SUMMARY AND CONCLUSIONS

Two developments in the evolution of the world trading system have dominated the international trade policy scenario. One is the extension and strengthening of the multilateral system, beginning with the initiation of the Uruguay Round of Multilateral Trade Negotiations of the GATT in 1986, and culminating in its ratification and the establishment of the World Trade Organization in 1995. The other, is the growing number of regional trading groups, which have become a highly important basis for the conduct of trading policy. A substantial proportion of world trade is now covered by regional agreements; and barring a few countries, almost all the Members of the WTO are part of at least one such arrangement.

DEVELOPMENTS IN REGIONALISM

This surge in the establishment of regional trade agreements, however, is not a recent phenomenon. Four decades ago, the concept of regionalism, in theory and practice, spread across the world with the creation of the European Economic Community (EEC) by the Treaty of Rome in 1957. Europe’s long history of wars and the devastation that followed convinced countries of the necessity for closer cooperation to prevent further conflicts and facilitate reconstruction efforts.
The history of post-World War II regionalism can be categorized into two distinct phases – the pre-Cold War or the First Regionalism, and the post-Cold War or the Second Regionalism. The first phase occurred in the 1950s and 1960s, and was largely confined to Western Europe (the EEC) in the developed world; and Latin America in the developing. In North America, regionalism remained virtually non-existent, with the key economic power – the USA – showing a strong commitment to the multilateral approach to trade policy. Though not itself supportive of regionalism, the US did act as an external federator to the European process of integration.

Barring Europe, this phase of regionalism ebbed in the early 1970s primarily because the attempts that had been made to liberalize trade among the members of the various regional blocs had generally failed. In the years that followed, unilateral non-discriminatory trade liberalization became the order of the day and regionalism was relegated to the background.

The second emergence of regionalism came in the latter half of the 1980s, and had its starting ground in North America, wherein the most important development was the conversion of US philosophy towards regionalism. Thus followed the US-Israel Free Trade Area in 1985 and the CUSFTA in 1988, heralding the second phase. In the current wave,
regionalism has engulfed all the major players in the world economy; and the importance of trade blocs in increasing the bargaining potential of its members is gaining in credibility. The words of the 19th century American President Benjamin Franklin, that "no nation was ever ruined by trade" appears to be the adage guiding countries flocking to form and join regional groupings.

The NAFTA, the MERCOSUR, the ANZCERTA, the ASEAN Free Trade Area (AFTA), the APEC, the SAFTA, the FTAA, the potential TAFTA - these are a few of the trade blocs gaining in dominance. And of course, the steadily expanding and deepening European Union which has evolved through various stages of integration, straddling both the phases of regionalism.

At a theoretical level, the basic foundations of the concepts of regional integration and international cooperation were laid within the disciplines of political science and economics. The theories of functionalism and neo functionalism are of fundamental importance in this regard. David Mitrany and Ernst B. Haas are the acknowledged fathers, respectively, of the two schools of thought which have provided a conceptual understanding of developments in international organization. These theories have subsequently been revised to accommodate the actual
trends in regional and multilateral cooperation, most notably taking into account factors in European integration.

In handling the concept of regional integration from an economics point of view, the contribution of Jacob Viner and his analysis of the trend in terms of trade creation and trade diversion, is considered of paramount importance. The former relates to newly created trade between the member countries of a customs union, the latter to trade diverted from a foreign (third) country to a member country, both consequent upon the abolition of tariffs within the union. According to Viner, the beneficial effects of the union will predominate if trade creation outweighs trade diversion.

Viner's theory, which is now considered a static analysis of regional integration, has been given wider dynamic dimensions by a host of economists including Murray Kemp, Charles Cooper, Richard Brecher, Paul Krugman, and Jagdish N. Bhagwati, to name a few. New thinking on regionalism has evolved, one aspect of which is the concept of 'open regionalism', which broadly refers to plurilateral agreements that are non exclusive and open to new members.

Economic integration can take several forms that represent varying degrees of integration. These are, free trade area, customs union, common market, economic union, and complete economic integration. These are not
stages in a process which eventually leads to complete political integration, and each of these forms exist in its own right. While encompassing the features of one or the other of these classical forms, some of the current regional trade agreements go far beyond mere trade liberalization in terms of coverage.

A number of factors have led countries to seek regional integration, and the motivation varies from group to group. Some countries look for traditional trade gains through reciprocal exchanges of concessions; others look to increase their bargaining powers towards third countries by entering an RTA, with common external barriers. Market access to a larger partner is a key motivating factor. Also because, in an RTA fewer trading partners are involved than in a multilateral trade negotiation, countries see a higher chance of successfully resolving issues. That apart, strategic linkage can also be an important rationale.

