Appendix A: Regional Integration Arrangements Involving Developing Countries

This review provides some background information on the main regional groupings involving (small) developing economies. It serves to clarify the references made in the main text. The organizations covered are those with a regional economic integration mandate, though, in most cases, they also cover other matters. There are also many regional organizations dealing only with a specific type of functional cooperation, for example, transport, education and finance. These are not included in the review. Groupings that have not been very active recently are also not included. Bilateral arrangements are not covered, as this would be beyond the scope of a brief review. For each regional arrangement, its origin, main objectives and main achievements are summarized together with an appreciation of its general prospects. Table A1 contains a few basic figures on the main regional integration arrangements involving small developing countries.

There is extensive literature on most of the organizations covered. A detailed overview has been prepared by UNCTAD (1996). Brief overviews, also covering arrangements between industrial countries, are contained in IMF (1994), Lawrence (1996) and Frankel (1997).

Africa

Regional integration in Africa was stimulated by the founding, in 1963, of the Organization for African Unity (OAU). At present all African states are members of the OAU, with the exception of Morocco. South Africa became a member shortly after its first democratic election in 1994. Its headquarters is in Addis Ababa, Ethiopia, where the seat of the United Nations Economic Commission for Africa (UNECA) is also located. Even though the OAU's activities lie mainly in the political area, it has been at the origin of the idea of pan-African economic integration. This led first to the Lagos Plan of Action, approved in 1980, on which the OAU collaborated closely with UNECA. In 1991, it led to the Treaty on the African Economic Community (AEC) that was signed in Abuja, Nigeria. The AEC foresees gradual deepening of economic integration over a period of 35 years leading eventually to a pan-African economic and monetary union. The first stages involve the consolidation of the existing regional communities (see discussion below). Although the Abuja Treaty has been ratified by more than the required two-thirds of the African states, its practical significance

Table A1 Basic data of regional integration arrangements involving small developing countries

	GNP 1996 (US$ billion)	*Population 1996 (million)*	*Number of members*	*Exports 1996 (US$ billion)*	*Intra-trade* (%)[1]
Sub-Saharan Africa					
ECOWAS	65.0	213.8	16	26.3	8.9
UEMOA	24.6	63.7	8	8.5	9.5
ECCAS	25.0	86.2	10	9.2	2.1
CEMAC	16.8	27.8	6	7.0	2.2
COMESA	135.2	344.3	20	20.8	7.7
SADC	175.0	180.0	14	48.7	11.4
SACU	142.9	43.6	5	35.1	–
EAC	19.7	77.5	3	5.1	–
Latin America and the Caribbean					
CACM	40.7	30.7	5	11.1	15.7
Andean Com.	230.0	103.4	5	54.2	10.4
CARICOM	20.1	13.6	15	6.2	13.2
OECS	2.1	0.6	7	–	–
MERCOSUR	1032.4	204.8	4	87.4	22.7
Asia and the Pacific					
ASEAN	687.9	478.9	9	398.9	22.9
SAARC	471.4	1241.6	7	63.4	4.3
ECO	412.7	345.3	10	70.6	7.1
GCC	229.3	27.0	6	–	–
FIC	8.3	6.3	14	3.8	–
MSG	7.2	5.4	3	3.6	–

Notes

– = not available.

Data are generally for 1996, but membership is for 1998. For several small developing countries no comparable data could be found, so that the aggregate figures are an approximation. Exports are the total for goods and services. For the GCC, the GNP figure is for 1997.

1. This is the percentage of total exports within the bloc. For SACU there are no regular statistics, but the dependence of Botswana, Lesotho, Namibia and Swaziland on imports from South Africa is estimated to be above 80 per cent. Taking into account the high intra-SACU trade, the figure for intra-SADC trade would rise to around 20 per cent. For the FIC, intra-trade is estimated to be around 2 per cent.

Source: World Bank.

so far is limited. Over the past few years, the OAU has stepped up its activities related to conflict prevention and peace-making. The latter subjects are outside the scope of this review.

Regional integration in Africa is characterized by a multitude of partly overlapping arrangements. Sometimes there is rivalry between different regional organizations. The OAU, together with UNECA, have been involved for a long time in efforts towards rationalization and harmonization of regional organizations, but progress is very slow. African regional organizations are on the whole weak and their activities are hampered because of low political commitment of many member states and limited resources.[1]

Economic Community of West African States (ECOWAS)

Creation: The ECOWAS Treaty was signed in 1975 and revised in 1993.

Membership: Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo.[2]

Background and main objectives

ECOWAS is part of the first integration wave in Africa, probably inspired by the success of European integration. It is considered to be one of the main building-blocks of the AEC. It was set up shortly after the first oil price shock. Nigeria is the dominant member state, accounting in 1996 for approximately 53 per cent of the population and 43 per cent of GNP. During the 1970s and 1980s, when oil prices were high, Nigeria's economic weight in the region was even greater.

The original ECOWAS Treaty called for achieving a Customs Union over a period of 15 years. The revised Treaty of 1993 envisages an economic union. The trade liberalization schedule has been modified and postponed several times. The present schedule provides for elimination of all tariffs on *originating* industrial products by the year 2000. The more industrialized member states (Ghana, Côte d'Ivoire, Nigeria and Senegal) are expected to liberalize faster than the others.

In 1979, a Protocol on free movement of persons, right of residence and establishment in ECOWAS was adopted, to be implemented over 15 years.

The West Africa Clearing House (WACH) was set up in 1975 as an affiliated organization. After an initial successful period, activities of the WACH gradually declined, following the accumulation of arrears mostly owed to the members of the CFA franc zone. In 1992, the WACH was transformed into the West African Monetary Agency (WAMA), an autonomous specialized agency of ECOWAS. One of the tasks of WAMA is to oversee the achievement of a monetary union.

Main achievements and assessment

ECOWAS has made only limited progress towards its core integration agenda of trade liberalization. Despite its objective of becoming a Customs Union or even an Economic Union, origin rules were put in place restricting trade liberalization to industrial products of companies owned within West Africa. This caused problems, particularly for French-owned companies in countries such as Côte d'Ivoire. Closer cooperation in the monetary field has not succeeded. Significant progress has been made on the movement of persons and in functional cooperation (telecommunications and transport infrastructure). Member states do not attach great importance to the implementation of agreed measures. Deadlines have not been met. ECOWAS has tried to set up a fund to compensate member states for revenue losses, but this has not worked well. The Secretariat, since 1998 based in Abuja in Nigeria, has been weak and under-resourced. On the whole, economic and non-economic preconditions for success have been lacking. Several member states have been or still are affected by civil strife and instability that frequently spills over to neighbouring countries.

Future progress will be constrained by factors such as the relatively large number of member states and the wide disparities between them. Despite its lack of achievements, ECOWAS has a clear appeal to civil society and the private sector in the West African region. There is scope for gradually implementing a realistic, but shallow, integration agenda. There is also potential and need for increased collaboration in areas such as trade facilitation, transport, communications, education and research. ECOWAS could also play a useful role in relation to the participation of its member states in the WTO. If the UEMOA, a subgroup of ECOWAS, is successful, it could become a stimulus for integration at ECOWAS level. But this view appears not to be widely shared in non-UEMOA member states, where UEMOA is sometimes seen as a threat for ECOWAS. The progress of economic stabilization and adjustment programmes has certainly improved the outlook for ECOWAS. The future of the organization will, to an important extent, depend on the stability and leadership of Nigeria. The democratic transition in Nigeria in 1998 could provide a window of opportunity.

It should be mentioned that, over the recent past, ECOWAS's most prominent and effective role has been through the peace-making operations in Liberia and Sierra Leone of the ECOWAS Monitoring Group (ECOMOG).

West African Economic and Monetary Union (WAEMU)

Creation: The Treaty to establish the WAEMU, better known in French as the 'Union Economique et Monétaire Ouest Africaine' (UEMOA) was signed in 1994.

Membership: Benin, Burkina Faso, Côte d'Ivoire, Guinea-Bissau (1997), Mali, Niger, Senegal, and Togo. All members are also members of ECOWAS.

Background and main objectives

The UEMOA is the successor of the West African Economic Community or in French 'Communauté Economique de l'Afrique de l'Ouest' (CEAO), which was created in 1973, around the same time as ECOWAS. UEMOA combines the economic responsibilities of CEAO with the West African Monetary Union. But the membership of CEAO was slightly different, comprising Mauritania, but not Togo. UEMOA was created immediately following the long-overdue 50 per cent devaluation of the CFA franc that took place at the beginning of 1994.

The members of UEMOA are all small economies. In 1996, the combined GNP and population were only US$ 25 billion and 64 million respectively. Because of their size and remoteness, transport costs are high for the three landlocked countries (Burkina Faso, Mali and Niger). Disparities within the region are important, but not excessive. Except for Guinea-Bissau, the most recent new member, the common language and institutions resulting from the colonial past are a favourable factor for integration. Again, except for Guinea-Bissau, the political stability and security situation has been reasonable, even though there have been some tensions in most member states.

UEMOA's objectives are ambitious: achieving a full economic union in addition to the existing monetary union. This implies eliminating all intra-regional tariff and non-tariff barriers, putting in place a Common External Tariff, liberalizing factor movement and harmonizing fiscal and macroeconomic policies. Policy harmonization involves installing a system of macroeconomic surveillance.

An aspect that contrasts UEMOA from virtually all other South–South integration initiatives is the setting-up of supra-national institutions, including the Council of Ministers, the Commission, the Court of Justice and the Court of Auditors. Under the Treaty, UEMOA legislation prevails over national legislation. The institutional set-up is similar to the EU system. However, for some critics, the UEMOA copies too much from the EU.

Main achievements and assessment

The CEAO, the predecessor of UEMOA, was generally considered as one of the more successful regional integration initiatives in Africa. Until the second half of the 1980s, economic growth in the sub-region was reasonably high. Côte d'Ivoire and, to a lesser extent, Senegal were the engines of this growth. Côte d'Ivoire developed a significant manufacturing production capacity that partly supplied the rest of the region. Other member states, particularly Burkina Faso, benefited because of important labour migration into Côte d'Ivoire. Benin and, to a lesser extent Togo, are in a special situation because of their closeness to Nigeria. The extent of informal trade is sizeable throughout the region. Being part of the CFA franc zone, the region benefited from monetary stability at a time when the exchange rates of other West African countries became massively overvalued and unstable. Towards the end of the 1980s and during the early 1990s the economic parameters changed drastically. Commodity prices declined, the CFA franc became seriously overvalued and manufacturing exports lost competitiveness. The CFA zone became an important destination for smuggling, benefiting mainly the non-UEMOA members of ECOWAS. This was one of the factors leading to the CFA franc devaluation (halving its value) at the beginning of 1994. The CEAO had not succeeded in establishing its planned Customs Union. The tariff system remained excessively complex partly due to restrictive origin requirements. The compensation mechanism did not work satisfactorily.

It is too early to judge the success of UEMOA because implementation is only beginning. The economic performance of most of the UEMOA member states, particularly Côte d'Ivoire, has improved significantly since 1995, as a result of the devaluation and a rise in commodity prices. The UEMOA has made rapid progress towards tariff liberalization. This implies agreements on commodity classification, speed of internal tariff reduction and movement towards the Common External Tariff (CET). But the details for temporary exclusions, commodity valuation and verification of origin continue to be controversial.

In contrast to most of the earlier integration initiatives in the region, the discussions in UEMOA involve the IMF and the World Bank as well as France and the EU. In this way, the UEMOA programme is made fully consistent with the national structural adjustment programmes. For example, these programmes take into account the fiscal consequences of the UEMOA. A start has been made with the macroeconomic surveillance mechanism. A tight deadline has been agreed to achieve a CET by the year 2000, comprising three non-zero rates: 5 per cent, 10 per cent and 20 per cent.

The coming few years will be critical to see whether UEMOA will make genuine progress towards regional integration. It was mentioned above that the institutional set-up of UEMOA is supranational. But it remains to be demonstrated whether the national governments will play by the rules if, at some stage, national interests may have to be subordinated to regional ones.

Economic Community of Central African States (ECCAS)

Creation: The Treaty to establish ECCAS was signed in 1983.

Membership: Burundi, Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea, Gabon, Rwanda, Sao Tomé & Principe, and the Democratic Republic of Congo.

Background and main objectives

ECCAS has been mainly promoted by the OAU and UNECA as one of the sub-regional organizations that would become building-blocks for pan-African integration. Its objectives are the same as those of ECOWAS: to achieve free movement of goods, services, people and capital, to harmonize national policies and to engage in functional cooperation.

Main achievements and assessment

If a number of preconditions for successful integration have not been fulfilled in the case of ECOWAS, this applies with even more force to ECCAS. Many of its member states have been confronted by severe political instability, widespread insecurity and civil conflict. Disparities within the region are very large. The member states are only weakly connected due to lack of cross-border infrastructure. Macroeconomic management has been deficient in several member states. Given these circumstances it comes as no surprise that ECCAS has not made progress towards its integration objectives. Notwithstanding this lack of progress, Angola has recently reiterated its interest, indicating that ECCAS has a certain appeal as a political forum for the sub-region. In fact, Angola was a participant in the original discussions leading to the creation of ECCAS, but there was no follow-up because of its civil war.

Central African Economic and Monetary Union (CAEMU)

Creation: The Treaty to establish the Central African Economic and Monetary Union (CAEMU), better known in French as the 'Communauté Economique et Monétaire de l'Afrique Centrale' (CEMAC) was signed in 1994.

Membership: Cameroon, Central African Republic, Chad, Congo (Brazzaville), Equatorial Guinea and Gabon. All members are also members of ECCAS.

Background and main objectives

CEMAC replaced the Central African Economic and Customs Union, known in French as the 'Union Douanière et Economique de l'Afrique Centrale' (UDEAC), which was created in 1964. UDEAC belonged to the early-wave African integration initiatives. Equatorial Guinea became a member in 1983. All the members of UDEAC are also in the CFA franc zone. The UDEAC states are all small economies and their combined GNP and population amount only to US$ 17 billion and 28 million respectively. Cameroon dominates the grouping, accounting for about half of its GNP and population. The economies of Gabon, Congo, Cameroon (to a lesser extent) and Equatorial Guinea (increasingly) are dominated by oil exports.

