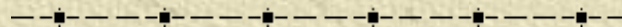


Module 1.

Trade Liberalization versus Economic Integration: Convergence Criteria

ECN330

Analyzing Trade Liberalization and
Economic Integration



2023

1. Globalization, liberalization and integration

1.1 Global economy and globalization

- ✦ Basic definition
- ✦ Trade liberalization
- ✦ Economic integration

1.2 Drivers of the process

2. Integration: Convergence Criteria

2.1 Convergence: economic, political and legal

2.2 Trilemma: integration, democratic principle, sovereignty

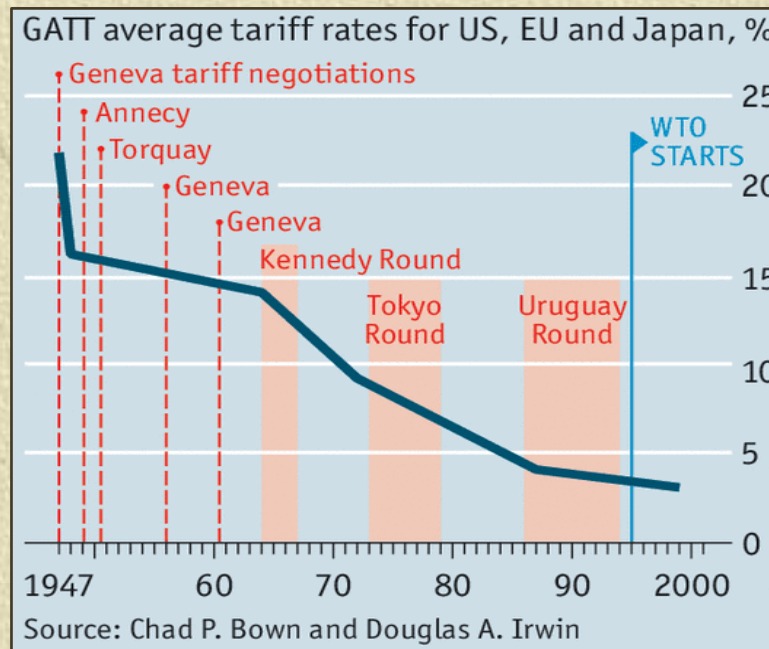
2.3 Theoretical construct

Integration criteria	Basic assumptions – conditions for convergence				No technology barrier / constraint	
	Competitive mkts	Identical goods, services, factors	No gov't policy/regs			No transactions costs
			Trade policy	Non-trade regs		
Trade in goods						
Trade in services						
Int'al K-mobility						
Int'al L-mobility						

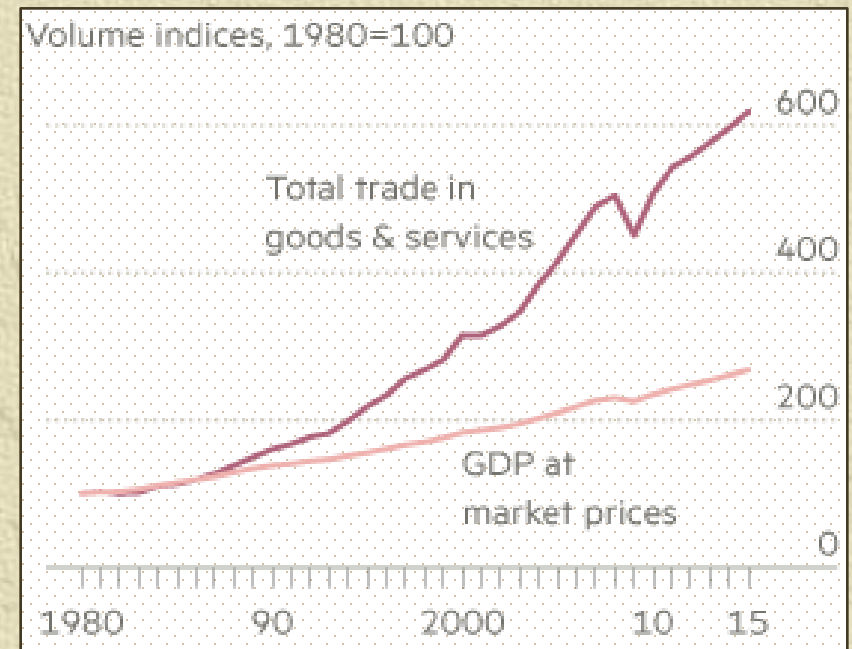
Integration: Convergence Criteria, continued . . .

2.4 State of global economic integration and convergence

- ✦ Historical account
- ✦ Trends: evidence of paths toward/obstacles to integration
- ✦ Current state
 - ◆ Liberalization and trade



Economist, “Trade blockage”, Briefing on the world trading system, 21 Jul 2018, p. 15-8.



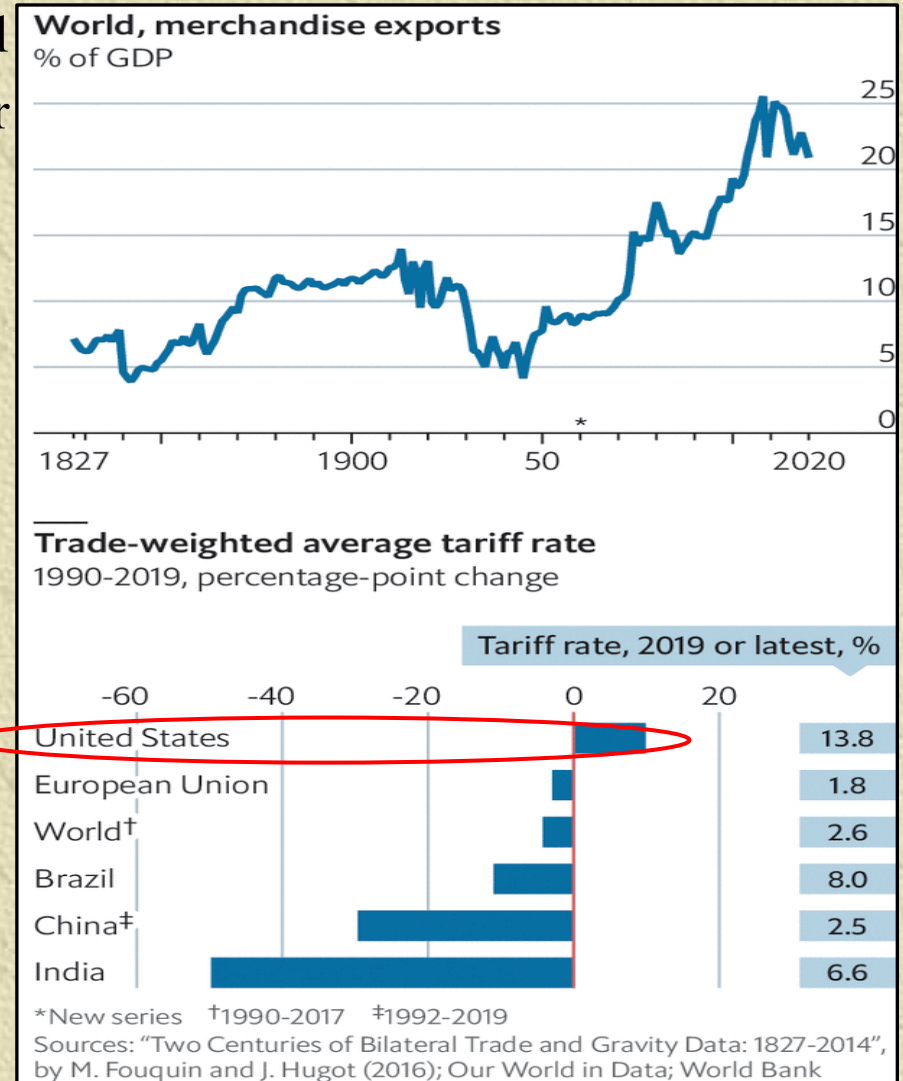
Financial Times, “Embattled future of global trade policy”, by M. Wolf, 13 May 2015, p. 9.

