

**ADVANTAGE OF REGIONAL TRADE AGREEMENT FOR
ENSURING DISTRIBUTION OF GOODS IN ATTAINING GLOBAL
JUSTICE**

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Introduction

“That trade which, without force or constraint, is naturally and regularly carried on between any two places, is always advantageous, though not equally so, to both.”¹

One of the most striking development in the world trading system since the mid 1990s is a surge in Regional Trade Agreements (RTAs). From about 50 till 1990, the number of RTAs notified to the World Trade Organization (WTO) has crossed 250 in the era of 2000 and presently the figures indicate that over 400 RTAs are in effect in the year 2015.² During the initial phase when RTAs have started flourishing, WTO encouraged the growth of RTAs because it believed that regional integration initiatives can complement the multilateral trade regime and thereby would ensure the distribution of goods in attaining global justice.³ However, with the current scenario it can be seen that high proliferation of RTAs in global trade and increased diversion of trade through this route is increasingly becoming a cause of concern for the multilateral trading system under WTO.

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¹ Frank J. Gracia, ‘Is Free Trade Free?’ Seattle Journal of Social Justice, *See also:* Adam Smith, ‘The Wealth of Nations’, Books IV-V, Andrew S. Skinner ed., Penguin Books 1999), p.70 (1776).

²World Trade Organization- Facts and Figures, Available at: https://www.wto.org/english/tratop_e/region_e/re_gfac_e.htm, Accessed on: Dec 5th, 2015.

³ Mohammad F. A. Nsour, ‘Rethinking the World Trade Order: Towards a Better Legal Understanding of the Role of Regionalism in the Multilateral Trade Regime’, Sidestone Press, p. 98, (2010), Available at: https://books.google.co.in/books?id=trDI5ExieRQC&dq=why+wto+encouraged+rta&source=gbs_navlinks_s, Accessed on: Dec 5th, 2015.

It is a well-known fact that, Regional Trade Agreements represent an important exception to the WTO's principle of non discrimination⁴ and according to the WTO rules; countries within a RTA can trade among themselves using preferential tariffs and easier market access conditions than what is applicable to other WTO Member countries. And as a result of this WTO Member countries that are not a part of the RTA lose out in these markets. Also trading within the regional trade blocks does not come under the purview of WTO. As increasing amount of global trade is being diverted through this route, there is a certain amount of apprehension about the role of regional trade agreements in WTO. The WTO Annual Report 2003 expresses deep concern about this latest development and comments⁵:

“RTAs can complement the multilateral trading system, ensure distribution of burdens and benefits evenly among the global discourse, help to build and strengthen it. But by their very nature RTAs are discriminatory; they are a departure from the MFN principle, a cornerstone of the multilateral trading system. Their effects on global trade liberalization and economic growth are not clear given that the regional economic impact of RTAs is ex ante inherently ambiguous”.

This gush in regionalism has been further fuelled by the failure of the Seattle, Doha Development Agenda and the Cancun Ministerial Conference of WTO. The Economist⁶ suggests that these failures have highlighted the inherent problems of the multilateral trading system and are likely to push many countries to divert their negotiating energies into regional trade agreements. To add more to this, in December 2009, a Ministerial meeting was concluded

⁴Understanding the WTO: Cross-Cutting and New Issues Regionalism: Friends or Rivals?, Available at: https://www.wto.org/english/thewto_e/whatis_e/tif_e/bey1_e.htm, Accessed on: Dec 5th, 2015.

⁵ WTO Annual Report 2003, p. 27, Available at: https://www.wto.org/english/res_e/booksp_e/anrep_e/anrep_03_e.pdf, Accessed on: Dec 5th, 2015.

⁶ Jeffrey Schott, “Unlocking the benefits of world trade”, The Economist, Oct 30th 2003, Available at: <http://www.economist.com/node/2173129>, Accessed on: Dec 5th, 2015.

at the WTO. It was reported that ‘Ministers reaffirm the need and their desire to conclude the Doha Round by the end of next year’.⁷ This was a clear cut case of *déjàvu*: since the current round of multilateral trade negotiations began in 2001, there have been numerous promises that it would be concluded in the ‘near term’ and time and again, those expectations have been frustrated. These are the few instances that lead to the growth of RTAs in the WTO regime.

In this backdrop of resurgent regionalism, this paper gives an overview on Regional Trade Agreements (RTAs) and analyses whether these agreements are advantageous for distributing burdens and benefits within the globe and that whether they are effective in distribution of goods and in attaining global justice or is it a myth.

