

**THE ROLE PLAYED BY FREE TRADE AREAS AND REGIONAL TRADING  
BLOCS IN PROMOTING GLOBALLY REGULATED TRADE REGIME:  
A GENERAL OVERVIEW**

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**Abstract**

*Trade drives the world economy and forms the basis upon which development can be realized. Towards the turn of the 20th century into the new millennium, a proliferation of multilateral institutions dealing with trade within the form of Free Trade Areas (FTAs) and Regional Trading Blocs (RTBs) has been witnessed. The extent to which these institutions are facilitating the establishment of a globally regulated trade regime has largely been questioned. Therefore it is the purpose of this paper to examine the extent to which FT As and RTBs facilitate such a role, noting the challenges and prospects for a globally regulated trade regime.*

**Introduction**

In the world today, what appears noticeable is that Regional Trading Blocs (RTBs) and Free Trade Areas (FTAs) are growing and some that had faded are re-emerging. The question that arises is whether these moves are necessitating the existence of a globally regulated trade regime, which is the overall objective in enabling better trading practices for the benefit of all international actors that matters. The paper therefore seeks to establish whether FT As and regional trading blocs are contributing towards a unified global economy or are in themselves stumbling blocs towards the effort to realize a global multilateral trading system. An attempt will also be made to evaluate the relevance of a globally regulated trade regime especially in a world that features

unequal power amongst states and where anarchy prevails.

### **Conceptual Framework**

A Free Trade Area refers to a form of economic union between states in which members agree to abolish tariffs and other restrictions on stipulated goods between themselves vis-à-vis the rest of the system in which they continue to maintain their existing tariffs (Evans G. and Newham 1990:103). A regional trading bloc is a group of actors with common interest in better trade relations with a possibility of leading to closer cooperation and integration in the long term (Evans G. and Newham 1990:320). Typically trade pacts that define such a bloc specify formal adjudication bodies, e.g. NAFTA trade panels. This may include even a more democratic and participative system, as the EU and its parliament. Since the demise of most of the world's empires, a number of regionally based economic blocs have been developed to promote trade between member states ([http://en.wiki/Trade\\_bloc](http://en.wiki/Trade_bloc)).

Varieties of economic blocs include free trade areas, customs unions, single markets, and economic and monetary unions ([http://en.wikipedia.org/wiki/Trade\\_bloc](http://en.wikipedia.org/wiki/Trade_bloc)).

Regional trade blocs are intergovernmental associations that manage and promote trade activities for specific regions of the world ([http://ucAtlas.ucsc.edu/trade/subtheme\\_trade\\_blocs.php](http://ucAtlas.ucsc.edu/trade/subtheme_trade_blocs.php)). In international trade, free trade is an idealized market model, often stated as a political objective in which trade of goods and services between countries flows unhindered by government-imposed tariff and non-tariff barriers. This arrangement is supported by microeconomic analysis and nearly all economists, who argue that the benefit of trade is a net gain to both trading partners. (<http://en.wikipedia.org/wiki/Freetrade>).

It is accurate to assert that FTAs and RTSs have actually increased in the contemporary world particularly given the pace at which globalization is moving. In relation to this, Shalla and Shalla (1997) have noted that the past decade has witnessed the emergence of regional economic groupings and the revitalization of existing ones. Examples can be drawn from the developed world's North American Free Trade Area (NAFTA), Central European Free Trade Area (CEFTA), the European Union (EU), and common Market for Southern Cone (MERCOSUR) and also from developing world, Southern African Development Community (SADC), ASEAN, Common Market for East and Southern Africa (COMESA). Some draw membership from both the developed and developing countries like NAFTA, Asia Pacific Economic Cooperation (APEC) and African Caribbean Pacific Group (ACP-EU).

### **Role in Facilitating Global Trade**

The prime force has been globalization, where a desire has emerged to tackle common problems that arise as a group of countries rather than confronting the negatives of globalization as individual states and mostly being weak and vulnerable, and also the desire to move the world towards each group's interest.

An analysis of the trends of contemporary moves towards FTAs and regional trading blocs is necessary to bring the reasons behind the renewed interest. According to Shalla and Shalla (1997) the new groups have emerged under the paradigm of economic liberalization and market regulation. This has emerged with the end of the cold war era where the world economy has become increasingly interdependent. The effect this has on many countries especially those in the developing countries is that of liberalizing trade unilaterally as a component of reforms in macro economic, trade and industrial policies.

