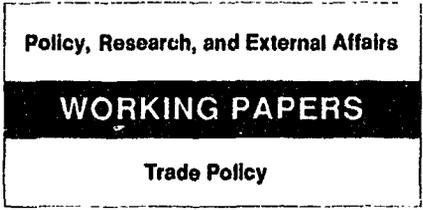


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# **Regional Integration among Developing Countries, Revisited**

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**The formation of new, powerful economic and trading blocs and the transition to market economies in Central and perhaps Eastern Europe has fostered a trend toward new regionalism in the world economy — which the virtual failure of the GATT negotiations may speed up. To minimize economic losses and avoid marginalization, regional groups of developing countries must increasingly work out common positions and join one of the influential groups.**

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This paper — a product of the Trade Policy Division, Country Economics Department — is part of a larger effort in PRE to study new developments in regional integration and their relation to trade strategies. Copies are available free from the World Bank, 1818 H Street NW, Washington, DC 20433. Please contact Dawn Ballantyne, room N10-001, extension 37947 (51 pages).

Economic integration among developing countries became an important policy issue in the 1960s and early 1970s. But although intraregional trade increased in some trading groups, it remained a modest share of total trade, tended to decline in the 1970s, and stagnated during most of the 1980s. In addition, ambitious plans for joint industrialization could not be implemented.

This failure could be attributed partly to the smallness of most of the markets, different political and economic policy orientations, the low level of economic, industrial, and infrastructural development, and similar production and export patterns. Also, serious problems arose in implementing the main objectives. Trade liberalization was blocked or substantially slowed down, highly protective barriers to trade remained untouched or were harmonized regionally, and controversy about the distribution of gains and losses could not be resolved. Dramatic changes in the world economy further affected the environment for regional integration and cooperation.

But the formation of new, powerful economic and trading blocs — such as the single market of the European Community, the U.S.-Canada free trade area, initiatives in the Pacific basin, and the transition to market economics in Central and perhaps Eastern Europe — seems to have fostered a trend toward new regionalism in the world economy. The virtual failure of the GATT negotiations may speed this up. To minimize economic losses and avoid marginalization, regional groups of developing countries must increasingly work out common positions and join one of the influential groups. Both factors require the gradual yet rapid dismantling of barriers to the free flow of production factors within regional groups.

New approaches to regional cooperation have emerged. Attempts to revitalize dormant regional groups, to form new blocs, and to set partly new priorities are on the increase. Trade is the most important element of the new initiatives, but assessments of the possibilities and limits of regional integration have changed since the 1960s.

Stabilization and adjustment policies have created more open, export-oriented, liberal, and competitive economies. Higher exports have generated more growth and regional demand. Industrial restructuring has improved competitiveness, attracted international capital and technology, and opened up areas of intra-industrial division of labor. Export-oriented economies have proved increasingly competitive in extraregional markets.

In most cases it was not the regional training but successful outward-looking policies that improved competitiveness within the region and resulted in higher intraregional trade volumes. The strengthening of the private sector and closer cooperation in infrastructure development (mostly the more efficient use of human resources) support the shaping of an environment conducive to new opportunities for better regional trade.

Obviously, intraregional trade cannot become an alternative to trade flows that are basically oriented to the world market. But in the 1990s, intraregional trade and economic relations are likely to grow parallel to, or even at a higher rate than, extraregional contacts.

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## REGIONAL INTEGRATION AMONG DEVELOPING COUNTRIES REVISITED

### I. Introductio.,

Economic integration among developing countries became an important research topic and a major policy issue in the 1960s and early 1970s. In the years that followed, however, implementation failures and shortcomings as well as changing international economic conditions substantially reduced the attention paid to this topic. Although most developing countries remained members of at least one regional grouping, poor, if any, results in trade, industrial cooperation or institutional development were reported.

Since the mid-1980s, internal and external shocks, adjustment requirements, and changing economic policies have given birth to new approaches. It is still premature to assess the success or failure of these attempts, because most new initiatives are scheduled to be implemented in the months and years to come. A number of initiatives, led by the ambitious target of creating a common market by 2010, emerged in Sub-Saharan Africa. The Union of Arab Maghreb was founded in early 1989, with the just-recently declared aim of introducing unified import tariffs by 1991 and achieving full customs union by 1995. In addition, the Gulf Cooperation Council, a previously loosely-organized regional cooperation group became active in trade, financial, and infrastructural areas. ASEAN (Association of South East Asian Nations), which in the past had emphasized extraregional economic and trade orientation, has taken steps towards the establishment of a regional common market. In Latin America, the revival and dynamization of the Central American Common Market may acquire urgency following the latest political changes in the area. The until-now dormant Andean Pact is considering the elimination of barriers to intraregional trade by 1993, hoping to achieve harmony amongst the member countries' economic policies. Meanwhile, Argentina and Brazil

have been engaged in strengthening bilateral contacts that are expected to set the foundation for broader regional integration in the future.

Simultaneously, also rationalization trends in developed parts of the world economy explain the apparent comeback of the idea of regional integration and cooperation. Some examples of these trends are: The US-Canada free trade agreement; ongoing negotiations for Mexico to establish a free trade area with the United States, the Bush initiative for the creation of conditions conducive to free trade in the Western Hemisphere, proposals for trade preferences in the Pacific basin, and most importantly, the EC '92 program of the single market, which forces developing countries to reconsider the chances of broader regional cooperation.

The EEC (European Economic Community), established in 1957, was a major factor behind the decision in the 1960s of many developing countries to form regionally integrated groups. For reasons to be discussed later in this paper, these imitations generally failed while the EEC became a successful trade bloc with substantial international economic influence. At present, the challenge is no longer how to voluntarily imitate the EC but how to adjust to new realities.

Is regional integration among developing countries (RIDC) an adequate response to this challenge, and will it prevent the further marginalization of several national economies? Should the new approach be different from the traditional, one-sided trade policy-oriented concept? If yes, what kind of new instruments can or should be applied? Will regional cooperation and integration contribute more efficiently to economic adjustment than do economic policies formulated and implemented within a national framework? In sum, is there justification for narrowing the wide gap between the RIDC's declared goals and

achieved results, and for solving the fundamental contradiction between "brilliant perspectives and formidable everyday constraints" (Tavares de Araujo, 1987), experienced by regional integrations in the last decades?

This paper concentrates on some of the crucial issues and lessons raised by the development of integration processes among LDCs (least developed countries). We have collected, on a comparative level, statistical data and practical experience covering ten regional integrations. Four of the groups selected are from Latin America: Central American Common Market (CACM), Caribbean Common Market (CARICOM), Latin American Integration Association (LAIA), and the Andean Pact. Another four are from Africa: Economic and Customs Union in Central Africa (UDEAC); Economic Community of West African States (ECOWAS), Southern African Development Coordination Conference and Preferential Trade Area of Eastern and Southern African States (SADCC-PTA), and the Arab Maghreb Union. We have also included one bloc from Asia, the Association of South East Asian Nations (ASEAN), and one from the Middle East, the Gulf Cooperation Council (GCC). (See the annex for list of the member countries.)

This paper is divided into two fundamental parts. Section II analyzes the most important elements in the RIDC's failure during the 1970s and 1980s. It concentrates on theoretical issues, implementation failures, adverse impacts of the international economy, and fundamental sociopolitical differences. Section III describes recent or revived arguments in favor of regional integration, and points to new approaches in critical areas of trade policy, cooperation in infrastructural development, and joint activities vis-a-vis third (non-regional) countries or their groups. Section IV summarizes lessons and conclusions.

## II. Why Did the RIDC not Succeed?

### A. Incorrect Theoretical Setting

#### 1. Trade Theory

The first two phases of economic integration, the creation of a free trade area and the establishment of a customs union, were originally elaborated and proposed for groups formed by developed industrial countries. The abolition of barriers to intraregional trade and the implementation of common external tariffs in relation to third countries were expected to increase welfare by replacing higher priced domestic products by lower priced products purchased from the integrated area. Although the efficiency of this substitution process has been hampered by the imposition of common external tariffs that provided preferences to higher-cost regional imports compared to lower-cost imports from outside the region, the benefits due to trade creation were supposed to outweigh potential losses from trade diversion.

This theory was based on the assumptions that: (a) by integrating developed economies, a large and differentiated regional market would emerge; (b) the member countries had diversified production patterns in which industrial goods prevailed, so that competition and specialization efforts would become stronger; and (c) member countries had a long history of intensive trade and capital flows and an efficient infrastructure long before common trade policy had been initiated.

