THE RACE FOR PREFERENTIAL TRADE AGREEMENTS – CAUSES, PATTERNS AND EFFECTS

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Abstract

Over the last decade, members of the World Trade Organization (WTO) have increasingly turned towards negotiating preferential trade agreements (PTAs) as a means for achieving improved market access for exports of goods and services, and investment. In particular, the year 2013 witnessed a remarkable revival of the regional trade agenda, with numerous new PTA negotiations being launched, including by WTO members accounting for substantial shares of world GDP and global trade and investment – the so-called ”mega-PTAs”. While PTAs are not new to the WTO system, striking is however the fresh impetus to regionalism worldwide, which manifests itself not only in the steep numerical rise, but also the unprecedented pace and scale of new PTA initiatives.

Against this backdrop, this paper addresses several key issues related to the new active phase of regionalism from the perspective of the multilateral trading system governed by the WTO. It first looks at the systemic factors underlying the unabated drive towards PTAs among WTO membership, and distils the rationale behind the current surge in regionalism. Second, it examines the patterns of new PTAs and evidences the qualitative differences vis-à-vis previous PTAs in terms of scope, composition and depth. Finally, it discusses the economic and geopolitical factors driving the new PTAs, and highlights some of the potential effects upon the world trading system and global trade patterns.

Key words: preferential trade agreements (PTAs), trade policy, trade negotiations, world trading system, World Trade Organization (WTO), Doha Round

JEL classification: F10, F13, F15, F23, O19

1. Introduction

Over the past decade, members of the World Trade Organization (WTO) have increasingly turned towards negotiating bilateral and regional trade

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arrangements – named hereafter preferential trade agreements (PTAs)\(^2\) – as a means to further market-opening and rule-making outside the multilateral trading system. In particular, the year 2013 witnessed an outstanding revival of the regional trade agenda, with a whole range of new regional and bilateral PTA negotiations being launched, including by WTO members accounting for substantial shares of world GDP and global trade and investment. These include several large regional and bilateral PTAs – the so-called ”mega-PTAs” – initiated by the major trading powers, namely the US, EU and Japan.

PTAs are not new to the world trading system governed by the WTO since 1995, or its predecessor, the General Agreement on Tariffs and Trade (GATT) signed in 1947 by 23 nations. The proliferation of these agreements started already in the 90s and has intensified since then constantly, especially after the establishment of the WTO. PTAs have in common that, unlike unilateral preferential trade agreements, they are reciprocal trade agreements between two or more partners. The multilateral trading system has always allowed for preferential trade arrangements to be created, and both the GATT and now the WTO have specific rules providing scope for this. Such deals are permitted under the GATT/WTO system as a derogation from the most favoured nation clause, which lies at the foundation of the multilateral trading system. However, WTO members (as, previously, GATT contracting parties) are bound to notify the agreements in which they participate.

Not even mega-regional agreements are entirely new, as their forerunners date back to the mid-1990s. Relevant examples are the European Single Market, which has been largely completed at the beginning of 1993, and the North American Free Trade Agreement (NAFTA) between Canada, Mexico and the US, which came into force one year prior to the establishment of the WTO in 2015. And worth mentioning is also the Free Trade Area of the Americas (FTAA), the project launched in 1994, but failed in 2005, which sought to tie 34 economies in the Western Hemisphere into a single economic bloc. All these initiatives had in common the pursuit of a much deeper regional integration among the partner countries than the global integration provided for among WTO members (Koopman and Wittig, 2014, p. 1). They also offered models to further extend and refine the original WTO rules as well as those embedded in the PTAs concluded later on.

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\(^2\) Throughout this paper we use the term preferential trade agreement (PTA) to refer to customs unions, free trade agreements, and other interim arrangements leading to one of these forms of integration, according to the provisions of GATT Article XXIV and GATS Article V. Its connotation is similar to the term regional trade agreement used by the WTO, both terms being equally usual in the literature.
Hence, the PTAs concluded over the last decade, including the recent new mega-regional initiatives – such as the Trans-Pacific Partnership (TPP) currently under negotiation among 12 developed and emerging countries in Asia-Pacific, or the bilateral EU-US Transatlantic Trade and Investment Partnership (TTIP) – have to be seen, first and foremost, as the continuation of a trend in regional cooperation that dates back to the mid-1990s, with the US and EU as its main supporters.

But whereas PTAs are not new to the GATT/WTO system, these preferential trade deals show every sign of continuing to increase both in number and complexity. Apart from growing at an unprecedented rate over the last decade, striking is the spread of new PTA initiatives involving multiple parties and/or major trading countries that have a significant combined economic weight. In addition, PTAs concluded or negotiated in the twenty-first century are qualitatively different from previous PTAs in their scope, composition, depth as well as consequences for the international trading system.