Regional trade agreements: basic issues

Regional Trade Agreements are groupings of countries which are formed with the objective of reducing barriers to trade between member countries or it may be defined as reciprocal trade agreements between two or more partners.⁸ It is to be noted that contrary to what the name suggests, these groupings or associations may be concluded between countries not necessarily belonging to the same geographical region. Therefore, depending upon the level of integration they have, RTAs can be broadly divided into five categories: Preferential Trade Agreements (PTAs), Free Trade Agreements (FTAs), Customs Unions (CUs), Common Markets and Economic Unions. A PTA is a union in which member countries impose

⁷ Seventh WTO Ministerial Conference, 2 December 2009, Day 3: Ministers show ‘political energy’ for ending Doha Round, Available at: https://www.wto.org/english/news_e/news09_e/mn09a_02dec09_e.htm, Accessed on: Dec 5th, 2015.

⁸ Regional Trade Agreements and Preferential Trade Arrangements, Available at: https://www.wto.org/english/tra_top_e/region_e/rta_pta_e.htm, Accessed on: Dec 5th, 2015.

lower trade barriers on goods produced within the union, with some flexibility for each member country on the extent of the reduction.⁹ A Free Trade Area (FTA) is a special case of PTA where member countries completely abolish trade barriers (both tariff barriers and non-tariff barriers) for goods origination within the member countries.¹⁰ It should be clarified here that in most cases, countries do not abolish trade barriers completely even within Free Trade Areas. Most agreements tend to exclude sensitive sectors. A Customs Union (CU)¹¹ provides deeper integration than an FTA because, unlike FTAs where member countries are free to maintain their individual level of tariff barriers for goods imported from non-member countries, in a CU, member countries also apply a common external tariff (CET) on a good imported from outside countries. The CET can vary across goods but not across union partners. PTA, FTA and CU are called ‘shallow integration’ arrangements in trade literature. Apart from these shallow arrangements there are two types of regional agreements which provide “deep integration”. The first ‘deep integration’¹² stage is called Common Markets, where member countries attempt to harmonize some institutional arrangements and commercial and financial laws and regulations among themselves. A common market also entails free movements of factors of production, i.e. removal of controls on free movement of labour and capital. The final ‘deep integration’ level is the

⁹ Id.

¹⁰ The World Trade Organization (WTO) & Free Trade Agreements, Available at: <http://dfat.gov.au/international-relations/international-organisations/wto/pages/the-world-trade-organization-wto-free-trade-agreements.aspx>, Accessed on: Dec 5th, 2015.

¹¹ Custom Union, Available at: <https://stats.oecd.org/glossary/detail.asp?ID=3130>, Accessed on: Dec 5th, 2015.

¹² Deep vs. Shallow Integration in Trade Agreements, International Economic Law and Policy Blog, Available at: <http://worldtradelaw.typepad.com/ielpblog/2011/07/deep-vs-shallow-integration.html>, Accessed on: Dec 5th, 2015.

‘Economic Union’ where countries implement common economic policies and regulations and adopt a single currency.¹³

Among the Regional Trade Agreements, a large majority of the agreements are shallow integration agreements, i.e. they are mostly PTAs or FTAs.¹⁴ In contrast, there are only a handful of Customs Unions, Common Markets and Economic Unions worldwide. Most of these deep integration arrangements are found in Europe. For example, the Maastricht Treaty and the EU Single Market programme are examples of deep integration schemes. The ANDEAN Pact and the Central American Common Market (CACM) are examples of Preferential Trade Agreements. However, most new PTAs tend to be free trade areas. North American Free Trade Area (NAFTA) and the ASEAN Free Trade Area (AFTA) are examples of FTAs. MERCOSUR is an example of a customs union. In the last few years there has been an enormous proliferation of Regional Trade Agreements (RTAs) across the world. The WTO Annual Report¹⁵ points out that currently more than 50 percent of global trade now takes place through the regional trading groups. The scope and geographical reach of Regional Trade Agreements have expanded significantly in the recent years. Apart from merely removing tariffs on intra-bloc trade in goods, the newer agreements tend to have deeper coverage. The new generation of RTAs, especially those comprising developed countries, includes more regional rules on investment, competition and standards; as well as provisions on environment and labour. Most of these new agreements also include preferential regulatory frameworks for mutual services trade.

¹³ Id.

¹⁴ Joseph E. Stiglitz and Andrew, ‘Free Trade For All’, Oxford University Press, 1st Edition, (2005).

