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Introduction

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Since the 1990s, the number of bilateral or regional free trade agreements (FTAs) that have been signed, or are under negotiation or feasibility study, has increased dramatically. In the Asia Pacific region, for instance, along with countries like the United States, Canada, Mexico and Chile that have included FTAs as one of the options in pursuing their trade policy objectives by early 1990s, countries like Japan, Korea, China, Australia and New Zealand, which traditionally gave policy priority to multilateral liberalization, have started to promote their own FTAs in recent years. In addition, original members of the Association of Southeast Asian Nations (ASEAN), particularly Singapore and Thailand, now see the formation of FTAs with extra-regional countries as an important and tangible policy option, though they used to prioritize the ASEAN Free Trade Area (AFTA) as their most important trade liberalization framework. Considering these trends, there may emerge an intricate "web" of FTAs in the region by the end of this decade.

In neoclassical economic theory, it has been argued that global free trade would maximize economic benefits and minimize costs both in individual countries and globally at the same time. If all countries are to maximize economic welfare by acting according to the theory, they would reduce their tariffs and other trade barriers unilaterally, if these existed in the first place, on a most favored nation (MFN) basis. There would be no need for multilateral liberalization processes or the formation of FTAs. However in reality, completely free trade has never been realized even at the level of an individual country because policy decisions are made not only to pursue pure economic welfare of the country as a whole, but also to achieve other objectives according to domestic political and strategic preferences.

Under these circumstances, the General Agreement on Tariffs and Trade (GATT) system after the World War II has been working relatively well towards the purpose of achieving “freer” trade in “wider” area of the globe. At the same time, the GATT and its successor, the World Trade Organization (WTO), allowed regional and bilateral trade arrangements including FTAs to be formed with some conditions under its Article XXIV, the General Agreement on Trade in Services’ Article V and such other provisions as an “exception” to its basic principles of multilateralism and non-discrimination.

Promoters of FTAs often argue that trade liberalization is like riding a bicycle: it will fall over if you stop pedalling. Thus, maintaining liberalization momentum through FTAs is better than nothing. Also, virtually all countries that are moving towards FTAs assert that their FTAs are consistent with the GATT/WTO rules and would not hinder the multilateral liberalization process under the WTO. Moreover, they often claim that FTA formation will play an important role in promoting or complementing multilateral liberalization. They argue that FTAs can make trade liberalization easier as they allow countries to open their markets to a few countries before opening their markets multilaterally through WTO negotiations and exposing them to the full force of international competition. These arguments indicate that the superiority of the philosophy and principles of the WTO—maximizing global and individual economic welfare at the same time by the optimal resource allocation through multilateral and non-discriminatory trade liberalization—to bilateral and regional agreements is still preserved, though the WTO has lost its role as the sole platform of reciprocal trade liberalization.

FTAs eliminate trade barriers between the contracting countries. However, there is no assurance that an intricate web of FTAs necessarily promotes smooth economic transactions among the countries inside, because FTAs are discriminatory in nature and the web would complicate tariff rates and rules applied to the same products. In recent FTAs, the web also complicates rules on new areas such as trade in services, investment, competition policy, government procurement and migration. The creation of “hubs and spokes”¹ would not resolve the problem as trade barriers will remain between spokes and the extent of each spoke’s access to the hub market is likely to vary (Findlay and Pangestu 2001: 13). These costs arising from FTAs through discrimination and complication would have to be borne by private trading firms, not the governments.²

In addition, it is not at all assured that countries will aim for multilateral liberalization after forming FTAs. There are arguments that FTAs do impede multilateral liberalization. For instance, Panagariya (1999: 29–30) indicated that, for various reasons, there is considerable empirical evidence that

countries increase outside (MFN) tariffs following the implementation of FTAs. Snape (1996: 61) pointed out that the "hub-and-spoke" system could resist multilateral liberalization. He argued that "[a]s each spoke country has 'bought' discrimination in its favour from the hub country, each could object to the hub country then lowering its barriers against the rest of the world, particularly if these were to erode the protection of the special deals for sensitive products." More generally, Findlay (2002: 20) argues that FTAs inevitably produce vested interests. If the only options are protectionism and free trade, it is rational for export interests to choose the latter. However, if an FTA was formed and exporters benefited from it because of its trade diversion effect, they would not seek further liberalization that might force them to give their vested interests up: rather, they would become opponents of multilateral liberalization. This argument is similar to that which observes that vested interests produced by protectionism oppose any kind of liberalization. In any case, the logic behind why the formation of FTAs and the eventual emergence of a web of FTAs should promote multilateral liberalization remains ambiguous and conditional. Thus, the recently articulated concept of "competition in liberalization" or "competitive liberalization" that presupposes FTAs would stimulate multilateral liberalization always has the risk of becoming "competitive enclosure," which may divide the world economy into parts.

Whether multilateral liberalization and FTAs and their web could be practically consistent with each other is a very important question for countries that depend for their economic development and stability on the international flow of goods, services, capital and information. To be consistent with the global free trade that the WTO is ultimately pursuing, FTAs are required to become "multilateralized" eventually. In other words, and in logic, FTAs ultimately need to increase the number of their contracting parties to cover the globe and/or apply their contents to non-members.