Starting from these few introductory remarks, this paper addresses the recent revival of trade regionalism through the lens of the multilateral trading system governed by the WTO, with a view to shed light on its drivers and patterns as well as some of its consequences for global trade and its governance mechanisms. In doing so, it draws on insights from current literature and relies on statistical data provided by the WTO and other relevant international organizations. The paper is organized as follows: Section 2 provides an overview of the numerical surge in PTAs concluded by WTO members over the last decade, and highlights the outstanding speedup of the regional trade agenda since 2013. Section 3 looks at the key structural transformations that have marked the WTO over recent decades, and distils the systemic factors underlying the fresh impetus to regionalism worldwide. Section 4 discusses the patterns of twenty-first century PTAs vis-à-vis previous PTAs in terms of scope, composition and depth as well as economic relevance. The analysis in Section 5 focuses on the economic and geopolitical reasons behind the current race for bilateral and regional approaches, while the final section outlines some of its consequences, and concludes.

2. The exponential increase in preferential trade agreements: facts and figures

The recent surge in trade regionalism worldwide manifests itself not only in the steep rise in the number of new bilateral and regional initiatives, but also their scale and pace. Particularly visible is this trend since 2013, with the pace and scale of negotiations on PTAs witnessing an unprecedented speeding up.
Major PTA developments in 2013 have included the start of negotiations on several large regional and bilateral PTAs – the so-called "mega-PTAs" – by major trading powers, such as the US, EU and Japan. Particularly remarkable is the pace of these initiatives, namely:

- the start of negotiations, in March 2013, on an EU-Japan free trade agreement;
- the joining by Japan, in March 2013, of the negotiations on the Trans-Pacific Partnership Agreement (TPP), involving 12 developed and emerging countries in Asia-Pacific; and
- the launch of negotiations, in July 2013, on a Transatlantic Trade and Investment Partnership (TTIP) between the US and EU.

And this image of prominent WTO members being strongly involved in the regional agenda has to be completed with two other undertakings in 2013, which, though not related to PTAs as such, are of particular relevance, given the large share in global trade and investment flows of the partners involved, i.e.:

- the launch of plurilateral negotiations, in March 2013, on a new Trade in Services Agreement (TISA) among 23 WTO members (including the EU); and
- the start of negotiations, in November 2013, on an EU-China investment agreement, followed by similar negotiations between the EU and Myanmar/Burma since March 2014.

Moreover, to these most recent initiatives a whole series of PTAs should be added such as the EU-Canada, EU-Singapore, China-Switzerland, and Australia-Korea agreements, which are waiting for final approval or ratification (UN/DESA, 2014, p. 58). And apart from the PTAs that have been signed and will soon enter into force, a number of agreements are currently being negotiated, most of them between partners in different geographical regions. Hence, the unabated push towards regionalism is unlikely to be stemmed. Moreover, this is likely to be further reinforced through the recent new initiatives, including those related to large regional and bilateral PTAs – the mega-PTAs – that are being negotiated.

PTA activity has been particularly robust among the WTO membership over the past decade, with the number of such agreements in force increasing exponentially. According to WTO figures, on average 14 PTAs have entered into force annually since 2003 (WTO, 2014a, p. 53). Unlike unilateral preferential trade agreements, PTAs are reciprocal trade agreements between two or more partners, and WTO members are bound to notify the agreements in which they participate.
As of April 2015, some 612 notifications of PTAs (counting goods, services and accessions separately) had been received by the GATT/WTO, of which 406 were in force. These WTO figures correspond to 449 physical PTAs (counting goods, services and accessions together), of which 262 are currently in force (90% representing free trade agreements and 10% customs unions (WTO, 2015a). Yet the WTO Secretariat furthermore estimates that there are almost 100 agreements in force but that have not been notified to the WTO (WTO, 2014a, p. 53).

It is important to note, that PTAs have grown much more rapidly since the WTO came into being compared to the days of its predecessor, the GATT. Whereas GATT received just an average number of 3 notifications annually, the WTO has received from its members on average 24 notifications per year (WTO, 2014b). While in the period 1948-1994 the GATT received 124 notifications of PTAs (relating to trade in goods), of which 50 were active in 1995, since the creation of the WTO over 400 additional preferential arrangements covering trade in goods or services have been notified (WTO, 2015b). Several factors account for the stronger upward trend in regionalism in the context of the WTO as compared to the GATT-rulled system. These pertain basically to the important changes in the multilateral trading system following the creation of the WTO in 1995, which we refer to as the systemic drivers of trade regionalism, and which we are going to tackle in the next section.

3. WTO and the systemic drivers of the regional trade agenda

Trade regionalism appears to be a phenomenon deeply embedded in the multilateral trading system itself. As frequently stressed by the WTO Director-General Roberto Azevêdo, the multilateral trading system of today has its roots in the reciprocal trade agreements that countries had been pursuing for many years prior to agreeing the GATT. In fact, those PTAs pre-dated the multilateral trading system inasmuch as it may be argued that the GATT itself was effectively a multilateralisation of the network of previous reciprocal trade agreements. So these initiatives are important – they co-exist with the multilateral system – and they can bolster it in a significant way. But while they are important for the multilateral trading system, they cannot substitute but only complement it (WTO, 2014b). Hence, a question of utmost importance in this context is how to make PTA provisions complementary to the multilateral trading system, and how to ensure that PTAs are "building blocks” and not "stumbling blocks” for this system.

