

**Regionalism in the Multilateral Trade Regime**

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## **I. Introduction**

“Acting like termites, PTAs are eating away at the multilateral trading system relentlessly and progressively” (Bhagwati, xii). The preferential trade approach, at the center of debate in recent years, has important implications for the international trade policy arena. Reports estimate that preferential trade arrangements (PTAs) cover anywhere from one-third to one-half of total world trade (WTO Annual Report 2002 and World Bank 2003). Despite the lack of agreement in the exact numbers, it is safe to say that a substantial share of world trade is controlled by PTAs. The trend of increasing proliferation of PTAs is a point of agreement among the international community.

Many of the scholars who have written on the subject of regionalism have focused on the implications of PTAs and do not focus on answering the question of why there is such a prevalence of PTAs in the first place. It is mostly mentioned in passing but not analyzed in depth. Because a substantial share of world trade is taking place outside of the jurisdiction of the WTO, it has been difficult for the WTO to understand this proliferation and how best to promote the interests of an increasingly discriminatory trade system. Perhaps the answer to this question will be able to contribute to the identification of policy solutions on how to manage this phenomenon as well as how to ensure that countries use the preferential approach to strengthen, rather than undermine, the multilateral trade regime.

The purpose of this Capstone will be to analyze why free trade agreements have become so prevalent, examine the literature in depth, and draw conclusions as to what role regional integration agreements (RIAs) should play in the international trade

regime—should regionalism be allowed to prevail over multilateral efforts in the quest for free trade?

Scholars list a myriad of reasons as to why free trade agreements exist. Some of them include protectionist means, political goals such as creating spheres of influence or integration, and the “impulse” to achieve integration like that of the European Union. But what have been the most influential factors in the most recent proliferation? There are many facets that may help to explain the prevalence of preferential trading arrangements. Factors at the domestic, international, regional, and multilateral levels must be taken into consideration. According to the research, the most influential factors for the proliferation of RIAs seem to be the shift in American and European economic policy, interdependence in an increasingly globalized economy, influence of special interests at the domestic level, and legal flaws at the GATT/WTO level. The paper is structured as follows: a brief review of the literature regarding the regionalism versus multilateralism debate, a historical overview of the existence of PTAs, a statistical profile of the agreements, the role of the United States and Europe in the current proliferation in triggering a chain reaction, influence of special interest groups, legal issues within the GATT/WTO, perceived political factors, and future recommendations for the WTO.

## **II. The Debate**

Multilateralism can be defined as the method to achieving free trade based on non-discrimination, implying the participation and inclusion of as many countries as possible in the trade liberalization process. Regionalism, on the other hand, is loosely defined by Winters as “any policy designed to reduce trade barriers between a subset of countries regardless of whether those countries are actually contiguous or even close to

each other” (Winters 2-3). Winters’ definition of regionalism is functional for the purposes of this paper. It is important to note that the preferential trade policy approach is inherently discriminatory. Even though it eliminates trade barriers for the participating countries, the countries that are excluded are disadvantaged. Because the external trade barriers of participating countries remain the same, outsider countries experience increased competition from those who produce in the participating countries (Bhagwati 17). “So FTAs are two-faced: they free trade among members, but they increase protection against nonmembers” (Bhagwati 17). This distinction is important in the analysis of FTAs because they do not constitute part of “free trade.” Free trade arrangements do not, in fact, result in free trade. The differing methods being used to liberalize trade—the latter discriminatory, while the former is not—raises many questions and is the basis for debate among the international community. Does regionalism conflict with the free trade agenda or can it complement multilateral efforts? Will regionalism undermine the international trade system and make it harder to manage? What does this mean for the World Trade Organization and its eroding role in the international trade policy arena?

Many scholars argue that “free trade” agreements threaten to undermine multilateral trade negotiations (MTN) as it lessens the incentive to conclude them. Scholars such as Bhagwati, Wolf, and Viner claim that the negative effects of regional trade agreements override any positive effects that it may have. Effects such as trade diversion and the gradual corrosion of the World Trade Organization’s (WTO) authority and relevance must be avoided if the trade regime is to advance and prosper. Others argue that trade blocs such as the European Union have created a model that has become

very influential in taking free trade to a level never before seen. However, the European Union is the only regional agreement that has been deeply committed to integration. Another perspective is espoused by renowned economist L. Alan Winters, who concludes that regionalism may be an effective but risky strategy in reaching progress at the multilateral level. Regionalism is coercive in nature therefore countries feel the need to join RTAs to avoid the costs of exclusion (Winters 58). To avoid the costs of exclusion, countries may be persuaded by influential RTA members to pursue deeper integration. Other scholars such as David Henderson claim that “open regionalism,” where the developed countries allow open membership of the lesser developed countries (LDCs), is favorable as it promotes the integration of developing countries into the global economy (Trade Blocs 132). Others argue that the presence of free trade agreements actually harm developing countries and hinders economic development. Because bilateral trade treaties are difficult to create, negotiate, and implement, it can sometimes result in poor use of government resources and poor policymaking in the lesser developed countries. Also, rules of origin often disadvantage low income countries since they usually need to import many of the materials for their export products (Baldwin and Thornton xii-xiii).

Rules of origin are emphasized as one of the primary components of regionalism that causes inefficiency in international trade. Bhagwati, along with several other economists, believe that inefficiency caused by rules of origin result in the “spaghetti bowl” phenomenon. Because the participating PTA countries have separate external tariffs, the countries are too preoccupied with determining which products originated within the free trade area and what constitutes home country origin. This creates a

system that is too technical and bureaucratic, which takes the focus away from trade liberalization. In Bhagwati's words: "As PTAs proliferate, the main problem that arises is the accompanying proliferation of discrimination in market access and a whole maze of trade duties and barriers that vary among PTAs" (Bhagwati 866).

### **III. Historical Overview**

After World War II, when establishing a new international economic regime, many policymakers were traumatized by the economic policy experience during the 1930s, where many countries resorted to beggar-thy-neighbor, protectionist policies that ultimately resulted in the Great Depression. Following the war, citizens and policymakers alike shied away from the policies that caused the deterioration of the international economic regime. With the exception of the European project, policymakers embraced a new order based on multilateralism, trade liberalization, and non-discrimination.

