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**Proliferation of FTAs and the WTO**

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## I. Introduction

Global financial and economic crisis, which was triggered by the Lehman shock in September 2008, has had enormous negative impacts on the global economy. Global GDP growth rate became negative in the fourth quarter of 2008 and continued negative through the third quarter of 2009, while global trade in goods and services is projected to register -11 percent in 2009<sup>1</sup>. The magnitude of the decline in economic activities was so huge that this crisis has been characterized as “once in a century” crisis, comparable only to the Great Depression in the 1930s.

This crisis, which began in the US, spread to the rest of the world mainly through two channels. One is the financial market, where supply of financial resources declined, thereby resulting in slowing down of economic activities. The other channel is foreign trade. As demand for imports in the US, which absorbed huge amount of imports from the rest of the world, especially from East Asia, before the crisis, declined, the countries, whose dependence on exports to the US was high, suffered tremendously.

Faced with the global financial and economic crisis, G-20 Leaders’ meeting was convened in November 2008, to discuss the ways to deal with the crisis and to find the way for recovery. They called for joint actions on expansionary macroeconomic policy as well as appropriate financial regulation measures. Furthermore, the leaders confirmed the importance of not resorting to protectionist policies.

Responding to the expansionary fiscal and monetary policies, many countries, especially those in East Asia, started to recover in 2009. The situation on protectionist policies is quite different. Although most measures do not violate WTO rules, many countries, including the G-20 countries, have adopted a variety of trade distorting

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<sup>1</sup> IMF, World Economic Outlook, October 2009.

protectionist measures, which include the increase in applied tariff rates to the level below the bound rates, provision of government subsidy to troubled companies, etc. These protectionist measures undoubtedly distort trade flows, causing inefficiency in the allocation of resources.

One would expect that the introduction of these protectionist measures slows down and eventually stops, as economic recovery takes hold. However, it is not clear if these protectionist measures will be rolled back to the pre-crisis situation because industries protected by these measures would oppose the rollback. If not, litigation accusing violation of the WTO rules is likely to arise.

The application of these protectionist measures could have been avoided, if the WTO rules prohibit these protectionist measures. Despite these limitations, the WTO played a role of restraining the WTO members from adopting obvious protectionist measures such as raising the tariff rates beyond the bound rates that are outright violation of the WTO rules. Indeed, there is a view that the presence of the WTO contributed to economic recovery by avoiding the beggar-thy-neighbour measures like those adopted during the Great Depression period.

The global trading environment would have been more favourable to open and free trade, if the WTO rules had been better established by dealing with the gray protectionist measures. Improvement of the WTO trading system requires successful WTO multilateral trade negotiation. However, the current round of multilateral trade negotiations under the WTO, or Doha Development Agenda (DDA), has been deadlocked. There are a number of problems behind this stalemate such as the decision making system, issue coverage, treatment of developing countries, and others. The controversy over agricultural trade policy between the US and India was the direct cause of the breakup of the DDA in July 2008.

Faced with the deadlock in the DDA, many countries have turned to free trade agreements (FTAs), under which trade barriers are removed between and among the member countries, with a like-minded country (countries) concerning trade liberalization. The interest in region-wide FTAs has increased in East Asia after the crisis, as the East Asian countries realized the importance of reducing their dependence on the US and European countries, to avoid the negative impacts of another crisis. Since an FTA violates the most favoured nation (MFN) treatment of the WTO members, one of the fundamental principles of the GATT/WTO, a surge of FTAs may undermine the global trading system. It is known that global trade liberalization under the WTO is the best policy for the world as a whole and that an FTA is at best the second best policy. As such, policy makers have to make every effort to revive and conclude the DDA. However, at the same time, it is important to make an assessment of FTAs and try to formulate the policies that would turn FTAs into global FTA or WTO liberalization, once one realizes that FTAs are not going to go away in the near future.

With these observations in mind, in the remaining parts of the paper I will first review FTA developments in the world with a focus on East Asia, then I assess the FTA developments from theoretical as well as empirical perspective. In the course of the discussions on the factors leading to the proliferation of FTAs, I will discuss some of the problems facing the WTO. I will then discuss possible ways of making FTAs turn into WTO trade liberalization. I will conclude the paper by presenting a few remarks.

