

DOI: 10.7251/EMC1602212B

Datum prijema rada: 14. septembar 2016.

Datum prihvatanja rada: 9. decembar 2016.

UDK: 339.923:341.241.8

Časopis za ekonomiju i tržišne komunikacije

Godina VI • broj II

str. 212-232

ORIGINALNI NAUČNI RAD

THE EFFECTS OF MEGA-REGIONAL TRADE AGREEMENTS ON THE MULTILATERAL TRADING SYSTEM

Vlatka Bilas | Associate professor, e-mail: vbilas@efzg.hr, Faculty of Economics and Business, University of Zagreb, Croatia

Sanja Franc | Assistant professor, e-mail: sfranc@efzg.hr, Faculty of Economics and Business, University of Zagreb, Croatia

Abstract: *The aim of this study is to investigate the motives and effects of mega-regional trade agreements on the multilateral trading system using the example of Trans Pacific Partnership (TPP) and Transatlantic Trade and Investment Partnership (TTIP). Multilateralism and regionalism, although opposite trends, coexist simultaneously. While many arguments can be given for both approaches one has to recognize that the number of regional trade agreements is increasing and that regionalism is becoming a prevailing trend. The response to the regional trade agreements, especially mega-regionals, will mostly depend upon the effect on the third countries' trade interests. Since it is expected that, over time, many of the currently excluded emerging economies will become a part of some mega-regional agreement, it is not likely that new global standards and rules will be created on a strictly regional but rather on multilateral level.*

Key words: *mega-regionals, multilateral trading system, TPP, TTIP*

JEL Classification: *F15*

INTRODUCTION: RISING TRENDS OF MULTILATERALISM AND REGIONALISM

Globalisation and multilateralism are considered to be the processes that have the global perspective as a common characteristic. Multilateralism, in its broadest sense, may be defined as international cooperation between more than two countries, designed to solve international problems and conflicts arising from anarchy in international relations (Krause Joachim, 2004). The predominant point of view is that multilateralism is the most effective way to structure international relations and to tackle problems and challenges in many fields.

Contrary to globalisation, of late, there has been an evident trend of regionalisation or creation of regional economic integration models in different parts of the world (Mato Grgić, Vlatka Bilas and Sanja Franc, 2012). It is believed that regional trade agreements may add to, rather than replace, multilateral rules and progressive multilateral liberalization.

Regional trade agreements (RTA) are not a new trend but dimension that they have reached is new: they include more partners, from different levels of development and different regions, covering larger volume of trade, and aiming at reaching agreements of a deeper nature on a wide scope of issues.

Trade agreements can induce changes in all economic sectors and create a domino effect in a globalized trade world. In general, the purpose of trade agreements is to lower tariffs. But as history records, as trade expanded it shifted from already low tariffs to non-tariff barriers, increasing the role of rules and regulations. These aspects may take a complete or incomplete form by helping or being an obstacle in the economies' development, but general reason for their existence is to protect workers, consumers, the economy and the environment (Gotu Ioana, 2016).

Recently, there was a surge of regional trade agreements. Some of these agreements with their design, content and qualitative character will affect the creation of a new world order and economic governance (Melendez-Ortiz Ricardo, 2014).

As mentioned, provisions of free trade agreements can go well beyond multilateral accepted standards and include provisions such as: new rule for internet and digital commerce, across the board national treatment for foreign investors, streamlined regulations through standardized principles, enhanced intellectual property protection, government procurement protection, competitive neutrality for state-owned enterprises, labor and environment codes ad etc.

The economic significance of RTAs has also been changing. While in the past RTAs may have been defined more by geopolitics, the new trend is a greater emphasis on commercially meaningful associations that address several emerging policy concerns. Today, more and more RTAs are organized around a set of deeper integration issues that fosters transnational collaborative production and global value chains. They could be termed as production-sharing or regulatory integration RTAs (Melendez-Ortiz, 2014).

Current trends in RTAs include the following (Melendez-Ortiz, 2014):

- organization around substantive current or potential trade and foreign investments value,
- consolidation RTAs in which existing ones are expanded through new members or by merging with other RTAs,
- mega-regional RTAs which assume deep integration partnerships in the form of regional trade agreements between countries or regions with a major share of world trade and foreign direct investments and in which two or more parties are in a paramount driver position or serve as hubs in global value chains.

Mega-regional trade agreements can be defined as regional agreements that have systematic and global impact. They are sufficiently large and ambitious to influence trade rules and trade flows beyond their areas of application (World Bank, 2016).

Mega-regional agreements include a number of partner countries, but also at the same time exclude a large number of third countries. The reactions of third countries will have an impact on the global trading system and the success of mega-regional agreements. The multilateral trading system will also depend on the nature of such agreements, and their openness or closure to new members.

As the trend of creating mega-regional agreements is in its full spread, the aim of this study is to investigate the motives and effects these agreements on multilateral trading systems using the example of Trans Pacific Partnership (TPP) and Transatlantic Trade and Investment Partnership (TTIP) that is currently being negotiated.

LITERATURE REVIEW

The debate over the benefits and costs of multilateralism and regionalism is extensive, especially over the past two decades. Some authors believe that globally free trade might imply an optimum generation of wealth, but where achieving balance between political, economic and cultural objectives is concerned, regional integration arrangements have the priority (Velde Dirk Willem and Fahnbulleh Miatta, 2003). Bearing in mind cultural similarities, as well as the fact that democracy works best in a limited geographical area, this argument is understandable.