Another historical event that set the stage for the current proliferation of preferential trade arrangements was the first wave of regionalism in the 1960s. Many countries were influenced by the integration project of Europe at the time and they attempted to follow suit. However, the movement was not nearly as successful as the current wave, or rather the Second Regionalism. Because of the growing popularity of import substitution policies among developing countries, developing countries expressed interest in the FTA route to take advantage of economies of scale to reduce the high costs of such policies (Bhagwati 29). This was the exact opposite of the economic integration project in Europe, and instead was an attempt to control trade from within. Instead of liberalizing trade to promote comparative advantage specialization, Latin American

countries tried to do the reverse. They attempted to arbitrarily choose the products in which to specialize to stimulate trade (Bhagwati 30). Latin American countries quickly realized that import substitution policies were a wasted investment. As the most influential economic power in the world after the United States, examination of European events that occurred in the lead-up to the Second Regionalism in the early 1990s should prove enlightening in the endeavor to discover the reasons why regionalism was able to proliferate.

Various scholars also believe that the First Regionalism was not successful because the United States was committed to multilateralism and non-discrimination in the international trade structure; the U.S. had not forgotten the tough lesson it had learned regarding protectionism and the Great Depression. The U.S. only overlooked the discriminatory aspects of European integration because of strategic political and security interests in combating communism during the Cold War. Thus, the U.S. influenced other developed countries to refrain from enacting preferential trade relations throughout the Kennedy Round. Despite U.S. support for European integration, the U.S. made it clear that it disapproved of the European Free Trade Area, a discriminatory arrangement (Bhagwati 30-31). The Second Regionalism, on the other hand, has been extremely successful. Analysis of the United States role in the multilateral regime will be crucial to uncovering the factors that created and nurtured an enabling environment for preferential trade.

The new regionalism has distinctive qualities that set it apart from the first wave. During the First Regionalism, agreements were usually between industrial economies or among developing countries. This new regionalism is characterized by an ever-

increasing complex combination of agreements between developing, transition, and developed economies. The current proliferation also consists of cross-regional alliances while the old regionalism was based on geographical proximity (Das 64). Another unique characteristic is that countries can belong to multiple RIAs; there is no obligation to remain exclusive to a specific PTA alliance. Also, Das is of the opinion that trade liberalization at the multilateral level has contributed to the emergence of new RIAs, especially among developing and transition economies. Increased foreign direct investment (FDI) in particular has been a contemporary feature in this new period that had not been present previously. Developing countries are now more invested in the multilateral trade system and their strengthened participation has become a huge factor in the proliferation of PTAs. The increasing complexity of regional integration agreements in the new era, summarized briefly in this section, is discussed in more detail in below.

#### **IV. Statistical Profile of Regional Trade Agreements and Emerging Trends**

Examining the statistical landscape will uncover certain trends in the current proliferation that are worth noting. The statistical trends will provide a basis for further analysis of certain themes throughout the paper. During the past two decades, the share of global trade covered under regional trade arrangements has increased significantly.

“As of 1 November 2008, 418 regional trade agreements have been notified to the GATT/WTO, 227 of which are currently in force” (WTO 2008). The failure to finalize the Doha Round may have important implications, as it highlights the increasing gap between discriminatory and free trade avenues to liberalizing trade (Fiorentino et al. V). This proliferation is even more significant if one takes into account the number of operational PTAs that have not been notified to the WTO, which is approximately 70 as



of 2006. The 30 agreements that have been negotiated but are not yet operational as well as the 65 RTAs that are in the negotiation stage are also important to consider. Also, approximately 30 RTAs are in the proposal stage, where countries have expressed interest in entering negotiations in the near future (Fiorentino et al. 5). If all of these categories are taken into account, there will be about 400 regional trade arrangements present in the international trade arena.

According to the statistical data, PTA proliferation began in the 1990s and has risen exponentially since. Evidence indicates that free trade agreements, which are a subset of regional trade arrangements (RTAs), make up 84 percent of operational RTAs that have been reported to the WTO. Partial scope agreements and customs union agreements account for 8 percent each. Of the expected RTAs that will come into force, 92 percent are meant to be free trade agreements, 7 percent will be partial scope agreements, and only 1 percent intends to become CUs. This indicates that free trade arrangements are best meeting the strategic policy needs for a given country (Fiorentino et al. 5). Countries' inclination to implement FTAs indicates that they prefer certain characteristics that FTAs have, such as speed and flexibility. The attraction that the FTA holds is that it allows countries flexibility to pick and choose the goods and services covered as well as its partners. Countries' ability to select their partners in any given arrangement seems to hold particularly true in the explanation to the current wave of cross-regional FTAs, which have tended to focus on "strategic market access or strategic political alliances, unbound by geographical considerations." FTAs do not necessarily have to be comprehensive in scope (Fiorentino et al. 6). This flexibility gives countries the ability to control trade policy over excluded parties, thus preserving their sovereignty

(Fiorentino et al. 6). The trend of the FTA design, however, demonstrates that countries are now favoring protectionist policies. This trend has serious implications for the current trade regime and will most likely impede future multilateral trade rounds if FTAs are allowed to continue existing unchecked. WTO provisions require that FTAs liberalize trade substantially but this rule is mostly ignored by the international community. A study of the overseer of the current international trade system will be crucial to meeting the objectives of this paper.

Customs unions (CUs) on the other hand seem to be less desirable because it requires a sacrifice of sovereignty by member countries. Because a customs union goes beyond an FTA to include the implementation of a common external tariff, it restricts member countries' ability to exercise the full range of trade policy instruments. CUs represent the "traditional objective of regional integration among geographically contiguous countries" such as the European Union or MERCOSUR. It is apparent that the current trade environment has made it politically infeasible to comprehensive integration projects. In regard to partial scope agreements, they are not very desirable to those committed to broad trade liberalization as it only covers a small amount of trade and partners are limited due to WTO statutes (Fiorentino et al. 7). Partial scope agreements have very limited economic or political benefits and are therefore seldom used. However, many partial scope agreements are used as a first step toward eventually becoming a free trade arrangement.

Another important aspect of the RTA landscape is that bilateral and cross-regional RTAs are currently increasing while the amount of plurilateral agreements has decreased. Bilateral agreements make up 80 percent of all operational, reported regional trade

arrangements, 94 percent of the concluded arrangements and those under negotiation, and all of the RTAs at the proposal stage (Fiorentino et al. 8). This indicates that countries currently do not have many incentives to negotiate with more than one country, predicting negative implications for the future of multilateralism. Countries are signing random, hastily designed free trade agreements that are making the trade system a bothersome and unpredictable environment in which to navigate. In the long-run, countries will most likely have to pay the price for such decisions and reverse some of the damage to promote more efficient trade flows. Examining the political motivations will also be important to meeting the objectives of this paper.

