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trade agreements
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*AS MULTILATERALISM EBBS, PTAS ARE ON
THE RISE*

Shahid Yusuf

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As Multilateralism Ebbs, PTAs are on the Rise¹

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The first globalization dates back to the mid nineteenth century when the UK unilaterally took steps to promote trade by lowering tariff barriers². Other countries followed suit once the benefits of a more open trading regime became apparent. The dismantling process continued through the first decade of the twentieth century when globalization crested. World War 1 and its aftermath undid decades of gradual trade liberalization. The upsurge of protectionism in the 1930s sharply curtailed both the growth of exports and the increase in GDP (Figure 1).

1. GATT and the Multilateral Trade Rounds

Post WW2 recovery commenced in the late 1940s with the signing of the General Agreement on Tariffs and Trade by 23 countries on October 30th, 1947. Eight rounds of trade negotiations followed³. Each one chipped away at the trade barriers that had emerged during the interwar years so that by the time the Uruguay Round was completed in 1994, the multilateral trade agreement signed by 123 countries had brought average nominal tariffs down from to 5 percent from 40 percent in 1946. Support from developing countries gained momentum from the 1980s onwards as the failure of protectionism to induce industrialization became apparent, the export-led growth performance of East Asian economies gained recognition and international organizations such as the World Bank, began aggressively championing the cause of free trade. Thanks to this second globalization, trade rebounded and contributed to the increase in GDP growth worldwide (Bhagwati 1988)⁴.

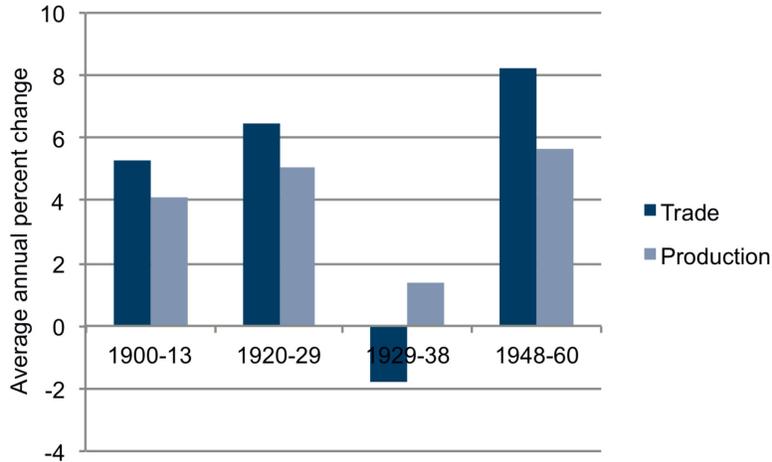
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² "From the 1840s [trade] policy was determined unilaterally. It ... reflected a growing belief that cheap imports were the key to prosperity because they would benefit the consumer as well as reduce business costs and help to maintain industrial supremacy. After 1846, the idea of using tariffs to protect British agriculture and industry from foreign competition, or to give preferential treatment to Britain's overseas empire, was also abandoned ...The essential features of the system were complete by 1860, survived the war of 1914 -18 and were not fully overturned until 1932". Cain (1999) <http://www.ehs.org.uk/dotAsset/11cabff5-3f6a-4d69-bba0-1086d69be6c7.pdf>
The repeal of the Corn Laws in 1846, signaled the start of trade liberalization by Britain. Richard Cobden persuasively argued for the advantages of free trade whether or not trading partners offered reciprocal concessions.

³ https://www.wto.org/english/thewto_e/whatis_e/tif_e/fact4_e.htm

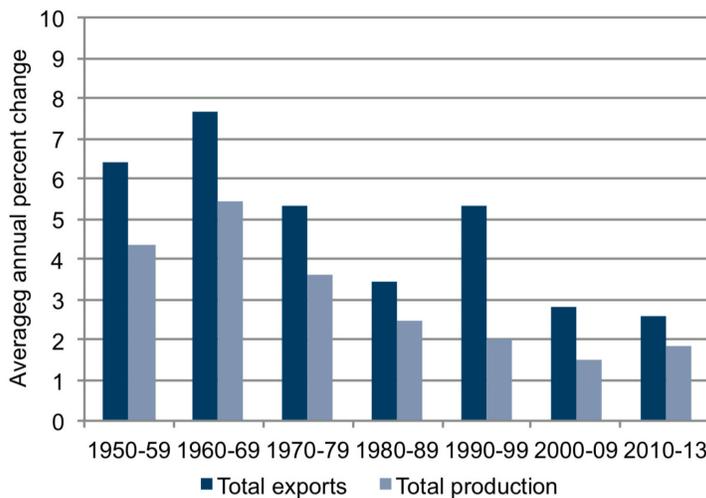
⁴ Bhagwati (p.5) maintains that relationship between trade and growth is not uni-causal but bi-directional. J. Bhagwati (1988). *Protectionism*. MIT Press. Not all countries shared in the growth associated with the second globalization. Convergence has been uneven with many countries left behind. Baldwin and Martin (1999) <https://www.nber.org/papers/w6904>; Johnson and Papageorgiou (2018) <https://www.aeaweb.org/articles?id=10.1257/jel.20181207&&from=f>

