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ADVANCING REGIONAL INTEGRATION IN SOUTH ASIA

How Has Regional Integration Taken Place in Other Regions? *Lessons for South Asia*

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As the momentum for multilateral trade liberalization has slowed, an increasing amount of liberalization is taking place at a regional level. As of April 2015, there are 406 regional trade agreements (RTAs) in force worldwide, more than double the number in force in 2000.[1] These agreements cover over half of international trade. Countries engage in regional cooperation for a variety of reasons. First, it is easier to achieve agreement among a small number of regional partners than it is globally. Second, regional cooperation takes advantage of existing natural tendencies for regional trade that arise from geography and shared culture. This reinforces the regional division of labor already taking place among firms. Global value chains, in which lead firms organize a division of labor for complex products among many countries, often turn out to have a regional focus. Think, for example, of the electronics value chain in East Asia, and the automotive value chains focused on the United States, Germany, and Japan. South Asia itself is a small but growing part of value chains in textiles and apparel with both regional depth and cross-linkages to East Asia.

More importantly, it is possible for regional agreements to go deeper than the more general standards applied by the World Trade Organization. The types of issues covered in such agreements often go beyond the traditional topics of tariffs and quantitative restrictions, and cover provisions related to trade facilitation, non-tariff measures (NTMs), and investment. Practical forms of inter-regional cooperation, such as in energy, may arise because of natural linkages among geographic power networks. These may be taken up in separate institutional structures that sit parallel to traditional trade agreements.

Regional cooperation has taken hold among countries at a variety of levels of development. There are regional agreements primarily among high-income countries (e.g. the European Union) and linking countries at different stages of development (e.g. North American Free Trade Agreement and the proposed Trans-Pacific Partnership). Increasingly, there are south-south regional agreements such as Association of Southeast Asian Nations (ASEAN) in Southeast Asia, Southern Common Market (Mercosur) in South America, Common Market for Eastern and Southern Africa (COMESA), Economic Community of West African States (ECOWAS) and Southern African Development Community (SADC) in sub-Saharan Africa. Each of these agreements has its own features, allowing for countries to develop closer ties in a manner suitable for regional conditions.

This piece will focus on four aspects of trade liberalization (trade facilitation, non-tariff measures/barriers, intra-regional investment, and energy cooperation) that go beyond traditional preferential tariff reduction to illustrate both the potential of south-south liberalization and some of the particular challenges faced by South Asia. There is widespread agreement that deeper regional engagement in these areas will benefit the people of South Asia.

Trade Facilitation

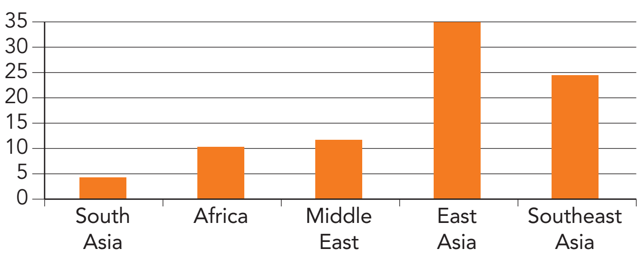
As tariffs are reduced, it is becoming increasingly apparent that the main costs involved in trading arise from problems with moving goods around—getting goods from the factory or farm via a road to the port, across the ocean, through the port again, down the road in the importing country, and through the wholesale and retail network. It is estimated that even for high-income countries, the price of goods at the importing country's retail level averages 170 percent higher than the price received at the factory or the farm in the exporting country.[2] Worldwide, reducing trade costs associated with border administration, transport and communication infrastructure even halfway to global best practice would lead to an additional $2.6 trillion in global GDP (4.7 percent).[3]

On a percentage basis, the potential gains to trade facilitation in South and Central Asia, at 8 percent of GDP, are almost twice as large as the global average.[4] Challenging issues such as the difficult border procedures between India and Pakistan, the equally challenging land transport environment between Bangladesh and India, and the landlocked status of Afghanistan, Bhutan and Nepal imply that much can be done to reduce trade costs. Average level of trade costs between country pairs in South Asia is 85 percent higher than between country pairs in East Asia.[5] High trade costs have contributed to South Asia being the least integrated region in the world (Figure 1). [6]