Unfortunately, none of these preconditions are sufficiently present in the RIDC. All regional groupings of developing countries have modest aggregate national income and small collective markets (Table 1). The GNP of the relatively most powerful Latin American Integration Association (LAIA) is only 16 percent higher than that of EFTA, and is similar to that of France. ASEAN's

total GNP equals Spain's; the Maghreb's GNP is comparable to Turkey's; and CARICOM's GNP does not surpass that of Uruguay. The CACM and UDEAC in Central Africa each, have an aggregate GNP lower than that of Hungary. Considering all regional blocs formed by developing countries, and even when membership duplications occur in more than one group, their total GNP is about one-third of the EC's GNP.

In light of import figures, the market size of the RIDC is even more limited. This is not only due to its modest GNP but also due to its long history of closed, autarchic, import-substituting development patterns. For example, LAIA's total imports are as high as Hong Kong's, and the import markets of CARICOM, CACM, or UDEAC are the same as that of Kuwait. Even ASEAN, whose member countries pursued export-oriented economic policies, imports 80 percent less than EFTA and less than 10 percent of total imports by the EC. All the RIDCs considered in Table 1 have an aggregate import market that is less than 10 percent of world imports and is comparable to imports by West Germany.

These facts do not justify the frequently-used argument that the large populations of some RIDCs are a major potential advantage of integration. Certainly, LAIA is more populous than the EC, and ASEAN's total population is rapidly approaching the EC level. However, low per capita income, aggravated by highly uneven distribution, and generally extremely low import per capita figures, impose a major constraint on the total volume of effective regional demand.

In addition, potential gains from specialization are usually small. Member countries often display modest differences in relative factor endowments. They tend to export competing goods that are produced in every or several member

countries and import goods, services, and production factors (capital, technology) that are not available within the region.

In historical retrospect, trade and economic contacts have been fundamentally established with and shaped by extraregional markets. As a result, neighboring markets are often unknown and the infrastructure within a regional group is generally underdeveloped, which is a major barrier to enhanced intraregional trade. In 1989, intraregional exports by the RIDC totalled \$40.5 billion or 1.34 percent of world exports, and less than 5 percent of intraregional trade in the EC (Table 2). Even compared to total South-South trade, the RIDC's share amounts to only 31 percent, with about 70 percent being interregional trade flows. Only ASEAN's and LAIA's intraregional exports (\$22.6 billion and \$9.3 billion in 1989, respectively) deserve some attention as volumes of international significance. On examining the share of intraregional trade in total trade for the groups selected, ASEAN's 18 percent figure stands out, while that of CACM, CARICOM, and LAIA is in the 10 to 13 percent range. In all other groups this figure is far below 10 percent, and in some cases even below 5 percent. Compared with the same indicator of more than 60 percent for the EC, the decisive role of extraregional to intraregional trade is indisputable.

## 2. The Training Ground Theory

This theory starts out from the hypothesis that the international competitiveness of developing countries can be gradually improved by relying on the regional market in the first phase of industrialization. Free trade among members and usually high (common) external tariffs on extraregional imports temporarily protect infant industries and provide, at the same time, sufficiently large markets for future development. Entrance into the world's market may be

considered after reaching a certain degree of efficiency, due to advantages of economies of scale, technical development, and specialization on the regional level. Thus, regional integration provides a transitional period in the way to global division of labor.

The facts, however, do not support this theory. The approximately two dozen newly industrialized and newly exporting countries (NICs and NECs) that emerged in the last 10 to 20 years, became industrial exporters primarily by entering the highly competitive world market and not because of help from protected regional markets. Except in specific cases, economies focusing on the regional market for industrial products could not usually gain international competitiveness. In 1970, 39 percent of South-South trade consisted of manufactured goods, compared with only 20 percent of the South's exports to the North. By 1989, exports to the developed countries became structurally more developed than those to other developing economies -- 58.7 percent against the 53.4 percent represented by industrial products (United Nations, 1990).

To summarize, the regional training ground argument has been weakened by several factors: (1) the fundamentally narrow regional markets did not offer economies of scale advantages; (2) the structural pattern of extra- and intraregional exports differed widely; and (3) little or no structural upgrading took place as a consequence of the regional "learning process".

### 3. Dependency Theory

From the very beginning, some politicians and economists considered the RIDC a useful tool for loosening and gradually eliminating the historically deep economic and structural dependence of LDCs on the developed world. As national import substitution became not only increasingly costly but also started to

increase dependence on vital external sources, regional integration, i.e. import substitution on the regional level, was expected to break up the traditional dependence pattern. In some cases, the fundamental aims to be achieved through the RIDC were the strengthening of self-reliance and improvement of the collective terms of trade with regard to developed countries, combined with the common struggle against growing protectionism.

However, the path taken led to increasing inefficiencies, low quality production, lack or loss of competitiveness, and perpetuation of regional underdevelopment. Dependence on the external world could not be reduced; on the contrary, it tended to increase, as financial flows, technological and managerial skills, and in most cases also trade links could not be substituted by intraregional assets. Even if some opportunities for self-reliance seemed to open up, the low level of most and the lack of some regional resources, as well as the similar or identical product pattern of the member countries put serious constraints on "independent" development. Substitution possibilities between intra- and extraregional markets remained generally very poor, because the potential or intraregional trade could usually absorb only a slight portion of extraregional trade. As a result, competition for scarce resources and export markets increased among member countries belonging to the same regional group.

Although international protectionism grew in some sectors in which developing countries traditionally had comparative advantages, the general level of tariff protection declined in the last two decades, and a number of new, dynamic markets emerged. At the same time, the fact that intraregional trade faced higher barriers than those erected by extraregional markets, was often overlooked.

The theory of collective terms of trade improvement ignores the fact that a particular regional integration (in most cases even the developing world as a whole) controls only a modest share of world production and market. This market share is unlikely to offer sufficient bargaining power for a long period.

#### B. Unsatisfactory Implementation

Although the failure of the traditional approach to integration cannot be separated from incorrect theoretical assumptions, the practical shortcomings of the implementation of the agreed-upon goals, are also obvious.

A comparison between the basic documents prepared by various regional groups of developing countries and those elaborated by the EC, or the most recent free trade agreement between the US and Canada, reveal striking differences (Tavares de Araujo, 1990). First, while the U.S.-Canada trade agreement contains an extremely detailed description of mutual commitments, the documents establishing the RIDC are a summary of loosely-formulated general proposals, without quantitative projections or an accurately-detailed legal and institutional framework. Thus, the effective impact on the member countries cannot be properly assessed, nor can member countries be compelled to observe fundamental commitments made. Second, the objectives of the RIDC try to cover almost all areas of potential cooperation, rather than concentrating on one or a limited number of priorities. Third, developed market economies are prodded into regional integration by major economic participants. Only then do the government or other institutions involved in the integration respond with adequate policy measures. In contrast, in the RIDC the integration schemes are essentially derived from political concepts and efforts. While, in the developed market economies development is organic, from bottom to top, from economic

realities towards political decision-making, in the RIDC, the opposite occurs and politically generated agreements are imposed on economically insufficiently prepared national economies.

In the international literature on regional integration, the main indicator of success used to be a growing share of intraregional trade in total trade, while a decreasing share is an indication of failure. This approach, however, can be attacked from at least two sides. First, the impacts of regional integration cannot be reduced to intraregional trade. Joint industrial development, establishment of basic infrastructural links and better communication on the enterprise level generally precede growing trade volumes. More importantly, higher intraregional trade shares may be the result of substantial trade diversion from more efficient extraregional imports to less efficient intraregional sources. In this case, the international competitiveness of regional integration is threatened and its share in world trade is likely to decline. Therefore, growing intraregional share can only be seen as a positive development if it is accompanied by increasing competitiveness of the region in global trade.

In the last decade, the RIDCs absorbed a modest and mostly decreasing or stagnating share in its member countries' total trade. Surprisingly enough, ASEAN, whose member countries have been pursuing export-oriented development policies, has the highest intraregional exports, both in its volume and as a share of total exports. After a temporary upswing through 1983 (to 23 percent), however, its intraregional exports stagnated in the 16 to 18 percent range. LAIA was unable to break out of this stagnation in the 1980s and CACM, once the most successful regional group, experienced a sharp decrease of intraregional export

shares after 1980. All the other, even less important regional groups reveal stagnating or slightly changing intraregional trade shares (Table 2).

This general picture becomes less homogeneous when trade orientation of the individual member countries is analyzed. Smaller, landlocked economies generally show above average regional orientation. As an example, in 1987 intraregional exports amounted to 30 percent of Uruguay's total exports, while the corresponding figures were 45 percent for Paraguay and 62 percent for Bolivia.

