrogated RTAs.<sup>7</sup> When ten new countries joined the EU in 2004, 65 RTAs between the EU and the new members and among the new member countries were subsumed into the EU RTA. Thus in Crawford and Fiorentino's "most prolific RTA period in recorded history" the net RTA formation was minus 22. The period could equally well be called the biggest withdrawal from RTAs in recorded history!

The main problem with using counts of RTAs as measures of the increasing importance of regionalism is that, while some agreements are important, many RTAs are inconsequential. Clearly, all notified RTAs should not carry equal weight. By any reasonable criterion, the May 2004 EU enlargement was far more important than a Moldova-Bosnia RTA, but by the counting logic each has equal weight.

To provide an idea of the dataset on which RTA counts are based, Table 1 lists the RTAs notified to the WTO during a recent six-month period: the first half of 2005. Several technical features stand out. The numbers are inflated because RTAs which cover both trade in goods and trade in services (Australia-Thailand, Japan-Mexico, and Panama-El Salvador) require MFN waivers under both GATT and GATS; such double-counting only occurs after 1995 when the GATS came into effect, which biases comparison of the numbers notified before and after the establishment of the WTO. Second, the notification date bears little resemblance to when an RTA takes effect; while the Thailand-Australia and Japan-Mexico RTAs entered into force at the same time as they were reported to the WTO, the Croatia-Macedonia RTA had been in effect since 1997 and the Romania-Israel RTA since 2001 (see Appendix table).

The most striking feature of Table 1 is that most of the RTAs are of minor importance to the global economy. Twelve are bilaterals involving pairs of eastern European countries, mostly involving regions of former Yugoslavia, i.e. reflecting regional disintegration. Others involve small trading nations, such as the agreement between Tunisia and EFTA (Iceland, Liechtenstein, Norway and Switzerland), the Israel-Romania RTA or the two Panama-El Salvador notifications. Even when the

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<sup>7</sup> The current numbers may also be inflated because of delays in notification. One of the RTAs notified in 1995 was the Treaty of Rome, which came into force in 1958, but whose signatories only needed to notify its service terms after GATS. There is also a bunching effect when a new WTO member notifies a raft of pre-existing RTAs (eg. the Kyrgyz Republic, Armenia, Georgia and Moldova in the Appendix).

RTAs involve larger economies (Thailand-Australia or Japan-Mexico) the restrictive terms of the agreement make it unlikely to have a big impact on the bilateral trade.

**Table 1:** RTAs notified to the WTO January-June 2005

<b>Agreement</b>	<b>Notification date</b>	<b>WTO Provisions</b>	<b>Type of agreement</b>
Thailand-Australia	5 January	Article XXIV	Free trade agreement
Thailand-Australia	5 January	GATS Art.V	Services agreement
Moldova-Bulgaria	28 January	Article XXIV	Free trade agreement
Moldova-Bosnia &H	28 January	Article XXIV	Free trade agreement
Moldova-Serbia &M	28 January	Article XXIV	Free trade agreement
Moldova-Croatia	31 January	Article XXIV	Free trade agreement
Moldova-FYROM	31 January	Article XXIV	Free trade agreement
Romania-Bosnia &H	14 February	Article XXIV	Free trade agreement
Romania -Serbia &M	14 February	Article XXIV	Free trade agreement
Romania -FYROM	14 February	Article XXIV	Free trade agreement
Bulgaria-Bosnia &H	11 March	Article XXIV	Free trade agreement
Bulgaria -Serbia &M	11 March	Article XXIV	Free trade agreement
Panama-El Salvador	18 March	Article XXIV	Free trade agreement
Croatia-FYROM	1 April	Article XXIV	Free trade agreement
Panama-El Salvador	5 April	GATS Art.V	Services agreement
Japan-Mexico	22 April	Article XXIV	Free trade agreement
Japan-Mexico	22 April	GATS Art.V	Services agreement
Romania-Israel	25 April	Article XXIV	Free trade agreement
FYROM-Bosnia &H	11 May	Article XXIV	Free trade agreement
EFTA-Tunisia	7 June	Article XXIV	Free trade agreement

Source: <http://www.wto.org> – see Appendix for a more extensive listing of RTAs notified from 1995 to 2006.

Counting RTAs is not just a poor measure of the extent of regionalism; it can lead to nonsensical conclusions about trends in the global economy due to the treatment of regional disintegration and integration. The replacement of a regional bloc by a web of bilateral or plurilateral agreements increases the number of RTAs, and by the counting criterion indicates an increase in regionalism. Conversely, the replacement of a network of minor RTAs by a single RTA can be interpreted as a decline in regionalism. This is not an abstract point; it is the main driving force behind the GATT/WTO indicator since 1989.

The main reason for the rapid increase in the number of RTAs during the 1990s was the proliferation of bilateral and plurilateral free trade agreements among countries of the former Council for Mutual Economic Assistance and among successor states to Yugoslavia, the USSR and Czechoslovakia. The new Eastern



European RTAs were a response to regional disintegration, ie. the dissolution of a larger regional bloc (the CMEA) or of individual countries, rather than a trend towards regionalism in Central and Eastern Europe.<sup>8</sup> As the Kyrgyz Republic (1998), Georgia (2000), Moldova (2001) and Armenia (2003) joined the WTO, they notified the WTO of their bilateral agreements with other members of the Commonwealth of Independent States; nothing changed in their CIS trade relations, but for these small Soviet successor states WTO accession was an important step in emphasising the priority of multilateral over regional trading arrangements. In sum, the increased number of RTAs in the 1990s and early 2000s was largely driven by a decline in regionalism and shift towards multilateralism on the part of two dozen formerly centrally planned economies.

Conversely, although the replacement of the myriad trade agreements among the eight eastern European countries which joined the EU in May 2004 by a single customs union should by the numbers criterion imply a major retreat from regionalism, the 2004 EU enlargement can more reasonably be seen as an extension of the ambit of a major RTA. The number of pre-2004 eastern European RTAs is a misleading guide to their promotion of regional trade because in the many bilateral agreements and also in the Central European Free Trade Area (CEFTA) sensitive products were excluded or put into Appendices with special conditions. This was less possible in EU negotiations where the *acquis communautaire* had to be accepted.<sup>9</sup> A similar phenomenon of reduced number of RTAs being associated with an extension of regionalism would arise if the EU brought the Balkan non-member countries into a customs union similar to that between the EU and Turkey; the customs union would displace a tangle of RTAs of which 31 have been reported to the WTO.<sup>10</sup>

In sum, the common practice of citing the number of RTAs notified to the WTO as a measure of the extent of regionalism in the global trading system is

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<sup>8</sup> Disintegration of a country led not only to new international trade agreements among the successor states, but also increased the number of RTAs of third countries, eg. Romania notified to the WTO RTAs with Bosnia, Serbia and Macedonia (Table 1) whereas in the 1980s a single RTA with Yugoslavia would have sufficed.

<sup>9</sup> For many observers, a surprising feature of the eastern European countries' accession negotiations and formal EU membership in 2004 was that they boosted trade, eg. *The Economist* (26<sup>th</sup>. November 2005) quoted former EBRD Chief Economist Willem Buiter as saying "I thought the free-trade arrangements agreed in previous years had already exhausted the potential. But it seems that quite a few people were willing to make the necessary investments only when these countries were in the EU". One reason for failure to exhaust potential was the incomplete pre-accession trade liberalization; trade among CEFTA countries in milk, for example, was restricted and only boomed after EU accession.

