

THE REGIONALISM IN THE WORLD ECONOMY : NOVEL EXPECTATIONS FROM AN OLD HABIT¹

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Abstract

World economic relationships have recently been transformed by a process of globalisation whereby economic activity between nations and blocs of nations has become influenced by and (arguably) inextricably linked to the resurgence of the regional integration arrangements (RIAs). This article postulates that, despite the fact that regional bloc formation is not something new, the old theory and practice of regionalism cannot adequately describe the spirit and structure of modern RIAs. This study attempts to assess what countries expect to gain from membership of RIAs and tries to distinguish the motives and forces which derive them towards such organisations. In this respect, modern RIAs are compared with the initial, post-war, model of regional integration. The authors seek to establish that, as regional economies have become increasingly interdependent and homogenous, ever deeper regionalism has become the favored means of economic regulation unless prompt and wide-ranging multilateral solutions are available to reverse this trend.

1. Introduction

It is a self-evident phenomenon that the economic activity of the world is becoming increasingly globalised within a complex framework of internationalisation. International trade has grown consistently faster than world production. World visible

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exports have increased on average, by 6 percent annually in the period 1990-1995. The lion's share of this increase is attributable to a group of sophisticated goods requiring ever higher technologies and a more integrated system of production, such as office equipment, telecommunications, and transport vehicles. Combined world trade in visibles and invisibles already exceeds \$ 6000 billion. Capital flows augment this figure even more. Over the last two decades, the world has witnessed a sudden, dramatic surge in the level of foreign direct investment (FDI). Outward FDI of the OECD countries increased annually between 1985 and 1995, from around \$ 60 billion to around \$ 300 billion. As the WTO Annual Report of 1996 puts it "the keen interest in FDI is also part of a broader interest in the forces propelling the ongoing integration of the world economy popularly described as *globalisation*".

Another noteworthy aspect of this trend is the fact that the production processes of and increasing array of products involve plants not in a single location but in many different parts of the world, often involving a miscellany of disparate countries. The term "national good" has become an ambiguous concept. This fragmentation of the production side is also reflected in the way goods are marketed. As Lawrence (1996: 19) clearly indicates, the technological innovations led to undertakings dissipating their fixed costs by increasing their sales to a larger community of consumers, thus requiring, greater access to markets outside their domestic ones. Arguably, the result is a borderless economy with a *new division of labour* with geographical connotations and consequences.

Nevertheless, whilst a more functional economic integration is apparent one cannot say that this process has been painless. This era of change has not been without turbulence and turmoil in the world economy. Unemployment soared during 1970s and early 1980s. A reactionary wave of protectionism in world trade shrank the exports of both developed and developing countries. The introduction of non-tariff barriers in their severest forms in the name of the fair trade arguments were one of the consequences of the tensions in the international trading and monetary system. The financial problem, on the other hand, is a persistent problem. The latest financial crisis started in Asian financial markets. The crisis is not a local problem, but has repercussions in other parts of the world. It is indeed no exaggeration to say that *global markets have global problems*.

Although the process of global integration is dynamic, the mechanisms for managing the world economy in a sustainable way lag behind. The pace of market globalisation exceeds the ability of governments to legislate for the framework of rules and regulations necessary to ensure stability. As the problems become more globalised their solutions need an increasingly integrated and diverse approach. A solution at local or national level might be possible for some of the issues but for others a global outlook is essential.

Before analysing the possible approaches to this problem, it is necessary and helpful to take a brief look at the intrinsic reasons for globalised problems. The domestic economy generally needs domestic regulation. National governments are expected to provide the tools and systems to prevent market failures. This type of regulation is possible through domestic institutions which have authority over fiscal, monetary, commercial and similar economic policies. Sometimes, this is not enough because the failures have an international character. Stability and sustainable economic relationships in international economic matters may require inter-governmental co-operation. However, such co-operation, no matter how helpful it is, might not be a desirable process by all the parties and this leaves the problems unsolved. Therefore, regulatory processes are sometimes institutionalised around international economic regimes with their norms, principles, rules and procedures². The Bretton Woods institutions (the IMF and the World Bank) and GATT have operated as the principal bodies of the international monetary, finance and trade systems. Nonetheless, in view of the current phase of change in the world economy and the growing interaction and interdependency of global economic forces, perhaps these ageing institutions should be transformed into one coherent body³.

For example, the Uruguay Round of multilateral trade negotiations has been completed and brings a fundamental restructuring to the old GATT trading system. The multilateral process compelled the international community to operate in a rule-based system. Today, more than 130 countries are members of the World Trade Organisation (WTO), representing almost 90 percent of world trade and a similar proportion of the world's GDP, and all of them participate in this process. The establishment of WTO as a permanent successor to GATT is essential for the further liberalisation of world trade, serving as a forum for negotiation and equitable dispute settlement and for curbing the use of protectionist and discriminatory measures in trade relations.

At the same time the world economy has, in the last decade, witnessed a strong *revival* of regional trade arrangements. These have become fashionable, although they are not new to the world economy. Various *regional integration arrangements (RIAs)* began to emerge in different parts of the world between member countries of the WTO. Naturally, it seems unclear at first sight as to why such countries are still willing to participate in regional trading arrangements in a world that is al-

2 See Krasner (1982) and Ruggie (1982) for a good analysis of regime theories.

3 There has been a large debate concerning the restructuring of the world economic system upon the effects of globalisation. The post-war period institutions have therefore been taken into a close scrutiny. There is a voluminous literature concerning the GATT regime and the world trading system. For the discussions see especially Jackson (1990); Bhagwati (1991); Finlayson and Zacher (1982). For the Bretton Woods institutions, see Holland (1994), Haq et.al. (1995) and Cavanagh et.al. (1994).

ready globalising. Does the WTO's brand of multilateralism not satisfy the expectations? This is, of course, a crucial question and the answer is evident in the motivating forces behind the process of *regionalisation*.

This study comprises three sections. Firstly, it describes the transformation in the motivations that led many countries to take part in RIAs. The succeeding section further evaluates these motives within the major RIAs. The final section brings conclusive remarks concerning their role of regionalism in the harmonisation of divergencies in national policies.

2. Regional Motivations : The New versus the Traditional

Traditional trade theory argues cogently that completely free trade maximises global welfare. Nevertheless, its propositions as to the implications of regional schemes are vague. It may divert trade as well as create it due to its discriminatory nature. For some⁴, removing trade barriers between a group of countries without raising barriers to other trading partners seems to be the right step to take. The economists, then tried to find assumptions under which a net trade creating area might occur⁵. However, generalising such assumptions may be dangerous. There are no strict rules and an empirical case study for each is necessary. The experience of the post-war period indicate that RIAs have not *always* been successful. The first wave of such arrangements, especially among the developing countries, during 1950s and 1960s (which we may call the first or "*old wave of regionalism*") ended in disappointment. As Bhagwati (1992) observes, it "virtually died by the end of the decade, except for the original European Community and EFTA".

More recently, there has been a sudden interest in similar initiatives, especially during 1980s and 1990s, which we may call the "*new wave of regionalism*"⁶.