There are also substantial differences in the commodity pattern of intra- and extraregional exports. In the 1960s and part of the 1970s, raw material- and capital-intensive manufactured exports were preferably sold on the regional market, while primary goods and labor-intensive industrial products revealed a clear extraregional orientation. The less developed a member country was, the more pronounced the bias. In the 1980s, countries pursuing outward-looking economic policies were likely to experience decreases in the differences in the commodity pattern of intra- and extraregional exports. Growing structural harmonization could be identified, even in regional groups containing less export-oriented economies (LAIA, Andean Pact, UDEAC), although intraregional exports usually had a higher share of manufactured goods than extraregional exports (Rodriguez, 1990). (A broad statistical comparison of the changing pattern of intra- and extraregional exports in various regional integrations between 1976 and 1986 is in progress.)

Trade liberalization was a slow and selective process, not only in the mainly import substituting economies but also in more export-oriented groups (ASEAN). As a result, original timetables were not observed. As regional trade liberalization approached the highly protected "hard core" of domestically

produced goods, the process usually stopped and sometimes was even reversed. In the first stage, tariff cuts were abundant, but they did not affect national production. Part of the liberalized items have never been imported, others have never been produced within the regional group (Greenaway and Milner, 1990). Products that have been manufactured within the group, particularly if production was located in more than one country, were generally phased-out of trade liberalization and put on the list of "sensitive products".

Additional protection was provided by widely used non-tariff barriers and strong national rules of origin (e.g. in Latin American car production). In this context, it is not surprising that several countries found it easier to export to extraregional markets than to have access to the regional market, particularly if they enjoyed preferential treatment in third countries -- for example, African exports to the EC (Intra-Regional Trade, 1988). In this way, trade liberalization did not create substantial additional trade within the region. More importantly, it maintained the old and inefficient national production even in areas in which regional competition and reallocation of resources might have resulted in increased international competitiveness, emerging intra-industry linkages and greater intraregional trade.

Common external tariffs (CET) established in the CACM and the UDEAC, as well as common minimum external tariffs implemented in the Andean Group, tended to reinforce structural distortions and production inefficiencies. If there was regional production of a certain product, the CET was fixed in the higher range or on the highest level of different national tariffs. In case of ongoing production (joint industrial projects, infant industries), a sufficiently high tariff was placed for effective protection. Consequently, relatively more efficient producers started to lose their comparative advantages by using high-

priced and several times qualitatively less-demanding regional inputs. Recognizing this danger, some more competitive national economies did not apply the CET, thus leading to growing disagreement within the group. To make matters worse, they started to import from outside the region, particularly if sufficient foreign exchange was available and if production based on extraregional input promised international competitiveness. Thus, to a certain extent, the impact of the CET's trade diversion could be mitigated. Moreover, in some cases "negative trade diversion" occurred, when new national and regional industrial projects required additional imports available only from outside the region (Khazeh and Clark, 1990).

Joint industrialization remained far behind its ambitious goals of enhancing output, diversifying production patterns and implementing equal redistribution of costs and benefits. As trade liberalization excluded most current production from tariff preferences, the establishment of new industries has been seen as the main beneficiary of tariff cuts. Distribution of production rights and thorny questions of joint financing have provided sufficient explosive material. Even if generally very costly development project packages have been agreed on, their implementation met a number of barriers in the individual national economies. Often, aggregate regional demand fell short of the effective capacity of just one joint project. This situation notwithstanding, parallel capacities have been created in one or several member countries. Thus "cathedrals in the desert" were erected practically everywhere (Aghrout and Sutton, 1990). But even if regionally planned industrialization could have avoided the capacity underutilization trap, the oligopolistic structure would have blocked the way to meaningful intra-industry specialization.

The fewer the economic gains achieved through regional integration, the greater number of regional institutions that have been established. In Africa, there are more than 200 organizations of cooperation, 80 percent of which are intergovernmental bodies (Inter-African Cooperation, 1988). They require substantial financial resources, time, and expert knowledge that could be used more efficiently in other areas. Parallel to the proliferation of institutions, some countries became members in different regional groups. Simultaneous commitments to different regional efforts raise questions about the member country's commitment to any serious undertaking. At the same time, no attempt has been made to integrate the objectives of the regional integration into the system of national development planning.

### C. Adverse World Economic Impact

From the mid-1970s on, world economic development began to exert a substantial impact on the fate of the RIDC. Economic recession, drastic price and terms of trade changes, balance of payments disequilibria, and dramatically growing indebtedness, had great impact on the economic conditions that had given birth to regional integration.

Almost all regional groups split into two parts. Some countries (mainly oil-producing and -exporting countries) were, temporarily, in a better position than others (oil-importing countries). In this situation, intra-group economic power relations were reshaped, and regional solidarity was increasingly threatened.

More importantly, increased efforts to enhance exports and attain international competitiveness required a sometimes dramatic change in the basic economic policy orientation of the member countries. However, this export-

orientation would seem to contradict the basic philosophy of regional integration, the import substitution on the regional level. External challenges called for the reassessment of previous economic strategies, the reshaping of production patterns, and the geographic reorientation of exports. The sources of technology, management skills, and most importantly, direct capital -- all necessary elements of a competitive development strategy -- were almost exclusively outside the boundaries of regional integration. Similarly, orientation on the world market required quick production and marketing decisions that could hardly be taken by a group of countries of any size, characterized by different economic interests and lengthy coordination and decision-making procedures.

Worsening terms of trade and increasing deficits resulted in growing indebtedness. This, in turn, made higher exports the cornerstone of a viable import and debt financing policy, even in countries that did not opt for an export-oriented growth strategy. Given their small and dramatically contracting national and regional markets, exports had to be directed to extraregional markets. Although relatively rich oil-exporting member countries offered a temporarily growing import market to regional partners (as Colombia's exports to Venezuela, Indonesia's growing imports from ASEAN and Nigeria's purchases from neighboring ECOWAS economies), this potential remained rather modest, compared to extraregional opportunities, and mostly used by more efficient extraregional suppliers.

Other factors too, had a negative impact on the importance of the regional market. As a result of increasingly difficult financing, interest in buying higher-priced and lower-quality goods produced by the regional partners and protected by high (common) external tariffs, rapidly vanished, and because

international competitiveness of exports could only be achieved if inputs from competitive imports were used, a growing shortage of convertible currencies led to substantial import cuts and substitution processes on the national level. Intraregional imports generally suffered more, because they consisted mainly of substitutable, "non-vital" items (mostly consumer goods and intermediate products). In turn, a number of goods, only available from outside the region, remained non-substitutable, "vital" inputs, regarding domestic production, consumption and competitive exports.

Declining or negative growth rates, accompanied by sluggish investment activity, further constrained intraregional trade. For example, intraregional imports of manufactures in the CACM amounted to 10 percent of total regional consumption of manufactured goods in 1980, but had declined to 6 percent in 1985, while the share of extraregional imports in regional consumption remained unchanged in the same period (Trade Liberalization, 1989).

Meanwhile, the role of trade policy instruments influencing intraregional trade flows had also been changing. First, the external trade liberalization cum stabilization policies adopted by various countries in LAIA practically abolished earlier granted preferential treatments (Manzetti, 1990). The trade liberalization achievements of some member countries became more and more difficult to integrate into the system of regional preferences. Second, foreign currency shortages and the protection of newly established high-cost import-substituting production led to what was hoped would be a "temporary" reintroduction of earlier lifted QRs and increased tariffs. Even when no new barriers were introduced, the original time-table for intraregional trade liberalization was either completely abandoned or it was determined that longer transitional periods were needed. The Andean Group gave some consideration to

"managed trade" (comercio administrado) in order to avoid the spreading of national exemption lists and to prevent individual actions that seriously threatened the existence of the integration. Third, the need to finance growing budget deficits limited the viability of trade policies which required substantial intraregional tariff cuts that would have resulted in decreased government revenues.

In the 1980s, compensatory payments facilities that had been financing relatively high volumes of intraregional trade in the 1960s and 1970s, either partly collapsed or suffered substantial contractions. This was due to the fact that either pressing debt problems impeded the transfer of even modest sums to the compensatory fund, or rapidly growing bilateral trade disequilibria and the level of accumulated deficits made further financing by surplus countries impossible. In 1988 in Central America, less than 1 percent of intraregional trade was financed through the compensation mechanism (Bendesky and Sanchez, 1990). The compensation level of intraregional trade in LAIA (as well as in LAFTA, its predecessor), which was as high as 77 percent between 1986 and 1979, declined to 71 percent in 1982 and reached its peak of 84 percent by 1986. Although this helped member countries save considerable amounts of convertible currency, neither the fund's facilities nor interregional trade expanded during this period. Argentina's dramatically increasing trade deficit had, in just two years, undone the \$400 million bilateral trade financing scheme established between Argentina and Brazil in 1986.

