

Future of Mega-Regionals in Asia Pacific from Regionalism to Nationalism

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Abstract: - The rise of Mega-Regionals has been prominent since the global financial crisis in 2008, where the countries opted for regionalism to spur growth in the domestic economy. Further, the need for these Mega Regional Trade Agreements (MRTAs) was amplified by the failure of the Doha Development Round and WTO's incompetence in regulating 21st-century trade issues like global value chains, competition policy, e-commerce, etc. The economic clout these MRTAs have on the world is hefty with engagement in WTO-Plus and WTO-Extra issues, and therefore, have been debated for replacing the existing multilateral trading system. However, withdrawal of the United States from the Trans-Pacific Partnership (TPP) and India from the Regional Comprehensive Economic Partnership (RCEP) has raised a question on these agreements. The divergent interests of member economies of the agreements make it difficult to achieve the targets with the initial set of countries. The shift of countries to more protected trade policy may affect the future of MRTAs in replacing the WTO. The paper concludes that at present, these MRTAs in the Asia Pacific region would not be able to replace the WTO as it would require concordance between them including all the major trade players of the region.

Keywords: Mega Regional Trade Agreements, Regionalism, WTO, RCEP, CPTPP

I. INTRODUCTION

The 21st century has witnessed proliferation of free trade agreements (FTAs) and regional trade agreements (RTAs) for liberalising trade and non-trade issues and deeper integration between the countries or regionals. This has been earmarked by emergence of Mega-Regional agreements, dominating the world with strong hold on economic factors in terms of quantity and quality. However, this trend of 21st century agreements have been induced by the flaws of the trading system including deadlock in the WTO negotiations and its inability to regulate new trade issues. Such a situation has raised the importance of MRTAs as they have been compared to the WTO and also recognised as a substitute of multilateral trading mechanism.

Yet, there have been examples where the countries are inclined towards nationalism and protecting their domestic industries deeper regionalism through Mega-Regionals. Additionally, the entire WTO system cannot be defined as redundant when many countries are relying on WTO's redressal system and trade policy review mechanism. This paper tries to answer the uncertain future of the multilateral trade organisation and identifies a middle way approach for trade governance in the 21st century.

The paper is divided into six sections, where section II discusses the rationale behind rise of Mega-Regional agreements. Section III represents the current status of these agreements in the world economy contributing their

dominance. However, there are anomalies where countries are protecting their domestic economies through withdrawing from these agreements and rising tariff rates, which has been discussed in section IV. It has also been argued that the Mega Regional Trade Agreements (MRTAs) have the capability to replace the present multilateral trading system, hence section V discusses the credibility of such a threat and VI tries to suggest a future governance mechanism with the WTO and MRTAs.

II. RISE OF MEGA-REGIONALS

A. Plight of Developed Nations

Liberalisation through multilateralism was construed by the developed nations, where the tariff rates on industrial products reduced from 22 per cent in 1948 to 5 per cent in 1994 [1]. Unlike the developing and least developed nations, majority of the developed nations had already reached a lower level of import duties in the initial years of the WTO. The lower most-favoured nation (MFN) tariff rate of developed countries made them less beneficial in bilateral or regional trade agreements focusing on tariff liberalisation of goods and services in the 20th century, as it provided less bargaining power to them in the negotiations. This entitles the developed nations to use non-tariff barriers (NTBs) to restrict imports from developing countries and uses NTBs as bargaining chips in the RTAs; thus, changing 20th century trade agreement, dealing with liberalisation of tariff rates of goods and services, into 21st century trade agreement

concerning various areas like NTBs, liberalisation of domestic regulations for value chains productions, e-commerce, public procurement, etc.

On the other hand, developing countries enjoyed benefits from the RTAs with tariff liberalisation under the South-South trade agreement. Challenges for the developed nations also increased with the growing economic powers in the hand of the emerging economies and their increased participation in the global value chains. The global financial crisis in 2008 exasperated the plight of the developed economies by affecting the already low growth rate of the gross domestic product (GDP). However, the economic growth of the emerging countries was better than the developed nations owing to their high resilience in the external sector. Simultaneously, the Doha Development Agenda (DDA) was in a standstill, which limited any hope for multilateral liberalisation. This made industrialised countries move towards MRTAs to increase their gains through integration with emerging and other developing countries. These MRTAs are not confined to *Singapore Issues*; rather it covers various WTO-Plus and WTO-Extra issues, beyond the purview of the WTO.

