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TRADE BLOCS AND THEIR IMPLICATIONS FOR NATIONAL ECONOMIES

Dr.Haydar AKSOY[1], Dr.A.Ercan GEGEZ[2] & Müge ARSLAN[2]

[1] M.Ü. İ.İ.B.F. İşletme Bölümü, Doçent

[2] M.Ü. İ.İ.B.F. İşletme Bölümü, Araştırma Görevlisi

ÖZET: ***Son yıllarda giderek önem kazanmaya başlayan ticaret blokları, oluşumlarıyla birlikte çok çeşitli baskı grupları açısından etkili olmaktadır. Ticaret blokları sadece üyelerini değil aynı zamanda bu üye ülkelerin ticaret ortaklarını da etkileyebilmektedir. Bu çalışmada ticaret bloklarının oluşumunda rol oynayan faktörlerle ticaret bloklarının milli ekonomiler üzerindeki olumlu ve olumsuz etkileri incelenecektir.***

I. INTRODUCTION

Technological advances in transportation, communications and production have enabled many firms to exploit worldwide market opportunities. Instead of searching for individual markets around the world. firms try to view the world as one big market and sell their products and/or services anywhere they can. In the eighties, hasty developments experienced in the international business arena caused a process of transition and novelty. These changes in economic dynamics have led the way to both new opportunities and threats. One of the salient developments of our times is the emergence of trading blocs. Trade blocs and their changing of the competitive environment has become the password for nations that seek growth in trade opportunities and economic prosperity. The chief aim of this paper is to examine the case of trade blocs and then shed light on their probable impacts on national economies.

II. EMERGENCE OF TRADING BLOCS

The region rather than the nation-state has gradually become the focal point of international attention. Indeed, a wide range of integrated regional groupings have been established all over the world[1]. Today, as we approach the turn of the century, it can closely be seen that along with the trend toward regionalism issues such as trade blocs. strategic alliances. international product and technology sharing have turned out to be a necessity rather than a preference. Morrison. Ricks and Roth[2] point out that in 1989, 21 of the 22 richest industrialized nations in the world (the exception being Japan) belonged to a regional trading group. Considering opportunities and/or threats, economically no matter how weak or powerful, nations have been hastily moving into regional economic integrations among themselves. For instance, Wu and Longley[3] point out that over the last four decades, Japan and a number of NICs such as Taiwan, South Korea, Hong Kong and the Singapore have adopted an export-oriented economic policy for their economic growth.The U.S. expected that a free trade zone in North America would rationalize the production process in the country, thereby enhancing industrial productivity and achieving economies of scale. As a result, the U.S. would be in a better position to compete with these emerging economic powers in the Asia-Pacific region. Actually, in order to benefit from the regional integration taking place in the Asia-Pacific region, instead of competing with it, the U.S. has always been eager to be included in APEC (Asia-Pacific Economic Community).

After the devastating experience of World War II, there emerged a growing desire for greater European co-operation, especially in economic and social policies[4]. This intention was also supported by the expectations of a peaceful Europe in the following years.

Not only the Second World War, but also the Soviet Threat has forced Western Europe to bind together. Nations that had been fighting for centuries (particularly France and Germany- who had fought four long hard wars against each other in the previous 150 years) now not only had the incentive and impetus to work together but now this binding together has become a sheer necessity of a life or death crisis. The experiences gained from working together in a defence-related posture. later proved invaluable to assist in co-operation in the economic sphere[5]. The heavy economic burden and agony of war forced people to focus on the idea of a peaceful and economically sound Europe. One of the other reasons why nations are trying to take place in economic integrations is the growth of the global economy. In addition, cut-throat competition among not only the firms but also nations has eventually forced nations to become involved with trade blocs. Therefore, the emergence of trade blocs requires the formulation of new trade policies at both the national and company level. Most of the time, nations have to compete with blocs rather than single national economies. Now it is a well-known fact that in order to be, and more than this, in order to remain competitive, every nation should be supported by a trade bloc.