Starting from the above assumption and having in mind the continuous rise in the number of PTAs since the mid-1990s, and especially in the last decade,
we may argue that the recent revival of regionalism worldwide should be seen as a shift in focus rather than a fundamental course change in the evolution of the regional trade agenda. It also follows, that the factors underlying this shift have to be sought, to a large extent, in the structural transformations that have marked the multilateral trading system and the WTO itself in the wider context of the changing global political and economic environment. Therefore, a brief insight into the main developments that have shaped the organization over the recent decades seems appropriate for shedding light on the systemic factors that are driving regionalism, including in our days.

According to the Marrakesh Agreement on the establishment of the WTO, as a result of the Uruguay Round (1986-1994), the organization fulfills five basic functions, namely, it provides for: (1) a set of rules designed to govern the conduct of international trade; (2) a forum for negotiating trade liberalization; (3) a trade dispute settlement mechanism; (4) transparency of trade relations; and (5) coherence in global economic policy-making. By virtue of these functions and the whole body of multilateral trade agreements that is administered by the WTO, the organization lies at the very heart of the global trading system and plays a central role in global trade governance. And precisely the WTO’s centricity is at stake when it comes to discuss the outstanding surge in preferential trade deals concluded outside its remit.

The years following the creation of the WTO have been characterized by robust global trade growth, with world trade in goods and services substantially outpacing world GDP growth – a trend that has lasted until the outbreak of the global economic and financial crisis. Along with strong expansion, global trade flows have been also accompanied by sweeping structural changes in the patterns of international trade and organization of global production. Rapid advances in technology, and especially new information and communication technologies, but also market opening worldwide ranked among the main factors driving these changes. As a result, new actors and new forms of trade have emerged, and important changes have occurred in the hierarchy of traders, in the geographical orientation and structure of trade, and its very nature. Together, these changes have triggered an unprecedented increase in interdependencies among economies worldwide. In this context, two important and interrelated developments stand out for their major consequences for global trade and its governance mechanisms.

Firstly, numerous developing countries, especially in Asia, have emerged as major players in global trade, such as the BRICS (Brazil, Russia, India, China and South Africa). These countries account today for more than half of the world’s economic activity and over half of global exports, with China emerging as the number one world exporter. A similar picture of shifting composition
arises with respect to foreign direct investment (FDI), with the share of emerging and developing countries in global FDI inflows rising to over half over the last decade.

The rise of emerging economies and the subsequent shift in economic power and influence within the world economy have profound implications not only for international trade, but also international trade cooperation and global leadership. Essentially, this means that the long-standing equilibrium in global trade cooperation inherent in the GATT/WTO system based on the traditional two-speed model of a world divided between developed and developing countries no longer reflects today’s economic realities. Hence, serious conceptual adjustments are needed and a new balance between reciprocity and flexibility must be found if the WTO is to deliver on multilateral trade opening and designing global trade rules (Lamy, 2013). Yet, the two major group of countries cannot agree upon what would exactly constitute a proper balance of rights and obligations within the WTO. This is essentially a political issue that needs a political solution. Consequently, adjusting politically and organizationally to the new economic realities will take time, and until a new equilibrium in global trade cooperation will emerge multilateralism is likely to be under heavy pressure.

Secondly, the last decade has also seen the rapid expansion of global production networks (GPNs) or global value chains (GVCs). These are in effect “global factories”, as firms increasingly locate various stages of the production process in the most cost-efficient markets. As a result, a vast and growing amount of world trade is now conducted through global supply chains, whereby parts and components cross many borders since production is shared in many different locations. About 80% of global trade in goods and services is, in one way or another, linked to supply chains, according to estimates (UNCTAD, 2013a, p. 135). Essentially, this new form of trade – known also as ”supply-chain trade” or ”twenty-first century trade” – combines traditional trade in goods with services, FDI and knowledge (Baldwin, 2012, p. 1). This is not only more complex than traditional trade, but is also the fastest growing segment of global trade, and calls for a deeper integration among participants. But the WTO is not equipped to deal with issues related to supply-chain trade since its current rules and disciplines have been designed to facilitate only traditional trade, i.e. selling goods and services internationally (Baldwin, 2012, p. 1). In the absence of global regulation, the rules related to supply-chain trade have been devised outside the WTO, predominantly through PTAs. It follows, that the WTO is faced with the challenge to take better account of the growing importance of global production networks by devising proper trade and investment rules to support the evolution
of these networks, which currently involve not only developed but also developing economies.