Integration: Convergence Criteria, continued . . .

Trade in goods and avg tariff rates

- Liberalization was multilateral
 - Global trade is now multipolar
- 25 largest EMEs by pop
% of total trade is with:
- ◆ 43% western bloc
 - ◆ 19% China-Russia bloc
 - ◆ 30% Non-aligned
 - ◆ 8% Other

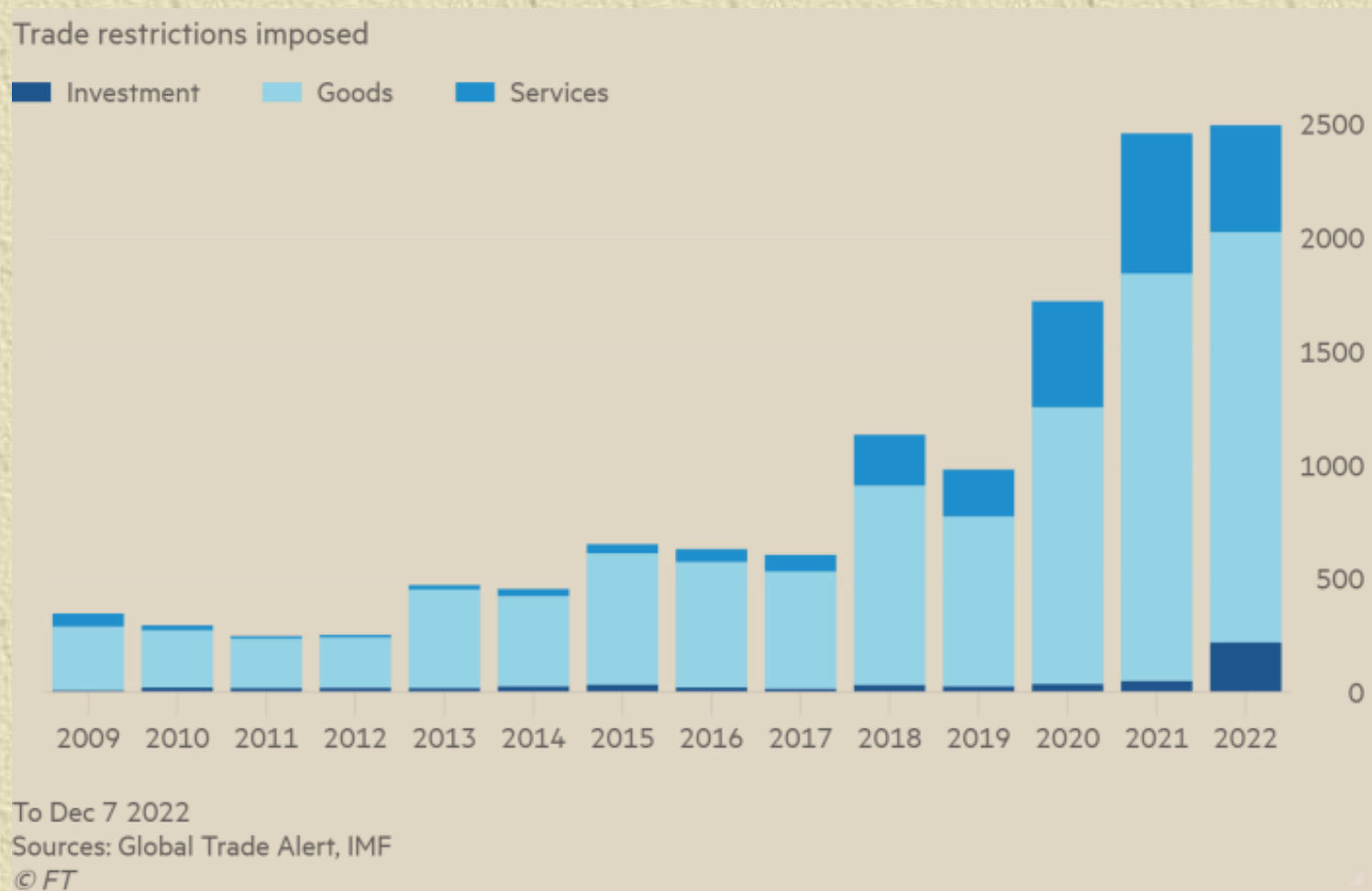
Trump's trade war →



Source: *Economist*, "World trade: The new order of trade", Special report on the world economy, 9 Oct, 2021. WTO Secretariat

Integration: Convergence Criteria, continued . . .