Regional agreements widely differ one from another, but they have all a common objective: to lower trade barriers among their member states and enhance economic growth, development and reduce poverty. The approach of the “new

regionalism” defines regional integration as a multidimensional process that goes beyond trade and economic integration and that involves other dimensions such as politics, diplomacy, culture and policy harmonization (Hettne Bjorn, Andras Inotai, and Osvaldo Sunkel, 1999).

In fact, regional economic integration may be in the function of achieving multilaterally free trade. The Doha Declaration (2001), a draft for negotiations on multilateral trade liberalization, confirmed that regional trade agreements could play a significant role in promoting liberalization and expansion of trade and in stimulating development. However, they could also hamper trade relations between some countries outside the region and the countries within the region. In addition to this, they could discourage further opening of the market and hence limit the growth perspective for all.

One of the ways in which regional trade arrangements may act as a stumbling stone to global liberalization is when they encourage their member states to increase external tariffs applicable to non-member states. This way, they enhance the total level of protection in the global market.

Smaller countries are encouraged to form regional trade integration because of the possibility to access a larger market and the potential utilities that are available in the group of higher external tariffs (Panagariya Arvind, 1998).

If we assume that preferential trade agreements and multilateral processes are independent, is it possible to continue further expansion of preferential trade agreements until free trade is achieved across the globe?

In every country there are both advocates and opponents to the membership in a regional bloc. Deeper integration within a bloc is detrimental to the profit of non-member states’ companies and will, therefore, stimulate these countries to carry out more intense political activity and strive to join the bloc. Even if a government is initially indifferent to the membership, the export activity may very easily lead it to the point of accession. Furthermore, if the bloc enlarges, the cost for non-member states increases because they are left with no advantage in a growing number of markets. The second round of effects will bring about even more political activities in favour of accession, which may then lead to further expansion of the bloc.

Robert Baldwin’s (1993) domino theory uses the influence of interest groups in non-member states to prove the positive effects of regionalism. He claims

that trade and investment diversion within a trade arrangement will generate such forces in the excluded countries that will entice them either to join the arrangement or create new trade arrangements between themselves. This pressure will grow in line with the size of the trade arrangement. A momentum is created through asymmetric lobbying – the losers lobby more than the winners. The exclusion from trade blocs will strengthen the pro-liberalization forces that are affected by trade or investment diversion. This process causes bilateral trade barriers to fall as dominoes. Baldwin's work represents a simple model that shows how deeper integration of an existing regional bloc may initiate requests for membership from the countries that were previously satisfied with the non-member status.

Panagariya (1998) gives two key limitations to the analysis of Baldwin. In line with the tradition of economic-geography model, Baldwin formalizes trade barriers as transport costs and, therefore, joining the preferential trade area becomes equivalent to a reduction in transport costs. This means that the expected tariff revenues from trade barriers are entirely absent in his theory. It is not clear if his conclusion will be valid if transport costs are replaced with tariffs and the effect of tariff revenue achieved by entering the preferential trade area. Secondly, even if we neglect this problem, Baldwin assumes that member states do not block the entry or the enlargement of the integration model. However, it can be assumed that after the preferential trade area has expanded to a certain size, its members will be motivated to block further entries and enlargement rounds.

Levy Philip I. (1997) examines how the option of creating a free trade area affects multilateral liberalization. This issue involves the world with many countries in which the voters in two countries are entitled to vote on the free trade area and multilateral liberalization, in that order. It is voted positively for the free trade area only if it increases the utility of the median voter above the autarky equilibrium.

Examining a three-country model, Krishna Pravin (1998) shows that enhanced trade diversion in a free trade area between two countries reduces the incentive to eventually liberalize with a third country.

One of the arguments in favour of the harmful effect of the free trade area on multilateral liberalization is the idea that free trade areas may unify protectionist lobbies and turn them into effective obstacles against multilateral liberalization. Given the fact that preferential trade arrangements are usually negotiated

between developing countries, this argument becomes even more significant. Multilateral negotiations involve both developed and underdeveloped countries and draw less attention to protectionist lobbies, as their powers weaken in such a framework.

Lawrence Robert Z. (1995) has advocated regional agreements claiming that, unlike multilateral liberalization, they stimulate deeper integration through coordination and policy harmonization (for example, through product standardization, regulatory regimes, environmental protection policies, investments, labour standards and other). He claims that such deep integration may offer benefits to its members by reducing the costs of production and by increasing the overall efficiency.

Trade blocs are often formed for non-economic reasons, such as national security, peace and assistance in developing political and social institutions. Since these reasons are mostly shared by a limited number of countries, usually neighbouring countries, they are more likely to be achieved on a regional, rather than a multilateral basis.

Furthermore, RTAs are also often a step toward larger agreements through the process of competitive liberalization (Baldwin Richard and Dany Jaimovich, 2010).

In principle, regional integration can have both positive and negative effects on multilateral free trade. This is why some advocate the respect of the World Trade Organization (WTO) framework of action in order to minimize the negative effects and maximize the positive effects on multilateral liberalization.

It is clear that countries cannot stick to multilateralism only, since they are at different levels of development. It is also a fact that negotiations within the WTO take a rather long time. Regionalism, therefore, represents an alternative, at least for countries that are geographically close to each other and especially for countries that have close economic interests and a larger volume of mutual exchange.

