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Please cite this paper as:

VanGrasstek, C. (2011), "The Political Economy of Services in Regional Trade Agreements", *OECD Trade Policy Working Papers*, No. 112, OECD Publishing. doi: 10.1787/5kgdst6lc344-en

OECD Trade Policy Working Papers
No. 112

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JEL Classification: F13, F15, F59

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Abstract

THE POLITICAL ECONOMY OF SERVICES IN REGIONAL TRADE AGREEMENTS

by

Craig VanGrasstek

Do the services commitments that countries have made in their post-Uruguay Round regional trade agreements (RTAs) indicate the types of concessions that they would be willing to multilateralise in the General Agreement on Trade in Services (GATS)? While there are important legal and economic dimensions to ponder in answering this question, considerations of political economy must also be taken into account. This paper focuses on issues in political economy that underlay RTAs in general, and especially the specific commitments and concessions that countries make on trade in services. It examines in detail the way that considerations of political economy have helped to shape the RTAs of Chile, Japan, the European Union and the United States. These four case studies help to develop and test a series of hypotheses regarding the international and domestic political factors that influence why RTAs are negotiated in the first place, between what kind of countries and with what kind of content, especially with respect to their provisions affecting services. The analysis rejects on a preliminary basis the hypothesis that RTAs create constituencies opposed to multilateral liberalisation, and finds empirical support for other hypotheses that are more multilateral-friendly.

Acknowledgements

Dale Andrew, Sébastien Miroudot, and Iza Lejárraga of the OECD Trade Policy Linkages and Services Division of the Trade and Agriculture Directorate provided comments on earlier drafts.

JEL classifications: F13, F15, F59

Keywords: regional trade agreements, political economy, trade in services, WTO, GATS, multilateralising regionalism

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Executive Summary

This paper focuses on issues in political economy that underlay regional trade agreements (RTAs) in general, and especially the specific commitments/concessions that countries make on trade in services. May we safely conclude that the services commitments that countries have made in their post-Uruguay Round RTAs indicate the types of concessions that they would be willing to multilateralise on either a *de facto* basis (by autonomously extending them to other parties) or *de jure* (by inscribing these commitments in their GATS schedules)? While there are important legal and economic dimensions to ponder in answering this question, considerations of political economy must also be taken into account.

This analysis is an exercise in political economy, a social science that examines how states and other actors pursue objectives of both power and wealth. The effort here is not to develop a deterministic set of rules regarding how the services provisions of RTAs are negotiated, but instead to unearth any patterns that help us to understand the relevant trends and to consider the implications for RTA partners, third parties, and the trading system. It does so by putting forward a series of hypotheses and testing them against the available data, seeking to determine whether the actual decisions made by states conform to these expectations. The examination encompasses two distinct yet related levels of inquiry. One is at the international level, where political and economic factors shape countries' objectives in their relations with specific partners and their aspirations for the multilateral system. Another concerns the domestic politics of trade policy, as played out within government (in its various branches and levels) and the contending segments of civil society. At both the international and the domestic level there are numerous issues in political economy that might serve either to advance or retard any given country's interest in treating their RTAs as multilateral building blocks rather than discriminatory stumbling blocks.

Part I of this study reviews the broader issues in the political economy of RTAs and the services provisions in these agreements. Part II examines in more detail the way that considerations of political economy have helped to shape the RTAs of Chile, the European Union, Japan, and the United States. These four case studies, supplemented by data on the RTA practices of other countries, help to develop and test a series of hypotheses regarding the international and domestic political factors that determine why RTAs are negotiated in the first place, between what kinds of countries, and with what kind of content, especially with respect to their provisions affecting services. Part III provides conclusions and implications, as well as recommendations that stem from these views.

Political considerations play a more important role in RTAs than in multilateral trade initiatives, and infuse the choices that countries make in the launch and conduct of RTA negotiations. Even more than a multilateral trade agreement, an RTA may represent the use of a commercial instrument to achieve political ends. The multilateral-friendliness of a given RTA depends in part on the strategic motivations of the countries that crafted it.

Some RTAs are deliberately designed with the multilateral system in mind, and are intended to set precedents on either big matters (e.g. the inclusion of new issues) or smaller ones (e.g. specific deals within those issues). An RTA might alternatively be intended for purposes that inhibit multilateralisation, such as cementing the special relationship between two countries or, in the shorter term, as a reward or inducement that one country offers to another.

In the domestic political economy of RTAs and services, policymakers generally oppose the practice of rulemaking-by-treaty. By comparison with tariffs and other issues affecting trade in goods, there are far more governmental institutions (different ministries, regulatory agencies, parliamentary committees, sub-national units of government, etc.) involved in the regulation of trade in services. Countries' willingness to make commitments in services are often inhibited by the horizontal fragmentation of power either between branches of government (executive versus legislative) or within them (trade ministries versus other ministries or agencies), and in some countries the problem is further exacerbated by the vertical fragmentation of power (national governments versus subnational units of government). These sometimes quarrelling institutions may be willing to liberalise the laws that govern services sectors and to make commitments on these matters in trade agreements, but only if the reforms follow that sequence.

The paper teases out these points by presenting and testing seven hypotheses about the political economy of services provisions in RTAs. While one of those hypotheses is unsupported by the evidence, and hence should be rejected, six are either strongly or partially supported by the data.

The one hypothesis that is rejected may be the most significant. It states that those agreements that are inspired in large measure by one country's desire, for reasons of foreign policy, to extend preferential treatment to another may be less likely than other agreements to include provisions that are intended to set precedents for multilateral liberalisation. While the concerns over captive markets and managed trade may be very real for trade in some goods sectors (e.g. apparel), the data examined in this report suggest that there is little reason to fear that this will be the case for services. The European Union and the United States are more likely than others to negotiate RTAs that are politically motivated. The evidence shows that while the services provisions of the RTAs of the EU and the United States do differ according to the type of trading partner with which they are reached, these agreements offer little in the way of preferential treatment. One important implication of this observation is that these RTAs do not create disincentives to multilateral bargaining on services. In this negative sense, therefore, we might conclude that the services deals reached in RTAs are not multilateral-unfriendly.

Four other hypotheses concern the international political economy of RTAs and services, and are either multilateral-friendly or not intrinsically problematic:

- RTAs may be used by countries as a means of advancing issues that have either not made it on the agenda of the multilateral negotiations or on which progress has stalled.

- The more trade-dependent countries will be attracted to RTAs with countries that represent large shares of their trade. Countries that are larger and less trade-dependent may be more attracted to RTAs with smaller countries.

- Wealthier countries in which services account for a larger share of the economy are more likely to include services in the scope of their FTAs than are less developed countries where services are less prominent.

- In negotiations between partners of asymmetrical size, it is likely that the larger partners will extract deeper concessions from the smaller.

Put another way, RTAs tend not to be negotiated between the larger industrialised countries, and when they are negotiated between developing countries they tend not to cover services, but when a large, industrialised country negotiates an RTA with a developing country and that agreement covers services it will often provide for GATS-plus commitments, especially on the part of the developing country. The agreement might also provide for some commitments that set precedents for areas of "unfinished business" in the GATS, such as government procurement.

The hypotheses relating to the domestic politics of RTAs and services carry less favourable implications. Evidence is presented here to support both of them:

- To the extent that legislators, civil servants, and other domestic policymakers involved in the regulation of services are willing to (1) enact market-opening rules (laws, regulations, etc.) and to (2) approve international agreements that consolidate these reforms they will prefer that the steps be taken in that order and not vice versa.

- RTA negotiators may sometimes over-estimate the extent to which they may liberalise sensitive sectors. This can result in confrontations at home that affect the terms of the agreement in question and/or future RTAs.

The implications of these points, especially the first, depend on the degree of ambition that one has for the trading system. If one has very modest goals, it may be sufficient for trade agreements to consolidate the reforms that countries have already undertaken in their domestic laws and regulations and not to produce new reforms that must then be reflected in international agreements. RTAs that adhere to this precept may serve a useful purpose by providing a means by which (1) some of the older reforms that were not yet consolidated in the original GATS schedule are now inscribed in an RTA schedule (we might call this "removing the old water"), and (2) those reforms that have been enacted since the end of the Uruguay Round are also consolidated in RTAs ("removing the new water"). The precedents that are thus set in the RTAs might then be generalised in the GATS schedule when the Doha Round is concluded.

If one is more ambitious, an RTA would ideally produce liberalisation that is both (1) real and (2) extended on an MFN basis to non-parties. That appear to be quite possible in principle, but it is difficult to quantify just how often that has happened, or will happen, in actual practice. To develop a complete answer to the question we would need a comprehensive set of data not only on those commitments that countries make in their GATS schedules and in RTAs, but also on what their applied measures are and any discrimination that might be made in the application of these measures. There nonetheless appear to be at least some cases in which countries have made commitments in RTAs that achieve real liberalisation, and that they then extend the application of these reforms not only to their RTA partners but to other partners as well. The *de facto* multilateralisation that is thus achieved might later be made de jure if it is inscribed in the country's revised GATS schedule. In this sense RTAs may also be seen as multilateral-friendly, but only to

a degree that is empirically uncertain, could be legally fragile, and is ultimately contingent upon completing a multilateral negotiation that currently has no end in sight.

This report makes a few, modest recommendations for future reform. One is to remove some of the opacity of the relationship between domestic laws, the commitments in RTAs, and countries' GATS schedules by producing detailed information on each country's applied and bound measures (both in GATS and in RTAs) in all commercially important services sectors. Reforms might also be considered in the ways that services negotiations are conducted in the WTO. This could include a mechanism by which countries are encouraged to update their GATS schedules in order to reflect in their multilateral commitments what has already been achieved in their national laws. That should be an especially easy step in the case of any reforms that were initially achieved through domestic reform, were later inscribed in RTAs, and then extended to third countries on a de facto basis.

Part I: The Political Economy of Services Provisions in RTAs

Introduction

What impact do regional trade agreements (RTAs) have on the multilateral trading system in general, and on trade in services in particular? This is an issue that is often examined from legal and economic perspectives, but also needs to be seen through the lens of political economy. RTAs are arguably the most political of all instruments in conventional trade policy, due both to the motivations that give rise to them and the effect that they have on excluded parties, and one cannot understand why countries choose this option or how they craft their agreements without taking into account matters of economic statecraft and domestic politics.

RTAs have long been a source of controversy. For over half a century analysts and policymakers have debated the impact that these agreements have on multilateralism. One important question concerns the extent to which RTAs might serve as either "building blocks" or "stumbling blocks" for multilateral agreements (Lawrence, 1991). On the positive side, they may constitute down-payments that countries might later incorporate, in whole or in part, in their commitments at the multilateral level, while also establishing precedents for the inclusion of new issues within the scope of trade policy. On the negative side, the proliferation of RTAs may contribute to a balkanisation of the trading system, the multiplication of competing rules of origin, and the creation of national constituencies that are more interested in preserving preferential arrangements and exploiting captive markets than in promoting global deals. Are the concerns over RTAs as stumbling blocks as justified for trade in services as they are for the more traditional issue of trade in goods? To find an answer we must examine the political dynamics of RTAs and their services provisions.

The examination that follows is an exercise in political economy rather than economics *per se*. It puts forward a series of hypotheses regarding the way that states negotiate RTAs, especially with respect to services, taking into account political considerations at both the national and international level. It then tests these propositions against the available data, recognizing that the data here are not as complete as one would ideally wish.[1] The analysis is undertaken in full recognition of the fact that international economic negotiations are multifaceted undertakings, and that no set of objective data can fully capture all of the subjective considerations that affect countries' decisions to enter into negotiations or their conduct within these talks. No attempt is made here to find any "prime movers" or to devise "iron laws" of state action with respect to services and RTAs. To the extent that there are identifiable patterns that can be discerned in countries' choices, however, it is possible to reach at least preliminary conclusions on how states and other actors behave, and to consider the implication of these patterns for the states

1. As discussed in the concluding section, the analysis that follows would be improved if more and better data were available not just on the commitments that states make in their RTAs but on their applied measures.

that negotiate RTAs with one another, for third parties, and for the trading system as a whole.

The political dynamics of RTAs and their services provisions can be seen at two levels, which we may identify as economic statecraft (international political economy) and the domestic politics of trade (national political economy). At the risk of oversimplification, we might say that economic statecraft informs our understanding of strategic issues and that domestic political economy helps us to understand matters at the tactical level. The main strategic questions are why countries choose to negotiate RTAs in the first place, with whom they opt to negotiate, and what kinds of content they seek for these agreements. The principal tactical questions concern what sectors are or are not covered in an agreement, responding to the expressed or assumed interests of a country's firms, industries, and workers, as well as the ministries, regulatory agencies, legislative bodies, and sub-national units of government that may be involved in the regulation of a sector.

The broad outlines of the kinds of considerations that emerge from these two levels of political economy are summarised in Table I.1. As shown in the table, there are a variety of different strategic orientations that countries might take with them into a negotiation, each of which carries different implications for the multilateral-friendliness of the resulting bargains. As discussed in the section immediately below, these can be divided into the grand-strategic orientation that might motivate the most influential participants in the WTO system, in which the kinds of RTAs that they negotiate may reflect their broader aspirations for the multilateral system, and a series of other strategic doctrines that might be adopted by countries at any level of economic development and political influence. The table also summarises the implications of issues that might arise in the domestic politics of trade, which might either promote or retard the efforts to multilateralise the bargains that are incorporated in an RTA.

