

## 2.8: Global Trade Agreements and Organizations

**What you'll learn to do:** describe global trade agreements and economic organizations that regulate and promote global trade

In this section, you'll learn about the organizations that oversee global economic cooperation and help facilitate global trade agreements.

### Learning Objectives

- Describe the role of the World Bank in promoting global economic development
- Describe the role of trade agreements in global business

### The World Trade Organization (WTO)

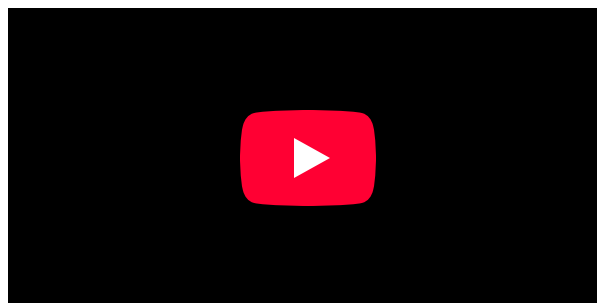
In the post–World War II environment, countries came to realize that a major component of achieving any degree of global peace was global cooperation—politically, economically, and socially. The intent was to level the trade playing field and reduce economic areas of disagreement, since inequality in these areas could lead to more serious conflicts. Nations agreed to work together to promote free trade and, with the help of key international organizations like the World Trade Organizations, they entered into bilateral and multilateral agreements.



### GATT: How the World Trade Organization Got Its Start

Before you begin your reading on the World Trade Organization (WTO), take a few minutes to watch the following video that will give you some background on **General Agreement on Tariffs and Trade (GATT)** and explain how it grew into the WTO we know today. Remember, the world is much smaller today than when your parents and grandparents were growing up, and international trade hasn't always been the norm. After watching the video, consider how impossible world trade would be without some type of agreement among nations.

Enjoy!





As you saw in the video, what began with one agreement (GATT) eventually evolved into the WTO. In fact, GATT was the only multilateral instrument governing global trade from 1946 until 1995. Given the difficulty of trying to regulate trade among more than one hundred nations according to a single document, it's easy to see why the WTO came into existence. It became clear to the participating nations that GATT was incapable of adapting to an increasingly globalized world economy. Moreover, when the Uruguay Round of GATT negotiations was launched in September 1986, it marked the largest global effort to structure trade in history. Today, GATT still exists as the WTO's umbrella treaty for trade in goods, but it's no longer the only legally binding global-trade agreement.

What does the WTO actually do? Among its various functions, the most important are the following:

- Oversees the implementation and administration of the agreements between nations that fall under the WTO's scope of authority
- Provides a forum for negotiations and settling disputes among nations.

In recent years, the WTO has also made it a priority to assist developing nations as they come under WTO regulation. Many developing countries and emerging markets lack the experience and technical expertise needed to deal with large and very comprehensive trade agreements. The WTO provides them with critical training and support, thereby ensuring that the WTO is inclusive and equitable toward both the wealthiest and the poorest nations in the world.

Part of the nondiscrimination mandate of the WTO is most-favored-nation (MFN) status. Most-favored-nation status requires that a WTO member must apply the same terms and conditions to trade with any and all other WTO members. In other words if a country grants another country (even a non-WTO member) a special favor, then every other WTO member must get the same treatment. You probably experienced a version of most-favored-nation status as a child, when an adult told you that if you were going to take gum or candy to class, you had to bring enough for everyone. In other words you couldn't just give gum or candy to your best friends, and if you didn't have enough for everyone in the class, then nobody got any. That, in effect, is how most-favored-nation status works.

One of the other key elements to the success of the WTO is its transparency requirement. WTO members are required to publish their trade regulations and follow a system that allows external parties to review and evaluate any administrative decisions and their impact on trade regulations. When a WTO nation changes its trade policies, those changes must be reported to the WTO.

Overall, the WTO's mission is to improve the stability and predictability of global trade. As a result, it tends to support free-trade, as opposed to protectionist, policies, and strongly discourages the use of quotas and other such restrictions on imports.

Whether or not the WTO is doing its duty and accomplishing its mission is a matter of ongoing debate. Nonetheless, the WTO currently has 104 members and twenty observer governments. WTO member states account for almost 97 percent of global trade and 98 percent of global GDP. Once the twenty observer governments become members, it is possible that the WTO will oversee the entire world economy. What began in 1947 in Geneva, with twenty-three nations focused solely on tariff reduction, has grown into a truly global organization that deals with agriculture, labor standards, environmental issues, competition, and intellectual property rights.

## The World Bank

World Bank Group president Jim Yong Kim visits an integrated child development services and skills center in Delhi, India.