While the CEMAC Treaty was signed in 1994, around the same time as the UEMOA Treaty, its full ratification and entry into force was delayed until 1999. The objectives of CEMAC are comparable to those of UEMOA; in other words, the creation of a fully-fledged economic and monetary union. The monetary union already exists in the context of the CFA franc zone.

Main achievements and assessment

Despite a number of favourable conditions for integration, such as the monetary union and the common history of its member states, achievements have been very limited. UDEAC did not develop into a real Customs Union. A complex system of border taxes, rules of origin and transit regulations prevented this. Enterprises were admitted to a system of reduced intra-regional taxation on a case-by-case basis. Unlike in the case of CEAO there was no meaningful increase in intra-regional trade. Cameroon developed some manufacturing capacity, but its exports to partner countries did not increase significantly. Economic development in Gabon and Congo was dominated by oil exports, which financed infrastructure and some import-substituting industries. Recurrent internal problems, especially in the landlocked member states of Chad and the Central African Republic, hampered progress.

In 1991, a renewed effort was made to achieve a Common External Tariff. With involvement of the Bretton Woods institutions, agreement was reached on the simplification of the customs regime. Products were classified in four categories with tariff rates ranging from 5 to 50 per cent. Around the same time a new system for transit traffic was elaborated.

The region was affected by the devaluation of the CFA franc in 1994, but the UDEAC member states did not show a growth response comparable to the UEMOA members. Likely explanations include the decline in oil prices since 1995 and civil unrest in some member states. Again in contrast to the UEMOA case, the signing of the CEMAC Treaty has not resulted in a renewed integration effort.

Common Market for Eastern and Southern Africa (COMESA)

Creation: The Treaty establishing COMESA was signed in 1993.

Membership: Angola, Burundi, Comoros, Djibouti, Democratic Republic Congo (1995), Egypt (1998), Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Namibia, Rwanda, Seychelles (1997), Sudan, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.

Background and main objectives

COMESA is the successor to the Preferential Trade Area for Eastern and Southern Africa (PTA) whose Treaty was signed in 1981. The COMESA Treaty of 1993 broadened and deepened the integration foreseen under the PTA. There has been full continuity between PTA and COMESA activities. COMESA is seen as one of the main building-blocks of the African Economic Community. In contrast to ECOWAS, for example, both PTA and COMESA have paid a lot of attention to bringing in new member states. The likely explanation is its rivalry with SADC (see below). It is sometimes difficult to know how many member states COMESA has. One of the original PTA countries has not (yet) signed the COMESA

Treaty (Somalia). Some signatories have given notice to withdraw (Tanzania) or have effectively done so (Lesotho and Mozambique). The most recent new member state is Egypt. One of Egypt's motivations appears to be its adherence to the African Economic Community, which implies the requirement to take part in one of the sub-regional organizations. Egypt may also wish to benefit from tariff-free access to the COMESA market.

Of the regional groupings in Africa, COMESA is the largest in terms of population (around 345 million, including Egypt) and number of member states (presently 21). But the large number of member states also implies certain limitations. Within COMESA, divergences of various kinds are extreme. Per capita GNP ranges from US$ 3700 in Mauritius and US$ 6800 in the Seychelles to less than US$ 100 in Mozambique and US$ 170 in Tanzania. Population ranges from 58 million in Ethiopia to only 80 000 in Seychelles. In other areas, such as culture and the political system, divergences are also large. Many countries in the region have been or still are confronted by internal conflicts. Recently, there has been an increase in difficulties and conflicts involving several member states in the Great Lakes and Horn of Africa areas. Clearly, the circumstances do not point to rapid progress towards integration at the COMESA-wide level. The COMESA Treaty acknowledged the difficulties of countries with very different circumstances moving ahead together, by allowing multiple speed and variable geometry. Hence, progress is bound to take place at the level of sub-groups.

The agenda foreseen in the COMESA Treaty calls not only for a Customs Union and a Common Market, but also for an economic and monetary union. In addition, the Treaty stipulates collaboration in a large number of sectors and themes. The targets for the trade liberalization, which have been postponed, are currently to achieve intra-regional free trade during the year 2000 and a Common External Tariff in 2004. The CET foresees three non-zero tariff rates with a maximum of 30 per cent. The planned rates are 0, 5, 15 and 30 per cent respectively on investment goods, raw materials, intermediate goods and final products. Other key objectives in the Treaty are trade facilitation and free movement of persons. In the monetary field, the PTA Clearing House was established in 1984.

Main achievements and assessment

It is clear from the brief description of the context that rapid progress towards regional integration at the COMESA-wide level cannot be expected. Notwithstanding these unfavourable factors, there has been significant progress in a number of areas. The main advance has been on trade facilitation. Implementation has proceeded well in matters such as harmonization of road transit charges, simplification of customs and transit documentation, insurance coverage and the trade information network. COMESA has also worked out a customs bond guarantee scheme, which would cut the cost of transit traffic, but implementation is delayed.

Satisfactory progress has been made in the area of trade liberalization. Most member states apply significant tariff preferences (between 60 and 90 per cent) on intra-regional trade. Some member states have rapidly increased their regional exports (for example, Kenya, Zimbabwe and Mauritius). There has been some progress towards the planned CET, but the 2004 objective will be difficult to reach. In fact, progress towards the CET has been mostly an aspect of unilateral trade liberalization of the kind promoted under structural adjustment programmes. Progress on trade liberalization was also part of the move towards a *Harmonized External Tariff (HET)* agreed by the countries that participate in the *Cross-Border Initiative* to facilitate trade, investment and payments in Eastern and Southern Africa. This initiative is co-sponsored by the African Development Bank, the European Commission, the IMF and the World Bank and has contributed to the consistency between national adjustment programmes and regional integration policies (regional dimension of adjustment). The HET implies three non-zero tariff *bands* and does not require identical tariffs, leaving countries free to take account of fiscal considerations. It is generally recognized that fiscal problems have hampered trade liberalization in other parts of Africa (for example, ECOWAS). Compensation mechanisms to redistribute fiscal revenues have typically not been successful. The COMESA Secretariat has been closely involved in this initiative, which also addresses the lack of capacity to formulate and implement trade and integration policies.

Like most other African arrangements, COMESA started its trade liberalization with very restrictive rules of origin. Countries had to negotiate which goods would be put on a *common list*, for which preferences would be granted. Agreeing on such a common list turned out to be a slow and ineffective process. The common list approach was abolished in 1994. The current rules of origin of COMESA are reasonably straightforward (see note 37 in Chapter 4). However, their practical application continues to pose problems, thereby diminishing the benefits of regional trade liberalization.

In the monetary cooperation area, the COMESA Clearing House, in contrast to its West African counterpart, functioned quite well until the early 1990s. Around that time, the clearing volume started to decline. Because many countries achieved current-account currency convertibility, the demand for clearing services diminished. The Clearing House is being transformed into an agency to improve financial services for cross-border economic activities. There has been no progress yet towards the objective of monetary union. However, the objectives of the monetary harmonization programme have been scaled down so that they are more realistic.

Southern African Development Community (SADC)

Creation: The Treaty establishing SADC was signed in 1992 in Windhoek, Namibia.

Membership: Angola, Botswana, Lesotho, Malawi, Mauritius (1995), Mozambique, Namibia, Seychelles (1997), South Africa (1994), Swaziland, Tanzania, Democratic Republic Congo (1997), Zambia and Zimbabwe.

Background and main objectives

SADC's predecessor, the Southern African Development Coordination Conference (SADCC) was founded in 1981, shortly after Zimbabwe's independence. SADCC's origin is the movement of the front-line states and its main objective was to reduce economic dependence on South Africa. Until the Windhoek Treaty in 1992, SADCC's objectives related to functional cooperation, focusing on areas such as: transport, food security, human resource development, energy and industry. In the area of transport, SADCC promoted investment in the corridors connecting landlocked countries to the sea without passing through South Africa.

The transformation of SADCC into SADC coincided with a reorientation of objectives in the direction of regional economic integration. Following its democratic election in 1994, South Africa joined SADC.

A majority of the SADC member states are also members of COMESA. The original exception was Botswana that apparently never considered PTA or COMESA membership. This may be related to the fact that the SADC Secretariat is located in Gaborone, Botswana. South Africa also did not join COMESA and more recently Lesotho and Mozambique pulled out, while Tanzania indicated its wish to leave. Following South Africa, Mauritius joined SADC in 1995. With 10 out of 14 SADC members also in COMESA, there is a very substantial overlap. This would not pose many problems if the subjects handled by both organizations were different, or in the event that they deal with similar subjects, that the objectives were at least consistent. But SADC's policy orientation after 1992 moved straight into COMESA's economic integration mandate. This is probably the main reason for some rivalry between the two organizations. In 1996, SADC approved its *Trade Protocol* whose main aim is to achieve free trade among SADC members over a period of eight years following ratification. For the many SADC members that also subscribe to COMESA, it is clearly not possible to implement the CET foreseen under COMESA together with the FTA under SADC. Moreover, the Trade Protocol also contains certain regulations on issues such as transit, trade defence measures and rules of origin that deviate from the COMESA trade regime.

The SADC Secretariat has only a general coordinating role. Each member state is responsible for one or more specific sectors or themes. There are *sector coordinating units,* which are usually part of the relevant ministry in the host country. For example, Zimbabwe is responsible for food security and the sector coordinating unit is in the Ministry of Agriculture. This set-up dates from the time of SADCC where functional cooperation was the main task. There are also sectors with a more horizontal responsibility, such as the finance and investment sector that is handled by South Africa.

Right from its origin, SADCC had an important political dimension, which was continued by SADC. South Africa's decision to join not only drastically increased its economic size, but also enhanced SADC's prominence as a political and security forum.

Main achievements and assessment

SADC is one of the best-known regional organizations in Africa. Its role in promoting and coordinating functional cooperation, especially in transport and food security, is generally recognized and appreciated. Its role as a political forum is also recognized. With South Africa taking part since 1994, SADC is the largest economic bloc in Africa, with a GNP of around US$ 175 billion. But it should be recalled that South Africa alone represents 75 per cent of this figure. Accordingly, the economic dominance of South Africa within SADC is even more pronounced than the weight of Nigeria in ECOWAS or Cameroon in CEMAC. Apart from South Africa, all SADC members are in fact small and very small economies.

As an organization for regional economic integration, SADC still has to prove its value. Since the signing of the Trade Protocol in 1996 progress has been slow. Three years after its signing, the Protocol has not yet been ratified by the required two-thirds of the member states for entering into force. Negotiations about practical implementation of the Protocol are tedious and frequently oppose some of the old SADC members to South Africa. A source of contention is the fact that several member states, including Malawi and Zambia, have implemented rapid *unilateral* trade liberalization in the context of structural adjustment programmes. In combination with the normalization of trade with South Africa, this has led to large and rising bilateral trade deficits between such member states and South Africa. Countries such as Malawi, Zambia and Zimbabwe have not been able to compensate for this through increased exports to the rest of the world. South Africa has not yet implemented much *additional* preferential trade liberalization, even though it is implementing the 'across the board' tariff reductions it agreed to under the Uruguay Round.[3] Partly stimulated by its growing regional trade surplus, South Africa has become an important investor in the SADC region. This should be to the advantage of the receiving countries at least in the medium and long run. But in the short term, these investments may force closure of companies previously sheltered by protection. As a result, there is a significant adjustment cost for these countries. To complicate matters further and underline the policy dilemmas, all this is taking place when unemployment in South Africa is increasing.

The fact that SADC is moving slowly on its integration agenda should not be considered as negative. The failure of virtually all other African integration arrangements to implement their agreed objectives suggests that, in fact, more preparation and longer transition periods may be desirable. Because of its weight, South Africa will determine the pace of integration in SADC. Complicating factors for South Africa, such as its negotiation on an FTA with the EU and the revision of the SACU regime (see below) may help explain why movement at the SADC level is slow.

Southern African Customs Union (SACU)

Creation: SACU was formed in 1910. The agreement was renegotiated in 1969 and again in 1990.

Membership: Botswana, Lesotho, Namibia, South Africa and Swaziland.

Background and main objectives

SACU is, in many respects, different from the other groupings in Africa. It predates all the other arrangements and is, in fact, *more* than its name would indicate. It is a Customs Union with also a pooling of excise duties and with reasonably free movement of labour and capital. On the other hand, there is no SACU Secretariat. The practical operation of the system is mostly handled by South Africa. At independence in 1990, Namibia chose to remain in SACU. Botswana, Lesotho, Namibia and Swaziland, referred to as the *BLNS countries,* represent only 15 per cent of the population and less than 10 per cent of the GNP of SACU. All the SACU member states are also members of SADC.

Customs and excise duties are pooled and shared according to an agreed formula. For South Africa, fund transfers to the BLNS are compensated for by the fact that the CET mostly protects South African industry that also supplies the BLNS. For Lesotho and Swaziland almost half of government revenue comes from the common pool. The shares for Namibia and Botswana are much lower, but remain sizeable at 30 per cent and 20 per cent respectively. During the apartheid period until 1994, the BLNS, especially Swaziland received inward investment because of the sanctions against South Africa.

All SACU members apart from Botswana belong to the Common Monetary Area (CMA) known also as the rand zone.

Main achievements and assessment

SACU's main achievement is that it clearly works to the benefit of its five member states. SACU constitutes an integrated economic area, with all the benefits that this implies in terms of scale and competitiveness. Furthermore, the CMA is a stable monetary zone. For the BLNS countries, a special advantage of SACU is that it is a convenient system for the collection of government revenue. For South Africa, an important benefit is the guaranteed BLNS market for consumer goods.

