TRADE LIBERALISATION IN EUROPE AND THE REST OF THE WORLD

Cristian **Spiridon**
Alexandru Ioan Cuza University of Iaşi, România
cristian.spiridon@feaa.uaic.ro

Abstract: *The present paper aims to disseminate how liberalisation processes were conducted around the globe and especially in Europe since the XIXth century up to date. The research objective is to review the liberalisation of trade dynamics and create an image of the architecture of the most important trading blocs. Analysis will be conducted considering the three major regional blocs: Europe, North America and East Asia. The main findings will show that, despite the few mutations that occurred in international trade as a result of the emergence of developing nations as major trade partners, the European Union and the United States remain the economic and trade hegemons.*

Key words: European Union, trade blocs, protectionism, regionalism, trade agreements, multilateral negociations, financial crisis
JEL classification: F10, F13, F14, F15, F36

INTRODUCTION

Since the intensification of the financial crisis in September 2008, the issue of protectionism has received considerable attention among the general public. These pressures of escalating protectionism threatened and still threaten to intensify such a practice in response to the downturn of the world economy. Early signs quickly became apparent to the world economies. Immediately after the commitment of the Group of Twenty most developed countries in the world (G20) to refrain from raising new barriers to investments or trade in goods and services, imposing new export restrictions or implementing disjointed measures to stimulate exports recommended by the World Trade Organization, 17 out of 20 states have announced protectionist measures (Newfarmer and Gamberoni, 2009). According to the World Trade Organization, 13 of the 20 G20 countries have implemented the announced measures, and issues such as"buy / invest / lend or hire locally" has taken the forefront of the political flavor urgings.

Protectionism explosion that took place after markets collapsed in 1929 contributed to the spread of a worsening economic depression. Between 1929 and 1933 world trade trend had turned into a complete downward spiral contraction of 66 percent (Grossman and Meissner, 2010). Protectionist policies implemented during the time of the Great Depression had taken a variety of forms. To illustrate, we can mention the surge in import tariffs on the ground of the U.S. Smoot-Hawley Act introduced in the 17th of June 1930, but many other non-tariff measures have been introduced in that period including: import quotas, competitive exchange rate devaluations, export subsidies and other indirect actions (Eichengreen and Irwin, 2009).

The probability that a similar event would materialize as a response to the current crisis is not negligible. Nowadays, similar to the period of the Great Depression, one could take into consideration promoting protectionism as a tool of macroeconomic policy management in times of severe fiscal and monetary restraints (Almunia et al*.,* 2010). The purpose of this paper is thus to capture the context of the escalating protectionism that can occur in response to the financial crisis burst in the late 2007. There would be observed the movements of the ”commercial tectonic plates” over the last two centuries which caused either the decay of the trade puzzle or conversely have brought the solution to the puzzle.

1. HISTORY OF TRADE FROM THE XIXth CENTURY UP TO DATE

Trade liberalization has acquired a pronounced character in the early nineteenth century, when the forefront of the global economy was the United Kingdom. Its economic domination could not have been translated in a sort of interstate ordered relations and in the construction of an open international economic environment. Thus, throughout the world, there were periods of global trade openness (1846-1879, 1945-1970) continued by periods in which protectionism had made its presence felt (1879-1914). Periods of economic openness during the nineteenth century and the twentieth century were overlapped by the succession of global hegemonic position of Britain and the United States. The repeal of the Corn Law by the United Kingdom (1846) and the Navigation Act signed in 1849 are seen as steps towards building a European free trade area (Ruffin and Dogan, 2012). The steps that followed were mostly shy, at least until the end of World War II. Britain's inability to turn, after 1815, its industrial and financial predominance in military domination of Europe did not allow the government of this country to securitize interests by force or threat of force. Military expenditures as a ratio of national income were the lowest compared with those of the Great Powers during 1820-1913. Thus, countries like Russia and France were considered the most powerful states with a real capacity to interfere in the social and political affairs of the continent (Lacher and Germann, 2012).