It is clear that reforms are being introduced with the aim of raising production and efficiency and increasing international competition. This would actually enhance a globally regulated trade regime as these groupings are doing with an open multilateral trade frame that would provide policy regimes that are identical throughout the world.

Recent trends in regionalism and development of FT As would differ greatly from the past particularly the period from the early 1980s and before. During this period, emphasis was put on policies that included discrimination, being inward looking, and protective tariffs as means of promoting growth and import substitution that disrupted the establishment of globally regulated trade. This was so because exclusion of others met disagreements and conflict that made it difficult to agree on major issues in trade. This would differ with open regionalism, which according to Garnaut (1994) denotes "regionalism without discrimination against economies outside the region", what is virtually associated with outward looking export oriented economies. Thus this would establish an environment that is aimed at consensus, as interaction is open to all rather than favoring others.

It appears that the new wave can be viewed more in terms of scale economies, product differentiation, efficiency gains and policy co-ordination rather than trade gains from diversion. This indicates that the move towards globally regulated trade is a long way. There are continued inter linkages in terms of trade especially given the role of foreign investment in regional integration after a genuine drive towards consensus on trade issues in both developing and developed world designs FT As and regional trading blocs in line with global trends. As such, one can acknowledge HAs in the contemporary world as a means of attracting foreign direct investment and achieving global competitiveness in trade which encourage rather than militating against a globally

regulated trade regime. This is particularly true given the fact that past regional integration moves did not go beyond linked preferential arrangement.

Today, according to SAPEM (2001), SADC takes into consideration overall policy framework for Africa as a whole embracing initiatives like the Abuja Treaty, Lagos Plan for Action, African union objectives and NEPAD as its rallying point fulfilling the role of policy coordination for the African country. The same objectives are being followed in West Africa paving way for better integration of regional trading blocs towards a globally regulated trade regime.

One move that is characterizing the recent growth of HAs and regional agreements is the realization for those who are left out to either form their own or join the existing ones to avoid marginalization. This is quiet critical to ensure that all participants become part and parcel of global trade with some policy framework hence working towards achieving the same objective. The most encouraging move has been the overlapping of membership in most of the HAs and regional blocs. For example, the Southern African Customs Union (SACU) whose members are also in SADC and some are also in COMESA. Also in Europe, where EU has a different composition in terms of members, with some, if not all, belonging to the European Free Trade Association (EFTA) whose members like France, UK have special trade links with the African Caribbean and Pacific (ACP) and British Commonwealth. The same can be said of NAFTA and APEC. This move actually encourages inter-linkages that necessitate the existence of globally regulated trade-In Bhalla and Bhalla's (1997) words this would enable members,

*To secure access to different regional minds particularly where regional blocs demonstrate protectionist tendencies against each other. In their diversifying trade and investment, regional blocs have a move to reduce*

*dependence on major trading partners such as US multiple memberships by major industrial countries may also be indicative of the desire to bring regionalism in line with multilateralism.*

An interesting phenomenon that will enable the move towards globally regulated trade has been the close cooperation between the North and the South. This enables the close linkages in terms of trade between the poor and the rich, the rich providing a backing that is necessary to enhance them within the global framework. The EU - ACP countries, NAFTA, The Enterprise for American Initiative (EAI) that include Latin American countries and the APEC where US is dominant and is helping harmonizing the concerns by enabling countries from developing countries to move from import substitution to export oriented trade are good examples.

There has been an argument that FTAs and trading blocs feature trade diversion, which injures multilateralism. Though this is true, what ought to be observed, according to Bhalla and Bhalla (1997) is that "trade creation and trade diversion can occur at the same time and the former may more than compensate to create a net positive effective on the growth of global trade".