¹⁵ WTO Annual Report 2002, Available at: https://www.wto.org/english/res_e/booksp_e/anrep_e/anrep02_e.pdf, Accessed on: Dec 5th, 2015.

Why countries are going for regional trade agreements?

As stated in the previous chapter this rapid growth of RTAs can be traced since the 1990s, and there have been attempts to identify the economic and political reasons which are pushing countries towards increased regionalism by the economists. The explanations given by them are classified into three broad categories. First being the conventional one which vouches for the welfare effects through trade liberalization and the resultant gains from trade at a regional level. On the other hand most economists are of the view that the reason for sudden increase of RTAs is the nature of the current multilateral trade regime and the dissatisfaction associated with it. Yet, another school of thought was of the view that it is because of the adoption of regionalism at a fast pace that other regions and countries have opted for RTAs. Following are the arguments in furtherance of the above discussion:

1. Theory of Trade Creation and Trade Diversion

The conventionalist theory was of the view that removal of trade barriers allows consumers and producers to purchase from the cheapest and most competitive source of supply. This ensures enhancement of efficiency as well as increases welfare. With this logic, it was believed that regional trade blocks should generate gains from trade as member countries reduce trade barriers among themselves.¹⁶

This view was first challenged by Viner in his 1950 book titled *The Customs Union Issue*¹⁷. Viner, in his seminal contribution, introduced the concepts of

¹⁶ Jo-Ann Crawford and Roberto V. Fiorentino, 'The Changing Landscape of Regional Trade Agreements', Discussion Paper, WTO Publications, p. 2, Available at: https://www.wto.org/english/res_e/books_p_e/discussion_papers8_e.pdf, Accessed on: Dec 5th, 2015.

¹⁷ Juyoung Cheong and Kar-yiu Wong, 'Economic Integration, Trade Diversion and Welfare Change', University of Washington, p.1, (2007), Available at: <https://faculty.washington.edu/karyiu/papers/trade-divert.pdf>, Accessed on: Dec 5th,

'*trade creation*' and '*trade diversion*' and depicted that the net effect of trade liberalization on a regional basis is not unambiguously positive. In his book he points out that RTAs can lead to trade creation if, due to the formation of the regional agreement, RTA members switch from inefficient domestic producers and import more from efficient producers from other members of the RTA.¹⁸ In this case, efficiency gains arise from both production efficiency and consumption efficiency. On the other hand, trade diversion takes place if, because of the RTA, members switch imports from low-cost production in the rest of the world and import more from higher-cost producers in the partner countries.¹⁹ Trade diversion lowers welfare of not only the partner countries but the rest of the world also. In Viner's own words:²⁰

"...where the trade-diverting effect is predominant, one at least of the member countries is bound to be injured, the two combined will suffer a net injury, and there will be injury to the outside world and to the world at large."

So it can be deduced from the above view that trade creation and trade diversion have opposite welfare implications and the net effect will depend upon which of these two effects dominate. However, Viner was unable to establish the net welfare effect of RTAs.

Subsequent to this, several studies tried to address the net welfare effects of RTAs by introducing dynamic effects into the model.²¹ Nevertheless, these efforts and analytical advances could not yield the net welfare effect of RTAs,

2015. See also: Viner, Jacob, *The Customs Union Issue*, Carnegie Endowment for International Peace, New York, (1950).

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Supra* at note 16, at 44.

²¹ Christopher S. P. Magee, 'New Measures of Trade Creation and Trade Diversion', p. 8, Available at: <http://www.facstaff.bucknell.edu/cmagee/trade%20creation%20and%20diversion,%20magee,%20august%202007.pdf>, Accessed on: Dec 5th, 2015, See also: Lloyd and MacLaren, 1999, 'On the Dynamics of Trade Diversion: Evidence from Four Trade Blocs,' *International Finance Discussion Papers* 637.

and it still remains to be theoretically ambiguous. All these arguments had resulted in a big discussion among the economists about the above stated differing points. A group of economists are of the opinion that regional trade agreements are likely to be more welfare enhancing because according to them, trade diversion is only likely to have a benign impact on the member countries.²² These economists also argue that if the member countries are geographically proximate and have very high trade dependence among each other (Natural Trading Partners), then the risk of trade diversion is minimal.²³ Expressing similar views, Krugman is of the opinion that the beneficial effect of a regional trade agreement will depend on whether there is enough 'inherent regionalism' in the transport costs between the member countries of the RTA.²⁴

This view has been contested by Bhagwati²⁵, Panagariya²⁶ and Bhagwati and Panagariya²⁷. According to these authors, trade diversion is more likely to dominate trade creation in most situations. They were of the view that in case of multilateral trade, wherein, countries import from and export to union members as well as outside countries, it is not possible to avoid trade diversion. Likewise, if the members in a regional trade agreement are few (which is always a case as compared to the outside world), there are certain

²² L. Summers, 'Regionalism and the World Trading System'-Policy Implications of Trade and Currency Zones. Wyoming: Federal Reserve Bank of Kansas City, (1991).