Figure 1: Growth of Trade and GDP (1900-1960)



Source: Irwin (2015) https://voxeu.org/sites/default/files/file/Global%20Trade%20Slowdown_nocover.pdf

Figure 2: Trade and GDP Growth 1950-2013



Source: Irwin (2015) https://voxeu.org/sites/default/files/file/Global%20Trade%20Slowdown_nocover.pdf

To tackle issues that the Uruguay Round had been unable to resolve, yet another round of trade negotiation was launched in Doha in November 2001. Developing countries wanted developed ones to reduce subsidies for agricultural products and trim the tariff protection afforded to farm products. The priority for developed countries was to increase the penetration of services such as banking and finance into the markets of developing nations. There was also a felt need to tighten rules governing anti-dumping, dispute settlement and the protection of intellectual property⁵. After multiple unproductive meetings, the effort to conclude the Doha

⁵ <https://www.thebalance.com/what-is-the-doha-round-of-trade-talks-3306365>

round was abandoned⁶. The consequence is a spaghetti bowl of FTAs and PTAs, which are taken up in the balance of the note.

2. The Rise of FTAs/PTAs

The failure of multilateral initiatives to scale back some of the remaining impediments and to improve trade facilitation, set the stage for bilateral and regional deal making to arrive at better trade outcomes with major partners. WTO rules allow countries to choose from among four options: (i) free trade agreements (FTAs/PTAs) according to which two or more countries reduce or eliminate tariffs on goods originating from partners but retain control over their trade and tariff policies. FTAs require countries to agree on rules of origin in order to identify goods that satisfy “originating” requirements. FTAs lead to “shallow integration” of partner countries; (ii) countries that enter into a customs union eliminate all tariffs on goods from members and agree upon a unified commercial policy and a common set of tariffs on imports from non-members; (iii) a deeper integration results from the formation of a single common market whereby members adopt a unified approach to trade, commercial and monetary policies, permit the free movement of capital and labor within the participating economies. A common set of tariffs is levied on imports from non-members; and (iv) the common market can lead to an economic and monetary union with all members adopting a single currency and coordinating their macroeconomic policies.

Most countries seeking to expand their trade have opted for FTAs/PTAs⁷. Regionalism and the spread of global value chains (GVCs) have nudged them in this direction⁸ but FTAs are also easier to negotiate and can leave countries with more degrees of freedom. Through FTAs, countries can strengthen linkages created by GVCs and forge other strategic ones as well leading to larger flows of FDI. Trade agreements covering a large region are particularly advantageous because firms can specialize and reap scale economies. In addition to greater access to markets, technology and skills, FTAs are attractive because they can spur reforms – as

⁶ Bellman (2014). The Bali Package negotiated in 2013 attempted to revive post Doha multilateral efforts but the intervening years have generated little momentum. <https://journals.openedition.org/poldev/1744>

⁷ “A cornerstone of the World Trade Organization (WTO) is the principle of non-discrimination: member countries may not discriminate against goods entering their borders based upon the country of origin. However, in an important exception to its own central prescript, the WTO, through Article XXIV of GATT and Article V of the General Agreement on Trade in Services, does permit countries to enter into preferential trade agreements (PTAs) in the form of Free Trade Areas (FTAs) and Customs Unions (CUs) with one another. Additional derogation of the principle of non-discrimination is include in the Enabling Clause, which allows one-way tariff preferences to be granted by developed to developing countries and permits preferential trade agreements among developing countries that are not subject to the disciplines imposed by the GATT Article XXIV”. Bhagwati, Krishna and Panagariya (2014) http://www.columbia.edu/~jb38/papers/pdf/paper1-the_world_trading_system.pdf