4 See for example, Dornbusch (1990 and 1993); Lawrence and Litan (1991); Bergsten (1997).

5 This is a reflection of the Kemp-Wan approach. However, one should bear in mind that there are no regional trading arrangements in practice that do not cause any trade diversion. The fact that the trade created is larger than the trade diverted, thus increasing the world's welfare, does not remove the case that there will, eventually, be countries that end up worse as a result, as Mundell (1964) first argued. These are, of course, the countries outside the region. The only solution to this is an "open" regionalism. According to this assumption, more open regional trading blocs are better than the closed ones. The most open region is complete free trade for the whole world where resource allocation is almost perfect. Therefore any regional trading arrangement is inferior to a multilateral process such as the WTO negotiations. In the theoretical sense, therefore, such initiatives are assumed to be "second best". It is this thinking that led Lipsey and Lancaster (1956) to state the "general theory of the second best".

6 For a general survey of regionalism in the world economy, see Anderson and Blackhurst (1993); de Melo and Panagariya (1992) and Demaret, Bellis and Jimenez (1997). A large literature exists for specific RIAs. For more information, see Akman and Dartan (1997).

In Europe, the European Community has been transformed into the European Union with a fully-fledged internal market. The uniting of Europe has created a single regional economy that accounts for about 40 percent of world's trade. The EU now has many regional ties with its surrounding neighbours. The three North American countries, namely the US, Canada and Mexico signed the North American Free Trade Area (NAFTA) in 1992, bringing their economies into a closer integration. As regards Latin America, progress towards closer regional ties has also been evident in recent years. New initiatives have revived established ones, such as the Andean Pact and CACM and fostered brand new ones such as MERCOSUR, the fourth largest RIA in the world. In Asia, ASEAN, which now has a significant regional economic role, is seeking freer trade area. There is some prospect of the eventual emergence of a larger Asian economic community. COMESA seems to be an ambitious regional grouping in Africa. Moreover, attempts at inter-regional integration have also become important. Asia Pacific Economic Co-operation (APEC), as a co-operative effort in a large area of the Pacific Rim, was established as a forum to discuss common problems and develop more co-ordinated policies, and a Free Trade Area of the Americas (FTAA) is in the pipeline.

The forces driving these recent developments are radically different from those which drove the first wave of regionalism in many respects. Let us examine them briefly:

1. *The desire to integrate into the world economy and search for improved access to other markets* : The first efforts at regionalism were generally ill-fated arrangements between the developing countries as a reaction to external effects and an extension of domestic import substitution policies under the philosophy of the planned economy. The members of such RIAs had a tendency of offering each other access to their markets only in those products which they could not produce domestically. The overall objective was to keep the region as self-sufficient as possible. The regional ventures among members having similar costs of production for similar commodities with similar factor endowments had a potentially small welfare improving character⁷. Also, because groupings like the EAEC (Langhammer, 1992), the Andean Group and LAFTA had restrictive structures allowing members to continue to protect the domestic industries, they failed to achieve the potential gains.

The changing economic climate and ideology of the early 1980s forced countries to pursue more open policies leading to more liberalisation in trade, a more hospitable attitude towards foreign investment, less governmental and more market or-

7 Think that the demand elasticity for the products of a country with a similar factor endowment would be less of reducing the potential for trade creation.

ientated solutions⁸. The new conventional wisdom was to replace import-substituting policies with export promoting ones. Therefore, a larger access to foreign markets became the objective. This was not only the case for the developing countries but also a phenomenon that we can observe in the demands of developed ones in their trade negotiations. The trade policies of large economies like the US, for example, started to place more emphasis on instruments forcing others to open their markets. Section 301 of the 1988 Omnibus Trade Act of the US penalises those which allegedly close their markets to American products (Bhagwati and Hudec, 1991). This export-oriented strategy was not easy to implement at the global level due to the imperfections in the then GATT system. Therefore, a revitalised and reformed GATT was necessary. RIAs increasingly became a means of complementing this strategy and accelerating the process of change. In other words, regionalism was perceived as a substitute method of improving trade where global solutions were not feasible.

The theory posits that smaller countries are the biggest beneficiaries of free trade. Due to their tiny markets and limited resources, specialisation is essential. Therefore, they are dependent on the openness of foreign markets. Hence, stable market access for their exports is fundamental to their economic well-being. This is the principal aim of trading systems based on non-discrimination (i.e. most-favoured-nation principle) and multilateralism. However, in practice, the MFN principle handicaps smaller nations because larger countries are often unwilling to reciprocate. Extending MFN status to a small country involved granting similar concessions (eg. in tariffs) to all other countries, thus opening up the economy of the larger partner to much more competition in that commodity than was originally envisaged. Therefore, RIAs for small countries act as life boats where large countries would otherwise be more eager to open their markets to their goods without reciprocating to others outside the region. This explains why many East European and Mediterranean countries have entered into regional arrangements with their major market, namely the European Union. The same may be said for Mexico, which had an interest in joining NAFTA as soon as it acceded to GATT or Paraguay and Uruguay for their participation in MERCOSUR.

2. The incidence of new RIAs is both "larger" and "deeper" in comparison with the old regionalism. There are two dimensions to this:

Firstly, the old trade theory which underpinned the RIAs was mostly concerned with liberalising the trade regimes for industrial products and commodities. Inevitably, as these economies developed, so the issues of *foreign investment* and trade in *ser-*

8 Rodrik (1992) explains the reasons of the drift toward liberalisation policies in developing countries in 1980's in a compelling way.

vices became increasingly important. As the global competition intensified, market access became more dependent on new factors, especially for certain types of products. For the more developed RIA economies, service provision and its place in the trade regime, is now complementary to the issue of trade in commodities and manufactures. Firms know that a local presence outside their domestic markets can be a prerequisite for the successful marketing of their products. This is especially true for developed countries whose export composition currently includes a large proportion of products which need a more sophisticated approach to consumers. As manufacturing firms expand abroad, other firms providing complementary inputs and services (like financial services, advertising and consultancy) often seek to follow them.

Secondly, the new RIAs differ from those which arose under the old regionalism in that they seek not only to eliminate barriers to trade across national boundaries but often strive towards an altogether deeper form of integration⁹. However, once tariffs are removed, there remains a complex issue concerning domestic regulatory policies. The traditional approach assumes that this issue should be determined at a national level. Increasingly, however, globalisation creates pressure to reconcile the divergence in national economic policy with the interests of global regulation. This point will be elaborated upon later.

It is important to remember that the US and the EU both exerted pressure for services to be included in the negotiations of the Uruguay Round of GATT talks¹⁰. A General Agreement on Trade in Services (GATS) is the first multilateral trade arrangement dealing with the service sector. TRIM is another such a mechanism by which global regulation may be applied to trade and investment measures. However, once this mechanism becomes inadequate to cope with the aims and objectives imposed upon it and as the negotiating process becomes more complex, due to the increasing number of competing nations with divergent national interests, then regional agreements may come to be regarded as the operating on the right level for such issues to be resolved satisfactorily¹¹.

9 This is really what brings our definition of regional integration arrangements into its exact meaning. In theory and old practice only earlier stages of integration (albeit some exceptions like European Community and two association agreements between the EC - Greece and EC - Turkey anticipating further stages of integration) in the form of free trade areas and customs unions were explicitly mentioned in the related GATT Article XXIV. The new regionalism introduces a discussion of further and related issues not traditionally covered by the old.

10 For a detailed study of trade talks in these new issues in the Uruguay Round, see Finger and Olchowski (1987) and Schott (1994).