Exchange rate policies have affected the development of intraregional trade also. Steady (gradual) and necessary devaluations, which sometimes ended at damaging devaluation competition, also diverted trade from intra- to

extraregional markets or, at the very least, allowed extraregional exports (consisting mainly of primary goods) to be valued higher than intraregional exports. As a result of diverging stabilization policies and the ensuing diverging official exchange rates of national currencies in relation to the U.S. dollar, national currencies became over and sometimes under-valued. Member countries with the least overvalued (or most undervalued) currency have benefitted the most from intraregional trade. At the same time, however, regional deficits accumulated rapidly and prevented further intraregional trade expansion. The monetary union could, in some cases, prevent national economies from different degrees of devaluation, but at an unprecedentedly high price. In the case of UDEAC (which, since 1948, had a fixed rate of 1:50 between the French franc and the CFA), the region became chronically uncompetitive, its production highly distorted, and the official intraregional trade practically negligible. In turn, unrecorded trade, i.e. smuggling, is estimated to have reached figures several times higher than those revealed by official trade statistics.

Although practically all national economies have been challenged by dramatic world economic changes, not all of them have been equally affected. Indeed, very different national economic policies have been formulated as a response to the changing environment. But even if economic policies had been based on the same principles, the economic and social backgrounds for their implementation would still have been substantially different, and, consequently, would have led to different developments from country to country. The emerging differences were then compounded by the technical failures of policy implementation. In sum, the international economy tended to hinder rather than support the harmonization of national economic policies in regional integrations.

#### D. Different Sociopolitical and Economic Systems

RIDCs were usually based on geographical considerations, as reflected in the official name of most regional groups. Considerably less attention was paid to the sometimes substantial differences in socio-political and economic orientation among member countries. Market-oriented and centrally-administered economies belonged to the same group (Colombia and Peru or Allende's Chile in the Andean Pact, Costa Rica and Nicaragua in CACM, Kenya and Tanzania in the former East African Common Market), as did countries governed by democratically-elected parliaments or those under military rule. The legacy of permanent territorial problems and unsolved ethnic issues made cooperation even more complicated. Fragile governments and unstable domestic power relations made the formulation and implementation of longer-term common regional development strategies more difficult. National governments tried desperately to tie-in national sovereignty with economic integration, but were unwilling to give up even a small fraction of the former. On the contrary, economic integration was often considered (at least by the larger members of the integration) to be an instrument of economic expansion and to strengthen the nation-state.

### III. New Approaches to Regional Integration

Despite the overwhelmingly negative experience with RIDC in the past two decades, most recently, the idea of regional integration seems to reveal some signs of revitalization. This can be seen, in part, in the growing number of new initiatives, even among countries that, in the past, have been fundamentally separated for political and economic reasons. At the same time, the share of intraregional trade in most groups has been increasing since 1985, and

particularly after 1987. Although in most cases it did not even approach earlier achieved peak levels, and intraregional trade remained a modest part of total trade, the short term trend is quite unequivocal. More importantly, this increase was not caused by the trade diversion that resulted from previously applied and frustrated trade policies. On the contrary, some regional groups substantially enhanced their exports to the world, while others (with the clear exception of CACM, the Maghreb, and UDEAC) kept pace with the expansion of world trade. It is with this in mind that the increasing share, i.e. the above average growth of intraregional exports, should be assessed. With the exception of LAIA, GCC and SADCC-PTA, intraregional exports grew faster than the region's total exports and grew at a substantially higher rate than world exports, at current prices between 1987 and 1989 (Table 3).

Does this mean that a renaissance of RIDC may yet occur? And, more importantly, does this new approach promise more success because of the lessons learned from the earlier experiments of the last decade? It is still too early to give a straightforward answer to these questions. Unfortunately, there are no common features that would apply to all regional schemes. At least two of the arguments in favor of integration can be shown to be heavily influenced by the individual countries' expectations of medium-term economic prospects.

On the one hand, several national economies with clear adjustment deficits, almost hopeless underdevelopment, and growing marginalization, insist on the traditional arguments in favor of regional integration. They argue that if underdevelopment cannot be overcome and if their economies remain desperately uncompetitive in the world market, then economic integration as a second best (or second worst?) scenario may help alleviate the crisis, avoid increasing poverty, break historical dependencies, and strengthen elements of self-

reliance. Repeated efforts to create an African common market are primarily based on this set of arguments.

On the other hand, national economies that in the last decade underwent substantial restructuring and pursued more open, world market-oriented policies, seem to have rediscovered the opportunities offered by regional integration. Indeed, regional integration is no longer seen as an instrument of import substitution on the regional level, but as part of a new strategy based on more competitive production and export patterns, and on the acceptance of the rules of the game that characterize international trade and economic relations. Although economic liberalization might have broken some of the earlier and usually non-competitive regional links and replaced them with extraregional contacts, it has laid the foundation for efficient regional cooperation.

Some of the specific effects of economic liberalization are as follows: (1) it generated higher growth rates that led to higher internal demand. Various potential exporters, including those from the region, had expanding markets as their objective; (2) structural upgrading, coupled with the changing of production patterns based on comparative advantages in international trade, created growing opportunities for intra-industry division of labor; (3) the general opening up of the economies lessened protectionist pressure and helped a new entrepreneurial spirit to emerge -- for example, contacts among representatives of private business, such as producers, exporters, importers, bankers, etc., became much more frequent; (4) because the liberalization process as well as the instruments used, were similar in various countries, national economic policies became more transparent, and differences between countries were lessened; (5) rapidly expanding regional markets prompted multinational companies to reassess their strategies, which had previously focused on setting up

production in protected national markets. The economic liberalization of various national economies in the same region is likely to shift investment decisions towards fewer, but more efficient, projects that produce for several countries in the region. The expected forward- and backward-linkages may support regional integration on the microeconomic level, as is already the case in ASEAN.

In some cases, common economic (debt strategies, trade agreements with major trading partners, sustainability of stabilization and adjustment programs) and political interests (stability of new, democratically-elected governments) led to regular meetings and working contacts. Better understanding of each other's perceptions and goals, as well as the unquestionable priority of pressing economic problems, resulted in decreasing political controversies and in the settlement of a number of inherited conflicts (primarily in Latin America).

The new regional approach can be identified in three main areas: (a) in trade policy; (b) in infrastructural cooperation; (c) in joint actions vis-a-vis third countries or groups of countries.

#### A. Developments in Trade Policy and Performance

Several countries who had paid little attention in the 1980s to the possibilities for intraregional trade are now rediscovering the relative importance of regional markets. This, however, should not be interpreted as an effort to return to old-fashioned regionalism. Rather, it is more of an adjustment process, following a decade or more of predominantly extraregional export orientation.

Those same companies that have achieved substantial success in exporting outside the region and become competitive on the global scale, are often also the same ones which show interest in getting access to the regional market.

Because past experience has taught them that trade is the engine of growth, they have deduced that all untapped potential that might increase trade, should be used in order to promote growth.

In some cases, the regional market's demand for traditional labor- and material-intensive products, which in the past 10-20 years had been exported to developed extraregional markets, may become more important, in light of growing sectoral protectionism in the principal traditional markets. More importantly, new trends towards regionalization in the world economy, the expected impact of the single European market, the transition to a market economy in Eastern Europe, and growing East-West economic interaction, and doubts about the strength (or viability) of longer-term export-led development, will lead to a reassessment of the future role of intraregional trade.

It should, however, be emphasized that this kind of (partial) trade reorientation is led by national economies that have successfully adjusted to the world economic environment and pursued and will be pursuing an open, liberal trade policy. Intraregional trade is by far the most important, both in its share and in value terms, for the ASEAN countries that were among the champions of export-oriented development patterns in the last decade. In effect, it was their global export expansion that enabled them to increase intraregional trade despite a number of barriers. Similarly, Brazil's or Chile's export successes in the region, as well as Colombia's good regional performance in the 1970s, have all been based on previously achieved international competitiveness.

Growing involvement by competitive sectors and firms in intraregional trade explains why efforts to abolish obstacles to this trade have been gaining ground recently. At the end of 1987, ASEAN decided to reduce the share of tariff items for sensitive products to 10 percent of total and 50 percent of

intraregional exports. The Gulf Cooperation Council<sup>1</sup> abolished national tariffs in intraregional trade all at once in 1983. By September 1988 CARICOM had taken measures to remove all barriers restricting intraregional trade. Both ASEAN and CARICOM promised that member countries would not apply new non-tariff barriers and that they would eliminate the existing ones within three (CARICOM) to five (ASEAN) years. In order to support economic transparency and strategic investment decisions, ASEAN implemented automatic annual tariff adjustment schemes for 10 years. Most recently, LAIA nations have agreed that beginning on August 1, 1990, tariff barriers on intraregional trade would be lowered and that non-tariff barriers would be eliminated. ASEAN has relaxed its rules of origin, now giving preferential treatment to products with a local content of 35 percent (rather than the 50 percent required earlier).