The step taken by Britain unilaterally towards free trade was not followed by other European countries. The lack of bargaining power or persuasion with regard to mutual tariff reduction and the integration of its trade partners in an institutionalized system of free trade caused the island state to abandon trade agreements based on the principle of tariff autonomy and to refrain from exercising military force on open markets in the continental Europe, to undertake a non-interventionist policy, and to give up its attempts of peacefully persuasion by using the hegemonic leadership related tools. The critical result of the British government insistence on a unilateral focus on promoting free trade and tariff autonomy was the absence of an engine strong enough to put in motion a mechanism of institutionalization under British leadership. No attempt to punish or prevent commercial libertinism and the return to the protectionist policies of its commercial partners has been undertaken by the island state. Therefore, the first European network of trade agreements that sprang from Anglo-French Treaty signed in 1860 had France as an architect and not the United Kingdom. This endeavour being taken, the Most Favoured Nation principle was institutionalized, which was subsequently borrowed by the United States and promoted as a mechanism of reciprocity.

The isolation of Great Britain has manifested most in the monetary and financial sectors. Even after the gold standard monetary system replaced the system based on bimetallism - promoted by France (1880) - Great Britain assumed no responsibility for creating or maintaining a stable international monetary system. The slow and diffuse spread of the system based on gold standard among other nations by the mid-1870s underlines the supremacy of the local political considerations over liberal internationalist motivations and the dynamics of geopolitical competition to the detriment of hegemonic stability.

The monetary system based on gold fell in 1914. European countries had adopted this system as an effort to establish a unified currency, to improve control over the banking sector and to create stable conditions for foreign investments. Giving up the gold standard indicated a divergence of economic policies on the continent and beyond. World War I was the key event that anticipated the split of the world into military and economic blocs. The Smoot-Hawley Act (1930) triggered trade wars raged between the United States and Germany, Italy, Japan and the Soviet Union. Behind these conflicts there were hidden autarchic and militaristic motivations. Small countries in Europe have formed the Group of Oslo (1930), while France and Britain have supported their colonial empires applying preferential trade tariffs within.

The early 1950s brought with them the establishment of the General Agreement on Tariffs and Trade (GATT). The conflict between Britain, which insisted on the reduction of trade tariffs on British goods, and the United States - that was calling for the abolition of the British system of imperial preferences - threatened to strangle the agreement in the bud. At that time Great Britain (and the colonies) was still the most important actor on the stage of global trade. By 1963, the European Economic Community (EEC) appeared on the firmament. Great Britain formed the European Free Trade Association (EFTA) with Northern Ireland, Denmark, Norway, Sweden, Austria, Switzerland and Portugal, and applied to join the EEC. Many colonies were represented by independent states that imposed tariffs on manufactured goods of British origin. Rich countries have become richer while the poor led a race track at a distance. In particular, Europe has experienced extraordinary GDP (gross domestic product) growth rates and North America keep up with the old continent. In the 1960s there were already outlined two major trade centers: Western Europe and North America. A large fraction of global trade has been carried out within or between these two hubs. Trade flows between these two centers and various ”spokes” - Latin America, Africa, The Middle East, Asia and Japan - were very small (insignificant was also the trade between spokes).

This model of bipolar commercial development has continued to evolve during the second half of the nineteenth century, with one major exception: the emergence of Asia. Japan trade grew by about 5% in the total volume of global trade and was followed by China's assertion and the increasing of intra-Asian relations. Currently, Asia accounts for about 25% of the world trade. Trade between and within Western Europe and North America represent about two-fifths out of the total (O'Driscoll and Cooper, 2008).

With regard to tariffs, in the 1950s the average tariffs exceeded 15% both in Europe and North America. However, the main obstacle to trade was represented by quantitative restrictions (imposed in most cases on behalf of the balance of payments interest). In other parts of the world prices were also higher in the early 1960s, but with the Kennedy Round they went on a downward trend. To give the appropriate extent to the impact of the negotiation rounds in the General Agreement on Tariffs and Trade on the Asian trade, the situation can be exemplified by Japan, a country where rates fell from 18% in 1960 to about 3% in the close 2000. In the same period, the average applied tariff to imports of manufactured goods and services in the U.S. and Europe was 4%.