⁸ FTAs/PTAs do increase the trade in parts and components among partnering countries. For example, following Costa Rica’s US-CAFTA-DR agreement with the US and an agreement with China, annual trade with the US grew by 11 percent per annum after 1995. Trade in parts and components grew at double that rate mainly cycled through GVCs with China as the principal trading partner absorbing one-half of CR’s exports in that category. WTO (2011) https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report11_e.pdf

in the case of China prior to its accession to the WTO – including trade liberalization and bring about a simplification of rules governing trade. Hence FTAs/RTAs have proliferated⁹. A domino effect may be at work. In order not to be left behind, countries are likely to enter into FTAs if neighbors and competitors do – geopolitical circumstances permitting (Bhagwati 2002)¹⁰. Countries can also be motivated to seek trade agreements to help defuse or deflect protectionist tendencies that once again appear to be surfacing¹¹. As of January 2019, 291 regional trading arrangements were in force worldwide¹². Asian countries have been especially active in this regard with South-South FTAs outnumbering South-North ones. The ASEAN region has taken the lead in this regard. The ASEAN-China FTA (ACFTA) covers a region with 1.9 billion people; the ASEAN-India FTA (AIFTA) region is equally populous.

3. Are FTAs Trade Promoting?

FTAs are popular but do they lead to an increase in trade flows? In other words, are they “stumbling blocks” or “building blocks” towards freer trade? Much of the research has relied on gravity models that test for cross-sectional variation in the flow of trade between countries with reference to incomes, distance between any two countries, and dummy variables that represent trade agreements and factors such as a common language or shared borders. The earlier studies that treated trade agreements as exogenous right-hand side variables were unable to detect any significant effects of FTAs on trade and pointed to the likelihood of trade diversion (Bergstrand 1985; Ghosh and Yamarik 2004)¹³. These results were traced to the endogeneity of the FTA dummy because countries entering into agreements were doing so because they already engaged in substantial trade. Countries entering into agreements tended to be established trading partners, often similar in size, with democratic governments and sharing other characteristics (Bergstrand and Baier 2009; Baier, Bergstrand and Egger 2007)¹⁴.

⁹ FTAs account for three fourths of all Preferential Trading Agreements in effect. Wang (2011)

<https://www.cambridge.org/core/journals/american-journal-of-international-law/article/chinas-ftas-legal-characteristics-and-implications/DE0C8F0CCE5FFE62E176750AC681D63B>

¹⁰ Bhagwati (2002, p.117) conceptualizes this as the Nash pursuit of individual interests in an uncoordinated fashion with the multiplication of bilateral deals compelling those left out to seek their own arrangements and end up with a system that is “riddled with complex preferences and rules of origin”. J. Bhagwati (2002). *Free Trade Today*. Princeton University Press.

¹¹ “The danger is that greater reliance on a bilateral or regional approach to trade liberalization may undermine and supplant, instead of support and complement, the multilateral GATT approach. Hence, the long-term result of bilateralism could be a deterioration of the world trading system into competing, discriminatory regional trading blocs, thereby stifling world trade. Just such a disastrous experience in the thirties prompted the creation of the current multilateral trading system and makes its repair and refurbishment today an urgent task”. Irwin (2012)

<https://www.econlib.org/library/Enc1/FreeTradeAgreementsandCustomsUnions.html>

¹² https://www.wto.org/english/tratop_e/region_e/region_e.htm

¹³

https://www.researchgate.net/publication/24094359_The_Gravity_Equation_In_International_Trade_Some_Microeconomic_Foundations_And_Empirical_Evidence;

https://www.researchgate.net/publication/223760620_Are_Regional_Trading_Arrangements_Trade_Creating_An_Application_of_Extreme_Bounds_Analysis

¹⁴

https://www.researchgate.net/publication/24094359_The_Gravity_Equation_In_International_Trade_Some_Microeconomic_Foundations_And_Empirical_Evidence; <https://ideas.repec.org/a/eee/inecon/v77y2009i1p63-76.html>

More recent econometric studies have made allowance for the selection bias that is responsible for endogeneity with the help of instrumental variables, non-parametric techniques and the use of Probit models (Mansfield and Reinhardt 2008)¹⁵. Once endogeneity is accommodated, FTAs do seem to lead to trade creation – and some trade diversion. Trade creation is more likely when a number of countries participate in an FTA/PTA and less so with bilateral FTAs. (Urata and Okabe 2014)¹⁶They can also reduce the volatility of exports. Tests using synthetic control when applied to 104 country pairs, show trade increasing even more – by as much as 3.8 percent per annum (Hannan 2016)¹⁷. These ex post studies have received qualified support from ex ante research using CGE models that project an increase in trade but to a lesser extent (Hertel et al 2004; Ando and Urata 2007)¹⁸.

