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It Takes Two to Tango: The Case of FTA Explosion World-Wide for 1948-2012

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A B S T R A C T

Embarking on the second decade of the 21st century, we see an explosion in the number of free trade agreements (FTAs) already in effect or under negotiation. FTAs are an exercise of sovereignty negotiated for the purpose of eliminating trade barriers and creating ground rules to manage a trade relationship in a beneficial manner. The reduction of trade barriers and the creation of a more stable and transparent trading and investment environment make it easier and cheaper for companies to export their products and services to trading partner markets.
Trade liberalization through FTAs has paid enormous dividends to partnering signatories and expanded world trade and economic growth. This paper looks at the evolution of FTAs from the post-World War II era to the beginning of the second decade of the 21st century. It explains FTAs, their advantages and disadvantages, their role in promoting global trade and investment, the impact of their growth on the global trading environment, and their potential relationship with the WTO structure.

Keywords: Free Trade Agreements, Trade Barriers, Global Investment

Ⅰ. Introduction

Free Trade Agreements (FTAs) are vehicles for countries to negotiate bilateral agreements for specific purposes which are meant to help open markets for exports, expand economic growth, and eliminate tariffs and nontariff barriers on trade in goods within the free trade area. At the same time, each country maintains its own trade policies on trade outside the region including tariffs. FTAs continue to expand in today's business world but not without debates on their advantages and disadvantages. FTAs have been on the forefront of the trade policy agenda for over 40 years since the Treaty of Rome—the precursor to today's European Union (EU)—became the first modern free trade agreement to enter into force in 1958.

The last two decades have seen an unprecedented surge in FTAs as part of efforts to promote regional trade and investment. According to WTO estimates, 300 agreements were in force worldwide in 2010 compared to only 70 in 1990 (World Trade Organization, 2011). For example, the United States had FTAs with only four countries in 2000, and it has now concluded FTAs with 20 countries. Additionally, regional FTAs are on the rise. The Association of Southeast Asian Nations (ASEAN) has entered into FTAs

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with China, Japan, South Korea, India, and most recently, Australia and New Zealand. In an effort to establish free trade among Pacific Rim countries, the United States is currently negotiating a Trans-Pacific Partnership with Australia, Chile, Vietnam, New Zealand, Brunei, Singapore, Malaysia, and Peru (Meltzer, 2011). The steadily increasing trend is likely to be strengthened by the many FTAs currently under negotiation. As of November 15, 2012, some 505 FTAs, counting goods and services notifications separately, have been notified to the GATT/WTO. Of these, 367were notified under Article XXIV of GATT 1947 or GATT 1994, 36 under the Enabling Clause, and 102 under Article V of the GATS. At that same time, 354 agreements were in force. The growth of FTAs from the post-World War II period until the end of 2012 is depicted in Figure I.

