Part III

Asia and Latin America

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Preferential Trading and Asia

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I Introduction

For diametrically opposite reasons, both East Asia and South Asia remained virtually untouched by the first wave of preferential trade arrangements (PTAs) which engulfed much of Africa and Latin America during the 1960s and 1970s. Countries in East Asia found the key to their economic development in world markets. Countries in South Asia, on the other hand, concentrated on their domestic markets, and viewing the world markets (including regional markets) as a potential threat to domestic industrialisation, applied import-substitution strategies.

The Association of Southeast Asian Nations (ASEAN), founded at the First Summit of member nations in 1967 and often viewed as a preferential trading arrangement, in fact, began as a cultural organisation and grew out of security and strategic concerns.[2] The ASEAN Preferential Trading Area (APTA) was launched in 1977, but even APTA remained an essentially dormant organisation with preferential trade accounting for a minuscule portion of the member countries' trade. Despite a concerted effort at the Third Summit in 1987, member countries remained reluctant to offer meaningful trade preferences to each other.

There was no region-wide institution in South Asia until 1985 when the South Asian Association of Regional Cooperation (SAARC) was founded. Like ASEAN, SAARC also remained essentially devoid of any economic components during the first decade of its existence. While India had a long history of exchanging tariff preferences with other developing countries, they were insignificant.[3]

The regionalisation process in Asia was given a slight impetus during the late 1980s. Recognising the urgency of successful completion of the

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1 The paper draws on my last several years of research on the subject. I thank Ajay Panagariya for assistance in preparing this paper.

2 The original membership of ASEAN included Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand. Vietnam joined the group in July 1995 and Burma, Cambodia and Laos in July 1997.

3 As Pursell (1996) reminds us, India had agreements dating back to 1967 with Egypt and Yugoslavia, an agreement inherited from pre-independence era with Myanmar, the 1976 Bangkok Agreement with Bangladesh, South Korea and Sri Lanka, another 1976 agreement with a group of 13 developing countries, a 1986 agreement with Mauritius, Seychelles and Tonga and a 1989 agreement with 24 developing countries.

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Uruguay Round, and fearful of the adverse impact on Asia of the rising tide of regionalism in the Americas and Europe, after consultation with Korean President Roh Tae-Woo, in January 1989 Australian Prime Minister R.J.L Hawk proposed the forum for Asia Pacific Economic Cooperation (APEC). APEC was intended to serve as an inter-governmental consultative body devoted to bringing the Uruguay Round to a successful conclusion and facilitating liberalisation of trade and investment policies at the regional level. An additional objective was promoting projects of common interest to member countries.[4]

In December 1990, Malaysian Prime Minister Mahathir Mohamed proposed the exclusively East Asian grouping called the East Asian Economic Group (EAEG). This proposal was vehemently opposed by the then US Secretary of State James Baker whose efforts at the ASEAN post-ministerial conference in July 1991 resulted in downgrading it to an East Asian Economic Caucus (EEAC). Baker also dissuaded Japan and Korea from joining the grouping. The EEAC has remained largely ineffective.

A somewhat more effective development was the supersession of ACTA by a framework agreement to form the ASEAN Free Trade Area (AFTA) at the Fourth ASEAN Summit in January 1992. According to this agreement, the member nations decided to establish a Free Trade Area (FTA) among themselves by 2007. The agreement requires that all quantitative restrictions on intra-regional trade be removed and all intra-union tariffs be reduced to 0-5% range. In 1994, the date of completion of AFTA was advanced to 2003.

In South Asia, under the aegis of SAARC, the new regionalism manifests itself in the creation of a South Asian Preferential Trade Area (SAPTA) with the eventual goal of creating a South Asian Free Trade Area (SAFTA). Though SAPTA was announced in 1993, there was no action on it until April 1995 when India announced some minor tariff concessions to Sri Lanka. This was followed by further minor concessions by India and Pakistan in November 1995.

This paper critically examines the desirability and likelihood of promoting preferential trade arrangements in Asia. I argue that the PTA route is neither desirable nor likely to be supported widely in Asia. Having benefited greatly from an open global trading system, East Asia as a whole has

4 APEC was launched in November 1989 at a ministerial meeting held in Canberra. Though Prime Minister Hawk had not consulted the United States prior to his January 1989 proposal, the latter quickly moved to ensure a seat for herself and its FTA partner Canada. The original membership of APEC consisted of twelve countries: Korea, six ASEAN members and five developed countries including the United States, Japan, Canada, Australia and New Zealand. In 1991, Korea negotiated the inclusion of China, Hong Kong and Taiwan while in 1993-1994, Mexico, Chile and Papua New Guinea were also admitted.

resisted, and will continue to resist, the promotion of discriminatory trade policies in that region.[5]

In assessing a regional arrangement, it has become customary to begin by examining the extent of intra-regional trade flows. This practice is the result of the so-called "Natural Trading Partners" hypothesis put forth by Wonnacott and Lutz (1989) and popularised by Krugman (1991, 1993) and Summers (1991). These authors argue that the greater the extent of trade among potential union members, the more likely that an FTA among them will be trade creating and, hence, welfare enhancing.

While I offer the interested reader the information on intra-regional trade flows in Tables 1 and 2 for East Asia and South Asia, respectively (at end of paper), it is important to note at the outset that the Natural Trading Partners hypothesis does not have a sound basis in economic theory. Recently, building on Bhagwati (1993) and Panagariya (1995, 1996), Bhagwati and Panagariya (1996) have systematically exposed the fallacy of this hypothesis.[6] We demonstrate, *inter alia*, that the extent of intra-regional trade has no definite relationship to the welfare effects of an FTA on the union as a whole. Intra-regional trade is an "average" concept whereas welfare effects are determined by what happens at the margin. A large intra-union trade simply means that there is less *scope* for trade diversion – it says nothing about the extent of *actual* trade diversion which is determined by responses at the margin. With this in mind, let me begin with the discussion of localised regional arrangements of AFTA and SAPTA and then consider the wider institution, APEC.[7]

II Evaluating AFTA and SAPTA

The most elementary argument against AFTA and SAPTA is that these regions are small in relation to the world market. In 1994, ASEAN members accounted for only 6% of world exports. If we exclude Singapore which has complete free trade and, hence, no scope for trade preferences, this share falls to 3.74%. The share of SAARC countries in the world mar-

5 This theme was developed in detail in Panagariya (1994, 1997a). The discussion on APEC later in the paper draws on Panagariya (1997b).

6 Also see Panagariya (1997) in this context.

7 I will not discuss the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) which came into existence in January 1983. Nor will I refer to other regional institutions, driven by academic or private-sector initiatives, such as Pacific Area Free Trade and Development (PAFTAD), Pacific Economic Cooperation Council (PECC) and Pacific Basin Economic Council (PBEC). An excellent summary of these institutions can be found in Ariff (1991, Chapter 5).

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kets is currently less than 1%. Thus, there is substantial scope for trade diversion within these regional arrangements.

At least in the case of AFTA countries, initial political-economy conditions are unfavourable to preferential trade liberalisation. The member countries have had highly disparate levels of trade restrictions. Singapore has long been a free-trading country while Malaysia has had generally low tariffs. By contrast, Indonesia and Thailand have had a history of high tariffs and the Philippines falls somewhere in-between. As I will demonstrate shortly, an FTA among countries with such disparate tariffs leads to a substantial income redistribution from high-tariff to low-tariff countries. Consequently, mobilising support for an FTA among them is an uphill task.

To make this point as concisely as possible, imagine the formation of an FTA between Singapore which has complete free trade and Indonesia which initially has relatively high tariffs.[8] This FTA consists of Indonesia offering a tariff preference to Singapore without a reciprocal preference from Singapore and will lead to a redistribution of income from Indonesia to Singapore. More surprisingly, the larger the quantity of imports into Indonesia from Singapore, the greater the income redistribution will be.

Thus, in Figure 1 (see next page), let us distinguish Indonesia by subscript I, Singapore by S and the rest of the world by W. Curve M_IM_I represents Indonesia's import demand for the product on which tariff preference is given, say, video-cassette recorders (VCRs). Curve E_SE_S represents Singapore's supply of exports of VCRs while P_WE_W represents the supply of VCRs from the world market. It is assumed that Indonesia and Singapore are small in relation to the world and take the world VCR price as given.

Initially, Indonesia levies a non-discriminatory tariff on imports equalling $P_WP^t_W$ per VCR so that export supply curves of Singapore and the rest of the world, as viewed by Indonesian consumers and producers, are represented by $E^t_SE^t_S$ and $P^t_WE^t_W$, respectively. The price of VCRs in Indonesia is P^t_W. The country imports OQ_1 from Indonesia and Q_1Q_3 from the rest of the world, collecting GSNH in tariff revenue. The consumers' surplus is given by triangle KSG.

Suppose now that, as a result of the FTA agreement, Indonesia eliminates the tariff on Singapore but maintains it for the rest of the world. This will shift the supply curve from Singapore down to E_SE_S. As long as any VCRs continue to come from the rest of the world, the price in Indonesia

8 The point was made originally in Panagariya (1995, 1996) and developed further in Bhagwati and Panagariya (1996). A general equilibrium treatment of the same problem is provided in Panagariya (1997c, 1997d).

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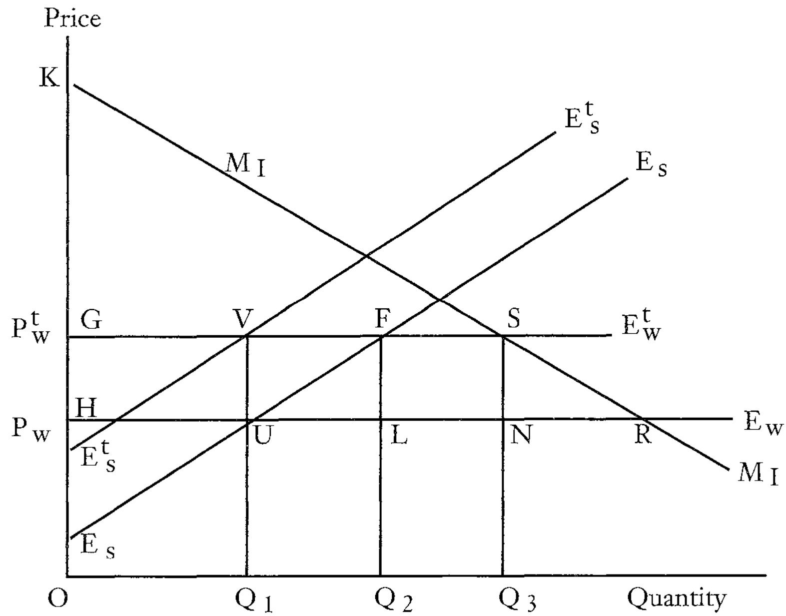
Figure 1 An FTA between Singapore and Indonesia



will remain unchanged at P^t_W. Imports from Singapore will rise to $OQ_2$and those from the rest of the world will fall to Q_2Q_3. Indonesia will lose the rectangle GFLH while exporting firms in Singapore will be able to boost their profit by trapezium GFUH. Triangle FLU will be a deadweight loss due to trade diversion. As a result of the large redistribution effect, which is a rectangle, the loss to Indonesia in this example is much larger than the deadweight loss from trade diversion which is a triangle. And the larger the quantity of trade with Singapore, the larger the redistribution and the greater the loss.

Interestingly, if Indonesia chooses to remove the tariff on a non-discriminatory basis, no such loss occurs. In this case, the tariff is also removed on the rest of the world and the price of VCRs in Indonesia falls to the world level. The lost tariff revenue, which was transferred to Singaporean exporters under the FTA, is now transferred to Indonesian consumers. In addition, the country makes a net gain of triangle SNR from improved efficiency.

This analysis is perhaps at the heart of the developments with respect to preferential trading among ASEAN countries during the last two decades.

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While unilateral liberalisation has made very substantial progress, preferential trading has proved to be an elusive goal. In 1987, a decade after APTA had been launched, preferences actually granted under it were minimal. Based on the 50% (or 35% if agreeable) ASEAN content requirement, there were 12,783 items on the PTA list. Out of these eligible items, only 337 items, or 2.6% of the total, were actually granted tariff preferences. Furthermore, only 19% of the total value of imports of these items enjoyed the preferential tariff.

At the Third Summit in 1987, the member countries adopted several changes aimed at strengthening tariff preferences. Systematic data on the progress resulting from these changes are unavailable, but from what is available, progress appears to have been less than sparkling. For example, the share of Indonesia's exports to ASEAN, which benefited from tariff preferences, rose from 1.4% in 1987 to 3.5% in 1989. Similarly, Indonesia's imports entering under preferential tariffs as a proportion of its total imports from other ASEAN countries rose from 1.2% in 1987 to 1.6% in 1989. Considering the fact that Indonesia's trade with the ASEAN 4 (ASEAN minus Singapore which has no preferences to offer and Brunei which is very small) was less than 3% during these years, these tariff preferences amount to virtually nothing.

In the past, to lengthen their lists, member countries have gone so far as to include snow ploughs among items to receive preferential tariffs. There are also instances of tariff preferences on zero-tariff goods. Even as late as July 1992, after AFTA had been signed, Indonesia announced a list 250 tariff cuts, but 90% of these were on different types of batik cloth only produced in Indonesia. The distributional conflict is well illustrated by a remark made by the former Indonesian foreign minister, Dr. M. Kusumaatmadja, at a 1992 meeting celebrating ASEAN's 25th anniversary.[9]

> "Singapore and Malaysia are always telling us to lower tariffs and duties and let their goods into the country. But in return, how about the free movement of labour? We will take your goods if you will take our surplus labour supply. When they hear this and think about all those Indonesians coming to work in their countries, then they say, 'wait a minute, maybe it's not such a good idea'."

It may appear that the September 1994 meeting of ASEAN Economic

9 Financial Times, January 26, 1993.

10 Accordingly, all tariffs on intra-regional trade are to come down to 5% or less by the year 2003. To qualify for these low tariff rates, a product must satisfy a content requirement according to which 40% or more of the product's value added must originate within the region.