Despite the benefits of SACU, there has been increasing dissatisfaction with the system. A widespread view in South Africa is that the payments from the common pool to the BLNS are too high. At the same time, the size of the common pool is diminishing because of the implementation of SACU's tariff dismantling offer under the Uruguay Round. For their part, the BLNS want a greater role in the management of the system and would like to transform SACU into an institution in which they have a real say. Discussions on the reform of SACU have been ongoing since 1994.

Another contentious issue is the planned Free Trade Area between the European Union and South Africa. The BLNS did not participate in this negotiation, and fear negative effects on their economy. The EU–South Africa FTA will reduce the size of the common revenue pool. It will expose the BLNS countries to increased competition, not only on the South African market where EU products will become cheaper, but also on the EU market where they would lose a preferential advantage over South Africa. However, some of the anticipated dynamic effects are positive for the BLNS and could more than compensate for the negative effects.

Despite divergent views among the BLNS and South Africa about some aspects of SACU, it is likely that all its member states derive significant benefits. The future success of SACU will be dominated by what happens with the South African economy. SACU could play an increasing role as the anchor economic zone for Southern Africa.

East African Cooperation (EAC)

Creation: East African Cooperation was revived in 1995 and builds on the legacy of the East African Community, which was created in 1965 and disbanded in 1977.

Membership: Kenya, Uganda and Tanzania.

Background and main objectives

The East African Community was preceded during the colonial era by a Customs Union between Kenya and Uganda to which Tanganyika was later added. Created in 1965, the Community was a clear example of the first-wave South–South regional integration. In addition to being a Customs Union, the East African Community constituted the umbrella for several joint companies of the member states such as East African Railways, the East African Shipping Company and the East African Development Bank.

Despite their common history and proximity, divergences in economic development strategy increased quickly during the post-independence period. This added to the tensions that were caused by the different levels of industrialization inherited by the newly independent states. Industrial capacity was concentrated in Kenya. There was some capacity in Uganda, but almost nothing in Tanzania. These unbalanced initial conditions strongly affected the trade patterns between the three countries. Tanzania considered that the result was an unfair distribution of the gains from the Community, with Kenya benefiting most. Tanzania believed that a more autonomous development strategy, involving import substitution and protection, would be more beneficial. At a more general level, Tanzania started its experiment of 'African socialism', which, in trade policy, implied high protection and extensive controls. The Tanzania experiment was widely supported by the donor community including the World Bank. Political problems added to the economic divergences, leading to the break-up of the East African Community in 1977.

During the second half of the 1980s and the 1990s, *de facto* convergence of the economic policies in the three countries increased. They all implemented structural adjustment programmes and subscribed to the integration objectives of the PTA and COMESA. The end of the civil war in Uganda in 1986 marked the beginning of an economic revival. Being a landlocked country, it needs regional cooperation in order to sustain its economic growth. Uganda strongly favoured a revival of East African Cooperation. Kenya and, to a lesser extent, Tanzania benefited from the economic growth in Uganda. Kenya again became one of the main suppliers for Uganda in addition to its vital transit role. In all three countries the revival of cooperation has been wholeheartedly promoted by the private sector.

In 1993, the three countries agreed on the establishment of the Permanent Tripartite Commission for East African Cooperation. The Secretariat of this Commission was installed in Arusha, Tanzania, in 1996. A draft Treaty was prepared during 1998. Its signature was planned by the end of 1999. It is interesting to observe that before putting this draft into the government decision-making mechanisms, it was widely discussed among academics, private operators and civil society in general. This contrasts with most other agreements and treaties in Africa which were decided without much public debate and scrutiny.

Main achievements and assessment

It is too early to discuss and assess the effects of the revival of East African Cooperation. Clearly, the new East African Cooperation differs from the old one in many respects. All three economies have significantly liberalized trade and payments. Unlike in the past, they all recognize the importance of the private sector. The new cooperation has led to progress in some concrete matters such as convertibility of national currencies, agreements to avoid double taxation and simplification of border formalities. The Commission for East African Cooperation is preparing actions in a large number of areas.

The draft Treaty envisages a deepening of East African integration. Such deepening is compatible with the more shallow integration at the level of COMESA of which all three countries are members. However, for Tanzania, there is a problem because it is also a member of SADC. Moreover, there is a fear in Tanzania of a repetition of the experience with the old East African Community, which was considered to be unfair to Tanzania.

The success of the revival of East African Cooperation will not only depend on its economic decisions, but also very much on political and security factors. The countries are affected by the problems in the neighbouring Great Lakes states and in Southern Sudan. Rwanda's application to join East African Cooperation, supported by Uganda, may change the nature of the cooperation arrangement. It is hard to predict whether this will strengthen or weaken East African Cooperation.

Latin America and the Caribbean

For a long time regional integration has been high on the agenda for the Latin American and Caribbean countries. Within the developing world, these countries were the most active in promoting the first wave of regional integration. This led, in 1960, to the creation of the Latin American Free Trade Association (LAFTA) comprising all the independent states in South America plus Mexico. The Central American Common Market (CACM) was founded in the same year. The intellectual basis for economic integration in the region was provided by the Economic Commission for Latin America. Under the leadership of Raoul Prebish, regional integration was advocated as the way towards successful industrialization via import substitution. The Andean Pact created in 1969 and the Caribbean Community (CARICOM) in 1973 completed the picture.

The regional integration initiatives of the first wave did not live up to the expectations held at the time of their creation. In 1980, LAFTA was transformed into the Latin American Integration Association (LAIA), better known by its Spanish abbreviation: ALADI. But ALADI did not represent a fundamental change. The debt crisis which confronted many countries was particulary severe during the first half of the 1980s. As in the African situation, economic difficulties interacted with political tensions, internal strife and sometimes conflict between different countries. Gradually, inward-looking economic policies were replaced by more outward orientation. In a parallel development, authoritarian rule was replaced by democratically elected governments. The 'lost decade' of the 1980s was followed by a return of economic growth during the 1990s.

The reorientation of economic policies and the political system was accompanied by a renewed regional integration drive. Two fundamental developments were the creation, in 1991, of the Southern Cone Common Market, better known as MERCOSUR and the participation of Mexico in NAFTA in 1994. Another striking event was the revitalization of the idea of hemispheric integration with the planned Free Trade Area of the Americas (FTAA).[4]

Central American Common Market (CACM)

Creation: The CACM Treaty was signed in 1960.

Membership: Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua.

Background and main objectives

CACM is a grouping of small economies. Regional integration is seen as a way to overcome the limitations of the small economic size. Following its creation, CACM made rapid progress in terms of tariff dismantling and movement towards a Common External Tariff (CET). Because of the import substitution objective, the CET rates were quite high, ranging from 11 per cent for capital goods to

106 per cent for consumer goods. Agriculture was largely excluded (as in many other integration agreements). This penalized Honduras. Still, intra-regional trade as a share of total trade went up rapidly and reached almost 27 per cent in 1970, which is a very high level, taking into account the limited overall size of the grouping: population of 31 million and GNP of US$ 41 billion (in 1996).

After the initial success, the integration process came to a halt and even reversed as a result of political and economic crises (including civil war and even armed conflict between some of the member states). Borders between some member states were closed, and there was a general increase in non-tariff barriers. The Clearing House and the Monetary Stabilization Fund that had been installed ceased to function. The share of intra-regional trade declined to around 15 per cent in 1989.

From the end of the 1980s onwards, following improved security and political stability, the Central American integration process was revitalized. Some of the member states implemented significant unilateral trade liberalization. Costa Rica went furthest in this direction. In 1991, Panama started collaborating with CACM. A new target structure for the CET was agreed in 1992 with rates between 5 and 20 per cent, much lower than the original rates. Costa Rica did not subscribe to these rates because its unilateral reductions had resulted in even lower values. In 1996, the target rates for the CET to be achieved by the year 2000 were lowered further to zero per cent for capital goods and 15 per cent for consumer goods.

Main achievements and assessment

The revitalization of the CACM can be considered as an example of the second wave of regional integration initiatives. It builds on the unilateral liberalization of most of the member states and is generally outward-oriented. The new approach has brought some success. From its low level in 1989, the share of intra-CACM trade in total trade has exceeded 20 per cent since 1994. Still, the transformation from inward-looking policies towards outward orientation is not yet completed. The weakest economies, Honduras and Nicaragua, have not yet seen much improvement.

Another aspect is that CACM is increasingly acting as a unit for the economic relations between the Central American states and the other countries and regional blocs in the Western Hemisphere. Relations with CARICOM were established in 1992, and an agreement was reached on free trade with the Dominican Republic in 1998. In the past, bilateral negotiations involving individual CACM member states were very common. There are clear advantages if CACM enters into deals as a bloc.

Andean Community

Creation: The Andean Pact Treaty was signed in 1969. In 1996 the name was changed to Andean Community.

Membership: Bolivia, Colombia, Ecuador, Peru and Venezuela.

Background and main objectives

The Andean Pact was set up in 1969 with the Cartagena Agreement as a subgroup of LAFTA to deepen integration. The creation of the Andean Pact was a reaction of the smaller countries to the larger ones that dominated LAFTA.

Venezuela joined the group in 1973 and Chile left in 1976. Among the integration groupings in the Americas, the Andean Pact has developed the most elaborate institutional structure.

The Andean Pact has made little progress towards its objective of a Customs Union. No agreement could be reached during the 1970s and most of the 1980s. Trade liberalization speeded up only at the time of the second wave of regional integration around the beginning of the 1990s. But even at that time, it was not possible to overcome divergent views about the tariff level. Bolivia and Peru preferred a lower level than Colombia and Venezuela. In 1992, Peru unilaterally decided to suspend preferential treatment to imports from within the zone.

The Cartagena agreement included the objective of harmonious regional development of industry. An attempt was made to install a joint industrial programming mechanism that provided for an allocation of specific industries to specific member states. These industries would be allowed to supply the protected regional market. This system of regional import substitution behind high tariffs did not work in practice. In 1989, the joint industrial programming approach was replaced by a more outward-oriented policy.

In 1996, the change of the name to Andean Community coincided with a second revitalization, including an institutional reform. Targets for achieving a Customs Union were again set. A Common External Tariff comprising four tariff levels: 5, 10, 15 and 20 per cent should be achieved by 2005. Trade in services will also be liberalized.

Main achievements and assessment

Despite a number of favourable factors, such as a common history and culture, and a shared dissatisfaction about the wider integration process advocated by ALADI, progress towards market integration has been very slow. Targets frequently had to be revised and it has generally been difficult to reconcile the divergent views of the member states. Political difficulties both within and between member states are a likely explanation. The reintegration of Peru into the preferential system is going slowly and the plan is for it to be completed fully only in 2005.

Nevertheless, the second revitalization has a good chance of being more successful than earlier efforts. The formation of MERCOSUR and NAFTA, and the hemispheric discussions on the FTAA have acted as a catalyst for Andean integration. On the other hand, the fact that Bolivia made an agreement for free trade with MERCOSUR illustrates that cohesion is still not yet very strong. However, a positive view of this agreement is that it could pave the way for an FTA between the Andean Community, MERCOSUR and Chile.

Caribbean Community

Creation: The Treaty of Chaguaramas establishing CARICOM was signed in 1973.

Membership: Bahamas, Barbados, Belize, Guyana, Haiti (1997), Jamaica, Trinidad & Tobago, Suriname (1995), and the OECS members (see below).

Background and main objectives

CARICOM was preceded by the Caribbean Free Trade Association (CARIFTA), established in 1966 and modelled largely on the European Free Trade Association.

CARIFTA's Secretariat was based in Guyana, which had pushed for its creation. During the early 1970s, it was decided to broaden the integration initiative beyond trade matters, and this led to the creation of CARICOM in 1973. From the beginning, a distinction was made between *more* developed member states and *less* developed member states. The more developed countries are the relatively larger ones: Barbados, Jamaica, Trinidad and Tobago and Guyana. The less developed countries are the OECS member states plus Belize. The latter receive special and differential treatment in the implementation of integration policies. All the member states of CARICOM are small economies. In 1994, the total population was only 6 million and overall GDP amounted to US$ 17 billion. With the recent accession of Suriname and, especially, Haiti, the population more than doubled to over 13 million, although the GNP went up by less than US$ 3 billion.

The main objectives of CARICOM are economic integration through the creation of a 'single market and economy', functional cooperation in specific sectors and coordination of foreign policies.

The Caribbean Development Bank (CDB) is an associate institution that was established in 1969. It is particularly geared to financing infrastructure in the less developed member states of CARICOM. Among comparable development finance institutions, the CDB has built up a good reputation.

Main achievements and assessment

Progress towards the CARICOM 'single market and economy' has been much slower than anticipated. The target dates for achieving internal trade liberalization and a Common External Tariff have been postponed several times. The target rates have been lowered in line with what has happened elsewhere. It has been difficult to reconcile the interests of the less and more developed member states. The former prefer a higher maximum tariff rate for revenue purposes and, at the same time, a lower minimum rate for import substitution (to provide cheap inputs). The goal, set in 1992, was to achieve minimum and maximum rates for industrial goods between 5 and 20 per cent by the end of 1998. The less developed members are allowed to apply a zero minimum rate. For agricultural products, the maximum rate is 40 per cent. However, there are several member states that apply other duties and charges and non-tariff barriers in addition to the CET.

Intra-CARICOM exports as a percentage of total exports went up from around 5 per cent in the early 1980s to about 13 per cent around the mid-1990s. Given the small size of the CARICOM economies, this is a very high share. However, intra-CARICOM trade is very much dominated by oil exports from Trinidad & Tobago. The Caribbean Common Market does not (yet) include the Bahamas and Haiti. In 1999 an agreement was reached about gradually including Haiti.

CARICOM has produced a number of positive results in the area of functional cooperation such as the University of the West Indies, the Caribbean Export Development Agency and the Meteorology Institute.

