

The Nature of Mega-regional Trade Agreements in International Political Economy

Abstract

In the following essay, I will put the emphasis on three different dimensions of the nature of mega-trade deals. At first, I will examine how the arrangements could be interpreted with the application of various theoretical paradigms, such as liberalism and mercantilism.

Furthermore, I will also draw attention to some of the probable outcomes of mega-regional trade agreements for global governance. Secondly, I will take the political economy of mega-RTAs under scrutiny and highlight the positions as well as the ‘clash of interests’ between the interested parties. Last, I will attempt to propose an outline in order to be able to evaluate the new deals in a systematic way, since if and when the mega-regional trade agreements are agreed upon, there will be a lot of interests in the effects of the deals. The essay will be concluded by taking a look at the likely consequences for the world economy of reaching an agreement with the Trans-Pacific Partnership in October, 2015.

1. Introduction

The negotiations of free trade agreements have paved the way for a multilateral trading system in an entirely distinct geopolitical dimension. Considering the example of the Trans-Pacific Partnership, the Transatlantic Trade and Investment Partnership and the Regional Comprehensive Economic Partnership, it could be reasoned that mega-trade deals are more ambitious and have a broader scope of activities than RTAs in a traditional sense. In addition, they are often associated with the world trade regime as well as non-party states. In relation to the World Trade Organization, it must be pointed out that these arrangements have caused stalemate in the talks, making the future of the Doha Round uncertain. More importantly, mega-RTAs are believed to be responsible for the intensification of power asymmetries among the major players, such as China, the European Union and the United States of the global trading system. (ECIPE, 2014, p. 5)

The following paper puts the emphasis on three different dimensions in terms of the nature of mega-trade deals. At first, I would examine how the arrangements could be interpreted with the application of various theoretical paradigms. Besides, I would draw attention to some of the probable outcomes for global governance. At second, I would take the political economy of mega-RTAs under scrutiny and highlight the positions and the ‘clash of interests’ between the involved parties. At last, I would attempt to propose an outline in order to be able to evaluate the new deals in a systematic way.

2. The Interpretation of Mega-RTAs

2.1. Key Elements

In his academic writing titled ‘Is trade multilateralism being threatened by regionalism?’ Pascal Lamy identifies the most crucial and defining factors of mega-RTAs, such as the *enormous size and encompassing nature of the arrangements* (with the implicit implication of the share of mega-RTAs in world trade), *the ambition of the agreements to achieve deeper*

integration across issues of a wider scale and the change in the political reality of regulatory convergence. (Lamy, 2015, pp. 67-71)

Concerning the first aspect, the attention might be drawn to the fact that certain economies, such as Australia, Brunei, Japan, Malaysia, New Zealand, Singapore and Vietnam are included in the negotiations of both the Trans-Pacific Partnership and the Regional Comprehensive Economic Partnership with the United States being a participant in the TPP and the Transatlantic Trade and Investment Partnership. Furthermore, it could be indicated that the TPP represents approximately 30% of the world trade, while the RCEP and TTIP add up to about 40% of it.

In relation to the second element, Pascal Lamy argues that this could be the main specifying factor of mega-RTAs, as the phenomenon entails the development of linkages in production on a global scale and the loss of importance concerning protective measures on tariffs. With the emphasis on deepening instead of widening in terms of the integration, the purpose of mega-trade deals are to establish stronger connections between the included nations, instead of focusing on the involvement of more entities, which might impose a burden on the fate of mega-trade deals.

The third feature is about regulatory convergence between the smaller and larger economies, which is thought to result in decreased transaction costs and the intensification of trading relations between the involved parties due to the economies of scale. This microeconomic theory point out that production-efficiency is related to the production of goods and services in a directly proportional manner. Hence, with an increase in production, the price customers need to pay for a given product may decrease as a consequence of fixed costs being spread out over a huge amount of goods. Yet the matter ought to be subjected to serious policy considerations, since while larger economies find it beneficial due to the reduction of prices as well as the accessibility of bigger markets; for small- and medium-sized nations it could also prove to be disadvantageous witnessing their costs going up as a result of growth in the volume of production.