Do FTAs naturally aim to nullify their own existence? It seems not, since each country that participates in FTAs attempts to achieve political and strategic objectives, as well as pure economic gains from their respective FTAs. Thus, for FTAs to promote and complement the multilateral liberalization process, it seems that some forms of artificial "mechanisms" (or rules, institutions) to "multilateralize" FTAs need to be developed. And for these mechanisms to be actually employed, what is ultimately important is to attract support from the individual countries that have established FTAs. If these mechanisms could attract enough support from FTA parties to form a "critical mass" in multilateral negotiation

platforms such as the WTO, they may well have a chance to be realized. To examine whether individual FTA countries could support such mechanisms, it is essential to identify objectives (or factors, incentives) that drive them towards FTAs even though they are aware that the move may not necessarily be consistent with the WTO philosophy and principles. It is also important to study whether individual countries consider that FTAs are the best option available to achieve their objectives, in other words, whether they have policy alternatives to FTAs to achieve same objectives.

These are the underlying questions of this book. For the purpose of laying a further foundation for the following chapters, this chapter will pursue three tasks. First, by briefly reviewing the post-war development of bilateral/regional trade agreements, it will point out the characteristics of recent FTAs. Second, the general objectives of FTA formation, which have been indicated in theories and experiences, will be reviewed. Third, the mechanisms to multilateralize FTAs will be discussed. It will try to present several mechanisms categorized in two types and three levels. It will be argued that all mechanisms are interrelated and, again, what is most important for them is to attract support from individual countries. In the last section, the overall aims and the structure of the book will be introduced.

The Characteristics of Recent FTAs

Looking back at the development of bilateral and regional trade deals since the end of the World War II, there have been three recognizable waves (see also Chapter 4).³ The first wave started in the 1950s with the initiative in Western Europe. The creation of the European Coal and Steel Community (ECSC), then the European Economic Community (EEC), were aimed at economic integration to form a single market. Moreover, by integrating economies first, these Western European initiatives had a plan for the future political integration of the region. Subsequently, regional agreements by developing economies mainly in Latin America and Africa followed the European lead. Many of the deals took the form of customs unions (CUs). Though the number of agreements in the first wave trade deals was relatively small, these initiatives were notable as the first experiments to see whether super-national authorities would work in international relations. However, as it became clear by early 1970s that the case in Western Europe is the only success, the first wave eventually ended.

The second wave emerged in the latter half of 1980s. Again, Western Europe led the way with the Single European Act of 1986 to a higher level of integration and the formation of the European Union (EU) in 1992. When the Uruguay Round of trade negotiations stalled, the United States opted for establishing a bilateral FTA with Canada and the US-Canada FTA came into force in 1989. Faced with these moves by economic and political powers, developing countries followed suit mainly by using the Enabling Clause of the GATT.⁴ For instance, the process of realizing AFTA started in 1992. To bridge these initiatives across the Pacific, Asia-Pacific Economic Cooperation (APEC) was established in 1989 and initiated regional trade and investment liberalization and facilitation in mid 1990s, though it was not to become an FTA.

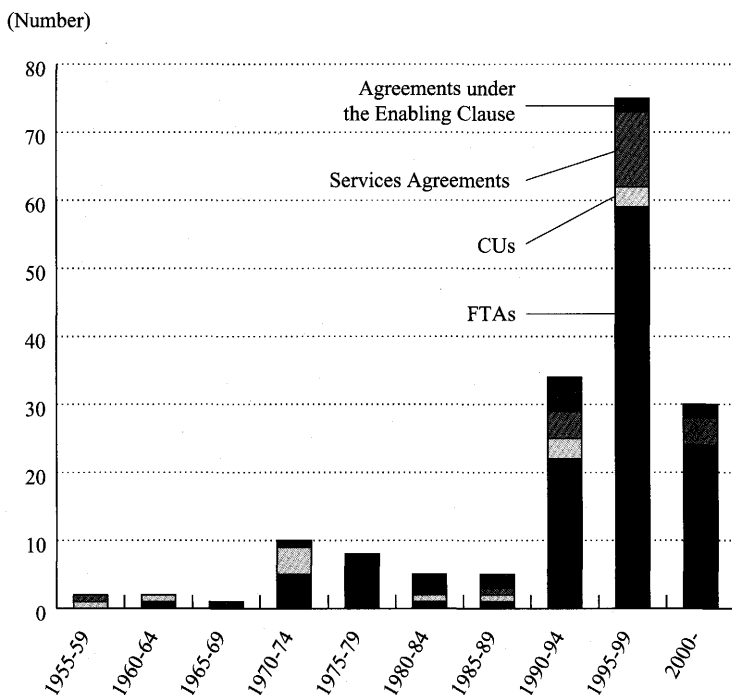
The third wave is the recent surge of bilateral and regional trade agreements that originated in early 1990s, overlapping with the second wave. The first characteristic of the third wave is the unprecedented pace of proliferation of FTAs. FIGURE 1-1 shows the number of regional trade agreements (RTAs)⁵ notified to the GATT/WTO since 1955 by five year period in which they came into effect. Since early 1990s, 139 RTAs have come into effect. That number comprises 80 per cent of the total number of RTAs. In just over seven years between 1995 and 2002, almost a half of all RTAs (83) came into force and, of course, this number does not include the most recent FTAs such as the Japan-Singapore, the Singapore-Australia and the Korea-Chile, nor initiatives like the proposed FTAs between ASEAN-China, ASEAN-Japan, Japan-Mexico, Australia-Thailand and Australia-the United States, which are still under study or negotiations. It seems that countries are driving towards RTAs in order "not to be left behind," among other reasons. Another phenomenon that can be observed in FIGURE 1-1 is the significant increase of FTAs compared with other forms of RTAs. Until the 1980s, the number of CUs and FTAs were, more or less, the same. By the end of the 1990s, however, the majority of all RTAs were FTAs. These trends may indicate that economic integration through CUs has been gradually abandoned with the exception of the EU. On the other hand, it can be seen that the functions of FTAs have become attractive to countries for their trade strategies.