²³ R. G. Lipsey, "The Theory of Customs Union: Trade Diversion and Welfare"-*Economica*, p. 24, (1957).

²⁴ P. Krugman, 'Is Bilateralism Bad?' in E. Helpman and A. Razin (eds.), *International Trade and Trade Policy*, Cambridge, Mass.: MIT Press, (1991).

²⁵ J. Bhagwati, 'U.S. Trade Policy: The Infatuation with Free Trade Areas'. In Bhagwati, J. & Krueger, A. eds., *The Dangerous Drift to Preferential Trade Agreements*, Washington, D.C., American Enterprise Institute for Public Policy Research (1995).

²⁶ A. Panagariya, 'The Free Trade Area of the Americas: Good for Latin America?' *World Economy* 19, no. 5, September, 485-515, (1996).

²⁷ J. Bhagwati, & A. Panagariya, 'The Economics of Preferential Trade Agreements', Washington, D.C. AEI Press, (1996).

chances of very little trade creation taking place. As a result of this, trade diversion is likely to be the more dominant effect, under these conditions.

It is a noticeable fact here that the above mentioned entire discussion is on the negative effects of trade diversion. If this assumption is relaxed, the welfare effects of trade diversion are ambiguous and may be even positive. For example, though the creation of Mercosur has led to trade diversion, it has helped to preserve employment within the Southern cone countries.²⁸

2. Dissatisfaction with the Current Multilateral Trade Regime

The conventional analysis of RTAs does not explain why there has been a sudden increase in regionalism during the 1990s and there is lot of ambiguities surrounding it. That is why it led to an emerging consensus among economists that frustration with the multilateral trading system is one of the prime reasons behind the current growth of regionalism. In 1993, answering a question about “what are the problems of the GATT that lead countries to turn to their neighborhood”,²⁹ suggests that countries find regionalism an easier alternative because large number of participants in multilateral trade negotiations reduces the cost of non-cooperation and creates rigidity in the system. In addition to this, he was also of the view that it is difficult to negotiate in a multilateral forum and modern trade barriers are much more complicated. So most of the countries find it easier and would prefer to deal with these issues on bilateral or regional level. In the post Uruguay Round era the concerns about the multilateral trading system have intensified.³⁰ Major parts of the world especially the developing countries

²⁸ Christopher S. P. Magee, ‘Trade Creation, Trade Diversion, and Endogenous Regionalism’, Bucknell University, Lewisburg, Available at: <http://www.facstaff.bucknell.edu/cmagee/trade%20creation,%20trade%20diversion%20and%20endogenous%20regionalism.pdf>, Accessed on: Dec 5th, 2015.

²⁹ P. Krugman, “Regionalism versus Multilateralism: Analytical Notes” in *New Dimensions in Regional Integration*, eds. J. de Melo and A. Panagariya, CUP, Cambridge, (1993).

³⁰ *Id.*

were dissatisfied with the promises of the Uruguay Round agreement to expand global trade which ultimately had never come into existence. Particularly for developing countries, the promised expansion of trade in three key areas of agriculture, textiles and services has been dismal. Also, lack of willingness from the developed countries have also prompted many developing countries to look for regional alternatives as they were not getting market access on a multilateral basis by the developed nations. This has led dissatisfaction towards WTOs multilateral agreements and the North-South divide started appearing in the WTO ministerial meets. This has induced many countries to adopt regionalism as an alternate option for expanding their markets. It is not surprising that there has been a sharp increase in the formation of regional trade agreements after the failure of Seattle Ministerial meet of WTO.³¹

3. Consequence of Regionalism

Many economists including Bhagwati³², Panagariya³³ and Bergsten³⁴ were of the view that one of the major reason behind surge in regionalism is USA's transformation from a supporter of multilateralism to a follower of regionalism. According to Bhagwati³⁵ *"the main driving force for regionalism today is the conversion of the United States, hitherto an abstaining party to Article XXIV."* To support this hypothesis, it is pointed

³¹ Terence Fernandes, 'The Doha Development Round and Challenges to Multilateral Trade', E-International Relations Students, Available at: <http://www.e-ir.info/2015/07/13/the-doha-development-round-and-challenges-to-multilateral-trade-negotiations/>, Accessed on: Dec 5th, 2015. See also: Marc Wu, 'Why Developing Countries Won't Negotiate? The Case of the WTO Environmental Goods Agreement', 6 Trade L and Devlp., 93, (2014).