B. Failure of the Doha Round

The WTO supersedes the General Agreement on Tariffs and Trade (GATT) by including an improved agreement of trade in goods, agreement of trade in services, and trade in intellectual property. The organisation again tried to include other issues like agriculture, trade facilitation, rules on Non-Tariff Measures (NTMs), environment, etc., in its most ambitious and criticised effort—the Doha Round in 2001. The preliminary aim of the round was to incorporate concerns of the developing countries in the trade talks. However, the difference in opinions between some developed countries and some developing countries have stalled the DDA. For instance, developing countries have been demanding reduction or elimination of export subsidies in agriculture sector, whereas developed countries are asking for liberalised manufacturing sector as reciprocal concession. Such contentions between the two groups of countries have resulted in an acrimonious stand-off in the Doha Round due to two principles governing the WTO — consensus-based decision making and single undertaking.

The principle of consensus-based decision making has been embedded in the WTO mechanism as it is a rule-based organisation based on the decision agreed upon by all the members. However, with increase in the members in the WTO and the complexity of trade issues, it is very difficult to gain consensus of the members in matters such as agriculture subsidies, environmental goods, e-commerce, etc. Additionally, the principle of '*nothing is agreed until everything is agreed*' or the single undertaking has thrown

the DDA into a deadlock. The situation was worsened with the global financial crisis in 2008 as it had hit the economies very badly, which resulted in protectionist behaviour of the economies rather than liberalising trade through multilateral forum. The *modus operandi* of the WTO has been criticised all over the world and has also raised questions about the credibility of the WTO.

C. New Trade Issues

A paradigm shift in the world trading system has been evident with the emergence of global value chains increasing the interdependence of countries for production and trade. Trade through value chains has increased over the years and accounts for more than 60 per cent of global trade [2] [3]. It has also changed the notion of '*producing domestically and exporting abroad*' to '*producing internationally*' where semi-finished goods and part and components are being traded among the countries while being in the production process. This has led to countries' concern over the domestic rules and regulations of the partner countries engaged in the production networks. Hence, negotiations in the trading agreement are not confined to reduction of tariffs and non-tariff barriers *at the border*, but have gone *beyond the border*. Issues, like e-commerce, environmental and labour standards, government procurement, competition policy, that are commonly negotiated in the 21st century trade agreements go beyond the realm of the WTO [4].

The inability of the WTO to monitor and regulate these new trade and related issues and the inability to conclude its DDA have led to the rise of Mega-Regionals. With the majority of strong economies being a part of MRTAs¹, this regional approach has become an alternative to the multilateral liberalisation. This has also questioned the existence of the WTO based on threats to be replaced by 21st century agreements.

II.CHARACTERISTICS OF MRTAs

MRTAs have been defined in the literature as one, where two or more countries enter into an agreement having more than 24 per cent of the gross domestic product contributed by the world with having major influence on the global investment [6], or two, where a quarter of world's trade is accounted by the trade agreement which simultaneously deals in WTO-Plus and WTO-Extra issues [7]. These Mega-Regionals are empowered with a strong clout of macroeconomic variables like GDP, trade, investment, etc. Including this quantitative strength, the trade agreements are

¹ A set of 54 economies are part of MRTAs [5].

also equipped with trade subjects which are not a part of the WTO at present, providing qualitative importance as opposed to the 20th century agreements. This has also raised existence threat to the WTO where experts are debating that the MRTAs with their qualitative and quantitative significance would be able to replace the multilateral trading system in near future.

Table 1: Economic Clout of MRTAs, 2019

Variable	C JK	CPT PP	RCE P*	TT IP
GDP	24 .6	13.1	30.1	46. 5
FDI, Outflow	34 .3	32.8	39.8	38. 4
FDI, Inflow	15 .4	19.6	29.9	41. 9
Exports in G&S	18 .9	13.4	26.4	49. 6
Imports in G&S	18 .3	13.1	25.3	50. 9

Source: World Development Indicators, World Bank, 2020 [8].

Note: Values represents the share of MRTAs in the world and RCEP* includes 15 countries (excluding India).

Table 1 represents the contribution of major MRTAs in selected macroeconomic variables. It is evident from the table that MRTAs contribute more than a quarter share of world's GDP. Transatlantic Trade and Investment Partnership (TTIP), including the United States and the European Union, stand for 46.5 per cent of world's GDP in 2019. This is followed by share of RCEP and China-Japan-Korea (CJK) FTA with 30.1 per cent and 24.6 per cent share, respectively, whereas the share of Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) has been reduced to 13.1 per cent because of the fallout of the United States from Trans-Pacific Partnership (TPP). The share in Foreign Direct Investment (FDI) outflows of all the four MRTAs have been higher than 30 per cent and the same for FDI inflows is more than 15 per cent in 2019. The share of their exports and imports of goods and services (G&S) in the world has been nearly same for the year. Regional Comprehensive Economic Partnership (RCEP) and TTIP together accounts for 75 per cent of world's trade. These agreements have majority of dynamic economies of the countries evincing strong quantitative hold on the world economy. Additionally, these agreements are

endowed with 21st century trade subjects like digital trade, environment and labour standards, competition policy, etc., and a platform for liberalising and regulating these new trade issues with like-minded countries. Yet, there are evidences where these Mega-Regionals have not been able to achieve their set targets for negotiations with the original member of countries.