Data collected by the WTO suggest that the trade augmenting consequences of FTAs/PTAs are likely to be modest because of the tariff reductions already negotiated under the GATT/WTO agreements. As of 2008, half of all goods traded are subject to zero MFN tariff rates. A third of trade is of high MFN items that are exempted from PTAs. In effect, 84 percent of trade is subject to MFN terms. Because most tariffs are already at low levels, PTAs had reduced average trade weighted tariffs by only 1 percent. Moreover, as the WTO (2011) notes, reciprocal preference regimes account for almost all of this reduction, “Only 2 per cent of global imports are eligible for preferential tariffs where preference margins are 10 per cent or more. For most large exporters, preferential tariffs matter little for the bulk of their exports. This is not always true for individual sectors especially in certain smaller economies exporting a narrow set of commodities (mainly sugar, rice, bananas, fish, and garments), where preference margins may be more substantial”¹⁹. To take three examples: just 10 percent of Korea’s imports are subject to preferences but a preference of more than 10 percent applies to virtually none. Five percent of India’s imports are in the preferred category and again the number in the over 10 percent margin are tiny. Because Chile has actively pursued PTAs, 95 percent of its exports are to countries with which it has negotiated such treaties, but preferences benefit only 27 percent of its exports and 3 percent fall into the over 10 percent margin (Bhagwati, Krishna and Panagariya 2014). Where preference margins are low, firms are reluctant to utilize the preferences. An ADB survey found that as many as half of all firms did not take advantage of the preferences. In some cases, the costs and complications in establishing rules of origin²⁰ can discourage exporters but there are other factors as well.

¹⁵ https://econpapers.repec.org/article/cupintorg/v_3a62_3ay_3a2008_3ai_3a04_3ap_3a621-652_5f08.htm

¹⁶

https://www.researchgate.net/publication/5020661_The_Impacts_of_Free_Trade_Agreements_on_Trade_Flows_An_Application_of_the_Gravity_Model_Approach

¹⁷ Hannan (2016) <http://pubdocs.worldbank.org/en/960821480958611562/5-Swarnali-paper.pdf>

¹⁸ <https://www.gtap.agecon.purdue.edu/resources/download/2883.pdf> Ando and Urata (2007) find that ASEAN+3 stand to benefit the most however, FTAs can be an economic plus once capital accumulation, trade facilitation and incentives for FDI are factored in. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3077835

¹⁹ https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report11_e.pdf

²⁰ Rules of origin (ROO) single out goods that receive preferential tariff treatment and exclude others that are being exported by a third country to a low tariff FTA member so as to gain entry to the market of a high tariff member of the same FTA. The complexity of ROO and a paucity of data can raise transaction costs and hinder

4. Where Trade Agreements are Heading

Early proponents of FTAs/PTAs were of the view that they could somewhat circuitously support the cause of multilateralism that was then and now seen as the first best approach to trade liberalization and the one that minimizes the risk of trade diversion. That optimism has faded. Larger countries and those that are determined to keep non-trade and politically sensitive issues off the agenda, find that bilateral or plurilateral agreements are more advantageous and less contentious. Bigger countries can extract better terms from partners when they engage in bilateral negotiations. Such deals also have the support of MNCs that are interested in protecting their internationally dispersed investments from competition that could result from multilateral agreements (Rodrik 2018)²¹.

Mainstream economic thinking strongly favors free trade and champions multilateral trade agreements as these are likely to be the most trade creating and growth promoting²². However, the second globalization has triggered protectionist sentiments in a number of advanced countries²³ that are having a dampening effect on the growth of trade and making it harder for countries to coalesce around multilateral trade agreements. During the medium term at least, any attempts at lowering the barriers to trade will be the outcome of FTAs or RTAs of which a number are in progress. While these might on balance, lead to increased trade between country pairs, larger countries will have the upper hand and developing countries entering into FTAs need to carefully weigh the benefits. Moreover, the experience with SAFTA (South Asian Free Trade Agreement) shows that political opposition within and political frictions between countries can negate the gains from FTAs. Making them work to the advantage of all partners requires political will, careful preparation and the collection of detailed relevant data, clarity with regard to objectives, canvassing of the views of parties likely to be affected by the FTA, and mobilizing the support of key stakeholders (Kawai and Wignaraja 2009)²⁴.