ASEAN is a good example of a south-south agreement where regional cooperation has enhanced trade facilitation, reduced trade costs and enhanced intra-regional trade. In ASEAN, most countries have established either Trade Information Portals or Single Windows. A Trade Information Portal allows traders to electronically access all the documents they need to obtain approvals from the multiple units of government involved in exporting and importing. A Single Window also allows for electronic submission of such documents. These windows, which are national initiatives, are linked in the ASEAN Single Window (ASW), which allows compatibility of national windows using international open communication standards. This facilitates trade both within the region and with other countries using similar standards. The ASW supports a unified ASEAN Customs Declaration Document and exchange of the intra-ASEAN certificate of origin. In the area of trucking, three ASEAN countries (Malaysia, Singapore and Thailand) are piloting the ASEAN Customs Transit System as of November 2014.

Trade facilitation can apply to trade in services as well as goods. In the case of services, one barrier to trade involves the movement of national persons—accountants, engineers and consultants who may move from one country to another on a temporary basis to offer a wide range of business services that can enhance development in manufacturing, mining and agriculture. In Mercosur, the Residence Agreement, which was implemented in 2009 among full and associate members, allows workers to reside and work for up to two years in a host state.[7] This residence permit can be extended to a permanent one if the person proves that they can support themselves and their family through work. While there are some national differences in implementation of the Residence Agreement, it represents a major step in facilitating trade in those kinds of services that require personal presence to deliver most effectively.

FIGURE 1: Intra-regional trade share (percent of total trade), 2012



Source: Authors' calculations based on WITS (World Bank Group) data.

Non-Tariff Measures (NTM)/Barriers

Countries impose a wide range of NTMs affecting international trade.[8] Some of these are relatively heavy-handed measures prohibiting trade in certain categories of goods, or requiring a non-automatic license to be allowed to import. Other measures have the stated intent of promoting human, animal, or plant life and health, or workplace and product safety. These include sanitary and phytosanitary standards (SPS) and technical barriers to trade (TBT). While such measures may pursue legitimate national policies, they can be designed in such a way as to be more trade-restrictive than necessary or to constitute a disguised barrier to trade. In most but not all cases, an NTM becomes a non-tariff barrier (NTB) to the extent that the measure applies only to imports and is not imposed on domestic production.

To reduce the incidence of NTBs, NTMs need to be streamlined. This requires initiatives to (1) identify the existing stock of NTMs; (2) identify those policies of most concern to traders; and (3) where possible, streamline the most problematic measures so they can achieve their regulatory ends.

Within ASEAN, there is a commitment by all members to document their NTMs using an internationally recognized classification scheme developed by UNCTAD. ASEAN members have also formed intra-governmental committees to identify the most problematic NTMs and select candidates for streamlining or removal. The World Bank Group has been heavily engaged in this work. Separately, ASEAN has also harmonized regulatory regimes for electrical and electronic equipment, going substantially deeper than the zero-tariff commitments in the Information Technology Agreement, and has also implemented a Cosmetics Directive.

Among the African Economic Communities (COMESA, EAC, SADC) there is an online Mechanism for Reporting, Monitoring and Eliminating NTBs (http://www.tradebarriers.org). This type of mechanism for collecting complaints can be very effective, helping to resolve disputes in a transparent and multi-country setting, thereby also contributing to building trust between trading partners. So far, the Mechanism has addressed nearly 500 cases, of which more than 80 percent have been resolved, according to the website.[9] Traders may address a wide variety of complaints, including rules of origin, customs clearance and border procedures.

Some ways to reduce trade frictions arising from NTBs are harmonization of regional standards and mutual recognition of standards (countries allow imports on an agreement that the other country's standards provide for the same degree of safety or protection, but the details can differ on a national basis). Mercosur has established guidelines for recognition of equivalence in food control systems, and designed harmonization of regulations in telecom technologies, and is moving forward with a protocol on harmonization of industrial design standards.

