GLOBAL REALIGNMENT: THE NEW WORLD ECONOMIC ORDER

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Candidate's Certificate

I certify that the thesis entitled 'Global Realignment: The New World Economic Order' and submitted for the degree of Master of Business Studies in International Business is the result of my own research, except where otherwise acknowledged, and that this thesis (or any part of the same) has not been submitted for higher degree to any other university or institution.

Signed..

Date.........21/8/96...

Contents

PART II: ANALYSIS -THE TRIPOLAR GLOBAL REALIGNMENT

PART III: CONCLUSION

FIGURES

TABLES

DEDICATION

I dedicate this thesis to my *Martha, Pitha, Guru and Devo* (to my mother, to my father, to my teacher and to my God)

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ABSTRACT

The purpose of this thesis is to describe the current state of the global environment in the study of international business. The thesis explains the shift in the economic forces away from multilateral arrangements to regional groupings. In particular the shift is towards regionalism, 'seen' as a medium measure, before 'globalism'. The study takes the view that the world is moving towards a tripolar global economic focus namely the European Union, the North American Free Trade Area and the Asia Pacific Economic Cooperation. The focus in the latter is on the development of the East Asian economies.

The research was developed on the assumption that the concept of competition is changing from rivalry to collaboration and from independence to interdependence. This is true for nations as well as corporations. The research also attempts to describe the forces of change and the impact of change factors such as technology and information systems on the nature of competition.

This research covers new developments in the study of the environments of international business. APEC and NAFTA are new institutions which have developed since 1989, and the European Union, whose history goes back to 1948, has in 1992 created a single Europe. These new developments require conceptualisation, academic focus and to be directed towards the teaching of international business. This research, its is hoped, does just that.

Acronyms and Glossary

- **AFTA (ASEAN Free Trade Agreement).** Formed in 1992 to create free trade between members of ASEAN. Its objectives are to reduce intra ASEAN trade tariffs to below 5% by 2003. AFTA's creation was the result of ASEAN concerns about the impact of APEC.
- **Andean Pact**. A regional trade agreement. The members are Bolivia, Columbia, Peru, and Venezuela.
- **Anti-Dumping Clauses**. Clauses preventing goods imported at prices below the cost of production, or below the selling price in the country of export.
- **APEC (Asia Pacific Economic Cooperation).** A political forum to encourage free trade in the Asia Pacific and beyond. Formed in 1989, it has 18 members including USA, Japan and China. Its objective is to have fully open trade between members by 2020.
- **ARF (ASEAN Regional Forum).** Formed in 1994 to promote regional security and to act as a forum to peacefully resolve disputes within the ASEAN region.
- **ASEAN (Association of South East Asian Nations).** Formed in 1967 by five South East Asian nations: Philippines, Thailand, Malaysia and Singapore. Brunei Darussalam joined in 1984. It was formed in response to regional security concerns and aims to promote regional cooperation on a wide range of issues.
- **ASEM (Asia-Europe Summit**). This was an exploratory meeting between Asian countries and the European Union. It was held in Bangkok in February/March 1996 and represented by the seven ASEAN countries, Japan, South Korea and China, and member countries of the European Union.

- **Asia Pacific Region.** Encompasses the countries that borders the Pacific Ocean. This includes countries in East and South East Asia, the Indian subcontinent, Australasia (Australia, New Zealand and Papua New Guinea), North America, Mexico and countries on the west coast of South America.
- **Asian Tigers**. A reference to the rapidly growing and newly industrialised countries of South Korea, Taiwan, Hong Kong, Singapore and Malaysia.
- **BENELUX**. Formed in 1948 as a customs union. Its members are Belgium, the Netherlands and Luxembourg.
- **Bilateral Trade Agreements**. An agreement between two countries to trade with each other on mutually acceptable terms.
- **Bretton Woods**. A generic reference to the agreements reached at the United Nations Monetary and Financial Conference held at Bretton Woods, New Hampshire in 1947. The conference agreed among other things on a new regime for international currency based on the convertibility of the US dollars for gold. The gold system collapsed in 1971. The Conference resulted in the creation of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD).
- **CAEU**. A regional trade bloc. Its members are Guatemala, Honduras, El Salvador, Nicaragua, Costa Rica and Panama.
- **CAP (Common Agricultural Policy).** The CAP was adopted in 1960. It has been a controversial element of European economic policy. The focus of the policy when formulated was to build agricultural self sufficiency and preserve European farming. The CAP is in fact best known for the subsidies that have been provided to support European agriculture. The key elements of the CAP are: a single market, community preference (protectionism) and joint financial responsibility.
- **Caricom (Caribbean Community).** Established in 1973 with the purpose of achieving a Caribbean common market. Its members are Antigua, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montseratt, St Kitts-Nevis, Anguilla, St Lucia, St Vincent & Grenadines, Trinidad and Tobago.

- **CER (Australia and New Zealand Closer Economic Relations)**. Created in 1983 to encourage closer economic ties between Australia and New Zealand. Trade between Australia and New Zealand was fully liberalised in 1990. This treaty superseded the New Zealand Australia Free Trade Agreement signed in 1965.
- **CIS (Commonwealth of Independent States).** Reconstitution of some of the former USSR states after the collapse of the USSR in 1992.
- **Comparative Advantage**. An economic concept first expounded by David Ricardo states that in international trade if each country specialises in the products in which it has a comparative advantage, the possible levels of consumption will increase in each country.
- **Council of Ministers (of the EU).** The legislative arm of the EU. Each state has a delegate who specialises in a certain area and each member is allocated a certain number of votes. Certain decisions require unanimous votes.
- **Canada-US FTA (Canada-US Free Trade Agreement).** A free trade area between Canada and the US established in 1989.
- **Dumping in economic terms** refers to the practice of flooding a market with a good, e.g., butter, to get rid of a stockpile. If this is done by another nation, for example flooding the French market with cheap New Zealand butter, then the potential is there to damage the local domestic butter industry severely.
- **EAEC (East Asian Economic Caucus).** A grouping of East Asian nations located within APEC. This is a forum whose purpose is to discuss issues peculiar to East Asia. This was initiated in 1992 by Dato Dr Mahathir Mohamad, Prime Minister of Malaysia.
- **EAEG (East Asian Economic Grouping).** This was initially proposed by Dato Dr Mahathir Mohamad, Prime Minister of Malaysia, as a trade bloc for East Asia. Due to opposition from the West, especially the US, the proposal was altered to the EAEC and a forum for East Asian nations within APEC.
- **East Asia**. Encompasses China, Hong Kong, South Korea, Taiwan, Vietnam, Cambodia, Laos and the ASEAN.

- **EC (European Community).** Established in 1967 by the merging of three European organisations, the EEC, ECSC and EURAATOM, primarily as a result of the achievement of the initial objectives of the EEC. The EC was superseded by the EU in 1993. The period was notable for expansion of membership (particularly Great Britain in 1973), the establishment of the European Monetary System (EMS) in 1989, and further efforts to establish a single European market (Single European Act approved in 1987).
- **Economic sanctions** are retaliatory instruments imposed on nations to bring them into line with the 'normal' practices of the international economy. For example, economic sanctions were imposed by the United Nations on South Africa to force the country to repeal apartheid laws.
- **ECSC (European Coal and Steel Community).** Established in 1951 by six European nations for the purpose of cooperation and regulation of the members' coal and steel industries. ECSC represented one of the first attempts at European cooperation.
- **ECU (European Currency Unit).** Devised in 1978 the ECU is a notional currency used as a reference value for various purposes. The ECU is a basket of member currencies based on their economic size. The proportions utilised are reviewed every five years.
- **EDF (European Development Fund).** An EU organ used to assist external developing nations.
- **EEA (European Economic Area).** EEA Treaty came into effect in 1993 to help to the EFTA countries gain access to the EU.
- **EEC (European Economic Community).** Often referred to as the Common Market, the EEC was established in 1957 following the signing of the Treaty of Rome. At establishment its members were West Germany, France, Italy, and the Benelux countries (Belgium, the Netherlands and Luxembourg). The objective of the EEC was to remove trade barriers between members. The EEC was superseded by the establishment of the European Community (EC) in 1967.

- **EFTA (European Free Trade Association).** Established in 1960 at the initiative of the United Kingdom. It established a free trade area between Denmark, Norway, Sweden, Switzerland, Austria and Portugal. On admission to the European Union most members withdrew from EFTA.
- **EMCF (European Monetary Cooperation Fund).** Established in 1973 to provide short term funding to members to support the pegged exchange rate system. Its functions have been taken over by the European Monetary Institute (EMI).
- **EMI (European Monetary Institute).** The EMI has taken over the functions of the European Monetary Cooperation Fund (EMCF) and its purpose is to co-ordinate policies to achieve price stability. The EMI is charged with undertaking the technical preparations for the European Monetary Union (EMU).
- **EMS (European Monetary system).** The EMS started in 1979 and is an exchange rate mechanism to provide more or less fixed parity between the various currencies operating within the EU.
- **EPG (Eminent Persons Group).** Set up by APEC as an advisory body to suggest directions for APEC, this group is made up of highly respected personages. This group does not have structure and it is not necessary for APEC to accept any proposal it puts forward.
- **ERDF (European Regional Development Fund).** The fund is intended to address the main regional economic imbalances between various EU regions.
- **ERM (Exchange Rate Mechanism).** A set of procedures established by the EC in 1979 to improve currency management within the EC and to provide more certainty amongst members regarding exchange rates. The system links all participating currencies with each other and restricts day-to-day movements within specified ranges.
- **ESCB (European System of Central Banks).** An EU organ designed to take centralised and collective decisions on the supply of money, credit and exchange rate levels.

- **EU (European Union).** Established in 1993 when the Treaty of European Union (or Maastricht Treaty) was ratified by the 12 members of the EC. The EU represented a further phase in the goal of achieving European integration. The EU created amongst other things, a political structure that is able to override national interests, a commitment to a timetable for establishing a common currency and monetary policy, European citizenship, the aim of a common foreign and security policy, and a social charter on human rights.
- **EU Commission**. The executive arm of the EU which, in conjunction with the European Parliament, administers the EU.
- **EURATOM (European Atomic Energy Commission).** Formed in 1957 as a result of the Treaty of Rome. Designed to create cooperation in the production of atomic energy. It has proved to be of little significance as national governments preferred to keep control of nuclear energy activities.
- **Euro MPs**. Members of the European Parliament who since 1979 have been directly elected by the citizens of member states. The Parliament contains 624 Euro MPs allocated according to the population of each member state.
- **European Circles**. A proposal by the French and the Germans, similar to European Clubs, expresses the frustration of member states at the proposals for a 'single Europe'. The European Circles proposal divides Europe into five circles or membership categories. For example the inner circle or circle one, would be full membership and hence fully integrated, and circle five might be some sort of associate membership.
- **European Clubs**. A counter proposal to the European Circles by the British. This allows member nations to participate only in those components of the EU that were acceptable to them.
- **European Council**. The meeting of the heads of government of member states, usually held every six months.
- **Europol (European Central Criminal Investigation Office**). This is Europe's integrated police service introduced in 1992.
- **FDI.** Foreign Direct Investment.

- **FTA (Free Trade Area).** An agreement between countries to remove trade barriers to facilitate trading among member countries while retaining the barrier of each individual member on trade with non-member countries.
- **FRG (Federal Republic of Germany).** Formed in 1945 from the part of Germany that was occupied by the Allied Forces. FRG reunited with East Germany (German Democratic Republic) in 1990 to form Germany.
- **G3.** A regional trade arrangement involving Columbia, Venezuela and Mexico.
- **G7 (Group of 7).** These are industrialised economies of Japan, the USA, UK, France, Germany, Italy and the Netherlands.
- **GAL (General Agreement on Labour**). This was introduced in the GATT Uruguay Round in 1994.
- **GATS (General Agreement on Trade in Services**). This was introduced in the GATT Uruguay Round in 1994.
- **GATT (General Agreement on Tariffs and Trade).** The GATT agreement was reached by 23 non communist nations at the Geneva Trade Conference in 1947. Its purpose was to encourage free trade. Trade negotiations or 'rounds' formed the basis of GATT operation and there were eight rounds in total. The three most important rounds were the Kennedy Round, Tokyo Round and the Uruguay Round. GATT was superseded by the World Trade Organisation (WTO) at the termination of the Uruguay Round in 1994.
- **GDP (gross domestic product).** The monetary value of all goods and services produced by factors of production located within a nation. GDP is generally preferred over GNP (gross national product) as an economic indicator.
- **GDR (German Democratic Republic).** More commonly known as communist East Germany, formed in 1945 as a result of the partition of Germany following World War II . In 1990 East Germany was reunified with West Germany.
- **Glasnost.** Russian for restructuring. A political catch phrase created by Mikhail Gorbachev, General Secretary of the USSR Communist Party from 1985 until close to the end of the disbandment of the USSR in 1991. Glasnost,

returned to the country of origin (usually the US). American Spanish terminology which originally referred to the practice of millers keeping a portion of milled grain in settlement of millers' fees.

- **Marshall Plan.** The plan named after the US Secretary of State, G.C. Marshall (1947-1949), involved massive aid (US$13 billion) for the reconstruction of Europe after World War II. The programme began in 1947 and ended in 1952. The aid was in part humanitarian, but was also a key plank in the Truman Doctrine, the aim of which was to contain the expansion of the USSR influence in Europe.
- **Mercosur (Southern Common Market**). A regional trade agreement established in 1991 involving Brazil, Argentina, Paraguay and Uruguay.
- **MFN (Most Favoured Nation).** A key foundation stone on which GATT was built, namely that the member nations must extend to each other tariff treatment as favourable as that extended to anyone else.
- **Multilateral trade agreements**. Trade agreements between more than two nations for the supply of a variety of goods and services amongst each other.
- **NAFTA (North American Free Trade Area).** A free trade bloc formed in 1994. Its members are the US, Canada and Mexico. Chile is currently seeking membership. NAFTA is widely seen as a device for the US to protect its trade interests. Along with Japan, Canada and Mexico are the US's largest trading partner.
- **NAFTAmath.** This term is used to refer to the concept of an expanded NAFTA encompassing both North and South America.
- **NATO (North Atlantic Treaty Organisation).** A regional collective security arrangement focused on Western Europe. NATO was formed in 1949 in part as a response to the USSR's blockade of Berlin. The treaty is still in place today. NATO was a key plank in the Truman Doctrine of seeking containment of the expansion of the USSR influence.

- **NICs (Newly industrialised countries).** Industrialising countries with a GDP per capita in excess of US$2000 and below that of the developed country status (US$10000).
- **OECD (Organisation for Economic Cooperation and Development).** Formed in 1961 to promote economic development and open trade. Has 24 members who are all industrialised countries.
- **OPEC (Organisation of Petroleum Exporting Countries).** Formed in 1960 to co-ordinate crude oil production and cooperate on issues of mutual concern. Has 12 members representing most of the major oil producers.
- **Open Regionalism**. The concept introduced by APEC whereby the members of the group extend the benefits enjoyed by the members to non-members provided trading rules are reciprocated.
- **OPTAD (Organisation for Pacific Trade and Development).** A 1967 OECD-like proposal for the Pacific.
- **PAFTA (Pacific Free Trade Area).** A free trade area proposal first made by Japanese Professor Kojima in 1966.
- **PBEC (Pacific Basin Economic Council).** A business person's group which began in 1967 and holds conferences on regional economic issues.
- **PECC (Pacific Economic Cooperation Conference).** A forum formed in 1980 of academics, businessmen and government officials acting in a private capacity to promote open and free trade. Associated with APEC.
- **Perestroika.** Russian for openness. Similar to Glasnost (restructuring), this was a catch phrase introduced by General Secretary Mikhail Gorbachev to re-energise the ailing economic outlook in the USSR.
- **PPP (Purchasing Power Parity).** A way of defining an exchange rate. This theory originated in the 19th century, and was used to discuss the correct value of currencies in relation to gold. In general terms, it states that equilibrium exchange rates will allow people to buy the same amount of goods in any country for a given amount of money. In other words the PPP would allow a shopper to buy the same basket of goods for the same price in a reference,

usually the US dollar. Although the architects of PPPs say they should not be used as the sole measure of a currency's value, it does indicate trends and relative values.

- **PRICS**. A classification to describe the industrialised countries of the Pacific rim region.
- **Reganism.** The right wing political philosophies espoused by US President Ronald Regan.
- **Regional Trade agreements**. Terms of trade drawn up between a number of nations that occupy a similar geographic region and obtain collective benefit by trading together.
- **Renminbi.** Unit of currency used in mainland China (PRC).
- **SEA (Single European Act - 1987).** Enacted to speed the EC's progress to economic integration. It attempted to speed up the EC's decision-making, gave greater power to the European Parliament, and committed the members to a range of common policies and practices on such things as taxes, health and employment and reinforced the EMS.
- **SEM (Single European Market).** A proposal in 1985 to achieve a single common market with free movement of goods, services, people and capital.
- **Social democracy**. A term used to reflect socialist policies implemented within a democratic process. A much abused term which means different things to different people.
- **South East Asia**. Encompasses the ASEAN (Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand), Burma, Cambodia, Indonesia, Laos and Vietnam.
- **SPARTECA (South Pacific Trade and Economic Cooperation Agreement).** A forum established in 1983 linking countries of the South Pacific, including Australia and New Zealand.
- **Subsidies.** A payment made usually by the government to producers of goods and services to keep the price down or encourage production.

- **Tariffs.** A customs levy (tax) paid on the value of goods imported or exported. There are two types of tariffs which may be imposed. Protective tariff are designed to insulate domestic producers from foreign competition; revenue tariffs are placed on both exports and imports as a means of raising revenue for the government. Revenue tariffs are used extensively by developing countries.
- **Tariff Quota**. A limit on the quantity of goods that may be imported at a given rate of duty.
- **Thatcherism.** A reference to the right wing economic policies espoused by Margaret Thatcher, the first women Prime Minister of Great Britain (1979-1990).
- **The Court of Auditors** (EU). Established to monitor the EU's financial activities.
- **The Court of Justice** (EU). Established to ensure that European treaties are implemented in accordance with EU law.
- **Third world nations**. Originally coined to refer to those nations not directly aligned with the two post World war II super powers, the US and the USSR. The term has been loosely used to refer to all less developed countries (LDCs).
- **Treaty of Rome**. Signed in 1957, the treaty resulted in the formation of the European Economic Community (EEC) and the European Atomic Community (EURATOM).
- **Treaty of Versailles**. The Treaty was signed by Germany and the Allies at the end of World War I at Versailles (near Paris) in 1919. The Treaty detailed the terms of the German surrender and resulted in the creation of the League of Nations which was charged with supervising the implementation of the Treaty.
- **Truman Doctrine**. The Doctrine named after the US President Harry Truman (1945-1953) was a foreign policy strategy to prevent the feared expansion of the USSR communist power. The Marshall Plan and NATO were significant manifestations of this doctrine.
- **UNCTAD (United Nations Conference on Trade Aid and Development).** The first conference was held in 1964. UNCTAD's goal was to act as a

comprehensive forum for dealing with trade and aid issues focused on economic development in the developing nations.

- **United Nations**. The successor to the League of Nations. Formed in 1945 its goals amongst other things were to maintain peace and security and encourage respect for human rights. Membership at formation was 50 nations, today membership exceeds 180 nations.
- **Uruguay Round.** A reference to the last major GATT trade negotiation which started in 1986 and completed in 1994.
- **USSR (Union of Soviet Socialist Republics).** Formed in 1917 as a result of the Russian Revolution which ended Czarist rule. The nation was characterised by the complete domination of the Communist Part over all walks of life. Under the Warsaw Pact, the USSR controlled Eastern Europe for the bulk of its existence. The USSR collapsed in 1991 under the weight of its doctrinaire social and economic policies. The USSR constituted of 15 republics. Eleven of these are now the reconstituted Commonwealth of Independent States (CIS).
- **Value chain**. The process of economic value added at each step in the economic process.
- **Vienna Congress**. A European conference (congress) in 1814 to re-establish the political divisions of Europe at the end of the Napoleonic Wars following the defeat of Napoleon.
- **Visegrad Three** (now four). The EEC negotiated cooperation arrangements with Czechoslovakia (now Czech Republic and Slovakia), Hungary and Poland. These countries came to be known as the Visegrad countries in reference to the place where the discussions took place.
- **Warsaw Pact.** A communist military alliance established in 1955 in response to the formation of NATO. The Pact was signed in Warsaw by the USSR and its Eastern European satellites. This Pact was dissolved in 1991.
- **Werner Plan**. Named after the then Luxembourg Prime Minister the Plan was floated in 1970, and proposed fixed and unchangeable exchange rates between the currencies of Europe.

- **Western Europe**. The nations of EU and EFTA.
- **World Bank**. Also known as the International Bank for Reconstruction and Development. Established by the UN in 1944 as a result of the Bretton Woods Conference. The Bank operates as a development fund provider to member nations.
- **WTO (World Trade Organisation).** The WTO superseded GATT from 1 January 1995. The WTO was established at the end of the Uruguay Round, and takes on all the functions of GATT and has expanded responsibilities in such areas as trade disputes. It has an autonomous structure and will be able to develop new policies and ideas.
- **WWC (World Wide Companies).** Companies that are global in nature such as Coca Cola, McDonalds and Levi.
- **Yaounde Convention**. Created in 1963 the Convention was an agreement between the EEC and 18 African countries which established reciprocal trading rights.

PART I

THEORETICAL FOUNDATIONS AND CONCEPTS

In Part I, the meaning of global realignment and the factors contributing to this 'global phenomenon' are discussed. The term is used to illustrate the economic manoeuvring currently occurring throughout the world and gaining increased momentum following political upheavals over the last decade that have seen a major shift in the balance and focus of power from one of militaristic strength to that of economic strength. As a result of this restructuring a fundamental paradigm shift in terms of political thinking and policy making has taken place which has seen 'cooperation', and 'interdependence' replace 'competition' and 'independence'. A new era has been heralded that demands a new type of politician and a new type of politics. One in which the needs of a country are balanced with the needs of the region, and where national sovereignty gives way to regional growth.

The term global realignment, may be extrapolated to represent a move towards' 'internationalism' or 'globalism' where the concept of national dependence gives way to regional interdependence inevitably leading to global interdependence.

In Part I we also look at factors such as the spread of democracy, the demise of communism as a national philosophy, achievements in technology and processes, and the emergence of new markets, especially in the newly industrialised countries, as contributing to global realignment.

Chapter 1
Global Realignment

The world trading environment is altering rapidly. Essentially we are in the midst of a worldwide economic revolution, occurring against a backdrop of poor economic growth in the industrialised countries.

This worldwide economic revolution is bringing about many structural changes that have required significant shifts by all the key players in the world economy. For example, infrastructure improvements in transportation and communications have facilitated increased integration of individual economies, particularly through greater trade and foreign investment.

This chapter will present the features of this current phase of world economic activity, and will show some of the emerging trends that are shaping the future of world trade, as well as some of the global events that have either contributed to, or resulted from, these trends.

INTRODUCTION

Since the demise of the colonial powers, the global economy has been in turmoil. The economic power base has shifted from Europe to the US, and more recently to Japan, and the Asian region in general (Adler et al, 1986). Consequently, new trade alliances are being formed as nations cope with the power shift. This chapter discusses the formation of these alliances and their effects on trade in an increasingly global economy.

Indications are that we are witnessing the emergence of a new world order. The destruction of the Berlin wall, the collapse of Soviet communism, and the rapid emergence of East Asia as an economic power are indications of both the decay of old orders and the development of a new global environment. The world is currently witnessing the shifting of alliances and agreements and the formation and dismantling of enmities among world powers.

Within this changing political environment, world trade has expanded, led mostly by corporations that have responded to the challenge of an ever decreasing world 'size'. As these corporations have expanded their activities beyond an increasing number of national boundaries, the forms they are taking have given rise to the coining of such terms as 'transnational', 'global' and 'worldwide companies'.

With increasing awareness of the interdependence of national economies, governments are consistently looking beyond their boundaries to control further the process of trade liberalisation that is being driven by the true 'global' corporations. The formation of regional trade agreements and the laboured victories of the GATT rounds are the obvious results of this political activity.

What is of current significance is the potential contradiction between the increasing globalisation of economic activity and the protectionist nature of the increasing number of regional bi-national and multi-national agreements. Are these agreements an evolutionary stage in the development of global free trade? Or is the formation of these regional economic communities a determined effort by nations to control the liberalisation of global free trade to protect their domestic industries and markets?

The outcome of previous ten year period in our history can be compared to the magnitude of change that we have witnessed during the past decade.

Some events worth noting are:

- The decline of Communism
- The establishment of the US as the only super power, matched by the decline of the USSR
- The embracing of capitalism in China
- The growth of the Asian Tigers and the world's increasing awareness of their share of the world's trade, their population, and their contribution to current and future economic growth.

Recent cataclysmic events are beginning to be placed within trends that either result from, or contribute to, the social, political and economic forces of the world. The rapidity and extent of change have created an environment of opportunity for an increasing number of players. The size of these opportunities, for example China's opening market, has initiated an unprecedented level of comment and conjecture as to the future we are creating for ourselves. The interdependence of nations, both regionally and globally, is becoming the major factor influencing the formation of new alliances and agreements.

POWER SHIFTS IN GLOBAL ECONOMICS

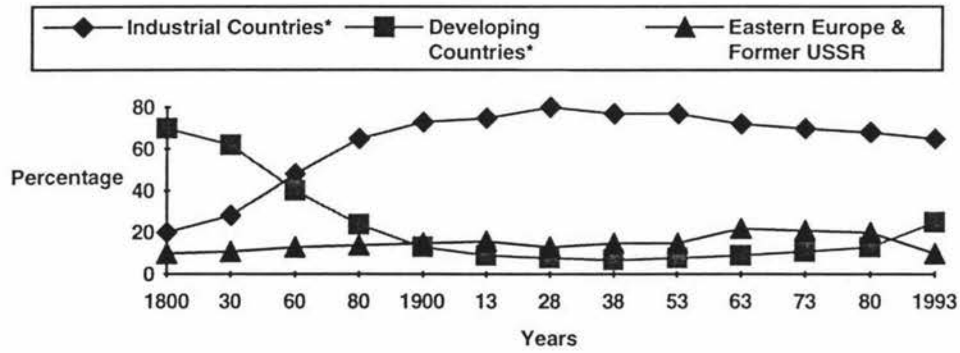
The achievement of swift and continual growth in East Asia since the 1960s has resulted in an overall redistribution of the world's economic power towards the region. In 1960, East Asia accounted for just 4 per cent of world economic output. Its current share is 25 per cent (*The Economist*, 1-7 October, 1994:9).

While GNP in Europe and the United States has grown at an average rate of 2.5 per cent to 3 per cent per annum over the last twenty five years, many East Asian countries have managed an average annual rate of growth of 6.5 per cent to 7.5 per cent, and this is not expected to decline over the next five year period. Between 1992 and the year 2000, it is anticipated that 40 per cent of all new purchasing power created in the world will derive from East Asia. The region is also expected to absorb between 35 per cent and 40 per cent of the global increase in imports (Schwab and Smadja, 1994). Furthermore, East Asian central banks now hold almost 45 per cent of the world's foreign currency reserves (The *Economist*, 1-7 October, 1994:9). While the United States and the major European countries continue to increase their foreign debt levels, Japan, Taiwan, and Singapore, and Hong Kong remain debt-free.

The shift in global economic power to East Asia has to some extent taken the world by surprise. The speed at which the NICs (newly industrialised countries) have increased their growth rates has astonished the world. Only a few years ago Japanese goods such as plastic wear were considered inferior products, and were sold in Woolworths and in countries like Korea, Malaysia, Hong Kong, Taiwan and Singapore, which were third world countries. Co-ordinating global free trade, however, will be a difficult and drawn out exercise, especially for countries that have suffered economic isolation for many years.

Large third world nations such as China and India, with their increasing gross domestic product (GDP), look poised to have economies larger than the US in the next century. As illustrated in Figure 1.1, these countries held dominant positions before the advent of the Industrial Revolution in Europe. As late as 1830, an estimated 60 per cent of all manufactured goods came from China and India (The *Economist*, 1-7 October, 1994:9). Providing China's infrastructure continues to grow and cope with the economic growth, and India successfully deregulates its economy and provides a stable platform for investment and manufacture, these two economies will inevitably become economic giants again. Together, they make up 50 per cent of the world population. India's growth rate of between 4 and 5 per cent, its increasing foreign reserves and decreasing trade deficit due to a 20 per cent increase in exports, should see the country out of its poverty circle by the end of this decade (McDonald, 1994:50).

Figure 1.1: Global Economic Cycle: 1800-1993



Source: Paul Bairoch, cited in the Global Economy Survey
The Economist, October 1, 1994, p.9
* Based on current definitions. 1993 is *The Economist* estimate

It has dawned on nations that alliances are the keywords to free trade and prosperity. Porter's view of 'alliance' (Porter, 1990:66), while relating to industries, may also apply to nations negotiating for a group of industries. It must be remembered that while governments negotiate trade agreements with other nations, they are in effect only representatives of their own business communities. In effect they pave the way for industries to have unrestricted or less restricted access to foreign markets. They provide opportunities to compete more easily in an increasingly competitive world. Alliances also allow smaller countries access to larger markets where economies of scale would otherwise exclude them from these markets.

Economically, these developments have given rise to tripolar world with the three centres of power residing in Western Europe, North America and East Asia. The world is currently witnessing East Asia's ascendancy to global economic power over the stalwarts of the previous global economy where the focal points of political and economic power rested in Europe, the US and the USSR.

GLOBAL TRENDS

The whole aim of trade agreements is to work out an equitable and workable alliance that does not ruin national economies while allowing them time to adjust to their relative competitive advantages and dismantling their protectionist industries. The increase in trade competition and the resulting trade realignments among nations have left the world wondering where it will end. Nations and businesses involved in a global economy will need to be as smart and as efficient as possible to cope successfully in the international environment.

A WORLD VILLAGE

The world is shrinking as modern technology brings places closer together. Communication and transportation are fundamental elements of international trading. New technology has created an information highway which has increased the speed and ease of global communication. World computerised communication network systems make it possible to search quickly for regional and global information. Satellite technology has been widely used in the areas of television and telecommunications. For instance, for the first time, the world watched international forces battle President Saddam Hussein live on CNN during operation Desert Storm. This type of international coverage has shown the world, like never before, the globalisation of nations.

In the area of transportation, new aircraft technology has produced sophisticated aircraft such as B-777, M-900, A-300 and Concorde, giving a safe, fast and reliable way of transporting people and goods to a variety of destinations around the world. Using modern underground mining technology, transportation routes go under as well as on land and sea, for example the tunnel between England and France.

The increased use of global communication and facilities such as the Internet will have a major impact on world trade in the years to come. As the Internet grows, its frequent use will have a contracting effect on the world as a whole, making it appear even smaller. In terms of international trade, this will mean an easing of the trading process. For example, a consumer article can be purchased from an on-line catalogue based anywhere in the world and requested through a home computer to be shipped to a foreign destination. The cost can be debited to a bank account either in the home country or a foreign country. Similarly a person can make a deposit in their bank in Kuala Lumpur, for instance, fly to Los Angeles and withdraw money from that same account through an automated banking machine. These advances illustrate the difficulties of keeping borders and nations closed, as the information 'super highway' transcends these borders. Such technology will invariably cause changes in the way international trade is conducted. It becomes more and more difficult for nations to remain closed.

GLOBAL CULTURE

Gaining a better understanding of each other's culture is an important outcome of wider global trade. People involved in international trade are from various cultural backgrounds with their own languages, lifestyles and customs, making cross cultural understanding a necessity. Cultural differences become more acceptable as international communication and understanding increases. Consequently, when trading internationally many products or services must be adapted to the cultural needs of another country.

Today, culture crosses borders more than in any previous period of history. For example, the Western man's business suit is recognised as formal dress in most countries, whatever the traditional dress is. Similarly, fast food outlets are to be found all over the world, and ethnic restaurants are growing in popularity with people of different cultural backgrounds. In some way, all these create a congruence in cultural thinking, tolerance and greater understanding of different cultures.

The effect of an East Asia-led world recovery will not be confined to business. As in the past cultural influences follows trade - Anglicisation and Americanisation results from trade. Economic strength will invariably translate into political power and influence.

SOCIAL GOALS

A significant factor in the development of the global economy is the labour force (Fong, 1993). Countries require different types of labour depending on their economic performance, for example in the United States there is a high demand for well paid skilled labour but in Indonesia, Malaysia and Thailand the demand is for cheap unskilled labour. Most countries seek the right skill mix based on their particular stage of economic development.

A problem that arises from fast economic development is full employment. Nations require certain amount of 'slack' labour force to meet economic growth and further development of the economy. Labour shortages and the resulting increases in labour cost often push a country towards industrialisation. The effect is a shift from the production of primary produce to manufacturing and value-added goods. This shift requires the up-skilling of the labour force through training and education. Singapore faced this situation in the 1980s, while Malaysia is currently experiencing it. Both countries, to meet the increased labour demand and people with new skills, have resorted to external labour recruitment.

Labour mobility also creates additional social problems for nations. Governments are acutely aware of the social problems arising from acculturation patterns of new immigrants. Initially, global labour flowed from eastern to western countries looking for better employment and lifestyle. However, with the economic growth of Asia in more recent years, this has become a two-way flow.

Unemployment has become a serious problem in many Western countries. There are 35 million unemployed people in the OECD (Organisation for Economic Co-operation and Development) countries, with perhaps another 15 million who have given up seeking work or are in part-time employment. This represents 8.5 per cent of the OECD labour force and is an enormous waste of human resources. It also reflects inefficiency in economic systems (OECD, 1994). Unemployment also causes social problems. Many governments, weighed down with huge social welfare payments, are being forced to reconsider the principles of a 'welfare state'.

ENVIRONMENT

Environmental concerns are now a global issue as they affect us all. One country's environmental problem is now a common environmental problem for the others. Problems such as acid rain or the lake and waterways pollution of the Great Lakes in North America provides evidence that environmental problems cross national boundaries. Consequently, such problems are forcing international co-operation in order to find solutions.

The growth of developing countries has an increasing impact on the earth's natural environment. Just as the US, Australia and New Zealand deforested their countries in the process of economic development, many developing countries are currently doing the same. The difference between now and two hundred years ago is the level of awareness of the importance of ecology to the environment. It is now known that forests and jungles provide most of the earth's oxygen, and that the increasing amount of carbon dioxide in the atmosphere, caused by deforestation, contributes to global warming.

As growth increases in the developing countries, their populations are increasingly attracted to western consumer goods. In the past five years, Bangkok's traffic congestion has caused serious detrimental effects on the already polluted atmosphere (Tarker, 1994). Currently, China has one car per 1000 people compared to 570 per 1000 in the US. China and other developing countries reaching the same levels of western car ownership will provide the world with a more alarming problem than currently exists (*The Economist*, 1-7 October, 1994:35). Caring for the environment costs money, which developing countries argue they cannot afford. Their major priority is industrialisation, and to most of these economies environmental costs are seen as a burden that may distract foreign direct investment and decrease their competitive advantage.

RECENT GLOBAL EVENTS

As described earlier, modern communication has made the exchange of information easier. It is also accessible to people in the remotest of places. Modern media has announced to the world that development of economies is faster through free participation and exchange of trade than through a controlled economic system. Many governments belonging to the command economies have begun to change their systems and to re-evaluate their position as members of the international economy. In this new age of co-operation instead of rivalry, nations are forming new relationships. The year 1989 seems to stand out in history. Political and economic changes included the following:

- **The end of the Cold War** - Collapse of Communism within the Soviet Union
- **The Dismantling of the Berlin Wall** - The reunification of Germany
- **The Chinese democratisation process** - The events associated with Tianamen Square made the world focus on China's progress towards an open market economy.
- **The formation of APEC** - The formation of a 'forum' of nations in the Asia pacific region based on the concept of open regionalism.
- **The formation of NAFTA** - an agreement creating the largest retail market in the world.

THE END OF THE COLD WAR

For more than 40 years, confrontation between America, its allies and the Soviet empire with its proxies was the central focus of world affairs. The political, military, economic and social order was determined by the existence of this confrontation.

In recent years, there has been growing momentum in the communist countries to end the disparity between socialist ideologies and to recognise that economic growth was being hampered by repressive authoritarian governments. In other parts of the world, Thatcherism, Reganism, social democracy and authoritarian military regimes were all generating hopes and beliefs that could not be met without a substantial world realignment. In 1989 this momentum reached its zenith (Selvarajah, 1994). Changes were to occur that would alter the future focus of world affairs and the balance of power.

The dissolution of communism during the last five years has led to a post cold war openness with the West. The security objectives and suspicion of the communist bloc are no longer applicable. The removal of the communist threat has begun to affect economic alliances, in that nations no longer require trade based on security.

COLLAPSE OF COMMUNISM IN EASTERN EUROPE

'Perestroika and Glasnost' - Mikhail Gorbachev introduced radical reforms that signalled the end of Marxism/Leninism in the Soviet Union and there was wide acceptance of a market economy. It was hoped that the previous shortages and surpluses caused largely by the price fixing of central planners would be resolved by the free interaction of supply and demand (Cook, 1990).

The dissolution of communism has had a profound effect on the European Union, especially on Germany. The progression of the former East Germany, from a centralised control regime to that of a market or mixed economy will be difficult, especially catching up with the sophisticated systems of the West. Many former Eastern bloc nations are increasingly disillusioned about the ease with which they thought they could adapt to democratic systems and a Western lifestyle. There is growing resentment in former East Germany and in Poland, and many believe that they were better off under communist rule (*The Economist*, 21 May 1994:22). Conflicts such as those in Bosnia and Chechnya only highlight this point as the old Eastern Bloc moves from communism to a more democratic system of government.

Russia is facing difficult times as the economy is in the grip of recession. The political scene is dangerously unstable, and law and order problems are surfacing. Russia is rich, but painful reforms have to proceed before APEC or EU admission is possible. This delay may cause Russia the benefits of freer trade offered by regional groupings. However, if Russia can make the transition to a free market economy it will be a force to be alongside, if only from the point of view of size.

Western Europe would gain most from the communist march towards freer markets. Exports to Russia and its satellites in 1987 were ten times greater than to America, and eleven times greater than to Japan. The combined GNP of former East Germany, Hungary and the now divided Czechoslovakia exceeds that of China (Kirkland, 1989).

THE DEMOCRATISATION OF CHINA

What happened at Tianamen Square in Beijing in 1989 was a setback for the new democratic movement that had engulfed the Soviet Union and was about to rise in China. Following the boom of 1988, with a 30 per cent inflation and a shortage of foreign currency, there was widespread protest from Chinese students about the slow pace of economic liberalisation and the lack of commitment towards democratisation by the Old Guard. Immediate change was demanded by the movements seeking democracy, the continued 'slow plodding' by the old 'octogenarian' guard was no longer acceptable. Government response was swift and severe, but the message demanding changes was recognised. The protest at Tianamen Square was a test of will of the governing body and, in the end, the militia was sent in resulting in, a bloody massacre.

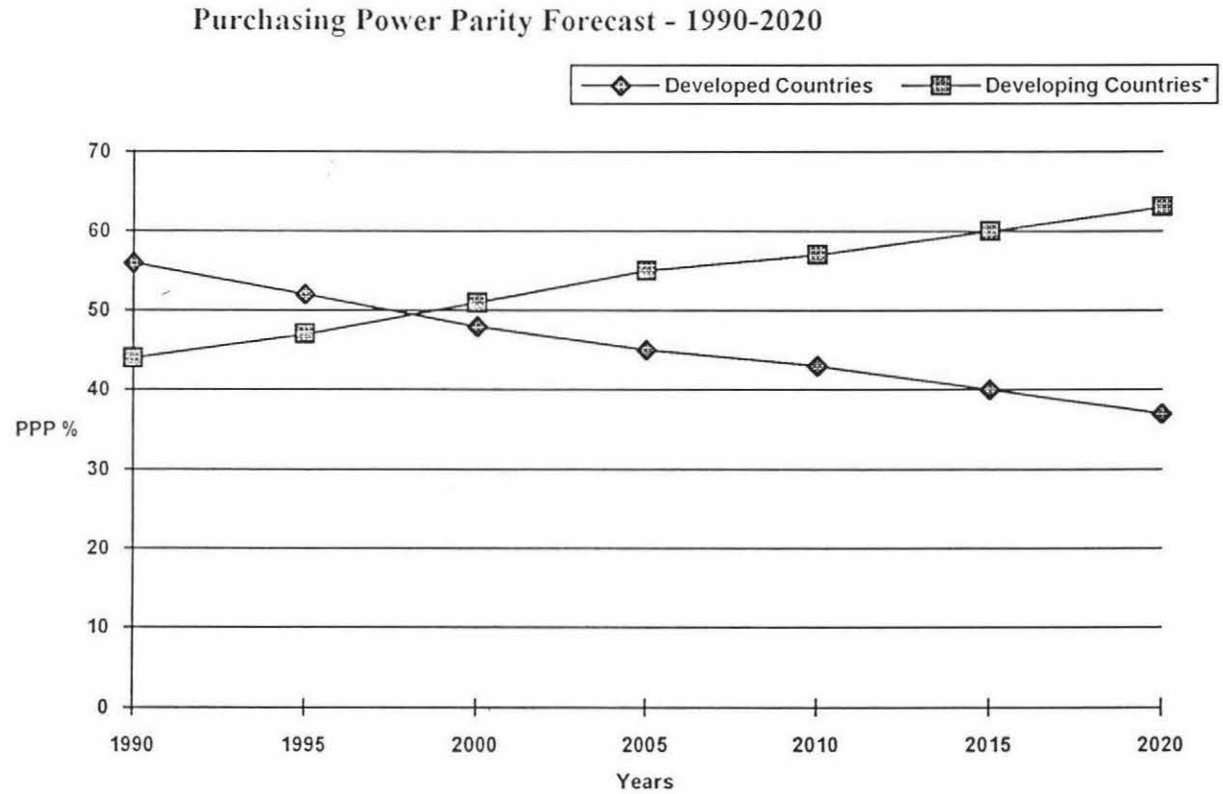
The effects of the Tianamen Square incident were not altogether negative. It became quite apparent that China's future as a communist nation was limited and that the people of China were ready for change. Since the 1980s, China has slowly been liberalising its economy under Primer Deng's control, and its policy is to avert a collapse of its government and economy such as happened in the USSR.