SAFTA is an example of agreement that has foundered because political issues have had the upper hand and subsumed a serious analysis and discussion of the gains from trade. SAFTA was signed in 2004, came into effect in 2006 but it has generated very little trade among members. Intra-regional imports equal 3 percent of the total and exports just 6 percent. In fact,

compliance with FTAs. Wignaraja (2011) <https://voxeu.org/article/south-south-free-trade-agreements-work-progress>

²¹ Rodrik (2018) notes that FTAs can stimulate trade flows between partners but there is plenty of scope for rent seeking activities, veiled protectionism of entrenched interest groups. FTAs can also result in a redistribution of income that is deliberate or unexpected. <https://www.nber.org/papers/w24344>

²² <https://www.weforum.org/agenda/2019/03/why-tariffs-spell-trouble-for-economic-growth/>

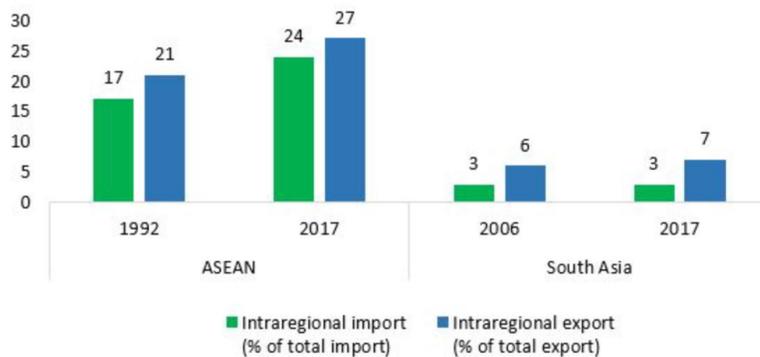
²³ <https://www.wsws.org/en/articles/2018/11/24/wtow-n24.html>; Fajgelbaum et al (2019)

<https://voxeu.org/article/return-protectionism>; DiTella and Rodrik (2019) <https://voxeu.org/article/labour-market-shocks-and-demand-trade-protection>. "Economists have been aware of the senselessness of protectionism since at least Adam Smith ... tariff increases have adverse domestic macroeconomic and distributional consequences. Output falls after tariffs rise because of a significant decrease in labor productivity. That is, the wasteful effects of protectionism lead to a meaningful reduction in the efficiency with which labor is used, and thus output". Furceri et al 2019. <https://voxeu.org/article/macro-reasons-loath-protectionism>

²⁴ <https://www.adb.org/sites/default/files/publication/155999/adb-wp144.pdf>

intraregional trade in South Asia is among the lowest for any region amounting to 5 percent of total regional trade (Figure 3). Because of persisting political tensions, SAFTA is likely to stagnate absent a political rapprochement between India and Pakistan. A World Bank report (2018)²⁵ lists three economic factors that account for the high costs that have hobbled the growth of intraregional trade: (i) a long list of sensitive imports and exports that are excluded from negotiations on future tariff reduction. Furthermore, over a third of intraregional trade does not receive preferences whereas 96 percent of intraregional trade in the ASEAN region is not subject to import tariffs; (ii) South Asian countries have imposed a large number of para-tariff and non-tariff levies on imports that raise effective barriers, are non-transparent, discourage trade, and fall outside the ambit of trade negotiations: and (iii) restrictions on the products that are allowed to enter through overland ports of entry, which means that the majority have to be shipped by sea thereby adding to the expense.

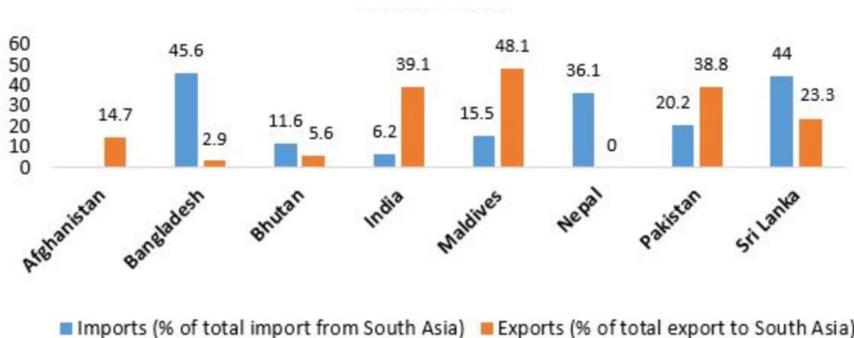
Figure 3: Intraregional Trade in ASEAN and SAFTA



Source: Calculation based on UNComtrade data through WITS

Source: World Bank (2019) <https://openknowledge.worldbank.org/handle/10986/30246>

Figure 4: Percent of South Asian Trade on Sensitive list



25

<https://openknowledge.worldbank.org/bitstream/handle/10986/30246/9781464812941.pdf?sequence=8&isAllowed=y>

Source: World Bank (2019) <https://openknowledge.worldbank.org/handle/10986/30246>

The World Bank maintains that a systematic pruning of these two impediments could lead to a threefold increase of trade from \$23 billion to as much as \$67 billion. The Bank believes that rising trade flows would also help attract much needed FDI into tradable activities. For example, the China Pakistan Economic Corridor (CPEC) agreement has channeled Chinese investment into energy and transport projects in Pakistan but FDI in export-oriented activities has been negligible thus far.