11 One of the most compelling reasons for including a comprehensive agreement on investment in the WTO –which is particularly essential for the debate over regional vs. multilateral approaches to liberalisation– is the need to establish common multilateral rules for the complex and overlapping web of bilateral and regional agreements currently in application. The WTO Report (1996 pp. 43-81) examines them in detail.

Indeed, many modern RIAs contain provisions with respect to investment, competition, services and internal taxation. This demonstrates the strong belief of those countries on the degree of liberalisation that may be achieved under regional auspices as opposed to the existing multilateral regimes. This explains why many RIAs are often seen as supplementing or even pioneering for the management of economic issues of global significance.

3. Private actors are more active in the new regionalism than in the old : Private organisations and institutions, such as multinational corporations, play a much greater role in shaping RIAs than they did in the past. This new aspect of RIAs has brought a more focused and concrete approach to how RIAs are shaped. Clearly, many multinational corporations view these RIAs as promoting their interests. In Europe, for large firms, a fragmented Europe will prevent them from benefiting from scale economies. Similarly, it was strong corporations which drove the NAFTA negotiations in the US and Canada. Indeed, it is not only private firms who have taken a keen interest in the way RIAs are drafted. Other interested institutions include the labour unions and non-governmental organisations (for example, pressure groups). These institutions seek to influence RIAs in fields such as immigration, labour adjustment policy, environment and investment for their interests, but their involvement in the RIA negotiating process seems to be a result of regional initiatives rather than a cause¹².

The principal supporters of free trade agreements seem generally to be the business councils. Private foreign investors call for investment to be included as they would be the main beneficiaries of an RIA covering such issues. The influential role of the IKV (Economic Development Foundation), a prominent representative of the Turkish private sector, in Turkey-EU relations in the establishment of Customs Union with the EU, is a good example of the role played by private organisations in the RIA negotiating process. Most modern RIAs have institutionalised the role of private sector even though many remain at the consultation stage. It is not therefore a surprise, for example, to see the "Pacific Business Forum" as an advisory body in APEC. In COMESA, an African RIA, the role of the "Committee of the Business Community and other Interest Groups" is emphasised as a separate organ of the Common Market.

It is clear, therefore, that domestic interest groups play a very significant role in the formation of regional arrangements. Those seeking to protect domestic industry may also be closely involved in obtaining diverse concessions to protect their industries against imports competition arising from other members and non-members

12 There were, of course, opponents of as well as supporters for NAFTA. As Hellman (1994, p.194) stated that in the US "The trade unions are joined in their opposition by an assortment of human rights advocates and environmentalists, as well as small manufacturers and growers who fear they will lose out to cheaper Mexican imports".

of RIAs. The European (EU) manufacturers in sensitive areas such as textiles, clothing, chemicals, foodstuffs and steel were effective in keeping the level of protection higher for like products from Central and Eastern Europe with which the Union had "Europe Agreements". As Hoekman and Kostecki (1995) argue, protection-seeking lobbies benefit from large returns under RIAs as they have larger protected markets at a regional level. These protectionist groups, at a national level, may establish region-wide organisations such as industry associations or private lobbying groups at the regional level. Many industries in the EU have "Eurolobby" groups such as Eurofer for steel, CEFIC for chemicals or CCMAC for cars (Schuknecht, 1992). In MERCOSUR, the exemption of certain goods in special lists from the general tariff liberalisation are partly due to the pressures from strong domestic producers.

3. The Regional Integration Agreements in Practice

The regional integrations are becoming giant trading units. The value of total exports and imports of the EU (15) and APEC are above 2.000 billion dollars whereas it is over 1.000 billion dollars for NAFTA. The intra-regional trade is also increasing in almost all major RIAs. Its share is above 70 per cent for APEC and 62 per cent for the EU. For others it is also rising (see Annex for merchandise trade of selected RIAs in 1990s). The RIAs not only possess a commercial character but extend into the economic sphere.

3.1 *The case among the developed countries*

In Europe, the European Union (EU) in its current form is a monument to the vision and dedication of its founders. It is the culmination of a unique project to pool a certain amount of its members' economic and political sovereignty in an effort to integrate a vast range of its members interests. The Treaty of Paris established the European Coal and Steel Community in 1951, centralising control of each members' coal and steel production. The Treaty of Rome in 1957 established the European Economic Community and the European Atomic Energy Community. Latterly, the Single European Act 1986 and crucially the Maastricht Treaty 1992 consolidated this unity by binding Members States' economies and sovereign interests more closely than any preceding conventional agreement between sovereign states.

The EU began life as a customs union with limited supranational powers. Since then, not only has its membership increased from six to fifteen, but its economy has become a single market with most members adopting common policies under a similar economic philosophy. European Economic integration is founded upon the principal of internal trade liberalisation coupled with a common external trade policy. Integration in the EU has undergone, broadly, four stages of development (Levy, 1994: 216 et seq).

Firstly, customs duties and quantitative restrictions were eliminated. The legislation to complete the customs union envisaged by the Treaty of Rome was in place by 1968, introducing a common external tariff.

Secondly, in 1973, the EC widened to admit the UK, Denmark and Ireland. Greece was admitted in 1981, followed by Spain and Portugal in 1986 and finally Sweden, Finland, and Austria in 1993. The Community adopted an open policy vis-a-vis potential members. Today, the enlargement process is still an essential element of European integration. Whilst placing a great deal of emphasis on its policy of "deepening", the EU also pays attention to the issue of horizontal integration or "widening".

Thirdly, the implementation of the Single Market in 1992 ("Europe 1992") marked the completion of the internal market for the free movement of goods, services, capital and labour. The purpose of the Single European Act was to complete the process of internal trade liberalisation that had begun in 1958.

Fourthly, the process initiated by the Single Market culminated in the ratification by Member States of the Maastricht Treaty. If current plans come to fruition, this process will become further advanced, turning the EU into an economic and monetary union (EMU), perhaps by the end of the century.

In 1996, the external exports of the Fifteen (excluding trade between Member States) amounted to more than \$ 798 billion. The Fifteen accounted for 20 per cent of total world exports compared with 15.5 per cent for the US and 11.8 per cent for Japan (WTO, 1996: 4).

During the 1980s and 1990s the EU negotiated a series of RIAs with non-member countries under a "hub-and-spoke" regime¹³. These agreements established free trade areas (known as "*Europe Agreements*") with third countries, such as the countries of Central and Eastern Europe and a *European Economic Area (EEA)* with EFTA states¹⁴.

During the second half of the 1980s, the EU's relationship with Central and Eastern Europe changed dramatically. The collapse of socialism led to the removal of the political barriers that once separated the economies of the Continent. As the Soviet Union eventually disintegrated and German reunification was achieved, so the EU had to deal with the new states. The EU (then the EC) has since negotiated Eu-

13 In a "hub-and-spoke" structure there are "spoke" countries (i.e. the associates) each attempting to become the members of a large "hub" (the European Union) at the centre (Henning et.al.1994, pp.94-96). EFTA, another hub, has fallen off rapidly after the EEA Agreement and the accession of some of its members into the EU, leaving the latter as the sole hub in Europe. In this structure, the spokes are not necessarily connected with each other by RIAs. For more on "hub-and-spoke" structure see, Hoekman and Kosteci, 1995 and Wonnacott, 1991.

