





likely frustration with the WTO multilateral approach, where many inconsistent interests make the decisional process very slow, plays an important role in the current integration trend.

Professor Simona Beretta analyses in depth this topic in her recent paper *Economic principles of Regional Integration*, included in the book *Elements of Regional Integration. A Multidimensional Approach*, publication edited by ZEI, Center for European Integration Studies at the Rheinische Friedrich-Wilhelms-Universität Bonn. This book presents the different dimensions of regional integration through a multidisciplinary approach, from the intensified economic cooperation to political, legal and cultural aspects of integration.

Professor Beretta's paper reports both political and economic reasons as explanations to this impressive spreading. International integration is presented in its natural ambivalence. Whether taking into

account the comparative advantage producing inter-industry trade or the absolute advantage perspective, integration produces winners and losers. Whether the determinant of the comparative advantage is difference in technologies or difference in proportions of factor endowments, integration will lead to inter-industry specialization and trade. But the ambivalence is evident: while consumers are happy to buy imported cheaper foreign goods, less efficient domestic producers are replaced by more efficient foreign producers: domestic producers of the imported good are damaged by integration.

Intra-industry trade has been the fastest growing component of international trade: it occurs when markets are non-competitive, due to product differentiation and/or economies of scale. In these cases, regional integration will trigger a self-reinforcing "circular causation": big firms will gain more and more market shares through integration, relocation of their production and so on, fostering the collapse of the smaller,

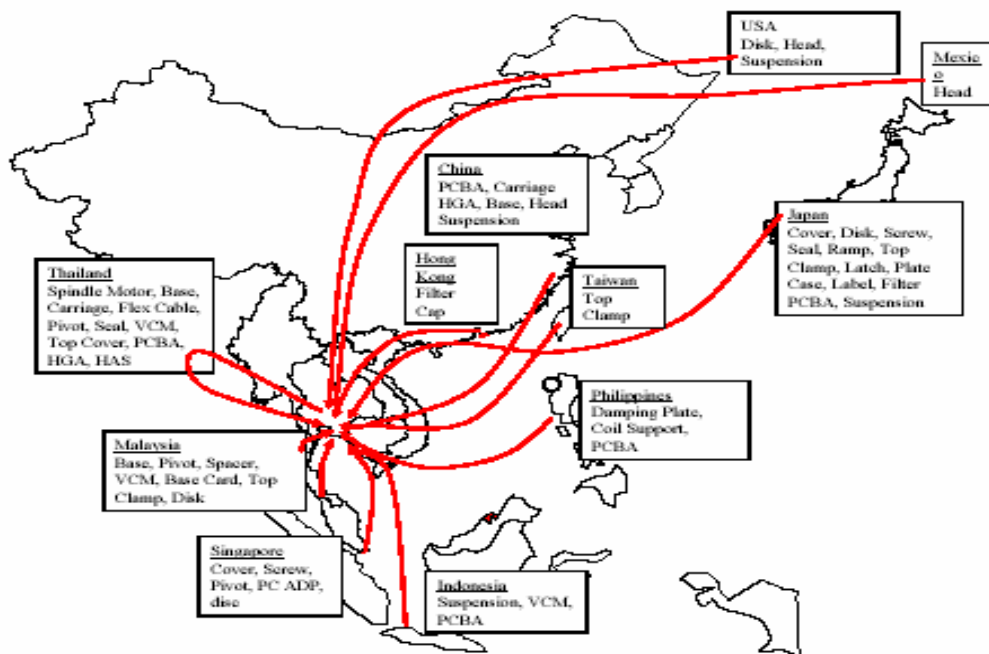


less innovative firms which are the losers in this case. The figure below shows at a glance an example of global production unbundling in an IT good: there is a long list of nations where parts are sourced for a hard-disk in

development, ambivalence shows up in terms of different levels of factor remuneration. Higher wages in the country with an absolute advantage in terms of total factor productivity will induce migrations, amplifying the

An example of global production unbundling in an IT good.

Source: R. E. Baldwin, *Multilateralizing Regionalism*, Geneva, 2006.



Thailand that is then shipped on to many different markets to be used in various electronics. Any regional system must be able to cope with and to favour this complicated map of trade routes.

In a dynamic perspective, which is more evident in case of integration between partners at different levels of

negative trend in the declining region. In this case, counterbalancing policies may be needed to save the losing economies. But how to choose such policies? Will they respect the WTO's rules and the principle of non-discrimination defined in the GATT?

Losers tend to react by lobbying politicians in order to receive



“protection” and limit their losses in exchange for political support. That’s the game policy makers have to play during the decisional process about trade policy, where both economic and political considerations matter.

In trade policy decisional process, the principle of the median voter seems to fail in favour of the collective action logic: the first approach is in fact eroded by the strength of pressure groups and in particular of the losing producers that have more vigour, due to resources and organizational capacities, in claiming protection for their survival and in offering their political support to the party that will take care of their interest.