<sup>10</sup> Such a proposal is discussed in "Third time lucky?" *The Economist* (London), 14<sup>th</sup>. January 2006.

unfounded and misleading. It is unfounded because not all notified agreements are of equal significance. It is misleading because it interprets the fallout from a major event of the 1990s (the transformation of eastern Europe and the USSR) in simplistic terms as an increase in regionalism in the global economy.

### **3. The Share of World Trade covered by RTAs**

An alternative measure of the extent of regionalism is the share of world trade conducted under RTAs. All WTO members except Mongolia have signed RTAs. According to Crawford and Fiorentino (2005), for some WTO members preferential trade represents over 90 percent of their total trade. Schiff and Winters, co-leaders of a major World Bank research project on RTAs, state that “some 55 to 60 percent of world trade now occurs within such trade blocs” (1998, 178). These percentages suggest that the unconditional MFN treatment required by Article I of the WTO’s Charter applies to less than half, or perhaps even less than ten percent, of world trade.

Although less self-evidently faulty than the count criteria, this is also a dubious measure of the extent of regionalism. Take for example trade between the USA and Canada, the biggest bilateral trade flows in the world. After the 1987 Canada-US trade agreement, all of this trade could be considered to be under an RTA. Yet CUSTA is commonly viewed as having had only a minor impact on trade flows, because most US and Canadian tariffs were already below 5%. Thus, preferential access to each other’s markets made little difference to bilateral trade flows because MFN tariffs were low.

Why then was CUSTA signed? Essentially for non-trade reasons on the US side and for Canada as an insurance against unilateral protectionist measures by the USA. Thus, if some Canadian exports enter the US market unimpeded by antidumping or countervailing duties which would have been imposed in CUSTA’s absence, then that trade might be ascribed to the RTA. When we do not observe the counterfactual, however, it is hard to measure the RTA’s impact.<sup>11</sup>

The inclusion of Mexico to create NAFTA was a different matter because Mexico still had some significant tariffs in 1993. However, even if we accept that

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<sup>11</sup> US-Canada trade disputes continue to exist within CUSTA and NAFTA, eg. the four-times recurring softwood lumber dispute, so the issue is whether Canada would have come out on even worse terms without NAFTA.

NAFTA stimulated US-Mexican trade, it is still unclear whether all of this trade should be ascribed to NAFTA – and, if not all, then how much? Mexico was engaged in substantial unilateral trade liberalization at the same time as it was negotiating NAFTA, so that it is not valid to compare trade flows before and after NAFTA came into effect and ascribe any increase to NAFTA-related liberalization.<sup>12</sup>

The general point is that even if WTO members are parties to RTAs which eliminate tariffs on most of their trade, in a world with low MFN tariffs such tariff reductions are unlikely to make much difference to actual trade flows.<sup>13</sup> The contrast between this conclusion and the perceived large effects of RTAs may be because modern RTAs go beyond trade, to cover all kinds of “behind-the-border” obstacles to trade. These trade costs are important (Anderson and van Wincoop, 2004), and, as border measures such as tariffs and non-tariff barriers to trade diminish, the significance of other trade costs becomes more apparent. The role of RTAs in diminishing them will be addressed in the next section. The extent to which behind-the-border trade costs are reduced by an RTA and hence increase trade is, however, not captured by the size of trade flows between the signatories of the RTA.

#### **4. Deep Integration and the Specificity of Recent RTAs**

A novel feature of the second wave RTAs of the 1980s such as the Australia-New Zealand Closer Economic Relations, the Canada-US Free Trade Agreement, or the EU enlargements, was that they involved countries with fairly low tariffs. Supporters of the deeper EU, NAFTA or the CER argued that these were new forms of regionalism going into areas such as increasing-returns industries, policy harmonization, or service activities. Robert Lawrence (1996) popularised the term “deep integration” to capture regional agreements in these new areas. Such deep integration can improve market efficiency and, in view of the difficulties associated with policy harmonization, RTAs can provide a testing ground for alternative policy

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<sup>12</sup> Again a difficulty is that the counterfactual situation is not observed. There may also be an endogeneity problem if Mexico’s multilateral trade liberalization was related to successfully improving access to the US market through NAFTA. In the USA, obtaining Congressional approval of “free trade” within NAFTA in 1993 was seen as preparing the ground for approval of the more general trade liberalization incorporated in the 1994 Final Act of the Uruguay Round.

<sup>13</sup> With high tariffs, as in the 1930s, the share-of-world-trade criterion would be more insightful. In the mid-1980s I applied this criterion to show that most of world trade was conducted under discriminatory trade agreements (Pomfret, 1985), by which time the criterion was already inappropriate and the conclusion misleading.

blueprints. On the other hand, the complexity of deep integration also offers potential for welfare-decreasing RTAs.

Deep integration has the potential to be welfare-improving by reducing non-tariff barriers to trade and by cutting behind-the-border trade costs. Non-tariff barriers hamper regional integration, and in many cases are used by producers to segment markets in order to enjoy local monopoly power. Major steps in improving the operation of the EU internal market involved establishing principles of mutual recognition and disallowing minor variations in safety, health or environment standards, although this has led to tedious case-by-case judgments.

A positive building block argument for regional agreements is that they can be testing grounds for international policies in new areas. On the other hand, turning a policy designed by a few countries into a global institution may arouse fears of it being moulded to the designers' interests.<sup>14</sup> Examples of bilateral agreements which have gone beyond WTO commitments with respect to TRIMS (trade-related investment measures) and TRIPS (intellectual property rights) are discussed below; WTO-Plus articles in a North-South agreement, which benefit the partner from the North but preclude desirable policy options of the partner from the South, may be a poor blueprint for global agreements.

An alternative building block argument is to recognize that regional agreement in a controversial new area may be easier than global agreement. The EU's harmonization of competition policy illustrated the difficulty of reaching agreement even among countries with fairly similar economic structures. The Korea-China FTA goes beyond the WTO in its articles on government procurement.