5. China's FTAs

Prior to its accession to the WTO, China had not entered into any FTAs. The very first few were with Hong Kong and Macau in 2003 and New Zealand in 2008²⁶. "China's strategy was to begin local and small, in part reflecting the ease of negotiation and also the learning experiences involved in sequential negotiation...With the notable exception of the ASEAN agreement, all of the first 12 China's RTAs [were] with relatively small trading entities. In this way, it has been easier to achieve precedents in coverage and for later negotiation, as well as pursuing new initiatives" (Whalley and Li 2014)²⁷. Interestingly, the ASEAN agreement went well beyond the minutiae of tariff adjustments and embraced broad cooperation on development, illustrative of China's readiness to tailor its agreements so as to maximize longer term benefits through interaction with developing countries. China has also sought to deepen the trading links by subsequently entering into Bilateral Investment Treaties (BITs)²⁸.

China's approach to FTAs indicates that economic considerations are not necessarily uppermost²⁹. Salidjanova (2015)³⁰ is of the view that there is no single modus operandi. Some offer generous terms to the trading partners while others aggressively protect China's domestic industries. Of the 14 FTAs negotiated to date (Figure 5), security related concerns appear to be the primary motivation for those with Hong Kong, Macau and the ASEAN countries; securing

²⁶ The treaty with Korea was much more limited in scope with many exclusions. Political considerations trumped economic ones. Schott et al (2015) <https://ideas.repec.org/p/iie/pbrief/pb15-24.html>

²⁷ <https://voxeu.org/article/china-s-regional-and-bilateral-trade-agreements>

²⁸ Laget et al (2018) observe that "The depth of trade agreements contributes to increase GVC trade among parties. This impact is higher for industries with higher share of value added in total production, suggesting that deeper trade arrangements help countries to integrate in industries with higher levels of value added... for trade agreements between developed and developing countries, this effect is mostly driven by the presence of provisions that are currently outside the domain of the WTO and that deal with behind the border policies, such as investment and competition policy. Deep preferential trade agreements (PTAs) increase the domestic value-added content of exports mainly through GVCs. Adding a provision to a PTA boosts domestic value added of intermediate goods and services exports (i.e. forward GVC linkages) by 0.48 percent, while an additional provision in a PTA increases foreign value added of intermediate goods and services exports (i.e. backward GVC linkages) by 0.38 percent. We also find evidence that deep trade agreements improve forward linkages particularly for more complex GVCs". <http://documents.worldbank.org/curated/en/356541529933295649/Deep-trade-agreements-and-global-value-chains>

²⁹ Both economic and geopolitical factors have induced Pakistan to enter into FTAs with China.

³⁰ <https://www.uscc.gov/sites/default/files/Research/China's%20Trade%20Ambitions%20-%202005.28%2015.pdf>

supplies of strategic materials is a second motivation, which is apparent in the FTAs with Australia, New Zealand³¹ and Peru; some of the FTAs ease Chinese firms into GVCs and help China accumulate experience in negotiating these agreements; FTAs with small economies can serve geopolitical objectives while requiring China to make few concessions that would arouse opposition from domestic industries; China also uses FTA as a way of validating its claim to having become a “market economy” a status not accepted as yet by other members to the WTO such as the U.S. and the EU³².

The opening gambit for China when engaging in negotiations, is to limit negotiations to a restricted list of commodities with carve outs that protect agricultural products and a number of strategic industries. The FTAs also generally sidestep anti-dumping safeguards, issues relating to subsidies, domestic regulations, government procurement³³, and the FTAs do not spell out procedures for settling disputes. These latter (as with Peru and Chile) are lacking in transparency, do not call for panel hearings, consultations with stakeholders or the release of a report on a fixed schedule.