Finally, according to Aho and Ostry[6] the reason why trading blocs have emerged in recent years is a weakened and inadequate GATT which caused nations to find other solutions such as forming trade blocs.

III. MOTIVES FOR REGIONAL ECONOMIC GROUPINGS

In the early postwar period, economic integration among developing countries was considered primarily as a way of extending the policy of import substitution on a regional scale[7]. Considering the import substitution policies, it is clear to say that such a policy's chance of success is primarily dependent on a country's domestic market, industrial structure and manufacturing abilities. It is quite certain that many newly developing countries do not have a suitable industrial structure and a sophisticated demand which will ensure expected economic development. By taking into account the shortcomings of import substitution policies, we can say that these kinds of obsolete policies cannot be motives for economic integrations anymore. Nowadays the formation of a trading bloc can also be based on some other motives.

According to Jain[8] nations can get together in terms of economic, political, geographic and social factors (see figure 1). It should be noted that geographic, social and to some extent, even political rationales for constituting an economic integration are not as important as the economic rationale. Although geographic proximity results in important border trade, it does not always result in an economic integration since the economic systems, whether be it a market economy or a centrally planned economy, might totally be different among the nations within a particular region. Under these circumstances, forming a trade bloc on the basis of geographic factors would be useless. It cannot be denied that member nations of many trade blocs today seem to be geographically proximate but it also always holds true that they are dictated by economic factors as well.

Nations may form a trading bloc on the basis of social factors as well. As a further step, these nations may want to initiate economic relations in addition to social relations. Conventional wisdom suggests that social factors alone are not a good reason to initiate a trading bloc.

Another integration rationale is political rationale. Due to political or ideological similarities, nations may constitute economic groupings. But it certainly is doubtful whether these groupings are economically sound or not. The COMECON grouping which protected iron curtain nations for many years is a good example of such an integration. Lindert[9] points out that between 1949 and 1989, socialist countries discriminated strongly against trade with capitalist economies, in favor of trade among themselves. This forms a good example of a trade bloc which is doomed to die since it is based on politically sound but economically weak motives. Needless to say, political thoughts and ideologies are not agreeable motives in forming economic integrations.

As noted above, economic motives are sound bases in forming a trade bloc. The former U.S. - Canada Free Trade Agreement, which now includes Mexico and is called NAFTA, was a good example of this kind of agreement. Each year the two countries exchange more goods, services and capital than any two nations in the world. U.S. exports to Canada exceed exports to the entire European Community (EC) and are more than double that to Japan. Indeed, U.S. trade with the province of Ontario alone exceeds U.S. trade with Japan[10]. The virtual closure of the EC, Japan and developing countries to the entry of Canadian manufactured exports as a result of restrictive government purchasing practices, technical standards, import quotas and 'administrative guidance' has oriented domestic producers towards the American market[11].

In the light of this consideration, any kind of motive not supported by economic rationale is not a good starting point in forming a regional economic integration. Going a step further Herbig and Day[5] point out that the key for a successful trading bloc can be obtained by nations which have similar per capita income and similar trading regimes within the same region. This is all very well but this logic can still lack some other considerations. Therefore, it would be better to state that regional groupings with economic infrastructure would reach better results when they are supported by social, political, geographical or any combination of these motives. Historically, successful economic integrations are formed on the basis of economic motives and are supported by other motives.

IV. PROBABLE EFFECTS OF TRADING BLOCS

It is clear that trade blocs offer both advantages and disadvantages to its members. Though at first it may appear that being a member of a trading bloc is highly advantageous, there are still some drawbacks to probable members. Considering the everlasting negotiations among the members and/or probable members, deciding on whether to become a member of a trading bloc or not is a very crucial decision for a nation since her membership can easily overturn or reform her economic policies and economic future.