Second, active utilization of the functions of FTAs saw the emergence of FTAs that go beyond the traditional concept of a region defined by geographical proximity. These include the Japan-Singapore (2002), Japan-Mexico (under negotiation), EU-Mexico (2000), Jordan-US (2001), New Zealand-Singapore (2001), Singapore-US (agreed on core elements in November 2002) and many others. In most of these cases, it seems that

political and strategic functions, on top of economic benefits, are working as important objectives of FTAs.

Third, while some FTAs go beyond the concept of geographical region, there emerged some initiatives that would expand the traditional concept of a “regional community” with a shared history and culture as well as proximity in geography. These initiatives include the Free Trade Area of the Americas (FTAA), the eastward expansion of the EU and the ASEAN+3 (ASEAN members plus China, Japan and Korea). These initiatives look to pursue the

FIGURE 1-1
RTAs COMING INTO EFFECT
(AS OF JUNE 30, 2002)



Source: Made by author using a WTO material. (http://www.wto.org/english/tratop_e/region_e.htm). Downloaded on October 4, 2002.

- Notes: 1. Numbers include new entries into existing RTAs (e.g. EC/EU).
2. Two RTAs (the Economic Cooperation Organization and the Gulf Cooperation Council) with unspecified years of effectiveness are counted in the period when they were reported to the GATT.

creation of new and expanded regional communities of the “Americas,” “Europe” and “East Asia” respectively. The end of the Cold War in early 1990s must have made it easier for countries to consider these expansions, while the globalization of economies during the 1990s seems to have made the expansion necessary.

Fourth, the third wave FTAs tend to cover areas and elements beyond traditional FTAs. Most traditional FTAs, as a main tool for regional (economic) integration until the 1970s, covered only the liberalization of trade in goods, thus concentrating on reducing/eliminating tariffs and quantitative controls between the contracting parties. However, most of the recent FTAs cover broader areas and elements like trade in services, factor mobility, investment rules, intellectual property rights, government procurement and other trade facilitation measures such as mutual recognition of product standards and harmonization of customs and quarantine procedures. Some FTAs also include the abolition of antidumping, countervailing duties and emergency protection measures such as safeguards between countries (World Bank 2000: 80). Moreover, there emerged FTAs that include areas not directly related to trade. For instance, the North American Free Trade Agreement (NAFTA) includes rules on labor standards and environmental protection in its supplementary accords (see Chapter 5), and the EU-Mexico agreement even contains a clause on the development of democracy (see Chapter 6). All these areas and elements have not been fully dealt with at the WTO, and are often called “new age”, “new generation” or “WTO plus” areas/elements.⁶

Objectives of FTAs: General Explanations

Why have so many countries opted for forming FTAs in recent years? What do they expect to gain from these FTAs? Can the objectives be achieved only through FTAs?

In economic terms, a basic objective, naturally, must be to secure mutual preferential access to partners’ markets.⁷ By doing that, FTA parties can enlarge the market for their products, thus increasing their exports to partners. The increase of production and exports creates better utilization of economies of scale. Moreover, a larger market and increased number of producers will, more likely than not, induce increased competition. While consumers in FTA parties can enjoy reduced prices of products through more competition, the producers that have survived will gain competitiveness also in the international market outside the FTA because of reductions in inefficiencies. Furthermore, FTAs may assist in attracting foreign direct

investment (FDI), if they enlarge the market considerably. FTAs intended to attract FDI are numerous among those negotiated by developing countries, but developed countries may also have such objectives in some cases.

These economic gains expected from FTAs are indicated in most economics literature on FTAs.⁸ Broad coverage of WTO plus elements would enhance these gains, if introduced, since the new elements will promote a "deep" integration of the economies of the FTA parties. Deep integration minimizes the remaining trade restrictions other than tariffs and quantitative controls between the parties and substantially assures market enlargement and more intra-FTA competition.

Can these economic gains be achieved only through bilateral or regional trade agreements such as FTAs? Some multilateralists argue that, since the new round of trade negotiations at the WTO has already been launched, there is no need to pursue bilateral/regional trade agreements at least for the time being.⁹ If the objectives of FTAs were confined only to the economic gains mentioned above, their argument may well be valid since the effects of multilateral liberalization (or even unilateral liberalization) are supposed to deliver almost all of the economic gains expected from FTAs. However, for each FTA, there are political and strategic motives as well that sometimes may be more important than these economic gains.

In practice, there are several political objectives that have been pointed out (World Bank 2000: 12–25). First, FTAs can be used for the purpose of promoting national security. This security objective is based on a traditional functionalist concept that regular contacts between political leaders and government officials on economic issues will build mutual confidence, and a liberal observation that deep economic interdependence makes war materially impossible.¹⁰ The best example is the post-war development of regional community in Europe. It is a well-known fact that one of the main reasons for establishing the ECSC, the predecessor of the European Community (EC) and the EU, in 1951 was to create a community that would avert internal wars by collectivizing essential goods for economic activities. More recently, after the simultaneous multiple terrorist attacks on September 11, 2001, the United States looks to be intending to utilize FTAs with countries like Australia, Morocco and ASEAN members for the strategic purpose of strengthening political and economic ties to fight against terrorism (see Chapters 5 and 11).¹¹