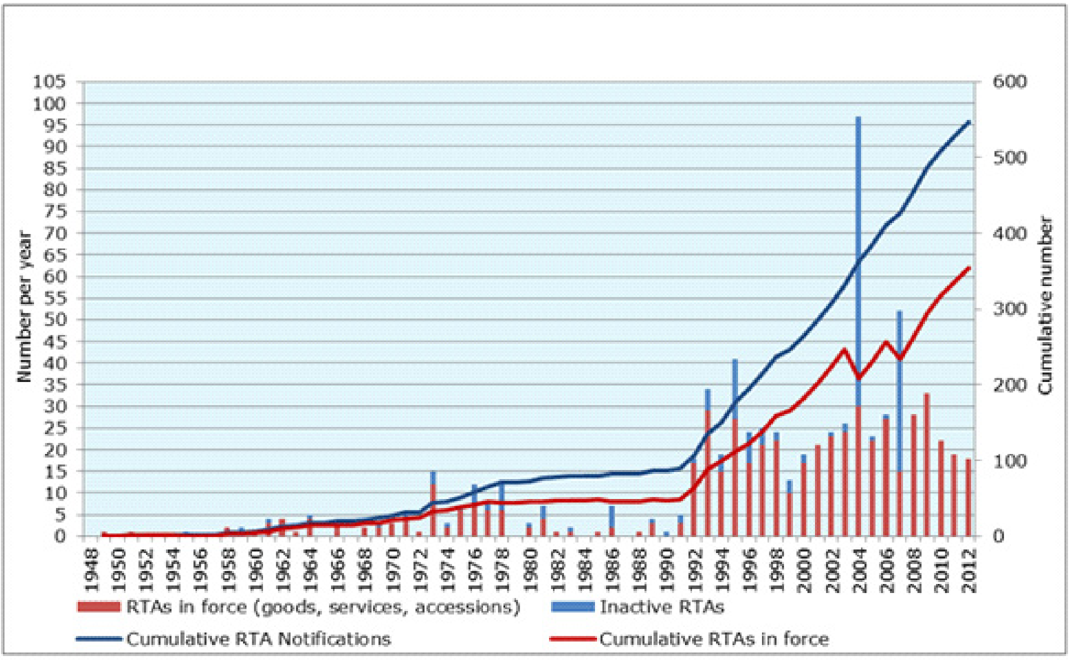
Ⅱ. Theory behind FTAs

The traditional theory of economic integration starts with the paradigm of Viner (1950) which accounts for the net effect of trade creation and trade diversion in a world composed of a protectionist bloc and the rest of the world.

Later on, this conceptualization evolves to a world composed of several *natural* blocs with the acknowledgement of transport costs. The natural trading bloc model focuses on the possibility of improving partners' welfare without worrying about the possible deterioration of trade with the rest of the world. One of the searches for an arbitrage opportunity between regional and global welfare resides in a radically different treatment of new regionalism. In contrast to trading protectionist blocs, new regionalism encourages the development of the multilateral trading system. The *old regionalism* regroups countries with similar levels of development. In contrast, *new regionalism* is characterized by an asymmetric level of development among members in the context of outward policies (Ithier, 1998b). Meanwhile, the new regionalism is inserted into a framework of policy reform that promotes open and competitive private market-based economies (Toh Mun Heng, & Gayathri, 2004).

From a theoretical perspective, FTAs can provide both advantages and disadvantages which are rooted in the twin concepts of trade creation and trade diversion. Trade creation

Figure I. Evolution of Regional/Free Trade Agreements in the World, 1948-2012



Source: WTO Regional Trade Agreements: Facts and Figures, 2013 occurs when a member of an FTA replaces domestic production of a good with imports of the good from another member of the FTA because the formation of the FTA makes importing cheaper to than production domestically. The creation of the trade is said to improve economic welfare within the group because resources are being shifted to more efficient uses. Trade diversion occurs when a member of an FTA switches its import of a good from an efficient nonmember to a less efficient member because the removal of tariffs within the group and the continuation of tariffs on imports from nonmembers make it cheaper to do so. Trade diversion is said to reduce economic welfare because resources are being diverted from an efficient producer to a less efficient producer (Cooper, 2012).

Given the importance of the topic, it is no surprise that a large literature on FTAs exists. Bhagwati et al. (1999) and more recently Saggi and Sildiz (2011) provide excellent reviews of some of the important contributions in the area. Aghion et al. (2007) examine a country's choice between sequential and multilateral bargaining of FTAs, and they identified both positive and negative effects of FTAs. Jackson and Wolinsky (1996), Krishna (1998), Goyal and Joshi (2006), and Furusawa and Konishi (2007) have applied the network formation game to examine whether or not a given trade configuration is pair-wise stable. Under symmetry, they find that the continued formation of bilateral FTAs leads to global free trade while asymmetric agreements often act as restrictions to global free trade. However, Krishna (1998) has shown that the formation of an FTA between two countries reduces their incentives to liberalize trade with respect to a third country.

Effects in trade theory:

Following are some of the common effects that FTAs have according to a number of trade theories:

The love of variety effect: Consumers benefit from being able to spread their expenditure across a wider variety of goods (Krugman, 1979) or being able to buy at lower cost goods to meet specialized individual taste (Lancaster, 1979).

The competitive (profit margin) effect: In imperfectly competitive sectors, firms will charge lower profit markups with correspondingly lower welfare cost where they face keener competition. This is generally the case where it is easier for foreign firms to enter the market after an FTA is formed. There is also a related bargaining effect in some models where keener product market competition restrains union wage-setting.

The scale effect (Krugman, 1979): Firms may be able to reap economies of scale after an FTA is formed by operating at a bigger scale across two markets. For this to happen requires a shakeout of some existing capacity.

The profit shift effect: In an imperfectly competitive model, the prices charged by firms exceed marginal cost. Consequently, if the foreign country raises its market share in the importing country following an FTA, foreign firms will gain higher profits at the expense of local firms. There will therefore be some redistribution of income between members of an FTA.