A disadvantage of the second wave RTAs is that their increased complexity means that interest groups, who are well-informed about a particular sector, may become involved in design of the agreement and may shape the RTA to their own, but not necessarily the national, benefit. Trade diversion is often more politically acceptable than trade creation because the losers from trade diversion (domestic taxpayers and non-preferred foreign suppliers) have little impact on the policymaking

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<sup>14</sup> The ill-fated multilateral investment agreement designed by the OECD is perhaps an example; the low- and middle-income countries were never likely to accept a global regime on foreign investment designed by the rich countries which were the home of most transnational corporations. It is not my purpose to assess the validity of these building block arguments here, but it may be noted that designing new policies in deep integration areas can be done in global as well as in regional fora; reducing behind-the-border obstacles to trade is an issue in WTO Doha Round negotiations, and was the subject of the WTO's 2004 *World Trade Report*.

process, whereas the costs from trade creation are born by domestic producer interests, who are typically better organized and more powerful in shaping policy. Thus, there is a potential trade-diverting bias in RTA design, which is one justification for the GATT/WTO requirement that an FTA should cover virtually all trade so that countries cannot customize RTAs to include only sectors where trade diversion is more likely.<sup>15</sup> With deeper integration the exclusions may be less transparent. In NAFTA, the rules of origin (RoOs) have been designed, especially for textiles and apparel and for automobiles, to favour trade diversion. More broadly, the very detailed RoOs in NAFTA serve to manage trade, often to the benefit of specific US firms, while as a tax on intermediate inputs the RoOs' global impact is presumed to be negative (Krueger, 1999).<sup>16</sup> The extension to service sectors in deep integration arrangements almost inevitably increases the opportunity for rent-seeking, because most service providers are governed by regulations which may be desirable but which also offer the opportunity to erect discriminatory barriers to trade.<sup>17</sup>

Third wave RTAs take up deep integration issues or address very specific trade issues. One reason for being concerned with a trading partner's domestic policies or service sector structure is a sense that trade should be fair as well as free. If behind-the-border trade costs vary from country to country, then the trade playing field is not flat. Foreigners will find greater difficulty in penetrating the market of a country with poorly developed infrastructure, financial institutions and other support services. This concept of unfairness has been most often voiced by the USA, which sees its home market as easier to supply than other countries' markets, and hence US exporters and import-competing producers are at a competitive disadvantage.<sup>18</sup>

Especially when pushed by the USA or Singapore, whose home financial sectors are relatively efficient, third wave bilateral trade agreements often include

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<sup>15</sup> Despite the restriction in GATT Article XXIV, European producers managed for several decades to ensure through the use of non-tariff measures that the preference margins were especially high on agriculture, textiles and clothing, cars and steel - all sectors where trade diversion was likely to exceed trade creation (Pomfret, 1986).

<sup>16</sup> The 900+ pages required to document the North American Free Trade Agreement illustrate the point that many RTAs described as FTAs do not fit the formal definition of a free trade area, which would require a very simple agreement to abolish tariffs on internal trade. This applies to all of the so-called free trade agreements in Table 1.

<sup>17</sup> Messerlin (2005) cites the example of the high-level French lobbying to exclude bailiffs, notaries and barristers to the Supreme Courts from the EU Directive on Services.

<sup>18</sup> This US attitude predates the third-wave bilaterals; in the 1980s aggressive threats of targeted unilateral action were used by the USA to open, for example, South Korean insurance markets (Bhagwati and Patrick, 1990). Similar market opening pressures became a feature of the EU's market deepening, especially with respect to financial services after the last national-level capital controls were removed in the early 1990s.

measures of financial sector liberalization. The 2002 Japan-Singapore Economic Partnership Agreement, for example, had little to do with tariffs, which were already low on goods of interest to the two signatories, but aimed to reciprocally liberalize one another's financial markets.

More controversial has been the US position of going beyond WTO commitments on TRIMS and TRIPS. WTO-Plus on TRIMS has included references to indirect expropriation (ie. requiring compensation if policy changes reduces the expected profitability of a foreign investment) or mechanisms requiring compulsory international arbitration. On TRIPS, obligations to register patents on existing drugs if new uses are found, as in the US-Morocco FTA, may extend a patent's life beyond the requirements of TRIPS – a practice sometimes called “evergreening” of patents. In both of these areas, the WTO-Plus features benefit US transnational corporations but reduce the partners' policy flexibility, and may constrain negotiating options within the WTO (IISD, 2004, 25).

Third wave bilateral trade agreements are replete with examples of highly specific agreements. The typical scenario is announcement of free trade negotiations accompanied by data on the total trade between the negotiating countries and estimates of the potential welfare gains from trade expansion, and then several years later the governments sign a highly specific agreement, which may achieve limited goals, but also reflects a desire not to lose face by abandoning the “free trade agreement”. The 2004 Australia-US FTA, for example, involved two countries with substantial bilateral trade, but the outcome was almost trivial; Australia failed to achieve its major goals of reducing obstacles to its farm exports to the USA, but still signed the agreement, while the USA obtained a specific TRIPS concession from Australia.<sup>19</sup> In the negotiations between Thailand and Japan the key issues for Thailand were reducing barriers to agricultural exports and to labour mobility and for Japan the key issue was reducing Thai tariff peaks which hindered the integration of production by Japanese subsidiaries in the Thai car industry. The Japan-Thailand

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<sup>19</sup> For Australia's Liberal government bilateral trade negotiations were intended to produce a comprehensive agreement which would show the value of the special relationship with the USA. In the face of widespread and increasing domestic discontent over military support for the USA in Afghanistan and Iraq, it became impossible for the government not to obtain a trade agreement. The final agreement excluded sugar and included only limited access to US beef and dairy markets with an 18-year phase-in period (all three products had been initially identified by the Australian negotiating team as deal-breakers). For the USA the TRIPS agenda was narrowly focussed on forestalling changes in Australian patent laws that would facilitate export of generic pharmaceutical products to Asia.

FTA addressed these issues: Japan reduced the import duty on chickens from 6% to 3% and allowed Thai cooks to work in Japan, and Thailand reduced the 80% tariffs on cars and parts to 60%. It is difficult to think of a metric which would capture the significance of these minimalist results for the global trade regime, although it is clear that simply adding two more to the number of RTAs or including all of Thai-Japanese trade in a measure of trade covered by RTAs would be grossly misleading characterizations of the “Thai cooks agreement” as it is called by Japanese economists.

The specificity of these “beyond trade” arguments in support of second and third wave RTAs makes it difficult to generalize about their desirability and almost impossible to measure the extent of regionalism in the global economy. One issue is that, even though regional arrangements with deep integration or the recent bilateral agreements are not concluded in global fora, their impact is often non-preferential and beneficial to the global trading system. Improved operation of the EU-wide financial system, for example, helps to make trade finance competitively available to external as well as internal suppliers to EU markets. Measures such as improvements in customs clearance efficiency should facilitate all trade.<sup>20</sup> A second issue is the difficulty of quantifying the effect of measures that reduce trade costs. Whereas the impact of a tariff cut or removal of a non-tariff barrier affecting a specific product can be estimated, at least as a first approximation, with a partial equilibrium model, quantifying the impact of a measure that reduces trade costs in general requires a general equilibrium model. In principle, computable general equilibrium models can estimate the impact of a deep integration measure or a trade-facilitating non-tariff item in a bilateral treaty and they can contrast regional implementation with global implementation, but in practice CGE models are too coarse to capture the specificity of such measures.<sup>21</sup> Before concluding on the extent of regionalism, the next section reviews how patterns of regionalism differ from one part of the world to another.

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<sup>20</sup> In practice, there may be discrimination for technical reasons, eg. if Thai customs expand the electronic clearance facility this may benefit Malaysian exporters to Thailand but be infeasible for Lao exporters to Thailand who do not have computers. There are some explicitly preferential trade facilitation measures, such as the US fast-tracking container clearance which is limited to trading partners with whom the US has a trade agreement (eg. a container from Singapore does not require the individual inspection legislated post-9/11 as long as it has been certified and sealed in Singapore, but a container from Indonesia will not be exempted from inspection).