2.2. Analysis by Theoretical Paradigms

Since global trade negotiations have been stalemated for many years, the importance of mega-regional trade agreements seems to be reinforced. Not surprisingly, these arrangements have sparked the heat of discussion with opponents as well as proponents standing up to their righteous cause. In the following, I would like to outline the essence of mega-RTAs observed from the different theoretical paradigms of *liberalism* and *mercantilism*.

Liberalists would reason for the advancement of efficiency and specification in the economic domain as a possible outcome of the reduction of trade barriers. The argument is originated in the traditional theory of comparative advantage (O'Brien, Williams, 2013, pp. 13-17; pp. 111-113) that revolves around the liberalization of trade. Based on this perspective, imports provide benefits for international commerce, while exports are the price to pay for receiving them. As long as trade expansion is stabilized, meaning that it occurs in a well-balanced way, the gains acquired are going to be on an increase continuously in all nations. According to the liberalists, arrangements in trade have nothing to do with the establishment of jobs; they are only responsible for their industrial reallocation.

On the contrary, the mercantilist proponents of mega-RTAs would argue that the advantages of mega-trade deals could be realized by the dramatic growth of job possibilities, since there will be an increased number of foreign markets available as an outcome of new trade agreements. Furthermore, mega-RTAs are thought to boost the level of exports. To put it simply, in a mercantilist point of view exports are desirable and imports are not. Nations that choose to export more than they do import will definitely reap the increase on their net exports, therefore they are likely to be the winners of the trade-offs according to the mercantilists. The other countries that are not willing to follow the same strategy are believed to lose. Besides, mega-RTAs can pave the way for the creation of jobs but only at the expense of destructing others. This last argument could be justified by the mercantilist's strictly competitive game metaphor; the zero-sum game, which represents a situation where both the gains and losses of each participant are equaled. Despite the fact that the goals are mutually-contradictory in the theoretical paradigms of liberalism and mercantilism, the advocates of the RCEP, TTIP and TPP would still advance the following arguments. (Ibid. pp. 9-12; pp. 113-115; Rodrik, 2015)

2.3. The Consequences for Global Governance

There is no commonly accepted definition given for the term 'global governance', yet it can be explained as an embracing system that deals with the management of international relations across the entire world, encompassing the regulations as well as the economic growth and development on a worldwide basis. (Ibid. p. 295) In the next section, I would like to take two key elements in order to reveal their effects for global governance, namely the *provisions* and the *regulatory framework* of mega-RTAs.

Mega-trade deals ought not to be considered as free trade agreements on a larger scale. The real difference lies in the nature of the arrangements, since it could be argued that mega-RTAs have a deeper understanding in comparison to FTAs. While the latter is related to the regulation of tariffs in most cases, the former is overarching to a wider horizon of measures that could be deeper than tariffs.

Provisions concerning mega-RTAs can be categorized in three distinct ways, reflecting hard, soft and non-preferences. The first group describes the example of a certain country being biased towards another one at the expense of others, thereby suggesting the existence of discrimination. The consequences can be realized by the creation of trade linkages for some of the countries and the diversion of trade for others. It could also be reasoned that mega-trade deals are likely to bring about a certain degree of discrimination in tariffs. Currently they are quite low between the members of mega-RTAs, but there are still areas with high tariffs that would probably disqualify due to political reasons. The main problem is however constituted by the absence of a successful discrimination strategy that would be destined to establish a bureaucratic and legal framework with the purpose of outlining rules of origins that could be applicable to modern corporations' nationalities.

It can be highlighted that provisions in mega-trade deals will contribute to the creation of rules and practices in terms of intellectual property, uniform treatment of companies, capital and services. Nowadays, it is getting increasingly difficult to identify the nationality of products, companies, expertise and services while it remains relatively easy to circumvent the rules. Thus the benefits of mega-RTAs in these areas will imply soft instead of hard preferences. Provisions of deep regional trade agreements, such as RCEP, TTIP and TPP are therefore similar to unilateral liberalizations bound by RTAs.

On the contrary, the third category; the provisions on non-preferences take after the characteristics of multilateral liberalization as members have to comply with many arrangements that are already in existence and due to their ‘openness’, there is no preference established. These free trade agreements are responsible for dealing with internal reforms with multilateral applications.