³² J. Bhagwati, 'Regionalism and Multilateralism: An Overview', in Melo and Panagariya eds. *New Dimensions in Regional Integration*, Cambridge University Press, Cambridge, (1993).

³³ A. Panagariya, 'The Free Trade Area of the Americas: Good for Latin America?', *World Economy* 19, no. 5, September, 485-515, (1996).

³⁴ C. Fred Bergsten, 'Competitive Liberalization and Global Free Trade: A Vision for the Early 21st Century', *Asia Pacific Working Paper Series No. 96-15*. Washington: Institute for International Economics, (1996).

³⁵ Supra at note 31 at 29.

out that many big developed countries like the USA and the European Union are increasingly getting involved in Free Trade Agreements with developing countries on a bilateral or regional level.³⁶ This has prompted many developing countries to seek participation in Free Trade Agreements with developed countries as a defensive necessity against a possible exclusion from these markets. The motivation to go for an FTA with a developed country will be particularly strong for a developing country if other countries, with which it is competing to supply goods to the developed market, are part of a preferential trade agreement with the developed country. If these non member countries cannot form an FTA with the developed country, they attempt to create their own market by joining a regional trade agreement among excluded members. This creates a bandwagon effect where no countries want to be left of some major regional groupings.³⁷ Baldwin³⁸ in his '*domino theory of regionalism*' describes similar motivation for joining regional groupings. However, Baldwin differs with Bhagwati and Panagariya in one important aspect. He believes that regionalism did not occur because countries have lost faith in GATT or because USA has adopted regionalism. Instead he feels "*resurgent regionalism was caused by idiosyncratic events that were multiplied many times over by a domino effect. In particular, announcement of the US-Mexico FTA created powerful forces for inclusion that led to NAFTA and a sequence of NAFTA membership requests. Since these requests were put off, the forced vented themselves in a series of overlapping bilateral and plurilateral agreements in the Americas. One of the –Mercosur-is generating its own domino effect.*"³⁹

³⁶ Id.

³⁷ Id.

³⁸ Richard E. Baldwin, 'A Domino Theory of Regionalism' in R. Baldwin, P. Haarparanta and J. Kianden eds. *Expanding Membership of European Union*. CUP, Cambridge, (1995). See also: Ricard E Baldwin, 'The Causes of Regionalism' - *The World Economy*, Vol. 20, No, 7, pp 865-888, (1997).

³⁹ Id at 884.

4. Other Factors

Among other important economic factors which are propagating regionalism today are foreign direct investment and the advantages associated with economies of scale. According to the World Trade Report 2003⁴⁰, preferential access to large regional markets is one of the key determinants of FDI in developing countries. As FDI has become the most important source of foreign capital inflow for developing countries, the WTR 2003 suggests that countries join RTAs to attract FDI.⁴¹ On somewhat similar reasons, it has also been suggested that smaller countries join RTAs because it can offer domestic firms the advantage of economies of scale. However, this argument does not make the case in favor for regionalism as opposed to multilateralism.

Regional Trade Agreements: Burdens Or Benefits?

As we have heavily discussed in the previous chapter about the reasons behind the recent surge in regionalism, there is another pertinent issue regarding the RTAs about whether regionalism can help or hinder the multilateral trading system thereby helping or hindering the global distribution of goods? The question is, whether regional trading blocs are “building blocks” or “stumbling blocks” of the multilateral trading system?⁴² Should we celebrate the expansion of RTAs, or should we be concerned with this trend, which seems to be only accelerating since it took off in the early 1990s? In a survey of the theoretical and empirical literature on regionalism, we conclude that although countries should approach regionalism with care, to date RTAs have been more of a blessing than a burden for the multilateral

⁴⁰ Supra at note 4.

⁴¹ Id.

⁴² Bhagwati, J. N. (2008), ‘Termites in the Trading System: How Preferential Agreements Undermine Free Trade’, Oxford: Oxford University Press, Available at: <http://object.cato.org/sites/cato.org/files/serials/files/cato-journal/2008/11/cj28n3-10.pdf>, Accessed on: Dec 5th, 2015.

trading system and thus beneficial for distribution of goods in attaining global justice.