Second, if small and/or middle-sized countries (such as Singapore, Thailand, Australia, New Zealand, Argentina and Brazil) could form FTAs, they may be able to strengthen their bargaining power against bigger countries (like the United States, the EU, Japan and China), or at multilateral

negotiation tables (such as the WTO and APEC). For small and/or middle-sized countries to strengthen their bargaining positions significantly, the simplest way may be to form an FTA with one of the political/economic powers. However, this option could be dangerous as the bigger partner may force them to accept its FTA preferences that are not necessarily shared. Small and/or middle-sized countries can still increase their bargaining power at international negotiations through coalition building among themselves. The results of activities by the Cairns Group illustrate the point. Even if they could not acquire substantial bargaining power by forming FTAs, they can at least expect a better chance of being noticed (World Bank 2000: 19). In fact, this "bargaining power" objective is not confined to small and/or middle-sized countries. For example, one of the reasons that Japan has started to seek FTAs in recent years is said to be "finding friends." As Japan had prioritized multilateral trade liberalization over bilateral agreements, its negotiators felt isolated in the multilateral negotiations and bilateral trade disputes (with the United States in particular). Negotiating FTAs was seen as a quick and effective answer to find supporters (see Chapter 8).

In addition, a political motive for covering WTO plus elements in FTAs, particularly those that aim at setting new rules on investment, intellectual property rights, labor standards, environmental issues, competition policy, finance and others, is closely linked with this "bargaining power" perspective. By setting new rules on these issues in FTAs, the parties involved could expect not only free trade and investment between them but also a better negotiating position at the WTO.¹² If the FTA parties are influential enough, they may be able to make their "local" rules into "global" rules through multilateral negotiations. To become influential enough, it seems, FTA parties need to include at least one economic power (the United States, the EU or Japan), which can set one of the main rules almost by themselves, and strategically mobilize others who would accept their rules at multilateral negotiations. All this process, however, depends on the condition that FTA parties could find a common stance and negotiate as a single entity.¹³

Third, countries undergoing the process of economic adjustment can use FTAs for the purpose of "locking in" their reform agenda. "Adjustment to reform typically involves investments, but these investments will not be made unless investors are confident that reform will persist. ... If the investments are not made, then government is likely to face increasing pressure to reverse the reforms. ... To escape from this trap governments often need institutions that enable them credibly to lock in to decisions." (World Bank 2000: 23). Since FTAs are international treaties that usually require domestic ratification procedures in contracting parties, they would

work as international commitment mechanisms for the reform of domestic economies. Domestic economic sectors that would benefit from, thus support, reform policies are expected to offset traditionally strong opposition from particular sectors. The case of Mexico joining NAFTA is a good example. The Mexican government started to reform its economy in mid 1980s, and NAFTA was seen both by the Mexican and US governments as a follow up step to lock in the reform policies (see Chapter 6). Even non-economic reform agenda such as democratization can be locked in through FTAs as the Mexico-EU FTA and Mercado Común del Sur (MERCOSUR) have demonstrated.

This “locking in objective,” however, can be achieved by making active commitments under multilateral systems (e.g. the WTO) and/or through unilateral liberalization. The reason that some countries prefer FTAs to multilateral/unilateral liberalization for this purpose seems to lie in their domestic politics. By choosing suitable partner(s), a country may expect to lock in the reform agenda in a “softer” way than multilateral or unilateral liberalization through controlling the extent of new competition. For instance, one of the Japanese government’s rationales for signing an FTA with Singapore was to advance its structural adjustment policies (see Chapter 8). Singapore was the most suitable country for Japan with which to establish its first FTA, because Singapore did not have agricultural, forestry and fisheries sectors of meaningful size. These sectors were, and still are, the strongest proponents of protectionism in Japan. Thus, it is not surprising that the Japanese government resolved that the political and economic consequences of multilateral or unilateral liberalization were too severe and, by negotiating an FTA with Singapore, it aimed at locking in the reform policies while protecting vested interests at the same time.¹⁴

Fourth, FTA formation can be used as an “insurance policy” to realize free trade at least bilaterally or regionally when multilateral trade liberalization is stalled or proceeds slowly (Findlay and Pangestu 2001). At the same time as assuring “partial” liberalization, economic powers can also put pressure on the participants of multilateral negotiations to liberalize faster and in line with their intentions, by showing their will to discriminate. In fact, the pressure would work not only during multilateral negotiations but also during the implementation and pre-negotiation period as the FTAA initiative showed in the latter half of the 1990s.

Fifth, FTAs may be employed for the purpose of “training” or “capacity building” before multilateral liberalization (Findlay and Pangestu 2001). It is likely that this “training” objective is sought mainly by developing countries. However, more developed countries with no or little experiences in FTA

formation (like Japan and Korea) may express the need to pursue this objective (see Chapter 8). The problem, of course, is that there is no assurance that countries concluded FTAs for this purpose would aim for multilateral liberalization as a next step.

In sum, since there are a number of economic and political objectives and combinations for FTA formation, every FTA and FTA party should be considered to have different policy objectives and motives. Also, it should be noted that political and strategic objectives are important factors that drive countries towards FTAs. Therefore, it can be seen that the trend of FTA formation will not die down just because the new round of trade negotiations has been launched.

No FTA is formed only for purely economic reasons: all FTAs have different mixes of political and strategic objectives as determined by the preferences of individual countries. Differences in the contents of every FTA arise from the different foreign policy strategies and domestic politics of the countries negotiating individual FTAs. For instance, the content of an FTA that country A signed with country B may well differ from the contents which A signed with country C, reflecting the foreign policy strategy of A based on its domestic political and economic circumstances. Moreover, the motives and policy objectives of each party in the same FTA can differ. In other words, what countries A and B attempt to achieve from the A-B FTA could differ, even though they are obliged to comply with the same articles of the same FTA.