14 The EEA today consists of only the EU, Iceland and Norway after the accession of former EFTA countries namely Austria, Finland and Sweden. Liechtenstein participates as an observer country. For more on EEA see, Wijkman in Henning et.al. (1994).

rope Agreements separately with Czechoslovakia, Poland and Hungary in 1992 and with Romania, Bulgaria and the Czech and Slovak Republics in 1993. These Agreements operated on an interim basis until their ratification in 1994 and 1995. In accordance with their terms, most industrial products originating from signatory countries enter the EU market free of tariffs and quantitative restrictions¹⁵. Subsequent to the Europe Agreements, trade between the EU and the CEEC grew but the share of these countries in the total trade of the EU remains small.

When the EU has also finalised an agreement establishing a European Economic Area with EFTA, a bloc initially established as an alternative RIA to the EC, it included over 400 provisions and like the Europe Agreements envisaged a full economic integration between the two sides. The share of the EFTA countries has always been significant in extra-EU trade since 1960. EFTA represented over one-fifth of total Community exports until the 1990s and almost a quarter in the early 1990s. Its share in total imports of the EU rose from 15 percent in 1960 to 23 percent. Traditionally the EFTA countries have been the closest in the external relations of EU Members States. Following the accession of Austria, Finland and Sweden, only Norway, Iceland and Liechtenstein remain as EEA countries¹⁶. The EU has finalised the Customs Union with Turkey, whose eventual accession is on the agenda¹⁷.

This complex web of regional arrangements is complemented by reciprocal links between EFTA states, Eastern European and Mediterranean countries. The preferential scheme of the EU covers association agreements with neighbouring Mediterranean countries (Maghreb and Mashreq as well as Cyprus and Malta) and the ACP countries under the Lome Convention which grant privileged access for certain of their products to the European market (note that these preferential agreements are not regarded as RIAs within the context of this study). Though the share of the Mediterranean countries in the total merchandise trade of the EU has been steady at around 10 percent, the significance of the ACP countries diminished from almost 10 percent in 1960 to 3-4 percent during the 1990s, although the EU continues to have close links with them. In 1995, a Euro-Mediterranean Partnership was

15 The agreements include several issues in addition to trade provisions. They include measures concerning the free movement of services, workers and capital and economic and monetary cooperation, thus extending them far beyond the traditional free trade areas into deeper integration. Actually, at the European Council meeting in Essen in 1994, the EU decided on a strategy for the eventual membership of these countries. The EU started negotiations with some of these countries following the Luxembourg Summit in December 1997.

16 Switzerland has refused to take part in the EEA after a negative vote in a referendum in 1992. See supra note 14.

17 The Customs Union entered into effect as of January 1, 1996 based on the Decision of the Association Council 1/95 dated March 6, 1995. This union had been envisaged in accordance with Article 2 of the Ankara Agreement (1963), establishing an association link between Turkey and the then EEC. For a concise review of Customs Union Decision see Kabaalioglu (1997). The Luxembourg Summit results in 1997, did not give affirmative signals for the final accession of Turkey into the EU for a foreseeable future.

established in Barcelona whereby the EU decided to form, by the year 2010, a free trade zone with the countries in the region under which manufactured products will circulate freely and the trade in agricultural products will be gradually liberalised.

The "spoke" (those with which the EU has a kind of RIA) and "preferential" countries constituted 38.5 percent of the total imports of the EU in 1994. This compares with 33.4 percent in 1960 and over 40 percent in 1985. These countries, in return, represent over 40 percent of EU export markets, though this has been higher since 1960. The figures show that RIAs and preferential schemes with these countries have not brought the expected increase in their traditional trade patterns with the EU. This may be explained partly by the fact that these agreements still contain protectionist clauses especially in sectors that both sides deem to be sensitive for their domestic markets. Secondly, it should be appreciated that trade with the rest of the world is simultaneously being liberalised under GATT at the same time.

In North America, ever since 1846, when Great Britain abandoned colonial preferences in favour of free trade, Canada has tried to obtain maximum access to the US market. The 1965 Auto Pact and Free Trade Agreement (CUFTA) of 1989 were signed to institutionalise the state of affairs. Negotiations for a more comprehensive free trade agreement had been underway since the 1960s. CUFTA was the forerunner of *The North American Free Trade Agreement (NAFTA)*. In February 1991, the US, Canada and Mexico together declared their intention to create a trilateral free trade zone. NAFTA was signed on 17 December 1992 and implemented on 1 January 1994. NAFTA contains no provisions for political institutionalisation, instead confining itself to development of a new free trade area and the resolution of issues such as immigration control. One of Mexico and Canada's chief concerns was that they should not concede sovereignty to the US- the only participating superpower. By confining the project to addressing only specific economic issues, problems of policy adjustment and economic development were the last to be resolved independently by each of the parties. Institutionalisation on the EU model with its accompanying surrender of sovereignty was thereby avoided.

The scale of NAFTA is enormous. It is now a market of 360 million people with an annual GNP in excess of \$ 6 trillion (Bello and Holmer, 1993: 591). Its objectives may be summarised as follows: removal of trade barriers, promotion of fair competition, increase in investment opportunities, granting of appropriate legal protection for commerce, introduction of appropriate arbitration mechanisms and the promotion of trilateral and multilateral co-operation.

The NAFTA signatories' principal aims are to completely abolish trade barriers between themselves and thereafter to permit the free movement of capital in 15 years, starting from 1994. Free movement of labour is not one of NAFTA's aims due to Mexico's vast population and small per capita income. Furthermore, certain "sen-

sitive sectors" have been excluded from the ambit of the agreement¹⁸. However, there is scope for a degree of harmonisation in the fields of environmental protection and labour regulation (Harrison and Weigel, 1993; Hufbauer, 1993).

Trade between the US, Canada and Mexico was extensive long before NAFTA. Indeed, trade between the US and Canada generates the world's largest bilateral trade flow (Proff, 1993: 279). The USA constitutes the largest export market for both Canada and Mexico, although US exports to these countries represent only a small fraction of the US total. Nevertheless, Canada is the largest trading partner of the US, with Mexico in third place. Trade between Mexico and Canada is very small in comparison.

The driving forces behind NAFTA are diverse and reflect the motives lying behind the new regionalism discussed above.

Canada's chief problem is that its internal market is too small to make mass production of high value added products a viable proposition. NAFTA gives Canada the chance of access to a wider market her economy needs. In the long term, this should result in a more diversified, internationally orientated Canadian economy. Furthermore, membership of NAFTA allows Canada to sidestep the increasingly protectionist trade regulations of the US. This is crucial for the Canadian economy, given its dependence on the US market (Trebilcock and Howse, 1995).

Mexico's interest in NAFTA is chiefly concerned with attracting maximum direct investment as a means to rapid industrialisation. As Eastern Europe opened up and East Asia grew spectacularly during the 1980s, so international capital flows tended to move towards these areas rather than Latin America and Mexico in particular. NAFTA is expected to change this. Mexico's large and rapidly growing population meant that a vast number of new jobs must constantly be created in the country. Mexico's efforts in this respect are hampered, however, by rampant inflation and the effects of the attendant deflationary fiscal policy. Mexico's already vast burden of public sector debt means that raising fresh capital on international markets is difficult and expensive. Foreign direct investment capital is therefore crucially important. Mexico's other reasons for entering NAFTA are similar to Canada's, namely access to the US market and the avoidance of US protectionism.