Ministers, which advanced the target date for the conclusion of AFTA from 2007 to 2003, made a break from this past trend.[10] Yet, available information indicates that all significant liberalisations in the region have taken the non-discriminatory form. Of particular importance are trade liberalisations in Indonesia during 1995 and 1996. Despite the fact that these liberalisations were partially undertaken to satisfy AFTA requirements, they were non-discriminatory. It remains to be seen, however, whether this non-discriminatory approach will survive as we approach the 2003 deadline and tariffs on even sensitive products must be reduced to 5% or less.

The case for preferential trading among SAARC countries, especially when compared to the alternative of unilateral liberalisation, is also weak. Though the direction of tariff-redistribution effects in this case is difficult to assess since all member countries currently have high tariffs, the likelihood of trade diversion in this regional arrangement is extremely high. As noted above, the region supplies less than 1% of the world exports.

A case for SAPTA or SAFTA has also been made on political grounds. It is argued that the countries in South Asia have been traditionally hostile to one another. This hostility has manifested itself, for instance, in Pakistan's refusal to grant India Most Favoured Nation (MFN) status even though both countries are among the original 23 signatories to the General Agreement on Tariffs and Trade (GATT). According to this argument, SAPTA may help contain hostility among countries of the region by expanding intra-regional trade. I am sceptical of the argument. There are perhaps better targeted instruments to achieve harmony than tariff discrimination. Moreover, if the countries in the region continue on the current path of non-discriminatory liberalisation and trade on an MFN basis, intra-regional trade among them will grow anyway without the fear of trade diversion.

In part, the political argument is based on the mistaken impression that preferential trading among ASEAN members promoted peace and harmony among its members. As I have already documented, preferential trading has played a minimal role in ASEAN. In fact, during the period preceding the formation of ASEAN, attempts at preferential trading had led to discord and a disruption of peace in the region. Thus, in 1959, Singapore won the freedom for internal self rule from the British and the People's Action Party (PAP), led by Lee Kwan-Yew, came to power. Under the British, Singapore had already accumulated a long history of non-discriminatory free trade.[11] In its election manifesto, PAP had called for the establishment of a common market with the Federation of Malay to obtain free access to

11 In 1867, under Straits Settlement, Singapore became a Crown Colony and was given the free-port status.

the latter's market. Therefore, when Tunku Abdul Rahman, Prime Minister of Malayan Federation, proposed the formation of a Federation of Malaysia comprising his own nation, Sarawak, British North Borneo and Brunei, Lee Kwan-Yew supported it and prevailed. In September 1963, Singapore became a part of the Federation of Malaysia. The merger proved a mistake for Singapore, however. Indonesia, its second largest trading partner, refused to recognise the Federation of Malaysia and adopted a policy of confrontation. Singapore's entrepôt trade suffered a serious setback and, for the first time since the Second World War, the country experienced negative growth of -4.3% (Ow,1986). This was a case of regional integration which led to more, not less, hostility.[12]

III An APEC Free Trade Agreement?

During its first two or three years, APEC was a low-profile organisation. Because of its diverse membership, member countries proceeded cautiously, aiming to develop closer ties through consultation, cooperation and consensus rather than formal negotiations. Indeed, during its first four years, APEC operated without a formal secretariat. This has changed, and today APEC has become the central focus of trade relations among member countries. Some preferential-trading enthusiasts would like to see APEC turned into yet another FTA.

As Barfield (1996) correctly points out, "it was the Clinton administration that moved to change the focus of APEC from an informal consultative mechanism to a more formal organisation promoting trade liberalisation – and ultimately preferential trade arrangements – within the Pacific region." Perhaps to pressure the European Community into yielding to the additional concessions the United States was seeking at the Uruguay Round negotiations, the Clinton administration proceeded to upgrade the 1993 annual meeting of APEC ministers in Seattle to a meeting of the heads of state and signalled its intention to promote free trade in the Asia-Pacific region through APEC.

The impetus provided by Clinton at the Seattle meeting in November 1993 culminated the following year in the Bogor declaration. Led by President Suharto of Indonesia, APEC members agreed to establish free trade by the year 2010 in the developed member countries and by 2020 in the developing member countries. Though the meaning of 'free trade' in this context has remained unclear and no strategy for achieving the goal

12 By August 1965, Singapore had separated from the Federation and established itself as a separate country.

has been articulated, the agreement has permanently changed the dynamics of APEC, turning it into a high-profile body aiming to promote a more liberal trade and investment regime among its members.

How can and should APEC proceed to attain its new goal of free trade by 2010/2020? The APEC members agree that any liberalisation that takes place should be GATT-consistent. Indeed, given the recent tightening of multilateral rules under the Uruguay Round, it is difficult to imagine that any significant liberalisation can be pursued in a manner that is not consistent with GATT. Short of initiating another round of multilateral negotiations, this fact narrows down APEC's options to four modes of liberalisation: one-way trade preferences by developed to developing member countries under the Generalised System of Preferences (GSP), reciprocal trade preferences between developing member countries under the Enabling Clause of GATT, FTAs and customs unions under GATT Article XXIV, and unilateral liberalisation on the MFN basis.

Of these four modes, the first two are unlikely to play any significant role in the APEC framework. Developed country members are not likely to offer trade preferences on a non-reciprocal basis. Nor are developing member countries in East Asia keen to trade preferences with each other on a discriminatory basis. As already discussed, AFTA falls under this category but the exchange of trade preferences based on it has been minimal. Instead, the member countries have chosen to lower trade barriers on a non-discriminatory basis.

This leaves an APEC FTA and non-discriminatory reductions in trade barriers as the possible options. Both of these approaches are characterised by tension between the United States and Asian members of APEC. The tension in non-discriminatory approach comes from the fact that the United States is entirely disinterested in offering reductions in trade barriers without reciprocity. The US opposes the approach on the ground that it gives EU additional access to the US market without offering any reciprocal liberalisation. At the APEC ministerial conference in Osaka in 1995, Mickey Kantor, the US Trade Representative at the time and now the Commerce Secretary, insisted that future trade liberalisation will allow "no free riders." (Barfield, 1996).

Therefore, if trade liberalisation within the APEC framework is intended to incorporate all members without violating GATT, the logical outcome is an APEC FTA or customs union. Though the US Administration has not explicitly advocated such a bloc, it is the only possible implication of the demand for reciprocity with GATT consistency. And an FTA does sit well with Clinton Administration's new-found wisdom on trade policy which has elevated PTAs to essentially the same status as multilateral liberalisation. Thus, the 1995 President's Report (pp. 214-215) notes,[13]

> "Possibly the most distinctive legacy of this Administration in international trade is the foundation it has laid for the development of open, overlapping plurilateral trade agreements as stepping stones to global free trade. The Administration's plurilateral initiatives in North America, the rest of the Western Hemisphere, and Asia embody principles of openness and inclusion consistent with GATT. They will serve as vehicles for improving access to foreign markets..."

The Asian members countries do not share the US enthusiasm for either reciprocity or "negotiated liberalisation." Instead, they have shown a clear preference for adherence to the MFN principle. At Osaka, the Asian view of "concerted unilateralism" prevailed with each member being offered the opportunity to voluntarily adopt its separate path to liberalisation. In pursuit of the Bogor goal of free trade by 2010 or 2020, the member countries were asked to first provide a "downpayment" for free trade at the next annual meeting in the Philippines in December 1996. The result was the adoption of the so-called "individual action plans" by member countries at the Philippines summit. These plans offered little additional liberalisation beyond the countries' unilateral trade-reform programmes. Likewise, the 1997 summit in Vancouver, Canada did not produce any substantive results in terms of trade liberalisation.

For the foreseeable future, Asian members of APEC have successfully countered the US insistence on reciprocity. As an aside, it may be noted that the members of the Eminent Person's Group, headed by Fred Bergsten of the United States, which had pushed for converting APEC into an FTA have been allowed to disband at the expiration of their term rather than continuing for another term.

We may ask the model for future regional arrangements, especially major arrangements such as the Free Trade Area of the Americas and the Trans-Atlantic Free Trade Area. Indeed, a good case can be made for this approach. If regionalism is here to stay, the APEC model has some clear advantages. Most importantly, it does not intend to be a PTA and, as such, is not accompanied by trade diversion and the "spaghetti bowl" of tariffs which is being created by PTAs in Europe and Latin America. APEC's commitment to the Most Favoured Nation principle ensures that countries do not lower tariffs merely to exclude non-members from their markets. APEC has also been more forthcoming in adding new members on equal footing.[14] If adopted by the planned Free Trade Area of the Americas and

13 I may also note in passing that in early 1994, the Administration had also discussed the possibility of extending NAFTA to Korea. See Saxonhouse (1996) for details.

14 In this context, the decision by member countries at the Vancouver summit to place a 10-year moratorium on new entrants is unfortunate and inconsistent with APEC's goal to be open.

the Trans-Atlantic Free Trade Area, these characteristics will go a long way towards preserving the integrity of the global trading system.

IV Concluding Remarks

It is a folly to push for PTAs in general and in Asia in particular. In addition to the possibility that PTAs can slow down progress on the multilateral front, there are at least four reasons which justify skepticism towards PTAs as an instrument of trade liberalisation. First, since they are discriminatory in nature, they can and do lead to trade diversion. Because weaker, uncompetitive industries are often the ones that succeed in lobbying against foreign competition, PTAs are often voted in when trade diversion is the dominant force. This is a point made forcefully in the recent theoretical work by Grossman and Helpman (1995) and Krishna (1995). Similarly, the careful empirical work of Kowalczyk and Davis (1996) shows that in NAFTA, the sectors which were allowed the longest phase-out periods for implementing the accord in the United States were the ones where the US lobbies were most powerful. Most importantly, the recent World Bank study by Yeats provides systematic evidence of wholesale trade diversion in the Southern Cone Common Market popularly known by its Spanish acronym Mercosur. Thus, the "natural trading partners" hypothesis has been shown to have no foundation in theory by Bhagwati and Panagariya (1996) and in reality (Yeats, 1996).

The second problem with PTAs is that they can lead to increased protection against outside countries. In bad times, pressures for protection grow and when a PTA member is unable to raise trade barriers against a partner, the burden of increased trade barriers falls disproportionately on the outside countries. Such increases in trade barriers can turn even an initial trade creation into trade diversion.[15] This is not idle speculation. External tariffs in Israel went up after it concluded FTAs with both the EU and the United States.[16] Similarly, in the aftermath of the Peso crisis, Mexico raised tariffs on outside countries on 503 items from less than 20% to 35%. Another way of transferring the burden to outside countries is through increased anti-dumping and safeguard actions against outside countries.

Third, the rules of origin in FTAs have been creating a spaghetti bowl. This problem is bound to be compounded as overlapping FTAs proliferate. As an example, NAFTA's rules of origin are already complicated, but

15 This point was made forcefully by Bhagwati (1993).
16 For details, see Halevi and Kleiman (1994).

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suppose that Chile, who already has an FTA with Mercosur, joins NAFTA. Since Mercosur does not have an FTA with NAFTA, the rules of origin for Chile's entry into NAFTA are likely to be more complicated than those for NAFTA. The rules of origin will open a further avenue for trade diversion. Thus, a manufacturer in Chile will have to make a decision on whether to buy his components in the Southern Cone or North America depending on whether he wants to sell the final product in Mercosur or NAFTA. If he relies on a single source of supply, he will be able to satisfy the rules of origin for only one of the two destinations. Moreover, if the most efficient supplier happens to be in Asia, trade diversion will be inevitable.

Finally, measures which are WTO inconsistent have begun to sneak back into PTAs. One such example is the trade-balancing requirement within Mercosur. The WTO has just outlawed this Trade-Related Investment Measure or TRIM. Yet it has been introduced by the members of Mercosur on firms operating within the union. Thus, an Argentine company operating in Brazil must export as much Brazilian goods to Argentina as it imports from the latter. Similarly, though voluntary export restraints (VERs) have been outlawed by the Uruguay Round Agreement, VERs were resurrected on tomato imports into the United States from Mexico within the context of NAFTA. We do not currently have evidence of the extent of such WTO-inconsistent measures, but they certainly have the potential to subvert the multilateral process down the road.

Given the history of adherence to the MFN in Asia and the reliance on world markets rather than regional markets for growth and cultural and political diversity, the promotion of preferential trade makes even less sense than elsewhere in the world. Indeed, the best policy for APEC is to bring its 2010/2020 agenda to the World Trade Organization and press for a comprehensive round which will promote free trade in textiles and clothing (which interest developing Asian countries) and not merely in products such as information technology (which interest the United States and the European Union).

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Table 1 East Asian Exports
(in millions of dollars)

	ASEAN			Northeast Asia (excl. Japan)			Japan			World		
	1984	**1989**	**1994**	**1984**	**1989**	**1994**	**1984**	**1989**	**1994**	**1984**	**1989**	**1994**
Indonesia	2,490	2,431	5,302	1,187	2,538	7,098	10,353	9,252	11,711	21,881	21,941	37,958
Malaysia	4,306	6,314	15,870	1,606	3,071	8,048	3,770	4,016	7,010	16,563	25,049	58,748
Phillipines	516	542	1,626	484	722	1,550	1,034	1,581	2,020	5,343	7,754	13,433
Singapore	7,125	10,276	27,489	2,502	6,233	16,907	2,255	3,828	6,766	24,070	44,769	96,419
Thailand	1,053	2,290	5,832	690	2,026	4,647	965	3,422	7,524	7,414	20,175	41,757
Vietnam	55	120	606	80	108	610	47	261	1,227	250	1,936	4,706
ASEAN	**15,548**	**21,973**	**56,725**	**6,549**	**14,698**	**38,868**	**18,424**	**22,360**	**36,258**	**75,521**	**121,624**	**253,021**
China	1,960	3,008	6,710	6,586	21,916	38,983	5,155	8,395	21,490	24,824	52,916	120,822
Hong Kong	2,361	4,947	9,974	6,353	23,416	55,772	1,251	4,525	8,436	28,314	73,113	151,393
Korea	1,402	3,814	12,418	1,540	4,635	16,950	4,610	13,167	13,523	29,259	60,496	96,040
Taiwan	2,163	6,418	13,202	2,557	7,930	29,769	3,197	8,913	10,719	30,435	65,573	93,672
Northeast Asia (excl. Japan)	**7,886**	**18,187**	**42,304**	**17,036**	**57,897**	**141,474**	**14,213**	**35,000**	**54,168**	**112,832**	**252,098**	**461,927**
Japan	14,149	25,943	60,880	26,932	51,789	92,581	–	–	–	169,748	274,590	395,201
World	**66,952**	**114,805**	**253,764**	**93,561**	**220,153**	**433,823**	**115,672**	**185,666**	**254,230**	**1,790,300**	**2,963,100**	**4,184,000**

Source: IMF, *Direction of Trade and Statistics* (various issues). Taken from Soesastro (1996).