Intra-Regional Investment

A high share of international trade—as much as 80 percent by some estimates—is associated with direct investment, either because firms engaged in foreign direct investment (FDI) are also large traders or because such firms engage in trade in their own intra-firm networks. Thus, promoting intra-regional investment is an important tool for promoting intra-regional trade. In addition, maintaining policies that are attractive to FDI are now widely understood as important for attracting current technology and capital. As a result, many RTAs now include investment provisions. Such agreements aim at insuring non-discrimination between domestic and foreign investors, limiting such requirements on foreign investment as domestic content and hiring provisions and restrictions on repatriation of assets or profits, and providing for some type of dispute resolution mechanism between investors and states.

An example of such provisions is the ASEAN Comprehensive Investment Agreement (ACIA), which entered into force in 2012.[10] This agreement protects investments made by non-ASEAN parties in ASEAN countries. These parties are guaranteed fair and equitable treatment, and ASEAN governments agree not to make arbitrary decisions and to enforce their own laws. Foreign investors are also protected against unlawful expropriation, and to the extent feasible, extended security in the event of civil unrest. Free transfer of funds into and out of ASEAN are also guaranteed to foreign investors.[11] The role of investment in ASEAN's economic development has grown substantially in recent years. In this context, intra-regional investment, which currently stands at 17.4 percent, has played a central role.[12] The ASEAN experience also suggests that in order to take full advantage of a regional investment framework, each South Asian Association for Regional Cooperation (SAARC) member would have to undertake reforms to improve its respective investment climate.

FIGURE 2: SIEPAC regional transmission line connects six countries

Source: Global Energy Network Institute (GENI)[16]

Energy Cooperation

National geography often affords opportunity for regional cooperation in power generation and transmission. In Central America, the Central American Electrical Interconnection System (SIEPAC) is fully operational as of 2013, and interconnects the grids of six Central American nations over 1,790 km of 230 kV transmission lines extending from Guatemala to Panama (Figure 2). SIEPAC was financed by a variety of sources led by the Inter-American Development Bank, and is owned by a regional operations entity with public-private ownership (75 percent from integrated utilities and transmission companies, and 25 percent from Spanish and Colombian power companies).[13] SIEPAC is expected to lower rates throughout the region and has been credited with helping Panama to recover from an energy crisis that had arisen due to drought-depleted reservoirs. Similar geographical circumstances afford opportunities for energy cooperation in the South Asian region, where sharp differences in elevations make for untapped hydropower resources.

Countries in the Greater Mekong Sub-region (GMS) have been successful in trading power since 1971. This exchange intensified in the 1990s with the formal launch in 1992 of the GMS Economic Cooperation Program. These countries have overcome possible issues relating to size asymmetries of the countries involved. Initial years of the GMS Program focused on networking, studies, and building trust. The GMS is now in the process of transitioning from bilateral power purchase agreements to grid-to-grid trading between bilateral pairs of countries.[14] [15]

Implementation

Regional agreements suffer from a gap between intentions and implementation. One way to address this would be to set up credible institutional mechanisms to monitor compliance and outcomes, housed in regional secretariats such as COMESA, or, in the case of South Asia, SAARC.

The other lesson is that regional integration is a long and incremental process. Improved regional outcomes, such as higher trade volumes, price convergence, reduction in border crossing times, or increase in energy trade, take time and patience, and require political will and institution building. South Asia can capitalize on recent political momentum in the region and keep pushing on issues that have a strong developmental impact—energy sharing, reducing costs of trade, and encouraging intra-regional investment.

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Endnotes

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4. Calculated from ESCAP-World Bank International Trade Costs Database
5. Simple average of trade costs between available bilateral pairs. Figure based on authors' calculations using the ESCAP/World Bank International Trade Costs database.
6. This is true in the aggregate, but it does obscure the fact that for countries like Afghanistan, Nepal and Bhutan, intra-South Asian trade dominates their overall trade.
7. Arcarazo, D.A. (2014), 'Is free movement in Europe an anomaly? The new open borders policy in South America', web blog post. PolicyBristol Hub, November 25.
8. An NTM is any measure other than an ordinary customs tariff which applies to imports or exports. Identifying an NTM as an NTB implies that the measure in question is needlessly restrictive, unfair, or violates some agreed norm. It is easier to catalogue NTMs than to identify NTBs.
9. Not all cases are resolved to full satisfaction, but the important point is that there is a multi-country forum for reporting, monitoring and resolution.
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