WORLD TRADE REPORT 2011

The WTO and PTAs: From Co-existence to Coherence

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KEY FINDINGS OF THE REPORT

• Continuing proliferation and deepening of PTAs

• The amount of preferential trade and preferential margins are small

• New forms of organizing global production (e.g. international production networks) can explain deepening of PTAs

• Asia is at the leading edge of many of these changes

• New paradigms beyond trade-creation and trade diversion to analyse PTAs are needed

• Going beyond “building bloc-stumbling bloc”: the relationship between the WTO and PTAs
OUTLINE OF THE PRESENTATION

A. PTAs: current trends
B. Causes and effects of PTAs: it is all about preferences?
C. Anatomy of PTAs
D. Increasing coherence between the WTO and PTAs
PTAs: current trends
STYLIZED FACTS ABOUT PTAS

• There has been a huge increase in PTA activity in recent years (Figure 1)
• Nearly half of all PTAs concluded in the last decade involved Asian countries (Figure 2)
• PTAs activity has become more widespread
• In 2010, there were about 300 PTAs in force; on average a WTO member is party to 13 PTAs
• The coverage of policy areas in PTAs has widened and deepened over time
CUMULATIVE NUMBER OF PTAS IN FORCE, 1950-2010
NOTIFIED PTAS INVOLVING ASIA-PACIFIC MEMBERS
HOW PREFERENTIAL IS TRADE?

- PTAs explosion has not been matched by an expansion of preferential trade flows.
- At the maximum, only 16% (30% including intra-EU trade) of global merchandise trade receives preferential treatment (Table 1)
- Low values of preferential trade can be explained by
  - The huge reduction in tariff barriers since the end of WWII; average MFN rate is 4% with half of global trade at zero MFN duties
  - Exclusion of "sensitive" products from significant tariff reduction: about 66% of products with tariffs of 15% or more have the same tariffs in PTAs
  - Need to account for other preferential exporters
    - More than 87% of all trade (79% of all tariff lines) involved “competition-adjusted” preferences that were no greater than 2% in absolute value
At a maximum, 16% of global merchandise trade is entitled to preferences
Causes and effects of PTAs: is it all about preferences?
THE STANDARD ANALYSIS AND DEEP INTEGRATION

• The standard analysis of PTAs focuses on the trade creation and trade diversion effects of preferential tariffs
• We may need to rethink this paradigm
• “Deep integration” characterizes an increasing number of PTAs
• It refers to any PTA that goes beyond tariffs and includes regulatory policy areas
• There are two distinct dimensions of deep integration: extensive and intensive dimensions
WHY IS DEEP INTEGRATION GAINING MOMENTUM?

• Greater trade links among nations increase policy spillovers
• The rise of global production networks which unbundle stages of production across borders
• Asia has seen a large increase in global production networks
  • Trade in parts and components is “proxy” for production networks
  • Parts and components trade in Asia is regionalized: about 63% of it goes to countries within the region (rising from 44% in 1990)
• Global production networks require good governance on a number of regulatory areas such as infrastructural services, investor protection, intellectual property protection, competition, technical barriers to trade,
• This governance structure is being supplied by deep PTAs
HOW TO GO BEYOND STANDARD ANALYSIS

• Unlike preferential tariffs, regulations may not cause trade diversion

• Tradeoffs involved in deep integration
  • Differences in policy preferences vs. magnitude of policy spillovers (Oates’ Decentralization Theorem)
  • Risk of regulatory segmentation

• What countries should form a deep agreement?
  • Countries with similar policy preferences
  • Countries whose policies have a greater impact on others

• Which policy areas should be the object of a deep agreement?
  • Common decisions should be taken on policy prerogatives characterized by large cross-border effects
Anatomy of PTAs
WHAT EVIDENCE IS THERE FOR DEEP INTEGRATION?

• What evidence do we have that preferential tariffs are not that important anymore? What evidence do we have of “deep integration” and the motives for it?
• Evidence on “competition-adjusted” preference margins
• Evidence of broadening sectoral coverage of PTAs and their enforceability
• Evidence based on analysis of specific areas (services, investments, TBT, competition policy)
• Econometric evidence
• Case studies: ASEAN, Costa Rica, Africa
SECTORAL COVERAGE OF PTAS

• PTAs go beyond tariffs, and provisions are legally enforceable
• Use list of policy areas identified by Horn, Mavroidis and Sapir (2009):
  • WTO+ (14 areas covered by WTO agreements)
  • WTO-X (38 areas not covered by WTO agreements)
  • Used concept of “legal enforceability”
• Examine 96 PTAs (notified and not notified) with highest volume of trade among members
• Results (enforceable areas)
  • WTO+: Tariffs, trade remedies, TBTs, services, TRIMS, TRIPS (Figure 3)
  • WTO-X: Competition, investment, movement of capital (Figure 4)
  • Analyse pattern over time and by level of development
NUMBER OF AGREEMENTS WITH WTO+ PROVISIONS
NUMBER OF AGREEMENTS WITH WTO-X PROVISIONS
DETAILED ANALYSIS OF PROVISIONS