The predominant pairing of PTA agreements is between a developed country and a developing country (“North-South”), followed closely by developing to developing country pairs. These pairings account for 27 and 25 percent respectively of the total number of notified RTAs in goods (Fiorentino et al. 10). Analysis of these two groups will be important to determine why PTAs have become widespread. Motivations for both developed and developing countries to engage in preferential trade as well as motivations for developing countries to join PTAs among themselves will be explored further in future sections.

#### *Increasing Complexity and Sophisticated Designs*

The complexity of RTAs is gradually increasing due to agreements being negotiated outside of a country’s geographical region. Although only 12 percent of these cross-regional agreements have been reported and operational, the figure changes to 43 percent when examining signed agreements that are not yet in operation and agreements currently being negotiated. In addition, the figure increases to 52 percent for the

agreements at the proposal stage (Fiorentino et al. 9). It is true that PTAs have traditionally been among countries of geographical proximity, but this trend of cross-regional RTAs may indicate that countries have run out of RTA options within their geographical area and are looking abroad for further discriminatory trade expansion (Fiorentino et al. 9). Cross-regional agreements indicate that regionalism remains a strong movement and shows no sign of slowing down. Failure to conclude the Doha Round is most likely encouraging discriminatory vehicles to trade liberalization.

Cross-regional agreements may also help to explain the decreased commitment to deep integration. It does not seem politically feasible to engage in comprehensive economic integration that is anywhere near the depth of the European project with countries that are not geographically contiguous. This lack of commitment to deeper globalization will hinder the multilateral trading system in the long run. As Fiorentino et al. confirm: “Perhaps with the exception of Europe...all other regions manifest growing asymmetries between regional integration processes and the scope and depth of the cross-regional RTAs to which individual countries are parties” (Fiorentino et al. 9).

Cross-regional RTAs also demonstrate that long-established trading patterns are evolving. One of the reasons the international economy has not achieved full globalization is that countries still have a tendency to trade more with their geographical neighbors. The prevalence of cross-regional agreements demonstrates that countries are showing more inclination to increase trade with countries outside of their proximity. The concept of PTAs has allowed countries to engage in trade without too much risk. This may be a positive aspect of regionalism, but the discriminatory effects of PTAs remain a risky long-term strategy.

Along with the shift in PTA partner preferences, the complexity of the RTA designs has also increased. In addition to bilateral and plurilateral agreements, there are now arrangements where one of the members is an RTA by itself. These kinds of alliances have been gradually increasing. Another especially complex design that is gaining popularity is a bilateral RTA where each of the participating parties is a separate RTA (Fiorentino et al. 8).

The “hub and spoke” model is influential in the discussion of regionalism and is helpful in demonstrating how complex the international trade system has become. The EU and the U.S. are considered the main hubs of regional integration agreements and the spokes are the countries and other RIAs with which the hubs have signed agreements (Koopmann 118). According to Koopmann: “...supraregional links are being created or reinforced between the ‘spokes’ (for example, between Canada and EFTA) and between ‘hubs’ and ‘spokes’ (such as between the EU and Mercosur).” To make it even more complicated, the hubs are both involved in PTA schemes in other regions, mainly in Eastern Asia (Koopman 118).

A more recent trend, the scope of these agreements has also become more sophisticated as they have broadened to include services. The increasing sophistication of these agreements may help to uncover the motivations behind PTAs. If their original intent was discriminatory, why are these countries expanding their agreements to include features such as intellectual property, foreign direct investment, and antitrust? The increasing complexity in the design demonstrates that countries are willing to employ discriminatory trade liberalization than no trade liberalization at all. The WTO’s

relevance is rapidly eroding and it must create solutions fast before the process is too damaging to be reversed.

## **V. The Roles of the U.S. and Europe in the Second Regionalism**

Because of the U.S. and Europe's economic dominance, they are able to influence the framework of international economic relations, essentially setting the tone.

European and North American regional arrangements directly govern 40 percent of world trade, and their members account for half of world income. These agreements affect trade with non-member nations, so it is important that two-thirds of world trade is with North Atlantic nations that have discriminatory deals with their main commercial partners (Baldwin 867).

Many scholars believe that the United States was a staunch supporter of multilateralism and discouraged regionalism. These scholars list the United States' deviation from a multilateral trade policy as one of the primary factors in the recent proliferation of free trade arrangements. However, evidence will show that the United States always had its eye on bilateral approaches. This demonstrates the theme in international relations that every country will always do whatever it takes to promote its strategic interests in the end. Due to its vast influence, the reasons as to why the United States included a bilateral trade strategy in tandem with its promotion of the Most Favored Nation principle will uncover a substantial piece of the PTA proliferation puzzle.

An aspect that might have contributed to this deviation is the doubt of U.S. politicians in the slow, time-consuming process of WTO trade negotiations. As time progressed, U.S. policymakers who were supporting economic liberalization believed that *anything* that would liberalize trade was good. Many politicians did not grasp that bilateral trade agreements were not the same as multilateral agreements. As Bhagwati states: "It was as if an economist were to say, if you wish to cut spending in the national

budget, just do it: every cut is as good as any other—a proposition that would soon be recognized as absurd” (Bhagwati 16). However, history demonstrates that the United States had begun to take interest in regionalism at an early stage. One example that demonstrates the United States’ mixed trade policy approach was present from the very beginning of the establishment of the GATT is its long history of attempting to establish a free trade agreement with Canada. “...ever since the GATT was signed, the U.S. has almost continuously sought to liberalise bilateral trade [with Canada]” (Baldwin 869). In 1948, the two countries secretly negotiated a draft agreement to get rid of most of their bilateral tariffs and quotas. Although, this proposal would ultimately be rejected by Canada, trade liberalization in certain industries such as defense arms and auto occurred gradually as time progressed. In 1974, the Trade Act gave the U.S. president the authority to negotiate an FTA with Canada. What is most interesting is that this authority was granted during the initial stages of the Tokyo Round. Congress had almost simultaneously approved a comprehensive agenda at the multilateral level. As the Tokyo Round gained momentum, Congress continued to pursue a bilateral trade agreement with Canada. The same year that the Tokyo Round was concluded Congress passed the Trade Agreements Act of 1979, section 1104 of which mandated the President to examine “the desirability of entering into trade agreements with countries in the northern portion of the western hemisphere” (Wonnacott 19). Canada continually rejected all U.S. proposals for a bilateral free trade area until the 1980s, which marked a heightened protectionist sentiment in U.S history (Baldwin 869). To protect its trade interests, Canada finally relented to a regional agreement in the form of CUSFTA.