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Table 2 South Asian Trade
(in millions of dollars and percentages)

Country	Year	Exports to			Imports from		
		SAARC	World	SAARC as % World	SAARC	World	SAARC as % World
Bangladesh	1986	54	889	6.1	91	2,550	3.6
	1993	55	2,277	2.4	477	4,015	11.9
India	1986	277	9,135	3.0	73	15,051	0.5
	1993	763	19,964	3.8	95	22,493	0.4
Maldives	1986	5	25	20.0	9	78	11.5
	1993	12	66	18.2	24	218	11.0
Nepal	1986	51	134	38.0	102	314	32.5
	1993	43	389	11.0	96	545	17.6
Pakistan	1986	109	3,383	3.2	95	5,367	1.8
	1993	216	6,701	3.2	147	9,492	1.5
Sri Lanka	1986	58	1,163	5.0	144	1,829	7.9
	1993	86	2,846	3.0	363	4,311	8.4

Source: Bhuyan (1996).

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Regional Integration in South Asia

Miria Pigato[1]

I Introduction

I am going to discuss two issues. The first is the rise of regionalism in South Asia and its specific characteristics. The second issue concerns the potential benefits that South Asian countries would derive from a regional trade agreement. I will conclude by explaining why we, at the World Bank, still believe that regional integration in South Asia is desirable in spite of apparently modest economic benefits.

II The Rise of Regionalism in South Asia

The rise of regionalism in South Asia is quite recent. The South Asian Association for Regional Cooperation (SAARC), which includes India, Pakistan, Nepal, Bangladesh, Bhutan, Sri Lanka and the Maldives, was created in 1985. But very little happened until 1993 when there was a major initiative to promote a South Asian Preferential Trade Arrangement (SAPTA). This arrangement became operational in 1995. The first round of negotiations led to a few tariff concessions, discussed on a product-by-product basis, and achieved only after endless discussions among the states. Only 6% of traded goods was involved. In 1996, however, a stronger determination to regional integration led the countries to undertake a second round of negotiations, which included more extensive trade concessions and a commitment to establish a free trade area by 2000 or 2005 at the latest.

Why did South Asia take such a long time to move to regionalism? Before 1947, the region was characterised by intense trade and the countries were integrated – even from a monetary point of view. But after independence, trade essentially disappeared. Currently, intra-regional trade accounts for only 4-5% of total trade in the region, compared to 40% in East Asia, 43% in NAFTA and even 12% in Sub-Saharan Africa.

Why did trade disappear? First, it disappeared as a result of political and

1 The opinions expressed here are those of the author and do not necessarily represent those of the World Bank.

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military turmoil. There have been three wars between India and Pakistan. During the last war in the early 1970s, Bangladesh emerged as an independent nation. But border confrontations have continued to shadow the political dialogue between India and Pakistan. Second, up to 1991, all of the countries in the region adopted protectionist policies. Before 1991, the nominal average tariff rate in India was 125% and the highest was 335%. Furthermore, most imports were protected by quantitative restrictions. Despite much progress in deregulation and trade liberalisation in recent years, nominal protection rates are still around 20-25% – much higher than in developing regions where the average is 15%. South Asia remains one of the most protected and least integrated regions in the world.

In addition to trade protection, transit barriers still exist. India has denied transit facilities to Nepal and Bhutan for export to Bangladesh. And Bangladesh has denied India transit through its territory to reach the northern Indian states. Of course, illegal trade has flourished. Our estimates indicate that the volume of *illegal* imports from India to Bangladesh is basically the same as the volume of *legal* imports.

We see the movement toward regionalism as a very positive phenomenon. First of all, it is an initiative that comes from new governments and new leaders, at least in Bangladesh, India and recently Pakistan. These new leaders claim that they want more cooperation and peace in the region. And in fact, this year, we have witnessed the signing of a water agreement between India and Bangladesh ending a historical dispute over the Ganges; another agreement between India and Nepal on the Mahakali River; and the signing of the India-Nepal trade treaty giving preferential access to Nepal's exports into the Indian market.

In this context, SAARC has really represented a forum for coordinating policies of liberalisation. Regionalism in South Asia does therefore not represent a withdrawal from the international economy in order to create a protected region or market. On the contrary, it is part of a strategy that all of the countries in the region have undertaken to open up and become outward oriented.

III The Benefits from a Regional Arrangement

Would the region gain from promoting a free trade area? A number of studies have examined this issue. Srinivasan, for example, using a gravity model, found that only the smaller countries would derive substantial benefits from a free trade agreement with their neighbours. By contrast, the larger countries, India and Pakistan, would gain more by liberalising their trade in a non-discriminatory way. In our own calculations, using a general

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equilibrium model of the world economy, we arrive at basically the same conclusion. Our results suggest that India's welfare gains are much larger in the non-preferential liberalisation hypothesis. This is derived from the fact that trade creation would not be significant since the rest of South Asia is much smaller than India. Moreover, terms of trade gains would also be small for India because protection in the rest of South Asia is lower than in India. It is important to note that the model is based on 1992 tariff data, and I suspect that if we were to conduct the analysis with 1997 data, we would find that the gains for India would be even smaller. In contrast, the benefits the rest of South Asia would derive from a preferential trade arrangement would be larger than those from non-discriminatory liberalisation – the smaller countries would indeed obtain significant terms of trade gains from open access to the highly protected Indiana market.

While our calculations indicate that the welfare benefits of a regional trade agreement would be limited, we believe that political and social considerations justify a positive assessment of regional integration. First, we believe that an intensification of the process of regionalisation would increase the chances for settling border disputes and would encourage cooperation. A by-product of a more peaceful environment would be a reduction of military spending. This would be a major achievement, as military spending represents such a large share of public revenue (37% in Pakistan). A common market would also help attract foreign direct investment and multinational enterprises, particularly in the textile and garment industries, thus accelerating industrial restructuring in these sectors. Finally, regional integration would also lend support to India's quest for becoming a member of APEC. Given its philosophy of open regionalism, APEC ought to be more interested in an India that is practising a good neighbour policy than in an India that is persisting with the style of policies from the past.

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Towards an Evaluation of Regional Integration in Latin America in the 1990s

Robert Devlin and Ricardo Ffrench-Davis[1]

I Introduction

The decade of the 1990s has witnessed a wave of regional integration initiatives in Latin America: more than 14 agreements – free trade areas or customs unions – since 1990 with a handful more in varying degrees of negotiation (see Table 1 at end of paper). However, this was not just a Latin American phenomenon as regionalism has more than ever become a global trend (Mistry, 1996). Indeed, now Japan, South Korea and Hong Kong are the only World Trade Organization (WTO) members which are not signatories of at least one preferential trade agreement (WTO, 1995).[2]

Regional integration is not new to Latin America. Economic integration played an important role in the region's early post-war economic history. The 1960s and 1970s saw a number of very ambitious initiatives inspired by the successful Western European experience (Ffrench-Davis, Muot new to Latin America. Economic integration played an important role in the region's early post-war economic history. The 1960s and 1970s saw a number of very ambitious initiatives inspired by the successful Western European expey set in by the late 1970s and the discussion of regional integration was all but silenced by the external debt crisis of the early 1980s.

The renaissance of regional integration has not been uncontroversial. Some, including the authors, view regional integration as a potentially valuable tool for modernisation and development in a second-best world. Others, however, interpret regional integration as an inferior, costly policy option, which is harmful to the countries involved, and the multilateral system more generally. The purpose of this article is to review the strategic dimensions and rationale of regional integration, place potential costs and benefits in their proper perspective and outline directions for future

1 We thank F. Ballestero, A. Jessen and A. Panagariya for their helpful comments and Brenda Simonen and Francois Dionne for their statistical assistance. The opinions expressed here are those of the authors and do no necessarily reflect those of their respective institutions (IDB and ECLAC).

2 Of course Hong Kong has just been transferred to China, which has yet to become a member of the WTO.

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research and economic policy. Section I is a brief review of trends in intra- and extra-regional trade and some of the factors driving it. This is followed by a discussion, in Section II, which places regional integration in the broader Latin American policy context that is conditioning its effects. Section III outlines what countries expect to achieve from regional integration and the costs that can be confronted. Section IV attempts to put the costs and benefits into perspective and offers directions that might help us better evaluate the full effects of integration and thereby soften some of the rougher edges of the policy debate. Section V concludes with policy suggestions that should contribute to amplifying the benefits and minimising the costs for the participants in regional integration agreements and the world community at large.

II The Growth in Trade[3]

The 1990s have witnessed a rebound in the region's trade after the crisis of the previous decade. Between 1990 and 1996, the region's exports expanded by 76%; imports grew even faster, at 127%. Imports as a percentage of the region's GDP now equals 18%, up from 10% in 1990[4] (Figure 1). Moreover, the region's growth of imports has consistently exceeded that recorded at the world level: according to WTO estimates, the value of world imports grew by an average 7% a year between 1990 and 1996, compared to 15% for Latin America.

A closer look at the region's trade performance in the 1990s reveals the following trends:

- Intra-regional trade has grown more rapidly than trade with countries outside the region. This trend is particularly pronounced in the case of *exports* (Table 2). Since 1990, the value of intra-regional exports has grown by 18% a year on average, compared to 9% for extra-regional exports. Intra-regional exports now account for 18% of total Latin American and Caribbean exports, up from 12% in 1990. Without Mexico, the figure reaches 27%, from 15% at the beginning of the decade.
- It is interesting to compare real (constant prices) changes in exports to GDP growth. Overall, the GDP of the region grew 20% between 1990 and 1996. The quantum of total exports rose 59%, thus increasing by one-third the export ratio of Latin America. The leading destinations by

3 For a more detailed overview of intra-regional and extra-regional trade, see ECLAC (1997) and IDB (1997).

4 When Mexico is excluded, the figures are 14% and 8% respectively.

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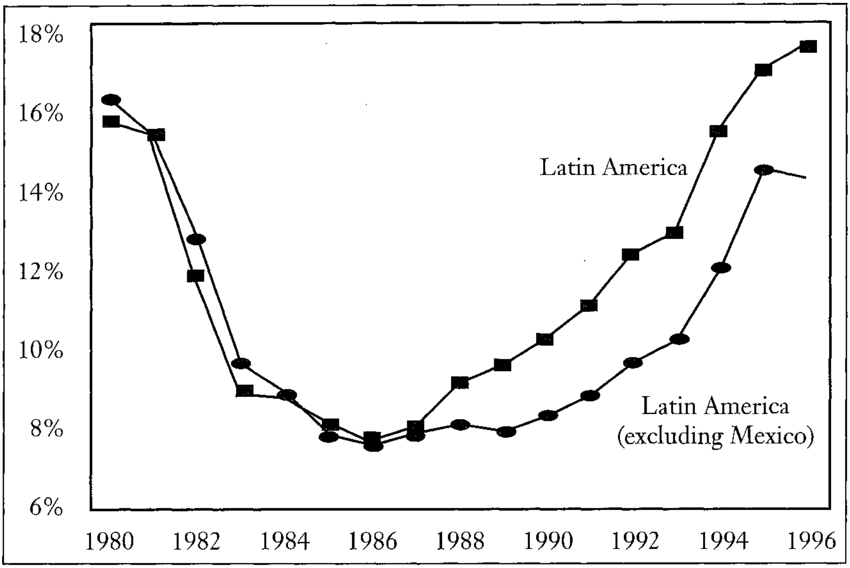
Figure 1 **Latin America Imports as a percent of GDP**



Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues, ESDB database.

far were intra-regional markets, which expanded 160%. However, extra-regional exports also increased much faster than GDP, more than doubling the latter's rate of growth.

- Growth rates for intra- and extra-regional *imports* have been more homogeneous (Table 3). While intra-regional imports expanded by an average of 18% a year between 1990 and 1996, extra-regional imports also grew very fast, by 14% a year, reflecting a generalised import boom in the region. This, coupled with the aforementioned important growth of extra-regional exports, confirms that regional integration has been consistent with open regionalism.

The marked difference in the growth rates of the region's overall exports and imports (76% and 127%, respectively) reflects a large imbalance in the growth of trade with *extra-regional markets*, with imports from these sources expanding nearly twice as fast as exports to extra-regional destinations. For the trends in direction of trade, see Figures 2a and 2b.

