# Research Report

## The Economic and Social Council

### Encouraging and Managing Free Trade Agreements

MUNISH

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| **Forum** | ECOSOC |
| **Issue:** | Encouraging and Managing Free Trade Agreements |
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## Introduction

In order to fully comprehend this particular issue of the forum, it is important to be acquainted with the current role and impact of free trade in the world. The economic theory behind free trade is quite simple. This research report will explore free trade, what it implies, and present two examples of the most significant free trade agreements today. The aim of this issue is to maintain such agreements and further promote free trade to other nations. Free trade is a governmental policy in which a country does not discriminate against foreign goods and services nor exports, thus limiting tariffs, subsidies or quotas on such products. Tariffs are taxes on goods and services a country imports. Given the law of supply and demand which states that demand for a product falls as price increases, ceteris paribus, consumers would tend to purchase domestic, or national, products rather than those that are imported. Governments use subsidies to support a particular domestic industry economically, thus reducing costs for consumers all around the world, and boost exports for favorable balances of trade. The outcomes of such policies, called protectionism, are still an important subject of debate. Some parties argue that protectionism will support domestic industries, thus increase incomes in that particular country, and with that, standards of living would rise. On the other hand, supporters of free trade oppose protectionist policies, and strive for the elimination of tariffs and subsidies. Such supporters believe free trade policies will promote specialization, with every country specialization in their most competent industries. This would, in their eyes, lower total costs for goods and services which would then be more efficiently produced. Furthermore, free trade would promote innovation. Higher quality goods entering a country will force domestic firms to either reduce costs or increase quality. This would ensure fair competition in a global market, more business opportunities and jobs, and further develop countries.

Most free trade agreements are signed between neighboring nations. However, there are exceptions to this, notably the World Trade Organization (WTO), and the Trans-Pacific

Strategic Economic Partnership Agreement (TPP). World trade is founded on rules laid out by the WTO that help ensure that trade agreements and obligations between countries are open and fair.

## Definition of Key Terms

### Free Trade Agreements

The purpose of free trade agreements (FTAs) is to increase the overall efficiency and the fairness of competition in terms of trade between countries signing the agreements. FTAs aim to eliminate tariffs imposed on foreign goods as well as promoting economic integration and expansion of opportunities for citizens of the countries signing the agreements, for example, the Eurozone.

### Tariffs

Taxes levied on foreign goods entering a country. "Customs duties on merchandise imports are called tariffs. Tariffs give a price advantage to locally-produced goods over similar goods which are imported, and they raise revenues for governments." (WTO)

### Subsidies

Economic aid given to a particular industry to promote the production and consumption of a good or service. (For example, cereal production in France.) "A country can undermine its market access commitments by providing subsidies to import-competing industries. In addition, subsidies given to competing exporters in third countries can divert trade away from a country that had relied on negotiated market access to another market." (WTO Repot 2006)[1]

## General Overview

Free trade agreements generally follow the following features:

1. Trade of goods without taxes or trade barriers
2. Trade of services without taxes or trade barriers

[1] http://www.wto.org/english/res_e/booksp_e/anrep_e/wtr06-2b_e.pdf

3. The absence of trade-distorting policies such as laws and regulations that give some firms advantages over others (such as subsides or taxes)

4. Free access to markets

5. Free access to market information

## Status today

A substantive amount of countries today are members of the World Trade organization. The WTO aims to limit tariffs and subsidies that certain countries give to particular domestic industries as well as facilitating access to foreign markets, but does not completely eliminate such barriers to trade. Additionally, many countries are part of regional free trade agreements.

The European Economic Area within the European Union and the North American Free Trade organization are currently the world's largest FTA's.

### *Enabling Trade Index*

An "enabling trade" index was developed to measure governmental policies, services and various factors to determine and rank in which countries trade in goods across frontiers is facilitated. The four sub-indexes are market access, broader administration, transport and communication infrastructure, and business environment.

Here is a list of the top twenty countries ranked using the enabling trade index[2]:

| Rank | Country |
|---|---|
| 1 | Singapore |
| 2 | Hong Kong |
| 3 | Denmark |
| 4 | Sweden |
| 5 | New Zealand |

[2] http://www3.weforum.org/docs/GETR/2012/GlobalEnablingTrade_Report.pdf

| | |
|---|---|
| 6 | Finland |
| 7 | Netherlands |
| 8 | Switzerland |
| 9 | Canada |
| 10 | Luxembourg |
| 11 | United Kingdom |
| 12 | Norway |
| 13 | Germany |
| 14 | Chile |
| 15 | Austria |
| 16 | Iceland |
| 17 | Australia |
| 18 | Japan |
| 19 | UAE |
| 20 | France |

## North American Free Trade Agreement (NAFTA)

The NAFTA became effective on January 1, 1994, previously signed by the United States, Mexico and Canada. The agreement created a trilateral trading block across the North American continent. Thanks to NAFTA, 450 million people can now export to each other at lower costs. According to the USTR, it is responsible for over 1.6 trillion dollars in goods and services every year, and estimates that NAFTA increases the US GDP (Gross Domestic Product, a country's total income, or total output) by 0.5% annually. NAFTA has benefited member states in a number of ways. Firstly, the elimination of tariffs has decreased the costs of importing and thus kept inflation to a minimum. The reduced costs of trade with increased agreements on international rights for business investors has boosted investment and growth for both big and small businesses, thus creating jobs in some sectors of the economy. With trade increasing as much as from $297 billion in 1993 to $1.6 trillion in 2009, US farm exports went from making up 22% of US exports in 1993 to 30% in 2009. In addition to this, foreign investment across all countries increased economic growth. Some economists argue that NAFTA has benefited business owners and elites in North America and negatively impacted mexican farmers who could not compete wtih the mass agriculral production in the US. US manufacturing jobs were also hurt by the competition coming from Mexican workers.