There has also been progress towards the coordination of foreign policy. Increasingly, the CARICOM member states have been speaking with one voice in international forums. Significant developments include the establishment of formal relations with the Central American Common Market in 1992. In addition CARICOM signed preferential trading agreements with Venezuela (in 1992) and Colombia (in 1994). In 1996, a *joint regional negotiation machinery* was created to increase capacity to participate in various trade arrangements. More recently, in 1998, agreement was reached in principle to liberalize trade between CARICOM and the Dominican Republic. However, the negotiations on practical implementation are moving slowly. The CARICOM was also instrumental in the launching of the Association of Caribbean States (ACS) in 1994. Trinidad & Tobago will host the Secretariat of the ACS (see note 4).

The CARICOM faces a number of major challenges. CARICOM's preferences in the markets of industrial countries have been eroded because of multilateral liberalization. The creation of NAFTA has aggravated this because of increased competition from Mexico in the United States and Canada. Future ACP–EU cooperation could entail the creation of a Free Trade Area between CARICOM and the EU. At the same time negotiations are under way towards the Free Trade Area of the Americas. It would be in the best long-term interest of CARICOM members to move in parallel towards free trade within the Western Hemisphere and with Europe. However, the adjustment cost at the level of specific industries and at the level of the government budget will be large. The challenge for the CARICOM region is to participate in the wider integration process, while at the same time strengthening its position in activities with a comparative advantage such as services. The OECS subgroup faces additional challenges (see separate section).

Despite the fact that many targets have not been met within the agreed deadlines, the achievements of CARICOM are sizeable. The organization also contributed towards raising the profile of its member states on the international scene.

Organization of Eastern Caribbean States (OECS)

Creation: The Treaty establishing OECS was signed in 1981.

Membership: Antigua & Barbuda, Dominica, Grenada, Montserrat, Saint Kitts & Nevis, Saint Lucia, and Saint Vincent & the Grenadines.

Background and main objectives

The OECS groups the very small English-speaking economies of the Eastern Caribbean. Its central secretariat is in Saint Lucia, while its economic affairs secretariat is based in Antigua. The combined land area and population are only 3000 square kilometres and half a million respectively. The OECS GNP is around US$ 2 billion. All the OECS members are also members of CARICOM, so the OECS can be considered as an example of variable geometry. The OECS builds on cooperation arrangements that were already set up during the colonial era. Montserrat is an overseas territory of the United Kingdom.

The main OECS objectives are market liberalization and functional cooperation. An important aspect of cooperation has been the establishment of the Eastern Caribbean Central Bank in 1983, which maintains a common currency, the Eastern Caribbean dollar. Hence, the OECS constitutes a monetary union.

Main achievements and assessment

Despite the disadvantages resulting from their small economic scale, the OECS countries have been successful in maintaining a reasonable growth rate. With an average GNP per capita above US$ 3000, the OECS is in the category of upper middle-income countries.

The OECS members have obtained good results in the area of functional co-operation. Examples include investment promotion, civil aviation and fisheries. They have also benefited much from relatively generous flows of concessional funds and preferential arrangements with industrial countries.

The dependence of the OECS countries on preferential arrangements such as the EU's banana regime illustrates their vulnerability. The banana industry has become established as a viable and regular source of revenue for small independent farmers that previously were plantation workers or subsistence peasants. In some OECS countries, the banana sector employs around a third of the labour force. The EU's preferential banana regime has been rejected under the WTO dispute settlement mechanism, following complaints from the United States (on behalf of large banana trading companies) and a number of Latin American banana producers. It is recognized that economic diversification is vital, but the extreme dependence on EU commodity preferences leads to a sizeable adjustment cost.

Southern Cone Common Market (MERCOSUR)

Creation: The MERCOSUR Treaty was signed in 1991.

Membership: Argentina, Brazil, Paraguay and Uruguay.

Background and main objectives

The origin of MERCOSUR can be traced to the gradual coming together, during the 1980s, of the two main economic powers in South America, Argentina and Brazil. This *rapprochement* took place against the background of political changes and economic policy reform leading to a more outward orientation in both countries. Two smaller economies in the region, Paraguay and Uruguay, asked to participate in this process and the four countries signed the Treaty of Asunción establishing MERCOSUR in 1991. Its secretariat is located in Montevideo, Uruguay. In 1996, the population of MERCOSUR was 205 million and its GNP reached US$ 1030 billion.

MERCOSUR is an ambitious integration initiative, partly inspired by the EU. Its main objectives include free movement of goods, services and production factors between the member states, and the adoption of a Common External Tariff towards third countries. Other objectives are the coordination of macroeconomic policies and functional cooperation in matters such as transport, communication and energy. In the area of trade liberalization MERCOSUR adopted a very different approach from that of ALADI. Rather than undertaking laborious product-by-product negotiations, MERCOSUR agreed on automatic across-the-board tariff reductions and elimination of non-tariff barriers.

Main achievements and assessment

Following its creation, MERCOSUR quickly captured the headlines as a new type of integration organization of developing countries. Even though the timetable for tariff dismantling was ambitious, progress was generally on schedule during the first five years of implementation. The share of intra-regional trade in total trade went up rapidly from 9 per cent in 1990 to 22 per cent in 1996.

By 1995, a Customs Union, albeit an imperfect one, was achieved. The Common External Tariff rates are between zero and 20 per cent, with an average of

12 per cent. However, temporary product exclusions are allowed. Paraguay has the largest number of exclusions, but the other countries also maintain sizeable exclusions. In addition, automotive products and sugar are subject to a special regime. At the end of 1997, Brazil and Argentina adopted an increase of 3 per cent in the maximum level of the CET. Paraguay and Uruguay reluctantly agreed, but were allowed to exempt certain products from the increase. In 1998, in the wake of the Asian financial crisis, intra-MERCOSUR trade fell for the first time in many years. At the beginning of 1999, Brazil devalued its currency. This led to trade tensions between Argentina and Brazil and some unilateral measures were taken. However, there has not been any serious backtracking. Rather, ideas for moving towards monetary and fiscal harmonization were put on the table.

In 1996, MERCOSUR signed agreements to gradually establish free trade with Chile and Bolivia. These agreements demonstrate the attraction of MERCOSUR as a trading bloc. Negotiations are taking place for a wider agreement between MERCOSUR and the Andean Pact. Discussions on trade liberalization between the EU and MERCOSUR have also started.

Asia and the Pacific

In contrast to Africa, Latin America and the Caribbean, regional integration has generally been a less prominent issue in Asia and the Pacific. The best-known regional organization is the Association of South East Asian Nations (ASEAN) that was founded as far back as 1967. ASEAN's original objectives were mostly political, regional integration only becoming an important agenda item at the beginning of the 1990s. It is fair to say that the first wave of *economic* integration initiatives hardly touched Asia and the Pacific. During the 1990s, interest in regional integration has been increasing in the Pacific.

Association of South East Asian Nations (ASEAN)

Creation: The Bangkok Declaration was signed in 1967.

Membership: Brunei (1984), Indonesia, Laos (1997), Malaysia, Myanmar (1997), Philippines, Singapore, Thailand and Vietnam (1996).

Background and main objectives

The origin of ASEAN, during the 1960s, was the desire to set up closer political and security cooperation in the South East Asian sub-region. The five original members that signed the Bangkok Declaration in 1967 were Indonesia, Malaysia, the Philippines, Thailand and Singapore. Brunei joined in 1984, Vietnam in 1995 and the most recent new members, Laos and Myanmar, were admitted in 1997. Cambodia's admission was foreseen for the same year, but was postponed because of renewed political problems and unrest. The founding member states are all large economies. Even though the population of Singapore is only 3 million, it is not a small economy because it has such a high per capita income. The size of its economy is US$ 90 billion. Brunei's population is very small, around 300 000. However, because of its high oil revenue, it cannot be considered to be in the category of small developing economies. On the other hand, Laos and Myanmar are small developing economies, although economic data for Myanmar are not reliable.

Following its creation, ASEAN served, in the first place, as a political discussion and collaboration forum. In addition to the promotion of peace and stability in the sub-region, ASEAN's objectives include functional and economic cooperation. Functional cooperation covers areas such as social development, culture, science and technology, the environment, drugs and narcotics. The most important elements of economic cooperation are trade liberalization, industrial development, finance and banking, and investment. The initial approach towards trade liberalization did not lead to much progress. Lengthy negotiations led to limited reciprocal opening of markets. Trade liberalization was intensified only in 1992, with the decision to establish the ASEAN Free Trade Area (AFTA) over a period of 15 years. The instrument to establish AFTA is the Agreement on the Common Effective Preferential Tariff (CEPT). During the 1990s, new themes have been added to the economic cooperation agenda, including tourism, services and intellectual property.

Various schemes of industrial cooperation have been set up during the 1970s and the first half of the 1980s. In 1976 ASEAN Industrial Projects (AIPs) began establishing large-scale industrial projects. Another scheme is the ASEAN Industrial Complementations (AICs), which was introduced to encourage specialization and trade in the automotive sector. The ASEAN Industrial Joint Venture (AIJV) scheme was designed to encourage greater investment into and within the region. Products of such joint ventures received tariff preferences in the ASEAN countries.

ASEAN has a light institutional structure: a small Secretariat was established only in 1976, in Jakarta, around the time of the first agreement on preferential trading arrangements. In 1992, following the agreement on AFTA and the broadening of functional and economic cooperation, the Secretariat was enlarged. A special unit has been set up to monitor the implementation of AFTA.

Main achievements and assessment

Until the early 1990s, ASEAN's main achievements have been in the domain of political and security dialogue and some aspects of functional and economic cooperation. Gradually, ASEAN has also become an instrument for expressing common positions of its member states in international economic forums. Even in the absence of progress towards economic integration, the fact that ASEAN acted as a bloc has increased the bargaining power of the member states. Most of ASEAN's member states experienced almost two decades of rapid economic growth, until the onset of the crisis in East and South-East Asia in 1997.

The share of intra-ASEAN exports in total exports decreased during the 1960s to around 15 per cent in 1970. The share gradually went up to around 19 per cent in 1990 and further to 22 per cent in 1995. A large part of ASEAN's intra-trade involves the hub economy, Singapore, and reflects networks among businesspeople of Chinese background.

In line with experience in Latin America, ASEAN's industrial cooperation schemes are not considered successful. It was not possible to strike a balance between diverse national public and private sector interests.

ASEAN's early trade liberalization initiatives did not lead to many results. This was due to a slow product-by-product approach, national safeguards and restrictive rules of origin (at least 50 per cent of the value-added must be from within the region). The approach initiated with the AFTA agreement in 1992 is much more general and automatic. The original target period was shortened from 15 to 10 years. The ASEAN Free Trade Area should be achieved by the year

2003. The origin rules have been somewhat relaxed in comparison to the earlier schemes.

AFTA will not lead to complete free trade within the sub-region. Each country must divide its tariff lines into four categories: inclusion list, temporary exclusion list, sensitive list and general exception list. For the products in the inclusion list, tariffs must be between zero and 5 per cent by the year 2003. All non-tariff barriers should also be eliminated. The general exceptions list contains products excluded for security reasons. Originally, all unprocessed agricultural products were also excluded. However, negotiations are underway gradually to include such products. At present, 82 per cent of the tariff lines are in the inclusion list, and 16 per cent are in the temporary exclusion list. This leaves only about 2 per cent of products in the sensitive or general exception lists. The newest member states (Laos and Myanmar) have much smaller inclusion lists to facilitate adjustment. Moreover, they receive technical assistance to help them with the implementation of AFTA.

There is no doubt that ASEAN has grown into an important regional integration grouping. In comparison to most groupings in Latin America and Africa, ASEAN has been modest in setting its trade liberalization targets. Following the adoption of the AFTA agreement in 1992, progress in this area has not been fast, but it has been steady. A Customs Union is not envisaged for the moment. Regional industrial policy at the ASEAN level was not a success. It seems that the initially more planned approach has given way to one aimed at harmonizing the regulatory framework for investment in the form of the ASEAN Investment Area (AIA). ASEAN has been successful in representing its member states in international negotiations.

South Asian Association for Regional Cooperation (SAARC)

Creation: The Charter was adopted in 1985.

Membership: Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

Background and main objectives

The proposal for an association of the nations in South Asia was first made by Bangladesh in 1980. Preliminary contacts led to the adoption of a charter on the SAARC in 1985. SAARC groups some of the largest developing countries with some very small ones. The range of population size is from 950 million for India to only 260 000 for the Maldives. Four of the seven member states – Bangladesh, Bhutan, Maldives and Nepal – are least-developed countries.

The SAARC arrangement involves mostly functional cooperation in areas such as agriculture, poverty alleviation and people-to-people contact. Trade and economic cooperation was initiated through the South Asian Preferential Trading Arrangement (SAPTA) that was signed at ministerial level in 1993 and entered into force in 1995. SAPTA foresees the gradual reduction and eventual elimination of tariffs within SAARC. It is seen as a step towards the creation of a South Asian Free Trade Area (SAFTA).

Main achievements and assessment

SAARC's main merit is that it constitutes a forum for exchange of views among countries with a long common history and important common interests, but with often divergent views and in some cases territorial conflicts. History and geography dictate that there should be some measure of regional cooperation. Regular meetings of heads of state and government have been organized. India dominates the sub-region and has borders, often very long, with all the other member states except Sri Lanka and the Maldives, which are island states. Functional cooperation is vital in areas such as forestry and the struggle against erosion, management of inland water and coastal resources and transportation.

It is probably too early to make an assessment, but progress towards trade liberalization has been very timid. Genuine progress would call for an across-the-board approach rather than the proposal by each country of products to be liberalized. The share of intra-regional trade in total trade is small and declined from around 5 per cent during the 1970s to around 3.5 per cent by the early 1990s. In comparison to other developing regions, SAARC member states, with the exception of Sri Lanka, maintain relatively high levels of protection. Regional trade liberalization should move in parallel with liberalization towards the world economy.

Economic Cooperation Organization (ECO)

Creation: The Treaty of Izmir was signed in 1977 and amended in 1990 and 1992.

Membership: Afghanistan, Azerbaijan, Kazakhstan, Kyrgyzstan, Iran, Pakistan, Tajikistan, Turkey, Turkmenistan and Uzbekistan.

