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*Regionalization Versus  
Globalization of World Trade*

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# **Regionalization Versus Globalization of World Trade**

by Murray Weidenbaum

Two conflicting trends are pulling at conventional international trade policy — regionalization and globalization — and the outcome is in doubt.

On the most visible and obvious level, governments are entering into regional coalitions or trading blocs. Witness the rise of the European Community and the pending North American Free Trade Agreement. At a more subtle but perhaps more fundamental level, individual enterprises are learning how to overcome the trade and investment barriers erected by governments.

One result of these two contrasting developments is that the role of the individual nation-state is diminishing, especially as a force in trade policy. This does not necessarily make the General Agreement on Tariffs and Trade (GATT) obsolete. These developments do, however, underscore the need to update traditional approaches to trade policy. But first let us evaluate the implications of those two conflicting trends.

## **Implications of Regionalization**

Let us begin by examining the development of the European Community. It has become fashionable to focus on the growing ability of people, goods, services, and investments to move freely within the Community. That truly is a highly desirable situation. Elimination of national restraints permits economies of scale which promote efficiency and productivity.

However, another basic result of regionalization commands far less attention. It is the development of more insular or inward-looking patterns of international commerce.

The raw statistics on intra-EC commerce are disconcerting. In 1960, before the

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Common Market gained momentum, more than 60 percent of the foreign trade of those twelve nations was outside of what is now the EC. But currently, 60 percent or more of the trade of the EC-12 stays inside the Community, a complete reversal. The completion of the EC-92 process is bound to increase that ratio further.

The inclusion of the European Free Trade Area (EFTA) nations — Austria, Switzerland, Norway, Sweden, Finland, and Iceland — in the expanded European Economic Area is a noteworthy development. That could quickly bring the ratio of intra-Western-European trade to the neighborhood of 70 percent.

At the danger of introducing a disconcerting note, I must report that I am not aware of the EC bringing down any of the common trade barriers that surround the twelve member nations. When I inquire about domestic content and reciprocity restrictions, my friends in Brussels say not to worry, that those provisions are not aimed at the United States. But I do not know how good their aim is. Even if the EC restrictions are limited to Asian producers, North Americans will be affected. Are we not the alternate market for their products?

My second example of regionalization is less formal. It is the rise of the Asian rim economies under the business leadership of Japan. Those nations surely represent the world's fastest growing market area. There is no formal intergovernmental structure involved comparable to EC or EFTA. However, some Japanese executives are referring to the phenomenon as the Greater East Asia Co-Prosperity Sphere, a term that has not been heard for half a century.

Once again, the numbers are impressive. Like the EC, over 60 percent of the trade of the Pacific rim nations stays within the area. The six nations making up ASEAN or the Association of Southeast Asian Nations (Malaysia, Indonesia, Philippines, Thailand, Singapore, and Brunei) are now a larger market for Japan than the United States. However, many of those "imports" become components of items that ultimately are exported to the EC or North America.

An examination of the substantial flows of investment from within the Asian rim — especially from Japan, Taiwan, and South Korea — to the newer industrialized nations in the area such as Thailand, Malaysia, and Indonesia is instructive. The development of a unified trading area is now taking place.

In some cases — notably Malaysia and Indonesia — Japan has become their leading trade partner, for exports as well as imports. By 1995, it is likely that Japan will provide the largest market for the exports and perhaps also the imports of most of the Asian rim nations.

Given the expansion of trade and investment in both Western Europe and East Asia, it should not be surprising that the nations of North America have, belatedly, developed their own response. Following the U.S.-Canadian Free Trade Agreement, a similar tripartite arrangement with Mexico is being formulated. Conceivably, this arrangement will extend to other major trading nations in the western hemisphere in the future.

The question then arises: on balance, will regionalization reduce or increase world trade? The data will be difficult to interpret. I say that because the continued rise in regionalization is likely to coincide with the growth in international commerce. However, it will not be a cause and effect relationship. It is another development — the globalization of business — that will pace the growth of world trade. Technological advance, for example, will be a far more powerful force than governmentally imposed restraints.

### **Implications of Globalization**

Let us now turn to the rise of the global firm. It is commonplace to say that Germany exports wine — and BMWs — to the United States and that the United States exports jet airliners to Germany. But neither nations nor governments do more than record and perhaps tax those cross-border transactions. Typically, it is business firms that engage in international commerce.

When we examine foreign trade from that viewpoint, we gain new insights. For example, about one-half of what governments call foreign trade actually involves cross-border transactions between different parts of the same company. That ratio holds true for Western Europe, the United States, and Japan. That is, a domestic firm may be shipping goods to or receiving items from an overseas subsidiary — or a foreign firm may be engaged in similar transactions with its divisions in this country.

