

Forming a Mega-Competitive QUINTET : Place of China and India

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Abstract

The traditional TRIAD Power anchored by Japan, USA[NAFTA], Germany[EU-4] - referred to here as JUG - boasting the three largest global economies for over three decades, is now joined by the powerhouses of China and India to form the QUINTET. During the last 30 years the weight of the world economy has gradually shifted from the USA and industrial giants of Europe [EU-4] to Japan, signifying the concentration of economic and trade prowess in a TRIAD, which currently is reshaped

*by emerging mega-competitive China and India. The paper examines the roles and concentration of economic power in a QUINTET that will guide the distribution of a larger share of world output [GDP], global trade, investment flows, mergers and acquisitions and foreign exchange reserves featured by the sum of competitive advantages of the QUINTET vs. TRIAD. QUINTET's power has resulted in advancing Free Trade Agreements [FTAs] in this e-global age where technologies and information flows are borderless. The paper also identifies the *raison d'être* for Free Trade Agreements, growth of Regional Economic Cooperation [REC] - APEC's success as a New Model and SAARC's constraints to form a FTA, economic impact of FTAs and policy implications for the respective FTA countries, and the rest of the world. The RECs and FTAs in effect are portrayed to highlight the comparative geographic and economic profiles along with the United Nations and countries of the TRIAD and QUINTET. The expanding global FTA network is pushed by the lagging WTO talks. Also included are Brazil, Russia, India, China, Korea and*

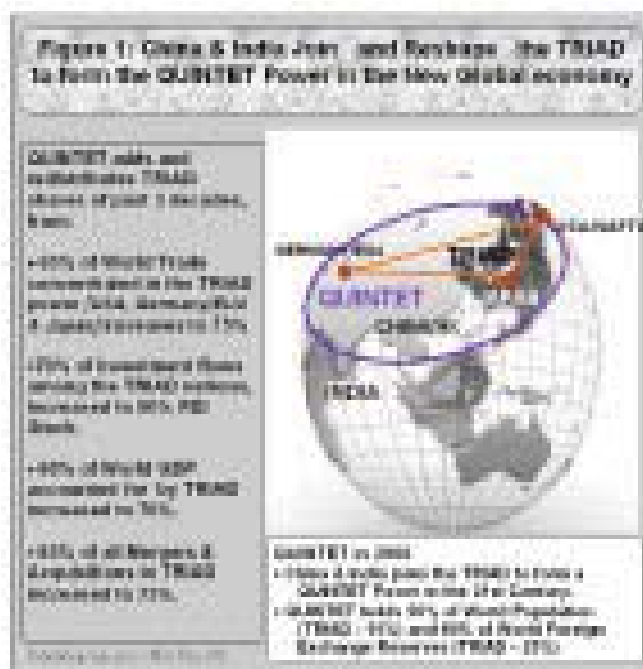
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South Africa [BRICKS]. The continued proliferation of RECs and FTAs as they join the mega-competitive global marketplace is also noted.

Keywords: TRIAD = Japan + USA [NAFTA] + Germany [EU-4]; JUG = Japan + USA + Germany, QUINTET = TRIAD + China + India, Emerging Markets, Regional Economic Cooperation [REC] Free Trade Agreements [FTA] APEC; SAARC; ASEAN; BRIC = Brazil + Russia + India + China, BRICKS = BRIC + Korea + South Africa

1. Introduction

For over a century the United States has been the largest economy in the world. Major shifts have, however, been under way progressively during the past 30 years. These trends will continue in the 21st century, bringing about a historic transformation of the world trading system and creating a new global economy. This has changed from the traditional TRIAD^[26] to a new conglomeration with the emergence of China and India, converting the new economy and world trading system into a new QUINTET^[10]. The industrialized countries of Europe have seen the greatest decline in global GDP share by 4.9 %, followed by the US and Japan with a decline of about 1% each. Since 1990, within Asia the declining global share of Japan has



*Expanded version of a paper "Mega-Competitive QUINTET Reshapes TRIAD Power and Advances FTAs in the E-Global Age" presented at Pan Pacific XXV Confab in Costa Rica 2008. Author information follows references.

been more than made up by the rising share of China and India. *ASEAN* countries and South Korea, along with China and India, contributed to the rising share of Asia in world *GDP* and significant growth in trade with a proliferation of FTAs. In the 1990s, Japan's share of world *GDP* fell by 1% while that of South Korea, *ASEAN*, India and China rose by 1%, 1.2%, 2.2% and 9.2%, respectively. Thus, Virmani [2005] says: India's gains since 1980 have been much larger than *ASEAN's* and South Korea's but much less than those of China. In 2007 China and India recorded impressive *GNP* growth rates of 11.5% and 9.0% respectively. In 2007 China led industrial production with an increase of 17.3% change one year ago, India 11.8%, Germany 6%, Japan 4.7% and US 2.1%^[45]. In this highly uncertain global environment of 2008 and 2009, world output is expected to grow by around 3 per cent in 2008, almost one percentage point less than in 2007, and in developed countries, *GDP* growth is likely to fall to about half this rate. By contrast, growth in emerging and newly developing countries can be expected to remain about 5-6% or even higher by India and China [7-9%], the new *QUINTET* global powers, during 2009-2012.

At the start of the new millennium, USA, the largest economy, was more than twice the size of the next largest economy, Japan, and nearly twice that of China plus Hong Kong, and nearly three times that of Germany. The emerging fourth largest economy, India, is a little over one-quarter the size of the US economy. USA, Japan and Germany anchored in the *TRIAD* with concentrated economic and competitive power in the mid 1980s through 1990s; is now joined by China and India to form a mega-competitive *QUINTET* with characteristics anew, as shown in Figure 1.

In the coming years the new global economy will be transformed from the current focus on the *TRIAD* to the *QUINTET*. China and India are the driving forces for change. China is projected to share the enviable position of the two largest economies in the world along with the USA by 2020. Though India is not too far behind China, its share in world *GDP* will continue to grow. In another decade, with current trends and sustained economic growth, India's economy will become larger than that of Japan, thus taking it to the third place, behind the USA and China. The incremental impact of the Indian economy on the rest of the world through trade, and other non-resident income (NRI) and FDI investment flows, contributing to *GDP* at the current exchange rate are taken into account. By the end of the decade, China and India are poised to become a larger driver of global growth than the European Union's six largest economies. The combined impact of the Asian giants China [+Hong- Kong] and India will exceed that of Japan, USA and Germany, the current powerhouses in exports dominating the world trading system of yester-years. It is noteworthy that the South Korean economy leading in a number of industrial and trading sectors, in contrast is expected to grow and join the major world trade players, and extend the *BRIC* concept to form the *BRICK* with Korea's participation, and to expand to *BRICKS* adding resource-rich South Africa, a leading economic reformer in Africa.

As we approach the final years of the first decade of the 21st century, the largest shares of the world output [*GDP*], trade and investment have been shared by the US [*NAFTA*], Japan, China, India, and Germany {+*EU4*} forming a *QUINTET*, replacing the traditional *TRIAD*. The *QUINTET*, with a much larger share of world population, a rapidly growing middle-class with enhanced propensity to consume, diffused international relations forte, is advancing the global presence

in new bilateral ventures via a large number of Free Trade Agreements [FTA], and rapid growth of information technology sectors in the e-global age.

The FTA bilateral partnerships are increasingly giving e-global age 'born-global' entrepreneurs who are among the most intensive users of the internet/web new opportunities for global trading, supply chaining and customer services. E-business levels the playing field for all categories of companies to compete. E-business drives the firm's globalization activities across geography and time zones performing work components around the world all day and night every day. The FTA business partners engaging in e-business can benefit as follows^[49] :

"First, it increases productivity and reduces transactional costs in worldwide value-chain activities through online integration and coordination of production distribution and after-sale services. Second, it creates value for existing customers and uncovers new sales opportunities by increasing customer focus, enhancing marketing capabilities, and launching entrepreneurial initiatives. A key benefit is the ability to implement marketing strategy on an international scale and integrate customer-focused operations worldwide... Third, it improves the flow of information and knowledge throughout the firm's worldwide operations. The internet allows the firm to move information quickly throughout its operations worldwide, and to interact more effectively with customers, suppliers, and partners."