China now is the fastest growing world economy, with a huge consumer base of more than 1.1 billion people. The confidence shown by the international community in China's liberalisation can be seen by the increasing amount of investments being channelled into China by Chinese living overseas. In 1992, the total investment by overseas Chinese from ASEAN countries amounted to US$7.3 billion spread over twelve projects (Selwyn, 1993:25) One of the major obstacles to investment in China is the non-convertibility of the Renminbi. However, this is expected to change during the next three years. At present the Renminbi can be traded on China's Foreign Exchange Adjustment Centres, although restrictions are placed on what the foreign currency can be used for.

THE ECONOMIC INFLUENCE OF DEVELOPING COUNTRIES

As Figure 1.2 indicates, developing countries are overtaking the productivity of developed countries. This trend is creating greater interdependence between the economies of developed and developing countries. As the developing countries have capitalised on the competitive advantage of a cheaper labour supply, the developed countries have witnessed the demise of some labour intensive domestic industries.

Figure 1.2. GDPs of Developed and developing Countries

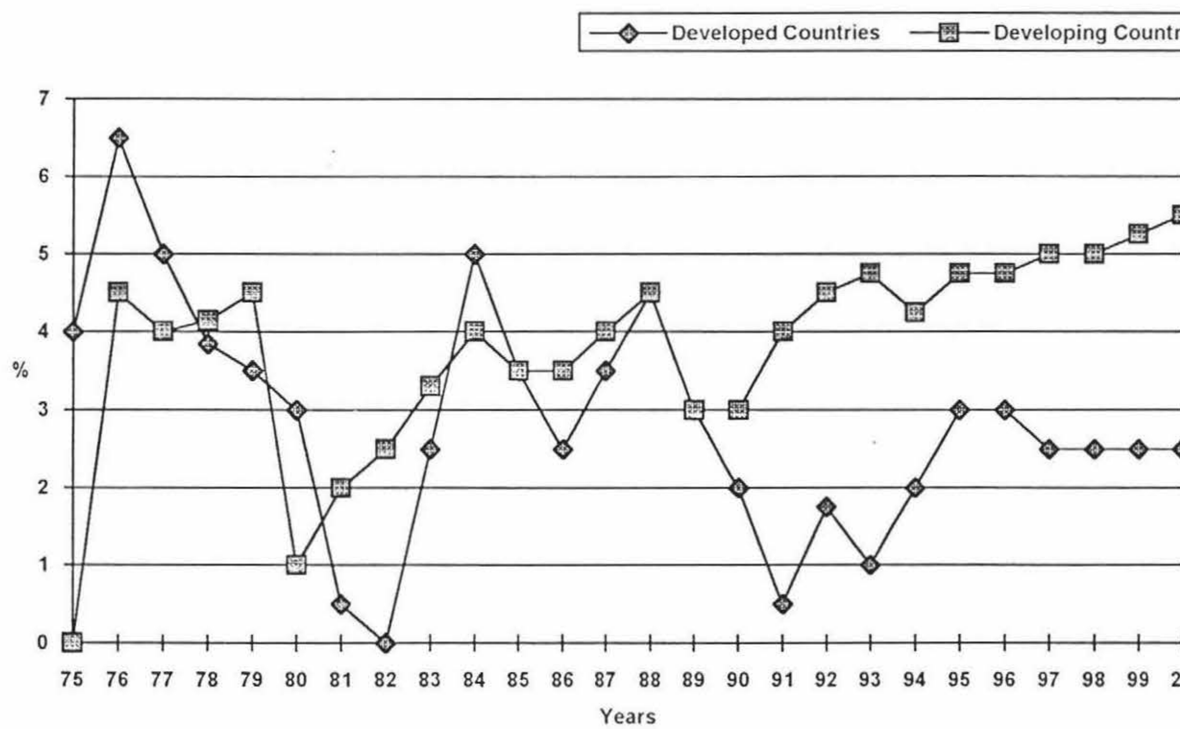


Source: World Bank

* Including Eastern Europe and former Soviet Union

Increased imports from developing countries have reached a point where they have become an independent source of growth in the world economy. The forecast in Figure 1.2 suggests that before the year 2000 the developing countries' purchasing power parity (PPP) will exceed that of the developed countries. Furthermore, Figure 1.3 identifies 1989 as the year in which the economies of the developing countries began to improve. Before this their GDP growth sat quietly in the shadow of the industrialised countries.

Figure 1.3: GDP % change from year earlier

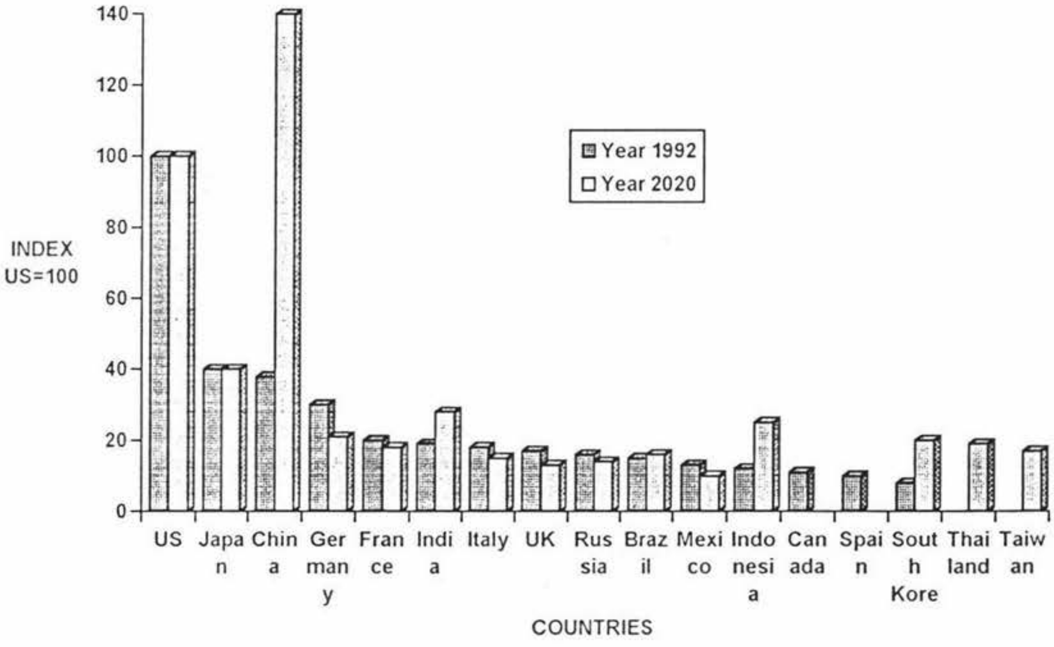


Source: World Bank

* Excluding Eastern Europe and Former Soviet Union

These trends are creating a significant shift in the balance of economic power. Figure 1.4 illustrates the changing order of nations based on the size of their economies. It identifies a shift from two developing countries out of the first eight in 1992 to a projected five developing countries within the first eight countries by the year 2020.

Figure 1.4: 15 largest economies in 1992 and 2020* (in 1992 US = 100)



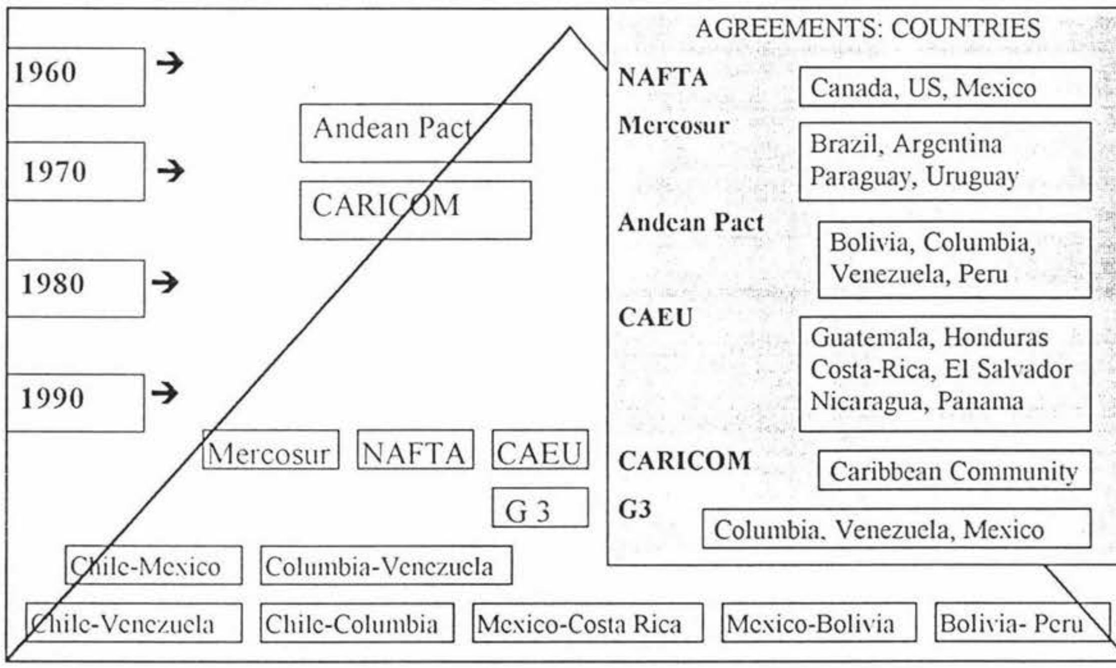
Source: World Bank
* Forecast assume countries continue to grow at the regional rates projected in the World Bank's Global Economic Prospects

REGIONAL TRADE AGREEMENTS

An increasing number of regional trade agreements indicate the progressive recognition by governments of the changing world trade environment. Driven by agreements offering varying degrees of exclusivity, individual nations have pursued similar relationships, sometimes solely from the fear of being 'left out'. The result has been the new, collective markets of Western Europe, South East Asia, the Pacific Rim and North America. Small countries have, to varying degrees, recognised the powers of these markets and looked for any opportunity to balance that power. For some this has meant application to join the larger economic communities. For others, the prospect of forming new communities. Figure 1.5

illustrates the recent explosion of agreements among countries of the Americas alone.

Figure 1.5: Regional Agreements in the Americas



Source: Time Magazine

The US, already involved in APEC and NAFTA cross membership, promoted a free trade area from Anchorage to Tierra del Fuego with 33 other North and South American leaders at the December '94 'Summit of the Americas'. As Nigel Hollaway (1994a) highlights, the declaration that free trade negotiations will end by 2005 is comparable to APEC's declaration of completion of a free trade area by 2020. One might ask if the US is positioning itself so that it has close ties in three directions: across the Atlantic, the Pacific and the Caribbean.

With the increasing convergence of economies there has been a flurry of bilateral and multilateral trade agreements. Some of the more important regional agreements are discussed in the next few pages and in detail in chapters 3 to 5.

EUROPEAN UNION (EU)

In 1945 the Second World War came to an end. Western Europe was devastated, occupied, blitzed and bankrupted. World War II destroyed an age-old idea that the state was all powerful and capable of protecting its citizens. It was recognised that interdependence not independence was the key to economic and political survival.

The European Union was first formed as the European Community (EC), then becoming the European Economic Community (EEC) in 1958 under the Treaty of Rome. The European Union Act created the European Union, which came into effect on 1 January 1991.

On January 1 1993 the EU established a single market of 340 million consumers. Although progress has been slow in such areas as monetary and labour reforms, considerable progress has been made in eliminating trade barriers in highly protected industries such as airways, telecommunications and automobiles.

Development of the EU has principally excluded the countries in North and South America, together with the countries of the Pacific. Such exclusion has led to fears of economic, social, political and security isolation by the rest of the world. In response, we have seen the strengthening of ties under NAFTA and APEC. Some see the formation of the EU, the NAFTA and the APEC as initiatives to become more global and less internalistic, thus the supporting GATT/WTO philosophy of free trade (Bergsten, 1994).

The recently expanded EU borders Russia, the former Eastern Communist bloc and former Yugoslavia. Russia is a likely APEC candidate, but Norway and the

Eastern European countries are definite EU candidates. However, significant economic reform is required by a number of these countries before acceptance is received.

The EU has made recent efforts to improve diplomatic ties with Asia preferring dialogue rather than restrictive trade action. This led, in January 1996, to the first ever summit with ASEAN and signals the growing recognition of the Asia Pacific region and the need for wider global dialogue.

North American Free Trade Agreement (NAFTA)

The threat of exclusion from Europe, and the development of a similar sized market (EU population 370 million, NAFTA 360 million) are powerful motivators in the establishing of NAFTA. Members of NAFTA also enjoy 'cross membership' as members of APEC.

The intention of NAFTA was to provide a platform for economic security and social support in the region. Parties to NAFTA enjoy sympathetic trade negotiations with trilateral trade. Lucrative government contracts such as defence can be shared across the economies, and common manufacturing standards have been employed. The following reasons are seen to be important contributions to the formation of NAFTA:

- Awareness of the strengths generated by the EU and East Asia and the growth in inter regional trade as compared with intra regional.
- Recognition of the potential of a large consumer and retail market by combining the growing cheap Mexican labour market of 86 million people with the Canadian raw material resources and the US capital and technology.

For all the parties involved, the promotion of free trade on a regional basis protects each member internally but more importantly it also protects them from the EU and Asian nations. The possible gateway of Mexico to Latin America offers not only enormous economic gains but also a closer view of the politics and the defence of the respective nations. The establishment of this significant trading bloc certainly protects and advances US interests, which were seen by the US to be weakened under GATT.

The NAFTA members' (USA, Canada and Mexico) cross-membership in APEC will help the drive towards global free trade.

It is expected that Chile and other South American countries will be candidates for future admissions thus boosting the labour pool, providing investment opportunities and adding significant numbers of consumers wanting the technological advances of the US and Canada.

ASIA PACIFIC ECONOMIC CO-OPERATION (APEC)

APEC was in response to an emerging 'Global Asia' and the need for declining Western economies in the Asia Pacific region to forge a link with the booming nations of Asia. For the Asian nations APEC created a large consumer market and an outlet for their increasing manufactured products

Formed as a multilateral open forum for the promotion of region-wide co-operation, among Asian and Pacific economies, the focus of APEC is on trade, investment, and economic co-operation through a process of Working Groups.

Associated with APEC is the Pacific Economic Co-operation Conference (PECC) which has a less structured format.

Within the APEC group of countries is the Association of South East Asian Nations (ASEAN). This was formed in 1967 as an association for promoting economic co-operation and development. ASEAN is covered below and in some detail in chapter 5. Regional security is also a major concern of this group and recently the ASEAN Regional Forum (ARF) was formed. The ASEAN Free Trade Agreement (AFTA) was formed in 1992. New Zealand and Australia sought admission in 1994 but to-date no consideration has been made to expand the current membership, at present made up of ASEAN member countries only.

The Australia and New Zealand Closer Economic Relations (CER) and NAFTA are the other two trade agreements located within APEC. CER is basically a free trade agreement between Australia and New Zealand that came into effect in 1983. Its purpose was to have free trade between the two countries by 1995. This date was brought forward to 1990 and both countries now enjoy free trade with each other. This agreement is quite similar to NAFTA as trade is only liberalised between the member countries but each member has separate tariff structures with third countries. See chapter 5 for more details on PECC, ASEAN and CER.

Although APEC was not formed as a free trade area, it will move to this by the year 2010 for developed countries and 2020 for all other members. The Asia Pacific Region has the potential for continued growth and the ability to achieve a clear position as global trading leader. The 'Spirit' of co-operation, problem-solving and liaison between member countries is unique as this moulds a multitude of differing cultures, politics and economies.

The four major threats to this region's strength are:

1 The possible competing interests of the ASEAN group. Having been formed to promote themselves collectively, ASEAN has been 'swallowed' up by APEC which has increased its global presence.

2 The possible dominance of APEC by the US, which the Asian countries do not want. Instead they prefer the US to have its own unique presence and mix in APEC.

3 The presence of two of the world's major economic players, Japan and the US, could be damaging if differences continue to occur. It is possible that both the US and Japanese economies could experience some real problems in the next 10 years for reasons indicated in Table 1.1.

Table 1.1: Possible problems that Japan and the US could face in the future

Japan	USA
Over-production	Slow growth
Over-staffing	Outward investment flow
Politically instability	R & D stagnation
Urban versus rural interests	Stretched resources
Non innovativeness	

4 A recent report from PECC indicates that China will be the major contributor to the projected growth in the Asia Pacific. Growth is forecast at 8.2 per cent in 1995 and imports have surged 25 per cent in the past two years. However, fuelling a 15-20 per cent inflation rate (Islam, 1994a:30), the double digit growth is thought to be unsustainable and the concern is whether there will be a slow down or a crash. If the latter, then there will be serious ramifications for the Asia Pacific region.

ASSOCIATION OF SOUTH EAST ASIAN NATIONS (ASEAN)

The formation of ASEAN brought together countries with diverse backgrounds. Most of them have different colonial backgrounds, religions and languages. The reason for establishing ASEAN was political. It was a grouping of democratic nations bordering communist nations to the north. At the time of its formation and for the first ten years, its progress was slow - members were at time suspicious of each other. However, in the last twenty years, having to some extent overcome their differences and emphasising on mutual growth and prosperity in the region, the ASEAN nations have progressed economically. Furthermore, the admission of Vietnam in 1995, and the likely admission of Myanmar after years of international and regional isolation, points to the realignment of nations that is occurring today. According to Barker (1994), these two countries are resource rich and have the potential to emulate the economic success of the Tigers.

The three major threats to this Association's strength and prosperity are:

1 Internal politics and security problems.
2 The social problems that are starting to emerge due to the consistent growth and increased (relative) wealth of individuals.
3 The inability to reach firm and defined objectives quickly. This may be the Asian way but the 'competition' is now moving at a faster pace.

GLOBAL SECTORS OUTSIDE THE MAJOR GROUPINGS

As the world is realigning into three major spheres of economic control, Europe, North America and East Asia, parts of the world are being left out of this economic 'race'. In this category we can include Africa, the Middle East, Russia, South America and the Indian Subcontinent.

India

After the demise of the Soviet Union, India's major trading partner, India had embarked on major restructuring of the economy under former Finance Minister Mr Manmohan Singh. The restructuring of the global economy had forced India to abandon the Gandhian philosophy of self sufficiency which had been its major economic platform since independence. Over the last five years, India has maintained a GDP growth of between four and five per cent. With further deregulation of the economy, and maintenance of its current growth rate, India is expected to play a major role in the development of the Subcontinent, and to contribute further to the growth of Asia.

India, if it maintains its current growth rate, is predicted to become the fourth largest economy by the year 2020 (World Bank, 1994). Like China, India had previously been a world economic power but lost this position as Europe advanced by means of technological superiority. However, it is an emerging country of significance and, unlike China, its expansion may be rapid as it already has a strong technological base. Furthermore, the country is an important member of the Commonwealth, has a fairly good infrastructure, western knowledge and influence, relatively high education levels, and a good supply of skilled labour. India is currently not part of a trade bloc but because of its size may not be disadvantaged in this respect.

Africa

Africa as a region has performed poorly in economic terms, and there appears to be no respite in the short term. The increase in tribalism and its politically disruptive nature as shown, for example, by the Rwandan crisis of 1994 will mean that the continent is unlikely to move out of its sluggish erratic growth in the foreseeable future. It is estimated that it will take 10 years to repair the damage done to the Rwandan economy, with social damage taking longer. With the exception of South Africa, the average growth rate for the African continent between 1965 and 1990 was 0.2 per cent compared with the South East Asian region's of 5.3 per cent for the same period (The World Bank, 1993:2). Sustained economic growth requires social and political stability together with an educated population. Investment cannot be created in a nation in chaos where business is likely to be destroyed at any moment.

Due to political instability, Africa could well be left behind as far as trade alignments go. While many states are WTO signatories, they will not benefit from the closer economic relations that trade groups bring. With the 're-entry' of South Africa into the world economy, the prospect for economic development in Africa may eventually come about. With political stability, the development of the African continent may be via economic advancement in South Africa.

SOUTH AMERICA

Despite an uneven political background, South American nations appear to be settling down. Economically they still have a long way to go as political instability in many of the South American countries has disrupted economic development. Chile is the exception and has managed sustained economic growth over the past few years. Chile has not aligned itself with the other South American nations, believing it can have greater economic growth on its own, and has applied to join NAFTA (Williamson, 1993). If Chile becomes the first South American nation to join NAFTA, the other countries could follow suit in the future. The free trade region will then have to be renamed to reflect both North and South American membership. Chile was admitted as the eighteenth member of APEC in 1994.

MIDDLE EAST

The Middle East, with a combined population of 184 million, accounted for 2.5 per cent of global GDP in 1989 (World Bank, 1991). There is no realistic prospect of the Middle East forming a trade bloc such as NAFTA or the EU in the foreseeable future. Improved economic performance will come from each country independently pursuing its own economic programmes.

The Middle East has always been viewed negatively despite increasing wealth and discretionary spending. Major religions such as Christianity, Islam and Judaism were founded in this region and had great impact on the various cultures of the world. In the area of economic impact, the Middle East has made its mark with oil and this is where it may stop. In the promotion of regional trade, it is considered unlikely that these nations will be cohesive enough to form their own regional group; rather they may become members of neighbouring regions. Religious differences are the biggest hurdle to progress in the Middle East, and along with Africa, it could well be left out of trade alignments. Most of the countries in the Middle East are WTO members. However, due to their differences, it is unlikely that they will form closer economic relations with their neighbours.

Political stability is returning to the region but there is still a lot of distrust. Some areas of excessive oil wealth exist and the potential for economic development is promising. These were once strong trading nations with established international trade routes. The meeting of cultures, East and West, continues, and the markets, although different in each country, provide opportunities for traders.

THE BATTLE FOR SUPREMACY

In the 1990s, the volume of trade in and across the Pacific Ocean has surpassed that of the Atlantic. In fiscal terms, it amounts to US$3 trillion a year market, growing at the rate of US$3 billion a week. In his sometimes provocative book, Cragg (1993) foresees a coming battle for economic supremacy between the Pacific rim countries and the new economies of Eastern Europe. Considering the differences between the Asia Pacific entrepreneurship and the Eastern European history of mismanagement, combined with Asia Pacific capital, Cragg believes that Asia Pacific is where global focus will rest. Certainly the power of the PRICs (Pacific rim industrialised countries) will contribute to the strength of the Asia Pacific region and this will continue to change global trading patterns.

What has to be considered is that there are emerging markets in every region and that within the PRICs, growth economies such as the NICs will have an import demand of staggering proportions that will have to be met not only from within the region but also from NAFTA and EU members. This is illustrated in Table 1.2 which indicates the share of world trade by countries in East and South Asia.

Asian firms are now moving into Europe. Nearly every big Asian conglomerate is expanding into Europe for a number of reasons, but more particularly to be situated in the world's largest single market, close to their customers.

Table 1.2 : Shares of world trade output

Country shares in world trade in goods (1992)	Exports (US$ bill)	Share of World Trade %	Pro-rata Share of Trade gain (US$ bill)
World	3,731.0	100.00	75.0
Developing Asia*	573.2	15.4	116.3
Hong Kong	119.5	3.2	24.2
China	85.0	2.3	17.4
Taiwan	18	2.2	16.6
South Korea	76.6	2.1	15.9
Singapore	63.5	1.7	12.8
Malaysia	40.6	1.1	8.3
Thailand	32.5	0.9	6.8
Indonesia	29.3	0.8	6.0
India	19.6	0.5	3.8
Philippines	9.7	0.3	2.3
Pakistan	7.3	0.2	1.5
Sri Lanka	2.6	0.06	0.5
Bangladesh	2.1	0.06	0.5
Japan	340.0	9.1	68.7

*Does not include Brunei, Cambodia, Laos, Macau, Myanmar, Nepal, Vietnam
Source: GATT IMF

The USA has worked towards current APEC and NAFTA cross-membership due to concerns about its overall balance of payments deficit and to take advantage of Asia's global thrust. NAFTA, by increasing further membership, will increase in size significantly in the next ten years to rival the EU and operate as a massive voice within APEC, and it may replace ASEAN's current favoured position in APEC. Table 1.3 shows the growth rate and the size of world trade of the three major regions; EU, NAFTA and East Asia.

Table 1.3: GDP and World Trade by Region

REGION	% GDP GROWTH RATE	% OF WORLD TRADE
East Asia	6.6	22.3
EU	2.3	40.0
NAFTA	2.4	17.1
OTHER	N/A	20.6
TOTAL	3.2	100.0

Source: GATT IMF

Global realignment

The changes of 1989 have led to substantial growth in world trade, by enabling free trade to develop through a significant removal of barriers and market entry. The challenge of the future is whether the 'regionalised' economic groups of EU, NAFTA, APEC and ASEAN can work co-operatively to establish a system of global economic development. Self-centred national interest has to give way to economic regionalism, and from regionalism move to a truly global economy. This is the main proposition of this thesis.

Inhibitors to global realignment

Global realignment is not without its problems, as we have seen. The following are some of the obstacles to globalisation from a macro viewpoint:

- Governments have not only lost the power (or need) to defend borders by military strength, but also are losing control over their respective economies. These factors are very much decided by the greater concept of globalisation. Free trade barriers such as protectionism still exist. For example, in Japan there is heavy protection of agriculture, especially rice; in the US, textiles. However, in the last ten years there has been a 40 per cent reduction in tariffs worldwide (Sutherland, 1994).

- There is likely to be a continuing short-term clash between socialist expectations and free market economics. High expectations of social security, medical care, affordable housing and job security are, for example, entrenched in two generations of Poles, Czechs, Hungarians, Germans and Russians. These cultural perceptions will take time to resolve (Barnet, 1990).

- For realignment to continue there are several concerns regarding existing blocs and treaties which will need to be clarified. There are obvious signs of social, cultural, political and economic unease that may continue to prevent some blocs and treaties from succeeding in developing within a complete geographical area. This is true as much in the ASEAN as it is in the EU or in NAFTA.

- The EU is a transnational rather than international market. The focus tends to be on trade between individual members, rather than for common good. Considerable disparity between the economies of eastern Europe and western Europe requires addressing.

ENABLERS OF GLOBAL REALIGNMENT

The following are factors, from a macro point of view, that will help realise the goal of globalisation:

- Changes in the global economic *infrastructure* could become a significant factor in the success of global realignment, particularly if we consider this as a resource. As an example, it was estimated by the World Bank that in 1993 Asian banks held 34 per cent of the total world funds, and that this would increase to 66 per cent by the year 2020 (World Bank, 1994). This increase in wealth and disposable income in Asia will make changes to the manner in which finance and trade are negotiated. Similarly, there will be new financial institutions supporting this new thrust.

- In the GATT negotiations of the Uruguay Round considerable success was achieved in recognising the political, economic and environmental concerns of member nations. This Round also produced the General Agreement on Trade in Services (GATS) and the General Agreement on Labour (GAL). Service was never included as a trade issue in past GATT rounds, and with the growth of the service industry western nations such as the USA will be the main benefactors. The World Trade Organisation has taken over from GATT and has made a promising start with 123 countries signing the WTO Agreement.

- Success has been enjoyed by many transnational companies. In the case of New Zealand, companies such as Fisher and Paykel, Watties, Pacific Dunlop, Fletcher Challenge and Goodman Fielder have, under CER, developed contacts and fostered partnerships with Australian companies (Wells, 1995). These innovative and energetic companies have not waited for governments to establish the ties, but have moved progressively forward and are now poised to take full advantage of the markets in Asia. Governments have created the openings but it is the businesses that have taken up the challenge.

- APEC has global rather than regional aspirations. Cross-membership by NAFTA members seems unnecessary when they are already members of APEC, which is expected to become a free trade area by the year 2020. Details on APEC are covered in chapter 5.

  ASEAN nations, however, are sceptical of APEC domination by larger members, especially the US. Being resource rich but technologically poor, they seek to modernise and develop their economies. As mentioned earlier both New Zealand and Australia have sought membership of AFTA. This raises the question of cross membership as both these countries are members of CER.

STANDARDISATION OF TECHNOLOGY

Every country has its own product standards for its domestic market. However, the impact of conflicting national standards between countries causes problems. For example, electricity supply in Japan is 220v but in the United States it is 110v. This can complicate global trade. Electrical appliances need to be produced for the country they are exported to. Health regulations are another area where standards are critical, as many countries find they cannot export goods to a country unless they comply with the local health regulations.

The solution for this problem is to create global standardisation and this can perhaps be achieved first through regional co-operation. The European Union has a six-year programme to convert electrical power sockets and plugs (both domestic and commercial) to one standard throughout the member countries by the year 2000. Standardisation will give the advantage of an international alignment in products and compatibility. This would also make products available to a wider consumer base and bring about a reduction in cost due to economies of scale.

THE ROLE OF WORLD WIDE COMPANIES

WWCs which span countries and regional groupings will help to bring national economies closer together. One difficulty with this concept is that World Wide Companies (WWCs) such as McDonalds, KFC, Coca Cola and Levi already determine consumerism in the countries in which they operate. This occurs without any real accountability for their action, and is conceivably not the best model for the nationals of the foreign culture.

The political risk in each nation may not prove as great to the WWCs. The desperation for western technology and the need for capital, especially in developing countries, makes WWCs welcome.

CONCLUSION

There is no question regarding the ideal of a global free trade environment. The reality is that all countries are operating with mixed levels of success, and development within 'controlled' trade environments and the transition is certain to involve upheavals. Added to this is the uncertainty generated as the world powers shape up to one another in relationships of increasing complexity. Neither China nor Russia are suddenly about to embrace the American way of life wholeheartedly and live on a diet of democracy and capitalist self-interest alone. America's current lack of clear foreign policy is a strong indication of the self scrutiny the West is undertaking as power bases and economic alliances form, disband and reform again. Against this backdrop of political quagmire, governments are attempting to negotiate free trade policies.

The increasing regionalism is also, perhaps, a result of government bureaucrats clinging to their diminishing levels of influence and importance within the world of trade. The degree of this bureaucratic control is glaringly exposed in the European Union member governments' conspiracies to hinder their own regional, single-market ambitions. These ambitions, contained within the Single European Act (SEA) agreed to in 1985, set out the progressive establishment of an internal market, to be completed by 1992. *The Economist*'s survey of the European Union identified a number of levels of 'conspiracy' to undermine this SEA (*The Economist*, 1 October 1994:11).

One level is represented by the agreed delays in the single market. For example, free trade in insurance services and in investment services though established in July 1994 was delayed until January 1996. Similarly, liberalised basic telephone services are delayed until 1998.

Another level is the convenient parliamentary delays, including the required transposing into member country legislation of 222 of the 282 measures needed to create the single market. The slowest legislation to have occurred was in the area of public procurement, where only 59 per cent of the required national laws had been passed by the end of 1993.

In addition, there is the conspiracy creating the greatest obstacle to the single market: the use of state aid to maintain loss-making state monopolies. Protected in the SEA by their placement within 'reserved sectors', member governments have been increasingly creative at maintaining the protection, even after the monopolies have been legislated away.

Regionalism would therefore appear to be contradictory to increasing globalisation. Attractive tariff levels and other non-tariff incentives exclusive to member nations smack of protectionism and would appear to indicate that the same trade barriers exist. The term 'open regionalism' has been used to counter these claims and promote these agreements as milestones on the path to free trade. Present reality is perhaps closer to an even tie than an outright win for trade liberalisation. Hope for the future lies with the global customer and the demand for quality products and services at the best price.

To this end there is an important role for governments to play. They must ensure that the national environment is supportive of the consumer receiving the best product at the best price. This involves a shift away from the traditional role of governments which has been to protect producers and jobs.

An example of this is the successful lobbying of American peanut growers in Congress for protection from Mexico importing peanuts from China or Argentina and re-exporting them to the US. The National Peanut Growers Group timed their lobby to coincide with the tense lead-up to the NAFTA signing, and were able to offer the swinging of votes in exchange for a clause in NAFTA that protected them. Further, the US Secretary of Agriculture, in the closing of the Uruguay Round, secured a provision in GATT excluding foreigners from 97 per cent of the American peanut butter market.

Congress described this as patriotism and produced publicity material that stated that 89 per cent of American mothers were willing to support the higher quality of American peanut butter by paying a higher price. The level of the US subsidies to peanut farmers in 1989 was about US$200 million per annum.

Are nations in competition? Basically competition will disappear as evidence of the benefits of shifting from nationalism to regionalism to globalism is witnessed. Furthermore, core competencies for a nation will be generated by companies who, upon becoming global in their operations, will make the nations-in-competition scenario obsolete. WWCs have a major role to play in the expansion of free market philosophies.

Global realignment in other parts of the world economy will happen as a necessity. The only worry is that the current 'admission criteria' seem to include improved economic performance, leaving backward nations behind.

Following on from the discussion in this chapter of issues relating to global realignment of trade arrangements, based on regionalism, we will consider the aspects and nature of competition in chapter 2.

Chapter 2

The Nature of Competition

In today's world, despite a strong belief by some nations that it is possible no country can survive in economic isolation. All facets of our economy are linked to the economies of our trading partners, this linkage being carried out through the international movement of goods and services, labour, business enterprise, investment and technology. In those countries whose economies contribute to the major share of the world's gross domestic product (GDP), for example the G7, national economic policies should not be formulated without evaluating the probable impact on the economies of other countries. For example, for a small trading nation such as New Zealand, the decisions made by G7, the European Union and to a lesser extent the 'Asian Tigers', which are the consequence of trade restrictions and the formulation of trading blocs can often have wide spread implications. In this chapter we will look at the nature of competition from a trade perspective. Some of the basic trade theories relating to competition and the concepts of trade blocs and open regionalism with regard to free trade will be examined. These concepts form the foundation for understanding global realignment and the formation of regional arrangements such as the European Union (EU), the North American Free Trade Agreement (NAFTA), and the Asia Pacific Economic Co-operation (APEC).

INTRODUCTION

The 20th century has seen nations compete with each other for trade with more fervour than at any other time in history. As we have seen in the last chapter, the past 20 years have seen a shift of trading alliances away from traditional trading partners to new ones. Increasingly these trading partners are in East Asia.

Historically, international trade has suffered from problems created by distance and means of transportation from one nation to another. In the last one hundred and fifty years, however, international transport has become a relatively risk free exercise and new trading frontiers have been added to international trade routes. This ease of transport, brought about by the invention of the steam engine and the ensuing Industrial Revolution, enabled Britain, France and Germany essentially to carve up the globe between them, creating the empires on which their economic power was based. The end of the First and Second World Wars saw the dissolution of these empires, with the colonies receiving independence. For the next few decades, the newly independent colonies tended to continue trading under past agreements. In Australia's and New Zealand's case, more than 60 per cent of their exports continued to be shipped to Britain until the latter's entry into the European Economic Community (now the European Union) in 1973.

With Britain moving into the European Economic Community (EEC), the Commonwealth countries, which included New Zealand and Australia, had to find new markets for their products, forcing a realignment in their trading alliances. In response to the strengthening and formation of a single European market, Canada, the US and Mexico formed their own trading group, the North American Free Trade Association (NAFTA) on 1 January 1994.

This realignment of trading partners, as we introduced in chapter 1, continued over the following years to the point of a global realignment in trade. This global realignment is defined as a move away from bilateral trade agreements, and a move towards multilateral trade agreements and open regionalism (Selvarajah, 1994).

This increased globalisation of trade has been facilitated by:

- Communication improvements
- Increased ease of international transportation
- Deregulation of financial markets around the world
- The effect of the General Agreement on Tariffs and Trade (GATT)
- Technological improvements (especially in Information Technology)
- Development of common international procedures and standards

This global realignment in trading alliances has been brought about primarily by increased competition in the global marketplace and its effect on a nation's economy. Whereas earlier this century nations formed military alliances to counter potential aggressors, the aggressor has changed from wielding armies to wielding finance and is capable of devastating a country's economy through such tactics as dumping and economic sanctions. In an effort to maintain some control over their internal economies while the world goes through a transitional phase towards a more non-discriminatory economy nations are seen to be entering regional trade arrangements and alliances, as a way of countering economic threats of nations and the promotion of freer trade.

The past decade has also seen the world economic focus shift from Europe and the US to the Asia Pacific Basin. Coupled with this shift, trade alliances have been formed in an effort to limit the effects of competition from other countries, especially the Far East.

COMPETITION

The Free trade argument is in principle persuasive. It states that if each nation produces what it does best and permits trade, in the long run all nations will enjoy lower prices and higher levels of output, income, and consumption than could be enjoyed in isolation. In a dynamic world, comparative advantage is constantly changing owing to shifts in technologies, input productivities, and wages, as well as tastes and preferences. A free market compels adjustment to take place. The efficiency of an industry must improve or resources will flow from low productive uses to those with higher productivity. Tariffs and other trade barriers are viewed as tools that prevent the economy from undergoing adjustment, the result being economic stagnation.

THE THEORY OF COMPARATIVE ADVANTAGE

The Theory of Comparative Advantage was advanced from the Ricardian version, when the concept of factors of production and production processes which transformed them into goods and services was introduced. Competitiveness is the process which generates production factors and the organisational arrangements which combines them. International competitiveness is therefore the ability of an industry or sector to profitably maintain or increase its market share over time (Latimore, 1992). This means that industry can sustain growth over a period of time, while using resources efficiently. Comparative advantage is used to measure a country's international competitiveness with that of its trading partners, or in markets which have not yet been developed. However, competition may be internal or external and measures of competitiveness can distinguish between the two by simply ignoring domestic sales or focusing on foreign sales alone. Competitiveness and comparative advantage are concerned with maximising the efficiencies of global resource allocation.

Pareto Optimality Principle states that if all barriers to free trade are dismantled, countries will trade in those commodities in which they have a comparative advantage, leading to an efficient distribution of income, resources and consumption. Nations benefit from international trade if '...each country ....specialises in the production and export of those goods that it can produce at a relatively low cost (in which it is relatively more efficient than other countries); conversely, each country will... import those goods which it produces at a relatively high cost (in which it is relatively less efficient than other countries' (Samuelson and Nordhaus, 1995:679). They further states (681), 'when people specialise in the area of comparative advantage and trade their own products for goods in which they have a relative disadvantage, then when borders are opened to international trade, the national income of each and every trading country rises'. The assumption is that in a free trade environment, a country will import those commodities that it produces at a relatively high cost while exporting commodities that can be produced at a relatively low cost. Since resources are channelled from uses of low productivity to those of high productivity, gains from trade are made permitting higher levels of consumption and investment.

Free trade leads to a change in the conditions of production and can provide a nation's consumers with a wider variety of goods and services than would be available without trade. Benefits from trade also lead to specialisation of labour and enlarged scale of operations as nations use their comparative advantage to compete in world markets. Competition from imports also forces domestic producers to keep the prices of domestic substitutes to a reasonable level so that they can compete. In order to compete, producers are forced to become more efficient and productive, measures which in the long run increases national income. This can be seen in the retail banking industry where the opening up of the domestic market to foreign competitors, has led to the introduction of new financial services and an interest rate war in the home mortgage market.

Free trade, is however, seen by many nations as a theory and not workable in the real world. This has resulted in virtually all countries imposing some type of restriction on the international flow of goods and services through devices like tariffs and quotas. Modern trade theory assumes perfectly competitive markets whose characteristics tend to depart from real world reality - as evidenced by the existence of monopolies and cartels (for example Telecom and the Organisation of Petroleum Exporting Countries, OPEC). Those that argue for some type of protectionism may agree that economic losses occur with tariffs and other restrictions but argue that other non-economic benefits such as national security offsets these economic losses.