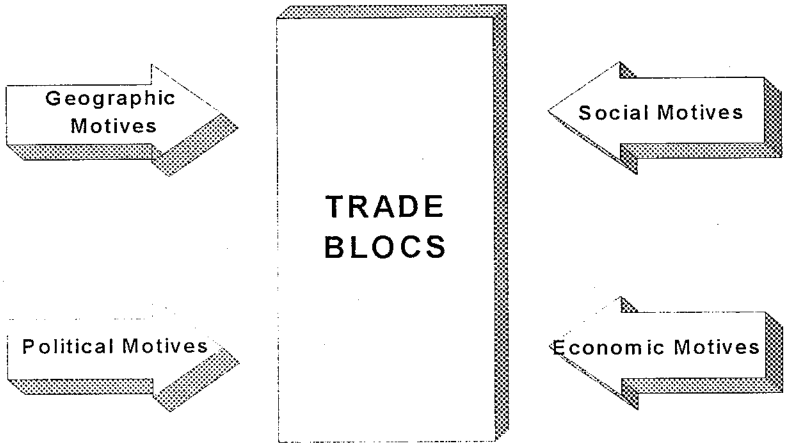

Figure 1: Motives For Regional Economic Groups

Generally speaking, the real advantage of membership in a trading bloc lies in its promise of a higher economic growth rate and supported industrialization. In addition, new market opportunities within the large bloc area attract other nations who cannot enter these somehow "closed markets" (to others). Otherwise, the economic impact of trading blocs on a nation can be remarkable. For instance, Jewell[4] points out that the Single Market in Europe has created a more competitive and dynamic economy. According to some estimations, savings from the integration of the national markets of the twelve member countries will amount to 140 billion Pounds per year. It will create millions of jobs throughout Europe and put Europe on an upwards trajectory of economic growth lasting into the next century. Quraeshi and Luqmani[12] explain the beneficiary effects of trading blocs in terms of supply side and demand side. Supply effects can be summarized as economies of scale, increases in productivity and innovation rate and administrative cost savings. From the beneficial standpoint, demand effects include lower prices, greater consumer choice and improved quality as a result of increased competition. However all these results have an effect on member countries only. Meanwhile some dramatic changes may be experienced by non-member countries. First of all, the increasing cost of trading with nonmember countries will prevent member countries to trade with these countries in terms of tariff rates. Thus, this situation will divert the trade from nonmember countries to member countries. As a result, a trade creation effect will emerge due to eliminated tariffs within the bloc region.

One of the most important impacts of trade blocs on member countries is internal trade increase and new market opportunities. In general, elimination of all trade barriers among member states means a shift of international trade into domestic trade. Given the advantage of eliminated tariff barriers, member nations, at least many of them, would prefer to trade among themselves rather than buying from other nations and paying extra tariff costs. Ultimately, this will result in increased internal trade figures. These kinds of agreements revive the trade for not only giant firms but also for medium to small sized firms that will try to take advantage of these arising new beneficiary circumstances.

It can be deduced that with the elimination of tariffs, new market opportunities will arise among bloc firms. As a result of economic integration, the once closed doors of some abundant markets will now easily open up and increased trade wil create new job opportunities. In addition, the GNP of member countries will rise.

In response to growth in internal trade, trading relations of a nation also change once she becomes a member of a trading bloc. In other words, the elimination of tariffs causes a change in trade partners. For example, when two countries form a trade bloc, tariffs of trade will be eliminated between themselves. However, their tariff rates will still remain for nations that are not members of this union. In this case, trade between union members will no longer be subject to duty. In many ways it will be cheaper for member countries to import from each other rather than from other countries that are not members of the union. Specifically, exports from a new member will enter the bloc market duty free while exports from third countries will still have to face tariff and even nontariff barriers stemming from the common external trade policy of the trade bloc (unless the union is a free trade agreement which does not require common external tariffs). Indeed, this situation may offer some new market opportunities, and the usual trading partners can be replaced by new ones whether members want it or not. This is one of the reasons why many countries are willing to initiate negotiations preferentially with their major trading partners to form a trading bloc. Instead of changing the direction of trade and starting from scratch with other nations, many countries try to strengthen their economic relations with their major partners. This holds true both for The U.S.-Canada Free Trade Agreement and The U.S.-Israel Free Trade Agreement. In many respects, firm economic relations are, and should be, the first step toward economic integration.