Assessing the impact of RTAs

In order to understand the impact of RTAs, it is first important differentiate between multilateral trading system (under the regime of WTO) and unilateral liberalisation. In the former case, countries lower trade barriers on all sources of imports of a good by exactly the same extent which is oppose to an RTA, wherein tariffs fall on imports from the other members of the agreement, but they need not change on imports from non-members. And that is why; RTAs constitutes and imply both trade liberalisation and trade discrimination. Though it is also an established fact that majority of the economists are in near-consensus that trade liberalization is desirable and that is not true for the other aspect of RTAs.

Trade liberalisation within a trading bloc tends to be beneficial when it promotes a shift of resources from inefficient domestic suppliers to more efficient producers within the region. Economists call this phenomenon ‘trade creation’.⁴³ Conversely, a trading bloc is likely to be harmful if it generates a shift of resources from efficient external producers to inefficient producers within the region. This is a consequence of trade discrimination, which economists call ‘trade diversion’.⁴⁴

In principle, either trade creation or trade diversion can prevail within an RTA and there are almost no evidences to show that both can co-exist.⁴⁵ In this

⁴³ **Caroline Freund, Emanuel Ornelas**, ‘Regional trade agreements: Blessing or burden?’, CEPR Policy Portal, (2010), Available at: <http://www.voxeu.org/article/regional-trade-agreements-blessing-or-burden>, Accessed on: Dec 5th, 2015.

⁴⁴ *Id.*

⁴⁵ Athanasios Vamvakidis, ‘Regional Integration and Economic Growth’, Oxford University Press, Vo. 12, No. 2, (1998), Available at: http://www.jstor.org/stable/3990091?seq=1#page_scan_tab_contents, Accessed on: Dec 5th, 2015.

point, there are theoretical arguments that support the primacy of each effect under similar circumstances. Thus, in the end, which effect dominates is an empirical matter.⁴⁶ Unfortunately, estimating trade creation and trade diversion is no easy task. It requires knowledge of the counterfactual: what would have happened to trade if there were no trade agreement? As this is unknown, assumptions must be made.

A variety of approaches have been employed. While results inevitably vary depending on the methodology employed (as well as the time period, the trading bloc in question and the level of aggregation in the data), at least two general messages arise from the large set of studies investigating trade creation and trade diversion in RTAs around the world:⁴⁷

- First, trade creation tends to be the norm in RTAs – and trade diversion is the exception.
- Second, when trade diversion is observed, its magnitudes are normally relatively small.

Trade Creation versus Trade Diversion

Why is there such a dominance of trade creation over trade diversion? The answer is in two parts. First, governments seem to be choosing their RTA partners well. For example, variables that suggest greater gains from a bilateral RTA (such as proximity between the members, a similarity in their GDPs and a large difference in their factor endowments) are also sharp predictors of whether the two countries actually have a common RTA.⁴⁸ Second, when countries form an RTA, their governments not only lower

⁴⁶ Id.

⁴⁷ Id.

⁴⁸ Scott Baier and Jeffrey Bergstrand, 'Economic Determinants of Free Trade Agreements', *Journal of International Economics*, p. 64, (2004), Available at: http://www3.nd.edu/~jbergstr/Working_Papers/Growth_of_Bilateralism.pdf, Accessed on: Dec 5th, 2015.

tariffs vis-à-vis their RTA partners, as they are supposed to do; they also bring down the trade barriers on imports from countries outside the bloc. This is not part of the agreement, so governments liberalise externally because they choose to do so and without any type of reciprocity from the favoured non-members of the bloc.⁴⁹

There is increasing evidence of external trade liberalisation following an RTA, especially in developing countries. For instance, an analysis of how Latin American countries changed their import tariffs on non-members after forming or expanding their trade ties during the 1990s.⁵⁰ The lower external tariffs provide a double blessing, they imply that RTAs are responsible for more trade liberalisation than they mandate (amplifying trade creation) and for less trade discrimination than might be expected (limiting trade diversion). Though it may seem to be odd that governments, due to special interests would voluntarily lower their external tariffs without any compensation from the favoured countries, but it does make sense.

Suppose that domestic special interest groups pressure the government and induce it to set relatively high tariffs, which allow the domestic industry to maintain high prices and enjoy a large market share. If subsequently the country enters into a RTA, export-oriented firms benefit (and support the agreement) because of the better access to foreign markets, whereas purely domestic firms suffer from the tougher competition from the RTA partners.