Removal of tariff and non-tariff barriers is expected to increase intraregional exports and, at the same time, to improve the international competitiveness of the most efficient regional producers. This path, however, has difficulties of its own. The elimination of barriers to intraregional trade should not be accompanied by higher protection vis-a-vis third countries. In order to allow for temporary regional preferences it is necessary to make certain that barriers on intraregional trade are lower than barriers on extraregional partners, and not to increase the level of external protection in exchange for more liberal treatment of intraregional suppliers.

In addition, the liberalization processes started by national economies often had different contents, time schedules, and gradualism, leading to the emergence of widely different tariff levels, structures and policies in the region. In order for regional cooperation to succeed, it is necessary that member countries should adjust their trade policy and instruments to those of

the most open economy in the group. This, however, is difficult to achieve in the short run, particularly when the original differences among members are great.

#### B. The Infrastructural Approach to Regional Integration

The classical trade-oriented economic theory of regional integration sees regionally coordinated development of infrastructure as an issue of cooperation rather than integration. Nevertheless, it was the previously created joint infrastructure and the network of institutional services that gave birth to some RIDCs after colonial rule (the former East African Common Market, CARICOM). Growing disintegration processes fueled by diverging national economic policies and political interests eliminated or substantially changed most of these common activities. At the same time, new initiatives based on the common natural infrastructure and its planned joint utilization, emerged (Mano River Union, River Plate Group).

There are several reasons to explain why there have been few attempts in the last two decades to create or improve the regional infrastructure. Lack of financial resources, negative experiences with earlier joint projects that proved to be very expensive, inefficient and sometimes chronically underutilized (yet growing) extraregional trade orientation, help explain this behavior. Also, the modest and often falling volumes of intraregional trade and economic relations could not usually be handled by the previously established infrastructural network.

In recent years, however, practically all regional groups have become increasingly interested in infrastructural cooperation. These new groups view joint infrastructural development as a priority area of cooperation. Three main

factors support this change of mind: (1) the failure of trade-centered integration is partly attributed to the lack or feeble condition of regional infrastructure; (2) international experience shows that high growth rates, structural changes, and increasing international competitiveness are, to a large extent, based on well-designed and long-term investment and development strategies in different areas of physical and human infrastructure; (3) lessons drawn from recent national adjustment and restructuring policies clearly demonstrate that their success or failure was closely related to the availability of an efficient infrastructure.

Arguments in favor of regionally coordinated infrastructural development can be classified in three main groups: financial, trade-related, and socio-political.

The financial arguments emphasize that a number of infrastructural projects are extremely costly, at least compared to the sometimes very modest economic, technical, and financial resources available in national budgets. Therefore, the combining of regional resources is essential. In several cases, regional demand can be met by establishing only one efficiently utilized project instead of a number of fragmented national projects. In this way, duplications and substantial underutilization of infrastructural capacities can be avoided. Also, national infrastructural development plans can be coordinated in order to support a comprehensive regional development. In sum, development costs can be minimized and competitiveness increased. As an additional argument, regionally coordinated development projects are expected to attract external financing more easily and in larger volumes than national projects. Therefore, a part of national (regional) resources can be devoted to other pursuits.

Trade-related arguments differentiate between the direct and indirect positive impacts of developing infrastructure. According to widespread experience, infrastructural underdevelopment led to high transportation costs that made intraregional trade non-competitive. The newly constructed railway between Argentina and Brazil is expected to double the transportation capacity, accompanied by a substantial saving in time and a 40 per cent reduction of costs. A lack of infrastructure is also a barrier to national economic integration in many countries. In turn, a developed infrastructural background is essential in order to create trade. On the one hand, lower transaction costs and better opportunities for intraregional division of labor improve competitiveness in all markets. On the other, exports to extraregional markets may require infrastructural developments that, for geographic reasons, may involve more than one member country. For example, the opening up in May 1983 of the trans-Mediterranean pipeline enabled Algerian gas to be transported to Italy through Tunisia.

Improved conditions for trade produce a chain reaction. Through trade, more information on previously unknown factors becomes available. This information may influence business decisions and even promote additional trade and economic links. For instance, as contacts between buyer and seller become regular, information on the size and pattern of demand and specific features influencing demand (e.g. taste) in other member countries will be widely available. Also, development plans will increasingly consider the available infrastructural background, and new development poles in the region are likely to be created along the regional "infrastructural backbone". The unfolding confidence-building process may strengthen the "integration capability" of regional groups. This is particularly important, considering that in several

regional integrations, high transaction costs resulted in such a high level of competitive disadvantage that could not be compensated for even by substantial regional trade preferences. Low transaction costs (as in ASEAN) can pave the way for closer economic integration without making any progress in the institutional integration schemes (Amelung, 1990).

Socio-political arguments emphasize the role of cultural affinity among neighboring countries and the advantages resulting from the better understanding of each other's aims, reactions, opportunities, and limits. Cooperation in the development of human resources (e. g. education, training, research) is expected to contribute to the elimination of political hostility. Similar educational roots and mentality may help develop an influential group favoring regional cohesion. For landlocked member countries particularly, the improvement of the infrastructural network helps lower unilateral dependence on the country that controls the key export and import channels, and information centers. This was the main reason why SADCC identified joint transportation and telecommunication projects as priority areas of cooperation. Also, cooperation in human resource development may alleviate the brain drain situation, which deprives developing countries of valuable development resources.

Infrastructural cooperation is generally based on identical or similar features of natural and economic geography in the (neighboring) member countries. In most groups, there are at least some member countries which have similar soil and climatic conditions, environmental and geological structures, and belong to the same river system. Their populations often speak the same language and this makes educational cooperation much easier to achieve (see earlier attempts between Colombia, Ecuador and Peru in the Andean Group).

Areas of practical cooperation include a wide scope of activities that have been growing in number and variety in the last few years. In general terms, there has been a shift from "hardware" cooperation (developing physical infrastructure) to "software" cooperation (concentrating on human resources). This is partly explained by the sometimes chronically underutilized and costly inherited physical infrastructure which never handled the volume of intraregional trade that it was meant to. Another reason is the growing importance of "software" in infrastructural development on a global scale.

Joint transportation projects that previously concentrated on creating new highways, ports, and frequently inefficient joint regional transportation companies, have started in recent years, to give priority to the improvement of maintenance of existing facilities and to harmonize national transport and traffic rules (technical standards, environmental requirements, transport tariffs and schedules, contract laws, etc.).

In the field of energy cooperation, there is recently less emphasis placed on energy production. In the past, this was responsible for creating vast (hydroelectric) production capacities for regional markets that were unlikely, in the foreseeable future, to absorb the potential output. In turn, the establishment of a joint regional energy network emerged as a prospective field of cooperation. According to the Latin American Energy Organization (OLADE), member countries suffered on average a 25 percent power loss (almost double the technically accepted level) as a consequence of insufficient integration of national energy-producing capabilities. The interconnection of national energy systems, assistance in energy-related emergencies, and harmonization of technical standards could result in substantial savings of energy. Simultaneously, a

promising new market for energy-generating machinery could be created, with beneficial impacts on intraregional trade (Sanchez and Sierra, 1988).

Dramatic changes in worldwide information technologies and international deregulation of related services prodded member countries to create joint information and telecommunications networks. In the last few years, also joint protection by neighboring countries of the rapidly deteriorating environment has become a priority task.

To some extent, the development of physical infrastructure has a particular impact on border areas within regional integrations and stresses the need for increased "border integration". It is obvious that some border areas have substantial development potential, both for the national economies involved and for the regional integration (geological resources, irrigation for agricultural purposes, water supply, etc.). National territories previously hard to reach or completely inaccessible may now be organically linked to the respective national economies. At the same time, intraregional trade can be expanded. As an additional advantage, cooperation in border areas offers the possibility of easing political tensions and conflicts that once had an adverse impact on regional cooperation and integration.

The idea of joint development of human infrastructure is supported by cost and capacity utilization reasons. The implementation of specific training on the regional level (in such areas as meteorology, air traffic, customs procedures, computer programming, industrial and financial management, medical technology, etc.), may be very costly or impossible to implement by individual member countries. The overall improvement of regional information flows, with special emphasis on activities involving intraregional trade and cooperation (aims and instruments of regional integration, competition rules, bureaucratic

procedures, customs and tax administration, public procurement, evaluation of investment bids in member countries) is expected to contribute to improved intraregional trade and economic relations. Regional trade promotion and information centers, joint fairs and expositions, closer contacts between national industrial and economic chambers and entrepreneurs, and factory visits may also strengthen the commitment of a well-trained and informed group to regional cooperation.

