Not all trade agreements are good

FRIENDLY country? Want a trade deal with America? Join the lengthening queue. On November 15th, the Bush administration announced that it intended to negotiate trade agreements with Oman and the United Arab Emirates. The United States is, therefore, now working on bilateral trade accords with 12 countries. It has already finished such deals with another dozen.

Foreign policy, more than economics, drives some of these deals. The Oman and UAE agreements, for instance, are deemed to be "important steps" towards boosting growth and democracy in the Middle East. But Mr Bush's trade team also believes that freer global trade is best served by "competitive liberalisation": pushing trade deals at the bilateral, regional and global level simultaneously.

America is merely the latest fan of a broader global trend. As a new World Bank report, "Global Economic Prospects 2005", points out, regional and bilateral trade deals are all the rage. Almost 230 such agreements exist today, up from a mere 50 in 1990, and a further 60 or so are being negotiated. The average African country belongs to four different trade agreements. The average Latin American country belongs to eight.

Alas, the passion for such agreements may be misguided. Economists have long pointed out that the gains from multilateral trade liberalisation are far greater than those from bilateral or regional deals. At best, regional deals offer smaller benefits. At worst, they do damage, artificially diverting trade away from excluded countries or clogging up commerce with fiendishly complicated "rules of origin". These are needed to define whether imported goods, which may consist of inputs from many different countries, qualify for favoured treatment.

Though the Bank's report tries to emphasise that regional trade agreements can boost trade, the record is not encouraging. Two-thirds of the tariff reduction seen globally between 1983 and 2003 was due to unilateral reforms by individual countries. A quarter came from commitments made in the Uruguay Round of global trade talks. Only a tenth of global tariff cutting is due to regional and bilateral deals.

Most bilateral agreements are far from ideal. Those between poor countries often exist more on paper than in practice. Bilateral deals between rich and poor tend to be better implemented, but are marred by restrictive rules of origin and by the routine exclusion of important agricultural products.

In fact, the Bank's boffins point out that most poor countries would be worse off in a world of rampant bilateral deals than they are today. A simulation in the study estimates that a broad global trade agreement could increase world income by $263 billion by 2015, of which $109 billion would go to poor countries. If developing countries all had bilateral agreements with big rich trading partners (the European Union, the United States, Canada and Japan), global income would rise by much less: $112 billion. The rich would scoop
all this, and more: $133 billion. Although a handful of developing countries, such as Brazil and China, would gain a bit, poor nations as a group would be worse off than they are today.

While the Bank’s exact numbers should be taken with a pinch of salt, the broad lesson is clear. Bilateralism may be a route to freer global trade, but it is, at best, a risky one.