<sup>21</sup> A common approach by CGE modellers is to assume that the RTA will reduce trade costs by  $x\%$  (and test for sensitivity to various choices of  $x$ ). While this avoids the crass simplification of share-of-world-trade measures of the impact of RTAs, it is too general to capture the specific measures in actual

## 5. Differing Continental Patterns

Europe is the prime example of regional integration over the last half century. The EU now covers all of what might be considered to be Europe, apart from a few gaps of fairly small countries and a couple of larger countries to the east. As a customs union it is an RTA, but the EU is much more and at least some of its citizens see the EU as a stepping-stone towards economic, and perhaps political, union. In this respect the EU was practically unique in the second half of the twentieth century. The only close parallel is the relationship between Australia and New Zealand, with much shared culture and history, and the CER is the deepest RTA apart from the EU.

Between 1957 and the early 1970s the EU used trade agreements as a tool of foreign policy and constructed a “pyramid of preferences” which challenged the nondiscrimination principle upon which GATT was based. These discriminatory arrangements have become less significant since the 1970s, as the EU has found superior foreign policy instruments, and less complex, as the intended goodwill effect was eroded by preferred partners’ concerns about their relative position in the pyramid. Preference margins were eroded by cuts in the EU’s MFN tariffs in the various rounds of multilateral trade negotiations, and the 2001 Everything But Arms regulation granted duty-free access to EU markets to all least developed countries’ exports other than arms.<sup>22</sup> The 1995 Barcelona Process to create a Euro-Mediterranean free trade area by 2010 and the 2000 Cotonou Partnership Agreement with African, Caribbean and Pacific countries are essentially artefacts from the earlier era, which now aim to create simplified reciprocal free trade regimes with the two broad groups of most preferred partners rather than to create a finely delineated hierarchy of partners and clients.

The USA was the main defender of non-discriminatory trade policies until 1980, but after that it began to use RTAs to strengthen western hemisphere ties among market-based democracies and as an instrument of foreign policy. The Caribbean

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RTAs and given the side restrictions in many agreements it is likely to overstate the trade impact.

<sup>22</sup> As with the EU’s GSP scheme, however, utilization of the EBA regulation was limited by restrictive rules of origin (Candau and Jean, 2005). The pyramid of preferences was an example of what Bhagwati (1995) later termed the spaghetti bowl effect of overlapping RTAs, as some countries may have been covered by several schemes which were not consistent with respect to RoOs, product-specific quotas, etc.; in consequence, resources were expended in understanding the complex rules and opportunities to benefit from preferential access to the EU were not realized due to lack of information.



Basin Initiative, which was in 1982-3 the first step in this new direction, now includes 24 Caribbean nations, with Cuba as the significant exception. The USA used NAFTA to cement reforms in Mexico, and then at the December 1994 Summit of the Americas in Miami advocated a Free Trade Area of the Americas (FTAA).<sup>23</sup> The FTAA has been resisted in parts of Latin America (eg. Argentina, Brazil and Venezuela) and the original 1<sup>st</sup>. January 2005 deadline for concluding negotiations has passed. In South America, Mercosur is an alternative vehicle for regional integration, but Mercosur has been characterized by conflicts between the two big members (Brazil and Argentina) and by complaints from Paraguay and Uruguay about their actual access to those countries' markets.

Outside the western hemisphere, RTAs have limited economic significance for the USA. They are largely aimed at achieving specific goals and used as an instrument of foreign policy. The first such RTA was the 1985 US-Israel free trade agreement, which was in response to an EU-Israel FTA and clearly a special case. The bilateral trade agreements negotiated by the USA since 2001 (Jordan, Singapore, Australia, Bahrain, Morocco, and South Africa) are intended to reward allies. Such agreements can be expected to benefit the smaller partner, although their economic content is minor as any sensitive products are likely to be excluded.<sup>24</sup> The USA has exerted some trade diplomacy at a regional level, proposing a Middle East Free Trade Area and the Enterprise for ASEAN Initiative, but with little concrete to show for it.<sup>25</sup>

Proposals for RTAs made minimal progress in Asia before the late 1990s. In East Asia regional integration has increased since 1985, but it has been market- rather than policy-driven.<sup>26</sup> ASEAN was formed as a political bloc and despite many ideas

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<sup>23</sup> The USA has also signed bilateral agreements with Chile in 2003 and with five Central American countries and the Dominican Republic (CAFTA) in 2004. The USA has been negotiating with four Andean nations (agreement was reached with Peru in December 2005, but negotiations with Colombia and Ecuador are stalled, and talks with Bolivia were halted after the 2005 election) and Panama. Canada has also signed bilateral agreements with Chile and Cost Rica.

<sup>24</sup> Trade agreements between a big country and a small country typically reflect political motives on the part of the large country and economic motives on the part of the small country. The standard analysis of the economic consequences of RTAs shows that if one partner is a price-taker (ie. a small country in trade theory terms) then it will reap all the benefits from preferential tariff reductions; see Schiff and Winters (2003) for a recent restatement.

<sup>25</sup> The USA has also signed Trade and Investment Framework Agreements (TIFAs are described by the USA as a prerequisite to a subsequent free trade agreement or a bilateral investment treaty) with Indonesia, the Philippines, Thailand, Brunei and Malaysia, ie. all the ASEAN countries except Singapore (which has a FTA with the USA) and the four newest members (Cambodia, Laos, Myanmar and Vietnam).

<sup>26</sup> The 1985 Plaza Accord encouraged Japanese corporations to move assembly operations offshore. The booming high-performing Asian economies created market demand whose growth outpaced that in any other part of the world and hence created markets for one another's products. The emergence of

for joint industrial projects or for preferential tariffs it had little economic content until the ASEAN free trade area (AFTA) began to be taken slightly more seriously in the 1990s.<sup>27</sup> Malaysia's proposal for an East Asian Economic Caucus in the late 1980s was successfully opposed by the USA and Australia, and the "open regionalism" (ie. coordinated non-discriminatory trade liberalization) of Asia-Pacific Economic Cooperation (APEC) became the model for the region; the Bogor Declaration at the 1994 APEC summit expressed consensus on the multilateral approach. Japan, South Korea, China, Hong Kong and Taiwan stood out as economies without RTAs.

The 1997 Asian Crisis stimulated ideas about the need for regional coordination, but initial proposals were for monetary rather than trade cooperation, and these proposals appeared to hit a wall after the 2000 Chiang Mai Initiative (Pomfret, 2005). The stimulus for the changed attitude towards RTAs came from China, which had espoused a global perspective up to about 1998, but then switched to advocating regional agreements.<sup>28</sup> The switch may have reflected completion of WTO accession negotiations at which point China may have thought it had more freedom of action. Another catalyst was the sense of lack of appreciation by the USA for China's role in the Asian Crisis when it opposed Japan's proposals for an Asian Monetary Fund, and this cooling of relations was reinforced when the USA bombed the Chinese embassy in Belgrade. In any case, China became keener to negotiate with the ASEAN countries and to join the ASEAN+3 Chiang Mai Initiative, to which Japan and South Korea (the other elements of the +3) also reacted by embarking on negotiations for bilateral agreements.