Table I.1. Illustrative list of political-economy considerations behind RTAs that may retard or accelerate the multilateralisation of their provisions

Category	Classification	Degree of Multilateral-Friendliness
Grand-Strategic	RTA as game-changer: A leading purpose of the RTA is to establish the precedent for covering an issue that has not previously been "on the table" in multilateral negotiations, and to demonstrate how it might be covered.	High: The rules and commitments set in the agreement should definitely be seen as potential material for multilateralisation in a concurrent or later negotiation.
Strategic Economic	RTA as gap-filler: A leading purpose of the RTA is to "fill the gap" that is left by either the absence of multilateral negotiations or the failure to achieve rapid progress in them.	High: Because the main purpose of the RTA is to achieve piecemeal what the country eventually hopes to achieve globally, the commitments that it seeks and is prepared to make offer a preview of what it hopes the multilateral agreement will look like.
Strategic Political	RTA as the expression of a special relationship: A leading purpose of the RTA is to recognise and enhance an historic, special relationship between the partners.	Low: There may be a greater tendency in such agreements to establish higher levels of preference for the partner(s), and thus a greater reluctance to multilateralise.
Strategic Political	RTA as reward: A leading purpose of the RTA is to encourage or reward some desirable action taken by the partner(s) either in that country's domestic or foreign policy.	Low-to-Medium: A country might want the preferences in a special relationship to be unique and permanent, but deals that are made on a transactional basis might be repeated with other partners.
Domestic Economic	RTA as lock-in mechanism: The country has made significant reforms in its domestic laws in one or more sectors and wants to extend even greater confidence to foreign investors by locking the reforms into treaties.	High: The more agreements in which the reforms are locked in, and the larger the partners with which this is done, the more confidence those investors will have.
Domestic Economic	RTA as a means of promoting a national champion: The country has certain competitive sectors for which it seeks to promote exports, and wishes to open markets.	High: The country will be even more eager to open global markets for this sector than RTA markets.
Domestic Economic	RTA as captive market: The country hopes that by maintaining relatively high barriers to the world while establishing an open but managed relationship with certain partners it can sustain a troubled industry.	Low: The benefits for the dying industry depend on reaching agreements only with a limited circle of partners that are prepared to engage in managed trade. (Note: This is much more of an issue for trade in goods.)
Domestic Political	RTA as protector of sacred cows: Due to political or cultural reasons, certain sectors may be considered "off limits" in any trade negotiations.	High: But high only in the sense that the isolation of the sector will be sought in agreements at all levels of aggregation.

Economic statecraft

We may very loosely define "economic statecraft" here to be that set of practices in international relations by which states either employ their wealth in order to promote their power or vice versa.[2] It includes the use of such diverse instruments as trade barriers (and agreements to reduce or eliminate them), sanctions, investment policy, foreign assistance, exchange rate policy, etc., in order to achieve not only commercial objectives but also to promote such equally diverse ends as peace, victory, regional stability, the strengthening of allies, the weakening of actual or potential adversaries, security of supply for vital

2. For a more detailed definition of economic statecraft see Baldwin (1985), especially Chapter 3.

goods (food, fuel, and armaments), leverage to promote changes in the foreign or domestic policies of another country, etc. Economic statecraft thus encompasses a broader range of issues than does ordinary trade policy, which might be seen as a subset of the larger category. The main distinction is between means (the instruments of policy) and ends (the objectives of policy): Whereas in ordinary trade policy both the means and the ends may be defined in relatively narrow, commercial terms, in economic statecraft some of those same means may be employed in pursuit of altogether different ends.

The political ramifications of one class of RTAs can be vastly greater than the others. The negotiation of a customs union (CU) is sometimes a first step towards a common market, and necessarily implies a greater commitment on the part of its members to subordinate the exercise of their sovereignty. The ultimate objective may go even farther, with CUs and common markets being tied to political unification of formerly separate states. The negotiation of an FTA, which are far more numerous than CUs, is a more modest undertaking that will typically raise fewer issues over sovereignty. The significance of CUs as exercises in nation-building or region-building is taken up in the European Union (EU) case study, including the different approaches that the European Union takes towards those countries that are candidates for accession to its CU. Another and related issue concerns the efforts on the part of great powers not just to negotiate RTAs of their own but to encourage economic integration in regions where they hope to promote prosperity and stability.

Most of our attention here will be devoted to matters of policy that fall below such existential concerns, but that are nonetheless important. They may be divided into the grand strategic and the strategic uses to which a country might put RTAs. Grand-strategic considerations are those that speak to countries' aspirations for the trading system as a whole, or even the broader system of international relations in which trade is just one component, and are especially significant when examining the agreements reached by the largest and most influential participants in that system. The strategic political considerations are those issues in foreign and economic policy that countries of all sizes and levels of development take into account when deciding whether to negotiate RTAs in the first place, with whom, and on what terms.

A grand-strategic perspective requires that an analyst step aside from the legal assumptions that underlay the Westphalian system of sovereign equality and recognise that while all states are equal under the law, some states are more equal than others in power and influence. We may go further to say that while all states may have strategic aspirations for their trade policy, in the sense that all of the major decisions that countries make in trade policy are presumably part of a broader vision concerning the direction and objectives of their policies, not all WTO members are equal in their ability to pursue grand-strategic objectives for the overall regime. The RTAs that are negotiated by the largest and most influential members of the WTO are sometimes intended not merely to address the issues in their relations with the immediate negotiating partners, but instead for the system as a whole.[3]

While few can play at the grand-strategic level, all countries of all sizes have strategic perspectives. The term "strategic" is meant here to encompass both the principal motivations behind a given RTA negotiation and the broader economic objectives that the

3. See Part II for a brief discussion of how this same point applies to the more recent RTAs of the EU. See also Horn, Mavroidis, and Sapir (2009) for a comparative review of the different ways that the European Union and the United States use RTAs to promote "WTO-extra" provisions (i.e. issues that do not yet fall within the scope of WTO law).

agreement is intended to serve. Strategic considerations can be economic, political, or (most often) a combination of the two, and they define why a country opts (or not) to pursue RTAs as well as the main orientation that it will take towards the terms of the agreement. Depending on the nature of a country's strategy, that orientation may either increase or decrease the chances that the concessions it makes in a given RTA are susceptible to generalisation in a later, multilateral agreement.

The most basic strategic question is how a country's leadership perceives the place of RTAs in their broader goals. Countries differ in the extent to which their RTAs are intended to serve diplomatic, commercial, or other purposes. Even in countries where RTAs are seen only as economic instruments there are various strategic purposes that they might be intended to serve; they may be equally important to one country that is committed to liberalisation through all available means, and to another that is primarily interested in gaining or retaining preferential and exclusive access to a major economy.

One key strategic issue concerns the extent to which a country intends for an RTA to extend truly preferential treatment to a partner, and how long it might expect that preference to last. As a very general rule, we might conclude that the multilateral-friendliness of an RTA will be lowest in those cases where the parties to the agreement approached it primarily as a political undertaking, they intended to establish preferential treatment towards one another that was especially deep, and they hoped to maintain this preferential treatment for as long as possible. In such cases, the very existence of the RTA might be seen as a threat to the parties' commitment to further progress in the multilateral system. At the other extreme, the most multilateral-friendly RTAs will be those that are motivated more by commercial than political objectives, and that are seen by their proponents principally as a means of achieving with a small circle of partners in a short time-frame the same kinds of objectives that they eventually hope to multiply in a global agreement.

The domestic politics of trade

Domestic politics also shape countries' strategic decisions to negotiate RTAs, and are even more important in determining at the tactical level what kinds of commitments countries seek or grant in these agreements. As the evidence presented in Part II suggests, this aspect of political economy may pose greater problems for the multilateral-friendliness of the services provisions in RTAs than does the practice of economic statecraft.

To simplify, the political scientists who look to domestic political factors in order to explain countries' choices between openness and closure tend to fall into three general camps. The oldest and perhaps largest school of thought depicts this choice as the outcome of struggles between competing economic interests. Openness represents the triumph of pro-trade interests such as exporters, retailers, and consumers over import-competing industries, labour unions, or others that are typically trade-sceptical. A second category of explanations shifts the locus of conflict from civil society to government, and sees openness as the triumph of pro-trade institutions (e.g. the executive branch in general, the foreign ministry, etc.) over their trade-sceptical rivals (e.g. legislatures or client-oriented ministries). Yet a third approach pays more attention to ideas than to interests. Analysts in this school argue that openness represents the victory of liberal ideology over protectionist doctrines. While the debates among the proponents of these three schools of thought are sometimes conducted as if the

explanations were mutually exclusive, it is possible that each one captures some part of the truth. In any given country the decision to open the market may be influenced by a mixture of sectoral, institutional, and ideological factors.

These competing explanations of the domestic political economy of trade were all developed in studies of traditional (i.e. goods-centric) policy. But what of trade in services? How does the introduction of this topic affect the mix? One of the most interesting aspects of the domestic political economy of trade in services is that services differ from goods in ways that complicate each of these three schools of thought.

Consider first the sectoral explanation. One major difference between goods and services is that producers in some services sectors are less likely to think of themselves as producers in the first place, much less as actual or potential exporters. Service sectors differ tremendously in the extent to which their providers are aware and active on trade issues. At one end of the spectrum is the financial services sector in the industrialised countries, where a handful of firms (especially American Express and American International Group) were instrumental in convincing U.S. officials in the early 1980s to place a high priority on bringing trade in services within the scope of General Agreement on Tariffs and Trade (GATT) and FTA negotiations.[4] At the other end of the spectrum are those service sectors in which many of the providers do not think of themselves as being in an "industry" in the first place. That would include many of the services that are performed (in varying degrees in different countries) by governments, including educational, health, and social services. Even in the United States, for example, which consistently runs a major surplus on trade in educational services, associations representing teachers and administrators in higher education have been reluctant to join the for-profit segment of the industry in pressing for other countries' concessions in their sector. Matters are made all the more complicated by the fact that in some services sectors we find notable exceptions to the general rule that consumers are not active participants in public debates over trade policy. The consequences of this very important point are examined below in the discussion of the ideological school of domestic trade politics.

A second and perhaps greater difference between goods and services concerns the division of labour among governmental institutions. While it is now accepted in most countries that a given ministry has the authority (subject to established political and legal procedures) to negotiate on the country's behalf in traditional areas such as tariffs, that same ministry's authority is often not as clear in the case of services. Regulatory authority in services is always fragmented horizontally (i.e. there are typically a great many regulatory agencies or line ministries whose jurisdictions are at issue), and in many countries it is also fragmented vertically (i.e. subnational units of government such as states, provinces, *länder*, cantons, etc. may have exclusive or shared regulatory authority in some sectors). Matters are more complex when legislative institutions are involved; this third corner of the "iron triangle" (interest groups, agencies, and legislative committees) can sometimes be the sharpest, and they may be more concerned over the delegation of authority in services than is the case for tariffs.[5] Even when policymakers in

4. For an account of how this issue first became a U.S. priority and then part of the GATT agenda see Kennedy (1988).

5. Consider for example the difference between the delegation by the U.S. Congress of tariff-negotiating authority during the period of 1934-1962, which allowed the president to implement by proclamation any agreements that were reached within the limits set by law (i.e. executive agreements), versus the more demanding requirement since 1974 that any

these other divisions, branches, and levels of government can be convinced that issues within their jurisdiction should indeed be subject to international negotiations, they will often prefer that trade negotiators make no commitments that, from their perspective, put the cart before the horse. It may well be the case that they have already undertaken a reform program at home, revising laws and regulations to remove internal and external barriers to competition. In such cases they may have few or no objections to inscribing these reforms on the country's services schedule in either the GATS or an RTA (perhaps leaving some "wiggle room" for subsequent adjustment). There may be much greater resistance, however, to proposals that would mean making the country's laws adjust to its treaty obligations rather than the other way around. We can ordinarily expect policymakers in any branch of government (executive or legislative) and at any level of government (national or sub-national) to have a strong preference, both on policy and institutional grounds, for treaties that stay within the lines of the status quo over those that amount to rulemaking-by-treaty.

Finally, the ideological arguments surrounding trade liberalisation are more complex for services than they are for goods, involving as they do more fundamental questions of the proper roles of the market and the state in providing services. There are not many countries left in the world, and certainly not in the OECD, where there are serious arguments any more about whether the state or the market should take the lead in the production and supply of goods (apart from exceptional cases such as nuclear weapons). In many sectors, however, the provision of services is either the joint or the exclusive domain of the government. Countries differ widely in the precise sectors that they choose to treat as essential services that should be provided by the state, and thus be rationed not through markets and price signals but instead through government policy, but there is hardly a modern state that does not do so for at least some subsectors of the transportation, education, health, and other social service sectors. Proposals to place these services "on the table" are sometimes seen or at least portrayed by their providers (especially unionised civil servants), and even the broader public, as a threat that could reduce the supply of these services, raise the costs, and even undermine a country's social contract. The politics of the issue are further complicated by the involvement of consumers. Whereas consumer activism tends to be inhibited by the public-goods problem in most other areas of trade, some categories of consumers – for example, students and the elderly – are more easily organised. The result may be, at least in some countries and in the more sensitive sectors, a reduction in both the propensity of countries to request commitments from their partners, and the propensity of their partners to respond favourably to these requests.

trade agreements on non-tariff matters be subject to the development of implementing legislation that must then be approved by the legislature (i.e. congressional-executive agreements). The services sector is among the areas in which the development of this implementing legislation can require careful consultations between the two branches.

Part II: The Political Economy of RTAs and Services: Four Case Studies

Introduction

The main task in this second part is to examine the political economy of services provisions in RTAs, principally by using four case studies – Chile, the European Union, Japan, and the United States – but also by making reference to the RTAs of other countries. We proceed first by summarizing the role of RTAs in their trade strategies, then propose and test a series of hypotheses regarding the domestic and international political economy of RTAs. These cases respectively represent four waves in the evolution of discrimination in the multilateral system. Chile is among the countries that were interested in regional integration even before the start of the GATT period, and the predecessor arrangements to the European Union got underway shortly after GATT took effect, but the United States did not begin negotiating RTAs until late in the GATT period, and Japan did not do so until the WTO period had already begun.

One major difference among the cases is in their distinct levels of trade dependence. As shown in Figure II.1, trade is more economically important for Chile and especially the EU members than it is for Japan and the United States. The United States has not only the highest motivation to use trade as an instrument of statecraft (given the breadth of its global commitments), but can also do so at the lowest risk (less of its economy is at stake). It is reasonable to expect that balancing economic and political objectives may be a more delicate task for the European Union, given the group's high degree of trade dependence as well as the differing extent to which members have delegated authority on trade *versus* foreign policy; that Japan may be less inclined to use RTAs as a tool of statecraft because it has less expansive global commitments; and that Chile may be the least likely to do so, both because of its higher economic dependence and lower political profile.

These points should not be taken too far, as it would be too simplistic to reduce this observation down to a claim that "RTAs are economic instruments for countries that are trade-dependent, and political instruments for countries that are more self-sufficient." Non-economic considerations certainly played an important role in Chile's RTA negotiations,[6] for example, and even more so for the European Union, and no one could seriously argue that commercial interests are absent in the RTA negotiations of Japan and the United States. These are differences in degree rather than kind. Economics and

6. Schiff (2002) noted the geopolitical considerations that underlay Chile's RTA negotiations with its neighbours, while Edwards and Edwards (1992) stressed the importance of RTAs as an instrument for assuring the business community that the economic policies adopted during the military dictatorship would survive the transition to democracy.