Background and main objectives

The present ECO is a successor to a cooperation agreement of 1964 between Iran, Pakistan and Turkey. In 1977, these three countries formalized their cooperation by signing the Treaty of Izmir. Two years later, with the change of regime in Iran, the organization became dormant until it was revived in 1985. In 1992, six newly established states in Central Asia, which emerged from the collapse of the Soviet Union, became members of ECO. Afghanistan also joined the organization at that time, bringing the membership to ten. The three founding members (Iran, Pakistan and Turkey) dominate ECO in terms of population and economic size. Three of the member states, Kyrgyzstan, Tajikistan and Turkmenistan, are small transition economies.

ECO's main objectives are functional cooperation in areas such as agriculture, education, industry, transport, energy and narcotics. Objectives in the trade and customs area are moving towards gradual reduction of trade barriers. A Protocol on an ECO Preferential Tariff Arrangement was signed by the three founding members in 1991.

Main achievements and assessment

ECO can be considered as a reactivation of long-standing historical and trade connections ranging from Central Asia to the Mediterranean. While progress is currently hampered because several member countries are confronted by conflicts, there is undoubtedly potential for increased cooperation and integration. The economic transformation of the Central Asian states towards market orientation will prepare the ground for deeper integration.

Even though ambitious cooperation plans already exist, practical progress has been limited so far. One such plan is for the development of new transport infrastructure more or less along the classic 'silk route'. Such a scheme would create a trade connection to compete with the infrastructure that was put in place in Russia by the former Soviet Union. Progress in the area of trade liberalization, even among the three founding members, is so far very limited.

Gulf Cooperation Council (GCC)

Creation: The Charter constituting the GCC was signed in 1981.

Membership: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates.

Background and main objectives

Regional cooperation between the Arab states in the Gulf region developed rapidly following the first oil price shock in 1974. This led to the creation of the GCC in 1981. The member states are all small in terms of population (except for Saudi Arabia). However, they are upper middle- and high-income economies, deriving the bulk of their revenue from petroleum exports. The objectives of the GCC comprise political, functional and economic cooperation. Functional cooperation covers a broad area including education, culture, health, social affairs, industry, water resources and scientific research. In the economic field, the aims are for deep integration in the form of a common market. The GCC headquarters is located in Saudi Arabia.

Main achievements and assessment

Important progress has been made in areas of functional cooperation. As regards economic integration, the GCC moved quickly to abolish tariffs and other restrictions on their mutual trade in 1983. Agreement has further been reached to move towards a relatively low Common External Tariff, but its implementation has not yet been possible. There has been some progress towards the free movement of workers.

An achievement of the GCC has been to act as a bloc in trade policy matters. An example is the negotiation with the European Union aimed at reaching a Free Trade Area. However, progress has been very slow and no agreement has yet been reached.

South Pacific Forum (SPF)

Creation: The SPF was established in 1971. There is no written charter.

Membership: Australia, Cook Islands, Federated States of Micronesia, Fiji, Kiribati, Marshall Islands, Nauru, New Zealand, Niue, Palau, Papua New Guinea, Samoa, Solomon Islands, Tonga, Tuvalu and Vanuatu.

Background and main objectives

The South Pacific Forum is an informal political grouping of 16 independent and self-governing states in the South Pacific region, constituted in 1971. Its Secretariat is located in Fiji. The 14 developing countries, that is, all member states except Australia and New Zealand, are collectively referred to as the Forum

Island Countries (FIC). They are spread over a vast geographical area. Individual countries constitute archipelagos with large distances between the small islands. The exception is Papua New Guinea, which covers the eastern half of the mini-continent of New Guinea and the adjacent islands. In terms of population and economic size all the FIC are small. The combined population is only a little over 6 million and the GNP is about US$ 8.5 billion. PNG represents approximately two-thirds of the population and GNP. The most important asset of the FICs is their large sea area, containing within its boundaries almost a third of the world's total fish stocks.

Of the 14 FICs, eight are Members of the ACP group. The six non-Members are: Cook Islands, Federated States of Micronesia, Marshall Islands, Nauru, Niue and Palau. All six have applied to become Members of the ACP group.

The South Pacific Forum is a well-structured organization that is active in a large number of cooperation themes. For some of these themes, separate regional bodies such as the Forum Fisheries Agency with headquarters in the Solomon Islands and the South Pacific Regional Environment Programme with headquarters in Samoa have been formed. Other cooperation themes are trade promotion, civil aviation, telecommunications and tourism.

Main achievements and assessment

The South Pacific Forum is considered to be a successful organization for functional cooperation in several key areas of common interest such as fisheries, environment and tourism. The Forum is also important for political dialogue and for raising the concerns of the small FICs at the international level (for example, their disagreement with the French nuclear testing programme).

The Forum has recently become more active in a number of subjects related to economic integration. In June 1999 the Forum Trade Ministers endorsed in principle a Free Trade Area between the members of the FIC. Furthermore, work is planned on collective trade facilitation covering subjects such as phytosanitary requirements and customs procedures. Additionally, the Forum Secretariat is preparing its member states for the next round of WTO trade liberalization and for negotiations of the future trade regime with the EU. The FICs are also considering steps towards investment liberalization.

Melanesian Spearhead Group (MSG)

Creation: MSG was created in 1991.

Membership: Fiji (1996), New Caledonia (1996), Papua New Guinea, Solomon Islands, and Vanuatu.

Background and main objectives

The Melanesian Spearhead Group was established in 1991 by PNG, Solomon Islands and Vanuatu as a relatively loose body for political and economic collaboration. In 1994 the three founding members agreed that MSG would become a Free Trade Area. In 1996 Fiji and the French overseas territory of New Caledonia joined the arrangement, without, however, taking part in the trade agreement. The MSG is a sub-group of the South Pacific Forum Island Countries (FIC). The MSG members are all small economies, but within the FIC they are by far the largest ones representing more than 85 per cent of the combined population and GNP.

Main achievements and assessment

It is premature to discuss the trade liberalization of MSG. In order to limit the costs, no permanent secretariat has been established. MSG matters are handled by units within the administration of the member states. Progress on trade liberalization is very slow. It is constrained by the product-by-product approach that was adopted. So far only 35 products, mainly primary ones, have been liberalized. Given the new interest of the Pacific Forum in trade liberalization, the Spearhead Group has the potential to become the fast track for such liberalization within the FIC group.

Appendix B: Characteristics of Small Developing and Transition Economies

Table B1 Characteristics of small developing economies: Africa

Economy	*GNP*[1]	*GNP p.c. $ 1996*	*Pop. (mln) 1996*	*Special status*[2]	*WTO*[3]	*Openness*[4]	*ACP*[5]	*LDC*[6]
Angola	3.0	270	11.1	0	1	0	1	1
Benin	2.0	350	5.6	0	1	1	1	1
Botswana	4.4	3260	1.5	1	1	1	1	1
Burkina Faso	2.4	230	10.7	1	1	0	1	1
Burundi	1.1	170	6.4	1	1	0	1	1
Cameroon	8.4	610	13.7	0	1	1	1	0
Cape Verde	0.4	1010	0.4	2	0	–	1	1
Central Afr. R.	1.0	310	3.3	1	1	0	1	1
Chad	1.0	160	6.6	1	1	0	1	1
Comoros	0.2	450	0.5	2	0	–	1	1
Congo (Brazza.)	1.8	670	2.7	0	1	0	1	0
Congo (Kinsh.)	5.7	130	45.2	0	1	0	1	1
Côte d'Ivoire	9.4	660	14.3	0	1	0	1	0
Djibouti	0.5	780	0.6	0	1	–	1	1
Eq. Guinea	0.2	530	0.4	1	0	–	1	1
Eritrea	0.8	220	3.7	0	0	–	1	1
Ethiopia	6.0	100	58.2	1	0	0	1	1
Gabon	4.4	3950	1.1	0	1	0	1	0
Gambia	0.4	360	1.1	0	1	1	1	1
Ghana	6.2	360	17.5	0	1	1	1	0
Guinea	3.8	560	6.8	0	1	1	1	1
Guinea-Bissau	0.3	250	1.1	0	1	1	1	1
Kenya	8.7	320	27.3	0	1	1	1	0
Lesotho	1.3	660	2.0	1	1	–	1	1
Liberia	–	–	2.8	0	0	–	1	1
Madagascar	3.4	250	13.7	2	1	0	1	1
Malawi	1.8	180	10.0	1	1	0	1	1
Mali	2.4	240	10.0	1	1	1	1	1
Mauritania	1.1	470	2.3	0	1	0	1	1
Mauritius	4.2	3710	1.1	2	1	1	1	0
Mozambique	1.5	80	18.0	0	1	0	1	1
Namibia	3.6	2250	1.6	0	1	–	1	0
Niger	1.9	200	9.3	1	1	0	1	1
Rwanda	1.3	190	6.7	1	1	0	1	1
São Tomé	0.05	330	0.1	2	0	–	1	1
Senegal	4.9	570	8.5	0	1	0	1	0
Seychelles	0.5	6850	0.08	2	2	–	1	0
Sierra Leone	0.9	200	4.6	0	1	–	1	1
Somalia	–	–	9.8	0	0	0	1	1
Sudan	7.8	290	27.3	0	2	–	1	1
Swaziland	1.1	1210	0.9	1	1	–	1	0
Tanzania	5.2	170	30.5	0	1	0	1	1
Togo	1.3	300	4.2	0	1	0	1	1
Uganda	5.8	300	19.7	1	1	1	1	1
Zambia	3.4	360	9.2	1	1	1	1	1
Zimbabwe	6.8	610	11.2	1	1	0	1	0

Notes follow Table B4.

Table B2 Characteristics of small developing economies: Latin America and the Caribbean

Economy	*GNP*[1]	*GNP p.c. $ 1996*	*Pop (mln) 1996*	*Special status*[2]	*WTO*[3]	*Openness*[4]	*ACP*[5]	*LDC*[6]
Antigua and B.	0.5	7330	0.07	2	1	–	1	0
Barbados	1.7	6530	0.3	2	1	1	1	0
Belize	0.6	2700	0.2	0	1	–	1	0
Bolivia	6.3	830	7.6	1	1	1	0	0
Costa Rica	9.1	2640	3.4	0	1	1	0	0
Cuba	–	–	11.0	2	1	–	0	0
Dominica	0.2	3090	0.07	2	1	–	1	0
El Salvador	9.9	1700	5.8	0	1	1	0	0
Grenada	0.3	2880	0.1	2	1	–	1	0
Guyana	0.6	690	0.8	0	1	1	1	0
Haiti	2.3	310	7.3	2	1	0	1	1
Honduras	4.0	660	6.1	0	1	1	0	0
Jamaica	4.1	1600	2.5	2	1	1	1	0
Nicaragua	1.7	380	4.5	0	1	1	0	0
Panama	8.2	3080	2.7	0	1	–	0	0
Paraguay	9.2	1850	5.0	1	1	1	0	0
St Kitts and N	0.2	5870	0.04	2	1	–	1	0
St Lucia	0.6	3500	0.16	2	1	–	1	0
St Vincent	0.3	2370	0.11	2	1	–	1	0
Suriname	0.4	1000	0.4	0	1	–	1	0
Trinidad and T	5.0	3870	1.3	2	1	–	1	0

Notes follow Table B4.

Table B3 Characteristics of small developing economies: Asia and the Pacific

Economy	*GNP*[1]	*GNP p.c. $ 1996*	*Pop (mln) 1996*	*Special status*[2]	*WTO*[3]	*Openness*[4]	*ACP*[5]	*LDC*[6]
Afghanistan	–	–	24.2	1	0	–	0	1
Bhutan	0.3	390	0.7	1	0	–	0	1
Cambodia	3.1	300	10.3	0	2	–	0	1
Fiji	2.0	2470	0.8	2	1	–	1	0
Jordan	7.1	1650	4.3	0	2	–	0	0
Kiribati	0.07	920	0.08	2	0	–	1	1
Laos	1.9	400	4.7	1	2	–	0	1
Maldives	0.3	1080	0.3	2	1	–	0	1
Marshall Isl.	0.1	1890	0.06	2	0	–	0	0
Micronesia	0.2	2070	0.1	2	0	–	0	0
Myanmar	–	–	45.9	0	1	–	0	1
Nepal	4.7	210	22.0	1	2	1	0	1
Papua NG	5.0	1150	4.4	2	1	0	1	0
Samoa	0.2	1170	0.2	2	2	–	1	1
Solomon Isl.	0.3	900	0.4	2	1	–	1	1
Tonga	0.2	1790	0.1	2	2	–	1	0
Vanuatu	0.2	1290	0.2	2	2	–	1	1
Yemen	6.0	380	15.8	0	0	1	0	1

Notes follow Table B4.

Table B4 Characteristics of small transition economies

Economy	*GNP*[1]	*GNP p.c. $1996*	*Pop (mln) 1996*	*Special status*[2]	*WTO*[3]	*Openness*[4]	*ACP*[5]	*LDC*[6]
Albania	2.7	820	3.3	0	2	1	0	0
Armenia	2.4	630	3.8	1	2	0	0	0
Azerbaijan	3.6	480	7.6	0	2	0	0	0
Estonia	4.5	3080	1.5	0	2	1	0	0
Georgia	4.6	850	5.4	0	2	0	0	0
Kyrgyz	2.5	550	4.6	1	1	1	0	0
Latvia	5.7	2300	2.5	0	1	1	0	0
Lithuania	8.4	2280	3.7	0	2	1	0	0
Macedonia	2.0	990	2.0	1	2	1	0	0
Moldova	2.5	590	4.3	1	2	1	0	0
Mongolia	0.9	360	2.5	1	1	–	0	0
Tajikistan	2.0	340	5.9	1	0	0	0	0
Turkmenistan	4.3	940	4.6	1	0	0	0	0

Note
– = no information available.
1. US $ billion 1996.
2. 1 = landlocked; 2 = island; 0 = other.
3. 1 = member of the WTO; 2 = membership requested; 0 = not a member.
4. 0 = closed; 1 = open (as defined by Sachs and Warner, 1995).
5. 0 = not a member of the ACP group; 1 = member of the ACP group (the only ACP countries not in the tables are Dominican Republic, Nigeria and South Africa).
6. 0 = not a least-developed country; 1 = least-developed country (Bangladesh is the only least-developed country not in the tables).