## II. Growing Bilateralism and Regionalism in the World and in East Asia

FTAs have recently received a lot of attention in trade policy discussions. This section reviews recent developments in FTA formation. In addition to observing the increasing trend of FTA formation, I discuss the reasons behind the trend.

## II.1 Proliferation of FTAs in the World

The number of regional trade agreements (RTAs) began to increase notably in the 1990s (Figure 1).<sup>2</sup> The pace of the increase accelerated in the mid-1990s. Recognizing that FTAs, which violate the most-favored-nations treatment among the GATT/WTO members, one of the principles of the GATT/WTO system, the speedy spread of FTAs after the establishment of the WTO, which was set up to improve the world trading system under the GATT, is ironic and also reflects difficult problems facing the newly established WTO<sup>3</sup>. As of October 2009, the cumulative number of FTAs in force reported to the GATT/WTO stood at 195. Among the many FTAs, the North American Free Trade Agreement (NAFTA) involving the United States, Canada, and Mexico had significant impacts on the rest of the world. The establishment of the NAFTA was seen by the rest of the world as the change in the US policy toward FTAs, as the US appeared to have pursued the multilateral approach toward trade liberalization under the GATT. This impact was substantial because the open and free

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<sup>2</sup> RTAs include free trade agreement (FTA) and customs union. Under FTA FTA members remove tariff and non-tariff barriers on trade among the members while they maintain their own tariff and non-tariff barriers on trade with non-members. Under the customs union the members establish common tariff and non-tariff policies on their trade with non-members, in addition to free trade among the members. Since FTAs are dominant among RTAs and a relatively small number of RTAs are customs unions and since most if not all RTAs involving East Asian countries including Japan are FTAs, in this paper “FTAs” are used to mean RTAs unless otherwise stated.

<sup>3</sup> In the GATT/WTO, regional trade agreements (RTAs), which violate one of its basic principles of non-discrimination, are permitted under GATT Article XXIV with several conditions, which include liberalization of substantially all the trade of the members, not increasing trade barriers on non-members, and completing the RTA process within ten years. For developing members, more lenient conditions are applied under the enabling clause.

US economy, the largest economy in the world, was regarded to play a pivotal role in the open global trading system.

Several reasons can be identified behind rapid expansion of FTAs in recent years. First, an increasingly large number of countries have become unsatisfied with the WTO mainly because of the two reasons, turning to show an interest in FTAs. One is slow progress in multilateral trade liberalization and the other is limited coverage of WTO rules. Let us briefly discuss these points.

Many countries realize the benefits of trade liberalization as it has brought them economic growth<sup>4</sup>. Indeed, one of the important factors that led to rapid economic growth for many countries in the WWII was substantial trade liberalization carried out under the auspices of the GATT. However, multilateral trade liberalization has become increasingly difficult to be carried out because of disagreement among the GATT/WTO members, which have increased to exceed 150.

The Uruguay Round, which was the last multilateral trade negotiation of the GATT, started in 1986 and was scheduled to reach agreement within four years. However, it took twice as long as the initial schedule (eight years) to complete the round. After the WTO was established in 1995, developed countries demanded for launching a new round, but the opposition from developing countries, which were not satisfied with the outcome of the Uruguay round prevented the WTO from starting a new round. It was the end of 2001 when they actually agreed to start a new round (Doha Development Agenda, DDA). Although the DDA started, there was very little progress and indeed it was stopped in July 2008. The direct cause of the suspension of the DDA was the disagreement on agricultural liberalization between the US and India, but there are other reasons such as dissatisfaction of many members about the DDA.

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<sup>4</sup> See, for example, World Bank (1993).