In addition, a “small, but influential movement” began discussing the idea of a North Atlantic free trade agreement between the U.S. and Europe in the 1960s amidst the Kennedy Round negotiations at the WTO (Koopmann 118). These events put into serious question the perceived American commitment to multilateralism. Although the idea of a free trade agreement between Europe and the United States did not come into fruition, it provides evidence that the United States was wavering on its commitment to multilateralism from early on. The U.S. already had subtle bilateral tendencies immediately after it helped to establish the economic regime at Bretton Woods.

The U.S. outwardly promoted multilateralism, but had contradictory bilateral objectives. It is safe to say that the U.S.-abandoned-multilateralism explanation is not sufficient or accurate in demonstrating why preferential agreements are so prevalent. It also does not explain why the American government began to gradually increase its pursuit of bilateralism. The following historical events occurring in the U.S. domestic arena leading up to proliferation are more accurate explanations.

During the 1980s, President Reagan needed to overcome the challenge of an increasingly protectionist domestic sentiment. Because the dollar was overvalued, persistent private interests forced Reagan to give in to some protectionist legislation (the importance of special interests will be addressed in-depth in a later section). To counter the domestic sentiment, he was advised to “mobilize exporting interests by offering them markets abroad” (Bhagwati 38). The multilateral avenue was closed off at the time because Europe and developing countries were strongly opposed to beginning a new round of trade negotiations when the U.S. had pushed for one in 1982. The Uruguay



Round would not begin for another four years (in 1986) and so the U.S. saw no other option than to proceed bilaterally.

But the overvalued dollar improved, the Uruguay Round began, and still the U.S. proceeded further down the bilateral path. Bhagwati blames this occurrence partly on lack of leadership. Pascal Lamy, Director-General of the WTO, once said: “when trade ministers sign bilateral trade deals they get on television” (Blustein 15). Despite all of the publicity that FTAs invite, the economic impact of individual FTAs is in fact very limited. Trade liberalization at the WTO level throughout the twentieth century and the limited scope of many FTA designs has limited the exploitative effects of regionalism (Blustein 14). Many trade officials promoted free trade agreements simply because it showed to the public that they were doing their jobs and that they were doing it well. This factor in the prevalence of preferential avenues to trade is valid.

Additionally, government officials who pursued PTAs almost always received higher official ranks. Bhagwati confirms this statement when he writes that there is a positive correlation between the increasing number of negotiated PTAs and the number of bureaucrats attaining promotions (Bhagwati 40). This bureaucratic chain reaction led to state officials’ promotion of bilateral trade negotiations with countries of personal interest as well. Signing these agreements also gave trade officials concrete successes that would make them more marketable once they entered the private sector (Blustein 16). U.S. Trade Representative during the Bush administration Robert Zoellick, who made FTA negotiations the principal tenet of his approach to trade policy, is a prime example of this bureaucratic greed. He is now president of the World Bank.

Zoellick cemented a more frequent bilateral approach to trade policy during his term (2001-2005). Although he claimed to prefer multilateral trade negotiations over FTAs, he proceeded to pursue FTAs once it became apparent that the Doha Round was going to take much longer than expected. Fred Bergsten, head of the International Institute of Economics, and Zoellick justified signing an abundance of bilateral trade agreements by explaining that, coupled with simultaneous MTNs, they would act as “building blocks” by furthering trade liberalization at a faster pace (Bhagwati 39). It is becoming increasingly apparent that this reasoning might have been flawed. Instead of a global economy based on free trade, a huge portion of it operates on discriminatory access to markets. Some claim that Zoellick was talented in the “politics of substance, not the politics of politics.” He believed that the U.S. trade policy must remain dynamic and produce results. In his opinion, it was better to do something than nothing at all. He The trade representative is quoted: “Such bilateral agreements enable us to keep up the momentum abroad and at home” (Stokes 243).

As the analysis above demonstrates, the assumption that the United States was once solely committed to the multilateral approach is incorrect. Evidence has shown that the U.S. has pursued a mixed policy approach from the beginning. Perhaps the role that United States played in the Second Regionalism can be attributed to the domestic protectionist sentiment more than anything else. The protectionist sentiment mobilized U.S. special interest groups to pressure the government for a more proactive approach, while countries such as Canada changed their policies toward FTAs in order to retain its access to the most important economic, but increasingly protectionist, market in the world. The protectionist sentiments along with trade officials’ realization that PTAs were

good publicity are two influential explanations as to the encouragement of regionalism in the 1980s and 1990s. What occurred after can be explained by Baldwin's domino theory of regionalism (please see section IV).

### *Europe's Role*

Europe, as the second largest economic power, also contributed significantly to the proliferation of PTAs and the erosion of multilateralism. The European Community's (EC) trade policy structure and subsequent historical events set the stage for the global chain reaction expounded by the domino theory of regionalism. In the 1980s and 1990s, the EC's trade policy consisted of three levels. The first level included countries that had preferential access to the EC market, such as European countries with accession prospects as well as those who did not have membership objectives. Because the U.S. was so committed to facilitating European cohesion, it allowed the European Union to retain discriminatory preferences with its 18 former African colonies as well (Bhagwati 31). The second tier consisted of countries treated on an MFN basis, which was only a handful of industrial economies outside of Europe while the third tier was made up of countries granted less-than-MFN access, which was essentially made up of the Soviet bloc (Sapir 718). At this point, it is evident that the majority of the European Community's economic engagement with other countries was based on preferential relations.

After the formation of the European Community, the Maastricht Treaty of 1992 brought about further integration in the form of the Single European Market and a larger member base. The end of the Cold War also brought about the emergence of Eastern European countries into the EU's sphere of influence. After the Cold War, the third tier

of EC policy, which included the Soviet bloc, essentially disappeared, and the EU proceeded to add “spokes” to its hub when the former Soviet countries came to the forefront. The Eastern European countries graduated to the preferential first tier. Because of this, the formation of the Single Market and the end of the Cold War brought about an increased number of PTAs and helped to set off the domino effect which will be elaborated upon in a later section (Sapir 719). As U.S. commitment to multilateralism began to unravel, the EU was signing its own bilateral agreements to increase its sphere of influence. The U.S. unwittingly sent the message to the international community that Europe’s behavior was acceptable and essentially gave its official stamp of approval to what would become a complex, two-tier trading system.

## **VI. Interdependence and the Domino Theory of Regionalism**

An empirical analysis conducted by Egger and Larch focused on the factor of interdependence of joining a PTA, which emphasizes Baldwin’s domino theory of regionalism. Baldwin’s theory highlights that a country’s decision to join a PTA is not an isolated one, but that the formation of a PTA influences the excluded country’s decision to join such an agreement; the fear of losing prior economic benefits will exert pressure on the excluded countries to petition to join the PTA (Egger and Larch 385).

