

PASCN Discussion Paper No. 2001-03

## **Existing and Emerging Regional Trading Arrangements**

*Gwendolyn Tecson*



The *PASCN Discussion Paper Series* constitutes studies that are preliminary and subject to further revisions and review. They are being circulated in a limited number of copies only for purposes of soliciting comments and suggestions for further refinements.

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*Gwendolyn Tecson*

University of the Philippines

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September 2001

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## **Abstract**

This study presented selected existing and emerging Regional Trading Arrangements (RTAs) to show key features of the new regionalism and to determine if they help advance the cause of multilateralism. In its assessment, it found that these new RTAs go beyond mere trade in commodities and services and incorporate deeper forms of integration, such as liberalization of investment regimes, adoption of mutual recognition arrangements, and in some instances, harmonization of competition policy. Efforts are made to ensure true integration of national markets. Furthermore, the new RTAs tend to be more outward-oriented than the ones established more than two decades ago. Moreover, a number of them include both developed and developing economies, giving rise to possibilities for greater specialization in production and trade. All these suggest that the new RTAs upon up new opportunities to advance multilateral trade liberalization.

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# Existing and Emerging Regional Trading Arrangements<sup>1</sup>

Gwendolyn Tecson

## Introduction

This paper describes selected existing and prospective RTAs involving some APEC member economies to illustrate key features of the new regionalism and to assess if they help advance the cause of multilateralism. These new RTAs, it seems clear, go beyond mere trade in commodities and services to incorporate deeper forms of integration, such as, liberalization of investment regimes, adoption of mutual recognition arrangements, and in some instances, harmonization of competition policy. Efforts are made to ensure true integration of national markets. Furthermore, the new RTAs tend to be more outward-oriented than the ones established more than two decades ago. Moreover, a number of them include both developed and developing economies, giving rise to possibilities for greater specialization in production and trade. All these suggest that the new RTAs open up new opportunities to advance multilateral trade liberalization.

## Some Empirical Illustrations

Table 1 shows that with a few exceptions, namely, China; Hong Kong, China; Chinese Taipei; Japan; Korea; and Russia, the member-economies of APEC currently belong to one or more sub-regional blocs. In addition, most of them are in the process of establishing formal links with other blocs within and across continents. For instance, presently under study is the feasibility of forming free trade areas between existing blocs like AFTA and CER, or among NAFTA-MERCOSUR-Andean Community and other RTAs in the Western hemisphere. Individual economies, such as, Chile and Korea, have initiated studies and discussions at various fora to explore the possibility of trade-bloc formation.

**Table 1: Sub-Regional Trade Agreements within APEC**

<b>APEC Member-Economy</b>	<b>Sub-regional Integration Arrangement</b>
Australia	CER
Brunei Darussalam	AFTA
Canada	NAFTA; FTAA
Chile	Mercosur; FTAA; Chile-EU
China	
Hong Kong, China	
Indonesia	AFTA
Japan	

<sup>1</sup> The paper forms part of Chapter 2 of the 2000 APEC Economic Outlook Report which deals with the issue on the new regionalism.

Korea	
Malaysia	AFTA
Mexico	NAFTA; Mexico-EU FTA
New Zealand	CER; Singapore-New Zealand CEP
Papua New Guinea	Sparteca
Peru	Andean Community; FTAA
Philippines	AFTA
Russia	
Singapore	AFTA; Singapore-New Zealand CEP
Chinese Taipei	
Thailand	AFTA
United States of America	NAFTA; FTAA
Vietnam	AFTA

What features embodied in the new existing and prospective RTAs can help advance open multilateral trade? To arrive at some tentative answers, the next section looks at the following RTAs: Andean Community, AFTA, CER, MERCOSUR, and NAFTA. It also takes a cursory look at four proposed RTAs, namely, the AFTA-CER FTA, the Free Trade of the Americas (FTAA), the Singapore-New Zealand Closer Economic Partnership, and non-governmental efforts toward a Japan-Korea FTA.

### **Some Features of Existing RTAs**

#### *Comprehensiveness of Trade Liberalization*

The first feature that is examined is the extent to which existing RTAs are consistent with Article XXIV provision on comprehensiveness of trade liberalization.

The Andean Community, formerly known as the Andean Pact, is presently composed of five members Bolivia, Columbia, Ecuador, Peru, and Venezuela.<sup>2</sup> Formed on 26 May 1969, it has been hampered by several factors, including, changes in membership. Chile withdrew in 1976; Peru pulled out in 1992, but rejoined in 1997. Now back on track, the FTA seeks to include all products under tariffs. Furthermore, the group is gearing itself to the formation of a common market by strengthening the liberalization of capital and labor movements inside the bloc. In June 1998, members signed an agreement that would extend liberalization to services trade (Stephenson 1999).

