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THE BRAVE NEW WORLD OF CROSS-REGIONALISM

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NON-TECHNICAL SUMMARY

The paper deals with a new phenomena in the realm of preferential trading which has alternatively been called by various experts with different names: "Cross-Regionalism", "Transoceanic Agreements", "Preferential Trade Agreements", "Polilateralism", "Regionalism Without Regions", "Competitive Regionalism" and "Additive Regionalism". A distinctive feature of this new trend is the simultaneous participation of countries in various Free Trade Areas (FTAs). In many cases, these FTAs have highly differentiated trade rules (usually also being implemented over different periods) and include countries belonging to different geographic regions. The launching of agreements of the new sort challenges geographical proximity as a necessary element promoting and making integration viable. Geographic distance is no longer perceived as a criterion for choosing preferred trading partners. This paper has adopted the concept of "cross-regionalism" used by WTO experts to describe this new trend.

About one third of the FTAs currently under negotiation are among countries that belong to different world regions, with a growing share of North-South agreements. Cross-regional agreements account now for a large proportion of the total increase in PTAs (preferential trade agreements). Both the EU and the USA try to encroach themselves in the sphere of influence of the other. Some middle-income countries (such as Israel, Chile, Singapore, Mexico) strive to escape their initial uncomfortable status of so-called "spoke" by signing agreements with more than one "hub". The most daring of them go forward and conclude also side agreements with other high-income "spokes"(e.g. Chile with Canada or Israel with EFTA).

Every developing country seems to have realized, as some middle income countries did some times before (e.g. Israel and Mexico), that whereas a country can belong to only one Customs Union, it can be a member to an infinite number of Free Trade Areas. Nobody can prevent it from doing so, neither the USA nor the EU. Developing countries and middle income countries do not need to be a "spoke" of only one "hub"; and it can also become a "hub" as well. This dynamic is what would then explain the "free-for-all" atmosphere characterizing this new wave of preferentialism.

Individual PTAs increasingly overlap one with another. This was exceptional in the past but it is rapidly becoming the rule now. The "hub-and-spoke" model tends to disappear or at least to be diluted.

Confronted with this development, the WTO Secretariat has sharply reacted, by stating that the multiplicity of preferential tariff rates (depending on the countries, the groupings or the rules of origin applied) would bring the system to a confusing state of affairs that private sectors would not enjoy.

In fact, the number of actual cross-regional FTAs implemented already is still quite small for the moment; this is why not much can be said yet about the real quantitative and/or welfare impact these new agreements might have.

Assuming that proximity determines the geographic distribution of trade (something which is questioned in the paper), natural trading partners are from the same region or continent by extension. Of course technological change affecting transport costs might influence the degree of "naturality". Frankel (1998) correctly indicates that if these costs fall with time, the regionally-based FTA will be less and less beneficial. He also introduces the interesting concept of "supernatural FTAs". These are those FTAs concluded among continental partners that are welfare-reducing due to low intercontinental transport costs.

This being said, the rapid conclusion of cross-regional agreements between "non-natural" trading partners in recent years poses the theoretical question of why they are concluded. Economically, independently of who of the two partners gains or losses, the overall diagnosis should be that caeteris paribus they may not increase welfare, but rather decrease it. Politically the argument whereby preferential trading allows large countries to create around them spheres of influence or promote democracy cannot be invoked since the shares of trade of the large country in the small one are far from being dominant. Economically, the only justifications seem to be 1) to overcome Frankel’s "supernaturalism", i.e. to neutralize the deleterious effects derived from having previously signed with a neighboring country leading to too much costly trade diversion; 2) for the small country to overcome the transport cost differential favoring non-preferred neighbours with preferential market access to the large country. Politically for the small country to sign with a far-away large country implies a reduction of dependence vis-à-vis the local hegemon, which is positively evaluated by some politicians. In other words, whereas differential country size in semi-natural FTAs leads to economic gains for the small and political gains for the large trading partners, in the case of non-natural FTAs, the two sides have both economic and political gains insights.

Insofar as the Multilateral Trade System is concerned, there are some good news and some bad news deriving from the new wave of cross-regionalism:

1. There is no danger of trading blocs emerging nor of a clash between them.
2. There are no new exclusive spheres of influence being created.
3. The new foreign policy goal of preferentialism is to neutralize the influence exerted by rival trading powers in a given zone; reverse trade diversion in favour of the distant trade power must be considered as positive, since it unravels previous trade diversion.
4. Economic opportunity is what drives the choice of preferred trade partners made by developing countries.
5. The proliferation of PTAs is taking place without any control whatsoever.
6. Large negotiating partners are favoured by the proliferation of preferential trading.
7. Least developed countries tend to be less favoured by emerging economies than other more developed ones (including other emerging economies).

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