In a geopolitical sense, all of this is foreign commerce. But, from an economic viewpoint, these international flows of goods and services are internal transfers within the same firm. That is the global enterprise in full swing.

The resulting products, however, can be confusing to the average citizen. How truly American is the Pontiac LeMans? That car has a General Motors nameplate and is sold through the GM-Pontiac dealer network. But the product is assembled in Korea using components produced in many Asian nations and elsewhere. What about the Accord, a popular vehicle bearing the Honda nameplate and sold in the United States through the Honda dealer network? That supposedly Japanese product has far more U.S. value-added than the General Motors car.

Perhaps the most extreme case was cited by former U.S. Secretary of State George Shultz. He tells of a shipping label on integrated circuits made by an American firm, which reads: "Made in one or more of the following countries: Korea, Hong Kong, Malaysia, Singapore, Taiwan, Mauritius, Thailand, Indonesia, Mexico, Philippines. The exact country of origin is unknown."

Governments have set up myriad restrictions on imports to "protect" domestic jobs. Not all companies or consumers want to be protected, however. Recently IBM urged the U.S. government to remove an antidumping duty that it had imposed on certain computer display screens imported from Japan. Why is an American firm that is suffering from foreign competition such a strong advocate of free trade? Once again, we must look to the intricacies of the global economy for an explanation. The 63 percent tariff on that component had been levied in an effort to protect American producers of those display screens. However, the resultant increase in the price of that key component made American-built computers uncompetitive against models built in Japan. IBM claimed that it might soon be forced to move some of its production offshore if the tariff is not eliminated.

A more complicated, if not humorous, case is the formal complaint that American automobile producers, led by Chrysler, recently filed. They charged Japanese companies with "dumping" minivans in the United States. It turns out that the complaint, likely inadvertently, includes minivans being made by Mitsubishi for Chrysler — to be sold in the United States under the nameplate of the American firm.

Technological progress — especially in the fields of communication and transportation — makes possible a variety of business innovations which often overcome the obstacles imposed by parochial governments. Discussions of cross-border joint ventures and strategic



alliances have moved from the school room to the board room. Often electronics companies in Europe, Asia, and the United States together engage in joint ventures to develop new products, they co-produce existing products, they serve as sources of supply for each other, are customers of each other — and they compete against each other.

There is no set pattern. Partially owned subsidiaries, associated firms, licensing, franchising, and correspondent relationships are all increasingly popular ways in which business firms respond to changing threats and opportunities in the global marketplace.

A direct example of the power of technology occurred on the day of the Iraqi invasion. The manager of a Kuwaiti bank faxed the bank's records page by page to his office in Bahrain. Periodically, he was forced to stop because the gunfire seemed to be coming closer. By day's end, he had successfully faxed all the key documents.

The next day, the bank opened for business as a Bahraini institution, not subject to the U.S. freeze on Kuwaiti assets or to Iraqi control. The bank literally was transplanted from one nation to another by technology.

Clearly, technology and business innovation are outpacing traditional ways of thinking about international economics. The standard geopolitical map is out of synchronization with the emerging business and economic map.

### **An Optimistic Long-Run View**

Nevertheless, while private enterprise is increasingly global, government policy is still very parochial. Understandably, voters still care about their jobs and their country, state, province, and locality. And politicians are not reluctant to exploit those concerns. Yet there is another force that comes into play: the consumers who vote every day of the week, in dollars, marks, yen, pounds, francs, and lira. That is the reason to end this presentation on an upbeat note.

These same voters, as consumers, buy products and services made anywhere in the world. They give far more weight to price and quality than country of origin. Without thinking about it, consumers are adapting to the global economy.

After all, if consumers were not oriented to the global marketplace, the pressures on government to restrict international trade would not arise in the first place.

My favorite consumer is Senator Fritz Hollings of South Carolina. In the Congress he leads the battle to restrict imports of textiles and apparel. But he recently had another senator bring back a custom-made suit for him sewed in South Korea. I use this example not to pick on the distinguished legislator, but to show the positive force of economics.

In the years ahead, the combined power of economic incentives and technological change will increasingly compel voters and government officials to wake up to the positive implications of the global economy.

Where does this leave international organizations such as GATT? Without getting expectations up too high, perhaps GATT may be considered an economic counterpart to peace negotiations on the part of erstwhile military opponents. The meetings themselves may not result in dramatic agreements. But merely talking to each other provides opportunities for increasing understanding and developing new relationships of mutual benefit. Nevertheless, I expect that the real liberalization of trade in the years ahead will come from the competition among business firms in the private sector.