The capital movement effect: If an FTA results in expanding demand, and this raises returns on capital, then capital may flow into the FTA. This is particularly true in studies of previously isolated regions joining an FTA such as the EU accession states. The GDP gains need to be weighed against the opportunity cost of this capital.

The firm selection effect: This is currently the subject of much theoretical and firm-level analysis (Hironi & Melitz, 2005; Bernard, Eaton, Jensen, & Kortum, 2003). In models where firms are heterogeneous, increased foreign competition drives high-cost local producers out of the market while the efficient firms may survive. At the same time, there are typically fixed costs of entering a foreign market; lowering these costs results initially in a rise in output by only the more efficient local firms which start exporting. However, eliminating barriers which were initially low may have the opposite effect thus enabling relatively less efficient producers to start exporting.

Trade policymakers often encounter circumstances much more complicated than those depicted in economic theory. Many functioning and proposed FTAs encompass more than two countries and involve a range of products, both goods and services, making evaluating their economic impact much more challenging. To provide an analytical framework, some economists have developed sets of conditions under which, they conclude, an FTA would create more trade than it diverts. They state that trade creation is likely to exceed trade diversion under the following conditions: the larger the tariffs or other trade barriers among members before the FTA is formed, the lower the tariffs and other barriers in trade with nonmembers, the greater the number of countries included in the FTA, the more competitive or the less complementary the economies joining the FTA, and the closer the economic relationship among the members before the FTA was formed.

Ⅲ. Reasons for Free Trade Agreements

Free Trade Agreements are vehicles for countries to negotiate bilateral relationships for specific purposes and in many respects pursue similar objectives. Some reasons for FTAs include securing open markets for exports, eliminating tariffs and non-tariff barriers, protecting domestic producers from foreign unfair trading practices, controlling trade for foreign policy and national security reasons, helping foster global trade and economic growth, and delivering trade related benefits beyond what can be achieved through the WTO (Fergusson, 2008) .

While economic motivations are generally the major driving force for the formation of FTAs among countries, there are other reasons countries enter into FTAs including political and security factors. For example, one of Mexico's primary motivations for the unilateral trade liberalization efforts of the late 1980s and early 1990s was to improve economic conditions in the country, which policymakers hoped would lead to greater investor confidence and attract more foreign investment. This motivation was a major factor in negotiating the North American Free Trade Agreement (NAFTA) with the United States and Canada. The permanent lowering of trade and investment barriers and predictable trade rules provided by FTAs can improve investor confidence in a country, which helps attract foreign direct investment (FDI). Multinational firms invest in countries to gain access to markets, but they also do it to lower production costs (Fergusson, 2008). The advantages and disadvantages of FTAs are summarized in Table 1:

Ⅳ. Economic Impact of FTAs

The formation of FTAs worldwide raises the question of their impact on the countries included in an FTA and on the rest of the world. Economists have long studied and debated this issue, and interest in the issue peaked at various times in the post-World War II period. The first time was the formation of the European Common market. Interest peaked again with the current trends in FTAs. The debate relies largely on theory because empirical data are scarce save for the experience of the European Union. The debate has also divided economists between those who strongly oppose FTAs as an economically inefficient mechanism and those who support them as a means to build freer trade (Cooper, 2005; 2012).

Economists also continue to argue about the merits of free trade agreements relative to the multilateral system of the WTO. Much of the argument centers on the potential for FTAs to result in important amounts of trade diversion as importers redirect their purchases to new preferential suppliers and away from those in other countries that may be the lowest cost producers. Another argument that detractors raise is that FTAs are a political distraction from the WTO system; and that over time, the creation of additional bilateral agreements will undermine support for the global institution. From a practical standpoint, who wins these kinds of arguments is overshadowed by the fact there are now more and more FTAs in operation around the world and large numbers under negotiation compared to a decade ago.

In most cases, FTAs seem to lead to both trade diversion and creation with the net effects determined by the structure of the FTA. NAFTA is one of the most comprehensive regional free trade agreements in history, and it provides a good case study of the benefits and drawbacks of FTAs. Like many other FTAs, the formation of NAFTA has been a subject of much discussion and divided opinions on its benefits. Overall, significant evidence shows that NAFTA has been a trade creator in most sectors (Susanto, Rasson, & Adhock, 2007). Similarly, an IMF study (1999) and Eicher, Henn, and Papageorgiou, (2012) find that trade diversion is relatively rare – in fact, after controlling for multilateral resistance and bilateral heterogeneity, all the 12 major FTAs studied in the report including NAFTA resulted in net trade creation. Most studies have concluded that the European Community has resulted in more trade creation than trade diversion; but in some sectors such as agriculture, the net effect has been trade diversion because of the EU's Common Agricultural Policy that raised barriers to agricultural trade outside the EU (Holiday, 2007). On the other hand with respect to East Asia, Elliott and Ikemoto (2004) analyze the trade creating effects of the ASEAN FTA (AFTA) before and after its implementation with a