Turning now to the Association of Southeast Asian Nations, ASEAN evolved from a group established in 1967 to encourage cooperation in economic, political, and cultural fields among five members, e.g., Indonesia, Malaysia, the Philippines, Singapore and Thailand. It has since expanded to include Brunei Darussalam, which joined in 1984,

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<sup>2</sup> Information on the Andean Community is derived mainly from its website (<http://www.comunidadandina.org>).

and Vietnam, in 1995. New members joined the group in 1999: Cambodia, Lao-PDR, and Myanmar. Since 1978, when a preferential trade arrangement was put in place, several attempts at encouraging greater intra-regional trade have been attempted but were not successful. Proof is that as late as 1989, only about 3 percent of all goods were eligible for regional trade preferences. But in 1992, with Singapore in the lead, the members undertook a series of talks leading to the creation of the ASEAN Free Trade Area (AFTA).<sup>3</sup> The latter has a timetable for the elimination of tariffs on intra-regional trade covering nearly all sectors, including agriculture, although phase-in periods for some sensitive sectors extend up to 2010, and a small number of sensitive sectors are temporarily excluded. The timetable for completion of the free trade area has been accelerated from 2008 to 2003, then to 2002 for the six original signatories to the agreement on the Common Effective Preferential Tariff (CEPT). By 2000, about 80 percent of all tariff lines in intra-ASEAN trade are tariff free, and 98 percent with less than 5-percent tariff. A limited liberalization of services has also been underway since 1995 (Stephenson 1999).

Mercosur's original members – Argentina, Brazil, Paraguay and Uruguay – are not members of APEC, but Chile is now an associated member of Mercosur. Created in 1991, Mercosur seeks the formation of a common market, with free movement of goods, services, labor and capital. Since the beginning of 1995, a common external tariff has been introduced, with some exemptions to be harmonized over a six-year phase-in period. About 90 percent of intra-bloc trade is currently tariff-free, although some sectors are still exempt until 2000 (Frankel 1997).

The Australia-New Zealand Closer Economic Relations (CER) has its predecessor in a 1965 accord establishing a limited free trade area that removed tariffs on trade in forest products and some manufactures by 1977. In 1983, the two economies decided to expand this accord to include all trade under the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA or CER). It has a comprehensive coverage of trade barriers, touching on nontariff barriers, subsidies, countervailing duties, antidumping, and government procurement. Since 1988, the two members have agreed on national treatment of trade in most services.

On 1 January 1994, the North American Free Trade Agreement (NAFTA) was formed among the US, Canada, and Mexico. NAFTA superseded the previously existing Canada-US FTA (CUFSTA). Earlier, there were bilateral trade agreements between the US and Mexico that covered certain sectors, but involving some trade barriers such as subsidies and countervailing duties. The NAFTA is based on liberalization of goods trade, including agriculture, although for the latter there is a phase-in period of up to 15 years. It also liberalizes investment, services, and intellectual property rights. According to Frankel (1997), rules of origin have hampered some liberalization schedule for textiles and automobiles. Meanwhile, the energy sector is excluded due to Mexico's sensitive oil sector, although it was included earlier in CUSFTA.

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<sup>3</sup> The ASEAN Secretariat based in Jakarta regularly publishes books and monographs about economic and other forms of cooperation in ASEAN.

### *Levels of Protection vs. Nonmembers*

In line with Article XXIV, RTAs should not raise trade barriers against nonmembers any higher than their levels before the trade blocs were formed. But as noted by the World Bank (1999), there is a large difference between many developing economies' applied or actual tariffs and the ceilings of their formal bindings under GATT which makes tariff increases following RTA formation possible. The World Bank study cited Mexico's ability to nearly double tariffs on 503 import items from non-NAFTA economies in 1995 without violating the bindings it has committed itself to under GATT. And in further circumvention of the rules, some economies use contingent protection or technical barriers.

To determine whether regional bloc formation has made member economies more or less protectionist, Foroutan (1998) examined the external trade policies of RTAs involving developing economies. One of her findings shows that Latin American RTAs now exhibit the lowest average tariffs and non-tariff barriers among developing economies in contrast to non-RTA economies that have much less tariff cuts. Moreover, even under the Uruguay Round, Latin American RTA members are found to have reduced their tariffs more and bound more of them than economies that are not members of RTAs.

Although there are indications that RTAs do not necessarily lead to greater protectionism, it cannot be asserted with certainty whether they encourage or hinder multilateral or unilateral liberalization. Foroutan (1998) concludes that there is no causal link between trade liberalization and RTA membership. The reason behind this is that there are examples of both liberalizing economies that had not belonged to any regional arrangements and members of effective FTAs that did not liberalize.