According to Baldwin, the domino theory of regionalism explains the recent preferential agreement proliferation because “idiosyncratic incidents of regionalism triggered a multiplier effect that knocked down bilateral import barriers like a row of dominos” (Baldwin 877). In this Second Regionalism, two idiosyncratic events occurred in the Americas and Europe each to bring about regional proliferation—NAFTA and the European Single Market, respectively (Baldwin 880). Baldwin’s claim is well supported

by Egger and Larch's empirical analysis as well as the historical events discussed in the previous section.

The two most influential countries in the international economic regime began to increase their activities in the PTA sphere and other countries felt the need to follow suit for fear of experiencing trade diversion. The concept of interdependence is well-known in the globalization research community. The more integrated the global economy becomes, the more dependent nation-states will be on each other. The recent financial crisis demonstrates this heightened interdependence, as the actions and events that occurred in the U.S. did not leave any country unaffected. To strengthen his theory, Baldwin attempts to discredit certain mainstream explanations suggested by scholars regarding the Second Regionalism. Although some of his assertions may be misguided, he is correct in questioning long-held beliefs about the regionalism versus multilateralism debate.

## **VII. Mainstream Explanations for PTA Prevalence**

The explanations for the recent resurgence of the regional approach are based on two assumptions: frustration with the sluggish multilateralist approach has made countries resort to the faster method of regionalism, and the United States' change of policy from stalwart promoter of multilateralism to avid supporter of regionalism (Baldwin 866). This section will include some of Baldwin's perspectives regarding mainstream explanations expounded by Paul Krugman as well as the author's. Krugman lists several reasons as to why countries may feel that the bilateral approach is more convenient. First, because multilateral negotiations involve a large number of countries, it lowers the costs of non-cooperation and encourages inflexibility in the liberalization

process. For this first explanation, Baldwin counters by stating that PTAs are not as politically easy than some would believe. This may have been the case as the Uruguay Round experienced difficulties, but after trade negotiations were concluded, it was more difficult to convince the U.S. Congress of approving NAFTA, while the Uruguay Round was widely supported (Baldwin 867). However, Baldwin fails to consider that this was the largest regional initiative that the U.S. had ever engaged in. There were bound to be fears when a regional agreement included Mexico, a neighboring country whose market was not nearly as sophisticated as the United States'. Loss of jobs and border security issues, especially in terms of Mexico, were huge subjects of debate and understandably so. The American public will always care much more about issues that occur in its backyard no matter what the policy area (Please see section VIII). Also, as previously mentioned, domestic interests have much influence on trade policy. The multilateral framework is designed to minimize the intrusion of domestic interests to achieve broader trade liberalization. Governments have an easier time with multilateral negotiations because they know that there will be minimal political backlash aimed at any one politician. NAFTA, on the other hand, was a purely domestic political battle that would directly affect millions. Because of this difference, politicians were subject to public scrutiny and had to tread carefully to accommodate their individual constituencies.

Baldwin does not totally succeed in discrediting Krugman's assertion. Krugman's assertion that it may be easier for countries to engage in preferential policies than through a multilateral framework is correct to a certain point. Governments are shielded from domestic interests at the multilateral level, but it will always be a slow process in the accommodation of individual country concerns. There is inflexibility in

multilateral negotiations and FTAs allow countries to pick and choose what they want to liberalize. Free trade agreements allow countries the flexibility to pursue their own interests faster. However, the costs of non-cooperation are not reduced because of the large number of participants, but rather the incentive to cooperate decreases because of the existence of PTAs. This suggests a false causal relationship: PTAs may explain the disincentive to cooperate multilaterally, not the other way around.

Baldwin also cites Europe's political controversy in passing the Maastricht Treaty, their principal regional proposal, as evidence that regionalism is not easier than multilateralism (Baldwin 875). As mentioned above, Baldwin believes that if regionalism is not easier when compared to multilateralism then it does not explain its recent proliferation. However, Baldwin's view of history is skewed. The Maastricht Treaty implemented the most progressive economic and political integration initiatives ever seen. European cooperation expanded to areas beyond the economic to include justice and home affairs as well as foreign and security policy. It also led to European monetary union (Euro). The European Union has tackled issues that have never been handled at the WTO. There is also no membership inclination for the WTO to handle issues of monetary and political integration in the future. Monetary and political integration are special exceptions that require a significant loss of sovereignty, more so than multilateral concessions on goods and services. Most of the PTAs in the international system, whether they be in force, in negotiations, or at the proposal stage, are not trying to achieve the level of integration that the European Union has achieved. This is a special case that should not be used to argue that regionalism is more difficult

than multilateralism, because the kind of regionalism being referred to is nowhere near the type of integration that the EU has achieved.

Krugman's second explanation for the popularity of discriminatory trade is that there is an increased amount of trade barriers employed by countries today that are more complex and less transparent than the simple tariffs and quotas that had been handled by past GATT rounds. Krugman claims that this makes multilateral bargaining harder and makes enforcement much more difficult. Baldwin concedes that international trade is much more complicated than it used to be. However, Krugman's claim is irrelevant when discussing free trade agreements as opposed to in-depth regional integration. FTAs mostly deal with tariffs and quotas; to assume that regionalism is prevalent because the GATT is incapable of handling complex trade barriers is incorrect (Baldwin 875-876).

But Baldwin fails to consider that trade within FTAs is also becoming increasingly sophisticated. It is not that the GATT/WTO cannot handle complex issues; it is that the presence of increased, sophisticated regionalism has undermined its ability to handle such issues by creating a huge tangle of technical and bureaucratic trade agreements. Here again is the potential for a false causal relationship. Also, the GATT/WTO has evolved to handle many complicated barriers and has reformed its Dispute Settlement Mechanism to better manage the regime. Enforcement has been difficult in recent years, because of institutional weaknesses at the GATT/WTO more than anything else. Countries employing preferential trade policies have outright ignored WTO provisions. The complexity of trade barriers and the WTO's inability to handle them is not a factor in the explanation of 1990s proliferation. This is a *result* of



regionalism, not necessarily a cause. The real cause of the proliferation of PTAs is, again, due to institutional weaknesses within the GATT/WTO (please see section IX).

The third mainstream explanation that Krugman uses is that economic players have come onto the international arena and the U.S. is no longer the economic hegemon, making the international trade system harder to manage (Baldwin 1998 874). Although U.S. economic share has decreased over time, the U.S. was still the most influential country besides Europe that encouraged bilateral trade agreements. The system *is* harder to manage, but this is because its most influential participant has embraced regionalism. U.S. economic share has nothing to do with it; the U.S. did not lose control of its errant children, it indirectly promoted their behavior.