In brief, altough it seems paradoxical, trading blocs may lead to both trade creation and trade diversion. Trade creation is explained by volume increase due to the formation of a trade bloc. On the other hand, trade diversion is the volume of trade diverted from outside nations to bloc members because of the above mentioned reasons. Hine[13] emphasizes that trade diversion is disadvantageous for the focus country because it involves a deterioration in that country's terms of trade. But trade creation can be viewed favourably since resources are reallocated more in line with the country's pattern of comparative advantage, and the distortion of consumer choice is reduced. As a result, one can say that the gains and losses experienced with the formation of a trading bloc partly depends on trade creation and trade diversion effects.

Another tariffs-related effect of trade blocs is efficiency by increased competition. A trading bloc results in lowered or eliminated tariff barriers which eventually leads to intense competition among the bloc countries. In response to this situation, small firms will particularly suffer from this fierce competition and start to force the government to take some measures to compensate their losses. Unavoidably, trading blocs will have as many opponents as supporters. Paradoxically, as smaller firms suffer from antiprotectionist activities executed within a trading bloc, nations at the same time begin to reach efficiency with the remaining strong firms.

It is certain that lower duties on products will give the manufacturers a price advantage over their competitors in the market. Most probably, this is the most direct and obvious influence of trading blocs.

Economic sovereignity is another important issue in trading blocs. As noted by Clark[14], sovereignity differs from nationalism which says "ours is the best, the greatest, the most glorious". Contrary to this thinking, sovereignity says, "what's ours is ours so we are the only ones to control them".

Joining a trading bloc means, to some extent, decreasing economic sovereignity. Interestingly, some extremist politicians comprehend this situation as abandonment of national sovereignity. Once a nation joins a trade bloc, she is no longer independent and free in her economic decisions. For instance, during the free trade negotiations, the Mexicans and Canadians always feared becoming economic colonies of the U.S. Since every community has a common economic policy, all of the members of a particular community should pursue harmonized economic policies. To be able to act as a single market or single economic unit, individual nations should avoid economic decisions that are contrary to the general economic policies of their nation. This particularly holds true for tax and foreign trade policies. Otherwise, such a trading bloc will not work effectively. On the basis of this appraisal, whether good or bad, each nation should act in harmony with other nations of a particular trade bloc in order to reach shared economic goals as soon as possible.

Contrary to their decreasing sovereignity effect, trading blocs can enhance the political power of member countries. Almost always, economic stability and consistency leads to political power as well. Often, economically sound nations have much more bargaining power than non-member countries concerning political issues although this may vary depending on the trading bloc. Political power requires economic power. Given the case of trading blocs, this is one of the important reasons why many countries want to belong to a trading bloc.

Another important effect of trade blocs is access to lower cost inputs. Having the opportunity of operating in a large geographic area, firms of bloc member nations may get access to lower cost inputs which will lead to lower cost outputs. As long as the transportation costs are affordable, it will be to their own benefit to use lower cost inputs in their production. Machlup[15] points out that enlarged markets through the removal of tariffs among the member countries would permit potential economies of scale to be realized. Larger plants and larger firms could produce at lower unit cost which can also be reflected to their unit prices. In short, member countries of a trading bloc will mutually enjoy a better and easier access to cheap labor and components along with a growing export market.