• Policy areas examined: services, investments, TBT and competition policy
  • Do they involve changes in behind the border regulations? (All areas)
  • Do they involve some harmonization of policy areas? (e.g. TBTs)
  • Do they involve commitments that go beyond multilateral agreements? (e.g. services)
  • Other questions: Are there families or family resemblance in PTA provisions in these policy areas? (e.g. TBT and competition policy)
DEEP INTEGRATION AND PRODUCTION NETWORKS: SOME EMPIRICS

• The reports tests empirically the **two-way link** between deep integration PTAs and production networks using trade in parts and components as a proxy for global production sharing.

• **Results show that:**
  
  • Greater trade in parts and components increases the level of depth of newly signed agreements between PTA members.
  
  • Signing deep integration PTAs increases trade in production networks by almost 8 per cent on average.
CASE STUDY: ASEAN

- Created for political-security reasons in 1967
- **Chronology of economic integration**
  - Partial scope preferential arrangement in 1977
  - Free trade area established in 1992
  - Services, IP, Investment provisions agreed to in 1995-96
  - Has negotiated PTAs with China, Korea, Japan, Australia-NZ, etc.
- **Parts and components trade (a measure of production sharing)** grew dramatically during the 1967-92 period (Figure 5)
- **Was major destination of FDI (particularly Japanese FDI)**
  - Between a fifth to a sixth of all FDI flows to developing countries
- “Concerted” trade facilitation (Pomfret & Sourdin, 2009; 2010)
ASEAN PARTS & COMPONENTS EXPORTS

USD Millions

- Exports of Parts & Components
- Share of Parts & Components in Exports
Increasing coherence between the WTO and PTAs
DEEP INTEGRATION AND THE WTO

- Building-bloc vs. stumbling bloc framework is less relevant
- Deep integration provisions are often non-discriminatory
  - Changes in regulations are difficult to make partner-specific (e.g. investments, services, competition policy)
- Mechanisms supporting further liberalization are found in PTAs
  - “Non-party” MFN clauses
  - Spread or replication of liberalizing provisions (NAFTA telecomm competition rule)
- Caveat: mechanisms generating negative systemic effects
  - Regulatory “lock-in” and segmentation
  - Trade remedies (PTA provisions on anti-dumping and global safeguards)
CONFLICTING DISPUTE SETTLEMENT SYSTEMS?

- How PTAs deal with the forum issue
  - Fork in the road (complaining member chooses forum)
  - If the subject matter is regulated by PTA, PTA will be exclusive forum
  - If PTA obligation breached is equivalent in substance to a WTO obligation, go to WTO

- Forum issue has arisen in a small number of WTO disputes

- WTO members in PTAs have continued to use the WTO DSM in resolving disputes
  - About 30% of WTO disputes are between members who are parties to the same PTA

- At the moment, conflicts appear not to be a significant problem but need to consider possible fixes
PTAS IN THE GATT/WTO

• Evolution of PTAs in GATT/WTO: tolerant and non-litigious attitude

• Establishment of GATT
  • Exemption was desired by many founding contracting parties: Great Britain, the US, Syria and several Latin American countries

• Early years
  • No standing body examining PTAs
  • A policy of “tolerance” (Jackson, 1969)

• Toughening after Uruguay Round: Establishment of CRTA and Understanding on Art XXIV

• Expansion of MFN exemption (Enabling Clause and GATS V)

• Litigation of PTAs: issues relating to PTAs have not figured prominently in WTO dispute settlement
FUTURE WTO AGENDA ON PTAS

• **Change GATT/WTO rules (“hard law”)**
  • Removing ambiguities (“substantially all trade”)
  • Making rules consistent with economic theory (Kemp-Wan)

• **The “soft” law approach as transitional mechanism to hard law**
  • Transparency mechanism as first stage
  • Agree on a code of best practice in PTAs
  • Negotiate hard law

• **Multilateralizing regionalism**
  • Reducing transactions costs and minimizing risks of regulatory divergence
  • Seeking increased commonality in rules of origin
  • Banking (binding) preferential tariffs
  • Turning WTO+ and WTO-X into WTO

• **MFN liberalization**
  • Conclude Doha Round

• **Revisit WTO approaches to decision-making (critical mass instead of consensus)**
Thank you!

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http://www.wto.org/english/res_e/publications_e/wtr11_e.htm