Collective technological development projects, as harmonization of national standards, dissemination amongst group members of new technologies, joint access to technologies developed in third countries offer wide opportunities for regional cooperation. As an example, Argentina and Brazil opted for joint nuclear research activities supported by the International Atomic Energy Agency. Also health related issues (birth control, improving hygienic conditions, immunization campaigns, etc.) may be considered when potential areas of regional cooperation are to be identified.

This ambitious list notwithstanding, regional cooperation in infrastructural development has its obvious limits. Therefore, regional projects have to be analyzed carefully, and their costs and benefits have to be compared with those inherent in a national framework or extraregional cooperation.

Transportation costs grow with geographic distance, and therefore intraregional trade, at least theoretically, may have a cost advantage. However, the cost structure is made up of different components, whose particular costs do not change equally with growing distance. In the area of sea transport, for example, fixed costs (terminal costs) are much higher than freight rates. The smaller the distance, the greater the specific transport costs. Therefore, intraregional trade among island economies (CARICOM, Philippines in ASEAN) does

not have any meaningful transportation cost advantage, even when other conditions for intra- and extraregional trade are the same (although this is unlikely). First, intraregional trade is usually less important than extraregional trade. As a result, the smaller volume of goods traded in the region can easily have higher specific transport costs than higher volumes of goods exported outside the region. Second, cost increasing factors, such as insurance, communication capabilities, quality of related services, delays in customs procedures, connecting transportation facilities, etc., differ widely from country to country. Sometimes there is no national company in the region capable of offering these services comprehensively or guaranteeing competitive quality work. This is due, in part, to the sophisticated character and human and physical capital-intensity of the services provided. Third, the inefficiencies of national (frequently state-owned) monopolies -- which have been protected from international competition for decades, and may still be protected -- may be a substantial cost-increasing factor.

Intraregional transportation cost advantages also depend on the goods traded. In the export of transportation-intensive products (semi-manufactured bulk products, raw materials) intraregional trade may be higher than average. However, similar production and export structures, fundamental differences between export volumes and the size of the regional market, and frequently highly protected national markets may prevent countries from taking full advantage of these potential benefits.

The potential advantages of intraregional infrastructural development may be further diminished by the rapidly growing deregulation of services on the international scale. In particular, extremely costly developments may occur

when regional projects do not take into account the sometimes dramatically decreasing costs of international services (e. g. in telecommunications).

Regional infrastructural development possibilities are further constrained by the huge amount of financial resources that have to be mobilized. For instance, SADCC presented more than 150 infrastructural projects with a total cost of more than US\$ 3bn to be financed by the international community. Resources are generally scarce during the stabilization and adjustment process, and resource reallocation priorities are usually different from financing regional projects. There is an urgent need for finding high-profit investment possibilities with rapid return. This requirement clearly contrasts with the nature of large infrastructural projects that pay off only after a greater period of time has elapsed. This problem calls for substantial international cooperation.

Obviously, regionally developed projects can be less costly than national ones. Yet, this cost advantage, by itself, does not cause intraregional trade to increase unless the member countries' economic and trade policies also create an attractive environment for higher trade flows. The lack of financial and political confidence may also undermine otherwise rational economic decisions. The foreign exchange risk of import-intensive, joint developments is substantial for countries having inconvertible national currencies and facing major or continuous devaluations. Sudden and unpredictable political changes in one or more contracting countries may rearrange economic priorities and may cause some countries' interest in going on with joint projects to lessen or to disappear altogether. Uncertainties are even greater if, as often happens, international laws are not recognized, and thus not applicable, against violators of contracts.

Experience has shown that one of the major obstacles to regional infrastructural development is the uncertainty about the equitable distribution of expected or actual benefits. The main concern is generally not how to distribute financial resources but rather where regional projects will be located. In capital-intensive physical infrastructure projects, the national territory principle may be applied, while most human resource developments have relatively modest capital requirement. This is a highly sensitive issue both in the external and the domestic policy game.

In the foreign policy context, disagreement centers around national prestige considerations (e.g. frustrated efforts to create a regional airline of the Maghreb countries by combining existing national ones). Also, concerns about one-sided dependence may cause countries to hesitate. For example, Country A is contributing to the current expenses of a joint establishment (institution) but it cannot control the general environment in Country B, in which the joint establishment operates. Adverse economic trends or sudden political changes may lead to the disruption of regional activities. (A regional Rice Institute is well functioning in the Philippines and failed in Ibadan, West Africa.) In addition, it is feared that countries having regional institutions may have increased bargaining power against member countries that do not possess such projects. The longer-term and most evident issue is, however, the expected or virtual multiplier effect of the location. Countries or cities being able to attract regional organizations and institutions may have better development prospects. They generally get more foreign capital and resources; the growing and usually well-paid international professional manpower generates higher demand for goods and labor alike, with positive impact on general growth prospects; and host

countries with inconvertible national currency enjoy a growing inflow of convertible assets. In sum, intraregional differences may become more manifest.

Regarding the domestic policy setting, the streamlining of previously inefficient institutions and projects on the national level may produce strong opposition by that part of the national bureaucracy which is in danger of losing its influence and perhaps even its job.

Thus, in some cases, coordination of national infrastructural development may produce less tension. However, this results in underutilized capacities, overlapping activities and, as a consequence, high costs of functioning. Formal regional institutions, as suggested for the CARICOM (Policy Options..., 1990), may offer an in-between solution, at least in areas where sufficient local technical and managerial knowledge has been accumulated (University of West Indies Faculty of Agriculture and the Caribbean Agricultural Research and Development Institute). Gradual harmonization is likely to be achieved by following this path. Certainly, this approach has very little in common with earlier ambitious "prestige" projects, but it prevents huge misallocations of scarce resources and helps strengthen the microeconomic foundations of regional cooperation and international competitiveness.

### C. Joint Activities vis-a-vis Third Countries

The concept of joint, integration level protection of the member countries' economic interests against adverse or changing international economic developments is not a genuine product of RIDC. In the 1970s, more than one attempt was made by differently composed groups of developing countries -- within the framework of a "new world economic order" -- to redistribute or at least regulate the advantages (and disadvantages) produced by international economic

developments. These experiments failed, however, partly because common interest in changes or economic strength required to implement changes remained below the critical mass. Also, quick adjustments and economic policy responses by developed countries, as well as dramatically changing world economic priorities, raised questions about the viability of these efforts.

Trade policy approaches on the regional level were more successful. The unified external economic policy of the EC, after 1975, played a catalytic role. On the one hand, as Brussels started to negotiate trade policy issues as a regional integration, it provided an example to be followed by other regional integrations. On the other hand, the building-up of a pyramid of privileges induced third countries and their groups to try to obtain the best position on the ladder of trade preferences or, at least, to avoid slipping back into non-preferential status.

Group-to-group negotiations were conducted with African countries from as early as the 1960s. After the first enlargement of the EC, the Lomé Convention gathered countries that belonged to various integration schemes in Africa and the Caribbean. Regular meetings made it possible for developing countries belonging to the same integration to get better acquainted with each other's position and interests. As a result, they agreed on a system of limited cooperation that did not bring progress in intraregional affairs but offered trade and other economic advantages vis-a-vis the powerful European Community. Later on, the EC concluded trade agreements with other integrations such as ASEAN, CACM, and the Andean Pact. Most of them did not go beyond providing GSP treatment, but in some cases, by recognizing cumulative (regional) rules of origin and setting regional import quotas for certain products, they improved market access for exporters. Moreover, these agreements called for cooperation

in infrastructure, food aid, export promotion, and protection of foreign investment.

A second, although far less important reason for taking a joint position was political. In 1967, ASEAN was established in order to protect member countries from foreign military threat and stabilize a geographic area that was vitally important for Asian (and global) security. Economic cooperation within the group started only after 1976.

Five of the RIDCs' potential areas of joint external economic activity can be identified:

1. Increasing the bargaining power of a region in international trade negotiations. This includes protection of traditional export markets and products, tariff preferences for the whole region, higher regional export quotas for various sensitive products, and the recognition of regional rules of origin. In a certain sense, this is a specific trade creation function of regional integration, because the negotiated preferential conditions offer some advantages to the members of the group, as compared to other exporters. It is hardly surprising that ASEAN, the integration with the most world economy-oriented countries, exhibits a very dynamic trade diplomacy. It signed trade agreements with six partners, all from the developed world (EC, USA, Japan, Canada, Australia and New Zealand). Clearly, ASEAN's significant bargaining power is first of all due to rapid economic growth, outward-looking economic policies and growing integration into the world economy, and not to closer regional integration.