As was indicated earlier, increasingly large number of the WTO members has made it difficult to pursue negotiations, as decision making in the WTO negotiations requires consensus. Besides the large number of the members, various alliances such as the Cairns Group, G-20, Friends of Agriculture, etc, which represent different interests, have been formed, making the process of negotiation (or pre-negotiation) tenuous. One can also argue that the increasing opposition to globalization has made it difficult to pursue trade and liberalization under the WTO. Globalization has allegedly affected some groups negatively in the forms of reduction in employment opportunities, deterioration in environmental problems, and others. Indeed, in 1999 in Seattle, the WTO ministerial meeting, whose aim was to form consensus for starting a new round, was unsuccessful mainly because environmentalist groups, labor unions and NGOs aggressively held anti-WTO demonstrations. Even after the WTO Seattle meeting, these groups have been carrying on radical campaigns against World Bank/IMF conferences, G-7 summits and other conferences that seemed to support globalization.

Some WTO members are not satisfied with the coverage of the issue areas under the WTO. The coverage of international economic activities expanded under the WTO from the GATT, where the coverage was limited to goods trade. The WTO expanded to include trade in services, investment, intellectual property rights, and others which have become important in international economic activities. Although the expansion of the coverage is a major achievement, there still are various areas which are not covered under the WTO. Some of them include environment, labor standard, movement of natural persons and e-commerce.

Many WTO members that are not satisfied with the slow progress in multilateral trade negotiations and/or limited coverage of the WTO have opted for bilateral and plurilateral FTAs with like-minded countries. Indeed, many FTA



negotiations have been concluded within short time period because of the small number of participants. For example, Japan-Singapore FTA negotiations practically took approximately ten months. To deal with the limited coverage of the WTO, many FTAs have included areas such as labor and environment.

Proliferation of FTAs was inflicted by the Domino effect, in that one FTA led to another. Because an FTA is a discriminatory trade arrangement, a country that is excluded from the FTA has an incentive to form its own FTA. A case in point was the NAFTA, which led to the formation of the EU-Mexico FTA, which in turn resulted in the formation of the Japan-Mexico FTA. European firms keen on expanding exports to Mexico found themselves in a disadvantageous position vis-a-vis US firms, who have free access to the Mexican market because of the NAFTA. These European firms put pressure on their governments to establish an FTA with Mexico, leading to the EU-Mexico FTA. The same story can be told behind the Japan-Mexico FTA.

## II.2 Expansion of Bilateral and Mini-lateral FTAs in East Asia

East Asia was not active in the formation of FTAs until the turn of the century. (Table 1) Indeed, ASEAN (Association of Southeast Asian Nations) Free Trade Area (AFTA), which was established in 1992, was the only major FTA until Japan and Singapore enacted Japan–Singapore FTA (formally named a New Age Japan-Singapore Economic Partnership Agreement, JSEPA) in 2002<sup>5</sup>. However, the situation changed dramatically in recent years. Many countries in East Asia began to form FTAs with the countries not only in the region but also outside the region.

At the beginning of the FTA expansion period in East Asia bilateral FTAs such as the Japan-Singapore and Chile-Korea FTAs were actively established. However, the

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<sup>5</sup> For discussions on FTAs in East Asia, see for example, Aggarwal and Urata (2006), Urata (2005), and Sally (2006).

situation changed when China approached the ASEAN to form a mini-lateral China-ASEAN FTA, treating the ASEAN as a group. Responding to the China-ASEAN FTA, Japan quickly approached the ASEAN to form a Japan-ASEAN FTA. Korea, India, Australia-New Zealand individually followed these movements to set up an FTA with the ASEAN. As of mid-November 2009, the ASEAN has enacted FTAs with China, Japan, Korea and it is expected to enact FTAs with India, and Australia-New Zealand sometime soon. These developments indicate that the ASEAN has become a hub of FTAs in East Asia as an FTA involving China, Japan and Korea, the three largest economies in the East Asian region has not been established. Indeed, no official discussions of such trilateral FTA have been initiated.

Two initiatives for establishing a region-wide FTA covering East Asian countries have emerged, one covering ASEAN ten countries, China, Japan and Korea, or ASEAN+3 countries (East Asian FTA, EAFTA) and the other including ASEAN+3 countries, India, Australia and New Zealand, or ASEAN+6 countries (Comprehensive Economic Partnership in East Asia, CEPEA). EAFTA was proposed by an expert group that was set up to study a future vision of East Asia, while CEPEA was proposed by Japan. Feasibility studies of these two initiatives were conducted by the private sector study groups (track two groups) consisting of researchers from the respective member countries. Following the recommendations of the study groups, the ASEAN+3 Leaders and ASEAN+6 Leaders agreed to begin official discussions in 2010.

