

# Chapter 1

## Introduction: The Purpose, Design and Effects of Preferential Trade

### Agreements

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#### A. Introduction

Preferential trade agreements (PTAs), defined as agreements that liberalize trade between two or more countries but that do not extend this liberalization to all countries (or at least to a majority of countries), are mushrooming across the globe.<sup>2</sup> The European Union (EU) is currently negotiating trade agreements with countries such as India, Japan, Malaysia, Thailand, the United States (US), and Vietnam. The Transatlantic Trade and Investment Partnership (TTIP) envisaged by the EU and the US might eventually cover one-third of world trade. This mega project is mirrored by the negotiations for a Trans-Pacific Partnership (TPP), with participating countries such as Australia, Brunei Darussalam, Chile, Japan, Malaysia, New Zealand, Peru, Singapore, the US and Vietnam. The TTIP and the TPP are currently the most high-profile PTA negotiations under way, but a large number of smaller PTAs are being negotiated in parallel.

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<sup>2</sup> Many terms have been used for these agreements, including regional trade agreements, free trade agreements, or economic integration agreements. We use the term preferential trade agreements to stress the preference given to partners in the same agreement. Our definition excludes non-reciprocal agreements, where one side makes unilateral concessions (e.g., the General System of Preferences) and the “open regionalism” where a group of countries unconditionally extend trade liberalizing measures on a most-favoured-nation basis.

Together, the many smaller and larger agreements that have already been signed, or are currently under negotiation, make PTAs the most prominent and important governance instrument for regulating trade and investment flows of our times. They have become the main tool for achieving market opening and providing regulatory innovation, as multilateral negotiations within the ambit of the World Trade Organization (WTO) have only produced modest results for the last two decades. Moreover, negotiations on plurilateral agreements in the areas of investment (for the Multilateral Agreement on Investment) and intellectual property rights (for the Anti-Counterfeiting Trade Agreement) have failed to produce results that would have been acceptable to a larger number of countries and important segments of civil society. Countries have thus relied on PTAs to regulate issues ranging from trade in goods and services, to investment, intellectual property rights, competition, standards, and government procurement rules.

Although PTAs have attracted considerable scholarly attention, the jury is still out on several key questions. Why do countries sign PTAs? What explains variation in the design of PTAs? How effective are PTAs in promoting trade and changing domestic law and institutions? And what are the consequences of the spread of PTAs for the world trading system? This volume attempts to give answers to these questions and in doing so breaks new ground in several respects. First, the book brings together innovative research by economists, lawyers and political scientists. A multidisciplinary approach seems highly promising for a topic such as PTAs, which involves economic, legal and political aspects. Nevertheless, the various disciplines studying PTAs have produced literatures that hardly talk to each other. The purpose of this volume is to take stock of the empirical and theoretical advances that have been made in the study of trade agreements in the three disciplines. It also aims to stimulate cross-fertilization across these literatures, by showing how researchers from different disciplines tackle the same substantive questions.

Second, so far much of the literature on PTAs has failed to recognize that PTAs are very heterogeneous. Some PTAs include many member countries, others few; some PTAs cover a large number of different issues, from trade in services to government procurement, whereas others are very narrow; and some PTAs include very far-reaching provisions, whereas others are relatively shallow. A substantial proportion of the existing literature on PTAs consists of either case studies that fail to put the key features of a specific PTA into a broader context or quantitative studies that operationalize PTAs in the form of a dichotomous variable, that is, a variable that only captures the presence or absence of a PTA. This state of the art is problematic, as both the causes and consequences of PTAs should vary across agreements of different scope, depth and flexibility. In this volume, we take stock of and contribute to a recent literature that zeroes in on design differences across PTAs.

Finally, compared to the 1990s, when research on PTAs first started to pick up, the phenomenon under study has changed considerably. As discussed above, not only have many new agreements been signed over the past ten years, but these agreements also differ in key respects from the agreements signed even a decade before. By taking into account agreements signed in the 2000s, this volume allows for an assessment of which of the findings of the early studies remain valid, based on a much richer empirical foundation.

In the remainder of this introduction, we first put current PTAs into their historical context, illustrating how they have changed over time, before introducing four major questions that provide the structure for this volume. We discuss the literature related to these guiding questions and highlight the contribution of the various chapters to advancing our knowledge related to PTAs.

## **B. PTAs past and present**

Countries have been signing trade agreements for a long time. The nineteenth century, in particular, saw the spread of trade agreements in Europe (Pahre 2008). The Anglo-French

commercial treaty of 1860 was of great significance, as it ushered in a period of relatively free trade in Europe that lasted until the 1880s. In the period between the two world wars, countries also resorted to PTAs. In the Ottawa agreements (1932), for example, the United Kingdom exchanged preferential tariff concessions with its dominions and colonies. In parallel, the US used the Reciprocal Trade Agreements Act (1934) to conclude trade agreements with Latin American countries, as well as with Canada and the United Kingdom. The effects of these agreements, however, have been seen as far less benign than the agreements signed in the nineteenth century; many observers have blamed them for accentuating the negative effects of the Great Depression (Kindleberger 1973).

After World War II, with a few prominent exceptions, multilateral trade agreements within the framework of the General Agreement on Tariffs and Trade (GATT, 1947) trumped the formation of PTAs. The GATT itself, of course, was originally only a plurilateral agreement signed by 23 countries. But since most countries that engaged in significant amounts of international trade at that time were covered by the GATT's provisions, its discriminatory aspect was limited. Internally, the GATT was built on the principle of non-discrimination, meaning that any concessions towards one member had to be extended to all members of the GATT.<sup>3</sup> Under Article XXIV of the GATT, however, states were allowed to enter into PTAs, but only if these agreements removed 'substantially all' barriers to trade and if the agreement did not increase trade barriers against third countries (Jackson 1997). Only a few countries made use of this exemption in the first four decades of the GATT, the European Economic Community being the main exception.