The United States' prime motivation for instituting NAFTA was a desire to demonstrate its dissatisfaction with the current trade system under GATT. Treatment of trade in services is a fiercely contested issue under GATT and the US deliberately negotiated the explicit inclusion of services under NAFTA. In the Canadian market,

18 This demonstrates how private interests play a role in the formation of RIAs (see, Hoekman and Leidy, 1992. For a general survey about protectionist dynamics in RIAs see Akman and Dartan, 1997).

the US gained valuable concessions in this area, although its position was already dominant. By including Mexico in NAFTA, the US has laid down a clear challenge to other newly industrialised economies to liberalise trade in services, where of course, the US has a comparative advantage. Mexico's incorporation also gives US industry access to an already large market whose population is expected to reach 100 million by the year 2000. Trade was also important for Mexico, since the US accounted for almost 80 per cent of Mexico's external trade during the 1990's.

As emphasised above, the newer generation of RIAs address a diversity of issues, from *immigration* to the *environment* (NAFTA being a good example). Mexico's lax enforcement of environmental and workplace safety regulations has caused problems in the US Senate. Without action in this area NAFTA would have been politically impossible.

There has been *massive migration* from Mexico to the US. Between 1960 and 1990, 15.1 million emigres arrived in the US, of whom 18.1 per cent arrived legally from Mexico. Many more entered the US illegally (Pastor, 1993: 11). A survey conducted in Mexico during 1986 found that 50 per cent of those interviewed had a close relative living in the US – representing around 40 million Mexicans (Lustig et.al. 1992: 178).

One of the principal arguments against NAFTA in the US was the fear that lower *standards of regulation* and *worker protection* in Mexico would encourage US industry to migrate, generating unemployment in the US. While NAFTA agreement is silent on immigration, this was one of the most hotly debated issues during the negotiations. At an *environmental* level, there were fears that Mexico's rush to industrialise would destroy the environment and add to the population of Mexico City, already one of the world's most polluted cities (Lustig et.al, p.181). In relation to environmental matters, the NAFTA Agreement allows each signatory country to maintain and enforce its existing environmental standards whilst giving each the right to prohibit entry of goods which do not meet its domestic regulatory standards (Hufbauer and Schott, 1993 and Morici, 1993).

NAFTA may yet extend further into Latin America. Indeed, at the Summit of the Americas, held in Miami in December 1994, all the leaders of North and South America (except Cuba) adopted a Plan of Action for the creation of a *Free Trade Area of the Americas (FTAA)* by the year 2005. Should the plan succeed, the FTAA will be a market consisting of 850 million people with a trade volume of some \$ 13 trillion. The FTAA will be created by a merger of the six existing subregional trade agreements, namely; NAFTA, CARICOM, MERCOSUR, the Central American Common Market, the Group of Three, and the Andean Pact.

Chile, the only country in Americas that does not formally participate in any RIAs, was formerly invited to join NAFTA as its fourth member at the Summit. She

has one of Latin America's strongest economies and has a better record in market liberalisation and general economic performance.

3.2 *The developing countries*

Ever since the conception of the modern GATT regime in multilateral trade, *developing countries* have looked at the prospect of regional co-operation with great interest. Article XXIV of GATT stipulates that "customs unions or free trade areas should facilitate trade between the constituent territories and not raise barriers to the trade of other contracting parties with such territories". This Article, except in a small minority of cases, has not been respected.

In 1979, an Enabling Clause (or Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries) was agreed. The Clause provides for regional arrangements among less developed countries for the mutual reduction or elimination of tariffs and nontariff barriers. However, unlike Article XXIV, this Clause makes no provision for obliging signatories of RIAs to desist from raising barriers to trade with third countries. Many RIAs among developing countries were based on this Clause such as Andean Pact, AFTA, COMESA, LAIA, MERCOSUR or SAPTA. It is interesting to note that so many countries as developed as Argentina, Brazil and Singapore, use this mechanism, which was devised for only the use of less developed countries.

Latin America has long experimented with some form of regional economic integration as a means of achieving accelerated development and reduced dependence on its powerful neighbours in the North. Import substitution policies have been applied to this end across Latin America. The philosophy underlying these policies has been that larger markets attract more investment and provide improved prospect for economies of scale and specialisation. The principal motivating factor, however, was based on nationalism and Latin American countries' desire to reduce their dependence on foreign imports and foreign markets.

Two broader regional initiatives, namely *LAFTA* in 1960 and *LAIA* in 1980, have prepared the field for further integration within the region. Nevertheless, they had only limited results due to the large number of heterogeneous countries and the dimension of the geographical area covered, the predominance of protectionist-import substitution policies- and lack of a common strategic vision that might have given them more motivation and political energy.

These initial attempts at integration broadly failed. The debt crisis of the early 1980s had a gravely damaging effect on the entire region. The monetary tightening which followed led to Latin American states reducing imports rather than exporting

their way out of trouble. The entire region saw a massive increase in protectionism during this period. By the late 1980s, however, a new mood had swept the region as new agreements were negotiated and existing ones revised. In 1980, LAIA displaced LAFTA whilst taking on many of LAFTA's more advantageous features, such as its provisions for regular rounds of negotiations.

There have been subsequent attempts at Latin American regional economic co-operation, including :

Central American Common Market (CACM), established in 1961 by El Salvador, Guatemala, Costa Rica, Nicaragua and Honduras by the Treaty of Managua.

Andean Common Market (ANCOM), created in 1969 by Bolivia, Chile, Ecuador, Peru and Venezuela by Cartagena Agreement. (Later referred to as *Andean Pact*).

Caribbean Common Market (CARICOM), founded in 1973 by the thirteen English speaking Caribbean island states by the Treaty of Chaguaramas.

CACM and ANCOM underwent renegotiation leading eventually to a clear growth in trade between the participants.

The most recent attempt of regional integration in Latin America had been *MERCOSUR* –an acronym for the *Common Market of the Southern Cone*– established in 1991 by the Treaty of Asunción. Its initial aim was the creation of a free trade zone between Brazil and Argentina by 1995. Paraguay and Uruguay feared that such an arrangement might adversely affect their trade with, until then, their largest trading partners. Argentina and Brazil accepted their request to be included in negotiations and the Treaty was signed on 26 March 1991.

MERCOSUR still has a long way to go before becoming a common market and free movement of labour remains a distant prospect. Completely free trade within MERCOSUR is not anticipated before the year 2000, though a common external tariff has been adopted. A full customs union is unlikely to become a reality until 2006 since Paraguay and Uruguay have been granted a slower compliance timetable. Initially, 90 % of trade in goods between the participants moved free of duty from 1995. MERCOSUR will eventually constitute a market of some 200 million people with a GDP of almost \$ 1.1 trillion, ranking it as the fourth largest such zone behind the EU, APEC and NAFTA. Within MERCOSUR, Brazil accounts for some 70 % of members' GDP and population. Brazil is commonly regarded as having Latin America's most advanced economy whilst Paraguay is considered to be the least industrialised with a per capita income of just \$ 1,850 (Fidler, 1997a).