V. SOME SKEPTICAL POINTS: IS IT REALLY FREE TRADE AND WILL WE GAIN ON EVEN TERMS ?

Though there have been tariff elimination efforts all around the world, this does not mean that all the restrictive barriers are disappearing. However, free trade still carries the risk of increasing protectionism toward the rest of the world. If existing trading blocs prefer to be self sufficient by using existing tariff and nontariff barriers against the rest of the world, globalization of world trade will not go any step further than being a dream. Lindert[9] stresses that the European Community is allowing free trade between members, but at the same time via tax policies, is restricting imports from other countries. These kinds of discriminatory trade policies may serve protectionist achievements in the short run but as Coughlin, Chrystal and Wood[16] point out, the cost of protectionist trade policies far exceed the benefits. The losses suffered by consumers exceed the gains reaped by domestic producers. In many cases not only the producers but also the governments benefit from protectionist trade policies. The main interest of the government lies in high tariff revenues. It should be noted that tariffs are not the only means of achieving protectionist measures. A number of different non-tariff barriers can prevail on world trade. Due to the strong wave of nationalism, non-tariff barriers have unfortunately gained a lot of importance in recent years. For example, import prohibitions, quotas, and other quantitative restrictions can limit trade volumes easily. It is for certain that whilst decreasing tariff rates, governments will increase non tariff barriers. For example, even though the Japanese authorities claim that their trade regime is as open as it can be, due to the informal barriers (namely non tariff barriers), this is not the case. Machlup[15] draws our attention to two different extremes: free traders and protectionists. He claims that a regional trade bloc may end up with a group of happy free traders with abolished barriers in intra-bloc trade and a group of protectionists who insist on continuation of barriers against extra-bloc imports. Likewise, Turner[17] points out that regional trading blocs tend to widen the ambit of protectionism. Another supportive claim comes from Groth[18] who says that barriers against competition from sources external to the European Union will grow.

One of the most contentious problems of trading blocs is the unequal distribution of expected benefits among countries. Particularly as soon as negotiations start, many interest groups such as labor unions, opposition parties and environmentalists may have many objections in forming a trade bloc with other countries. Trade diversion issues may lead to some disturbances among major trading partners.

VI. CONCLUSION

The increasing tendency toward regionalism forces nations to be decisive about their economic future. Needless to say, this situation particularly causes developing countries such as Turkey to make important decisions. Today, nations not belonging to any trading bloc have almost no chance against giant integrated regional economies. For many types of products, it will be much more difficult to enter these bloc markets. Pursuing economic policies such as creating an economically self sufficient regional grouping and trying to meet their needs from their own sources at the first attempt, cause trade blocs to close their doors to nonmember countries. This situation may cause some important problems for the nonmember countries.

Given the situation that trading blocs will have highly considerable effects on both member and nonmember countries, developing countries have to be proactive rather than reactive to face the challenges of the 90's and beyond. It is plain to see that the world is separating into trading blocs and countries have no choice but to enter one of them. This thought stems from reactive motives which highlight the idea that these sorts of agreements would help nations compete against rival trading blocs of the world. The only way of belonging to such an economic grouping is by following the rules of liberal economics. Economies that are disintegrated from the world may fall into the trap of economic inertia. In today's world where everyone speaks in global notions, firms that are not working on an international basis and that only serve the domestic market have a competitive disadvantage. In a milieu where tariffs are virtually decreasing, even if you never try to enter your rivals' markets, it is very likely that they will soon enter your market. Historically, prevailing protectionist policies have lost their importance. It has been understood that protectionism is a trade off between short term gains and greater long term gains. Apparently, protectionist trade policies can cause negative implications on the customer side. Domestic firms can do whatever they want in markets where there is no foreign competition. In the long run, without any concern about quality and with a limited number of product variety, these firms easily lose their international competitive advantage. Surely, it is not practical to claim that customers always get satisfaction where there is almost no price and quality competition.

But considering the growing world market opportunities out of prevalent trade blocs, bloc countries cannot ignore new market opportunities by exploiting a closed door policy. But in the long run, a regional globalization (freer trade among the bloc countries) might be considered as a stepping stone toward worldwide free trade. By achieving the idea of regional free trade, nations can try to succeed in creating a more open, more competitive and freer trade worldwide.

In spite of their advantages, trade blocs are still worthy of skepticism and open to question. As previously mentioned, non tariff barriers are still one of the walls erected in front of the free trade aims.

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