Source: Asian Development Bank, 2008; Deardorff & Stem, 1994; Arnold, 2003.

special focus on possible anticipatory trade effects. Their results indicate that no significant trade creating or diverting effects were observed in the periods following its implementation in 1992.

Table 1. Advantages and Disadvantages of Free Trade Agreements

Advantages	Disadvantages
It may be easier for governments to reach agreement on important or contentious issues in smaller negotiations than in multilateral negotiations.	The preservation of preferential concessions undermines the WTO.
Reciprocal benefits are easier to identify and deeper integration is easier to achieve.	*Competition and anti-trust policies in FTAs can distort trade.*
FTAs can be first steps toward multilateral engagement.	*Developing or new industries may find becoming established in a competitive environmentdifficult with no short-term protection policies by governments.*
FTAs can draw in areas not (fully) covered by the GATS (e.g.: government procurement; strict subsidy disciplines).	With the removal of trade barriers, structural unemployment may occur in the short term.
The participating economy experiences lower administrative costs and more influence on the outcome in negotiating with a few partners.	*FTAs create a maze of regulations which undermine principles of transparency and predictability in trade. Overlapping memberships in FTAs create costs for traders, regulators, and customs officials in meeting multiple sets of trade rules.*
Regional agreements also offer the potential to establish arrangements at the regional level to address some of the social dimensions of trade.	*It may be difficult for developing countries to derive full benefits from improved market access provisions (including tariff cuts) because of limited supply capacities and competitiveness.*
They can help provide economies of scale especially for companies from smaller countries.	*Many FTAs require developing countries to absorb broader and deeper liberalization of trade in goods and services than the WTO requires.*
Consumers benefit in the domestic economy because they can now obtain a greater variety of goods and services.	*FTAs between developed and developing countries eliminate special and differential treatment provisions of the WTO.*
FTAs enable member countries to specialize in the production of those commodities in which they have a comparative advantage and to improve resource allocation.	Spaghetti Bowl of rules: FTAs create rules of origin to distinguish between products from within the free trade area and products from outside it and can create new rules on customs procedures, technical standard, and labeling.
Relative to non-hub countries, an FTA-hub country gains preferential access to more markets and thus enjoys improved export competitiveness. To the extent that such an advantage translates into more exports, the hub-and-spoke feature of overlapping FTAs can have a positive effect on trade.	Some agreements on liberalization in services adopt a *negative list* approach (i.e.: full liberalization in all sectors, except those listed). Since the services sector may not be well advanced in some developing countries, trade negotiators may not be sufficiently aware of all relevant sub sectors and thus not list all those that they may wish to exclude from liberalization.
Modern FTAs (also called as Closer Economic Partnerships or CEPs) typically contain many additional provisions on issues likeinvestment, competition policy, government procurement,facilitationstandards, quarantine), e-commerce andproperty.	FTAs confer economic advantages only when they are negotiated with countries which are significant trading partners. In addition, the negotiation of FTAs is resource intensive, and there can be an opportunity cost in devoting resources to bilateral as opposed to multilateral agreements.

V. Implications of FTA Proliferation for the WTO

FTAs discriminate against non-members by definition and always have potential to disadvantage outsiders; accordingly, the GATT/WTO rules allow them as an *exception*. This is why all economies negotiating FTAs assert that theirs are consistent with the GATT/WTO rules. Even if the GATT/WTO framework has lost its uniqueness in function as a vehicle for multilateral liberalisation, it still keeps its superiority over FTAs. Apart from this critique, several points should be made on the recent FTAs.

First, if the recent trend of forming FTAs continues without much coordination, various local agreements on the new issues, such as investment, facilitation measures, environment and labor, may emerge depending on the circumstances that each FTA faces. "The lack of specificity in the relevant WTO rules on the do's and don'ts of FTAs gives Members significant leeway in the design of such agreements" (Fiorentino, Verdeja, & Toquebeofu, 2006; Krugman, 1979). It may be difficult to unify varied rules after the formation of FTAs because some of them are quite sensitive domestically in some economies (e.g. environment and labors issues for developing economies). In other words, "FTAs as testing ground" for making multilateral rules may not work well in at least the short to midterm because FTAs are most likely to be formed by like-minded economies. It has been noted, for example, that the widely varying forms of China's free trade pacts may also exacerbate the difficulty of harmonizing them into broader arrangements toward trade liberalization in the future.