Underlying this free trade debate has been the General Agreement on Tariffs and Trade (GATT). For over forty years, much of the world's trade has been conducted under the rules of GATT. GATT was an agreement under which participating countries agree to lower their trade barriers, in particular their tariff barriers. When GATT was created however, many loopholes, existed in the agreement which allowed countries which followed GATT to create substantial trade barriers. This has led to groups of countries forming preferential trading arrangements where they lower restrictions on trade with each other rather than on trade with the outside world.

GLOBALISM

This increase in transnational activity by corporations has been driven by the constant search for competitive advantage. In more recent years the term 'globalisation' has appeared as an expression to describe this phenomenon.

Kenichi Ohmae, in his book *The Borderless World* (1994), identifies three stages in the development of a model for globalisation.

Stage I	Globalisation by the cloning of the parent company within each country of operation throughout the triad (Japan, Europe, US).
Stage II	After observing that companies enter fewer countries but penetrate each of them more deeply, the competitor focused model was proposed. This model stated that a company had to be present in and compete with its competitors in their home market to protect and maintain the company's strong position within its own home market.
Stage III	A model based on globalisation that is driven by customers whose needs and preferences have globalised and whose fixed costs for meeting them have soared.

It is this later model in Stage III that introduces the underlying motivating force of globalisation. In terms of trade the most significant contribution from advances in technology has been the increase in customer awareness and expectation. This increase in customer knowledge has occurred at the expense of a government's ability to protect its constituents from some of the harsh realities and benefits of embracing free trade policies. Governments have found themselves in a turmoil over the ramifications of a freer trade future, particularly when concerned interest groups have been successful in publicising their plight.

NATION STATES IN COMPETITION

It was expounded by Michael Porter in his book *The Competitive Advantage of Nations* (1990) that globalisation may increase the importance of 'Nation States'. This followed from the basic economic theory that Nation States were a source of competitive advantage.

Ohmae (1994) has, however, argued that nations must seek economic stability (growth is a factor), distribution of income, improved standard of living and security of trade free from conflict. Nations no longer seek to maximise their competitive advantage, but to participate in the economic growth of the region. Much collaboration is taking place, with competition becoming a myth of the past. Free markets mean an equitable sharing of resources. Ohmae states *Nations are not in competition they are in collaboration.* They are working towards common goals and will share in labour and rewards of given ventures. Nations do not compete for the same resources, but work co-operatively to achieve a common objective.

Tom Peters (1991) has defined the global business environment as "A seamless global economy, in which 'borderless' companies work with an ever-shifting array of partners to take advantage of new opportunities and to achieve mutually beneficial goals." Kenichi Ohmae (1989) adds that to operate globally, one has to think and act globally, and that means challenging entrenched systems that work against collaborative efforts.

He outlines a series of factors that are essential for Globalisation:

1 Principle of 'Equidistance' where local and foreign markets must both be treated with the same degree of focus.

2 Political boundaries which no longer determine the flows of finance and industry.

3 A free flow of information.

4 The sharing of a common language such as English which is gaining recognition as the accepted international business language.

5 Global citizenship, with freedom to travel and work in other countries.
Such relocation is not new, but there are four important reasons for its increase (Johnston, 1987):

* Increased aviation expansion.
* Removal of immigration/emigration barriers.
* Industrialised nations with ageing workforces, such as in Germany and Japan.
* Developing nations with a surplus of trained people, for example, technicians in India. We also recognise the rapid spread of religions across national borders, particularly with the adoption by western cultures of older Asian religions.

6 Universal products that are adapted to specific markets for maximum market penetration. For example, US laser technology adapted for use in Asian night-clubs. (Chan and Justis, 1990)

7 The establishment of strategic alliances are established to provide local market access.

8 Home or headquarters mentality becomes a thing of the past for multinational companies.

A region may gain a 'global identity' because of immigration, global commuting, improved communication and the accelerated mobility of capital (Selvarajah, 1994).

ORGANISATIONS IN COMPETITION

Credit for the development of regionally co-operative trading and unanimous adherence to principles can be claimed by the individual governments in the regions. It must be emphasised strongly, however, that free and open trading among the private sector corporations of the area led the way. For many years, corporations in the commercially free world have sought export opportunities without any ideological impediments. Branch establishment followed as technology allowed for globalised control. The institution of manufacturing capacity, whether by joint venture or strategic alliance, completed the integration. American corporations such as Coca Cola, Motorola, Microsoft and McDonald are well established in most APEC countries, as are such Japanese corporations of Mitsubishi, Sony and Toyota.

A new trend that developed in the 1980s was the emergence of multinational corporations from the other developed countries of the region and from the NICs. These organisations have also criss-crossed the region, further stressing and cementing the interdependence of the nations of the area for the services and resources that they share. Australia's Broken Hill Proprietary (BHP), the New Zealand Dairy Board, Korea's Hyundai and Samsung groups, Taiwan's Formosa Plastics, Evergreen Marine and Taiwan Semiconductor, Malaysia's Genting Berhad, and Hong Kong's Swire Pacific and Cathay Pacific Airways are examples of corporations that have expanded beyond their own shores into other markets.

In the 1990s, the emerging economies of APEC are producing companies capable of emulating the regional thrust. Indonesia's Indosat and Indofood have the resources to expand. Malaysia's Sime Darby already has international status, as does San Miguel of the Philippines. In Singapore, the leading companies are Singapore Airways and Singapore Telecom. Thailand's star corporation is the Charoen Pokphand Group which has significant investments in China, Indonesia and India.

Although nations may not be in competition, according to Porter (1990) organisations are. It is apparent that provided nations can create the opportunities, business will be the motivating factor in global realignment.

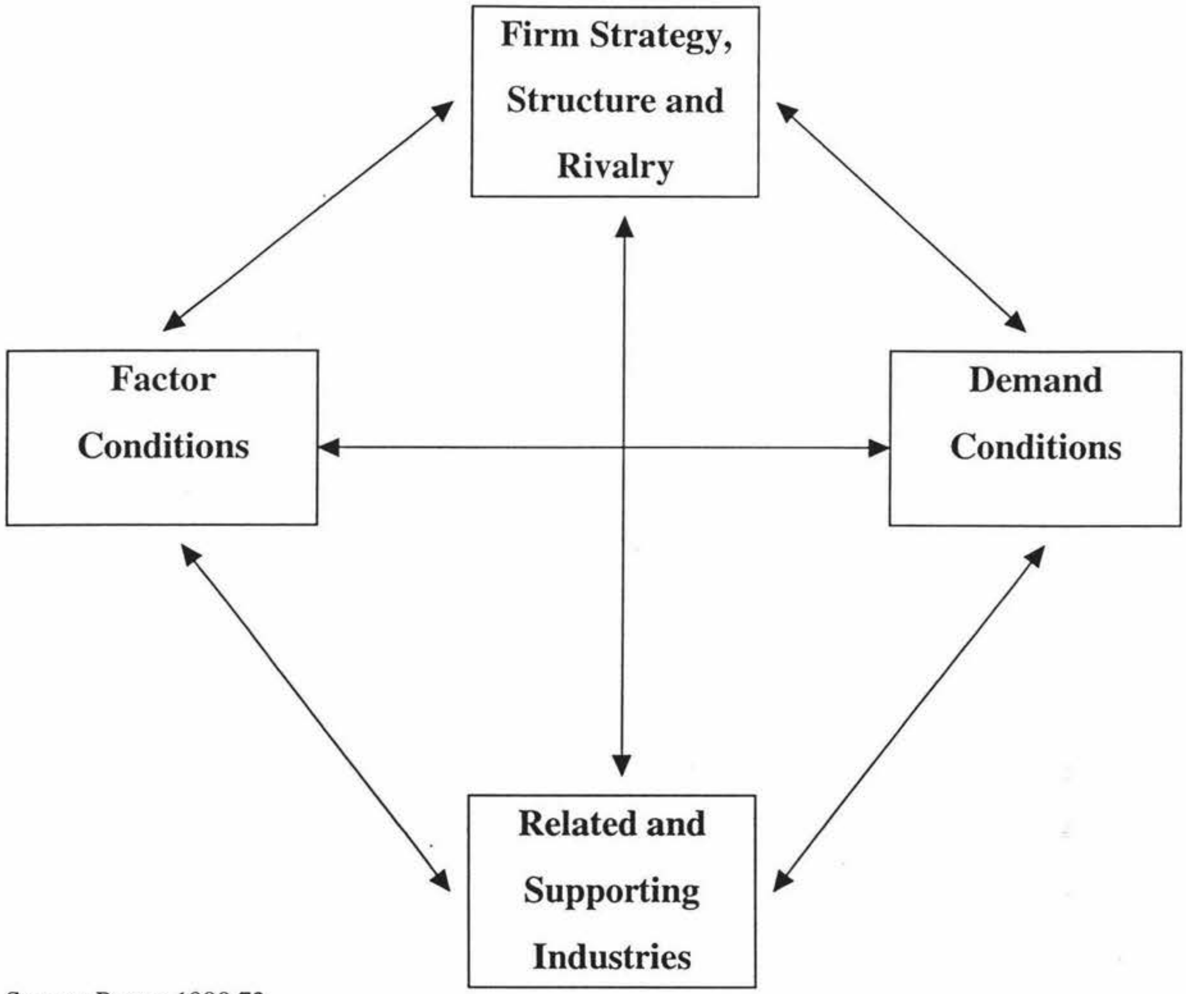
The number of transnational corporations in the world's fourteen richest countries has more than tripled over the past twenty five years, from seven thousand in 1969 to twenty four thousand in 1994. The world now boasts a total of thirty seven thousand transnational companies, which control about a third of all private sector assets and enjoy world sales of about $5.5 trillion - slightly less than America's GDP in 1993 (*The Economist*, July 30 1994).

To be successful in international trade a nation has to have a sustained competitive advantage in a particular industry. Five determinants of national advantage have been put forward, and briefly they are as follows (Porter, 1990:71):

1. **Factor conditions**, such as the skill of the labour force, infrastructure (roads, ports, etc.) and other factors of production required to remain successfully in business.
2. **Demand conditions**. The level of demand in the home country for the product. This is important as the home market will be used to perfect the good or service before exporting it.
3. **Related and supporting industries**. In some industries, where competitive advantage exists in a supplying / related industry in the value chain. An example of this is where New Zealand's competitive advantage in agronomy has been passed on to successful food processing industries.
4. **A firm's strategy, structure, and rivalry.** Success of a business trading in the international arena is similar to that of a company operating in the domestic environment except that the complexities of the international market place are greater. The appropriate strategy, structure and understanding of competitors is even greater in the international arena.

All these factors interrelate and determine an industry's competitive advantage as shown in Figure 2.1. Competitive advantage is, however, a dynamic force and requires constant vigilance to retain. Car manufacturers in the US did not view the small car as commercially viable and lost both their advantage and market to Japan who became the world's leading car manufacturer.

Figure 2.1: Michael Porter's framework



Source: Porter, 1990:72

Jarillo and Stevenson (1991), present us with an article that allows an analogy between firms and countries, where competitive advantage is based on co-operative advantage. The authors believe we must use competitors as allies by *working co-operatively rather than in competition.*

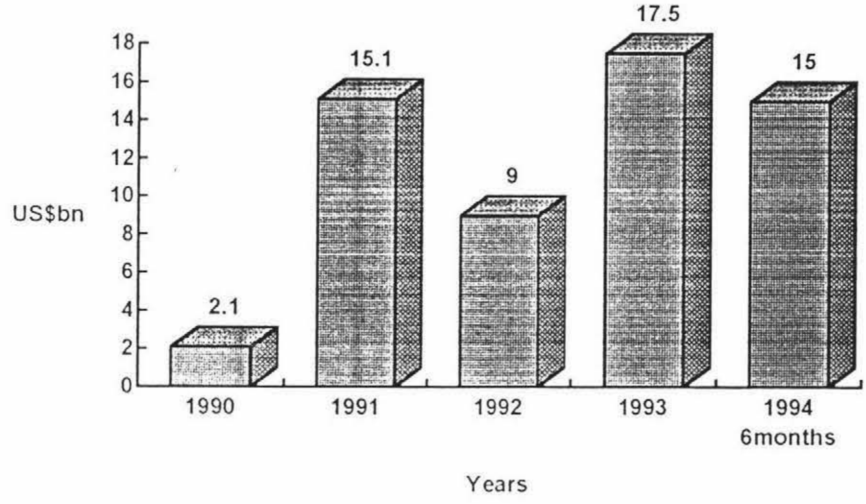
Firms (and countries) must concentrate on existing or developing competencies, while seeking to attain efficiencies from other firms. One way of achieving this, common to firms and countries, would be through strategic alliances. Such efficiencies might be in the form of lower costs, economies of scale, access to scarce resources, technology, intellectual property or passage through red tape. Successful examples are Compaq who competed with IBM but worked co-operatively with others in the industry, and Benetton who operated in a mature apparel industry and in a very hostile economic environment (expensive and unionised Italian labour), and sub-contracted 95 per cent of its activities. Both examples emphasise strong co-ordination with associates.

INVESTOR INVOLVEMENT

Only 15 years ago, equity investors and investment fund managers had minimal numbers of overseas investments in their portfolios. Like the corporations that have latticed the Asia Pacific region, so now investors with their funds have completed the interdependence of nations by taking it down to personal levels. One can argue that should an American's superannuation be dependent on, say, Japanese, Australian or Malaysian stock prices, there will be more than a little goodwill and concern shown to the welfare and security of those nations.

The amount of money crossing boundaries is increasing year by year. 'The long term trend of steadily rising investment in Asia appears irreversible, according to interviews with two dozen investors large and small across America' (Holloway, 1995). Overall, American investors made net purchases of US$31.3 billion of equities in Asia in the 18 months to June 1994 (See Figure 5.2).

Figure 2.2: Net Purchases of Asian Stocks by US investors, 1990-94 (US$bil)



Source: Nigel Holloway, *Far East Economic Review*, 12 Jauary 1995, 68.

INTERNATIONAL BUSINESS

Businesses are international when they trade in both domestic and overseas markets where a large percentage of foreign produced goods compete with the locally produced goods, providing the consumer choice of selection. The standard of living in most countries is based on products produced domestically and those for overseas, for example, the United States which is the world's largest single market. The list below shows the percentage of overseas products in the total US market.

Automobiles	44.3%
Apparel	36.8%
Footwear (non-rubber)	77.0%
TV and video cameras	72.0%
Telephone instruments	75.0%
Videotape recorders	99.0%

Source: *Sakach*, 1989

Many of the world's largest industries have set up international processing plants in the US. The automobile industry is one of them. Originally, Henry Ford built a 100 per cent American-made automobile in America and by 1940 it was the world's largest industrial complex. Now the industry's strategic plan is to increase their competitiveness by spreading their business internationally. So today car assembly plants are located all over the world and components are manufactured in the cheapest producing country. Ford's Festiva was designed in the United States, engineered by Mazda in Japan, and is being built in Korea principally for the American market. The Ford Escort was designed by Ford of Europe and Ford of North America, built in six countries and sold in more than 30 countries (Sakach, 1989).

World trade is profitable for all those who consider the world as their market place. From a nations' point of view, the revenue from sale of products or services to overseas markets is a preferred option to revenue from sales in its domestic market: foreign sales earn hard currency. Hard currency saving is vital to any country's prosperity and standard of living.

From a corporate point of view, high profit margins are a significant incentive to participate in global business. Table 2.1 illustrates the profit some world famous companies have generated on investments abroad and from overseas sales. In fact, sales in foreign markets are often better than in the domestic market.

Table 2. 1 Company profits generated abroad

Company	Foreign earning as % of total	Foreign Assets as % of total
IBM	60.7	52.2
General Motors Corp	30.3	29.2
Ford Motor Company	36.7	31.8
Eastman Kodak	43.6	29.5
Coca-Cola Company	61.2	40.0
McDonalds Corporation	41.7	43.2
Avon Products Inc.	55.9	39.9

Source: *Forbes*, 22 July 1991, 287.

INTERNATIONAL CAPITAL MARKETS

As mentioned before, people are moving in greater numbers from country to country to obtain better jobs and pay. Businesses (include products and services) are expanding internationally to achieve better economic results. This results in mobility of capital, for example, when General Motors planned to invest $10,000 in the production of a new car; $3,000 went to South Korea for labour and assembly; $1,850 to Japan for the engine, and electronics; $700 to Germany for design engineering; $400 to Taiwan, Singapore and Japan for small components; $250 to Britain for advertising and marketing services; $50 to Ireland and Barbados for data processing; $4,000 went to strategists in Detroit, lawyers and bankers in New York, lobbyists in Washington, insurance and health care workers around the world and to General Motors shareholders (Seich, 1991).

The majority of international investments are cross investments. The United States received a total of $355 billion direct investment from foreign investors in 1992 made up of: the United Kingdom $120.5 billion; Japan $83 billion; Northlands $64 billion; Canada $31.4 billion; and Germany $27.4 billion (Schlender, 1992). At the same time there is a reciprocal flow from the United States. Statistics in the United Nations Conference on Trade and Development (UNCTAD) report in 1994 show that during 1993 United States investors placed $50 billion, British $26 billion, German $17 billion and Japanese $12 billion in foreign affiliates. International investment in trade is a positive factor in promoting a global economy.

The Japanese have used cross investments as part of their corporate culture for sometime. The model of co-operation is the *Keiretsu* where firms with associated cross shareholdings form a group to work together for the sharing of resources. Such associations are seen as having long-term benefit to all parties and support group thinking.

PROTECTIONISM

With the ease of efficient transportation methods across the globe, the availability of more efficiently produced and therefore cheaper goods (primarily through decreased labour costs) leads to increased competition for markets. Given two identical items, consumers will normally choose the cheaper one (or the item that is of greatest value to them) in order to maximise their utility. To stem this tide, governments use protectionist measures to shield their domestic industries from foreign competition.

Governments are often obliged to bring in protectionist measures to remain in power (unhappy voters are votes to the opposition) and avoid social unrest generally as people view their livelihoods being threatened. More often than not, those individuals or groups coming under threat form a noisy vocal minority, while the rest of the population and the nation as a whole, who would benefit from cheaper imports, are not united and therefore too often silent.

Protectionist measures are inherently selfish and when used in times of unemployment can lessen its economic effects. Fiscal and monetary policy would have the same effect but without the 'beggar my neighbour' policy (Samuelson and Nordhaus, 1995:695). The introduction of protectionist measures in one country affects other nations as well as those who relied on that trade and therefore have to find new markets - this was the situation for New Zealand and Australia when the United Kingdom joined the EEC.

The reality of free trade theory is based on assumptions of static conditions of perfect competition, full employment, full production and immobility of capital, labour and technology that do not accurately reflect conditions that may exist in the global economy. It is this weakness in the free trade debate that is used by protectionists to justify trade restrictions being placed to protect jobs, to maintain living standards and to protect infant industries. In addition, non-economic arguments of national security, social and cultural reasons are advanced.

TARIFFS AND QUOTAS

For centuries, countries, have interfered with the flow of trade between one another and have erected barriers which result in trade obstacles. The major instruments used are the imposition of tariffs on imports, payments of subsidies to producers, import licensing or a mixture of all three. The use of these instruments can lead to distortions in world trade, depending on the size of the levying country, and can create barriers which effectively destroy any efficiency gains which had resulted from a country's comparative advantage.

While the Law of Comparative Advantage is an accepted standard in free trade, all countries produce certain goods which put them at a relative disadvantage. The disadvantage lies in goods themselves, in the fact that the countries could import those goods for a cheaper price or for less work than if they continued to manufacture them. The situation with Japanese and French farmers who require heavy subsidies and tariffs placed on foreign goods to make their farming operations commercially viable is an example of this. Japan has a 737 per cent value gap between the cost of domestic production and the cost of importing rice (Holloway, 1994b:49). To protect these inefficient industries from international competition nations set-up protectionist measures in the form of tariffs, quotas and other trade barrier permutations. These protectionist measures are economically inefficient in that '...the economic loss to consumers exceeds the revenue gained by the government plus the extra profits earned by the producers' (Samuelson, and Nordhaus 1995:692). In layman's terms this means that the subsidies given to the Australian shipbuilding industry or Japanese rice farmers could be more efficiently allocated to improve roads or build a new hospital; the money for the subsidy would benefit a greater proportion of the nation's population rather than a specific group.

Tariffs once in place may be inflexible and difficult to alter. The longer the tariff is in place the harder it is to remove. The result is reduced competitiveness in the domestic sector, misallocated resources, and higher domestic profits. Tariffs may encourage higher returns in one area than others, and as a result resources shift from competitive areas to the protected area to take advantage of these high returns. The siphoning off of these competitive resources can lead to a deterioration in the balance of payments or in incomes, which can be mistaken for a need to implement further controls.

The primary objectives of licensing, on the other hand, are first to help conserve foreign exchange and to assist the balance of payments. The second reason is to protect domestic industry from foreign competition and to encourage the promotion and diversification of import substitution. Import licensing is seen as a means of influencing the mixture of imports away from finished goods to raw materials and capital goods, of reducing the import of luxury goods to essentials, of encouraging and deterring imports from selected foreign trading nations, and of encouraging the establishment of specified industries.

Licensing system, however, may lead to distortion in market forces. The licensing system is designed to regulate the total volume and composition of imports and not to influence the demand for imports directly. If demand for certain types of imports is high and supply low, then higher prices are paid for available imports, causing inflation to rise. Consumers suffer as they are forced to pay higher prices while licenses holders receive higher profits. The consumers also suffer as the range and quality of products available is limited.

Import licensing does not always address the balance of payments problems, one of the reason for its existence. Imports may have been reduced but excess demand still remains and moves into non-licensed imports or into domestic output which is often import dependent. A further side effect is that import substitution industries are set-up, which may be inefficient or which rely on imports thereby negating any balance of payments savings. Furthermore, the licensing system is cumbersome and costly. Licensing on imports is not always issued according to industry needs because the nature, type and quantity changes rapidly as external and internal forces change.

As tariffs and the licensing system are set up to assist balance of payments problems, to encourage import substitution industries and to assist domestic industries and employment there appear to be no major differences between the two policies. Major differences do occur, however. Tariffs are set because of perceived or desirable levels of protection for a certain industry sector. This enables the industry to make some sort of adjustment. Import licensing predetermines the volume which is allowed to be imported and therefore limits the amount of flexibility of the industry sector. The distortionary effect of licenses is therefore greater: not only is volume controlled but prices are distorted even further than through the imposition of a tariff.

THE WORLD TRADE ORGANISATION (WTO)

After the Second World War, world trade was reorganised through the General Agreement on Tariffs and Trade (GATT). The main purpose of GATT was trade liberalisation, fair trading, the reduction of trade barriers and the promotion of trade across national borders. GATT was to be a transitional organisation until a formal world trade organisation could be established according to 'The Charter of Hawaii'. Initially GATT was signed by 23 nations on 13 October 1947 and became effective on 1 January 1948.

The Uruguay Round was the eighth round since the first in 1947. There were 116 participants in the last Round and the talks spanned a total of seven years. The Round set out to achieve: further cuts in tariffs; institutional reform within GATT; the removal of damaging exceptions to GATTs universal coverage of goods; and the introduction of new items such as intellectual property to make the agreement more relevant. The General Agreement on Trade in Services (GATS) which was negotiated as part of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) and the NAFTA. Services are the largest growing sector of the US economy. Passenger fares, royalties on American movies, banking, education, fees

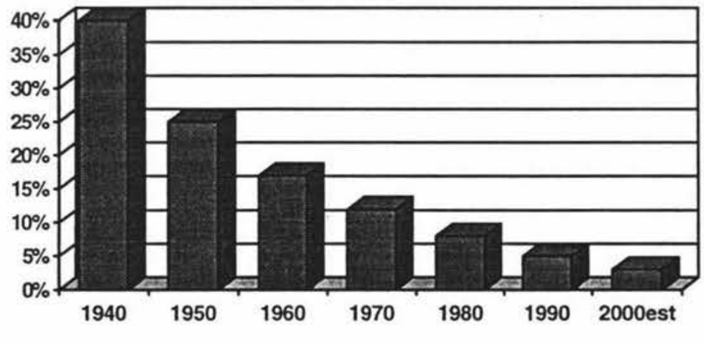
Figure 2.3: WTO Timeline

GATT	Signed at Geneva on 30 September 1947 by 23 countries. These countries accounted for four-fifths of world trade.
Kennedy Round	1964 - 1967. 54 countries participated. As economic integration of western Europe progressed, US was concerned at the prospects of remaining outside. Under the Trade Expansion Act of 1962, US secured tariff reductions of up to 50 per cent, subject to reciprocal concessions from the European partners. This led to the Kennedy round. *Significant outcomes*: * Moved away from item-by-item bargaining on tariff reduction to progressive reduction. * Agricultural products were added (in addition to) to industrial products in the scope of the negotiations. * Discussions on non-tariff obstacles included. * Non-reciprocity for economically less-developed countries.
Tokyo Round	1973 - 1979. 102 countries participated. *Significant outcomes*: * Series of tariff reductions over an eight-year period beginning 1980. * Code on Subsidies and Countervailing Duties negotiated.
Uruguay Round	1973 - 1979. 102 countries participated. *Significant outcomes*: * More open and fair trading conditions for agriculture. * Quota restrictions on textiles and clothings to be progressively phased out. * Reduced tariff barriers on industrial goods. * Multilateral trade rules for trade in services: trade related intellectual property rights (TRIPS) and trade related investment mass (TRIMS). * Improved trade rules controlling the use of subsidies and countervailing duties, anti-dumping and safeguards. * Procedures for settling international trade disputes to be reformed. * A framework for further trade liberalisation to be negotiated in such areas as movement of persons, telecommunication and financial services. * A work programme for the WTO to develop rules in such areas as trade and the environment and international competition policy.

for managing complex construction projects, telecommunications, insurance and other services provide substantial income to US businesses from foreign consumers. In 1991, services represented 25 per cent of the GNP (as opposed to 48 per cent for goods). Furthermore, 78 per cent of US citizens are employed in providing services, whereas only 22 per cent are employed in the manufacture of goods, according to the Coalition of Service Industries Inc. in Washington, DC. Three of the major rounds of GATT are described in Figure 2.3 WTO Timeline.

On January 1, 1995 the World Trade Organisation (WTO) was instituted at the conclusion of the Uruguay GATT round. The WTO is a permanent organisation that will continue the functions of GATT in promoting international trade. One hundred and twenty three countries have joined WTO representing 80 per cent of total world trade (Sutherland, 1994b:64). The success of GATT rounds in the reduction of tariffs in industrialised nations is illustrated in Figure 2.4.

Figure 2.4: GATT Round and tariff reduction in industrial nations



Source: Sutherland 1994b.

WTO / GATT is significant to world trade as 80 per cent of trade is conducted by and between member nations. It achieves this co-operation by removal of barriers, and enforcement via retaliation. The aim of WTO is to liberalise world trade through the reduction of tariffs and through eliminating other non-tariff trade barriers.

The main WTO principles are:

1 Trade without discrimination - embodied in the 'most favoured nation' clause.

2 Protection through tariffs - rather less transparent means such as quotas and import licensing.

3 Tariffs to be bound at levels negotiated between members - they can be increased only if compensation offered by importing country.

4 Consultations on the basis of equality - any country, regardless of size, can use the WTO dispute settlement procedures.

GATT maintained a stable environment for the conduct of international trade from its establishment in 1947 through to the early 1970s. During this time tariffs were reduced and most trade problems were addressed as they arose. This was achieved under the umbrella of a dominant US and its ideology of a free world economy in the post-war period.

As America's hegemonic power was eroded, however, the issues facing GATT became more complex. In the 1980s and especially the 1990s, world trade patterns have changed. Some of the traditional problems of GATT which had not been earlier solved, such as trade in agricultural products and textiles, have become more urgent; and a whole range of new issues such as trade in services and intellectual property rights present a challenging task for international negotiators.

GATT was not without its critics. Such moves to globalisation have belittled the role of governments in establishing economic policies. The traditional social welfare policies of European nations are being underscored as competition forces job cuts and decreased wages (Harbrecht, 1994).

The quintessential principle of GATT was that discrimination harmed trade. In the years between 1950 and 1975 the volume of world trade expanded five-fold and the world economy more than doubled in size. This has slowed since, and the Uruguay Round of was challenged with the task of getting this growth in trade back on target.

The GATT was an international agreement which aimed through multilateral negotiations to reduce barriers to trade. This was to be achieved through three basic principles: non-discrimination in trade through unconditional most-favoured-nation (MFN) clauses; the reduction of tariffs; and the elimination of import quotas. Trade negotiation rounds, which average about five years, are important in that countries from the developed and the developing countries seek trade guarantees and concessions for the period until the next round. The Uruguay Round, though completed successfully in December 1994, was riddled with problems.

Since the conclusion of the Tokyo Round the GATT system has been buffeted, in developed and developing countries alike, by strong protectionist pressures generated by the second oil shock, global recession, debt crises, and massive trade imbalances. Difficulties in dealing with these problems led to allegations that the multilateral process with its broad membership and agenda was too slow and complex. These perceived weaknesses in the GATT system, coupled with the reluctance of many countries until 1986 to engage in new multilateral negotiations, led both the United States and the EU to deploy unilateral measures (such as US Section 301 and anti-dumping actions).

The US, once the most 'pro liberal' trading nation, become more and more inclined to exercise bilateralism. The US has been seeking market access for its products by forcing its 'partner' countries to change their policies and become more 'open' (to US products). If 'partners' fail to respond to US requests they face retaliation. This US bilateral approach puts the decision in the hands of a single power, acting as both judge and prosecutor, rather than in a multilateral process.

Actually, the emerging regional blocs like NAFTA and EU could be more damaging to the WTO framework. An economic union, or free trade area, which creates the regional entities, was an acceptable exception to the rules of GATT when it was signed in 1947. Now Japan and other Asian countries have enough reasons to fret about the possibility of being shut out by these blocs.

On the other hand, the WTO / GATT is still held in great respect in most corners of the world, and is considered, even with its present limitations, to be a valuable forum. The best evidence for this is the on-going procession of new members into the WTO: more than a dozen countries (including Mexico) have joined in the last decade and new requests for membership have come from Venezuela, China, Taiwan, Russia and Bulgaria.

The WTO's future is being threatened as problems build and reduce its ability to function. Countries like the US are looking at multilateral regional trade to solve their problems. Regional trade blocs have been set up, one after another - are all these acting against the spirit of WTO, and do they present potential threat to free international trade?

One of the common characteristics of trading blocs is internal trade liberalisation but external trade protection. That is, internal barriers are removed but duties and restrictions on imports from non-members are kept. That will induce discrimination against outside exports. Obviously, a fall in non-member's exports to members is the main negative effect of a trading bloc. Consequently, the discriminatory arrangements of regional trading blocs causes the replacement of non-members' exports to members by intra-regional trade. In addition, as the economic size of trading blocs increase, the members' supply increases, the non-members' exports then will decrease and the terms of trade with non-members will be unfavourable.

REGIONALISM AND MULTILATERALISM

To address the key issues involved in global realignment it is useful to have a framework within which the issues can be defined and commented on in relation to world events.

Given the value of trade to a country's economic growth, what then explains the phenomenon of global realignment towards three massive regional trading blocs? There has been significant debate in the literature which attempts to address the question of whether regional trading blocs are a better route to global free trade than multilateral trade negotiations. Regionalism has been discussed in the light of its current revival, whether it is more durable this time around, and whether it is an instrument for promoting world free trade rather than one to replace it. The endurance and likely further development of the European Union has been key to the world dividing into three major trading regions, and there is much debate as to what impact these developments are likely to have on the welfare of the world generally and on individual participants in particular.

Regionalism: Trade creation or trade diversion

Two of the key questions which can be asked are: (1) Does regional integration increase or decrease global economic welfare?, and (2) will regional trading blocs lead to global trade more quickly than the multilateral process? Viner (1950) provided a traditional answer to this by introducing the concepts of 'trade creation' and 'trade diversion'. He argued that a regional free-trade area improves global welfare only if it creates more trade than it diverts. Consider the US and Mexico, for instance, in which each applies tariffs on imports from all other countries. With the formation of NAFTA, where US and Mexico enjoy free trade relations along with Canada - eliminating trade restrictions between them but maintaining tariffs on imports from the rest of the world - to what extent is this a change for the better? Using the footwear industry as an example, if the US begins to import shoes from Mexico, having previously made all its own footwear, then the free trade area has shifted production to a cheaper source of one factor input, namely labour. Trade has been created inside the free trade area with no fall in trade with the rest of the world, and as a consequence global welfare increases. If, however, the US originally imported shoes from South Korea, which produces shoes more cheaply than either the US or Mexico, then the increased trade between the partners has been at the expense of more efficient trade with South Korea. This is trade diversion, and the welfare of the free trade area and the world declines (de Melo and Panagariya, 1992). In this example, if trade creation is accompanied by no change in trade with the rest of the world and increased trade between partners, then the world as a whole has moved closer to free trade. By contrast, trade diversion is accompanied by increased trade within the free trade area at the expense of trade with the rest of the world. National protection is extended to the regional level and the world as a whole moves away from free trade. There are those who argue that regionalism is trade-creating and therefore positive, while others argue that it is destructive to the world trading system as a whole.

The second coming of regionalism

As previously noted, regionalism is back in fashion as countries fear being shut out of markets such as the European Union. The 'first regionalism' failed in the 1960s. It failed principally because the US was firmly committed to the multilateral approach and did not endorse the regional approach with the exception of the then European Community.

The main driving force behind the resurgence of regionalism can be attributed to a change in attitude by the US, notwithstanding that Washington professes commitment to multilateralism. In this respect the US used NAFTA as a spur to bring recalcitrant parties back to the GATT negotiating table. However, Bhagwati (1992) argued that the United States' decision to follow a regional approach tilts the balance of forces away from multilateralism to regionalism.

Bhagwati proposes several reasons to argue that the 'second regionalism' is here to stay:

- Regionalism has been presented as a complementary alternative to multilateralism;
- Regionalism has been used as an accelerant to multilateral process;
- The prolongation of the Uruguay round has caused some to argue that regionalism works faster than multilateral negotiations;
- Strong non-economic, political and cultural factors are influencing the development of regional trading blocs;
- Issues surrounding the management of debt and the economic assistance provided to South American nations have caused the US to respond regionally to protect its banks;
- The integration of Eastern Europe into the European Union created the fear that European investments could be diverted to Eastern Europe. President Salinas of Mexico stated that this was a critical factor which drove him toward the Mexico-US free trade area, as this would allow Mexico access to the investment it needed;
- There is now a significant shift in economic thinking towards trade liberalisation and market forces. The macroeconomic crisis of the 1980s led to microeconomic reforms and consequently more countries are responding positively to the prospect of free trading agreements.

Finally, of key importance to the resurgence of regionalism was 'Europe 1992' and the US-Canada FTA which caused other countries, particularly in Asia, to see that regionalism was inevitable and that they needed to establish their own trading bloc.

Controls on Regionalism

There are counter-arguments to the resurgence of regionalism. However, given the reasons for regionalism's endurance then what can be done to ensure that it does not damage progress towards global free trade?

There are possibly some approaches which could be successful in achieving this. One could be through the evolution of GATT to the WTO and its perceived strengthened status as a body to adjudicate on world trade issues. A second could be through the strengthening of two key WTO rules. The first is that only free trade areas which set a common external tariff at the lowest tariff of any member before the union was formed should be allowed. The current rule simply says that tariffs must be no higher than average. The second is that rules on anti-dumping actions and voluntary export restraints (VERs) could be changed. These anti-trade activities have increased in recent years as tariffs have fallen, and they risk making integration a route to protectionism.

OPEN REGIONALISM

Open regionalism, fostered by APEC, addresses the need for a collective promotion of stronger initiatives towards a freer flow of goods, services, capital, and technology among the Asia-Pacific economies and through common positions in the deliberations of multilateral institutions in the region. The definition of 'open regionalism', as stated in the San Francisco Declaration of the PECC 9th General Meeting in 1992, is regional economic integration within the region and open trade with the outside world on mutually agreed trade policies.

The following trade guidelines are applicable (Cheit, 1992:122):

1. Economies must increasingly remove barriers to trade, investment and technology flows;
2. GATT disciplines must be applied to trade and investment;
3. The region must provide commercial access to economies elsewhere and seek to ensure that these economies likewise provide commercial access on a non-discriminatory basis;
4. Liberalising sub-regional trading arrangements within the region must be accommodated; and
5. To maintain momentum, the region must actively promote policies that strengthen this dynamic process.

From one point of view, the EU, NAFTA and APEC belong to regional economic integration. Although all of them seek to promote trade liberalisation and to strengthen economic co-operation in their region, APEC should be distinguished from the EU and NAFTA in that it is non-discriminatory and open to third nation trade based on mutual and reciprocal trade arrangements. The EU and NAFTA are trading blocs, APEC is not. Both the EU and NAFTA are involved in discrimination against non-member countries through to external trade protection. They remove barriers from member countries but may create more barriers for non-members. On the other hand, APEC is formed on a non-discriminatory basis and invites outside nations to trade with APEC on similar trade arrangements.

THE EFFECT OF COMPETITION

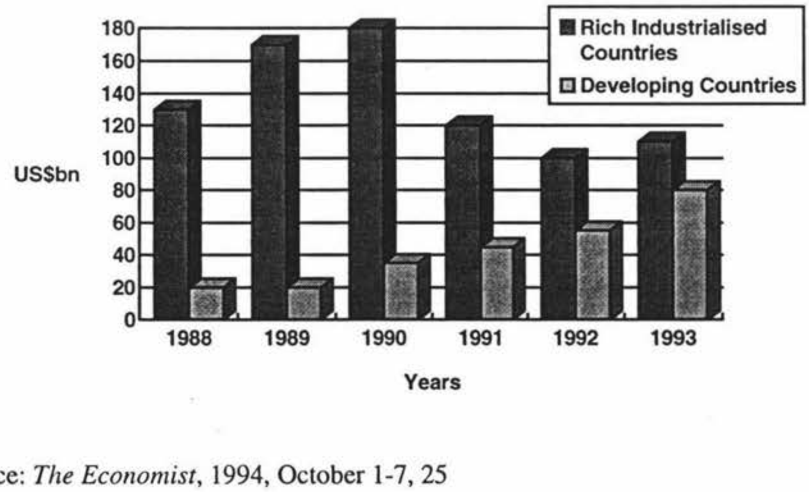
As mentioned earlier, one primary effect of competition in international business, is that economic competition has taken over from military might. Second, the economic engine moved eastwards from Europe (where it was at the beginning of the century) to the US after World War I and now to East Asia since the 1980s. The 'powerhouse' is presently in Japan, but should (or rather when) the two giants of China and India move into their next growth phase, the 'engine' of economic growth may move farther East.

The migration of economic power will affect a number of factors that are inherent to the growth of Western economies. These factors are discussed below.

MIGRATION OF RESOURCES

While many workers fear cheap imports as a threat to their livelihood, the migration of investment to growth areas with a cheap labour force is perhaps a greater threat. The deregulation of investment in countries like China, and in the South East Asian region in general, has caused billions of First World investment dollars to flow into those countries. Previously, these investments would have stayed in the developed world (Figure 2.4 and Table 2.2).

Figure 2.5: Inflows of Foreign Direct Investment



Source: *The Economist*, 1994, October 1-7, 25

Table 2.2: Recipient of FDI

Recipient of Foreign Direct Investment (FDI) Ten largest, Developing Countries	
Countries	**1988-92, $US billion**
China	25.6
Singapore	21.7
Mexico	18.4
Malaysia	13.2
Argentina	10.6
Thailand	9.5
Hong Kong	7.9
Brazil	7.6
Taiwan	6.0
Indonesia	5.6

Source: *The Economist*, 1994, October 1-7:25

The effect of this migration is that there are fewer investment dollars to finance growth, new businesses and therefore jobs in the developed world. The migration also involves human as well as raw resources as both will be attracted to areas of economic growth. This was evident in New Zealand's economic down-turn in the 1970s and 1980s in the form of a 'brain drain' of skilled workers leaving permanently. Singapore, which is in an enviable economic state at present, complained of brain drain to Australia in the 1960s and 1970s for similar reasons.

Much of this investment and industry shifting is geared toward low skilled, labour intensive industries such as manufacturing, electronics, textiles and leather goods. However, as capital costs, R & D and marketing costs increase in importance, the competitive advantage of low wages is eroded. As a result, the mass exodus of investment on a disastrous scale is likely to taper off. With twentieth century technology making the world smaller, it is possible for multinational businesses to do their manufacturing in Malaysia, designing in Italy and advertising in Britain. All that is likely to occur is a redistribution of the world's investment capital to areas with the most competitive advantage for that industry or process. Hence, industries will place increasing importance on gaining and maintaining their competitive advantage in areas where their manufacturing takes place, as well as the areas where their markets are.

INFLATIONARY EFFECTS

Increased demand for goods and capital may cause an increase in inflation in the global market. As sustained economic growth is fuelled by investment capital, increased demand will cause interest rates to rise, resulting in inflation. Once demand for capital investment exceeds the supply of domestic savings the excess demand must be obtained by overseas lending. Increased interest rates, while increasing domestic savings, will choke off investments that are unable to service the high cost of investment capital. As a result, there is a high risk that potentially successful businesses never get off the ground. Equally, the rising demand for raw materials and for energy to fuel the current round of global growth will also have an inflationary effect.