However, it can also be argued that belonging to an RTA can, in some cases, provide the stimulus for a country to liberalize its trade regime. The liberalization programs undertaken by other members in the regional bloc may provide the 'demonstration effect' needed by members that are still hesitant to adopt such policy reforms. Virtually tariff-free Singapore in AFTA provides an example of such effect. Moreover, the positive experience associated with trade liberalization with a smaller set of partner economies in a regional bloc may provide the confidence needed by policymakers to embark on liberalization programs on a wider, multilateral scale. The experience of New Zealand is a case in point. The initial fears of opening up its markets to Australia, a bigger, more economically advanced partner in a free trade area severely limited the scope of liberalization, thus constraining the effectiveness of earlier trans-Tasman trade agreements. However, as both Australia and New Zealand became more confident with outward-oriented policies, commitments made under the original CER were strengthened and the scope of the agreement was even extended to new areas of international commerce (see Bureau of Industry Economics 1995). Moreover, both economies undertook a substantial program of trade liberalization that reduced the high levels of protection accorded to their agricultural and manufacturing sectors. Such demonstrations of the possibilities of achieving the dynamic effects of bloc-formation

itself--such as, productivity improvements, scale economies, increased FDI--served as lessons to CER itself and to economies outside the regional bloc to move farther away from continued application of protection policy. In the case of the Philippines, one of the reasons for the adoption of a uniform tariff policy of 5 percent by 2004 is the avoidance of the trade-diverting effects of AFTA once the CEPT comes into force.

Evidently, economies belonging to sub-regional groups within APEC are also those that have put in place a number of policy initiatives that have led to more, rather than less, trade liberalization in relation to non-member economies. They are at the forefront of initiatives to restart a new round of WTO negotiations, even after attempts to do so have failed at Seattle. Apart from a new round, it can also be said that the Cairns Group (led by Australia and which includes as members a number of developed and developing agricultural exporters within APEC), the US, and MERCOSUR are spearheading the mandated negotiations on agriculture within the GATT-WTO framework, to tackle the issues of agricultural protection (see [www.wto.org](http://www.wto.org)).

### *Timelines of Liberalization*

Article XXIV of the GATT specifies that “any interim agreement shall include a plan and schedule for the formation of such a customs union or of such a free trade area *within a reasonable length of time*” (italics supplied). According to the “Understanding on the Interpretation of Article XXIV of the GATT,” the “*reasonable length of time*” means ten years. In the case of the 1994 Bogor Declaration, APEC Leaders have committed to open trade and investment in the Asia-Pacific region by 2010 for developed member-economies of APEC and 2020 for developing member-economies. The sub-regional groups within APEC are aiming at earlier deadlines for liberalization, for example, 2005 for the Andean Community to complete its customs union and 2010 for the original ASEAN members and 2015 for the four new members. The CER economies have already achieved full trade liberalization, and the Singapore-New Zealand Closer Economic Partnership envisages removal of all tariffs by 1 January 2001. Moreover, arrangements have been made to allow for periodic reviews of compliance with the scheduled liberalization.

The Bogor Declaration has taken APEC on the route to liberalization earlier than has been achieved under the multilateral negotiations of GATT-WTO. In the meantime, there are signs that sub-regional blocs within APEC can catalyze liberalization between participating economies in advance of the Bogor deadlines.

### *Intra- vs. Extra-regional Trade*

A fear that RTAs may serve as stumbling blocks to multilateral free trade stems from the possibility that their formation may bring about increased intra-bloc trade at the expense of nonmembers. Some authors, to show the tendency of regional blocs to divert trade into the region, have used simple intraregional trade as a proportion of the region’s total trade with the world. However, as Frankel (1997) notes, this measure is flawed because it is dependent on the absolute size of the regional bloc. If, for example, APEC

showed a much higher ratio (0.74 in 1994) than the Andean Community (0.10 in 1994), it may simply be because the former comprised a large group of economies that has a large share of the world economy, and hence, would inevitably trade a lot with each other. A way to correct this is to divide the intraregional trade share by the region's share of world trade<sup>4</sup> (Table 2).

**Table 2: Intra-regional Trade Concentration Ratios,  
1962 - 1994**

<b>RTA</b>	<b>1962</b>	<b>1965</b>	<b>1970</b>	<b>1975</b>	<b>1980</b>	<b>1985</b>	<b>1990</b>	<b>1994</b>
Andean Community	0.29	0.69	1.57	2.63	3.37	4.41	8.06	12.63
Mercosur	2.45	6.42	5.57	3.82	6.14	4.84	9.07	12.84
ASEAN 6	9.57	9.22	8.22	4.86	4.08	5.11	3.98	3.60
NAFTA	1.63	1.76	1.93	2.17	2.08	1.95	2.09	2.20
CER								
EU 15	1.24	1.28	1.33	1.41	1.47	1.58	1.51	1.63
APEC	1.64	1.69	1.82	1.86	1.82	1.74	1.76	1.63

Source: Table 2.2 in Frankel 1997.

One important observation is that the regional blocs generally tend to trade more intensely within the bloc than with the rest of the world, as shown by the concentration ratios that are greater than one. This may be due to a large extent to geographical proximity, since trade tends to be greater among economies that are geographically close to one another, whether or not there is a formal regional arrangement. However the question arises as to why such a trend seems to be rising for some (especially for the Andean Community and MERCOSUR), falling for others (ASEAN-6) and quite flat for still others (APEC). Clearly, this cannot be due to changes in geographical proximity. This suggests that trade is becoming “more regionalized over time in some parts of the world” (Frankel 1999, p. 31). However, whether this is due to the formation of RTAs in these regions or to other policies is not clear.