The factors behind active formation of FTAs in East Asia are similar to those discussed above for the explanation of the proliferation of FTAs in the world. In addition, East Asian countries have regarded FTAs as an important regional policy instrument. For example, China and Japan approached the ASEAN for the formulation of FTAs to deepen their economic and non-economic relationship with the ASEAN

with a hope to increase their influence in the region. Non-economic motives can also be found for active FTA policy for the ASEAN, Korea, India, Australia and New Zealand.

Two important features of implemented and proposed FTAs in East Asia may be noted. One is the inclusion of economic cooperation as an important component and the other is low level of trade liberalization. One of the distinguishable characteristics of the East Asian region is wide diversity in the level of economic development among the countries. In such a region reducing the development gap is important for achieving economic growth as well as social and political stability. In order to achieve this objective, economic cooperation has become a central part of EAFTA and CEPEA. Although it is commonly understood that FTAs with high level of trade liberalization is desirable for achieving economic growth in the long run, many FTAs in East Asia have adopted a pragmatic approach of excluding politically sensitive sectors from trade liberalization. One notable case is the exclusion of agriculture from trade liberalization in many FTAs, most evidently in the case of FTAs involving Japan.

While East Asian wide initiatives were being discussed, the US proposed an FTAAP, or Free Trade Area of the Asia-Pacific covering 21 APEC member economies in 2006. Behind the US proposal of an FTAAP is a concern that the US would be excluded from East Asia. It should be noted that the differences in the members between ASEAN+6 and APEC give rise to important implications of the groupings. Taiwan and Russia, important economic players, are included in an FTAAP but not in ASEAN+6, while India, a member of ASEAN+6, is excluded from FTAAP.

### III. FTAs and Global Trade Liberalization under the WTO

The previous section saw increasing active formation of FTAs in recent years in the world and in East Asia. Policy makers as well as researchers have shown concerns that FTAs become stumbling blocs to global trade liberalization under the WTO. This section provides a brief summary of the discussions of the impacts of FTAs on the WTO<sup>6</sup>. Let me first discuss positive arguments about FTAs and then turn to the negative arguments.

Some of the factors behind the proliferation of FTAs, which were discussed in the previous section, can be considered as positive factors toward global trade liberalization. They include speedy negotiation and broader coverage of issue areas. FTAs involving small number of members are likely to be able to conclude negotiations in a shorter time period compared to the WTO negotiations with 150+ members. Many FTAs have gone beyond the commitments at the WTO (or WTO plus commitments) by including, for example, liberalization in foreign direct investment, movement of natural persons, etc. Besides, they include trade and FDI facilitation, whose progress at the WTO has been slow. FTAs may contribute to trade liberalization at greater scale compared to the WTO liberalization. Under FTAs import tariffs are to be removed either immediately or within a certain time frame, while under the WTO negotiation gradual tariff reduction is pursued. FTAs may contribute to WTO negotiations as FTAs reduce the influential power of the opposition group against trade liberalization. Finally, the domino effect of FTAs, which was discussed to have contributed to the proliferation of FTAs in the previous section may eventually lead to global trade liberalization by consolidating FTAs into global trade liberalization. Somewhat from a different perspective and somewhat contradictorily, one may argue that proliferation of FTAs may lead to global trade liberalization as disintegration of

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<sup>6</sup> See, for example, Ravenhill (2006) for the discussions on these issues.

the global trading system caused by FTAs makes policy makers realize the importance of open global trading system.

Let us turn to negative aspects of FTAs, which would deter global trade liberalization. FTAs may divert the attention of bureaucrats, politicians, business people, and general public away from global trade liberalization. For example, business sector may lose interest in further liberalization, if it obtains trade liberalization in the sector in the country of its interest with an FTA. The domino effect was argued to contribute possibly to global trade liberalization, but it may contrarily deter global trade liberalization. The domino effect may lead to proliferation of FTAs with different rules of origin, giving rise to a “spaghetti bowl” effect that leads to the breaking up of the global trading system into a number of disintegrated groupings.