Post-war liberalization was the main focus in the industrial sector, in which bidirectional trade flows (imports of parts and components - exports of finished products with high added value) prevailed. Rich countries have liberalized more than poor nations did within the General Agreement on Tariffs and Trade and the various regional trade agreements (RTAs). Regional tariff reductions were accompanied by multilateral liberalization. Unilateral liberalization has gained importance in developing countries since the mid 1980s. Tariff reductions under the GATT began to be applied when the worldwide ceilings were very high and the process took at least 40 years till the initial targets to be achieved (Baldwin, 2006).

The motor of trade liberalization in the post-war were the United States. Lessons on the dangers of isolationism were well assimilated by the American politicians appointed to lead the destiny of this country in the second half of the twentieth century. United States assumed the lead quickly and consistently acted to create an open international trading system (GATT) and a stable monetary system (contributing decisively to the establishment of the International Monetary Fund). However, the establishment of the World Bank and the launch of the Marshall Plan simbolized the significant contribution and responsibility of the U.S. for peace and prosperity creation beyond its borders. U.S. hegemony has helped building the foundations for a sustainable economic growth of the countries in Western Europe until the early 1970s, and the rapid development of the Asian countries such as Japan or South Korea. The rapid ascension of the American continent has created concerns in other parts of the world, so that, stimulated by this example, many developed countries have followed a process of economic catching-up (in some cases countries have resorted on protectionist practices to ensure success). In this context, protectionist sentiment has begun to win preponderence mainly leading to a series of challenges to the traditional policy based on free trade. The financing of the war in Vietnam and the launching of social programs had fueled inflation, a phenomenon that has been exported abroad automatically given the role of the U.S. dollar as an international reserve currency.

In 1971 the United States abandoned the fixed exchange rate system established by the Treaty agreed at Bretton Woods, announcing a period of international exchange currency. The Oil crisis, followed by the world debt crisis, combined with the maintaining of a series of barriers in the way of international trade, have questioned the ability of american hegemony to ensure future stability and global interstate order.

In summary, the 1970s witnessed the assertion of largely protectionist sentiments in the United States of America, motivated by the suffering domestic industries engaged in international competition, sufferings caused by state interventionism practiced by the participants in the cross-border trade. However, the project of trade liberalization, which was launched in 1934 and revived after World War II, survived the wave of hostility (Chorev, 2005). This was accomplished by replacing existing institutions governing international trade at that time. In 1974 a new institutional agreement was signed - The Trade Act - which had raised more solid obstacles in the way of protectionist outburst. The United States of America have followed the path of free trade and, amid an extraordinary industrial development, have emerged as an economic and military hegemon in the second half of the twentieth century. Unlike the United Kingdom in the nineteenth century, the United States played a more active line of trade liberalization, both through multilateral negotiations and regional agreements (Baldwin, 2006).

The shaping of the U.S. hegemonic status after 1950 led to reactions across the Atlantic. After several failed attempts in the direction of economic integration, the six major European countries except Great Britain (Germany, France, Italy, Belgium, the Netherlands and Luxembourg) signed the 1957 Treaty of Rome that gave birth to the European Economic Community (EEC). The domino effect was reflected on Britain that, along with Norway and Switzerland founded the European Free Trade Association (EFTA). However, the success of the European Economic Community led Britain to join the EEC in 1961 and countries like Ireland, Norway and Denmark to apply for membership in the community. Trade liberalization within these regions has led the United States of America to find a way to rectify the situation. Thus, in 1961, President Kennedy began negotiations on establishing a common external tariff in relation to the EEC under the umbrella of GATT. Consequently, in 1962 the Trade Expansion Act was signed that triggered a fundamental change in how multilateral negotiations are held. Since the Kennedy Round, reducing trade tariffs occurred in a much smaller pace. The event kicked off a period of 30 years of increased trade liberalization. Kennedy, Tokyo and Uruguay Rounds have each reduced industrial tariffs by about one third. But more important is that each cutting limit imposed to trade brought a repositioning of pro-liberalization economic policies in relation to anti-liberalization forces in most countries that participated in the various trade agreements on a reciprocal basis. One of the most important sectors that made exception was agriculture. EEC's Common Agricultural Policy introduced in 1962 and the EFTA have not included in the agenda the agricultural liberalization issue.