In October 1996, Chile acceded to MERCOSUR as an associate member, adopting the free trade provisions of the Treaty though without enforcing the common

external tariff. Bolivia has also negotiated association on similar terms. Bloc-to-bloc negotiations began in 1997 with the Andean Pact countries for a free trade agreement. Whether Mexico will join remains uncertain - certainly, its position is made more complicated by its membership in NAFTA, which may in any case encompass most Latin American economies long before MERCOSUR negotiations can be concluded. Since coming into force, trade between MERCOSUR members has increased dramatically by an average annual rate of 27 percent between 1990 and 1995. MERCOSUR's trade with the rest of the world increased by only 7.5 percent during the same period. The intra-regional trade of MERCOSUR is now 20 percent. In 1990, this figure was just 9 percent. Much of this increase is due to increased trade between Brazil and Argentina, which increased fourfold between 1990 and 1996 to \$ 15 billion. Current projections anticipate this figure to double over the next 6 years (Fidler, 1997a).

Many *opponent* commentators claim that far from promoting world trade and economic efficiency, MERCOSUR is nothing more than a protectionist fortress, having a malign influence on multilateral trade and undermining the principles of GATT. They view the disproportionate increases in MERCOSUR's internal trade in comparison with the increase in its external trade as proof that the Agreement is hampering free trade between MERCOSUR members and the rest of the world. In a report to the World Bank Trade Division, Alexander Yeats found that intra-MERCOSUR exports had increased most rapidly in those sectors for which MERCOSUR has no natural comparative advantage. *Proponents* of MERCOSUR contend, however, that intra-MERCOSUR trade growth may be attributed to a rapid growth in the region's import of all resources since the liberalisation of the early 1980s. This is a doubtful point, and even MERCOSUR's most ardent supporters agree that imperfections remain and that there is necessarily an element of protectionism (Fidler 1997b).

In Africa, the expectation of economic gain combined with a desire to become more independent from previous colonial masters has led many countries to seek out some form of economic co-operation with their neighbours. Indeed, there had been a proliferation of such agreements during the old regionalism wave, particularly in Sub-Saharan Africa. The most important of these are as follows (Davenport, 1992: 235-236) :

West Africa has two associations of importance. Firstly, the *West African Economic Community (WAEC)* or Communauté Économique de L'Afrique de L'Ouest (CEAO) was founded in 1974 with membership drawn from the earlier Customs Union of West African States: Benin, Côte d'Ivoire, Mali, Mauritania, Niger, Burkina Faso and Senegal. Secondly, the *Economic Community of West African States (ECOWAS)* was established in 1975 by 16 West African Nations (including the WAEC/CEAO members): Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia,

Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo.

In Central Africa, the *Central African Customs and Economic Union (CACECU UDEAC)* was founded in 1964 by Cameroon, Gabon, Congo, Chad, the Central African Republic. Equatorial Guinea joined later.

Regional groupings in Sub-saharan Africa have failed, -mostly due to political instability, lack of economic critical mass and an inward-looking orientation causing a withdrawal from the world economy. The tariff eliminations and the common external tariff were made irrelevant by the implementation by member countries of varying import taxes and internal charges which discouraged intra-regional competition.

The WAEC appears to be Africa's most successful trade pact, reducing both tariff and non-tariff barriers and liberalising capital and labour flows. With the exception of Mauritania, member states share a central bank and adopt common limits on money supply and budget deficits. There is even a compensatory mechanism for redressing the economic imbalances produced by the system. Intra-regional trade levels recovered quickly from the crises of the late 1970s and early 1980s and at more than 12 per cent of total exports, thus representing a considerable achievement and an historically high level.

By contrast, the CACEU has not produced results comparable to those of the WAEC, although member states share the Central African Franc and have adopted the same investment code. Political disputes between members acted as a brake on economic gain and the common external tariff was often ignored as member states continued to pursue unilateral trade policies. Intra-regional trade was hampered and national infrastructure projects were promoted ahead of regional ones,

The most noteworthy RIAs in the region is *The Common Market for Eastern and Southern Africa (COMESA)*, founded by the Treaty of Kampala in 1993 and currently encompassing 23 countries, namely; Angola, Burundi, Comores, Djibouti, Eritrea, Ethiopia, Kenya, Lesotho, Malawi, Madagascar, Mauritius, Mozambique, Namibia, Rwanda, Seychelles, Somalia, Sudan, Swaziland, Tanzania, Uganda, Zaire, Zambia and Zimbabwe¹⁹.

African RIAs are something of a misnomer since they rarely achieve anything like full economic integration and seldom reap any of the benefits normally associated with such agreements (for example free trade areas or customs unions).

19 For Treaty of Kampala 33 I.L.M. 1067 (1994). COMESA is based on an original scheme of a preferential trade area established by 15 states in 1981.

COMESA countries have, however resolved to reduce trade barriers in order to establish a free trade zone by 2000 and a customs union by 2004. It has the ultimate objective of forming a common market in which members will have a joint adoption of macro economic policies, co-operate to develop a stable environment for foreign, cross border and domestic investment. COMESA aims subsequently to establish currency convertibility between its members and eventually, some kind of monetary union. In Lusaka summit in 1997, they agreed to replace the Unit of Account with the COMESA dollar. This pompous aim is an attempt to emulate the stages of European integration.

COMESA seems to follow a deeper integratory model by also addressing issues such as investment; free movement of persons, labour, services and the right of establishment; financial and monetary co-operation and the establishment of standards and certification. It seems to be more export oriented and more sympathetic to foreign investment and imports.

In Asia, historically, regional economic agreements have not been taken up with the same enthusiasm as elsewhere in the world²⁰. The *Asia-Pacific Economic Co-operation (APEC)* and *The Association of South East Asian Nations (ASEAN)* are the only examples of their kind in the region. Progress in this area has in the past been slow but is now accelerating. The ASEAN summit at Singapore in January 1992 laid down plans to establish a free trade zone, known as *AFTA*.

ASEAN was formed as long ago as 1967 by Indonesia, Malaysia, Singapore, Thailand and the Philippines. Brunei joined in 1984 and Vietnam in 1996. (Myanmar, Laos and Cambodia have been invited). From the creation of the association in 1967 until the beginning the 1990s, ASEAN was motivated by political rather than economic factors (Strassner, 1994: 289-98).

Between 1967 and 1992, ASEAN remained a very loose association with little being done to enhance economic integration between its members. Some measures were, nevertheless, introduced concentrating on trade liberalisation and industrial co-operation. By 1989, agreement had been reached on tariff reductions for 18,000 items. The impact of these concessions has been limited, however, accounting for less than 5 per cent of intra-ASEAN trade and most having little commercial significance (Dobbs-Higginson, 1995: 424). What is worse is the fact only about 17 per cent of total ASEAN exports have been attributable to intra-regional trade during the 1990s.

The end of the Cold War changed both the economic and political environment of the region. In the light of these changed circumstances, ASEAN's modest econom-

20 For more on the regionalism in Asia see Young (1993) and Pelkmans (1997).

ic ambitions metamorphosed in 1992 into plans for further economic integration. The leaders of ASEAN, however, agreed at Singapore to implement a free trade area by 2008 (Hilpold, 1996: 229). A preferential internal tariff has been introduced, aiming at a gradual reduction to less than 5 per cent on 15 groups of products within a 15 year period. As is often the case with trade agreements of this nature, however, there were two exceptions, trade in agriculture and services (Dobbs-Higginson, 1995: 428).