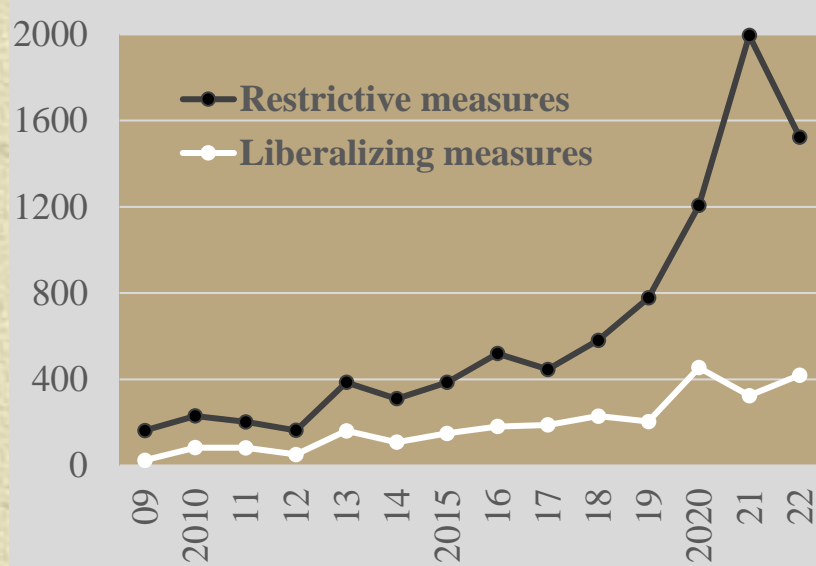
◆ Protectionism



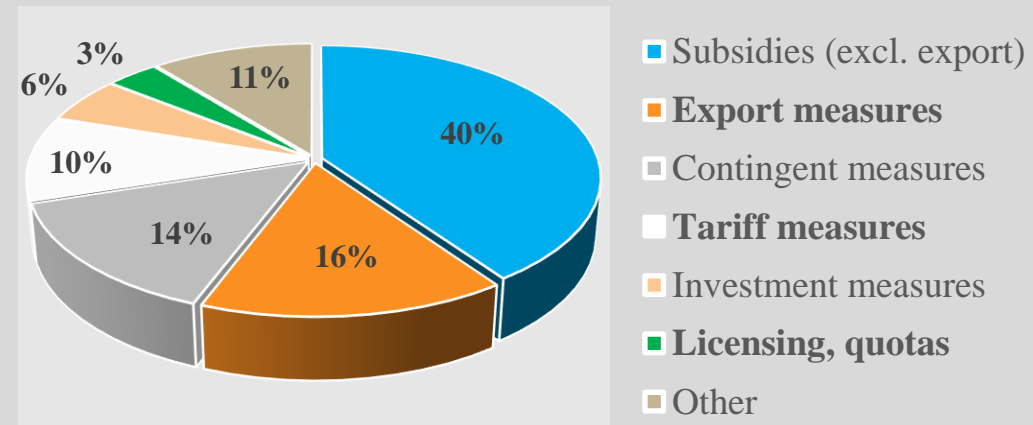
Integration: Convergence Criteria, continued . . .

◆ Restrictions on globalization

- New measures enacted against foreign commercial interests
- Restrictive measures by type, 2009-22 (total 8 888)

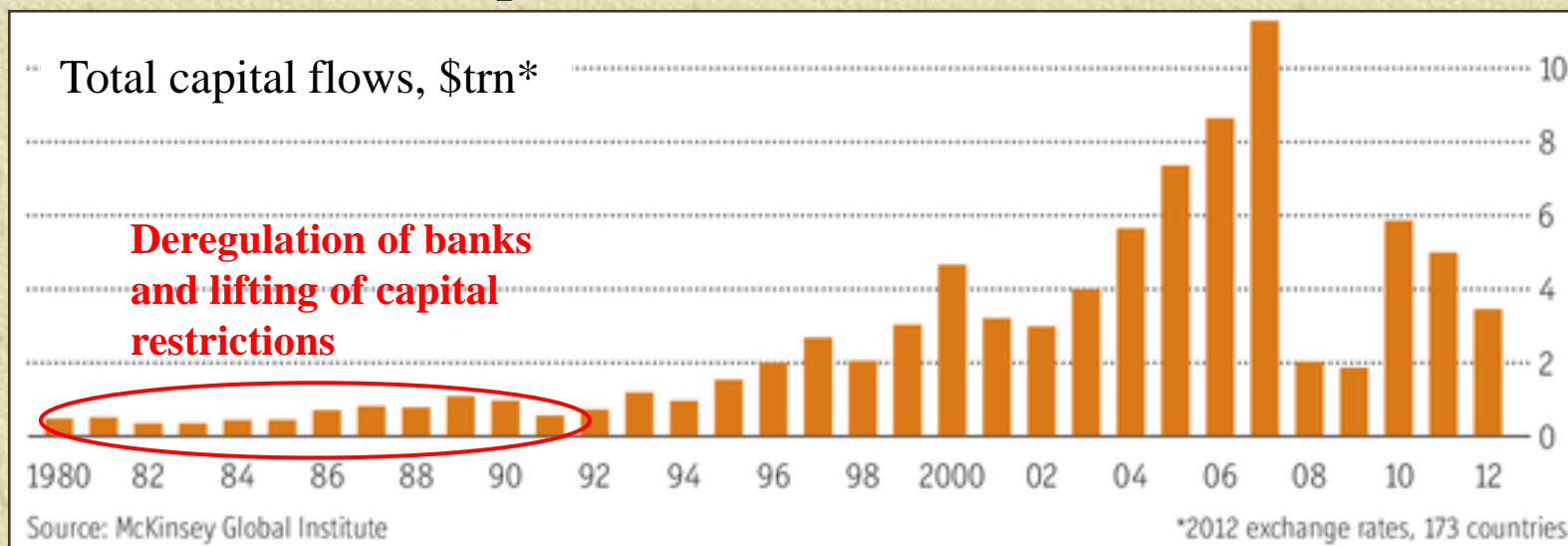


Restrictive policy measures, 2009-22

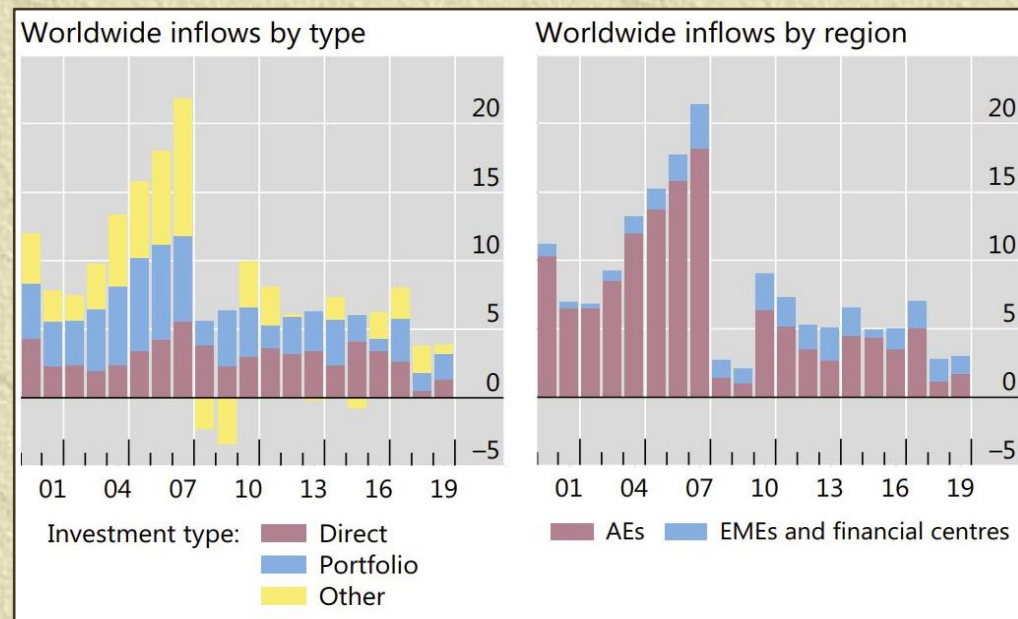


Integration: Convergence Criteria, continued . . .