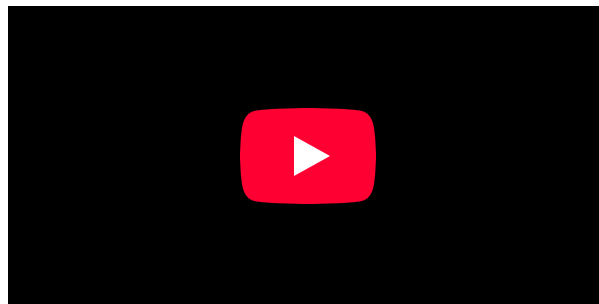
Created in 1944 at the Bretton Woods Conference in New Hampshire, the **World Bank** is an international financial institution that provides loans for capital programs to developing countries. It comprises two institutions: the International Bank for Reconstruction and Development (IBRD), and the International Development Association (IDA). Originally, the IBRD was tasked with supporting post-war reconstruction, but it has evolved to include the present-day mandate to alleviate poverty worldwide. The World Bank is a component of the World Bank Group, which is part of the United Nations system. The World Bank is comprised of 189 member countries represented by a board of governors. Although headquartered in Washington DC, the World Bank has a presence in almost every nation in the world.

The World Bank has set two goals to achieve by 2030:

1. End extreme poverty by decreasing the percentage of the world's population that live on less than US\$1.90 per day to no more than 3 percent
2. Promote shared prosperity by fostering the income growth of the bottom 40 percent in every country

The World Bank's primary function is providing low-interest loans and grants to developing countries. It tends to fund projects focused on education, infrastructure, natural-resource management, and public health. In many instances, the World Bank provides technical assistance as well as research and policy advice to developing nations. One of the projects currently underway is the Education Sector Support Project for the Republic of the Congo. The primary objective of this project is to improve education outcomes for primary- and secondary-school children by providing quality education in an appropriate teaching and learning environment. Other World Bank projects are aimed at improving basic infrastructure, such as building and maintaining safe water supplies and sanitary sewer systems in Africa and parts of Asia. For developing nations, many of these improvements would be impossible without the World Bank's help. Although the World Bank has come under fire in the past for budget overruns and poor project oversight, its role in promoting economic development has been undeniable.

The following video shows how a World Bank project works:



## The International Monetary Fund (IMF)

The **International Monetary Fund (IMF)** is an international organization headquartered in Washington, D.C., comprised of 189 member countries. The IMF works to foster global growth and economic stability by providing policy, advice, and financing to its members. It also works with developing nations to help them reduce poverty and achieve macroeconomic stability. Formed in 1944 at the Bretton Woods Conference in New Hampshire, it came into formal existence in 1945 with twenty-nine member countries and the goal of reconstructing the international payment system. It now plays a central role in the management of balance-of-payments difficulties and international financial crises.

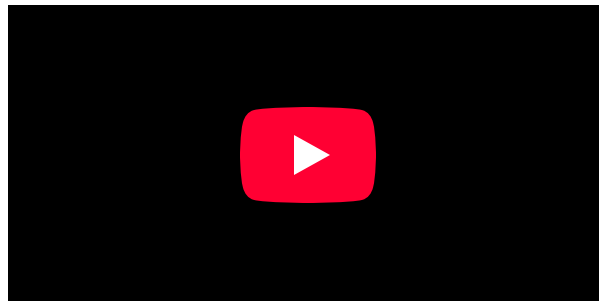


IMF member countries contribute funds to a pool, from which they can borrow if they are experiencing balance-of-payments problems. The rationale for this arrangement is that private international capital markets function imperfectly, and many countries have limited access to financial markets. Without access to IMF financing, many countries can only correct large external payment imbalances through drastic measures that can have adverse effects on their own economies and the world's. The IMF provides alternate sources of financing to countries in need that would not otherwise be available to them.

When the IMF was founded, its primary functions were to provide short-term capital to aid the balance of payments and to oversee fixed-exchange-rate arrangements between countries, thus helping national governments manage their exchange rates and prioritize economic growth. This assistance was meant to prevent the spread of international economic crises. The IMF was also formed to help put the pieces of the international economy back together after the Great Depression and World War II. In addition, it also sought to provide capital investments for economic growth and infrastructure projects.

The IMF's role was fundamentally altered by floating exchange rates post-1971. At that point the organization began examining the economic policies of its loan recipients to determine whether a shortage of capital was due to economic fluctuations or economic policy. The IMF also researched what types of government policy would ensure economic recovery. The current challenge is to help countries implement economic policies that reduce the frequency of crises among the emerging-market countries, especially the middle-income countries that are vulnerable to massive capital outflows. In order to meet this challenge, the IMF's activities have expanded beyond the oversight of exchange rates to surveillance of the overall macroeconomic performance of its member countries. Today it plays an active role in shaping and managing economic policy around the world.