Using a gravity model, Frankel has tried to isolate the effect of forming a regional trading bloc from other variables that determine bilateral trade, such as, market size, per capita income, bilateral distance, common borders, and common languages. His results show that belonging to a trade bloc is significant only for the Andean Community, Mercosur, and CER. The case of Mercosur<sup>5</sup> is interesting in that the bloc effect is insignificant during 1965-75, but after that it rises and becomes statistically significant especially after 1990. In the case of the Andean Pact<sup>6</sup>, the bloc effect is insignificant

<sup>4</sup> The figures then show whether there is a tendency for the region to concentrate trade within the region. If regional trade were according to geographic patterns that are proportionate to the distribution of world trade, then the concentration ratio would be equal to one. Ratios greater than one then indicates a trade is concentrated within the region. It should be pointed out that the data utilized have their limitations: (1) the results may be distorted to a greater or lesser extent by the performance of the dominant economy or economies in the group; (2) the data analyzed end in 1994, which means that they do not reflect the full effects of the Uruguay Round and other liberalization efforts.

<sup>5</sup> Chile is excluded in this estimation.

<sup>6</sup> Again Chile is excluded in membership of the Andean group, but includes Peru.

(negative) and becomes significant (positive) only after the reinvigoration of the Andean Pact in 1992. On the other hand, the bloc effect for ASEAN depends on whether other bloc effects are tested simultaneously. When the East Asian bloc effect is introduced, the strong bloc effect for ASEAN disappears, implying that ASEAN trades strongly intra-regionally only because most Asian economies do so. The effect of NAFTA, however, is almost never significant, even in 1992 when it was negotiated. However, this may be due to the small number of observations in Frankel's study (p. 91).

Frankel's results are somewhat mitigated by the results of Soloaga and Winters (1999) who test if the formation of new RTAs influenced trade in the nineties. They find a positively significant trend in the estimated coefficients for bloc members' overall imports only for MERCOSUR, not for the Andean Community. For ASEAN, the Soloaga-Winters study indicates that the intra-bloc trade coefficient is negative, especially between 1987 and 1995 and that the bloc's propensity to import from bloc members is even significantly lower in 1995-96 than in 1986-88 and 1980-82. For NAFTA, Soloaga and Winters confirm Frankel's results that intra-bloc trade coefficients are insignificant. The implication is that there is no appreciable impact of NAFTA formation either on intra- or extra-bloc trade when gravity variables are simultaneously present. Meanwhile, a study by Yeats (1997) shows disturbing signs that MERCOSUR's intra-regional trade is growing most rapidly in areas where the member economies are not internationally competitive and that domestic producers are re-orienting exports to local markets to take advantage of higher prices associated with more restrictive trade barriers.

Overall, the evidence does not seem supportive of the thinking that RTAs increase intra-regional trading activity at the expense of nonmembers. For AFTA and NAFTA, regional bloc formation has not prevented member-economies from trading with the rest of the world once gravity variables are taken into consideration. A World Bank study (1999) has likewise concluded that there is no evidence that regional agreements are a stumbling block toward multilateral trade liberalization, although it also says that it has found no compelling evidence that RTAs have served as stepping stones for multilateral liberalization.

#### *Trade Creation vs. Trade Diversion*

A major apprehension about RTAs pertains to trade-diversion effects away from nonmembers. The Soloaga and Winters study provides evidence of trade diversion only for EU and EFTA, but for other RTAs, they find that trade-creation exceeds the trade-diversion effects.

This is corroborated by CGE modeling studies undertaken by different authors at various time periods (see Table 3 from De Rosa 1998). For AFTA, two studies show basically trade-creating effects on a net basis. Two CGE models of MERCOSUR report that regional bloc would be ex-ante trade creating, even without a modest trade diversion. Meanwhile, Chile's accession to either MERCOSUR or NAFTA is seen to be beneficial, though not significantly, to Chile by the study of Hinojosa-Ojeda, Lewis, and Robinson

(1997). But a study by Harrison, Rutherford, and Tarr (1997)<sup>7</sup> suggests that Chile would benefit from accession only in NAFTA, not in Mercosur. The results for NAFTA likewise show net positive welfare effects, in varying degrees, depending on the assumptions of the studies.

These studies thus tend to allay the fear about the trade-diversion effects of the new regionalism.

### *Open Access to New Members*

Another way by which regionalism can be rendered supportive of multilateralism is if, according to Kemp and Wan (1976), nonmember economies are allowed to join regional blocs that are being formed. This would make the FTA an ever-expanding bloc, thereby tending to improve welfare of economies at every stage. In other words, there must be open access in membership. While possibilities for enlargement do not necessarily constitute total openness, there is a greater chance for regionalism to contribute to multilateralism if the regional bloc is receptive to admitting nonmembers, rather than shutting them out.

