

Preferential Trading Arrangements – Bilateral and Regional: Issues for East Asia

Robert Scollay

University of Auckland

New Zealand

**Paper presented at Fourth Asia Development Forum,
Seoul, 4-5 November 2002**

The views expressed herein are the views of the author and do not necessarily reflect the views or policies of the Asian Development Bank (ADB) or its Board of Directors or the governments they represent. ADB makes no representation concerning and does not guarantee the source originality, accuracy, completeness, or reliability of any statement, information, data, finding, advice, opinion, or views presented.

Proliferation of Preferential Trading Proposals in the Asia Pacific Region: A Preliminary Typology

- **Bilateral (BTA)**
 - **most numerous type, different classifications possible**
 - **intra-East Asia (e.g. Japan-Singapore)**
 - **intra-Western Pacific (e.g. Singapore-NZ)**
 - **trans-Pacific (e.g. Singapore-Chile)**
 - **“large” – “small” linkages (BTAs involving US, Japan, Korea with “small” partners)**
 - **“small” – “small” linkages (e.g. Singapore-NZ)**
 - **“large” – “large” linkages (e.g. Japan-Korea)**

Various “regional” configurations

- **“mega-blocs”**
 - **“ASEAN Plus three” (East Asian Bloc)**
 - **FTAA**

- **plurilateral**
 - **amalgamations of existing groups (e.g. ASEAN-CER) or existing bilaterals (e.g. Singapore-Chile-NZ)**
 - **“reduced form” versions of “mega-blocs” (e.g. ASEAN-China, ASEAN-Japan, ASEAN-U.S.)**

Forseeable Outcomes

- **“kaleidoscope” of overlapping/intersecting bilaterals and plurilaterals**
- **“bipolar Pacific” based on megablocs in East Asia (ASEAN Plus Three) and Americas (FTAA)**
- **“hub and spoke” arrangements based on large regional “hubs” (US, China, Japan, Korea)**
 - **ASEAN as a possible alternative “hub”**
 - **perhaps combined with the “kaleidoscope” of BTAs**

Common Characteristic

All are conceived as “preferential” (i.e. discriminatory) agreements

→ common term is “preferential trading agreement” (PTA)

Issues raised by PTAs

- **Deeper integration versus the “spaghetti bowl”**
 - **PTAs can go further, faster**
 - **modern PTAs extend well beyond conventional FTA, CU**
 - **scope for extensive “WTO-plus” provisions**
 - **membership of multiple PTAs with inconsistent provisions raises transaction costs for business**

- **trade creation versus trade diversion**
 - **trade creation: gains from trade liberalisation**
 - **trade diversion: costs of discrimination both members and excluded countries**
 - **net outcome**
 - **ambiguous for members**
 - **unambiguously negative for excluded countries**
- **investment implications an increasingly dominant consideration – importance of**
 - **size of market**
 - **availability of preferential access to other major markets**

- **“domino” effect**
 - **“small” economies impelled to negotiate new PTAs or seek membership of existing PTAs to counter threat of exclusion**
- **“hub and spoke” problems**
 - **unequal bargaining power**
- **potential precedent effects of provisions over “sensitive” issues**
 - **agriculture, labour, environment**

**“Building blocks” or “Stumbling Blocks”
for
more open multilateral trading system?
realisation of vision of Asia-Pacific as
region of open trade and investment?**

- **Possible routes are**
 - **expansion of existing PTAs**
 - **amalgamation of existing PTAs**
 - **multiplication of bilaterals**

- **Possible “stumbling block” factors include:**
 - **potential incentive for members of existing PTAs to resist expansion or amalgamation**
 - **scope for PTAs to cater for specific “sensitivities” (e.g. agriculture, labour, environment) may lead to preference for PTAs over multilateral liberalisations**
 - **conditions for “building blocks” include**
 - **PTA members reduce external barriers against non-members**
 - **openness to inclusion of new members**
- but no mechanisms exist to enforce these conditions**
- **WTO rules ineffective**
 - **APEC rules (if they existed) would be non-binding**

Some considerations from PTA modelling

- **Larger blocs (centred on “large” economies)**
 - **larger gains for members**
 - **negative effects on excluded countries**
 - **minor if include all countries with major trade links
(variation of “natural trading bloc” concept)
(e.g. effect on East Asian trade bloc on Latin America)**
 - **serious for excluded economies
(e.g. effect of East Asian trade bloc on Taiwan,
Australia, New Zealand)**

- **small economies derive large welfare gains from PTAs with “large” partners e.g. ASEAN-China, ASEAN-Japan, ASEAN-US, Australia-US, Singapore-Japan, Singapore-US**
(and suffer large welfare losses when “large” partners discriminate against them)
- **economic welfare effects of BTAs among small economies are generally negligible e.g. Singapore-NZ**

Some implications for alternative PTA configurations involving East Asia

- **Bilaterals among small economies**
 - **weak rationale as “end in themselves”**
 - **more easily explicable as tactical initiatives**
 - **manoeuvring to avoid future exclusion from larger arrangements**
 - **“demonstration effect”**
 - **signalling “availability”**

- **“East Asian trade bloc”**
 - **relatively benign in economic welfare terms if it includes all western Pacific economies**
 - **seriously damaging for any excluded western Pacific economies**
 - **cause for some concern to US**
 - **cuts across “trans-Pacific dimension” of APEC vision (“bipolar Pacific”)**
 - **contributes to formalisation of “three-bloc” world**

- **implications for multilateral trading system**
 - **danger of “trade wars” between blocs**
 - **“trade wars” will be mutually destructive**
 - **incentive for blocs to ensure WTO remains sufficiently effective to function as insurance against “trade wars”**

- **“Hub and spoke” pattern with “large” economies as “hubs”**
 - **for “large” economies**
 - **gains available from larger blocs are foregone**
 - **for “smaller” economies**
 - **can secure virtually all available economic gains if they can secure PTA with every “large” economy in the region**
 - **multiple membership of “hub and spoke” agreements may partly offset unequal bargaining strengths in individual “hub and spoke” arrangements**
 - **excluded “smaller” economies may suffer significant economic damage**

- **involvement of US helps to preserve the “trans-Pacific dimension**
- **obstacles to gradual “broadening” or “multilateralisation” through enlargement or amalgamation**
 - **neither “large” nor “small” members have a strong incentive to admit new “small” members**
(and “small” members may have an incentive to resist this)
 - **possibility that tailoring of individual “hub and spoke” arrangements to “hub” sensitivities on agriculture, labour, environment etc may lead “hub and spoke” groups to develop as mutually inconsistent and irreconcilable “islands” of trade preference**
- **especially acute problems for “very small” economies (Pacific island states)**