The challenges arising from these major shifts in geopolitics and economics for the WTO have to be seen, in our opinion, the major systemic factors that are underly ing the unabated drive of WTO members towards PTAs, including the current surge in trade regionalism. And to these factors a third one should be added, which relates to the dramatic transformations experienced by the WTO itself, whether in respect of the issues on its agenda or in geopolitical terms. Over the last two decades, WTO membership expanded by 33 new members to 161 at present, accounting together for 98% of world trade. The continual expansion of WTO membership and the integration into the multilateral trading system of a number of large emerging economies (e.g. China, Russia etc.) have radically changed the structure of the organization, hindering consensus-based decision making, reducing the effectiveness of its activity and affecting the conduct of multilateral negotiations under its aegis. Besides, trade policies and trade agreements have increased in complexity, since the very nature of trade barriers has evolved. Nowadays, trade deals are no longer confined to negotiating just the reduction of tariffs, but also non-tariff barriers and behind-the-border regulations, which have gained enormous importance but are more difficult to tackle (Lamy, 2013). In short, the world economy and global trade relations have become more complex.

This is why the first round of multilateral trade negotiations hosted by the WTO and launched in 2001 – the Doha Round – has evolved under much more complex and difficult circumstances than similar rounds of negotiations under the auspices of the GATT in the past. So, it is not surprising that the round could not be completed till now, though the original intention was to conclude it by the end of 2004.

Moreover, the Doha Round negotiations practically stalled in July 2008 largely over a major divide between developed and developing countries on major issues such as industrial tariffs, agriculture subsidies, and non-tariff barriers. And with this impasse, two of the WTO’s central functions have been also blocked, namely: (1) as a venue for multilateral trade negotiations, ensuring market-opening; and (2) its legislative function, responsible for developing new trade rules and disciplines. Consequently, the WTO trade rule-book could not be adjusted so as to keep pace with the dramatic changes in the global trade landscape over the recent decades. Basically, the bulk of these rules remained stuck in the mid-90s when they were negotiated and agreed as an outcome of the Uruguay Round (1986-1994) – which stands in fact for the last major market
access agreement under the auspices of the GATT/WTO and also the last period of active global governance. Under these circumstances, the market-opening and rule-making agenda required by twenty-first century trade shifted increasingly towards PTAs concluded outside the multilateral system governed by the WTO.3

Undoubtedly, lack of progress in the multilateral trade negotiations and hence the inability to adjust WTO rules and disciplines to the structural and geopolitical changes in the global economy and trade have led many countries of the world to increasingly resort to PTAs as a means for achieving improved market access for exports of goods and services as well as investment. The deadlock in the Doha Round has also increasingly reinforced the perception that decision-making at the multilateral level is inefficient. Actually, for the private sector both in developed and developing countries trade liberalization and rule-making via PTAs has proven to be more effective than multilaterally, the latter being seen as a cumbersome and too lengthy undertaking, and also unpredictable and overly politicized. But it is also true that the major traders’ growing interest in finding solutions for regulating and liberalizing markets outside the WTO has diverted substantial energies from the multilateral negotiations, by channeling them towards PTAs. And not least, opening trade and devising new multilateral rules has been further affected by the biggest economic crisis since the 1930s, which distracted attention from the global trade agenda and spurred the promotion of defensive trade policies and even protectionist actions worldwide. It was not until the Ninth WTO Ministerial Conference in Bali (Indonesia), in December 2013, that a window of opportunity arose for relaunching the Doha Round.4

3 Yet, trade liberalization progressed at an unprecedented rate in the 2000s. For example, the average tariff applied on imports stood below 1% in developed countries and averaged 4-10% in developing countries in 2012. As of 2012, almost 40% of world trade was fully liberalized under MFN terms, with an additional 35% free because of preferential trade regimes (UNCTAD, 2013b, p. 5-7). But the trade policy reforms backing up this liberalization have been implemented by means of deep PTAs as well as unilateral (national) reforms and bilateral investment treaties, and not multilateral initiatives within the WTO (Baldwin, 2013, p. 26; 2014, p. 26).

4 In Bali, WTO members have adopt the so-called Bali Package, consisting of a set of measures to liberalize and spur international trade, including the Agreement on Trade Facilitation, which represents the first comprehensive agreement achieved since the creation of the WTO in 1995. WTO members have also committed to conclude the Doha Round trade talks. For this purpose, the WTO was mandated to develop a clearly defined work program on the remaining Doha agenda issues by the end of 2014 (later extended to July 2015) (Ghibuțiu, 2015, p. 5).
4. Patterns and economic relevance of twenty-first century preferential trade deals

As in the case of agreements in force, most new negotiations are bilateral. Among the key bilateral negotiations in terms of the parties’ share in world trade rank: the TTIP between the EU and US, EU-Japan, EU-India, EU-MERCOSUR, as well as Australia-China, Canada-South Korea, and Canada-India (WTO, 2014a, p. 54).