What is the content of the East Asian trade agreements negotiated since 2000? For China they signalled regional engagement. From a historical perspective the ASEAN+3 grouping is a revival of the East Asian Economic Caucus, and it is viewed

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China as a major trading nation exacerbated these trends, and encouraged fragmentation of production in East Asia (Gaulier et al., 2006), so that the growth of trade in intermediate goods added to the proportion of intra-Asian trade in the countries' total trade.

<sup>27</sup> Regional cooperation agreements such as the Tumen River project, the Greater Mekong Subregion or Central Asian Regional Economic Cooperation (CAREC) did not contain trade policy components.

<sup>28</sup> This coincided with APEC's failure to deliver Early Voluntary Sector Liberalization in 1997-8, suggesting that the Bogor Declaration's goals might be unachievable and APEC a dead-end. The post-1997 monetary integration also played a role, as Japan had raised the issue of a trade agreement with Korea in 1998 (Feridhanusetyawan, 2005, 6), but the relative economic decline of Japan and rise of China during the 1990s were the underlying stimuli for later more concrete outcomes, eg. the Japan-Singapore Economic Partnership Agreement which was concluded in October 2001 is often seen as impelled by Japan's fear of loss of influence to China (IISD, 2004, 25).

with the same foreboding by neighbours who do not want to be excluded and by Japan which fears Chinese hegemony in such a grouping.<sup>29</sup> Japanese bilaterals have little impact; with Singapore there was little to liberalize, and with Thailand the most contentious product, rice, was excluded. South Korea's cautious approach to bilateral trade agreements is reflected in the choice of partners, starting with Chile. ASEAN is taking more serious steps to reduce internal trade barriers in AFTA, but within the context of reduced external trade barriers and so far with minimal deeper integration.<sup>30</sup> Since 2000 the dominant negotiating mechanism with non-members has been bilateral rather than through the ASEAN+3 process. Singapore's bilaterals go beyond trade, and mainly concern financial market liberalization, while Thai bilaterals seem to be primarily to offer the Prime Minister an international stage; to the extent that they do create special trade relationships, the bilateral agreements of Singapore and Thailand are anti-regionalism because they dilute ASEAN trade ties. Beyond East Asia Chinese negotiations tend to be single-issue deals, eg. in the China-Australia agreement China seeks abolition of its non-market-economy status in antidumping calculations.<sup>31</sup> In sum, the spaghetti bowl of recent East Asian RTAs makes for complicated artwork (as, for example, in Feridhanusetyawan, 2005, 10-11), but the RTAs have little economic impact.<sup>32</sup>

In other parts of the world RTAs have had even less impact. The League of Arab States dates from 1945, but even though the Arab League was mooted as a common market in 1956 (ie. before the EU's founding Six signed the Treaty of

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<sup>29</sup> China was a sponsor of the idea of an East Asia summit, but by the time the first summit was held in Kuala Lumpur in December 2005, China-Japan relations were poor and China was irked by Japan's insistence on the participation of Australia, India and New Zealand, which contradicted China's desire for a specifically East Asian grouping. For the immediate future, China's regional relations are likely to be focussed on its relations with ASEAN.

<sup>30</sup> The average MFN tariff of ASEAN members (apart from Cambodia, Laos and Vietnam, which have an extended transition period to AFTA) is 8% or less. Preference margins are small because the target is to reduce intra-AFTA tariffs to 5% or less (not necessarily to zero), and sensitive products like Indonesia's textile and petrochemical products, the Philippines' cement sector, or Malaysia's cars are excluded from AFTA. The 1995 ASEAN Framework Agreement on Services provides for voluntary commitments beyond GATS, but has made no significant progress (Feridhanusetyawan, 2005, 24).

<sup>31</sup> In the negotiations which began in May 2005 Australia's main goals concerned market access for services and for farm products, but China has created precedents which suggest that little will be achieved in these areas, eg. the China-ASEAN FTA deferred consideration of services for a later date and the China-Chile FTA specifically excluded wool even though Chile is an extremely minor wool exporter.

<sup>32</sup> Low (2004) and Feridhanusetyawan (2005) survey East Asian RTAs. Keeping track is not easy. Dates may refer to announcement, signing or implementation, and draft RTAs may differ from final RTAs. There are also some confusing overlaps, eg. the Trans-Pacific Strategic Economic Partnership Agreement (TPSEPA) between New Zealand, Singapore, Brunei and Chile, is separate from the Singapore–New Zealand bilateral agreement.

Rome) and a Greater Arab Free Trade Area agreement was signed in 1997 there has been little implementation.<sup>33</sup> In Africa dozens of RTAs have been signed but with little impact on trade. In South Asia, despite the existence of the South Asian Association of Regional Cooperation (SAARC) since 1985 and a preferential trade arrangement since 1995, the two largest countries, India and Pakistan, did not even grant one another full MFN treatment; since the signing of the South Asia Free Trade Area (SAFTA) agreement in 2004 relations are warmer, but still appear to be subordinate to bilateral agreements with countries outside the region.<sup>34</sup> In West and Central Asia, especially since the dissolution of the USSR, many RTAs have been signed, but few implemented. In all of these regions political leaders appear to take a talk-is-cheap attitude to trade agreements, happy to sign them at summit meetings and leave the details to lower officials who will bury the agreement when unpleasant consequences seem likely or political alliances shift.<sup>35</sup> None of this has much consequence for the global trading system.

In sum, we observe different patterns in different parts of the world, which are amalgamated under the rubric of “regionalism” but are in reality quite diverse. Should this be a cause for concern? The key components of the multilateral trading system are nondiscrimination and transparency. Attempts to form seriously discriminating RTAs have foundered in Latin America and Africa, and failed to get off the ground in Asia, largely because policymakers did not want to bear the trade diversion costs of importing from inefficient producers in partner countries. If the EU is treated as a single unit, as it is in WTO fora, then there is not much discrimination due to RTAs.<sup>36</sup> Transparency has been a greater victim due to the complexity of many RTAs.<sup>37</sup>

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<sup>33</sup> The 1981 Gulf Cooperation Council and the 1989 Arab Maghreb Union are the main existing RTAs in the Arab world, but the former covers few people and the latter is split by political divisions. Tunisia (1998), Morocco (2000), Jordan (2002), and Egypt (2004) have signed Euro-Mediterranean Agreements with the EU, and the 2001 Agadir Declaration committed them to creating a free trade area among themselves by 2006 (Dennis, 2006).

<sup>34</sup> India has had bilateral negotiations with Thailand and Singapore, Pakistan has signed framework agreements with China, Malaysia and the USA and is holding discussions with Indonesia, Laos, Singapore and Thailand, and Sri Lanka signed a Trade and Investment Framework Agreement with the USA in 2002 as a step towards a free trade agreement (Baysand, Panagariya and Pitigala, 2006).

<sup>35</sup> The extreme version of the talk-is-cheap pattern is the CIS, where several hundred free trade agreements, customs unions, common economic spaces, or other bilateral or plurilateral arrangements have been announced among the twelve Soviet successor states since 1991. None of these proposals has had a significant impact on national trade policies or on trade flows.

<sup>36</sup> The most important elements of discrimination in the current global trading system have come from other than RTAs, e.g. quantitative trade restrictions such as the Multifibre Arrangement quotas or the voluntary export restraints which blossomed in the 1980s, or the US steel safeguard policies of 2002

## 6. Conclusions

Claims that the world economy is experiencing a dramatic increase in regionalism are based on faulty measures and misrepresent the reality of an increasingly integrated global trading system based on non-discriminatory trade policies.