## European Single Market

The single market describes the EU's plan to promote free trade. This advanced level of economic integration includes the European Customs Unions, the single currency, and the Schengen Convention. The single market can trace its origin in 1957, with the Treaty of Rome, which outlined the four economic freedoms that it wanted; the free movement of factors of production, goods and services. The Maastricht treaty of 1992 began the final leg, by creating the economic and monetary union, which came into effect in 1999. The European Commission has been focused on increasing economic freedom across borders and improving competitiveness. While patents are yet to be harmonized and the energy sector liberalized, the 2011 Single Market Act involved 12 projects aiming to boost growth and competitiveness, by increasing labor mobility and protection of consumers.

### *How is it managed?*

In addition this vast area where people are free to move, trade goods and invest without having to deal with barriers, both technical and legal, the single market aims to provide ground for economies of scale, commerce ranging across Europe enabling faster growth. An example of a concrete policy established by the EU is the "Eurotariff", which limits the cost of calling within the EU, across borders, and warns customers spending over 35 pounds on data roaming. To regulate this agreement, the EU commission passes regulations, via directives, down to national governments, which then pass the law through their respective parliaments. Furthermore, the single market also helps in ensuring fair competition. For instance, the EU Commission fined

17 firms in the bathroom equipment industry over half a billion euros for price-fixing three year ago.

## Major Parties Involved and Their Views

### United States of America (USA)

The USA is involved in various free trade agreements. From the Theodore Roosevelt administration onwards, the US has become a major party in international trade, extensively negotiating with neighboring countries both in the Caribbean and Latin America. The United States currently leads along with other nations groups such as the GATF (General Agreement on Tariffs and Trade) until it was replaced by the WTO.

### China

China has signed 8 free trade agreements, has 14 FTA partners, which comprises 31 economies. China has played in increasingly important part in calling for free trade areas with its Asian and Pacific neighbors, including the 2004 proposal for a new East Asia Summit, which purposely excludes the US. It includes the Association of Southeast Asian Nations (ASEAN) Plus Three (India, Australia and New Zealand), and held its first summit in 2005. Additionally, China is a founding member of the SCO (Shanghai Cooperation Organization) with Russia and Central Asian republics. Since 2000, China is a "permanent normal trade relations" country with the United States, with the US allowing Chinese exports at low tariffs at the same level as goods from most other of its trade partners. However, some politicians from countries have said that the Chinese Yuan currency is undervalued, which allows China to exports cheaply, giving her an unfair trade advantage.

### European Union (EU)

Not only is the EU is world's largest single market, the EU is the world's largest trader, accounting for as much as 20% of world trade. Furthermore, free trade among its member states was one its main principles. The EU aims to open new markets in the world to create growth and jobs for Europeans. The EU works closely with the WTO as well as individual government to create its international trade network. It aims to ensure traceability, transparency, reduced child labor and environmental destruction. The EU also sees in a trade a way to develop the world's poorest nations, by allowing for lower duties to support small business and investment to create jobs and growth for such nations.

### World Trade Organization (WTO)

The World Trade Organization aims to promote the liberalization of international trade. Born in 1995, replacing the GATT, the organization supervises free trade agreements and provides a network for negotiations. It regulates trade between its member countries.

## Timeline of Events

| Date | Description of event |
|---|---|
| 1946 | The Bretton Woods system is set up. It worked to prevent trade barriers, as many after WWII believed the war was caused by the lack of liberalized trade. |
| 1947 | 23 countries agree to the General Agreement on Tariffs on Trade. |
| 1958 | European Economic Community |
| 1960 | European Free trade Association |
| 1992 | Maastricht Treaty |
| 1994 | NAFTA takes effect |
| 1995 | Creation of the WTO |
| 2002 | EU launches the Euro currency |
| 2005 | Central American Free Trade Agreement passed by the US, expanding the US Free Trade zone to Central American countries |

## UN involvement, Relevant Resolutions, Treaties and Events

The United Nations Conference on Trade and Development was established in 1964, and is a permanent intergovernmental body that deals with trade, investment and development. It grew from the view that the GATT/WTO/IMF/WB as institutions were not properly organized to handle economic problems in LEDCs. While the body does not necessarily deal with FTA's, it is likely to be involved in agreements in involving multiple least developed nations.

- Charter of Economic Rights and Duties of States[3]
- The role of International Investment Agreements in attracting Foreign Direct Investment to Developing Countries[4]

[3] http://unctad.org/sections/dite/iia/docs/Compendium/en/6%20volume%201.pdf

- **A/RES/52/209** Business and development[5]

## Possible Solutions

In order to increase the liberalization of free trade, the UN can serve as a platform for negotiations between member states in coming to various agreements. Although this is done, in a large part, by the WTO, the UN can play an important role in bringing various preexisting FTA's as well as the IMF the WTO and the WB together to discuss the promotion of free trade. The roles of government must emphasizes as they can further develop infrastructure in their respective territories to further enable access to markets and erasing technical barriers. Providing judicial frameworks to protect investors and entrepreneurs is necessary for an exchange of goods and services between nations. Combatting corruption and bribery is also necessary for a better international business environment.

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[4] http://unctad.org/en/Docs/diaeia20095_en.pdf

[5] http://unpan1.un.org/intradoc/groups/public/documents/un/unpan000708.pdf

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