

Chapter 2

Multilateral responses

The message of the previous section is not particularly encouraging: even if the shocks to excluded countries or sectors within them are material, there is not much that excluded country governments can do about them other than adjust and seek help from the offending parties. Their best hope is to negotiate, possibly by making market access concessions of their own, an attenuation of the harm they feel. Multilaterally, the situation is not quite the same.

The sum of the even small adverse effects on excluded countries may be significant and, acting together, the set of excluded countries will have a good deal of negotiating power if they choose to use it. Article 24 of the GATT offers one route into this negotiation, and it is far from definitive about what is WTO-consistent in the field of FTAs. Thus, for example, although the requirement to liberalise ‘substantially all trade’ is interpreted by the EU to mean the freeing up of 90 per cent of the partners’ mutual trade, presumably, as with the EPAs, comprising 100 per cent of EU imports and 80 per cent of India’s imports, this has never been tested in dispute or ruled upon by the WTO’s Committee on Regional Trading Arrangements. The threat of a concerted challenge by excluded countries could cause a rethink by the partners. One should not under-estimate the change in customary practice that such a challenge would imply within the WTO. The convention has been one largely of mutual tolerance – we will not challenge your FTA if you do not challenge ours. And it will require considerable coherence among the group of excluded countries. Nonetheless, it is the view of many trade economists that the trading system would be a stronger institution if it took more seriously its principle of non-discrimination.

Outside the WTO, excluded countries may conclude that they should ‘play the FTA game’ harder themselves, negotiating hard and seeking access to deep and meaningful FTAs with the EU and India – and, indeed, anyone else – in ways that reduce the discrimination they face and support their own reform programmes. As we noted above, this will require concessions and will certainly require a serious input of diplomatic, political and technical resources. It may eliminate net distortions in the world economy and result in greater market access and deeper institutional reform of their economies, all of which will tend to enhance their economic performance.

On the other hand, they may reason that negotiating FTAs diverts attention and effort from the multilateral system. For example, resources are devoted to writing and reading this report rather than contributing to the success of the multilateral round, and regionalism may reduce the interests of the business sector in non-discriminatory trade reform and liberalisation. Moreover, if the response to the EU–India FTA is for excluded countries to try to negotiate further FTAs for themselves (as Baldwin’s, 1997, Domino theory pre-

dicts), even small effects may be replicated many times over as the trading system fragments. Given that there is little reason to believe that we will be able to converge on free trade through the gradual accumulation of FTAs, the overall losses from proliferation could be quite serious. Nearly every country is excluded from nearly every FTA, so this cumulative effect is likely to gravitate to everyone's disadvantage eventually.

On this view, excluded countries may wish to oppose the process of creating FTAs in international fora, not in an instrumental way based on trade calculations of the sort we have performed here, but as a matter of principle and as a systemic issue which could eventually undermine the benefits of multilateralism which we currently tend to take for granted. Of course, in maintaining such a position, they would need to show a small amount of consistency and limit the extent to which they pursued FTAs themselves. If they conclude that this is the route to pursue, groupings such as the Commonwealth may become important focal points of their efforts.

It would be nice to conclude with a definitive recommendation on the question of the correct stance for small and poor countries on FTAs and the trading system. However, that is not the subject that we were asked to explore here. Moreover, the evidence about the relative merits of these two approaches is complex and ambiguous, and both the policy communities and the economics profession are divided on them, so a thorough discussion must be postponed to another occasion.

Part IV References

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