Second, even if one admits that it is hard for a government to undertake structural adjustment of its own domestic economy unilaterally, forming an FTA is not the only option available. The objective (structural adjustment via liberalization) can be achieved through a multilateral approach as well.

Third and very important, it is only natural that the content of every FTA differs when participants differ. Proliferated FTAs may leave investors confused by which rules, obligations, and incentives correspond to which partner. Therefore, membership in multiple trade pacts may create "obligations made in one that contradict those made by others" (Medved, 2010; Schiff et al., 2000). The differences in content are expected not only in the new issues mentioned above but in the traditional areas as well. For instance, the Japan-Singapore FTA excludes agricultural products from its tariff reduction scheme (Rajan, Sen, & Siregar, 2001). On the other hand, it is hard to imagine that any FTAs in which Australia or New Zealand are involved would exclude primary commodities and their processed products. The proliferation of FTAs might create different tariff rates applied to the same product depending on its origin. Similarly, uncoordinated FTA proliferation will likely produce various rules of origin (ROOs) in the region and in an economy if and when FTAs overlap. When different ROOs are applied to different economies' access, the work needed for individual producers and importers to know and keep records for a variety of ROO requirements will be enormous, and the complications associated with negotiations for accession of additional members to the FTA or for merging FTAs may discourage governments from doing so (Krueger, 1997). In practice, ROOs can actually raise transaction costs for firms and generate confusion over compliance. Increasing globalisation of investment and production ties trade policy in knots and facilitates protectionist capture (Bhagwati, 1995). In short, the proliferation of FTAs with different contents and overlaps could stall the progress in multilateral liberalisation under the GATT/WTO.

The hurdles to achieving a multilateral emphasis must, however, take into account the factors motivating the behavior of the largest developing countries as in the case of China. While we might focus on Chinese regional policies toward East and Southeast Asia from a unitary perspective at the national level, there are domestic institutional constraints on Chinese regional foreign policy in the area of trade and economics. Commentators have identified three major constraints: (1) a fragmented decision-making structure that has difficulty with coordination, (2) a relatively heavy reliance on top level decision-makers at a time when issues of Asian economic policy have relatively low priority for these same decision-makers, and (3) lack of autonomy for negotiators vis-à-vis top decision-makers in Beijing (Pearson, 2010). Moreover, at the same time China has pursued multilateral trade negotiations via membership in the WTO, it has embraced a regional approach to trade liberalization by entering into the growing number of bilateral and regional free trade agreements already noted. Why has China tended to focus more recently on the latter? Multiple factors are involved. While China's activism reflects considerations about enhancing the country's influence in the Asia-Pacific region, capturing the economic gains of FTA participation and minimizing the trade and investment diversion resulting from the competitive dynamics of regional trade liberalization, the move toward expanded FTAs is also consistent with the "desire to create alternative bargaining forums over trade issues that could help to stabilize expectations as well as the need to use FTAs to control the impact of trade liberalization so as to accommodate protectionist pressure emanating from domestic interest groups" (Zeng, 2010, p635) These domestic factors complicate achieving a resolution that might be most desirable from a multilateral perspective.

FTAs need to become multilateral and non-discriminatory eventually if they are to become truly consistent with the WTO's goal of global MFN trade. In response to rapid growth in the numbers of FTAs and RTAs during the 1980s and 1990s, the WTO established a Committee on Regional Trade Agreements (CRTA) in February 1996. It was charged with verifying compliance of notified RTAs with the relevant WTO provisions and to consider the systemic implications of such agreements and regional initiatives (Fiorentino, Verdeja, & Toqueboefu, 2006). Because the CRTA made no significant progress by the launch of the Doha Round in November 2001 and RTAs were continuing to increase, RTA rules were included in the Doha Development Agenda (Fiorentino, Verdeja, & Toqueboefu, 2006). In July 2006, this led to agreement on a Draft Decision on a *Transparency Mechanism for Regional Trade Agreements,* aimed at revitalizing the CRTA and improving WTO oversight of RTAs. This transparency initiative continues; therefore, it prompts a discussion of some mechanisms to be established at the time of FTA formation.