The Internet is stimulating economic development and a massive global migration of jobs, particularly in the services sector. Business Communications and information technologies are now in the process of connecting all of the knowledge pools in the world together.^[14] As a result, much of the written documentation in conducting business abroad will be accessible online.

The eight years of the 21st century is a prelude to *QUINTET*'s ability to redefine comparative and competitive advantage that enables a finale, by 2010, to record China plus Hong Kong to be the world's largest exporter. Current economic growth trends indicate that China and India are to be the 2nd and 3rd largest economies closer to USA rather than any one being first, replacing Japan and Germany around 2015. However, China and India may fall short of alleviating total poverty, expanding infrastructure to bring a balance between rural and urban sectors to comparable levels with distribution of income and enhance consumption consistent with quality of life aspirations of the countries to be replaced. These questions are raised because of the colossal size of China's and India's well over a billion population each. Similar questions did not arise in the take-off paths to economic development by Japan, Korea, Taiwan, Hong Kong, and Singapore. The projected changes in the relative size of *QUINTET* economies will have profound implications for global governance, the global balance of power, and the stability of Asia. Forecasts of continued phenomenal growth of China and India, are in the offing, forcing a new wave of global mega competition and redirection of the flow of goods and services in the world trading system to challenge traditional theories and say 'you ain't seen nothing yet!

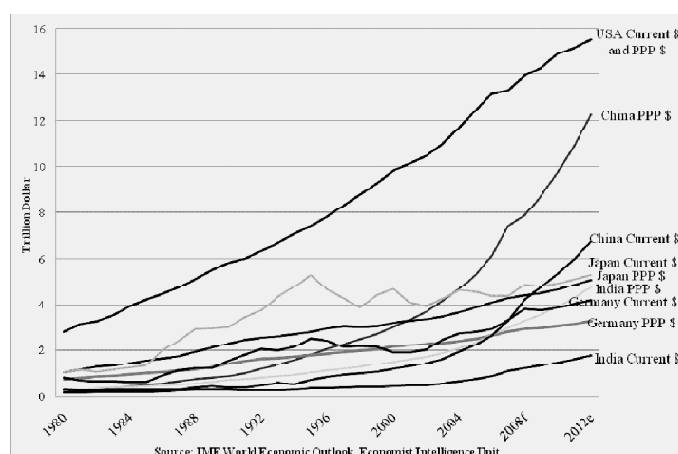
2. The Sum of Competitive Advantages of the QUINTET vs. TRIAD

Kenichi Ohmae [1985] postulated the *TRIAD Power: the Coming Shape of Global Competition* with Japan becoming the 2nd largest global economy; and now more a reality in the late 2000s by the strategic significance of USA [NAFTA] Germany [+EU4] Japan, China [+HK] and India forming the author's postulation of the *QUINTET*, where:

1. Mega-competition is conspicuous, more so than experienced in the *TRIAD*, because the *QUINTET* commands a much larger population of nearly 50% of world's total compared to less than 15% in the *TRIAD*;
2. The *QUINTET* nations have proliferated Free Trade Agreements and accounts for over 50% share of an estimated 184 FTA's in force and FTA enactments already signed. Nearly 100 FTAs are being negotiated due to complexities and delays in WTO negotiations;
3. Globalization is becoming unstoppable, exploring markets inescapable and integration is irresistible and where competition is more intense, yet more cooperative in FTA areas;
4. A greater middle class with increased purchasing power - the customer more universal, yet more distinct in taste and preferences, intelligent and knowledgeable in consumer choices;
5. Expanded R&D centers emanate new technologies translated to consumer products resulting in competitive challenges in many industrial and commercial products;
6. Over 60% of the world's foreign exchange reserves are accumulated and increasing in *QUINTET*;
7. Over 65% of world trade now transacted in *TRIAD* to be increased to 75% and redistributed among *QUINTET*;
8. Over 60% of world's GDP now produced by *TRIAD* to be increased to 70% and redistributed among *QUINTET*;
9. Over 70 % of current Foreign Direct Investment inflows and outflows has increased FDI stock to 80% in *QUINTET* (with significant in flows as well as out flows recorded by China and India);
10. Over 65 % of all mergers and acquisitions are expected to rise to 75% to increase productivity and profits of existing industries;
11. China's and India's addition to the scene has brought about entrepreneurs, beyond the public sector bureaucratic administrators, to compete in a new independent and interdependent business environment, and correspondingly expanding SME growth;
12. China price competes in manufacturing as China has acquired the status of the world's manufactory, joining the *QUINTET* as a major global supply chain player;
13. India sets the price for IT professional services by sharing technologies and skills.
14. Germany competes as the largest exporter three years in a row;
15. China and Hong Kong SAR became the 2nd largest exporter and becomes 1st by 2009-10;

16. USA drops to third place in exports, yet remains #1 importer in the world and resultant chronic largest imbalances in trade and current account;
17. Japan, Germany and China contribute positively to trade and current account balances to offset USA's deficits within the *QUINTET*;
18. Japan sets the price of automobiles, leading the industry with Toyota leading sales in USA and a major competitor in expanding auto manufacturing/sales in China and India as well as North America and Europe;
19. China attracts record FDI mainly from *QUINTET* colleagues related to manufactured exports cementing export led growth;
20. India operates the largest outsourcing ventures and gears FDI to generate local consumption;
21. China has the largest domestic savings and Foreign exchange reserves of nearly \$2 trillion;
22. Japan follows with nearly \$1 trillion in foreign exchange reserves and accumulated trade and current account balances;
23. Japan's domestic savings of nearly \$3 trillion have built the largest Postal Savings Bank;
24. In today's e-global age, the *QUINTET* dominates the mobile phone user market with China +Hong Kong and India as leaders followed by the US, Japan and EU. India's subscriber additions of 2006 totaled 73.6 million, up by 10% from 2005 and total subscribers 140 million (by 2006). China added 67.7 million in 2006 up by 17% and total subscribers in 2006 recorded 461 million; and .
25. The *QUINTET* inherits the largest skill-base of engineers, scientists and managerial expertise with China and India annually graduating twice the number of engineers and scientists compared to the *TRIAD*.

Figure 2: QUINTET Nations GDP at Current \$ & PPP \$ (1980-2012f)



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Figure 3: Competitive Economic & Trade Strengths of QUINTET Players USA, Germany, Japan, China+HK, India, 1950-2008 {\$billion}