In 1979, GATT contracting parties agreed upon the so-called "enabling clause", which allowed less-developed countries to grant each other preferences that do not meet the criteria

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<sup>3</sup> Dür (2010) shows how the principle of nondiscrimination was a response to the proliferation of PTAs in the interwar period.

specified in Article XXIV.<sup>4</sup> Under this cover, Latin American countries exchanged preferences in the framework of the Latin American Integration Association and South East Asian countries in the context of the South Asian Free Trade Agreement. Moreover, developed countries could grant developing countries one-sided preferences. Nevertheless, the number of agreements notified to the WTO under this clause remained limited; before 1990, only nine such enabling-clause agreements were notified to the WTO.<sup>5</sup>

Not until the early 1990s, therefore, did PTAs become a prominent tool for economic cooperation. The rediscovery of PTAs started with the deepening of European integration as a result of the Single Market Programme and the signing of the North American Free Trade Agreement (NAFTA) in 1992. In Europe, the end of the Cold War and the dissolution of the Soviet Union created demand for PTAs in the form of association agreements to manage economic relations with former members of the Warsaw Pact. In the Americas, countries started to sign PTAs in the wake of the creation of NAFTA. What followed was a spread of PTAs known in the 1990s as ‘new regionalism’ (de Melo and Panagariya 1992). While initially Asian countries hardly participated in this new wave of PTAs, this situation changed radically around the year 2000. Currently, the majority of the agreements under negotiation involve Asian countries.

More than 700 PTAs were signed between the end of World War II and 2013, the large majority since 1990 (see Figure 1.1).<sup>6</sup> More recently, the number of agreements concluded per year has again been falling, indicating that many of the country pairs that can benefit from a preferential trade link already have a PTA. Up to the early 1990s, European

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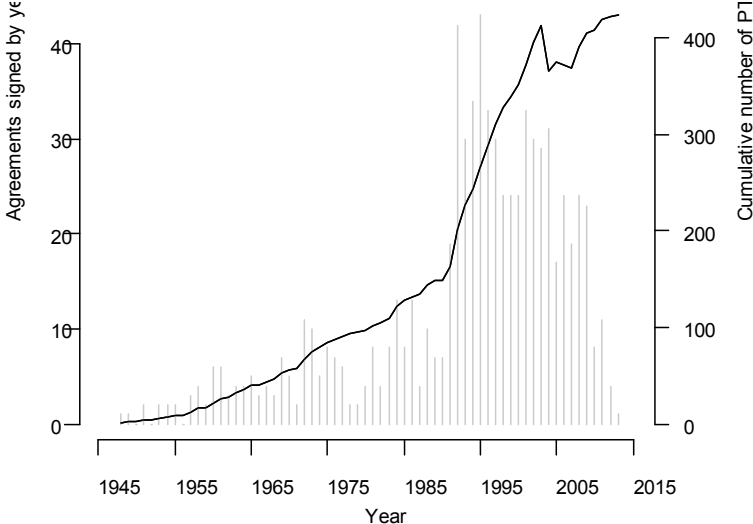
<sup>4</sup> [http://www.wto.org/English/docs\\_e/legal\\_e/enabling1979\\_e.htm](http://www.wto.org/English/docs_e/legal_e/enabling1979_e.htm) [last accessed on 10 February 2014].

<sup>5</sup> <http://rtais.wto.org/ui/PublicMaintainRTAHome.aspx> [last accessed on 10 February 2014].

<sup>6</sup> We draw on data from Dür et al. (2014). The data can be downloaded from [www.designoftradeagreements.org](http://www.designoftradeagreements.org) [last accessed on 10 February 2014].

countries were by far the most avid signers of PTAs (see Figure 1.2). In fact, by 1992, major countries such as China and Japan had not yet signed a PTA.<sup>7</sup> By 2013 countries in the Americas had nearly caught up with their European counterparts with respect to the number of agreements signed. Moreover, as noted above, Asian countries, such as Singapore, have become prominent actors in the spread of PTAs. Most recently, China has shown increasing interest in negotiating PTAs. Illustratively, Switzerland signed a PTA with China in 2013, and Australia and Norway are currently engaged in negotiations with that country.