#### IV. Economic Impacts of FTAs

In the previous sections we saw that FTAs are increasing and we found theoretically the impacts of FTAs on multilateral negotiations are ambiguous. In this section we analyze the economic impacts of FTAs on FTA members and non-members. Such analysis would be useful in formulating FTA and multilateral trade liberalization policies.

##### IV.1 Economic Impacts of FTAs

One can classify the economic impacts of FTAs into two groups: static effects and dynamic effects.<sup>7</sup> Static effects are “trade creation effects,” “trade diversion

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<sup>7</sup> The analysis here is intended to give concise explanation of the major points and therefore lacks theoretical rigor. For a detailed analysis of the economic impacts of RTAs, that is customs unions and FTAs, see, for example, Baldwin and Venables (1995).

effects” and “terms of trade effects,” while the dynamic effects include “market expansion effects” and “competition promotion effects.”

“Trade creation effects” result from the elimination of trade barriers among FTA members and, therefore, the new trade created among them, resulting in an improvement in resource allocation. “Trade diversion effects” address the ways that FTAs replace highly efficient products of non-member countries by imports from less efficient FTA members. In general and from the viewpoint of FTA members, “trade creation effects” have positive impacts while the impacts of “trade diversion effects” are ambiguous.

The analysis of trade creation and trade diversion effects above can be applied to a small country, which does not have any influence on international prices or the terms of trade. As such, the terms of trade effect of FTAs is not considered in the above analysis. For a large country or a large FTA group consisting of FTA member countries, the formation of an FTA enables a large country or a large FTA group to gain as it improves its terms of trade by expanding trade between FTA members at the expense of its trade with non-members.

Beyond the economic impacts of FTAs on their members, it is important to recognize that the static impacts of FTAs on non-FTA members are negative. Non-FTA members suffer from welfare loss because trade diversion effects reduce the level of their exports to FTA members and because the terms of trade effect would reduce non-members’ welfare as the terms of trade for non-FTA members deteriorate. Indeed, as was discussed above, the emergence of negative impacts of FTAs for non-FTA members leads to FTAs, resulting in the proliferation of free trade agreements, as non-FTA members try to cope with the negative impacts by creating new FTAs or joining existing FTAs.

As for the dynamic effects of FTAs, both market expansion effects and competition promotion effects contribute to economic growth of FTA members. “Market expansion effects” involves expanded market size needed to achieve efficient production/distribution and economies of scale. “Competition promotion effects” result from market integration in ways that would make regionally oligopolistic industries more competitive thus achieving higher productivity through the introduction of competitive pressures. For non-FTA members these effects are likely to have positive impacts as economic growth of FTA members tends to promote the exports of non-members to the members.

The theoretical analysis of the impacts of an FTA on FTA members and non-members is shown to be ambiguous, that is could be positive or negative. Having noted this ambiguity, if negative impacts would arise, it would be non-members that are likely to suffer from negative impacts, as they are discriminated against. In light of these observations the next section reviews empirical studies that examine the impacts of FTAs on members as well as non-members.

#### IV.2 Empirical Analysis of Welfare and Trade Impacts of FTAs

Two types of empirical research have been conducted to examine the impacts of FTAs on members and non-members. One is a simulation analysis using computable general equilibrium (CGE) models, and the other is to use econometric analysis. The former is characterized as ex-ante analysis, while the latter as ex-post analysis. Each approach has its strengths and weaknesses.

A CGE model is constructed to mimic the actual working of the economic system by specifying activities of economic agents such as producers, consumers and governments. A typical CGE model covers the world consisting of a number of

countries and a number of sectors. The most popular CGE model used for the analysis of FTAs is the GTAP (Global Trade Analysis Project) model. The strength of the CGE model is its theoretical consistency and comprehensive coverage in that it captures all economic impacts through the market mechanism including inter-industry and inter-country impacts of policy changes such as FTAs. At the same time, there are several weaknesses. One is the difficulty in constructing a model that reflects the actual economic system. For example, a typical CGE model assumes perfect competition. Although the perfect competition assumption may not be appropriate in many cases, a lack of knowledge on the type of actual competition forces researchers to make the perfect competition assumption. Another problem is the difficulty in obtaining appropriate data and parameters used for the model. Indeed, the more detailed and realistic the model becomes, the more difficult it is to obtain the appropriate data. The third problem is that the results of CGE model cannot be tested statistically, in order to evaluate the validity of the results.