Some factors influencing current trends are:

Geography. Areas dense in capital and population often tend to naturally

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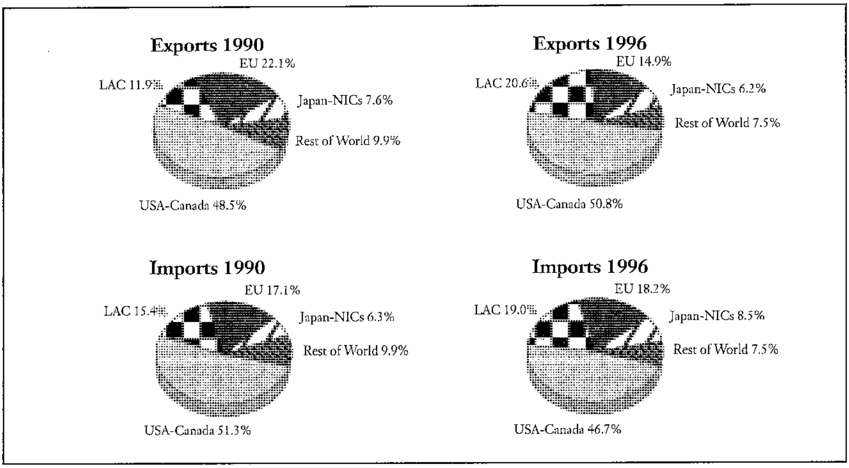
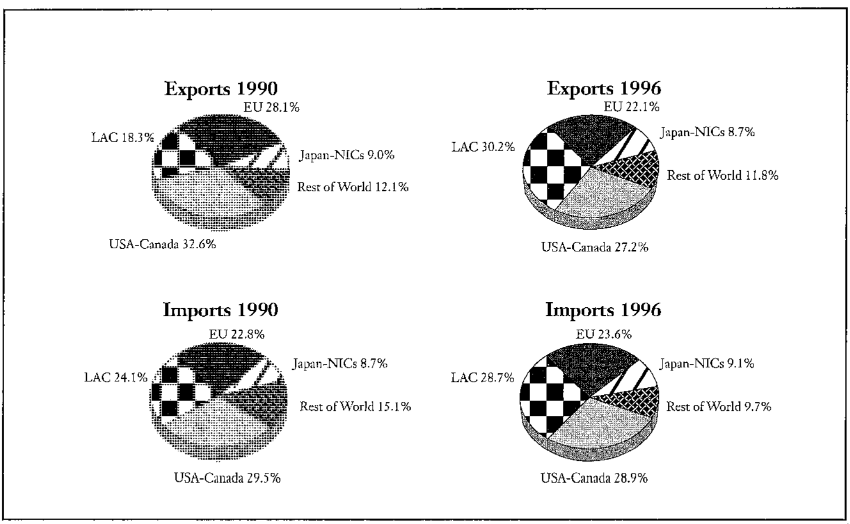
Figure 2a Latin America and the Caribbean – Direction of Trade



Note: Includes Mexico maquila trade. LAC is Latin America and the Caribbean. NICs includes Hong Kong, Korea, Singapore and Taiwan.
Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues.

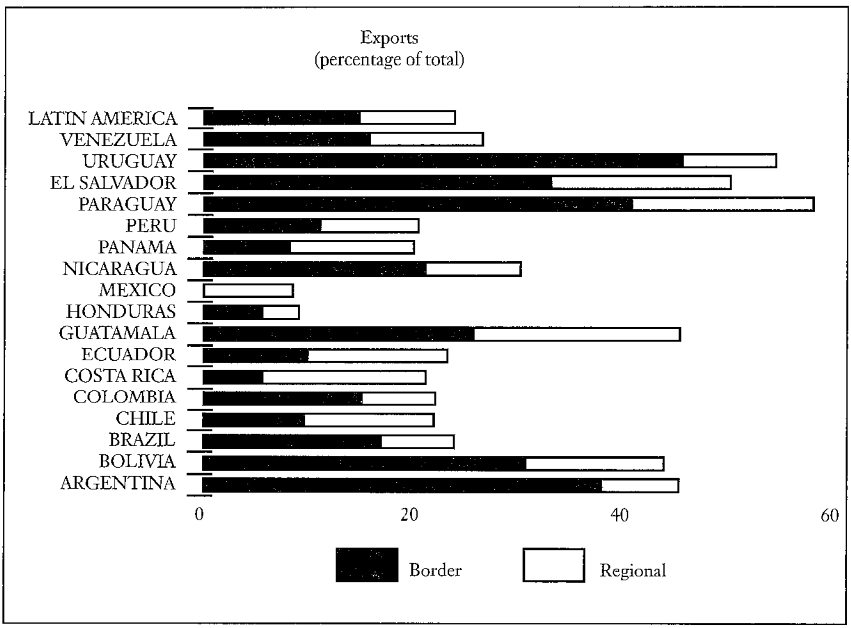
Figure 2b LAC excluding Mexico – Direction of Trade



Note: LAC is Latin America and the Caribbean. NICs includes Hong Kong, Korea, Singapore and Taiwan.
Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues, based on DATAINTAL.

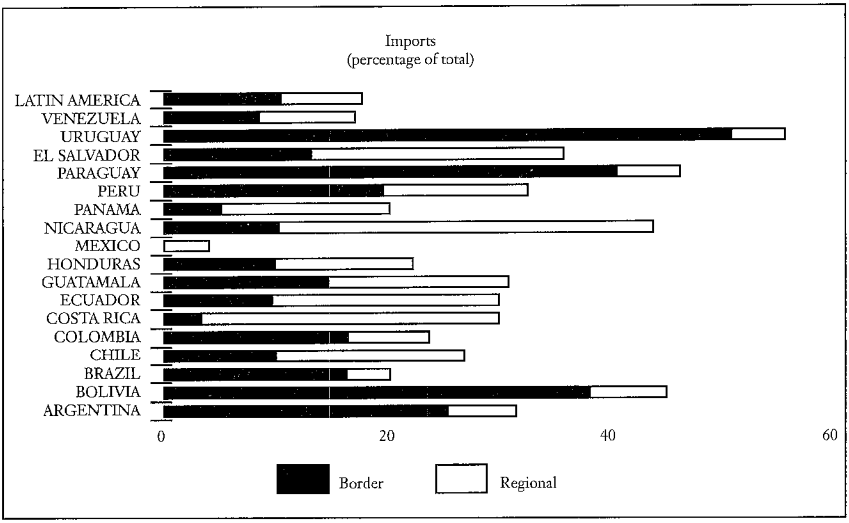
interact and trade relatively more intensively with increasing specialisation (Ballestero, 1996). Among the economic factors behind this are the positive externalities of location and agglomeration. The tendency can be further enhanced when income levels, cultures, tastes and languages are similar, as they are in Latin America, and when differentials exist in transport costs between contiguous and non-contiguous countries. On these criteria, large natural geographic areas of economic integration would appear to exist in Latin America in its Southern Cone, Venezuela-Colombia-Ecuador, Central America and North America for Mexico. In fact, the boom in intra-regional trade has largely been among neighbouring countries in the region (Figures 3a and 3b).

Figure 3a Intra-Regional and Border Exports, 1994



Note: The countries included are those that share borders and have available information. Mexican border trade does not include trade with the United States.
Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues.

Figure 3b Intra-Regional and Border Imports, 1994



Note: The countries included are those that share borders and have available information. Mexican border trade does not include trade with the United States.
Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues.

Relaxation of the External Restriction. The decline of world interest rates, debt relief and a return of external capital flows in the 1990s (Devlin, Ffrench-Davis and Griffith-Jones, 1995) have dramatically increased import capacity in the region with consequent reactivation of economic activity. Since intra-regional imports equal intra-regional exports, the generalised import boom has been reflected in the marked growth of intra-regional exports.

Real Exchange Rate Appreciation. The region's external trade performance has also been influenced by the exchange rate behaviour of Latin American and Caribbean countries. The simultaneous liberalisation of the capital account in many countries, coupled with a surge in supply of foreign capital and the use of exchange rate anchors in support of stabilisation programmes, contributed to real currency appreciations in an important number of countries (just when the opposite, a real depreciation, was need-

5 Some countries like Colombia and Chile have actively tried to slow down pressures for real appreciation by avoid anchors and resorting to, among other things, foreign exchange regulations and imaginative financial engineering (Devlin, Ffrench-Davis and Griffith-Jones, 1995).

ed to facilitate export-led growth). An exchange rate index, weighted by GDP, gives an average revaluation of 25% between late 1980s and 1994. This situation has tended to encourage imports while, at the same time, discouraging the region's exports.[5] Moreover, since real appreciation of exchange rates with respect to the rest of the world has been simultaneous among a significant number of neighbouring countries in Latin America in the 1990s, the dampening effects on exports have been relatively stronger in the extra-regional market.

Economic Reforms. The structural reforms undertaken in the late 1980s and 1990s have energised private market activity, facilitated the emergence of new investors and trade. Unilateral trade liberalisation in particular has been a key in exposing natural market opportunities for exports to neighbouring countries that heretofore were hidden behind the wall of national protection (IDB, 1996a).

Sub-Regional Trade Agreements. The aforementioned explosion of sub-regional and bilateral trade agreements in the 1990s has stimulated intra-regional trade through many mutually reinforcing effects; for example:

There has been an increased flow of information and public attention on opportunities in an adjacent market ("agreement-led" growth in trade).

Trade preferences are an integral part of the regional integration agreements and provide incentives for intra-regional trade. The absolute level of the preference over time will depend on the evolution of external tariff rates. Nevertheless, it is important to point out that many of the preferences of the older trade agreements in the region have been progressively eroded by the unilateral liberalisation of trade in the late 1980s and early 1990s.

In contrast to unilateral opening, the free trade arrangements have given the private sector reciprocal and legally binding market access which has reduced the risks of trade and investment barriers emerging in the affected market. This in turn increases private sector confidence. An example of the especially strong nature of a reciprocal commitment is Mexico, which during the peso crisis exempted NAFTA partners from a temporary increase of tariffs on 500 items (5% of total tariff lines).

A preferential agreement can signal the continuing commitment of public authorities to trade liberalisation, during a conjuncture in which unilateral or multilateral liberalisation is not possible or desirable. In agreements such as Mercosur, sub-regional trade liberalisation is accompanied by an additional commitment involving a much broader political message, pursued at the highest official levels, to promote deep economic integration and political cooperation among member countries.

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III The New Face of Regional Integration in Latin America and the Caribbean

Regional integration must be evaluated in the broader context of the overall contemporary economic policy which is conditioning its effects. The regional integration initiatives immediately following the Second World War inserted themselves into the prevailing development strategy of import substitution. Indeed, the integration schemes of that period were designed in part to enhance the efficiency of the import-substitution model through a strategic expansion of the highly protected national market.[6] While the integration initiatives achieved some important results – for example, the significant liberalisation of reciprocal trade in Central America – outcomes fell far short of objectives. On the one hand, the strong national political commitments to domestic protection made opening up even among associate countries an extremely labourious negotiating process that rarely achieved more than very partial results. On the other, the costs of trade diversion were amplified due to the general presence of high average tariffs on third parties and extensive use of non-tariff restrictions.

The traditional model of development in Latin America changed in the 1980s and this, in turn, has dramatically changed the face of regional integration itself. In effect, the regional integration of today has inserted itself into the broader overall strategy of opening up to the world economy. Countries have entered into multiple arrangements that are eliminating tariffs among partners across substantially all trade within a relatively short period of time, and which often involve other commitments that even go beyond the WTO's trade-related disciplines. In any event, Figure 4 and Table 4 respectively show, for a sample of regional agreements in Latin America, that the reciprocal liberalisation process is typically completed for the bulk of trade within a period of 10 years and negotiated exceptions have rarely exceeded 6% of total tariff lines.

In the initial stages of their development, regional integration arrangements link up with the overall economic reform process most obviously through its trade liberalisation component. In effect, regional integration is a third tier of a three-tier liberalisation process.

(i) Unilateral Liberalisation. The first and most dramatic level of liberalisation has been through unilateral measures to open up economies.

6 In some cases, as in the Andean Pact, there was the deliberate effort to drastically reduce the level and dispersion of effective tariffs.

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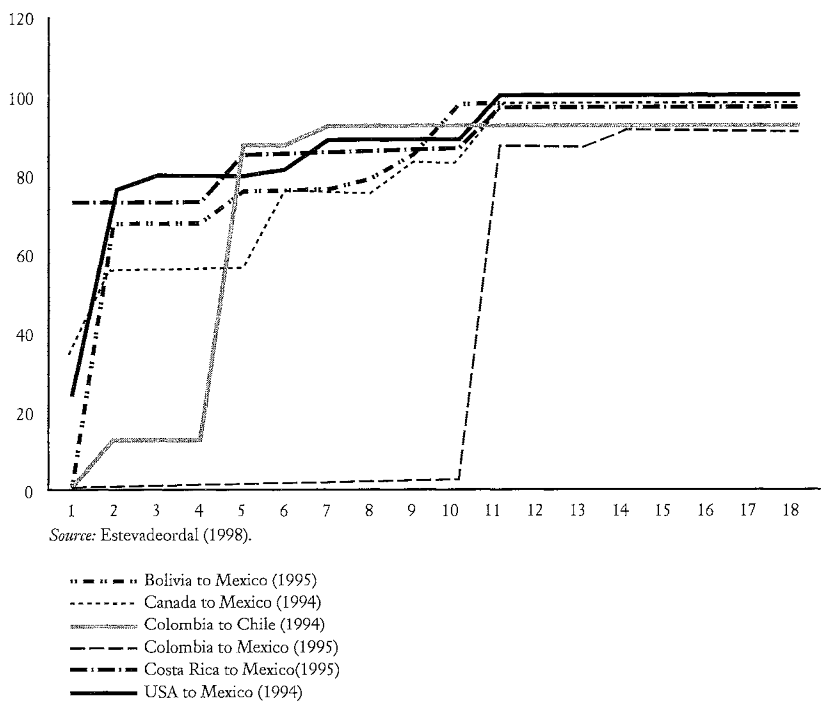
Figure 4 Selected FTAs in Latin America. Years to liberalisation
(percentage of tariff items liberalised)

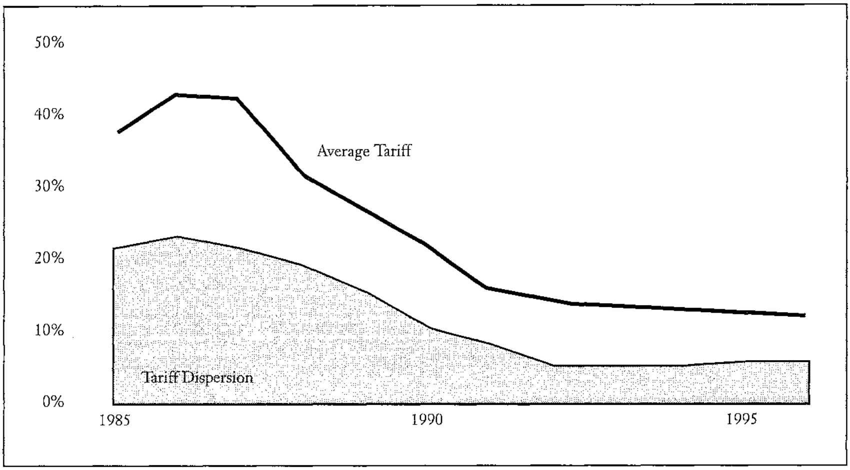


Source: Estevadeordal (1998).