Despite the increased attention being paid to regional arrangements, the hold of multilateralism is stronger than ever as practically all trading nations have now acceded to the WTO, with lower trade barriers and stronger trade dispute settlement procedures than ever before.<sup>38</sup> Perceptions of WTO enfeeblement reflect a tendency of news reporting to highlight conflict rather than accord. The end of the Multifibre Arrangement in December 2004 was a monumental step in global non-discriminatory trade liberalization which is surely good for global resource allocation and for people who wear clothes, but the press coverage in early 2005 highlighted negative effects on countries suffering from preference erosion (such as Bangladesh) and the impact on producers in powerful nations. Even as the USA and EU were negotiating safeguard measures against the surge of clothing imports from China, little mention was made of the fact that these were legal under China's WTO accession accord but limited in duration to 2008.<sup>39</sup> Other striking examples of the increased rule of law in international trade since the creation of the WTO are the ability of small countries to win cases against major trading nations (and have the offending policies modified) and the willingness of the US Congress to amend US tax law (on FISCs) to comply with a WTO judgment.<sup>40</sup>

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(Brown, 2004) or the use of special agricultural safeguards today (Hallaert, 2005).

<sup>37</sup> Estevadeordal and Suominen (2003), whose catalogue of RoOs shows them to be often product-specific and rarely consistent from one RTA to another, conclude that failure to harmonize RoOs exacerbates hub-and-spoke relationships and is an obstacle to freer global trade.

<sup>38</sup> The WTO is almost universal, with the main non-members (Russia, Ukraine, Kazakhstan and perhaps Iran) expected to join within the next decade. The strength of the GATT system by the late 1980s is a crucial reason why the disintegration of Eastern Europe did not follow the same pattern as in the aftermath of the ostensibly similar disintegration in 1919. Whereas in the 1920s and 1930s the multilateral trading system unravelled with the creation of preferential ties in Eastern Europe, after 1989 the increase in RTAs was a temporary phenomenon in Eastern Europe along the path to greater regional integration in Europe. The major trading nations all showed total adherence to their WTO obligations with no attempts to obtain national advantages through trade agreements (of course, it helped that the major European trading nations were in the EU with common trade policies, or in the case of Austria, Finland and Sweden about to join the EU).

<sup>39</sup> Liu and Sun (2004) point out that action could be taken against Chinese clothing exports under other WTO safeguard provisions after the specific textile provisions lapse at the end of 2008. My point is that the MFA was a huge sectoral exception to multilateral trading rules and this no longer exists.

<sup>40</sup> Venezuela's early victory in a petroleum-related case against the USA and the finding against EU

The most salient RTAs in the current world economy (the European Union, the North American Free Trade Area, or Closer Economic Relations between Australia and New Zealand) all have liberal external trade policies, so that they could properly be called regional arrangements for matters beyond trade. In a world where tariffs and simple non-tariff trade barriers have diminished, other trade costs come to the fore, and as markets become more regionally or globally integrated there are increasing pressures for harmonization in a greater number of policy areas. In this process, regional arrangements have a role to play as some policy regimes may desirably be supra-national but sub-global. Regional arrangements may also be testing grounds for innovations in policy coordination or harmonization, and hence act as building blocks towards identifying well-designed global policies.

This is not to argue for giving unrestricted *carte blanche* to beyond-trade-RTAs. They may be undesirable from a global welfare perspective and they may impinge negatively on the multilateral trade regime as the increased complexity of regional arrangements opens up opportunities for managed trade that can benefit insiders and become a stumbling block to progress at the global level. Nevertheless, it is important to keep a sense of perspective. Deep integration may affect trade but it goes beyond trade policy, and it is not in itself a sign of erosion of the multilateral trading system. Bilateral agreements, which focus on, say, aspects of financial liberalization to reduce a behind-the-border trade cost, in essence differ little from agreements such as double-taxation treaties, which have been signed for decades without being referred to as bilateral trade agreements or FTAs.

The fundamental difficulties in assessing RTAs today are the same as those highlighted in the classic treatment by Viner (1950); the second-best nature of RTAs in terms of economic analysis and the interaction of politics and economics. The second-best analysis (ie., because world trade is already distorted, reducing a distortion by preferential trade liberalization may be welfare-improving or welfare-reducing) is traditionally framed as trade creation versus trade diversion. It most often appears in the contrast between the grand announcements of RTAs by political

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banana policies were landmark victories for poor countries against powerful WTO members. Brazil's recent victory in its cotton case against the USA is also a significant example of action within the WTO leading to reform of rich country policies which were supported by powerful domestic lobbies and would not have been changed in response to bilateral complaints. Busch, Raciborski and Reinhadt (2006) further argue that the existence of the WTO dispute settlement mechanism discourages members from initiating trade restrictions (US antidumping actions in their empirical study) of doubtful WTO legality.

leaders wishing to make a foreign policy impact or to indicate their countries' friendship, and the implementation record as policymakers are lobbied by domestic producers or realize the costs of trade diversion.<sup>41</sup> Second-best considerations can also be seen in debates over whether RTAs produce beneficial WTO-Plus outcomes. All RTAs claim to be WTO consistent, but the imprecision of GATT Article XXIV and GATS Article V mean that this is not always clear, and WTO-Plus may be undesirable if it precludes negotiation of broader superior outcomes.

Politics have driven some of the major developments highlighted in the previous section, eg. the EU, FTAA and the competition between China and Japan for Asian hegemony. This can have large and unstoppable economic consequences for the global trading system (as in the road from the Treaty of Rome to the EU) or it can have negligible economic consequences (as in the current stand-off in East Asia). At times the outcome may be somewhere in between (does NAFTA mildly reinforce market-driven integration trends behind low external trade barriers, as in ASEAN, or does it create a trading bloc?), but the eventual outcome is likely to be one of the extremes. Politically motivated regional integration leads to the RTA becoming a country rather than a region (as happened earlier in Germany, Canada, Italy or Australia, and may be happening with the EU today). In large country – small country RTAs, the large country may draw back from RTAs with small partners as their flaws as a foreign policy instrument become apparent (as with the EU's pyramid of preferences) or be unwilling to offer sufficient economic incentives to the small country to make the RTA meaningful (as in recent US bilateral trade agreements).<sup>42</sup> The exceptions among large+small country RTAs are quasi-colonial, in which case the small partner is scarcely a country.

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<sup>41</sup> RTAs have failed when they were based on a regional form of import substitution (eg. the customs unions agreed among developing countries in Latin America or Africa in the 1950s and 1960s or RTAs within the CIS in the 1990s and 2000s). They inevitably led to conflict, because each member wanted a regional market for its own inefficient industries but was unwilling to buy the expensive or poor quality import-substitutes being produced by their partners.