THE MULTILATERAL DEVELOPMENTS

The multilateral trading system as embodied in the GATT-47 and now the WTO has completed fifty years of existence. Although multilateralism is a characteristic of the world economic system, it is a complex task defining the term. The basic philosophy of the multilateral trading system is that open markets, non-discrimination, and global
competition in international trade are conducive to the national welfare of all countries.

The key guiding principles of this system is Non-discrimination which is embodied in the Unconditional Most-Favoured-Nation (MFN) clause and National Treatment. Article I of the GATT underlines the MFN clause, which stipulates that all imported goods must receive the same tariff or non-tariff treatment irrespective of their country of origin. This is considered as the fundamental basis upon which sound international trade relations can be built.

Multilateralism as a basis of modern international trade relations can be traced to the signing of the General Agreement on Tariffs and Trade in 1947. The history of the GATT-47 saw eight rounds of multilateral trade negotiations culminating in the Uruguay Round which paved the way for the establishment of the WTO, which is the first international organization to encompass all aspects of trade in goods and services (the GATT remained a multilateral treaty).

With the outcome of the Uruguay Round, multilateralism has been given a fresh lease of life. The present system as it exists under the WTO is more far-reaching than the GATT’s mandate. Agriculture, new regimes in the areas of intellectual property rights, investment measures, and services have come under the umbrella of multilateral regulation.
REGIONALISM AND MULTILATERALISM

As mentioned, the MFN principle enshrined in Article I of the GATT is a multilateral obligation. In conjunction with this, the GATT Treaty also provides for certain exemptions to the principle of non-discrimination, the most important of which is contained in Article XXIV permitting GATT signatories to set up regional free trade areas and customs unions, subject to certain criteria. Thus the GATT itself (and now the WTO) has not in principle been antithetical to the idea of regionalism. In the realm of services Article V of the GATS is the counterpart of Article XXIV.

There have been wide-ranging views on the issue of whether regionalism has been detrimental to the spread of multilateralism, and whether the RTAs could even threaten the multilateral ethos. So far the trends in the world economy have been largely positive.

However, to maintain this equilibrium, one must also consider the options in future.

FUTURE TRENDS

1) It seems likely that the current growth of RTAs will be maintained or even increase. Of all the RTAs in existence, only a fraction have been notified. The Committee on Regional Trade Agreements has identified as many as 74 non-notified RTAs, which are in contravention to the provisions on regional integration contained in
the GATT/WTO. It is expected that some of these RTAs will, in due course, be notified to the WTO. While this will increase the total number of RTAs notified to the WTO, the change in status from non-notified to notified RTAs will not change the overall picture. Growth in absolute numbers will come from new RTAs concluded.

If, for example, the practice of the Central European Free Trade Area (CEFTA) Member Countries of concluding separate bilateral RTAs with other trading partners continues, this will contribute to the continuing growth of RTAs. This pattern of each individual member of a plurilateral RTA concluding separate bilateral RTAs with a single country can also be seen in the Americas, where for example, Mexico has concluded a bilateral RTA with each of the Members of the Central American Common Market (CACM). There is also an increasing emphasis on cross-regional trade groupings, example EC-Mexico, EC-MERCOSUR.

2) Membership in existing plurilateral RTAs is expected to grow, e.g. membership in the EC is expected to increase over the coming years, leading to greater complexity as more countries assume the common external tariff of the EC.
3) While membership in existing RTAs is expected to grow, the number of countries participating in RTAs cannot increase much, as a total of 159 countries already participate in RTAs.

4) The increasing incidence of clusters of plurilateral RTAs forming ‘super’ RTAs is likely to grow. Such clusters may act as a precursor to continent-wide RTAs, example the Free Trade Area of the Americas (FTAA). In Africa, this trend is slowly but surely taking shape, with the Economic Community of West African States (ECOWAS) uniting members of other RTAs in the region.

5) It is likely that the number of cross-regional RTAs will continue to grow. The Map (Appendix X) shows existing and potential cross­regional groupings for the year 2000, example, EC-MERCOSUR, EC-Andean Community or EC-Mexico.

RTAs differ substantially in their scope, coverage, and motivation, and hence one cannot pinpoint an explanation for their recent proliferation. However, some common themes do emerge. In particular, the increasing importance of international investment flows of private sector capital, both for developed and the developing countries, has increased the need not just for countries to put the right policies into place, but to provide certainty and credibility as to the direction of future policies and about the economic environment more generally. This is the common thread running
through the theoretical and empirical cause-effect analysis dealt with in the preceding chapter.

RTAs can serve a useful economic purpose over and above, and beyond the direct gains from trade liberalization by reducing uncertainties regarding future national or international economic policies or events; and by enhancing credibility – whether they be of a stable loyal environment in Poland, continued access to US markets for Mexican products, or a ‘local’ market of sufficient size for a new plant, in say Uruguay. In some cases, the reduction in uncertainty resulting from an RTA may even be a necessary precondition to realizing gains from liberalization.