However, a more recent development relates to establishing plurilateral PTAs or consolidating existing bilateral agreements among a group of members. Several ongoing negotiations illustrate this trend, including (WTO, 2014a, p. 54):

- negotiations in the Asia-Pacific Region for a Trans-Pacific Partnership (TPP) Agreement, launched in 2010, and currently involving 12 parties, involving the US and a number of American and Asian states;
- the Regional Comprehensive Economic Partnership Agreement (RCEP), negotiated since 2012 and aiming to harmonize existing bilateral agreements between the 10 economies of ASEAN and 6 other WTO members (Australia, China, India, Japan, South Korea, and New Zealand);
- the Pacific Alliance in Latin America, which brings together Chile, Colombia, Mexico and Peru; and
- the Tripartite Free Trade Area Agreement in Africa, striving to consolidate three existing plurilateral agreements related to the East African Community (EAC), the Common Market for Eastern and Southern Africa (COMESA) and the Southern African Development Community (SADC), and involving 26 parties.

Recent research by the WTO Secretariat based on PTAs notified since 2000 reveals that twenty-first century preferential trade deals are not only more numerous, but they are becoming increasingly complex. Of particular relevance are the following aspects (WTO, 2014b):

- While over 80% of PTAs notified are bilateral agreements, there are more and more large regional agreements.
- PTAs are increasingly concluded between countries in different regions, rather than between neighbours, which is very different from the patterns prevailing in the GATT system.
- In addition, many more developing countries are negotiating PTAs today than in the past.
- The last years have also seen a significant increase in the level of complexity of the rules enshrined in PTAs and in their relations with other
agreements. The continuous numerical proliferation of PTAs, with each having its own set of trade rules and disciplines has been dubbed the “spaghetti bowl” in WTO parlance. Most PTAs of today contain deeper and more extensive commitments, and have moved beyond commitments only in market access in goods. In terms of commitments undertaken by the parties through PTAs notified to the WTO since 2000, the following aspects are relevant (WTO, 2014b):

- Around 60% of PTAs contain commitments in both goods and services.
- Over half of PTAs contain rules on investment.\(^5\)
- More than half of the PTAs incorporate other issues than market access, such as provisions on government procurement, competition, technical barriers to trade, sanitary and phytosanitary regulations, trade defence measures and intellectual property rights. These are known as ”WTO-plus” provisions, as they go beyond existing multilateral WTO rules, in that they refer to areas already subject to commitments under multilateral agreements, but involve additional commitments.
- A smaller proportion of PTAs include additional issues such as environmental and labour standards and electronic commerce, which are not at all covered by existing WTO rules. These are known as ”WTO-extra” provisions, as they relate to new areas, which fall outside the scope of current multilateral rules and disciplines.

It follows, that the patterns of twenty-first century PTAs are quite different from previous PTAs in their scope, composition and depth.

Firstly, their major focus is regulatory behind-the-border barriers to trade rather than only tariff measures at the border. In this regard the new PTAs go well beyond existing provisions in the WTO and even earlier PTAs, aiming to promote deep integration between members. They strive to achieve high-standard integration through WTO-plus and/or WTO-extra provisions on regulatory measures, such as technical regulations, standards, services, investment, intellectual property rights, state aid, government procurement,

\(^5\) At the global policy level, trade and FDI are dealt with by different institutions and legal arrangements. While trade is covered by the WTO multilateral framework, FDI is dealt with by: (1) bilateral investment treaties – with a total number of 3,236 by the end of 2013 (UNCTAD, 2014, p. 114); and (2) bilateral/regional PTAs. In the absence of a multilateral framework, the rules governing global FDI are mainly implemented through PTAs. A growing number of PTAs contain trade and investment chapters, and the provisions on both are often included in the same legal article. This reflects the need to deal with trade and investment together in a context where trade increasingly takes place within individual companies, and where decisions about the location of economic activity involve both trade and investment as means of accessing markets (Ghibuțiu, 2015, p. 15).
competition policy, environment, and labour market regulations (UN/DESA, 2014, p. 58).

Secondly, in addition to full market opening, twenty-first century PTAs encompass behind-the-border regulatory measures that are consistent with the requirements of trade conducted through global production networks (GPNs), i.e. supply-chain trade or 21st century trade. In other words, they entail under various forms the set of new rules and disciplines that provide for the trade-investment-services-intellectual property rights nexus (Baldwin, 2013, p. 42). Hence, they are oriented towards a more comprehensive integration with a strong regulatory focus on providing a viable platform for GPNs by ensuring a duty-free and non-tariff-barrier free trading environment (UN/DESA, 2015, p. 55).

Thirdly, especially the new bilateral and regional initiatives currently being negotiated such as the TPP, TTIP and RCEP differ qualitatively from previous PTAs in their size and depth, as they are generally drawing on a template developed by major players and are striving for deep liberalization and high-standard, cutting-edge regulatory harmonization that covers an increasing share of the global economy. These new mega-PTAs relate to widespread trade deals involving a group of countries that have a significant combined economic weight, whether in terms of their share in world GDP and trade (Table 1) or global FDI flows (Table 2).