It is argued that the dominance of soft over hard preferences has paved the way for ‘reverse trade diversion’. While preferences help the growth in the volume of trade between the partners, an increase in imports from non-partners can also be seen, even though only to a lesser degree. As a consequence, mega-RTAs tend to establish trade linkages with the inclusion of both member and non-member states. (WEF, 2014, pp. 22-23)

The *regulatory framework* of mega-RTAs revolves around the harmonization of values, norms and regulations. The lack of similarity between the national standards of member states leads to additional costs for the company that exports its products, which can be manifested in the adaptation to the discrepant standards of countries and the acquirement of certification. The flaw of harmonizing measures is that although they are capable of reducing the costs originated in the technical barriers of trade, it is not to the same extent everywhere. For example, if a certain standard is agreed on, differences remain between a nation with ‘standard-settings’ and the country that does not qualify in this category. The access might be granted at a lower cost; however, the cost of adaptation to the standard should also be taken into account.

I have explained it in order to be able to argue that it is plausible for a corporation which is a non-member of a certain mega-RTA to enjoy the advantages of the members’ market. It is shown in Figure 1 by the blue arrow from China to the TPP nations. The red arrow to China on the other hand intended to highlight the nature of regulatory convergence to increase the level of exports of companies within the framework of RTA to countries that are not included in the arrangement. On top of that, based on the example of Norway and Switzerland in Europe, it could be reasoned that the adaptation of standards do not need to coincide with membership. Regulatory convergence puts forward practices that are also consistent with firms outside the agreements.

In brief, it could be pointed out that regulatory convergence resembles multilateral liberalization, since its gains can be realized by both member and non-member states, despite the fact that the benefits of the included participants exceed the advantages of the countries that did not join the arrangement. Regulatory convergence is therefore likely to boost commerce in mega-RTAs and to induce imports from the outside nations. (Ibid. pp. 23-24)

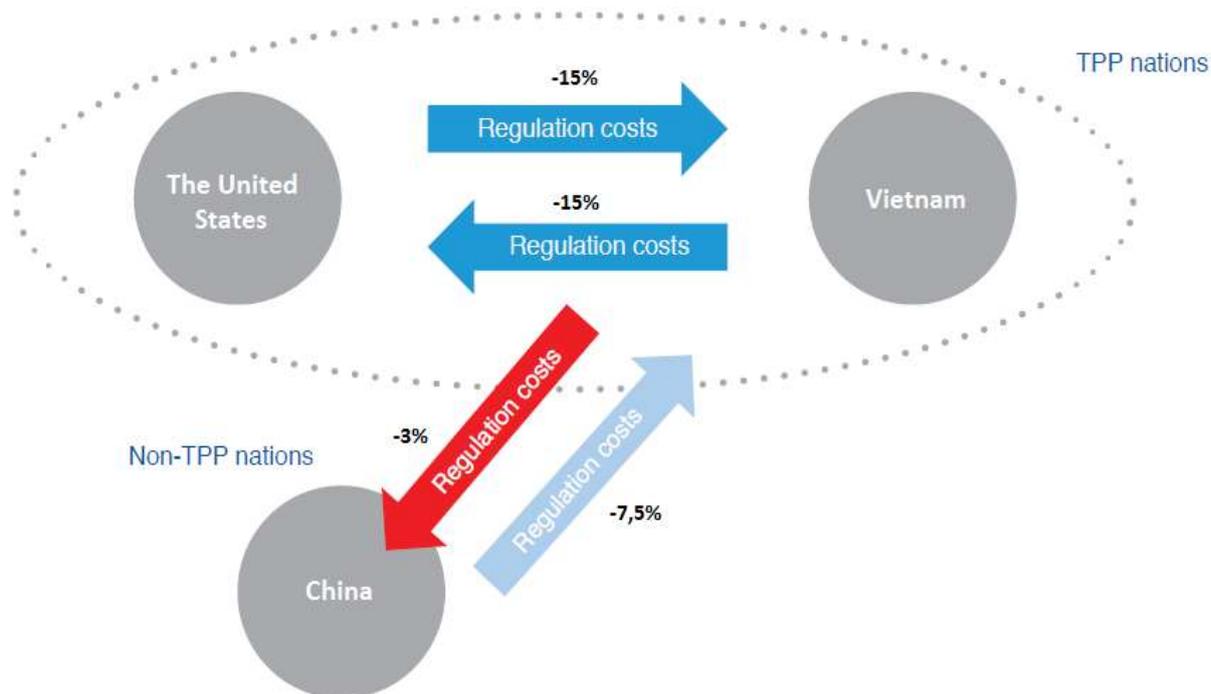


Figure 1: The Illustration of the Impact of Trade Costs in Regulatory Convergence