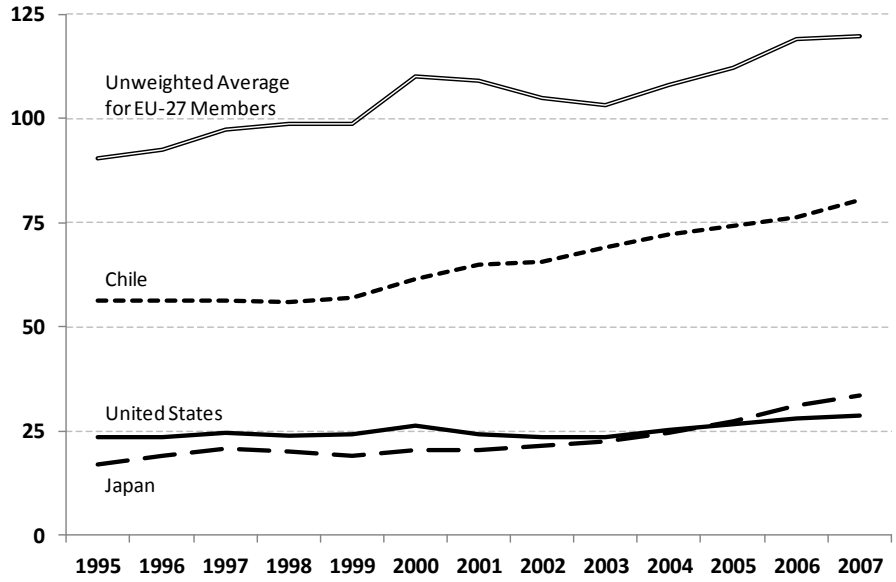
politics will always matter to all countries, but it stands to reason that the relative share of non-economic considerations is likely to be inversely correlated with the degree of a country's trade dependence.

Evolving strategic doctrines

We start by providing a quick review of the evolving role that RTAs have played in each of these three countries' trade strategies, in order of their turn towards RTAs. Every country can be said to have an implicit strategic doctrine on these instruments, even if it has no RTAs (which may indeed be the clearest strategy of all). Each of our four cases has experienced an evolution in its doctrine towards discrimination in the global trading system, and in its own use of RTAs as a tool of economic statecraft.

Figure II.1. Relative significance of trade for selected economies

Sum of Exports and Imports of Goods and Services as a Percentage of GDP



Source: Calculated from World Bank data at http://data.worldbank.org/indicator/NE.IMP.GNFS.ZS (for imports) and http://data.worldbank.org/indicator/NE.EXP.GNFS.ZS/countries (for exports), accessed 30 October 2010. EU-27 data include intra- and extra-EU trade.

RTAs in Chile's trade strategy

Chile's promotion of regional agreements predated the establishment of the GATT system. For generations Chilean trade negotiators showed much greater eagerness to pursue economic integration with other Latin American countries than with industrialised countries. That was the case in 1889-1890, for example, when the Chilean delegates to the failed International American Conference were the chief opponents of a U.S. proposal to establish a hemispheric agreement inspired by the German *zollverein*. A generation later, Chile was among the Latin American republics that did not negotiate reciprocal trade agreements with the United States during the 1930s and 1940s. Chile's desire "to give trade preferences to neighbouring Argentina, Peru, and Bolivia" proved to be a problem, as "Washington opposed any exception to the unconditional

most-favoured-nation principle" (Steward, 1975). Disputes over these matters ensured that the 1933-1944 negotiations over a Unitd States–Chilean trade agreement never produced a text.

Chile was a leading advocate for regional exceptions in the diplomacy that produced the Havana Charter and the GATT, where it "pressed hard for a general exception to the rule of most-favoured-nation treatment that would allow Latin American countries to continue to grant particular advantages to their neighbors" (Brown, 1950). Chilean trade policy from the founding of the GATT through the early 1970s nevertheless oscillated between openness and closure, with changes in government often leading to major shifts in policy. The military government that took control in 1973 imposed a more open regime, including low and uniform import tariffs, no exchange or trade controls, and minimum capital restrictions. These reforms were achieved autonomously rather than through negotiations. Once democracy was restored in 1989, concerns arose over whether the established economic reforms would survive the new political reforms. Could prospective foreign investors be confident that future governments would be equally committed to economic openness?

Chile responded to these concerns by pioneering the strategy of using trade agreements as a means of "locking in" autonomous economic reforms and making them credible over the long term. Employing an approach that one analysis called "additive regionalism" (Harrison, Rutherford, and Tarr, 2001), Chile embarked on a policy of comprehensive RTA negotiations while also pursuing regional and multilateral agreements. Successive Chilean governments have all accepted three essential propositions: (1) Chile is a competitive exporter that will benefit from open markets; and (2) while the country should promote openness at the multilateral level its influence within the WTO is limited; so (3) Chile should simultaneously negotiate agreements at the bilateral, regional, and multilateral levels in order to come as close as possible to open access to all of its export markets. Even on a unilateral basis, Chile is willing to reduce its barriers by establishing an across-the-board tariff that is low, uniform, and declining. Given that clear strategic direction, the commitments that Chile makes in its RTAs may be indicative of the types of bargains that it is prepared to make multilaterally.

Table II.1 summarises the trade agreements that Chile has reached with its partners throughout the world. Chile's first major RTA negotiation outside of South America came in 1995, when it held abortive negotiations over accession to NAFTA. Those talks failed due to an internal problem in the United States that postponed negotiations for several years, but did not prevent FTAs with the other two NAFTA partners. Since then Chile has been an especially active negotiator, and has become so prolific and proficient in this area that it has come to be seen by some partners as a source of advice and training. That has been especially notable in Asia: Korea approached Chile for its first FTA in 1999, hoping to use the talks as a kind of "on the job training" for FTA negotiators, and Chile was also an early FTA negotiating partner for Japan (after Singapore and Mexico) and China (after ASEAN).

Table II.1. The RTAs of Chile

Agreements in effect listed in chronological order; others in alphabetical order

Partner(s)	Year Entered into Effect	Type	Share of Chile's Trade (2009)	
			With Partner	Cumulative
Bolivia	1993	Partial Scope Agr.	1.27	1.27
Venezuela	1993	Partial Scope Agr.	0.94	2.21
Ecuador	1994	Partial Scope Agr.	1.41	3.62
MERCOSUR	1996	Assoc. member	12.23	15.85
Canada	1997	FTA	2.02	17.87
Mexico	1999	FTA	2.81	20.68
Costa Rica-El Salvador-Guatemala-Honduras	2002-2008	FTA	<0.99	21.67
European Union	2003	Econ. Assoc. Agr.	17.20	38.87
Republic of Korea	2004	FTA	5.59	44.46
United States	2004	FTA*	14.20	58.66
EFTA	2004	FTA	>0.75	59.41
Brunei-New Zea.-Singapore	2006	Econ. Assoc. Agr.*	>0.79	60.20
China	2006	FTA	19.56	79.76
India	2007	Partial Scope Agr.	1.48	81.24
Panama	2008	FTA	N.A.	81.24
Peru	2009	FTA*	2.19	83.43
Colombia	2009	FTA	1.92	85.35
Japan	2007	FTA	6.87	92.22
Australia	2009	FTA*	0.69	92.91
Malaysia	[Under way]	TPP*	0.26	93.17
Turkey	[Under way]	FTA	0.27	93.44
Vietnam	[Under way]	TPP*	0.25	93.69

Note that some of the agreements above supersede others previously reached with the same partners.

Note that data are missing for trade with Brunei Darussalam, Iceland, Liechtenstein, and Panama, and that data on trade with all of Central America and the Caribbean are aggregated.

* A partner in the Trans-Pacific Partnership negotiations.

Source: Compiled and calculated from Organization of American States and Banco Central de Chile.

RTAs in the EU trade strategy

While the RTA experiences of every country or group may be said to be *sui generis* to one extent or another, that of the European Union is more *sui* than the other three. A common market that negotiates FTAs and even CUs with other partners presents a more complex set of analytical problems than do the FTAs negotiated by single countries. The European Union's negotiations are the outcome of not merely two-level games (i.e. political economy at the national and international levels) but bring in the third dimension of regional politics. The lines that separate national and regional authority are already blurred, and becoming more so with the rising authority of the European Parliament to review and approve (or not) the European Union's trade agreements. While leaders in this legislature support the use of RTAs as a means of promoting EU foreign policy objectives in developing countries (Moreira, 2010), the body's growing

responsibilities may make the politics of EU trade policymaking ever more complex in the coming years.

The linkages between trade and foreign policy are arguably tighter in the European Union than anywhere else in the world, in the origins of the European Union itself if not always in the conduct of its external relations.[7] Consider the existence of the common market itself, which was inspired by two very political needs: to foster common interests among the major European powers in order to prevent the outbreak of a new war among them, and to band together in the face of the threat of possible war with the Soviet Union (Eilstrup-Sangiovanni and Verdier, 2005). The process by which Europe has moved from a customs union to a common market to a political union can be seen as a continental replication of that process by which economic integration often precedes political unification. The sequencing of economic and then political integration in the European Union and its predecessor arrangements is not entirely new, but represents instead a continental application of what Germany achieved in the 19th century. The parallels are in fact quite close, with the original *zollverein* of 1818 expanding both in geographic scope and in political substance until the founding of the German Empire in 1871 – a length of time (53 years) that is only slightly shorter than that which elapsed between the establishment of the European Coal and Steel Community in 1952 and the entry into force of the European Union's Lisbon Treaty in 2009 (57 years).

The links between trade and foreign policy are also evident in the European Union's selection of RTA partners. These negotiations tend to involve countries that are either candidates for membership in the European Union or were former colonies. Of all the countries shown in Table II.2, Korea is the only one that cannot be classified as either (1) part of Europe or (2) a former colony, protectorate, or mandate territory of one or more European countries. The negotiations with some European countries are part of the pre-accession process, and may aim at bringing the candidate closer to conformity with EU disciplines; they may thus be seen as something between an ordinary FTA and the expansion of the common market. As for those partners that were once part of the Belgian, British, French, Portuguese, or Spanish empires, they enjoy special relationships with their former mother countries and, through them, the European Union as a whole. Those special relationships have been expressed in a series of trade instruments, of which economic partnership agreements (EPAs) are the latest iteration. As we will see later, the approach that the European Union takes towards services in the RTAs reached with these two different sets of negotiating partners differs markedly.

The RTAs of the European Union are thus more multifaceted undertakings than those of the other three cases studied here. The European Union already has more RTAs in effect than Chile, but they tend to be with smaller partners. Even if all of the agreements now under negotiation were completed and implemented, they would still cover less than half of all extra-EU trade. The coverage of actual and potential EU RTAs (44.6% of 2009 trade) is in fact quite similar to the levels of coverage for the actual and potential RTAs of both the United States (41.6%) and Japan (38.4%), and – as taken up later – that is partly a consequence of one similarity in these large economies' negotiating strategies. Unless and until these three major trading powers negotiate RTAs among themselves, or with China, they cannot expect to see RTAs have anything near the same coverage as Chile.

7. For critical views of the EU's pursuit of external economic and political objectives, and with particular reference to how these affect Economic Partnership Agreements, see Brown (2005) and Pilegaard (2007).

Table II.2. The RTAs of the European Union

Agreements in effect listed in chronological order; others in alphabetical order

Partner(s)	Year Entered into Effect	Type	Share of European Union's Trade (2009)	
			With Partner	Cumulative
Syria	1977	FTA	0.2%	0.2%
Andorra	1991	CU	<0.1%	0.2%
European Economic Area	1994	Econ. Integ'n Agr.	11.9%	12.1%
Turkey	1995	CU	3.5%	15.6%
Faroe Islands	1997	FTA	<0.1%	15.6%
Palestinian Authority	1997	FTA	<0.1%	15.6%
Tunisia	1998	Assoc. Agreement	0.7%	16.3%
Israel	2000	Assoc. Agreement	0.9%	17.2%
Mexico	2000	Global Agreement	1.1%	18.3%
Morocco	2000	Assoc. Agreement	0.8%	19.1%
South Africa	2000	FTA	1.4%	20.5%
FYR of Macedonia	2001	FTA	0.1%	20.6%
Croatia	2002	FTA	0.7%	21.3%
Jordan	2002	Assoc. Agreement	0.1%	21.4%
San Marino	2002	CU	<0.1%	21.4%
Chile	2003	Assoc. Agreement	0.5%	21.9%
Lebanon	2003	FTA	0.2%	22.1%
Egypt	2004	Assoc. Agreement	0.8%	22.9%
Algeria	2005	Assoc. Agreement	1.4%	24.3%
Albania	2006	FTA	0.1%	24.4%
Bosnia & Herzegovina	2008	FTA	0.2%	24.6%
Montenegro	2008	FTA	<0.1%	24.6%
Cameroon	2009	FTA	0.1%	24.7%
CARIFORUM	2009	EPA	0.4%	25.1%
Côte d'Ivoire	2009	FTA	0.2%	25.3%
Serbia	2010	FTA	0.4%	25.7%
Colombia	[Signed]	FTA	0.3%	26.0%
Korea	[Signed]	FTA	2.3%	28.3%
Peru	[Signed]	FTA	0.2%	28.5%
All Other ACP	[Under way]	EPA	3.0%	31.5%
Canada	[Under way]	Comp. Econ. & Trade	1.8%	33.3%
India	[Under way]	FTA	2.3%	35.6%
MERCOSUR	[Under way]	FTA	2.7%	38.3%
Singapore	[Under way]	FTA	1.5%	39.8%
Gulf Cooperation Council	[Under way]	FTA	3.5%	43.3%
Ukraine	[Under way]	FTA	0.9%	44.2%
Central America & Panama	[Under way]	Assoc. Agreement	0.4%	44.6%

Source: Compiled and calculated from European Union statistics.

RTAs in the U.S. trade strategy

The United States has also gone through a series of changes in its approach to RTAs. The country had long been opposed to discrimination, which it equated with protectionism, and for the first four decades of GATT history was the most vocal proponent of multilateralism. Apart from an exceptional trio of preferential arrangements that carried over from the Spanish-American War of 1899 (i.e. with Cuba, the Philippines, and Puerto Rico), and one new responsibility that it took on in the immediate aftermath of the Second World War (i.e. the Trust Territory of the Pacific Islands), the United States conducted its trade on the basis of strict MFN treatment in the early years of the GATT system. Both for that reason, and because of the long-standing U.S. opposition to the Ottawa System of the British Commonwealth, it is not surprising that "[t]hroughout the entire history of the negotiation of the [Havana] Charter and the [GATT], United States leadership was directed towards the elimination of preferences" (Brown, 1950). American statesmen nonetheless came to favour the creation of the European Union and its predecessor arrangements, seeing this as a means of promoting European unity in the face of potential Soviet aggression.