Country		Year										
	Trade Facts	1950	1960	1970	1980	1985	1990	1998	2000	2005	2007	2008e
U.S.A.	Exports	10.3	20.6	43.2	225.6	218.8	393.6	682.1	782.0	858.2	1024	1301.6
	Imports	9.6	16.4	42.4	257.0	352.5	517.0	944.4	1259.0	1732.7	2020.4	2214.7
	Trade Balance	0.4	3.3	0.8	-31	-134	-123	-262	-477	-825	-854	-913
	Current Account	1	3	2	2	-118	-79	-214	-417	-729	-731	-665
	Per Capita*('000)	1.8	2.8	4.9	12.2	17.7	23.2	31.6	34.7	41.9	45.7	46.5
	PerCapPPP+('000)	1.8	2.8	4.9	12.2	17.7	23.2	31.6	34.7	41.9	45.7	46.5
Germany	Exports	1.9	11.4	34.2	192.8	183.9	421.1	543.8	551.8	970.9	1326.4	1624.5
	Imports	2.7	10.2	29.9	188.0	158.4	355.7	471.5	497.2	777.1	1058.6	1176.6
	Trade Balance	-0.7	1.2	4.3	4.9	25.4	63.9	72.2	54.6	194	266	448
	Current Account	1	2	1	-14	17	45	-16	-33	145	252	279
	PerCapita*('000)	0.3	0.9	2.3	10.7	8.3	19.5	26.6	23.1	33.8	40.4	46.4
	PerCapPPP+('000)	0.2	0.7	1.8	9.7	13.4	17.9	24.1	26.2	30.4	34.2	35.5
Japan	Exports	0.8	4.1	19.3	130.4	177.1	287.5	387.9	479.2	594.9	712.8	822.5
	Imports	1.0	4.5	18.9	141.3	130.5	235.4	280.5	379.5	516.7	621.1	681.5
	Trade Balance	0.1	0.4	0.4	-10.9	46.7	52.2	107.4	99.7	79.9	89.8	141
	Current Account	0	0	1	-11	51	44	119	120	166	211	194
	PerCapita*('000)	0.2	0.5	1.9	9.0	11.2	24.5	30.6	36.8	35.6	34.2	37.9
	PerCapPPP+('000)	0.1	0.4	1.8	8.9	12.9	18.7	23.8	25.2	30.3	33.5	35.0
China	Exports	0.6	2.6	2.3	18.1	27.4	62.1	183.7	249.2	761.9	1217.8	1464.0
	Imports	0.6	2.6	2.3	19.9	42.3	53.3	140.2	225.1	659.9	955.9	1209.4
	Trade Balance	0	-1	0	-1.8	-14.9	8.7	43.5	24.1	102	262.2	254.6
	Current Account	0.1	0.2	0.1	0.3	-11.5	12.0	31.5	20.5	160.8	371.8	399.3
	PerCapita*('000)	0.05	0.07	0.1	0.3	0.3	0.3	0.8	0.9	1.7	2.4	3.2
	PerCapPPP+('000)	0.04	0.06	0.09	0.3	0.5	0.8	1.9	2.3	4.1	5.3	5.9
Hong Kong	Exports	0.7	0.7	2.5	19.8	30.7	82.2	174.0	201.9	289.3	344.6	367.6
	Imports	0.7	1.0	2.9	22.4	29.7	82.5	184.5	212.8	299.5	367.9	395.8
	Trade Balance	0.0	-0.3	-0.4	-2.7	0.5	-0.3	-10.5	-10.9	-10.2	-23.2	-28.2
	Current Account	0	-1	-1	-1.4	2.6	4.8	2.5	7.0	20.2	28.0	26.2
	PerCapita*('000)	0.1	0.3	0.9	5.6	6.4	13.3	25.3	25.1	25.9	29.7	31.8
	PerCapPPP+('000)	0.1	0.4	1.2	7.2	10.4	16.9	23.2	26.1	35.5	42.1	44.4
India	Exports	1.1	1.3	2.0	8.6	9.1	17.9	33.4	42.3	99.6	145.3	178.9
	Imports	1.1	2.3	2.1	14.9	15.9	23.6	43.0	51.5	142.8	216.6	257.8
	Trade Balance	0.1	-1.0	-0.1	-6.3	-6.8	-5.6	-9.5	-9.1	-43.2	-70.1	-78.9
	Current Account	-1	0	-1	-2.3	-4.2	-7.9	-6.9	-4.6	-10.3	-15.5	-34.6
	PerCapita*('000)	0.05	0.07	0.1	0.2	0.3	0.4	0.4	0.4	0.7	0.9	1.0
	PerCapPPP+('000)	0.06	0.09	0.1	0.4	0.6	0.8	1.2	1.5	2.2	2.8	3.1

Source: IMF World Economic Outlook; UNCTAD Handbook of Statistics. WB & EIU 2008 estimates/forecasts
* Per Capita (GDP in current \$ '000) +PPP Purchasing Power Parity terms

3. The New Global Economy with *QUINTET* Mega-Competitive Power

Brought about by China and India joining the *TRIAD* to form a *QUINTET* and a mega-competitive force in the world trading system, the new global economy has emerged. This new global economy is also emerging to confront business enterprises in the traditional ways of doing business to rethink new paradigms and best practices emanating in companies focusing on core competencies in the light of mega-competition from around the world. Currently China and India and other emerging economies like South Korea, Russia, Brazil and South Africa are assuming leading economic roles challenging established economic powers of the *TRIAD* and even the newly formed formidable *QUINTET* - these five nations have maintained their competitive strength in commanding a larger share of trade, investment and merger and acquisition activity.

4. Globalization & Open Markets Foster Growth

Globalization is based on a simple recipe for success: national economics can accelerate growth by opening up national borders. The larger and more open the markets, the bigger the incentive to unfold individual capabilities and develop innovative new products and procedures. Open countries benefit from the international exchange of ideas and thereby participate continuously in technological progress. This creative technological progress increases productivity and is therefore the key source of long-term economic growth. A higher degree of openness also leads to more competition.

Globalization is not a force of nature but a politically-economically engineered process. The liberalization of international goods, services, investment and capital flows was pushed ahead with the help of the World Trade Organization (WTO), International Monetary Fund and Organization for Economic Co-operation and Development (OECD). Since the middle of the 20th century, a total of eight world trade rounds have resulted in extensive tariff reductions and the lowering of nontariff trade barriers on an international basis. The creation of the European internal market also induced a comprehensive process of regional liberalization. The driver of this next stage in automation is not technology per se, but changes in competition and how businesses operate and execute their strategies. The Internet may be the agent of change, but the engine of change is a need to cut costs and improve core business processes in increasingly competitive global markets. The competitiveness of a country, county or company depends on various factors which include levels of technology, capital, skill differences of labour, the differences in productive capabilities, management and organization, overall industrial imports, factor conditions and industry competition, exchange rate, competition, government policy and expenditure, labour management relationships, globalization, and the influence of multinationals.

5. Implications of the new forces reshaping the global economy

The new global economy is creating business environments that differ radically from those of the past. To survive and prosper in the 2010s companies will need to develop new strategies

and new paradigms. Today all business firms – small or large, domestic or international - must strive for profits and growth in an international economy that features enormous flows of products, technology, capital, and enterprise among countries. Even when companies stay at home, sooner or later they learn from hard experience that there are no domestic markets, only global markets.

Since Kenichi Ohmae's [1985] postulation of the *TRIAD* Power, the anchor countries the USA, Japan and Germany, in that order, have been the largest economies. Figure 3 portrays the competitive economic and trade strengths of *QUINTET* players the USA, Japan, Germany, China+HK, India, 1950-2008.

Many economists reckon that Chinese growth in 2009 will fall well short of the 9 per cent government officials are forecasting. GNP and exports slowed sharply in recent months. However, given the steep declines forecast for many developed economies, China will remain one of the main contributors to global growth. China overtook Germany to become the world's third-largest economy after the Chinese authorities revised upwards the figures for growth during 2007-2008. It is symbolically significant that China is now bigger than Germany and it will not be too long before its economy overtakes Japan. Goldman Sachs forecasts that the Chinese economy will overtake that of the US by about 2040. The Economist Intelligence Unit forecasts in terms of purchasing power parity – which adjusts for price differences between countries to reflect actual buying power of local incomes – China will outstrip the US by 2017. Despite rapid growth and hundreds of millions of people lifted out of poverty, China remains relatively poor. In the World Bank's rankings of GDP per capita for 2008 using purchasing power parity, China is at \$5,900 still performing better than India at \$3,100. China is also close to surpassing Germany to be the world's biggest exporter. The downturn and recession in the USA, Germany and Japan is regarded as the worst since the WWII dragging down economies world-wide, putting pressure on policymakers to implement emergency rescue packages. In addition to stimulus packages, countries around the globe should consider strong and complementary policy actions that help to fix the financial sector meltdown.^[50] If China and India maintain their GDP growth rates as forecasted by IMF and the World Bank, they probably will become the main players of the *QUINTET* in the next 15-20 years.