IV. PROTECTIONIST APPROACH

The Mega-Regionals in their initial years have always been regarded as agreements meant for changing the regional and global trading system. With high expectations the member countries started the negotiations, where some of the agreements are still in that stage. However, the ones completed or near completion of negotiations have experienced failure of reaching the conclusion without an important member of the grouping, for example, in case of the United States in TPP. Though, the country played an important role as an anchor to the rest of the member countries, the change in presidency led to withdrawal of the United States in 2017 for the Mega-Regional. This action was a consequence of this country's policy — '*America First*' — and aimed at working on a fairer and job creating deal for the country. On the similar lines for protecting countries interest in Mega-Regional, India too turned down RCEP after negotiating the deal for a decade and concluding the trade deal to be non-beneficial for the country in 2019.

Even though the WTO was able to regulate its members' protectionist behaviour during the time of global financial crisis with its consistent rules, the increase in number of non-tariffs barriers have led to a more protected world economy [9]. Countries have induced barriers related to non-trade issues like environmental concerns, labour standards, etc. This has also resulted in countries opting for RTAs to liberalise non-tariff measures rather than focusing on the multilateral negotiations in DDA. The second half on the recessionary period had also experienced developed countries moving away from regionalism. For instance, the United States policy of '*America's First*' and exit of the United Kingdom from the European Union where both of these countries are not shying away from bilateral free trade agreements but have protected their own interest by not following the path of regionalism. The protectionist behaviour has also been seen in developing countries like India where the country has increased import duties on many commodities while amending its Customs Act 1962 and the Tariff Act 1975 after withdrawing from RCEP [10].

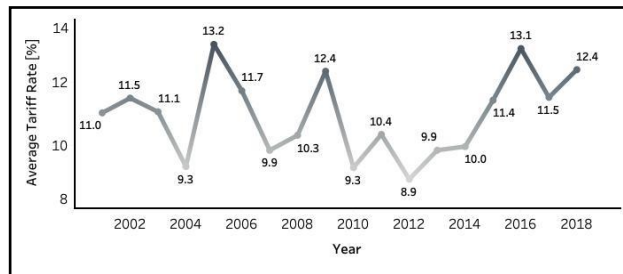


Figure 1: Trend of Average Tariff Rate in the World (%)

Source: Trade Analysis Information System (TRAINS), World Integrated Trade Solution (WITS), World Bank, 2020 [11].

Tariff rates in the world economy have decreased since the GATT was established, aiming at freer trade among the member nations. However, since the financial crisis of 2008 it has experienced a rise in the average tariff rates in merchandise goods. Figure 1 represents the average tariff rates of the world for the period 2001-2018, exhibiting a gradual rise in the tariff rates over the period. The buoyancy period and the first phase of recession represents volatile tariff rates on goods in the world economy. This volatility is majorly owing to volatility in tariff rates in developing countries, as developed countries have maintained a stable import duty structure over the years with minor exception after the global financial crisis. However, in the second half of recessionary period, from 2012, the import duties have increased resulting in increasing average tariff rates of merchandise imports across the globe, recording a rate of 12.4 per cent in 2018.

It has been argued that restrictive trade measures in 2018 has affected global merchandise trade nearly three times the same share accounted for global financial crisis [12]. A plausible consequence of increased protectionism is retaliation of other countries with increase in trade barriers and thus leading to trade wars. Trade wars follows with reduction in trade between the countries and fall in their GDP while affecting other non-party countries on various economic fronts like investment, global GDP, disruption in financial markets, etc., which has been visible in case of trade war between the United States and China recently. This has questioned the ability of MRTAs to be able to replace the WTO. The major economic powers restricting trade have raised adequate governance issue for the global trade system and the role of the multilateral and regional forums.

V.END OF THE WTO?

The WTO has been criticised over its old trading mechanism which has not been updated since its inception.

Unlike its predecessor, the WTO included three areas—goods, services and intellectual property through the General Agreement of Tariffs and Trade (GATT), the General Agreement of Trade in Services (GATS) and the Agreement on Trade Related aspects of Intellectual Property Rights (TRIPS). However, over the period of time, trade concerns of the member countries have gone far ahead of these three issues and included many other areas like digital trade, competition policy, labour standards, etc., which are also classified as WTO-Plus and WTO-Extra issues. These issues are widely seen in MRTAs².