On a positive note, increased competition through current trade agreements has the effect of allowing western countries easier access to countries with billions of potential customers in the fast growing Asian economies. The proportion of industrialised nations' exports in the form of capital, consumer goods and services heading to the East continues to grow with increasing demand from fast developing East Asian economies. For example, Western Europe exports twice as much to the developing countries of East Asia as it does to North America and Japan together.

This increasing demand for goods and services by developing countries will in turn assist the growth of developed nations through:

- **Improved terms of trade.** By importing consumer goods from developing countries, both nations benefit: the developing nations through the growth of a domestic industry and the rich nation through cheaper imports. Clothing prices in the US have fallen by 20 per cent in real terms over the past ten years as a result of cheaper imports. Undoubtedly, the local US clothing industry will have suffered. However, as stated earlier, the use of protectionism for inefficient industries causes externalities in the economy and costs more in the long term than the short term benefit of keeping people in jobs.
- **Competition.** Increased competition from the developing nations encourages rich economies to become more productive and efficient themselves, thus speeding up their own growth.
- **Economies of scale.** Allowing access to larger world markets increases the ability of industries to exploit economies of scale by spreading the costs over a wider field. The increased revenues could be used in more research and development to make the industry even more competitive.
- **Financial diversification.** The increasing growth of developing nations will attract further investment in those countries from rich economies. The resulting decrease in poverty will increase the political and social stability of those countries. This, combined with the higher investment returns available in the fast growing developing nations, will be of benefit to all.

Not all the effects of increased international competition will be beneficial, and there will be casualties. National competition and resultant global realignment will affect a country's aggregate or total income. The growth of developing economies for the industrialised nations is strongly beneficial, as we have indicated. However, the effect of this growth on individual jobs and wages in the industrialised economies is less obvious. Fierce competition from developing countries will force some firms to close down, throwing workers out of employment. Although new jobs will be created in export industries to offset this, unemployment could rise, at least in the short-term. The burden will fall most heavily on traditional, overwhelmingly male, low-skilled workers.

FREE TRADE / FAIR TRADE

Following from the notion of the Law of Comparative Advantage, nations that engage in free trade are termed open economies, while those that do not are termed closed economies. However, no country in the world is totally closed or totally open, though an area exists between the two extremes where a country may be open for trade in some products but not in others. Japan is an example of a fairly closed economy where vast arrays of import regulations and rules make life difficult for businesses wishing to export certain goods to Japan. An example of this is the difficulty of exporting rice to Japan; textiles, however, may come and go freely.

The rationale behind free trade is that:

- Nations are linked to the economies of their trading partners.
- Competitive advantage is gained through specialisation and economies of scale.
- Greater research and development opportunities are available.
- Access to wider capital markets is available.

The recent Uruguay GATT Round brought increasing bewilderment to member nations as to the fairness of GATT. Nations that had lowered their trade barriers faster than others gained more from GATT than those that did not. Apart from that, nations were able (under pressure from industry lobbyists) to impose non-tariff barriers that, while permissible under GATT agreements, were contrary to their spirit. Research undertaken by the World Bank has found that in the industries they examined (clothing, steel, cars and textile), non-tariff barriers were equal to a tariff of 24 per cent. While these protectionist measures saved 294,000 jobs in those industries, the cost to the economy was US$72,000 per worker per year (*The Economist*, 4-10 December, 1993:26).

In the area of international trade there is an increasing discussion about fair trade rather than free trade. Maurice Allais, the Nobel prize winner for economics in 1988, claimed that free trade with developing countries would lead to mass unemployment and huge wage inequalities as production and jobs shifted to low income countries, either due to a surge in imports or to a massive migration of firms to these countries (*The Economist*, 1-7 October, 1994:5). The result, he added, would be social explosion in the West, and the way to avoid it would be to erect import controls to keep out third world competition.

However, with their increased wealth, the developing nations, while providing the West with more competition for certain markets, will also provide a huge customer base for imported goods due to their population and insatiable appetite for Western manufactured goods. Therefore, western fears of a third-world take-over are unfounded.

CONCLUSION

The free trade versus protectionism debate is one that will never be fully resolved. Supporters of free trade maintain that trade liberalisation not only raises the wealth of individual countries, but improves the national income of the world as a whole. This liberalisation can only occur when protective barriers are removed, nations compete fairly and adhere to the principles of comparative advantage. Opponents of free trade believe that economic theory is not realistic, that trade liberalisation only benefits a few nations, and that restrictions are required to maintain living standards.

In 1947 the GATT Agreement was signed. This agreement sought to liberalise trade between nations and to provide the mechanism where this can be achieved. Failures inherent in the original agreement have led to further negotiations, but the apparent reluctance of many countries to adhere to trade liberalisation has led to the exploitation of existing loopholes and an apparent lack of will to free up trade. The success of the Uruguay Round may be the first step towards returning to the original philosophy of the 1947 agreement; and the establishment of the World Trade Organisation in 1994 is a step in this direction.

As the world settles into a new economic orbit caused by the shift in economic power eastwards, the ensuring scramble to retain past economic positions will cause nations to seek new alliances with those that can assure them of their own continued prosperity. This will lead to a trend toward global co-ordination in trade. The new concept of open regionalism is a step forward towards this.

While global realignment is viewed mainly as inter country, it could also be inter firm, allowing firms as well as countries access to economies of scale and learning as well as access to markets, technology or a government's requirement for local ownership. Porter (1990:66) states 'Alliances are frequently transitional devices. They proliferate in industries undergoing structural change or escalating competition, where managers fear they cannot cope'. While this quote relates to individual firms, it may equally apply to nations and governments facing political and economic crises.

Mature domestic industries are forcing companies to look offshore for new markets, thus creating a new global competitiveness that is independent of national borders. Global organisations such as IBM, McDonalds and Coca Cola are examples of this trend not only toward freedom of international trade, but also toward international investment.

The increased globalisation of trade and the realignment of trading alliances will also help to break down racial and cultural barriers that have existed for centuries as countries become more aware of each other and, via trade links, dissolve years of mistrust and suspicion.

PART II

ANALYSIS:

THE TRIPOLAR GLOBAL REALIGNMENT

The world is shaping into an economic three-way split between the Americas, Europe and Asia. This is unprecedented in world history as duality has been the main form of power balance. Indeed it appears that duality is the preferred means to establish global power base. This is seen with the US's attempt to having a 'finger in all pies' through its presence in APEC and in NAFTA, and also with the EU wanting to increase its presence in the Asian region. This suggests that Asia is the bargaining chip to be played for and that the major global payers (NAFTA and the EU) will vie for the spoils that Asia has to offer.

APEC seem to negate the natural constellation of nations within the Americas / Europe / Asia framework. To some extent this structure, as mentioned above, is imposed by Western interest in the Asia Pacific region, especially in the vast markets and opportunities in Asia, and by the urge to maintain the duality in the global balance of power.

In Part II the development and operations of the trade blocs, the EU, the NAFTA, and the APEC are discussed.

Chapter 3

The European Union

In the aftermath of World War II, Europe was in a shambles as a result of fighting and destruction. To assist rebuild the Europeans economies and to help encourage strong, friendly governments, the US Secretary of State, George Marshall, recommended that the United States, which had survived the war virtually unscathed, give aid to and work with the European countries in the process of reconstruction. Thus the Marshall Plan was born. The Plan was very successful due in large part to the Europeans willingness to work together. A milestone in this growing relationship was the Treaty of Rome which was signed in 1957 and came into effect on 1 January 1958. This treaty created the European Economic Community (EEC).

The present form, the European Union (EU) is part of a continuous evolutionary development from the inception of a customs union by the Benelux countries in 1948. The Union has expanded from a grouping of three nations attempting to maintain peace in a post-war Europe, to a major regional trading bloc aiming to reduce internal barriers while presenting a common front to the rest of the world.

This chapter examines whether the borders of Europe are truly vanishing, creating a single Europe, and whether phrases such as 'Frontier-Free Europe' and 'Europe without Borders' or 'Fortress Europe' reflect the European Union of the 1990s.

MAP OF THE EUROPEAN UNION AND NEIGHBOURING COUNTRIES

Current members

- Austria
- Belgium
- Denmark
- Finland
- France
- Germany
- Greece
- Holland
- Ireland
- Italy
- Luxembourg
- Portugal
- Spain
- Sweden
- United Kingdom

Prospective members

Norway	Bulgaria	Hungary	Cyprus
Switzerland	Czech Republic	Poland	Turkey
Iceland	Slovak Republic	Poland	Malta

INTRODUCTION

There is nothing new about the single European ideal. In the 19th century it was an inspiration for poets and romantics, only to be distorted by conquerors, who also had a single Europe in mind. This ideal did not receive full expression, in a practical form, until after the Second World War when a handful of courageous and visionary statesmen determined to put a stop to the loss of life that seemed to be the inevitable outcome of conflicts between nation states.

In recent years, the reunification of Germany, the end of the Cold War and the reordering of the European continent following the break-up of the Soviet bloc in 1991 have given added force to the ideal of European integration. The fall of the Berlin Wall in 1989 was an indication to the world economy that a new global order was about to take shape in Europe and the world generally.

It is becoming obvious that a European unification is in process and that this process is irreversible. Countries in Europe, once competing for resources both within and outside of Europe, are co-operating to create a European identity without national boundaries. This has become a fact of political and economic life influencing industrial strategies and altering the way in which Europe is perceived by the outside world. In direct contrast to European integration, is the alternative of returning to nationalism, insecurity and instability which nations in Europe wish to avoid.

The process of European integration started with the membership of the European Union growing from the six member countries of the original EEC, formed in 1958, to a present total of 15 countries. The goal of a united Europe, espoused at the end of World War II by French statesman Jacques Monnet, appears to be coming closer.

The abolition of internal frontiers and the establishment of the single market on 1 January 1993 has increased consumer choice, encouraged competition within the European Union and given the European economy the dimensions of a continental market (Urwin, 1995:242). There is, however, a danger that the economic recession and high levels of unemployment experienced by all EU countries will sow the seed of doubt in people's minds about the wisdom of opting for a united Europe. But faced with a crisis of structural adjustment, which calls into question the organisation and distribution of work in post-industrial societies, Europe has no choice but to pool its resources to improve its international competitiveness.

In 1995, Austria, Finland and Sweden, persuaded by the advantages of a united Europe, joined the Union. By the year 2000, a number of Eastern European countries will have revolutionised their economies to enable them also to become members of the European Union (Urwin, 1995). Those with only associate status are seeking to be admitted to full membership and the number of member countries could reach 25 with a total population of approximately 500 million people (*The Economist*, 1 October 1994:11). It will be a union based on geographical location rather than cultural similarity.

Further structural changes to the Union form and further steps towards political union needs support and commitment from all the countries in the Union. The Treaty on European Union, signed in Maastricht on 7 February 1992, provides answers to a number of questions Europeans have been asking about national identity, democratisation of the institutions and the respective roles of regional governments, national states and the Union (Bidwell, 1993). The next most important step in the evolution of European integration will be a single EU currency and monetary policy, after which internal borders will be of little significance. As discussed earlier, further expansion of the Union will take place. However before this happens, the Union needs to consolidate its position, its strength and its current status within existing membership. In particular, aspects of the Treaty on European Union, or, as it is more popularly known, the Maastricht Treaty may need to be reviewed in the light of its effectiveness thus far.

EUROPEAN HISTORY

The European Union has evolved from a number of initiatives by European countries after World War II to form alliances for mutual economic benefit. To understand the reasons for this evolution in Europe, it is useful to have some knowledge of recent European historical developments.

THE EUROPEAN ORDER OF 1815

The French Revolution, followed by the Napoleonic wars in the 1800s, changed the ideals and political forces within Europe. After the defeat of the French armies and the abdication of Napoleon in 1815 the grand monarchies of the time, Austria, Prussia, Russia, Britain and France reorganised the map of Europe at the Vienna Congress in 1814-15 (Thompson, 1966:84). A few weeks later Russia, Austria and Prussia formed an alliance to protect their common interests. This was the first attempt along modern lines to instigate a European system of joint security, and troops from this alliance were used to combat revolutions in Spain and Naples. Although the alliance helped create peace for several decades, it did not prevent conflicts such as the religious based Crimean War in 1853, the 'Seven Weeks' Austro-Prussian War of 1866 which precipitated a territorial dispute, and the Franco-Prussian War of 1870 seen as a necessity before the construction of a united Germany could be realised (Craig, 1971).

The Industrial Revolution and the advent of long distance transport and communication, made possible by railways and telegraph services, was instrumental in changing the face of Europe (Dale and Dale, 1992; Lane, 1978). The necessity for forming borders and administrative areas led to the birth of two new nations, Germany and Italy, and was followed by a period of intense imperialism. This began during the second half of the nineteenth century and led to rivalry and changing coalitions between countries. In addition, non-European powers such as Japan and the United States were beginning to enter the political arena. The possibility of a European war was becoming evident. During this period, several European treaties came into existence (Craig, 1971). These included the creation of the Red Cross in 1864, the International Telegraphic Union in 1865, the World Postal Union in 1874, the International Office for Rail Transport in 1890 and between 1875 and 1921 there was a common monetary zone between Belgium, France, Italy, Greece and Switzerland.

FIRST WORLD WAR

At the turn of the century the main European powers were engaged in an arms race and this, together with internal political and social problems because of multi-ethnic societies, led to increasing tensions. On 28 June 1914 the heir to the Austrian throne, Archduke Francois-Ferdinand was assassinated at Sarejevo (Henig, 1993). A month later Austria declared war on Serbia. Russia allied itself to Serbia and mobilised its troops, and on 1 August Germany declared war on Russia. Soon after, France, England and Belgium entered the conflict on the side of Russia and Serbia. Japan, Italy, Romania and the United States also entered the war, and Turkey and Hungary fought on the side of Austria and Germany. The end of the war in 1918 saw great political changes in Europe. The monarchies of Austria and Germany were conquered and the rulers of Russia disappeared as victims of revolutions. At the end of the war, terms and conditions dictated by the Allies were set out at the Treaty of Versailles, signed in 1919. Germany lost enormous territories and had to pay large sums in damages. This contributed to the development of nationalism and Nazism, and to a large extent germinated the Second World War.

In 1917 the Czar of Russia abdicated and the Russian revolution started. After several years of civil war the communists united and formed the USSR in 1923.

In an effort to avoid a repetition of the atrocities that had occurred during the war, to prevent large scale armament and to promote peace, the League of Nations (forerunner to the United Nations) was created at the end of the First World War by the Treaty of Versailles its headquarters were in Geneva.

SECOND WORLD WAR

The crash of the New York Stock Exchange in 1929 was the start of an economic depression for which there was no precedent and which undermined the establishment of the League of Nations. Countries sought to protect their own economy with protectionist measures. Socialist and nationalist governments forced out the democratic policies established after the First World War, and social and political problems were blamed on foreigners and Jews (Keegan, 1989). Under these conditions, a dictatorship came into being in Germany in 1933 with the election to power of Adolf Hitler. Germany then closed its doors to the League of Nations. A similar dictatorship had already been established in Italy in 1925 by Mussolini. In 1935 Italy attacked Ethiopia, also a member of the League of Nations, and economic sanctions were imposed. Co-operation among nations had been short-lived.

Meanwhile, Germany built up its arms and in 1939 its army attacked Poland and then rapidly expanded into vast areas of Europe and North Africa. The conflict turned into a world war with the attack by Japan on Pearl Harbour on 7 December

1940 and ended when the Allied forces crushed the fascist regimes of Italy and Germany in May 1945 and finally Japan in September 1945 (ibid). With the end of the Second World War, which cost 60 million lives, Europe lost its supremacy to Russia and the United States.

Conscious of the failings of the Treaty of Versailles, the victors imposed no penalties on the conquered nations. Instead, in 1947 they organised a programme of aid and reconstruction under the Marshall Plan largely financed by the United States.

On 26 June 1945 the international community created a new United Nations Organisation with 51 members as an international forum with the aim of promoting world peace and security (NZMFA, 1985). This replaced the League of Nations.

In 1946 the Prime Minister of Britain, Winston Churchill put forward the idea of a United States of Europe which he envisaged as incorporating only West European nations.

POST WORLD WAR II

However, since World War II, Europe has been divided by the East/West conflict (the Cold War) caused by the fundamental differences between the communist ideal of a closed economy and the open market economies of western countries.

Since 1985, confrontation has given way to co-operation. The then leader of the USSR, Mikhail Gorbachev, started a series of political reforms, 'Perestroika', which transformed Eastern Europe (Selvarajah, 1991). In 1990 Poland, Czechoslovakia, Hungary, Romania and Bulgaria became democracies and the communist regime in East Germany fell, reuniting East and West Germany. In 1991, by the Treaty of Varsovie, the union between Russia and its Eastern neighbours was dissolved, and in 1992 Czechoslovakia divided into two states. The former Soviet States and Yugoslavia broke into ethnic divisions. Grave conflicts have taken place and many of these states are currently facing serious economic and political difficulties.

EUROPEAN ORGANISATIONS SINCE 1945

Geographic ties and the lack of size led, in 1948, to the formation of the Benelux Union (Belgium, Netherlands and Luxembourg) to improve these countries' ability to trade with larger neighbouring countries. By having a free trade area within their area's boundary, they could lower costs of inputs purchased from other and produce a cheaper final product for internal consumption and export. Subsequent alliances were formed with France, Germany and Italy to form the European Coal and Steel Community in 1952, the European Atomic Energy Commission and the European Economic Community in 1958. These unions were merged in 1967 to form the European Community (EC). Table 3.1 shows in chronological order the formation of the European Union.

EUROPEAN FREE TRADE ASSOCIATION

Countries not belonging to the EEC, not wanting to be disadvantaged economically by the integration, formed the European Free Trade Agreement (EFTA) which was signed at the Stockholm Convention on 4 January 1960. The founding members were Switzerland, Austria, Great Britain, Sweden, Norway, Denmark and Portugal, followed closely by Finland, Iceland and Liechtenstein. Great Britain, Denmark and Portugal withdrew from EFTA when they joined the European Union.

Table 3.1: European Union Timeline

EUROPEAN UNION (EU)	
1945	End of World War II. Europe in disarray.
1947	General Agreement on Trade & Tariffs (GATT).
1948	Benelux countries (Belgium, Netherlands and Luxembourg) form a free trade area (customs union).
1952	European Coal and Steel Community (ECSC) formed by Benelux countries, France, West Germany and Italy.
1958	European Economic Community (EEC) and European Atomic Energy Commission (EURATOM) established as a result of the Treaty of Rome (March 25, 1957) by the same six countries.
1960	European Free Trade Area (EFTA) formed by Denmark, Norway, Sweden, Switzerland, United Kingdom and Austria.
1962	Common Agricultural Policy (CAP) of EEC introduced.
1963	Greece granted associate status in EEC, United Kingdom application declined.
1964	Turkey granted associate status in EEC.
1965	Yaounde Convention granted associate status in EEC to former colonies of France and Belgium (17 African States and Madagascar).
1967	United Kingdom application to EEC declined, Greece suspended due to military regime, European Community (EC) formed from merging of EEC, ECSC and EURATOM.
1971	Malta granted associate status in EC; Arusha Agreement granted associate status to Kenya, Uganda and Tanzania.
1972	In a referendum Norway's voters rejected the proposal to accept membership in the EC.
1973	United Kingdom, Ireland and Denmark granted full membership of EC; Cyprus granted associate status in EC.
1974	Greece readmitted to associate membership of EC.
1975	Lome Convention superseded Yaounde and Arusha Agreements.
1979	Greece upgraded to full membership of EC.
1979	European Monetary System established by EC.
1980	Lome Convention II.
1985	Lome Convention III.
1986	Spain and Portugal granted full membership of EC.
1987	Single European Act passed by EC.
1989	Fall of the Berlin Wall.
	Lome Convention IV includes Caribbean and Pacific countries.
1990	Reunification of Germany which admits East Germany to EC.
1992	Treaty on European Union (Maastricht Treaty)
1994	Norway again rejects entry to EU.
1995	Austria, Sweden and Finland granted full membership of EU.

EFTA did not have economic and political union as its goals (Wijkman, 1994). Its aims were to eliminate trade impediments between the member countries and to eliminate customs duties and taxes on industrial products (but not on farming products). In 1972 it eliminated tariffs with the European Union for industrial products. In addition, EFTA made similar agreements with other nations (for example Israel and Eastern Bloc countries).

The EFTA Council meets twice a year at its headquarters in Geneva. Decisions are taken unanimously and are binding on member nations. The Council is assisted by groups of experts, an economic commission and an advisory committee. It employs about 100 people and has an estimated annual budget of NZ$38 million (Dinan, 1994). The official language is English.

Table 3.2: European Free Trade Association Timeline

EUROPEAN FREE TRADE ASSOCIATION (EFTA)	
1960	Founding of the European Free Trade Association by Switzerland, Austria, Great Britain, Sweden, Denmark, Norway and Portugal.
1961	Signing of an agreement with Norway (which did not take up membership status)
1966	Programme for elimination of duties on industrial products.
1970	Iceland became a member.
1972	Bi-lateral agreements with the European Union.
1973	Great Britain and Denmark left to join the EU.
1976	A development fund of US$100 million set up in favour of Portugal.
1986	Portugal left to join the EU - Finland became a full member.
1991	Liechtenstein joined.
1995	Austria, Finland and Sweden left to join the EU

Although the EFTA has achieved its original goals, its future is uncertain. On 1 January 1995 Austria, Sweden and Finland became members of the European Union, reducing the membership of EFTA to four: Iceland, Norway, Switzerland

and Liechtenstein. Table 3.2 shows the sequence of events from the formation of EFTA in 1960 to the present.

The United Kingdom had some difficulty gaining membership of the EEC largely due to the opposition of France and President Charles de Gaulle who wanted a European Europe (Dinan, 1994). UK finally joined the EC in 1973. Norway's citizens have rejected membership on more than one occasion although their neighbours have joined.

A number of less developed countries have been granted associate status giving them preferential treatment in trading with EU countries. Some of these countries are former colonies of the developed countries in the EU. The area covered by the Yaounde Convention and the Lome Conventions, which set out these terms, extends from Africa to the Caribbean and the Pacific.

THE EUROPEAN UNION

The development of the European Union can be seen in four phases. The first phase is the formation of a free trade area by the Benelux countries, Belgium, Netherlands and Luxembourg, in 1948. The second phase is the formation of the European Economic Community in 1958. In the third phase, these three organisations, the EEC, EURATOM and ECSC, merged to form the European Community in 1967 - its goals and objectives being the same as that of the EEC. The fourth phase is the formation of the European Union in 1992.

Many common policies have been decided, the main one being the Single European Act (SEA) of 1986 to establish a single internal market, and the establishment of a single monetary policy (SME). Its goals have been expanded to include environmental issues and a common defence policy (Dinan, 1994:146). The

Single European Act gave the European Parliament a right of veto over the accession of new members to the EU and over association agreements with countries outside the Union. In addition, it gave Euro-MPs (who previously had only been 'consulted' by the Council of Ministers) the right to a second reading of some important categories of draft legislation. With an absolute majority and the commission's support behind them, the SEA gave the Parliament a particularly strong hand in the legislation of resolutions. This could only be overturned by the Council of Ministers by a unanimous vote of all the member countries. In effect these changes made the parliament something of an upper house, entitled to scrutinise, question, delay and sometimes amend.

The Treaty of Maastricht came into force in 1993 and at that time the EC had 12 members and headquarters in Brussels (Bidwell, 1993; Rothery, 1993). The Treaty provided for small but potentially significant changes in how Europe does business, including new powers for the Parliament. These extended 'co-decision' into a complicated procedure which entitled Euro-MPs to a third reading of some classes of legislation, and fixed a conciliation procedure for occasions when the Parliament and the Council of Ministers still failed to reach agreement. Areas for co-decision included laws on the free movement of persons, the internal market, education, culture, public health, consumer protection, R & D and environmental programmes. The Parliament's right to a second reading of legislation was widened to cover new areas including transport, aspects of social policy and some very limited aspects of economic and monetary union. The Treaty empowered the Parliament to request legislative proposals from the Commission on specified issues.

The Maastricht Treaty also laid the groundwork for greater co-operation on foreign policy and provided for a move to a single European currency by 1999 at the latest. It contained suggestions for intensifying European co-operation on education, health and culture.

SINGLE MARKET

The single market objective first envisaged by the Treaty of Rome, officially came into force on 1 January 1993. With 360 million inhabitants, the European Union is the largest single market in the world (see Table 3.3 for EU statistics). The four fundamentals of the single market are the free movement of merchandise, people, services and capital. Four principle themes of the Single European Act of 1987 are:

- Progress towards a frontier-free Europe.
- Development of an integrated economic and social area.
- Moves towards creating a 'European Society'.
- Strengthening the Community's role in the world.

Table 3.3: Essential data on European Union Statistics

Country	Pop in millions	GDP in US$ mill	Un-employment %	CPI Inflation %	Growth Rate %	Seats in EU Parliament	Pop per Euro-MP in 000's	as a % of total EU pop	as a % of total EU GDP
Austria	7.6	126.51	5.1	3.5	2.0	21	361.9	2.11	2.32
Belgium	10.0	156.8	9.6	2.5	2.2	31	403.3	2.78	2.87
Denmark	5.2	106.2	10.2	2.5	2.5	16	324.7	1.44	1.96
Finland	5.0	115.5	18.1	3.0	2.0	16	312.5	1.39	2.13
France	56.9	955.9	9.2	2.0	2.0	87	664.4	15.81	17.60
Germany	80.4	1337.7	4.8	3.5	2.0	99	819.2	22.34	24.63
Greece	10.1	54.2	10.3	11	2.1	25	415.6	2.81	1.00
Holland	15.2	223.7	6.9	3.0	2.0	31	495.3	4.22	4.12
Ireland	3.6	33.9	16.9	3.0	2.9	15	238.1	1.00	0.62
Italy	58.0	865.8	1.4	6.0	1.0	87	654.7	16.12	15.94
Luxembourg	0.4	8.1	1.3	3.2	3.5	6	65.0	0.11	0.15
Portugal	9.8	45.4	5.4	8.0	3.1	25	394.7	2.72	0.84
Spain	39.1	380.1	15.5	5.7	1.3	64	611.2	10.86	7.00
Sweden	8.5	189.9	6.5	2.5	2.3	22	386.4	2.36	3.50
UK	57.7	831.7	9.6	3.0	4.0	87	669.8	16.03	15.31
TOTAL	**359.9**	**5431.4**	**av. 8.7**	**av. 2.3**	**av. 2.3**	**626**	-	-	-

Source: *International Statistics Year Book*, 1994 and Information from the European Division of the New Zealand Ministry of Foreign Affairs and Trade.

Although there appears to be an agreement about the concept of a 'single market' allowing for free movement of Europe's workers, goods, services and money, there is no escape from the nationalistic culture of some member states. The French, for example, tried to prevent the United Kingdom from entering the Union, and more recently the British, Irish and Danes have been resolute in maintaining border control facilities in place for nationals of other EU countries.

Previously negotiated agreements between the EU and the Swiss Government (highly regarded applicant to the EU) regarding the free access of EU member countries' lorries onto Swiss soil have been rejected after a national referendum in Switzerland. On 20 February 1994, as a result of the referendum, the tonnage allowed to be carried across Swiss borders has been reduced significantly. In 1992 an agreement was made to limit lorries to 40 tonnes. In return the Swiss promised to build up the rail transport capacity, while allowing lorries of up to 28 tonnes free transit during weekdays up to the year 2004 (*The Economist*, February 2, 1994:52). The referendum (which identified a significantly cultural bias between French speaking and German speaking Swiss) now decrees that there will be no extension to this agreement.

Some degree of co-operation has been seen in other important areas, though, for example, cross-frontier merger acquisitions have risen from 2190 in 1987 to 4553 in 1992, and the success of Europol (Europe's integrated police service), only one year after its introduction (*The Economist*, June 18, 1994:13). In some areas, it seems that the fundamental aim of 'progressively establishing the internal market' of the EU is being achieved.

As early as 1985 the EC was moving toward a single internal market. The White Paper, 'Completing the Internal Market', set out a plan for the completion of the single market by the end of 1992. This was to be achieved by market liberalisation and the implementation of 282 proposals contained in its Appendix (Swann, 1992).

The White Paper proposed the free movement of people and goods within the market. An agreement on police co-operation and the Schengen Agreement on border controls (not ratified by the United Kingdom, Ireland and Denmark on the grounds of security) have addressed the former. A common passport is in use for EU citizens and in some countries this still needs to be shown. Students, retired people and non-working people have residency rights throughout the Union. There are still restrictions on workers.

In addressing the movement of goods, the Single Administrative Document was largely abolished in 1993, eliminating the need for customs documents for all but a few restricted categories of goods such as dual-use civilian-military products (McDonald and Dearden, 1992). Plant and animal health requirements have been set in place to control the spread of diseases and the shipment of contaminated fruit/vegetables which could arise from the lack of border control.

Movement of capital across borders has been facilitated with restrictions only allowed if they are necessary to maintain liquidity of local banks or as a response to major disruptions in foreign markets. Services such as banks, securities transactions and insurance companies have been set common rules which harmonise essential standards, have mutual recognition among supervisory authorities, and have home-country supervision.

MONETARY UNION

In 1970 the EEC adopted the Werner Plan which visualised the creation of a monetary union through 'irrevocable fixing of parities and the total liberalisation of capital movement' (McDonald, 1994b:42). However, the collapse of the

International Monetary Fund (IMF) system in 1973, the second devaluation of the US dollar in February 1973 (Riehl and Rodriquez, 1983:138), and the turmoil in the foreign exchange currency markets and the oil price shocks of 1973-74 saw the EEC member countries abandon the Werner Plan.

The resulting period of recession that followed, together with a period of highly volatile foreign currency movements between the EEC currencies, saw the integration process of the EEC flounder.

In 1979, an exchange rate mechanism, the European Monetary System (EMS), was introduced to overcome some of the difficulties resulting from the continued fluctuations of currency parities and the problems encountered in the EEC budgeting process. In line with the Bretton Woods regime, a group of West European countries under the auspices of the EEC formed a currency bloc. The EMS has three key components:

- The Exchange Rate Mechanism (ERM)
- The European Currency Unit (ECU)
- The European Monetary Co-operation Fund (EMCF)

By use of the Exchange Rate Mechanism (ERM) the EU nations intervene to keep their relative exchange rates within narrow limits so as to establish a predictable currency for trade (Minikin, 1993). The majority of members have their fluctuations limited to a margin of 2.2 per cent, but Italy, Spain and Britain have a margin of 6 per cent. The ERM has the ability to absorb outside influences, such as oil shocks and changes in USA monetary policy, by the EMS exchange rate floating up and down. However, recent crises caused by recession would seem to show that the attempt at controlled exchange rates is not working (Foley, 1994). The ERM is run by the finance ministries and central banks of the EU member nations on a day-to-day basis. All EU members are members of the EMS, but only

Belgium, Denmark, France, Germany, Luxembourg, the Netherlands and Spain are members of the ERM. The United Kingdom suspended its membership in September 1992 (*The Statesman's Year Book*, 1994-95:48).

Members of ERM are obliged to restrict the fluctuations of their currency to a specified band around a rate established by comparing the currencies in the ERM and the value of the ECU. If a currency reaches the top or bottom of the band, the respective central bank has to sell or buy the currency to ensure the currency remains inside the band.

The European Currency Unit (ECU) was established in 1979, and the European Council declared that the ECU will be the centre of the EMS. The ECU is primarily a reserve asset and a means of settlement between EMS members' central banks. It is, however, used in financial markets and is ranked as one of the top five international bond issues.

The 1989 Delors Report was an attempt to advance Economic and Monetary Union (EMU). It set out three stages for its implementation, with a timetable for lifting exchange controls and establishing free capital movement and the formation of a European System of Central Banks (ESCB). In addition, it proposed the locking of exchange rates in order to develop a common currency with a central system to establish monetary control. The third stage begins with intra-EU currencies fixed against each other and then the ECU replaces the member countries currency as the sole currency of the Union. The major concern that has risen from this, especially in the United Kingdom, has been the fear of the loss of sovereignty (Zis, 1994:55).

In addition to the selling or purchasing of foreign reserves in an effort to stabilise the currency, central banks of member countries have access to a central pool of funds held in the European Monetary Co-operation Fund (EMCF). This Fund was established to provide additional reserves to help members maintain currency stability.

The Maastricht Treaty that established the European Monetary Institute (EMI) and the European System of Central banks (ESCB) adopted the three-stage process advocated in the Delors Plan for the creation of the currency union but changed some of the procedures (McDonald, 1994:xxvii). The Delors Plan simply recommended the three-stage process but refrained from suggesting a precise time for each stage except that the process should start on 1 July 1990 (Zis, 1994:61) The Maastricht Treaty defined the commencement of stage two as 1 January 1994 and that, during 1996, the European Council will determine whether a majority of EU members qualify for monetary union membership. If this is the case the Council will set the date for it to become operational. The earliest possible date for the establishment of the currency union is 1 January 1997. If a majority of member states do not qualify for membership, the union will come into effect on 1 January 1999, even if only a minority of member states satisfy the membership conditions (ibid).

The EMI was established in stage two to pave the way for the establishment of the European Central Bank (ECB) in stage three by performing a number of necessary procedural and technical tasks. The EMI, which began operation in 1994, is empowered to develop procedures and rules for strengthening cooperation between the central banks of the member states. The ESCB will be composed of the heads of the central banks of the member states and the ECB, and will replace the EMI when the final stage of the monetary union takes place. The European Monetary Union will be launched when criteria on price stability, budgetary discipline, currency stability and interest rate convergence have been met. The ECB, the executive part of the European monetary system will be appointed by the European Council for a period of eight years (ibid). The ESCB will be responsible for the monetary policy of the member states that proceed to monetary union and will be independent of national governments and other institutions of the EU. Its prime objective will be to establish price stability in the member states.

The Maastricht Treaty rectified the weakness of the Delors Report of 1985 by specifying the criteria of convergence that had to be satisfied before a country can be considered for membership of the currency union. According to the Treaty, the following conditions must be satisfied (Zis, 1994:61):

1. its inflation rate must be no more than 1.5 per cent above the average of the lowest three inflation rates in the EMS;
2. its long-term interest rates must be no more than 2 per cent above the average of the lowest three member countries' rates;
3. it must have maintained its exchange rate within the narrow band of fluctuation of the Exchange Rate Mechanism (ERM) of the EMS for at least two years, without a realignment;
4. its budget deficit must be no larger than 3 per cent of GDP;
5. its National Debt must not exceed 60 per cent of GDP.

Despite the fact that the precise steps set out in the Maastricht Treaty to achieve monetary union may not be practicable, political leaders remain convinced that a single currency is a highly desirable objective that would bring great benefits to their citizens.

In the following pages some of the important policies and programmes of the European Union will be discussed. The Common Agricultural Policy (CAP), Integrated Pollution Prevention and Control (IPPC), the Social Charter of 1989, the Industry Policy paper of 1990 and the anti-trust laws passed by the European Union have created an inward looking Europe. Although some programmes have positive benefits, as an instrument of protection the CAP is seen to do more harm than good in the long run to the economies of Europe.

Common Agricultural Policy

Although the Common Agricultural Policy (CAP) was introduced by the EEC in 1962 originates in Article 39 of the Treaty of Rome which declared the objectives as follows (Gibbons, 1994:221):

1. to increase agricultural productivity
2. to ensure a fair standard of living for the agricultural community
3. to stabilise markets
4. to ensure the availability of supplies
5. to ensure that supplies reach consumers at reasonable prices.

The European Agricultural Guidance and Guarantee Fund (EAGGF) was set up to achieve the objectives of CAP. This was to finance a price support system and the development of a structure for European agriculture. Market price stability is achieved by interventionist pricing policies reviewed annually and by providing subsidies in the form of export refunds when the price of EU farm products set by the CAP exceeds the world market prices.

The logic behind maintaining a common agricultural policy which is expensive, complex and internationally criticised lies in European history. The memories of food shortage during World War Two and the strong protectionist stand on agriculture which already existed at national level, in a number of member states since the 1930s were important to the founder members of the European Union (Gibbons, 1994:222).

CAP has had a dramatic effect on those countries outside the Union (McMahon, 1990). It has provided protection for Union producers of wheat, dairy products, meat and other foodstuffs and prevented competitive prices on similar products from countries such as Australia, New Zealand, the US and Canada. It has established a minimum price for Union farmers for producing certain commodities and taxed non-members' imports to bring their prices up to meet it. This made the Union self-sufficient in almost all farm goods that could be grown within its member countries. When unrestricted production resulted in surpluses, the budget could not sustain the subsidies and, as a step towards reformation, in 1983 the common farm prices were lowered and quotas introduced. A further reduction was made by introducing quotas for milk production in 1984.

One of the contentious issues at the Uruguay Round of GATT was agricultural policies, with CAP being seen as a major stumbling block to agreement. The final ministerial meeting in December 1990 broke down largely because the Union refused to offer adequate cuts in farm subsidies. The major part of the EU's budget expenditure is in agriculture and is highly protectionist in nature (Coleman, 1983, Penketh, 1994:77). The EU's expenditure on agriculture in 1987 was 65 per cent of the total EU budget. This figure has been reduced over the last few years and is expected to be 52 per cent in 1995 (Penketh, 1994:80)

Further reform was introduced in 1992 with farmers receiving compensation for setting aside land from production instead of having their prices supported. The reduction of agricultural surpluses is expected to lower food prices and eliminate the export subsidies they formerly attracted.

ENVIRONMENTAL POLICY

Unlike recent years, environmental issues was not a major concern when the Treaty of Rome was drafted and as such no provision for environment policy was included in the Treaty.

As it became obvious that environmental difficulties were capable of disrupting the economic life of the Union, policies affecting waste management, water and atmospheric pollution were put in place (Hassan, 1994:187). Starting with a 1967 directive on classifying, packaging and labelling dangerous substances, and a 1970 directive on noise levels, the EU has increasingly legislated on environmental issues as these have become concern of the member countries. Legislation covers manufacturing, environmental impact assessment, protection of natural habitats and the species that inhabit them, all types of emissions (e.g. motor vehicle, fluorocarbons), water quality, waste disposal and the production and transport of environmentally dangerous chemicals.

Unfortunately, the Commission has had difficulty in enforcing total compliance from most of its members, except Denmark, in the area of environmental impact assessments. These are mandatory for certain installations and discretionary for a large number of others. A draft directive on Integrated Pollution Prevention and Control (IPPC) is causing some concern. The Commission estimates that complying with the directive on the emission of volatile organic compounds could cost solvents-using industries $6 billion per annum for 4-5 years (Roberts, 1994).

SOCIAL POLICY

As many of the member countries have socialist governments, there has always been a strong movement to promote social policy as a means of achieving a "people's Europe" (Dinan, 1994). The Social Charter of 1989 listed the following 12 categories of workers' fundamental rights (Dearden, 1994:151):

1. Improvements in living and working conditions.
2. The right to freedom of movement.
3. Employment and remuneration.
4. The right to social protection.

5. The right to freedom of association and collective bargaining.
6. The right to vocational training.
7. The right of men and women to equal treatment.
8. The right to information, consultation and worker participation.
9. The right to health protection and safety at work.
10. The protection of children and adolescents.
11. Elderly persons shall receive an income that guarantees a decent standard of living.
12. To enable the fullest possible integration of disabled persons in working life.

Although countries adopted the Charter, there is no binding legal force to ensure its implementation. One drawback has been the large increase in unemployment. Legislation by the Council of Ministers in 1992 included eight directives, mainly on health and safety issues, that arose from the need to give the Charter substance. Most of these directives are aimed at fostering worker mobility within the Union through enhancing training provision and establishing common health and safety requirements.

INDUSTRIAL POLICY

The Commission produced the *21st Report on Competitive Policy of the EC* in 1991 urging the need for competitive environment with limited government intervention. Recession in many of the members states has, however, prevented the implementation of this policy. Governments have sheltered certain industries from competition because of those industries' economic importance to their country.

Furthermore, the EU is hampered in promoting a coherent industry policy as member states have developed a mixture of industry policies of their own (Beije et al, 1987). The diverse approaches that the member states have taken falls under the following three main approaches to industrial policy (McDonald and Potton, 1994:116):

1. Market-based or negative industrial policy. In this approach, the general understanding is that the market conditions will determine industry structure, and government intervention is least preferred. In this situation, competition policy, removal of state aids to promote competitive markets and deregulation programmes are main features of industry policy. The United Kingdom tends to exhibit this approach.
2. Interventionist or positive industrial policy. The understanding in this approach is that market failure is the obstacle to an development of a dynamic industrial base and should be avoided. To avoid negative effects on social and regional factors, positive action and support by governments in business is necessary. This approach tends to support both declining and rising industries. France and Italy generally support this view.
3. Selective intervention or strategic industrial policy. This approach supports a strategic view of industry policy, and its main role is to aid the growth of rising industries. This approach is based on the view that the competitive environment is imperfect and requires timely intervention by government to maintain a balanced industrial policy. Selective state help to encourage the growth of industries with strong economies of scale and learning effects is necessary.