In the case of the Andean Community, there have been efforts to create a free trade area with MERCOSUR. Indeed, the formation of a free trade zone by 1 January 2002 has just been announced after a summit of twelve South American economies in Brazil in early August this year. Moreover, the Andean Community has been active in the launching of negotiations for the establishment of the Free Trade Area of the Americas (FTAA) that will link in an FTA agreement the entire Western hemisphere, with the exception of Cuba.

AFTA has expanded in the 1990s to include three more economies in Indochina, namely, Cambodia, Lao PDR and Myanmar. It has also been in dialogue with East Asia (Japan, South Korea and China), holding “ASEAN-Plus Three” meetings following the Manila Summit of 1999. Meanwhile, CER has shown interest in linking up with other regional groups, of which the most developed initiative is the AFTA-CER Linkage. AFTA and CER Ministers agreed in October 2000 to work toward a Closer Economic Partnership between the two groupings, taking account of recommendations made by a high-level task force.

In the case of MERCOSUR, a free trade zone is being formed with the Andean Community. Moreover, an accord with EU was agreed upon in December 1995 to establish an FTA by 2001 (see <http://worldbank1.org>). About membership, Chile has been an associated member since 1996, while Bolivia has been accepted as a member in December 1996. Peru has expressed interest in forging an FTA with MERCOSUR. Chile is pursuing free trade agreements with South Korea and the European Union, and it has

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<sup>7</sup> The Harrison, Rutherford and Tarr (1997) study, however, differed from other multi-country CGE models since it used an import-demand elasticity of substitution of 30, based on the rationale that in the long-run of about ten years or more, consumers will take every opportunity to substitute lower-priced imports for higher-priced ones, assuming that they are very similar.

already signed bilateral trade agreements with Canada, Mexico, Bolivia, Colombia, Ecuador, Peru, Venezuela and Central America (Costa Rica, Guatemala, Honduras, El Salvador and Nicaragua).

Even NAFTA, which initially rejected new members, does not seem to be averse to linking up with other economies and regional blocs (Hufbauer and Schott 1996). Indeed, preliminary talks held in Florida with other blocs in the Southern hemisphere centered on the possibility of forming the FTAA.

Evidently, there are afoot initiatives to link different existing regional blocs with one another or economies with either other economies or other regional blocs. Some observers are worried about a division of the world into three blocs (FTAA, an Enlarged EU, East Asian-CER FTA) that might stall the move toward multilateral free trade. However, since the linkages being mulled are between regional blocs or by economies across continents (e.g. Mercosur-EU, NAFTA-EU or the Transatlantic FTA, Mexico-EU; Chile and Korea, Singapore and Mexico, Singapore and New Zealand), the likely outcome seems more consistent with an ever-expanding bloc that is moving closer to a multilateralized world.

#### *Toward Deeper Integration*

Experience with trade liberalization has shown that integration of national markets cannot come about only with integration through trade (often referred to as shallow integration). This is because trade has become highly complementary with other areas, such as, services trade, investments, government procurement, and other policies (say, those bearing on competition, intellectual property), all of which have to be harmonized in order to bring about greater integration of national markets. For instance, Australia and New Zealand have realized that antidumping problems could be eliminated with harmonization of their competition policies, or that mutual recognition arrangements (MRAs) seem necessary so that technical standards do not serve as non-tariff barriers to goods trade.

All the sub-regional integration arrangements within APEC appear to go beyond preferential trading arrangements and incorporate deep integration arrangements. The Andean Community and MERCOSUR, envisaging the formation of common markets, both have provisions for the eventual free movement of labor and capital. AFTA, on the other hand, has evolved a number of commitments on liberalizing services trade (the ASEAN Framework Agreement on Services), investments (ASEAN Investment Area), and trade facilitation, from the adoption of a harmonized tariff nomenclature to the harmonization of products standards for priority sectors and development of sectoral or product-specific MRAs. CER looks quite mature at this stage; it covers a number of deep integration arrangements. It provides for free trans-Tasman trade in all services, with the exception of a number of services subject to existing government regulations at the time. Trade facilitation has led to standards harmonization, adoption of MRAs, quarantine harmonization, and customs harmonization. Successful harmonization of competition policies between Australia and New Zealand has led to a breakthrough in terms of

removing the possibility for applying anti-dumping procedures against each other. Moreover, harmonization is taking place in business laws and intellectual property rights. NAFTA embodies WTO-plus features, such as, pacts on investment, intellectual property rights, services, and labor/environment.

### *Other Issues*

Admittedly, RTAs still have to address a number of important issues that create stumbling blocks to the achievement of multilateral free trade. But most of these issues are not yet fully resolved even in the WTO.