Regional trade agreements are inherently discriminatory and deviate from the principle of the most favoured nation. Therefore, it comes as no surprise that trade between such blocs grows much faster than trade with non-members. On the other hand, trade with non-members grows at approximately the same rate as world trade in general. In some smaller and more dynamic regional trade agree-

ments, trade with non-members grows even faster than world trade. It is said that deeper integration is also useful for non-member states because domestic regulations allow for greater competition even from non-member countries (Crawford Jo Ann and Sam Laird, 2000).

According to some opinions, the problems surrounding negotiations within the Doha round will only speed up the proliferation of regional trade arrangements. Pessimistic viewpoints point out that there may be a possibility of reducing the initiatives for multilateral liberalization (Grgić, Bilas, and Franc, 2012).

MOTIVATION BEHIND REGIONAL TRADE AGREEMENTS

Most reasons for entering a regional economic arrangement may be divided into economic and political reasons. The main economic reasons are: a search for larger markets, deeper integration, retaining investment, a safer approach to more developed markets. Other economic motives are (Matthews Alan, 2003):

- using trade benefits of improved resource allocation and greater competition,
- easier market access to other countries and insurance against the break of multilateralism,
- providing credibility to politically difficult domestic policies,
- increasing multilateral bargaining power in international forums and towards third countries,
- attracting external assistance and investment to encourage deep integration.

Political motives include (Matthews, 2003): enhanced bargaining power, the success of political/economic reforms and ensuring or earning political support. Different authors define different political motives for regional integration. Therefore, in some papers it is possible to find the following additional political motives: the objectives of national security and regional integration as a step towards political unification.

The following motives are also found in reference literature (Grgić, Bilas, and Franc, 2012):

- enhanced trust among member states,
- dealing with issues of non-traditional security (environmental protection, for instance),
- the mechanism for strengthening reforms,
- politically stimulated economic deregulation,
- easier negotiations and agreement implementation.

Characteristics of the Trans Pacific Partnership and the Transatlantic Trade and Investment Partnership

The Trans Pacific Partnership (TPP) is a regional regulatory and investment agreement that was negotiated by 12 countries throughout Asia Pacific region, namely, Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States and Vietnam. Roots of this agreement can be found in Trans-Pacific Strategic Economic Partnership Agreement or "P4" signed in 2005 among four countries, New Zealand, Singapore, Brunei and Chile as founding members. This original agreement had an accession clause, allowing the members to encourage the accession of other economies (New Zealand Ministry of Foreign Affairs and Trade, 2005). Indeed, new members have joined. In 2008, the US joined the negotiations by expressing its intention to include the areas of financial services and investments in negotiations, areas not mentioned in the initial agreement. This decision was followed by Australia, Peru and Vietnam. Then, the effective negotiations of the new version of the agreement - Trans Pacific Partnership, started in March 2010 and took into consideration joining of a new member, Malaysia. Canada and Mexico were formally invited to join in 2012; Japan joined in 2013, while South Korea began to consult with negotiating partners in 2014 but has never made a formal request.

TPP agreement was negotiated within seven years, with 19 rounds of talks and numerous meetings held between 2008 and 2015, when the agreement was finally concluded and now each party has to ratify the text. This process should take no longer than two years.

This free trade agreement has 30 chapters as member parties envisioned the agreement to be comprehensive and high standard by eliminating tariffs and non-tariff barriers to trade in goods, services and agriculture (Gotu, 2016).

Since many and diverse economies were included in the agreement the scope of the negotiating activity was to seek an agreement that balanced the members' range of expressed interests and achieve a comprehensive and transformative agreement with shared benefits (United States Trade Representative, 2013).

Furthermore, the TPP is defined by five features which can set standards for the future agreements. These features include areas such as market access, regional agreement, cross-cutting trade issues, new trade issues etc. Another key issue is the facilitation of production and supply chains among the TPP parties. New trade challenges that promote a competitive business environment across the

TPP region is also an important feature, as well as being updated appropriately to the trade issues that may emerge in the future as a result of its expansion to include new countries, and the novelty of the trade issues that might occur (Gottu, 2016).

The following topics are reportedly included in the TPP agreement (Melendez-Ortiz, 2014):

- Market access for agricultural and industrial products. Parties aim for duty-free access for trade in goods, and it is being negotiated bilaterally.
- Services. The agreement will employ a negative list approach and cover financial services, including insurance and insurance-related services, banking as well as other financial related services.
- Government procurement. Agreement states common principles and procedures, as well as specific obligations for procurement; it aims at comparable coverage by all members while recognizing transitional measures for procurement markets in developing countries.
- Agriculture. It will include sanitary and phytosanitary standards, tobacco regulation and agricultural competition.
- Rules. Provisions that build on disciplines contained in the WTO's Uruguay round agreement to technical barriers to trade and intellectual property rights enforcement.

The TPP also includes social and environmental provisions that may impact trade and production chains (World Bank, 2016):

- Labor and environment. Standards for labor and environmental sustainability are politically contentious. The TPP seeks to incorporate International Labor Organization obligations (ILO), requires domestic laws to be consistent with international standards and provides for enforcement.
- Intellectual property rights. The TPP goes somewhat beyond the WTO's rules and requires penalties for the unlawful commercial exploitation of copyright work, and prescribes measures to reduce the illegal distribution.