The following video gives a good overview of the IMF and its role in promoting global trade.



## Trade Agreements

So far you have seen how international organizations such as the WTO, IMF, and World Bank support global trade, but this is only part of the story. Where global trade really gets a boost is from trade agreements (also called trade blocs). This where the term “global economic integration” gets its legs— from the process of modifying barriers among and between nations to create a more fully integrated global economy. Trade agreements vary in the amount of free trade they allow among members and with nonmembers; each has a unique level of economic integration. We will look at four: regional trade agreement (RTA) (also called a “free trade area”), customs unions, common markets, and economic unions.



**Regional trade agreements** are reciprocal trade agreements between two or more partners (nations). Almost all countries are part of at least one RTA. Under an RTA, countries “huddle together,” forming an international community that facilitates the movement of goods and services between them. For example, the North American Free Trade Agreement (NAFTA) enacted between Canada, the U.S., and Mexico facilitates trade among these countries through tariff reductions and elimination. The Association of Southeast Asian Nations (ASEAN), shown below, provides for the free exchange of trade, service, labor, and capital across ten independent member nations to provide a balance of power to China and Japan. The Central American Free Trade Agreement (CAFTA) (Costa Rica, Dominican Republic, Guatemala, Honduras, Nicaragua, and El Salvador) eliminated tariffs on more than 80 percent of U.S. exports and opened U.S. trade restrictions for Central American sugar, textiles, and apparel imports, thereby reducing costs on these products for American consumers<sup>[1]</sup>.



The Association of Southeast Asian Nations (ASEAN) as of 2015.

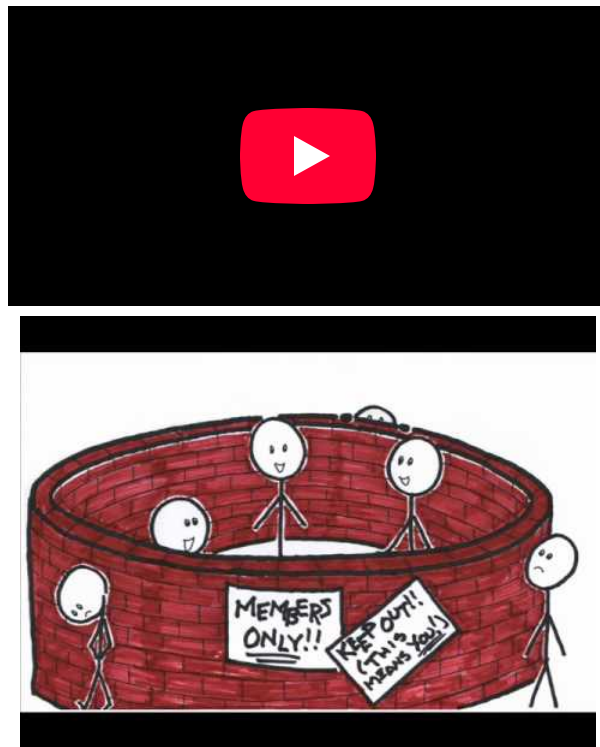
**Customs unions** are arrangements among countries whereby the parties agree to allow free trade on products *within* the customs union, and they agree to a *common external tariff* (CET) on imports from the rest of the world. It is this CET that distinguishes a customs union from a regional trade agreement. It is important to note that although *trade* is unrestricted within the union, customs unions do not allow free movement of capital and labor among member countries. An example is the customs union of Russia, Belarus, and Kazakhstan, which was formed in 2010. These countries eliminated trade barriers among themselves but have also agreed to some common policies for dealing with nonmember countries.

**Common markets** are similar to customs unions in that they eliminate internal barriers between members and adopt common external barriers against nonmembers. This difference is that common markets also allow free movement of resources (e.g., labor) among member countries. An example of a common market is the Economic Community of West African States (ECOWAS), comprised of Benin, Burkina Faso, Cape Verde, Gambia, Ghana, Guinea, guinea-Bissau, Ivory Coast, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo.

An even more economically integrated arrangement is the **economic union**. Economic unions eliminate internal barriers, adopt common external barriers, permit free movement of resources (e.g., labor), AND adopt a common set of economic policies. The best-known example of an economic union is the European Union (EU). EU members all use the same currency, follow one monetary policy, and trade with one another without paying tariffs.

The following video further explains and compares the different types of trade agreements:





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1. USTR, CAFTA-DR Dominican Republic-Central America FTA [↩](#)

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