6. *Raison d'être* for Free Trade Agreements

Free Trade Agreements [FTAs] are a vehicle for countries negotiating bilateral agreements for specific purposes and in many respects pursue similar objectives, viz:^{[21][34]}

- to secure open markets for exports and expand economic growth;
- to eliminate tariffs and nontariff barriers on trade in goods within the FTA, but each country maintains its own trade policies, including tariffs on trade outside the region;
- to protect domestic producers from foreign unfair trade practices and from rapid surges in fairly traded imports.
- to control trade for foreign policy and national security reasons;

- to help foster global trade to promote world economic growth; and
- to deliver benefits either faster or beyond what can be achieved through the WTO.

Figure 4: Trends of FTAs Worldwide, 1955-2008



Source : WTO website (www.wto.org/english/tratop_e/region_e-region_e.htm) as of July 18, 2008.

FTAs permit the products of FTA partners easy access to one another's markets by eliminating tariffs and some nontariff barriers. The 1989 FTA between the United States and Canada was arguably formed for this purpose. Developed countries have also formed FTAs with developing countries to encourage them toward trade and investment liberalization. After the "suspension" of the Doha Round of WTO talks, members shifted their trade focus to bilateral and regional agreements to promote trade and investment [24]. FTAs may be used to protect local exporters from losing out to foreign companies that might receive preferential treatment under other FTAs. In the case of the U.S.-Chile FTA some argued that U.S. firms are at a disadvantage *vice-versa* their Canadian competitors whose exports face no Chilean tariffs under the Canada-Chile FTA. Slow progress in multilateral negotiations has been another impetus for FTAs. For example, when the 1986-1994 Uruguay Round negotiations got bogged down, the impetus for the United States, Mexico, and Canada to form NAFTA seemed to increase. Arguably the surge in FTA formation worldwide in the past few years has been a result of the difficulties encountered in launching and implementing the Doha Development Agenda round of negotiations in the WTO [4].

The WTO reported that since 1995 it has received notification of more than 100 FTAs by 2000, roughly more than double the number that was reported to the GATT from 1947 to 1995. For example, Canada formed an FTA with Chile as did Mexico. The EU has formed FTAs with a number of countries. Japan, which had shunned the use of FTAs, completed negotiations with Singapore and is exploring the possibility of forming an FTA with Korea. FTAs in operation and being negotiated are listed below under QUINTET partners [5].

As of mid-year 2008, 148 free trade agreements (FTAs) [1] were in effect worldwide FTAs (including customs unions, and based on notification to WTO. One of the factors behind this sudden increase in the number of FTAs is the protraction of the previous Uruguay Round and the current Doha Round (New Rounds). At present, as many as 153 countries have joined the WTO, making the formation of consensus in the New Rounds more difficult. When the multilateral trade negotiations fail to show progress, FTAs are sometimes found more reasonable to the countries seeking access to overseas markets as they can be negotiated with more selected counterparts and can be concluded within a relatively short period of time. Further, creation of the situation where many countries rush to join FTA negotiations following the major trading countries shifting to FTAs, or "an FTA spurts the creation of yet more FTAs" in a way, is considered to be another factor concerning the sharp increase in the number of FTAs. FTA strategies of Europe and the US targeting emerging economies is evidence of benefits from advancing globalization. Until recently, the majority of FTAs were formed between neighboring countries and regions. Originally, it was in the natural course of events that the neighboring countries with strong political and economic relationships form FTAs looking for stronger or improved ties. The EU, with the philosophy of keeping "peace in the region" based on the reflection of the European countries that experienced two World Wars can be regarded as a highly political regional unification. On the other hand, as the economy further globalizes, many FTAs have cut across regional boundaries in recent years. In other words, FTAs are formed between countries belonging to different regions in an increasing number of cases.

7. The United States Free Trade Agreements [1] [23] [27] [32] [37] [39]

Countries form free trade areas for a number of economic and political reasons. Political considerations are also a motivation to form FTAs. The United States formed FTAs with Israel and, most recently, with Jordan to reaffirm American support for those countries and to strengthen relations with them. Additionally, USA has implemented bilateral free trade agreements with the following countries and blocs:

- Australia (2005); Bahrain (2006); Chile (2004); Israel (1985; Palestinian Authority included.); Jordan (2001); Morocco (2006); Peru (2007); Singapore (2004); CAFTA (2005) - Implementation with Costa Rica pending

The United States is negotiating bilateral free trade agreements with the following countries and blocs:

- New Zealand-US Free Trade Agreement
- Colombia Trade Promotion Agreement
- US-Oman Free Trade Agreement

- Panama - United States Trade Promotion Agreement (Agreement reached, awaiting ratification)
- U.S.-Korea Free Trade Agreement
- Indonesia; Kenya; Kuwait
- Malaysia; Mauritius; Mozambique; Thailand - US-Thailand Free Trade Agreement
- United Arab Emirates; Qatar, Ecuador
- Southern African Customs Union

While the U.S. has successfully opened 16 foreign markets through bilateral trade agreements, that success pales in comparison to the benefits Americans would gain from a successful Doha Round. One estimate is that a one-third reduction in global trade barriers would be equal to an average gain of \$2,500 for each American household of four, thus highlighting that businesses and families benefit from liberalized trade. "Trade Negotiating Authority-A Vital Tool for Advancing U.S. Economic Growth, Leadership and Competitiveness" [39]

Figure 5: FTAs by Year and Geographic Region, 1955-2008

(Unit Number of agreements)

	Europe, Russia and the CIS, Middle East, Africa	Americas	Asia-Pacific	Cross-regional	Total
1955-1959	1				1
1960-1964	1	1			2
1965-1969					
1970-1974	1	1		2	4
1975-1979	2		2		4
1980-1984	1	1	2		4
1985-1989		1		2	3
1990-1994	13	2	3		18
1995-1999	23	4		1	28
2000-2004	20	8	8	9	45
2005-2008*	13	2	14	10	39
Total	75	20	29	24	148

Notes as adapted from 2008 JETRO White Paper on "International Trade and foreign Direct Investment"

- (1). Of the 211 regional trade agreements (RTAs) listed on the WTO website ("Listing" signifies that GATT or WTO has been notified of the agreement and it is currently in effect), we have excluded 66 as duplicates due to 1) new participants in existing FTAs, 2) notification to both GATT and GATS, etc. Thailand - India FTA, the ROK-ASEAN FTA and the Japan-Brunei FTA are added to the total number above.
- (2). The year is based on the date of the agreement becoming effective. If that is unclear, the date of notification to GATT or the WTO is used.

Source : WTO website (www.wto.org/english/tratop_e/region_e-region_e.htm) as of July 18, 2008.

According to the National Foreign Trade Council [2007]: "With nearly one quarter of U.S. GDP tied to trade and 95 percent of the world's consumers living outside of the United States, trade agreements must be negotiated to remove trade barriers and expand access to those markets to ensure continued U.S. economic and job growth. By the tenth anniversary of NAFTA's passage, the U.S. had experienced dramatic job and income growth, and increased exports to Mexico and Canada by 85 percent [37].

Trade agreements are an exercise of sovereignty that are negotiated for the sole purpose of eliminating trade barriers and creating ground rules to manage a trade relationship in a beneficial and peaceful manner. In the absence of these agreements, the global marketplace would be dramatically more risky and unpredictable for businesses, consumers, and workers. The U.S. is a party to only 10 ratified FTAs with 16 countries. While the U.S. often takes a leadership role in international trade negotiations, foreign governments are in the process of negotiating their own free trade agreements that exclude the United States. For example, China has begun negotiating trade agreements with several U.S. allies and trading partners that would exclude the United States.

8. Japan's Free Trade Agreements

Japan's Free Trade Agreement (FTA) with Singapore is the very first it has forged with any country in 2002. Tokyo has at least two motivations: to avoid losing out to Beijing strategically and economically as the Chinese seek to forge an FTA with the Southeast Asian countries, and using Singapore (which lacks an agricultural sector) as the thin end of the wedge to push for FTAs with other countries. Japan has bilateral agreements with the following countries and blocs: Chile (signed in 2006); Brunei (signed in 2007); Indonesia (signed in 2007) Malaysia (signed in 2005); Mexico (took effect in 2005); Philippines (signed in 2006); Thailand (signed in 2007); Singapore (signed in 2002).