FTAs may become gradually multilateral and non-discriminatory in two ways. First, these phenomena can be accomplished outside of the FTAs. If WTO liberalisation proceeds, the margin between the MFN and the preferential tariff rates will be reduced. The new issues will be dealt with at the multilateral negotiations as well. The problem is, however, that as mentioned earlier, many aspects must be discussed and resolved even before starting the WTO round. Second, FTAs can be multilateralized by themselves. In other words, some measures (mechanisms or institutions) that will multilateralize FTAs can be built within them or between them.

The following are some possible ideas about multilateralizing FTAs:

- Automatic membership: If an FTA assures that anyone who wants to join *must* be admitted on the same terms as the original members, then originally excluded members continue to seek to join if that FTA is attractive enough. If and when a critical mass is formed, the content of this FTA will be applied multilaterally. An important aspect of this mechanism is that latecomers must be admitted even if they are not from the region where original members are geographically located. In other words, de-regionalisation of RTAs/FTAs is necessary.
- Gradual decrease in the ROO level: Even though ROO is the crux of the existence of any FTA—because outsiders can ride free without it—it will be necessary to reduce the ROO level of an FTA. Reduction may have to be a gradual process, but with close coordination with other FTAs, it can be included in the FTA clause.
- Whither "open regionalism"? Trade liberalization under the principle of open regionalism in its purest form (i.e. regional trade liberalisation initiative under the MFN application) may not work well in this regard. For example, the little progress that the Asia Pacific Economic Cooperation Individual Action Plan's (APED IAP)—that each country is required to provide annually —process has made over the last five years shows that without assured reciprocal liberalization by others, regional liberalisation will not create strong momentum. Instead, some economies, especially in the Asia Pacific region, may be better off pursuing Free Trade Area of the Americas-style (FTAA) FTAs and not killing the momentum for critical mass formation, provided the existence of mechanisms to merge them and ultimately make them multilateral and non-discriminatory (Findlay & Pangestu, 2011).

VI. The Continuing Debate over FTAs: Policy Implications

Interest in a new wave of FTAs is driving a spirited debate among experts, policymakers, and other observers over whether FTAs promote or damage the economic interests of the world at large. The differing views can be categorized into three main groups. One group consists of those who oppose FTAs because, as they assert, FTAs undermine the development of the multilateral trading system and act as a stumbling block to global trade liberalization. A second group supports FTAs because they believe that FTAs act as a building block to multilateral trade liberalization. The third category includes those individuals and groups that are opposed to trade liberalization in general because they believe trade liberalization's impact on workers in import-sensitive sectors or on the environment is unacceptable or because, as they assert, it undermines national sovereignty (Cooper, 2012).

The first group of experts includes international economists Jagdish Bhagwati and Anne O. Krueger, who have strongly advocated that national governments should not pursue FTAs at the expense of multilateral negotiations in the WTO. Bhagwati concludes that FTAs are by definition discriminatory and therefore trade diverting. He argues that tariffs remain high on many goods imported into developing countries and even on some labor intensive goods such as wearing apparel and agricultural products imported into developed countries. Consequently, he asserts that trade diversion will likely result when an FTA is formed. Bhagwati argues that firms actually prefer bilateral or regional FTAs to multilateral trade liberalization because they are able to achieve preferential treatment over their non-member country competitors (Bhagwati, 2007).

Both Bhagwati and Krueger criticize the "rules of origin" and other conditions of an FTA's establishment. Bhagwati claims, for example, that the rules of origin in one FTA more than likely do not coincide with the rules of origin in many of the other FTAs. Furthermore, he argues, the schedule of implementation of the tariff reductions and other conditions for one FTA will not match the schedule of other FTAs. The incongruity of these regulations across FTAs has created what Bhagwati sees as a customs administration nightmare and what he calls the "spaghetti-bowl" phenomenon (Bhagwati, 1995, p4; Bhagwati, 2008).

In her criticism, Krueger claims that in order to meet the input thresholds of rules of origin requirements, producers in one FTA partner will be encouraged to purchase as many inputs as possible from other partner countries, even if a non-FTA member can produce and sell the inputs more cheaply and even if the tariff rate on inputs from non-FTA producers is zero. Importing inputs from within the FTA to meet the rules of origin threshold allows the producer to sell the final product within the FTA duty free. Under such circumstances, imports of inputs are diverted from efficient producers outside the FTA to less efficient producers inside the FTA. A corollary to Krueger's conclusion is that the higher the threshold established in the rules of origin, the greater the chance that trade diversion will take place (Krueger, 1999).