Considering the Mechanisms for Multilateralizing FTAs

Diversity of motives and objectives and, in particular, the importance of political and strategic factors in FTA formation suggests that FTAs would not be automatically discarded in favor of the benefits of multilateralism. Thus, to assure that FTAs promote and/or complement multilateral trade liberalization, some kind of artificial mechanisms to multilateralize FTAs need to be developed and introduced. Snape, Adams and Morgan pointed out important elements to be included in FTAs if they were to complement and facilitate multilateral liberalization:

- (i) Full liberalisation of trade between the participants. Full internal liberalisation will make it easier to liberalise externally.
- (ii) Homogeneity of trade rules relating to determination of origin [rules of

origin, ROO], dispute settlement and similar issues. ... if the rules differ between members of a free trade union then the ability of that area to engage in external liberalisation is complicated greatly.

- (iii) Ability to negotiate [external barriers as an entity].
- (iv) Openness to new members on conditions similar to those faced by existing members.
- (v) Not raising external barriers on formation or subsequently, and readiness to negotiate external barrier reduction thereafter.

(Snape, Adams and Morgan 1993: 103–4)

Based on these points, this section will try to organize and develop the concept of such mechanisms further. The main purpose here is to illustrate the concepts referred to in the following case studies. Therefore, the mechanisms will be outlined without giving much attention to their practicability.

In logic, there are two types of mechanisms through which FTAs can be multilateralized. First, FTAs can be multilateralized in terms of their membership. Multilateralization of FTAs could be achieved by accepting new members into each FTA or by merging FTAs. These processes can happen at the same time until, theoretically, they cover the globe. Second, FTAs could be multilateralized by becoming less discriminatory to non-members, in other words, by gradually applying their contents to outsiders. In terms of tariffs, for example, if FTA parties could gradually reduce their external (MFN) rates unilaterally or in concert, thereby lessening levels of discrimination. On the other hand, the application of other FTA rules, such as ROO and investment rules, to non-members would require consensual decision and implementation between the parties.

Again in logic, the mechanisms can be considered at three levels: outside FTAs (international organizations that subsume FTAs and their parties); within FTAs themselves (building in the mechanisms in the FTA articles), and; within each FTA party's policies (unilateral or concerted initiatives through domestic political institutions). Setting the mechanisms at the first level implies strengthening the power of the international organizations that cover wide geographical areas (such as the WTO and APEC) to control FTAs more effectively.¹⁵ Also, measures to promote comprehensive and speedy multilateral liberalization through the WTO rounds can be seen as such a mechanism, as it would reduce the *raison d'être* of FTAs: reciprocal preferential treatment in trade, investment and other areas between the parties. A permanent international mechanism that picks up elements widely shared by individual FTAs and sends them to multilateral agenda may be

worth considering at this level. The mechanism is likely to be a new WTO institution and the elements are most likely to be picked up from the WTO plus areas of FTAs such as trade facilitation measures and rules on investment, finance and e-commerce.

The second level indicates preparing the mechanisms within FTA articles that will have, in the future, the effect of increasing the membership of an FTA and/or making an FTA less discriminatory. For instance, introduction of an "open membership" system, which assures easy accession of new members to an FTA provided that applicants agree to fulfill conditions required by the FTA, could be included as a mechanism to multilateralize FTAs. Institutionalizing the efforts to make contents of FTAs homogeneous may also be considered as such a mechanism. Though it does not directly lead to the expansion of membership, it would set a favorable environment for FTAs to merge at a later time.¹⁶ As mentioned earlier, the gradual reduction of MFN tariff rates and/or application of other FTA rules to non-members can be considered as means of making an FTA less discriminatory. The WTO plus rules, in particular, might be easier to be applied than traditional elements to non-members, as it would be better if those rules were applied in wider areas than just within an FTA, in terms of both reducing transaction costs and strengthening the negotiation position at the multilateral stages.

The third level involves the question of whether the domestic politics of individual FTA parties could support multilateral liberalization and/or the multilateralization of FTAs, and allow the mechanisms to be set at the first and second levels. If the domestic politics of some FTA parties allowed such mechanisms, then the way to align a coalition of those parties must be established at the international level. Otherwise, the parties with the intention of multilateralizing their FTAs would be disadvantaged by free riding. On the other hand, if the politics of individual parties do not allow such mechanisms, how the domestic policy making "institutions," in broad terms, can be adjusted to redirect the policy preferences of domestic constituencies should be studied. This may include the provision of incentives through various forms of side-payments. As a concrete measure to make FTAs less discriminatory at this level, Latin American interpretations of "open regionalism" are notable. Under the name of open regionalism, it is proposed to seek regional FTAs that are comprehensive in coverage and easier for new members to access, and at the same time, carry out trade liberalization on MFN basis (ECLAC 1994: 12).¹⁷ Chile, for instance, is unilaterally liberalizing its economy and actively pursuing FTAs concurrently (see Chapter 7).

According to the discussion so far, the mechanisms to multilateralize FTAs can be categorized as shown in TABLE 1-1.