### **The Challenges**

In as much as the above discussion has highlighted on FTAs and regional trading blocs enabling multilateralism in global trade and capturing the wishes of many economist and policy analyst, there is a doubtful mind to this. Firstly, according to Shalla and Shalla what appears to emerge is that regional blocs and FTAs fragment world trade thus, undermining the goal of globalization. This is true given that these formations are there to counter the force of the others. When it comes to bargaining, this may lead to

conflicts rather than enhancing global trade. An example could be drawn from major trading partners at the EU, NAFTA and East Asia nations. These powerful trading blocs according to Kruger have sizeable and growing markets, which do not make it imperative on them to respect the rules of multilateralism, or facilitate its enforcement. Some authorities like Shalla and Shalla (1997) have actually noted this, citing the behavior of the US, which joins regional arrangements in order to control the rules. This can be seen with the move to accept regionalism in North America but not elsewhere, as frequently it has opposed the Asian trade bloc led by Japan. It seems to be the reason why the US subscribed to APEC where it could counter balance Japanese influence by becoming a major participant in the forum. In so doing, one can actually note that FTAs and regional trading blocs have become enlarged states denoting that their behavior is not different from states themselves each with its agenda and interest to protect rather than fighting for bringing global consensus.

Secondly, despite the presence of Article XXIV of the World Trade Organization (WTO) what can largely be seen today in the behavior of regional trading blocs and FTAs is that trade diversion is rampant, of which, at most, its existence militates against the experience of globally regular trade. Shalla and Shalla (1997), draw examples of the creation of a single European Market, where, though tariffs barriers within Europe have decreased, tariff barriers against developing countries have increased. The Creation of NAFTA can be viewed in the same way especially with the continued inward looking policies of the US in the whole region and also the move to Japan in ASEAN where she wants to control those markets and effectively protect against foreign goods and services. At most, the regional blocs and FT As will reflect the desires of the leading countries that are not in harmony with multilateralism.

Though it has been argued that trade creation and trade diversion can work together to create multilateralism this is quite fallacious. This is because trade diversion leads to the creation of new interest groups who would oppose a move towards an open system. In the US for example, trade deficits and hardships resulting from structural adjustment forced on the US as a result of liberalization have created a build up of domestic pressures to protect certain sensitive sectors from extensive competition. This is likely to affect NAFTA and the US the leading member in NAFTA, as it will reflect an aggressive unilateralism to benefit itself. This will spark reverse application by other trading blocs. FTAs, for instance, ASEAN and Japan will retaliate and at individual level Japan, Cuba and China have even threatened retaliatory action.

Thus from political logic, it is difficult to bring multilateralism where rules governing global trade would be seen beneficial to all. Kruger has noted that this is so because those who benefit from trade diversion may be inclined to oppose an open multilateral trading system. EU for example is likely to withdraw support for multilateralism given its growing membership and higher level of intra-regional than extra-regional trade. At most it violates and undermines GATT's most favored nation (MFN) principle on non-discrimination and open competition because of its multitude of different preferential agreements with other regions like EFTA and ACP.

Another problem has to do with the inviolability of the state especially, its desire to be sovereign to issues that will further its interests. Multilateralism appears good only when it benefits citizens of a country or the region and if it hurts there is a likelihood of failure that would militate against globally regulated trade region. Most states have a tendency to pursue those policies that are advantageous to them and not necessarily that are beneficial to all. The problem affects mostly developing countries who have formed

FT As and trading blocs to ensure their survival in the globalizing world hence they will tend to be inward looking, practicing import substitution, where government rather than the market plays a role, discriminating against the rest of the world because of potential costs and encouraging south - south cooperation. This will actually generate a ground of opposition from the world over. Bhagwati (1995) has noted citing the case of the US where American Policy makers have invoked section Super 301 of the US 1974 Act where specific goods and services are protected and practices considered unacceptable by US regardless of whether they are acceptable by WTO standards or any other treaty are not observed. This preferential treatment by the US given also that it is the leader in the world economy will spark reactions leading to the development of FT As to counter such moves particularly by those countries who have been affected by this clause like Brazil, China and India, in 1989 and Japan in 1990. (Bhagwati 1995) This will militate against a globally regulated economy particularly given the move of the US in NAFTA and AEC.

It has to be highlighted that all developed countries have used protectionism, but usually reduced it as they gained more wealth. The Constitution of the United States explicitly prohibits state governments from enacting barriers to trade between citizens and firms of the various 50 states, making the United States the largest empirical example of free trade in the world .([http://en.wikipedia.org/wiki/Free\\_trade#Regional\\_trading\\_blocs](http://en.wikipedia.org/wiki/Free_trade#Regional_trading_blocs)).