It was not until the 1980s that the United States itself began to negotiate FTAs.[8] The very first FTA (with Israel) was pursued for political reasons, and there were some political aspects to the other agreements negotiated before 2000. It is no coincidence that the negotiations over the U.S.-Canada FTA (begun in 1986 and concluded in 1988) and the North American FTA that the United States reached with Canada and Mexico (begun in 1991, concluded in 1992, and revised in 1993) came during the start- and end-games, respectively, of the Uruguay Round. The first of these FTAs was intended by U.S. policymakers not only to govern the world's largest bilateral trade relationship but also to set significant precedents for the multilateral system. These included the question of whether the multilateral trade regime would encompass what were known at that time as the new issues (i.e. services, intellectual property rights, and investment). This was a point that was quite hotly contested in the mid-1980s, and for which the U.S. position ultimately prevailed. The threat to "go bilateral" was demonstrated most dramatically by negotiating the FTA with Canada; the United States-Canadian trade relationship is the largest such dyad in the world. The NAFTA negotiations then came at a later stage, and allowed the U.S. policymakers to build on the United States -Canada precedent and offer an example of how bargains can be reached between developing and industrialised countries on the new issues.

Prior to the administration of George W. Bush, it had been the policy of three successive presidents to use discriminatory agreements as a means of leveraging multilateral negotiations. In an approach articulated by James Baker (1988), who served in both the Reagan and the first Bush administrations, this strategy used the bilateral threat in order to inspire other trading partners to be more forthcoming first in the GATT. While that aspect of competitive liberalisation remains a part of the U.S. strategy, it also sits somewhat uneasily alongside another set of objectives. Over the past decade the United States has used FTAs as an instrument in diplomacy, linking them to such seemingly unrelated issues as security affairs (most notably in the U.S. efforts both to promote peace and to build a Coalition of the Willing in Iraq) and commercial diplomacy.

8. Prior to the negotiation of the U.S.-Israel FTA, the only important discriminatory trade agreement that the United States reached in the GATT era was the U.S.-Canada Auto Pact of 1965.

The degree of leverage that the United States enjoys in FTA negotiations is enhanced by the fact that most agreements negotiated since NAFTA have been reached with smaller countries (see Table II.3), and the diminutive size of some partners' markets makes clear that there are other considerations in play besides commercial objectives. The North American neighbours are the only FTA partners of the United States that individually account for more than 3% of U.S. merchandise trade. By contrast, the four Arab partners with which the United States has concluded FTAs collectively account for just over one-fourth of one percent of U.S. merchandise trade.

Table II.3. The RTAs of the United States

Agreements in effect listed in chronological order; others by category and in alphabetical order

Partner(s)	Year Entered into Effect	Type	Share of U.S. Trade (2009)	
			With Partner	Cumulative
Israel	1985	FTA	1.00	1.00
Canada	1989	FTA	15.94	16.94
Mexico	1994	FTA	11.35	28.29
Jordan	2001	FTA	0.08	28.37
Chile	2004	FTA*	0.59	28.96
Singapore	2004	FTA*	1.43	30.39
Australia	2005	FTA*	1.06	31.45
Morocco	2006	FTA	0.08	31.53
Bahrain	2006	FTA	0.04	31.57
CAFTA-DR	2006-2009	FTA	1.52	33.09
Oman	2009	FTA	0.08	33.17
Peru	2009	FTA*	0.35	33.52
Colombia	[Signed]	FTA	0.80	34.32
Panama	[Signed]	FTA	0.18	34.50
Republic of Korea	[Signed]	FTA	2.65	37.15
Brunei Darussalam	[Under way]	TPP*	0.01	37.16
Malaysia	[Under way]	TPP*	1.29	38.45
New Zealand	[Under way]	TPP*	0.18	38.63
Vietnam	[Under way]	TPP*	0.62	39.25
Ecuador	[Suspended]	FTA	0.36	39.61
S. African Customs Un.	[Suspended]	FTA	0.45	40.06
Thailand	[Suspended]	FTA	1.01	41.07
United Arab Emirates	[Suspended]	FTA	0.51	41.58

*: A partner in the Trans-Pacific Partnership negotiations.

Source: Compiled and calculated from inter alia Office of the U.S. Trade Representative and U.S. International Trade Commission.

RTAs in Japanese trade strategy

It is not an exaggeration to consider Japan "the last domino" among the major trading countries in the transition from a period in which RTAs were the exception to one where they are very nearly the rule. Japan long had reason for concern over discrimination against it by other countries. It did not join the GATT until 1955, and many of the other contracting parties invoked the non-application clause (GATT Article XXXV) upon its

accession. Many of the most restrictive measures that other countries imposed on imports in the 1970s and 1980s, such as the negotiation of "voluntary" export restraints, were targeted against Japan.

The shift in Japan's orientation towards RTAs began somewhat hesitantly in the early WTO period. In 1998 President Ernesto Zedillo of Mexico proposed bilateral negotiations, and a year later Prime Minister Goh Chok Tong of Singapore did so as well. Both proposals led to the establishment of bilateral study groups that then recommended that FTA negotiations be initiated, but the agreement with Singapore was concluded three years before the talks with Mexico were completed. Between the time that the FTAs with Singapore and Mexico were signed, Japan developed a formal policy on RTAs. That was soon followed by FTA negotiations with Korea and then with others as well (see Table II.4).[9]

Japan's turn to RTAs appears to have been motivated principally by economic interests, being inspired both by regional integration initiatives in Europe and the Americas in the 1990s and concerns over the prospects for progress in the multilateral system. If Japan did not negotiate RTAs of its own, it was feared, it might not gain market access to growing, mostly Asian economies. RTAs are also seen as a means of promoting structural adjustment in the Japanese economy, which was still recuperating from an elongated period of stagnation when the strategy was adopted, and that must also plan for a future in which the country faces significant demographic challenge. Political considerations have also played a role, especially with respect to the competition with China for influence both in and out of their shared region (Box II.1). A different set of political considerations may also be evident in the case of Japan's RTA negotiations with Peru, a country with a large Japanese diaspora.

Table II.4. The RTAs of Japan

Agreements in effect listed in chronological order; others in alphabetical order

Partner(s)	Year Entered into Effect	Type	Share of Japan's Trade (2009)	
			With Partner	Cumulative
Singapore	2002	EPA	2.37	2.37
Mexico	2005	EPA	0.85	3.22
Chile	2007	EPA	0.59	3.81
Philippines	2008	EPA	1.17	4.98
Rest of ASEAN*	2008-2009	EPA	11.40	16.38
Switzerland	2009	EPA	1.11	17.49
Australia	[Under way]	EPA	4.14	21.63
Gulf Cooperation Council	[Under way]	FTA	9.56	31.19
India	[Under way]	EPA	0.89	32.08
Republic of Korea	[Under way]	EPA	6.11	38.19
Peru	[Under way]	EPA	0.20	38.39

* Japan has EPAs with both ASEAN as a group and with individual members Brunei, Indonesia, Malaysia, the Philippines. Singapore, Thailand, and Vietnam. For the sake of clarity, only those bilateral agreements that entered into effect prior to the Japan-ASEAN agreement are listed here separately.

EPA = Economic Partnership Agreement.

Source: Compiled from Ministry of Foreign Affairs of Japan and Ministry of Finance of Japan.

9. See Urata (2005) for a review of these events.

Box II.1. RTAs as an instrument of Chinese "soft power"

China offers one of the clearest examples of a country that uses RTAs as a key tool of economic statecraft. It has agreements in place with ASEAN, Chile, Chinese Taipei, Costa Rica, Hong Kong, Macau, New Zealand, Pakistan, Peru, Singapore; is negotiating them with Australia, the Gulf Cooperation Council, Iceland, Norway, and the Southern African Customs Union; and is actively exploring negotiations with India, Korea, and Switzerland.

The topic of China's "soft power" has become the focus of a great many studies, most notably in U.S. think tank and government circles. See deLisle (2010), Kurlantzick (2006), Lum (2008), and McGiffert (2009) for examples of studies that tend to emphasise the power rather than the soft side of the equation, and depict the proliferation of China's FTAs as one of the many means by which that country both acquires and exercises influence. Among the issues associated with these FTAs are access to raw materials to fuel Chinese industries, territorial disputes, competition with Japan and the United States for influence in the Asia-Pacific region, and even – through the suspension of bilateral negotiations with Norway – Beijing's protest over the awarding of the Nobel Peace prize in 2010 to Chinese dissident Liu Xiaobo.

RTAs have also been one of the instruments used by both the People's Republic of China and Chinese Taipei in their competition for recognition by foreign governments. Consider China's FTA negotiation with Costa Rica, "which was formally kicked off only one year after the tiny Latin American country switched alliances to China by breaking up with Taiwan" (Gao, N.D.: 9). Moreover, China has sometimes sought to interfere with Chinese Taipei's negotiation of RTAs, especially – but not only – when they are sought with partners outside the circle of countries that recognise Chinese Taipei. For example, the two Chinas clashed over Chinese Taipei's efforts to negotiate an FTA with Paraguay in 2004; the fact that Paraguay recognises Taipei but its MERCOSUR partners recognise Beijing has complicated the efforts to conclude an FTA, and while the initiative has not been fully abandoned its outcome is doubtful (Bishop, 2004). The cross-straits competition over RTAs may now have subsided with the conclusion of the Economic Cooperation Framework Agreement between Beijing and Taipei. In addition to being an FTA between the two Chinas this initiative offers a framework through which China is expected no longer to object to Chinese Taipei's negotiations of FTAs with third parties (Jennings, 2010).

RTAs also play a role in the rivalry between China and Japan for influence in Asia, and these two Asian giants have engaged in negotiations with somewhat overlapping sets of partners. Each of them have begun or concluded talks with the ASEAN countries, Australia, Chile, select EFTA members, the Gulf Cooperation Council, and Peru.

Some policymakers have advocated RTA negotiations between Japan and China, perhaps as part of a larger grouping. There was a Chinese proposal in 2002 for a three-way FTA among China, Japan, and Korea, but Japan did not wish to negotiate such an agreement so shortly after China's WTO accession. In 2006 Japan's Ministry of Economy, Trade and Industry proposed an East Asia EPA consisting of ASEAN+3+3, with one of the "threes" being Japan, China, and Korea and the other being India, Australia, and New Zealand. No such talks have yet been launched, but if this initiative were pursued it could represent the first RTA negotiations between any pair of the four largest members of the WTO (unless that happens first through Japanese participation in the TransPacific Partnership).

Japan is among the few countries that has an explicit and publicly available FTA strategy. It has in fact developed this strategy over time, with a first effort (Ministry of Foreign Affairs, 2002) having recently been superseded by a "Basic Policy on Comprehensive Economic Partnerships" adopted in November, 2010 by the Ministerial Committee on Comprehensive Economic Partnerships. The new policy statement emphasises that Japan "will take major steps forward from its present posture and promote high-level economic partnerships with major trading partners that will withstand comparison with the trend of other such relationships." The regional emphasis of the strategy is on the Asia-Pacific region, which "is of importance for Japan, politically, economically, and with regard to security." It therefore provides for the conclusion of negotiations with Peru and Australia, resumption of the negotiations with Korea, and "work towards the realisation regional economic partnerships such as the China-Japan-Korea FTA, East Asian Free Trade Agreement (EAFTA) and Comprehensive Economic Partnership in East Asia (CEPEA)," as well as consultation with the member countries of the TransPacific Partnership. The strategy further provides for initiatives outside this

region, including a joint examination with the European Union and the strengthening of economic partnerships with newly emerging powers and resource-rich countries.

As a comparative late-comer to the practice of RTAs, Japan has fewer agreements in effect than many other OECD countries. As can be seen from the data in Table II.4, the only agreements currently in place are with the ASEAN countries (which might be counted either as one agreement or as several), Mexico, Chile, and Switzerland. Even if one counts the ASEAN-Japan agreements separately, it is notable that as of late 2010 Japan had only as many FTA partners as the European Union did in 1997, Chile did in 2003, and the United States did in 2006.

Testing the political economy of services and RTAs: Hypotheses and data

Part I of this paper presented a series of generalisations regarding the domestic and international political economy of RTAs in general, which were then modified somewhat to take into account the special nature of trade in services. In this section we refine these generalisations into more specific hypotheses that may be tested against data both for the three case-study countries and, where appropriate, others as well. The order in which these hypotheses are presented works generally from the higher to the lower levels of abstraction, but also retains a logical flow from one point to another.

Grand strategic: RTAs as precedent-setters

Hypothesis 1: RTAs may be used by countries as a means of advancing issues that have either not made it on the agenda of the multilateral negotiations or on which progress has stalled.

The RTAs that are negotiated by the largest and most influential members of the trading system can play an important role in establishing the contours of that system. That was true both for the ways that Great Britain and the United States used bilateral agreements with MFN clauses to create multilateral orders in the late 19th and mid-20th centuries, respectively, and also for the approach that the United States took towards introducing new issues into multilateral system in the late twentieth century. Without the precedents that were set by the U.S.-Canada FTA and NAFTA, as well as the implicit threat that the United States might "go bilateral" if the GATT system did not change, the scope of the trading system might not have been expanded to include services and other new issues (especially the protection of intellectual property rights).

The European Union has also used RTAs as a means of advancing issues on which it is a *demandeur*, though with an important difference in sequence. Whereas the United States first set precedents for its preferred issues in the United States-Canada negotiations before concluding multilateral agreements on them in the Uruguay Round, the European Union has fallen back on RTAs for its issues after having been rebuffed in the Doha Round. These include the three Singapore issues that were provisionally put on the table at the start of the Doha Round, but that were removed after developing countries voiced strong and sustained objections. While the European Union was thus blocked from pursuing its interests on government procurement, competition policy, and investment in the multilateral negotiations, it can make them a priority in its RTAs. Both the United States and the European Union also use RTAs as ways of advancing their positions on the relationship between trade, labour, and the environment.

Focusing more precisely on services, we might ask whether RTAs can once again serve as precedent-setting agreements. Can the post-Uruguay Round RTAs provide models for how we might "fill in the blanks" left by the original GATS negotiations? The GATS negotiators left four important pieces of unfinished business to be taken up in subsequent negotiations, one of which – government procurement of services – coincides with the Singapore issues that the European Union sought to include in the Doha Round. The other incomplete provisions of the GATS agreement include rules on emergency safeguards, subsidies, and domestic regulation. Interestingly, government procurement is the only one of these areas where RTAs have offered numerous examples that might be replicated at the multilateral level, and yet one finds those potential precedents more often in the RTAs of countries *other than* the European Union.