<table>
<thead>
<tr>
<th>PTAs under negotiation</th>
<th>Number of members</th>
<th>Percentage share in world exports</th>
<th>Intra-group trade as a percentage of global trade</th>
<th>Combined GDP as a percentage of world GDP</th>
<th>Number of bilateral agreements among parties</th>
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<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Exports</td>
<td>Imports</td>
<td></td>
</tr>
<tr>
<td>TPP</td>
<td>12</td>
<td>26.0</td>
<td>46.3</td>
<td>38.3</td>
<td>38.9</td>
</tr>
<tr>
<td>TTIP</td>
<td>2</td>
<td>43.9</td>
<td>17.3</td>
<td>14.3</td>
<td>45.4</td>
</tr>
<tr>
<td>RCEP</td>
<td>16</td>
<td>27.3</td>
<td>42.0</td>
<td>47.4</td>
<td>29.5</td>
</tr>
</tbody>
</table>

Source: Based on UN/DESA (2015, p. 56).

Note: Trade and GDP figures are for 2012. EU is counted as one entity. TPP = Trans-Pacific Partnership; TTIP = Transatlantic Trade and Investment Partnership; RCEP = Regional Comprehensive Economic Partnership Agreement.

Finally, it is noteworthy, that a significant proportion of PTAs involve either the EU or the US as partners, which is evidence of the prominent role of the two big trading powers in promoting preferential trade deals. Actually, the ‘EU and US have developed a ”hubs and spokes” system of bilateral agreements, within which they constitute the ”hubs” in the constellation of PTAs, while the ”spokes” are made up of different countries that are parties to their agreements
(Horn et al., 2009, p. 3). Through this "hubs and spokes" system of PTAs, the EU and US have sought to reduce regulatory divergences facing companies engaged in trade because of the complex and nontransparent rules inherent in these agreements (the so-called "spaghetti bowl of PTAs"). Indeed, this system alleviated to some extent the condition of companies placed in a "hub", but the problems remained unresolved in the case of companies from "spokes" countries, such as Mexico, Israel, Jordan, Chile, etc., that have signed deep PTAs with both the EU and US (Baldwin, 2013, p. 43).

Table 2: FDI inflows to selected mega-PTAs under negotiation, average 2005-2007 and 2013 (Billions of US dollars and per cent)

<table>
<thead>
<tr>
<th>PTAs under negotiation</th>
<th>Average 2005–2007</th>
<th>2013</th>
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<tr>
<td></td>
<td>FDI Inflows ($ billion)</td>
<td>Share in world total (%)</td>
</tr>
<tr>
<td>TPP</td>
<td>363</td>
<td>24</td>
</tr>
<tr>
<td>TTIP</td>
<td>838</td>
<td>56</td>
</tr>
<tr>
<td>RCEP</td>
<td>195</td>
<td>13</td>
</tr>
</tbody>
</table>

Source: Based on UNCTAD (2014, p. xvi).
Note: TPP = Trans-Pacific Partnership; TTIP = Transatlantic Trade and Investment Partnership; RCEP = Regional Comprehensive Economic Partnership Agreement.

Due to the continuous numerical proliferation of PTAs, the international trading system is currently managed not only by multilateral WTO rules and disciplines, but also a growing number of PTAs, most of which represent deeper trade deals that address rules beyond traditional tariffs or traditional preferential access. Consequently, the share of world trade covered by PTAs increased continuously. Nearly 60% of trade in developed countries has been covered by some PTAs in 2012, and each developed country had preferential access to an average of 23 countries in the same year – a steep increase from an average of 8 countries in 2002 (UNCTAD, 2013b, p. 18). And it goes without saying that these figures will further soar due the effects of the plethora of new PTAs, including the mega-bilaterals and regionals launched in 2013 by countries with considerable weight in the global economy. According to a recent report by the European Commission, the ambitious trade agenda pursued by the EU currently will lead to a radical expansion of the coverage of EU trade by PTAs: while less than a quarter of EU trade was covered by PTAs before 2006, the current figure is around one third, and is likely to rise to two-thirds of EU trade once all ongoing negotiations are concluded (European Commission, 2015a, p. 6).
Hence, if concluded successfully the new PTAs and especially the new mega-PTAs are likely to have important implications not only for the multilateral trading system and global trade patterns, but also the international investment regime and global investment patterns. Therefore, it is not surprising that the current negotiations of mega-PTAs have become a hot topic in the public debate worldwide, attracting both criticism and support.

5. The economic and geopolitical factors behind the race for PTAs

Beyond the systemic factors that account for the ceaseless proliferation of trade regionalism, and which relate in large part to changes in the multilateral trading system itself, the conclusion of PTAs is mainly driven by economic and commercial motivations, which can be both offensive and defensive in nature.