Settling trade disputes of the member countries through the Dispute Settlement Mechanism (DSM) has been an important and successful function of the WTO. About 60 per cent of the disputes cases reported under the DSM have been resolved³. Still the mechanism faces many challenges. The first and foremost problem with the DSM is the time taken to resolve the dispute. The entire mechanism to resolve trade dispute would take around 28 months on an average for the period 2007-11, which has increased from 23.21 months in 1995-1999 [15]. This increase in time period is attributable to increase in number of cases and complexity of cases. However, DSM faces many administrative challenges—blocked new appointment of members at the Appellate Body, small number of staff at permanent post, staff hired on part-time basis, etc [15], [16].

The WTO has tried to include new trade issues especially for developing and Least Developed Countries (LDCs). However, with principles like consensus-based decision making and single undertaking, many of the WTO Rounds have failed and the best example is its fourth Ministerial Conference (MC4) in Doha. Yet, the WTO negotiations came up with the Bali Package in MC9 as a sense of relief for member nations to retain their belief on the multilateral organisation for trade liberalisation. On the DSM, it has been noticed that countries which are engaged in non-multilateral trade agreements are approaching the WTO to resolve their disputes in many trade areas. It has been estimated that around 15 per cent of the total disputes in the WTO are among the countries which have bilateral and regional RTAs [17].

The other function of reviewing and monitoring the trade policy of the member nations is being undertaken regularly by the WTO trade policy review mechanism where members have to submit their policy towards external trade for transparency in the multilateral trading. Though there are

² A total of 52 areas under various trade agreements have been classified into WTO-Plus and WTO-Extra issues in the literature [13].

³ WTO Dispute Settlement Database, 2019 [14].

areas where the WTO needs improvement—inclusion of WTO-Plus and WTO-Extra issues, resolving administrative challenges for DSM, etc., the WTO is trying to proceed with the negotiations through plurilateral trade agreements like Information Technology Agreement (ITA) and Government Procurement Agreement (GPA). Moreover, a multilateral organisation is responsible for all of the member countries in the world, which cannot be replaced by a regional organisation or agreement like MRTAs.

VI. MULTILATERALISING MRTAs

As [18] argued in favour of the WTO, global problems need global solutions. The WTO is an important global organisation for multilateral trade monitoring and dispute resolution. The continuous trade policy monitoring with ‘trade policy review’ mechanism and effective dispute settlement mechanism have ceaselessly kept its desideratum in the world trading system intact. Though there have been evidences of member countries losing their faith with deadlock in the WTO negotiations, members not withdrawing their membership from the organisation is in itself the hope for WTO’s revival from the current doldrums. However, WTO, with less interested members to reach a consensus, alone cannot achieve the liberalisation in the 21st century trade subject. Neither MRTAs can replace the WTO with its regional approach.

The world at present is experiencing formation of MRTAs which are unifying large economies and dynamic economies to liberalise tariffs and rules *beyond the borders* in the areas beyond the WTO ambit. However, these are regional agreements and the rules of the agreement are valid for the regional caucus and not applied to the world as a whole. Moreover, various MRTAs would lead to many rules and tariffs rates on the areas negotiated, let alone what are currently present in the 20th century bilateral and regional trade agreements. This would further enhance the ‘*spaghetti bowl*’ problem of regionalism as defined by [19], whereas in this case the cobweb would not only be created between the bilateral and regional trade agreements but also with these Mega-Regionals.

Nonetheless, a world trading system where both the WTO and MRTAs exist simultaneously is predicted to be more experienced in the past and the present. On one hand, the WTO believes that regional trading arrangement has been aiding its liberalisation process by providing trade issues, like investment, services, intellectual property, competition policy, for multilateral negotiations. It has also given a platform to negotiate trade issues, where multilateral approach is not working, in a plurilateral forum with like-minded countries like ITA and GPA. It is argued that the

Mega-Regionals can also provide new trade negotiating issues and list of countries which are in accordance to liberalise the issues at a multilateral platform. The WTO, on the other hand, can provide a global reach to these regional agreements with established secretariat and other administrative forums to work for monitoring and regulating trade at a global level. The WTO has time and again proved its requirement for the world trading system like in the case of global financial crisis. It helped in regulating the protectionist behaviour throughout the crisis.

There is no denying the fact that the responsibilities of a world trade mechanism can only be fulfilled by a global organisation and not a regional forum. Hence, the future course of action should be to multilateralise these MRTAs and recollect the common features of all these regional agreements and work on them at a multilateral platform with the WTO. However, one must be very cautious of aiming to multilateralise MRTAs as the Doha deadlock and withdrawal of the United States and India from their respective MRTA justifies the challenges countries would be facing due to unification of these Mega-Regionals. Such a situation would leave the world trading system with a two tier system. As discussed by [20], one pillar would be held by the WTO which would be responsible for traditional trade issues and the new trade issues in the MRTAs will be held as the second pillar. As both — the WTO and the MRTAs — are here to stay.

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