Table II.5 shows how provisions on government procurement of services figure in many of the RTAs of our case-study countries, as well as agreements negotiated by some others. Each of the countries on which we are presently focused includes such provisions in at least some of their RTAs. Looking at all nine of the countries or groups whose RTAs are profiled, we may distinguish between the one country that *almost always* includes such provisions in its RTAs (i.e. the United States), the one country that *never* does so (i.e. China),[10] and those that *sometimes* do (i.e. all others listed horizontally in the table). It is especially noteworthy that, despite the fact that it was the *demandeur* on government procurement in the Doha Round, the European Union is the one among our four that is least likely to include rules on government procurement of services in its RTAs. That is due primarily to the fact that, as discussed below in Hypothesis 3, many of the European Union's RTAs do not cover services in the first place. As shown in Table II.5, when an RTA of the European Union does cover services it will usually provide rules on government procurement.

The overall pattern suggests that government procurement in services is a subject that, for several countries, presents a troublesome *lacuna* in the WTO regime. The status quo is something of a double-negative, in the sense that (a) government procurement provisions in the GATS have yet to be written, and (b) the WTO Agreement on Government Procurement is on the short list of surviving plurilateral agreements (i.e. not all WTO members are obliged to become parties to the agreement). Unless and until either the GATS is revised or the government procurement agreement is brought within the single undertaking, this will remain a subject where the patchwork of RTAs represent the only set of commitments entered into by many countries. The provisions in the RTAs identified in the table might conceivably offer models for a multilateral agreement,[11] but that would presuppose a greater degree of consensus on the need for such provisions than presently seems to exist among the WTO members.

10. The lack of services/government procurement provisions in the RTAs of China stems in part from the fact that China's preferred approach towards RTAs is to negotiate an agreement on trade in goods first and to postpone supplementary talks on trade in services to a later stage.

11. See for example World Trade Organization Working Party on GATS Rules (2003) and (2004).

Table II.5. Provisions in RTAs of selected countries and groups establishing disciplines in government procurement of services

	United States	Japan	Chile	European Union	Mexico	Singapore	Australia	EFTA	China
United States	—		■		■	■	■		
Japan		—	■		■	■			
Chile	■	■	—	■	□	■	■	■	□
European Union			■	—	■			■	
Mexico	■	■	□	■	—			□	
Singapore	■	■	■			—		■	□
Australia	■		■				—		
EFTA			■	■	□	■		—	
China			□			□			—
Korea	■			□		■			
Canada	■		□		■				
New Zealand			■				□		□
ASEAN		⦸					□		□
India			⦸						
Costa Rica	■		■		■				
Dominican R.	■			■					
Panama	■		□			■			
Colombia	■		■		■			■	
Peru	■		□						
Egypt				⦸				⦸	
Jordan	□			⦸		□		⦸	
Lebanon				⦸				⦸	
Oman	■								
South Africa				⦸				⦸	
Services Procurement Provisions	92.3%	75.0%	60.0%	44.4%	75.0%	75.0%	50.0%	44.4%	0.0%

Blank = No RTA.

⦸ = RTA that does not cover services.

□ = RTA that covers services but has no section dealing with government procurement of services.

■ = RTA with a section dealing with government procurement of services. These provisions may variously be in a chapter dealing with services or (more often) in a chapter dealing with government procurement of both goods and services.

The table does not cover every RTA negotiated by the nine countries and groups; the list was abbreviated for reasons of space. Note also that in some cases the individual countries shown are parties to an agreement reached on a subregional basis.

Source: Adapted from data in Mattoo and Sauvé (2010), supplemented by additional information from the author's review of further agreements.

The RTAs have proven to be a less productive "laboratory" for experimentation on the other issues that were left undone in the original GATS negotiations. In the case of emergency safeguards, most RTAs either make no provision for such rules or, like GATS, provide merely that they will be negotiated in the future. It would appear, per Mattoo and Sauvé (2010), that the only exceptions to this general rule come in two South-South agreements: The ASEAN Framework Agreement on Services (1995) and the Treaty of Chaguaramas (2001) among the members of the Caribbean Community. The situation is not much better for subsidies provisions, which can be found (to varying degrees of completeness) in the European Union's Treaty of Rome (1957), the Europe agreements, the FTA between EFTA and Singapore (2002), and the Closer Economic Relations agreement between Australia and New Zealand (1988). Domestic regulation of services is also dealt with in some RTAs, with Article 11.8(3) of the United States-Chile FTA offering an interesting example. After providing for general principles in this area, the article states that if the GATS Article VI:4 negotiations "enter into effect, this Article shall be amended, as appropriate, after consultations between the Parties, to bring those results into effect under this Agreement." The negotiators of that agreement apparently believed that this is an issue that should ideally be handled at the multilateral level.

Strategic: The selection of partners

Hypothesis 2: The more trade-dependent countries will be attracted to RTAs with countries that represent large shares of their trade. Countries that are larger and less trade-dependent may be more attracted to RTAs with smaller countries.

The most important strategic question for a country, apart from whether it will negotiate RTAs in the first place, is with whom it will seek them. Each of our cases has done so with multiple partners, and has concluded agreements with countries outside of its own region. When one charts negotiations according to the relative size of their partners, as is done in Table II.6, the pattern is striking: Whereas Chile negotiates RTAs with countries of all sizes, including eight of the top ten world markets for goods, Japan, the European Union, and the United States have thus far preferred somewhat smaller partners.

Perhaps the most important kind of RTA is the one that, at least so far, does not exist: An agreement between any pair of the four largest members of the WTO. Taken together, the European Union, United States, Japan, and China collectively accounted for just over half (51.0%) of world merchandise imports in 2008. And while all four of them have RTAs either already in effect or under negotiation with multiple partners, sometimes the very same ones (e.g. Chile, Singapore, and members of the Gulf Cooperation Council), among themselves they form what might be called a "Zone of Non-Negotiation." While there have been some proposals for the negotiation of FTAs among some pairs of these largest partners, such as Japan-China, Japan-United States, or United States-European Union, to date no such talks have been launched. The cut-off point has thus far drawn at Korea (agreements reached or implemented with three of the Big Four) and Canada (two RTAs launched or implemented with this group). That could change, with (for example) the Japanese strategy of late 2010 expressing interest in RTA negotiations with China, the European Union, and (through the TransPacific Partnership) the United States, but as yet these remain only hypothetical possibilities.

Table II.6. The RTA negotiations of selected countries

(◆ = RTA Negotiations initiated (whether or not concluded or agreements in effect)

	Global Goods Imports	EU-27	United States	China	Japan	Korea	Canada	Chile
EU-27*	**18.35**					◆	◆	◆
United States	**17.45**		The Zone of Non-Negotiation: No RTAs among the Big Four			◆	◆	◆
China	9.11							◆
Japan	**6.13**							◆
Republic of Korea	3.50	◆	◆		◆	—	◆	◆
Canada	3.36	◆	◆			◆	—	◆
Hong Kong, China	3.16			◆				
Mexico	2.60	◆	◆		◆	◆	◆	◆
Singapore	2.57	◆	◆	◆	◆	◆		◆
India	2.36	◆			◆			
Russian Federation	2.35							
Chinese Taipei	1.93							
Turkey	1.62	◆				◆		◆
Australia	1.61		◆	◆	◆	◆		◆
Switzerland	1.47	◆			◆	◆	◆	◆
Brazil	1.47	◆						◆
Thailand	1.44		◆	◆	◆			
United Arab Ems.	1.33	◆	◆	◆	◆	◆		
Malaysia	1.26		◆	◆	◆			◆
Indonesia	1.01			◆	◆			
Saudi Arabia	0.93	◆		◆	◆	◆		
South Africa	0.80	◆	◆	◆				
Norway	0.72	◆		◆		◆	◆	◆
Ukraine	0.69	◆					◆	
Viet Nam	0.65		◆	◆	◆			◆
Israel	0.54	◆	◆				◆	
Chile	0.50	◆	◆	◆	◆	◆	◆	—
Philippines	0.48			◆	◆			

*: Data for the European Union based solely on extra-EU imports.

Source: Import shares calculated from WTO data for merchandise imports in 2008.

There is a logic to these patterns. From the perspective of a relatively trade-dependent country, a trade agreement is fundamentally about trade and there are solid reasons for targeting one's limited resources on those partners that offer the largest opportunities to increase exports. For large less trade-dependent countries, however, there are at least two major reasons why it makes sense to by-pass the other, biggest players. One is a matter of trade strategy: Foregoing RTAs with their peers allows large countries to retain leverage when the time comes to deal with them multilaterally, especially on issues that are not easily handled in RTAs (e.g. agricultural subsidies).[12] A second reason reflects a fundamental precept of economic statecraft: A country's ability to leverage RTAs for non-economic ends will be greater in talks with smaller, more trade-dependent countries.

12. For an elaboration on the implications of this point see VanGrasstek (2008).

In Hirschman's classic study of state power and trade he argued that in a "world of many sovereign states it [is] an elementary principle of the power policy of a state to *direct its trade away from the large to the smaller trading state*" (1945; emphasis in the original). The resulting increase in the smaller country's dependence on the larger is not merely a mundane fact of economic life, in this view, but something that the larger state will seek to magnify economically in order to exploit politically.

What do the observed patterns mean for the multilateral-friendliness of the RTAs concluded by our four cases? A positive spin can be put on each of their choices. Looking first at Chile, it is evident from Santiago's words and deeds that bilateral and regional negotiations are seen not as substitutes but as complements to the multilateral talks, and that they are meant to fill the gap that will remain until the global negotiations can be concluded. As for the European Union, Japan, and the United States, the fact that they have not yet initiated RTA negotiations with one another or with China is evidence that they are holding back some of their chips for bargaining at the big table. In the event that any of these Big Four were to pair off in an RTA negotiation, however, the implications for the multilateral system might be disquieting for multilateralists, and it could set off an altogether new phase in the practice of competitive liberalisation.

Strategic: The decision to put services on the table

Hypothesis 3: Wealthier countries in which services account for a larger share of the economy are more likely to include services in the scope of their FTAs than are less developed countries where services are less prominent.

Having decided to negotiate RTAs and selected the countries with which to negotiate them, one must then choose what to negotiate. Among other things, this means deciding whether or not services will be on the table. The answer is often no. According to one tally, only 27.9% of the RTAs notified to the WTO cover services as well as goods.[13]

As is shown in Table II.7, the coverage of services is not a random occurrence, but instead reflects the differing proclivities of negotiators from industrialised and developing countries. Unlike the case of trade in goods, where nearly every country will have some mix of industries at various levels of competitiveness (some are competitive, export-oriented *demandeurs*, others are uncompetitive and demand protection, etc.), in many countries there are few (if any) service sectors that are world-class exporters. This is a point that has evolved over time; most developing countries believed at the time of the Uruguay Round that they had no export interests in this area, but many now perceive at least some offensive interests in services. As a general rule, however, most of the demands in services are still made by the industrialised countries (or what in this context might more properly be called the "post-industrial countries").

13. Mattoo and Sauvé (2010: Table 1). Note that while that count is based on the same source as used here for the data in Table II.7 (i.e. the WTO's RTA database), Table II.7 is different insofar as (1) it excludes all RTAs negotiated prior to the time when services became part of the multilateral negotiating agenda, (2) it provides data only for selected countries, and (3) is based on averages across countries rather than the global total.

Table II.7. Inclusion of services in the post-1985 RTAs of selected countries

Number of RTAs that do or do not cover trade in services

	RTAs with OECD Members		RTAs with Other Countries		Total RTAs	
	Yes	**No**	**Yes**	**No**	**Yes**	**No**
OECD Members						
Chile	***8***	***0***	***2***	***5***	***10***	***5***
EU-27*	***4***	***1***	***5***	***16***	***9***	***17***
Japan	***2***	***0***	***7***	***1***	***9***	***1***
United States	***4***	***0***	***8***	***0***	***12***	***0***
Australia	4	0	2	0	6	0
Canada	2	2	1	1	3	3
EFTA*	1	3	2	9	3	14
Israel	0	5	0	0	0	5
Korea	2	0	3	2	5	2
Mexico	4	1	7	0	11	1
New Zealand	2	0	4	0	6	0
Turkey	0	3	0	11	0	14
Average Share	69.6%	30.4%	60.7%	39.3%	60.2%	39.8%
Other Major Econs.						
China	0	1	5	1	5	2
India	1	1	1	9	2	10
MERCOSUR*	0	0	1	1	1	1
South Africa	0	2	0	2	0	4
Average Share	16.7%	83.3%	35.8%	64.2%	34.5%	65.5%
Others						
Bahrain	1	0	0	2	1	2
Bangladesh	0	0	0	4	0	4
Chinese Taipei	0	0	3	0	3	0
Colombia	1	0	0	2	1	2
Costa Rica	3	1	1	1	4	2
Egypt	0	3	0	3	0	6
Malaysia	3	1	2	2	5	3
Morocco	1	3	0	2	3	5
Thailand	5	1	1	3	6	4
Average Share	*67.2%*	*32.8%*	*32.5%*	*67.5%*	*46.1%*	*53.9%*
All Non-OECD Shown	*53.4%*	*46.6%*	*33.4%*	*66.6%*	*43.0%*	*57.0%*
All Countries Shown	*61.8%*	*38.2%*	*44.9%*	*55.1%*	*50.6%*	*49.4%*

*: Does not include RTAs in which individual EU-27, EFTA, or MERCOSUR countries are members.

Note that the table includes data only on those RTAs that were concluded during the period since services became part of the multilateral negotiating agenda in 1986, and have been notified to the WTO. There appear to be several agreements not recorded here due to the second criterion.

Average shares are unweighted averages calculated first by determining the percentage distribution within each category (OECD, non-OECD, and total) for each country and then averaging within groups.

Source: Calculated by the author from WTO data at http://rtais.wto.org/UI/PublicSearchByCr.aspx.