*Non-tariff Barriers:* While there is a general agreement on the objective of removing tariffs on goods trade, some regional groups have remained quite vague on the issue of non-tariff barriers (Frankel 1997). In particular, most of the regional blocs (except perhaps CER, which has strengthened, instead, competition policy between the two members) retain the possibility of imposing contingent protection, especially the use of antidumping duties on bloc members. Within MERCOSUR, Argentina has lodged 33 antidumping cases against Brazil between 1992 and 1996 (Tavares and Tineo 1997, cited in World Bank 1999). In NAFTA, Canada and US have not abandoned the possibilities for anti-dumping against each other (Gagné 2000). In agricultural trade, some trade-retarding issues remain to be addressed. For instance, the application of sanitary and phytosanitary standards (SPS), which though science-based, may be applied in such a manner as to constitute a nontariff barrier to trade.

*Standards:* Efficient systems of standards serve to reduce the costs of doing business. On the other hand, standards may be used to limit market access and thus serve as technical barrier (Findlay 2000). This has been the case with EU until the landmark ruling of the International Court of Justice on MRAs. Among the options for adopting common standards among member economies are harmonization and mutual recognition.

*Services Trade:* The specific sub-regional RTAs, including, APEC member-economies seem to envisage liberalization in all or most goods, generally in line with Article XXIV. However, the freeing of services trade even among members has not proceeded at the same speed as that in goods trade, in spite of GATS V. On the other hand, since mid-1990s services trade liberalization has been manifesting itself not so much at the multilateral as at the national and sub-regional levels (Stephenson 1999, p. 2). In particular, the efforts at services trade liberalization in APEC and FTAA are being cited as important complements to the multilateral effort under GATS. Several reasons have been cited why RTAs may offer a complementary route to liberalization under the GATS: (1) labor mobility may be involved in service liberalization, and it may be more politically acceptable if limited to RTA members rather than achieved in a non-discriminatory manner; (2) quality standards must be set for which procedures must be drawn up, and again this might be much more easily achieved within an RTA (World Bank 1999).

Even then, practically speaking, the inclusion of services under APEC's "early voluntary sectoral liberalization" (EVSL) is turning out to be problematic in the light of the recent Asian crisis. In the case of FTAA, a liberalizing modality will have to be agreed upon before the rules and disciplines can be written up, and an agreement can only become effective after 2005 (Stephenson 1999).

*Rules of Origin:* While necessary to avoid trade deflection in the case of free trade areas, rules of origin (ROO) have nevertheless been used to hinder rather than hasten the achievement of free trade within RTAs. They can be restrictive enough to cause member economies to source high-priced intermediate inputs from other member economies due to local content requirements attached to the rules of origin. Alternatively, they might drive member economies to increase value adding, even though inefficient, just to be able to take advantage of free trade within the bloc. This has been the concern of New Zealand with regard to its textiles, clothing, and footwear industries and has, therefore, sought reductions in the CER local content requirements for duty-free entry into Australia (BIE 1995, p. 20). Moreover, even the implementation of the ROO can be made so complex, as the in the case of NAFTA with its 200 pages of documentation on ROO. ROOs must therefore be made more transparent and straightforward so as not to become an instrument of protection within an RTA.

### **Prospective RTAs and Other Initiatives**

The burst of regionalism in the 1990s does not seem to have abated. The stalled attempts to start a new multilateral round of negotiations in Seattle have only served to fan more interest in RTAs, perhaps, as an insurance protection against the risk of failure at the multilateral front. New RTA initiatives are underway to form trade blocs within and across continents.

One initiative proposes to create a free trade area between the members of two existing FTAs, namely, AFTA and CER. A high-level task force was established by Ministers from AFTA and CER in October 1999 to examine the feasibility of an AFTA-CER FTA. The members of the task force have found it both feasible and advisable to form such an FTA for the political and economic benefits that it will bring. Its report is referred to as the Angkor Agenda 2000. Ministers from ASEAN and CER considered the Angkor Agenda at a meeting in Chiang Mai, Thailand, on 6 October 2000. They agreed to work towards a Closer Economic Partnership (CEP) between the two groupings, taking into account the recommendations of the Angkor Agenda and other issues relevant to closer economic integration. Senior officials will report back to the Ministers with recommendations in October 2001.

The content of a future CEP will be decided by ASEAN and CER Ministers. Nonetheless, it may be useful to examine the shape of the economic integration arrangement proposed in the Angkor Agenda. Among others, the task force proposed that:

- a. The AFTA-CER FTA would represent a separate arrangement which would be comprehensive, covering all goods, services, and investments, and would lead to the elimination of all forms of tariff and non-tariff barriers to trade in goods and services. AFTA and CER would maintain their respective identities;
- b. The pace of liberalization within the AFTA-CER FTA should proceed faster than that agreed within APEC. The AFTA-CER FTA would not normally go beyond the pace of liberalization which AFTA has already agreed for ASEAN members, i.e. elimination of tariffs for manufactured goods by 2010 for ASEAN-6 and 2015 for the four newer members, with some flexibility. CER would progressively reduce tariffs for ASEAN from the conclusion of negotiations, reaching free trade by 2005;
- c. The proposed FTA should provide development assistance in the form of capacity-building measures and technical assistance and the adoption of a longer time-frame for the newer members of ASEAN; and
- d. The AFTA-CER FTA would be open to accession by any other country or regional grouping.