**Figure 1.1: Number of PTAs over time, 1945-2013**

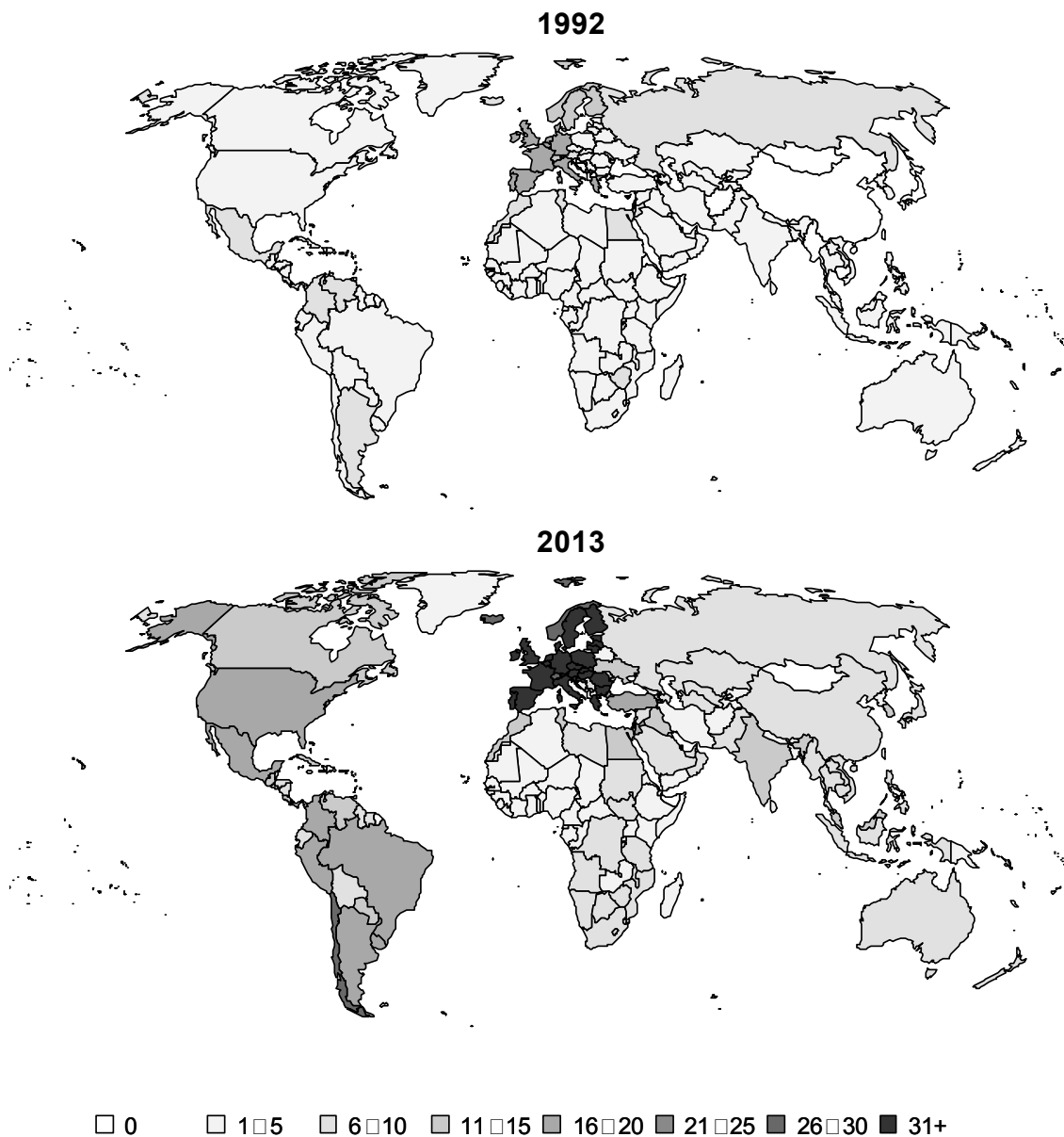


*Source:* authors’ illustration based on data from Dür et al. 2014.

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<sup>7</sup> We compare here to the situation in 1992, as this is the first year after the dissolution of the Soviet Union, meaning that most countries that are in existence in 2013 also existed in 1992.

Figure 1.2: PTAs 1992 and 2013



Source: authors' illustration based on data from Dür et al. 2014.

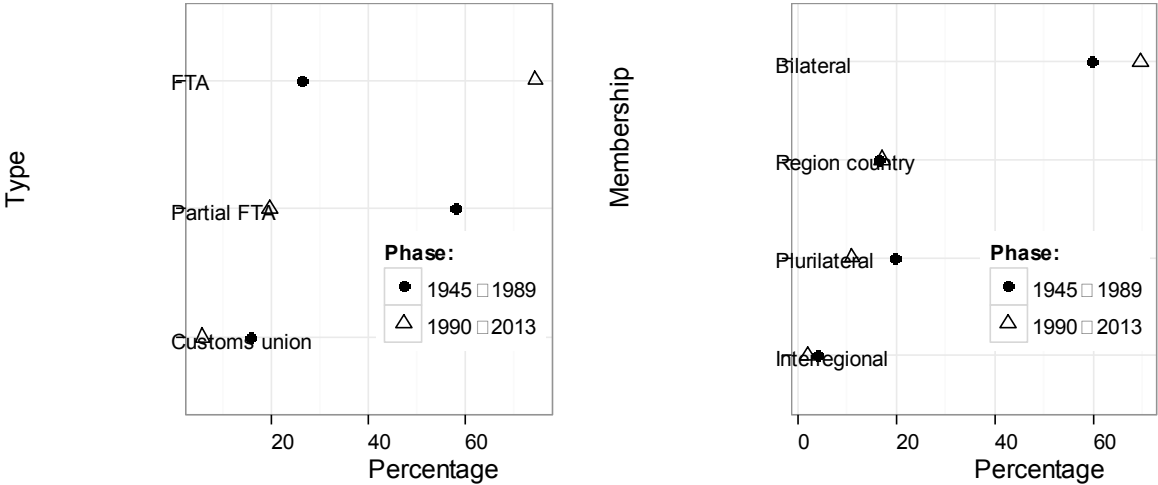
Even more striking than the shift from Europe to the Americas and Asia as the hot spots of PTA negotiations is that many of the new agreements are signed by countries from different continents. No fewer than 26 of 39 PTAs currently (as of November 2013) listed by the WTO under the label of 'early announcement' go beyond a continent.<sup>8</sup> This includes the

<sup>8</sup> See <http://rtais.wto.org/UI/PublicEARTAList.aspx> [last accessed on 10 February 2014].

