

Bilateral and Regional Free Trade Agreements

Some Critical Elements and
Development Implications

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MARTIN KHOR

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Third World Network



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CHAPTER 1

Bilateral Free Trade and Economic Agreements

SEVERAL developing countries are now either part of bilateral and regional free trade agreements (FTAs), or are involved in negotiations to create them.

There are two broad categories of FTAs. One category involves South-South arrangements, usually among neighbouring countries, and in regional groupings, such as ASEAN, SAARC, SADC, Mercosur, Andean Community. The second category involves an FTA between a developed country or entity (such as the US and European Union) and a developing country or a grouping of developing countries. Examples are the US-Singapore and US-Central America FTAs and the EU-ACP Economic Partnership Agreements (EPAs).

This paper deals with FTAs between a developing country and a developed country. Such FTAs usually cover a range of issues beyond simply trade in goods. They include market access in trade in goods; services; investment liberalisation and protection of investor rights; intellectual property; government procurement; competition policy; labour and environment standards.

In particular, the paper mainly examines FTAs involving the United States and developing countries. In doing so, examples of the US FTAs with specific countries, particularly Singapore and Chile, are used. The chapters in these FTAs (on services, investment, government

procurement and so on) reflect what a “typical” FTA with the US is like. This is because, as is quite well known, the US makes use of a “template” for its negotiating position in its bilateral FTAs. Its recent bilateral FTAs are rather similar in chapter headings as well as in text. It may well be that the US would not agree to conclude an FTA unless its text basically is in accordance with the template.

There is less information available on the European Union’s FTAs. The main negotiations currently undertaken by the EU are the Economic Partnership Agreements with the African, Caribbean and Pacific (ACP) countries. The paper also contains a brief section on these EPAs.

The brief conclusion is that many of the chapters of the FTAs reduce, in some cases very significantly, the policy space that developing countries have. In the area of market access in goods, the elimination or drastic reduction of tariffs in almost all categories of goods will remove an important and powerful instrument (the tariff) that developing countries have as a crucial component of industrial and agricultural policy. The agreement to make use of a “negative list” approach puts greater pressure on the developing country to liberalise and reduces the policy space to be able to choose which sectors to liberalise and when. The chapters on the “Singapore issues” (investment, competition policy and government procurement) drastically curtail the ability of the developing country to regulate the establishment and operations of foreign enterprises and their funds, and also put up new restraints on governments that make it much more difficult for them to provide assistance to domestic enterprises.

The paper argues that entering an FTA with developed countries, with the kind of template that they have for their FTAs, is a serious matter for a developing country to have to consider. An assessment of benefits and costs should be undertaken by the country before embarking on negotiations.

CHAPTER 2

Disadvantages of FTAs Compared to Multilateral Trade Agreements

It is generally recognised that bilateral agreements, especially between a developing and a developed country, are not the best option and that multilateral negotiations and agreements are preferable. The reasons for this include:

1. Bilateral agreements usually lead to “trade diversion”, in that the partners divert away products that may be more cheaply priced in favour of products from the FTA partner, even if they are not cheaply priced, thus resulting in inefficiency.
2. In an FTA between a developed country and a developing country or countries, the latter are usually in a weaker bargaining position due to the lack of capacity of their economies, their weaker political situation, and their weaker negotiating resources.
3. In the World Trade Organisation (WTO), the principles of special and differential treatment, and less than full reciprocity, are recognised. Thus, developing countries are better able to negotiate on the basis of non-reciprocity and for non-reciprocal outcomes, in which they are not obliged to open up their markets (or undertake other obligations) to the same degree as developed countries. However, these “development principles” are usually absent in FTAs, or they are only reflected in longer implementation periods for the developing country. The FTAs are basically on the basis of reciprocity. This “equal treatment” of parties that are unequal in capacity is likely to result in unequal outcomes.



4. The FTAs contain many items that are not part of the rules of the WTO. Many North-South FTAs include rules on investment, government procurement and competition law, which have so far been rejected by developing countries as subjects for WTO negotiations or rules. Developing countries have also objected to making labour standards and environment standards subjects of discussion in the WTO. All these topics are now entering “by the side-door” through the FTAs, even though the same reasons for developing countries to reject rules on these issues should apply in FTAs as they do in the WTO.
5. Even where issues are already the subject of rules in the WTO (e.g. intellectual property and services), there are many “flexibilities” and options open to developing countries in interpreting and in implementing obligations in these areas. However, there are attempts by developed countries to remove these flexibilities for developing countries in the FTAs. If these attempts succeed, the policy space for developing countries to pursue development and socio-economic goals would be significantly reduced.
6. The proliferation of so many agreements also puts pressure on personnel and financial resources in developing countries and requires a lot of technical expertise which may be not adequately available, given the large number of agreements and the limited resources.