The most obvious reason for pursuing trade agreements is to achieve improved market access for exports of goods and services and FDI. Among the traditional motives of the public and private sector for using PTAs to expand access to international markets are: the search for growth markets, diversification of markets and risk, economies of scale, the enhancement of competitiveness, export-led growth, insertion into and/or increased participation in global supply chains, and the use of trade agreements to self-impose domestic economic reforms (Schwab and Bhatia, 2014, p. 18).

More importantly, conclusion of PTAs brings about another series of such arrangements, usually as a trade policy response from excluded countries (defensive reasons), triggering a "domino effect". According to many observers, trade regionalism generates a competitive dynamics: if two countries negotiate a preferential reduction of trade barriers, one or more non-participating countries will be hurt. As a result, the excluded countries will have an incentive to negotiate PTAs themselves, and this process would go on until achieving the goal of global free trade, at least theoretically (Subramanian and Kessler, 2013, p. 59). Actually, the guidelines currently underlying the US and EU’s trade policy options are basically rooted in the theories of regionalism as promoting competitive liberalization.

Under the impact of the global economic and financial crisis and the slow and uneven recovery in the world economy, the economic motivations driving PTAs have become more acute, particularly as the major advanced economies failed so far to wholly overcome the adverse effects of the crisis. From such an angle, the large trading powers’ recent offensive to conclude new PTAs is an attempt to definitely exit the crisis (Ghibuțiu and Oehler-Șîncăi, 2013, p. 4-5). By promoting assiduously business opportunities for their firms in international markets, the EU, US and Japan aim to stimulate growth domestically,
especially as the slowdown in global production and trade in the aftermath of the crisis has been largely caused by subdued economic activity and weak import demand in these countries.

The new mega-regionals also aim to meet the need of developed countries to liberalize trade and investment flows through promoting the creation of high-level standards that would enable them to tap the potential of trade and investment constrained by existing rules and regulations imposed by the WTO and bilateral arrangements (Yong, 2014, p. 20). The new deals are essentially meant to place these countries at a competitive advantage, given that they are used as vehicles for breaking new ground on tackling regulatory barriers to trade and setting a global template for regulatory issues, especially as tariffs continue to come down around the world, and behind-the-border regulatory measures are in turn increasingly gaining importance as barriers to international trade.

But apart from purely economic motives (offensive or defensive in nature), the explanation for the hasty rise in PTAs in general and mega-PTAs in particular has to be sought in geopolitical factors. The new mega-PTAs should be seen, above all, as policy responses by the large trading powers to the challenges raised by the shift of economic and commercial power towards developing and emerging countries. From such a perspective, the US, EU and Japan’s recent initiatives demonstrate their firm option for PTAs as a swift way to ensure market opening by their trading partners, in the wider context of reconsidering the very fundamentals of their economic and trade policies. Actually, we are witnessing an attempt by these countries to counter the growing erosion of their position in world trade and reposition themselves in the global trade landscape, as with the decline in their share of world trade, the US and EU’s role as the leading exporters of the world’s standards and norms is also at risk.

Though the cumulative weight of the US and EU does not exceed one third of world GDP (at PPP) and a quarter of world trade (excluding intra-EU trade), the two great powers are traditionally viewed as the ”regulators of the world” since they account together for around 80% of the norms governing the functioning of world markets (Horn et al., 2009, p. 4). The fact that all WTO-extra provisions in the US and EU’s new trade deals relate to domestic regulations (such as investment protection, competition policy, labour standards and environmental protection) provides evidence that the new PTAs are effective tools for the two ”hubs” to export their own regulatory systems to their PTA partners and preserve thereby their primacy in determining the rules applicable to trade and investment in the 21st century. And there is a widely

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6 According to a recent EC report, ”the TTIP negotiations with the US have a particularly important strategic dimension as a comprehensive Agreement including strong regulatory disciplines could not only boost trade between the Parties but also establish an innovative
shared perception that this primarily serves the interests of the two "regulators of the world", i.e. the US and EU (Horn et al., 2009, p. 43). This perception is further reinforced by the finding that the WTO-extra provisions in the US and EU’s new PTAs, which aim at creating new rules in areas that are not covered by WTO rules, have been the subject of earlier, but failed, attempts by the EU and/or the US to incorporate them into WTO rules, against the wishes of developing countries. To the extent that these provisions can be seen as breaking new ground compared to existing WTO agreements or PTAs, it should not come as a surprise that they give rise to concerns about unfairness and even potentially abusive behavior in international trade relations. When taking also into account that PTAs are often negotiated under substantive power asymmetries among participating countries, such concerns seem all the more justified.

And certainly, behind the US and EU’s interest to keep a decisive role in the formulation of global trade and investment rules are also other geopolitical considerations, which relate particularly to US endeavours to mitigate China’s growing influence in the global economy and prevent the emergence of a China-centred East Asia economic bloc (Yong, 2014, p. 7). In fact, the mega-regionalism promoted by the US is an attempt to exert pressure on China, that is increasingly asserting its economic hegemony. An agreement by the US and EU to common regulatory standards through the conclusion of the TTIP deal would pre-empt China from imposing its own standards in international markets and even force China to adhere to these common standards (Subramanian and Kessler, 2013, p. 56). Ultimately, at issue is – in our opinion – how the US and EU handle the shift in economic power and influence from the advanced countries towards the emerging countries in general, and the rise of China in particular.

