

GLOBALIZATION AND THE NEW WAVE OF INTERNATIONAL TRADE BLOCKS

Rituranjan*

ABSTRACT

Under a regime of Globalization, the whole world appears to be turning into a close-knit village i.e. a 'Global Village' wherein the realization of their increasing interdependence has induced the various nation states to co-operate and integrate with each other in virtually all spheres of human endeavor. Consequently, the International Order emerging in the 21st Century is the one based on Regional Integration Agreements (RIAs) which in the economic arena assume the form of International Trade Blocks and Agreements. In what ways does the wave of new International Trade Blocks and RIAs represent an improvement over their predecessors? How has the process of Globalization affected the perceptions of nation-states as regards Regional Economic Integration? What considerations have led to the formation of the new type of International Trade Blocks and what is their likely impact on International Economic Order especially from the perspective of the developing countries of the Third-World? These are some of the crucial issues addressed in this article.

Introduction

Against the backdrop of an extensive use of rapidly advancing information technology and state-of-the-art communication networks at the global level, the world is getting increasingly interdependent day-by-day. This interdependence among nation-states is not only confined to the economic sphere but is all-pervasive in as much as it covers the social, cultural and emotional aspects of life.

Consequently, different economies and societies of the world are rapidly coming closer so much so that the whole world appears to be turning into a close-knit village i.e. a 'Global Village' so to say. This phenomenon or the process of the gradual integration of different parts of

the world, be it different economies, societies or cultures, which is generally referred to as Globalization, gained momentum in the 1990s.

Evidently, under a regime of Globalization, the international relations among various nations too have undergone a perceptible change in recent years. More specifically the realization of their increasing interdependence at all levels in the contemporary regime has induced the various nation states to co-operate and integrate with each other in virtually all spheres of human endeavor. As a result, the International Order emerging in the 21st Century is the one based on Regional Integration Agreements (RIAs) which in the economic arena assume the form

* Dr. Rituranjan is Reader in the Department of Economics at Shri Ram College of Commerce, University of Delhi, Delhi-110 007

of International Trade Blocks and Agreements.

There is no denying the fact that even in 1960s and 1970s, some sort of Regional Economic Integration used to exist at the global level in the form of regional trading agreements between different countries. But it must be realized that the new wave of International Trade Blocks which have essentially come into being against the backdrop of Globalization in the 1990s, are markedly different in their nature from their counterparts in 1960s and 1970s.

In what ways does the wave of new trade blocks and RIAs represent an improvement over their predecessors? How has the process of Globalization affected the perceptions of nation-states as regards Regional Economic Integration? What considerations have led to the formation of the new type of International Trade Blocks and what is their likely impact on International Economic Order especially from the perspective of the developing countries of the Third-World? These are some of the crucial issues addressed in this article. At the very outset, it must be conceded that there are no ready-made or straightforward answers to such critical questions as a lot depends on the specific case and the associated environmental setting under consideration. Some broad generalizations can, nevertheless, be made after a thorough appraisal of the functioning of some of the new International Trade Blocks and RIAs.

What is needed for such a comprehensive analysis is an altogether new approach towards the study of regional economic integration that goes well beyond the simplistic static framework of *trade creation* and *trade diversion* as laid down by **Jacob Viner** way back in the early nineteen fifties.

This is the precise spirit in which the present article is written and the motivation for it has been provided by the latest research work that

is being undertaken in the World Bank which has also led to the development of the modern approach to studying regional economic integration agreements at the global level.

We begin by taking a closer look at the concept and meaning of Globalization.

Globalization? A Myth Or Reality?

Though the term 'Globalization' is quite frequently used nowadays to signify an increased interaction between different economies, societies and cultures facilitated by modern information technology at the global level, yet there is more to globalization than meets the eye.

For globalization is a multifarious concept and accordingly different people prefer to interpret it differently. To some, globalization is nothing but the replacement of local restaurants by international food-chains such as McDonald's, Burger King and Pizza Hut around the globe as has been pointed out by **Marrewijk (2002)**.