A number of simulation exercises have been conducted to investigate the possible impacts of FTAs by using CGE models.<sup>8</sup> Indeed, it has become customary to conduct a CGE model simulation when policy makers formulate FTA policies. The results of CGE studies show two common trends. First, FTA members are shown to gain in terms of economic welfare and GDP, while non-FTA members generally lose. These findings are consistent with the theoretical predictions. For example, Scollay and Gilbert (2001) obtain the following results from their analysis of an FTA comprised of ASEAN, China, Japan, Korea, Australia, and New Zealand. All the members gain in terms of economic welfare, while non-members such as the US, the EU and Taiwan lose. The world as a whole is shown to gain. Similar patterns of gains

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<sup>8</sup> See Ando and Urata (2007) for a survey of the CGE studies on East Asian countries.



and losses are found by Ando and Urata (2007), who examine the static as well as dynamic impacts of FTAs involving East Asian countries using the GTAP model.

Another general trend observed from the results of CGE simulation studies has to do with the number of FTA members or the country coverage. Generally, it is observed that the greater the number of FTA members, the larger the gain from an FTA. This can be seen by comparing the results of FTAs with different country coverage using the same model. Scollay and Gilbert (2001) find that the welfare gains for the world as well as FTA members tend to increase through wider coverage of countries under liberalization as the coverage of FTAs change from a group consisting of ASEAN, China, Japan, Korea, Australia, and New Zealand to a group of economies belonging to APEC and then to all the countries in the world. A similar pattern was observed by Ando and Urata (2007). These observations are consistent with the theoretical analyses in that the scope for trade creation increases and the scope for trade diversion declines with the number of FTA members.

An econometric analysis of the impacts of FTAs typically examines the impacts of FTAs on foreign trade. Specifically, the gravity model, which is constructed on the assumption that the magnitude of bilateral trade depends on the economic size of the two countries and the distance between them, is estimated to examine the trade creation and diversion effects of FTAs. One weakness of the econometric approach in the FTA analysis is its inability to incorporate simultaneous changes in a number of policy variables. For example, econometric analysis finds it difficult to deal with simultaneous removal of tariffs in many sectors from many countries, as they result in a complicated interplay of the effects. Another problem is the difficulty in dealing with a large change such as the removal of tariffs under FTAs, which tends to have

substantial impacts not only on trade but also on other economic activities such as production and employment, which in turn would affect trade.

Similar to the case of CGE model studies, a number of gravity model estimations have been conducted to examine the impacts of FTAs on foreign trade. Many studies found that FTAs promoted intra-FTA trade, indicating the presence of the trade creation effects. For example, Frankel (1997) conducted a gravity model estimation covering 63 countries in the 1965-94 period with a variety of different model specifications. He finds that intra-regional trade in Western Europe, East Asia, APEC, and the Western Hemisphere is significantly higher than the predicted values. A recent study by Baier and Bergstrand (2007) reports very significant trade creation effects as they find that an FTA approximately doubles two members' bilateral trade after 10 years.

Relatively few studies examined the presence or absence of the trade diversion effect. Urata and Okabe (2007) analyze the impacts of selected FTAs on trade by explicitly considering trade between FTA members as well as trade between FTA members and non-members. Their results indicate the presence of trade creation effects for most FTAs they study. Specifically, out of 11 FTAs they examine, only three FTAs, ASEAN-China, Singapore-Japan, and Singapore-US, were found to have no significant trade creation effect. As to the trade diversion effect, five out of 11 FTAs were shown to have significant trade diversion effects. These findings indicate that FTAs tend to promote trade between and among FTA members, implying that FTAs are welfare enhancing for FTA members, while FTAs may divert trade away from non-members, reducing welfare of non-members.

## V. Multilateralizing FTAs

In terms of economic welfare it is global or multilateral trade liberalization under the WTO that is optimum and thus regionalism or FTAs are at best the second best policy. Despite their second best nature, FTAs are not going to go away. Recognizing this observation, what we need to do is to formulate the ways how FTAs may be turned into global trade liberalization.