Looking at all of the RTAs, the OECD members typically include services provisions in about three-fifths of their agreements, *versus* less than half of the RTAs reached by the non-OECD members shown in the table. This pattern is repeated and intensified when one looks at the RTAs that these two sets of countries negotiate with their respective peer groups. When a pair of OECD members negotiates an RTA the agreement will typically include services over two-thirds of the time, while a grouping of non-OECD countries will include them one-third of the time. The kind of RTA that is least likely to cover

services in not a South-South agreement, however, but one between an OECD country and one of the other major economies; that finding may, however, be an artefact of the small number of agreements that fall in this category. These averages mask a great deal of heterogeneity within each group,[14] but the broad pattern is clear: Industrialised countries are more interested in including services in their RTAs than are developing countries.

Turning to our four cases, it is evident that the European Union is a special case. Whereas services are included in all of the post-1985 RTAs of the United States, nine out of ten of Japan's and two-thirds of the Chilean agreements, just one-third of the RTAs of the European Union include services. That is more notably the case in its RTAs with non-OECD economies, less than one-fourth of which include services, but even in one of its RTAs with another OECD country (i.e. Turkey) the European Union did not reach an agreement on services. As a general rule to which there are exceptions, it would appear that the European Union tends to include services in those RTAs that it reaches with candidates for accession, and tends not to include them with others. On this point see the discussion of Hypothesis 6, below.

Strategic: The results of asymmetrical negotiations

Hypothesis 4: In negotiations between partners of asymmetrical size, it is likely that the larger partners will extract deeper concessions from the smaller.

One might read the services commitments that a country makes in an RTA for signals of what it is willing to offer at the multilateral level, but in so doing one should also remember that schedules are the result of demands as well as supply, that negotiations are exercises in which power is always relevant, and that power is usually asymmetric. It should therefore not surprise us if the outcomes of these negotiations were to reflect the relative power of the parties, such that the larger partners are able to obtain relatively greater concessions from their smaller partners. Commitments in this area may be seen as part of the "price" that an industrialised country asks a developing country to pay in exchange for free access to its market for goods (along with other matters such as TRIPs-Plus commitments on intellectual property rights). To the extent that a North-South RTA does provide for nominal or even real liberalisation on services, therefore, the new commitments may be deeper and more numerous on the part of the developing country partner(s).

The data in Table II.8 partially support the hypothesis, but with some anomalies. Looking first to our four cases, it comes as no surprise that the European Union and the United States obtain the deepest concessions from their partners at the lowest relative cost to themselves (as measured by the ratio of concessions obtained to concessions given), but it is not immediately apparent why Chilean negotiators did better by this metric than did their Japanese counterparts. Going beyond these four, we find some countries whose relative place is about where we should expect it and others that perform above or below expectations. The strongest support for the hypothesis comes in the fact that the two

14. Among the OECD members, for example, there are some countries (i.e. Australia, New Zealand, and the United States) that include services provisions in 100% of their RTAs, whether the partner is an OECD member or not, two (i.e. Israel and Turkey) that never include services in its RTAs, and some (i.e. Chile, Japan, and Korea) that include services in all RTAs with other OECD members but not in all of their RTAs with non-OECD members.

largest WTO members, at least as measured by their share of world merchandise imports, are in precisely the positions we should anticipate. The data for these biggest players confirm that they obtain the deepest commitments, whether that is measured in absolute terms (the percentage of commitments obtained from a partner that are GATS-plus) or relative terms (the ratio of those concessions obtained to GATS-plus concessions made in return). It should also be noted that this observation provides a major asterisk to what we saw in examining Hypothesis 3: While it remains the case that the European Union often leaves services out of its negotiations, it tends to leverage the deepest commitments when it does include them.[15]

It is also worth noting the apparent pattern whereby the results obtained by Asian countries consistently fall short of what one would expect relative to the size of their economies. That latter observation implies the possibility that there may be some issues of culture or negotiating style that are at play here. This observation is also consistent with the findings of Fink and Molinuevo, who concluded in their study of services provisions in East Asian RTAs that this "menagerie [of trade agreements] includes plenty of timid pandas and the few tigers that stray around do not roar much" in the sense that "many FTAs offer only limited value-added relative to multilateral services commitments" (2007). It is also possible that some of the seeming anomalies might result from the different sets of partners with which countries chose to negotiate, the different approaches they took to the negotiations, or the different weights that they placed on specific sectors.

It does not necessarily follow that the country that makes the most concessions should be seen as the "loser" in a negotiation. Developing countries may perceive real utility in making relatively deep commitments to their industrialised country counterparts, insofar as the RTA may be used as an instrument for the attraction of foreign investment. That is especially true for commitments that follow upon reforms that have already been made through domestic legislation or other rulemaking procedures (see Hypothesis 5). By comparison, the wealthier partner to the RTA may feel little or no incentive to make new commitments in an agreement. It may instead perceive a strong reason to hold off commitments until it is negotiating with more and larger partners in a multilateral forum. Moreover, the developing country partner may not perceive much benefit in seeking such commitments in the services sector in the first place, apart from those related to Mode 4 (which may encounter sharp resistance from its partner), and concentrate its demands instead on issues affecting trade in goods.

15. See also the discussion of Hypothesis 6 below, which shows that the EU leverages the deepest commitments from those negotiating partners that are actual or potential candidates for accession.

Table II.8. Depth of market-access commitments on services obtained and made by selected countries in their RTAs

Average market-access commitments determined to be GATS-plus

	Average GATS-Plus Market-Access Commitments Obtained from RTA Partners (A)	Average GATS-Plus Market-Access Commitments Made to RTA Partners (B)	Ratio (A:B)	Rank in World Imports of Goods
European Union	**71.8%**	**47.7%**	**1.51**	**1**
United States	**62.3%**	**44.9%**	**1.39**	**2**
New Zealand	41.3%	39.5%	1.05	40
Canada	61.9%	69.1%	0.90	6
Australia	44.6%	45.8%	0.97	14
Chile	**43.3%**	**49.8%**	**0.87**	**27**
Mexico	38.0%	46.0%	0.83	8
Japan	**33.4%**	**41.8%**	**0.80**	**4**
Singapore	31.7%	53.2%	0.60	9
Korea	29.5%	49.8%	0.59	5

A "GATS-plus" commitment is defined to be one in which the party makes a commitment in an RTA in a sector that was not included in its GATS commitments, or the commitment represents an improvement over the one it made in that sector in its GATS commitments.

Note that the calculations are based only on those agreements and partners that were included in the source document.

Note that data in the source document are not sufficient to calculate figures for China.

Source: Calculated from data in OECD (2010), Annex 3, Table 6. Rank in world imports calculated from data in Table II.7 of the present document.

Domestic: The sequencing of reforms and the aversion to rulemaking-by-treaty

Hypothesis 5: To the extent that legislators, civil servants, and other domestic policymakers involved in the regulation of services are willing to (1) enact market-opening rules (laws, regulations, etc.) and to (2) approve international agreements that consolidate these reforms they will prefer that the steps be taken in that order and not vice versa.

Reforms that are "locked in" by an RTA or other international agreement differ from purely autonomous liberalisation in one key respect: The other part(ies) to the RTA acquire a legal right to the maintenance of those commitments that are inscribed in the agreement. Prospective foreign investors may be more likely to have more confidence in the permanence of those economic reforms that are thus solemnised than they are in the decisions that are made, and might just as easily be unmade, through autonomous and purely domestic procedures. That logic may be sufficient to persuade countries to remove "water" in their services schedules, but the trade ministry that is prepared to make a commitment that requires additional reforms may face greater resistance at home from other ministries, the legislature, or sub-national units of government. The evidence in

support of this last proposition may be largely anecdotal, but sometimes "anecdote" is merely the singular form of the word "data."[16]

The experience of Chile in financial services may be cited as an example. Chilean negotiators have generally viewed RTAs as a means for consolidating service-sector reforms that the country has made autonomously, rather than for the negotiation of new liberalisation. Under this approach, liberalisation through RTAs would be a "third-best" alternative to autonomous action or multilateral liberalisation. Chile undertook a lengthy series of financial service reforms from the early 1970s through the 1990s, and its commitments in multilateral agreements and RTAs have generally "played catch-up" with these reforms. In the Uruguay Round Chile did not even consolidate the measures that were then applied, a sense of caution that can be attributed to the fact that domestic legislative and regulatory changes were still pending at the time of those negotiations. Later, when Chile negotiated nearly simultaneous FTAs with the European Union and the United States, "Chile's negotiators decided their stance would be that the negotiations should not lead to reforms of Chile's financial legislation or to additional liberalisation" but instead "at most Chile would agree to lock in the status quo" (Sáez, 2010: 137). The financial services commitments in the FTA with the European Union fell short of even that modest goal, being mostly a "cut and paste" of the commitments that Chile had already made in the GATS and related protocols. In the agreement with the United States, however, Chile made did make one concession that required a change in domestic financial laws (i.e. allowing the establishment of insurance providers through branches).

What is less clear is the extent to which the Chilean case may be exceptional. The reforms undertaken by Colombia in its FTA with the United States were somewhat greater (Arbeláez, Flórez, and Salazar, 2010), for example, and those of Costa Rica were far more significant (Echandi, 2010). While it is reasonable to expect that most regulatory authorities in most countries would prefer that the laws within their jurisdiction not be put on the block, we do not have sufficient data available yet to state with any confidence whether the services provisions in the typical North-South RTA more closely resemble the sequence followed by Chile or by Costa Rica.

One way of checking would be to examine the implementing legislation that countries enact for their RTAs. It is the practice in at least some countries to produce a comprehensive legislative package that makes all of the changes in law and regulation that are required in order to come into compliance with a trade agreement. That is the case, for example, in the various implementing bills that the U.S. Congress has approved under "trade promotion authority" (formerly known as the "fast track"). In recent years it has also been the policy of the United States to require that its FTA partners enact comparable legislation of their own before the United States will permit the agreement to enter into effect.

Let us examine the implementing legislation enacted by the legislatures of the United States and Guatemala when these two countries approved CAFTA-DR. According to the calculations in the OECD (2010) analysis, in that agreement precisely 50.0% of the

16. The author has had occasion to discuss the conduct of services negotiations with a wide range of government officials from countries in distinct regions and levels of economic development, and has never yet spoken to one who disagreed with the general proposition that domestic regulatory agencies and ministries tend to view with great suspicion the proposition that the trade ministry should have the authority to make binding commitments affecting the regulation of services that fall within the other body's jurisdiction.

services market-access commitments made by the United States were GATS-plus (i.e. the bindings for half of the sectors were set at a more liberal level than was the case for the U.S. GATS commitments), and the corresponding figure for Guatemala was 84.7%. The gap between these two nominal levels of liberalisation is consistent with the asymmetric pattern discussed above. When one looks at the actual changes in the two countries' laws that were needed in order for them to meet their RTA obligations, however, the gap is much wider. Whereas the Guatemalan implementing legislation[17] made sixteen amendments to the country's services laws (most of them being in the area of telecommunications services), the U.S. implementing legislation and related instruments[18] did not amend a single law or regulation regarding trade in services. Or to put it in rough terms, the only services commitments that the United States made in CAFTA-DR amounted to removal of water between its GATS commitments and its applied measures, while the Guatemalan commitments required real liberalisation.[19]

In Japan, too, there is opposition to rulemaking-by-treaty in the field of trade in services. There the conflict is carried out largely through government ministries with differing views of what should be on the table in RTA negotiations. Four Japanese ministries are principally involved in RTA negotiations – the Ministry of Economy, Trade and Industry (METI), the Ministry of Foreign Affairs (MOFA), the Ministry of Agriculture, Forestry, and Fisheries (MAFF), and the Ministry of Finance (MOF) – and the sometimes strained relations between these and other ministries are among the obstacles that need to be overcome in devising and achieving national objectives in these talks. Struggles over "turf" are at least as intense in Japan as they are in other countries, a factor that is only exacerbated by the operation of interest-group politics and the weak control that prime ministers have traditionally wielded in the selection and promotion of key staff in the ministries.[20] Whereas both METI and MOFA have promoted the increased use of RTAs as an instrument of Japanese trade policy, MOF and (to an even greater extent) MAFF have tended to be reluctant about undertaking serious reforms to their respective areas of policy through this approach. Among the more contentious issues in the negotiation of Japan's RTA negotiations with its ASEAN partners, and especially Thailand and the Philippines, concerned liberalisation of the movement of natural persons in such fields as cooks, nurses, massage therapists, and care-givers for the elderly. According to Urata (2005), "nurses associations and medical associations strongly opposed importation of these people because it would threaten job opportunities for Japanese nurses and other medical-care givers" and their views were then successfully represented by Japan's Ministry of Welfare and Labor.

17. Decreto No.11-2006, published in the *Diario de Centro América* of May 29, 2006 (Volume 229 Number 38).

18. This statement applies not only to the "Dominican Republic-Central America-United States Free Trade Agreement Implementation Act" (Public Law 109-53), but also to the accompanying statement of administrative action and the various regulations and other CAFTA-related documents published in the *Federal Register* in 2006-2007.

19. It should also be observed that the changes that Guatemala made were generic in nature, and did not extend any form of preference to either the United States or the other CAFTA parties. The result was thus multilateral on a *de facto* basis, even if this liberalization was not yet *de jure* (i.e. inscribed in the Guatemalan GATS schedule).

20. Note however that the office of the prime minister did receive enhanced powers as a result of a reorganization of governmental functions in 2001, and that prime ministers have sometimes used these powers to break deadlocks in RTA negotiations.

Strategic: RTAs as preferential instruments of foreign policy

Hypothesis 6: Those agreements that are inspired in large measure by one country's desire, for reasons of foreign policy, to extend preferential treatment to another may be less likely than other agreements to include provisions that are intended to set precedents for multilateral liberalisation.

A preferential program or agreement that is created for essentially political purposes may produce disincentives to multilateral liberalisation, to the extent that this means diluting the benefits extended by that preferential arrangement. The motivations behind the program or agreement might variously be based upon propinquity (e.g. the industrialised country believes that it is in its interest for its immediate neighbours to be economically prosperous and politically stable), ties of blood and history (e.g. the developing country in question may be a former colony), alliances (e.g. the developing country may give the industrialised country support in a war or other major undertaking), or other security issues (e.g. preferential access may be part of an anti-narcotics/ crop-substitution policy). While there may be additional partners to whom similar treatment might later be extended, especially if they share the same political characteristics that led to the preferential treatment in the first place, both the industrialised country and its favoured developing country partners will want to limit the extent of preferences in order to ensure that they are indeed preferential.

We might stipulate from the start that concerns of this sort may well be justified for RTA treatment of some highly protected goods sectors, most notably textiles and apparel, but the question arises as to whether the same dynamic is at work for trade in services. There are two grounds on which this seems to be not the case. Both in legal principle and in actual practice, it appears that in the case of services there is less scope for the liberalisation extended via RTAs to form a barrier to the multilateralisation of commitments.