◆ Cross-border capital flows, total in \$trn



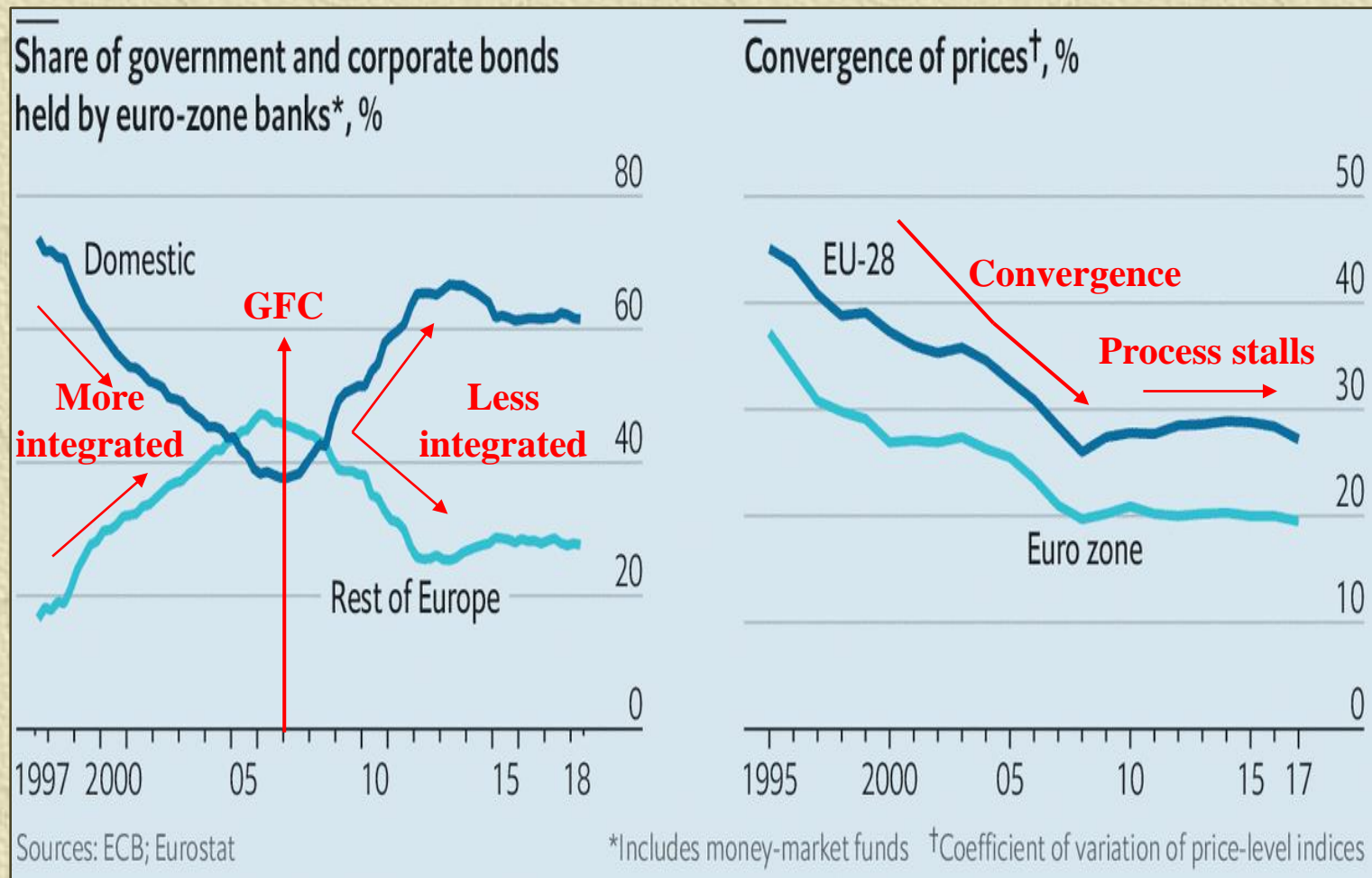
◆ Inflows, % of world GDP



Economist, special report: World Economy, 12 Oct 2013; BIS, "Changing patterns of capital flows", CGFS Papers, no. 66, May 2021, <https://www.bis.org/publ/cgfs66.pdf>

Integration: Convergence Criteria, continued . . .