Some scholars assume that the United States was the “driving force” behind regional initiatives when this is not the case. The United States considered bilateralism as one of its policy instruments from the very beginning. Throughout history, this policy was used sparingly but it gradually began to increase during the 1980s and 1990s, setting off a chain reaction. An example that strengthens the statement that the United States did not necessarily outwardly encourage other nations to engage in regional initiatives (at least during the 1980s and 1990s) is the surprising willingness of Latin America, not the U.S., to lower their import barriers in the 1980s and 1990s. Latin American countries were known for being wary of globalization and had many protectionist policies. The formation of MERCOSUR, a regional initiative consisting of Latin American countries, came about partly because the U.S. was opposed to bilateral negotiations (Baldwin 877).

### **VIII. The Influence of Special Interest Groups**

As mentioned throughout this paper, the influence of special interest groups is a crucial factor that created an enabling environment for preferential proliferation in the 1980s and 1990s. It is also a factor of the *continued* proliferation that is resulting in an ever-complex trading system. As Baldwin states: “The force-for-inclusion is strengthened by a peculiar tendency of special interest groups. They fight harder to avoid losses than to secure gains” (Baldwin 879). This tendency of special interest groups is important to consider in the discussion of multilateralism versus regionalism. Domestic interests are an important factor when discussing RIAs because they have the power to influence a country’s trade policy. Because PTAs are inherently discriminatory, exporters in the non-member countries will be negatively affected. Exporters are more likely to demand compensation for the discrimination of a PTA than to lobby for the success of a MTN.

In addition, producers who have to compete against imports are often the most effective lobbyists. For example, steel producers make up one of the most influential special interest groups in the United States, because they represent a significant minority that is disadvantaged by import competition. Producers are often interested in discriminatory trade liberalization because “it limits the increase in international competition to which home country industries are subjected.” Discriminatory agreements also provide better market access in the partner countries, giving the home country economic leverage over excluded countries (Trade Blocs 27). As discussed above, the U.S. has historically attempted to build a free trade area with Canada from the very beginning. This consistent objective is understandable when one considers that U.S. exporters have much influence on U.S. trade policy and Canada is their most important

market (Baldwin 876). Ethnic groups have also played a small role. As bilateralism became official U.S. policy, many ethnic groups began to push the U.S. government to sign agreements with their countries of origin (Bhagwati 40).

## **IX. Legal Issues – GATT/WTO**

Special interest groups are an influential factor at the domestic level. At the international level, GATT/WTO institutional issues are a major factor in the explosion of preferential arrangements. This chain reaction of discriminatory trade agreements seems to be irreversible. Ironically, the discriminatory approach to trade liberalization has become prevalent “under a multilateral framework of laws and regulations (GATT and WTO)” based on the principle of non-discrimination (Fiorentino et al. 13). Instead of taking an anti-PTA stance on the grounds that they are inherently discriminatory, Article XXIV allows for the passage of free trade agreements as long as they are “substantial” in nature. This loophole opens the door for much debate regarding the role of PTAs in the global economy. The WTO must resolve this ambiguity as soon as possible so that it can better cope with the presence of PTAs and attempt to reestablish itself as the main vehicle for achieving trade liberalization.

According to Fiorentino, Verdeja, and Toqueboeuf: “Clearly the MTS (Multilateral Trading System) is not functioning properly and as the Uruguay Round experience first revealed, the propensity for RTAs is likely to increase at times when the WTO is perceived as failing to deliver its Members” (Fiorentino et al. 13). Because of the increasing popularity of preferential trade arrangements, there has been a steady erosion of the MFN principle. Preferential mechanisms, such as the Generalized System of Preferences, were implemented to grapple with the development gap between higher

income and lower income members, and other mechanisms such as Regional Trade Agreements were allowed since the creation of the GATT so that GATT/WTO members could promote more comprehensive trade liberalization at a faster pace. RTAs were viewed as a way to minimize the effects of the slow, time-consuming Multilateral Trade Negotiations (MTNs) and further the trade liberalization agenda (Fiorentino et al. 26).

In 1947, the inclusion of preferential approaches to trade was seen as favorable in furthering trade liberalization. It was perceived that true regional agreements which promoted broad trade liberalization among clusters of Members would complement multilateral trade negotiations, enhancing the Multilateral Trading System (MTS) (Fiorentino et al. 26). Members engaging in preferential trade policy are subject to certain WTO provisions apparent in GATT Article XXIV for trade agreements in goods, and GATS Article V, for trade agreements in services. These stipulations are “transparency, commitment to deep intra-region trade liberalization, and neutrality vis-a-vis non-parties’ trade.”

The GATT/WTO has had issues regarding the interpretation of Article XXIV, which might help to explain why free trade agreements have proliferated despite the fact that the present international trade system is based on multilateralism. “It...became progressively clear that bureaucrats could walk horses, if not elephants, through the ambiguities that clever lawyers could find and exploit in Article 24” (Bhagwati 22). Phrases such as “substantially all trade” must be covered and “reasonable” length of time left much ambiguity in the WTO’s policy regarding regionalism. Some still question the European Union’s compliance with Article XXIV, and according to Jagdish Bhagwati, rightly so (Bhagwati 24). But ultimately, it is difficult to obtain political support for

stricter guidelines and enforcement when virtually every Member is part of such agreements (Bhagwati 25). Consequently, “The WTO watchdog has turned out to be a friendly poodle” (Bhagwati 25). In addition, there is not an effective enforcement framework in place to determine Member compliance with the fundamental requirements. Although the Committee on Regional Trade Agreements (CRTA) was established to determine Article XXIV consistency, it has not made much progress on its mandate due to difficulties in the interpretation of the article’s provisions (Fiorentino et al. 27).

In addition, the Enabling Clause waives developing countries’ obligations under GATT Article I, or the MFN principle, when engaging in preferential agreements with each other. Typically, the Enabling Clause only requires a small amount of transparency in RTAs negotiated among developing nations (Fiorentino et al. 26-27). The tense relationship between multilateral and regional approaches became so problematic that WTO reform of bureaucratic and legal processes and reform of the CRTA were added to the Doha Round agenda (Fiorentino et al. 27).