But this also weakens the domestic firms' stance on protection against non-members. The reason is that the free access to the domestic market enjoyed by the partners' exporters under the RTA lowers the market share of the

⁴⁹ Antoni Estevadeordal, Caroline Freund and Emanuel Ornelas 'Does Regionalism Affect Trade Liberalization towards Non-members?', *Quarterly Journal of Economics* p. 123, (2008), Available at: http://eprints.lse.ac.uk/19584/1/Does_Regionalism_Affect_Trade_Liberalization_Towards_Non-Members.pdf, Accessed on: Dec 5th, 2015.

⁵⁰ *Id.*

domestic industry. As a result, the RTA makes any price increase generated by a higher tariff less valuable for the domestic industry: now whenever the government attempts to help domestic producers through higher external tariffs, the partners' producers absorb part of that surplus.

In other words, the RTA creates 'leakage' in the trade policy redistributive channel. External protection also becomes more costly, because of the trade diversion that accompanies the RTA. As a result, external tariffs tend to fall after the formation of an RTA both because the economic marginal cost of external protection rises and because the political economy marginal gain from external protection falls.

For developing countries, empirical research supports this rationale because trade preferences tend to lead to lower external tariffs. Results for the United States and the European Union (EU), however, indicate that they are less likely to reduce external tariffs on goods where preferences are offered.⁵¹ But since the tariffs of both the United States and the EU are very low to start with, and cannot be raised because of their WTO commitments, there is not much room for change anyway.

Are RTAs welcome for trade justice?

The benign view that trade creation dominates trade diversion does not imply that RTAs are necessarily welcome. In fact, some commentators argue that the multilateral negotiations at the WTO are stuck because RTAs are spreading. Their basic argument suggests that governments' resources are scarce, so if officials are busy negotiating bilateral agreements, they will be unable to focus on more evolving multilateral negotiations. On the other hand, there are arguments indicating that the opposite may be true. A simple

⁵¹ Nuno Limao 'Preferential Trade Agreements as Stumbling Blocks for Multilateral Trade Liberalization: Evidence for the US', *American Economic Review*, p. 96, (2006)

one is that negotiating RTAs helps officials to develop the expertise and the frameworks to implement international trade agreements, and these could be useful at subsequent WTO negotiations.

But the question arises, which of them dominate? When faced with opposing theoretical results, the solution is typically to scrutinise the divergent predictions empirically. The problem here is that the nature of the question whether regionalism helps or hinders multilateralism does not lend itself easily to testing. Simply put, at any point in time we observe a single realisation of WTO negotiations. Would they have been any faster, or easier, had there been fewer (or more) RTAs? This is a very difficult question. Consequently, to date empirical scrutiny has not been able to help us distinguish good (that is, empirically relevant) from bad (empirically inconsequential) theories.⁵²

Hence, to the extent that we can measure, the increasing wave of regionalism has been largely beneficial to the world trading system. Most empirical analyses indicate that trade creation, not trade diversion, is the norm, both because governments choose well when forming RTAs and because they adjust other trade policies to moderate the distortions from discrimination.

Regional trade agreements and trade justice

Trade justice is a crucial issue on which theory is fast developing, but the judgments offered by the major theories of trade justice often remains unanswered or rather ambiguous. This is because there are many empirical questions involved and there are a lot of conflicts regarding them. And that is the reason why potential impact of these trade policies is not clear. But this is

⁵² Marsha A. Echols, 'Regional Economic Integration', *The International Lawyer*, Vol. 31, No. 2, p. 453-462, *International Legal Developments in Review: 1996 (Summer 1997)*, Available at: http://www.jstor.org/stable/40707325?seq=1#page_scan_tab_contents, Accessed on: Dec 5th, 2015.

not in case of global justice where there is some amount of guidance as to what are the normative standards of trade and if these are applied in international trade, are available.⁵³

In the present chapter we shall examine the contours of what global minimalists and global egalitarians have had to say about the issue of justice in international trade and how it can be related to regional trade agreements. Generally speaking, as we would expect, global minimalist have always been concerned about setting out the minimal standards of fairness to which trade ought to conform.⁵⁴ They have sometimes argued that it ought, for instance, to be broadly, non-exploitative, and that the rules of trade should not be set by more powerful countries in their own interests. But minimalist are sometimes reluctant actually to apply standards of distributive justice to trade, or to argue that it is wrong, from the point of view of justice, if the benefits of international trade are spread unequally. So long as countries are able to participate in international trade on generally fair terms, and so long as the outcomes do not threaten their independence, we should not be concerned if the eventual outcomes are unequal.