A range of economists, policymakers, and other experts embrace a second view that FTAs can enhance trade and should be pursued. Economist Robert Z. Lawrence argues, for example, that recent FTAs involve much more economic integration than the elimination of tariffs. NAFTA, he points out, has led to the reduction in barriers on services trade, foreign investment, and other economic activities not covered by the GATT/WTO. In addition, under NAFTA, Mexico has affirmed its commitment to economic reform, making its economy more efficient. Lawrence asserts that the theory traditionally applied to FTAs [by Bhagwati, Krueger, and others] does not take into account these dynamic welfare-enhancing characteristics of FTAs, which he believes are likely to outweigh any trade diversion that results from the elimination of tariffs (Lawrence, 1999).

A CATO Institute study by economist Edward L. Hudgins argues that while it may be preferable to liberalize trade multilaterally, countries should take any available avenue, including bilateral or regional FTAs, even if they lead to some trade diversion. Furthermore, Hudgins asserts that FTAs can be more efficient vehicles for addressing difficult trade barriers than the WTO, where the large membership requires compromise to the least common denominator to achieve consensus. He also claims that FTAs have also provided momentum for GATT/WTO members to move ahead with new trade rounds (Hudgins, 1995/6).

Economist C. Fred Bergsten holds a position similar to the one expressed in the CATO study that in lieu of multilateral trade negotiations, FTAs are the next best thing because they do promote global trade liberalization. Bergsten advocates establishing U.S. FTAs with New Zealand and with South Korea (Bergsten, 1997). Economist Jeffrey Schott argues that some U.S. firms are being discriminated against because FTAs are rapidly forming in which the United States is not a participant; therefore, in his view, the United States must negotiate FTAs. He cites the example of Canadian firms which have obtained competitive advantages over American firms because Canada has an FTA with Chile (Schott, 2001).

Bergsten and others have also advocated structuring FTAs in a manner that could serve as building blocks of a global free trade system. Using the APEC plan as a model, Bergsten argues for an FTA based on "open regionalism," that is establishing the road map for free trade and investment in the Asian-Pacific region for 2010/2020 among the members but allowing other countries to join if they agree to accede to the conditions. In order to minimize trade diversion, he suggests that trade and investment could be implemented on an MFN principle, perhaps conditional MFN in order to limit the free rider effects. Other countries and other regional groupings, Bergsten presumes, would be willing to accept the conditions having been enticed by the trade and investment opportunities until most of the membership of the WTO would be engaged in forming a free trade area (UAW, 2013). A Heritage Foundation report draws up a similar proposal for a Global Free Trade Association (Hulsman & Schavey, 2001). On the other hand, the assumption that preferential concessions will at some point be extended at the MFN level is not applied in practice since it is rare, if not unheard of, for countries to extend their RTA preferences on an MFN basis unless as part of a multilateral round of trade negotiation (Fiorentino, Verdeja, & Toqueboefu, 2006 Krugman 1979). Baldwin (2006), Estevadeordal et al. (2008), Gasiorek et al. (2007), & Harris (2008) carefully evaluate the ROO-related costs and suggest that FTAs could be compatible with multilateralism through the harmonization and cumulation of ROO. Estevadeordal and Suominen (2003), Augier et al. (2004), and Gasiorek et al. (2007) quantitatively estimate the trade effect of ROOs, focusing on restrictiveness and different cumulation provisions of ROO by using gravity regression analysis, and they reason that FTAs could be compatible with multilateralism.

A third group opposes not only FTAs but also trade liberalization or globalization in general. Included in this group are representatives of import-sensitive industries, labor unions, and representatives of social action groups such as some environmentalists who question the wisdom of trade liberalization whether accomplished through multilateral negotiations or through bilateral and regional trading arrangements. They assert that trade liberalization unfairly affects workers by exporting jobs to countries with lower wages and undermines the nation's ability to protect the environment by allowing companies to relocate to countries with less stringent environmental regulations (Stoler, 2004). For example; the United Auto Workers (UAW) union asserts the following position regarding the FTAA:

> Such an agreement would provide broader protections for the rights of corporations, further undermine the ability

of governments in the region to regulate their economies in the interests of their citizens, and intensify the downward pressure on workers' incomes through competition for jobs and investments. All of this would take place in the absence of any counter-balancing protections for workers, consumers, or the environment. This is why the UAW has consistently opposed the direction of these negotiations, the positions taken by the U.S. government, and worked closely with other organizations in the region to oppose the creation of an FTAA. (Cooper, 2012, p.14)