Having looked at an overall positive picture of RTAs, it is important to analyse the workings of the multilateral trading system, and its provisions on RTAs to see how best the two systems can coexist for continued and non-discriminatory expansion of world trade.

The WTO has gone further than regional integration agreements in a number of areas, complementing the process of regional liberalization and extending those disciplines across all current and future trading partners on a global basis. For example, the TRIPS Agreement complements related provisions in regional agreements (most notably in the NAFTA) which cover a limited number of trading partners. The WTO has also been provided with a strengthened dispute settlement system as well as a
monitoring function, which together will bring increased transparency and predictability to trade and economic policies. Consequently, parties to regional integration agreements have ensured – by virtue of being members of the WTO – the adoption of an enhanced set of policies, and procedures for their trade and economic relations, including with respect to each other.

REFORM OF RULES ON REGIONAL INTEGRATION

This takes the analysis to the next crucial question of how adequate are the existing GATT/WTO rules regarding the formation of RTAs? What changes, if any, are required to monitor the current wave of regionalism?

The need to improve the existing GATT rules as set out in Article XXIV was addressed in the Uruguay Round of Multilateral Trade Negotiations. It was also during the period that the fundamental flaws in the provisions on regional integration were pointed out. The Understanding on the Interpretation of Article XXIV of the GATT 1994 seeks to clarify certain provisions, and the WTO deals with RTAs on those premises. With the establishment of the Committee on Regional Trade Agreements to examine and monitor regional integration agreements, there appears to be more coherence as far as their impact-assessment in concerned. However, the task of the CRTA is made difficult by the proliferation of RTAs which have not been notified to the WTO. Their compliance with the provisions
of Article XXIV or the Enabling Clause is difficult to monitor. Besides, there is no regulatory authority within the WTO whereby any Member-country entering into one or more RTAs need necessarily to notify the agreement to the WTO.

Broadly speaking, one can draw six principal conclusions from the study of the impact of regional integration agreements on the pace of international economic integration.

A. Economic integration within an area comprising several countries is not a qualitatively different process from integration within a single sovereign state, hence RTAs do not pose an inherent threat to efforts to promote continued integration on a worldwide basis. More generally, RTAs are not inherently discriminatory or non-discriminatory, but rather depend for their orientation on
i) their detailed provisions; ii) the way in which they evolve; and iii) their influence on the trade policies of third countries.

B. RTAs are only one of several factors that led to the substantial growth of cross-border integration from the 1950s right down to the 1990s. Outside of Western Europe, the story of post-war economic integration (and disintegration at times) can be told with little reference to RTAs.
C. The integration efforts currently under way in Western Europe and North America are likely to have a net positive impact on the pace of international economic integration. Whether or not this assumption turns out to be correct, the world is not witnessing the creation of three well-developed and inward-oriented ‘trading blocs’. Not only does extra-regional trade continue to be very important for Europe, North and South America, and Asia, but the differences between what is occurring in each of these three areas are fundamental, with respect to both existing cross-border relationships and their prospective evolution.

D. Peer pressure is a key ‘enforcement mechanism’ in the WTO and countries generally try to forestall future conflicts by keeping their multilateral obligations in mind when drafting and administering RTAs. As a consequence, *ex post* evaluation and surveillance can have a greater impact on compliance with the rules than is implied by the virtual absence of *ex post* revision to agreements. Implementation of the provisions in the Understanding on the Interpretation of Article XXIV would improve certain aspects of the multilateral surveillance process and more importantly, provide for the first time multilateral rules for the services-related parts of RTAs.
E. While post-war RTAs almost certainly have made a net positive contribution to broader international economic integration, the record to date is less favourable when it comes to careful observance of the multilateral rules in Article XXIV and the efficient functioning of the multilateral surveillance procedures. This record is a cause for concern because i) in the absence of improved compliance (and probably some reform in the rules), one cannot be confident that RTAs will continue to play a supportive role; and ii) the perceived neglect of the rules and procedures for RTAs not only sets questionable precedents, but also has an adverse effect on the credibility of the WTO’s rules and procedures in other areas.

F. Efforts to improve compliance with WTO principles and rules face two challenges:

i) how to improve compliance in the case of free trade areas and customs unions which are driven primarily by economic goals; and

ii) how to improve compliance when the trade provisions are only a part of a larger agreement driven by the pursuit of political goals.

Although the second challenge is a good deal more manageable than the first, the issue of rule credibility makes it important to seek some accommodation that improves the current practice of tacitly looking the other way when Article XXIV comes up against overriding political goals.
To sum up, it is a monumental task to decisively resolve the regionalism versus multilateralism issue. Most renditions of contemporary economic history agree that regional and global liberalization have proceeded together and that they have tended to reinforce each other. The balance of evidence suggests that the interactions have been largely positive throughout the postwar period.