3. The Political Economy of Mega-RTAs

When it comes to analyzing the political economy of mega-regional trade agreements and identifying the most crucial players as well as their viewpoints about the deals, the history of mega-RTAs ought to be traced back to the mid-1990s. RTAs have risen to the agenda simultaneously with the increased dominance of the World Trade Organization. The establishment of the North American Free Trade Agreement initiated changes that brought about a new phenomenon, which is usually referred to as 'new regionalism'. Since the mid-1990s the world could witness the expansion of free and preferential trade agreements, integrating economies by opening up mutually a great variety of areas. The rise of mega-trade deals shows an on-going tendency in regional cooperation.

As the Doha Round was concluded without reaching an agreement concerning multilateral trade, the results of negotiations cast a shadow over the inefficacy of decision-making in the political sphere. Nonetheless, in order to explain the outcome of the talks, all the intermeshing factors need to be taken into consideration. Obviously, with the WTO encompassing more and more members, it was hard to come to an arrangement with the reconciliation of point of views. Furthermore, the financial crisis of 2008 brought protectionism to the fore, which rendered the situation more difficult. On top of that, the transformation in the roles of emerging markets need to be stressed as China, India and Brazil intended to have greater influence in policy-making, although they were not willing to make concessions regarding market access and come to terms with the developed nations' demands.

Following the beginning of the 2000s, a geopolitical realignment has taken place in international political economy. The United States seemed to have reached the peak of its strength and started to become exposed to the loss of its influence in relation to the emerging countries that encountered rapid growth and development. Hence, it could be argued that one of the reasons the U.S. intended to join the TPP was to compensate for the relative loss of

influence in the Asian region, especially after China began to have a more dominant position in the area. Another reason behind the participation of the United States in the TPP was probably connected to its desire to have a say in the implementation of stricter intellectual and property rights. Despite the fact that their effects on innovation are not known, they could certainly constitute a vast base of rents for the proprietors of copyrights and patents in the United States. (Rodrik, 2015) In addition, according to the U.S. the TPP can be regarded as a tool for both procrastinating and counterbalancing a China-led economic partnership in the East Asian region. Besides, the United States might also use the TPP as a restraining force on Australia, Japan and South Korea in order to draw them away from the increasing economic influence of China. However, considering the prospective welfare of those economies, it must be pointed out that China and not the U.S. is their major trading partner. Moreover, the United States was striving to include Japan in the negotiations of the TPP in order to possess a substantial percentage of the GDP. Yet it also served the interests of Japan whose intention was to position itself closer to the U.S. in security matters. Lately, Taiwan, an important partner of the United States in economic and security affairs expressed its desire to join the TPP, which idea was widely cherished in the U.S., since it was argued that the country could keep China's growing authority under surveillance in the region.

The Regional Comprehensive Economic Partnership can be perceived as a FTA including both ASEAN and non-ASEAN member states. Due to its openness in terms of widening, even the partners of the nations comprised of the ASEAN Free Trade Area can decide whether they would enter into negotiations. Furthermore, in pursuit of extending its influence, the participation of outside members with economic ties attached to the region is highly encouraged. Besides, as China was left out of the TPP and TTIP, Europe and the United States are hoping to be able to constrain China to adapt to the rules of trade created by them. It might seem to be an ambiguous strategy, since on the one hand there may be an intention to assimilate the East Asian country to the liberal world economy, but on the other hand the seclusion of China with setting obstacles in front of it in profitable markets also remains plausible.

Regarding the Transatlantic Trade and Investment Partnership, it could be argued that if and when it is attained, both the European Union and the United States can take advantage of the agreements as a result of deeper integration. However, the economic benefits of the partnership can only be realized after reforming the regulatory framework. There should also be arrangements made concerning the access to each other's markets of financial services, pharmaceuticals and foods. On top of that, the TTIP is expected to deplete the space available for regulatory actions domestically in both Europe and the United States as a consequence of the destruction of non-tariff barriers between the countries.