At the level of principle, many RTAs include MFN provisions for trade in services. Article 108 of the Chile-Japan agreement is one such provision, stating that, "Each Party shall accord to services and service suppliers of the other Party treatment no less favourable than that it accords, in like circumstances, to services and service suppliers of any non-Party." For example, if after reaching this bilateral agreement Chile were to make a deeper commitment on financial services with a new RTA partner, those benefits would be automatically extended to Japan. Not all RTAs include such provisions, and those that do are not always as automatic in their extension in MFN treatment,[21] but this is one means by which the commitments that countries make in their RTAs may gradually be extended to third parties – though only to those third parties that are in their circles of RTA partners. At a time when some major trading powers can count their RTA partners in the dozens, however, accounting for close to half of their total trade, the inclusion of such clauses in their RTAs makes it more difficult for them to cut exclusive deals with individual partners.

Moving from principle to practice, when one closely examines the commitments made in the more "political" RTAs it is difficult to find evidence of special treatment in

21. See Fink and Molinuevo (2007) for a discussion of the different kinds of MFN provisions in the services chapters of RTAs, which sometimes extend MFN automatically and sometimes provide only for the favorable consideration of such requests.

services. Among our four cases it is the United States that is most prone to using RTAs as an instrument of foreign policy, and hence offers the best opportunity to test the proposition. FTA negotiations have a long association with the cluster of U.S. goals in the Middle East, which combines the promotion of peace in the region with opposition to terrorism and the pursuit of U.S. energy security.[22] The very first FTA that the United States ever negotiated was with Israel, and Jordan was (after Canada and Mexico) the fourth U.S. FTA partner. The profile of RTAs in U.S. policy towards this region rose when President Bush proposed in 2003 "the establishment of a U.S.-Middle East free trade area [FTA] within a decade" (2004). This policy led to FTAs with Bahrain, Morocco, and Oman, as well as failed talks with the United Arab Emirates[23] and the exploration of negotiations with Egypt and Kuwait. Even countries outside the Middle East can see their FTA negotiations become linked to these issues, having been a factor both in the negotiation of the FTA with Australia (a member of the Coalition of the Willing) and in the end-game of the FTA with Chile (which held a seat on the United Nations Security Council).[24]

The FTAs that the United States has negotiated with Middle Eastern countries can, to varying degrees, be considered apart from the other RTAs that the United States has concluded. The FTAs with Israel[25] and Jordan follow a completely different pattern than all the others, being an extremely short agreement[26] that imposes relatively few disciplines on the partners, and – in a departure from the pattern of U.S. FTAs since NAFTA – being based on a positive rather than a negative list. Commercial objectives could not have been uppermost in the U.S. approach to the negotiations with Jordan, and the resulting agreement must be considered a virtually *sui generis* pact that does not appear to have been intended to be replicated elsewhere. The agreements with Bahrain and especially Morocco bear closer resemblances to the FTAs with other countries, at least in their length and structure, but still tend to be less demanding on some points than those reached with larger U.S. partners.

The question is, does the same pattern hold for trade in services? Table II.9 offers evidence to test against the contention that these agreements are more preferential than other U.S. FTAs. The only way in which the Middle Eastern FTAs appear more preferential than the rest is in the negative sense of making fewer demands on the partner country than is the case for countries in other regions, and even here the evidence is clear only for Jordan: Over one-fourth of that country's services sectors were left entirely

22. For more details on the role of RTAs in U.S. Middle East policy see VanGrasstek (2003). For a comparison of the U.S. and EU RTAs in this region see al Khouri (2008).

23. The FTA negotiations with the United Arab Emirates were suspended in 2006, due in part to a political dispute over the proposed operation of U.S. ports by Dubai Ports World.

24. The debate over approval of the FTA in the U.S. Congress coincided with Chile's tenure on the United Nations Security Council and the deliberations over a U.S. invasion of Iraq. The resulting friction between the United States and Chile did not ultimately prevent the approval of the FTA by the U.S. Congress, but did produce concerns and delays. For accounts of how these matters came to be linked see *El País* (2007), Muñoz (2008), and Weintraub (2004: 91)

25. Note that this agreement is not included in Table II.9 because it did not include sectoral commitments on services.

26. The main text of the U.S.-Israel FTA was just 21 pages, while the one with Jordan ran to 19 pages. These agreements were thus shorter than the intellectual property chapters in most other FTAs of the United States.

unbound in the agreement, compared to an average of 5.5% for non-OECD countries outside the Middle East. The United States left an even larger share of its sectors unbound in that agreement, suggesting that the services aspects of this negotiation were not a high priority for either of the parties. As for the commitments that the United States made to its partners, one would expect to see a very high percentage of GATS-plus commitments in any agreement that is intended to be preferential. The data confound that expectation when it comes to services: Only 39.8% of the U.S. commitments in the average Middle Eastern FTA were GATS-plus, well below the shares reached in FTAs with other developing countries (48.2%) or OECD members (52.7%). Looking more specifically at the level of GATS-plus commitments that the United States made to the Middle Eastern countries other than Jordan, these were very close to the levels in the FTAs reached with Latin American countries (both those in and outside the OECD).

There is more evidence for differential treatment of partners in the RTAs of the European Union, but not in a way that raises concerns regarding overly preferential treatment in the more "political" agreements. The European Union's RTAs tend to fall into three broad, geographic categories. In ascending order of services coverage, they are: (1) countries in the Middle East and Africa that appear to have been "given a pass" by leaving services out of the agreement altogether,[27] (2) countries in the Americas that fall into a middle category where services are in their RTAs but the commitments are not extensive, and (3) countries in Europe that are actual or potential candidates for accession and with whom the services provisions are thus required to be much more comprehensive.[28] The differences in the treatment of services in the RTAs reached with American and European partners are quite evident from the data in Table II.10. Those concluded with countries in Europe, which might more properly be seen as steps toward expansion of a CU rather than one-off FTAs, bind all services sectors without exception and include a great many GATS-plus commitments. RTAs reached with developing countries in the Western Hemisphere leave more sectors unbound. Comparing the data in tables II.9 and II.10, one can also see that the RTAs that Chile, the Dominican Republic, and Mexico reached with the European Union did not go nearly as far on services as the ones that they reached with the United States.

27. The post-Uruguay Round RTAs of the EU that that do not cover services include those with Algeria, Cameroon, Côte d'Ivoire, Egypt, Israel, Jordan, Lebanon, Morocco, the Palestinian Authority, South Africa, and Tunisia. Note however that in some cases the intention appears to have been to conclude the negotiations on goods first without awaiting the the time-consuming negotiation of a services agreement. Some of these RTAs may thus be supplemented in the future by additional agreements on services.

28. Note that this is not a universal rule, as services were not covered in the RTAs that the EU reached with other European countries in the pre-Uruguay Round period, nor have they been more recently with candidate country Turkey (entered into force in 1995), nor with potential candidate countries Bosnia and Herzegovina (2008) and Serbia (2010), nor with the other European states of the Faroe Islands (1997) and San Marino (2002). Services were covered by the RTA reached with potential candidate country Montenegro (the services provisions of which entered into force in 2010), but that RTA is not included in Table II.10 because the agreement was not analyzed in the source document.

Table II.9. Depth of market-access commitments on services made by parties to the RTAs of the United States

	% Sectors Unbound		% GATS-Plus	
	Partner	**United States**	**Partner**	**United States**
Middle East				
Bahrain	15.0	5.2	69.2	53.5
Jordan	29.8	33.9	30.5	4.8
Morocco	3.5	7.7	87.9	51.5
Oman	6.3	7.4	42.3	49.5
Average	*13.7*	*13.6*	*57.5*	*39.8*
OECD Members				
Australia	2.4	7.9	46.9	40.5
Canada	6.5	7.4	53.5	60.3
Chile	17.9	8.5	41.0	49.5
Mexico	7.6	7.4	57.9	60.3
Average	*8.6*	*7.8*	*49.8*	*52.7*
All Other				
Costa Rica	1.3	8.5	90.0	50.0
Dominican Republic	6.6	8.5	71.7	50.0
El Salvador	4.7	8.5	93.9	50.0
Guatemala	9.0	8.5	84.7	50.0
Peru	3.5	8.5	88.5	48.4
Singapore	7.6	7.9	76.6	40.5
Average	*5.5*	*8.4*	*84.2*	*48.2*

A "GATS-plus" commitment is defined to be one in which the party makes a commitment in an RTA in a sector that was not included in its GATS commitments, or the commitment represents an improvement over the one it made in that sector in its GATS commitments.

Source: Calculated from data in OECD (2010), Annex 3, Table 6.

Table II.10. Depth of market-access commitments on services made by parties to the RTAs of the European Union

	% Sectors Unbound		% GATS-Plus	
	Partner	**European Union**	**Partner**	**European Union**
Europe				
Albania	0.0	0.0	56.6	71.0
Croatia	0.0	0.0	63.5	71.0
FYR of Macedonia	0.0	0.0	69.8	71.0
Average	*0.0*	*0.0*	*63.3*	*71.0*
Americas				
Chile	29.5	30.0	64.8	11.0
Dominican Republic	29.4	20.6	63.4	39.0
Jamaica	39.4	20.6	45.0	39.0
Mexico	62.1	39.2	2.7	0.0
Average	*40.1*	*27.6*	*44.0*	*22.3*

A "GATS-plus" commitment is defined to be one in which the party makes a commitment in an RTA in a sector that was not included in its GATS commitments, or the commitment represents an improvement over the one it made in that sector in its GATS commitments.

Source: Calculated from data in OECD (2010), Annex 3, Table 6.

These patterns are generally consistent with what we observed in the case of the United States, namely that the only evidence of preferential treatment comes in the form of fewer demands on some partners. In this case, "fewer demands" means no services coverage at all in many of the RTAs. At the other extreme, the RTAs with the European partners are special cases: Croatia and the Former Yugoslav Republic of Macedonia are both EU candidate countries, and Albania is a potential candidate country. It is to be expected that their RTAs with the European Union will be pre-accession agreements that are a step towards acceptance of the *acquis communautaire*. As for the partners in the Americas, here we see – as was the case for the RTAs of the United States – that it is the partner country and not the European Union that makes the most GATS-plus commitments. These observations are more in line with what we saw in Hypothesis 4 (i.e. the results of negotiations between partners of asymmetrical size) than what is implied in Hypothesis 6.

It should nonetheless be noted that there are still a great many RTAs that remain under negotiation between the European Union and former colonies in the African and Pacific regions. The only negotiations so far among the European Union and the African, Caribbean, and Pacific (ACP) countries that have so far produced agreements that have entered into effect are those with the three C's – Cameroon, CARIFORUM, and Côte d'Ivoire – with only the CARIFORUM agreement covering services. When available, the results of the remaining negotiations should be examined closely to determine whether they more closely resemble (1) the RTAs reached so far with most African and Middle Eastern countries (i.e. with services off the table altogether), (2) those reached in the Americas, or (3) a possible new pattern that might suggest a greater degree of preferential treatment. If current trends hold, option (3) seems the least likely.

To return to the key theme of multilateral-friendliness, this is one area where RTAs may be less troublesome than we might expect in the abstract. The evidence in support of Hypothesis 6 is so weak that it should be rejected on at least a provisional basis (pending any new data that might emerge from the remaining EU negotiations with African and Pacific partners). While it may well be that the preferential treatment that RTAs extend to favoured partners in goods trade will create disincentives to multilateral liberalisation in certain sectors, it would appear that there are fewer preferences – and hence less resistance to their spread – in the case of services. This might be best described not as a matter of RTAs being multilateral-friendly, but of avoiding a potentially important source of multilateral-*un*friendliness.

Domestic: The consequences of over-reaching

Hypothesis 7: RTA negotiators may sometimes over-estimate the extent to which they may liberalise sensitive sectors. This can result in confrontations at home that affect the terms of the agreement in question and/or future RTAs.

If a country includes a concession on a specific service sector in one RTA, may we conclude that it is prepared to make that same concession in future RTAs and the GATS? Simple logic would so imply, but we should avoid the temptation to assume that this happens always or automatically. Each RTA is the product of a negotiation between at least two countries, and the fact that Country A was willing to make a given concession to Country B might say as much about the importance that B attached to its demand as the willingness of A to multilateralise the result. We should also consider the possibility that

in some cases the negotiators who made this commitment will find out that it was much more controversial at home than they thought it might be, and will be under great pressure not to repeat it. They may even be forced to revoke it.

This is a point for which once again the experience of the United States can be instructive. While it is true that the United States was the original *demandeur* on services, and that services remain a higher priority for the United States than for most countries, that position is modified by two other factors. One is that some segments of the U.S. services sector are indifferent or even hostile towards liberalisation, and either make no demands of their own or insist on retaining protection. The other is that the Congress has great authority in the making of U.S. trade policy, and that there is little that the executive can do in this area without the approval of the legislature. Taken together, these two facts have produced some notable incidents that demonstrate the potential difficulties of domestic politics in this field.

Every country seems to have at least one sacred cow in the services field that its negotiators are well-advised not to touch, and in the United States the maritime transportation sector is the leading candidate for this distinction. For reasons of both economics and national security, the sector benefits from various forms of support and protection. In the draft FTA text that was released in October, 1987, however, the Canadian negotiators secured a concession on the cargo-preference laws (i.e. requirements that specific percentages of government-financed shipments be carried in U.S. vessels) providing that any future extensions in the scope of cargo preference laws would be open for bidding by Canadian shippers. A coalition of maritime firms, unions, and associations was concerned not just with the immediate issue of competition with Canada, but also by the precedent that might be set for the Uruguay Round, and convinced members of Congress to exert leverage on the negotiators. Legislators threatened to permit amendments to the maritime provisions of a FTA implementing bill, notwithstanding the general rule against amendments to bills that were subject to "fast track" approval. The Reagan administration took these threats seriously and set out to change the offending section of the draft agreement, and (in consultation with Canada) eventually removed the transportation annex altogether from the agreement. Even more significant, the U.S. negotiators have never since attempted to negotiate any significant reductions in the maritime service industry's protections in either the GATS or in RTAs.