TABLE 1-1
CATEGORIZING THE "MECHANISMS" FOR MULTILATERALIZING FTAS

| Types Levels | Increasing FTA Membership | Making FTAs Less-discriminatory |
|--------------------------------|---|---|
| Outside FTAs | (1) Strengthening the WTO's power to control FTAs (2) APEC FTA guidelines (3) Creation of an international environment that facilitates FTA multilateralization (4) Provision of international incentives (side-payments) to opposition ... | (1) - (4) (5) Comprehensive and fast WTO liberalization (6) Creation of a mechanism that picks up certain FTA contents (mostly "WTO plus" elements) and put into the multilateral agenda ... |
| Within FTAs | (7) Open membership (8) Making contents of FTAs identical with each other ... | (9) Gradual reduction of external (MFN) tariffs (10) Gradual application of other FTA contents to non-members ... |
| Within Policies of FTA Parties | (11) Initiatives to merge FTAs (12) Realignment/adjustment of policy making institutions to allow the mechanisms (13) Provision of domestic incentives to opposition ... | (12), (13) (14) Simultaneous use of FTAs and unilateral liberalization ("open regionalism" in Latin America) ... |

Source: Author.

It should be noted that, for the mechanisms to function, all levels need to be strongly connected as each mechanism is likely to be employed in combination with others, if that happens. For example, if the power of international organizations to control FTAs is to be strengthened to enable measures such as the rigorous application of the GATT Article XXIV and the introduction of "APEC FTA guidelines" that may include a regional multilateralization clause, support from most members is naturally and essentially required. The same support is needed to make the WTO round, or

the APEC liberalization process, comprehensive and speedy. If articles to allow easy accession to an FTA and/or make an FTA less discriminatory are to be built into the FTA itself, the international environment should be prepared to assure those FTA parties will be advantaged, or at least not disadvantaged. One of the best ways to do this is to encourage more and more parties to include articles of this kind in their own FTAs. To create these dynamics, the restructuring of domestic political institutions will be necessary. Focusing on individual FTA parties, realignment/adjustment of domestic policy institutions will have a significant impact on regional and/or global trends such as the prioritization of multilateral liberalization, the homogenization of the contents of FTAs, and allowing the occurrence of open membership systems and the merger of their FTAs.

In any case, what is ultimately important for the mechanism to be practicable is support from individual FTA parties and that such support must come from as many countries as possible, as this would contribute to a critical mass at the international stages.

The Aims and the Structure

Whether the recent surge of the "third wave" of FTAs promotes/complements multilateral liberalization remains ambiguous. The emergence of a web of FTAs in the near future would further complicate the problem. FTAs must gradually become less rewarding if they are not to hinder multilateral liberalization, but it seems that FTAs do not naturally aim for redundancy. Thus, the artificial mechanisms to multilateralize FTAs need to be developed. Such mechanisms, however, cannot be developed fully without analyzing domestic policy preferences of individual FTA parties from political economy perspectives as the practicality of the mechanisms ultimately depends upon each FTA party's will to support them.

The main aim of this book, therefore, is to examine the concrete objectives (factors, incentives) that countries aim to achieve through FTAs. The examination will be conducted from theoretical, institutional and empirical perspectives. It is only after these analyses that the second aim of the book can be discussed more meaningfully: how mechanisms to multilateralize FTAs could be developed and adopted.

Part I consists of three chapters that deal with theoretical and institutional perspectives. In Chapter 2, Yamamoto reviews the international economics literature on the relationship between FTA formation and multilateral liberalization. He draws on theoretical writing on incentives to form FTAs to

argue that, without “counterfactual” assumptions or conditions, FTA parties may not aim to multilateralize their FTAs if they act rationally. Thus, he argues, it is important to re-investigate the political feasibility of the counterfactual assumptions of international economics to realize FTA multilateralization.

In Chapter 3, Yanai looks into the institutional background of FTA proliferation. She examines the historical development of the international trade systems in detail, focusing on the modification of the concepts and functions of “MFN treatment” and “reciprocity.” She points out that, as the GATT’s “package approach” to multilateral liberalization with “diffuse” reciprocity is facing problems (remember how long it took to conclude the Uruguay Round and recall how the Doha Round is proceeding), individual countries have started to seek other means to ensure reciprocal liberalization. Therefore, an institutional factor in the recent surge of FTAs, she argues, is the lessening of the GATT/WTO’s function to assure even diffuse reciprocity in trade negotiations without delay.

In Chapter 4, by examining international political economy (IPE) literature on FTAs, Oyane attempts to provide viewpoints to understand the causes of FTA proliferation. First, he extracts two main characteristics of the “third wave” FTAs: competitive formation and diversity in declared purposes. Next, Oyane tries to explain these characteristics and test the practicability of FTA multilateralization by reference to three theories of IPE: neorealism, neoliberalism and constructivism. He observes that all these theories can explain parts of the characteristics of the third wave FTAs—in other words the causes of their proliferation—but not fully. Nevertheless, he points out that the constructivist concept of the “permeation of ideas,” in particular policy “bandwagoning,” is a promising paradigm.

Part II deals with the empirical perspectives by conducting case studies on individual countries’ FTA policies. The case studies of eight countries (the United States, Mexico, Chile, Japan, Thailand, Malaysia, Australia and New Zealand) are to illustrate answers to the questions of: why and how do they pursue FTAs, what kind of contents of FTAs do they aim for, and with which partner(s)? To do so, it is important to review the historical development of each country’s trade policy to ascertain the factors that contributed to the policy change, or the factors why its trade policy remained stable. Through answering the above questions, each case study will examine, explicitly or implicitly, what its experiences on FTA policy and policy making suggest to the theoretical and institutional explanations and viewpoints in Part I, and the practicability of FTA multilateralization mechanisms.