9. India's Free Trade Agreements

Since independence, India has always tried to keep healthy trade relations with her neighboring countries. From the following data we can see the zeal of the Indian government to pave the way for free trade with at least the southern countries of Asia. By 2016, India will be trading at zero duty with a dozen countries. India is already enjoying free trade with Thailand and Sri Lanka. Very soon she will enjoy the same with Singapore. India is likely to soon initiate formal negotiations for a free trade agreement (FTA) with China, the third largest destination for Indian goods and the biggest source of imports. A task force comprising officials from both countries recently submitted its report saying the FTA was feasible. India's FTA's signed and ongoing are: Indo-Thailand (9 October, 2003);

Indo-Sri Lanka (28 December, 1998) Brunei, Indonesia & Malaysia; Philippines, Cambodia, Laos, Myanmar & Vietnam; China and Singapore ; Proposed at the third ASEAN-India summit the feasibility of an Asian economic community which will include ASEAN, China, Japan, Korea and India.

10. Major Characteristics of China's Free Trade Agreements

To date, China has negotiated nine FTAs with 27 countries and regions, accounting for close to one-quarter of China's trade volume in 2004. In the past few years, the number of FTAs has gradually increased: the Mainland-Hong Kong and Mainland-Macao Closer Economic Partnership Arrangement ("CEPA") was implemented; a tariff reduction programme of the China-ASEAN Free Trade Agreement was launched; the China-Chile FTA was formally signed; and FTA talks began with New Zealand, Australia, the Gulf Cooperation Council ("GCC"), and Pakistan.

FTA is one of the most important forms of regional trade arrangements in the world. In recent years, it has been developing rapidly as an approach to regional economic cooperation, facilitating free trade and investment. In the 21st Century, China's economy has been increasingly integrated into the world. As a result of globalization, and to respond to the needs of a market economy opening to the outside world, the Chinese government has geared up its efforts in exploring, negotiating, and establishing FTAs in different regions. The dynamic development of regional trade arrangements in the world coupled with China's economic boom has provided a sound foundation for China to seek regional economic and trade cooperation. So far, more than 20 economies have approached China for FTA, of which the FTA between China and ASEAN, Closer Economic Partnership Agreements (CEPA) respectively between China's mainland and Hong Kong and Macau are being implemented; the FTA with Chili has been signed; and FTAs respectively between China and the six Gulf Cooperation Council member countries, Pakistan, India, New Zealand, and Australia are in negotiation. China is also exploring the possibility of FTA with South African Customs Union countries, Iceland, and South American Common Market (MERCOSUR), Peru.

China has more FTAs with neighbors than other countries in the region. China has 15 immediate neighbouring countries. Except DPRK area, Mongolia, Afghanistan, Bhutan, and Sikkim all have signed or are negotiating FTAs with China. China-ASEAN FTA covers Viet Nam, Burma, and Laos. China-India, China-Pakistan FTAs are being negotiated. Central Asia countries and Russia are under the framework of the Shanghai Cooperation Organization, and may move a step further to establish into FTAs with China. Among its 14 non-immediate neighbours, China discussed FTAs with Japan and ROK, and is negotiating FTAs with the two countries separately. In Southeast Asia, Philippines, Thailand, Malaysia, Singapore, Brunei, Cambodia, and Indonesia are under the umbrella of China - ASEAN- FTA, Sri Lanka and Bangladesh are parts of Bangkok Agreement^[42].

11. FTA Related Issues Faced by China

China didn't start FTA negotiation until 2001, when China became a member of WTO. Compared with many other countries, it is a late comer in this area as well as in other aspects of economic globalization. When China began to negotiate FTAs with other economies, there were already more than 200 FTAs globally, so it needed to catch up with the rest of the world quickly. The FTAs signed and being negotiated by China covers more than 20 economies, but many of them are under the umbrella of other FTA frameworks (10 ASEAN nations, for example.) The number of bilateral FTA agreements is very small. There are only five FTA agreements being implemented: China-ASEAN FTA, Bangkok Agreement, China-Chile FTA, and CEPAs respectively between China's Mainland and Hong Kong and Macau. China is still on the learning curve of FTA arrangements.

12. Germany's Part in The European Union Trade Agreements [12] [13]

The EU has bilateral agreements with the following countries and blocs:

- Algeria European Union Association Agreement
- Croatia Stabilization and Association Agreement
- Egypt European Union Association Agreement
- Macedonia Stabilization and Association Agreement
- Morocco European Union Association Agreement
- Palestinian Authority European Union Association Agreement
- Chile; South Africa; Switzerland
- Tunisia European Union Association Agreement
- Mexico - EU FTA

Germany benefits as EU is negotiating or is planning bilateral agreements with the following countries /blocs:

- Bosnia and Herzegovina Stabilization and Association Agreement
- Serbia and Montenegro Stabilization and Association Agreement
- Albania Stabilization and Association Agreement
- Syria European Union Association Agreement
- Mercosur; Andean Community
- Russia (EU-Russia Common Economic Space)

13. Regional Economic Cooperation

One of the most important developments in the world trade system in the 1990s has been the emergence of regional cooperation. The end of the Cold War reduced political tensions between countries in Asia as well as globalizing production processes and increasing vertical integration. Regional cooperation provides a competitive model to attract investment and technology for developing countries in pursuit of the alleviation of poverty and economic growth. Yet regional economic cooperation and attempts at free trade agreements of developing countries have a mixed record of success.

14. APEC --A New Model for Regional Economic Cooperation

The 18-member Asia-Pacific Economic Cooperation (APEC) has made big successes in less than eight years since its founding in 1989. It is generally held that APEC's development will not only have an enormous and far-reaching impact on the Asia-Pacific economy, but also contribute to peace and security in this region and the whole world as well. This paper will focus on the characteristics of APEC as a new model for regional economic cooperation, and its impact on regional development as well as peace and stability. The efforts to propel Asia-

Pacific regional economic cooperation have been on for nearly 30 years. Explorations into the concept of cooperation had been in progress for some 20 years before leading to the eventual affirmation of the term of "open regionalism." APEC is not a strictly institutionalized organization, and makes no binding resolutions. It is a kind of voluntary community. The truth of the matter is that "voluntary community" is exactly where the strength of APEC lies. The historical and present facts tell us that "the economic development of the Asia-Pacific is propelled by the market, not by agreements or treaties; and the unilateral action of each economy is taken in accordance with the market demands, but not forced by any supranational authority." [11]

Economists continue to argue about the merits of free trade agreements relative to the multilateral system of the WTO. Much of the argument centres on the potential for FTAs to result in important amounts of trade diversion as importers redirect their purchases to new preferential suppliers and away from those in other countries that may be the lowest cost producers. On top of this economic argument, certain pundits claim that FTAs are a political distraction from the WTO system and that over time, the creation of additional bilateral agreements will undermine support for the global institution. From a practical standpoint, who wins arguments like these is increasingly irrelevant as there are now nearly 200 FTAs in operation around the world and about another seventy under negotiation. [35]

15. Increasingly Different Patterns are Emerging in Regional Trade Agreements

The European Union is a highly integrated marketplace, with two-thirds of its trade transactions taking place within the region. In 2007, intra-trade accounted for slightly more than half (51 per cent) of the exports of the North American Free Trade Agreement (NAFTA). In 2000, this share was 56 per cent. However, as trade with countries outside NAFTA's area has been growing at a somewhat faster pace than intra-NAFTA trade, this share has been declining. Other trade blocs, such as MERCOSUR, the Andean Community or ASEAN, show a less pronounced integration. MERCOSUR countries carry out only around 14 per cent of their trade with other countries in the agreement, the Andean Community only 8 per cent, and ASEAN a quarter. Brazil, India and China are illustrative of a clear trend of vigorous growth among a number of emerging economies. While this growth implies a growing share of world trade, the share in world exports remains relatively small for most of the emerging economies individually. The share of Brazil and India, for example, is still just over 1 %, while China's share is approaching 10%.