By 1973 Western Europe had already established a virtual free trade area if we take into consideration the concatenation that was produced between the EEC, EFTA and the series of Free Trade Agreements (FTAs) between members of these interstatal organizations. This deepening and widening of the free trade area in Western Europe was perceived as a threat to the other major players in the international trade - the United States, Japan and Canada (trade diversion effect).

Tokyo Round negotiations (1973-1979) had made official the asymmetric treatment of the developing countries. Similar to the past periods, regionalization, unilateral liberalization and multilateral trade were complementary in a multicoloured landscape. The focal point of the Tokyo Round of negotiations was to cut off non-tariff barriers. The two oil crises (1973 and 1979) taken together with the failure of the monetary policies accros the globe have established stagflation in the major nations involved in the international trade. The economic climate characterized by a high unemployment rate and a rampant inflation has dissipated the excitement posed on unilateral, regional or multilateral liberalization. Europe sank into pessimism and the United States turned to an aggressive unilateralism after giving up the fixed exchange rate system based on dollar.

In 1986, after the stagflation phenomenon had been defeated and economic growth had been recovered in the main countries involved in the international trade, a new session of negotiations was launched in Uruguay. Prices set by the United States and Europe in the Most Favoured Nation Clause fell by 2% to the level that is present today. Similar to the developments recorded in the 1960-1980 period, regional trade liberalization occurred in parallel on both sides of the Atlantic, on one hand as a result of the domino effect and on the other hand due to the realignment of the economic policy forces in the nations participating in the global trade - in this way making any liberalization politically optimal. European Economic Community has grown visible, signing and ratifying the Single European Act (1986) that has been translated into a consistent set of directives regarding liberalization and deeper economic integration. EFTA sought an agreement with the EEC, negotiations being finalized only in 1993. In the North America area, Canada proposed to the U.S. to sign a free trade agreement (CUSFTA – Canada and United States Free Trade Agreement) which came into force in 1989. Australia and New Zealand also took the path of regional integration in 1983 ratifying the close economic relations (ANZCER – Australia New Zealand Closer Economic Relations).

The liberalization pattern was maintained throughout the 1980s. Unilateral or multilateral negotiations have taken the place of regional integration, so that regionalism has been especially intensified not enlarged. Contrary to the expectations, the free trade agreement signed between the U.S. and Canada had not created a domino effect because of the expected resistance of Mexico to open out its trade in general and its trade with the United States in particular. Faced with a series of debt crises and severe recessions in the 1980s, Mexico began to liberalize trade unilaterally, then became a signatory to the GATT, and later joined Canada and the United States in the North American Free Trade Agreement (NAFTA) in 1994. This event led countries such as Chile, Brazil, Argentina, Paraguay and Uruguay to seek agreements with the U.S. on the establishment of Free Trade Zone. As the U.S. Congress rejected many of these requests, Latin American countries had reacted the same way that Britain did in 1960 - formed blocs along with the excluded states. The most important of these was by far the MERCOSUR (Mercado Comun del Sur – Common Market of the South, March, 1991). The idea started from a bilateral agreement between Brazil and Argentina, and the domino effect drew Paraguay, Uruguay, Chile, Bolivia, Colombia, Ecuador, Peru and Venezuela as associate members.

2. THE FALL OF THE USSR

In the late 1980s the failures of the Soviet Union on the economic ground had imposed application of pro-market reforms (perestroika) and greater openness to foreign trade (glasnost). By 1991, the East European bloc disappeared and the USSR split into several independent republics. The European Union seized the opportunity and signed a series of bilateral trade agreements with 12 countries from Central and Eastern Europe (CEECs countries). To avoid trade discrimination, the EFTA countries have signed bilateral agreements with all 12 countries in CEECs. This created a"hub and spokes" situation type around the European Union (Baldwin, 1995 in Baldwin, 2006). The domino effect manifested in this case, the Mediterranean countries seeking to conclude free trade agreements with the EU (Turkey, Tunisia, Israel, Morocco, Jordan, Palestine Liberation Organization, Egypt, Algeria, Lebanon, and Syria).

By 1997, the European Union (EU 15) established the Pan-European Cumulation System (PANEURO) with EFTA states and 10 countries from Central and Eastern Europe. In 1999 the PECS included Turkey.

