

The WTO and FTAs: Does "Competitive Liberalisation Really Work?"

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When the global trade talks in Cancun collapsed last September, some people in this country blamed Canberra, arguing that a misplaced focus on bilateral FTA negotiations with the United States had diverted scarce resources away from what should have been the main game and undermined Australia's position in the WTO.

Mark Vaile, like Bob Zoellick in Washington, countered that the FTA talks were an exercise in "competitive liberalisation" where progress through bilateral trade deals could support the multilateral agenda and contribute to a positive outcome in WTO negotiations.

Who's right here? Does competitive liberalisation really work?

Well, let's have a look at the evidence. I think it shows that a well-directed competitive liberalisation policy can lead to some impressive results.

When Vaile and Zoellick left Cancun, they made clear that they weren't going to waste too much time working with countries that were more interested in piling up political points than they were in negotiating trade deals.

The countries that blocked progress in Cancun and their NGO mentors had a few months to contemplate the consequences of their actions in Mexico. By the end of December, it was clear that the real losers in the stalemate were the world's poorest countries and it was not lost on them that others were not sitting on their hands. It didn't hurt for them to get the idea that the rich countries might have alternatives to the WTO.

Of course, neither the US nor Australia had abandoned the WTO. A major initiative from Zoellick in January was instrumental in getting the Round back on track, as was Vaile's Costa Rican meeting of the Cairns Group.

When the Doha Round was saved last month with agreement in Geneva, it was the agreement reached on agriculture that was at the core of the result. The agriculture package was largely the product of work undertaken by a group that came to be known as the "Five Interested Parties" – made up of the United States the EC, India, Brazil and Australia.

How interesting. The WTO Members that are arguably the most active players in the bilateral FTA arena in fact played the key leadership roles in getting the WTO talks back on track. And make no mistake about it, today those active on FTAs includes the Brazilians and Indians as much as it does the Americans and Australians.

How this competitive liberalisation plays out in practice can be explained by political and economic dynamics at both the global and national levels. Globally, FTAs by demonstrating that countries with real market power have an alternative to the WTO, help to keep pressure on the multilateral talks. Domestically, FTAs help to change political economy dynamics by strengthening pro-trade forces.

Robert Baldwin explains that it is initially easier for pro-trade forces to gain national agreement to free up the import regime with a small number of competitors, as in an FTA. Once the FTA enters into force, it further strengthens the position of the pro-trade forces and contributes to the weakening of the country's protectionist lobby – some of whom will likely go out of business as a result of the FTA's impact. Over time, as this process is repeated through successive trade deals, the pro-trade forces get stronger and the opposition to liberalisation gets ever weaker.

When the time comes to support freer trade through WTO -- the pro-trade forces are much more likely to carry the day if they have been strengthened by the country's participation in FTAs.

This is good news when you look at the sheer number of FTAs operating in 2004. Close to two hundred FTAs are now on the books and about another seventy agreements are under negotiation. Have a look at our region. A couple of days ago, you might have seen the story where the Chairman of the APEC Business Advisory Committee called for action on an APEC-wide FTA. And the sort of thing that's happening here is also happening around the world.

This brings me to another important facet of today's competitive liberalisation. Beyond the impact of FTAs on countries' willingness to open markets globally or risk exclusion from preferential deals, there is clearly a competitive dynamic at work in the area of rule-making.

WTO does not have multilateral rules on foreign direct investment, competition policy or government procurement. WTO doesn't -- but most modern FTAs do. For example, both the US and Australian deals with Singapore have investment and competition chapters. Over time, the comfort level will reach a critical mass and subjects like investment will be accepted for coverage by the global system. It's how FTAs and competitive liberalisation will work over time to enhance the scope of the WTO.

What about the argument that all of these FTAs are fragmenting the global system and undermining governments' faith in the WTO?

In last year's World Trade Report, the WTO authors suggested a test that might be applied in the case of particular FTAs to help us to judge whether the pact would likely complement or compromise the WTO system. The test consists of two questions. Let's look at these questions and how they might apply to the recently agreed Australia-US deal.

The first question is: are the two governments including any topics in the FTA that they would be unwilling to subject to negotiation in the broader multilateral system? Well, I think it's clear that in the US - Australian agreement, the answer to this question is "no". Although the FTA is "WTO Plus" in its scope, neither the US nor Australia have opposed the negotiation in WTO of investment or competition policy issues, for example. We pass the first test.

The second question is: would the two governments be prepared to extend their FTA to other countries if they wished to join? The US and Australia have demonstrated through their actions and words that this is the case. That much is clear from the APEC Bogor commitments and also from the fact that both the US and Australia

have already negotiated agreements similar to their bilateral FTA with third countries. So we pass the second test as well.

This is competitive liberalisation at work. It's "win – win". Through their FTA, the US and Australia will further integrate their two economies and buttress their global goals at the same time.

Clearly, the events of the last twelve months have demonstrated that new regional and bilateral trading agreements can helpfully open new markets and expand the coverage of worthwhile rules while at the same time contributing to progress in the WTO. Competitive liberalisation works.