Profound trade reforms have been undertaken in Latin America as part of a broad-ranging process of change, in which international competitiveness and exports play a leading role. Most countries are in search of export-led development. Nonetheless, in contrast with the experience of East Asian nations, the main instrument of trade reform has been a relatively indiscriminate and rapid liberalisation of imports (Agosin and Ffrench-Davis, 1995; ECLAC, 1995). The aim is to expose producers of importables, which had often been receiving a high level of protection, to outside competition, while also encouraging the output of exportables. It is expected that this will result in higher productivity, the absorption of new technologies and increased specialisation.

Most of the countries' trade reforms could be described as sudden and drastic. The experience is reflected in the fact that the average tariff in Latin America and the Caribbean has declined from 45% in the second half of the 1980s to 13% in 1995, accompanied by a sharp reduction of tariff dispersion as well (Figure 5). Furthermore, over the same period the share of the region's imports subject to non-tariff barriers has declined from 31% to 11%. Specific tariffs have virtually disappeared even while they are still common in the industrialised economies (ECLAC, 1995; IDB, 1996).

Figure 5 Tariff Liberalisation in Latin America



Source: IDB, Department of Integration and Regional Programs, Division of Trade, Integration and Hemispheric Issues (weighted on imports).

(ii) Multilateral Liberalisation. The second level of external opening is multilateral. The region has assumed the new disciplines that emerged from the Uruguay Round. Indeed, it was the only developing region to bind 100% of its tariffs (although the binding was at a level more than double that of average applied tariffs). With Panama joining the WTO in 1995, all of the region is now subject to the rights and obligations of the WTO.

(iii) Regional Integration. The third tier of opening has been through regional integration. It is often overlooked that in the new context of policy change in Latin America, regional integration is an additional instrument to open economies to competition, and complementing levels one and two of the trade liberalisation process. Indeed, the insertion of regional integration initiatives into the overall liberalisation strategy of the 1990s gives the process the character of "open regionalism." Moreover, the fact that tariffs are different from zero, but generally at relatively moderate lev-

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els, leaves space for reciprocal tariff preferences with more limited trade diversion than in earlier trade agreements.

IV Why Do the Countries Pursue Regional Integration?

Regional integration has various dimensions. The simplest form of integration is a free trade area in goods only, in which there is a progressive elimination of tariffs on most trade among partner countries. The next level of commitment would be a more comprehensive free trade area that includes services and even WTO "plus" disciplines in other trade-related areas. Even deeper commitments would involve ceding sovereignty over commercial policy, by creating a customs union with a common external tariff protecting the liberalised sub-regional market. Deeper still is a common market with free movement of factors of production. All these schemes are currently reflected in the objectives of Latin America integration.

While the benefits and costs of integration depend on which type of scheme one is considering and the overall policy context, limits on space permit only some general appreciations in this regard.

A. Some Common Motivations for Regional Integration

Without being exhaustive and recognising that many goals can be interrelated, some frequently mentioned objectives are outlined below.

Politics

Many initiatives emerge under a political umbrella designed to bring nations closer to one another. The degree of commitment varies but the motive is often present. Latin Americans share a common heritage, language and culture. There is a side of Latin Americans that makes them like to be more together; these sentiments indeed extend back to Bolivar and independence. The phenomenon is sometimes hard for non-Latinos to understand and could seem contradictory given the long history of serious political disputes among Latin American nations. But the fact remains that the centrifugal forces of disagreement have co-existed with, and often have been overcome by, the centripetal forces of a common heritage and culture. These opposing forces of course can be especially intense in the various geographic sub-regions of Latin America.

Today's integration in Latin America is often driven by powerful political objectives. This is most clearly manifest in Mercosur (including asso-

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ciates Chile and Bolivia), where countries with a history of conflictive relations are using economic integration to draw themselves more closely together into a common purpose of peace and prosperity. A similar phenomenon can be found with the reactivation of integration in other subregions such as the Andean Community.

Practising the Art of the Possible in Trade Liberalisation

Unilateral and multilateral liberalisations are always staged. Unilateral liberalisation has the benefits of creating trade and raising competition through importables and lowering input costs; but it also has immediate fiscal costs and real resource costs through creating obsolete capital and redundant labour as well as public psychological costs because of the real and imagined threats of globalisation. Thus, the process of adjustment must move in tandem with the political and economic capacity to digest those costs. The large and rapid liberalisation of recent years encountered initially considerable "water" in national tariff schedules; and the necessary fiscal adjustments were quite straightforward. But now tariffs are presumably closer to actual differential margins of competitiveness between home and abroad, while fiscal options are narrower. The liberalisation process, however, is made more complicated by exchange rate appreciations that have taken place in the 1990s in a number of Latin American countries (which has further cut margins of protection) and the simultaneous action of stabilisation programmes which usually raise the cost and reduce the supply of domestic credit. Meanwhile, multilateral rounds come in spurts, the schedule of which is largely out of the control of developing countries. In the case of the Uruguay Round the region still is in the process of digesting existing commitments.

In this context, authorities can use regional integration as a window of opportunity to continue pursuing liberalisation, but in the more predictable and controlled environment of a reciprocal agreement of circumscribed scope. In fact, regional integration adds a compensatory ingredient to unilateral import liberalisation, by fostering reciprocal exports in tandem with reciprocal imports. Hence, the doses of positive and negative impulses to economic activity and investment are more balanced with regional integration, than is the case in pure unilateral import liberalisation. Moreover, the regional agreement does lower the average level of protection vis-à-vis the status quo, creating trade, raising competition and promoting specialisation in the sub-regional market. The arrangement can meet less political resistance (and indeed even be quite popular as in the case of Mercosur) because of a number of associated factors such as public sentiments about "getting together" with a known neighbour, compensa-

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tion through reciprocity with guaranteed market access, and more limited impacts on fiscal income (the starting point for most integration agreements has involved modest levels of trade and rather symmetric tariff structures).[7]

Strategic Impulse to Development

Regional integration also builds on strategic considerations arising from imperfect and incomplete markets at home and abroad, which handicap the spread of efficiency gains in certain sectors and the development of new productive patterns with progressively higher degrees of value added.

The conventional literature on the benefits and costs of economic integration focuses on tariff preferences in a framework of optimal competitive equilibrium. This equilibrium is assumed to be disturbed only by the existence of import restrictions. In this framework, integration is beneficial only if it implies a move toward free trade; that is, if the effects of trade creation (shift toward cheaper sources of supply) are larger than those of trade diversion (shift toward more costly sources of supply).[8] The crucial issue, however, is how costs are measured; in the standard approach it is at actual market prices net of tariffs, assuming away transitional costs and incomplete markets, as well as acquirable competitiveness. The assumptions lead to the obvious conclusion that overall unilateral liberalisation is always the optimal national policy and better than regional integration.

But the real world is more complicated. For many non-traditional products, access to markets is more limited and unstable, making economies of scale, the emergence of externalities of location and agglomeration, and specialisation more difficult to achieve. It is for these types of products that regional integration becomes a potential platform for diversifying growth of exports, and to improve trade's contribution to development. In the face of distortions in world markets, guaranteed access to regional foreign markets can be a catalyst for exploiting potential externalities; indeed, this is a leading objective of policymakers and a major force encouraging regional integration. Moreover, in face of economies of scale, what otherwise would be a costly trade diversion can become a cost-reducing and welfare-enhancing effect (Corden, 1972; Ffrench-Davis, 1980).

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7 A regional arrangement can additionally serve to lock-in policy commitments that otherwise are more easily reversible. North-South agreements in particular are often cited for these confidence-building effects (Fernandez, 1997). A good example is the incorporation of Southern Europe into the EU, which was instrumental in the former's economic transformation and consolidation of democracy.

8 There is also the effect à la Lipsey, of an eventual reduction of price distortions on consumption.

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Meanwhile, local factor markets are incomplete or distorted. Labour training, technology and long-term capital are scarce, with inexistent or infant markets, and foreign direct investment (FDI) – a potential bearer of some of these scarce factors – is frequently coquettish, playing one national suiter off against the other in a world of imperfect information.[9] These market failures are more significant for non-traditional exports of differentiated products, whether of natural resources, manufactures or exportable services. If access to external markets is improved for these exportables, it can be a catalyst for completing markets and diluting segmentation.

Infrastructure, trade financing and knowledge of markets (marketing channels, organised transportation, standards, etc.) have often been biased against intra-regional trade in LDCs. All these "factors" of trade have been traditionally more developed for transactions with the great metropolitan centres (often linked to the cumulative effects of a colonial past) while they are inexistent or rudimentary for trade among LDCs neighbours. This is a significant variable explaining why intra-regional trade has been lower among Latin American countries than what the gravity of geography would often suggest.

These are serious restrictions on the expansion of production and trade in goods and services with relatively more knowledge content and longer learning curves, elements which are now recognised as key components of the growth process. Regional integration can be a strategic tool to partially overcome these obstacles by:

- expanding market size to facilitate greater specialisation and industrialisation through economies of scale and possibilities to exploit economies associated with the agglomeration of production activity.
- enhancing the forces of competition, enlarging a market with guaranteed reciprocal access, and intensifying the specificity of information flows, all of which in turn should induce new domestic investment and permit better conditions to attract efficient foreign investment.
- creating the security of sub-regional market access, preferences, and exploiting the familiarity of neighbourhoods, which combine to accelerate the emergence of new exporters of manufactured goods. In effect, the learning curve associated with sub-regional export experience can serve as a platform for new international exports. This is an important consideration since history has shown that developing countries can achieve new dynamic comparative advantage on the road of their long-term convergence with industrialised countries.[10]

9 Moreover, it must be recalled that FDI represents only 6 to 10% of capital formation in the world.

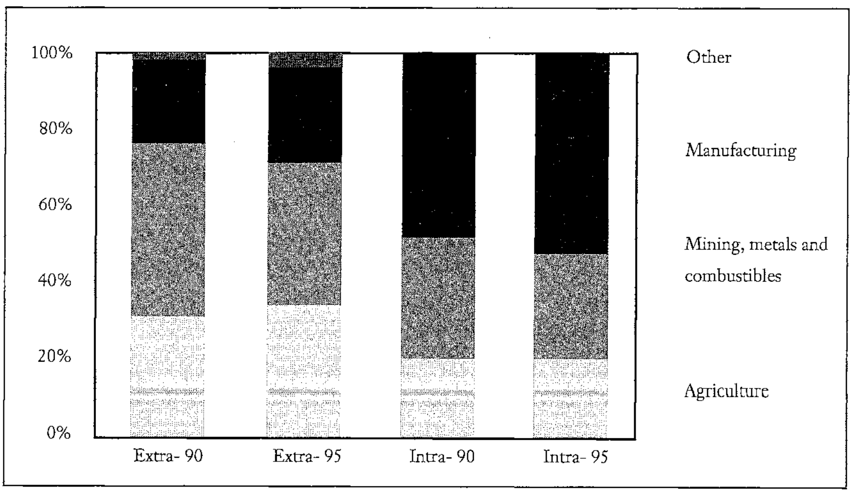
10 For an example of intra-industry trade patterns set off by an important sub-regional agreement, see Echavarria (1997).

The expected enhanced international competitiveness brought about by regional integration should build confidence and prepare countries for globalisation and further advances in multilateral liberalisation. And as mentioned earlier, regional integration can also be viewed as a way to move ahead with liberalisation while the region awaits consensus on development of a new round of reciprocal multilateral disciplines.

To appreciate the strategic dimension of integration it is useful to examine the profile of intra-regional exports. Intra- and extra-regional exports from Latin America display marked differences in terms of their product structure and technological content, with manufactures accounting for a much larger share of intra-regional commerce. This pattern is evident even if Mexico – whose *maquila* trade with the United States accounts for a large share of Latin America's overall exports – is discounted from the regional average. Excluding Mexico, manufactures account for approximately 50% of intra-regional exchanges, compared to around 23% for extra-regional exports (Figure 6). The annex to this article discusses the composition of intra-regional exports and their technological content in more detail.

All these aspects of regional integration are of course potential developments rather than guaranteed outcomes; what happens in practice depends on the nature of policy implementation, a point we will return to in the concluding section.

Figure 6 LAC Exports by Sector (excluding Mexico)



Source: IDB, Department of Integration and Regional Programs, Division of Trade, Integration and Hemispheric Issues (weighted on imports).

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B. The Costs of Regional Integration

The potentially positive aspects of regional integration are accompanied by costs too. Some of these have received much attention in the literature of late. A brief summary of the most frequently cited costs would be:

1. Preferences in regional trading arrangements can divert trade away from possibly more efficient firms which are located in non-member countries (Yeats, 1996; Bhagwati and Panagariya, 1996). This has costs for the non-member countries that lose market share. The trade diversion risks locking the partner economies into patterns of inefficient production.
2. Regional integration agreements can improve the terms of trade of member countries at the expense of non-member countries and give rise to incentives for maintaining or increasing preferences and protection.[11]
3. When there are serious asymmetries in average tariff levels among prospective partners of an integration agreement, the loss of tariff revenue in the preferential liberalisation process can have serious redistributive effects among the countries (Panagariya, 1996). In effect, part of what would have been realised as tariff revenue on imports from the partner country prior to the agreement is transferred to the partner's producers, as tariffs are preferentially eliminated.
4. While regional integration can clearly induce foreign direct investment in the expanded sub-regional market (Bloomstrom and Kokko, 1997), this is an expensive source of financing for which compensating positive spillovers can be ambiguous. Integration induced investment can also involve diversion of FDI from more efficient non-members (Winters, 1997).
5. In regional integration, benefits are often asymmetrically distributed and initially concentrated in some members while others are dependent on uncertain spillover effects (Puga and Venables, 1997).
6. An explosion of free trade areas creates a spaghetti pattern of agreements with multiple hubs and spokes that give rise to distortions in trade, excessive administrative costs, rent seeking and a difficult to predict distribution of gains among countries (Wonnacott and Wonnacott, 1995).
7. The emergence of regional agreements creates defensive reactions, in which a country joins an agreement not because it is the best option, but

11 Looked at from another angle, rather than improving the terms of trade, regional integration may be able to soften a worsening of the terms of trade that could occur if Latin American countries keep on producing more of the same basket of traditional exports.