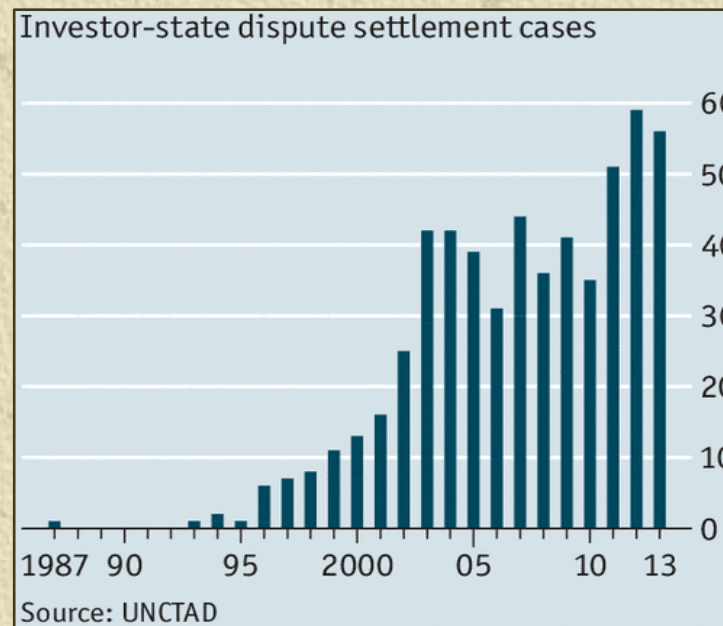
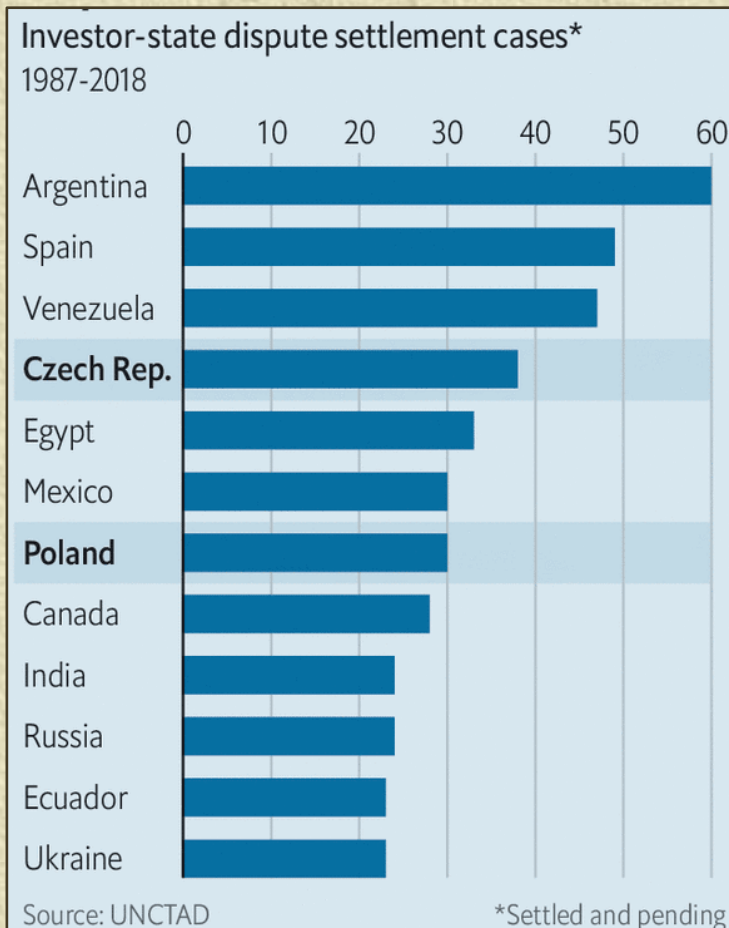
◆ Convergence within euro zone stalls



Integration: Convergence Criteria, continued . . .

- Disputes involving foreign investment

Bilateral investment treaties include investor-state dispute settlement (ISDS) provisions to encourage investment by protecting investors against discrimination or expropriation. A large share of the 942 ISDS cases during 1987-2019 involve post-communist states that joined the EU-15 in 2004 (Cases in Czechia, 38, and Poland, 30, account for 7%).

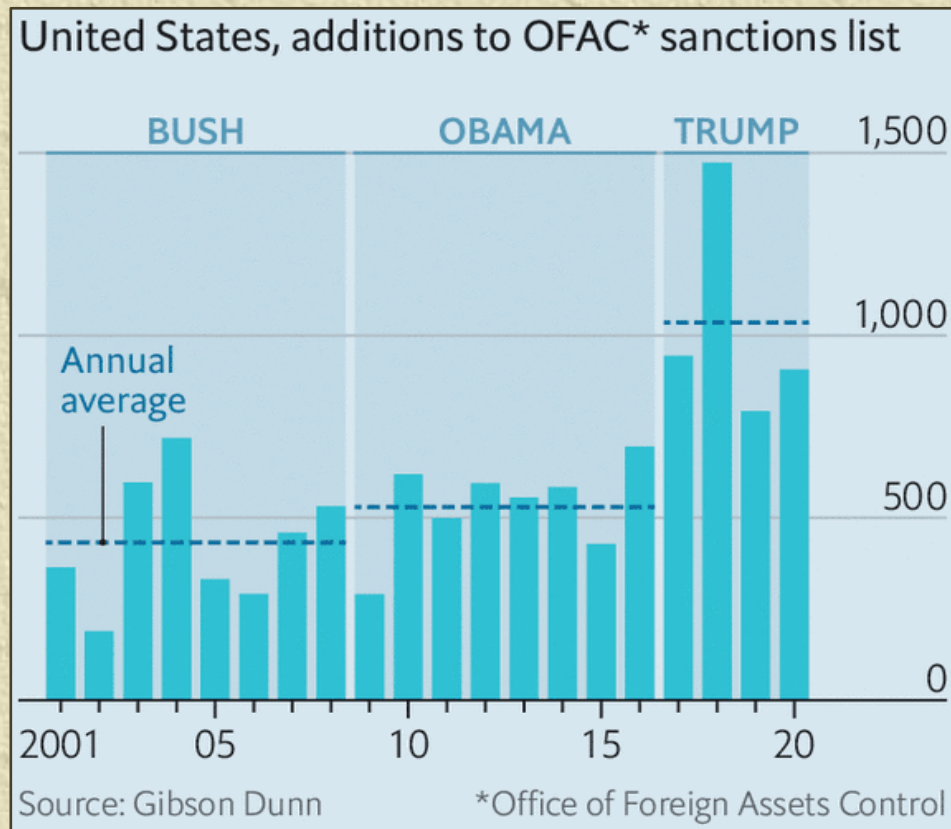


Economist, “Foreign-investment disputes: Kafkaesque”, 8 Jun 2019, p. 60.

Economist, “ISDS: The arbitration game”, 11 Oct 2014, p. 74.

Integration: Convergence Criteria, continued . . .

- Sanctions: foreign policy instruments restricting trade
 - ♦ Rise of extra-territorial enforcement of unilateral restrictions
 - ♦ China's in-kind response



In 2021 China passed a law stating the gov't can seize the assets and block transactions of firms complying with US or EU measures against China.

Economist, "Tit-for-tat struggles: Try this for size", 19 Jun 2021, p. 52.

Economist, "Handle with care: Sanctions are central tool of government's foreign policy", 24 Apr 2021.

3. Stages of Liberalization and Integration

3.1 Theoretical case for multilateral trading system

✦ Uni-, bi- and multilateral liberalization: convergence

✦ Debate on regionalism vs multilateralism

Argument	Regional bloc	Multilateral accord
[1] Static gains	Benefits concentrated; trade creation/diversion	Max global benefits; trade creation
[2] Promote trade; greater liberalization	Greater MA, esp if there are common regs; preferential	Rules-based MA; fewer exceptions; non-discriminating
↓ Facilitate trade talks	Blocs grow and merge	Blocs slow talks; EU: all 27 must agree before talks start
	Blocs ↓ number of players; ↑ profile of smaller countries	Blocs exclude poorest; Regional bully defines terms, blocs are political
[3] Dynamic gains or L-R integration	Integration is built-in agenda; integration → ↑ integration	Gains follow own course; Integration not formally covered
	Effect on competition / specialization from: (1) ΔP ; (2) Δ tech (economies of scale); and (3) Common/approx regs	

Stages of Liberalization & Integration, continued . . .