The difficulty of developing a EU industrial policy is exacerbated when member states such as the UK are generally market-based, while France and Italy have more interventionist views of industrial policy. Although generally there is a shift towards a more market-based approach in the EU in areas such as transport services, telecommunications services and airlines, large-scale protection of declining industries and widespread use of state aid by many member countries are reminders that interventionist industrial policies are still a potent force.

COMPETITION POLICY

Member states of the EU are free to determine their own policies towards competition within their national boundaries (Kemp, 1994: 101). However, in matters affecting intra-Union trade, EU policy takes precedence. The competition policy of the EU is embodied in Articles 85 and 86 of the Treaty of Rome. These ensure free competition within the EU, with the responsibility of applying the legislation resting with the European Commission (Kemp, 1994:104). The creation of the Single European Market (SEM) demands a greater degree of harmonisation, and with the move towards a monetary union, the independence of national governments to deal with matters of internal trade diminishes.

Competition policy of the EU fall into two categories, one that covers the activities of private enterprises and the other the activities of member states and state sponsored bodies. The first generally refers to anti-thrust laws and the latter, state aids (Dinan, 1994:272).

Articles 85 and 86 of the EEC Treaty relate to the Union's antitrust policy. The EU passed antitrust laws to prevent private companies making agreements that restrict trade or using a dominant position to distort trade between member states. In an effort to control the latter, there is close scrutiny by the Director of the Commission for Large Mergers and Acquisitions, Joint Ventures and Collaborative Agreements. The recent increase in petrochemical producer alliances has caused attention to become focused in this area (Milmo, 1994)

The other policy area is state aid. This is prohibited except in special circumstances (for example, supporting a poor area), when it is reported to the Commission and shown to fall within the EU's permitted parameters (MacDonald and Potton, 1994:117). The enormous increase in state aid in the 1980s led to stricter enforcement of these criteria and the reporting of any non-compliance to the Court of Justice. Despite this, Germany, France, Italy and the United Kingdom have increased state aid, mainly in the more affluent areas of the EU.

PERSONNEL AND BUDGET

The departments of the European Union comprise 25,000 employees and utilise an annual budget of approximately US$71 billion (*The Economist*, 22 October, 1994:66). The European Union has nine official languages. Bureaucratic problems contribute to the high budget cost of the European Union. Parliament is split between Strasbourg (where plenary sittings are held), Brussels (the base for committee work) and Luxembourg (the seat of the parliament's secretariat), and the costs of just moving documents between the staff in these three centres is around 50 million ECUs (US$31m) a year. Translation of documents into each of the nine official languages swallows up 30 per cent of the Parliament's budget.

THE LEGAL PROCESS OF THE EUROPEAN UNION

Legislation is mainly in the form of rules and directives. The texts originating from the Commission are approved by the Council of Ministers, generally after they have been considered by the European Parliament. Rules are binding on all member States, but directives are not binding. It is left to each member state to decide how best to implement a directive within its own nation and according to its own laws.

PROSPECTIVE FUTURE EU MEMBERS

The inclusion of Sweden, Finland and Austria on 1 January 1995 seems to be a natural move for both the EU and the three newcomers, as they have much in common and, through the EU-EFTA co-operation have already been close trading partners. With these three new members, the total GNP for the EU has increased by seven per cent and the population from 338.8 million to 359.9 million people. The GNP per capita has increased by one per cent, as the comparative GNP for these three countries (EU average index = 100) are Austria = 122, Sweden = 114 and Finland = 88. The richest countries per capita are still Luxembourg = 168, Denmark = 140, and Germany =126 (*Berlingske Business*, 1994:5).

Swedish and Finnish are now official EU languages along with nine other European languages. This is another issue that needs to be addressed. With more borders vanishing and an increase in the number of countries entering the EU, the cost of translation will increase. Before Sweden and Finland joined the EU, it was reported (*The Economist*, 21 May, 1994:22) that 30 per cent of the EU Parliament budget of 692 million (roughly NZ$1.2 billion) was spent on 72 permutations of simultaneous interpreting.

As well as the breaking down of boundaries by the redefinition of the older trading groups into the EU cluster, the boundary is also breaking down between Western Europe and the previously communist countries of Eastern Europe. The two Europes, far from becoming a single economic, social and political space, are in the process of dividing into several such spaces, seemingly independent of each other.

An example of the difficulties faced is exhibited in the policy consequences of the absorption (or as some would have it the reunification) of East Germany (GDR) into the Federal Republic of Germany (FRG). This has, as the currency turbulence of September 1992 illustrates, affected Germany's relationship with other member states. Notwithstanding the increased ferment of nationalisation created by the Eastern migration into FRG and its consequential lowering of living standards, German unification has created a pressure to accelerate European integration. Before it has had time to settle relationships between existing member nations, the

EU has, therefore, been drawn into the problems of managing post-communist transition and of developing relationships between western and eastern European societies.

THE EAST EUROPEAN APPLICANTS

The main aims of the EU have been prosperity and security, which it has been fairly successful in achieving. To the east of the Union, from the Baltic to the Balkans, are the former Eastern Bloc countries with a population of 170 million people (not counting Russia or the rest of the Commonwealth of Independent States, CIS). The question is, will an opening of membership to the EU to these countries mean further prosperity and security in Europe? In 1993 Bulgaria, the former Czechoslovakia, Hungary, Poland and Romania also traded in excess of US$70 billion with OECD countries (*The Economist*, 5 November, 1994:108). The OECD countries are made up of all the EU countries, New Zealand, Australia, Japan and Switzerland. Therefore the EU cannot afford to close off trading with the old iron curtain nations by forming a trade bloc with tariffs and quotas against Eastern Europe.

Since the collapse of communist control in 1989, the Czech Republic and Slovakia, Hungary and Poland have embraced the concepts of privatisation reforms and free enterprise. They are working toward achieving a level of democracy and economic reform that will enable them to join the EU. Since the reunification of Germany, there has been a constant stream of migrants across its eastern borders as poorer neighbours seek a more prosperous life. It is, therefore, in the EU's interest, and specifically in Germany's interest, that the East European nations improve their economies, as membership to the EU may not be too distant. The eastern European countries of Poland and Hungary have already applied for membership. The Czech Republic and Slovakia are expected to do so.

Although they too are expected to apply, the East European countries of Estonia, Latvia, Lithuania, Bulgaria and Romania do not seem likely candidates for some time. There is not the same progress toward change. To bring in large agricultural areas at this time would have severe repercussions on CAP.

The three Baltic states are discussing setting up their own union based on the EU. Since independence Ukraine and Belarus have not managed well economically and they hope rejoining the Russian economy will fix this.

The East European countries present a much larger problem since they currently have not only different economic structures, but also different internal relationships between State and society. There is little basis as yet, either in patterns of interdependence or institutionally, for replicating the European model of integration that has developed in Western Europe.

The German Chancellor Helmut Kohl promised on 24 March 1994 that under German Presidency the EU would strengthen its links with the Eastern European countries wishing to join (*The Economist*, 18 June, 1994:13). Provisionally though, the EU has closed off future attempts to expand into the Eastern area and has excluded all former Russian republics with the exception of the three Baltic States. The Hungarians, Pole and Czechs are impatient to join and already have some free trade agreements in place with the EU, but clearly want full membership by 2000. It is apparent that the other states may be offered 'partnership' status in the interim to cope with foreign and security policies only, and would postpone economic integration for an undefined period.

Membership of the EU requires, under the Maastricht Treaty, that countries have attained a specific level of economic and political development - development high enough to enable easy adaptation to the standards of existing EU member states. The average income in the advanced countries in Eastern Europe (Poland, Hungary, Slovakia and Czech Republic) is less than a third of the US$ 17,000 average income in the EU (*The Economist*, June 18, 1994:13). The terms and conditions of entry have been made more extensive and rigorous in an effort to assist existing membership and to induce the Visegrad Four - Hungary, Poland, the Czech Republic and Slovakia - to build and transform their economies and democratic structures before entering the EU. At present the perceived idea is that the Visegrad Four will use the EU to help develop change in the vacuum created by the demise of the Soviet Union. One major factor here is that the Maastricht Treaty requires an 'absence of budgetary deficit' for prospective members. However, ten of the existing member States have deficits in excess of the Treaty guidelines.

It can be argued that allowing Eastern European countries with newly won democracies to gain membership of the EU would ensure peace and security across Europe. These countries would, therefore, be part of a common security policy rather then being on their own or going back to some form of the Warsaw Pact. The security reason for wanting to allow east European states to join the EU may be based not so much on fear of external military insecurity as on political instability and fear of civil war actions within European countries, such as is happening in the former Yugoslavia.

An important issue is also the environmental 'security' of the EU. The former Eastern Bloc countries have very low environmental standards which have badly affected many EU country's air and water qualities. An example of this, after the fall of communism in Romania, was the ensuing display, to the horrified world of the economic damage done in that country through very low environmental standards (Roberts, 1994). Admission to the EU will mean allowing the EU superpowers to supersede member countries in pollution control (member countries can set tougher levels than EU standards, but not lower).

As discussed earlier, different patterns of economic, political and social development in these countries also make the prospect of early membership unlikely. Some EU member states and institutions believe their accession would cause institutional problems and there is a consensus that accession by the Visegrad Four and Turkey would put considerable strain on the Union. The Union faces an extraordinary challenge. It will not be an easy task to secure internal development and provide political and social stability within a greater Europe. The European Union requires a mechanism to manage high levels of interdependence and interpenetration between member states, and development of a parliamentary institution will be the basis of that mechanism.

PROSPECTIVE EUROPEAN MEMBERS

Norway

Norway has again declined EU membership, as the influence of farmers and fishermen has prevailed. The farmers are concerned about losing protection under CAP and the fishermen fear loss of national control over Europe's richest fish stocks. The country has its own oil supply and feels the EU needs it more than it needs the EU (Henriksen, 1994).

Switzerland

Member of EFTA. The loss of its neutrality is regarded as too big a price to pay for EU membership. An application is not expected in the near future.

Iceland

Member of EFTA. Another country that fears for its fishing industry. Its small size would be a disadvantage in the power stakes. It is not seeking EU membership.

Turkey

Its political system is not democratic and this is stalling its application. Although its co-operation in the Gulf War has given it more credibility, the March 1995 political unrest caused by Islamic fundamentalist groups within the government has eroded this. If accepted into the EU, Turkey would be the only Islamic nation in the Union.

Cyprus

The political division of the island is a handicap to its attempt to join. The EU is proposing the admittance of the Greek portion of the island and this, along with the banning of Turkish Cypriot goods from sale in the EU, can only worsen the situation.

Malta

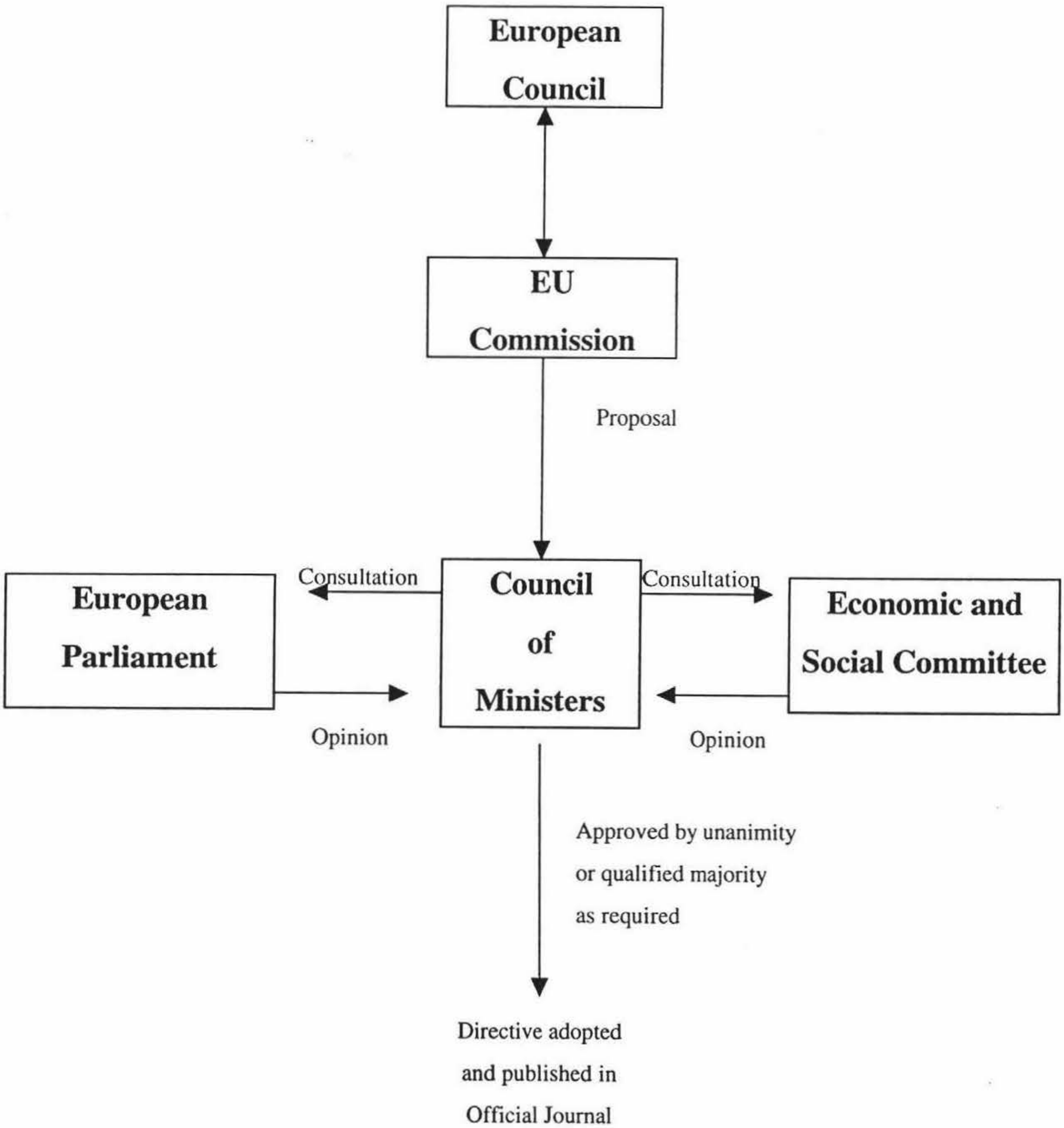
Despite its small size the EU has indicated that it is prepared to consider admitting Malta in its next intake (*The Economist*, 6 August, 1994).

THE EUROPEAN INSTITUTIONS

The Union, comprising 15 member states as of 1 January 1995, is managed by common institutions: a democratically elected Parliament; a Council of Ministers representing member states and composed of Government Ministers or, more rarely, Heads of State or Government; a Commission which acts as guardian of the treaties and has power to initiate and implement legislation; a Court of Justice which ensures that the Union law is observed; and a Court of Auditors which monitors financial management of the Union. In addition, there is the European Council which came into being in 1974 to resolve problems at the highest political level (McDonald, 1994). There are also a number of advisory bodies which represent economic, social and regional interests. As a part of the preparations for enlargement, and as indicated previously, member states will review the procedures for the enlargement of the Union in 1996.

The Union's legislative process begins with a proposal from the European Commission to the Council of Ministers of the European Union (see Figure 3.1:). The Council seeks the views of the European Parliament on the proposal. The Parliament adopts a formal opinion after the specialist committees (see Table 3.4:) have considered the proposal. When opinions have been received the Council will decide, with most decisions formed on a majority basis after the reservations of individual members states have been taken into account. The approved text may differ substantially from the original proposal.

Figure 3.1: Decision making process of the EU



Source: *Deloitte's 1992 Guide*.

Table 3.4: European Parliamentary Committees

Nineteen committees prepare the work of the plenary sessions:

1. Committee on Foreign Affairs and Security
2. Committee on Agriculture Fisheries and Rural Development
3. Committee on Budgets
4. Committee on Economic and Monetary Affairs and Industrial Policy
5. Committee on Energy, Research and Technology
6. Committee on External Economic Relations
7. Committee on Legal Affairs and Citizens Rights
8. Committee on Social Affairs, Employment and the Working Environment
9. Committee on Regional Policy, Regional Planning and Relations with Regional and Local Authorities
10. Committee on Transport and Tourism
11. Committee on the Environment, Public Health and Consumer Protection
12. Committee on Culture, Youth Education and the Media
13. Committee on Development and Co-operation
14. Committee on Civil Liberties and Internal Affairs
15. Committee on Budgetary Control
16. Committee on Institutional Affairs
17. Committee on the Rules of Procedure, the Verification of Credentials and Immunities
18. Committee on Women's Rights
19. Committee on Petitions

THE EUROPEAN PARLIAMENT

Elected by direct universal suffrage since 1979, the European Parliament currently comprises 626 members. Parliament has its seat in Strasbourg, although committee meetings and some part sessions are held in Brussels. Its Secretariat is based in Luxembourg and comprises 3,500 officials plus staff of several political groups.

The European Parliament is composed of political groups organised at Union level. Representing 360 million people, the parliament's main role is that of political driving force, generating various initiatives for the development of Union policies.

Some progressive individuals, like Klaus Hansch (1994), would like to see this role expanded to provide a balance against the over-riding influence of the Council. Under the Treaty of Rome, Union legislation is formulated by a three-way process: the Commission proposes and the Council decides after consultation with the Parliament. The 1986 Single European Act increased the Parliament's powers respecting Union legislation by introducing a co-operation procedure which called for two readings of Union proposals by Parliament and the Council. Hansch's arguments were taken up in the 1992 Treaty of European Union when a further step was taken towards recognition of the legislative power of Parliament. The Treaty provided that, in conjunction with the Council, Parliament had the power to adopt regulations and directives on an equal footing. Further, the Council can only act on international agreements and accessions of new members with the assent of the Parliament. Hansch has argued that the Parliament should be the final arbiter of power, and the Council the supervisory body through which EU law is administered. At present, the European Parliament acts more in an advisory capacity, and as such its powers are limited in comparison with national parliaments.

The 626 delegates of the parliament, elected for five years, are made up as follows: Belgium, 25; Denmark, 16; Germany, 99; Greece, 25; Spain, 64; France, 87; Ireland, 15; Italy, 87; Luxembourg, 6; Holland, 31; Portugal, 25; Great Britain, 87; Austria, 21; Finland, 16; and Sweden 22. The delegates make decisions without relation to their national interests. The functions of the Parliament are essentially limited to control of the Commission and the Council of Ministers. It can veto legislation in 15 areas, including the internal market, health and safety, the environment and consumer protection. It has a say in the choice of the new Commission and its president, and it must give formal approval for international treaties such as WTO. In addition, it has a measure of control over allocation of the European Union annual budget, which in 1996 is estimated at ECU 71 billion. (Penketh, 1994:80).

Called the 'talking shop' of the EU, it serves as a general deliberative body. It has the power to dismiss the Commission on a motion of censure approved by two-thirds of its members. It comprises representatives elected by the voters of the country they represent. The number of representatives per country varies depending on the member country. Size is not the only referent in deciding this number.

At the Maastricht Summit in December 1991, Parliament was given power by the Treaty on European Union to veto Commission proposals on consumer protection, health, education, trans-European networks, culture, environmental strategy, research and the single market by an absolute majority if, after three readings, acceptable amendments had not been made. It has the power to scrutinise Union finances, to appoint an ombudsman and set up committees of inquiry to investigate alleged contraventions/maladministration of the implementation of Union law.

THE EUROPEAN COUNCIL

Established in 1974, the European Council is made up of the Heads of Government (or in the case of France, the Head of State) and the President of the European Commission, assisted by Foreign Ministers and a member of the Council of Ministers. The European Council has established a pattern of three meetings a year, with special summits called to discuss major issues (McDonald, 1994:xxv)). The European Council acts as a guide and driving force and determines the overall policy of the European Union.

The European Council summits are chaired by the member state which holds the Presidency of the Council. The summits are generally strongly influenced by the member state which holds the Presidency. All decisions of the European Council, however, must be unanimous. Each minister has one vote and one right to veto.

The Treaty on European Union gives it certain operational responsibilities in relation to foreign and security policy and economic and monetary policy. No major developments in the integration process would be possible without the approval of the European Council (McDonald, 1994:xxvi). It is, therefore, through the European Council that member governments control the integration process of the Union.

THE COUNCIL OF MINISTERS

The Council of Ministers is the legislative arm of the European Union. Each state has a delegate who specialises in the field, for example, Ministers of Agriculture will deal with agricultural matters. Each member State in rotation provides a President for a six month period. The Council has a dual role, in the first place it adopts the main decisions on Union policies on the basis of proposals put forward by the Commission; and in the second place it is responsible for the intergovernmental co-operation introduced by the Treaty on European Union. This relates to common foreign and security policies, justice and home affairs, where most decisions require unanimity. Each member state has a certain number of votes as follows:

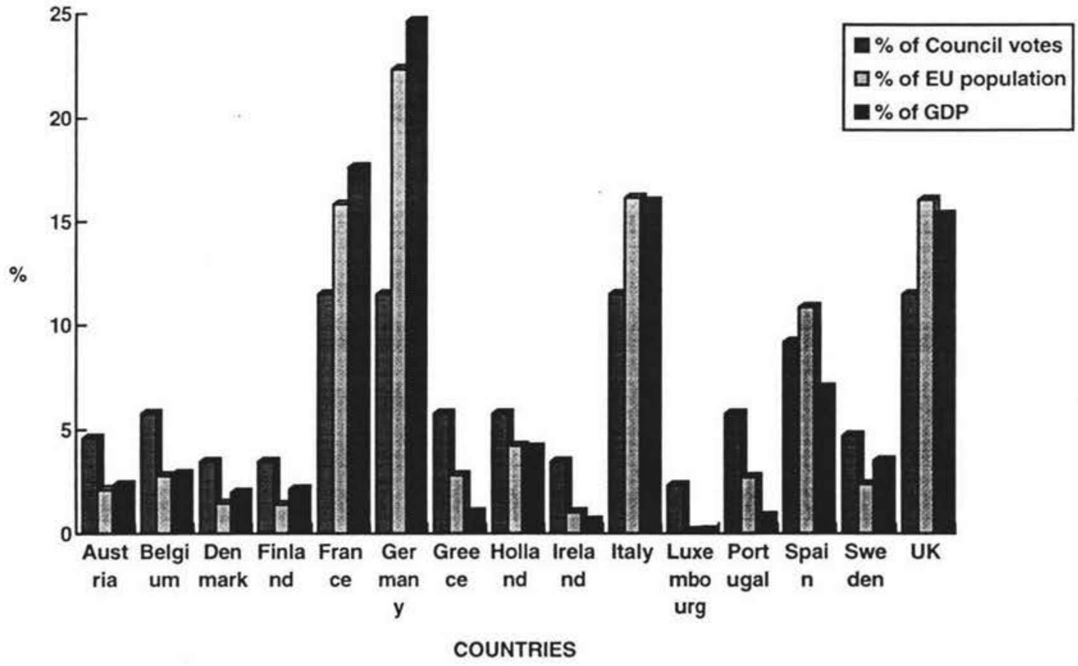
Germany, France, Italy and Great Britain	10 votes each
Spain	8 votes
Belgium, Greece, Portugal and Holland	5 votes each
Austria and Sweden	4 votes each
Denmark, Finland and Ireland	3 votes each
Luxembourg	2 votes.

Certain important decisions - for example, monetary policy or the joining of a new member state require unanimous votes. Realisation of a single market requires a great deal of work and effort over the adoption of standard policies and rules in all nations - for example, standard regulations for technology and for security.

The Council of Ministers, attended by the appropriate government ministers from the member countries, is the EU's legislature, and the only one in the democratic world which normally deliberates in secret (Dinan, 1994).

There still remain, though, serious questions about the balance in the make-up and voting rights of the council. The newly proposed calculations are significantly out of balance between voting rights, population and GDP, as indicated in Figure 3.2 below. This issue will become a major topic for discussions at the Inter-Governmental Conference in 1996.

Figure 3.2: Imbalance in European Council voting rights



Each representative has a number of votes depending on which countries he or she represents. large countries have more votes in the Council of Ministers so they cannot be out-voted by a gaggle of small ones. In turn, small countries are protected by a system of weighted voting. Of the Council's 89 votes, 61 are needed to form a 'qualified', or decisive majority, and only 27 are therefore needed to form a blocking minority. The present arithmetic means that the Big Five, with 48 votes between them and representing four-fifths of the union's population, can muster a qualified majority only if they gain the support of at least four or five small states. Similarly, to get their way, the small states need the backing of three big states. Roughly speaking, a qualified majority normally represents 70 per cent of the EU Council votes, a blocking minority is then 30 per cent.

THE EUROPEAN COMMISSION

The European Commission now has 20 members: two each from Germany, France, Italy, Spain and the United Kingdom, and one from each of the other member states. In 1995 the term of office was raised from four to five years, bringing it into line with the European Parliamentary term. Members of the Commission are obliged to be completely independent of their national governments and act only in the interests of the EU as a whole. Each member has a special responsibility for one or more policy areas, but decisions are required to be made on a collective responsibility basis.

The Commission is first and foremost the guardian of the Treaties. As an impartial body it sees that the Treaty provisions and Union decisions are properly applied, and helps in the area of enforcement it has the right to initiate infringement proceedings and refer the matter to the Courts of Justice. It is the executive body of the European Union.

The European Commission is a collegiate body with members who are appointed by national governments, but pledged to act in the EC's interests. Despite the impression of equality, larger countries tend to have more power and more commissioners. Commissioners are now allocated portfolios by the Commission President in consultation with the heads of state. The holder of the position of President must be agreed to by all members. Jacques Santor, the successor in 1995 to Jacques Delors who had held the post from 1985, was elected after the United Kingdom had vetoed the appointment of the original nominee Jean-Luc Dehaene (*The Economist,* 2 July, 1994; also see 23 July, 1994).

The Commission meets weekly to discuss and resolve various initiatives and proposals to go before the Council of Ministers. It can initiate administrative legislation but has only limited authority to execute policy. The Commissioners are supported by a civil service, headed by directorates-general.

Since the disintegration of the USSR, the Commission has assumed responsibility for co-ordinating Western aid to Hungary and Poland. From this it has increasingly become the channel for dealings with the new democracies in Central and Eastern Europe and with the former Soviet republics.

THE COURT OF JUSTICE

The European Court of Justice whose headquarters is in Luxembourg, comprises thirteen Judges and six Advocate Generals, all of whom are appointed on a six year term of tenure. The Court's role is to ensure that the European Treaties are interpreted and implemented in accordance with EU law. The Court passes judgement at the request of a Union institution, member state, or any legal or institution instrument or body within the Union. The Court can also pass judgements at the request of a national court, providing there is no higher national court available in the host country of the requesting body. Member States and individuals are obliged to comply with the Court's decisions and judgements, which also overrule national court judgements. Furthermore, the court is empowered to fine member States that do not comply with its judgements.

Established in 1989, the Court of First Instance is a subsidiary court of the Court of Justice It deals with cases involving competition, ECSC, staff and claims for damages arising in these areas.

THE COURT OF AUDITORS

The Union's financial activities are monitored by the Court of Auditors, consisting of 12 members appointed by unanimous decision of the Council after consultation with the Parliament. The Court has extensive powers to check accounts ensuring that all Union revenue has been collected and expenditure incurred in a lawful and regular manner. Public and political concern about fraud, waste and mismanagement of the Union's resources has led to an increase in the importance attached to their work. It consists of twelve nominated members from member countries with experience in the financial control of public funds.

CREATING A EUROPEAN SOCIETY

The Union member nations represent a very diverse range of national and cultural differences, with a wide range of economic and structural developments. A major aim of the Single European Act was to reduce the internal barriers within the Union and create a seamless European society. The Union has targeted two primary areas in an effort to reduce or totally eliminate internal barriers, namely the regional disparities brought about by differing economic developments, and the social issues from the unification of the Union.

DEALING WITH REGIONAL DISPARITIES

Many areas of the Union have tended to specialise in specific industry types which are affected unequally by economic cycles. This has contributed to the regional disparities that exist in an economic sense within the Union.

Until 1970, little was done to relieve the disparities between regions within the Union, although an implicit concern for these was embodied in the Treaty of Rome. In 1975, the European Regional Development Fund was established with a small budget to provide investment grants and loans for specific projects to regions that exhibited (McDonald, 1992:104):

- a per capita income below the EC average, or
- more than 20% of the population engaged in agriculture, or
- unemployment more than 20% above the EC average, or
- particularly high levels of migration.

Funds were allocated on the basis of a predetermined national quota, based on the level of national economic growth - for instance the largest allocation was received by Italy 40 per cent and the UK 28 per cent, reflecting the less prosperous states compared with other members. This method of distribution was changed in 1977 to allocate funds on specific regional development needs, rather than on a national quota basis.

As part of a process towards implementation of the Single European Act, an agreement was reached in early 1988 to double the size of the development fund by 1992. Major reforms were also implemented with the funds being targeted towards (McDonalds and Dearden, 1992:107):

- Development of structurally backward regions
- Reconverting regions in industrial decline
- Combating long-term unemployment
- Combating youth unemployment
- Adjustment to agricultural structures
- Development of agricultural areas.

With the restructuring that from the implementation of the Single European Act, and the ability of goods, services and individuals to freely move about within the European Union, disadvantaged regions suffered as industrial resources were moved to take advantage of economic disparities. The open market placed traditional industries and previously subsidised industries in jeopardy, thereby multiplying the negative effects in the disadvantaged regions.

The overall effect of the reforms and the funds was to reduce the regional disparity within the Union and to ensure that regional aid was fairly distributed, making certain that the benefits of a single European market were felt throughout all member nations and regions.

SOCIAL ISSUES

The Treaty of Rome laid down the fundamental rights of the Union's citizens, the right to establish themselves in another country, or sell goods or services there on the same basis as nationals of that country. However, some problems remained unresolved, particularly those relating to social security benefits and taxation. Therefore, the European Commission decided to impose residence restrictions through an adequate means test on those intending to migrate but who were not economically active.

At the Strasbourg Summit in December 1989 the UK opposed the European Commission's proposal for a Charter of Fundamental Social Rights and the proposal failed. At the Maastricht Summit the UK again opposed the proposal. However, this time the other eleven members of the EC adopted the Charter based on the rights in the Treaty of Rome and the Single European Act.

The Social Charter included the following social commitments (McDonald and Dearden, 1992:96):

- Improvement in living and working conditions, with a specific call for the establishment of a maximum working week,
- The right of freedom of movement,
- All employment must be fairly remunerated,
- All citizens of EC are entitled to adequate social protection,
- The right to freedom of association and collective bargaining,
- The right to vocational training,
- The right of men and women to equal treatment,
- The right of information, consultation and worker participation,
- The right to health protection and safety at work,
- The protection of children and adolescents, with the minimum working age set at 16 years,
- The receiving by Elderly people of an income that guarantees a decent standard of living,
- The fullest possible integration of disabled people with respect to training, integration and rehabilitation for work.

STRENGTHENING THE UNION'S ROLE IN THE WORLD

With growing size and economic strength, the Union has a significant part to play in global affairs, not only through trade but through aid and political influence as well. In Table 3.5 the EU's GDP growth, though not spectacular when in comparison with the growth of East Asia, is comparable to that of NAFTA and APEC as a region. For comparative figures on world trade flow between regions see Table 5.4 in chapter 5.

Table 3.5: A World regional comparison of GDP growth

	Average 1975-84	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
World	3.3	3.7	3.6	3.9	4.6	3.4	2.2	0.6	1.7	2.0	2.2
EU	2.0	2.5	2.9	2.9	4.2	3.5	3.0	0.8	1.1	-0.4	2.8
NAFTA	3.4	3.5	-0.1	3.0	3.4	2.7	1.8	1.2	2.0	3.0	3.8
APEC	2.9	3.7	3.4	3.7	4.0	2.1	1.2	2.8	4.7	5.1	5.3
East Asia	6.3	7.3	7.0	8.1	9.0	5.5	5.7	6.1	7.8	8.7	8.6
Australia	2.9	4.8	1.9	4.4	4.4	4.6	1.3	-0.9	1.8	2.5	3.1
New Zealand	1.5	-1.0	3.3	-0.8	0.5	-1.0	0.2	-2.0	2.8	3.0	6.1

Source: *The World Economic Outlook October 1993, IMF*

Table 3.6 shows the percentage changes in world trade flows between 1970 and 1990. The region most affected by the formation of the Union are countries such as Australia and New Zealand in the South Pacific. Exports to South Pacific nations have dropped by 43 per cent while imports from these nations have decreased by 27 per cent over the same period. North American loss is 12 per cent in terms of its exports and 25 per cent in terms of its imports. The percentage changes of exports and imports to Western Europe as a whole is negligible. The greatest increase in trade flow is between the European Union and the East Asian region. The European Union's exports to East Asia have increased by 58 per cent while the percentage change in imports are approximately half that of its exports. The increase in the volume of trade between East Asia and the EU is in the EU's favour, and a positive trade relationship between the two regions is seen to be of importance. The percentage change in trade flow between the rest of the world and the European Union, though increased between 1970 and 1990, is small.

Table 3.6 Changes in World Regional Trade Flows 1970-1990 (%)

	East Asia	North America	South Pacific	APEC	Western Europe	Rest of World
European Union						
Exports	+ 58	- 25	- 43	- 18	- 0.08	+ 7
Imports	+ 27	- 12	- 27	- 7	+ 0.06	+ 11

Source: *The Australian National University Economic Databank*, compiled from United Nations, International Monetary Fund, and national statistics. (adapted from Bergsten and Noland, 1993, pp.184-185)

THE EUROPEAN UNION AND THE REST OF EUROPE

With the disappearance of the Warsaw Pact and COMECON from the economic and political scene of Europe and the diminishing importance of NATO and EFTA in European affairs, the concept of Europe taken to stand for Western Europe alone is fast disappearing (McDonald et al, 1994:271).

The European Union has put in place a series of agreements with other nations in Europe to help prepare them for EU membership. Much of the assistance given has come via the European Economic Area (EEA) Treaty, which came into effect in 1993. This Treaty provides the EFTA countries (Norway, Switzerland, Iceland and Liechtenstein), access to the main advantages of the post-1992 single market in exchange for their adopting the necessary EC legislation (Rothery, 1993). The EEA Treaty created a European free trade area that helped to break the barriers to trade within Europe between members of the Union and the remaining members of EFTA.

THE EUROPEAN UNION AND THE DEVELOPING WORLD

The relationship of many of the members of the Union with developing countries is based on past colonial links, and special preferential treatment has been sought for the colonies. France required the inclusion of its overseas territories in the customs union, including special arrangements for Morocco and Tunisia, as did Italy with Libya. In the Treaty of Rome there was provision for the inclusion of non-European countries that had special relationships with the Community members.

In 1975 the Lome Convention agreement was signed to address the problem of the growing number of associated countries benefiting from the less developed country status (Dearden, 1994a:253). The Lome Convention, a response to the entry of the UK and its associated Commonwealth LDC trade preferences, granted associate status to a total of 69 countries, mainly ex-French colonies from Africa, the Caribbean and the Pacific. The Convention offered duty-free access for the associate country's exports of manufactured and non-CAP agricultural products. Subsequent economic pressures saw some protection imposed on selected products such as textiles. Although 70 per cent of goods from associated countries entered the Union duty-free before the Lome Convention, the benefit arises from products that otherwise face artificially set high prices within the Union.

In 1971, the Community subscribed to the worldwide scheme, the General System of Preferences (GSP), which provides non-associated LDCs duty-free access to developed country markets for manufactured goods. In the 1980s, the Community used the GSP in an increasingly discriminatory manner, on both a product and a country basis. The complex nature of trade preferences faced by exporters to the EU is identified in the seven following categories (Dearden, 1994a:254):

1. Tariff-free trade. Free trade status between EU member states, tariff-free access to manufactured and processed agricultural goods from EFTA nations and Israel.
2. Lome associated LDC associate states. Duty free access for manufactured and most non-CAP agricultural products.
3. Super GSP status to poorest LDCs. Duty free access on a limited range of products. In 1990 temporary status was given to Bolivia, Columbia, Ecuador and Peru, and in 1992 to Central American nations. These temporary status expired at the end of 1994.
4. Special arrangements with 14 Mediterranean countries and Eastern European States. This provides duty free access for most manufactured goods and tariff

reductions for agricultural products in exchange for MFN treatment of EU exports.

5. Non-Lome LDC associate countries that qualify for GSP, such as ASEAN countries.
6. GATT signatories that qualify for MFN status.
7. Least favoured: Vietnam, Cambodia, North Korea, Albania and Taiwan.

Of the LDC trade preferences, The NICs of Asia have had the largest growth in trade with the EU. In 1980 the NICs accounted for 15 per cent of all EU's imports from LDCs, and this increased to 32.4 per cent by 1990 (Dearden, 1994a:256). Although the value of EU's imports from LDC countries increased by US$4.1 billion between 1979 and 1989, the value of exports from the LDCs to the US over the same period was US$36.9 billion. In 1986, GSP status was withdrawn for products from countries where per capita income was higher than US$2000.

In addition to providing access to the European markets, the Lome Convention provided aid through the European Development Fund (EDF). A new Lome Convention is established every five years, and with each new convention a new EDF is established. In Lome Three which started in 1986, ECU 7.4 billion was dispersed in aid (Dearden, 1994a:261).

THE EUROPEAN UNION AND THE USA

Post World War II saw the US take a compassionate attitude to Europe, with aid in the form of the Marshall Plan. However, with the failure of the Bretton Wood System, the decline in the value of the US dollar, and the strengthening industrial power of the European Union, the Americans' attitude changed (McDonald, 1994c:307). Although the major dispute with the Union has been on CAP issues, a crisis in the world steel industry in the 1970s and 1980s saw trade disputes erupt between the US and the Union. This was partially due to both parties protecting and subsidising their steel industries, with the US using import quotas and the Community using various protectionist policies under the ECSC.

This dispute led to a further souring of relationships and the US imposed an embargo on European firms using US goods, patents and licences to build the Siberian pipeline which carried natural gas from Siberia to Western Europe. The US Government also sought to impose taxes on American companies' earnings from Europe.

In 1988, the US passed the Omnibus Trade Act which required the Government to identify countries with unfair trade practices discriminating against the US and to ensure these practices were stopped. If the practices did not stop, the US government imposed unilateral trade restrictions against that country. This Act helped further sour trade relations Between the EU and the US.

The US and the EU have complained about each other's trade practices. The US has complained about the public procurement programme which opens government tenders to companies within the EC to the exclusion of companies from other countries. The EU on the other hand has complained about the US public procurement programme, which is controlled by numerous federal, state and local government rules and regulations.

On the whole, the EU has generally regarded relations with the US as less important than those with the neighbouring Eastern European and EFTA countries.

VISION FOR EUROPE BEYOND 1995

The European Union works in a very complicated and bureaucratic environment. The average European citizen finds it hard to see through and understand the European system. This lack of understanding is the likely reason why there is a general rejection of a European Parliament with supernational powers. The myriad procedures make it very difficult for the Parliament to be a workable entity. At present, too much money and time is spent on power struggles between the Parliament, the European Commission and between the national governments and the EU institutions. Although the Single Market Act of 1986 and the Maastricht Treaty of 1992 give the centre greater powers, it is still not enough for the European Parliament to function as an effective democratic institution for a united Europe. In fact, there is a great reluctance by member countries, such as the UK, Denmark, Spain and Italy, to give the centre this power. With the addition of new member countries, the number of Euro-MPs in the Parliament is an increasing concern. At present the Parliament has 626 Euro-MPs.

There is growing support for a rationalisation of the Union structure and two major schools of thought are emerging. The first, forwarded by John Major, the British Prime Minister is the notion of countries as 'Clubs', and the second is 'Circles', a vision shared by the past French Prime Minister, Mr Edourard Balladur, and Mr Helmut Kohl, the German Chancellor (*The Economist*, 10-16 September, 1994:23).

EUROPEAN CLUBS

John Major has proposed an EU where each member country only participates in those policies and issues in which it is interested. This means a country like Sweden, with its long-standing neutral military status, can commit itself to the EU monetary union but does not have to participate in a common European defence policy. The proposal is to make Europe into a number of clubs, where countries with strong national interests can be accommodated. Britain for example, would like to remain in the EU but does not fully support monetary or fiscal union.

The lack of support was very apparent after the signing of the Maastricht Treaty, and many national governments are not in favour of the speed with which the changes are taking place in a united Europe.

EUROPEAN CIRCLES

The other main vision proposed by the Mr Balladur and the Mr Kohl is to divide Europe into five major circles. The first circle (innermost) will have member countries which want full integration and a decision on all issues. Countries preferring to maintain certain or some national control of policies and issues would then belong to outer circles based on their levels of participation. What policies would be in each of the five proposed circles are yet to be decided.