16. The Case of Highly Populated SAARC for a Free Trade Agreement

The South Asian Association for Regional Cooperation (SAARC) is an economic and political organization of eight countries in Southern Asia. In terms of population, its sphere of influence is the largest of any regional organization: almost 1.5 billion people, the combined population of its member states. It was established on December 8, 1985 by India, Pakistan, Bangladesh, Sri Lanka, Nepal, Maldives and Bhutan. In April 2007, at the Association's 14th summit, Afghanistan became its eighth member. The objectives of the Association [SAARC] as defined in the Charter are: [29]

- to promote the welfare of the peoples of South Asia and to improve their quality of life;
- to accelerate economic growth, social progress and cultural development in the region and to provide all individuals the opportunity to live in dignity and to realize their full potential;
- to promote and strengthen collective self-reliance among the countries of South Asia;
- to contribute to mutual trust, understanding and appreciation of one another's problems;
- to promote active collaboration and mutual assistance in the economic, social, cultural, technical and scientific fields;
- to strengthen cooperation with other developing countries;
- to strengthen cooperation among themselves in international forums on matters of common interest; and
- to cooperate with international and regional organizations with similar aims and purposes.

The Declaration on South Asian Regional Cooperation was adopted by the Foreign Ministers in 1983 in New Delhi. During the meeting, the Ministers also launched the Integrated Programme of Action (IPA) in nine agreed areas, namely, Agriculture; Rural Development; Telecommunications; Meteorology; Health and Population Activities; Transport; Postal Services; Science and Technology; and Sports, Arts and Culture. The South Asian Association for Regional Cooperation (SAARC) was established when its Charter was formally adopted on 8 December 1985 by the Heads of State or Government of Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

Afghanistan was added to the regional grouping at the behest of India on November 13, 2005 and became a member on April 3, 2007 [3]. With the addition of Afghanistan, the total number of member states was raised to eight. [44] In April 2006, the United States of America and South Korea made formal requests to be granted observer status. The European Union has also indicated interest in being given observer status, and made a formal request for it to the SAARC Council of Ministers meeting in July 2006 [28]. On August 2, 2006 the foreign ministers of the SAARC countries agreed in principle to grant observer status to the US, South Korea and the European Union [48].

Over the years, SAARC members have expressed their unwillingness to sign a free trade agreement. Though India has several trade pacts with Maldives, Nepal, Bhutan and Sri Lanka, similar trade agreements with Pakistan and Bangladesh have been stalled due to political and economic concerns on both sides. India has been constructing a barrier across its borders with Bangladesh and Pakistan. In 1993, SAARC countries signed an agreement to gradually lower tariffs within the region, in Dhaka. Eleven years later, at the 12th SAARC Summit at Islamabad, SAARC countries devised the South Asia Free Trade Agreement which created a framework for the establishment of a free trade area covering 1.4 billion people. This agreement went into force on January 1, 2006. Under this agreement, SAARC members will bring their duties down to 20 per cent by 2007. The Russian Federation intends to become an observer as well, and is supported by India. The People's Republic of China has shown its interest in joining SAARC [43]. While Pakistan and Bangladesh support China's candidature, India is more hesitant

about the prospect of Chinese membership, while Bhutan does not even have diplomatic relations with China. However, during the 2005 Dhaka summit, India agreed to grant observer status to the PRC along with Japan. During the 14th summit, Nepal along with Pakistan and Bangladesh, announced their support for the membership of China. Seeking greater involvement in the SAARC, however, finds it too early to apply for full membership. The Republic of South Africa has participated in meetings [47].

17. The Outlook for the South Asian Free Trade Area

The Agreement on the South Asian Free Trade Area is an agreement reached at the 12th SAARC summit at Islamabad, capital of Pakistan on 6 January 2004. It creates a framework for the creation of a free trade area covering 1.4 billion people in India, Pakistan, Nepal, Sri Lanka, Bangladesh, Bhutan and the Maldives. The seven foreign ministers of the region signed a framework agreement on SAFTA with zero customs duty on the trade in practically all products in the region by end 2016. The new agreement i.e. SAFTA, came into being on 1 January 2006 and will be operational following the ratification of the agreement by the seven governments. SAFTA requires the developing countries in South Asia, that is, India, Pakistan and Sri Lanka, to bring their duties down to 20 percent in the first phase of the two year period ending in 2007. In the final five year phase ending 2012, the 20 percent duty will be reduced to zero in a series of annual cuts. The least developed nations in South Asia consisting of Nepal, Bhutan, Bangladesh and Maldives have an additional three years to reduce tariffs to zero. Pakistan has signed but not ratified the treaty; though there is hope in India that it will some time in 2008-2009 [46]. So far, four rounds of trade negotiations have been concluded under SAPTA covering over 5000 commodities.

18. Economic Impact of FTAs

Using the USA as an example, the surge in U.S. interest in FTAs and in the formation of FTAs worldwide raises the question of their impact on the countries included in an FTA and on the rest of the world. It is an issue that economists have long studied and debated. Interest in the issue has peaked at various times in the post-World War II period. The first time was when the European Common market was formed. Interest has peaked again with the current trends in FTAs. The debate has relied largely on theory since empirical data is scarce save for the experience of the European Union. The debate has also divided economists between those who strongly oppose FTAs as an economically inefficient mechanism and those who support them as a means to build freer trade [6]. Economists usually base their analysis of the impact of FTAs on the concepts of trade creation and trade diversion. These concepts were first developed by economist Jacob Viner, who focused his work on the economic effects of customs unions, but his conclusions have been largely applied to FTAs and other preferential trade arrangements. His analysis was also confined to static (one-time) effects of these arrangements

**Forming a Mega-Competitive QUINTET :
Place of China and India**

Figure 6: Comparative Profiles of Regional Blocs and Free Trade Agreements

[Data as noted 2006 and 2007est]

Regional bloc ¹	Area		Population	GDP (\$US)				Member states ¹
	km ²	sq mi		in millions (PPP)	in millions (nominal)	per capita (PPP)	per capita (nominal)	
AU	29,797,500	11,504,879	897,548,804	1,515,000	1,131,850	1,896	1,261	53
ASEAN (2007e)	4,497,493	1,736,000	566,500,000	3,115,480	1,173,000	5,541	2,041	10
CACM	422,614	163,172	37,816,598	159,536	84,792	4,219	2,242	5
CARICOM	462,344	178,512	14,565,083	64,219	24,020	4,409	1,649	(14+1)
CCASG / GCC	2,285,844	882,569	35,869,438	536,223	717,800	14,949	20,011	6
CEFTA	298,148	115,116	28,929,682	222,041	122,001	7,675	4,217	(7+1)
EU (2007 e)	4,324,782	1,669,808	497,000,000	14,953,000	16,574,000	28,213	33,482	27
EurAsEC	20,789,100	8,026,720	208,067,618	1,689,137	1,125,528	8,118	5,409	6
EFTA (2007 e)	529,600	204,480	12,660,623	567,500	743,300	44,828	60,000	4
GAFTA	9,421,946	3,637,834	280,727,416	1,341,298	N/A	4,778	N/A	(16+1)
GUAM	810,506	312,938	63,764,600	456,173	106,469	7,154	1,670	4
NAFTA (2007e)	21,783,850	8,410,792	445,000,000	15,857,000	15,723,000	35,491	35,564	3
PARTA	528,151	203,920	34,137,339	858,970	N/A	2,954	N/A	(12+2)
SAARC	5,136,740	1,983,306	1,467,255,669	4,074,031	N/A	2,777	N/A	8
Unasur/Unasul	17,339,153	6,694,684	370,158,470	2,868,430	N/A	7,749	N/A	12

