Agricultural and Resource Economics
UPDATE
GIANNINI FOUNDATION OF AGRICULTURAL ECONOMICS • UNIVERSITY OF CALIFORNIA
V. 12 no. 4 • Mar/Apr 2009

The Role of Regional Trade Agreements in Trade Liberalization

Renée A. Vassilos and Alex F. McCalla

Multilateral trade liberalization is usually the first casualty of a recession. There has been a proliferation of Regional/Bilateral Trade Agreements (RTA's) in recent years. Are these a substitute for multilateral liberalization? This paper explores the recent evolution of RTA's and presents a case study of the U.S.–Malaysia Trade Agreement as it relates to fruit, nut, and vegetable exports. It argues that while there are benefits to the United States, multilateral liberalization still seems to be a better option.

Also in this issue

History shows that a recession brings with it a national shift toward protectionist policies. In past recessions, such a shift has proven troublesome. The Smoot-Hawley Tariff Act of the 1930s raised U.S. tariffs on over 20,000 imported goods to record levels and had a disastrous effect for the United States and its trading partners. In fact, it was the significant negative impact of the protectionist trade policies of the United States and other nations which stimulated the creation of the General Agreement on Tariffs and Trade (GATT) in 1948, the predecessor organization to the World Trade Organization (WTO).

Trade liberalization has been shown to produce benefits to competitive producers. In the post WW II period trade has expanded much more rapidly than GDP, leading to growing prosperity. Agricultural trade, however, remains more protected. Most analyses done regarding agricultural trade liberalization suggest competitive producers, as are most U.S. producers, gain from having freer access to international markets.

There are three means by which a country can liberalize and expand international trade: multilateral, regional, and bilateral trade agreements. Multilateral trade agreements are the most efficient way to advance a free trade policy and thus promote open markets. Unfortunately, despite having been in discussion since 2001, the latest round of multilateral trade talks at the WTO, the Doha Round, has stalled. Disagreements over domestic agricultural subsidies blocked an agreement in July 2006. In 2007, no agreement was reached due to conflicts regarding opening agricultural and industrial markets and farm subsidies of developed nations. A disagreement over a Special Safeguard Mechanism requested by certain developing countries blocked an agreement in July 2008. While multilateral trade agreements may be considered a better tool for reducing discriminatory trade practices and encouraging governance reform among member countries, current talks remain stalled.

However, in the interest of producers, it is important to continue talks. Of particular importance to the globally significant agricultural sector, is that such negotiations are critical to open and expanded trade relations. While multilateral negotiations are currently stalled, the opportunity exists for continued trade development at the bilateral and regional level. While not a substitute for multilateral negotiations, development can continue through regional trade agreements (RTAs) with fewer complications in the negotiations. Virtually all members of the WTO use regional trade agreements as a trade policy tool. Such agreements allow countries to open their markets to one another through the granting of preferential access.

These regional agreements are used as a policy tool in addition to

Table 1. U.S. Free Trade Agreements: Implemented or Pending Implementation	
Australia	January 2005
Bahrain	August 2006
Canada	January 1994 (NAFTA)
Chile	January 2004
Colombia	Pending Congressional Approval
Costa Rica	Pending Implementation (CAFTA-DR)
Dominican Republic	March 2007 (CAFTA-DR)
El Salvador	March 2006 (CAFTA-DR)
Guatemala	July 2006 (CAFTA-DR)
Honduras	April 2006 (CAFTA-DR)
Israel	August 1985
Jordan	December 2001
Mexico	January 1994 (NAFTA)
Morocco	January 2006
Nicaragua	April 2006 (CAFTA-DR)
Oman	September 2006
Panama	Pending Congressional Approval
Peru	Pending Implementation
Singapore	January 2006
Republic of Korea	Pending Congressional Approval
U.S. Free Trade Agreements: Under Negotiation	
Under the South African Customs Union (SACU): Botswana, Lesotho, Namibia, South Africa, and Swaziland	
Malaysia	
Thailand	
United Arab Emirates	

multilateral agreements because of their speed, the fact that they allow liberalization of specified markets at a faster pace than multilateral agreements, and their flexibility. Furthermore, RTAs are not as cumbersome, allowing interested parties to negotiate trade policy scope and choice of partner. The content of the negotiated trade policy often includes topics which present great difficulty in the multilateral arena, such as agriculture, and also includes topics not in the multilateral negotiations at all, such as government procurement, competition policy, and investment. The influence of special interest groups is, however, more dominant in RTAs versus multilateral negotiations, resulting in sensitive trade areas being left out of RTAs completely. The major driver for the use of RTAs as a trade policy tool is the relative speed and flexibility possible in their negotiation.

The appeal of RTAs is evident in their proliferation over the last 13 years. The WTO (established 1995) has been notified of close to 300 RTAs, as compared to the GATT's 47-year existence when notifications only numbered 124. Currently, there have been over 400 regional trade agreement notifications sent to the WTO and 230 in force.

The United States has 14 trade agreements (TAs) in place, with four additional agreements under negotiation (Table 1). In order to maintain and increase its position in global trade, it is desirable for the United States to continue to pursue TAs. Implementation of a TA positively benefits producers—gaining preferential access in international markets results in more competitive exports.

Table 2: U.S. Fruit and Vegetable Exports to Malaysia, 2006	
Fruit: fresh & prepared	$86,221,000
Vegetable: fresh & prepared	$6,101,000
Nuts	$7,966,000
Total	$100,288,000
Source: USDA, Foreign Agricultural Service	

Case Study

A case study was conducted in November of 2007 that analyzed the U.S.–Malaysia TA, under negotiation since March 2006, and the impact it would have on the U.S. fruit, nut, and vegetable sector. Malaysia is a strategically important trading partner for the United States, as its tenth largest trading partner in the world and the largest in Southeast Asia. A TA with Malaysia would allow greater access to the Southeast Asia market, with annual trade valued at $3 trillion.