The proposal would have Germany, France and the three Benelux countries, Belgium, Netherlands and Luxembourg, in the inner circle (circle one), made up of those countries fully committed to total integration. In what outer circles each of the other countries would be depends on what would suit them.

The first danger with this system is that many countries would have to participate in some policies in which they were not interested, in order to participate in the ones they were interested in, and vice versa. Not to participate in some would avoid participating in others. A second danger is that countries in an inner circle might not work with countries in outer circles on a common issue. This would again create power struggles and bureaucracy in which countries would slip in and out of the circles.

Germany and France have proposed this model to enable them to go ahead with integration without being slowed down by less pro-unification countries.

The trouble with both schools of thought is that it is very difficult to decide categorically on those issues and policies that would be favoured at any future point. Countries like Britain and Denmark would probably not commit themselves to an all or nothing agenda. Denmark has already, at the first referendum regarding ratification of the Treaty of Maastricht on June 2nd 1992, decided not to be part of a monetary union, of police co-operation, of a united social policy (refugees), and of a united European defence force (*The Economist*, 1 May, 1993:52). John Major's proposal seems too fluid and may give more support to decentralisation rather than centralisation, the aim of unification. The French and German proposal may give various levels of 'status' to countries within the Union, based on their level of participation, and this in itself may create a huge bureaucracy and a complicated mechanism, far worse than at present.

CONCLUSION

Monnet's dream is facing some challenges as the EU suffers growing pain. Its development towards a European Union has at best been a halting process, in which a range of plans and reports on content and definition have failed to reach sufficient agreement between Union partners. Members had, and continue to have, fundamentally differing views about the objectives of European integration, and this heterogeneity has increased with the addition of new members. The member states of the European Union are collectively experiencing some difficulty in casting off and ceding sovereignty to European institutions. The thought that more can be achieved together than independently seems difficult for some to come to terms with. However, the attractions of a unified Europe are starting to replace the pessimism and nationalism that has daunted improvement over the last four decades. Indeed, the attractions grow stronger with each report of the EU's resurgent economies, and even the timetable for economic monetary union is beginning to look reasonably feasible.

The question of the future shape of the European Union lies at the heart of any discussion on the prospect for integration and co-operation in Europe. The Union is the pre-eminent pole of attraction in Europe and, with the breakdown of the Communist regimes throughout Eastern Europe, it will need to address the role of assisting the reform process within the developing Eastern European Bloc and providing the benefits of a Common Market for all EU member states. The present Treaties had not foreseen the demands being placed on the Union and, as already demonstrated in the unification of Germany, even ethnic and cultural similarities do not necessarily mean the going will be easy.

Growth in size will become a major problem as less developed economies with large agricultural sectors, are admitted which will strain the budget of CAP. Adjustments will have to be made to CAP to accommodate this, as the EU is already finding it cannot sustain its cost within the present membership.

Despite the EMU initiative, economic issues will continue to be a problem due to the recession currently affecting Europe. Implementation of directives that in any way threaten sovereignty continue to be blocked through the Court of Justice which appears to have more say under the new EU structure.

The European Union, as established by the Treaty of Maastricht, has as its aims the achievement of monetary and economic union among its member states by the creation of a single currency and a central European bank. The European Monetary Institute (the forerunner of the European Central Bank) is sited in Frankfurt, and Alexander Lamfalussy is its first president. Public disenchantment regarding monetary union is evident in the large number of negative votes in the referendum in France and Denmark and adverse opinion poll findings in Germany

(Foley, 1994). However, a majority of political leaders remain convinced that a single currency is a highly desirable objective which would bring great benefits to their citizens.

The Union also aims to achieve a common foreign and defence policies which again do not have unanimous support within the Union.

There is widespread apprehension over the prospect of Euro standards. A recent publication, *The European Community: Facts and Fairytales*, published by the UK Foreign Office (1994), has documented some stories circulated within the UK which influence the UK European voting population:

- EU bans curved cucumber
- Home-made jam will be banned
- Sandwiches must be made on their day of sale
- EU hygiene rules will force butchers' shops to close
- Charity shops can't sell second-hand toys
- EU will ban prawn cocktail crisps, soft cheeses, farm-fresh turkeys, milkmen, beef, mince etc.
- EU will allow export from UK of live horses for slaughter
- EU insists carrots are fruit
- EU requires standard road speed limits.

The success of the European Union depends considerably on how it deals with the following issues:

- its structure, which is considered to be too centralised
- the interests of its minorities
- the large economic and social disparities within its member states
- the establishment of a common foreign policy.

Major projects that need to be dealt with include those aimed at:

- Environmental protection
- Reducing unemployment
- Fighting organised crime
- A common foreign and security policy

Europe is now made up of a 'multi-speed' collection of countries pulling in different directions and choosing only what is good and convenient for themselves. The question still remains whether it is possible to have a 'one-speed' Europe.

Chapter 4

North American Free Trade Agreement

Over the years, advocates of free trade have learned to devise trading rules with only a few nations at a time, and to focus first on their neighbours. Healthy trade with neighbours contributes to more friendly political relations. Economic exchange and political harmony seem to go hand in hand. These initiatives help account for the post World War II proliferation of regional and continental trading blocs, notably the European Union (EU) which we discussed in chapter 3. In general, most bilateral (two-nation) and multilateral (many nation) pacts aim to liberalise trading or to make it freer by reducing and eliminating government tariffs, quotas and other barriers. Such agreements often include provisions that protect certain industries from the negative effects of free trade. Not surprisingly, these protected industries resist further liberalisation of world trade. 'Resistance comes from political forces, especially those who identify freer trade with the loss of national sovereignty and self-determination' (Swanson, 1994:8).

Despite resistance, following on the development of the European Union, two major advances were made in 1994. First NAFTA (North American Free Trade Agreement) was adopted, significantly liberalising trade within North America. Second, new accords, developed under the Uruguay Round of the General Agreement on Tariffs and Trade (GATT), were finally approved, significantly liberalising trade between trading nations throughout the world. In this chapter we will look at the reasons for the formation of NAFTA, and the effects of NAFTA on the three member countries and the rest of the world.

MAP OF THE NAFTA REGION

INTRODUCTION

Europe has long been an established market for the US. Under former President Harry Truman, the US came of age as a global power. After the defeat of Germany and Japan at the end of World War II, America took on the burden and the glory of world leadership from an exhausted Britain. Assisted by gifted and confident advisers like Dean Archeson, George Kennan and George Marshall, Truman created a new liberal order based on democracy, free trade and market economies. Archeson, Kennan, Averell Harriman and others, later came to be known as the 'Wise Men' or the 'Establishment', a self-perpetuating elite which first devised and then implemented a new post-war US foreign policy (Barber, 1992:29). The Bretton Woods system, the Marshall Plan, the NATO Alliance and the Truman Doctrine set out the policy of 'containment' of Soviet power, and together formed the cornerstones of this new world order, which succeeded beyond all expectations.

Had Marshall failed to spell out his plan for the recovery in Europe at Harvard University on June 5, 1947, the US would have risked not only a humanitarian disaster, but social economic and political disintegration in Europe (Dinan, 1994:17). By acting, the US preserved Western Europe not just as a political ally in the struggle against the Soviet Union, but also as a market for American goods.

In short, the US policy was a remarkable combination of selflessness and self-interest, of idealism mixed with a hard-headed calculation that the recovery of the German and the Japanese economies served the vital interests of US business and commerce. This action secured a market for American goods, but this scenario changed under the EU with emphasis on the alleviation of problems in European industries, rather than free trade. Also, with the collapse of the Soviet Union, there is less degree of dependence on the US by the EU for a security umbrella.

During the 1970s and 1980s the US competitive advantage in the production of goods and services was reduced through strong competition from Japan and other developing Asian nations, especially in motor cars and electronic goods (Salvatore, 1994:29). With the establishment of the EU, trading partners outside the Union found it increasingly difficult to trade with the Union. The EU, as we discussed in chapter 3, became an effective trading bloc for other countries, including the US which had once contributed US$12 billion for the reconstruction of Europe under the Marshall Plan (Dinan, 1994:17)).

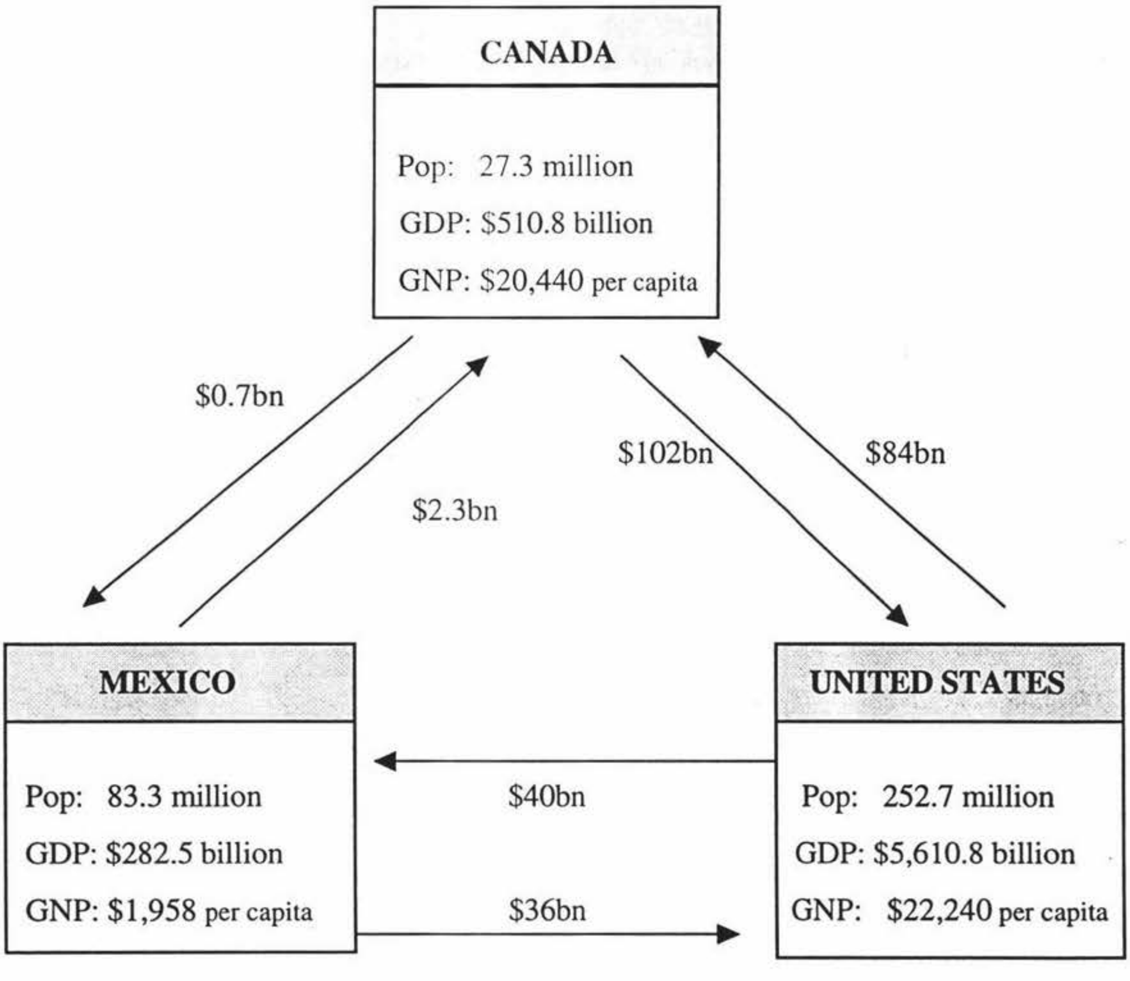
As the US's competitive advantages have weakened or disappeared, government policies have increasingly changed (Bhagwati, 1993). Playing the multilateral game, under GATT rules, was inadequate as the sole means of protecting and advancing American interests. Thus, continued efforts to reduce barriers through GATT must be accompanied by a mixture of other approaches, such as:

- threats of unilateral retaliatory actions, if necessary, to press the claims of American enterprises for better access to overseas markets;
- bilateral arrangements to liberalise trade and investment with selected partners, notably in the Western hemisphere and in the Pacific; and
- the promotion of free trade on a regional basis - NAFTA is the implementation of this approach.

NAFTA represents an important policy change by the United States to international trade and development in recent years. The United States used its global dominance in the post-war period to promote the reduction of barriers to trade and investment on a multilateral basis (Bhagwati, 1993). It generally opposed the discriminatory application of trade barriers, and worked actively to encourage the gradual removal of preferences in the British Commonwealth.

The creation of NAFTA brings together two rich industrialised nations and one developing nation. This creates a US$7 trillion market with over 368 million people, making it the largest retail market in the world (*The World Development Report*, 1993). Figure 4.1 illustrates the strengths of the affiliation.

Figure 4.1: NAFTA - 1992 Statistics (in US$)



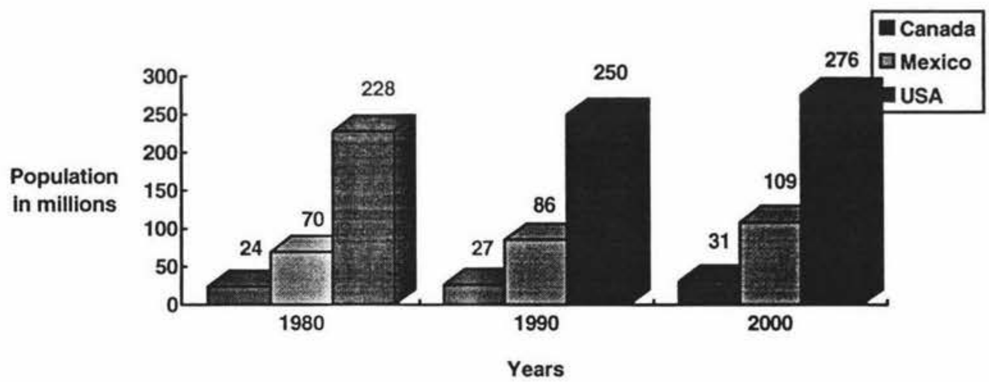
Source: *The World development Report* (1993) and *IMF* (1993)

The population within NAFTA is also expected to increase greatly from the present 363 million to an estimated 416 million people by the year 2000 (see

Figure 4.2). This increase is predominantly from the increase in the Mexican population. Sixty nine per cent of NAFTA's current population of 363 million people reside in the US. However, the US and Canadian populations are expected to grow by 11 and 17 per cent respectively during the current decade, while Mexico's population will grow by more than 25 per cent.

Another of Mexico's demographic contributions to NAFTA is its youthful productive population. Almost one quarter of all US and Canadian citizens are under 20 years of age but in the case of Mexico this figure is more than 47 per cent (Ready, 1993:9). With a developing economy such as Mexico, the youthful population is seen not only as an asset feeding the labour market, but as a sizeable product market as the population matures.

Figure 4.2 NAFTA Nation Populations (in millions)



Source: *US Department of Commerce*, March 1994

NAFTA FORMATION

The formation of NAFTA was swift, allowing little time for public debate. In fact, this is seen as a political ploy by both President Bill Clinton and past President George Bush to remove it from the public arena for a speedy implementation (Fatemi, 1994:4).

In June 1990, the President of Mexico, Carlos de Gortari, and the then President of the United States, George Bush, announced their intention to negotiate a free trade agreement between their countries. In mid-1990, Canada joined the dialogue process, which culminated in formal negotiations in June 1991 for a trilateral free trade area (Herremans et al, 1994:118). The NAFTA agreement was eventually signed on 17 December 1992, and came into effect on 1 January 1994.

NAFTA is the most comprehensive free trade pact (short of a common market) ever negotiated between regional trading partners, and the first reciprocal free trade pact between a developing country, in this case Mexico, and the industrialised countries of the United States and Canada.

In spirit, NAFTA is a new, improved and expanded version of the Canada-US Free Trade Agreement (Canadian-US FTA). The NAFTA agreement mostly involves commitments by Mexico to implement the degree of trade and investment liberalisation promised between its northern neighbours in 1988 (Ready, 1993). However, NAFTA goes further by addressing unfinished business from the Canadian-US FTA, including protection of intellectual property rights, rules against distortions to investment, for example, local content and export performance requirements, and coverage of transportation services.

In essence, NAFTA is a three nation trading alliance that:

- stretches from the Yukon to the Yucatan Peninsula (covering Canada, USA and Mexico);
- enables the freer cross-border exchange of goods and services produced throughout North America and of investment capital between the three nations;
- signals increased co-operation and collaboration in other such areas as labour relations and workplace standards. As economic interdependency grows, so does the need for a broader concurrence.

Advocates for NAFTA argued that it would provide an arena for member nations' businesses to test their wings in a rapidly globalising economy (Nicholson et al, 1994:67). If they can compete with each other directly, they might become competitive in worldwide markets. NAFTA is a geographical trade grouping and is expected to include more members, perhaps through the redefinition of the geographical spread to include all or some of the South American countries. Negotiations began in January 1995 to admit Chile as the fourth member.

EU BARRIERS TO US TRADE

Since the formation of an economic union in Europe, the US had difficulty exporting its goods and services to the Union (Bhagwati, 1993). This is illustrated in the following examples of goods and services exported to the European Union.

In 1986, the US threatened to block $1 billion of agricultural imports from Europe - a trans-Atlantic trade sanction of unprecedented size - if proposed EC barriers against imports of American feed grains were not retracted. The French government gave uncompromising support to its farmers, but this time France was unable to act on its own. Although trade policy was co-ordinated by the European Commission in Brussels, the US government undermined EC support by carefully targeting the major farm products of its members - olives from Italy, cognac from France, whisky and gin from Britain, cheese from the Netherlands - a strategy that led journalists to dub the affair 'the Yuppie War' (Evans et al, 1993:3-4). The European Commission attempted to support the French position, calling for a counter-threat, but these were resolutely blocked by the others, and the issue was quickly settled on American terms. Former US Trade Representative Carla Hills said, '....the EC has to open its market for electrical equipment. We must insist on opening markets in a reciprocal fashion. I was harsh with the French when they tried to keep our oil seeds out. We exhausted all our GATT remedies' (Morris, 1993:32), She also said that EC procurement rules, revised in 1993, discriminate against foreign companies.

Provision of services to the EU by foreigners is also restricted. Trade in services is a relatively new matter in international trade negotiations, and one that is important to the US trade. Services was first addressed in the United States' free trade agreement with Israel in 1985 (de Melo and Panagariya, 1994). However, this agreement was a non-binding declaration of the need to develop reciprocal market access and national treatment for services trade. The 1988 the Canadian-US FTA covered services and obliged each country (and its provinces or states) to give national treatment to the other's service providers.

For example, in 1989, six European countries (France, Greece, Ireland, Italy, Portugal and Spain) did not permit the direct insurance of risks in their territory by insurers not authorised and established there; three countries (Denmark, Luxembourg and the then West Germany) permitted customers to deal with foreign insurers, but prevented intermediaries (brokers and agents) from engaging in the placing of business across frontiers; and three other countries (Netherlands, United Kingdom and Belgium) generally had no restrictions in this respect (Gorman, 1993:18). However, it now appears that the EU single internal market will not be a barrier to US firms providing insurance services within Europe. But this is based on assurances from EU representatives to the United States, rather than any public commitment or the actual experience of US insurers. The unsettling feature of the EU's insurance reciprocity policy is that it nowhere commits the EU to a non-discrimination policy regarding foreign insurers. However, any open denial of access to the services market would be against the spirit of WTO.

US-CANADA TRADE

Bilateral trade in goods and services between the two countries, the world's two largest trading partners, totalled nearly $195 billion in 1990 (Wallace, 1991) and in 1993 the total stood at $237 billion (*The Economist*, 14 January, 1995a:34), an increase of 22 per cent. The Canadian-US FTA of 1989 was signed to facilitate freer trade between the two countries.

Within a year of the Canadian-US FTA implementation on 1 January 1989, an 18 per cent increase in US merchandise exports (reaching $84 billion in 1990) to Canada occurred. In effect, the Canadian-US FTA was the beginning of the NAFTA.

Some of the benefits to the US and Canada of the Canadian-US FTA are (Wallace, 1991):

- **Accelerated tariff removal.** Countries in the US and Canada are anxious to move to free trade, as demonstrated by the number of industry petitions to remove bilateral tariffs faster than specified in the Canada-US FTA. Based on industry requests, tariffs on some 400 products were removed in April 1990, generating $6 billion in bilateral trade.
- **Standards simplification.** Under the Canada-US FTA umbrella, and through the efforts of the private sector, progress was achieved in harmonising standards. For example, 12 Canadian and US standards have been combined to form one single standard. The big benefactors are manufacturers who can now produce to only one standard. In addition, consumers have wider product selection at lower cost.
- **New government procurement opportunities.** Since the implementation of the Canada-US FTA, more than 200 additional Canadian government contracts totalling nearly $13 million (for the period 1 January 1989 to 31 December 1989) have been awarded to US companies of all sizes. Without Canada-US FTA these contracts would not have been open to US exporters. Added to this are the spin-offs of the Canada-US FTA: Americans and Canadians are discovering new ways to work together in business, tourism, education and the manufacturing environment. For example, a New Brunswick manufacturer of file folders began buying paper stock from a US company in Raleigh, North Carolina. Canadian tariffs on paper, previously as high as 25 per cent have been reduced by 60 per cent, making American products more price competitive.

CANADA'S MOTIVATION FOR WANTING A FTA WITH THE US

There were several key reasons that led Canada towards a free trade area with the United States. The following are some of the main reasons:

Increasing global competition

Historically, Canada's competitive strengths have emanated from its resource endowments - grains, fish and food products, forest products, energy and basic metals and minerals. However, prospects for rapid export growth in these areas are limited.

In agriculture, Canadian grain producers are highly dependent on exports. They face tough challenges of slowly growing export markets and the adverse effects of agricultural protectionism. In forest products, growth prospects appear constrained by the adequacy of future timber supplies. For many metals and minerals, new technologies and materials have reduced the demand for important Canadian exports (for example, nickel, copper, zinc, and lead), and new sources of supply have reduced many Canadian market shares. In energy, export prices for petroleum and natural gas are currently about half their 1981 levels (Morici, 1991, 89).

These trends have created a decline in the contribution of natural resources to Canadian exports. Raw materials, in which Canada had a competitive advantage, were diminishing, and Canadians began to realise that their market opportunities in resource products would no longer be sufficient to sustain adequate growth, and that the country must therefore become more competitive in manufacturing (Levy, 1994:103).

After seven rounds of GATT-sponsored multilateral trade negotiations, Canada's tariffs were no longer sufficient to protect its manufacturing from foreign competition, and foreign tariffs were no longer the major impediment to Canadian exports (*The Economist*, 14 January, 1995b:35). The main obstacles to the restructuring of Canadian manufacturing have been foreign non-tariff barriers and the threat of new barriers, especially in the United States. The US trade actions noted above galvanised the view that the US trade protection was a main threat to Canadian manufacturing.

US protectionism

Large trade deficits and adjustment problems in the United States, gave rise to increased protectionist pressures. US trade actions in, for example, the steel and forest products industries and threatened measures in non-ferrous metals, raised concerns about continued Canadian access to the US market (Morici, 1991:14). In Canada, US protectionism has been channelled into complaints about unfair foreign trading practices and the threat by the US to impose penalty duties adversely affects the investment climate in Canada and unleashes political pressures on the Canadian government. Thus, countervailing duties and other remedies against unfair trade became a central Canadian concern during these negotiations.

The goals of the Canadian government in the bilateral negotiations were to seek secure access to the US market by limiting the effects of the US trade remedy laws and exemption from US safeguard actions aimed at third countries; to achieve a clearer, bilaterally agreed upon definition of a countervailing subsidy; and to enhance access to the US market by eliminating tariffs and liberalising non-tariff barriers.

UNITED STATES MOTIVATION FOR WANTING FTA

The following are some key reasons for the USA wanting to have a free trade area with Canada.

International trade politics

Multilateralism has been the basic thrust of a US post-war trade policy. Admittedly, competitive pressures and the limitations of GATT have caused the United States to manage trade and seek bilateral solutions to trade problems.

As US competitive advantages in many agricultural, high-technology and service industries have narrowed or disappeared, the government has focused increasingly on impediments to foreign market access. US negotiators have been forceful in placing agriculture, services, investment, subsidies, government procurement, intellectual property rights, and product standards on the agenda of the Uruguay Round, and in keeping these talks moving forward (Baneth, 1994:149). This agenda includes many of the same issues the United States and Canada discussed in their free trade area negotiations and at the conclusion of the Uruguay Round.

The attention of US negotiators has increasingly focused on the limitations of GATT in agriculture, services, and the wide variety of practices that can affect foreign market access for US high-technology products, trade-related investment policies, subsidies, treatment of intellectual property rights, government procurement and product standards. An agreement with Canada perhaps provided a pointer to GATT in several of these areas and indicated to the EC, Japan and others that the United States is prepared to pursue other avenues if the Uruguay Round fails to satisfy with its benefits.

Economic problems with Canada

In essence, the FTA offered the United States an opportunity to eliminate higher Canadian tariffs and to keep improvements in the trade and investment environment, achieved by the Canadian Government, unchanged, as follows (Wallace, 1994):

- The United States sought assurances that Canada would not again impose aggressive screening and performance requirements on US investment, or limit US access to Canadian energy and other resources.
- Regarding Canadian non-tariff barriers, the United States sought to eliminate or reduce discrimination in federal and provincial procurement and impediments to trade created by product and technical standards and testing.
- The United States wanted to establish controls on Canadian subsidies and eliminate Canadian duty remissions granted to foreign firms in exchange for sourcing or producing in Canada. In the US view, duty-remission benefits for Asian and European automakers compromised the Automotive Agreement of 1965.
- The United States sought a comprehensive agreement on trade in business services and improved market access in financial services.

US-MEXICO TRADE

Economic growth in Mexico will enrich Mexico's consumer base and create additional opportunities for US and Mexican firms. 'The bottom line will be more jobs, lower prices, greater consumer choices for North American workers and an enhancement of their competitive position in the world' (Wallace, 1991:4).

MEXICO'S MOTIVATION FOR WANTING AN FTA WITH THE US

In order to improve its trade performance, Mexico implemented reforms in 1985. Liberalisation proceeded gradually at first, and was consolidated in 1988. It made fundamental changes in its trade policies from high protectionism and looking inward for markets for manufactured goods, to reduced protectionism and a drive to promote manufactured exports. It became evident that some measures were necessary to protect growing Mexican exports of manufactures to the North American market, especially to the United States.

In 1990, Mexico announced its desire for a free-trade regime with the United States. In response, Presidents George Bush and Carlos Salinas de Gortario called for gradual and comprehensive elimination of barriers in their bilateral trade (Fatemi, 1994:5). Mexico's decision to seek free-trade with the US was due to a number of internal and external factors. The following were some direct reasons for its decision to seek a free trade area with the US.

Weakening World Oil Markets

The collapse of the old structure of development became evident when oil prices fell in 1981, and was clearer when oil prices fell again in 1986. The price of oil fell from an average of US$25.5 a barrel in 1985 to US$12.0 a barrel in 1986. Mexican oil exports in 1985 had been $14.8 billion, dropping to $6.3 billion in 1986. Oil amounted to almost 70 per cent of Mexico's total exports in 1985, and less than 40 per cent of the total in 1986 (EIU/Mexico, 1995:33).

The oil shocks made the Mexican government concentrate on two objectives. In the short run it focused on protecting the balance of payments and avoiding a depletion of reserves in foreign currency. In the medium term, the objective was to reduce Mexico's dependence on world oil prices.

Mexico's Debt Crisis

In mid-1982 Mexico was in deep economic crisis (Jaffe, 1994). The international environment was unfavourable to Mexico because of its high foreign debt. World interest rates were high, the price of oil low and thus the revenue from oil, Mexico's main export, was falling. Commercial banks stopped lending and Mexico was on the brink of bankruptcy

Despite the rapid expansion of non-oil exports in 1983 and 1984 by 32.5 per cent and 20.7 per cent respectively, the share of oil to total exports was still as high as 68.2 per cent in 1985. The Mexican economy was extremely susceptible to the influence of oil prices and the reduction of Mexico's dependence on oil revenues became a major target (Lustig, 1992:39).

In 1988, trade liberalisation, combined with the freeze on the peso, forced exports up. Although non-oil exports rose by 15 per cent, those of oil fell by 22 per cent. Thus the trade surplus was reduced to only $1.7 billion. In 1989, imports grew by 24 per cent, exports rose by only 11 per cent and the trade deficit was US$645 million. In 1990 the trade deficit shot up to US$4.4 billion (EIU/Mexico, 1995:33).

US Protectionism

In 1992, 63 per cent of Mexico's exports went to the United States. For manufactured goods, the proportion exported to the United States was around 80 per cent (Morici, 1990:106). In other words, the success of Mexico's new trade and industrial policies - if development is to be export driven to the extent contemplated - hinges on continuing and growing dependence on the US market. The extent to which industrial efficiency develops in Mexico, should permit penetration of many markets. However, for the foreseeable future, the crucial external market, indeed the only major foreign market, is the United States.

US economic measures and performance have great influence on Mexican policies. However, inadequate relief from the burden of interest payments on external debt could force the Mexican government to take unilateral action. An increase in the US and world interest rates could create problems for the Mexican economy. Because of the combination of export-led growth and great reliance on the US market, any faltering in the US economy would also have severe impact on Mexico. Growing US protectionism poses a great danger to Mexico, and would prevent it from effectively pursuing its liberalisation policy.

Attraction of Foreign Investment.

Foreign direct investment was never a large share of total investment in Mexico. In the 1980s it was about 10 per cent of total gross fixed investment. In 1979, accumulated foreign direct investment amounted to US$6.8 billion. By 1989 accumulated foreign direct investment had risen almost fourfold to US$26.6 billion, and over 60 per cent of this investment came from the United States. The US share in new foreign direct investment in 1989 was even higher, at 72 per cent of the total (Lustig, 1992:125).

Mexico embarked on a dramatic liberalisation of its foreign trade regulations in 1985. Requirements for import licences were relaxed. In 1985, 92 per cent of domestic output was protected by licences, but by the end of 1990 the ratio had been reduced to about 18 per cent (Lustig, 1992). Similarly, tariffs were reduced from 100 per cent in 1985 to 20 per cent in 1987.

In May 1989 a new set of rules repealed all previous regulations governing foreign investment and expanded the range of operations. One hundred per cent foreign ownership was allowed, provided certain conditions were met. The new rules were also designed to standardise requirements and increase efficiency in the authorisation process. For example, approval for any application would be automatic if the regulating body did not rule otherwise within forty-five days (Lustig, 1992:125-128).

UNITED STATE'S MOTIVATION FOR WANTING AN FTA WITH MEXICO

The benefits of a bilateral agreement between Mexico-US are largely political. The US wished to strengthen Mexican democracy by backing its economic reform.

In the late 1980s, Mexico began a process of internal economic reforms, reducing subsidies and restrictions on foreign investment, slashing tariffs, and eliminating import quotas (Jaffe, 1994). Political stability in Mexico was dependent on the success of these economic reforms, and in turn their success was dependent on expanding manufactured exports to the United States. US national interests are clear: political stability in Mexico was vital to US security.

The Caribbean Basin is one of the principal focuses of traditional US security interests in the world (Shelburne, 1994). Although Washington's attention to Cuba seems to stem more from ideological than security considerations, Cuba represented a major obstacle in relations with the former Soviet Union. Although Latin America's security significance to the United States has been declining steadily, the region's security still tends to be perceived as important.

Mexico's strategic position between Latin America and the US could become increasingly significant for the United States in the context of new security interests. Complex issues such as migration, environmental protection, drug trafficking and economic and political stability will require even more US attention to Mexico in the coming years.

United States net gains from the creation of a free trade area with Mexico are limited by the considerable difference in economic size. Trade with Mexico (the third largest trading partner of the United States) represents just 6 per cent of the total US foreign trade, although it contributes about 50 per cent to the total US-Latin American trade flows (Hartlyn, 1992:173). For the future of the continent the United States sees trade liberalisation and regional agreements as one important vehicle for fostering development in Latin America and keeping close relations with these potential markets.

If free trade works, it would increase productivity and jobs for both the US and Mexico. Also, it is the best solution to resolve the issue of illegal Mexican immigrants to the US. With greater economic opportunities at home, there is little necessity for Mexicans to seek employment in the US. Mexico offers the United States some of the same kinds of opportunities that Eastern Europe offers the EU, in other words a large and growing market of 85 million people and inexpensive labour. Mexican President Carlos Salinas said that Mexico prefers to export Mexican tomatoes rather than Mexican tomato pickers. NAFTA is essential for the creation of jobs in Mexico so that 'no more Mexicans go to the US looking for jobs' (Cornelius, 1993:1).

Mexican emigration may not increase massively, despite extensive restructuring and displacement from traditional agriculture, for the following reasons:

- Many rural residents in Mexico have diversified their sources of income, making them less dependent on income earned from producing agricultural commodities like corn, which will be most affected by NAFTA.
- A free trade zone might induce more US agricultural producers to expand into Mexico during the 1990s, creating additional jobs there, instead of in the United States as they did in the 1980s.
- The links between internal migration in Mexico and emigration from Mexico are not as direct as is often assumed; even if economic restructuring increases internal population movements in Mexico, this may not translate into a great deal of international emigration.
- European experience teaches that free trade and economic integration can be phased in a manner which does not produce significant emigration, even with complete freedom of movement. NAFTA-related economic displacement in Mexico may yield an initial wave of migration to test the US labour market, but this migration should soon diminish if the jobs that these migrants seek shift to Mexico.

The admission of Mexico to NAFTA opens significant opportunities for US producers, particularly in Mexico. The services market will also be an area of bountiful return for US service providers. In the insurance field, for example the newly allowed ability of US insurers to acquire Mexican brokerage operations will add value to the US insurers' operations (Otis, 1992:34).

IMPLICATIONS OF A FTA BETWEEN THE US AND MEXICO ON CANADA

US interest in an agreement with Mexico bring significant challenges to Canada. During the 1980s, Mexico substantially increased its exports of secondary manufactures to the United States to compensate for lower oil prices, to service its external debt and, to drive its domestic economic reform and trade liberalisation programmes (Levy, 1994). In the process, Mexico's exports to the United States became similar to and competitive with those of Canada. A Mexico-US trade pact could further reduce many benefits of preferential access to the US market that Canadian-based manufacturers had anticipated from the Canada-US FTA.

In September 1990, Canada asked to be included as a full participant in the negotiations for a free-trade agreement between Mexico and the United States (Herremans et al, 1994). It was motivated mainly by the desire to protect its own agreement with the United States in a number of areas.

Impact on Canadian exports

Mexican exports have not been as substantial or as rapidly growing in the traditional areas of growth of low-wage, industrialising economies such as footwear, apparel and steel. Mexico's export drive came after the United States and other industrialised countries had established policies to limit imports in these categories (Jaffe, 1994; Levy, 1994). A trade agreement with the United States would give Mexico preferential status with negative impact to Canadian producers. Canadian producers had been rationalising and restructuring their industries to meet increased competition from US imports and to penetrate the larger US market. Canadian commercial interest with the US will be compromised if a free trade arrangement between Mexico and the US eventuated; especially so if the arrangement excluded Canada.

Canadian interests could be compromised if the US decided which integrated US/Canadian industries would be sheltered from Mexican-based competition through whatever transitional provisions or trade management agreements emerged from the US-Mexican negotiations. The best way for Canada to protect these interests was by participating directly in the negotiations.

Also, Canada had a significant stake in ensuring that the arrangements that liberalised US-Mexico trade became increasingly consistent with free trade area rules and disciplines as they evolved. Comparable rules for US trade with both Mexico and Canada would better ensure the ability of each to hold the United States to its commitments in areas such as countervailing duties.

Effects of the Maquiladore operations

This programme originated from the private activities of US companies and Mexican landowners, whereby the US companies wanted a cheaper way to assemble American made parts into final products (Fatemi, 1994). In the past, Canada had also undertaken to invest in Maquiladore operations in Mexico.

The existence of such a programme is in Canada's interest. It would be far more productive to use cheap labour in labour intensive industries in Mexico rather than concentrate on labour intensive operations in a high wage environment such as Canada. However, there is concern among the Canadian industrialists as the contribution of Canadian-US border programmes to inter-corporate trade is around 50 per cent, illustrating the importance of having corporate connections on both sides of the border (Bosworth et al, 1992).

Some 20 per cent of the US-Mexican trade is of an inter-corporate trade nature and is growing rapidly, while such trade between Canada and Mexico is still in its infancy (Bosworth et al, 1992). Therefore, to protect Canadian interest it is essential for Canada to participate in direct investment in Mexico. It is in Canada's interest to participate along with the US in the export opportunities of a growing Mexican economy.

To sum up, Canada wished to preserve the US-Canada free trade area and to prevent Mexico from gaining a margin of preference in the US market as a result of a bilateral agreement between the US and Mexico. This was the basis for the Canadian politicians' motives for entering into a trilateral free trade arrangement.

TRILATERAL NEGOTIATIONS IN THE FORMATION OF A NAFTA

Table 4.1 NAFTA Timeline

1989	US-Canada FTA established on 1 January
1990	Mexico announced its interest for a FTA with the US
	Canada asked to be included as participant in the US-Mexico negotiations
1991	Canada announced its intention to join a trilateral FTA on 5 February
	Trilateral meetings began formally in Toronto on 12 June
1992	Negotiations completed on 12 August
	NAFTA signed on 17 December
1994	NAFTA came into force on 1 January

The trilateral NAFTA negotiations proceeded rapidly over the next fifteen months. They were conducted by six major negotiating groups divided into twenty teams (Globerman and Walker, 1992). The groups covered market access, trade rules, services, investment, intellectual property and dispute settlement. Outside the NAFTA negotiations, but related to the agreement's eventual approval by the United States and Canada, were parallel negotiations with Mexico on environmental issues and on safety and labour standards. Rules of origin, especially in the automotive sector, and the length and nature of transition phases, particularly in agriculture, provoked serious conflicts. Canada eventually decided to negotiate a separate agreement with Mexico covering agriculture. This differs from the Mexican-US agreement in agriculture, mainly by giving Canada and Mexico more protection against each other's exports of sugar, eggs, poultry and dairy products.

A draft text of NAFTA was announced on 12 August 1992 and initialled in San Antonio, Texas, on 7 October. Formal signing of the agreement, before to submitting it to the respective legislatures for approval, took place in the three national capitals on 17 December 1992 (Fatemi, 1994).

NORTH AMERICAN FREE TRADE AGREEMENT: NAFTA

The NAFTA agreement came into effect on 1 January 1994 (Salvatore, 1994:21). NAFTA's goals include the elimination of tariffs over the next 15 years, promotion of competition, and opportunities for increased investment in member countries.

NAFTA's newest potential member is Chile. A formal invitation was sent after NAFTA's Miami summit meeting in 1994. The admission process was expected to take one year, provided that fast track procedures were endorsed and that Chile's application was considered separately from the presidential election in 1996 (Stutchbury, 1994:10). This process, however, has been complicated by the Presidential election, and Chile's membership is likely to be considered after the elections.

NAFTA - THE TRADE AGREEMENT

With its freedom of access between countries and markets NAFTA goes further than any other trade agreement signed in the 1990s. The agreement offers increased trade opportunities for regional businesses and concessions that are larger than the EU or the WTO, particularly in finance, investment, intellectual property, labour rights, transportation and environmental issues. NAFTA's aim focuses on the liberalisation of trade barriers, whereas GATT was a forum for the setting of future trade and tariff negotiations (*Business Mexico* - Special Edition 1994:11).

MAIN FEATURES OF NAFTA

The NAFTA document is a 2,000 page agreement and took only 14 months to negotiate. According to Article 102 of the NAFTA text, the agreement's objectives are to (Fatemi, 1994:5):

1	eliminate barriers to trade in, and facilitate cross-border movement of goods and services between the United States, Canada and Mexico;
2	promote conditions of fair competition in the free trade area;
3	substantially increase investment opportunities in the three countries;
4	provide adequate and effective protection and enforcement of intellectual property rights in each country;
5	create effective procedures for the implementation and application of the agreement, for its joint administration and for the resolution of disputes; and
6	establish a framework for further trilateral, regional and multilateral co-operation to expand and enhance the agreement's benefits.

Regional Free Trade Area

The objectives were not to duplicate the EU document, which was more an economic union, but to establish a regional free trade area where over a period of 10-15 years tariffs and other non-tariff barriers would be eliminated. This means that tariffs to non-member countries remain in force, as trade will first be fostered among member countries. The agreement provides for 50 per cent of all tariffs to be eliminated immediately; for a further 15 per cent to be removed within 5 years; and the remaining tariffs to be removed within 15 years. Rules were also established to determine products incorporating foreign content so that if more than 50 per cent of the good originates from the NAFTA end, it is allowed free access (Solocha, 1994). If less than 50 per cent, then a tariff will apply.