<sup>42</sup> The limited coverage of the recent bilateral trade agreements in Asia or involving the USA is a variant of the talk-is-cheap pattern (footnote 35); political leaders make the gesture of announcing a free trade agreement, whose political significance may be touted by the foreign ministry, but as the trade ministry negotiates the details the agreement's coverage shrinks. The economic side to the sustainability of large country – small country RTAs is that interest groups in the large country which are strong enough to maintain external trade barriers will prevent lowering of these barriers on a preferential basis if there will be any significant increase in trade, while the RTA is useless for the small country if it cannot generate any increase in trade. If the only increase in bilateral trade is due to trade diversion, then the disadvantaged third countries are likely to object (as in the EU banana case).

Regionalism is difficult to measure. The most popular approaches, counting RTAs notified to the WTO or measuring the proportion of world trade between RTA signatories, are clearly inadequate. The desirability of RTAs, which due to their second-best nature is impossible to determine *a priori*, is also difficult to assess. Nevertheless, the threat to the multilateral trading system does not appear to be as large as is often reported, because the long-term dynamics of RTAs lead either to state formation, which is important but rare, or to ineffectiveness, which is the fate of the vast majority of RTAs. The debate about whether RTAs are building blocks or stumbling blocks for global freer trade, which was so virulent in the 1990s, faded because, whatever the answer to the question, in practice RTAs have made so little difference either way.<sup>43</sup> Apart from the deep integration of a handful of RTAs or narrowly specific measures in recent bilateral agreements, which go ‘beyond trade’, the impact on the global trading regime of the hundreds of RTAs notified to the GATT/WTO as being in contravention of the MFN principle has been trivial compared to the establishment of multilateral trade law based on the nondiscrimination principle.

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<sup>43</sup> Similarly, the spaghetti bowl effect (footnote 22), a vivid image which has launched dozens of economists as artists, is overworked because the lines in most spaghetti bowl diagrams are thin to non-existent. At the IIS seminar Ronald Findlay suggested that an ‘angel-hair bowl effect’ may be a better image, but even that overstates the impact of most RTAs.



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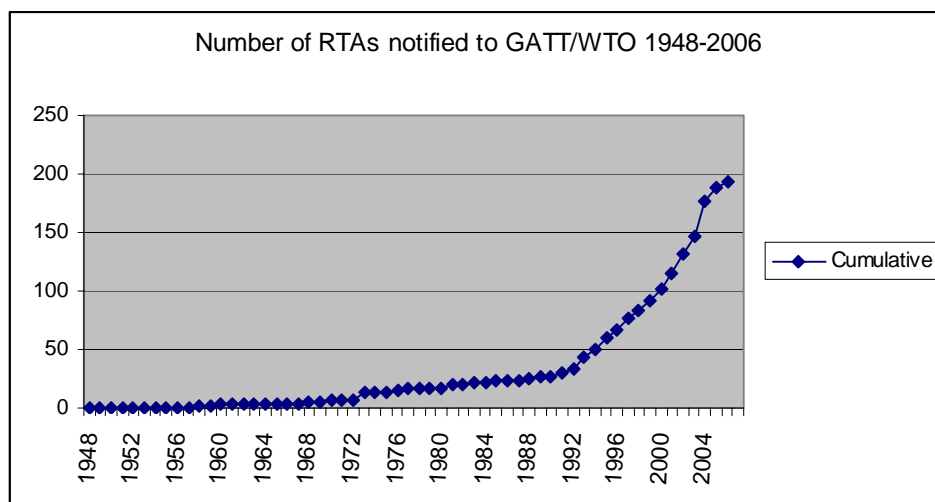
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## APPENDIX



**Appendix Table: RTAs Notified to the WTO since 1<sup>st</sup>. January 1995**

Agreement	Notification date	WTO Provisions	Entry into force
EC Accession (Austria, Finland, Sweden)	20 January <b>1995</b>	Article XXIV	1/1/95
EC Accession (Austria, Finland, Sweden)	20 January	GATS Art.V	1/1/95
NAFTA	1 March	GATS Art.V	1/1/94
COMESA	29 June	Enabling Clause	8/12/94
EC (Treaty of Rome)	10 November	GATS Art.V	1/1/58
CER	22 November	GATS Art.V	1/1/89
EC-Turkey	22 December	Article XXIV	1/1/96
Iceland - Faroe Islands	23 January <b>1996</b>	Article XXIV	1/7/93
Switzerland - Faroe Islands	8 March	Article XXIV	1/3/95
Norway - Faroe Islands	13 March	Article XXIV	1/7/93
EC- Romania	9 October	GATS Art.V	1/2/95
EEA	10 October	GATS Art.V	1/1/94
Canada – Israel	23 January <b>1997</b>	Article XXIV	1/1/97
EC - Faroe Islands	19 February	Article XXIV	1/1/97
EC – Bulgaria	25 April	GATS Art.V	1/2/95
EC – Palestinian Authority	30 June	Article XXIV	1/7/97
Canada – Chile	26 August	Article XXIV	5/7/97
Romania – Moldova	24 September	Article XXIV	1/1/95
Canada – Chile	13 November	GATS Art.V	5/7/97
CEFTA Accession (Romania)	8 January <b>1998</b>	Article XXIV	1/7/97
EC-Andorra	9 March	Article XXIV	1/7/91
Romania – Turkey	18 May	Article XXIV	1/2/98
Israel – Turkey	18 May	Article XXIV	1/5/97

EC – Tunisia	23 March <b>1999</b>	Article XXIV	1/3/98
CEFTA Accession (Bulgaria)	24 March	Article XXIV	1/1/99
EAEC	21 April	Article XXIV	8/10/97
Bulgaria – Turkey	4 May	Article XXIV	1/1/99
Kyrgyz Republic – Uzbekistan	15 June	Article XXIV	20/3/98
Kyrgyz Republic – Ukraine	15 June	Article XXIV	19/1/98
Kyrgyz Republic – Russia	15 June	Article XXIV	24/4/93
Kyrgyz RepublicMoldova	15 June	Article XXIV	21/11/96
EFTA – Palestinian Authority	21 September	Article XXIV	1/7/99
Kyrgyz Republic – Kazakhstan	29 September	Article XXIV	11/11/95
CIS	1 October	Article XXIV	30/12/94
MSG	7 October	Enabling Clause	22/7/93
Bulgaria – FYROM	19 February <b>2000</b>	Article XXIV	1/1/00
WAEMU/UEMOA	3 February	Enabling Clause	1/1/00
EFTA – Morocco	18 February	Article XXIV	1/12/99
EC – Morocco	1 August	Article XXIV	1/7/00
CEMAC	29 September	Enabling Clause	24/6/99
EAC	11 October	Enabling Clause	7/7/00
EC – Israel	7 November	Article XXIV	1/6/00
EC – Morocco	8 November	Article XXIV	1/3/00
EC – South Africa	21 November	Article XXIV	1/1/00
Kyrgyz Republic – Armenia	4 January <b>2001</b>	Article XXIV	27/10/95
Turkey – FYROM	22 January	Article XXIV	1/9/00
EFTA – FYROM	31 January	Article XXIV	1/1/01
Georgia – Ukraine	21 February	Article XXIV	4/6/96
Georgia – Turkmenistan	21 February	Article XXIV	1/1/00
Georgia – Russia	21 February	Article XXIV	10/5/94
Georgia – Kazakhstan	21 February	Article XXIV	16/7/99
Georgia –Azerbaijan	21 February	Article XXIV	10/7/96
Georgia – Armenia	21 February	Article XXIV	11/11/98
Mexico – Israel	8 March	Article XXIV	1/7/00
Chile - Mexico	8 March	Article XXIV	1/8/99
Chile - Mexico	14 March	GATS Art.V	1/8/99
EFTA – Mexico	22 August	GATS Art.V	1/7/01
EFTA – Mexico	22 August	Article XXIV	1/7/01
New Zealand - Singapore	19 September	GATS Art.V	1/1/01
New Zealand - Singapore	19 September	Article XXIV	1/1/01
EC – FYROM	21 November	Article XXIV	1/6/01
EFTA – Croatia	22 January <b>2002</b>	Article XXIV	1/1/02
EFTA - Jordan	22 January	Article XXIV	1/1/02
USA – Jordan	5 March	Article XXIV	17/12/01
Chile – Costa Rica	14 May	Article XXIV	15/2/02
Chile – Costa Rica	24 May	GATS Art.V	15/2/02
EC – Mexico	21 June	GATS Art.V	1/3/01
India – Sri Lanka	27 June	Enabling Clause	15/12/01
USA – Jordan	18 October	GATS Art.V	17/12/01
Japan - Singapore	14 November	Article XXIV	30/11/02
Japan - Singapore	14 November	GATS Art.V	30/11/02