The Uruguay Round is yet another explanation for the rapid increase of free trade agreements in the past two decades. A number of countries reacted to the prolonged Uruguay Round by implementing a preferential trade policy approach in case of failure at the multilateral level. The fall of the Soviet Union and the emergence of the transition economies onto the international economic stage created various RTAs among the transition countries as well as with the European Union. At the country level, the European Union began, which was predominant in RTA policy, began to be rivaled by various countries who had previously been opposed to such policies. The creation of NAFTA, MERCOSUR, and AFTA spurred other countries to pursue a regional

integration approach. Also, the trade strategy of “additive regionalism” emerged, where countries such as Chile, Mexico and Singapore attempted to foster preferential policies with their major trading partners. According to the WTO Secretariat, “Albeit sporadic in their manifestation, these combined developments have laid the seeds for the surge in RTAs that we are witnessing today” (Fiorentino 13). Until countries realize that the long-term well-being of their economies and the trade system as a whole is to have a multilateral liberalization method as opposed to a two-tier discriminatory approach, it will be harder and harder to conclude MTNs.

#### **X. Secondary Factors: Perceived Political Benefits**

According to a World Bank Report, “The purpose of integration is often political, and the economic consequences, good or bad, are side effects of the political payoff” (Trade Blocs 11). The perceived political benefits of RIAs seem to be secondary factors in the grand scheme. Although political motivations demonstrate why these agreements continue to exist, they do not explain what caused their proliferation in the first place. The political benefits of preferential trade alliances are not new and do not explain the arrival of the Second Regionalism. However, they are important to note as they contribute to the *continued* prevalence of preferential approaches. Various political reasons as to why countries choose to enter into regional integration agreements include security, bargaining power against outside countries, and appeasement of domestic interests. In terms of economics promoting intraregional security, the European Union is a perfect example. The European integration project was fostered in the attempt to end the constant conflicts that resulted in two world wars and to finally forge lasting peace. It was believed that strong economic ties among the countries would make it too costly for

conflict to arise; this turned out to be true as the EU is a unanimous success. Other examples of regional integration agreements that were signed for the promotion of intraregional security include MERCOSUR, to reduce the likelihood of conflict between Argentina and Brazil, and ASEAN, for the promotion of continued peace between Indonesia and Malaysia (Trade Blocs 12-13). Agreements between a hegemon and a smaller country also emerge to symbolically announce the support of the hegemon in economic and security matters. For example, the U.S.' first PTA was negotiated with Israel in 1985 (USTR). The U.S. entered into this agreement for entirely political motives to strengthen its support of Israel as an ally.

Aside from the European Union and other successful agreements, there is also statistical evidence supporting a positive correlation between trade and peace. Using the Conflict and Peace Data Bank, Polachek found that, between two countries, increasing trade by half reduced the risk of conflict by approximately 17 percent (Trade Blocs 13). Some scholars add to the explanation of such a correlation by citing that negotiating closer economic ties allows political leaders to build trust and future collaboration. Also, as mentioned earlier, tighter ties among strategic industries, such as coal and steel in Europe, would make it too costly to indulge in conflict with each other (Trade Blocs 13).

However, regional integration can sometimes worsen rather than reduce political tensions, especially if the original intent of the agreement was not based on intraregional security. If the economic benefits derived from the agreement are unevenly concentrated in one place, causing uneven income distribution, then the countries that do not benefit, or are worse off, might develop animosity toward the other country (Trade Blocs 14). An example of this occurrence is the East African common Market, the uneven income

distribution of which contributed to future conflict between Tanzania and Uganda in 1979 (Trade Blocs 15). The European Union avoided such conflict by having a culture of compromise. On a similar note, sometimes countries are motivated to employ regionalism to protect against common external threats as well (Trade Blocs 16).

Another motivation to enter into RIAs is for political leverage. As the World Bank Report states, “By joining together, the weak can become strong” (Trade Blocs 17). Some of the smaller developing countries especially might band together and forge an agreement so that they can increase their standing and influence in the international arena. RIAs are also a way to improve one’s reputation. Signing a RIA shows to the other countries and to the general international community that you are committed to trade liberalization. A country that has been unreliable in the past will increase the confidence of the other parties that the country is committed to trade liberalization despite any unreliability in its history (Trade Blocs 23).

### *Developing Country Participation*

The ability of developing countries to waive Article XXIV altogether has contributed to the proliferation of PTAs (Bhagwati 28). Lower income countries are entering into RTAs with the wealthy, developed countries despite options to waive certain trade obligations through mechanisms such as the Generalized System of Preferences and the Special and Differential Treatment (SDT) clause at the WTO level (Fiorentino et al. 11). RTAs are gradually changing the North-South relationship to focus more on reciprocity and “ambitious trade policy scope.” Approximately half of the reported North-South trade arrangements include trade liberalization in services and covers issues such as competition, government procurement, intellectual property, and



investment. In addition, many of the projected RTAs intend to have a section on services, demonstrating a growing trend of deeper liberalization within developing countries (Fiorentino et al. 13). This seemingly positive aspect of the RTA proliferation is that it seems to be making increased headway in the inclusion of lesser developed countries. As discussed above, the negative effects on developing countries cannot be discounted.

There are several reasons why developing countries view joining PTAs as advantageous. One explanation for the increased proliferation is that many developing countries were wary of globalization and trade liberalization, and perhaps still are. The tricycle theory demonstrates that some developing countries believed that learning to compete with each other before proceeding to liberalize based on the MFN principle would be the most strategic route. Although there is no evidence that suggests that this assumption is necessarily true (Countries such as South Korea managed to take advantage of trading opportunities without utilizing the preferential approach), it may help to explain why there has been a surge in developing to developing country agreements (Bhagwati 41-42).

Aside from improving their bargaining position, there is also the “monkey see, monkey do” explanation. If many other countries are doing PTAs, there must be some benefit, or at least that is the assumption (Bhagwati 42). A developing country might feel like it is being left out of a major movement that might put them in a disadvantaged position in the long-run. Many lower income countries are also claiming that PTAs will “insure” against a failed Doha Round. The prime minister of Singapore best described this tactic: “[With the Doha Round in limbo], we need to buy insurance and the way we buy insurance is to negotiate bilateral free trade agreements with our major trading

partners.... In case the world trading system runs into trouble...” (Bhagwati 43).

However, this so-called “insurance” explanation does not explain much the proliferation among the poorer developing countries. The major trading partners of developing countries are not other developing countries; their major trading partners are developed economies. Also, there is no basis for assuming that the failure of the Doha Round will result in increased protectionism. This explanation may be valid for a country such as China, which is still “vulnerable to substantial market-denying possibilities via antidumping and other harassments” (Bhagwati 43).