MAIN ISSUES OF NAFTA

The NAFTA agreement provides for the elimination of all duties, allowing for freedom of entry into member nations' markets. Where this is not practical, a programme has been designed over five, ten and fifteen years to initiate full compliance. GATT on the other hand only provided for the elimination of duties in certain areas. The EU has instigated a common external tariff and, within this, 65 per cent of all exports are traded within the tariff net. (Goldstein, 1994:36).

The substantial significance of this freedom of entry is demonstrated when US firms can establish subsidiaries in Mexico and market the same range of services as an equivalent Mexican firm. The US firm would not be required to hire nationals or limit the size of their operations. An example of this is in telecommunications, where major marketing opportunities exist for US companies who are looking for investments. In comparison, the EU is still struggling with deregulation of its communications sector. Within the EU, the United Kingdom is the only member country that has deregulated its telecommunication industry and invited open competition.

The impact of increased deregulations has seen 130 new competitors enter into competition with British Telecom. Interestingly, 62 of these providers are Cable TV companies who are expected to achieve a seven per cent market share of the traditional telephone subscribers by the year 2002 (*The Economist*, 16 July, 1994:57).

Motor Vehicles

Motor vehicles were one of the more contentious areas of the negotiations. While the 50 per cent rule mentioned above applies, it is to rise to over 60 per cent in the next eight years (Holmes and Falconer, 1992:14). The system of valuing is to be on a net cost basis to protect industries in Canada, the US and Mexico and make it more difficult for imports of motor vehicles from countries such as Japan.

Oil

Mexico has significant oil reserves. It is estimated to have the eight largest oil reserve in the world, twice the size of the US (Holmes and Falconer, 1992:14) with strict laws on exploration and refining rights. The Mexican government-owned company PEMEX is a major player in the economy, but is in debt. In the oil industry, there is scope for increased efficiencies using technology, proper investment, marketing and management, and Mexico is expected to open up the energy sector to downstream activities such as electricity generation and non-basic petro-chemical goods. The Mexican government is expected to retain control over its resources, but has agreed to NAFTA rules on import/export restrictions, tax and national security. The currency crisis of 1995 may well erode the Mexican government's control of the oil industry as the US has demanded joint control in exchange for aid in support of the peso.

Steel

There is already considerable trade in steel between the NAFTA countries (Solocha, A. (1994). Tariffs apply, but these will be eliminated. It is expected that current development will change in this industry when tariffs are lifted. The US is pursuing a world steel agreement through GATT negotiations. Already the US has increased its exports of steel to Mexico, and all three countries stand to gain as imports from other countries decline. US exports to Mexico tended to be high quality steel products while the imports were generally lower-quality steel products. In 1990, the US had a $.0.3 billion trade surplus in steel products with Mexico (Hufbauer and Schott, 1992), but the country needs further investment in its industry to maximise its performance.

Electronic Goods

The US is a significant supplier of electronic equipment and machinery to Mexico, and Mexico and Canada are large suppliers of finished goods to the US (Hufbauer and Schott, 1993). The intra-trade between the three is substantial. Most of Mexico's exports go to the US and third country imports where value is added before re-exporting. There are opportunities for US exporters of machine tools and machinery to Mexico, as the high duty rates have been reduced.

Anti-Dumping

The NAFTA agreement has provision to review anti-dumping and countervailing duty determination by administrative authorities in each country. Both Canada and Mexico have been subject to US dumping in the past (Martin, 1993). The agreement also provides for members to take safeguard actions to provide temporary relief to industries affected by surges in imports.

Government Procurement

In an effort to help domestic suppliers within the Association, NAFTA has provided for the gradual liberalisation of the government procurement market in each member country. Government departments' procurement for goods and services are now open to member countries (Martin, 1993:184). For example, parts of the multi-billion dollar US Government Supply tender market is now open to bids from suppliers of all three member countries.

Services

Most trade agreements do not address the services industry, but NAFTA makes provision for the suppliers of services to be treated no less favourably than their own nationals. Some of the services considered for immediate liberalisation are transport, telecommunications, public networks and finance (Martin, 1993:188).

Health, Safety and Environmental Issues

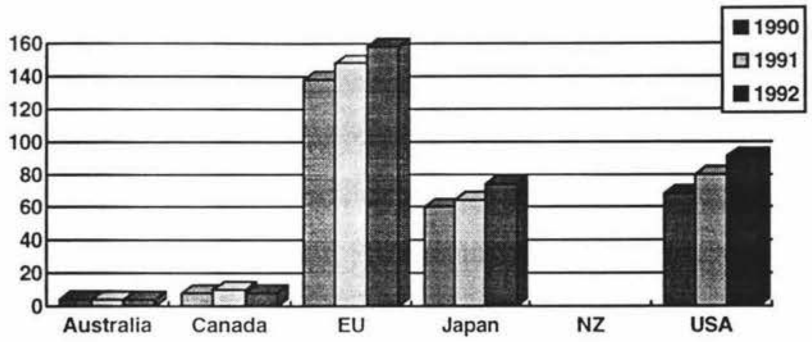
Groups opposed to NAFTA are concerned about issues like lower health, safety and the environment, in particular about industries moving into Mexico where they do not have to meet the same standards. NAFTA provides some protection against this as each member may not lower its own standards. In addition, the Mexican government has made large sums of finance available to help relieve serious environmental problems, especially on the border with the US. One of the problems to be addressed is to ensure that internal labour is not reduced in moving industries to Mexico where standards are lower.

Agriculture

NAFTA addresses the issue of tariffs by programming their removal or reduction. This is in contrast to GATT, which, for the first time, froze tariffs at their current level in an effort to reduce them. The EU is still struggling with farm subsidies, which in 1990 equalled US$134 billion and in 1992 US$158 billion. The USA subsidies were $70 billion in 1990 and $90 billion in 1992. Canada's subsidies were approximately $12 billion (see Figure 4.3). One limitation of NAFTA is that it does not address existing in-country agreements for export subsidies or in-country agriculture subsidies, such as the US wheat aid programme. One example is the US export enhancement programmes, which has been a contentious issue with the Australian Government, particularly as it distorts the cost of wheat production in the US (Thompson, 1994).

Agriculture has been a major hurdle to be overcome in the negotiations. There is much intra-trade between the three countries. Mexico has 20 per cent duties on fruit and vegetables, as well as protection of producers by various means (Martin, 1993). The US and Canada subsidise their grain farmers. The final decision was that 50 per cent of restrictions in each country would be lifted immediately and most other duties would go in 10 years except some sensitive imports such as corn, fruits and vegetables, that would be phased out over 15 years. There are many poor farmers in Mexico who will need time to adjust. In some areas where protection is in place, restrictions by the other countries will continue to apply to those sectors.

Figure 4.3: Farm subsidies - total costs (US$bn)



Source: OECD, presented by G. Thompson, Dept of Foreign Affairs and Trade, Canberra, *ABARE Outlook '94*

Textiles and Clothing

NAFTA has eliminated quantitative controls and provides for the removal of duty on qualifying articles. It is expected that this provision, combined with the freedom of investment, will see labour intensive industries move to Mexico where the labour rates are $1.40 per hour as opposed to the US rate of $14 per hour (*National Business Bulletin*, November 1994:47). An indirect consequence of the move to Mexico by US plants is that consumers will have increased purchasing power, benefiting the US as well as lowering costs of production passed onto the consumer.

Access of Mexican textiles and apparel to the US and Canada has created considerable opposition. Much of Mexico's exports are made up of US parts and then re-exported. The US has a reasonably high duty, and the removal of the duty in the US and Canadian quotas will allow Mexico to compete in both markets. Canada could suffer, as Mexico takes up a larger share of the US export market.

Before President Carlos Salinas becoming President, Mexico had a trade surplus with the US. In 1993, Mexico had a trade deficit of $6 billion largely due to the lowering of tariffs (*Fortune*, August 23, 1993:42).

On January 3 1995, the new President of Mexico, President Ernesto Zedilloo Ponce de Leon, released his economic package on the restructuring of the Mexican economy. The devaluation of the peso had a serious impact on the economy, and the purpose of this package was to attract investment into Mexico from the US, Canada and major European financial institutions. According to a study by Bear, Stearns & Co., Mexico's GDP may fall from its previous 1993 figure of US$333 billion to US$250 billion in 1995, and incomes are expected to drop from US$3,600 to US$2,700 (*Sydney Morning Herald*, Tuesday, January 3, 1995:24.).

Transport

Rules that previously restricted trade or discriminated against US transport companies, banking securities and insurance providers will all be liberalised. As in the EU, US trucking, railway and bus companies will have free inter-country movement after a phase-in period of three years for buses and six years for the trucking firms. NAFTA allows the US to maintain and enforce its standards on how foreign trucks and buses, in particular Mexican, must operate in the US (Walsh, 1994:27).

Intellectual Property Rights

One of the most contentious issues has been that of intellectual property. However, the agreement requires each member to provide adequate and effective protection of intellectual property rights that must be enforceable internally and at borders, in such areas as copyrights, computer programs, patents, designer label products, trademarks etc.

NAFTA's policies on the protection of trade secrets, patents copyright, integrated circuits, industrial design and intellectual property are similar to the GATT's, except that the NAFTA provisions are more comprehensive. NAFTA's additional focus is on piracy of software, biological patents and, between the US and Mexico, copyright of audio visual products and services. These provisions will substantially benefit the US movie industries, record companies and computer/software manufacturers as they start to transfer their expertise to member countries (Walsh, 1994:27).

Environment

The influence of environmental groups is a growing trend world-wide and NAFTA is said to have the *greenest* trade agreement yet negotiated. The agreement has an environmental focus and is explicit in its protection provided, it is based on scientific evidence and administered in a non-discriminatory fashion. As part of this agreement, NAFTA has instituted an environmental commission to allow member countries the use of trade sanctions where environmental agreements have been breached (Lande and Crigler, 1994:12).

Labour

NAFTA's Labour Commission is included in this agreement (Lande and Crigler 1994:12). It assists the maintenance of employee agreements, particularly as living standards improve and workers have the ability to move between member countries. One of the challenges today is the restructuring of the Mexican economy where employees are asked to accept or hold current incomes that are 10 per cent below 1980 levels. In this environment having a Labour Commission is important, but it is debatable just how much impact it will have when the current demand for new jobs in Mexico is increasing by one million new job seekers each year (*Business Week*, 16 January 1995:44).

MEXICO

The following are the main reasons for Mexico's entry in NAFTA.

Broadening Mexican export opportunities in the US market

Trade between Mexico and the United States equalled US$52 billion in 1989. Almost 70 per cent of Mexico's exports go to the United States, with about the same proportion of its imports coming from the United States (Cohen, 1990:3). Given the relative weight of the United States as a source of imports and a market for exports, bilateral liberalisation for Mexico, strictly speaking, means liberalisation in full.

However, many Mexican products face a US tariff higher than the 20 per cent maximum tariff prevailing in Mexico. Clearly, there is room for trade creation through further reductions on both sides. Nonetheless, the elimination of non-tariff barriers may be more important to both countries. For example, about 20 per cent of Mexican imports are still subject to licensing, with import licenses for agricultural products and livestock the most widespread. The automotive sector is still subject to import restrictions (Levy, 1993). The United States also places important restrictions on the import of textiles, steel and agricultural products. The following specific goods are subject to restrictions: wool tailored suits, trousers, skirts, shirts, acrylic fibres and cotton webs in the textile category; tubes, wires, metal sheets and special steels in the steel category; and avocados, potatoes, milk products and sugar products in the agricultural category.

In the United States, protectionism is often disguised through what is called 'contingent protectionism' (Lawrence, 1993). This occurs when US producers, faced with alleged unfair trade practices, such as foreign subsidies or dumping, take or threaten to take action to limit trade or impose countervailing duties. In practice, charges of unfairness presented by US producers have become a common protective device. This is the kind of protectionism that the Mexican government, like its Canadian counterpart, is particularly keen on eliminating. For that reason the creation of a dispute settlement mechanism acceptable to all parties is a crucial item on the NAFTA negotiators' agenda.

Guaranteed increased external capital inflow

Mexico is looking at potential inflows of FDI and the repatriation of capital from nationals due to the improved market access for export oriented activities. Forecasts indicated that a free trade area would expand its domestic reforms, resulting, it is hoped, in boosting investor confidence.

Capital and technology will be the key ingredients for Mexico's development in the near future. However, attracting capital means competing with countries that have similar need. The conditions that make a country attractive for foreign investment are increasingly those which are created by its social environment and less by those provided by its resource endowments.

Mexico's geographical location bordering the US, which is the world's most important economy at present, its cheap, and semi-skilled labour and its political and social stability are all advantages in attracting American capital investment (Rugman and Verbeker, 1994). For Mexico, the potential effect of a free trade area with the United States on direct investment and, more generally, on capital flow could be sizeable. The Mexican economy could also take full advantage of economies of scale and external economies by securing access to domestic and foreign firms in an enlarged market.

A free trade area could also improve the general business climate as a result of diminished uncertainty regarding the future evolution of domestic economic policies and stable access to Mexico's large export market. For Mexico, NAFTA could act as an anchor for economic reforms, further help penetration into the North American economies, and provide an environment more conducive to obtaining appropriate financing for large current account deficits.

CANADA

In contrast to Mexico, Canada aimed to remain competitive by ensuring access to a pool of low wage labour (Mexico), maintaining the status quo in the US-Canada agreement, and preventing discrimination by a US-Mexico bilateral agreement.

NAFTA highlights Canada's need to protect its interests and the preferential access to the US market that had been obtained in its own bilateral agreement. By joining NAFTA, Canada ensures its competitive position relative to the United States in Mexico, and perhaps in Latin America more generally. It also equalises the advantage that US producers would have had through low-cost Mexican imports in competing with Canadian exports on the US market. Importantly, NAFTA also ensures that, as a location for direct investment, Canada is rendered as attractive as the United States for serving the North American market.

Trade between Mexico and Canada is comparatively modest; it reached Canadian $2.3 billion in 1989. In the same year, Mexico exported 1.2 per cent of its total exports to Canada and imported 1.8 per cent from Canada. In 1989, Mexico's share in Canadian imports equalled 1.3 per cent and in Canadian exports, 0.5 per cent. Although Canadian imports from Mexico are small, they have been growing rapidly. In 1989, for example, they increased by 27.9 per cent (Lustig, 1992:135)

It is evident, then, that the bilateral relationship between Canada and Mexico cannot be the sole motivation for seeking free trade between them. Both want to have free trade with the United States, and Canada wants to avoid the trade or investment diversion effects that would result from not sharing in the benefits granted to Mexico in a bilateral agreement (Bhagwati, 1993).

The fear that free trade with Mexico would benefit Mexican workers at the expense of Canadian workers is one of the major issues faced by Canada (as well as the United States). On the contrary, such trade would result in lower production costs, and help Canada to be more competitive in high skill, high wage jobs.

It should be noted that Canada imports a great deal from low income, developing countries, to the benefit of its consumers and without any adverse effects on Canadian industry (Levy, 1994; Herremans et al, 1994). Also, several factors, such as lower productivity and poorer infrastructure, offset Mexico's labour cost advantage.

THE UNITED STATES

A prosperous Mexico means an even larger market for US goods in the future (Jasinowski, 1993:54).

- More than 700,000 US jobs already depend on exports to Mexico.
- The average Mexican spends more than $450 a year buying US products compared with $295 for the average European and $385 for the average Japanese (with five times the income).
- Mexico is US's second-largest market (after Canada) for manufactured exports

Discriminatory trade remedies against unfair competition have been largely directed at Japan and the East Asian economies, the most competitive exporters. NAFTA provides new ways to discriminate against these countries in trade. The introduction of rules of origin/local content into regional trade agreements reduces intra-industry trade with third countries. New technical standards, including environmental protection measures, and specific measures to manage trade with other regional members, will also obstruct third country access. Ultimately, however, the costs of this protection and slower growth are borne by the importing countries.

The risk of discriminatory protection for the world trading system must be assessed against the facts about world trade. Inter-regional trade has been growing faster than intra-regional trade, even during the NAFTA negotiations. The relationship between world trade and economic growth remains strong. The danger is that new discriminatory protection, particularly that against Japan and East Asia, will slow trade growth, with consequences for overall economic growth (Bhagwati, 1993). If the threats of new forms of protection and discrimination arising from NAFTA come to pass, the costs will fall first on those small countries most dependent on GATT rules.

One of the strong attractions of new regionalism to US authorities is that it allows them to discriminate against competitive manufactured exports from Japan and its East Asian neighbours.

The importance of East Asia to the United States as a trade partner should arouse concerns about the effects of discriminatory trade policies. Likewise, the value of NAFTA as a trade partner for East Asia is second only to East Asia's regional trade. The importance of intra-regional trade in East Asia is illustrated in Table 4.2.

Table 4.2 Regional Trade Flows, 1986-91

Exporter	**NAFTA**	**Western Europe**	**East Asia**	**World**
NAFTA	12.6	14.5	17.0	13.1
Western Europe	5.0	12.6	20.6	11.5
East Asia	5.8	16.3	19.6	12.4

Source: Australian National University, International Economic Databank; IMF, *Direction of Statistics, June 1992.*
Notes: East Asia - ASEAN, NICs and Japan; Western Europe - EU and EFTA

EFFECT OF NAFTA ON US, CANADA AND MEXICO

NAFTA has reduced and ultimately eliminated most of the remaining barriers to trade and investment between Canada, Mexico and the United States. NAFTA symbolises a much larger change in economic relations, particularly between Mexico and the United States.

EFFECTS OF NAFTA

Trade has been increasing between member nations, especially as multinational companies continue to look for new opportunities to expand, diversify and, where appropriate, relocate. The US economy is growing, and in 1990 the US GDP was only 12 per cent less than the EC GDP of US$6,034. The projections of GDP growth for 1995 are three per cent for the US and 4.3 per cent for Canada (HSBC, 1994:51).

During 1993 Canada, Mexico and the US invested approximately $11.7 billion in each other's country, double that invested in 1992 (see Table 4.3).

Table 4.3: NAFTA cross border investments (in $US billion)

1993 Investor	**US**	**Mexico**	**Canada**	**Totals**
	In Mexico $2.5	In US $0.5	In Mexico $0.9	
	In Canada $3.8	In Canada $0.0	In US $4.0	**$11.7**
1992 Investor	**US**	**Mexico**	**Canada**	**Totals**
	In Mexico $0.3	In US $1.1	In Mexico $0.2	
	In Canada $2.5	In Canada $0.0	In US $1.0	**$5.3**

Source: KPMG Peat Marwick, printed in *International Business*, March 1994, 98.

Most of this large scale investment was from the multi corporations in the US, investing in 1993, $3.8 billion in Canada and $2.5 billion in Mexico, 106 transactions in Canada and 28 in Mexico. According to Stephen Blum, Peat Marwick's National Director of Corporate Finance, New York, the difference in the investment ratio is because of the investors limited understanding of Mexico's economy (Thurston, 1994:99).

We shall look at one example of the types of investment being made: Conc Mill Corp, a $769.2 million company from Greensboro, North Carolina, whose speciality is denim manufacturing. In June 1993, Conc acquired a 20 per cent ownership ($21 million) of Mexico's Compania Industrial de Parras SA. In 1994, year Conc invested another $39 million, $9 million in the US and the rest in Mexico, to upgrade its manufacturing facilities (Thurston, 1994:99). Conc is maximising its business opportunity, utilising cheaper labour resources in Mexico and expanding its distribution in the US. The advantages for Mexico are the creation of employment and investments; the US benefits from a quality product at a cheaper price.

Apart from textiles, other investment opportunities in Mexico are in automobiles, auto products, advertising/media and office equipment supplier industries (Thurston, 1994:99).

For Canada, growth industries will be in the sectors that are currently experiencing success in the US. These include capital goods, finance, telecommunications, software, oil and gas services. NAFTA has helped Canadian companies rethink their strategies on how to do business in Mexico. Current strategies are to develop alliances and joint ventures. Duff Mitchell, Director of Business Development for the Automotive Manufacturers Association in Toronto, said 'this will not necessarily mean a plant relocation, although there have been some Canadian companies that have done that.' (Thurston, 1994:100). Mitchell then went on to explain that in his opinion Canadian and Mexican companies were similar in size. Due to similarities, the potential for Canadian companies would be in capital for plant modernisation in Mexico.

Theresa Pugh, a lobbyist in Washington for the American Electronics Associations, supports the view that Mexico represents a large market for US companies that want to capitalise on the distribution systems, warehousing, financial and other services plants (Thurston, 1994, 100). Pugh also cautions that even though there are opportunities for manufacturing, allowances must be made for the existing supply agreements that Japanese and American companies have negotiated with a third of the 2,000 export assemblies.

For Mexico, it is a major change in policy, as it was a country with closely regulated ties with other countries. Since the mid-1980s, Mexico has pursued a policy of economic liberalisation, sharply reducing restrictions on trade, cutting domestic subsidies, and expanding the role of private markets. In this respect NAFTA is only a formal recognition of changes that have already taken place. This agreement is, however, very important as it puts the policy changes in black and white and gives them a certain amount of permanence. This, in turn, attracts much needed foreign capital and technology for future growth that the United States and Canada are able to supply.

NAFTA is a major step for the United States, as Mexico is the third largest and most rapidly growing market for US exports. Taking into account the long and accessible border between these two countries, the agreement that nurtures economic growth and political stability in the developing Mexico greatly benefits the United States. NAFTA is also seen as a model for expanding trade relations between the United States and the rest of Latin America.

NAFTA joins countries that are currently at widely different stages of economic development. Most members of the European Union had somewhat similar levels of income per capita when they entered the European Community. Likewise, the levels of income and technology were similar when the United States and Canada formed their free trade alliance in January 1989. In most cases, the main benefits for freer trade are expected to stem from efficiency gains generated by economies of scale and growing competitive pressure due to a broader market (Lipsey, 1957).

When trade is expanded between countries that have relative differences in capital and labour skills, the efficiency gains are more associated with increased specialisation and the reallocation of production facilities (Lipsey, 1957). This has been prevalent as the United States has increased trade with Mexico. Large companies have relocated their manufacturing into Mexico, to (a) bring higher levels of technology into the country and (b) utilise the larger volume of cheap labour available. This would have the effect of greater dislocation of jobs in the United States and Canada. There is also the concern that the expansion of bilateral trade would be at the expense of trade with third world countries. Thus, some of the benefits to Mexico may result from a diversion of US imports from other low-wage countries, and the export gains of the United States may come at the expense of other industrialised countries.

RELATIONS WITH THE EUROPEAN UNION

Discussions between the EU and the NAFTA are basically between the EU and the US as these two countries are each other's most important trading partners, although the Americans continue to enjoy a growing trade surplus with the Europeans. Apart from the importance of trade in goods and services, both partners possess major direct investments in each other's territories (Abghari, 1994). When the EU was completing its internal market and NAFTA had just been signed, it was natural for all those interested in the healthy evolution of the international economy to be concerned about the implications of these trading arrangements.

The EU first came into being through the Treaty of Rome of 1958. The single European Act came into force in 1978. Intra-European trade grew extremely rapidly under the impetus of increasing liberalisation in the Common Market, increasing eight times in volume terms between 1985 and 1987. At the same time, the growth of European trade with countries outside the Union also increased in volume 3.5 times, in part because Europe was growing rapidly and in part because of trade liberalisation under successive GATT rounds (Cushing, 1993:24).

However, in the early 1990s, two identifiable forces for increased protection appeared within the EU against the rest of the world (Cushing, 1993). The first was the emergence of the Eastern European countries and the countries of the former Soviet Union, and their desire to integrate into the world economy. This led to protectionist pressures on the part of those European economic activities that felt vulnerable to competition, especially agriculture, textiles, clothing and steel. The second was the dragged-out negotiations of the Uruguay Round of GATT, especially as much of the disagreement centred on EU-US differences over agricultural protectionism, making it difficult to bring the Round to a successful conclusion.

The completion of the internal market is expected to increase competition and reallocate resources within the EU. In theory, inefficient plants should contract or close down as economies of scale improve efficiency in the wider competitive market. In practice, the threat of plant closures and unemployment in some regions will increase pressures for protection against third-country suppliers such as NAFTA.

The completion of the EU internal market calls for the removal of all internal borders and the adoption of common standards and practices. This requires the elimination of remaining national trade restrictions by EU countries against outsiders. Both NAFTA and the Single European Market (SEM), as discriminatory and reciprocity-based instruments, are unlikely to move the multilateral trading system forward, despite their internal liberalisation of trade.

The protection record of the EU and the introduction of new impediments to trade with third countries through rules of origin/local content, technical standards etc., by the EU and NAFTA suggest that regionalism is not just the reorganisation of discriminatory protection, but also the raising of barriers against non-members. With the major traders pursuing non-transparent instruments of flexible protection, small and medium-sized traders, and particularly developing countries, will be the first to suffer.

NAFTA and the SEM will account for a large share of world trade. Their trade policies will have important effects on the world trading system. The character of the two regional agreements, their effects on trade, and their role in stimulating new regional trade agreements will have far-reaching effects on third countries and on the WTO system.

Both NAFTA and the EU have comparable market size; NAFTA with 368 million people and the EU with 370 million people. Market size is an important trump card in trade negotiations, especially in arranging trade facilitation (e.g., lifting tariffs) between countries or trading blocs. A good example of this is the recent aviation market row between New Zealand and Australia under the umbrella of CER. The former Australian Premier, Paul Keating, felt that any freeing up of the skies between the two countries would be to the detriment of Australian airline operations (especially Qantas) because New Zealand's market size of about 3.5 million people did not offer the same commercial opportunities as Australia's 18 million people did to Air New Zealand. With market sizes of almost similar proportions, both NAFTA and EU have advantages to gain from inter-bloc trading.

Now let us hypothetically imagine the US trying to break into the EU without the clout of NAFTA behind it. The US would have:

- a market size of 250 million people expected to increase to 276 million in the year 2000 while the total for NAFTA is expected to increase from 368 in 1992 to 416 million by the year 2000.
- it would not have unrestricted access to a cheap source of raw materials from Canada to make its final products competitive internationally
- it would not have unrestricted access to a cheap pool labour from Mexico
- it would still have to compete with Canada and Mexico in penetrating the EU. Furthermore, by themselves NAFTA countries will not be able to use their countries' comparative advantage to compete. There could be a waste of resources if these resources were channelled into uncompetitive products which were ultimately state subsidised for export.

THE EFFECT OF NAFTA ON GLOBAL FREE TRADE

The vote that passed the NAFTA agreement through the US House of Representatives on 17 November 1994 was, above all, a vote for regional free trade (Fatemi, 1994). As some people have stated, this vote, which had its moment of triumph, also demands some reflection. Free trade sounds good; the word 'regional' less so.

The question needs to be asked: Are predictions of a world, policed for ever by GATT, in which big regional trading blocs displace the multilateral trading order established after 1945, coming true? The answer to this question is both Yes and No.

Yes, the world is moving towards separate trading blocks, fenced off from one another. The test of NAFTA, as of the European Union before it, is whether it raises barriers against outsiders rather than merely removing them from insiders - and so far, for the most part, it does. Having said this, it must be recognised that there is another liberal force that is supporting open regional trade, and this is APEC. Its membership is also fast growing and at present covers most of the Asia-Pacific region. We will cover this region in some detail in the next chapter.

One must, however, acknowledge that there is a big trend in the world economy towards regionalism, and countries are moving towards economic areas. This is not due to trade agreements, but to politics, although market forces are driving it forward. NAFTA, being a regional trade agreement among three countries, is a major geographical economic area and will undoubtedly have an effect on the way other countries trade with them.

This then leads us to think that the area extending from the North to the South Pole could turn into possibly the largest free trade zone in the world. We are naturally talking about the 'Americas", an area containing 740 million people with a combined gross domestic product of more than $7 trillion.

Nine months after the North American Free Trade Agreement became a reality, the idea of free trade across the hemisphere is moving very quickly ahead; and faster than anyone expected. Countries within the Latin American area are pushing for a reduction in tariffs and quotas, with the aim of creating an 'Americas' Common Market after the turn of the century. The Brazilian Foreign Minister is predicting that a free trade area would include all of South America within the next ten years. This is being called the 'NAFTAmath' (Rocca and Weatherly, 1994; Thurston, 1994). A major step towards this goal was taken in September 1994, when the southern common market (Mercosur) countries - Brazil, Argentina, Paraguay and Uruguay - finalised a free trade pact that had been signed in 1991. This agreement, which goes into full effect on 1 January 1995, embraces a region of 200 million people with a combined GDP of $550 million. See Figure 1.4 in chapter 1 for regional agreements in the Americas.

Other free trade agreements have recently sprouted between Brazil and Venezuela, Chile and Columbia, and Mexico and Costa Rica. The Mexican President Carlos Salinas de Gortari has said that Latin America is taking concrete steps towards the integration of all countries.

With trading areas being set up in all areas of the world - APEC, the European Union, NAFTA, AFTA, Mercosur and CARICOM - there is a distinct possibility that areas where these trading agreements reside will become no-go zones to countries wishing to (a) increase their export potential and (b) develop bilateral trade agreements with other countries. The idea of an 'open world market' with no barriers and/or borders is well and truly becoming a faint hope, with more and more countries deciding and formatting effective ways to protect their trade agreements. But one of the most important considerations with pacts such as NAFTA is the ability of the partners, in this case Canada, Mexico and the United States, to gain maximum benefits with minimum adjustment costs. This depends on maintaining domestic economic policies that ensures growth. Companies are looking first and foremost at the microeconomic climate in each participating country before setting their investment priorities.

A new trade initiative put forward by the US President Bill Clinton at the Group of Seven summit in Naples in July 1994, entitled *Open Markets 2000*, was totally rejected (Clinton, 1994)). It was a modest proposal and basically asked the G7 leaders to review the remaining barriers to trade before the next summit in Halifax, Nova Scotia. This initiative was rejected by those leaders from the European Union, and instead, the 'rich' world's leaders agreed to continue the momentum of trade liberalisation and to review the process. In many peoples' eyes, initiatives such as those presented by Clinton are seen as naive. They can be viewed as moves by the world leaders to get countries to remove 'their' tariff barriers so as to allow the free movement of goods while maintaining a form of protection within their 'agreement zones'.

NAFTA OPPONENTS

While the US has been the driving force behind NAFTA, not all believe that NAFTA is the correct answer. Some of the arguments against NAFTA are:

- The developed countries will capitalise on the poverty of developing countries and exploit their low environmental, health and safety and wage standards. At the same time they will displace locally owned businesses by closure and re-establishment in the developing countries; e.g., Mexico.
- The negotiations were all held in secret, designed to stop citizen participation or awareness. To negotiate on trade the US President appointed trade advisory committees consisting of business representatives with only token labour representation.
- The agreement of 2,000 pages is so complex that it is barely understandable.
- Concerns have been expressed at safety standards in the manufacture of in cars. Under NAFTA it could be argued that cars produced in Mexico to Mexican safety standards without airbags meet the international standard. Opposition to this could be a non-tariff barrier which could result in sanctions against the US.

- The fast track approval of the NAFTA process through government limits Congress's ability to scrutinise and modify trade agreements. The ability of citizens to make representations is denied where fast track legislation is concerned.
- The dispute resolution mechanism is too closed and should be more open, more fair and more sensitive to consumers and the environment.
- The closure of American-based plants and their transfer to Mexico because of lower labour cost is a reality and would cost the US hundreds of thousands of jobs.
- The NAFTA agreement extends beyond just free trade. It lacks a regulatory framework and seeks to eliminate all social, economic, consumer protections and environmental regulations.
- Canadians believe Canada should establish a free trade agreement with Japan that will connect to the Indian and Chinese markets - why hitch the nation to a star that is close to burnout. Furthermore, the US has imposed countervailing import duties on Canadian magnesium because it uses low cost electricity from Quebec and on the low stamp fee paid to provincial governments as it represents a subsidy to the manufacturers.

FUTURE CHALLENGES

The following are seen as major challenges for the NAFTA member nations:

ANTI DUMPING

As tariffs and other trade barriers are reduced, domestic firms in the US will have to face cheaper competitors from Mexico and Canada. The US's traditional defence has been anti-dumping laws that are amongst the most stringent in the world. NAFTA did not address these issues, but instead relied on the countries' existing provisions. This has always been a contentious issue between Canada and the US and now, under NAFTA, is a contentious issue for Mexico.

According to Keith B Anderson, a former economist at the ITC, there were 197 successful anti-dumping actions brought against 42 nations in 1990. Anti-dumping cases have been costly for American consumers. In one example, Anderson calculated that collectively, consumers paid $723,000 for each of the 32 employment positions saved after the US added 139 per cent duty to the importation of silicon from China in 1990 (Richman, 1994:47).

The EU has resolved this problem by standardising anti-dumping laws between member countries (Richman, 1994:46).

TRADE CURRENCY AREAS.

Currently there are three major trade currency areas:

- The European community, whose currency is based mainly on the Deutschmark
- The North Asian community that tends to operate on the Yen
- NAFTA which is based on the US dollar

The potential danger is that if there is a trade war amongst the three major trading groups, the world economy could be seriously affected because of the different currencies involved. Today, the Deutschmark and Yen are overvalued and the Dollar undervalued.

CHANGING SOCIETY.

Although NAFTA may not be directly responsible for the shifts in employment due to a relocation of industries it will, however, heighten awareness of this trend. Relocation and scaling down of American industries has taken place before the formation of NAFTA, and the shifts were often to the low income and high labour markets of Asia. This shift eastwards may be halted to some degree with Mexico as a member of NAFTA. These changes, plus the relocation of firms, have created massive labour movements in the US markets, raising the awareness of the public to movements of investments to regions outside the country. Society does re-deploy, but because of an individual's limited skill set, the only positions available are generally substantially lower in status and remuneration than the position they held previously. This lowering in income status is seen as a major problem in the current US labour market.

In the US, the average length of unemployment is six months. Multinational corporations such as IBM are cutting costs and staff to increase productivity due to intensive competition from similar Asian products. In 1989, IBM had about 400,000 employees, and this was reduced to 220,000 by 1994, with an increase in output. Labour productivity has been increasing by 2.6 per cent per year (Goldstein, 1994:38).

Under NAFTA, unemployment may increase because manufacturers will have choices and options. This may result in Unions becoming more active in the US, in to protect jobs. This could indirectly heighten racial tension between the US, Mexico and Canada (Goldstein, 1994:38).

GREEN PROTECTIONISM

The Green movement has been recognised in the NAFTA agreement, but its recognition does imply a potential trade barrier. The US was the first country to require all cars to be fitted with converters for unleaded petrol, and this immediately restricted a number of foreign car manufacturers, like Volkswagen, from exporting to the USA.

Just how far environmental controls will go as a division for competitive trade is unknown. Other considerations may include the limiting of tuna imports from Mexico because of the use of long line fishing nets that capture dolphins (Goldstein, 1994:39).

Patrick Low, a World Bank economist, suggests that the world's worst environmental problem is poverty. If the major powers continue to suppress trade, this would raise living standards but deprive poorer nations of the ability to invest in their environment (Richman, 1994:49).

CONCLUSION

NAFTA has only been operating since January 1 1994 and it is difficult to judge its success at this time.

Mexico has the greatest to gain and also the greatest to lose. As a developing country wanting to diversify its exports from a dominating oil export base subject to fluctuations in world prices, it sees free trade as the panacea to its previously highly regulated and controlled economy. In January 1995, the US made loans totally $14 billion available to help Mexico (*EIU / Mexico*, 1994). This was seen as an endorsement by the US of Mexico's new economic reforms. Approximately half of this amount was to stabilise the currency and hold the peso from further devaluation. Canada also put up $1 billion, along with several other banks.

Within 10 years all goods and services will be free to travel across the borders of the three nations. Agriculture subsidies and tariffs will have a further five years to change. NAFTA covers financial services, telecommunications and patent protection, which WTO was reluctantly addressing. Never before has such an agreement been so open in terms of markets. There are a few concerns: textiles containing fibre made outside of NAFTA are subject to top tariffs. It is similar with cars: 62.5 per cent of the content must originate from NAFTA countries; the content currently stands at 50 per cent.

For the US, the establishment of a regional trade bloc looks successful. The longer term of 10-20 years should see substantial benefits for US and Canada. Mexico is likely to see benefits in the short to medium term. Politically it has been a very good strategic move for US President Bill Clinton. It will help improve inter-American relations and advance the cause of global trade liberalisation. The signing of the agreement has dealt a savage blow to the anti-NAFTA groups that have included unions, environmentalists, consumer groups and others. While there is some scepticism on the huge loss of jobs to Mexico, this has not so far occurred. While some jobs may go with the transfer of companies to Mexico and the pursuit of cheap Mexican labour, trade is occurring both ways and new jobs are being established in the US, especially in export industries to Mexico. The US has a substantial investment in Mexico and will not let the Mexican economy fold. It wants Mexico to become a success story. With a potential population of 90 million population, it will become a valuable future trading partner for the US.

Canada seems to be much happier with the allocation that have been made to NAFTA from its previous agreement, Canadian-US FTA (Stewart and Litz, 1994). Canada still has a number of issues to resolve internally, especially with Quebec wanting independence. On a more positive note, it has a new trading partner in Mexico, which is potentially good for Canada in the long term. With Chile seeking admission, and possibly other South American countries joining NAFTA, the regional trading bloc is looking strong.

NAFTA is an agreement that has developed out of economic necessity and has been driven by the need for political stability, geographical location and the ability to expand markets that were previously bilateral. NAFTA provides the opportunity for a country to invest in other countries. This will result in increased distribution of wealth between the member nations. It will result in member countries, economic growth and, in the case of Mexico, increasing in wages with resultant higher living standards and increased marketing opportunities (Thurston, 1994:102).

The speed at which NAFTA has been implemented is recognition of its success in the trading world, especially when compared with the long process of the EU. Comparisons of this nature, however, are not valid as the process taken by the EU is towards a 'full' economic union, whereas NAFTA is only a free trade agreement.

The EU is a more sophisticated agreement than NAFTA, and was designed to develop member countries' economies by providing lower prices, economies of scale, higher employment and free inter-regional access. The EU members collectively agreed to tax imports from non member countries.

Chapter 5

Asia Pacific Economic Cooperation

The economic crisis of the post-war period and the waning global influence of colonial powers such as Great Britain and the Netherlands, forced the US to come out of isolation and to this day the country has led the world economy both in economics and in politics. The global economy is now undergoing changes again and the sphere of global influence is shifting from the West to the East (Adler et al, 1986). Asia is seen as the next focal point of global trade and wealth but because of the fragmented nature of politics and history in the region, a united Asia is still a distance away. In the absence of a united Asia and the formation of the Asian triad as predicted by Ohmae (1985), APEC has been promoted as a 'legitimate' equal. In this chapter, East Asia and ASEAN are seen as important subsets of APEC.

In the first part of this chapter, the development of East Asia will be discussed, followed by the background of the Asia-Pacific region, and then economic cooperations in the area will be reviewed. APEC, and to a lesser extent ASEAN, will be discussed in detail.

The Asia-Pacific Economic Co-operation (APEC) was formed in 1989. It serves as a multilateral forum in which Asian and Pacific economies can improve economic co-operation and mutual assistance in developing key economic sectors. It is the only organisation applying economic policy for Asia (especially North East Asia) in a comprehensive way. It is also the only formal framework for closer economic co-operation with East Asia, Australia and the United States that New Zealand is in. In the second part of the chapter we will discuss APEC's development in the last six years. The latter part of the chapter will cover the role of APEC in world economics, its benefits, challenges, key factors and future prospects.

MAP OF THE ASIA PACIFIC REGION

INTRODUCTION

As a result of significant events throughout the global community in recent times, the nature and structure of how and which nations trade with each other has undergone something of a metamorphosis. Acronyms such as GATT, WTO, EU, and NAFTA inundate the global economic community, especially in trade related issues. Whilst each of these acronyms do in fact represent groupings of nations pursuing a common cause, the underlying reasons for their creation and continuous existence is of greater interest.

Relationships are of paramount importance in every facet of international trade and diplomacy. The nations of East Asia and the Pacific region have in most cases enjoyed friendly, reconciliatory awareness over several decades. This has helped the development of the Asia Pacific Economic Co-operation (APEC), a grouping of countries within the Asia Pacific rim with free trade as its major objective. APEC is a relatively new body and as such has a long way to go to achieve its aims. Its goals, however, have to some extent been clearly circumscribed. Despite its relative youth it is already commanding more of the world's trade and resources than the older European Union (EU).

As mentioned above, APEC is a grouping of countries based on free trade and open regionalism. On the other hand, NAFTA is a grouping of nations with free trade within the group while each nation maintains a separate external tariff structure for countries outside the free trade area. The European Union has totally removed tariffs between members and imposes a single tariff structure for countries wishing to trade with Union members. The APEC establishment supports regional trade liberalisation and economic co-operation, and its relationship with non-member countries is based on reciprocity. It therefore differs from the EU and NAFTA in that APEC stands on a non-discriminatory base and is more open to non-members.