U.S. agricultural exports to Malaysia totaled more than $550 million in 2007, with $100.3 million from fruit, nut, and vegetable exports (Table 2). The removal of tariffs and other restrictions on agricultural exports would result in gains for U.S. agriculture producers.

The study focused on grapes and apples—the largest (by value) fruit commodities exported to Malaysia—and raisins, the largest processed fruit product (by value) exported (Table 3). The three commodities had a combined export value of $63 million in 2006. These three commodities were analyzed, with the results extrapolated to determine the potential gains from a TA for U.S. fruit, nut, and vegetable exporters to Malaysia.

Potential gains for exporters of these commodities were estimated through

Table 3: U.S. Grape, Apple, and Raisin Exports to Malaysia, 2006	
Grapes, fresh	$40,318,000
Apples, fresh	$18,969,000
Raisins	$3,946,000
Total	$63,233,000
Source: USDA, Foreign Agricultural Service	

Table 4: Calculated Elasticities of Demand for U.S. Fruit Exports in Malaysia			
Commodity	Price Elasticity of Demand	Standard Error	Observations
Grapes	-.977*	.382	107
Apples	-.946*	.375	120
Raisins	-.593*	.375	114

**Significant at the .01 level*
Source: Authors' Calculations

the calculation of Malaysian demand for the commodities. Using the calculated demand in the Malaysian market, the price elasticities of demand for these commodities were estimated. The elasticities were then used to calculate the prospective monetary gains for U.S. exporters based on 2006 export levels.

U.S. exporters face increasing competition in the Malaysian market for their products. Through a TA, U.S. exporters would gain from the removal of the 5% tariff they currently face in the Malaysian market.

Competition for U.S. grapes comes mainly from Australia, whose annual export volume to Malaysia is nearly equal to that of the United States. Though Australia is in the Southern Hemisphere and has opposite growing seasons to the United States, it is aided by recent developments in production which have created longer growing seasons and increased storage capabilities. These developments minimize the impact of the different growing seasons. China is the major competitor in the apple market, with greater annual exports to Malaysia than the United States. However, U.S. apples maintain market share through their distinction as a higher quality product. Iran is the major competitor for raisins. The United States currently maintains the larger market share for raisins, although Iran is increasing its exports to Malaysia annually.

A U.S.–Malaysia TA is not only a strategic move to help increase U.S. market share in Southeast Asia, but also a potential defensive move, since both Australia and China are currently negotiating TAs with Malaysia. Australia is in direct bilateral negotiations, while China is negotiating with Malaysia through the Association of South East Asian Nations (ASEAN) as part of a regional trade agreement initiative.

In the case study, Malaysian consumer demand for grapes, apples, and raisins was estimated using a double-log model. The elasticities of demand obtained from the demand estimates ranged from -.593 to -.977 (near unitary elastic demand) (Table 4). If the negotiated agreement removed the 5% tariff on the commodities and this was translated into a 5% price decrease on the market for Malaysian purchasers—U.S. apple sales would increase 4.7%, raisin sales would increase 3%, and table grape sales would increase 4.9%. At the 2006 value for export commodities, this would translate into an increased export value of nearly $3.62 million for the three commodities analyzed. Total fruit, nut, and vegetable exports could increase by roughly $4.1 million were tariffs removed. This calculation is based on an average of the elasticities for fresh grapes and apples applied to the fresh portion of exports and the elasticity for raisins applied to the processed portion of exports (Table 5).

Facing tough competition, any advantage in a market is important. In this specific case of grapes and apples, the TA may also prove be a defensive move to hold current market share if Australia and China also sign TAs with Malaysia.

Implications

This study provides a narrow view of world trade: the U.S. fruit, nut, and vegetable exports to a relatively small export market, Malaysia. However, the results may be extrapolated to provide a wider look into the current state of international trade. The U.S. agricultural industry is facing, in certain sectors, increasing competition

Table 5: Fruit, Nut, and Vegetable Exports to Malaysia, Fresh versus Processed	
Fresh: Fruits, Nuts, & Veg	$88,204,000
Processed: Fruits & Veg	$12,084,000
Total Exports	$100,288,000

from both the developed and developing world. This competition is no longer simply limited to increased exports, but also includes TAs being negotiated and implemented between U.S. trade partners and third country competitor nations. The continual development of trade agreements is therefore critical for U.S. export interests. The potential gains for the agriculture sector can be significant with trade agreements opening markets to expanded U.S. production.

With every nation grappling with the impacts of the global recession, nations may find themselves pushing aside international trade agreements in favor of what are believed by some to be national interests. A move toward protectionism is not, however, in the interest of efficient producers in the United States. The U.S. economy has benefitted from trade expansion driven by the liberalization of trade in manufactured products. Agriculture has lagged behind and therefore has experienced less benefit. While the benefits of bilateral trade liberalization are likely to be less than for multilateral liberalization, they still are to be preferred to a reversion to increased protection. This is particularly true for U.S. producers who want to expand production beyond servicing domestic markets.

Renée A. Vassilos earned her M.S. degree in the Department of Agricultural and Resource Economics at UC Davis in 2007. She is a market analyst with John Deere (China) Investment Company in Beijing, China. Renée can be contacted by e-mail at ReneeVassilos@gmail.com. Alex F. McCalla is an emeritus professor of agricultural economics at UC Davis who can be contacted by e-mail at alex@primal.ucdavis.edu.