There is a more daunting issue centered on the TPP and TTIP, namely the provisions in relation to the Investor-State Dispute Settlement. These factors contributed to the creation of an entirely new legal procedure that lies outside the nations' judiciary, stating that companies have the right to prosecute governments for the infringements of arrangements. In economic terms, although, the ISDS might have positive effects; at least for countries with efficient rule of law, but also for nations that lack its efficiency, since it leads to the increase of investment opportunities. Yet it still does not clarify why the provisions of ISDS are necessitated for the TTIP, which encompasses the highly-developed United States and Europe. (Ibid.)

After the conclusion of the Uruguay Round in 1994, the developed nations could be relieved, having been able to maintain their crucial positions in regard to the multilateral trade. Yet

when the Doha Development Agenda was commenced in 2001, the emerging nations indicated that developed nations had not yet completely implemented their existing WTO obligations which were aimed at opening their markets, signaling the Doha Round to put the emphasis on the topic of development. Since then the situation has remained unresolved with intensifying conflict of interests between the participants. According to the perspective of the United States, the developing economies of Brazil, India and China are responsible for reaching stalemate, as they were not willing to make an increased number of concessions in terms of market-opening. Hence, the U. S. has committed itself to a hardline method of trade arrangements in the Asian region, joining two-sided FTAs and the TPP, focusing on policies that are aimed at the rights of state-owned enterprises and environmental issues. (WEF, 2014, pp. 20-21)

4. The Systematic Evaluation of Mega-RTAs

The rise of mega-RTAs might be seen both as a beneficial and a harmful phenomenon in our globalizing world. The pace of liberalization and the previously unprecedented volume of trade have indicated significant changes in international world economy. Trade liberalization was severely reinforced by various reforms in policies that were directly linked to bilateral investment treaties, the “spaghetti bowl effect” of RTAs and one-track reforms. The advantage of mega-trade deals can be realized by their capability to ‘untangle’ and simultaneously rearrange the spaghetti. On the contrary, the disadvantage is that mega-RTAs might put an end to the dominant role of the WTO in the global trade system. Considering the policy reforms, it can be argued that neither have uni-, nor bilateralism ever constituted any systematic danger to the world economy, but mega-RTAs are prone to have devastating consequences for the WTO’s centrality in terms of writing the trade rules.

In the following section I would like to take the *potential transformation in the WTO’s rule-writing* and the *probable changes in regulatory convergence* under scrutiny in order to be able to provide a systematic evaluation of mega-trade deals.

It is mainly the investments, services and commerce that could prove to be weakened in the rules-writing of the WTO. Firstly, it may be reasoned that the way norms of trade had been annunciated changed. Initially the universal acceptance of trade rules reflected relative equality among the nations, however, with the rise of mega-RTAs the asymmetries in power relations seemed to have been revealed. In relation to the RCEP, TTIP and TPP the dominance of the major players, such as China, the European Union, Japan and the United States cannot be ignored in comparison to the smaller, developing economies. Indeed there is always a balancing factor in case of the participation of more giants in a particular RTA. Yet it remains uncertain whether the norms would also be widely respected in the absence of legitimacy deriving from unity and multilateralism. Taking the example of India, China and Brazil; the nations that could benefit from their lucrative markets thought technology and investments without entering into a mega-RTA may come to the rejection of trade rules. It is feared that the spread in lack of confidence would induce ‘competitive liberalization’, tunneled behind a U.S. strategy in order to surround the countries by mega-trade deals.

Secondly, I would argue that the WTO is still needed for investments, services and commerce. Lacking a forum so fundamental for multilateral trade negotiations would confessedly render the management and logistics of trade policies more difficult than ever before. While both the demands of the developed and developing nations are likely to be met in the short run,

countries such as Brazil, China and India would not be satisfied with the arrangements. As a result, they would try to lay out rules and norms that served their own interests. However, due to the absence of firms fostering innovation and technology, these nations could not benefit from reforms after the relocation of their businesses to foreign countries in pursuit of lower costs. In the long term, they might; but by that time the rules of the E.U., Japan and the U.S. will be set in stone. If and when mega-trade deals are agreed on, they will have been directly attached to international trade as well as the laws and regulations of the domestic sphere. BITs have played the major role in the progression of services, commerce and investments and the authority of the WTO has remained essentially the same so far, although the increasing power asymmetries are disquieting. From today's perspective it seems certain that the European Union, Japan and the United States will have the final say in trade governance; it is rather the reception of India, Brazil and China we might be more curious about.