Harmonization of labor and environmental standards within the TPP could have important implications for participating developing countries such as Malaysia, Mexico, Vietnam and Peru. While such harmonization which goes beyond product standards to encompass production process standards has social and environmental benefits, it may also affect competitiveness of firms in countries that currently do not meet those standards (World Bank, 2016).

The areas of concern, especially for developing countries, include agriculture, and some of the new standards and rules that could be a particular burden for them to implement, such as intellectual property rights protection. But many of the provisions in newer areas are not fully enforceable under the agreement and may have little impact on behavior, or trade or investment (Ciuriak Dan and Natassia Ciuriak, 2016).

Overall, the outcome of negotiations reflects the asymmetry of bargaining power between the United States and smaller parties to the agreement, particularly Vietnam and other mentioned developing countries (Elliot Kimberly, 2016).

The large number of free trade agreements being implemented between Asian and Pacific states suggests that the effect of tariff liberalization may be low despite the significant share of global trade accounted for in this region. Cheong Inkyo (2013) underlines the extent to which free trade agreements may dilute the effect of liberalization on goods trade, with Asia-Pacific region having signed close to 100 free trade agreements. He also states that gains for member states from goods trade liberalization through TPP are likely to be negligible for most of them. There are some estimates that gains may be somewhat larger when non-tariff barriers are included.

The Transatlantic Trade and Investment Partnership (TTIP) is another mega-regional agreement currently being negotiated, involving two of the largest economies in the world, the United States of America (US) and the European Union (EU). Its aim is to reduce the already low trade barriers to zero and protect, as well as encourage, investments on both sides of the Atlantic, by encouraging trade facilitation and job creation.

Cooperation between the two partners has a long history but the predecessor of the TTIP can be considered the Transatlantic Declaration signed in 1990 by then European Community and the US. The initiative continued by creating a pressure group of business people under the coordination of public authorities in 1995. Communication and cooperation continued between Europe and the US by creating firstly, the Transatlantic Economic Partnership, and subsequently the Transatlantic Economic Council (Gotu, 2016).

It can be said that the idea of signing the TTIP follows the growing trend of transcontinental bilateralism which implies that agreements are increasingly signed among partners that are not on the same continent.

TTIP is designed to have 24 chapters divided into four parts (European Commission, 2016): (1) market access, (2) regulatory cooperation and technical barriers to trade, (3) trade rules and (4) institutional provisions. The first part includes tariffs on trade in goods, services, procurement and rules of origin. The second part includes the areas of regulatory coherence, technical barriers to trade, food safety and animal and plant health, information and communication technology and pharmaceuticals. The third part covers areas such as sustainable development and trade facilitation, small and medium sized enterprises, investment protection, competition, intellectual property rights, etc. The fourth part includes institutional, general and final provisions that determine or regulate the governing body, decision-making process, fulfilling commitments, the possibility of future accession of new members to the agreement and the like.

According to some estimates, the comprehensive agreement will lead to an increase in gross domestic product (GDP) of 119 billion euros in the EU and 95 billion in the United States (European Economic and Social Committee, 2014). However, the expected effects of the tariff removal are not so large, as tariffs between the US and the EU are already low. The exception is the liberalization of trade in several sensitive sectors or product groups (such as textiles). The reduction of non-tariff barriers could have a much greater effect (Felbermayer Gabriel and Mario Larch, 2013). So, significant gains are expected from the removal of non-tariff barriers and harmonization of standards that currently represent an impediment to trade, investment and public procurement.

Motivation for the Trans Pacific Partnership and the Transatlantic Trade and Investment Partnership

In order for integration to be successful, mutual respect, equality, mutual trust, mutual benefit and

‘win-win’ cooperation are needed. In addition to this, fostering of economic development, political and social stability, the growth of trade and technological progress should be present in all member states. This implies that integration should bring about greater benefits to its members than the costs.

Many speculate about the motivation behind TPP and TTIP. In general, debates on how to frame the two agreements fall into three broad categories (Griffith Melissa, Richard Steinberg, and John Zysman, 2015): (1) trade and investment liberalization, (2) geo-economic motivation, and (3) geo-strategic motives.

Reducing regulatory and other barriers promises more competitive markets, lower prices, and broader diffusion of innovations and enhanced consumer welfare (Bull et al. 2015). Moreover, three primary matters are often seen to be driving incremental liberalization (Griffith, Steinberg, and Zysman, 2015). First, efficiency gains from liberalization improve welfare. Second, there are over 500 free trade agreements in the world. This “spaghetti bowl” of agreements is increasingly detrimental to businesses that now face more complexities and associated transaction costs that are difficult to navigate. The emergence of TPP and TTIP represent an attempt to address the complex network of trade regimes that ultimately failed to converge with the multilateral system. Third, while both the EU and the US have pursued free trade agreements, they have not done so at similar rates. Their agreements are not equally distributed across liberal economies and the EU is covering a larger number of countries, and scope of global trade. These differences in the scope and distribution of trade agreements may undermine the US attempts to push its own politics globally. Overall, it is probable that the effects of these two mega-regionals will be smaller than firstly expected, partially because all members included are already members of the WTO, so there is already substantial market access and liberalization in place.

Geo-economically, the TPP and the TTIP may be leveraged to bolster the Washington Consensus through plurilateral agreements, outside the WTO (Griffith, Steinberg, and Zysman, 2015). The two agreements may become the basis for new multilateral trade regime. That regime might be either very attractive to other states or it can strengthen standards from which no other WTO member can afford to be excluded. This includes China, Brazil, India and Russia, which are absent from these agreements. Remaining outside these structures could lead to significant trade and investment diversion, pressuring them to adopt some tenets of deep liberalization in order to gain entrance.