Egalitarians accounts do often a direct concern with the unequal outcomes which international trade produces.⁵⁵ They do not look forward to the ideas of minimalist instead they had the view that international trade should assessed from the perspective of justice, and that the current account of justice for these purpose is egalitarian in fundamental principle.

The author would support the views of egalitarian principles in doing international trade specifically regional level international trade so as to

⁵³ Chris Armstrong, *Global Distributive Justice: An Introduction*, Cambridge University Press, p. 168, Available at: <https://books.google.co.in/books?id=LJU0djAZ1osC&q=regional+trade+agreements#v=onepage&q=trade%20justice&f=false>, Accessed on: Dec 5th, 2015.

⁵⁴ *Id* at 166.

⁵⁵ *Id*.

achieve equal outcome for both the developed and developing nations.⁵⁶ This is so because gulfs in income or living standards across the various countries of the world are regrettable, which is evidently unjust in its nature. Similarly, it can also be argued that why more privileged people such as citizens of developed countries have some kind responsibility to respond to the fact that other people lack access to clean water, adequate nutrition or basic education, which ought to imply that they have an obligation of justice and this can be attained by the trade agreements.⁵⁷ It is also true that why some have a great deal more than others simply because of the country they happen to have been born into and declare them to be unjust.

Now if we to go about the idea favored by minimalist then it would again lead to inequality as they favor minimal level of justice that is meted to the actual people who need it the most. This argument is in itself morally arbitrary as why people should suffer because of that which they had no option to choose i.e. nationality. Therefore this argument is self-destructing and favors the mighty nations which were never contemplated in the concept of international trade. Therefore it is hereby put forth that the idea of trade justice should be following the fundamentals of egalitarianism so as to achieve global justice.

Coming to the regional trade agreements, it is true that it has brought many positive results in the global trading system but it is also a fact that this has not achieved or followed the principles of egalitarianism. The fact that Doha declaration and Cancun declaration failed reveals that the powerful and developed nations were reluctant to agree on the terms of the developing

⁵⁶ Darrel Mqellendorf, *The World Trade Organization and Egalitarian Justice*, *Metaphilosophy*, Vol. 36, No. 1/2, Blackwell Publishing Ltd., (2005), Available at: http://www.readcube.com/articles/10.1111%2Fj.1467-9973.2005.00360.x?r3_referer=wol&tracking_action=preview_click&show_checkout=1&purchase_referrer=onlinelibrary.wiley.com&purchase_site_license, Accessed on: Dec 5th, 2015.

⁵⁷ *Supra* at note 53 at 11.

nations which assure distributive justice to all indulged in trade. Therefore, in the light of the above discussion we can infer that regional trade agreements are just when entered into between same levels of economies that is among developing nations or among developed nations and it would render injustice if entered into between unequal partners.

Conclusion

This paper gives an overview of the main issues associated with the contradiction between regionalism and multilateralism and whether RTAs contribute towards attaining global justice in the distribution of goods. As the above discourse shows, at a theoretical level, economists are divided over the desirability of regional trade agreement in a multilateral trade regime. Even after fifty years of debate, there is still no consensus about this issue. However, regionalism, with its advantages and drawbacks, is a reality of the current global trade regime. And given the economic and political situation of the current world order, the wave of regionalism is likely to intensify in near future. If the explosive growth of regionalism continues, then it is bound to have positive effect on trade justice and mobilization of goods in the world's economy. The survey of literature indicates that the explosive growth of regionalism in the 1990s happened mainly because of two reasons. Among developing countries, the growth in regionalism took place mostly due to the dissatisfaction with the multilateral trading system. Also, due to a host of political and economic reasons, major developed countries like USA have perused regionalism aggressively during the 1990s. Many economists believe that this has led to a bandwagon effect of regionalism as most countries wanted to be part of at least some major trade blocks.

In this context, South-South RTAs are particularly useful as they allow developing countries to expand their markets without having to bow before

hegemonic powers. However, there are some obvious pitfalls with regionalism. Apart from the problems of trade diversion, the complex web of regional agreements can also introduce uncertainties and opacity in the global trade system. Secondly, the problems associated with unequal power structure and exploitation of smaller members by a bigger economic power can be more acute in a regional trade block. Also, it is always possible that if the world is divided in a few mega trade blocks, then the weakest countries will be marginalized. Therefore, theoretically speaking, regionalism does not offer the best solution. However, in the current state of distorted multilateralism, regionalism has turned out to be one of the more viable alternatives for developing countries to expand their market access and thus to a great extent has ensured trade justice.