Representing the largest integration effort involving developed and developing economies, the Free Trade Area of the Americas (FTAA)<sup>8</sup> is envisaged to formally link up all the 34 economies of the Western Hemisphere – with the exception of Cuba – into a free trade area. The information reported here is sourced mainly from the proceedings of the 1997 Summit of the Americas held in Brazil. Formal negotiations began in March 1998 and will conclude no later than 2005. Its common objective is that of achieving free trade and investment in goods and services; it is envisioned to be fully WTO-consistent, specifically with Article XXIV and GATS V. However, the goal of deeper integration is envisaged in areas not presently under WTO, such as, a common investment regime, government procurement, and competition policy. For this purpose, nine negotiation groups have been set up: (1) market access; (2) investment; (3) services; (4) government procurement; (5) dispute settlement; (6) agriculture; (7) intellectual property rights; (8) subsidies, antidumping and countervailing duties; and (9) competition policy. The envisioned arrangement specifically professes the principle that the construction of the FTAA will not raise barriers against nonmembers and will continue to avoid to the greatest extent possible the adoption of policies that adversely affect trade in the hemisphere. In consideration of the differences in the levels of development and size of participating economies, the negotiations will ensure the integration of the smaller economies so that they will be able to benefit equally from the trade liberalization. A novel feature of the FTAA is that it will allow elements of civil society to make their views known on issues to be negotiated. A Committee on Civil Society will be created to facilitate the input of the business community, labor, environmental, and academic groups on issues under negotiation.

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<sup>8</sup> Information on the FTAA is mainly derived from [www.alca-ftaa.org](http://www.alca-ftaa.org).5

Negotiations between Singapore and New Zealand have led to the forging of an “Agreement Between New Zealand and Singapore on a Closer Economic Partnership.” As described in the agreement document, all tariffs will be eliminated upon entry into force. A number of arrangements have also been agreed upon touching on non-tariff barriers. For instance, all export subsidies on goods, including those on agricultural products, will be prohibited under CEP. Anti-dumping provisions have been retained, but are based on the WTO anti-dumping agreement, with changes that marginally tighten the thresholds before anti-dumping investigations can be started. With regard to services trade liberalization, schedules set out each country’s initial commitments, in line with the APEC objective of free and open trade in services by 2010. A meeting between the two economies is scheduled for 2007 to identify the services sectors or measures that Singapore or New Zealand may not be able to liberalize fully by 2010. The CEP Agreement goes beyond trade matters and incorporates deeper-integration features, such as, on investments, technical, SPS regulations and standards, government procurement, and intellectual property. Openness to new members is assured, as the CEP includes a provision that enables any other member of the WTO or any other state or separate customs territory to accede or associate itself with the Agreement, subject to agreement of New Zealand and Singapore. Robust dispute settlement procedures have been agreed upon. The CEP also provides for a periodic review of the CEP to take place every five years.

Even East Asia, which had not known any RTAs in the past, seems to be nursing thoughts about creating some. On May 23, 2000, the Institute of Developing Economies, JETRO of Japan and the Korea Institute for International Economic Policy (KIEP) issued a joint communiqué to present the results of their study on the feasibility of creating a free trade area between Japan and Korea. The idea is based on the need for closer economic relations between the two economies, articulated during a visit to Japan in October 1998 of President Kim Dae Jung who declared with Prime Minister Keizo Obuchi an “Action Plan for the New Korea-Japan Partnership for the 21<sup>st</sup> Century”. As proposed by the study, the FTA will aim at a comprehensive framework to encompass an array of market-integration measures, such as investment promotion, trade facilitation, and harmonized trade and investment rules and standards, in addition to eliminating tariffs and non-tariff barriers to trade between the two economies. The communiqué explicitly mentions that FTAs are “increasingly being regarded as a pragmatic approach to achieving global liberalization”. Deep integration arrangements, therefore, are being envisioned. Bilateral cooperation is one important avenue to maximize the benefits of the FTA, so that both sides have emphasized the need for it, particularly, in industry and technology fields. There is a proposal by KIEP to establish a Korea-Japan Investment Development Bank to encourage the investments and thus reap the dynamic benefits that accrue from them. Korea, however, seems to maintain a cautious attitude on the establishment of an FTA, but KIEP sees the creation of a development bank and a committee for technical cooperation.

And even as Japan and Korea are contemplating the idea of an FTA, both economies are each in the process of talking with different trade partners: Korea with Chile, Israel, New Zealand; and Japan on non-governmental level with Singapore,

Mexico, and Chile. In particular, the proposed Japan-Singapore FTA will be a “new age FTA” in that it envisions going beyond the traditional WTO-consistent trade liberalization, investment promotion, MRAs on rules and standards, together with effective ROO and safeguard measures.