TTIP and the TPP, but also less obvious pairings, such as Canada–Ukraine. ‘Regionalism’ thus is no longer an appropriate label for this development.

PTAs also vary in terms of type and number of members (see Figure 1.3). The term PTA encompasses partial free trade agreements, full free trade agreements and customs unions. Partial agreements only cut tariffs for a select number of products, and often these cuts do not reduce tariffs to zero. Full free trade agreements, by contrast, liberalize all or substantially all trade among member countries after a negotiated transition period. Customs unions add a common external tariff to a free trade area. While early agreements were mainly of the partial free trade agreement type (with a few customs unions), most recent agreements establish full free trade areas, with customs unions particularly having become very rare.

**Figure 1.3: Change in type and membership over time**



*Source:* authors’ illustration based on data from Dür et al. 2014.

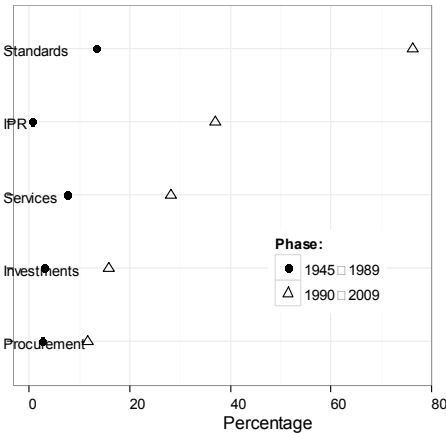
Moreover, a substantial number of the early agreements were of a plurilateral type, that is, they had more than two member countries (see the right-hand pane of Figure 1.3). Many of these agreements are open to new members. The Rome Treaty that established the European Economic Community (1957), for example, was originally signed by six countries, and then expanded to include 28 member countries by 2013. Similarly, the agreement creating



the Central American Common Market (1960) was signed by four countries and then expanded to also include Costa Rica in 1962. More recent agreements, by contrast, are slightly more likely to be of a bilateral nature. The membership of bilateral agreements does not tend to expand; rather, we see that existing members of bilateral agreements sign new agreements with third countries. Not yet captured by the data shown in Figure 1.3, the ongoing negotiations for “mega-regionals”, namely the TTIP and the TPP, may suggest a return to plurilateral agreements in the near future.

But arguably the largest shift in the negotiation of PTAs has been with respect to the contents of these agreements (see Figure 1.4). With a few notable exceptions, most agreements prior to NAFTA only covered trade in goods. NAFTA heralded a much more encompassing type of PTA that contains provisions on trade in goods, but also on behind-the-border issues such as technical barriers to trade, government procurement, investment, services, competition law and intellectual property rights (IPRs). As can be seen from Figure 1.4, many PTAs now have a similar breadth to NAFTA.

**Figure 1.4: Change in the contents of PTAs**



*Source:* authors’ illustration based on data from Dür et al. 2014.

Increasingly, the scope of PTAs even goes beyond the regulation of economic issues: non-trade issues have become more prominent, ranging from environmental concerns, the

promotion of human and labour rights, to addressing new and old security threats (e.g. Hafner-Burton 2005, Spilker and Böhmelt 2012). It is this increasing scope and variation in actual commitment levels that makes PTAs such a fascinating object of study. Building on this discussion, we now move on to present the four key questions that inform this volume and briefly outline the contributions by the authors.

### **C. Why do countries sign PTAs?**

The question why countries sign PTAs started to attract scholarly attention at the time of the formation of the first PTAs in the decades following World War II. A prominent early explanation for the creation of the EU (originally the European Economic Community, which in turn followed the European Coal and Steel Community) focused on the key actors' pursuit of geopolitical goals such as peace and security. As summarized by Andrew Moravcsik (1998: 6), these arguments suggest that 'Postwar European leaders who constructed and extended the EC [European Community] sought to tie down the Germans, balance the Russians, establish a third force against the Americans, overcome right-wing and Communist extremism at home, or suppress nationalism to realize a distinctive vision of European federalism.' Similar arguments have been made for other PTAs. A government may value a PTA for geopolitical reasons if it can use the PTA to increase another country's dependence, allowing it to extract concessions from that country (Hirschman 1945). Alternatively, the aim of a PTA can be to increase a country's military capacity, by creating more trade and thus increasing national income (Gowa 1994). A final geopolitical motivation for trade agreements may be to tackle new security threats, including terrorism and organized crime.

PTAs may also be created to generate welfare gains for the participating countries. In fact, Scott Baier and Jeffrey Bergstrand (2004) found that variables that capture the net aggregate economic gains of the participating countries alone can successfully explain the

overwhelming majority of PTA ties.<sup>9</sup> A specific welfare-related objective for PTAs may be to allow governments to reduce tariffs, without incurring negative terms of trade effects (Bagwell and Staiger 1998). Countries may also benefit in welfare terms if PTAs give firms the opportunity to exploit economies of scale. PTAs offer firms a larger market for their products. A larger market, in turn, allows firms to increase their production and thus to reap gains from lower unit costs. Even if a government is indifferent to its country's welfare, lobbying by firms that expect gains from economies of scale may motivate it to sign PTAs (Chase 2005). Pressure in favour of a PTA may also come from exporters that expect gains from a PTA (Grossman and Helpman 1995). Such exporter lobbying may be particularly strong in countries that are excluded from existing PTAs. Discrimination may impose costs on exporters in these third countries, creating an incentive for them to become politically active and to push their governments to also pursue PTAs (Baldwin 1993; Dür 2010; Baccini and Dür 2012).