Many analysts point out that the TTIP and TPP will ensure that the US and Europe remain “standard makers, rather than standard takers” in the global economy, subsequently ensuring that producers worldwide continue to gravitate towards joint US-EU standards (Yong Wang, 2014). Under this view, the rise of mega-regionals could diminish the role of the WTO and undermine multilateralism.

Geo-strategically, the emergence of the two mega-regionals has been framed by some as an attempt to contain rising powers, particular China and Russia, or an attempt to reinforce traditional security alignments (Griffith, Steinberg, and

Zysman, 2015). TTIP especially is perceived as a return of the transatlantic community and a commitment to a core transatlantic pole in world politics. Through TPP, the US and Japan seek to enlist other Pacific Rim countries in economic integration and governance reform to counter China, as well as to promote their respective economic objectives (Bull et al. 2015). However, the arguments that these mega-regionals are an attempt to contain emerging powers such as China or Russia does not make much sense considering that TPP and TTIP are being negotiated and ratified at similar time and they will have to coexist.

Nonetheless, mega-regional agreements are necessary for effective regulatory implementation and enforcement when goods and services, such as pharmaceuticals, food, automobiles, banking, air travel and others cross borders through supply chains. In addition to strengthening regulatory programs, mega-regionals can economize scarce regulatory resources by sharing the burden among regulators of multiple trading partners (Bull et al. 2015).

POTENTIAL IMPACT OF MEGA-REGIONALS ON THE MULTILATERAL TRADING SYSTEM

Trade liberalization in the past decade or so, has consisted of three parts: deep regional trade agreements, bilateral trade agreements and unilateralism. Unilateralism is not a threat to multilateral trade system under the WTO. Similarly, bilateral agreements have long coexisted with the WTO. Deep regional agreements and mega-regionals however, are likely to erode, or at least change the WTO's central place in world trade governance (Baldwin Richard, 2014). Some believe that proliferation of regional trade agreements could eventually lead to reexamination of the WTO trading system. Mega-regionals are therefore seen as a way around the WTO consensus requirements.

The analysis of the relation between regional trade arrangements and multilateral trade regimes imposes three key results (Estevadeordal Antoni and Kati Suominen, 2006):

1. Temporal interaction: the largest waves of regional trade arrangements occurred at the time of problems and failure of multilateral trade agreements. This does not mean that the number of regional trade arrangements increases only when there is a shortfall in the progress of multilateral agreements. Historically speaking, there is a parallel increase in the degree of trade liberalization at both, multilateral and regional levels.
2. Geographical fault lines of trade agreements: there is transcontinental bilat-

eralism. The countries are increasingly concluding agreements with partners across the oceans. Regional trade integration has globalised.

3. **Comprehensiveness of trade agreements:** the latest wave of regional trade agreements contains highly comprehensive agreements that not only liberalize trade in almost all products, but they also involve the rules on investment, services, state procurements, etc. This particularly refers to the regional agreements concluded in America and Europe.

Considering the TPP, there are chapters with extensive obligations to improve market access for investors, service providers, and e-commerce beyond what the WTO requires. The WTO's General Agreement on Trade in Services created a framework for addressing barriers in this area, but it has done relatively little to reduce them in practice (Elliott, 2016). Under the WTO rules countries use the positive list approach which makes it easier for them to exclude a broad part of their economies from the rules application. The United States has been more successful in pushing the negative list approach to services trade in its bilateral agreements, including TPP. However, as Hufbauer Gary Clyde (2016) states, although the US pushes for negative list approach it has made little in the way of new market opening commitment. Gelpner Anna (2016) concludes that TPP's progress in removing barriers to financial services is incremental but real.

As for investments, the US and other more advanced economies go well beyond the WTO rules. The TPP investment chapters, like the service chapter, adopt a negative list approach, so that economies will be open to foreign investors except for those sectors or investment policies explicitly excluded. The investment chapter allows foreign investors to sue host country governments in certain situations. Over time, investor-state dispute settlement mechanism expanded to include indirect or regulatory expropriation. As a consequence, multinational companies began to use the investor-state dispute settlement mechanism to evoke environmental and health regulations. After a lot of criticism about the dispute settlement mechanism and public health regulation, TPP allows countries to exclude tobacco product control regulation from the investor-state dispute settlement provisions. The TPP includes other notable reforms to investment provisions including the tightening up of language as to what constitutes "fair and equitable treatment" or regulatory appropriation.

In the TPP there are new chapters on development, competitiveness and business facilitation, small and medium sized enterprises, and regulatory coherence that generally call for increased transparency, dialogue and cooperation. The TPP suc-

ceeded in creating new enforceable disciplines on digital trade and state-owned enterprises, as well as new provisions regarding customs and trade facilitation, but the chapter mostly mirrors the WTO agreement on trade facilitation. Other chapters not subject to dispute settlement include the WTO-extra chapters on competition policy and capacity building, as well as transparency and anti-corruption chapter (Elliott, 2016).

The chapter on sanitary and phytosanitary standards, covering food, plant, and animal safety goes beyond the previous approach of simply affirming each party's commitments under the WTO provisions. However, given the deep political sensitivities around food safety, it remains to be seen how countries will implement and enforce these new commitments under the TPP.