In sum, the new initiatives in forming more sub-regional trading arrangements within the APEC appear to embody the features that make regionalism not only supportive of multilateralism but may even surpass it in terms of results. While being WTO-consistent, they go beyond trade and into deeper forms of integration not yet covered by WTO negotiations, such as, competition policy and e-commerce.

**Table 3: Quantitative Studies of Regional Integration Arrangements**

<i>Researchers</i>	<i>Description Model</i>	<i>Sectors Included</i>	<i>Economies</i>	<i>Change in Economic Welfare; Percent of Annual GDP</i>
<b><u>NAFTA</u></b>				
Bachrach & Mizrahi (1992)	Ex-ante, CGE, perfect competition for Mexico & USA with differentiated products, constant returns to scale, inter-industry flows, 1988.	36 trade goods sectors, 8 services sectors. Primary factors of production, including capital, labor and energy resources.	Mexico USA	0.32 0.02
Brown , Deardoff & Stern (1992)	Ex-ante, CGE, imperfect competition with differentiated products, increasing returns to scale, inter-industry flows. 1989	23 traded goods sectors, 6 non-traded goods sectors. Capital and labor perfectly mobile between sectors but internationally mobile.	Canada Mexico USA Rest of world	0.70 1.60 0.10 (0.00)

<i>Researchers</i>	<i>Description Model</i>	<i>Sectors Included</i>	<i>Economies</i>	<i>Change in Economic Welfare; Percent of Annual GDP</i>
Roland-Horst, Reinert & Shiells (1992, 1994)	Ex-ante, CGE, imperfect competition with differentiated products, increasing returns to scale, inter-industry flows. 1988.	26 sector aggregation, with 20 tradable sectors. Capital and labor domestically mobile between sectors but internationally immobile.	Canada Mexico USA	10.57 3.38 2.07
<b><u>ASEAN Free Trade Area (AFTA)</u></b>				
De Rosa (1995)	Ex-ante, CGE, perfect competition with differentiated products, constant returns to scale and inter-industry flows. 1988.	27 sectors including a non-traded sector. Capital specific to individual sectors; labor mobile between sectors. All primary factors internationally immobile.	Indonesia Malaysia Philippines Singapore Thailand	0.23 1.30 0.41 3.86 0.56
Lewis & Robinson (1996)	Ex-ante, CGE, perfect competition with differentiated products, constant returns to scale and inter-industry flows. 1992	12 sectors, including one service sector. Primary factors (capital, land two types of labor) domestically mobile between sectors but internationally immobile	Indonesia Malaysia, Singapore Philippines Thailand China Korea Taiwan Japan USA EU	0.03 0.04 0.14 0.18 (0.01) 0.00 0.00 0.00 0.00 0.00
<b><u>MERCOSUR</u></b>				
Flores (1997)	Ex ante, CGE, imperfect competition with	9 sectors with 5 sectors identified as imperfectly	Brazil Argentina NAFTA	0.10 0.11



<i>Researchers</i>	<i>Description Model</i>	<i>Sectors Included</i>	<i>Economies</i>	<i>Change in Economic Welfare; Percent of Annual GDP</i>
<b><u>Asia Pacific Free Trade Area</u></b>		specific to individual sectors; labor mobile between sectors. All primary factors internationally immobile.		
Lewis, Robinson & Wang (1995)	Ex-ante, CGE, perfect competition with differentiated products, constant returns to scale, inter-industry flows, labor migration. 1990.	Production factors (capital, land, two types of labor) domestically mobile between sectors but internationally immobile.	USA Japan China ASEAN-4 Asian NIEs Rest of world EU	0.04 0.74 0.13 0.36 2.44 0.05
<b><u>Western Hemisphere Free Trade Area</u></b>				
Hinojosa-Ojeda, Lewis & Robinson (1997)	Ex-ante, CGE, perfect competition with differentiated products, constant returns to scale, inter-industry flows, labor migration. 1990.	11 sectors, including services sector. Capital, land, 4 types of labor domestically mobile between sectors. Unskilled labor mobile between US and Mexico.	USA Mexico Argentina Brazil Chile	0.00 0.23 0.13 0.12 0.14

UTR (unilateral trade liberalization): tariffs reduced to optimum level estimated at about 8%.

Source: Table 3 of De Rosa (1998); Roland-Horst, Reinert & Shiells (1994).

## **Conclusion**

The work here has not attempted to introduce new issues about RTAs. It merely reviewed and tried to update existing issues. The motivation for the update on the debate about RTAs stems mainly from the expectation that RTAs are here to stay, judging by the new initiatives being announced. In APEC, the concern is how to make sure that existing and prospective RTAs, particularly, when some of its member economies are involved, promote open multilateral trade.

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