To others, globalization manifests itself when viewers of Satellite Television around the world are touched by watching on BBC the tragic plight of famine victims in the African States of Ethiopia and Somalia. Still others associate globalization with the erosion of national borders and national sovereignty.

Likewise, environmentalists visualize globalization in terms of events such as the burning of forests in Indonesia bringing climatic changes in the whole South East Asia or the news of a hole in Earth's ozone layer over Antarctica coming as a warning of global disaster for the chemical industries world over.

The increasing use of INTERNET across the globe and rise in international communications through fax machines and mobile phones could also be taken to be a feature of globalization as witnessed in recent years. Similarly, a wider

cultural exchange via overseas sales and distribution of Bollywood and Hollywood movies too connotes a certain measure of globalization. In addition, a surge in international travel and tourism in recent years is also conveying a rising pace of globalization.

In an economic sense, however, we can identify globalization with the gradual opening up of different economies and their rapid integration with the rest of the world owing to the adoption of more liberal trade and economic policies by different countries in recent years. Consequently, there has been a *significant rise in the international trade in goods and services, a freer flow of labor and capital across national boundaries, an increasing operation of Multi-National Corporations and a rapid development of global financial markets*, all of which could be reasonably considered to be a sufficient evidence of globalization especially since the early 1990s.

It is actually on account of such a globalization that when Japanese manufacturers lower the prices of various electronic gadgets, the prices of VCRs, TVs and microwave ovens fall in America.

In a similar manner, when American consumers started purchasing less expensive East Asian textile products, the textile manufacturers in the USA were forced to lay off workers. Then in order to strengthen their position in the textile market, American entrepreneurs sought to invest in high technology West German textile machines. These machines were purchased with the money that was deposited by Saudi prices in Italian banks. Another manifestation of globalization in recent years is that an aircraft flew Japanese businessmen to Indonesia to secure oil for Japanese industries. French financiers used the same aircraft to track their investments in stock markets in London, New York, Tokyo and Hong Kong.

There are in fact numerous such instances that signify the process of globalization being underway in recent years. Yet some academicians treat globalization to be more of a myth than reality. The rationale behind such skepticism is an extremely narrow approach pursued by these critics, whereby, 'globalization' is looked at as elimination of nation-states and national frontiers. Since globalization as observed in the present-day world has not led to a dissolution of national boundaries, the skeptics prefer to call it 'internationalization' rather than 'globalization'.

On closer examination, however, we do not find much logic in such a rigid posture adopted by the critics and thus can reasonably infer that far from being a myth, *Globalization is more of a practical reality in the present-day world* that manifests itself in numerous ways ranging from freer trade and capital flows at the international level to greater cultural exchange at the global level and in line with **Legrain (2002)**, we can consider globalization to be a chance for mutual enrichment rather than a route to global impoverishment.

The New Wave of International Trade Blocks

According to the latest 'World Trade Report' of the World Trade Organization (2003), the global trading system has seen a sharp increase in regional trade agreements (RTAs) over the past decade or so.

What this essentially means is that during the 1990s, when the process of globalization was gaining momentum, the world witnessed an unprecedented growth of International Trade Blocks and Regional Integration Agreements (RIAs). This was quite natural as the growing realization of their interdependence on the part of various nation-states could be reasonably expected to induce them to come closer and

co-operate with each other.

The point to be noted, however, is that the new wave of regional economic integration at the international level *i.e.* the International Trade Blocks that came into being against the backdrop of globalization in the 1990s were quite different in their underlying nature from the RIAs that used to get formed earlier say in the 1960s and 1970s. In this connection, a study conducted by the World Bank Group (2001) entitled 'Trade Blocs' has also observed that the last 10 years have witnessed qualitative as well as quantitative changes in regional integration schemes.

To be specific, the thrust of the wave of new international trading agreements was on 'Deep Integration' rather than the simple reduction in tariffs and quotas alone. What this essentially implies is that the new trade blocks of the 1990s went much beyond what in the terminology of Lawrence (1996) could be regarded as 'Shallow Integration' *i.e.* the mere removal of trade barriers or trade liberalization, as their focus had shifted to a deeper harmonization of the domestic policies of the member countries.