The chapter on e-commerce also goes beyond the WTO rules in creating binding obligations in a new area of increasing importance. Besides the existing practice of prescribing tariffs for e-commerce products and providing for non-discriminatory treatment for digital products crossing borders, the TPP creates binding rules to ensure free cross border flow of data and discourages localization requirements that tend to be arbitrary or discriminatory. Branstetter Lee (2016) notes, however, that the TPP leaves the content of those regulations to national governments, which consequently leaves space for conflicts arising from different levels of national privacy protection.

The chapter on state-owned enterprises is the only completely new chapter that is legally binding and subject to dispute settlement procedures. However, some authors believe that provisions in the mentioned area, including for sovereign wealth funds, are so weak and the exceptions are so broad, that the US negotiators should reopen the chapter so it would not become a negative precedent (Scissors Derek, 2015).

The TPP pushed forward in some areas of labor and environment regulation relative to previous agreements, most notably in the area of intellectual property rights. Only in few areas new provisions are added, such as addressing forced labor. The TPP explicitly prohibits the waiving or relaxation of labor laws in export processing zones. In addition to these general provisions, the US negotiated bilateral plans with Brunei, Malaysia, and Vietnam to ensure the consistency of their laws with international standards.

Considering environmental provisions, instead of requiring that parties adopt and implement seven specified environmental agreements (as it was done in the

US preferential trade agreements), in the TPP member countries are obligated to enforce only three (Elliott, 2016): the Convention on International Trade in Endangered Species, the Montreal Protocol on Ozone Depleting Substances, and the agreement on marine pollution.

Considering the TTIP agreement, since tariffs in both markets are low and two-way direct investment are high, the main goal is not to eliminate traditional trade barriers but to effectively regulate trade remedies which could be an area of substantial gains for bilateral trade relations. However, there are two implications of market access negotiations for third countries (Elliott, 2016). The first is that the TTIP is unlikely to eliminate barriers on sensitive agricultural products or to address domestic subsidies, thereby emphasizing the meagre prospects for progress on these issues at the global level. Second, strict rule of origin could disrupt supply chains to the detriment of developing countries exporters.

On services and investment, the US and the EU take different approaches. As mentioned, the US takes the negative list approach, whereas the EU takes the positive list approach. As Francois Joseph, Bernard Hoekman and Doug Nelson (2015) conclude, if the EU and the US negotiators are unwilling to negotiate much liberalization in services sectors where it really matters, that is, where barriers are relatively high then the TTIP will not have much influence in this area.

On regulatory cooperation, the two parties again have different approaches. US negotiators are primarily interested in agreeing on a process-oriented agreement on horizontal regulatory coherence, while the EU negotiators want to go further and encourage greater convergence in regulatory cooperation. Conclusively, TTIP chapter on regulatory coherence, including sanitary and phytosanitary regulation, is likely to be excluded from formal dispute settlement, as with the TPP chapter.

Another aim of the TTIP is to agree on standards that will possibly become global. However, developing countries are concerned that they will not have a voice in the negotiations of these standards and that these may be inappropriate for poorer countries.

Areas of labor and environment are regulated in a similar way in the two regions, except that the core provisions in the US trade agreements are enforceable under the same dispute settlement procedures as the rest of the agreement, whereas in the EU preferential trade agreements those are not enforceable. It is important

to notice that no matter how the enforcement matter will be negotiated, provisions in both, the US and the EU trade agreements, are based on international standards propagated by the International Labor Organization or on multilateral agreements in these areas.

In any case, it is clear that revision of the WTO system is necessary because if the mentioned mega-regionals come into force, they will account for a majority of international trade value (Brouse Kelly, Vy Nguyen and Sarah Lohschelder, 2015). Furthermore, if China and India join the TPP agreement then the discussion could return to the WTO because there is no use in having regional trade agreements when everyone is party to these agreements (Brouse, Nguyen and Lohschelder, 2015).

Meanwhile, currently existing or negotiated mega-regionals exclude some 160 world countries and their responses are to be expected. Since any response requires long lead times, many of the excluded countries may decide to wait and see further developments before they react. Also, since any response requires commitment of negotiating resources and political capital, the excluded countries will be inclined to look for strategies that are robust to the many possible outcomes (Dadush Uri, 2014).

While much of the impact on excluded countries will occur in specific sectors and thus call for monitoring of the provisions being negotiated on the micro level, there may also be some systematic effects of the mega-regionals on global trade rules and standards. The adoption of new standards will be of great significance to exporters and import competing firms around the world (Dadush, 2014).

CONCLUSION

The debate over the role, success and coexistence of multilateralism and regionalism is not new. However, one has to recognize that the environment in which countries perform is constantly changing and thus the rules and approaches to trade have to be adequately modified.

Both multilateralism and regionalism have their opponents and advocates. The opponents to regionalism believe that regional trade agreements bring about a diversion in trade and reduce the total benefit for global trade compared to multilateral trade liberalization. Regional trade agreements may also reduce the

initiative of countries for multilateralism and complicate multilateral trade negotiations. The advocates of regionalism claim that regional trade agreements are a form of transition towards multilateralism and a multilateral trade system. They believe that the initiatives for regional and multilateral integration are mutual complements, rather than an alternative to opening to trade. On the other hand, there are views that multilateralism is the most effective way to structure international relations and to solve problems and challenges in many fields.

