

POL 396: International Organization

Precept 8

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The European Union

Timeline:

- 1951: The European Coal and Steel Community
 - Initial members (6): France, Germany, Italy, Belgium, the Netherlands, and Luxembourg
- 1958: The European Economic Community (EEC)
- 1993: The European Union (EU)

Current membership: 27 countries

The European Union

Divisions of power

- **Legislative:** Council of the European Union; European Parliament
- **Executive:** European Council + European Commission
- **Judicial:** Court of Justice of the European Union (CJEU)

The European Monetary Union

- 1979: European Monetary System
 - Fixed Exchange Rate + Open Capital Flow
 - Germany kept **high** interest rate; others pegged to the German Mark
 - Gave up Sovereign Monetary Policy
- 1981: Challenge by socialist French president – Mitterrand
 - Want to have it all (sovereign monetary policy)
 - Specifically, want **lower** interest rate (for lower unemployment rate, which is good for labor)
 - Leads to friction with Germany

The European Monetary Union

- 1981 - 1983:
 - France pushed for lower interest rates
 - Germany wanted to maintain exchange rate stability and combat inflation
 - Mitterrand (France) backed down.
- 1988: Start planning the European Monetary Union
- 2002: Euro
 - Gave up sovereign monetary policy entirely

Reading: McNamara (2008)

- Key question: Will Euro compete with the dollar as the key international currency?
- Short answer: No
- The foundations of political power and their embodiment in social processes are not adequately developed in the EU case to allow the Euro to overtake the dollar as the international currency of choice.

McNamara (2008) — Key Concepts

International Reserve Currency

The currency most often held by governments and institutions as part of their foreign exchange reserves. (what people use for global trade and financial transactions, etc.)

Focal Point

A concept where people tend to coordinate their actions around a particular point. When one does not have information about what other people plan to do, it still can be possible to coordinate decisions if there is a focal point that both people consider reasonable.

Pros and Cons of International Reserve Currency

Benefits

- Finance fiscal deficits (print more money)
- Enhance international prestige
- Debt denoted in your own currency

Costs

- Monetary policy autonomy is hindered
 - Vast magnitude of currency held abroad
- Currency overvaluation
 - Cheaper & Easier to Import
 - Expensive & Harder to Export

Why EU might not be the international reserve currency?

- No equivalent tool as the US treasury bill at the EU level
- Unclear leadership (who bails you out?)
- So USD is still the focal point
 - The more people use it, the more effective it is

Questions to think about

- Read about the history of EU bailout of Greece after the financial crisis. What does it tell you about decision-making and leadership for the Euro?
- What are the pros/cons of having USD as the single dominant reserve currency vs. having diverse reserves?
- What scenarios can you think of where other currencies challenge the USD in the future? (Chinese RMB, IMF SDR, Bitcoin, etc.)

World Trade Organization (WTO)

Timeline

- 1944: International Trade Organization
 - Failed. Discussed at Bretton Woods.
- 1947: GATT signed
- 1948: GATT entered force with 23 members
- 1995: WTO

The WTO is a small IO:

- Staff: ~ 600
- Budget: ~ \$200 million

9 Bargaining Rounds

- 1947 Geneva
- 1949 Annecy
- 1951 Torquay
- 1956 Geneva
- 1960-61 Dillon Round
- 1964-67 Kennedy Round
- 1973-79 Tokyo Round
- 1986-93 Uruguay Round
- 2001-??? The Doha Round

The rounds are getting longer because remaining issues are more difficult.

WTO: Functions

1. Set of principles and rules → forum for negotiations
2. Intergovernmental bargaining process → administers trade agreements
3. Dispute settlement mechanism

1. Principles and Rules

Two main principles:

1. Market liberalization (increase in aggregate welfare)
2. Nondiscrimination
 - Most Favored Nations (MFN): Treat all countries equally
 - National treatment: no discrimination against foreign firms

Exceptions to the MFN

- Generalized System of Preferences (GSP): lower tariffs can be applied to developing countries to facilitate export to developed countries
- Regional trade agreements: preferential tariff rates to partner countries

2. Intergovernmental Bargaining Process

Tariff and **non-tariff barriers (NTBs)**

- health regulations, environmental standards, quotas, licensing, labeling conditions, anti-dumping, etc.
- more extensive discussion than tariffs these days (and these are harder for countries to agree upon, so the negotiations (“bargaining rounds”) are taking much longer)

3. Dispute Settlement Mechanism

Functions

- Resolve disputes through arbitration
- Authorizes punishment: legitimize retaliation → higher cost of escalation

Consequence

- Foreseeing the punishment, countries tend to resolve the dispute before escalating to an actual panel (deterrence effect)

[But this key function of WTO has been challenged since WTO Appellate Body Crisis (2017-): there are no judges!]

Regional Trade Agreements (RTAs)

- Free Trade Agreements (FTAs)
 - Most are bilateral (e.g., KORUS, CAFTA) than trilateral or more (e.g., NATFA, CPTPP)
 - More common
- Customs Union: Common tariff policy towards non-members
 - More commitment

Busch (2007): Forum Shopping

RTAs open up venue for **forum shopping**

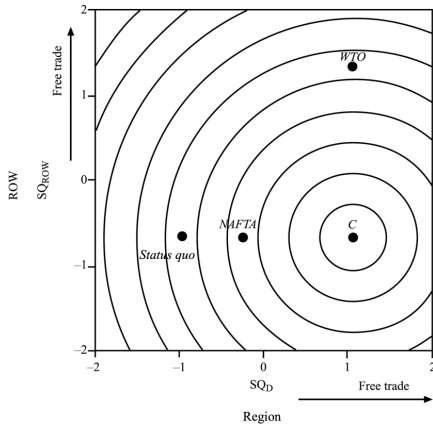
- Countries may choose the dispute settlement forum that best suits their interest

Shop under what interest?

- What kind of precedents a complainant wants to establish?
- regional/multilateral/none

Who is Busch arguing against?

- View that countries shop for whatever is closest to their “ideal ruling”



- Complainant (C) prefers $(SQ_D, SQ_{ROW}) = (1, -0.5)$
- Status quo is $(-1, -0.5)$
- If goes to WTO, outcome is $(1, 1.5)$
- If goes to NAFTA, outcome is $(-0.1, -0.5)$
- So NAFTA is better than WTO (closer to C's ideal point).

- The preference has two dimensions! (Region vs. ROW)
- WTO is not ideal if C only wants regional liberalization.

Additional Resources

Take a look at the evolution of Preferential Trade Agreements (PTAs) over time:

<https://www.designoftradeagreements.org/visuals/>

I will present two papers related to international organizations. You are more than welcome to take a look and let me know if you have any thoughts! (click below to the draft)

- U.S. Reaction to the Founding of China's AIIB
- Is flexibility good for international institutions?