Opinion piece

Can regional and multilateral trade liberalization work in tandem?

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The World Trade Organization was established 30 years ago, following the conclusion of the Uruguay Round of trade negotiations, the world's last major advance in multilateral trade liberalization. Since then, progress has been sporadic and limited to specific areas. More troubling, since the financial crisis of 2008-09, the multilateral trading system seems to be moving backwards, with the propagation of discriminatory trade barriers and a growing number of trade disputes being left unresolved. Could a move toward deep regional trade agreements be a solution?

The world did not stop reducing trade barriers in 1995. The key difference was in the approach to trade liberalization, which transitioned from multilateral to preferential/regional. In the two decades following the establishment of the WTO, the number of regional trade agreements (RTAs) grew more than six-fold. Although the pace has slowed in the last decade, new RTAs are still being signed, with 371 currently in force.

Is this the way to go? Should we be comfortable with the near-paralysis of multilateral trade negotiations if trade continues to be liberalized through RTAs? For many years, the answer has seemed to be yes. Except for the European Union, which is unique in many ways, most other RTAs until the early 2000s were "shallow", focusing primarily on eliminating bilateral trade barriers. While in theory the effect of those RTAs is ambiguous, the evidence shows that they created more trade than they diverted (Freund and Ornelas, 2010).

One key reason is that, as countries liberalized within the trading blocs outlined in the RTAs, they also (unilaterally) lowered trade barriers for countries outside those blocs. This suggests that tariffs for bloc insiders and outsiders are viewed as complementary: when one decreases, so does the other, albeit at a slower pace. The upshot is that the trade and welfare impact of RTAs have been much larger than studies prior to the formation of the agreements suggested.

More recently, RTAs have become increasingly "deeper", tending to extend beyond the bilateral reduction of tariffs to include a wide range of non-tariff barriers and regulatory issues. While "depth" sounds benign, the jury is still out on the merits of these additional provisions – see, for example Fontagné et al. (2023).

In fact, the extra depth often relates to measures that could hinder rather than boost trade and welfare. In particular, the tariff complementarity of shallow integration does not need to extend to those other measures. Moreover, these RTAs often include rules that transcend WTO rules, as is the case for some product standards and other technical barriers to trade. This may lead to concerns that the expanding network of deep RTAs could render the WTO's multilateral framework unworkable – if not irrelevant. This is troubling, because it could undermine a system that has proven very effective in bringing down trade barriers and in providing stability to world trade.

An unproven hypothesis, consistent with current trends, is that the multilateral trading system could coexist with the spread of RTAs, provided that the latter focus on the core issue of reciprocal trade liberalization – that is, the bilateral reduction of trade barriers. However, deep RTAs with provisions that conflict with existing multilateral rules may render progress in multilateral negotiations unattainable.

If this hypothesis holds, it would be necessary to call for restraint in the scope of future RTAs, to ensure that they do not impede broader multilateral liberalization. "Deep" issues, important as they are, might be better addressed within the WTO.

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