Although many arguments can be given for both approaches one has to recognize that the number of regional trade agreements is increasing and regionalism is becoming widely accepted trend. The response to the regional trade agreements, especially mega-regionals, will mostly depend upon the effect on third countries trade interests. When considering mega-regionals such as TPP and TTIP, it is expected that most of the export sectors will not be affected since tariffs among members are already low. The effect of reducing non-tariff barriers is expected to be larger and will depend upon the scope of barriers and divergence in regulation. Positive effects are anticipated via income effect. If the TPP and the TTIP come into force, the US and the EU are likely to become richer and increase their production, as well as demand for goods and resources, thus countries within the American and European production chain will also experience benefits from increased demand.

Since it is expected that over time many of the excluded emerging economies will become a part of some mega-regional agreement, it is not likely that new global standards and rules will be created solely on a regional but rather on a multilateral level. Thus, regionalism and multilateralism are expected to continue to coexist.

BIBLIOGRAPHY

- Baldwin, Richard. 2014. "The systematic impact". In: *Mega-regional trade agreements, game changers or costly distractions for the world trading system?* World Economic Forum.
- Baldwin, Robert. 1993. "A Domino Theory of Regionalism." NBER Working Paper Series No. 4465. NBER.
- Baldwin, Richard, and Dany Jaimovich. 2010. "Are free trade agreements contagious?" NBER Working paper 16084. National Bureau of Economic Research, Cambridge, Massachusetts.
- Branstetter, Lee. 2016. *TTP and digital trade*. In: *Assessing the Trans-pacific Partnership*. Vol. 1. PIIIE Briefing 16-1. Peterson Institute for International Economics, Washington.
- Brouse, Kelly, Vy Nguyen, and Sarah Lohschelder. 2015. "CETA, TPP, TTIP and the Canada-U.S.

- trade relationship". CUSLI expert group roundtable report. *Canada-United States Law Journal*, 39: 1-6.
- Bull, Reeve T, Neysun Mahboubi, Richard B. Stewart, Jonathan B Wiener. 2015. "New approaches to international regulatory cooperation: the challenge of TTIP, TPP and mega-regional trade agreements". *Law and Contemporary Problems*, 78 (1): 1 -29.
- Ciuriak, Dan, and Natassia Ciuriak. 2016. "Regulatory Coherence and the Trans-Pacific Partnership." *Canadian Business Law Journal* 58(3).
- Cheong, Inkyo. 2013 Negotiations for the Trans-Pacific Partnership Agreement: Evaluation and Implications for East Asian Regionalism. <http://www.adbi.org/files/2013.07.11.wp428.trans.pacific.partnership.east.asian.regionalism.pdf> [3 January 2014].
- Coldicott, Dean. 2004. "Norm Formation and Complex Multilateralism in the World Trade Organization". The Globalism Institute. <http://rspas.anu.edu.au/ir/Oceanic/OCIS Papers/Coldicott.pdf> [16 February 2010].
- Crawford, Jo Ann, and Sam Laird. 2000. "Regional Trade Agreements and the WTO". Research Paper No. 00/3, Centre for Research in Economic Development and International Trade.
- Dadush, Uri. 2014. "Possible responses to mega-regionals by excluded countries". In: Mega-regional trade agreements, game changers or costly distractions for the world trading system? World Economic Forum.
- Eicher, Theo S., Christian Henn, and Chris Papageorgiou. 2012. "Trade creation and diversion revisited: accounting for model uncertainty and natural trading partner effect". *Journal of Applied Econometrics*, 27 (2): 296-321.
- Elliott, Kimberly. 2016. "How much „mega“ in the mega-regional TPP and TTIP: implications for developing countries". CGD Policy Paper 079. Center for Global Development.
- Estevadeordal, Antoni, and Kati Suominen. 2006. Regional Trade Agreements and Global Cooperation. http://www.iadb.org/intal/aplicaciones/uploads/ponencias/Foro_INTAL_2006_11_03_Estevadeordal-Suominen.pdf [24 June 2015].
- European Commission. 2016. EU negotiating text in TTIP. <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1230> [10 July 2016].
- European Economic and Social Committee. 2014. "Opinion of the European Economic and Social Committee on Transatlantic trade relations and attitudes". EESC on enhanced cooperation and a possible free trade agreement between the EU and the United States. Brussels.
- Felbermayer, Gabriel, and Mario Larch. 2013. "Transatlantische Handels und Investitionspartnerschaft: weiche effekte sind su erwarten?" *Ifo schnelldienst* 6/2013: 3-6.
- Francois, Joseph, Bernard Hoekman, and Doug Nelson. 2015. "TTIP, regulatory diversion and third countries". In: Sait Akman, M., Evenett, SJ., Low, P. (Eds) *Catalyst: TTIP 's impact on the Rest*. CEPR Press, London.
- Gelpern, Anna. 2016. "Financial services". In: *Assessing the Trans-pacific Partnership*. Vol. 1. PIIIE Briefing 16-1. Peterson Institute for International Economics, Washington.
- Gotu, Ioana. 2016. *The TTP and TTIP trade agreements: the international negotiation process*. Vol. VIII, Issue 1, Center for Economic Studies.