Moreover, governments may sign PTAs to tie their hands or lock-in specific policies. In the words of John Whalley (1998: 71), 'by binding the country to the masthead of an international trade treaty, any future reversal of domestic policy reform becomes more difficult to implement.' Finally, democratic governments may use PTAs as a signal to domestic audiences (Mansfield and Milner 2012). The argument is that voters have limited information about government preferences and policies. When the country experiences economic difficulties, the median voter may then punish the incumbent, not knowing whether government policies or an exogenous shock are responsible for the economic downturn. Voters do not oust governments that signed PTAs, however, because signing PTAs is a credible signal that the government is pursuing economically sound policies.

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<sup>9</sup> Some of these variables, such as geographic distance, may also capture other factors, such as geopolitics.

In the first part of this volume, five chapters contribute to this literature. In Chapter 2, Moonhawk Kim argues that changes in what he calls the technological and political infrastructure can explain the broad patterns of the historical development of PTAs. The available technology determines the ease with which goods and services can be traded across borders, and thus the demand for PTAs; and the number of states in the international system, the distribution of power among states, and the presence of war shape the supply of PTAs. Based on an analysis of five periods (1840–1914; 1920s and 1930s; 1947–1990; 1991–2000; and 2001–2013), he finds support for this argument. Edward Mansfield and Helen Milner (Chapter 3) then test a series of explanations for the creation of PTAs, including the role of economic factors, international politics and domestic politics. Based on a dataset that covers PTAs signed up to 2011, they find support for all three explanations. Most importantly, they reconfirm their previous finding that domestic institutions matter: democratic countries are more likely, and countries with many veto players are less likely, to sign PTAs.

In Chapter 4, Jean-Louis Arcand, Marcelo Olarreaga, and Laura Zoratto take up the idea that governments may use PTAs to lock-in specific policies. They find not only empirical support for this argument, but also estimate the welfare benefits that accrue to a country from applying this lock-in strategy. Among their more specific findings is that credibility reasons are particularly important for weak governments and for small countries that sign PTAs with large ones. Importantly, PTAs signed for credibility reasons lead to an increase in imports that is substantially larger than that from comparable agreements. Víctor Umaña, Thomas Bernauer and Gabriele Spilker (Chapter 5) then use a survey experiment to investigate to what extent public opinion may explain different aspects of the new regionalism. Among other things, they find that voters in democracies favour PTAs with other democracies, and with culturally and geographically close countries. These findings may contribute to an explanation of key aspects of the recent spread of PTAs: democratic countries are indeed more likely to sign PTAs with other democracies and cultural proximity also tends to explain the formation

of PTAs. Recent PTAs, however, often include geographically distant countries, which begs the question of what factors trump public opinion.

In Chapter 6 Soo Yeon Kim asks why, after some delay, Asian governments have jumped onto the bandwagon of signing PTAs. Her explanation focuses on the role of production networks that create demand for greater cross-border integration. She shows empirically that production networks can also explain the design of PTAs. The greater the share of trade in parts and components in the overall trade of two countries, the deeper is the agreement that these two countries will sign.

Overall, these five chapters included suggest that there is not a single cause that drives the spread of PTAs. Domestic factors are clearly important (Chapters 3–5); but international factors cannot be neglected either (Chapters 2 and 3). However, what also becomes clear is that considering variation in the design of PTAs may help answer the question of the causes of PTAs. Explanations for the design and a discussion of design differences of PTAs make up the second part of the volume.

#### **D. The design of PTAs**

The second part of the book looks in more detail at the design features of PTAs. This focus is important, because countries' reasons for signing trade agreements can only be fully understood by focusing on the content of PTAs; states are *ex ante* only willing to enter an agreement if they anticipate some gains from liberalizing specific areas. Gaining insights into variation in PTA design will also benefit research on the impact of these agreements on a wide array of issue areas (see below). Multiple attempts have thus been made in the past ten years to collect data on issue-specific areas (Estevadeordal et al. 2009, Kucik 2012), the PTAs of key trading powers (Horn et al. 2010) and PTAs in particular regions (Hicks and Kim 2009). In this context, the Design of Trade Agreements (DESTA) Database has been the most ambitious project to collect design data over time and across areas (see Dür et al. 2014).

This research has been used to measure the extent of concessions in relation to liberalization (the depth of an agreement), the degree of opt-outs both short and long term (flexibility), and how PTA provisions can be enforced through dispute settlement mechanisms (enforceability). Using these measures, the literature has shown that some design features are a function of PTA-inherent characteristics. For instance, the flexibility and depth of an agreement are related (Baccini et al. 2013), and there also is a relationship between depth and enforceability (Downs et al. 1996).

Building on this literature, the contributions to this volume offer a series of novel explanations for the design of PTAs. In Chapter 7, Leonardo Baccini, Andreas Dür and Yoram Haftel argue that in designing PTAs, countries select from a series of ‘model PTAs’. Concretely, countries can decide whether they want to sign an EU-type, a NAFTA-type, or a Southern-type PTA. Using data from DESTA, they explain which countries opt for which model. They find that over time, countries are increasingly signing NAFTA-type agreements; by contrast, the appeal of the EU model seems to be declining. Bilateral and North–South agreements are particularly likely to follow the NAFTA model. The level of development, however, does not seem to influence the choice of PTA design.