2. Few experiments have been undertaken to shape common export policies on the regional level. These efforts have focused on protecting the member countries' export markets for similar or identical products. So far, four LAIA countries have agreed to support clothing exports to outside markets, and since 1980, ASEAN's Association of Textile Industries has been formulating common positions on MFA negotiations. Recently, the CACM has formulated plans for promoting regional exports, without specifying, however, its instruments.
3. Regionally coordinated imports of raw materials and other bulk products may offer better purchasing terms (price, after-purchase-services) and shared transportation and insurance costs. However, underdeveloped regional infrastructure, different geographic orientation of the member countries, and relatively small regional demand may substantially limit the volume of potential savings.
4. More recently, common activities emerged in order to attract higher volumes of external financial resources. By 1988, SADCC could ensure external financing for 20 industrial projects, and is now working on getting additional resources for 11 more projects. The ASEAN Fund of US\$5 billion, provided by Japan, is scheduled to finance regional projects in the private sector and in industrial upgrading. The EC also contributes to regional development in ASEAN, although in a very modest way.

5. Modest direct, but probably much more important indirect impacts are expected from actions promoting trade and cooperation among a region's entrepreneurs. These actions may include the creation of regional marketing boards, conferences on industrial cooperation and joint ventures, organization of trade missions and expositions, and establishment of the microeconomic infrastructure of business cooperation (business councils, regional economic and commercial chambers, regional standardization and quality control centers, training and management facilities). More attention is being given to the support of small- and medium-sized private companies. Regional banks may play an important role in financing the institutional framework of regional firm-level cooperation.

It is expected that the common position regarding the external world is going to become a major element of integration-level strategies in the coming years. The emerging Single European Market and the regionalization tendencies of other parts of the world require adequate responses and sometimes even substantial policy changes from developing countries (Basdeo, 1990; Brune, 1990; Rainford, 1990).

Developing countries are likely to face more and qualitatively different challenges coming from the EC in the next years than at any other time since its founding, in 1957. In the early 1960s, imitation of the EC measures was limited to trade liberalization, which, given the RIDCs' markedly different economic environment, usually ended up in failure. At present, the world economy is much more open and deregulated than 30 years ago. Economic interdependence has become an everyday occurrence. Moreover, the creation of the Single Market

has a comprehensive set of goals and instruments that go far beyond trade and also include the free movement of services, capital, and manpower.

In contrast to the 1960s, when different viable options were available, today there is hardly any other reasonable alternative than adjustment to the requirements of the largest market in the world economy. While, in earlier times, economic marginalization of countries and groups of countries was the consequence of self-chosen and failed economic policies, in the 1990s marginalization may be involuntary and imposed by powerful international economic developments. Deregulation and regionalization, as parallel and decisive international processes, are likely to affect all countries that cannot forge stronger economic alliances, not just among themselves but also with one or more of the major centers of world economic and technological growth.

The common position of RIDCs will be challenged in three main areas:

First, the establishment of the single market and the gradual integration of the reforming Central and Eastern European economies into the (Western) European network of economic cooperation substantially modifies Brussels' previously established pyramid of trade and economic preferences. As a result, those regional integrations, whose vital economic interests are likely to be damaged, will engage in joint actions and will do their best to protect their privileges. However, it is unlikely that they will be able to maintain most of their earlier privileges. First of all, African integrations whose member countries participate in the Lomé Convention, as well as CARICOM and Maghreb, may have to face strong challenges as (a) the preferential import regime will be diluted, (b) national import quotas eliminated, (c) competition stiffened, (d) the common agricultural policy transformed, (e) Spain's and Portugal's accession completed, (f) new association treaties with some Central and Eastern

European countries concluded and (g) migration possibilities strictly controlled. In addition, progress on the road to monetary union will send serious shocks to the currency integration of the CFA zone with the likely outcome of ending with the system of fixed exchange rates and perhaps also with the present form of UDEAC or ECOWAS.

The second challenge may have a fundamentally creative impact. The unfolding large and dynamic European market will be developing a number of new opportunities for third countries. For economies of scale reasons, and due to keener competition, most of the potential advantages are likely to be used only if scarce national resources are put together. In this way, the single market is expected to increase regional cooperation in those areas where better extraregional export possibilities are offered or where unified regional services (e. g. tourism) may attract growing demand from Europe. Success in agribusiness or winning bids on the market of public procurement may forcefully push national companies to regional mergers and help create regional multinational firms. The EC's standardization and harmonization of technical, health, and environmental regulations will necessarily force different national rules to be harmonized and adjusted to international standards. This, in turn, is not only a precondition of maintaining traditional or conquering new markets but it may also have a favorable impact on regional harmonization that could not have been achieved through pressure by relatively weak regional lobbies and institutions.

A third factor is that the spread of regional preferential zones with the participation of the major economic powers, exerts an integrative impact on RIDCs. It is clear that the strengthening of regional integration, as a defiant response to regionalization trends in the main export markets, is a blind alley for economically less developed and poorer groups of countries. However, stronger

regional links, as part of continent-wide approaches, may promise more success. As a first reaction to the EC '92 program, the US-Canada free trade agreement and the rapidly changing political and economic environment of intra-European relations, several regional integrations have reconsidered or are now pondering the potential of regional cooperation. Most recently, even the temporary failure of GATT negotiations immediately strengthened this kind of potential policy response. Looking at the Bush initiative, intraregional trade could be substantially accelerated in LAIA. The Maghreb countries recently concluded that unified tariffs on imports should be introduced by 1991 and full customs union by 1995. On the regional level, conditions for attracting more foreign direct capital should also be improved on the regional level.

Some regional groups are planning to link intra-group trade liberalization to strengthening economic links with one or more of the leading economic powers. Maghreb and GCC wish free trade pacts with the EC. The CACM proposed to negotiate a preferential trade agreement, similar to the Lomé Convention, with the EC, and wishes to extend the Caribbean Basin Initiative, launched by the United States, to Central American exports to the US market. There is a growing understanding among Latin American governments that the free trade area that at the moment includes the United States and Canada and is planned to be extended to Mexico, should cover the whole Western Hemisphere. ASEAN member countries are examining the viability of an Asia-Pacific trading bloc. Regional integrations with the most limited internal resources (CARICOM) try to establish relations with larger neighboring groups (LAIA). As a most recent development, Mexico and the member countries of CACM signed an agreement leading to free trade by 1997.

African integration schemes seem to be in the least encouraging position and much of the continent seems to be on the losing side in the unfolding world

of trading blocs. Most member countries of different regional groups are unilaterally dependent on the EC whence strong economic impacts threatening the previously achieved preferential trade advantages are expected to come after 1992. It is a poor consolation that most of the preferences enjoyed in the past by African economies were used relatively inefficiently anyway. At the moment, there are no alternative dynamic partners on the horizon. Thus, it is not surprising that arguments in favor of warming up old and frustrated regional integration schemes have been gaining ground recently (Asante, 1990).

#### IV. Conclusions

Economic integration among developing countries (based on import substitution on the regional level) fell far short of initial expectations. Although at first intraregional trade increased in some trading groups, it remained a rather modest share of total trade, it had a tendency to decline in the 1970s, and stagnated in most of the 1980s. In addition, ambitious plans for joint industrialization could not be implemented.

The reasons for failure were partly predetermined by the heritage of most member countries: small size of the market, low level of economic, industrial and infrastructural development, similar production and export patterns, and different political and economic policy orientation. Additional problems emerged during the implementation of the main objectives. Trade liberalization was blocked or substantially slowed down, highly protective barriers to trade remained untouched or were harmonized on the regional level, and controversy about the distribution of gains and losses could not be settled in a satisfactory way. Dramatic changes in the world economy further affected the environment for regional integration and cooperation. Different countries were affected in

different ways, and each one reacted differently to the situation, and sometimes substantially different national economic policies were produced.

Despite generally negative experiences, new approaches to regional cooperation started to reemerge in recent years. Attempts to revitalize dormant regional groups, to form new blocs and to set partly new priorities are on the increase. Although trade remains the most important element of the new initiatives, fundamental changes have taken place in the assessment of the possibilities and limits of regional integration, as compared with the basic concepts in the 1960s.