Source: Population and GNP data World Bank, *1998 Development Report and Atlas*.

Notes

1 Introduction

1 During the Middle Ages, regular long-distance trade took place between China, India, the Middle East, North Africa and Europe.
2 There is also a microeconomic dimension of globalization, emphasized by Oman (1994 and 1995). In his view, competitiveness is more affected by the capacity to adopt innovations than by availability of raw materials.
3 The current list of applicants still includes several prominent trading nations such as China, Russia, Ukraine, Taiwan, Saudi Arabia and Vietnam.
4 The work to define and agree on standards in a particular industrial sector takes place through technical committees and working groups. These bring together the main economic players in the sector, including companies, consumer organizations and government authorities.
5 The Asian financial crisis, which started in mid-1997, did not fundamentally change the long-term picture. Still, it led to formidable economic problems and hardship for the countries affected and to unprecedented and controversial interventions by the international community. At the beginning of 1999, there were signs that economic growth would resume in some of the countries. The crisis led to a reassessment of the liberalization of capital flows and the importance of banking supervision.
6 There is also a debate on the complementarity and the sequencing between openness and other major areas of economic reform such as privatization and deregulation as well as reform in the area of political institutions, governance and the legal system.
7 This widely used formulation is attributable to Bhagwati (1992).
8 One might pose the question whether a hegemonic economy could *ever* be benevolent and resist the temptation of deploying its full power. Clearly, even such an economy will suffer in the long term if the consequence of its behaviour is to destabilize other nations. A hegemonic economy may therefore participate in a positive-sum game.
9 Critics point to the protectionist aspects of the Common Agricultural Policy (CAP) as well as protection in textiles. However, protection in those sectors has been a widespread phenomenon across most OECD countries. Sometimes, countries that are among the most liberal in industry can be the most protective for agriculture (for example, Norway and Switzerland). Agricultural protection has always been linked to the specific nature of agricultural markets and the social aspects of the rural economy. The gradual and orderly transition of rural societies is a long-standing objective of the CAP.
10 This should not be interpreted as providing an argument for *large* developing economies to pursue autarkic or closed policies. However, they have possibilities of integration into the world economy that are not available to *small* developing economies.
11 The characteristics of *Small Island Developing States (SIDS)* have been the subject of several international meetings. A programme of action was adopted

at the Barbados conference on sustainable development of SIDS in 1994.

12 For example, a report of the Commonwealth Secretariat (1985) defined a small state as one with a population of around one million or less. More recently, the Commonwealth Secretariat (1997) revised its cut-off point to one-and-a-half million to reflect the increase in world population. Another study of Armstrong and Kervenoael (1998) proposes an upper limit of three million persons to define small size. With the latter limit, Singapore just qualifies as a small state.

13 The arbitrariness of the criterion is demonstrated, for example, by the fact the Dominican Republic, usually considered to be a small developing country, is not included, because its GNP just exceeds the cut-off value.

14 A few countries below the cut-off point, but classified by the World Bank as high-income (with per capita GNP above US$ 9000 in 1996) are not included, because of their special situation.

15 The criteria used by the UN to define Least Developed Countries are: per capita GDP, physical quality of life index and an economic diversification index. The physical quality of life index comprises life-expectancy at birth, per capita calorie supplies, combined primary and secondary enrolment ratio, and adult literacy. The economic diversification index takes into account the share of manufacturing in GDP, the share of employment in industry, per capita electricity consumption and export concentration. The list is reviewed every three years.

16 There has been increased attention on the concept of *vulnerability* of small developing countries, whether or not they are least developed. It is argued, for example, by the Commonwealth Secretariat (1997) that the vulnerability of such countries justifies certain concessions of their industrial trade and cooperation partners that would not necessarily apply to large developing countries with a comparable per capita income. This reasoning is presently used by Vanuatu and the Maldives to underscore that their graduation from the list of Least Developed Countries should be postponed. Within the United Nations, work is ongoing to define a 'vulnerability index'. An example of such an index has already been worked out by Briguglio (1995). His index combines three groups of variables: exposure to foreign economic conditions (such as dependence on trade), remoteness and insularity, and disaster-proneness. Briguglio demonstrates that small island developing states have indeed a higher vulnerability index than other developing countries with similar per capita GNP.

17 Even though the emphasis is on trade aspects, it is understood that, in addition to WTO membership, the base-line strategy should also include membership of the IMF with subscription to current account convertibility.

2 WTO Membership: What's in it for Small Developing Countries?

1 The World Trade Organization was formally established on 1 January 1995. As an institution, the WTO has equal standing with the International Monetary Fund (IMF) and the World Bank. The WTO is responsible for administering the General Agreement on Tariffs and Trade (GATT) 1994, the General Agreement on Trade in Services (GATS), and the Agreement on Trade Related Intellectual Property Rights (TRIPs). 'GATT 1994' consists of (a) the

original 'GATT 1947', (b) the amendments to GATT 1947 and (c) the Understandings reached under the Uruguay Round.

2 There is extensive literature on the topics covered in this chapter. This presentation draws particularly on Hoekman and Kostecki (1995), IMF (1994), Krueger (1995), Martin and Winters (1995) and Page and Davenport (1994). It is not meant to provide a comprehensive treatment of the multilateral trading system, but a coverage that helps to demonstrate its importance and limitations for small developing economies.

3 It is remarkable that neither the GATT nor the WTO has a clear definition of developing countries. The practice is that developing-country status is based on self-selection. This is not the case for the sub-category of the least-developed countries (LDCs), where a UN definition based on objective criteria is employed (see also Chapter 1, note 15).

4 Tariff bindings are obligations not to raise tariff rates on specific products above a certain level without compensating reductions in other tariffs. The actual applied tariffs may be lower than the bound rates. The larger the difference between applied tariffs and bound rates, the easier a country can unilaterally raise its tariffs, while still fulfilling its WTO obligations.

5 The other basic principle is non-discrimination or Most-Favoured-Nation (MFN) as set out in Article I. MFN implies that any concession granted by a contracting party to a product or service of another country is automatically granted to like products or services of all the other contracting parties. The MFN obligation is complemented by the national treatment rule (Article III), requiring that foreign goods, once they have satisfied whatever border measures that are applied, such as customs duties, be treated no less favourably in terms of taxes and equivalent measures than identical goods of domestic origin.

6 Since 1973, the Multifibre Arrangement (MFA) has regulated trade in textiles and clothing between importing industrial countries and exporting developing ones as well as Central and East European countries. Imports into industrialized countries are restricted through a complex system of country and commodity-specific quotas.

7 See, for example, Martin and Winters (1995). The predicted loss to sub-Saharan Africa reflects the anticipated rise in food prices resulting from the reduction of agricultural protection in industrialized countries.

8 The first ministerial meeting following the creation of the WTO, which took place in December 1996 in Singapore, demonstrated these tendencies. The WTO Secretariat proposed a draft plan of action in favour of the least-developed countries. With respect to market access, the plan called upon *developed and developing countries* to grant duty-free preferential access for the exports of least-developed countries. The plan also called for assistance in the area of capacity-building. What is remarkable about the plan is that, for the first time, it explicitly called on the more advanced developing countries to help the least-developed countries. The plan was broadly endorsed at the ministerial meeting and was further worked out during a meeting organized jointly by WTO, UNCTAD and the International Trade Centre (ITC) in October 1997.

9 Countries such as Mauritius and Jamaica that are members of the Lomé Convention have been exempted from the MFA for their textiles and clothing exports to the EU. Hence, the phasing-out of the MFA implies a loss of their advantage (see Chapter 5).

10 Even though the EU and the US, which together account for about 40 per cent of agricultural trade, dominated the discussions on agriculture, the negotiations were also influenced by a new kind of coalition of traditional agricultural exporters called the Cairns Group. The coalition comprises industrial countries (Australia, Canada and New Zealand), developing countries (Argentina, Brazil, Chile, Colombia, Fiji, Indonesia, Malaysia, the Philippines, Thailand and Uruguay) and a transition economy (Hungary). Of the developing country members only one, Fiji, is a small developing economy.
11 For example during 1994–95 Mexico introduced 18 cases, Brazil 12 and India nine. This is to be compared with 37 cases for the EU, 30 for the United States and nine for Canada.
12 According to Sachs (1998), an estimated one-third of merchandise trade is composed of shipments among the affiliates of a single company, as opposed to trade among separate exporters and importers.
13 International investment regulations have long been discussed in the OECD. A Multilateral Agreement on Investment (MAI) has been under preparation. The MAI would be open to non-OECD members. It intends to establish non-discrimination, national treatment, protection and transparency. It also foresees a mechanism for dispute settlement complementing WTO provisions. However, developing countries and non-governmental organizations were not at all in favour of a system designed exclusively to serve OECD members, with little attention for social and environmental issues. During 1998, when it became clear as well that several OECD member states were not in favour, preparations were stopped. It has been suggested that the discussions on investment should move to the WTO in order that developing countries can also participate.
14 It is too early to guess the medium- and long-run effects of the economic crisis in East and South–East Asia that started in 1997 and deepened during 1998. There will certainly be a slower growth of their imports in the short run. By the beginning of 1999 there were signs of resumed growth in some of the affected countries.
15 The limitations for small countries in relation to dispute settlement were underlined in a presentation by the Ambassador of St Lucia at a hearing of the European Parliament in May 1997, in Brussels. In the banana regime dispute, St Lucia, together with its partners in the Organization of Eastern Caribbean States, used the services of a legal specialist. However, this lawyer could not attend the WTO panel because he was not an official delegation member. Larger countries can afford to have legal advisers as full-time members of their delegation.
16 Even though developing countries' contributions to the budget are not very high, at the beginning of 1997, 23 developing countries had not paid for more than three years. This excludes them from receiving technical assistance. Another seven developing countries were more than one or two years in arrears and therefore barred from chairing WTO bodies (see Michalopoulos, 1999).

3 Unilateral Economic Liberalization

1 See also the discussion on Trade Related Investment Measures (TRIMs) in Chapter 2.

2 A comprehensive overview of experience with trade liberalization in the context of structural adjustment programmes was made by Thomas, Nash and associates (1991).
3 Current-account convertibility means that local currency can be freely exchanged for foreign currency in order to import goods or to pay for factor services. However, capital transactions to invest or transfer funds abroad may still face various restrictions.
4 A weakness of the Sachs and Warner measure is that it does not reflect the intensity of openness or closedness. For example, a 20 per cent overvalued exchange rate is quite different from a 500 per cent overvaluation, but both lead to a classification as closed. A monopoly on major exports can still be compatible with an open economy, depending on how it is handled. Without a monopoly, small exporters of farm products may be at the mercy of monopsonist buyers.
5 Corden (1974) draws a distinction between divergences and distortions. A divergence can be any difference between private and social cost, or private and social benefits. A distortion is a divergence that is caused by government policy of some kind, such as a tariff or subsidy. Divergences that are not distortions are typically caused by market failures.
6 The welfare gain obtained through the optimal tariff occurs at the expense of the rest of the world. However, it is possible that other large economies or trading blocs retaliate by also imposing tariffs.
7 An exception is Lawrence and Litan (1986). They discuss how dislocation effects of trade liberalization in an affluent economy can be mitigated without restoring permanent protection. Possible measures include temporary relief to displaced workers while providing incentives for mobility. Such measures are difficult to set up in a small, poor economy.

4 South–South Regionalism

1 Integration initiatives of developing countries frequently take on board certain aspects of the European approach. This copying can be risky because the context is very different. It is therefore useful to explain some aspects of the European experience.
2 The terminology is somewhat problematic and even controversial. Bhagwati and Panagariya (1996) use the abbreviation PTA for 'Preferential Trading Area' which can be an FTA, a CU or even a Common Market. In their view, 'Free Trade Area' sounds too positive because imports from third countries are in fact not free. In other words, an FTA discriminates against third countries. In this text, we follow the more usual definition. Another term used by Frankel (1997) to refer to *one-way* concessions is *preferential trade arrangement*. These are the subject of Chapter 5.
3 The dividing line between free trade in services and free movement of production factors is not always clear. For example, provision of financial services across borders is closely related to capital movements and construction services require labour movement (see Frankel, 1997).
4 Deep integration is often associated in the literature with the 'new regionalism' (see, for example, Robson, 1993).
5 The principle of mutual recognition of standards was an important aspect of the completion of the European single market in 1993. The strategy was

to rely as much as possible on mutual recognition and limit harmonization to essential health and safety requirements. Furthermore, the task of developing harmonized standards was given to private sector standardization organizations (see Tsoukalis 1997).

6 For some of these discussions see Frankel (1997), McMillan (1993), Nagarajan (1998) and Snape (1993).

7 Even under Article XXIV, some exceptions are possible given the ambiguity of the concept of 'substantially all' trade. Sometimes, 90 per cent coverage of trade is used as a benchmark. Hence there may still be lobbying from pressure groups to exclude certain products. There may also be a case for temporary exclusion of infant industry products, with a potential of real productivity gains.

8 Nagarajan (1998) points out that the Understanding introduced a discrepancy between the rules for CUs and those for FTAs. The assessment for CUs shall be based on applied rates, but for FTAs it is not clear whether bound or applied rates shall be used. This ambiguity can have important practical implications. For example, there were negative consequences for EU exporters when Mexico, following its 1994 currency crisis, raised applied tariffs towards the EU and other third countries whereas it did not raise them towards its NAFTA partners.

9 An exception is Hufbauer and Schott (1994). In order to assess the prospects for Western Hemisphere economic integration, they developed the concept of 'readiness indicators'. These are price stability, budget discipline, external debt, currency stability, reliance on trade taxes, market-oriented policies and functioning democracy. Apart from the last one, they are all economic indicators. By assigning target values to the indicators they rank countries in terms of their chances of progress towards economic integration.