In entering into FTAs, China emphasizes that it is an economy led by the market and not one that is state led. However, since 2013, the importance given to state owned enterprises means that they have a bigger voice in FTA negotiations and China’s approach has become steadily more protectionist³⁴ and less market centric. China’s relatively decentralized system of government also affects implementation and enforcement of trade agreements. Many subnational agencies have a role in implementation, and they do not always strictly abide by the rules agreed to by Beijing. De facto outcomes for trading partners can therefore diverge from de jure agreements. In addition, as noted above, there are “many carve-outs for politically-sensitive sectors in goods and services and little discipline as regards antidumping duties, agricultural subsidies, or domestic regulatory barriers.” (Ka Zeng 2016)³⁵. China is highly

³¹ “The New Zealand-China Free Trade Agreement (FTA) has been a success story. Since the FTA came into force in 2008, two-way trade (exports and imports of goods and services) has more than tripled from \$9 billion to over \$32 billion. The FTA [has catalyzed] trade and economic cooperation [between the two] countries. In the March 2019 year, the top exports to China were milk powder, butter, and cheese, reaching \$4.5 billion and accounting for one-quarter of New Zealand’s exports to China. Logs and wood were the second-largest export, worth \$3.1 billion. Travel was also a significant contributor to New Zealand’s overall surplus with China, worth \$3.0 billion. In the March 2019 year, imports from China were valued at \$13.1 billion. Top imports were electrical machinery and equipment (such as mobile phones), mechanical machinery and equipment (such as portable computers), and textiles and textile articles (such as clothing)”. <https://www.cato.org/blog/negotiating-trade-deals-china>

³² The US has classified China as a Non-Market Economy since 1981 a classification that China has resisted since 2016 and filed a case with the WTO in its pursuit of a Market Economy Status.

<https://fas.org/sgp/crs/row/IF10385.pdf>

³³ Government procurement is off-limits to foreign suppliers and even to private Chinese firms.

³⁴ Court (2019) <https://itif.org/publications/2019/01/28/china's-digital-protectionism-and-mercantilist-policies-rank-among-world's>. Tariff rate, applied, simple mean, manufactured products (%) in China was 7.84 as of 2016. Its highest value over the past 24 years was 40.75 in 1992, while its lowest value was 7.78 in 2014.

<https://www.indexmundi.com/facts/china/tariff-rate>

³⁵ <https://academic.oup.com/cjip/article-abstract/9/3/277/2352049>

selective in opening its market to imports of agricultural products in particular grain (rice, corn) and meat³⁶.

Figure 5: China's FTAs (2017)

Partner	First Signed	Phasing in of Agreement
ASEAN	2002	Framework (2002), goods (2004), services (2007), investment (2009)
Hong Kong	2003	Single undertaking
Macau	2003	Single undertaking
Chile	2005	Goods (2005), services (2008)
Pakistan	2006	Goods (2006), services (2009)
New Zealand	2008	Single undertaking
Singapore	2008	Single undertaking
Peru	2009	Single undertaking
Costa Rica	2010	Single undertaking
Switzerland	2013	Single undertaking
Iceland	2013	Single undertaking
Republic of Korea	2015	Single undertaking
Australia	2015	Single undertaking
Georgia	2017	Single undertaking

Sources: China's Ministry of Commerce (MOFCOM)³⁵ and Salidjanova (2015, 6).

Note: China had signed 14 FTAs by end 2017 and was negotiating 8 others

Source: Leblond (2017) <https://www.cigionline.org/sites/default/files/documents/China%20Canada%20Trade.pdf>

The FTA between China and Pakistan illustrates the gains as well as the downsides of a trading agreement between the world's second largest economy with a GDP of \$13.6 trillion and a lower middle-income nation with a GDP of \$313 billion in 2018. The first FTA was finalized in 2006; phase 2 was signed in 2019³⁷. Trade between the two countries that had amounted to a little less than \$800 million in 2000 rose to 3.5 billion in 2006 with the composition of Pakistan's imports from China increasingly taking the form of machinery, telecom equipment, transport equipment, textiles, yarn, and iron and steel. Pakistan in turn exported mainly textile yarn, fabrics and resource-based products (Figure 6)³⁸. Since then, total trade has risen to approximately \$13.5³⁹ billion with Pakistan importing \$11.5 billion worth of manufactures from China during FY 17-18 and exporting \$1.7 billion with little change in the composition of products⁴⁰. While Pakistan's exports have doubled China's have risen threefold suggesting that

³⁶ The recent outbreak of African swine fever, which has decimated China's hog population has forced China to massively increase its imports of pork and poultry. <https://www.wsj.com/articles/poultry-shares-heat-up-with-lifting-of-china-export-ban-11572462328>

³⁷ This should benefit agricultural exports and others such as leather goods and confectionery. <https://www.aa.com.tr/en/asia-pacific/2nd-phase-of-china-pakistan-free-trade-deal-in-effect/1661413>

³⁸ Musleh-ud Din, Ghani and Qadir (2009) https://www.researchgate.net/profile/Usman_Qadir/publication/254428380_Recent_Experience_and_Future_Propects_of_Pakistan's_Trade_with_China/links/550ed4f80cf27526109f2148.pdf

³⁹ In FY19 it rose to \$15.6 billion.