Though it has been argued that contemporary FTAs and regional trading blocs have a new dimension such as that it is market driven, export oriented, non discriminatory. North-South membership and overlapping membership makes it possible to establish a globally regulated trade regime, but what seems to exist in reality is that old dimensions are in existence threatening as they have done before. In actual fact,

marginalization is growing. In Africa for example, regional blocs remain marginalized raising the possibility of developing countries' FTAs and regional trading blocs to fight globalization (Bhalla and Bhalla 1997). For example, moves to the African Economic Community seem to slow down the pace, which the world desires of a globally regulated regime. In Asia, import substitution is rampant; for example, SMRC differs with ASEAN, which is more open creating an atmosphere of misunderstanding in the region itself, and possibility of trade wars likely.

In America, NAFTA discriminates against Caribbean Basin and Central American Countries whose clothing industry is quite competitive. In Europe, EU has been labeled the Fortress of Europe because of its policies that are highly protectionist especially the Common Agricultural Policy (CAP), the Voluntary Export Restraint anti-dumping distorting the fair conduct of world trade affairs. In addition, European countries favor colonies for instance France - ACP and British Commonwealth relations. In Europe also, the increase in membership especially after the end of the cold war has created demand for protection of sensitive products against external competition. However, this does not overlook the fact that the addition of once commonest economies into liberal ones is one step further to the understanding required for globally regulated trade regime.

A globally regulated trade is important and it appears a grouped world in the form of regional trading blocs and FTAs will make it easier to negotiate global reductions in trade barriers than if all countries entered on their own. But given weaknesses that often develop with FTAs and regional blocs in attempting to harmonise issues in trade what should be the way forward? According to Shalla and Shalla (1997) three things need to be done. Firstly, regional trading blocs should lead to net trade creation rather than trade diversion. Thus if both intra-regional and ex-regional trade expand as is the case with

APEC, regional blocs will not act as stumbling blocs to growth of trade thus leveling trade barriers against member. Secondly, FTAs and regional trade blocs need to be growth inducing. This should contribute to the expansion of extra regional exports and imports from the rest of the world (Shalla and Shalla 1997). Thirdly, the formation of regional trading blocs would make it possible for more effective regulation for achieving the positive results of multilateral trade as the EU has done under the Uruguay Round (Shalla and Shalla 1997).

Another solution to the problems is that FTAs and regional trading blocs should shape behavior to bring ways that are marginally useful and minimally damaging and consistent. For example the US in NAFTA should line up with the South American countries into NAFTA and encourage Japan to line up of all the Asian countries all the way to the Indian sub continent into AFTA. Japan and the USA, the two hubs would then meet to collate into large FTAs.

Bladwin advises that Reform of the Article XXIV of WTO will be necessary to close loopholes, which allow the dialogue between goods of regionalism and multilateralism. WTO rules have not been able to control the frequent resort to contingent protection such as the misuse of anti dumping sections particularly by the EU and the increasing use of fair trade laws by the US will necessitate the move towards globally regulated trade.

A question that is often raised is whether globally regulated trade will benefit all. To the weak developing economies, it appears benefit is not likely to accrue, as it will to developed economies. According to Mokheber and Wiesman, the WTO hurts the third world, through its demands to open their economies to rich countries, abandon efforts to protect infant industries and opening foreign imports, which will trigger massive social

unrest. This makes it impossible for developing countries to feel, through FTAs and regional trading blocs, that they constitute a formidable force in the creation of a globally regulated trade regime. Though it creates winners and losers, the broad consensus of the economics profession is that free trade is a large and unambiguous net gain for society ([http://en.wikipedia.org/wiki/Free\\_trade#Regional\\_trading\\_blocs](http://en.wikipedia.org/wiki/Free_trade#Regional_trading_blocs)).

### **Conclusion**

It is very difficult to conclude whether FTAs and regional trading bloc's mayor may not contribute towards a globally regulated trade regime. But it appears apparent that moves being pursued today are harmful to the objective of establishing multilateral trade regime. Everything depends on the policy response of the US, EU, and Japan to evolving trade and domestic constraints. The Uruguay Round is supposed to move beyond inward looking tendencies by regional blocs since it is difficult to enforce discussion relating to Article XXIV of GATT and WTO. Greater success is dependent on how the WTO responds to changing dynamics of trade so that it will prevent nations from acting unilaterally with a regional framework to protect their own interests.

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