6. Concluding remarks

The increasing prevalence of PTAs is the most significant challenge to the multilateral trading system governed by the WTO.

While PTAs are not a new phenomenon for the GATT/WTO system, striking is however the speed, scale and complexity of twenty-first century model for regulatory convergence and set a global template. An ambitious deal with the US could thereby consolidate and further project the EU’s role as a global regulatory leader” (European Commission, 2015b, p. 10).

Investment, competition policy, government procurement and trade facilitation were initially included in the Doha Round agenda under pressure from the EU and US. But due to vehement opposition from developing countries, these subjects were removed from the agenda in 2004 (except for trade facilitation, where a multilateral deal was agreed at the last WTO Ministerial Conference in December 2013).
PTAs. Unlike other similar undertakings in the past, the new bilateral and regional initiatives such as the **TPP**, **TTIP** and **RCEP** have the potential to cover an overwhelming proportion of global trade and investment and go well beyond provisions in existing WTO rules and disciplines and even PTAs. Hence, if successfully concluded, they are likely to reshape not only the global trading system but also the international investment regime, and thus trigger substantial changes in the patterns of global trade and investment.

The outstanding revival of the regional trade agenda since 2013 and particularly the major trading powers’ new trade initiatives have prompted worldwide discussions on the future of the world trading system. While proponents of PTAs view the new preferential trade deals as alternatives to multilateral liberalization and updating of trade rules, the opponents raise serious doubts over their reach and effectiveness, arguing that the surge in PTAs in general and mega-PTAs in particular will have a potential negative impact upon developing parties and non-parties, and upon the wider trading system and patterns of international trade.

Indeed, to the extent that the new PTAs will include issues not currently covered by the multilateral agreements administered by the WTO this represents an opportunity to negotiate new trade rules and disciplines on these issues, thus helping to improve the global trade rule-book and promote trade liberalization worldwide. Besides, the new mega-PTAs, once in force, have the potential to reduce the ”spaghetti bowl of PTAs”, especially if they supersede existing bilateral agreements and develop common rules (e.g. rules of origin) to be applied by all the parties to the agreement. However, with behind-the-border policy regimes becoming so important in the new PTAs, the multilateral trading system runs the risk of regulatory divergence and resulting fragmentation of markets. This may further reduce transparency and uniformity in the global trading system and increase transaction and administration costs, thus diminishing trading opportunities. Ultimately, there is a real risk of scattering instead of levelling the trade playing field, which is economically harmful for the whole trading community.

Furthermore, the new PTAs may discriminate against those WTO members who are not parties to the agreements and result in trade negotiations at two speeds. A significant number of countries, ranging from the most dynamic emerging economies (such as the BRICS) to the smallest and most vulnerable ones, are excluded from their coverage. And since these new trade deals will cover a substantial part of world trade and investment and establish new global rules and regulations, these might be inappropriate for the level of development or trade interest of excluded countries. Hence, fear of marginalization and negative consequences for their competitiveness could lead many outsiders to
seek alternative solutions, including the launch of new PTAs, thereby weakening even more the multilateral trading system.

As the new mega PTAs currently under negotiation such as the TTP, TTIP and RCEP would all create giant economic zones covering substantial proportions of both world trade in goods and services and investment, they could affect incentives for multilateralism, and further undermine world trade governance by eroding the primacy of the multilateral system and WTO’s centricity as the forum for liberalizing trade and creating new trade rules. Moreover, as multilateral market-opening and rule-making practically stopped in the last decade, with the major actors pushing more aggressively than ever for PTAs, there is a risk for the world trading system to be again dominated by power politics, similarly to the 19th century, with the smaller and poorer countries being deprived of the ability to negotiate on an equal footing with the great powers.

The current race for regional and bilateral PTAs does not seem to meet the stringent need for closer and more efficient multilateral cooperation required by the increasingly interconnected and interdependent world economy. Instead, we are witnessing a paradox which the former WTO Director General Pascal Lamy described this way: “While the world is multipolarising at an unprecedented scale and speed, and production and trade value chains are multilateralising, trade governance seems to be bilateralising” (WTO, 2013). Undoubtedly, the plethora of bilateral and regional trade agreements would produce a multitude of regulatory standards with which businesses will hardly comply. Therefore, the question arises whether these bilateral rules will adequately respond to the needs of global value chains that now make up a majority of world trade. A further question of utmost importance is how to make PTA provisions complementary to the multilateral trading system, and how to ensure that the current push for regional and bilateral PTAs does not lead to an even greater fragmentation of the world trading system and the world economy? Yet, for the time being these remain open questions.

References