Thirdly, there ought to be a reform in order to bring mega-RTAs under the authority of the WTO. Despite the fact that adjudication within the framework of the intergovernmental organization proves to be functional, it must be pointed out that it is only the case as long as regulations are infrequently updated. If mega-regionals were responsible for rules-writing, multilateralization would have to take place with the purpose of updating the rules of WTO. However, it is thought to entail serious political consequences. The rise of mega-RTAs can be perceived as threat from the standpoint of global trade in terms of the erosion of WTO's centrality. This trajectory is expected to continue unless reforms are introduced so that new norms could be established *inside* the WTO. It could be argued that the future of the organization may be secured by the creation of a multi-pillar trade governance with the Marrakesh Agreement and the Dispute Settlement System being the balusters of it. Since frictions between the nations are likely to be resolved easier outside than inside of the WTO, they are advised to be discussed in a less-restraining political environment. Basically, this mechanism would be similar to the BITs in regard to the formation of parallel tracks without the erosion of the WTO's dominance. To be honest, it is a rather optimistic outcome. The other side of the coin is the question whether global trade can remain to rely on regulations and principles instead of power relations in the future. According to this view, if and when power asymmetries and mega-RTAs prevail, the major players of international trade would dictate all the rules with the small- and medium-sized economies having no influence at all.

Concerning regulatory convergence, it should be emphasized that the number of binding rules must be limited in order to reduce the restraining effect of TBTs. It could be achieved by either harmonization or mutual recognition, generating a set of principles all the nations could universally respect.

The aspirations of countries to harmonize norms have proved to be politically unattainable so far. Indeed, the creation of standardized rules is highly desired by each economy, the companies seem to be reluctant in a way that they would all prefer their own norms to prevail. Furthermore it is getting an increasingly difficult and drawn-out process to assess whether the regulatory protection could be applied in a uniform way. It is also crucial to study the impact of changes commercially in regulatory convergence, since the benefits are thought to be spread out among the nations equally. Based on those elements, I would argue that harmonization is unsuitable as there are a lot of constraining factors that can hinder the success of establishing a universally-accepted set of norms. As a consequence, regulatory convergence has to revolve around the mutual recognition of norms. However, it ought to be stressed that it is all about faith put in another country's system of governance and therefore a rather likely occurrence among wealthy nations. To illustrate the point, a comparison could be

made between the TPP, TTIP and RCEP. Out of those the TTIP is the most likely to be concluded on the basis of convergence, since it contains nations with an advanced regulatory framework, while with the TPP and RCEP the differences that have to be bridged are greater. The moral of the systematic evaluation of mega-RTAs is that it is basically the poorer economies which come off badly in comparison to the rich ones, hence the importance of power relations should always be reckoned with. (Ibid. pp. 26-27; Lamy, 2015, pp. 72-73)

5. Conclusion

The success of reaching an agreement with the Trans-Pacific Partnership in October, 2015 spurred optimism concerning the fate of other mega-RTAs. Especially that both the TPP and TTIP are based on the same logical foundation that can be traced back to the desire of the United States to be in sole control of the multilateral trading system. Moreover, the TPP and the RCEP can be regarded as ‘mutually reinforcing parallel tracks for regional integrations’ (MTI, 2012, p. 3) that target the Asian-Pacific region, attempting to become the driving force of trade reforms on a global scale. In addition, the arrangements can be seen as depictions of a competition between China and the U.S in terms of soft power and ideology. The emerging nations of the world economy are troubled as well, since they do not want to experience the downside of trade-diversion created by mega-RTAs. The only rational solution left is that they also start entering into FTA negotiations. Nevertheless, this phenomenon is likely to induce tensions between trading partnerships, paving the way for the fragmentation of world economy. Can peace be preserved or are we approaching the time of escalating conflicts?

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