Across the Atlantic, Mexico took advantage of the bilateral agreements with the United States and Canada and signed other agreements with the European Union and Japan, as well as with 40 other nations. Chile along with the EFTA states took the example of their neighbour, the United States. The effect of this multiplicity of bilateral agreements – a situation when small states seek free trade agreements worldwide - was the transformation of the three classic trade blocs (Europe, North America, East Asia) in regions with unclear borders and multiple links (Chortareas and Pelagidis, 2004).

3. TARIFF REDUCTIONS IN THE UNITED STATES OF AMERICA

Subsequent to the creation of NAFTA and the Uruguay Round, the United States returned to the liberalization model based on three levels (unilateralism, bilateralism and multilateralism) used since the 1960s. Regarding unilateral liberalization, a noticeable innovation was the African Opportunity and Growth Act 2000. On the front of multilateralism, the United States were completely involved in taking the Doha commitment for further tariff reduction, especially in the agricultural and services sectors (Bussiere et al., 2011). At the bilateral level, the policy was taken to increase the number of such agreements (agreements were concluded with Singapore, Jordan, Chile, Australia, Morrocco, El Salvador, Nicaragua, Costa Rica, Honduras, Bahrain, Guatemala, Korea and many other countries in the East Asia).

Signing many trade agreements conducted only to an increase of the complexity of the global landscape.

4. TRADE LIBERALIZATION IN ASIA

By the early 1980s, the reduction of trade tariffs in Asia was limited to the liberalization undertaken by Japan in the Most Favoured Nation Clause (GATT) and the unilateral extension of preferences to other nations. Since 2006 one can see the emergence of an economic integration process outside regional free trade arrangements. The only major trade agreements - the free trade agreement between ASEAN (the Association of Southeast Asian Nations) and China, the Free Trade Agreement between ASEAN and Korea have not generated the expected results because they were not completed, and the only Asian arrangement officially implemented - AFTA - was characterized by very low usage rates.

The liberalization process has received a big boost when China decided to open global economy. This has accelerated the erosion of the industrial comparative advantage held by East Asian nations with higher incomes and increased the attractiveness of offshoring. Race to attract FDI pushed China and ASEAN countries to reduce tariffs unilaterally (Kuchiki, 2003 in Baldwin, 2006). As the complexity of the Asian Factory increased and the speed of the production process had become a key competitive factor, the time spent and the costs of tariff negotiations and agreements for certain products or companies could have emerged in the failure of the business relations within the continent. Therefore, Asian countries have considered appropriate to shift their attention from special agreements to tariff reductions without discrimination under the Most Favoured Nation Clause (Wei, 2011). The results were really impressive. Most developing countries in East Asia have reduced tariffs unilaterally in the past 20 years, especially in the 1990s.

China's accession to the World Trade Organization has represented a key event that may indicate the start of a regional or multilateral liberalization process (Lee, 2011). The agreement signed by China with ASEAN induced a domino effect on Japan and Korea, which, following the example of Great Britain in 1960, began a series of bilateral agreements concluded within the continent. In the last few years trading powers were included from outside East Asia, like Australia, New Zealand, India and the U.S. But the nature of bilateral trade agreements within Asia creates a web of trade flows charged differently from one arrangement to another.

CONCLUSIONS

The shaping of the regional trading blocs in the world along with the implementation of an array of bilateral agreements between different countries provides a hub of global connections and spokes. Economic and financial crisis have shaken the foundation of these tectonic trade plates and challenged the uncertainty of the hegemonic position of the United States and the European Union. The economic downturn has raised the possibility that protectionist measures would test the vulnerability of the nations affected by the crisis phenomenon. Such a scenario is likely to stop the progress made towards trade liberalization in several areas of the globe. The economic growth associated with a growing degree of openness to trade in goods and services will slow as the „spokes" connections to the „hubs" will break. The domino effect will produce reversed results accordingly to the ones liberalization induced.

The main result of this study was the capture of the development of international trade through interstate connections. Unilateral liberalization, regionalization or multilateralization of trade relations occurred in complementary relationships over the past two centuries. Since the ratification of the General Agreement on Tariffs and Trade and the foundation of the World Trade Organization (WTO) one tried to implement multilateral liberalization solutions, covering a broad range of countries within an area characterized by relationships based on reciprocity.

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