10 Casual observation and writing often simply point to the low level of recorded intra-regional trade as an explanation for the lack of success of regional economic integration of developing countries. The reasoning goes on to point out that many countries export identical primary commodities or labour-intensive manufactures and concludes that there is no potential for intensified trade. These views miss the point that in many cases, regional integration is simply not implemented because certain preconditions are not satisfied or because the design is not appropriate. Furthermore, it should not be forgotten that there is often a large amount of unrecorded trade, especially when the economies suffer from macroeconomic distortions. In the case of small or very small economies, it is natural that intra-regional trade is relatively small. In addition, cross-border infrastructure may be inadequate so that trade with more distant industrial countries is relatively cheap. Therefore a low *level* of intra-regional trade does not allow conclusions on the success or the potential of integration among developing countries.

11 This might change in the future. There are recent examples where developing country arrangements took into account political criteria. In April 1996, MERCOSUR partners made it clear that the anticipated military coup in Paraguay would have negative consequences for its participation. In August 1997, ASEAN countries decided to postpone Cambodia's accession, following a coup and renewed civil strife. However, around the same time, Myanmar did become a member of ASEAN even though many third countries criticized its human-rights situation. In Africa, the Democratic Republic of Congo

became a member of both COMESA and SADC despite political unrest and, later on, conflict involving several countries in the region.

12 This observation is consistent with the comment in Chapter 3 that adjustment programmes with a focus on unilateral liberalization can have negative spillover effects on countries in the same region. Hence the need to take into account the regional dimension in these programmes. Expressed differently, adjustment programmes that are regionally coordinated and compatible in terms of reform measures and pace will facilitate successful regional integration.

13 There are four convergence criteria to be met by a country for entry into the European Monetary Union: no more than 1.5 per cent inflation above the average of the three lowest-inflation member states; a government deficit no larger than 3 per cent of GDP; a public debt no higher than 60 per cent of GDP; long-term interest rates not more than 2 percentage points above the levels in the three lowest inflation countries. On the public debt it is added that a country qualifies if its debt/GDP ratio approaches the target level at a satisfactory pace. In addition, the national currency should not have been devalued within two years prior to the entry into the monetary union.

14 The European Commission 1997 Communication: 'Agenda 2000 for a stronger and wider Union' contains a detailed description of the accession criteria as well as an assessment of the extent to which these criteria are fulfilled by the present candidates for EU membership.

15 The Trade Policy Review Mechanism is briefly described in Chapter 2.

16 Differences in language and history did not, however, prevent Suriname becoming a member in 1996 and Haiti in 1997. The population of Haiti also exceeds the combined population of the other CARICOM members.

17 For more complete, but still concise overviews, see for example Bulmer (1994) or CEPR (1995).

18 It is also argued sometimes that rapid technological change and globalization erode the sovereignty of small countries, especially in economic decisions. By pooling resources and power, groupings of countries can recapture some of this loss and again become significant players – for example, in areas such as scientific research.

19 Referring to sub-Saharan Africa, it is striking that groupings with a large number of countries such as ECOWAS (16 members), COMESA (around 20 members) or SADC (14 members) are making slow progress on trade liberalization and other integration policies. While it is too early to draw firm conclusions, the progress of UEMOA (8 members) and EAC (3 members) seems to be faster.

20 Article 3b of the Maastricht Treaty states: 'In areas which do not fall within its exclusive competence, the Community shall take action, in accordance with the principle of subsidiarity, only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community.'

21 Amendment ten of the US Constitution states: 'The powers not delegated to the United States by the Constitution, nor prohibited to it by the States, are reserved to the States respectively or to the people.'

22 As an illustration, one could refer to the overlap in the mandates of smaller and larger groupings in Africa. Under subsidiarity smaller groupings could

focus on matters such as cross-border infrastructure whereas larger groupings could deal with issues such as customs documentation and transport regulations.

23 The line between variable geometry and multispeed integration cannot always be drawn accurately. Some member states may decide upon slower implementation, but if implementation is further postponed, what seemed only multispeed may turn into *de facto* variable geometry. This could be applicable to the European Monetary Union. The Euro zone was launched on 1 January 1999 by 11 countries. Two member states opted out (for the moment) and for two others the entry conditions were not fulfilled. This situation could be characterized as variable speed. However, if those who opted out decide to stay out indefinitely it becomes variable geometry. Variable speed or geometry is also applicable in the EU in the social field and in the area of movement of persons where a subgroup of EU members created a 'passport union' (i.e. the Schengen agreement). This digression demonstrates that some variable speed or geometry is likely whenever a grouping contains a relatively large number of member states.

24 In the European context, the main areas for the common base recommended by the CEPR group are the single market, including trade and competition policy, the structural and cohesion funds, the harmonization of indirect taxation and a mechanism for coordinating monetary policy to avoid competitive devaluation. Moreover, in the non-economic sphere, the common base should include an acceptance of basic principles such as democratic government, respect for human rights, mutual non-aggression and the rule of law. In the view of the CEPR group, a reformed version of the controversial Common Agricultural Policy (CAP) might be part of the common base, but not monetary union and a common social policy.

25 By imposing a tariff, a large country, in contrast to a small one, can restrict imports in order to obtain price concessions. In this way, a tariff can improve its terms of trade and hence welfare, at the expense of the welfare of the trading partners. The *optimal tariff* is the one that maximizes the gains. A large trading bloc has an incentive to use tariffs to its advantage. However, other trading blocs may retaliate and the end-result may be a trade war in which all traders lose. One of the main objectives of the multilateral system is to avoid a tariff war where welfare at world level would certainly decline.

26 The supply curve of the partner country is horizontal over the import range of the home country. This is compatible with the small-country assumption. At a larger supply level, the partner country's supply curve can be rising.

27 Demand and supply of the home country can be subtracted for each price so that only demand for imports remains.

28 These include: perfectly competitive markets, full capacity utilization, homogeneous goods and absence of other distortions. If other distortions are present, because of market conditions or policy interventions, the theory of second best applies. This means that it is not certain whether elimination of one kind of distortion, for example tariffs, while others remain present, will increase welfare.

29 Bhagwati and Panagariya's criticism is mainly addressed against regional arrangements involving 'trade hegemons'. They consider arrangements of

developing countries such as MERCOSUR with some favour even though they do not find them the best strategy. More generally they consider regional arrangements justified when they deepen towards a common market with free movement of production factors or an economic union implying policy harmonization.

30 An example is De Rosa's (1995) estimate of the effects of the ASEAN-planned FTA, usually referred to as AFTA. Intra-ASEAN trade is estimated to expand by 19 per cent, largely in the form of trade creation. Welfare effects range from less than 0.5 per cent for the more protected economies of Indonesia, the Philippines and Thailand to 1.3 per cent in Malaysia and 3.9 per cent in Singapore.

31 The Kemp–Wan theorem is a direct application of the fundamental theorem of welfare economics, stating that any competitive equilibrium can be sustained by a suitable price vector. When a CU is formed, there exists an internal price vector that sustains the same level of trade and thus world prices. The difference between the internal equilibrium price vector and the unchanged world price vector defines the Common External Tariff.

32 See, for example, Perroni and Whalley (1994) and Whalley (1996). An illuminating overview is provided by Fernandez and Portes (1998).

33 The *domino theory of regionalism* proposed by Baldwin (1995) can be seen in the same light. If a large trading bloc is deepening its integration, the cost to private firms of being outside increases. This triggers lobbying to encourage outsiders to become members. With more countries joining, the pressure to apply for membership increases. The domino theory provides a nice explanation of why the East European countries wish to become part of the European Union.

34 These effects were mentioned in Chapter 3 in relation to unilateral liberalization, referring to Rodrik (1998).

35 Another possibility is that the CU comprises a dominant country which sets the CET unilaterally. In fact this is what has happened so far in the SACU where South Africa has decided on the tariff schedules. An example is the offer made during the Uruguay Round, without much involvement from the four smaller member states. One of the important aspects of the current negotiation on the reform of SACU is to set up a structure where all the member states are involved in decisions.

36 The concept of a Harmonized External Tariff (HET) has been encouraged in Eastern and Southern Africa by the African Development Bank, the European Commission, the IMF and the World Bank in the context of an initiative to facilitate cross-border economic activities (see European Commission 1998).

37 For example, the rules of origin of COMESA are as follows: 'Goods must be consigned directly from a member state to a consignee in another member state and:
- be wholly produced or
- contain an import content of not more than 60 per cent CIF value of the total cost of materials used in production or
- contain not less than 45 per cent ex-factory value added or
- contain not less than 25 per cent value added if the final product is considered to be of particular importance to the economic development of member states (a list of such approved goods is available at the Secretariat).

'All goods eligible for COMESA tariffs should be accompanied by a COMESA

Certificate of Origin, duly completed, stamped and authenticated by the authorized signatories in the country of origin.' (See COMESA website: www.comesa.int.)

38 Efforts are being made towards gradual harmonization of the different EU systems of origin verification.

39 An example to illustrate this possibility, worked out by Krueger (1993) is car assembly in Mexico. If an automobile carries a 50 per cent duty in the United States and the components carry comparable duties, a Mexican assembler will be obliged to import components from the US in order to fulfil the rule of origin (for example 80 per cent of the components' value must be from within NAFTA). It can be demonstrated that a higher origin requirement amounts to an extension of US protection of components to Mexico. In other words, Mexico is obliged to buy components within NAFTA rather than from the cheapest source, if it wishes to qualify for duty-free car exports to the US.

40 If the customs duties are pooled and flow to a common budget, it does not matter who collects the duties. This is the situation in the EU where all customs duties go the EU budget. However, in the European situation, customs duties are only 0.25 per cent of GDP and the EU budget represents around 1.2 per cent of GDP. For most developing countries, customs duties represent a sizeable part of government revenue and of GDP often exceeding 25 and 5 per cent respectively. Hence if customs duties are pooled, there must be a system that enables the funds to flow back to the national budgets. In fact, this is what happens in SACU. All duties are pooled and an agreed formula is applied to give a share to each member state. South Africa administers the system. An important discussion item in the SACU renegotiations is to agree on a formula that satisfies all member states (more background on this is provided in Appendix A). The alternative to pooling is that each member state collects duties on the goods that enter. For landlocked countries, a transit system must be set up involving a customs bond guarantee. An importer from a landlocked country must provide a financial guarantee to the transit country as long as the goods are in transit. Needless to say, such a system constitutes a trade barrier and an extra cost to the private sector. It is interesting to recall that Viner's (1950) original definition of a CU also includes a requirement of 'apportionment of customs revenue between the members in accordance with an agreed formula' (p. 5). This condition has been almost completely neglected in the literature, probably because it referred mainly to industrial countries for whom customs revenue was not significant.

41 This point is emphasized by the European Commission (1998). The theme is also developed by Mistry (1996) in relation to Southern Africa.

5 Non-Reciprocal Arrangements with Industrial Countries

1 Nevertheless, the US maintained a preferential trade relationship with the Philippines from 1900 to around 1940.

2 The Yaoundé Conventions stipulated that the associated states should not impose any customs duties or charges having equivalent effect on imports from the EC. However, they were allowed to retain or introduce customs duties necessary to meet development or budgetary needs. The Convention

did not stipulate free trade among the associated states, but only recommended the formation of customs unions or free trade areas. The associated states were required to give treatment to imports from the EC no less favourable than treatment of the most-favoured third country and to provide information on their trade policy. As it turned out, development and budgetary needs provided ample justification for import duties, so that there was, in reality, no free trade between the EC and the associated states.

3 The origin of UNCTAD is briefly described in Chapter 2.

4 The EU system was started by the six original member states. Following EU enlargement, the new member states integrated their own GSP into the EU scheme.

5 A comparable arrangement implemented by Canada in favour of the Caribbean Commonwealth states is CARIBCAN. Another non-reciprocal preferential arrangement set up by Australia and New Zealand, and benefiting the Pacific Island Countries, is the South Pacific Regional Trade and Economic Cooperation Agreement (SPARTECA).

6 See also the discussion on infant industry as an argument for protection at the country level in Chapter 3.

7 There is extensive literature on EU preferential trading arrangements. An interesting overview, including a description of the historical background, is provided by Grilli (1993). Another overview is Faber (1990). The Lomé trade system is described for example by Davenport, Hewitt and Koning (1995). The European Commission (1993 and 1997b) published two volumes on the role of EU as a world trade partner, including a description of preferential arrangements.

8 Some non-ACP countries have market access that is comparable to the Lomé regime. However, these are based on *reciprocal* arrangements such as the European Economic Area (EU, Norway, Iceland and Liechtenstein), the Customs Union with Turkey and the 'Europe agreements' with the Central and Eastern European countries. There remain only six countries with pure MFN treatment: Australia, Canada, Japan, New Zealand, Taiwan and the United States; and one country with less-than-MFN treatment: North Korea (Sapir, 1998).

9 The situation is evolving constantly. The Barcelona agreement in 1995 started a process that should lead to an EU–Mediterranean Free Trade Area. As a result, the non-reciprocal association agreements are gradually being replaced by FTAs between the EU and the Mediterranean states. The first agreements were concluded with Israel, Morocco and Tunisia. The move towards FTAs between the EU and developing countries falls under the subject of North–South integration dealt with in Chapter 6.

10 See Appendix Tables B1 to B3. Several Pacific states as well as Cuba are candidates to join the ACP group.

11 Respect for human rights, democratic principles and the rule of law were introduced as *essential elements* of the Lomé Convention. If the obligations in respect of essential elements are not fulfilled, the partial or full suspension of application the Convention is possible.

12 A brief general discussion of rules of origin can be found in Chapter 4.

13 The case of fish is rather complicated. Fish caught inside the territorial 12-mile zone is always considered originating. Outside the 12-mile zone, fish must be caught by ACP vessels. There are stringent provisions to determine

whether a vessel can be considered as an ACP vessel: registration, flag, ownership and crew composition.