The result of the game is then a protectionist bias that can operatively be translated in many different instruments: tariffs, import quotas and voluntary exports restraints (VER) with all their differences in terms of effectiveness, efficiency (see the rent seeking effort of some agents to gain import licences) and equity. But even some internal policies can turn into

protectionist instruments: production subsidies to local producers or domestic regulations imposing some medical or environmental standards to imported goods become “technical barriers to trade” (BTB) and charge real costs to foreign producers in meeting the requirements. These are the new forms of protectionism that become more and more important due to the progressive dismantle of the traditional measures agreed during the WTO rounds. But do these new forms of protectionism answer to the interest of the entire society or meet just the interest of some groups defending themselves against foreign competition?

In this sense regionalism may seem to be contradictory to the WTO’s multilateral trading system, but in some cases it has allowed groups of countries to negotiate rules and commitments that go beyond what was possible at the multilateral forum.

Preferential Trade Agreements (PTAs) also exhibit ambivalence: cutting the tariffs on the imports from just few countries could lead to import



good from a non efficient producer, but a producer that seems to be efficient just for the absence of a tariff and not for the price of the good. However a trade expansion among the members of the PTA is recorded (trade creation), but the exchanges are not as efficient as they could be without the agreement (trade diversion).

PTAs could then turn into protection instrument rather than being a step towards liberalization.

The overlapping of different PTAs makes the systemic configuration very complicated till the shaping of a *spaghetti bowl* where Rules of Origin can easily become a protectionist instrument and political considerations prevail on efficiency.

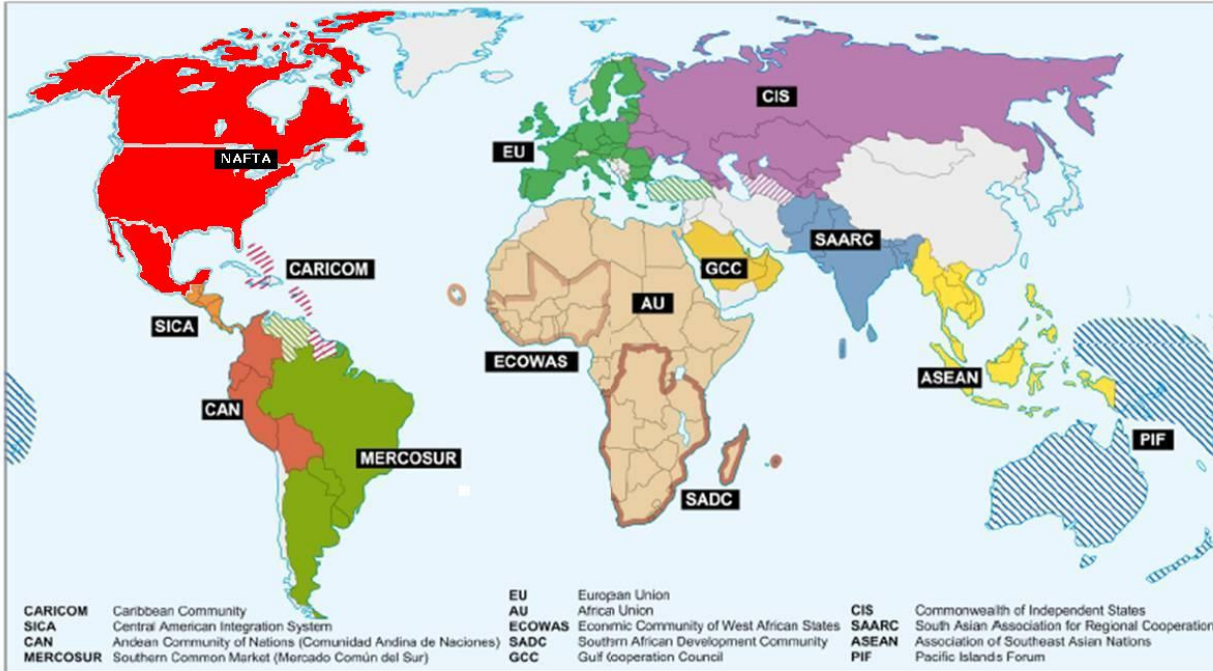
PTAs are now spreading even in the form of North–South and South–South agreements. In the first case, South countries afford big costs, like a little tariff reduction by North countries against a huge reduction of their high tariffs and the compliance with North standards, in order to attract de–location of North industries and foreign direct investments. On the

contrary South–South agreements seem to be a good attempt to develop institutional capacity in a more familiar context than that of the global competition.

Despite the different forms that regional integration can assume, the process will require more and more harmonization and mutual recognition of standards as the European example shows in order to be the local path towards global integration.



### A world of regions



Source: *ZEI Regional Integration Observer*, Vol. 1, No. 1, November 2007.