3.2 Stages of integration – not theoretically precise

✦ FTA and customs union

✦ WTO definitions: GATT Article XXIV

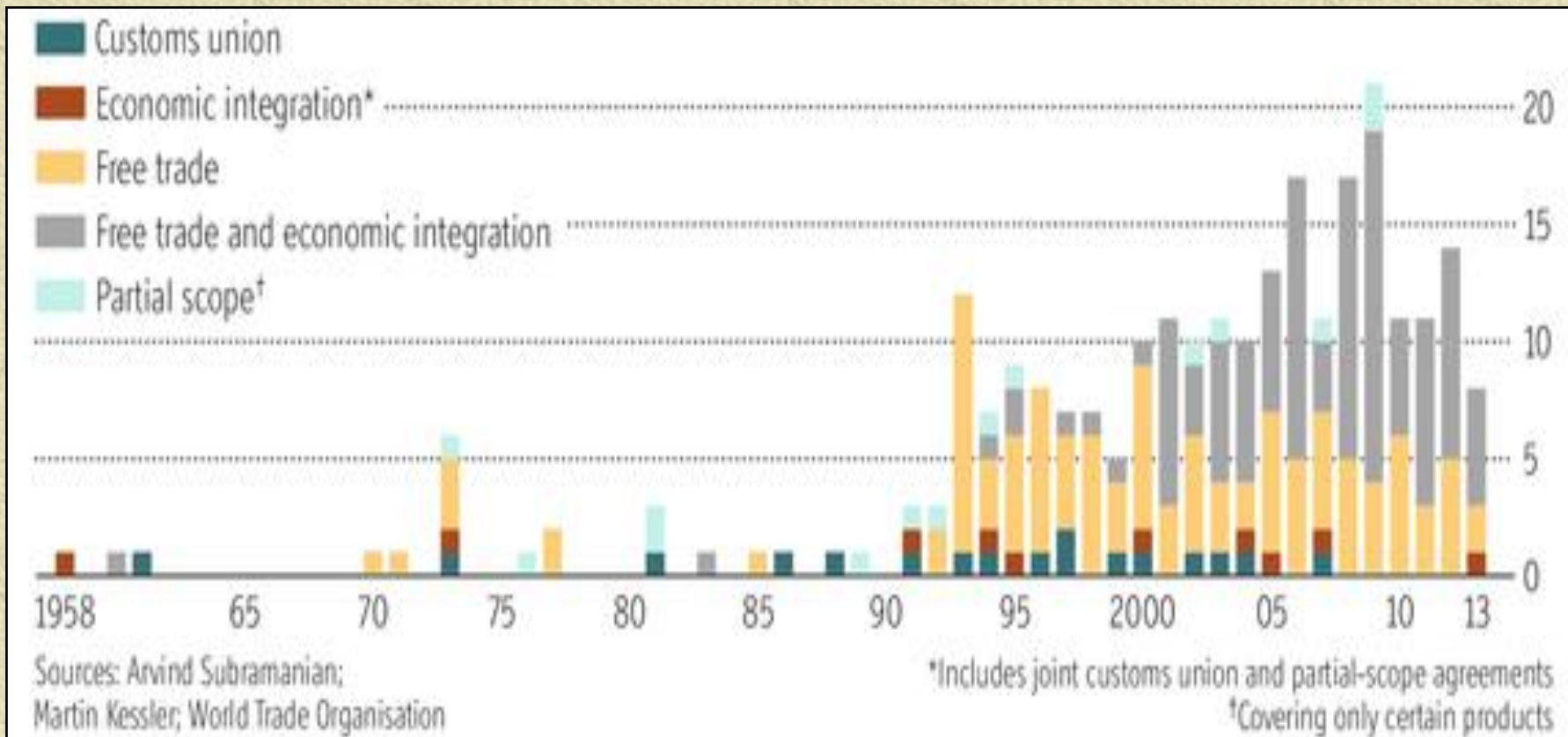
Clauses	Compliance issues
Para 4	Facilitate trade between territories (from para 2, those with separate tariffs or other regulations of commerce) without raising barriers to non-members
Para 5	Create FTA/CU withing a <i>“reasonable length of time”</i>
	Restrictions during phase-in period cannot be higher or more restrictive than generally applied
Para 8	FTA/CU defined as territories in which duties/restrictions of commerce are eliminated on <i>“substantially all trade”</i>
	CU requires CET on <i>“substantially all trade”</i>
Para 9	Conditions on transshipment of non-FTA goods: collect duty equal to a rate that eliminates arbitrage

Stages of Liberalization & Integration, continued . . .