⁴⁰ <https://www.dawn.com/news/1423551>. Exports to China in FY 19 were \$1.9 billion. <https://dailytimes.com.pk/461070/pakistan-china-trade-where-we-stand/>

larger and more industrially developed nations frequently have the upper hand. By strengthening its ties with China, Pakistan can count on China's support in global fora, in bolstering its defense capabilities and assistance in surmounting economic crises, but cheaper and better quality imports of manufactures from China are driving Pakistani firms out of business and there is a risk that instead of compelling industry to become competitive, this pressure could accelerate the process of deindustrialization. In asymmetrical FTAs, especially with the likes of large economies such as China, the smaller and weaker countries need to ensure that in pursuit of medium-term gains, their long-term growth drivers are not compromised.

The experience of ASEAN countries with the ACFTA through 2013 was more positive possibly resulting from the China's general tariff rate and the preferential rate afforded to ASEAN countries. Taguchi and Lee (2016)⁴¹ find significant evidence of trade creation with ACTFA yielding more positive results than either AJFTA or AKFTA.

A bilateral FTA between China and Cambodia is in the works and because Cambodia exports few agricultural products to China, negotiations are likely to be proceed more rapidly than with Vietnam and Thailand that are major exporters of grain and other agricultural commodities⁴².

Figure 6: Pakistan's exports 2017



Source: <https://oec.world/en/profile/country/pak/>

6. Concluding Observations

The weight of economic research supports multilateral trade agreements because they confer more advantages than bilateral and plurilateral ones. However, until such time as multilateralism revives, the noodle bowl of FTAs/RTAs will serve as the second-best pathway to trade liberalization. If the benefits of such agreements are to outweigh the costs, countries particularly the smaller ones, need to thoroughly prepare for the negotiations, assemble an

⁴¹ https://mpr.ub.uni-muenchen.de/72503/1/MPRA_paper_72503.pdf

⁴² <https://www.khmertimeskh.com/659652/feasibility-study-on-china-cambodia%E2%80%8B-free-trade-agreement-to-be-launched/>

inter-ministerial team with clear objectives and provide it with the resources to ensure that the FTA delivers the sought after gains from trade and minimizes trade diversion. Businesses assessing the benefits they might derive can be usefully guided by the following checklist:

- “Examine whether or not your products are included under the specific FTA;
- Examine whether the FTA includes any other benefits such as withholding or dividend tax reductions;
- Where applicable, include any applicable treaty benefits into your pre-incorporation business plan and articles of incorporation;
- Examine any customs registration processes that may require additional registration and intent to invoke treaty status. This certainly applies in China;
- If you have not completed this process or are unsure, seek professional advice to remedy the situation. Even given fees, the tax amount saved will almost certainly cover them in year one alone.
- When completed, your business is FTA enacted and will save on the import and services taxes that would otherwise have been due”. (China Briefing 2014)⁴³

In a publication on Free Trade issued 19 years ago, Jagdish Bhagwati (2002, p.120) thought that “the world trading system is at a crossroads ... and that the headlong rush into preferential trade has left free trade in a sorry state”. He believed optimistically “that such folly cannot persist”. Yet nearly two decades later, the world trading system finds itself at the very same crossroad having filled the noodle bowl of FTAs/PTAs to the brim⁴⁴. The case for multilateral progress towards freer trade is no less solid but the political support has weakened as has public belief in the advantages of globalization.

⁴³ <https://www.china-briefing.com/news/understanding-chinas-free-trade-agreements/>

⁴⁴ PTAs now cover almost one half of global trade and they have substantially lowered tariff barriers. Espita et al (2019) report three findings. “(i) Whereas 42% of the total value of trade traded freely under MFN rates in 2016, preferential trade agreements have fully liberalized an additional 28% of global trade. Furthermore, approximately two-thirds of countries participating in preferential trade agreements have reduced trade-weighted average preferential tariffs to less than 5%... (ii) [However,] several lower-income countries still have trade-weighted average tariffs well above 5%. PTAs have ... not eliminated the high levels of protection for a handful of sensitive products that account for 3% of world trade and include agricultural products, textiles, and footwear. (iii) The widening coverage of preferential trade agreements is in itself an antidote to trade diversion. The average preferential margin – the difference between the MFN rate of duty and the preferential rate for members of preferential trade agreements – for trade covered by preferential trade agreements is low because one-fifth of world trade under preferential agreements is already duty-free. Still, on the face of it, more than a quarter of world trade is subject to an average preference margin of 7.4%”. <https://voxeu.org/article/assessing-preferences-preferential-trade>

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