This deeper harmonization could itself be achieved by setting up a Common Market, an Economic Union or even a Monetary Union depending upon the degree of harmonization that is sought to be achieved. Accordingly, in the strict sense of the term, the International Trade Blocks truly became 'Regional Integration Agreements' whose members not only tried to ensure a free flow of commodities, labor and capital among each other but side-by-side also aimed at a unification of their monetary, fiscal and general economic policies and even went to the extent of establishing a common currency for themselves.

The classic example of such an 'International Trade Block' or to be precise such a 'Regional

Integration Agreement' at the global level is provided by the European Union (EU) which came into effect in 1993. It is worth noting that the EU is not only characterized by a free movement of goods, services and factors of production across all its 25 member nations from Europe but has also introduced the single European Currency called 'Euro' that was put into circulation in 2002 in 12 of its members *viz.* Germany, France, Italy, Greece, Spain, Portugal, Austria, Belgium, Finland, Netherlands, Ireland and Luxembourg. The only EU members that had not adopted Euro are the United Kingdom, Sweden and Denmark.

Once these remaining member countries too accept Euro as their Currency, the EU which is presently an 'Economic Union' would technically become a 'Monetary Union' which shows the highest level of Regional Economic Integration.

Such a high degree of regional integration introduced by the EU in the 1990s has set a new trend in the contemporary regime of globalization wherein with a view to achieving an effective regional integration; even other International Trade Blocks across the globe are getting inspired by the philosophy of 'Deep Integration'.

Apart from the incorporation of deep integration, another significant improvement observed in the wave of new International Trade Blocks over their predecessors of 1960s and 1970s is that in a sense, "Closed Regionalism" has given way to "Open Regionalism".

For, prior to globalization, regional economic integration especially among developing countries was perceived as a means of putting a check on the international trade and commerce of member nations. Such a regulation and control over the global trade of members was in turn achieved by setting high external trade barriers for the rest of the

world *i.e.* the non-member countries. This for instance was the characteristic feature of CACM (Central American Common Market), CARICOM (Caribbean Community and Common Market) and ECOWAS (Economic Community of West African States) established in 1960, 1973 and 1975 respectively, all of which were based on the model of import-substituting development thereby adhering to the philosophy of "Closed Regionalism" so to say.

With globalization, however, the underlying perceptions underwent a sea change in the 1990s as Regional Economic Integration now came to be regarded as a vehicle of promoting rather than blocking world trade. Accordingly, the new International Trade Blocks formed in the 1990s as also the old agreements resurrected against the backdrop of globalization are more outward-looking and committed to boosting international trade and commerce. For instance, the Southern Common Market MERCOSUR (Mercado Common del Sur) and COMESA (Common Market for Eastern and Southern Africa) formed in 1991 and 1993 respectively as well as the ANDEAN Pact resurrected in 1991 are relatively more outward-looking in line with the ongoing trend of globalization. This in a way reflects a move from "Closed Regionalism" to "Open Regionalism" as the members of new International Trade Blocks are more open to the rest of the world *vis-à-vis* their counterparts in the 1960s and 1970s.

Still another significant development in international relations against the backdrop of globalization as observed in the new wave of regionalism is the advent of International Trade Blocks encompassing both Rich and Poor Countries.

This new trend was established in 1994 with the coming into being of the NAFTA (North

American Free Trade Agreement) which was a *radical experiment* in as much as its member countries had radically different levels of development. More specifically, NAFTA has 3 member nations of which the United States of America (USA) and Canada are industrially advanced and high-income countries, whereas, Mexico is a developing and hence relatively poor economy. Yet the USA, Canada and Mexico are at equal footing under 'NAFTA' whose success story has inspired the formation of such heterogeneous trade blocks all across the globe in recent years.