Nevertheless, ASEAN may turn out to be problematic in practice:²¹

Economic and political co-operation between member states may be hampered by structural and developmental differences. ASEAN includes, for example, Singapore, which is highly developed together with newly industrialised nations such as Thailand and more backward economies such as that of Indonesia. This diversity can only increase as more members are admitted over time, such as the Indo-Chinese states with economies which are predominantly agricultural (Kodama, 1996: 385).

A further impediment to increased regional economic co-operation is Asean members' concentration on trade with external, usually Western, economies. Indeed, it is this outward looking stance that has contributed to the region's economic success.

The economic emphasis within ASEAN has nevertheless increased since 1992, although it took 25 years to arrive at a consensus on AFTA and full implementation is still 10 years away. Even then, AFTA will not constitute a truly free trade area. Singapore is ASEAN's only truly free trade member, and indeed, Singapore owes most of its economic success to this policy. Excluding Singapore, only 5 per cent of ASEAN's benefits derive from any kind of preferential tariff (Panagariya, 1994: 817).

ASEAN traditionally has not been sympathetic to the concept of "integration" in a deeper sense. The countries in the region, notably Singapore, had generally more open economies compared to other parts of the developing world. While keeping this openness, the ASEAN countries now emphasise services (there is now a Services Framework Agreement) and investment matters (ASEAN Investment Region). It is no surprise that, under the new regionalism, an altogether different label was chosen for the future "The Agenda for a Greater Economic Integration".

3.3 APEC, an inter-continental integration movement

APEC (Asia Pacific Economic Region) was founded in 1989 and was the only scheme of its kind to be established until then. Its members now include the US, Can-

21 For more details on the internal and external factors, which make it difficult to develop a regional co-operation in East Asia, see Panagariya, A., 1994, "East Asia and the New Regionalism in World Trade", pp. 817-839.

ada, Japan, South Korea, Australia, New Zealand, ASEAN, Mexico, Papua New Guinea, Taiwan, China, Hong Kong and Chile. Russia, Peru and Vietnam are expected to join in 1998, bringing the total number to 21. APEC arose out of a pressing need to deal with a number of new economic and political phenomena and to reflect the future of the current global environment.

During the 1980s, increased trade and unprecedented levels of economic growth in the region led to increased economic interdependence. This in turn encouraged improved international co-operation. Moreover, the rapid growth of the smaller economies in the region led these nations to recognise the economic benefits of joining a regional organisation whilst enabling them to avoid being dominated by the larger regional neighbours.

The end of the Cold War provided added impetus to the need for improved regional co-operation, though there remain significant ideological differences between Far Eastern Asian nations – especially between China and her neighbours. Economic, if not political, reform has gone some way to mitigating these differences. China being the most obvious example. South East Asia and the Pacific regions are fast becoming economically integrated whilst remaining ideologically separate.

APEC has increasingly become a policy forum. It has become an active supporter of arrangements negotiated under the GATT-WTO regimes and has sought to discourage alternative regional arrangements. APEC has become an ardent advocate of the modern multilateral trade regime. As APEC develops, so it is likely to negotiate agreements with other trade organisations such as NAFTA. In this respect, it seems to be a promoter of, rather than an alternative to the WTO system.

Due to the cultural diversity of its members, APEC must avoid acquiring a cultural or ideological emphasis. Its success thus far has been due to its economic pragmatism and liberal outlook. As the region's other, smaller economies grow, so APEC should be encouraged to admit new members – India would be an obvious candidate. However, whether APEC will be able to avoid becoming a supranational organisation as it develops is as yet uncertain. It is most likely to remain international, flexible and expansive and may in the future give rise to some sort of free trade arrangement.

During the inaugural meeting in Canberra in 1989, members affirmed their commitment to the existing multilateral trade regime and to its increased openness and to the cultural and political diversity of the region within an expansive and flexible economic framework. Ministers attending the meeting announced funding and political support for projects including (Kodama, 1996: 369-371) the interrelation of investment, technology and human resources in the region together with traditional commercial matters such as trade liberalisation, improvement of data collection in respect of regional trade flows and economic development.

Significantly, APEC members expressed their willingness that China, Taiwan and Hong Kong should eventually become members.

In 1994, the Sixth Ministerial Meeting at Jakarta and the Second Leaders' Meeting at Bogor showed important progress in economic co-operation, though members maintained their original goals of GATT-consistency and intra-regional diversity. The APEC Leaders' Declaration of Common Resolve represented their agreement to aim for improved regional economic liberalisation and to establish specific deadlines. For example, APEC members should achieve free and open trade and investment by the year 2020. The deadline for industrialised economies is 2010 and for developing economies is 2020. Detailed arrangements for this ambitious and political viability remains uncertain (Kodama, p.375).

Given the difficulties experienced in the past by the EU, arguably an institution less culturally and politically diverse than APEC, the deadlines of 2010 and 2020 seem unrealistic, although the current pace of economic development in the region is unprecedented despite the recent crisis. The new version of Article XXIV in GATT 94 stipulates a transition period of ten years but this will depend on APEC choosing in the end to conform to WTO rules and its goal being complete economic liberalisation. APEC should extend liberalisation to non-members on a most-favoured-nation basis.

APEC leaders have defined their goal as "the actual reduction of barriers not only among APEC economies but also between APEC economies and non-APEC economies." They added that non-APEC developing economies would also "benefit from the trade and investment liberalisation in conformity with WTO provisions." There is ambiguity here, however, as GATT rules prescribe that any partial liberalisation at regional level be accompanied by reciprocal arrangements with outsiders, APEC should clarify whether it will develop along these lines or not.

In 1995, APEC leaders met at Osaka, Japan for their Seventh Ministerial Meeting. They reaffirmed APEC principles and a start was made on the liberalisation programme set out at Bogor in 1994. These principles are comprehensiveness, WTO consistency, comparability, non-discrimination, transparency, standstill, flexibility and co-operation. Member states also reaffirmed the principle of voluntary liberalisation – consistent with the main tenets of the WTO whilst maintaining flexibility in implementation. APEC members also agreed on the need for an arbitration regime for the resolution of disputes, although details remain to be finalised. At the Osaka Conference, APEC leaders laid down a flexible timetable for implementation of the new liberalisation project. A Framework laid out for implementation of an "Action Agenda" and early 1997 was nominated as the start date.

What will determine the future success of APEC will largely be the existence of a flexible and bureaucratically unobtrusive institutional structure considering the re-

quirements of the nations in the region and providing for an atmosphere in which the countries may develop constructive mechanisms for their problems for which intervention at the national level is inadequate and for which no suitable global regime yet exists. An "open" APEC will also escape the malign effects of closed blocs, such as discrimination.

4. Harmonisation Issue : Another Service of Regionalism?

GATT has long strived for, by means of its multilateral character, the elimination of measures directly limiting trade. Nevertheless, it has not been effective in preventing its members from applying measures that indirectly prevent or restrict trade, such as rules concerning packaging, labeling, health and safety regulations, various customs procedures. Nor has it wholly succeeded in preventing measures that may have an adverse effect on trade such as diverse policies related to regional development, subsidies to industry, national social security, environmental policies or changes in fiscal policies. As has been stated before, these have been areas which have traditionally been regarded as the province of national governments' domestic policies.