- Griffith, Melissa K., Richard Steinberg John, Zysman. 2015. "Great power politics in a global economy: origins and consequences of the TPP and TTIP". Proceedings of the conference Unpacking the Transatlantic Trade and Investment Partnership Negotiations, Bruxelles, October 17 2015.
- Hettne, Bjorn, Andras Inotai, and Osvaldo Sunkel. 1999. *Globalism and the new regionalism*. London: Macmillan Press.
- Hoekman, Bernard, and Alan L. Winters. 2007. "Multilateralizing „Deep Regional Integration“: A Developing Country Perspective". Proceedings of the conference on Multilateralizing Regionalism, 10 December, 09. Geneva.
- Hufbauer, Gary Clyde. 2016. "Liberalization of services trade". In: *Assessing the Trans-pacific Partnership*. Vol. 1. PIIE Briefing 16-1. Peterson Institute for International Economics, Washington.
- Krause, Joachim. 2004. "Multilateralism: Behind European Views". *The Washington Quarterly*, 27 (2): 43-59.
- Krishna, Pravin. 1998. "Regionalism and Multilateralism: A Political Economy Approach". *Quarterly Journal of Economics*, 113, (1): 227-250.
- Lawrence, Robert Z. 1995. *Regionalism, Multilateralism and Deeper Integration*. Brookings Institution, Washington.
- Levy, Philip I. 1997. "A political-economic analysis of free-trade agreements". *American Economic Review*, 87 (4): 506-519.
- Matthews, Alan. 2003. "Regional Integration and Food Security in Developing Countries". Food and Agriculture Organization of the United Nations training materials for agricultural planning 45. FAO, Foma.
- Melendez-Ortiz, Ricardo. 2014. "Setting the Stage". In: *Mega-regional trade agreements. Game changers or costly distractions for the trading systems*". World Economic Forum.
- New Zealand Ministry of Foreign Affairs & Trade. 2005. Trans-Pacific Strategic Economic Partnership Agreement. <https://www.mfat.govt.nz/en/about-us/who-we-are/treaty-making-process/trans-pacific-strategic-economic-partnership-tpsep-or-p4/> [5 July 2016].
- Organization for Economic Cooperation and Development. 2003. Regional Integration Agreements. <http://www.oecd.org/dataoecd/39/37/1923431.pdf> [5 June 2010].
- Panagariya, Arvind. 1998 The Regionalism Debate: An Overview. [http://www.columbia.edu/~ap2231/Policy%20Papers/overview-we\(1\).pdf](http://www.columbia.edu/~ap2231/Policy%20Papers/overview-we(1).pdf) [22 February 2015].
- Scissors, Derek. 2015. *Grading the Trans-Pacific Partnership on Trade*. Washington: American Enterprise Institute.
- United States Trade Representative. 2013. TTIP: list of lead negotiators, fact sheet. United States Trade Representative. <https://ustr.gov/sites/default/files/lead%20negotiators%20list%20TTIP.pdf> [22 July 2016].
- Velde, Dirk Willem, and Miatta Fahnbulleh. 2003. "Investment related provisions in regional trade agreements". Paper prepared for the project on Regional Integration and Poverty, EP/R03/013, funded by UKDFID under the EC-PREP programme. <http://www.odi.org.uk/resources/download/1299.pdf> [24 June 2010].

Yong, Wang. 2014. "The political economy of the rise of mega-regionals". In: *Mega-regional trade agreements, game changers or costly distractions for the world trading system?* World Economic Forum.

EFEKTI MEGA-REGIONALNIH SPORAZUMA NA MULTILATERALNI TRGOVINSKI SUSTAV

Vlatka Bilas, Sanja Franc

Sažetak: *Cilj ovog rada je ispitati motive i posljedice sklapanja mega-regionalnih trgovinskih sporazuma na multilateralni trgovinski sustav koristeći pritom primjere Trans-Pacifičkog Partnerstva (TPP) i Transatlantskog sporazuma o trgovini i investicijama (TTIP). Multilateralizam i regionalizam, iako suprotni trendovi, koegzistiraju istovremeno. Mnogo je argumentata u korist oba pristupa, no činjenica je da je broj regionalnih trgovinskih sporazumima u porastu i da regionalizam postaje široko prihvaćen trend. Odgovor na regionalne trgovinske sporazume, a osobito na mega-regionalne sporazume, uglavnom će ovisiti o učinku na trgovinske interese trećih zemalja. Kada je riječ o mega-regionalnim sporazumima poput TPP-a i TTIP-a, očekuje se da većina izvoznih sektora uključenih zemalja neće biti pogođena, jer su carine među zemljama članicama ionako niske. Upravo stoga se očekuje znatno veći učinak od smanjivanja neocarinskih prepreka i ovisit će o obuhvatu prepreka te razlikama u regulaciji. Pozitivni učinci očekuju se putem dohodovnog učinka. Naime, hipotetski gledano, nakon što sporazumi stupe na snagu, SAD i EU će vjerojatno da će postati bogatije i povećati svoju proizvodnju, kao i potražnju za dobrima i resursima, čime će zemlje unutar američkog i europskog proizvodnog lanca također ostvariti koristi od povećane potražnje. Budući da se s vremenom očekuje da će većina trenutno isključenih zemalja u razvoju postati dio nekog mega-regionalnog sporazuma, nije vjerojatno stvaranje novih globalnih standarda i pravila isključivo na regionalnoj, već ipak na multilateralnoj razini. Dakle, može se zaključiti da će regionalizam i multilateralizam i dalje istovremeno koegzistirati.*

Ključne riječi: *mega-regionalni sporazumi, multilateralni trgovinski sustav, TPP, TTIP*

JEL: F15