Regional bloc ¹	Area		Population	GDP (\$US)				Units
	km ²	sq mi		in millions (PPP)	in millions (nominal)	per capita (PPP)	per capita (nominal)	
UN	133,178,011	51,420,318	6,411,682,270	55,167,630	48,245,198	8,604	7,524	192
Brazil (2007e)	8,514,877	3,287,612	183,888,841	1,804,000	1,067,706	10,073	6,842	27
Canada(2007e)	9,984,670	3,855,103	33,000,000	1,274,000	1,406,000	38,200	42,738	13
India (2007 e)	3,287,590	1,269,346	1,120,000,000	4,726,000	1,089,000	4,182	1,004	35
Japan (2007 e)	377,873	145,898	127,433,494	4,894,000	4,546,000	33,800	39,341	47
China(2007e)	9,596,960	3,705,407	1,321,851,888	7,043,000	3,420,000	5,300	2,800	33
Russia (2007e)	17,075,200	6,592,772	142,500,000	2,076,000	1,286,000	14,600	9,056	83
USA (2007e)	9,826,630	3,794,083	302,000,000	13,543,000	13,794,700	43,500	45,594	50
Germany	357,021	137,847	82,217,800	2,812,000	3,320,000	34,212	40,000	16
Korea	255,062	98,480	48,379,392	1,206,000	957,100	25,000	20,015	9+7
South Africa	3,159,557	1,219,912	48,782,756	467,800	282,600	9,700	5,915	9
México	5,108,881	1,972,550	109,955,400	1,353,000	893,400	12,400	9,716	31

Source: CIA World Factbook, IMF WEO Database, IMF nominal figures for 2006. JETRO WPIT, 2007 & 2008
Legend: **AU** African Union; **ASEAN** Association of South-East Asian Nations; **CACM** Central American Integration System; **CARICOM** Caribbean Community; **CCASG/GCC** Gulf Cooperation Council; **CEFTA** Central European Free Trade Agreement; **EU** European Union; **EurAsEC** Eurasian Economic Community; **EFTA** European Free Trade Association; **GAFTA** Greater Arab Free Trade Area; **GUAM** Georgia Ukraine Azerbaijan Moldova; **NAFTA** North American Free Trade Association; **PARTA** Pacific Islands Forum; **SAARC** South Asian Association for Regional Cooperation; **Unasur/Unasul** Union of South American Nations
Note data for the People's Republic of China does not include Hong Kong, Macau, or Republic of China (Taiwan).

Trade creation occurs when a member of an FTA replaces domestic production of a good with imports of the good from another member of the FTA, because the formation of the FTA has made it cheaper to import rather than produce domestically. The creation of trade is said to improve economic welfare within the group because resources are being shifted to more efficient uses. Trade diversion occurs when a member of an FTA switches its import of a good from an efficient nonmember to a less efficient member because the removal of tariffs within the group and the continuation of tariffs on imports from nonmembers make it cheaper to do so. Trade diversion is said to reduce economic welfare because resources are being diverted from an efficient producer to a less efficient producer^[4]. In most cases, it appears that FTAs lead to both trade diversion and creation with the net effects determined by the structure of the FTA. Therefore, even if two or more countries are moving toward freer trade among themselves in an FTA, the FTA could make those countries and the world as a whole worse off if the FTA diverts more trade than it creates, according to economic theory^[20].

Economists continue to argue about the merits of free trade agreements relative to the multilateral system of the WTO. Much of the argument centers on the potential for FTAs to result in important amounts of trade diversion as importers redirect their purchases to new preferential suppliers and away from those in other countries that may be the lowest cost producers. On top of this economic argument, certain pundits claim that FTAs are a political distraction from the WTO system and that over time, the creation of additional bilateral agreements will undermine support for the global institution. From a practical standpoint, who wins arguments like these is increasingly irrelevant as there are now more than 200 FTAs in operation around the world and about another seventy under negotiation^[35].

America's trade with other countries has spurred U.S. growth, jobs, and prosperity. Since World War II, trade liberalization has increased annual incomes by \$9,000 per American household and more than 57 million American jobs are connected to international trade. In the fourth quarter of 2006, for example, U.S. trade accounted for approximately 50 percent of U.S. GDP growth. A forward-looking trade agenda that seeks to open markets and expand trade is a vital component of continuing to advance this growth^[40].

Trade policymakers encounter circumstances much more complicated than what is depicted in economic theory. Many functioning and proposed FTAs encompass more than two countries and involve a range of products, both goods and services, making it much more challenging to evaluate their economic impact. To provide an analytical framework, some economists have developed sets of conditions under which, they have concluded, an FTA would create more trade than it diverts. They state that trade creation is likely to exceed trade diversion based on -^{[25] [34]}

- The larger the tariffs or other trade barriers among members before the FTA is formed;
- The lower the tariffs and other barriers in trade with nonmembers;
- The greater the number of countries included in the FTA;
- The more competitive or the less complementary the economies joining the FTA;
- The closer the economic relationship among the members before the FTA was formed^[30].

Economists also have determined that, along with the immediate, static effects of trade diversion and creation, FTAs generate long-term dynamic effects that might include:

- Increased efficiency of production as producers face increased competition with the removal of trade barriers;
- Economies of scale, that is decreased unit costs of production as producers can have larger production runs since the markets for their goods have been enlarged; and
- Increased foreign investment from outside the FTA as firms seek to locate operations within the borders of the FTA to take advantage of the preferential trade arrangements^[31].

Until recently not many FTAs were in operation; therefore, available data on their impact has been limited to the experience of the formation of the European Common Market and subsequently the European Union. Most studies have concluded that the European Community has resulted in more trade creation than trade diversion, but in some sectors such as agriculture, the net effect has been trade diversion because of the EU's Common Agricultural Policy that raised barriers to agricultural trade outside the EU^[15].

19. FTAs and the WTO

A basic principle of the General Agreement on Tariffs and Trade (GATT) that is administered by the WTO is the most-favored nation (MFN) principle. Article I of GATT requires that "any advantage, favor, privilege, or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties." FTAs, by definition, violate the MFN principle, since products of FTA member countries are given preferential treatment over nonmember products. However, the original GATT signatories recognized that FTAs and customs unions, while violating the MFN principle, improve the economic welfare of all members, if certain conditions are met to minimize trade diversion^[7].

20. The Continuing Debate over FTAs: The Case of Policy Implications in USA

Interest in a new wave of FTAs is driving a spirited debate among experts, policymakers, and other observers over whether they promote or damage U.S. economic interests and the economic interests of the world at large. The differing views can be categorized into three main groups. One group consists of those who oppose FTAs because, they assert, FTAs undermine the development of the multilateral trading system and act as a "stumbling block" to global trade liberalization. A second group supports FTAs because, they believe, FTAs act as a "building block" to multilateral trade liberalization. The third category are those individuals and groups that are opposed to trade liberalization in general because they believe trade liberalization's impact on workers in import-sensitive sectors or on the environment is unacceptable, or because, they assert, it undermines U.S. sovereignty^[8].

Among representatives of the first group of experts are international economists Jagdish Bhagwati and Anne O. Krueger, who have strongly advocated that the United States and other national governments should not pursue FTAs at the expense of multilateral negotiations in the WTO. Bhagwati has concluded that FTAs are by definition discriminatory and therefore trade diverting. He argues that tariffs remain high on many goods imported into developing countries and even on some labor intensive goods (such as wearing apparel and agricultural products) imported into developed countries. Consequently, he asserts, trade diversion will likely result when an FTA is formed. Bhagwati argues that firms actually prefer bilateral or regional FTAs to multilateral trade liberalization because they are able to achieve preferential treatment over their non-member country competitors^[2].