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because of the real or potential costs of being left out of an integration process.
8. Regional integration distracts attention from multilateral rounds of liberalisation and delays further unilateral opening.

V Putting the Costs and Benefits into Perspective

Evaluating regional integration processes and their costs and benefits is no easy task. Part of the problem is the nature of the subject matter.

First, regional integration is a complex general equilibrium phenomenon with dynamic processes, making it difficult to dissect for purposes of causal explanation. The process involves issues that link growth to technology, learning, externalities, political economy and politics, all of which economists have trouble grappling with at a national level not to mention among several countries simultaneously. A further complication which one finds in Latin America is that the integration processes are an integral part of the profound structural reforms that have touched all levels of the economy and create big changes. Moreover, initial conditions, and the phases and sequencing of these reforms, are usually quite different among the partner countries.

Second, regional integration is a medium/long-term process. When successful, one expects to see initial costs compensated by benefits that play out over the medium to long-term.

Third, regional integration is very much a second-best world where generic prescriptions can be especially dangerous.

Fourth, regional integration is typically evaluated in light of what would have happened in its absence. Moreover, economists are interested in measuring changes in welfare; given the complications of defining this for a particular sub-region they often use a proxy expressed in a summary statistic reflecting growth or trade (Winters, 1997).

These characteristics place great burdens on analysts. It is well known that counterfactual analysis faces a daunting epistemological problem: contrary to fact, conditionals can never be verified by realising their antecedent (the "if" clause); thus the resulting explanation is never correct or incorrect but rather only persuasive or not persuasive. We also know that counterfactuals are more likely to be persuasive: (i) the more simple the causal process studied; (ii) the shorter the time period in question; (iii) the smaller the changes considered; and (iv) the less analysis turns on exact magnitudes. Reflecting back on the characteristics of integration processes it can be seen that our counterfactual analysis is challenged on all these counts.

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Conclusions about regional integration are rarely based on the entire story. Much of the debate centres on static trade creation and trade diversion effects, first pointed out by Viner (1950). This is partly because many economists consider these effects to be the fundamental dimension for evaluating regional integration. One problem, however, is that the static analysis frequently uses a partial competitive equilibrium framework to jump to general conclusions about a process that is a general equilibrium phenomenon. Worse, the existence of trade diversion alone (never mind the net effects with trade creation) in new integration agreements has been sufficient for some to categorically condemn them and regional integration more generally (Yeats, 1996).[12]

But more importantly, conventional trade creation vs. diversion is clearly only part of the story and many other economists (e.g., Mistry, 1996; Fernandez, 1997 and the authors) would argue that it is not the major part. This is because the net benefits of the dynamics of integration can be several times larger than their static reallocation effects. Problems exist here too because our models of dynamics and empirical foundations for testing them are very deficient, so much so that some have even characterised analysis in this area as "mystical" (Winters 1997). It is true that the empirical foundation of dynamic analysis is still weak. Nevertheless, the models of dynamics are sufficiently specified to suggest that the benefits behind the dynamics of integration are potentially large. It therefore is worth the effort to go beyond static trade creation-diversion analysis (which has its ambiguous dimensions as well) to begin to better understand, even if only very imperfectly, the longer-term dynamics.

The empirical bottlenecks to understanding Latin American integration should not be underestimated. Even basic data such as the evolution of preferences, rules of origin, non-tariff measures, intra-regional investment flows, firms' cost structures, etc., are unavailable or incomplete. The many gaps sometimes induce questionable *ad hoc* compromises in our analytical techniques or cause us to ignore important phenomena altogether through the convenient use of the *ceteris paribus* clause. Better data development and more field research will not eliminate the debate over regionalism but it would certainly help to ground the debate more in reality; and it may also help to narrow our differences.

The starting point is to better complement our powers of scientific

12 This latter study set off a major controversy by concluding that Mercosur was harmful to itself and the rest of the world due to trade diversion. It concluded this by discovering intense intra-regional trade in some sectors with high preferences. The study, however, did not control for the fact that protection might be independent of Mercosur nor for other potentially important explanatory factors, and overlooked indications of much trade creation in the 1990s (see Devlin, 1997 and IDB, 1996b).

deduction with much more empirical field work and case studies of the disaggregated dimensions of the dynamics of regional integration. In other words, instead of examining what would have happened in the absence of integration we might want to spend more time discovering what is actually happening and how it is happening in Latin American integration. In effect, one would examine the different objectives of a specific integration arrangement, see whether these different objectives are being realised, and begin to catalogue the causal factors contributing to developments without necessarily being overly concerned about precise weights. For example, one frequently stated objective of regional integration is to enhance competition; hence we can examine how sectoral markets are changing their competitive structure and the forces behind that. Is intra-industry specialisation increasing in the sub-regional market? Are the different parameters of the integration agreement stimulating firms to invest? Are firms' technology and cost structures improving in the direction of greater international competitiveness and is there room to reduce preferences? Are new international exports and comparative advantages emerging out of experiences in the sub-regional market?

This type of research is at "ground zero" and examines the integration agreement from the bottom up. Field research does not generate elegant analytical structures. It is time consuming and expensive, often requiring the building of primary data bases. It also will not generate summary statistics of welfare or permit categorical evaluations of integration processes. But it has four potential benefits:

1. It will allow for better observation of what is actually happening in the different dimensions of integration. The analyst gets "inside" the process where the action is and examines the dynamics of sectoral markets and firms which actually move the process forward.
2. By working at relatively low levels of aggregation one might be able to identify causal factors that are not easily captured in existing theory or more aggregated analysis.
3. While such analysis will not permit the adding up of effects into a summary statistic of welfare, the examination of multiple disaggregated dimensions of an integration process will permit a series of analytical vignettes which taken together can build a tentative story of whether the integration process is achieving expected goals in strategic areas.
4. The empirical work will feed our economic modelling of integration with better informed assumptions and better data for testing.

In sum, the suggested approach of more intensive interaction between deductive and inductive methods should enhance our powers of discovery and evaluation of a process that is ever more present in our world economy.

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Until we have better ability to measure and evaluate the *full* story of integration we should be careful about our evaluations. Any major transformation has costs, usually concentrated up front. Therefore it is no surprise that regional integration has costs. For instance, since regional integration is a strategic compromise among economies with different economic and political characteristics, a degree of unwanted trade diversion is inevitable.[13] However, countries justify these costs by the greater benefits that are expected, which are derived from a combination of political returns, lock-in effects, trade creation and the aforementioned dynamic forces of transformation which are spread out over a longer period of time.

Thus when examining up-front costs, analysts should be careful to interpret them as only a piece of a story which plays out over a longer term, and thereby refrain from categorical overall assessments, except in the most extreme cases. Meanwhile, since regional integration is a strategic decision, participants should have their objectives clearly articulated. One objective is to minimise costs; thus any constructive analysis that sheds light on them would also be welcome. Moreover, vigilance about costs is extremely important. On the one hand, while fashionable, not all integration arrangements make economic sense. On the other, even those that do can potentially go awry. Finally, there are systemic costs arising from the sum effect of many regional initiatives which individually may make sense.[14]

VI Conclusions

Regional integration is a fact of life in Latin America and indeed in most of the world. Regional integration is being pursued in Latin America for political reasons as well as for its value as a strategic tool of development in a second-best world. No one denies that it can have important costs. But much of the attention on costs has been focused on the short-term up-front costs that are part of any major transformation. These costs must be

13 As mentioned earlier, in a "dynamic" setting some trade diversion could be a benefit to the extent it ultimately would contribute to lower costs, increased competitiveness and growth.

14 The clearest example of this is the spaghetti effect of many integration arrangements in the hemisphere which reduce transparency and raise transaction costs. However, the problem may be less severe than appears at first blush because the majority of arrangements follow the umbrella concepts laid out by ALADI (e.g., Chilean bilaterals) or NAFTA (e.g., the Mexican bilaterals). Moreover, the complex network of arrangements provides incentives for consolidation, as witnessed in Mercosur's emerging free trade association in South America, the Free Trade of the Americas process and, perhaps someday soon, at the world level in a new multilateral round aiming at a target of zero tariffs (which would eliminate the simplest free trade areas).

measured against the benefits, and the bulk of these are expected in the medium to long-term through the dynamics of economic transformation. These dynamic processes could be better understood and measured if more attention were given to micro and sectoral field research where much of the process of regional integration takes place. This ground zero research would complement our more aggregate analysis and model building.

Since regional integration is here to stay, it would be constructive to promote policies that are likely to minimise the risks of unacceptable costs and to amplify potential benefits. Some of the major challenges in this regard are:

1. Progressive Elimination of Imperfections in Sub-Regional Integration Schemes

There is a need for full implementation of agreements and effective enforcement. Politically feasible formulas are needed to gradually eliminate existing exceptions to agreed trade liberalisation because the opening up of sensitive sectors is usually very rich in trade creation effects. Integration of services is largely a frontier that still must be crossed, but special caution is needed regarding integration of financial services due to potential negative macroeconomic side effects (Zahler and Budmevich, 1997). Remaining trade distorting non-tariff measures (NTMs) must be eliminated or harmonised to the extent possible, and very importantly, rules of origin in free trade areas should be gradually substituted for common external tariffs or, alternatively, simplified and relaxed sufficiently (within the confines of rigour) to respect the status quo in trade patterns (Garay and Estevadeordal, 1995; Simpson,1997; Serra *et al.*, 1996). Latin America must also substitute its tradition of settling disputes through diplomatic channels (perhaps effective when the economies were state dominated) for modern transparent dispute settlement mechanisms (Devlin, 1995). Now that private markets are the driving force of the economy, it is necessary that integration arrangements are transparently rule-based; only in this way will the full potential for productive private investment – that is so important for the efficient specialisation which is at the heart of successful integration agreements – be realised.

Rationalisation of regional institutions is necessary. In the case of some traditional integration schemes which modelled themselves after Europe, the task is to downsize an overdimensioned and underfinanced institutional structure. For the new schemes of the 1990s the task is just the opposite: fortify incipient institutional arrangements so that instruments are compatible with objectives. Of particular concern for ambitious integration schemes is the need to have mechanisms in place to ward off dangerous imbalances in the distribution of costs and benefits of the process. Another area of concern is infrastructure (Vera, 1997). There is a need to create effective institutional mechanisms for the coordination of regional infrastructure networks and their financing, in order to better exploit the advantages of location.

Finally, integration schemes, especially deep ones, must improve official mechanisms for the interchange of information and analysis on macroeconomic developments in the sub-regions and monitor the processes of convergence which should emerge (Ben-David, 1996).

2. *Consolidation and Deepening of Structural Economic Reforms*

These reforms, including those leading to macroeconomic stability, have been underlying the recent success of intra-regional trade. However, there is concern that exchange rate appreciation linked to capital surges and indiscriminately open capital accounts, coupled with the use of the exchange rates primarily as anchors of domestic prices, is distorting resource allocation and trade, and may reduce the sustainability of macroeconomic balances and their contribution to growth (IDB, 1997; Ffrench-Davis, 1996). Sometimes short-run targets of stabilisation also have tended to contribute to a weakening of mesoeconomic policies (such as education, labour training, support to technological improvement of medium and small firms, infrastructure). All this tends to differ the reaping of profitable opportunities in processes of economic integration and opening, and worsens the balance of benefits and costs. In extreme instances of instability in the face of volatile capital flows, it would actually threaten the viability of the integration project itself. There clearly is a need to foster development of more direct instruments for stabilisation policy.

3. *Operational WTO Review of Regional Integration Processes*

Article XXIV of the GATT and Article V of the GATS are meant to ensure consistent, fair and transparent multilateral monitoring of integration arrangements. However, the articles and their implementation, even with the important clarifications of the Understanding attached to Article XXIV in the Uruguay Round, still suffer from a degree of imprecision. The doubts that sometimes are raised about regional integration could be more constructively dealt with in the context of operational Article XXIV reviews with multilaterally agreed criteria and strong empirical foundations (Serra *et al.*, 1996). Moreover, improved multilateral guidelines would help to broaden the common base among agreements and mitigate the potential costs of the spaghetti bowl of arrangements in the hemisphere and the world.

As long as countries are clear in their strategic objectives for an integration agreement, are vigilant of costs, continue to remedy shortcomings and ensure that the process remains an integral part of an overall policy framework of structural economic reform, there is good reason to be cautiously optimistic about the ability of regional initiatives to serve as an effective instrument of growth and development. The other essential element for Latin America and the rest of the world is further development of the multilateral system. Latin America has a vested interest in ensuring that regionalism is consistent with a healthy and progressively more liberalised rules-based world trading system, if for no other reason that 80 percent of its trade is extra-regional. Fortunately, there is growing consensus among economists and policymakers about the potentially positive contribution that the new "open" regional integration can make to the world trading system. The trend is well captured in a recent WTO Secretariat study which states "...to a much greater extent than is often acknowledged, regional and multilateral integration initiatives are complements rather than alternatives in the pursuit of more liberal and open trade" (WTO, 1995: 56).

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Annex

The Composition and Technological Content of Intra-Regional Trade

Composition of Intra-Regional Trade

The Latin American economies provide very important and dynamic markets for the sales of manufactures for many countries of the region (ECLAC, 1994). For instance, for Argentina, Chile, Colombia, Uruguay and Venezuela, this is by far the biggest market, be it for traditional industries, basic inputs or new industries. Latin America continues to be the almost exclusive destination for exports from the new industries of several countries; these exports have been markedly dynamic in the 1990s. The same is true of their respective sub-regional market as regards the new industries of Costa Rica and Guatemala. Brazil has channelled its export manufactures to different markets; the United States continues to be the main buyer of traditional industries, followed by Europe. As for basic inputs, other developing regions have displaced Latin America as the main destination, but in the case of new industries, the region is the most important market for Brazil. An exception is the case of Mexico, where the regional market has less relative importance than the United States.[1]

Technological Intensity

Development based on a growing and sustained international competitiveness is boosted by the dynamic effects derived from technological apprenticeship. The strategies to improve international linkages, based on productive development, emphasise the role played by trade in the process of stimulating the development of activities which make intensive use of knowledge and technology. In this sense, it is interesting that trade among developing countries is characterised by concentration in goods that are more technology-intensive than exports from developing to industrial countries.