The report “The Future of the WTO” commissioned by the WTO Director-General and which was published in January 2005 has criticised the proliferation of bilateral and regional trade agreements, which it says has made the “MFN” (most favoured nation) principle the exception rather than the rule, and which has led to increased discrimination in world trade. (WTO 2005).

However, it appears that FTA negotiations are moving ahead and negotiations on even more FTAs and RTAs (regional trade agreements) are being announced.

Several researchers have pointed out that whilst bilateral agreements may be tempting for a developing country to get some specific advantages from its developed-country partner, such as better market access for some of its products, there are also several potential dangers and disadvantages.

Developed countries such as the US and Japan are known to want to use the instrument of bilateral agreements to obtain from their partners what they failed to achieve at the WTO, in which the developing countries have been able to oppose or resist certain negative elements in various agreements. For example, the inclusion in FTAs of certain provisions that reduce the ability to make use of development flexibilities (such as compulsory licences) in the WTO's TRIPS (Trade-Related Aspects of Intellectual Property Rights) Agreement is known as "TRIPS-Plus". Another major element is the inclusion of the "Singapore issues" in FTAs involving the US and EU; these issues were removed from the WTO's Doha negotiations at the request of developing countries as they considered that they had adverse development implications. These issues, rejected at the WTO, have made a comeback through the FTAs.

The report on "The Future of the WTO" also criticises the tendency of recent FTAs to introduce "non-trade issues" which had been rejected at the WTO. It says: "One other unanticipated and significant issue that has arisen with the growth of PTAs [preferential trade agreements] is the injection of particular 'non-trade' objectives into trade agreements. Apart from comparatively ambitious and one-sided provisions on intellectual property rights, we have seen an increasing tendency on the part of preference givers to demand significant labour and environmental protection undertakings – and even restrictions on the

use of capital controls – as the price for preferential treatment. The evident fear is that such requirements become not merely ‘templates’ for further PTAs but the forerunners of new demands in the WTO. After all, as more and more countries concede non-trade provisions of this kind at the PTA level the less these WTO Members are likely to stand out against demands for their eventual inclusion in the multilateral rules. We would argue that if such requirements cannot be justified at the front door of the WTO they probably should not be encouraged to enter through the side door.” (WTO 2005)

CHAPTER 3

Changing Views on the Effects of Liberalisation

WHILST an advanced developing country which is already highly liberalised may be able to bear the pressures of faster liberalisation, other developing countries may not be able to compete with the faster opening of their markets or with other demands of the developed country.

Up to a few years ago, there was a widespread belief in the orthodoxy (promoted especially by the International Monetary Fund (IMF) and World Bank, and by policy makers in developed countries) that liberalisation is necessarily good for development, and the faster the liberalisation the better it is for development. This was the intellectual basis for developed countries to pressurise developing countries to quickly and deeply cut their tariffs and remove non-tariff barriers, as well as open up their services sector, financial sector and investment regime.

However, there has been growing skepticism not only from civil society but also policy makers regarding this orthodoxy, mainly because such rapid liberalisation has led to import surges in many developing countries, with adverse effects on the local industrial and agricultural sectors, and on the balance of payments and the debt position. The emerging paradigm is that developing countries require certain degrees of protection to enable the local firms and farms to compete in their own domestic markets, and that this was the way the now-developed countries arranged their own trade and industrial policies when they were at the development stage.



Bilateral and regional free trade agreements (FTAs) between developed and developing countries are proliferating. They usually contain tariff-reduction commitments and disciplines deeper than at the World Trade Organisation and also contain rules that are not in the WTO.

This book argues that the comprehensive and strict obligations these FTAs impose will seriously constrain the developing-country party's policy-making capacity to pursue national socioeconomic and development goals. As a result of this erosion of policy space and the drastic market-opening demanded by FTAs, no less than the country's development prospects would be undermined.

The book examines the development implications of FTAs for signatory developing countries in each of the major areas typically covered by these agreements, including trade in goods, trade in services, investment, government procurement, competition policy and intellectual property rights. In light of the very real risks posed, developing countries should assess the costs and benefits of an FTA before deciding whether to enter into or conclude negotiations.

The book uses the typical FTA that the United States adopts with developing countries as the main basis of its analysis. FTAs adopted by other developed countries share many of the same features.

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