At least two approaches can be considered, one is to consolidate FTAs to establish an FTA with a greater number of FTA members. One such example is consolidation of Japan's bilateral FTAs with individual ASEAN members to create a Japan-ASEAN FTA. In this case Japan plays a pivotal role. If the contents of Japan's bilateral FTAs with individual ASEAN members are similar, the consolidation is not that difficult. However, consolidation is very difficult if the contents of FTAs are different and the number of FTAs involved in the consolidation is large. In the case of establishing a Japan-ASEAN FTA, tremendous resources appeared to have been used for the negotiation. Indeed, it looked as if the members had to set up a new FTA, as the contents of individual FTAs were quite different.

Another approach is to enlarge an FTA by accepting a new member or a group of members. This approach may be characterized as merging or docking. An example is the EU enlargement. This accession process may require less resources and time compared to consolidation because it is only the new member that requires adjustment. In Asia-Pacific, P4 or Trans-Pacific Strategic Economic Partnership Agreement (TPP), which include Brunei, Chile, Singapore and New Zealand, may be able to play a pivotal role. Indeed, at present Australia, Peru, the US, and Vietnam have shown interest in joining TPP.

A core FTA, with which new members will be merged or docked, has to have several important features. The core FTA has to be of high level in terms of trade

liberalization, in order to contribute to achieving free and open global trading environment. The rules such as those on the rules of origin should be simple and transparent, so that the implementation and usage of the core FTA as well as merging or docking with the core FTA can be done smoothly. In order to facilitate an accession by new members, the conditions for accession should be clearly defined and indicated.

Having discussed the possible ways of turning FTAs into global trade liberalization, it is going to take time. In the meantime, many developing countries, especially those in Sub-Sahara Africa are likely to be excluded from the FTAs involving major countries. To deal with the problems arisen from discrimination, these low-income countries should be given an market access to the developed and emerging developing countries through preferential schemes such as the Generalized System of Preferences.

Finally, it should be emphasized that global trade liberalization has to be promoted in order to reduce discriminatory effects of FTAs.

## VI. Concluding Remarks

The ongoing global financial and economic crisis revealed both the strength and weakness of the global trading system under the World Trade Organization (WTO). The presence of the WTO prevented the crisis-ridden countries from adopting highly protectionist policies like those adopted during the Great Depression years, thereby contributing to relatively speedy recovery. Having noted the strength of the WTO, the WTO could not stop the countries from adopting protectionist measures, which were not outright violation of the WTO rules but did have trade distorting impacts. Many of these protectionist measures could have been avoided if the WTO had been successful in strengthening and improving its rules and their implementation. Once economic

recovery is more or less achieved, these protectionist measures may be rolled back. If not, litigation on these measures is likely to be initiated at the WTO, and then they will be phased out.

One important “protectionist” measure, which is likely to stay or even increase after the recovery, is regional preferential trade agreements such as free trade agreements (FTAs). FTAs started to increase rapidly before the crisis, but the pace of the increase appears to have accelerated because of the crisis. The trend is likely to continue if the DDA does not get restarted. Some observers argue that proliferation of FTAs undermines the global trade system under the WTO, while some others argue that the stalemate of the WTO’s Doha Round negotiations is a contributing factor to the proliferation of FTAs. Knowing that FTAs is not the best policy but at the same time that they are likely to stay with us for sometime to come, I argued in this paper that FTAs should be merged/docked to the core FTA. Once a core FTA is set up and the countries begin to join the core FTA, many countries would follow to join the core FTA in order to avoid negative impacts from discrimination. In Europe, the EU is a core FTA as it increased its members remarkably over time. In the Asia-Pacific region the TPP may play that role.

In order to facilitate merger of FTAs with a core FTA, a core FTA has to have high-level in terms of trade liberalization and simple and transparent rules. G-20 countries may become core members in a core FTA. Having discussed the possible contribution of the enlargement of a core FTA toward multilateral trade liberalization, efforts have to be made to promote multilateral trade liberalization. In this regard, G-20 may make contributions by setting up G-20 trade ministers’ meetings to discuss trade issues.