3.3 Trends in regional trade agreements (RTAs)

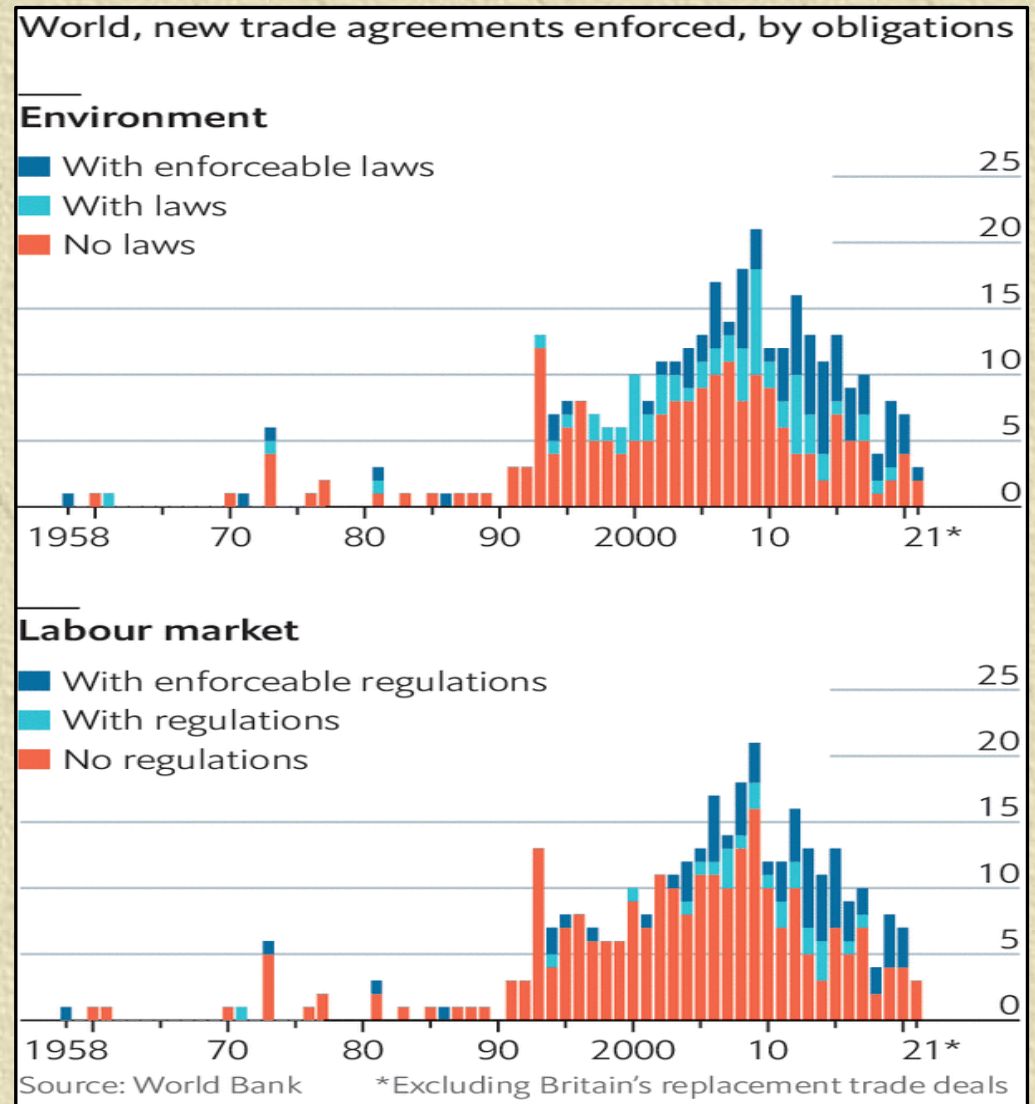
✦ Regional agreements

◆ By types (almost 300)



Stages of Liberalization & Integration, continued . . .

- ◆ Agreements including rules on environment and labor standards



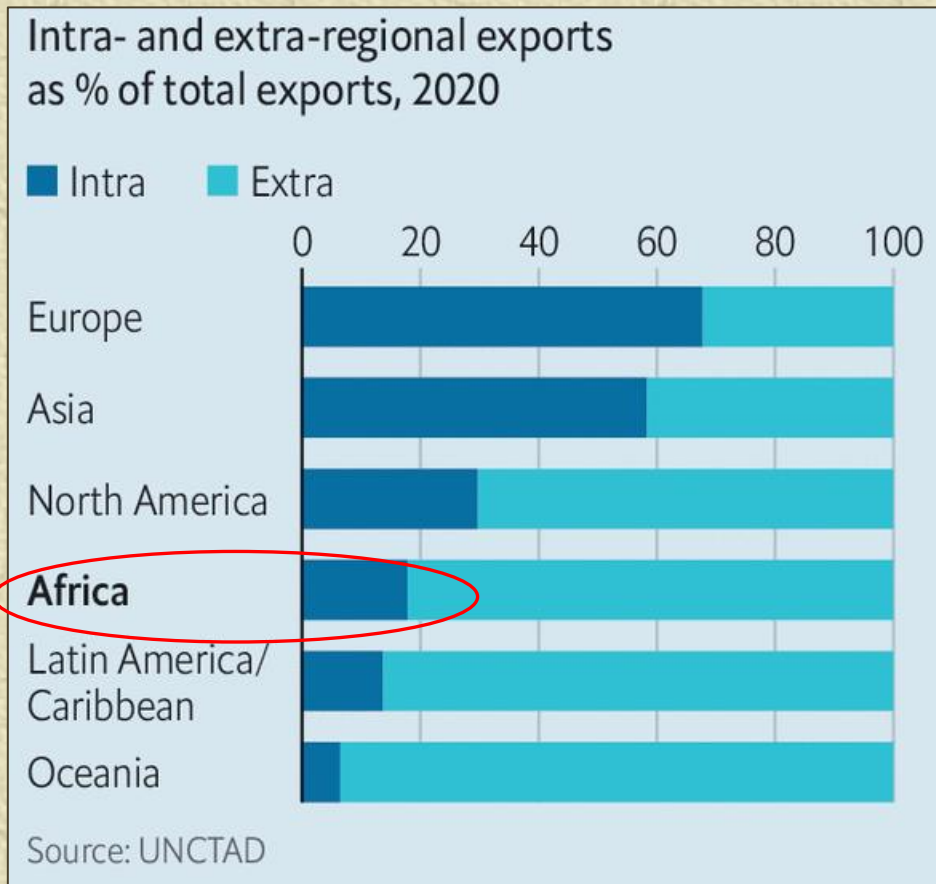
Economist, “World trade: The new order of trade”, Special report on the world economy, 9 Oct, 2021. WTO Secretariat

Stages of Liberalization & Integration, continued . . .

- ◆ Assessing RTAs – indicators in the literature
 - ↓ no. and degree trade barriers (tariffs, export subsidies)
 - ↑ trade: trade impact – intra- vs extra-group trade
 - Alignment of technical and regulatory measures
 - Stock mkt valuations correlated with trade deal announcement
 - How do politics affect the final deal? Existing deals?

Stages of Liberalization & Integration, continued . . .

◆ Measure of intra-RTA trade, % of total trade, 2020



African continental FTA

Problems in integrating:

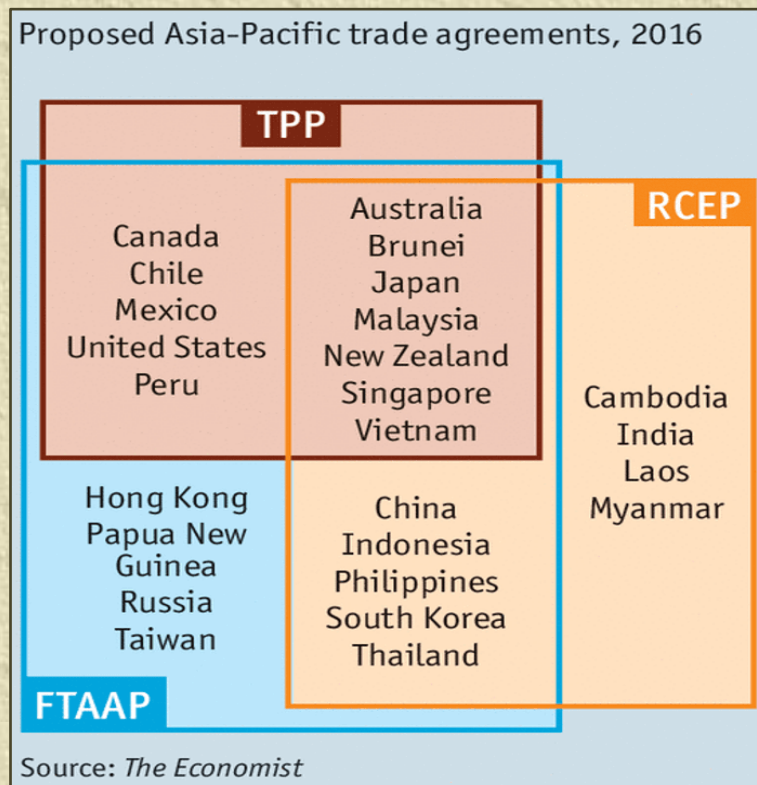
- Poor infrastructure (rail is limited; low road density for road transport)
- High cost of logistics (no set back-haul)
- Lack of transport cost info (no transport spot mkts; must sign L-T contracts)
- Rules of origin is current stumbling block

Source: *Economist*, “African economies: Trade flaws”, 26 Mar 2022, p. 29-30.