The substantial reduction in tariff levels, down to level of single figures in most developed economies, and further scrutiny of quantitative restrictions has led many exporting countries to claim, under the rubric of *fair trade*, that the above measures may well serve protectionist purposes. As Bhagwati (1993) observed "the fair trade notion now extends to *any* foreign policy that is different from one's own" and "this result in demands for getting these policies *harmonised*".

Two of the common arguments concern labour and environmental regulations. In developed economies, many domestic commentators have already begun to propose that under the free trade, more stringent domestic rules on the labour and environmental standards will make their production expensive and uncompetitive in comparison with like products from countries where such rules are more lenient²².

What the proponents of the fair trade approach advocate is the harmonisation of divergent domestic regulatory policies. This could either be done by imposing one's own policies on others thus forcing less regulated countries adopt the policies of the other or alternatively to set multilateral (globally recognised) rules which would be obligatory for all. Nevertheless, Harmonisation in GATT/WTO system is basically limited to measures directly affecting trade in goods and does not concern many do-

22 Thus, it is possible to understand why some groups raise the "fair trade" argument and try to protect domestic industries in the name of protecting the workers and the nature.

mestic policies which may indirectly affect trade. In other words, harmonisation is generally outside the scope and competence of the WTO, except in limited areas. Therefore, for fair traders, the approach at the global level is presently inadequate.

On the other hand, regional integration arrangements may make progress in harmonising domestic policies more effectively than governance under the WTO regime. However, RIAs may assist those protection-seekers who attempt to level the playing field²³. Indeed, during the NAFTA negotiations, US environmentalists sharply split into two groups (Esty, 1994). The first group claimed that free trade under NAFTA would encourage environmentally damaging industries in countries with lower standards, thus contributing to further damage to the environment. This group also claimed that freer foreign investment would mean reduced incentives to develop less environmentally harmful industrial technologies. The second group supported RIAs as a means of carrying out their aims from within. Esty claims that this second group has succeeded in putting relevant provisions and special side agreements into NAFTA.

RIAs also help their members to impose their own terms on newcomers. The European Union, for example, may require her Eastern neighbours to adopt the same regulatory policies. As Winters and Wang (1994) stipulated, The Europe Agreements impose EU competition law on aspirant countries, implying a degree of control from Brussels. This has been the experience of Turkey in the Customs Union under which Turkey is expected to harmonise her laws in fields such as competition, intellectual property, taxation and public procurement with those of the EC (see Kaabalioğlu, 1997).

RIAs, exerting both a negative and a positive influence in this respect, have played a unique role in the process of integration of the economies. From a broader perspective, regionalism is a dynamic instrument through which divergent interests may be balanced. This may be regarded as the *positive* element of regional initiatives. For large economic entities such as multinational companies, the regional path is often an expeditious means of enlarging markets as well as improving production efficiency. As Falk (1997) demonstrates, regionalism "is one approach to reconcile the quest for global governance (of a complex set of interrelationships) to a lesser extent while the preserving cultural diversity²⁴.

23 This is, indeed, the main concern of the multilateralist approach. RIAs are abused to accommodate purposes that cause more protection rather than serving to liberalise trade.

24 Paranthesis added. The diversity in culture here reflects national differences in the way of doing things in both the economic and social realms. This is apparent in the different and sometimes conflicting legislation of countries.

For others who seek ways of attaining an improved degree of harmonisation among a given subset of countries, regionalism constitutes a means of achieving that even if such an aim is not practical at a global level²⁵. RIAs may render themselves as alternatives to the multilateral process and an opportunity for strong countries to exert an hegemonic role over smaller ones which are obliged to follow. This is a double-edged sword. It is good that RIAs may help some nations to acquire new rules and institutions which they might otherwise have had difficulty in acquiring by themselves. Today, for example, all countries seeking to join the EU must consider ways of converging their economies towards the Maastricht criteria for economic and monetary union. Turkey acquired a competition authority only after the inauguration of the Customs Union with the EU. The *negative* side is that the stronger members of RIAs often succeed in influencing policies and institutions of their partners which are unrelated to trade. For example, anti-dumping regulations are used by some RIAs as an instrument of social policy (i.e. social or eco-dumping). Such regulations often exert a malign influence on neighbours who are too weak to fight back.

* * *

25 Attempts to set rules at the multilateral level are not totally absent but not easy either. Remember, US and French proposals to align trade and labour standards during the final negotiations for WTO in Marakesh failed to be realised due to the reaction mostly from the developing countries.

Annex :

Merchandise trade of selected regional integration arrangements, 1990-96
 (Billion dollars and percentage)

	Value	Share in total exports/imports			Annual percentage change		
	1996	1990	1993	1996	1990-96	1995	1996
APEC (18)							
Total exports	2183	100.0	100.0	100.0	9	17	3
Intra-exports	1594	69.1	71.6	73.0	10	17	2
Extra-exports	590	30.9	28.4	27.0	7	18	6
Total imports	2347	100.0	100.0	100.0	10	17	6
Intra-imports	1663	67.0	71.0	70.9	11	17	5
Extra-imports	684	33.0	29.0	29.1	7	16	8
EU (15) a							
Total exports	2110	100.0	100.0	100.0	6	23	3
Intra-exports	1313	64.9	62.5	62.2	5	25	1
Extra-exports	798	35.1	37.5	37.8	7	21	6
Total imports	2053	100.0	100.0	100.0	5	21	2
Intra-imports	1314	63.0	62.1	64.0	5	25	1
Extra-imports	739	37.0	37.9	36.0	4	15	3
NAFTA (3)							
Total imports	920	100.0	100.0	100.0	9	16	8
Intra-exports	438	42.7	45.9	47.5	11	11	11
Extra-exports	483	57.3	54.1	52.5	7	20	5
Total imports	1078	100.0	100.0	100.0	8	10	7
Intra-imports	423	34.4	36.8	39.2	11	11	11
Extra-imports	655	65.6	63.2	60.8	7	9	5
ASEAN (7)							
Total exports	339	100.0	100.0	100.0	15	23	6
Intra-exports	84	19.5	21.6	24.7	20	25	6
Extra-exports	255	80.5	78.4	75.3	14	22	6
Total imports	372	100.0	100.0	100.0	15	27	6
Intra-imports	72	15.9	18.9	19.3	19	21	10
Extra-imports	300	84.1	81.1	80.7	14	28	5
CEFTA (5)							
Total exports	77	-	100.0	100.0	-	33	3
Intra-exports	12	-	17.3	16.0	-	34	4
Extra-exports	64	-	82.7	84.0	-	33	3
Total imports	101	-	100.0	100.0	-	33	15
Intra-imports	11	-	12.5	11.2	-	38	8
Extra-imports	90	-	87.5	88.8	-	33	16
MERCOSUR (4)							
Total exports	75	100.0	100.0	100.0	8	13	6
Intra-exports	17	8.9	18.5	22.6	26	19	17
Extra-exports	58	91.1	81.5	77.4	5	12	3
Total imports	86	100.0	100.0	100.0	20	28	8
Intra-imports	17	14.5	19.6	20.0	26	16	20
Extra-imports	69	85.5	80.4	80.0	18	31	6

a The statistics are affected by changes in the methods of collecting trade data in the EU member States beginning with 1993.

Note: The figures are not fully adjusted for differences in the way members of the arrangements in this table record their merchandise trade.

Source: WTO Annual Report (1996), Volume II.

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