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Figure 1 FTAs in the World

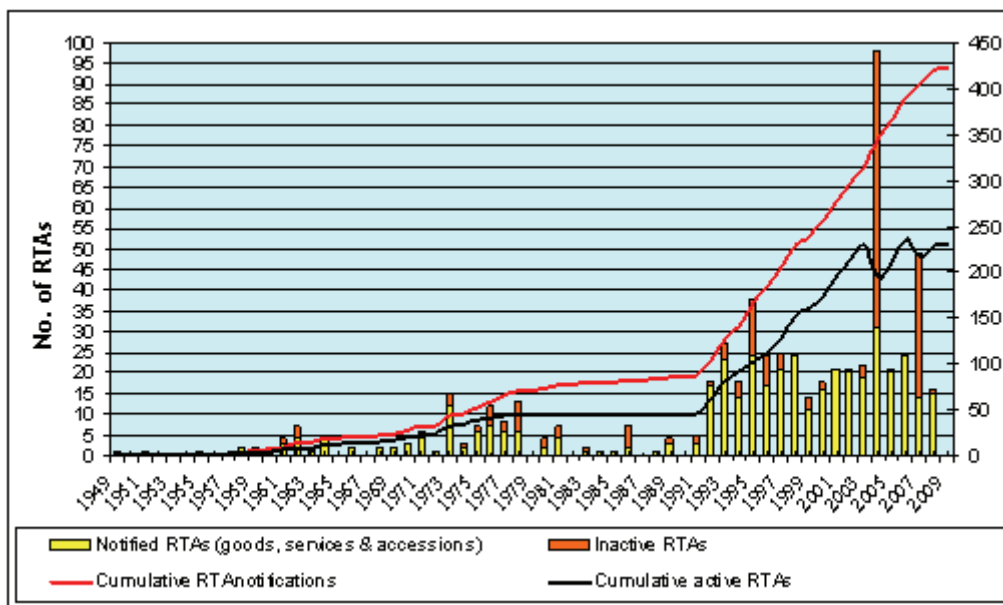


Table 1 Major FTAs Involving East Asian Economies (as of August 2009)

| In effect                  |                         | In negotiation  |                    |
|----------------------------|-------------------------|-----------------|--------------------|
| Bangkok Treaty(1976)       | Singapore-India(2005)   | Japan-Korea     | China-Singapore    |
| AFTA(1992)                 | China-Chile (2006)      | Japan-GCC       | Malaysia-Australia |
| Singapore-NZ (2001)        | Korea-Singapore(2006)   | Japan-Vietnam   | Malaysia-NZ        |
| Japan-Singapore (2002)     | Japan-Malaysia(2006)    | Japan-India     | Malaysia-Pakistan  |
| Singapore-Australia (2003) | Korea-EFTA(2006)        | Japan-Australia | Malaysia-US        |
| Singapore-EFTA (2003)      | Korea-ASEAN(2006)       | Korea-US*       | Singapore-Canada   |
| Singapore-US (2004)        | Singapore-Panama(2006)  | Korea-Canada    | Singapore-Mexico   |
| Korea-Chile (2004)         | Japan-Chile (2007)      | Korea-India     | Singapore-Egypt    |
| China-Hong Kong (2004)     | Japan-Thailand (2007)   | Korea-Mexico    | Sigapore-Qatar     |
| China-Macao(2004)          | China-Pakistan (2007)   | Korea-EU        | Singapore-Peru     |
| Singapore-Jordan(2004)     | Japan-Philippines(2008) | China-Australia | Thailand-EFTA      |
| Japan-Mexico (2005)        | Japan-ASEAN(2008)       | China-NZ        | Thailand-India*    |
| China-ASEAN(2005)          | Japan-Indonesia(2008)   | China-GCC       | Thailand-US        |
| Thailand-Australia(2005)   | Japan-Brunei(2008)      | China-Pakistan  | ASEAN-CER*         |
| Thailand-NZ(2005)          |                         | China-SACUFTA   | ASEAN-India*       |

Notes: \* indicates that treaty has been signed and waiting for the ratification by the legislative bodies.

Source: WTO website and respective government sources.



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