Stages of Liberalization & Integration, continued . . .

♦ Asia: overlapping agreements

- TPP dead but CPTPP continues (without US and China)
- Comprehensive deal unlike other Asia trade deals
- CPTPP: watered down many US demands; low intra-bloc trade



Economist, “The collapse of the TPP: Trading down”, 19 Nov 2016, p. 44-5.



Economist, “Free trade in Asia: Trump could not kill it”, 11 Mar 2023, p. 39-40.

4. Creating the EU

Motivate

4.1 Background: GATT, Marshall Plan, Treaty of Paris

✦ Why did Europe choose regional integration over multilateralism?

- ◆ GATT
- ◆ Marshall Plan
- ◆ Coal and Steel Community Treaty (Treaty of Paris)

Creating the EU, continued . . .

4.2 Phases of integration: treaties bringing Europe closer

Treaties	Date	Members	Main points: deepening+widening
Phase 1 CU, product mkt integration thru sectoral integration + legal developments			
Treaty of Paris	1952	EC-6: Be-Ne-Lux, IT, GE, FR	<i>Limited pooling</i> on coal + steel
Treaty of Rome	1958		Common external tariff + trade policy; mkt in goods, CAP; <i>↑ supra-nationality</i>
Atomic energy	1958		Common nuclear energy policy
Enlargement: 1973, 1981, 1986			UK, DK, Ire; GR; SP, Port
Phase 2 1980s: EC political/economic environment (supra-nat'al institution-building)			
Single European	1987	EC-12	Remove the <i>last internal barriers</i>
Enlargement: 1995; T. of Schengen			AU, FIN, SWE; Immigrate/border policy
Phase 3 1990s: Treaties that widen, deepen and complete the EU integration process			
T. of Maastricht	1992	EU-15	European + monetary union
T. of Amsterdam	1999		EU parliament, rights, employment
Treaty of Nice	2003		Commission + voting; common defense
Enlargement: 2004; 2007; 2013; Brexit			10 C. + E. European; Bul, Rom; Cro

Creating the EU, continued . . .

4.3 EC's approach

✦ Two guiding principles

- ◆ Create a customs union
- ◆ Pursue product market integration

✦ Mechanisms

- ◆ Integration through trade liberalization
- ◆ Legal development: “free movement of goods”
- ◆ Harmonization through approximation on regs

4.4 Degree of integration by EU

✦ Liberalization and approximation

✦ Successes and failures

✦ Acquis Communautaire - harmonization

Creating the EU, continued . . .

4.5 Economic freedoms of the EU

	TIG	L movement	K movement	TIS
Coverage of the freedom	<p>Products with commercial value & electricity/ natural gas: Remove trade barriers; harmonize domestic regs; CET, quantitative restrictions and measures with equivalent effect; rules on state monopolies; exceptions on justified grounds</p>	<p>Free movement of workers: right to move to different member state; non-discrimination regarding employment, remuneration and work conditions; excludes public sector</p>	<p>Financial investments, capital transfers; right of establishment of a foreign firm (FDI)</p>	<p>The residual freedom not provided elsewhere; Self-employed persons who move between member states</p>

5. Trade Liberalization under the Multilateral System

5.1 Multilateral liberalization: from GATT to WTO

✦ What was the GATT?

- ◆ Accomplishments and limitations
- ◆ Trade negotiation rounds
- ◆ Uruguay Round

✦ What is the WTO?

- ◆ Multilateral organization
- ◆ Gov't-to-gov't
- ◆ Body dealing with trade rules
- ◆ Forum for holding trade negotiations
- ◆ Settle trade disputes

Liberalization under multilateral system, continued

Round	Period/ parties	Coverage	Outcome
Geneva	1947 / 23	Tariff cuts item-by-item	26% cuts; 15000 concessions
Annecey	1949 / 33	Tariff cuts item-by-item	3% cuts; concessions on 5 000 lines; 9 accessions
Torquay	1950 /34	Tariff cuts item-by-item	4%; 8 700 concessions; 4 accessions
Geneva	1956 / 22	Tariff cuts item-by-item	3%; cut on existing commitment
Dillon Round	1960-61 / 45	Rebalancing due to the creation of the EEC	4%; 4 400 concessions
Kennedy Round	1963-67/ 48	Formula for tariff cuts; AD & customs valuation	35% avg cuts; 33 000 lines bound; agree on NTBs
Tokyo Round	1973-79 / 99	Tariff cuts and broad NTB negotiations	33% cuts that led to 6% ceiling on OECD manufactures imports; agreement across NTBs
Uruguay Round	1986-94 / 103 begin 117 end	Formula cuts and item-by-item cuts; NTBs, ag, services IP, disputes	33% cuts; ag, textiles, services subject to rules; rules apply to all members

Liberalization under multilateral system, continued

5.2 Structure of the WTO	Goods	Services	Intellectual property	Trade disputes
Basic Principles	GATT	GATS	TRIPS	Dispute settlement
Additional details	Agreements and Annexes			How does the WTO address TIG, TIS, and international mobility of L and K?
Specific sectors or issues	Agriculture Textiles Investment SPS + TBT	Air transport Telecom Financial Tourist		
Market access commitments	Schedule of Commitments			
Country-specific requirements	Listing of tariffs, quotas and subsidy levels	Listing of limitations on market access national treat		

6. Concluding comments: Module 1

- ✦ Globalization affected by whether multilateral process survives and large players to avoid unilateral processes
- ✦ Economic integration and trade liberalization have very different economic, political, and legal objectives
- ✦ Difficult to separate the two processes
 - ◆ Trade liberalization → greater economic integration
 - ◆ Greater economic integration → more trade liberalization
- ✦ Either process requires addressing political convergence
 - ◆ Whether approximation of reg is superior to harmonization requires a case-by-case and country-by-country analysis
 - ◆ TIG eventually affects services and TIS affects L,K-mobility