For preferential trade agreements between developed and developing countries, a different set of rationales becomes apparent. One primary motivation of developing countries to sign this type of agreement is to ensure security (Bhagwati 44). A PTA signed with a major power, such as the U.S. or Europe, signals to the international community that they are strategically involved in these regions. Once again, South Korea displays this reasoning; an FTA with the U.S. for security reasons is of significant importance since South Korea is geographically surrounded by North Korea, China, and Japan. Having the U.S. as a major economic and political ally is of great interest for the South Koreans. Another motivation is that PTAs are a good way to demonstrate that a developing country is committed to economic reforms and will therefore attract investment. According to Baldwin, some developing countries want to join an FTA with a wealthy nation to prevent the negative effects of trade diversion. A fourth explanation is that some countries may wish to join a PTA as a defense to another existing PTA. An example of this is the Asian region’s reaction to form their own regional trade agreement when the US ignored the region and concentrated on an FTA of the Americas. The US,

in turn, is now concerned that it may have “lost” the more investment-worthy region when it focused on the problematic and sluggish South American economy; the US is now promoting an FTA of the Asia-Pacific as an attempt to mitigate its disadvantaged position (Bhagwati 45-46).

“Hegemons’ biggest motivation to favor the PTA over the multilateral route for freeing trade has been the use of their PTAs to advance trade-unrelated agendas.” U.S. lobbies especially have exerted pressure on the government to enter bilateral negotiations with “weaker powers” to address issues such as labor and environmental standards (Bhagwati 46). This is a sign that the developed powers do not view the WTO as an effective vehicle to further these parallel issues. This assertion is cemented by U.S. Trade Representative Robert Zoellick: “I hope the bilateral agreements will enable us to make headway on environmental and labor issues consistent with free trade” (Stokes 243).

Although it is not in the WTO’s mandates to address environmental, labor, or human rights issues, these issues have fostered anti-globalization sentiments everywhere, which has undermined the trade regime. For the WTO to retain its relevance, it must be more dynamic and push for increased inclusion of these issues into its framework. However, it seems politically infeasible to do this when there is a rift between developed and developing countries about the inclusion of such issues into the framework. Labor and environmental standards put developing countries at an economic disadvantage.

Many of the political motivations discussed above are important to consider when determining the reasons why countries have signed so many preferential trade arrangements. However, these factors are only secondary factors that have contributed to

PTA proliferation. Although they explain why countries have continued to sign agreements, it does not explain why countries started doing so in the first place. The elements that enabled this environment for PTAs to flourish were past and current legal weakness of the WTO, the United States and Europe's gradual embrace of discriminatory policies due to historical events, and Baldwin's theory that centers on interdependence. In terms of the participation of developing countries in this phenomenon, the most influential factors would be the increased inclusion into the international trade system leading up to the Second Regionalism and the Enabling Clause of the GATT/WTO that allowed essentially any kind of PTA.

## **XI. Recommendations for the WTO**

The bottom line is that regionalism is not going to go away. To uphold the multilateral framework and the WTO's relevance, the WTO must take a more proactive approach to ensure that PTAs are more consistent with free trade liberalization than they currently are. Whatever positive benefits preferential trading arrangements may bring, "this tangle of trade deals is a bad way to organise world trade" (Baldwin and Thornton ix). To take a more active role, the WTO should create initiatives to encourage countries to include voluntary best-practices in RTAs. RTAs such as APEC and ASEAN have already done this on their own, and it is strange that the WTO took no part in this. However, the WTO should become the leader in this initiative. To begin, the WTO should introduce different categories of best-practice guidelines to better suit the "spaghetti bowl" of FTAs. The categories should be North-North, North-South, and South-South to address each type of RTA. The WTO should utilize its soft power to promote these best-practice norms (Baldwin and Thornton xi).

As mentioned earlier, one of the reasons for PTAs is that it signals to others that it is committed to trade liberalization, promoting competitive boosting reforms in the home country. This is particularly common in North-South agreements. The WTO framework has traditionally been the anchorage mechanism. However, many developing nations go the preferential route because they are reluctant to change their developing nation status and be forced to assume all WTO obligations. The WTO could work to find a middle ground between Article XXIV and the Enabling cause by establishing “anchorage building disciplines” that developing countries can commit to as well as their RTAs. “If the disciplines were well crafted, they could serve as a seal of good governance that would boost a nation’s locational competitiveness just as Bilateral Investment Treaties do now, but on a more comprehensive basis” (Baldwin and Thornton xi-xii).

Regarding the tangle of rules of origins, which are highly technical and disadvantage businesses attempting to establish international supply chains, the WTO should also take interest. Some countries have been trying to harmonize their rules of origins as a response to growing pressures from the business community. The WTO, again, has not been involved, but it should since this can have spill-over effects to outside nations. A supervisory role is needed to ensure that the harmonization promotes non-discrimination and to encourage nations to harmonize their rules of origins at the regional level (Baldwin and Thornton xii).

The WTO should also work to make the RTA movement better meet the needs of developing countries. As discussed earlier, developing country participation in bilateral trade treaties runs the risk of squandering government resources and making poor policy decisions. WTO advisory services or a committee specifically for developing countries

and their RTAs could really strengthen the WTO and its promotion of equitable development (Baldwin and Thornton xii). The WTO can utilize its influence once again to promote the inclusion of as many poor, developing nations into the scope of international supply chains within RTAs and minimize the disadvantages incurred by rules of origin (Baldwin and Thornton xiii). Although the political will to eliminate or limit PTAs in the international trade system is very low among WTO members, the WTO can still play a role, be it supervisory, regulatory, or diplomatic, to retain its relevance and prevent RTAs from derailing the multilateral agenda.

## **XII. Conclusion**

The debate of regionalism versus multilateralism has important implications for the international economy. Preferential trade arrangements have created a two-tier system to trade liberalization, one that is discriminatory and one that is not. Many scholars are involved in the debate of the effects the recent proliferation of PTAs will have on the global economy and how it will affect future international economic relations. This Capstone attempted to raise many of the arguments proposed by the research community to pinpoint exactly factors enabled this Second Regionalism. Historical actions and events leading up to the second wave of regionalism in the United States and Europe, the most powerful economic nations, are very important factors that enabled the proliferation of PTAs in the 1980s and 1990s. Interdependence as explained by Baldwin's domino theory of regionalism is the second influential factor, as it caused an irreversible chain reaction of discriminatory trade arrangements. At the domestic level, special interest groups will always have much influence over trade policy, and this is the third factor that caused the prevalence of regionalism. Consideration of the institutional

weaknesses at the GATT/WTO is crucial in understanding the PTA proliferation as well. The four factors are all pieces of the preferential trade puzzle and when pieced, provide an accurate picture of why the second wave of regionalism was successful where the first wave was not. Understanding how regionalism became a permanent fixture in the international trade system will hopefully aid in providing policy solutions that promote more efficient and non-discriminatory regime.

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