



**S. RAJARATNAM SCHOOL
OF INTERNATIONAL STUDIES**
A Graduate School of Nanyang Technological University

RSIS COMMENTARIES

RSIS Commentaries are intended to provide timely and, where appropriate, policy relevant background and analysis of contemporary developments. The views of the authors are their own and do not represent the official position of the S.Rajaratnam School of International Studies, NTU. These commentaries may be reproduced electronically or in print with prior permission from RSIS. Due recognition must be given to the author or authors and RSIS. Please email: RSISPublication@ntu.edu.sg or call (+65) 6790 6982 to speak to the Editor RSIS Commentaries, Yang Razali Kassim.

No. 171/2010 dated 15 December 2010

Time for Rethink: Need to Refocus on WTO

By Barry Desker

Synopsis

The sluggishness of the World Trade Organisation in recent years has led to the proliferation of free trade agreements (FTA). The resulting neglect of WTO negotiations is not in the interest of the global multilateral trading system.

Commentary

IT HAS become fashionable to speak of the failure, even demise, of the World Trade Organisation (WTO). Such a view has been fuelled primarily by the proliferation of free trade agreements (FTAs) since the late 1990s, particularly the bilateral and regional agreements in East Asia. This in itself represents a dramatic shift in the policy preferences of East Asian governments. Until 2000, East Asia was focused on strengthening multilateral institutions such as the WTO.

While the current trend towards bilateralism and regionalism can be explained in terms of being a response to the WTO's recent difficulties, it does not explain the shift in policy preferences. Indeed, given that the East Asian economies are largely open economies and reliant on international trade, the fact they have been pushing for FTAs is counter-intuitive.

Two Camps on FTAs

The open, export-oriented economies of East Asia should have an interest in maintaining and strengthening the multilateral trading system as embodied in the WTO. Furthermore, while the WTO facilitates trade creation, thereby stimulating investment, technology transfer and growth, FTAs are frequently criticised for causing trade diversion, undermining the uniformity of global rules and resulting in a net welfare loss. Jagdish Bhagwati, a leading critic of FTAs, argues that they lead to a "spaghetti bowl" or "noodle bowl" problem...characterised by a chaotic criss-crossing of preferences, with a plethora of different trade barriers applying to products depending on which countries they originate from.'

This debate draws our attention to the two deeply-opposed camps on the issue of FTAs. Those favouring FTAs argue that the name of the game is trade liberalisation, regardless of whether it takes place at the multilateral, regional or bilateral level. Trade liberalisation would have extra-trade impacts such as technology transfer, domestic economic reforms, and growth stimulus effects. Those against FTAs stress that they are basically a distortive mechanism, and thus constitute a 'second best' outcome compared to WTO-led multilateral free trade outcome. FTAs would also create further distortions such as rent-seeking behaviour and the misallocation of

resources. The key distinction between these two camps is the distinction between the 'preferable' and the 'possible'.

FTA negotiations have not been problem-free. The point, however, is that compared to multilateral trade talks, FTAs are easier to manage and can be concluded within a much shorter time frame. Furthermore, the WTO has been overloaded with issues of domestic governance, and tainted by perceptions that double-standards are practised by powerful members when it comes to the compliance with WTO rules, while the practice of rushed and non-inclusive negotiation sessions contributed to the highly protracted process of negotiation, as well as adding to the risk that talks will fail.

Strategic Considerations

Strategic considerations have also underpinned agreements to launch FTA negotiations such as the Singapore-US FTA, which reflected Singapore's close strategic relationship with the US, especially after the use of Singapore facilities were provided to the US following the US withdrawal from Subic Bay naval base and Clark airfield. Similarly, China's efforts to engage the ASEAN region culminated in its agreement on the China-ASEAN FTA with significant provisions for an early harvest in the agricultural sector by ASEAN. Sino-Japanese competition within East Asia led Japan to follow in China's footsteps with its move towards a Japan-ASEAN FTA.

Proponents of FTAs also argue that they enable WTO-plus market access. For example, the India-Singapore Comprehensive Economic Co-operation Agreement (CECA) permitted Singapore banks to set up 15 bank branches in India while the annual total quota for new bank branches is set by the Reserve Bank of India (RBI) at 18. The US-Singapore FTA provided for a significant liberalisation in services with the adoption of a negative list approach. Significantly, it removed the quota on qualifying full banks (QFBs) and wholesale banks for US banks after 18 and 36 months respectively of the entry into force of the USSFTA.

The Japan-Singapore Economic Partnership Agreement (JSEPA) provided Singapore with easier market access into the Japanese services sector than any other country. In the maritime sector, this included approval for Singapore-based shipping companies to call at Japanese ports, Japanese commitments on maritime freight forwarding and non-discriminatory access to inland transport services.

FTA negotiations also allowed states to move beyond the WTO agenda and to negotiate market access in areas such as investment, competition policy, taxation and civil aviation. CECA resulted in Singapore obtaining a Mauritius-type Double Taxation Avoidance Agreement and provisions enabling increased investment by SingTel in India. In the US-Singapore FTA, it committed Singapore to divest stakes in government-linked companies.

Time for Re-think

However, it is time for a re-think. As power shifts from the Atlantic to the Pacific, policy-makers in East Asia will need to address the question of whether it is in their interest to promote their short-term interests or whether they should strengthen multilateral institutions such as the WTO and facilitate effective global governance. There is a risk today that the emphasis on FTAs in East Asia within ministries of trade and ministries of foreign affairs is leading to a neglect of WTO negotiations, which are perceived to be more difficult to achieve.

Moreover, agreements seem increasingly sought for their symbolic impact. Such FTAs have high compliance costs and minimal benefits because of the low volume of trade in goods and services. As disparate parties are drawn into cross-regional negotiations, the question can be asked whether we would not do better to focus once again on WTO negotiations.

Barry Desker is Dean of the S. Rajaratnam School of International Studies (RSIS), Nanyang Technological University.