Chapter 8 by Mark Manger focuses on the depth of agreements. His analysis shows how the type of trade structure affects market access related to tariff elimination negotiated in PTAs. Focusing on a sample of PTAs including Asian economies, he finds that if PTA partners’ trade relations are characterized by intra-industry trade, this is more likely to lead to liberalization than a trade structure that is endowment-based. In Chapter 9, Kerry Chase then analyses provisions regarding audiovisual services in PTAs. Using a dataset of 116 services PTAs, he presents an index of audiovisual services commitments. He finds that countries make greater commitments when they have made concessions on audiovisual services liberalisation in the WTO, when PTAs are deep, when they opt for a negative-list approach, and when the US is a member of the PTA. Fewer commitments are observed when PTA

parties use a positive-list approach, when PTAs are concluded between developing and developed countries, and when PTAs include Canada or the EU.

The contribution by Tim Bütte and Anu Bradford (Chapter 10) focuses on competition-related content in PTAs. It is one of the first studies to address, in a systematic way, whether and how competition policy has been taken up in these agreements. Using a random sample from the list of agreements in the DESTA dataset, they first show a trend towards the inclusion of competition chapters and competition articles in trade agreements. They then present two theoretical perspectives on what states might achieve in regulating competition in PTAs. Their findings, although mixed, suggest that states are not concerned about the use of competition policy as a protectionist device, but have a genuine desire to combat anti-competitive practices. Countries include competition provisions in PTAs in response to the opportunities for cross-border collusion created by market integration.

Stephanie Rickard's chapter (Chapter 11) focuses on the public procurement rules in PTAs. She describes the commitments contained in PTAs and then provides potential explanations as to why they are included in PTAs. Her argument rests on the finding that the procurement rules contained in PTAs are rather shallow (and flexible) and do not seem to be effective, that is, they do not increase foreign buying by governments. This suggests that governments use procurement chapters in PTAs as political cover when they have to buy foreign goods or services.

An interesting and overlooked nexus exists between trade and security. Contributing to the study of this relationship, Chapter 12, by Yoram Haftel, focuses on the landscape of security institutions within a sub-set of PTAs: regional economic organizations. He shows how security sub-structures have become an important feature of formerly predominantly economic cooperation projects. He offers three explanations for the nesting of security institutions, namely intra-regional violent conflict, the existence of a regional hegemon, and the absence of regional rivalries within a region. He shows using a fuzzy-set qualitative

comparative analysis (fsQCA) which of the explanations presents a necessary condition for the presence of security cooperation institutions. The evidence lends support to the absence of rivalry explanation, but not to the other two.

Finally, in Chapter 13 Todd Allee and Manfred Elsig focus on the design and role of dispute settlement mechanisms in PTAs. They show that dispute settlement in PTAs exhibits more variation than has been acknowledged so far. After presenting various specificities of processes and obligations in the dispute settlement provisions, they present new ideas on how to think about dispute settlement in the context of PTAs. These concepts go beyond the usual narrow focus on how legalised litigation is. They portray more nuanced roles of dispute settlement systems, such as providing information, enforcing commitments, promoting the settlement, or allowing for targeted flexibility and suggest variables to measure these concepts and make them fruitful for empirical investigation.

### **E. The effects of PTAs**

Analyses of the effects of PTAs, especially on trade flows, have a long tradition. In his seminal contribution, Jacob Viner (1950) distinguished between the trade creating and trade diverting effects of PTAs. He showed that intra-PTA liberalization of trade can create new trade between partners in the PTA; it can also lead to a diversion of trade from more efficient producers outside the PTA towards less-efficient producers inside the PTA. In the decades following Viner's discovery, a steady flow of publications reported on studies of the trade effects of particular PTAs (e.g. Aitken 1973). Only in the late 1980s, however, did research on the trade effects of PTAs really take off. When the US first concluded the US–Canada agreement, and later NAFTA, economists tried to find out what consequences these agreements would have. Early on, Paul Wonnacott and Mark Lutz (1989) suggested that PTAs among 'natural trading partners' could be expected to be trade creating; for other PTAs, trade diversion would dominate. In his influential book, Jeffrey Frankel (1997) then found



that most regional trade blocs have a substantial effect on trade flows, and that trade creation often trumps trade diversion.

Much of this early literature, however, suffered from several shortcomings. First, PTAs are not exogenous to trade flows; larger trade flows may make countries sign PTAs. Interestingly, once this endogeneity is accounted for, the estimated trade effects of PTAs become even more pronounced (Baier and Bergstrand 2007). Second, the effects of PTAs on trade flows may differ depending on whether two countries already trade a specific product, or whether no trade has so far taken place. Research into this issue showed that PTAs do not create trade where none existed before; but they are related to an increase in positive trade flows (Egger et al. 2011). Finally, the early literature largely failed to account for the significant differences in the design of PTAs. Remedying this shortcoming shows that most trade is created by deep PTAs; shallow PTAs only have a small effect on trade flows (Dür et al. 2014).

The literature on the effects of PTAs is not limited to analyses of trade flows. Much research has also tackled the question whether PTAs attract foreign direct investment (for example, Bütte and Milner 2008; Peinhardt and Allee 2012). In addition, some recent studies have looked at the consequences of PTAs for human rights in member countries (Hafner Burton 2009). Finally, PTAs have been linked to the presence and absence of international conflict and war (Mansfield and Pevehouse 2000; Haftel 2012). Remarkably, for most of these areas, research has found that PTAs make a difference. Evidently, the relevance of PTAs goes far beyond trade.