Both Bhagwati and Krueger cite the "rules of origin" and other conditions of an FTA's establishment for strong criticism. Bhagwati claims, for example, that the rules of origin in one FTA more than likely do not coincide with the rules of origin in many of the other FTAs. Furthermore, he argues, the schedule of implementation of the tariff reductions and other conditions for one FTA will not match the schedule of other FTAs. The incongruity of these regulations across FTAs has created what Bhagwati sees as a customs administration nightmare and calls the spaghetti-bowl phenomenon^[9].

In her criticism, Krueger claims that in order to meet the input thresholds of rules of origin requirements, producers in one FTA partner will be encouraged to purchase as many inputs as possible from other partner countries, even if a non-FTA member can produce and sell the inputs more cheaply and even if the tariff rate on inputs from non-FTA producers is zero. Importing inputs from within the FTA to meet the rules of origin threshold allows the producer to sell the final product within the FTA duty free. Under such circumstances imports of inputs are diverted from efficient producers outside the FTA to less efficient producers inside the FTA. A corollary to Krueger's conclusion is that the higher the threshold established in the rules of origin, the greater the chance that trade diversion will take place^[18].

A range of economists, policymakers, and other experts embrace a second view that FTAs can enhance trade and should be pursued. Economist Robert Z. Lawrence argues, for example, that recent FTAs involve much more economic integration than the elimination of tariffs. *NAFTA*, he points out, has led to the reduction in barriers on services trade, foreign investment, and other economic activities not covered by the GATT/WTO. In addition, under *NAFTA*, Mexico has affirmed its commitment to economic reform, making its economy more efficient. Lawrence asserts that the theory traditionally applied to FTAs (by Bhagwati, Krueger, and others) does not take into account these dynamic welfare enhancing characteristics of FTAs, which, he believes, are likely to outweigh any trade diversion that results from the elimination of tariffs^[19].

A CATO Institute study by economist Edward L. Hudgins argues that while it may be preferable to liberalize trade multilaterally, countries should take any available avenue, including bilateral or regional FTAs, even if they lead to some trade diversion. Furthermore, Hudgins asserts that FTAs can be more efficient vehicles for addressing difficult trade barriers than the WTO, where the large membership requires compromise to the least common denominator to achieve consensus. FTAs have also had provided momentum for GATT/WTO members to move ahead with new trade rounds, he claims^[16].

Economist C. Fred Bergsten holds a position similar to the one expressed in the CATO study, that in lieu of multilateral trade negotiations, FTAs are the next best thing and promotes global trade liberalization. Bergsten has advocated establishing U.S. FTAs with New Zealand and with South Korea. Economist Jeffrey Schott argues that some U.S. firms are being discriminated against because FTAs are rapidly forming in which the United States is not a participant; therefore, in his review, the United States must negotiate FTAs. He cites the example of Canadian firms which have obtained competitive advantages over American firms because Canada has an FTA with Chile^[33].

Bergsten and others have also advocated structuring FTAs in a manner that could serve as building blocks of a global free trade system. Using the APEC plan as a model, Bergsten argues for an FTA based on “open regionalism,” that is establishing the road map for free trade and investment in the Asian-Pacific region for 2010/2020 among the members but allowing other countries to join if they agree to accede to the conditions. In order to minimize trade diversion, he suggests that trade and investment could be implemented on an MFN principle, perhaps conditional MFN in order to limit the “free rider” effects. Other countries, and other regional groupings, Bergsten presumes, would be willing to accept the conditions having been enticed by the trade and investment opportunities until most of the membership of the WTO would be engaged in forming a free trade area. A Heritage Foundation report draws up a similar proposal for a “Global Free Trade Association.”^[17]

A third group opposes FTAs but also trade liberalization or “globalization” in general. Included in this group are representatives of import-sensitive industries, for example labor unions, and representatives of social action groups such as some environmentalists, who question the wisdom of trade liberalization whether done through multilateral negotiations or through bilateral and regional trading arrangements. They assert that trade liberalization unfairly affects workers by exporting jobs to countries with lower wages and undermines the nation’s ability to protect the environment by allowing companies to relocate to countries with less stringent environmental regulations^[36]. For example, the United Auto Workers (UAW) union has stated the following position regarding the FTAA:

“Such an agreement would provide broader protections for the rights of corporations, further undermine the ability of governments in the region to regulate their economies in the interests of their citizens and intensify the downward pressure on workers’ incomes through competition for jobs and investments. All of this would take place in the absence of any counter-balancing protections for workers, consumers or the environment. This is why the UAW has consistently opposed the direction of these negotiations, the positions taken by the U.S. government, and worked closely with other organizations in the region to oppose the creation of an FTAA.”^[36]

21. Conclusion

Major shifts in the world economy during the past three decades will continue in the 21st century for the *QUINTET* to dominate expanding the economic clout and redistribute a greater

share of trade and investment flows than the *TRIAD* Powers. China and India joining the *TRIAD* with vast populations and impressive GDP growth rates coupled with the sum of comparative advantages makes the *QUINTET* a formidable force in the global economy and major competitors in the world trading system. A larger share of global FTAs has been negotiated or is pending in the *QUINTET* countries. Free trade agreements are viewed by many as a significant trade policy vehicle for the *QUINTET* and for other major trading nations for the advancement of mutual goals. In this highly uncertain environment, output in the world economy as a whole is expected to record around 3 per cent in 2008, almost one percentage point less than in 2007, and in developed countries as a group, GDP growth is likely to fall to about half this rate. By contrast, growth in developing countries as a group can be expected to remain quite robust, at more than 5% per cent or even slightly higher by China and India, the new *QUINTET* powers in the new globally economy.

With nearly 40% of the world's population, China and India joining the *TRIAD* to form a *QUINTET* and a mega-competitive force in the world trading system, creates a new global economy. This new global economy is also emerging to confront business enterprises in the traditional ways of doing business to rethink new paradigms and best practices emanating in companies focusing on core competencies in the light of mega-competition from around the world. Currently, China and India and other emerging economies like Brazil, Russia, Korea, South Africa are assuming leading economic roles challenging established economic powers of the *TRIAD* and even the newly formed formidable *QUINTET* that have maintained their competitive strength in commanding a larger share of trade, investment and merger and acquisition activity.

The financial turmoil that erupted in August 2007, and continued into 2008, the unprecedented oil price increases and the possibility of tighter monetary policy in a number of countries signify difficulties for the world economy as 2008 ends and 2009 begins. The impact of the sub-prime crisis has spread well beyond the United States, causing a widespread squeeze in liquidity and credit. And, price hikes in primary commodities, fuelled partly by speculation that has shifted from financial instruments to commodity markets, adds to the challenge for policymakers intent on avoiding a recession while at the same time keeping inflation under control. The situation could become even more difficult if large movements in the exchange rates of major currencies add to the turmoil in the financial markets, a risk that has increased in most of 2008. IMF says; world economic growth will fall to less than 1% in 2009, the lowest rate in more than 60 years.

With overall global economic growth slowing to a near standstill, 2009 will be the most challenging year for economies across the globe since World War II, with a recovery gaining pace gradually later in 2009. In advanced countries, including the United States, the Euro-zone nations, Japan, Canada and the United Kingdom, gross domestic product is expected to shrink by 2%. According to IMF, a vicious cycle of plummeting asset values, decreasing household wealth and sinking consumer demand will result in the first contraction of total advanced economies' GDP in the post-World War II era, global outlook. The United States, Japan and Germany, the mainstay anchors of the *TRIAD*, are in a recession, before gradual recovery sets in during the latter part of 2009. Recovery for the group in 2010 is predicated on continued progress in stabilizing international financial markets, and thawing the flow of

credit from its current frozen status. News from the USA, Japan, Germany and Europe has been poor but policy efforts may just about succeed in stabilizing these economies by mid-2009. These are common concerns for other *QUINTET* nations beyond the USA and developing countries like Sri Lanka in pursuit of the fruits of globalization coupled with trade liberalization, open markets, and elimination of trade barriers as they proceed to advance Free Trade Agreements [FTAs] to promote trade, investment flows and economic growth.

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