This is the broad conclusion of a study by Buitelaar (1993) which combines

1 Regressions carried out by ECLAC for the period 1970-91 show that there was a strong positive relationship between the importance of Latin America as a destination and the share of new industrial products in total exports of Argentina, a relationship that is positive but less intense for Brazil. In Chile, the exercise revealed a strong positive correlation for all manufactures. For Mexico, however, no significant relationship was obtained.

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data on foreign trade and on production. Three main conclusions emerge from the research:

i) The production of goods which depend to a greater extent on intra-regional trade has more sophisticated technological features. Such goods are to be found mainly in the chemical sector, non-electrical machinery and transport equipment. They are also sectors in which international demand tends to be more dynamic. Their price trends (factorial terms of trade) are more stable and evolve more positively over the long-term than prices of traditional exports.
ii) The sectors which exhibit a strong export drive toward the region also tend to show (sometimes with a lag) a drive towards extra-regional markets, which suggests that the promotion of intra-regional trade complements the promotion of extra-regional exports.
iii) These same sectors are those in which the region has a high dependency as regards extra-regional intermediate imports, and therefore intra-regional trade benefits from having access to inputs and equipment which may be imported from third countries. Thus, relaxation of excessive extra-regional import restrictions has contributed to foster and upgrade intra-regional exports.

To sum up, intra-regional trade, because of its characteristics, associated with location and the diverse channels which facilitate such trade, complements the Latin American countries' linkages with the global economy and provides a dynamic context of technological apprenticeship, leading to greater international competitiveness and a more diversified, balanced pattern of specialisation.

Table 1 Recent Regional Trade Agreements in Latin America1

Year	Agreement	Some agreements in discussion2
1990[3]	Andean Pact[4]	Caricom[5] – Central America
1991[6]	Central American Common Market[7]	Dominican Republic – Caricom
1991	Chile – Mexico	Dominican Republic – Central America
1991	Mercosur[8]	Chile – European Union
1993	Chile – Colombia	Chile – Central America
1993	Chile – Venezuela	Mexico – El Salvador, Guatemala, Honduras
1993	NAFTA[9]	
1994	Chile – Ecuador	Mexico – Belize
1994	Mexico – Bolivia	Mexico – European Union
1994	Mexico – Costa Rica	Mexico – Ecuador
1994	G-3[10]	Mexico – Peru
1996	Chile – Mercosur	Mexico – Panama
1997	Bolivia – Mercosur	Mercosur – Andean Community
1997	Chile – Canada	Mercosur - European Union
1998	Mexico – Nicaragua	

Notes:

1 Excludes partial agreements of the Latin American Integration Association (LAIA or ALADI in Spanish).
2 In different stages of development.
3 Date of reactivation of the free trade zone.
4 The Andean Pact includes Bolivia, Colombia, Ecuador, Peru and Venezuela.
5 The Caribbean Community includes Antigua and Barbuda, Bahamas, Barbados, Belize, Dominicana, Grenada, Guyana, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago.
6 Date of reactivation of the free trade zone.
7 The Central American Common Market includes Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.
8 Mercosur includes Argentina, Brazil, Paraguay and Uruguay.
9 NAFTA includes Mexico, Canada and U.S.A.
10 The G-3 includes Colombia, Mexico and Venezuela.

Source: IDB, Department of Integration and Regional Programs, Division of Integration, Trade and Hemispheric Issues.

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Table 2 **Western Hemisphere: Total and Intraregional Exports1**
(millions of dollars and percentages)

	1990	1991	1992	1993	1994	1995	1996	1990-96 average2
Western Hemisphere3								
Global Exports	658,234	684,995	727,241	765,511	859,185	996,945	1,067,489	
% growth	7.9	4.1	6.2	5.3	12.2	15.9	7.2	8.4
Extra Hemispheric Exports	341,515	357,391	364,017	365,905	394,303	472,187	493,073	
% growth	5.4	4.6	1.9	0.5	7.8	19.8	4.4	6.3
Intra-Hemispheric Exports	316,719	327,605	363,224	399,606	464,881	523,858	574,417	
% growth	10.7	3.4	10.9	10.0	16.3	12.7	9.7	10.4
Intra-Total	*48.1*	*47.8*	*49.9*	*52.2*	*54.1*	*52.6*	*53.8*	
Latin America and the Caribbean4								
Global Exports	137,781	136,242	145,504	155,644	181,573	218,989	242,758	
% growth	10.5	-1.1	6.8	7.0	16.7	20.6	10.9	9.9
Extra-LAC Exports	121,412	116,249	120,662	126,011	146,574	177,194	198,056	
% growth	10.9	-4.3	3.8	4.4	16.3	20.9	11.8	8.5
Intra-LAC Exports	16,369	19,993	24,843	29,633	34,998	41,795	44,702	
% growth	7.3	22.1	24.3	19.3	18.1	19.4	7.0	18.2
Intra-Total	*11.9*	*14.7*	*17.1*	*19.0*	*19.3*	*19.1*	*18.4*	
Latin America and the Caribbean (excluding Mexico)								
Global Exports	97,070	93,555	99,309	103,758	119,596	139,212	147,789	
% growth	8.4	-3.6	6.1	4.5	15.3	16.4	6.2	7.3
Extra-LAC Exports	82.223	75,317	76,771	76,678	87,204	101,515	108,050	
% growth	8.5	-8.4	1.9	-0.1	13.7	16.4	6.4	4.7
Intra-LAC Exports	14,847	18,238	22,538	27,079	32,392	37,696	39,739	
% growth	7.5	22.8	23.6	20.1	19.6	16.4	5.4	17.8
Intra-Total	*15.3*	*19.5*	*22.7*	*26.1*	*27.1*	*27.1*	*26.9*	
Central American Common Market								
Global Exports	4,058	4,138	4,697	5,065	5,509	6,864	7,676	
% growth	12.7	2.0	13.5	7.8	8.8	24.6	11.8	11.2
Extra-CACM Exports	3,402	2,356	3,697	3,961	4,280	5,408	6,149	
% growth	12.4	-1.3	10.1	7.1	8.1	26.4	13.7	10.4
Intra-CACM Exports	656	782	1,000	1,105	1,229	1,456	1,527	
% growth	14.6	19.1	27.9	10.4	11.3	18.4	4.9	15.1
Intra-Total	*16.2*	*18.9*	*21.3*	*21.8*	*22.3*	*21.2*	*19.9*	
Andean Community								
Global Exports	31,605	28,630	28,380	29,654	34,256	38,843	42,656	
% growth	26.1	-9.4	-0.9	4.5	15.5	13.4	9.8	5.1
Extra-Andean Exports	30,310	26,912	26,224	26,858	30,852	34,268	38,027	
% growth	26.2	-11.2	-2.6	2.4	14.9	11.1	11.0	3.9
Intra-Andean Exports	1,295	1,719	2,156	2,796	3,404	4,575	4,629	
% growth	23.5	32.7	25.4	29.7	21.7	34.4	1.2	23.6
Intra-Total	*-1.1*	*6.0*	*7.6*	*9.4*	*9.9*	*11.8*	*10.9*	

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Table 2 (continued)
(millions of dollars and percentages)

	1990	1991	1992	1993	1994	1995	1996	1990-96 average2
Mercosur								
Global Exports	46,425	45,911	50,561	54,162	62,112	70,401	75,030	
% growth	-0.3	-1.1	10.1	7.1	14.7	13.3	6.6	8.3
Extra-Mercosur Exports	42,302	40,808	43,341	44,132	50,157	56,018	58,881	
% growth	-1.2	-3.5	6.2	1.8	13.7	11.7	5.1	
Intra-Mercosur Exports	4,123	5,102	7,220	10,031	11,955	14,384	16,149	
% growth	10.8	23.8	41.5	38.9	19.2	20.3	12.3	25.6
Intra-Total	*8.9*	*11.1*	*14.3*	*18.5*	*19.2*	*20.4*	*21.5*	
NAFTA								
Global Exports	561,164	591,440	627,993	661,752	738,494	856,598	920,678	
% growth	7.8	5.4	6.2	5.4	11.6	16.0	7.5	8.6
Extra-NAFTA Exports	320,667	341,997	354,468	360,444	386,434	461,078	483,655	
% growth	5.2	6.7	3.6	1.7	7.2	19.3	4.9	
Intra-NAFTA Exports	240,497	249,443	273,465	301,308	352,060	395,520	437,023	
% growth	11.5	3.7	9.6	10.2	16.8	12.3	10.5	10.5
Intra-Total	*42.9*	*42.2*	*43.6*	*45.5*	*47.7*	*-16.2*	*47.5*	
Group of Three								
Global Exports	65,162	65,117	67,451	74,367	86,020	107,625	126,836	
% growth	22.2	0.9	36.1	10.3	17.1	23.8	16.7	11.7
Extra-Group of Three Exports	64,127	63,937	65,675	72,023	83,456	104,319	123,596	
% growth	15.5	-0.3	2.7	9.7	15.9	25.0	18.5	11.6
Intra-Group of Three Exports	1,305	1,180	1,776	2,344	2,565	3,306	3,240	
% growth	47.0	14.0	50.4	32.0	9.4	28.9	-2.0	20.9
Intra-Total	*1.6*	*1.8*	*2.6*	*3.2*	*3.0*	*3.1*	*2.6*	

Note: 1 Mexico's exports include maquila.
2 Average for Caricom is 1990-1995.
3 Western Hemisphere includes Latin America and the Caribbean (see following definition), the United States and Canada.
4 Latin America and the Caribbean here is Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela, Bahamas, Barbados, Belize, Guyana, Jamaica, Trinidad and Tobago, Haiti and the Dominican Republic.
e = estimate

Source: IADB, Department of Integration and Regional Programmes, Division of Integration, Trade and Hemispheric Issues, based on DATAINTAL. Caribbean, US and Canadian data, as a source country, are from IMF, *Direction on Trade and Statistics.*

From: Regional Integration and Multilateral Cooperation in the Global Economy
FONDAD, The Hague, 1998, www.fondad.org

Table 3 **Western Hemisphere: Total and Intraregional Imports1**
(millions of dollars and percentages)

	1990	1991	1992	1993	1994	1995	1996	1990-96 average2
Western Hemisphere[1]								
Global Imports	747,493	758,937	836,042	913,399	1,046,065	1,161,200	1,238,749	
% growth	5.4	1.5	10.3	9.1	14.5	11.0	6.7	8.8
Extra Hemispheric Imports	431,751	423,603	459,534	512,927	585,874	642,112	672,737	
% growth	4.5	-1.9	8.5	11.6	14.2	9.6	4.8	7.7
Intra-Hemispheric Imports	315,743	335,334	377,507	400,473	460,191	519,088	566,012	%
growth	6.6	6.2	12.6	6.1	14.9	12.8	9.0	10.2
Intra-Total	*-12.2*	*44.2*	*45.1*	*43.8*	*44.0*	*44.7*	*45.7*	
Latin America and the Caribbean[4]								
Global Imports	110,235	128,880	157,007	174,272	205,546	226,317	250,306	
% growth	11.9	16.9	21.8	11.0	17.9	10.1	10.6	14.6
Extra-LAC Imports	93,221	108,082	131,190	144,680	171,237	183,965	204,990	
% growth	12.1	15.9	21.4	10.3	18.4	7.4	11.4	14.0
Intra-LAC Imports	17,014	20,798	25,817	29,592	34,310	42,352	45,317	
% growth	11.0	22.2	24.1	14.6	15.9	23.4	7.0	17.7
Intra-Total	*15.4*	*16.1*	*16.4*	*17.0*	*16.7*	*18.7*	*18.1*	
Latin America and the Caribbean (excluding Mexico)								
Global Imports	68,643	78,914	94,877	109,163	125,367	153,876	162,140	
% growth	7.7	13.0	20.2	15.1	14.8	22.7	5.4	15.4
Extra-LAC Imports	52,685	59,703	71,021	81,874	93,983	113,531	118,979	
% growth	6.9	13.3	19.0	15.3	14.8	20.8	4.8	14.5
Intra-LAC Imports	15,958	19,210	23,855	27,289	31,384	40,345	43,161	
% growth	10.1	20.4	24.2	14.4	15.0	28.6	7.0	18.0
Intra-Total	*23.2*	*24.3*	*25.1*	*25.0*	*25.0*	*26.2*	*26.6*	
Central American Common Market								
Global Imports	6,535	6,868	8,874	9,456	19,224	12,087	12,304	
% growth	6.0	5.1	29.2	6.6	8.1	18.2	1.8	11.1
Extra-CACM Imports	5,895	6,058	7,805	8,326	8,950	10,580	10,743	
% growth	6.2	2.8	28.8	6.7	7.5	18.2	1.3	10.5
Intra-CACM Imports	640	810	1,069	1,131	1,274	1,507	1,561	
% growth	3.9	26.5	32.0	5.8	12.7	18.3	3.6	16.0
Intra-Total	*9.8*	*11.8*	*12.0*	*12.0*	*12.5*	*12.5*	*12.7*	
Andean Community								
Global Imports	17,425	22,3111	27,220	29,398	30,617	38,300	36,814	
% growth	3.0	28.0	22.0	8.0	4.1	25.1	-3.9	13.3
Extra-Andean Imports	16,243	20,665	25,129	26,753	27,345	33,423	31,954	
% growth	1.5	27.2	21.6	6.5	2.2	22.2	-4.4	11.9
Intra-Andean Imports	1,182	1,646	2,091	2,645	3,272	4,877	4,860	
% growth	30.4	39.3	27.0	26.5	23.7	49.1	-0.4	26.6
Intra-Total	*6.8*	*7.4*	*7.7*	*9.0*	*10.7*	*12.7*	*13.2*	