The contributions included in the third part of this volume nicely complement and build on this literature. In Chapter 14, Scott Baier, Jeffrey Bergstrand, and Matthew Clance argue that since PTAs are signed for different reasons, they are likely to vary in terms of their effects on trade. In fact, the authors' empirical analysis shows that the effects of PTAs on trade flows vary strongly across PTAs. Although nearly all agreements increase trade flows,

for some PTAs these effects are negligible and for others they are large. They find that variation in the depth of agreements only partly explains variation in the size of their trade effects. Other factors, such as distance between member countries, and common language, religion or legal origins, explain a large amount of the variation in trade effects.

The chapter by Peter Egger and Sergey Nigai (Chapter 15) addresses the same question of heterogeneous effects of PTAs, but comes to a quite different conclusion. Using a measure of scope based on the presence or absence of 48 cooperation areas in an agreement, they find that differences in design matter a great deal for the trade effects of PTAs. These gains in trade that result from deep PTAs also translate into welfare gains for member countries: deep PTAs on average thus are welfare-improving, with gains of up to 10 per cent for most countries.

Anirudh Shingal's chapter (Chapter 16) offers still another extension of this literature: not only can the effects of PTAs on trade be expected to vary across PTAs, but also a PTA may have different effects for different types of "products". Concretely, Shingal analyses the impact of PTAs on trade in services. His study takes account of the endogeneity of membership in services PTAs and also considers that services trade agreements are not implemented in one go. Moreover, the chapter advances the state of the art in drawing on a dataset that covers more countries for a longer time period. The findings show that PTAs increase trade in services but that much of this effect is driven by the EU.

In Chapter 17, Jeffrey Kucik shows that PTAs may not only affect levels of trade, but also volatility in trade flows. Volatility in trade flows leads to costs, for example by accentuating business cycles and reducing job security. Governments thus have an incentive to reduce volatility and PTAs offer one instrument to achieve this objective. But, Kucik, argues, PTAs will only be effective in achieving this aim if they both tie the hands of their members and offer them some flexibility to react to shocks. The empirical evidence does

indeed show that flexible agreements have a greater impact on the reduction of volatility than rigid agreements.

Finally, Chapter 18 by Chad Bown, Baybars Karacaovali, and Patricia Tovar investigates the effect of PTAs on the use of temporary trade barriers. Relying on four case studies, they show that governments can react in very different ways to the creation of a PTA. In some cases, they use temporary trade barriers to reinforce discrimination in favour of PTA members; in other cases, they use the same barriers to reduce discrimination. The contribution suggests that the relationship between PTA obligations and the use of temporary trade barriers needs further examination and that a more in-depth focus on the design could be one way forward.

These chapters thus offer support for this volume's main argument that it is important to study the design of PTAs. Clearly, the effects of PTAs vary depending on whether they are shallow or deep; and whether they are flexible or rigid. This may also prove an important insight for the debate on the relationship between PTAs and the multilateral trading system, which we take up in the fourth part of this volume.

#### **F. PTAs and the multilateral trading system**

The final part of the book focuses on the relationship between preferentialism and multilateralism. PTAs have dominated the international trade regulation landscape for the past 15 years. By contrast, progress in the WTO negotiations has been limited since the conclusion of a series of post-Uruguay agreements, including the Information Technology Agreement (ITA), in the late 1990s. The deal on food security and trade facilitation reached at the 2013 Bali Ministerial conference of the WTO has also not provided momentum to swiftly conclude the Doha Round of multilateral trade negotiations that has been ongoing since 2001. Nevertheless, with WTO rules having been integrated in PTAs, the multilateral trading system remains important. This point is reinforced by the fact that the WTO now has 159 members,

meaning that the fate of the WTO is crucial for global economic governance. The study of the relationship between preferentialism and the multilateral trading system thus remains pertinent.

The main question that has been debated in this context is whether PTAs are stumbling blocks or stepping stones for multilateral trade liberalization (for an overview of the debate, see Panagariya 1999). On the one hand, PTAs have been pictured as a stumbling block for further liberalization and rule-making in the WTO (Bhagwati 1991). By investing in bilateral and regional trade deals, so the argument goes, the pressure on states to liberalize multilaterally decreases. This also deprives the multilateral system, characterized by package deals, of the opportunity to offer sufficient benefits to all participating actors, because PTAs reduce potential multilateral gains. On the other hand, PTAs are characterized as stepping stones towards multilateral liberalization (Lawrence 1996). They serve as venues where innovation and further liberalization takes place, creating incentives not only to engage in ‘open regionalism’, but also offering possibilities for ‘multilateralizing’ PTA-specific rules (see Baldwin and Low 2009). This latter view sees PTAs and the multilateral system as complementary. As stated in the declaration of the Ministerial Meeting of the WTO in Doha (2001), ‘regional trade agreements can play an important role in promoting the liberalization and expansion of trade’ (World Trade Organization 2001: 1).

Despite much research into this question, particularly informed by a legal perspective that has focused on the compatibility of PTA commitments with WTO obligations (Bartels and Ortino 2006), on the empirical side, the jury is still out. The four contributions to this volume that address this topic bring out new and innovative aspects related to the PTA-multilateralism debate to advance on this state of the art. Thomas Cottier, Charlotte Sieber and Gabriela Wermelinger propose in Chapter 19 a legal-historical analysis of what they view as a dialectical relationship between multilateralism and preferentialism. That multilateralism and preferentialism can stimulate each other has so far been largely overlooked in this debate.