On similar lines, even the APEC (Asia Pacific Economic Cooperation), set up in 1989, is contributing towards strengthening of the links between high-income and developing countries. Likewise, by entering into bilateral agreements with the relatively less developed Mediterranean countries of Tunisia and Morocco in 1995 and 1996 respectively, even the European Union (EU) has reinforced the current trend of closer regional economic integration between the rich and the poor. This trend can be reasonably expected to continue and even accelerate in the coming future, thereby, bringing a new era of International Trade Blocks wherein the high-income industrial countries on the one hand and poor developing countries on the other will be equal partners.

Formation of Trade Blocks in the Contemporary Regime

Though on the face of it, one tends to gather the impression that the International Trade Blocks and Regional Integration Agreements get formed due to economic reasons, yet on closer examination we find that the regional economic integration especially in the contemporary regime is governed more by political rather than economic considerations.

There is no denying the fact that International Trade Blocks and regional integration at the

global level does entail some economic gains to the member nations but politics appears to be the prime mover or driving force behind the establishment of such blocks in the present-day world.

At times, economic aspects get so much intermixed with political ones that it becomes exceedingly difficult to separate the two particularly when economics take the shape of rhetoric and political propaganda. For instance, to suit vested political interests, some of the evident economic benefits of these trade blocks are usually emphasized upon and reiterated deliberately to the total neglect of their hidden economic costs in terms of a possible unfair distribution of benefits among the member countries.

Thus it is not easy to answer whether the formation of trade blocks in the contemporary regime reflects Good Economics or Good Politics as both the things need not necessarily go hand in hand. Nevertheless, the experience with a large number of contemporary International Trade Blocks bears testimony to the fact that the impetus for regional economic integration essentially generated on account of political considerations and its economic consequences were practically considered as just the side effects of the underlying political process. Let us therefore, have a closer look at the Politics behind the formation of trade blocks and regional integration agreements in recent years.

In this context, it is worth noting that the first and foremost political consideration that dictates different countries to co-operate and integrate with each other by forming a trade block is one of 'Security'. This security could either be with reference to the member countries of the proposed block or instead with respect to the rest of the world *i.e.* non-member nations.

For, when different countries join hands to form a trade block, it *per se* reduces the probability of an armed conflict between them in the future since each member knows for sure that any such dispute will deprive it from the potential economic gains from the block. That is to say, trade blocks are an effective means of preventing the possibility of a war among member nations as after the formation of such a block, any type of military conflict between members becomes too costly a proposition for all of them.

Evidently, when different countries join together in this manner, they are also in a better and stronger position vis-à-vis the other non-member countries as unity gives rise to strength. Thus, by entering into a regional trading agreement, the member countries are typically in a position to enhance their security with reference to the rest of the world.

In fact, apart from security, the collective strength also yields a good deal of 'Bargaining Power' to the member nations of an international trade block or regional integration agreement. For, when different countries collectively negotiate with the rest of the world, they are bound to get noticed in bargaining rounds and can be reasonably expected to get a better deal in comparison to what any single member could individually achieve.

In addition to providing security and bargaining strength, the formation of an International Trade Block is likely to build trust among member countries that could go a long way in facilitating other kinds of cross-border co-operation. For instance, once the members of a trade block develop an understanding through regular political contact, they can go about collectively building infrastructural network such as highways, railways, telecommunications etc.

It must, however, be pointed out that all such possible benefits of international trade blocks

and regional integration agreements such as enhanced security, rise in bargaining power and confidence building among member countries are likely to fructify if and only if they are able to arrive at a consensus on all the relevant issues and there is fair distribution of its benefits across all the members. Evidently, in case these crucial conditions are not fulfilled under any trade block or regional integration agreement, there is a threat to the very existence of such an agreement as sooner or later the concerned trade block will disintegrate *i.e.* fall apart.

The Economic Impact of the Wave of New Trade Blocks

Even if it is recognized that the essential motivation for the establishment of International Trade Blocks especially in the contemporary regime comes from political reasons, the Economic Impact of such blocks can neither be ignored nor taken for granted.