EFTA	3 December	GATS Art.V	1/6/02
EC- Jordan	20 December	Article XXIV	1/3/02
EC – Croatia	20 December	Article XXIV	1/3/02
Canada – Costa Rica	17 January <b>2003</b>	Article XXIV	1/11/02
EFTA - Singapore	24 January	Article XXIV	1/1/03
EFTA - Singapore	24 January	GATS Art.V	1/1/03
CARICOM	18 February	GATS Art.V	1/7/97
Bulgaria – Israel	14 April	Article XXIV	1/1/02
EC – Lebanon	4 June	Article XXIV	1/3/03
Turkey – Croatia	8 September	Article XXIV	1/7/03
Turkey – Bosnia & Herzegovina	8 September	GATS Art.V	1/7/03
Singapore-Australia	1 October	Article XXIV	28/7/03
Singapore-Australia	1 October	GATS Art.V	28/7/03
Croatia – Bosnia & Herzegovina	6 October	Article XXIV	1/1/01
USA – Chile	19 December	Article XXIV	1/1/04
USA – Chile	19 December	GATS Art.V	1/1/04
USA – Singapore	19 December	Article XXIV	1/1/04
USA – Singapore	19 December	GATS Art.V	1/1/04
China – Hong Kong	12 January <b>2004</b>	Article XXIV	1/1/04
China – Hong Kong	12 January	GATS Art.V	1/1/04
China – Macao	12 January	Article XXIV	1/1/04
China – Macao	12 January	GATS Art.V	1/1/04
EC – Chile	18 February	Article XXIV	1/2/03
China – El Salvador	17 March	GATS Art.V	1/6/02
China – El Salvador	16 February	Article XXIV	1/6/02
CEFTA Accession (Croatia)	3 March	Article XXIV	1/3/03
Croatia – Albania	31 March	Article XXIV	1/6/03
Albania – Bulgaria	31 March	Article XXIV	1/9/03
Albania – Kosovo	8 April	Article XXIV	1/10/03
Korea – Chile	19 April	Article XXIV	1/4/04
Korea – Chile	19 April	GATS Art.V	1/4/04
EU Enlargement	28 April	GATS Art.V	1/5/04
EU Enlargement	30 April	Article XXIV	1/5/04
Armenia - Ukraine	27 July	Article XXIV	18/12/96
Armenia – Kazakhstan	27 July	Article XXIV	25/12/01
Armenia – Moldova	27 July	Article XXIV	21/12/95
Armenia – Russia	27 July	Article XXIV	25/3/93
Armenia - Turkmenistan	27 July	Article XXIV	7/7/96
Bangkok Agreement Accession (China)	29 July	Enabling Clause	1/1/02
SADC	9 August	Article XXIV	1/9/00
EC – Egypt	4 October	Article XXIV	1/6/04
Albania – Serbia & Montenegro	19 October	Article XXIV	1/9/04
EFTA – Chile	10 December	Article XXIV	1/12/04
EFTA – Chile	10 December	GATS Art.V	1/12/04
Albania - Romania	14 December	Article XXIV	1/1/04
Albania – Bosnia & Herzegovina	14 December	Article XXIV	1/12/04
Albania – FYROM	14 December	Article XXIV	1/7/02

Albania – Moldova	20 December	Article XXIV	1/11/04
ASEAN – China	21 December	Enabling Clause	1/7/03
US - Australia	23 December	Article XXIV	1/5/05
US - Australia	23 December	GATS Art.V	1/5/05
Thailand-Australia	5 January <b>2005</b>	Article XXIV	1/1/05
Thailand-Australia	5 January	GATS Art.V	1/1/05
Moldova-Bulgaria	28 January	Article XXIV	1/12/04
Moldova-Bosnia & Herzegovina	28 January	Article XXIV	1/5/04
Moldova-Serbia & Montenegro	28 January	Article XXIV	1/9/04
Moldova-Croatia	31 January	Article XXIV	1/10/04
Moldova-FYROM	31 January	Article XXIV	1/12/04
Romania-Bosnia & Herzegovina	14 February	Article XXIV	1/7/04
Romania -Serbia & Montenegro	14 February	Article XXIV	1/7/04
Romania -FYROM	14 February	Article XXIV	1/1/04
Bulgaria-Bosnia & Herzegovina	11 March	Article XXIV	1/12/04
Bulgaria -Serbia & Montenegro	11 March	Article XXIV	1/6/04
Panama-El Salvador	18 March	Article XXIV	11/4/03
Croatia-FYROM	1 April	Article XXIV	30/10/97
Panama-El Salvador	5 April	GATS Art.V	11/4/03
Japan-Mexico	22 April	Article XXIV	1/4/05
Japan-Mexico	22 April	GATS Art.V	1/4/05
Romania-Israel	25 April	Article XXIV	1/7/01
FYROM-Bosnia & Herzegovina	11 May	Article XXIV	15/7/02
EFTA - Tunisia	7 June	Article XXIV	1/6/05
ECOWAS	26 September	Enabling Clause	1993
Turkey – Tunisia	15 September	Article XXIV	1/7/05
Turkey – PLO	15 September	Article XXIV	1/6/05
Croatia - Serbia & Montenegro	22 September	Article XXIV	1/7/04
EC – Chile	1 November	GATS Art.V	1/3/05
Mexico – Nicaragua	2 November	Article XXIV	1/7/98
Mexico – Nicaragua	2 November	GATS Art.V	1/7/98
Thailand – New Zealand	2 December	Article XXIV	1/7/05
Thailand – New Zealand	2 December	GATS Art.V	1/7/05
US - Morocco	16 January <b>2006</b>	Article XXIV	1/1/06
US - Morocco	16 January	GATS Art.V	1/1/06
Turkey - Morocco	21 February	Article XXIV	1/1/06
Korea - Singapore	24 February	Article XXIV	2/3/06
Korea - Singapore	24 February	GATS Art.V	2/3/06

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