Stabilization and adjustment policies have created more open, export-oriented, liberal and competitive economies. Higher exports generated higher growth and regional demand. Industrial restructuring improved competitiveness, attracted international capital and technology, and opened up areas of intra-industrial division of labor. Export-oriented economies proved competitive not only in extraregional but also increasingly in intraregional markets. In most cases, it was not the regional training ground that created international competitiveness, but the successful outward-looking policies that enhanced competitiveness within the region. In addition, the strengthening of the private sector and closer cooperation in infrastructural development (mostly the more efficient utilization of human resources, as identified earlier in this paper) support the shaping of an environment in which new opportunities for enhanced regional trade may be created. Obviously, intraregional trade cannot become an alternative to fundamentally world market-oriented trade flows. However, in the 1990s, intraregional trade and economic relations are likely to grow parallel to, or even at a higher rate than extraregional contacts.

The formation of new, powerful economic and trading blocs, such as the single market of the EC, the US-Canada free trade area, initiatives in the Pacific basin, and the transition to market economies in Central (and perhaps Eastern) Europe, seem to foster trends towards a new regionalism in the world economy. The virtual failure of the GATT negotiations may speed up this development. In order to minimize economic losses and to avoid marginalization, regional groups of developing countries will be increasingly forced to work out common positions and to join one of the influential groups. Both factors require the gradual yet rapid dismantling of barriers to the free flow of production factors within regional integrations.

AnnexList of Major Regional Integrations

|              |  |
|--------------|--|
| Andean Pact  | Bolivia, Colombia, Ecuador, Peru, Venezuela  |
| ASEAN        | Association of South East Asian Nations (Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand)  |
| CACM         | Central American Common Market (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua)   |
| CARICOM      | Caribbean Common Market (Antigua and Barbuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent, Trinidad and Tobago)  |
| EC           | European Communities (Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, United Kingdom)   |
| ECOWAS       | Economic Community of West African States (Benin, Burkina Faso, Cape Verde, Gambia, Ghana, Guinea, Guinea-Bissau, Ivory Coast, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone, Togo)   |
| EFTA         | European Free Trade Association (Austria, Finland, Iceland, Norway, Sweden, Switzerland)   |
| GCC          | Gulf Cooperation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates)  |
| LAIA         | Latin American Integration Association (Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay, Venezuela)  |
| Maghreb Arab | Maghreb Union (Algeria, Libya, Mauritania, Morocco, Tunisia)   |
| SADCC-PTA    | South African Development Coordination Conference (Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia, Zimbabwe) and Preferential Trade Area of Eastern and Southern African States (members of SADCC, minus Angola, plus Burundi, Comoros, Ethiopia, Kenya, Mauritius, Rwanda, Somalia) |

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**Table 1: SELECTED INTEGRATION GROUPS: BASIC INDICATORS  
(1988)**

|                   | Population<br>millions | GNP<br>\$bn | GNP per<br>head<br>\$ | Imports<br>\$bn | Imports<br>per head<br>\$ |
|-------------------|------------------------|-------------|-----------------------|-----------------|---------------------------|
| LAIA              | 368                    | 735.8       | 1999                  | 67.1            | 182                       |
| ASEAN             | 309                    | 227.2       | 735                   | 102.1           | 330                       |
| ECOWAS            | 188                    | 64.7        | 344                   | 11.4 x/         | 62 x/                     |
| SADCC-PTA         | 166                    | 42.6        | 257                   | 11.2            | 67                        |
| Andean Pact       | 90                     | 140.6       | 1562                  | 21.3            | 237                       |
| Maghreb           | 62                     | 109.6       | 1768                  | 22.7            | 366                       |
| CACM              | 25                     | 24.0        | 964                   | 5.7             | 228                       |
| UDEAC             | 23                     | 18.4        | 800                   | 3.4             | 148                       |
| GCC               | 20                     | 150.6       | 7530                  | 38.8            | 1940                      |
| CARICOM           | 6                      | 9.7         | 1617                  | 4.2             | 700                       |
| -----             |                        |             |                       |                 |                           |
| Memorandum items: |                        |             |                       |                 |                           |
| EC                | 325                    | 4401        | 13542                 | 1070            | 3292                      |
| EFTA              | 32                     | 637         | 19906                 | 184             | 5750                      |

x/ 1987

Source: The World Bank, World Development Report 1990; The World Bank Atlas 1989; IMF, International Financial Statistics; IMF, Direction of Trade various issues.

Table 2: SELECTED INTEGRATION GROUPS: INTRAREGIONAL EXPORTS

|                          | Value<br>in 1989<br>(\$ mn) | Share of Intraregional Exports in<br>Total Exports<br>in percent |      |      |      |      |      |      |
|--------------------------|-----------------------------|--|------|------|------|------|------|------|
|                          |                             | 1970   | 1975 | 1980 | 1985 | 1987 | 1988 | 1989 |
| ASEAN                    | 22,648                      | 14.7   | 15.7 | 17.8 | 16.8 | 17.7 | 18.3 | 18.6 |
| LAIA                     | 9,348                       | 10.2   | 13.5 | 13.5 | 8.9  | 10.7 | 10.9 | 9.7  |
| GCC                      | 3,612                       | .  | .    | .    | 4.6  | 5.6  | 5.4  | 5.2  |
| ECOWAS                   | 1,513                       | 2.1  | 3.1  | 3.9  | 4.2  | 5.5  | 7.9  | 7.2  |
| Andean Pact              | 1,157                       | 2.8  | 5.4  | 3.3  | 3.1  | 3.2  | 4.9. | 4.7  |
| CACM                     | 570                         | 26.8   | 23.4 | 22.0 | 15.0 | 11.9 | 11.9 | 12.5 |
| SADCC-PTA <u>x/</u>      | 537                         | .  | .    | 5.1  | 4.7  | 6.7  | 6.0  | 5.5  |
| Maghreb                  | 517                         | .  | .    | .    | .    | 1.5  | 1.8  | 2.1  |
| CARICOM                  | 426                         | 7.8  | 8.3  | 8.7  | 12.0 | 10.5 | 11.1 | 12.9 |
| UDEAC                    | 184                         | 3.4  | 3.9  | 4.1  | 0.7  | 0.9  | 3.9  | 3.9  |
| <u>-----</u>             |                             |  |      |      |      |      |      |      |
| <u>Memorandum items:</u> |                             |  |      |      |      |      |      |      |
| EC                       | 852,600                     | 48.9   | 49.4 | 52.8 | 54.9 | 58.8 | 59.9 | 62.5 |
| EFTA                     | 25,952                      | 28.0   | 18.5 | 14.8 | 13.6 | 14.7 | 14.1 | 13.9 |

x/ excluding intraregional exports by Botswana, Lesotho and Swaziland.

Source: A. Inotai, Regional Integrations in the New World Economic Environment, Akadémiai Kiadó, Budapest, 1986, p. 44; P. Robson, The Economics of International Integration, London: Allen & Unwin, 1987; OECD, Foreign Trade Statistics; IMF, Direction of Trade Statistics. Yearbook 1990

**Table 3: SELECTED INTEGRATION GROUPS: GROWTH RATES OF TOTAL AND INTRAREGIONAL EXPORTS**

|                     | Total exports   |                 |                     | Intraregional exports |                 |                     |
|---------------------|-----------------|-----------------|---------------------|-----------------------|-----------------|---------------------|
|                     | 1987<br>US\$ mn | 1989<br>US\$ mn | index<br>(1987=100) | 1987<br>US\$ mn       | 1989<br>US\$ mn | index<br>(1987=100) |
| ASEAN               | 82,085          | 121,467         | 148.0               | 14,529                | 22,648          | 155.9               |
| LAIA                | 55,107          | 69,188          | 125.6               | 8,595                 | 9,348           | 108.8               |
| GCC                 | 80,327          | 96,371          | 120.0               | 3,086                 | 3,612           | 117.0               |
| ECOWAS              | 16,091          | 20,946          | 130.2               | 885                   | 1,513           | 171.0               |
| Andean Pact         | 21,344          | 24,825          | 116.3               | 683                   | 1,157           | 169.4               |
| CACM                | 4,134           | 4,547           | 110.0               | 492                   | 570             | 115.9               |
| SADCC-PTA <u>x/</u> | 7,609           | 9,784           | 128.6               | 507                   | 537             | 105.9               |
| Maghreb             | 21,367          | 24,164          | 113.1               | 325                   | 517             | 159.1               |
| CARICOM             | 2,810           | 3,302           | 117.5               | 295                   | 426             | 144.4               |
| UDEAC               | 4,222           | 4,675           | 110.7               | 38                    | 184             | 484.2               |
| -----               |                 |                 |                     |                       |                 |                     |
| Memorandum item:    |                 |                 |                     |                       |                 |                     |
| World exports       | 2487,100        | 3026,300        | 121.7               |                       |                 |                     |

x/ excluding intraregional exports by Botswana, Lesotho and Swaziland.

Source: IMF, Direction of Trade. Yearbook 1990; United Nations, Monthly Bulletin of Statistics; The World Bank, World Development Report 1990

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