Ⅶ. Conclusion

A large number of countries seem to have anticipated the slow moving and delayed negotiations of the WTO Doha Round and placed greater faith, at least temporarily, in bilateral and regional agreements. The resulting proliferation of FTAs presents a number of challenges for the WTO's mandate to liberalize trade multilaterally. The most profound change impacting the WTO is that FTAs have increasingly become the means for liberalizing and advancing trade, investment, and economic growth. Trade liberalization, the major purpose of FTAs, has paid enormous dividends to signatories as well as expanded world trade. Currently, numerous large bilateral trade relationships not governed by FTAs remain for which the WTO remains the focus: US-EU, US-Japan, and US-China are three of the most significant.

FTA negotiations also raise concerns about equity, particularly when FTA rules are strategically used to develop WTO rules. Without suggesting that WTO negotiations have always been fair, they have provided opportunities for smaller countries, usually in coalitions with other like-minded countries, to carry enough weight which achieve outcomes on particular strategic issues. For example, least developed countries managed to have included in the Doha round a special consideration of the negative impact of agriculture subsidies on cotton. In contrast, bilateral FTA negotiations provide no avenue for coalition building and instead their outcomes usually reflect the relative power of the negotiating countries. For the United States, the European Union, China, and Japan bilateral and even regional FTAs maximize their ability to get their own way. Were these outcomes to become templates for future multilateral trade rounds, then a two-level game that leverages FTA outcomes into themight undermine the WTO's legitimacy.

The surge of FTAs has raised the question of how their operations might affect the partner FTA ***countries*** and the rest of the world at large. The lively debate that exists about FTAs' trade creation vs. trade diversion has brought two contrasting viewpoints and resultant effects. Those emphasizing trade creation aspects point out that by reducing and even eliminating trade barriers among partner countries, an FTA can bring improvements of trade, income levels, and competitive prices for consumers. The opposing school of thought argues that the reduction or elimination of trade barriers restricting trade with non-partners of a FTA are discriminatory and divert trade.

While empirical evidence is broadly supportive of their benefits, FTAs have their own costs for businesses and governments. A country with different FTAs with other countries creates a so-called spaghetti effecttrade rules, which raises costs for companies as they are forced to navigate competing FTA commitments. In some cases, countries may end up having more than one FTA apply to trade with the same country. For instance, the United States already has bilateral FTAs with Australia, Singapore, Chile, and Thailand and has indicated that these FTAs will continue to apply alongside the Trans-Pacific Partnership. More broadly, this tension in the FTA-WTO relationship may pose a threat to a balanced development of world trade through increased trade and investment diversion, particularly if liberalization on a preferential basis is not accompanied by concurrent MFN liberalization (Fiorentino, Verdeja, & Toqueboefu, 2006 Krugman 1979).

Another concern is that the development of regional FTAs will lead to a world divided by competing economic blocs as well as increasingly hostile north south competition. Calls for U.S. participation in the development of Asia's economic integration, for example, have been partly driven by a desire to avoid this outcome. A world divided by economic blocs could also increase international strategic and military competition. FTAs can also reduce global welfare if they end up diverting trade instead of promoting it. This arises when preferential market access granted under an FTA displaces imports from the most efficient producers located in a country that is not part of the agreement.

An important step in enhancing the benefits of FTAs would be to amend the WTO agreement to permit the WTO panel and appellate body to hear disputes that arise from FTAs. The ability for countries to settle disputes using WTO panels and to discuss questions of law to be appealed to the WTO appellate body is one of the signature achievements of the Uruguay round. A multiplicity of FTAs has created a "maze of different regulatory regimes that undermine the principles of transparency and predictability in trade relations" (Fiorentino, Verdeja, & Toqueboefu, 2006

Krugman 1979). Thus, despite the incorporation of bilateral dispute settlement provisions in many FTAs, countries have overwhelmingly preferred to settle disputes under the WTO. Allowing the WTO appellate body to hear FTA disputes would start defining and creating a relationship between the WTO and FTAs. It would also start providing legal coherence across the WTO and FTAs and between FTAs. Furthermore, the expectation that a WTO decision regarding one FTA could be applied by a WTO panel to another FTA would increase the certainty and predictability about the meaning of FTAs, which could enhance global trade and investment.

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