14 The sugar protocol is a remarkable arrangement under which a number of developing countries can export cane sugar to the EU at the internally guaranteed EU price. Because the EU sugar market is protected, this price is generally well above the world market price. The system boils down to an income transfer. The protocol dates back to the first Lomé Convention signed in 1975. However, unlike the Convention, the sugar protocol was meant to be of unlimited duration. According to Hermann and Weiss (1995), it resulted from the political pressure of a coalition consisting of the UK government, the UK sugar-refining company Tate and Lyle and the sugar-exporting Commonwealth countries. Its adoption was facilitated by the unusual marketing conditions around 1975 with very high world market prices and extreme volatility. The main operation of the sugar protocol is the annual quota allocated to 19 beneficiary countries. All these countries, with the exception of India, are small ACP states. Of the total amount of around 1.3 million tons a few countries get a very high share: Mauritius (491 000 tons), Fiji (165 000 tons), Guyana (159 000 tons), Jamaica (119 000 tons) and Swaziland (118 000 tons). The other allocations are much smaller. The one for India is negligible. The income transfer in an absolute sense and in comparison to GDP is several cases quite high. For example, Mauritius received an average of €80.0 million per year between 1975 and 1991 which amounts to 4.6 per cent of GDP. The corresponding figures for Fiji are €26.5 million and 2.1 per cent and for Guyana €24.7 million and 9.1 per cent (see Hermann and Weiss, 1995). Even though the sugar protocol is of unlimited duration, its economic effect will gradually diminish as the EU implements the Uruguay Round agreement which will bring the internal EU price closer to the world market price.

15 For earlier Conventions, the EU justified the Lomé trade regime by invoking a combination of Article XXIV (on Free Trade Areas and Customs Unions) and Part IV (allowing special and differential treatment of developing countries).

16 A more complete description of the main characteristics and trade effects of the CBI can be found in Davenport (1995) and Gill, Pellarano and Hess (1996).

17 See Gill, Pellerano and Hess (1996).

18 Or the other comparable regimes such as CARIBCAN and SPARTECA (see note 5).

19 Detailed surveys were prepared by Brown (1988) and Langhammer and Sapir (1988). Another detailed overview, with empirical analysis for the ASEAN countries is by Davenport (1987). A brief description can be found in Faber (1990). Most of the research on GSP was carried out during the 1980s. In the 1990s research interest has shifted towards regional integration and the multilateral system.

20 The old system included tariff preference quotas for sensitive and very sensitive items that were divided into fixed shares for each of the EU member states. Imports that exceeded the quota automatically faced the MFN tariff rate. For the products covered by the Multifibre Arrangement (MFA), preferences were offered only when the exporting countries agreed to apply a 'Voluntary Export Restraint'.

21 Of the 71 ACP states, 39 are least-developed countries. The others are developing countries in the WTO system, except for South Africa, which is considered an industrial country. Thus, of the 48 least-developed countries, only nine do not belong to the ACP group. (See also Appendix B, Tables B1–B3.)

22 A wide variety of methods have been used as reported by Brown (1988) and by Langhammer and Sapir (1988).

23 The smaller and least-developed countries benefited more from the other arrangements specifically geared to them, such as the Lomé Convention and the CBI.

24 Though it should be recalled that a large part of the phasing out of the MFA will only take place shortly before the year 2005 and that liberalization of agriculture is only beginning. Further dismantling of barriers in the agricultural sector will be dealt with during the planned 'Millennium Round' of the WTO.

6 North–South Regionalism

1 It is sometimes forgotten that disparities within groupings of developing countries can also be very large. For example, Bahamas and Haiti, both CARICOM members, have very different per capita incomes (US$ 10 180 and US$ 310 respectively). The gap between Singapore and Vietnam, both members of ASEAN, is even greater (US$ 30 550 and US$ 290).

2 The other members are Brunei, Chile, Taiwan, Hong Kong, Korea, New Zealand and Singapore. Taken together, the APEC countries represent almost 40 per cent of the world population and around 55 per cent of world output. This makes APEC by far the largest economic grouping, even though it is a shallow one and there is no intention of deepening integration.

3 The planned widening of the EU towards Central and Eastern Europe can also be compared to North–South integration.

4 Since the beginning of the 1990s, new forms of conditionality for development assistance have been introduced. This is another way to address some of the problems of the new interdependence. Conditionality is now widely applied to areas such as human rights, the rule of law, democratization, good governance and correct financial management. The practical implementation of such conditionality is not easy. A particular problem arises in relation to applying the same standards across developing countries that may be very different in size and strategic importance (for example, China in comparison to Myanmar or Togo).

5 The collaborative research programme of the African Economic Research Consortium (AERC) on regional integration and trade liberalization analysed the situation in Kenya, Mauritius, Uganda, Nigeria, Ghana, Côte d'Ivoire, South Africa, Zambia and Zimbabwe. Only Mauritius and Uganda did not reverse their trade liberalization process. Most other countries partially reversed trade reforms, while Nigeria experienced a total reversal (see Oyejide 1996).

6 Some would argue that South Africa could play the role of regional anchor economy. South Africa already assumes such a role *vis-à-vis* the neighbouring countries that participate in the Rand zone and the SACU. These countries are very small and have been economically integrated with South Africa for

historical reasons. Whether South Africa can extend its role of regional anchor depends on three main conditions: strong political leadership, macroeconomic stability and a willingness to assist the least-developed countries in the region.

7 Diminishing time-inconsistency of policies is seen as an important explanation of the willingness of Central and Eastern European countries to agree on reciprocal arrangements with the EU. This led to the 'Europe agreements', that also prepare for future membership of the EU.

8 See the discussion in Chapter 4 on the static outcomes of regional arrangements.

9 This is not always the case. It was mentioned above that the Lomé Convention is not a unilateral, but a negotiated agreement. By negotiating as a group, the ACP countries can expect to get a better deal than would be the case if they negotiate separately.

10 The Enterprise for the Americas Initiative (EAI) started in 1990 by President Bush already included a vision of free trade in the Western Hemisphere. As an intermediate step, it foresaw the possibility of free trade areas between the US and groups of countries or single countries. In order to start negotiations, countries were required to fulfil various criteria such as elimination of tariff and non-tariff barriers, liberalization in services and investment, protection of intellectual property, and ending of foreign exchange controls. The EAI also included investment grants and debt-forgiveness. A number of assistance programmes were implemented and framework agreements signed. However, no formal trade negotiations were started under the EAI.

11 This approach is also in line with the recommendations of an independent group of experts on 'smaller economies and Western Hemispheric integration', chaired by Sir Alister McIntyre.

12 Please refer to the discussion of these principles in Chapter 4.

13 Within the ACP group, using a GNP of less than US$ 10.0 billion as a cut-off point, only the Dominican Republic, Nigeria and South Africa are not small economies. South Africa became a member of the Lomé group in April 1997 with a special status implying among other things that it does not benefit from the Lomé trade preferences. The negotiations to establish an EU–South Africa Free Trade Area were concluded at the beginning of 1999. Implementation could start during 2000, with a transitional period of 12 years on the South African side and 10 years for the EU.

14 As seen in Chapter 5, the lack of success of the Lomé preferences must be qualified. In an aggregate sense it is true, but at the level of specific countries and products there are a number of success stories. Besides, it is difficult to tell what would have happened in the absence of Lomé.

15 The political dimension will become more important in the future. This will encompass a wide range of themes such as democracy, human rights, good governance, conflict prevention, arms expenditure, migration, drugs, organized crime and ethnic discrimination. These themes reflect a desire to get a better grip on the new interdependence problems, which is also an aspect of the FTAA process.

16 Fifty-eight of the 71 ACP states are presently members of the WTO.

17 For an overview of some of these discussions see McQueen (1998) and Solignac Lecompte (1998).

18 It is not clear whether the rule of thumb that is sometimes referred to, of

90 per cent coverage of total trade liberalization, refers to the average of trade in both directions. If 90 per cent is indeed an average, and taking into account the fact that EU liberalization already reaches more than 97 per cent, the ultimate ACP tariff dismantling could remain well below 90 per cent. This would leave considerable scope for continued ACP protection on infant industry, revenue or other grounds.

19 There is a qualification in the mandate to protect the interests of non-least-developed countries who are, for objective reasons, not in a position to join an FTA with the EU in 2004. Alternative possibilities will be examined to provide these countries with a new trade framework, which is equivalent to the current situation and in conformity with the WTO. This could be done by introducing more differentiation within the GSP (see the discussion on GSP in Chapter 5).

20 The ACP countries will anyhow lose their relative advantage in comparison to the Central and East European countries that have entered into Europe agreements and other developing countries that accept FTAs (for example, the Mediterranean countries).

21 This is illustrated, for example, in the debate on the recent United States initiative towards Africa. Improved access to the US market is offered to countries that consolidate trade liberalization. However, there remain important constraints on textiles, reducing the value of the offer for the African countries.

22 In small economies, many customs duties may not be protective, because the products on which duties must be paid cannot be produced efficiently locally. Such duties are, in fact, disguised consumption taxes and may be fully justified. Redefining them as consumption taxes, they should not be eliminated in an FTA. An example is cars, which cannot be produced efficiently in many small economies. But it can make a lot of sense to tax car imports.

7 Summary and Conclusions

1 There are cases of policies in small countries that could lead to reaction in other countries because they may have sizeable effects, for example in the area of intellectual property.

2 Mauritius is a member of several regional organizations, including COMESA, IOC and more recently SADC. Economic growth in Mauritius has been mainly export-led. Most export growth has been towards the North. However, Mauritius now has the capacity to export more to its integration partners in the region, when opportunities arise. But trade liberalization of its regional partners has been much slower than envisaged under the agreements.

3 From the beginning of European integration, customs revenue has been pooled and used for Community or Union level policies. The low and declining level of customs revenue probably explains why there was never much controversy on this subject. At present, customs duties cover a relatively small part of the EU budget (around 20 per cent), the largest part of the budget is being collected as a share of the Value Added Tax base. The EU budget itself is relatively small as a share of GDP, at around 1.2 per cent, or less than half of defence expenditures, for example. Another example of pooling of customs revenue is the Southern African Customs Union (SACU). In fact, South

Africa collects almost all the revenue and pays the other member states according to an agreed formula. The SACU reform is at present being negotiated and the revenue pooling and sharing is a key topic for the small member states.

4 There is an obvious concern to preserve sovereignty. Regional integration is often presented as giving up sovereignty. Two observations can be made in this regard. First, globalization implies an inevitable loss of sovereignty in relation to economic policies. Second, regional integration is not about giving up (what is left of) sovereignty, but rather about exercising and sharing sovereignty in a wider context. Regional integration may, in fact, help to recapture sovereignty in some areas where collective action is more effective than unilateral action.

5 If there is a substantial and measurable redistribution of customs revenue among member states a compensation mechanism can be set up. An example is the 'solidarity levy' set up by the UEMOA countries. A percentage of external tariff revenue is set aside for budgetary compensation.

6 Some of the EU's arrangements, such as those for sugar and bananas, are actually paid for by the European consumers through higher prices.

7 In the case of small developing economies entering into deep integration with the North, one cannot really speak of sharing of sovereignty, because the weight of the partners is so unequal. The situation is quite different for South–South integration, where it is correct to speak of sharing sovereignty.

Appendix A: Regional Integration Arrangements Involving Developing Countries

1 This review does not cover organizations that have not been active recently for a variety of reasons. These include: the Mano River Union (MRU) comprising Guinea, Liberia and Sierra Leone; the Economic Community of the Great Lake States or in French the 'Communauté Economique des Pays des Grands Lacs' (CEPGL) involving Burundi, Rwanda and the Democratic Republic of Congo; and the Arab Maghreb Union (AMU) to which Algeria, Morocco, Tunisia, Libya and Mauritania belong. Even though the tasks of the Intergovernmental Authority on Development (IGAD) grouping countries in the Horn of Africa (Djibouti, Ethiopia, Eritrea, Kenya, Somalia, Sudan and Uganda) have recently been broadened to cover trade integration as well, it is not reviewed because, so far, not much has happened on this subject. The Indian Ocean Commission (IOC), comprising Comoros, Mauritius, Madagascar, Seychelles and the French Department of Réunion is not included because its main activities are in functional cooperation. More detailed descriptions of regional integration in Africa on which this overview draws can be found in Bach (1999), Faroutan (1993), Holden (1998), Maasdorp (1996) and Oyejide *et al.* (1997). A broad analysis of regionalism in Africa was recently prepared by Asante (1997). Drawing on his experience as senior adviser to UNECA he specifically sets out the historical context and the present challenges for regional integration initiatives in Africa.

2 Membership in this list and those that follow reflects the situation around the end of 1998. For countries that recently joined the arrangement, the year of accession is indicated.

3 Besides its central role in SACU and its membership of SADC, South Africa

maintains a set of bilateral agreements in the Southern Africa region (for example, with Mozambique, Malawi and Zimbabwe). This set-up can lead to a 'hub-and-spoke' system, benefiting mainly South Africa. Some of these agreements imply tariff preferences, such as the one with Malawi. But in the case of Zimbabwe, preferences were in fact reversed to the discontent of Zimbabwean exporters.

4 The FTAA is examined in Chapter 6. ALADI is not included in the organizations reviewed because its economic integration role has been overtaken by the other groupings, even though it remains the broadest Latin American forum to discuss integration matters. The Group of Three (G3) agreement, signed in 1995 between Colombia, Mexico and Venezuela is not included because it contains no small economies and its future role is not fully clear. The Association of Caribbean States (ACS) was founded in 1994 following an initiative of the CARICOM Heads of State. It involves all the member states of CARICOM, CACM and the Group of Three plus the Dominican Republic and Cuba. The objectives of ACS include both economic integration and functional cooperation (Gill, 1995). Because it is not yet possible to say whether the ACS will become a significant player on regional integration matters, it also is not discussed separately. More details on regional integration in Latin America and the Caribbean can be found in Bouzas and Ros (1994), Bulmer–Thomas (1998), Lipsey and Meller (1997) and Nogues and Quintanilla (1993).

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Index