A somewhat lower-key dispute erupted in 2003 over provisions in the FTAs with Chile and Singapore that would have made concessions on the movement of natural persons ("Mode 4" in GATS parlance). Building on the NAFTA model, the negotiators in these two FTAs also included chapters on the temporary entry of business persons that provided *inter alia* for numerical limits. For example, an item in the U.S.-Chile FTA provided that "the United States shall annually approve as many as 1 400 initial applications of business persons of Chile seeking temporary entry … to engage in a business activity at a professional level." A similar provision in the U.S.-Singapore FTA provided for 5 400 such applications. These deals encountered very sharp criticisms from U.S. labor unions and Congress. In July, 2003, the House Judiciary Committee insisted that the new professional worker visas provided by these agreements be counted under the existing visa program. Legislators introduced bills that would explicitly restrict the authority of the U.S. Trade Representative to negotiate on these matters. Congress and the Bush administration managed to resolve this dispute in the short term by adding language to the implementing legislation and the statements of administrative action for the two agreements. To simplify, the terms of the clarifications made it explicit that these entries would come within the established U.S. visa programs. In the long term, this experience

convinced the U.S. negotiators to drop the temporary entry for business persons chapters from future FTAs.

Further examples of this kind of manoeuvring could be cited, such as the controversies surrounding a "cultural exception" in trade agreements. Those details matter less than the main point, which is that not all movement will always and irreversibly be forward. The fact that a certain concession is made in a given RTA does not necessarily mean that the country granting that concession is prepared to make it in the GATS. In fact, the country may not be prepared to make that same concession in other, later RTAs or even – in a few extreme cases – to keep it in the RTA in which it appeared in the first place.

Part III: Conclusions

Summary of key findings

Political considerations play a more important role in RTAs than in multilateral trade negotiations, and infuse the choices that countries make in the launching and conduct of RTA negotiations. That is true at the levels of both international political economy and the domestic politics of trade. But do these political considerations tend to make the services provisions of RTAs less multilateral-friendly? The analysis presented in this paper suggest that this is generally not the case for international political economy, but that the domestic politics of trade in services may make it difficult to achieve real liberalisation-by-treaty in either RTAs or multilateral talks.

The international political economy of services and RTAs

One sweeping generalisation that we might make is that issues in international political economy do not seem, on closer examination, to pose as great a problem for the multilateralisation of services commitments as we might anticipate in the abstract. The data reviewed here allow us to reject on at least a preliminary basis one reason to expect that RTAs might create constituencies opposed to multilateral liberalisation, while also showing that there are other aspects of the international political economy of RTAs that are more multilateral-friendly.

Perhaps the most significant finding concerns the dog that did not bark: The evidence reviewed here suggests that we need have little concern over the possibility that RTAs negotiated for political reasons will extend preferential deals on services that countries will be unwilling to include in their GATS schedules. The issue appears problematic in principle. To the extent that the purpose of an RTA is fundamentally political, there may be a temptation to establish preferential treatment that is permanent and exclusive. In actual practice, the data do not support Hypothesis 6 (i.e. those agreements that are inspired in large measure by one country's desire, for reasons of foreign policy, to extend preferential treatment to another may be less likely than other agreements to include provisions that are intended to set precedents for multilateral liberalisation). However serious this problem may prove to be in other areas (e.g. apparel trade), it does not appear to be significant in the case of services. The agreements that the European Union negotiates with current or prospective accession candidates are indeed much more comprehensive on services than are its other RTAs, but that is to be expected. Neither the other RTAs of the European Union nor the more "political" FTAs of the United States seem to extend degrees of preferential treatment to selected partners that appear likely to produce constituencies opposed to multilateralisation.

The multilateral-friendliness of a given RTA depends considerably on the strategic motivations of the countries that crafted it. Some RTAs are deliberately designed with the

multilateral system in mind, and are intended to set precedents on either big matters (e.g. the inclusion of new issues) or smaller ones (e.g. specific deals within those issues). We have seen how that was the case for RTAs that the United States negotiated at the time of the Uruguay Round, one purpose of which was to show how an agreement could cover trade in services. It is possible that a similar dynamic could be at work in the case of those areas where the GATS negotiators left "unfinished business" for the future, with RTAs establishing precedents that might be taken up in the WTO, but that seems more hypothetical than imminent. The review of Hypothesis 1 (i.e. RTAs may be used by countries as a means of advancing issues that have either not made it on the agenda of the multilateral negotiations or on which progress has stalled) found partial support for this contention, with some RTAs establishing rules on government procurement of services. Those precedents are available if the WTO membership wishes to take them up, but for the time being that "if" appears to be a big one.

Three other topics reviewed in the international political economy of services and RTAs concerned the choices that countries make regarding their negotiating partners, the issues that they put on the table, and the kinds of deals that they reach. The data confirm Hypothesis 2, which holds that while the more trade-dependent countries will be attracted to RTAs with countries that represent large shares of their trade, countries that are larger and less trade-dependent may be more attracted to RTAs with smaller countries. One consequence of this pattern is that countries in the latter category – or at least the four biggest trading powers – have not yet engaged one another in RTA negotiations. The existence of this "zone of non-negotiation" among the Big Four is at least indirectly favourable for the multilateralisation of deals reached in RTAs, in the sense that if those countries were to begin negotiating RTAs among one another that might be taken as (further) evidence of trouble in the multilateral system itself.

Looking more specifically at what countries actually negotiate, what might we conclude regarding the content of RTAs? The general pattern is one in which the largest industrialised countries do not negotiate RTAs among themselves (as noted above), and developing countries often leave services off the table in the RTAs they reach with one another, so that the one type of agreement most likely to produce new liberalisation is a North-South RTA. Two of our hypotheses back up and elaborate upon this contention. The data generally support Hypothesis 3: Wealthier countries in which services account for a larger share of the economy are more likely to include services in the scope of their FTAs than are less developed countries where services are less prominent. But while the weight of evidence supports this contention, there are some important exceptions. The European Union, for example, leaves services out of many of its RTAs. That point is counterbalanced, however, by the data in support of Hypothesis 4 (i.e. in negotiations between partners of asymmetrical size, it is likely that the larger partners will extract deeper concessions from the smaller). In those RTA negotiations in which the European Union does include services, it generally leverages more GATS-plus commitments from its partners than it makes. The same is true for the United States, though the pattern after that does not wholly conform to the expectations of the hypothesis. When one couples these two observations with the earlier point regarding the absence of preferential treatment for developing countries on services in the RTAs of the United States and the European Union, these observations point to the real possibility that the services commitments made in RTAs – and especially the commitments made by developing countries in North-South RTAs – may indeed be multilateral-friendly.

The evidence point in that direction, but there is additional information that we would need to have real confidence in that conclusion. The analysis in this paper has been

necessarily circumscribed by the same limitation that hobbles most investigations of services trade policy, namely that we know a great deal more about the nominal difference between the commitments that countries make in their RTA and GATS commitments than we do about the real difference between either of these sets of commitments (their bindings) and the actual laws and policies that countries have in place (their applied measures). When any given country makes a commitment in an RTA that is *prima facie* more liberal than its GATS commitments we may well suspect that it has made a commitment to liberalise its existing laws, but in fact we cannot know without further (sometimes painstaking) investigation whether this commitment merely (1) removes some of the "water" between its GATS commitments and its applied measures (i.e. binds somewhere between the bound and applied rates), (2) removes all of that water but no more (i.e. binds at the applied rate), or (3) actually provides for new and real liberalisation (i.e. binds below the applied rate). And if indeed that third level is reached, we cannot tell without still more investigation whether the country has opted to extend any new measure of liberalisation solely to its RTA partner (as well as any prior RTA partners who may enjoy MFN rights) or whether it has, on a *de facto* basis (i.e. one that is not yet made *de jure* through inscription in its GATS schedule), extended that liberalisation to all other trading partners.

The domestic politics of services and RTAs

While our review of the international political economy of RTAs and services was generally positive, the domestic side of the equation is more troublesome. Here the evidence suggests how difficult it may be to achieve true liberalisation – as opposed to international codification of measures already approved domestically – in the field of services.

Hypothesis 5 provides that to the extent that legislators, civil servants, and other domestic policymakers involved in the regulation of services are willing to (1) enact market-opening rules (laws, regulations, etc.) and to (2) approve international agreements that consolidate these reforms they will prefer that the steps be taken in that order and not *vice versa*. There tends to be less real liberalisation of services in trade agreements than is the case for trade in goods, and countries often bind at or above their applied measures. That is a reflection of the general aversion on the part of domestic political institutions to the practice of legislation-by-treaty. This is a point that cannot, in the absence of a vastly larger database, be definitively supported through a large number of examples across time, sectors, countries, and agreements. It is nonetheless one for which there are at least anecdotal cases to be cited, and one that – the author believes – most close observers of the politics of RTAs and services would likely find plausible. There is also anecdotal evidence in support of the related Hypothesis 7, which provides that RTA negotiators may sometimes over-estimate the extent to which they may liberalise sensitive sectors. This can result in confrontations at home that affect the terms of the agreement in question and/or future RTAs.

The question then arises, how troubled should we be by the limitations that domestic political considerations may place on the liberalisation of services via trade agreements? The answer depends in part on how high we set our sights for what we want the trading system to achieve, both at the bilateral/regional and multilateral levels. If the purpose of negotiations on trade in services is to produce liberalisation that is real and substantial then neither the GATS nor the RTAs have done very well so far. But that is not necessarily the only metric by which we might render a judgment.

At a lower level of ambition, we might see virtue in RTAs as an opportunity for countries to consolidate the reforms that they have already undertaken in domestic laws and regulations. Multilateral trade negotiations, at least as presently conducted, produce results only once a decade or so, and thus do not provide much opportunity for countries to consolidate their reforms in their GATS schedules. RTAs may serve a useful purpose by providing a means by which (1) some of the older reforms that were not consolidated in the original GATS schedule are now inscribed in an RTA schedule (we might call this "removing the old water"), and (2) those reforms that have enacted since the end of the Uruguay Round are also consolidated in RTAs ("removing the new water"). The precedents that are thus set in the RTAs might then be generalised in the GATS schedule when the Doha Round is concluded. If we are satisfied with this level of ambition, then we may indeed conclude that RTAs have a high potential to be multilateral-friendly.

A few practical recommendations

This report has shown that services are less often included in RTAs than are issues affecting trade in goods, the negotiations in which they are included tend to produce more domestic controversies (e.g. "turf battles" involving different ministries, legislative committees or factions, and sub-national units of government), this is an area where industrialised countries are more likely to be the *demandeurs* than are developing countries, and the commitments that countries make in these negotiations are less likely to produce real liberalisation or meaningful levels of preferential treatment than is the case for trade in goods. While those points are generally negative, we may still join Baldwin, Evenett, and Low (2009) and – politely ignoring the remarkably mixed nature of their metaphor – ask whether spaghetti bowls can be building blocks.

Some of the data discussed in this paper suggest that there are at least some cases in which countries have made commitments in RTAs that achieve real liberalisation, and that they then extend the application of these reforms not only to their RTA partners but to other partners as well. That appears to be more often the case for developing countries than for industrialised countries. The *de facto* multilateralisation that is thus achieved might later be made *de jure* if it is inscribed in the country's revised GATS schedule.[29] In this sense RTAs may be seen as multilateral-friendly, but only to a degree that is empirically uncertain, could be legally fragile, and is ultimately contingent upon completing a multilateral negotiation that currently has no end in sight.

There are nevertheless a few steps that might help to ease the conduct of these negotiations. One would be to remove some of the opacity of the relationship between domestic laws, the commitments in RTAs, and countries' GATS schedules. While we may well suspect there are many areas where countries' actual, applied measures on trade

29. Note that this distinction between *de facto* and *de jure* liberalization is not identical to the one made in other OECD studies of "bottom-up" *versus* "top-down" liberalization (i.e. that which is achieved initially in RTAs *versus* that which is achieved initially in the GATS). The *de jure/de facto* distinction is without a difference as long as we assume that both the liberalization undertaken by a country in an RTA and its choice to extend that liberalization to other countries are permanent. In the event that the country were later to reimpose restrictions on access to its market, however, only the RTA partner(s) would have a legal basis for demanding redress. Unless and until the country inscribes this commitment in its GATS schedule, third countries enjoy the access only as matter of policy and not of law. That is a difference that may affect the investment decisions of firms.

in services are more liberal than their GATS commitments, we do not have comprehensive and systematic information on this point. That is a problem not just for analysts, but also for negotiators, other policymakers, and services providers themselves. To use the common aqueous metaphor, we do not know just how much water remains in countries' GATS schedules, nor the extent to which the GATS-plus commitments in their RTAs have the effect of removing just some of the water, all of it, or actually achieving real liberalisation.

It is a cliché for a study to conclude with the recommendation that the matter be studied further, but in this instance we need not only analysis but raw data. It would be a great boon to all involved in this field if there were made available, publicly and on a systematic basis, detailed information on each country's applied and bound measures (both in GATS and in RTAs) in all commercially important services sectors. That is far easier said than done, as this implies a Herculean level of analysis of schedules, laws, regulations, and practices not just at the national level but, for many countries, at the level of states, provinces, *länder*, and the like, but there is no doubt that clearing away the informational fog in this area would be helpful to analysts, negotiators, policymakers, and service providers. The fact that work is underway on such a project in the OECD can only be applauded and encouraged.

Reforms might also be considered in the ways that services negotiations are conducted in the WTO. Let us suppose that the comprehensive information described above were in fact available, and that it identified many areas where countries had liberalised on either a purely autonomous basis or as a consequence of their RTAs (the results of the latter having been extended *de facto* to third countries as well as RTA partners). These may be areas where countries would be willing to take the next step of *de jure* liberalisation, inscribing these reforms into their GATS schedules, but in the negotiating system now in place they are invited to do so less than once a decade. The experience of the "built-in agenda" period between the Uruguay and Doha rounds suggested that it is entirely possible for WTO members to conduct fruitful negotiations on services outside of a round. It may be advisable, once this round is finally completed, to provide more opportunities for flexible, issue-specific means by which countries might negotiate for or even autonomously choose to bind their reforms.

The information exercise described above could be an important part of that process. In addition to facilitating sectoral negotiations along the lines of the agreements that were reached during the built-in agenda (notably on telecommunications and financial services), the information could also be used to achieve reforms outside of formal negotiations. One possibility would be to add a new element to the Trade Policy Review Mechanism, such that the reports on each country included a new section that (based on the new data set) analyzed in depth the extent to which countries' autonomous or RTA-led liberalisation has added "new water" to their GATS schedules. Countries might then be invited to update their GATS schedules in order to reflect in their multilateral commitments what has already been achieved in their national laws. That should be an especially easy step in the case of any reforms that were initially achieved through domestic reform, were later inscribed in RTAs, and then extended to third countries on a *de facto* basis.

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