For, it is quite conceivable that the visibly beneficial economic effects of a trade block may not materialize at all or may not fructify to the extent contemplated. Likewise, it is also quite possible that the gains accruing from such a regional economic integration at the global level may be overshadowed by the economic costs emanating from the same. This is particularly true in those cases, wherein, an international trade block distributes unequal economic gains across its member countries so that some of them especially the less developed and developing ones turn out to be net losers rather than net gainers from the concerned regional integration agreement.

As far as the apparent economic benefits of an international trade block are concerned, we notice that any such regional integration agreement yields the dual and rare benefit of *increased competition* coupled with *scale economies*.

The combination is rare since in any given market situation, a 'trade-off' is likely to exist between enhanced competition and economies of scale respectively. For, in order to derive scale economies, the scale of operation in the productive process by definition has to be very large which in turn can only be achieved by keeping a lesser number of firms in the market, thereby, reducing competition.

But when it comes to the formation of a regional integration agreement like an international trade block, it virtually amounts to an enlargement of the market in the sense that the separate markets of all the individual member countries in effect join together to form a Larger Single Market. Under this situation, the total market share as governed by the overall demand for a product in the block is distributed among the most efficient firms, whereas, the relatively inefficient firms are forced to close down, no matter which member country they belong to.

Thus, each of the efficient firms remaining in the market is now in a position to derive the benefits of *economies of scale* as catering to a larger market demand, it can operate at a relatively higher scale of production. Yet, side-by-side the competition in the market has also increased since owing to a larger demand coming from all the members of the trade block, the number of firms still existing in the market is higher than what was the case in any of the individual market of a member country.

In this way, by combining the market demand of individual member countries, an international trade block fosters *economic efficiency* and offers the unique combination of the economic benefits of enhanced competition and economies of scale.

It must, however, be realized that the beneficial impact of all these effects could be more than offset in case an international trade block leads to an unfair distribution of economic benefits

across its member nations. This problem may not be very acute in the case of trade blocks whose member countries have similar economic status and almost the same level of economic development.

But when we look at the emerging pattern or new wave of international trade blocks characterized by a large diversity of economic status and level of development across their member countries, we find that there is always a danger of such regional integration agreements benefiting the rich at the cost of poor. Evidently, such an unfair distribution of economic benefits is likely to create tension among the member countries which could eventually lead to a breakdown of the concerned International Trade Block itself.

Thus the need of the hour is to employ suitable safeguards for the relatively poorer and less developed countries of the Third-World beforehand *i.e.* prior to entering into such Rich-Poor regional integration agreements so as to ensure that there will be fairer distribution of the economic benefits of such agreements across all their members. This prescription assumes special significance in view of the recent eastward expansion of European Union 'EU' with effect from 1st May 2004 incorporating 10 transition economies of Eastern Europe *viz.* Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia and the expected southward expansion of NAFTA in the form of the proposed 'FTAA' *i.e.* Free Trade Area of the Americas covering in its domain 31 more countries from the Caribbean and Latin America that are essentially poor and developing in nature.

Conclusion

The process of Globalization has led to a new wave of regional economic integration in recent years, wherein, 'deep integration' is being combined with 'open regionalism' and an altogether new international economic order based on the international trade blocks between the rich and poor countries is emerging. The need for the formation of such blocks and regional integration agreements has largely been dictated by the political considerations of security, bargaining power and collective strength. Yet such international trade blocks yield visible economic benefits in terms of offering the rare advantage of enhanced competition, efficiency and economies of large scale production.

One should not, however, be overwhelmed by these apparent benefits as there is always a danger especially with reference to the new wave of International Trade Blocks between the Rich and Poor Countries that they might be instrumental in perpetuating rather than preventing global disparities.

REFERENCES

- Lawrence, Robert Z. (1996), *Regionalism, Multilateralism and Deeper Integration*, Washington D.C.: The Brookings Institution
- Legrain, Philippe (2002), *Open World: The Truth about Globalisation*, Abacus.
- UK. Marrewijk, Charles Van (2002), *International Trade and the World Economy*, Oxford University press
- World Bank Group (2001), *A study entitled 'Trade Blocs'*
- World Trade Organisation (2003), *World Trade Report 2003*