In Chapter 5, Yamada examines the FTA policy of the most influential country in shaping the direction of multilateral trade regimes: the United States. He concentrates on two substantial US initiatives, NAFTA and the FTAA, to analyze the objectives of US FTA policy. In these initiatives, the US administration sought and is seeking a number of objectives, considering its FTA policy as complementary, not an alternative, to multilateral liberalization. What is unique, in the strategy of the hegemon, is its "linear" way of thinking. The US administration believes that its FTAs will contribute to multilateralism because the contents of its FTAs should naturally and gradually be adopted in wider geographical areas: bilateral to regional and, ultimately global. Yamada points out that the US "regionalism" in this form is not without opposition both from domestic constituencies and potential FTA partners in the region.

Rosas deals with the Mexico's FTA policy in Chapter 6. She points out that Mexico's trade policy experienced dramatic changes as part of comprehensive economic reforms since the 1980s. The conclusion of NAFTA was a final step towards the completion of the reform. As a result of NAFTA, she argues, Mexico's economy, which was already dependent before the reform, has become even more dependent on the US economy. Though the Mexican government recognizes the importance of the WTO, it complies as long as the WTO and its liberalization process do not conflict with the US policy and NAFTA. Rosas also points out that trade liberalization including FTAs has had the effect of destroying local production chains. Thus, she insists the need for incorporating appropriate industrial policy into ongoing trade policy.

Kuwayama examines the Chilean FTAs in Chapter 7. Over the last decade, Chile has been one of the countries that most actively pursued FTAs and, as a goal, the government has set to conclude FTAs with trade partners that would cover 90 per cent of its total trade by 2010. However, Kuwayama points out, it is important to note that Chile has not only been pursuing FTAs but also unilateral and multilateral liberalization at the same time. He emphasizes that the NAFTA-like comprehensiveness both in terms of "width" and "depth" that Chile seeks in its FTAs, along with its unilateral moves towards liberalization, would minimize potential trade diverting effects. This Chilean concept of "open regionalism," he argues, will be a stepping stone towards multilateral liberalization.

In Chapter 8, Ogita analyzes Japan's trade policy change from multilateralism as the first priority to the promotion of bilateral FTAs. After reviewing the recent development of Japan's trade policy, he goes on to examine why and how the policy change was made. Ogita indicates that the

officially announced general aims of Japan's FTAs may not be very important. Instead, he points out, a series of events in the latter half of the 1990s (prolonged recession of Japan's economy, decline of East Asian countries' confidence in the management of their economies after the financial/economic crisis in 1997, the passive involvement of the United States in the reconstruction of East Asian economies and the growing hopes of East Asian countries for a greater regional role for Japan) have set a favorable environment for Japan to redirect its relative economic and diplomatic focus from the United States to East Asia. FTAs are not exceptions. Rather, Japan's "Asian orientation" is manifested in its FTA initiatives.

Nagai, in Chapter 9, focuses on why Thailand, which was enthusiastic about realizing AFTA, has come to seek bilateral FTAs with extra-regional partners. As regional liberalization under AFTA did not proceed as quickly as it hoped, Thailand started to pursue bilateral FTAs under its previous government in late 1990s. The change of government in 2001 to the Thaksin administration saw the acceleration of FTA initiatives. Nagai examines the continuity and change of FTA policy between the two governments and points out that Thaksin's initiatives are more aggressive in seeking better market access to major trade partners such as China, Japan and the United States. Thaksin insists that his FTA policy and domestic economic policy will have synergistic effects, but, Nagai argues, it remains to be seen. Nagai also notes that the current FTA initiatives of the government may lack an accurate understanding of WTO rules.

In Chapter 10, Suzuki emphasizes the importance of understanding the linkage between FTA policy and ASEAN diplomacy in the Malaysian case. Malaysia has been a supporter of AFTA, yet, as the deadline for the final stage of the AFTA tariff reduction approached, the government requested a delay. Meanwhile, when Singapore and Thailand started to seek bilateral FTAs with extra-regional partners, Malaysia strongly criticized them, arguing that their policies would harm AFTA. These attitudes which appear contradictory should be understood with the context of how Malaysia views ASEAN and its regional cooperation schemes. Suzuki argues that Malaysia sees that its FTAs need to be flexible like AFTA and, to assure their flexibility, they need to be "ASEAN based." She also points out that the East Asia Economic Group proposal by Prime Minister Mahathir in early 1990s still has strong influence on Malaysia's current policy in terms of its concept of the region.

In Chapter 11, Okamoto explains initially passive but later responsive nature of Australia's FTA policy. Contrary to previous governments' policies

of giving top priority to the multilateral liberalization process, the new government declared that it was ready for promoting bilateral FTAs in 1997. Nevertheless, it took more than three years to start a concrete FTA negotiation with Singapore. Okamoto points out that this "time lag" was caused by two hopes the government had: one for multilateral liberalization through APEC and the WTO and the other for the establishment of a regional FTA with ASEAN. As these hopes diminished over time, and other countries were rapidly proposing FTAs with its major trading partners, Australia finally moved towards concluding its own FTAs to prevent disadvantages that its firms would face otherwise. However, Okamoto argues that, after the completion of its FTA with Singapore, Australia now looks set to pursue the "competitive liberalization" concept through its FTAs.

Hoadley examines in Chapter 12 why and how New Zealand seeks bilateral FTAs by closely examining a concrete example of negotiations with Singapore. New Zealand has set its trade policy on four tracks in early 1990s: unilateral, multilateral, regional and bilateral. Already being one of the world's most liberalized economies and seeing multilateral (WTO) and regional (APEC) liberalization stagnate in late 1990s, New Zealand opted for bilateral FTAs to deliver what it wanted most: better access by its agricultural products to major markets. An FTA with Singapore would not satisfy New Zealand's immediate need but, Hoadley argues, it had the strategic motive of encouraging global liberalization. He also suggests that how the New Zealand government demonstrated leadership and handled domestic opposition may be an example of success.