Table 3 (continued)
(millions of dollars and percentages)

	1990	1991	1992	1993	1994	1995	1996	1990-96 average2
Mercosur								
Global Imports	27,326	32,140	38,536	47,823	61,851	75,311	83,217	
% growth	12.3	17.6	19.9	24.1	29.3	21.8	10.5	20.4
Extra-Mercosur Imports	23,204	27,016	31,266	38,427	49,989	61,218	66,125	
% growth	13.1	16.4	15.7	22.9	30.1	22.5	8.0	
Intra-Mercosur Imports	4,122	5,125	7,270	9,396	11,862	14,094	17,092	
% growth	8.0	24.3	41.9	29.2	26.2	18.8	21.3	26.8
Intra-Total	*15.1*	*15.9*	*18.9*	*19.6*	*19.2*	*18.7*	*20.5*	
NAFTA								
Global Imports	687,850	680,023	742,165	804,493	919,866	1,007,336	1,076,608	
% growth	5.2	0.2	9.1	8.4	14.3	9.5	6.9	8.0
Extra-NAFTA Imports	443,190	430,927	462,031	510,164	578,310	627,931	655,530	
% growth	4.8	-2.8	7.2	10.4	13.4	8.6	4.4	
Intra-NAFTA Imports	235,660	249,096	280,134	294,329	341,556	379,405	421,078	
% growth	5.9	5.7	12.5	5.1	16.0	11.1	11.0	10.2
Intra-Total	*34.7*	*36.6*	*37.7*	*36.6*	*37.1*	*37.7*	*39.1*	
Group of Three								
Global Imports	54,168	66,073	82,264	86,588	100,433	97,549	111,838	
% growth	14.4	22.0	24.5	5.3	16.0	-2.9	14.6	12.8
Extra-Group of Three Imports	53,450	65,110	80,795	84,626	98,242	94,379	108,600	
% growth	14.2	21.8	24.1	4.7	16.1	-3.9	15.1	
Intra-Group of Three Imports	719	963	1,470	1,963	2,191	3,170	3,238	
% growth	31.7	34.0	52.6	33.6	11.7	44.7	2.1	28.5
Intra-Total	*1.3*	*1.5*	*1.8*	*2.3*	*2.2*	*3.3*	*2.9*	

Note: 1 Mexico's exports include maquila. In principle, intraregional imports should equal intraregional exports. Slight variations between values of intraregional exports from Table 2 and intraregional imports in this table are due to exporting differences between the countries.
2 Average for Latin America and the Caribbean is for 1990-1996.
3 Western Hemisphere includes Latin America and the Caribbean (see following definition), the United States and Canada.
4 Latin America and the Caribbean here is Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela, Bahamas, Barbados, Belize, Guyana, Jamaica, Trinidad and Tobago, Haiti and the Dominican Republic.

e = estimate

Source: IADB, Department of Integration and Regional Programmes, Division of Integration, Trade and Hemispheric Issues, based on DATAINTAL. Caribbean, US and Canadian data, as the source country, are from IMF, *Direction of Trade and Statistics.*

Table 4 Selected Latin America Free Trade Agreements: Excepted Products
(number of tariff lines)

Sectors (SITC Rev. 2)	Canada to Mexico	Chile to Colombia	Colombia to Chile	Chile to Ecuador	Chile to Venezuela	Colombia to Mexico	Mexico to Colombia	Costa Rica to Mexico	Mexico to Costa Rica	Mexico to Chile	Chile to Mexico	Mexico to Venezuela
Food and live animals chiefly for food	72	128	128	114	46	203	115	85	51	35	38	114
Beverages and tobacco		6	7		6	14	3	15	3	6	6	3
Crude materials, inedible, except fuels		15	14	17	24	39	136	4	7	1	13	177
Minerals fuels, lubricants and related materials		15	24	16	15					17	18	
Animal and vegetable oils, fats and waxes	1	38	46	56	25	46	7	1	1	30	25	7
Chemicals and related products, N.E.S.	4	43	52	17	32	56	83	7	3			51
Manufactured goods classified chiefly by material		215	161	4	43	31	103					605
Machinery and transport equipment		172	9	3	153	26	65					15
Miscellaneous manufactured articles		40	37	2	6	180	146					145
Commodities and transactions not classified elsewhere in the SITC				5			4					4
Other (n.e.)		1	12			10	7					7
Total	**77**	**673**	**490**	**234**	**350**	**605**	**669**	**112**	**65**	**89**	**100**	**1128**

Source: Estevadeordal (1998).

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Floor Discussion of "Regional Integration Around the Pacific"

Political Commitment and Other Non-Economic Issues

While the economic aspects of regionalisation in Asia and Latin America ultimately received substantial attention from the conference participants, Barry Herman began a discussion of the non-economic aspects by suggesting a hypothesis. "It is worth noting that each of the panelists mentioned the importance of political organisations and institutions for regionalisation in the regions under discussion. While economic benefits and costs can be estimated and shared among participants, you cannot do the same with political benefits and costs. The latter are hard to measure because political dynamics are more complicated. Nonetheless, I would suggest that regional arrangements exist as long as there is a political glue to hold the arrangement together."

Stephany Griffith-Jones agreed with this and suggested that the European Commission's role in European integration could provide useful insight to Latin America. "Regardless of what one says about EC bureaucracy, it has played the role of keeping a vision of integration alive when individual countries have faltered."

Andrew Cornford asked Ricardo Ffrench-Davis for clarification regarding the benefits of preferential trade agreements (PTAs) in Latin America. "You seem to be saying that the PTAs in Latin America served as an enabling vehicle for constructing the necessary institutional infrastructure for trade between countries, and that without the PTAs, the infrastructure would not have been established because of political conflicts."

Ffrench-Davis confirmed this interpretation. "In Latin America, the institutional infrastructure and several other measures which helped to promote intra-regional trade were the result of the PTAs." Robert Devlin agreed. "Ricardo is absolutely right that the integration process induced thinking about the infrastructure that was not thought about before, and an example of this is Mercosur."

Arvind Panagariya, on the other hand, argued that a more convincing response with regard to the infrastructure issue would result from macroeconomic cost-benefit analysis. "If the issue is whether India should build a road to promote trade with Bangladesh or whether they should invest their resources in improving the port facilities which will hook it up better with the rest of the world – apply cost-benefit values to the two. If you think

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there is some extra value being generated in trade with Bangladesh or in trade with the rest of the world, you should add this to the benefit side. In my view, this should be the reasoning behind deciding what infrastructural projects should and should not be undertaken. There is really no need to attach infrastructural projects to PTAs. India and Bangladesh, for example, have completed their water-sharing agreements outside of the PTA."

Mohamed El-Erian wondered whether an external catalyst would be helpful. "It's clear that the amount of interaction in South Asia has been remarkably low, and that this has primarily been due to non-economic factors. In the case of the Middle East and North Africa, movement only started once they had the catalyst of the EU association agreements. Given the history of South Asia, are these countries able to move individually or would you need an outside catalyst?"

Pigato thought it unlikely that South Asia would be influenced by outside intervention. "I doubt India will accept anyone from the outside. And while India could perhaps play that role with the other countries, it has been less of a benevolent brother in the past – for obvious historical reasons. So I can't see any outsider playing that role."

Gavin Maasdorp turned the discussion to the peace dividend that might be gained from the South Asian Association for Regional Cooperation (SAARC). "I found Miria Pigato's statement about the peace dividend in SAARC interesting. If SAARC can establish itself as a highly stable free trade area, it would certainly be one of the building blocks for greater trade flows within the Indian Ocean rim. As a clarification, the Indian Ocean Rim Initiative is not envisaged as a free trade area but it is focused on regional cooperation."

Robert Devlin cautioned against relying too heavily on the peace dividend. "Increased trade and interdependence at the commercial level will not automatically guarantee peace. While it may be likely that increased interdependence and contact will reduce the risk of an outbreak of conflict, there are no guarantees." He then brought the discussion back to the issue of non-economic benefits. "Most of the regional integration agreements in Latin America, particularly Mercosur, are much more than PTAs. They are agreements in which the commitments go well beyond trade. In Mercosur, for instance, there is increased interdependence in trade and investment and there are projects to interlink universities. Mercosur has a common symbol which the public recognises. In fact, the polls show that the general public is behind bringing these countries together. So one has to go beyond economics and trade to see what is actually happening."

Percy Mistry stressed the importance of including non-economic issues in cost-benefit analysis. "Miria Pigato commented that a preferential trade agreement would be useful in Asia given the plethora of problems there.

This notion that there are non-economic gains from regionalisation raises an interesting issue: if the World Bank is willing to accept the price of preferential trade in order to get discussions started, what is the notional cost-benefit analysis that the Bank is undertaking in order to arrive at the conclusion that these losses from preferential trade are worth taking to achieve other benefits? What are these other benefits and why are you willing to make the trade-off?"

Miria Pigato answered by elaborating on the work done by the World Bank on South Asian countries' integration into the world economy. "When you look at South Asia, you face the fact that this is the poorest region in the world. There are 1.3 billion people and half a billion of them are living in poverty. This is also the most protected region in the world, and it is a region where political turmoil and governance issues are very present. We cannot really discuss development without taking these considerations into account. Twenty years ago, Sri Lanka was very open, and its level of human development was higher than any other country in the region – it could have been a miracle, but it is not. It has not developed as much as it could because of a 15-year civil war. All of the countries have now embarked on policies of opening up, and there is no turning back. This may ultimately result in a peace dividend."

Economic and Financial Issues

A discussion of the details of integration arrangements included issues such as the optimal level of tariffs, the effectiveness of regional financial arrangements and the appropriate macroeconomic policies of the countries involved. But first Salvatore Zecchini wondered about the type of integration emerging in Latin America. "It is not clear to me what kind of regionalism is developing in Latin America. Is this a regionalism that is just linked to tariff reduction and preferential trade arrangements or is it a regionalism that goes beyond tariff reductions into a real common market where enterprises from different countries can compete on a level playing field? You can reduce tariffs, but at the same time there are a number of other elements, such as taxation, which impinge on trade between countries. Are there any constraints on taxation, particularly indirect taxation, in these countries that have entered into the regional integration process?"

Robert Devlin answered that Latin American bilateral arrangements formally have the objective of a common market. He went on to say, "I think the only one which has a clear vision of where it is going is Mercosur. In the other arrangements, the declarations go far beyond the reality or the plans."

Stephany Griffith-Jones raised the issue of regional financial arrangements with a comment on Arvind Panagariya's presentation. "Most of your discussion was on trade, but in Asia finance has been and will remain a central issue. While the existing regional financial arrangements were initially strong enough to resist the currency crisis, they ultimately failed, and there is a lot of discussion about whether and how they should be upgraded. I think it would be interesting to include this issue in your analysis because there is a link between trade liberalisation and the willingness to create regional financial mechanisms."

Percy Mistry suggested that financial interrelationships were just as important in Latin America as in Asia and asked Robert Devlin and Ricardo Ffrench-Davis how they would construct regional financial arrangements in Latin America and whether they viewed them as an important step in the process of regionalisation, "especially considering the contagion effects of the debt crisis and the possibility of contagion effects of financial shocks emitted through global markets. How would these arrangements relate to national mechanisms and interlinkages with global defense mechanisms?"

Robert Devlin's impression was that in Latin America there was not too much activity with regard to financial arrangements. "Mercosur has, at this moment, no arrangements in the financial area. We are hoping to have a services protocol at the end of the year which will liberate financial services, but there are no larger financial arrangements to deal with surges in capital inflows or outflows. I think such arrangements are still quite far into the future because the countries are not even coordinating or exchanging information at the macro level. If it were to occur, it is likely to happen at the sub-regional level first."

Bertil Oden asked about the instruments for equalising the gains of regionalism. "As I understand it, for instance, this was a problem with the Andean Pact. Is this no longer a problem with the new type of regionalisation?"

Robert Devlin responded that this is still a worrisome issue in Latin America and that it could be traced to the 1960s and 1970s. "In this period, almost all of the schemes had compensatory mechanisms for the least developed countries. What ultimately happened, however, is that the mechanisms became permanent. There was no convergence or effort at convergence in the laggard countries, and this has created some resentment among the more advanced countries. As a result, the style of integration today is that everyone enters almost immediately on equal terms. This could be a shortcoming because we know that in all of these types of agreements there are asymmetric distributions which can become severe and undermine the whole integration process."

Salvatore Zecchini made three observations regarding foreign direct investment (FDI) and trade in Latin America. "It is believed that a substantial portion of trade expansion in today's markets is linked to FDI – exports of goods with exports of capital. In this respect, what is the evidence as far as Latin America is concerned? Second, is there any move to couple trade agreements with agreements to protect or promote FDI? My third point has to do with the commodity composition of trade once these countries enter into a preferential trade agreement. Is there a tendency toward trade specialisation in Latin America which would justify this move toward preferential trade agreements or is there an evolution toward intra-industry trade? If it is the latter, it invalidates the argument that you join a free trade area because you have complementarities in productions structures. I would be interested in knowing more about the evidence and conclusions in order to better characterise Latin American regionalism."

Following up on Zecchini's observations, Arvind Panagariya argued, "If you want to harmonise your investment policies, you don't necessarily have to attach it to a PTA. Many of the investment agreements are bilateral treaties, so if you really want to proceed on that front, you could do so without a regional arrangement."

Robert Devlin concluded the discussion by commenting on the issue of tariff and non-tariff barriers. "Regional integration arrangements tend to be second- or third-best strategic compromises to bring countries together that might not otherwise cooperate. But regardless of the external levels of protection specified in the agreement, it is important to reduce protection over time. This will erode preferences and insure that firms are eventually put to the test of the global market. It is certainly true that many arrangements, including Mercosur, include non-tariff measures which restrict trade. These are usually technical measures such as rules of origin, but these should be eased over time – presumably as the competitive position of the firm and the country improves. I see this as part of an evolution. In Mercosur, non-tariff barriers are the primary obstacle and there is a major project to eliminate these barriers between 1998 and 2000."

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