Moreover, whereas most work zooms in on tariff liberalization, their contribution addresses regulatory progress. They show that, for instance, the intellectual property rights part of the multilateral system (Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS agreement)) was inspired by bilateral agreements between European states in the early nineteenth century. By contrast, they trace how innovation in services regulation was strongly shaped both by progress in the 1980s in the GATT and the Uruguay Round negotiations leading to the General Agreement on Trade in Services (GATS) and some innovation in US and EU trade deals. The GATS commitments and regulatory philosophy today influences the services chapters of the new generation PTAs. Drawing from various examples, the authors are optimistic that innovation in today's PTAs can be brought back to the multilateral table.

While much of the debate has focused on the relationship between the WTO and PTAs, Chapter 20 by Joost Pauwelyn and Wolfgang Alschner suggests that the concerns of legal scholars about fragmentation of international trade law have not sufficiently addressed challenges stemming from the relations between PTAs themselves. In their contribution, they carry out an analysis of the contemporary PTA network that shows the existence of several regional PTA clusters (which confirms the results presented in Chapter 7), with the EU at the centre of the network. Pauwelyn and Alschner also show that the signing of the mega-regionals that are currently being negotiated would transform this network and lead to a “ball of wool”-like PTA network. Building on this network analysis, they then focus on double-PTAs, that is, agreements where the same countries find themselves parties to at least two different PTAs, usually with distinct compositions of PTA members. They not only focus on the reasons why states engage in double-PTAs, but also how these interrelate. This issue of overlapping membership in PTAs could have great implications for the WTO which have so far not been analysed.

Whereas the contribution by Pauwelyn and Alschner focuses on inter-PTA relations, Bernard Hoekman (Chapter 21) argues that PTAs might have led to a renaissance of sectoral or plurilateral approaches within (or in parallel to) the WTO. These mechanisms have received more attention in recent years as countries excluded from the mega-regional arrangements, such as the TPP and the TTIP, have started to explore ways in which to gradually multilateralize the best features of regulatory cooperation established in PTAs into the WTO. He encourages an active use of variable geometry with leadership provided by a number of middle powers, that is, countries with a moderate influence on world affairs.

Finally, the contribution by James Flett brings the reader back to what is currently the most successful feature of the WTO, its so-called jewel in the crown, the dispute settlement mechanism established with the creation of the WTO in 1995. Flett suggests ways in which this system could be made available for PTA parties in the interpretation of PTA law. He reminds the reader of the need to have a strong and binding dispute settlement system. One question that arises from this analysis is whether special terms of reference could be drawn upon to allow PTA disputes to be litigated in the WTO. According to him, such an approach would have advantages for both PTA and WTO Members. Finally, he addresses practical concerns related to financing, scheduling, third parties, adjudicative responsibility and WTO consistency. He shows how, if WTO and PTA members are willing, the WTO flagship institution could be ‘regionalized’.

These contributions show that the relationship between the multilateral system and PTAs is multifaceted, that legal questions of coherence start to become more prevalent in PTAs with increasing numbers of double-PTAs, and that innovation in plurilateral and sectoral agreements could prove important for multilateralizing PTAs.

## **G. Conclusion**

PTAs have become the dominant form of trade cooperation at the beginning of the twenty-first century. The chapters in this volume provide an overview of advances in the study on PTAs, offer new insights, suggest novel answers to long-standing research questions, and sketch new avenues for future research. The volume shows that research on PTAs in law, political science, and economics may profit from cross-fertilization between disciplines in order to push the research frontier forward. Law scholarship has so far mainly focused on the question of compatibility between WTO and PTA obligations. Future scholarship following in the footsteps of the legal contributions in this volume could develop a more diverse research agenda. Combining forces with other disciplines might help in particular to answer questions related to enforcement (see Horn et al. 2010) and implementation of PTA commitments and on how PTAs affect domestic law. Economics research has mainly focused on both the economic rationale for signing PTAs and the estimation of PTAs' effects on trade flows. Contributions to this volume show that paying greater attention to variation in the design of PTAs – a point that has been pushed mainly by political scientists and lawyers – can help advance economists' research agendas. Finally, political science approaches have sharpened our understanding of the politics surrounding the negotiations of trade agreements and have highlighted the multiple purposes these agreements might serve while taking the rule of law seriously and engaging with the economics literature on the design and effects.

What future avenues exist for PTA research? Certainly, the continued political attention devoted to PTAs and the ongoing work to provide more accurate data on PTAs will provide further momentum in the study of PTAs. In this future work, researchers should pay increased attention to the effects of PTAs not only on economic indicators, but also on domestic institutions, politics and law. Moreover, research should increasingly focus on the diffusion of best practices in PTA regulation and theorize the conditions under which, and what type of, regulatory innovation may be multilateralized through the WTO or unilaterally applied by non-PTA members. In addition, the new mega-deals that are on the horizon will

pose interesting research questions. Which templates will be agreed upon and to what degree are these suitable for other PTAs? To what extent will countries be able to deviate from the EU–US model? Finally, what will China’s trade cooperation strategy look like? This is not only a question of distributional consequences or the need to minimize transaction costs, but it suggests that PTAs may be used more and more as a prominent vehicle for pursuing strategic foreign policy objectives in a multipolar trade world. This volume might help prepare the basis for tackling these and other research questions as it calls for the study of PTAs using advanced methods drawing on a multidisciplinary setting and collecting systematic information on various PTA dimensions, such as scope, depth, flexibility, enforcement and implementation of these agreements.

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