Part III concludes the volume. Following the examination of theoretical and institutional incentives (objectives, factors) for FTA formation and proliferation in Part I, and concrete case studies on why, how, in relation to what contents, and with whom these particular countries pursue FTAs in Part II, Chapter 13 performs two tasks. First, the findings of case studies will be summarized and organized in comparison with theoretical and institutional perspectives of Part I. In doing this work, an attempt will be made to consider how best the recent proliferation of FTAs can be understood from the viewpoints of the IPE framework provided in Chapter 4. Second, the mechanisms for FTA multilateralization will be discussed further. The result of the first task should indicate the relevance of the concept and some concrete measures of the mechanisms developed earlier in this chapter. It will also be important here to consider whether the objectives of FTA formation articulated by the case studies can be achieved only through FTAs. If there were other means, countries could avoid potential deficiencies of FTAs by pursuing them.

Notes

- 1 If country A had separate FTAs with multiple countries (B, C, D, ...), country A is called a "hub" and country B, C and others are the spokes.
- 2 Bhagwati (1995) called this the "spaghetti bowl" effect. Krueger (1997: 22) stated that "[i]t is difficult to imagine that a series of overlapping FTAs, with different ROOs attendant for different countries' access, the need for individual producers to know and keep records for a variety of ROO requirements, and the complications associated with negotiations for accession of additional members, will lead to the WTO-plus world."
- 3 Except for those inherited from the pre-war period such as the British Commonwealth Preference system.
- 4 Under the GATT decision in 1979, developing countries were accorded a "differential and more favorable treatment" (Enabling Clause). Under this Clause, bilateral and/or regional trade deals between developing countries do not have to fully agree with conditions set under the GATT Article XXIV and related rules.
- 5 The WTO uses the term "RTAs" to include all kinds of bilateral and regional trade deals: CUs, FTAs, services agreements and those deals under the Enabling Clause.
- 6 In addition, to liberalize traditionally protected sectors (on a MFN basis) through FTAs can also be considered as a WTO plus element. In any case, and as a matter of fact, all trade agreements in history have contained GATT (or WTO) plus elements because, otherwise, they would not have been preferential trade agreements worth signing. In this sense, the "WTO plus-ness" of the recent FTAs itself is not new.
- 7 Findlay and Pangestu (2001) point out that the economic (business) objectives are mixture of aggressive and defensive interests. Governments' and businesses' aggressive interests relate to capturing a share of profits available in protected foreign markets, and their defensive interests are reactions to other countries' attempts to establish preferential trade agreements that exclude them.
- 8 See Bhagwati, Krishna and Panagariya (1999), in which the major economics literature on preferential trade agreements is compiled. See also Panagariya (2000), which concisely overviews the development of theories on the topic.
- 9 Interview with Australian academics in Canberra and Sydney. December 6 and 11, 2001.
- 10 See, for instance, Haas (1958), Deutsch (1967) and Keohane and Nye (1977).
- 11 For the United States' overall security strategy including the utilization of FTAs, see President of the United States (2002). For the US initiative for FTAs with ASEAN countries, see White House (2002).
- 12 Rajan, Sen and Siregar (2001: 8) pointed out that "FTAs could act as testing ground for exploring complex trade issues and may help establish some sort of precedent for multilateral negotiations." However, they did not elaborate "how."
- 13 In the case of CUs, finding common stances on negotiated issues may be easier than FTAs as CUs adopt uniform external tariff rates. In addition, it is also likely than not that they employ common policies on trade in services, factor mobility, customs procedure and product standards.
- 14 The problem with this kind of attitude is that the FTA signed may not work as an effective commitment mechanism, since foreign investors other than those in the FTA partner(s) may not have confidence in the government's intentions. In Japan's

- case, for instance, investors in the United States or the EU might not believe that the Japanese government had "locked in" reform policies, even though the FTA with Singapore was signed. Furthermore, the World Bank (2000: 25, 66) argues that, for the policy lock in objective to work, it needs to be supported by credible and effective sanctions from partner(s). If the perceived cost of breaking FTA commitments were low, there would always be an incentive to do so. In this regard, too, Japan's FTA with Singapore may be seen as a weak commitment to lock in reform policies, compared with other potential FTA with, say, the United States.
- 15 GATT Article XXIV already imposes certain conditions on any FTAs to be signed by developed economies. In reality, however, FTA parties can interpret those conditions relatively freely and, as a result, FTAs with a wide variety of contents have emerged. Moreover, since it failed to judge the first case of the EEC as inconsistent with the GATT principle (World Bank 2000: 109–10), the GATT/WTO system has lost the ability to determine which FTA is WTO consistent and which is not.
 - 16 Attempts to have identical FTAs could be made on a voluntary basis. If countries perceived a certain FTA as very successful, they may imitate it for their own FTAs as a model. This "demonstration effect" could homogenize the contents of multiple FTAs. A problem is that what will be perceived as success may differ from country to country. Some countries may find a comprehensive FTA to be a success while others may see effective protection of certain sensitive sectors as a success. To lead subsequent FTAs towards the direction of multilateralization, the "model" FTA needs to have a high level of WTO consistency.
 - 17 The concept of "open regionalism" in the APEC context differs from the Latin American interpretation. In the APEC context, and in its purest form, open regionalism is a regional (liberalization) initiative that will be automatically applied not only to members but also to non-members on an MFN basis. In other words, APEC liberalization under its open regionalism is already a unilateral (but concerted) action.

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