The premise of APEC is open regionalism. The concept of 'open regionalism' can be defined as regional economic integration with open regional trade. The concept introduced by APEC is that the members of the group extend the benefits they enjoy to non-members provided trading rules are reciprocated. According to the San Francisco Declaration of the PECC 9th General Meeting in 1992, the declaration specifies the following (Cheit, 1992:122):

1. Economies must increasingly remove barriers to trade, investment and technology flows;
2. GATT disciplines must be applied to trade and investment;
3. The region must provide commercial access to economies elsewhere and need to ensure that these economies also provide commercial access on a non-discriminatory basis;
4. Liberalising sub-regional trading arrangements within the region must be accommodated; and
5. To maintain momentum, the region must actively promote policies that strengthen this dynamic process.

From a regional point of view, the United States, Japan and China are the three main economic powers in the Asia-Pacific region. The United States also remains the world's largest national economy and trading nation. Japan has emerged as a technological leader and the world's largest creditor country, while China has had the fastest growth rate for the last decade and has launched fundamental economic reforms that could make China the single largest economy within the foreseeable future (Caplen, 1994a). Other developing countries in East Asia have tripled their share of global income and trade (Crovitz, 1993; Holloway, 1995). Before going into detail, it is necessary to define the Asia-Pacific region. This chapter will serve to give the background to APEC's establishment and the commitment of the governments of the region. Although wavering from time to time, the commitment has been found to be substantial. The resources of each nation are charted to enable the reader to perceive the vigorous characteristics of this group, which virtually encircles the Pacific Ocean.

The Asia-Pacific 'region' is made up of distinct areas of East Asia, the Pacific and North and South America, including New Zealand and Australia (Table 5.1).

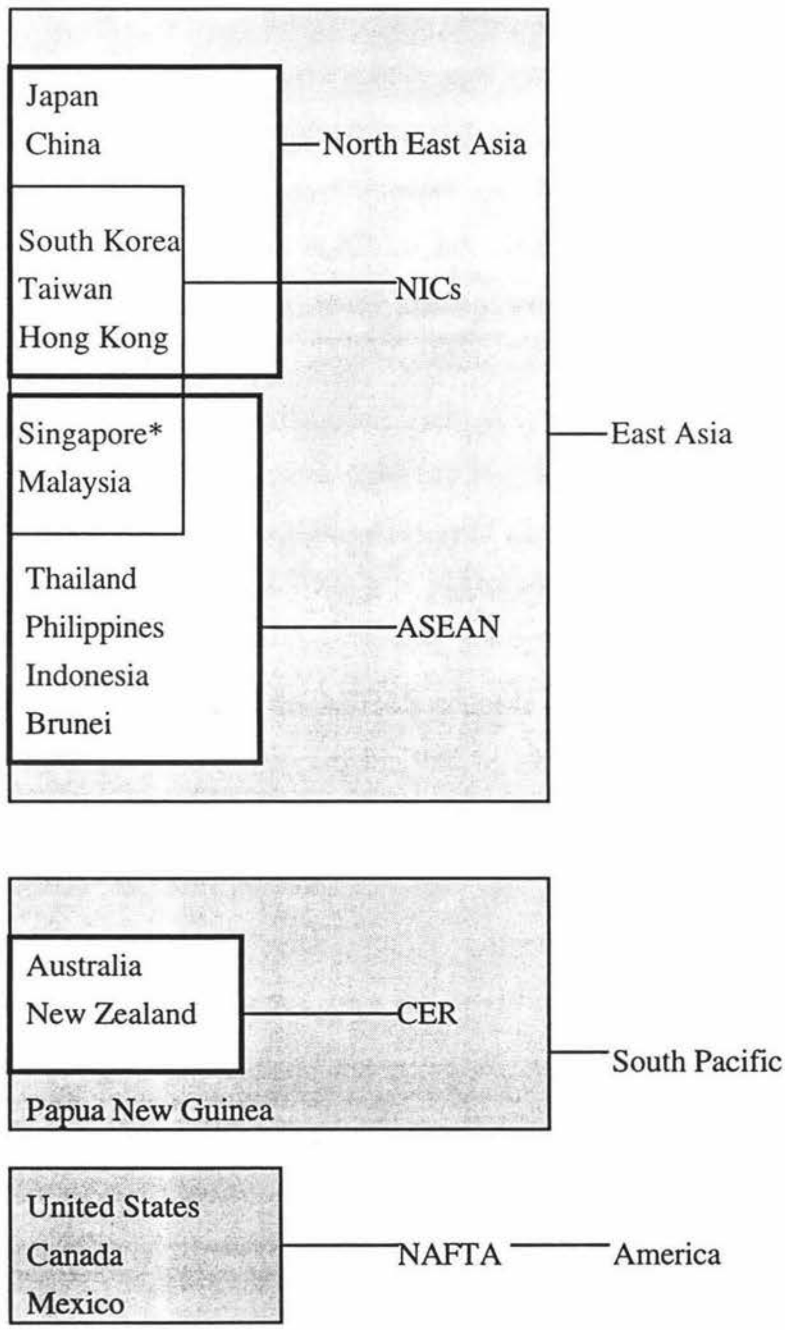
Table 5.1: APEC economies outlook

Country	Population (millions) (1991)	GNP (US$ b) (1991)	GNP/ Capita in US$ 1992	GDP Growth % (1992)	GNP/ Capita increase % 1985-92	Exports (1992) (US$ b)	Imports (1992) (US$ b)	Area in Sq. Kms
Australia	17.380	281	17070	1.8	0.7	42.542	43.734	7682300
Brunei	.276	12	17611	..	-0.2	2.597	1.780	5765
Canada	26.858	567	20320	0.7	0.3	134.056	129.154	9958319
Chile	13.813	37	2730	7.0	6.1			756629
China	1,168.309	371	380	13.0	6.0	80.517	76.354	9571300
Hong Kong	5.840	78	15380	5.0	5.6	119.512	123.430	1078
Indonesia	179.460	111	670	5.8	1.7	29.322	27.311	1904443
South Korea	43.189	274	6790	4.8	8.5	76.632	81.775	99313
Japan	123.960	3,387	2820	1.3	4.0	339.885	233.246	377750
Malaysia	17.365	46	2790	8.0	5.7	40.705	39.959	329758
Mexico	87.840	252	3470	2.6	1.1	27.618	48.160	1958201
New Zealand	3.369	43	12060	2.8	0.4	9.824	9.202	270534
P.N. Guinea	3.770	3	950	9.0	-0.1	1.810	1.485	462840
Philippines	62.870	46	770	0.6	1.9	8.839	12,944	300000
Singapore	3.013	39	15750	5.8	5.9	63.483	72.177	641
Taiwan	20.186	180	10202	6.6	7.7	81.419	72.181	36000
Thailand	58.950	90	1840	7.5	8.3	32.473	40.686	513115
USA	252.590	5,695	23120	2.6	1.1	448.164	553.923	9809155
Total	2,075.978	11,646		5.0		1,539.4	1,567.5	
World	5,351.000	21,464		1.7		3,645.7	3,763.5	
% of world	38.7%	54.3%				42.2%	41.6%	

Source: *The World Economic Fact Book 1993*. *The World Development Report 1993*. *World Table*, 1993 *International Financial Statistics Yearbook* 1993 IMF. *Hoover's Handbook of World Business* 1993. *The Europa World Book*, 1994.

THE ASIA PACIFIC

Figure 5.1: the Asia-Pacific region



* Singapore was declared a developed nation by the World Bank from 1st January 1996.
(Chile was expected to join NAFTA in 1996, but this has been delayed by the US Presidentia elections)

As shown in Table 5.1, APEC economies now account for 38.7 per cent of the world's population, 54.3 per cent of the world GNP, and 41 per cent of global trade. There is now a common observation that the Asia-Pacific region has economically become the most dynamic region in the world, with a concentration on the countries of East Asia. From an historical perspective, the economic success in East Asia lies firstly in Japan, followed by the newly industrialised countries (NICs) and more recently in China and the ASEAN countries. East Asia economies have maintained a steady growth, and in 1992 developing countries in Asia grew 7.8 per cent, with China recording 13 per cent growth, while the world growth rate was only 1.7 percent (see Table 5.2).

The Asia-Pacific region has already emerged as one of the top trading regions in the world and its economic growth is accelerating steadily. East Asia's share of world trade increased from 14.6 per cent in 1980 to 22.3 per cent in 1992, while the Asian NICs, China and the ASEAN countries as a group expanded their share of world trade from 7.5 per cent in 1980 to 14.6 percent in 1992. The share of APEC's economies in the world trade rose from 32.8 percent to 41.9 percent over the same period (see Table 5.3).

Table 5.2: GDP Growth Rate of the World, the US, the EU, and East Asia (Annual per cent change)

Region/ Country	Average 1975-84	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	Average 1989-94	Average 1975-94
World	3.3	3.7	3.6	3.9	4.6	3.4	2.2	0.6	1.7		2.2	2.0	3.1
US	2.5	3.2	2.9	3.1	3.9	2.5	1.2	-0.7	2.6	3.1	4.1	2.1	2.6
EU	2.0	2.5	2.9	2.9	4.2	3.5	3.0	0.8	1.1	-0.4	2.8	1.8	2.3
East Asia	6.3	7.3	7.0	8.1	9.0	5.5	5.7	6.1	7.8	8.7	8.6	7.1	7.4
East Asian Countries													
China	7.2	13.4	9.7	11.0	10.7	4.2	4.3	7.8	13.0	13.4	11.8	9.1	9.9
Japan	4.0	5.0	2.6	4.1	6.2	4.7	4.8	4.0	1.3	5.8	5.7	4.4	4.4
Hong Kong	8.9	0.2	11.1	14.5	8.3	2.8	3.2	4.2	5.0	5.8	5.5	4.4	6.1
Taiwan	8.6	5.0	11.6	12.3	7.3	7.6	4.9	7.2	6.6	6.3	6.5	6.5	7.5
Korea	8.0	6.9	12.4	12.0	11.5	6.2	9.2	8.5	4.8	5.5	8.3	7.1	8.5
Singapore	8.0	-1.6	1.8	9.4	11.1	9.2	8.3	6.7	5.8	10.1	10.1	8.4	7.2
Malaysia	7.0	-1.0	1.2	5.4	8.9	9.2	9.7	8.7	8.0	8.3	8.5	8.7	6.7
Thailand	7.0	3.5	4.9	9.5	13.2	12.0	10.0	8.2	7.5	8.2	8.5	9.1	8.6
Indonesia	5.9	2.5	5.9	4.9	5.8	7.5	7.1	6.6	5.8	6.5	7.4	6.8	6.0
Philippines	3.9	-4.4	3.4	4.8	6.3	6.1	2.4	-1.0	0.6	2.1	4.3	2.4	3.2
Vietnam						7.8	4.9	6.0	8.6	8.1	8.8	7.4	-
Laos						3.5	1.2	7.6	7.0	4.3	4.9	4.8	-
Cambodia						13	6.7	4.0	7.0	5.9	8.0	7.4	-

Source: International Monetary Fund, *World Economic Outlook*, (Washington, D. C., October 1993/94); OECD, *OECD Economic Outlook*, Paris, December, 1993/94.

Table 5.3: Asia-Pacific share of world trade

	Country/Region	1980	1985	1989	1990	1991	1992
Export	United States	11.6	11.8	12.5	11.8	12.3	12.3
	Japan	6.9	9.8	9.4	8.6	9.2	9.3
	Asian NICs	4.0	6.3	8.5	8.0	8.9	9.4
	ASEAN	2.5	2.5	2.6	2.6	2.9	3.1
	China	1.0	1.5	1.8	1.8	2.0	2.2
	North America	16.0	17.8	17.4	16.5	16.8	16.7
	South Pacific	1.5	1.6	1.6	1.5	1.5	1.5
	East Asia	14.4	20.1	22.3	21.3	23.0	24.0
	APEC	31.9	39.5	41.3	39.1	41.3	42.2
Import	United States	13.2	19.1	16.4	15.1	14.3	14.7
	Japan	7.3	6.9	7.0	6.9	6.7	6.2
	Asian NICs	4.5	5.7	7.9	7.8	8.7	9.3
	ASEAN	2.0	2.0	2.5	2.8	3.2	3.3
	China	1.0	2.2	1.9	1.6	1.8	2.0
	North America	17.3	24.0	21.2	19.5	18.9	19.4
	South Pacific	1.5	1.7	1.8	1.5	1.5	1.4
	East Asia	14.8	16.8	19.3	19.1	20.3	20.8
	APEC	33.6	42.5	42.3	40.1	40.7	41.6
Total Trade	United States	12.4	15.5	14.5	13.5	13.3	13.5
	Japan	7.1	8.3	8.2	7.7	7.9	7.7
	Asian NICs	4.3	6.0	8.2	7.9	8.8	9.3
	ASEAN	2.2	2.2	2.5	2.7	3.1	3.2
	China	1.0	1.9	1.9	1.7	1.9	2.1
	North America	16.7	20.9	19.3	18.0	17.9	18.1
	South Pacific	1.5	1.7	1.7	1.5	1.5	1.5
	East Asia	14.6	18.4	20.8	20.1	21.7	22.3
	APEC	32.8	41.0	41.8	39.6	41.1	41.9

Source: *The World Economic Outlook October* 1993, IMF

Most APEC economies have expanded their trade with member nations in recent years. Intra-East Asian trade showed an increase from around 30 per cent of the East Asian total in 1970 to around 40 per cent in 1990. Intra-APEC trade expanded from around 56 per cent of the Asia-Pacific total in 1970 to around 65 per cent in 1990 (see Table 5.4). The intra-regional share of Asia-Pacific trade was almost as large as the share of Western European trade, by 1990 (see Table 5.2).

Rising intra-regional trade and investment has resulted in economic interdependence among Asia Pacific countries. With the growth of economic interdependence, the regional economic cooperation will be more and more important than ever before. Obviously this is one of the important factors in the formation of APEC.

The question in the mind of 'East Asia watchers' is whether there will be a trade bloc in East Asia. AFTA is restricted to South East Asia and at present is not a real threat to global trade. In the following pages we will discuss the current economic position, the economic development of the East Asian region, and the status of the region in the present trend towards regionalism.

EAST ASIA POSITION IN WORLD TRADE

The economies of North East Asia and South East Asia are fast becoming integrated into a broad East Asian region. As we discussed above, this region has emerged as the most dynamic component of the global economy. The region is becoming increasingly dominated by Japan and it has over the last two decades also contained most of the world's fastest growing economies such as the East Asian NIEs, and more recently, Malaysia, Thailand, Indonesia and Vietnam from the ASEAN group of countries (Leger, 1994). East Asia also includes China, the most populated country in the world, which has discarded the ideals of pure communism and opened its economy to international competition. This country is now predicted to become the largest economy in the world in the 21st century (Caplen, 1994a).

Table 5.4: Asia-Pacific and world bilateral trade flows, 1970 and 1990 (%)

	East Asia	North America	South Pacific	APEC	EU	Western Europe	Rest of World
1970							
East Asia							
Exports	31.02	30.04	3.19	64.26	10.27	16.41	19.33
Imports	29.47	26.44	6.63	62.54	11.13	14.58	22.88
North America							
Exports	13.92	32.50	2.25	48.67	27.42	28.61	22.72
Imports	17.65	38.31	1.88	57.84	19.42	24.02	18.14
South Pacific							
Exports	33.13	16.33	5.93	55.39	26.38	27.54	17.07
Imports	17.08	26.98	5.84	49.91	29.35	39.61	10.48
APEC							
Exports	20.73	30.69	2.79	54.21	22.04	24.53	21.26
Imports	21.77	33.42	3.80	58.99	17.13	21.68	19.33
EU							
Exports	3.41	9.63	1.57	14.61	53.10	66.24	19.15
Imports	3.46	13.19	1.54	18.19	50.24	59.62	22.19
Western Europe							
Exports	3.35	9.31	1.47	14.13	53.85	66.75	19.12
Imports	3.45	12.3	1.34	17.09	50.97	61.90	21.01
Rest of world							
Exports	20.67	17.64	1.16	39.47	38.64	40.41	20.12
Imports	8.10	31.19	0.79	40.08	32.96	37.93	21.99
1990							
East Asia							
Exports	39.37	28.65	2.30	70.32	16.24	18.67	11.02
Imports	43.62	21.00	4.14	68.76	14.12	15.64	15.60
North America							
Exports	22.48	33.98	2.02	58.48	20.55	23.34	18.18
Imports	33.78	27.49	1.03	62.30	17.18	20.93	16.77
South Pacific							
Exports	49.87	12.44	7.25	69.56	15.11	15.83	14.61
Imports	35.25	23.15	7.29	65.68	21.53	27.61	6.70
APEC							
Exports	32.85	30.19	2.38	65.43	17.97	20.47	14.10
Imports	38.27	24.39	2.67	65.34	15.97	18.80	15.85
EU							
Exports	5.29	7.29	0.69	13.27	55.77	66.19	20.54
Imports	7.69	7.27	0.52	15.47	51.18	59.96	24.57
Western Europe							
Exports	5.29	7.29	0.69	13.27	55.77	66.19	20.54
Imports	7.69	7.27	0.52	15.47	51.18	59.96	24.57
Rest of world							
Exports	17.71	17.89	1.35	36.95	37.71	46.79	16.25
Imports	20.95	15.39	1.55	37.89	42.84	43.78	18.33

Source: *The Australian National University Economic Databank*, compiled from United Nations, International Monetary Fund, and national statistics. (adapted from Bergsten and Noland, 1993, 184-185)

Table 5.5 summarises the key economic indicators of the East Asian countries. While Japan reached the pinnacle of its economic growth during the 1960s, Hong Kong, Taiwan, Singapore and Korea, had their ascendancy from the 1960s with average annual growth rate over 8 per cent; they achieved NIE status in the 1980s. Recently Malaysia, joined their ranks (Selvarajah, 1994a). Thailand and Indonesia, with strong economic growth rates in recent years, are predicted to have NIE status before the end of this decade (Selvarajah, 1991). Economic growth in China has accelerated since the late 1970s when the government shifted to an open-door policy promoting foreign investment and export. The map of Asia illustrates the movement of growth from Japan to other Asian nations. Economist believe that the impetus of growth is just beginning and what has been seen so far is only a small part (Chowdhury and Islam, 1993). As was international trade in 1830 (see Figure 1.1), 60 per cent of world trade will eventually rest in the Asian region.

Table 5.5: Economic Key Indicators of the East Asian Countries, 1991

	Population (millions)	GNP (US $bil)	Exports (US$ bil)	Real GDP growth (%)			Export growth (% p.a.)	
				1961-70	1971-80	1981-90	1965-80	1980-90
Japan	124	3,387	314,892	10.9	5.0	4.0	11.4	4.6
China	1,150	371	71,986	5.2	5.8	9.7	5.5	11.5
Hong Kong	5.9	78	98,579	10.0	9.3	7.1	9.5	6.2
Taiwan	20.4	180	76,200	9.2	9.7	10.2	28.5	16.3
Korea	43.2	274	69,489	8.6	9.5	9.7	27.2	13.8
Singapore	3.0	39	59,188	8.8	8.5	6.1	4.7	8.1
Indonesia	181	111	29,142	3.9	7.6	5.3	9.6	2.4
Malaysia	18.3	46	36,749	6.5	7.8	4.9	4.4	9.8
Thailand	56.7	90	27,562	8.4	7.2	7.0	8.5	12.5
Philippines	62.7	46	8,840	5.1	6.3	0.7	4.7	1.3
Total	1,665	4,622	792,627	5.1	7.7	6.5	11.4	8.7

Sources: The Reference Press, *Hoover's Handbook of World Business 1993*. (Austin, 1993); World Bank, *World Development Report*, (Washington, D. C., 1992); UNCTAD, *Handbook of International Trade and Development Statistics*, (Geneva, 1992).

In the last thirty years, real GNP has multiplied 12 times in the Asian NIEs, 11 times in Japan and 6 times in ASEAN and China. This compares with 2.5 times for the United States and 3 times for the world economy (Kwan, 1994). In 1991, East Asia contained a population of 1.7 billion, about one fourth of the world population, and had US$ 4,622 billion total GNP outputs. This compares with US$ 6,213 billion for the EU and US$ 6,514 billion for NAFTA (Chai, 1993). If present growth rates continue, by the year 2010 East Asia will have a GNP larger than that of the EU and NAFTA combined and will then be the engine for world economic growth.

The integration of East Asia into the world economy has just begun (Caplen, 1994a). Before the 1970s most South East Asian countries were sole producers of primary material resources, varying from pepper and palm oil to rubber and rice. Although at present the region still produces and exports a wide range of primary resource commodities and dominates world production of several, such as tin, rubber and palm oil, manufacturing is becoming more and more important in the region's development. Several countries in the region have gone a step further and are developing their finance and producer services (Dobbs-Higginson, 1993). For the most part, as in the case of Hong Kong and Singapore, these are regionally oriented services.

The springboard for East Asian economic growth has been macro-economic reform and the implementation of outward-looking, export-orientated strategies (Selvarajah, 1994). This has brought large foreign investment into the region. The investment attraction in the region was not only cheap labour, but also other criteria, such as an educated workforce, good infrastructure and communication, government and the like. Furthermore, the East Asia region has emerged as one of the world's top markets and this is another good reason for investment flow into the region.

East Asia's importance in the world economy is due to the increased financial flows into the region and its overall increases in the volume of trade, particularly exports of manufactured goods. Table 5.5 shows that in the last thirty years the export growths of East Asian countries were higher than their GDP growths. In the case of South Korea and Taiwan, export growth was significantly high, an average annual growth rate of over 20 per cent. The exports of the region have progressed far beyond the toys and textiles stage and now encompass sophisticated products: for instance, the growing automobile exports from South Korea and more recently Malaysia.

The rapid development of finance and producer services in the East Asia region has also accompanied economic development. Nations such as Hong Kong and Singapore have sought to develop their financial and producer services purely to service the growing markets of East Asia. Japan has also had an impact in this area. The strength of the Yen has made Japanese banks by far the most dominant global group in terms of assets; this has induced a massive investment surge in land, property and production throughout the world (Koseki, 1993b; Rhee, 1993). However, Japan is by no means alone in such activity and several of the Asian NIEs, such as Singapore, Taiwan and South Korea, have built up impressive global investment portfolios.

Regional trade has also increased significantly and the nature and direction of trade has changed over the last few decades. The old colonial ties with Europe were rapidly replaced by the post-war pre-eminence of the United States as the principle trading partner in the region, a trend which was accelerated by the decolonisation process which the United States so warmly supported (Borthwick, 1992). More recently, although considerable variations in export markets exist for individual countries and the US remains an important export market, the US has been replaced by Japan as the trading giant of the region (Adler et al, 1986). The relative decline in the US economic power, and rising trade friction between nations on either side of the Pacific has made Asian countries diversify their export markets and trade more among themself. At the same time, Japan has also replaced the US as Asia's most important source of foreign direct investment and the Asian NIEs have emerged as major investors in the region (Rhee, 1993). The increase in foreign direct investment among the Asian countries has boosted intra-regional trade.

This trend supports the strong economic interdependence of the East Asian economies; with or without a formal trade bloc the region is showing strong signs of close cooperation and mutual development.

JAPAN AND CHINA

Japanese economic development since World War II has been characterised as 'the miracle of East Asia'. It started by copying US based manufactured products forty years ago. Since then, Japan has become a major high-technology product manufacturer. Some manufacturing products, such as electronics and automobiles, have even replaced the US dominant position of US products. In 1991, Japan, with a population of 124 million, had a GNP of US$ 3,287 billion. This accounted for 73 per cent of East Asia GNP (see Table 5.5). This makes Japan the dominant economy in East Asia. In recent years the ill effects of rapid economic expansion in the form of rising living standards and the high value of the Yen have made Japan modify its development strategy. To remain competitive, Japan has invested internationally, especially in the developing nations of Asia (Rhee, 1993). The dominant Japanese economic position in East Asia is being challenged by the fast developing Asian NIEs, and will increasingly face an even larger challenge from China in ten to twenty years time.

China, with a of GNP US$ 371 billion and 1.15 billion population (see Table 5.5), has seen accelerated economic growth since the late 1970s. Unlike most capitalist countries, socialist China's economic development largely depends on its political initiatives. Premier Deng's reforms in 1979 have accelerated Chinese economic growth which averaged 9.7 per cent between 1981 and 1990. However, China has several problems, such as a weak infrastructure and increasing urbanisation of the population. The need to change to a market economic system from an authoritarian command system is also causing some friction. In the summer of 1989, the conflict reached its peak with pro-democracy protests in Beijing, and the subsequent massacre in Tianamen Square on June 4th (*The Economist*, 4 June, 1994:17). The massacre led most countries to re-think their relationship with China resulting in a slowdown in direct foreign investments. The Chinese economy was notably damage after the 1989 incident but it recovered from 1991 onwards as the Chinese government relaxed its hard-line stand. With these changes, and with huge business potential despite the political instability, the country has attracted huge investments (Ibid).

THE ASIAN NIEs

The NIEs of Hong Kong, Taiwan, Singapore and South Korea (the 'four little dragons'), started their economic assent in the 1960s. Their development followed a path similar to that of Japan. The four countries reached NIE status in the early 1980s. Malaysia, reputed to be the 'tiger with a vision' (Selvarajah, 1993, 1994b) joined East Asian NIE rank in 1992. The average GDP of the East Asian NIEs has grown at an average annual rate of around 7 per cent since the mid-1960s. During the same period, the world GDP grew on average only 3 per cent, and the EU and the US managed only around 2.3 and 2.6 per cent respectively (See Table 5.2).

The East Asian NIEs carried out macro-economic reforms and implemented of outward-looking, export-orientated growth strategies as part of their economic development. These reforms drove the NIEs forward rapidly and also brought foreign investments into the region. Again, like Japan, the robust economic growth of the NIEs has been accompanied by extensive structural changes in manufacturing production; for example the contribution of manufacturing to the GDP of these nations has increased significantly (with the exception of Hong Kong). Taiwan, Singapore, South Korea and Malaysia have a high percentage of manufacturing in the GDP measure and accounted for 34 per cent, 29 per cent, 31 per cent and 28 per cent respectively in 1991 (See Table 5.6), This was greater than the average for the mature industrial market economies. Hong Kong, on the other hand, has developed as a finance, trade and service oriented nation due to its strategic location in the East Asia region. Singapore in recent years has followed Hong Kong's example and is concentrating on the finance service industry.

In 1991, the combined East Asian NIEs accounted for 13.3 per cent of the total GNP for the East Asian region (See Tables 5.1 and 5.6). The NIEs have now emerged as major investors in the East Asian region, particularly, China, Thailand, Vietnam and the Philippines. These countries are now moving steadily toward developed economy status. Since January 1996, the World Bank has recognised Singapore as a developed economy and classified Hong Kong as a 'high income' economy.

Table 5.6 Key Economic Indicators of East Asian NIEs, 1991

	Population (million)	**GNP (US$ bil.)**	**GNP % (US$)**	**Exports (US$ mil.)**	**Imports (US$ mil.)**	**Manufacture (% of GDP)**
Hong Kong	5.9	78	13,200	98,579	100,274	18
Taiwan	20.4	180	8,833	76,200	62,900	34
Singapore	3.0	39	12,890	59,188	66,257	29
S. Korea	43.2	274	6,340	69,489	81,114	31
Total	72.5	571	7,876	303456	310545	Average % 28

Sources: The Reference Press, *Hoover's Handbook of World Business* 1993. (Austin, 1993).

ASEAN COUNTRIES

The Association of South East Asian nations (ASEAN) brings seven countries together in a co-operative framework. ASEAN has promoted stability, security and development in the South East Asian region. It has been very successful in building regional confidence at the political level, and is now taking on a greater economic role.

The ASEAN (the Association of South East Asian Nations) comprises Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam. The ASEAN countries have a combined population of 386 million, have achieved remarkable economic gains (doubling their economies in a decade), GNP had totalling US$ 332 billion in 1991 (See Table 5.7), and rapid economic growth rates (See Table 5.1).

Table 5.7 Key Economic Indicators of ASEAN Countries*, 1991

	Population (million)	GNP (US$ bil.)	GNP p.c. (US$)	Exports (US$ mil.)	Imports (US$ mil.)	Manufacture (% of GDP)
Brunei	0.3	---	---	2,597	1,780	---
Indonesia	181	111	610	29,142	25,869	18
Malaysia	18.3	46	2,490	34,405	36,749	27
Philippines	62.7	46	740	8,840	12,945	25
Singapore	3.0	39	12,890	59,188	66,257	29
Thailand	56.7	90	1,580	27,562	37,518	25
Total	322.0	332	18,310	161734	181118	

Sources: The Reference Press, *Hoover's Handbook of World Business 1993*. (Austin, 1993); World Bank, *The World Economic Flatbook 1993*, (Washington, D. C., 1993).
*Vietnam was admitted in 1995, the country's data is not included

FORMATION OF ASEAN

ASEAN was established on 8 August 1967 with five members (Indonesia, Malaysia, Philippines, Singapore, Thailand); Brunei, joined in 1984 and Vietnam in 1995. The ASEAN Declaration (also known as the Bangkok Declaration), has seven aims and purposes. Clause 1 and 2, the most important, are as follows (Sandhu, 1992):

1) to accelerate economic growth, social progress and cultural development in the region through joint endeavours in the spirit of equality and partnership in order to strengthen the foundation for a prosperous and peaceful community of South East Asian Nations;

2) to promote regional peace and stability through abiding respect for justice and the rule of law in relationships among countries of the region and adherence to the principles of the United Nations Charter.

Generally, there have been three major phases of ASEAN economic co-operation (Church, 1995).

1) The first stage spanned the fifteen years from 1967 to the first Summit in 1976, during which time the countries basically tried to get to know each other and lay the foundations for co-operation.

2) The second stage spanned the subsequent fifteen years, from 1976 to the Fourth Summit of January 1992 there was active co-operation and formal though somewhat superficial agreements for economic co-operation among the member states, focusing mostly on building institutions for co-operation.

3) The third stage, from 1992 to 2007, will be one of consolidation in building AFTA and other forms of regional co-operation, characterised by much more active and productive economic co-operation in the region.

Much of its early activity focused on issues of regional security, particularly on the question of Indo-China and on internal communist rebellion. As the political stability of the region improved, it began to focus on the question of economic co-operation and the development of intra-regional trade.

ASEAN's achievements with regard to regional economic co-operation were relatively small during its early years. However, as the concept of 'ASEAN unity' took shape in the early to mid-1970s, the member countries of ASEAN became increasingly aware of the effect of joint action when pursuing both economic and political goals. This was reflected in the strengthening of ASEAN's internal political co-operation via the Kuala Lumpur Declaration or 'Zone of Peace, Freedom and Neutrality' signed in 1971 (Mak, 1993).

This unified approach was strengthened by several significant international developments in the 1970s: the 1973 oil shock; the Communist victories in Indo-China in 1975; the final Withdrawal of United States military power from the mainland of Southeast Asia in 1976; and the internal changes in China during its economic modernisation path. Such factors served to highlight the need for ASEAN to develop into a more closed entity.

ASEAN started regular discussions with seven dialogue partners who are ASEAN's major trading partners since the 1970s; (Naisbitt, 1995). They are: the European Community, since 1972; Australia since 1974; New Zealand since 1975; Canada, Japan and the US since 1977; and South Korea since 1986.

ECONOMICS OF ASEAN

Traditionally, all ASEAN countries have looked outside their region for their exports. Consequently, they have developed stronger economic ties with third countries than among themselves. The similarity of resource and factor endowments among ASEAN countries has rendered their economies competitive rather than complementary. Not surprisingly, therefore, internal trade within the ASEAN members is much smaller than external trade., Historically, the ASEAN economies have had close trade and investment ties with Western Europe, but during the last two decades ASEAN economies have been moving away from the Atlantic towards the Pacific. The Pacific now accounts for a large and growing proportion of ASEAN's exports and imports. In addition, the Pacific has also become an increasingly dominant source of foreign direct investment. It is only natural that ASEAN countries, located in the Pacific Rim, develop strong economic link with their dynamic Pacific neighbours.

Economic development in South East Asia has been heavily dependent on strategies of export-oriented industrialisation, and such strategies are highly sensitive to changes in the global trading environment. When the global trade environment faced increasing competition from the trade blocs like EU and NAFTA, the AFTA (ASEAN Free Trade Area) proposal received strong support in the ASEAN Foreign Ministers meeting in Kuala Lumpur in July 1991. Accordingly, the 1992 Singapore Summit adopted concrete measures for the establishment of an AFTA which came into force in 1994.

The motives of AFTA were both defensive and forward-looking, perhaps sending a signal to Europe and the US that the region was concerned about a perceived rise of protectionism at a time when GATT lay stalled at the negotiating table (Cleary and Bedford, 1993).

ASEAN countries were also seeking to develop intra-trade co-operation. Compared with other trading blocs, the percentage of intra-regional trade is relatively small for ASEAN. The basic problem is that ASEAN member countries are at markedly different stages of economic development, though they have been making efforts to change this situation. The potential for expanding trade between ASEAN members is thus considerable and the agreement of tariff reductions to 5% over a 15-year period in the Singapore Declaration 1992 is designed in part to stimulate this trade.

AFTA is likely to become an important market place for the following reasons:

1) a growing population, at present about 386 million, and particularly an expanding middle class;

2) the rapid industrialisation of ASEAN countries and the changing trade pattern and structure requires more natural resource-based imports;

3) the likelihood of an expanded ASEAN which may have a population of about 0.5 billion.

Economies of ASEAN are dynamic. ASEAN's political stability and macro-economic policies have been preconditions for growth, and the capacity and willingness to undergo rapid structural changes have been essential for sustaining high rates of growth (Stone, 1992). The rapidly growing economies have also benefited from close economic link with Japan and the NIEs.

The Philippines grew rapidly at an average annual growth rate of 5.7 per cent during the 1960s and 1970s but has since slowed down to an average annual growth 0.7 per cent in 1980s (See Table 5.1). The forecast for the country is unclear and is the last of the ASEAN economies yet to experience the dynamism that has become the positive economic feature of ASEAN. Despite its variety, the ASEAN regional economy has grown remarkably quickly since the 1970s and has become a notable economic entity in the East Asia region and the world in recent years. As a recognition of its growing economic importance, the EU had its first summit meeting with ASEAN in January 1996 (CNN Live, January 18, 1996).

ASEAN has become a successful political association of seven nations (future members will include, Laos Cambodia and Myanmer) in one of the most dynamic area in the world. The formation has significantly contributed to the security of the region. In July 1994 the ASEAN Regional Forum (ARF) was launched (ASEAN, 1996). The Forum includes the ASEAN countries, the seven dialogue partners (Australia, the European Union, Canada, Japan, South Korea, New Zealand and the US) and its observers (Laos and Papua New Guinea). Its purpose is to initiate a series of forums that will facilitate discussions on regional security issues such as territorial claims or disputes over resources such as fishing; dealing with more contentious issues involving major world players is also a strong possibility. This initiative is seen as the beginning of a multilateral regional forum for South East Asian security.

AFTA, signed at a summit meeting of the ASEAN Heads of Government in Singapore in January 1992 will move ASEAN countries to a free trade area over the next 15 years (Vatikiotis, 1993e). According to the agreement, from 1 January 1993, all product tariffs above 20 per cent will be brought down to a maximum of 20 per cent in five to eight years, and to a maximum of 5 per cent within 15 years. Tariffs at 20 per cent or below as at 1 January 1993 will be reduced to a maximum of 5 per cent within a time frame which two or more member states may arrange. Quotas and other non-tariff barriers are to be phased out within five years. Due to differences between the ASEAN members the AFTA was delayed a year and came into effect on 1 January 1994 (ibid). Nevertheless, the formation of AFTA marked a significant step forward in enhancing the economic role of ASEAN in East Asia.

AUSTRALIA AND NEW ZEALAND

Both Australia and New Zealand are isolated from the world. They, particularly New Zealand, have experienced long recessions since the 1970s (See Table 5.8), while the economies of their East Asian neighbours boomed during the same period. The two countries are trying to reboot their fledging economies by realigning with countries in the East Asia region (Wells, 1995). Both countries are initiating economic links with the East Asian economies and have shown interest in becoming members of AFTA (Ansley, 1994a).

Table 5.8 GDP Growth of Australia and New Zealand (Per cent Change)

	Average 1967-76	Average 1977-86	1987	1988	1989	1990	1991	1992	1993	1994	Average 1987-94
Australia	4.6	2.9	4.4	4.4	4.6	1.4	-0.8	2.0	2.5	3.1	2.7
N. Z.	3.4	1.4	-2.2	3.0	-0.7	0.5	-1.8	0.5	3.0	6.1	1.1

Sources: OECD, *OECD Economic Outlook*. Paris, December 1994.

Table 5.8 shows the GDP growth of Australia and New Zealand since 1967. After experiencing economic recession during the period between 1989 and 1992, the two economies are showing positive economic growth. In the case of New Zealand, the recession was even deeper and longer, but since 1992 it seems to have recovered and is showing strong economic growth.

New Zealand has almost completed an historic shift from a nation whose trading was largely directed toward the UK, to a diversified global market. In the year ended February 1994, more than 34 per cent of the New Zealand's exports were to East Asia, and that's increasing at a steady rate. Six of the ten largest New Zealand export markets are in Asia. South Korea, which took NZ$ 929 million or 4.9 per cent of the New Zealand's total exports, had an annual growth of 23.73 per cent. South Korea now looks set to displace the United Kingdom, which took NZ$ 1,187.6 million of New Zealand exports, which has an annual growth of 3.43 per cent, as New Zealand's fourth largest market (*Export News*, 18 April 1994:11).

A GLOBAL EAST ASIAN PROSPECTIVE

The discussion above indicates the emergence of the East Asian region into a more economically integrated regional economy than ever before. However, the general perception from outside the region is that it is not homogeneous and ready for a single united East Asia (Cragg, 1995; Drakakis-Smith, 1992; Mackerras, 1992; Martin, 1986). Indeed, the social, cultural, political and economic contrasts and conflicts that exist within the region make it one of the most potentially volatile area in the world (O'Neil, 1984). Though this may be the case, recent trends in East Asia seem to go against this perception.

The region is drawing synergy as never before and is forging a new cooperative dynamism.

Japan is one of the most wealthy nations in the world and has undoubtedly provided a role model for other Asian nations to follow. With its investment policy Japan has challenged other East Asian countries to follow its example (Leger, 1994).

The East Asian region has had and continues to have political, economic and social problems. It is clear that the division between socialism and capitalism remains one important dimension of regional fragmentation. The capitalist nations have probably experienced the worst of the communist insurgencies, but pockets of real and potential trouble still exist. Many political hot-spots exist in the region, such as the unresolved stalemate between the two Koreas, the transfer of power from the UK to socialist China of Hong Kong in 1997, and the separatist movements in East Timor. These situations can erupt quickly into violent expressions of dissatisfaction and repression.

A global Asian identity, however, seems to be emerging as a result of immigration, global commuting, improved communication and the accelerated mobility of capital. The overseas Chinese who have historically settled throughout South East Asia are the best illustration of a trans-national East Asian community and are helping to forge links between South East Asia and North East Asia, especially China, Taiwan and Hong Kong (Ch'ng, 1993; Kao, 1993; Simoniya, 1961). A similar trend is recognised where overseas Indians are forging links between South East Asian economies such as Singapore and Malaysia and the Indian subcontinent.

Increased protection of the American market and the formation of NAFTA is likely to be accompanied by a general reduction of the American presence in East Asia. The easing of global tension has particularly reduced the significance of the American military presence and there are clear signs that Japan is ready to replace the US in East Asian economic activity (Cragg, 1995). On the other hand, as discussed earlier, although Japan and the Asian NIEs are becoming main players in the global economy, East Asian integration cannot emerge as long as nations in Asia are dependent on the US markets for their exports (and so will not jeopardise their relationship with the US) and the US remains opposed to trade blocs in Asia.

REGIONAL COOPERATION - BACKGROUND TO APEC FORMATION

Whilst the world is ever-changing, a number of significant political events in the past seven years have caused nations to rethink their social and economic positioning, especially in terms of how they trade with each other. The creation of APEC is one such example. The significance of APEC, in terms of world economic affairs, has been reinforced by the importance placed upon it by the US. In the following section, the concepts, involvement and growth of regional cooperations in the region will be discussed.

OPEN REGIONALISM - THE PREMISE OF APEC

In a utopian world, open regionalism would mean free trade. The Eminent Persons Group (EPG) have defined the principle of open regionalism as 'a process of regional cooperation whose outcome is not only the actual reduction of internal intra-regional barriers to economic interaction, but also the actual reduction of external barriers to economics not part of regional enterprise' (*Report of the EPG*, 1994:2). It follows that free trade is the premise of APEC, and it encourages trade between every party within and outside the geographic region without restriction. Membership, based on geographical positioning within the Asia Pacific region, is free, and the only condition is that goods and services must be marketed without barriers or restriction between all participating countries.

Nevertheless, the road to free trade is likely to be long and difficult. Open regionalism, within the context of the EPG definition, suggests that through conciliation and the granting of trade concessions to each other trade could be extended unconditionally or on a reciprocal basis to non-members. Ultimately, such trade agreements would then create a region that allows its members to trade between themselves and with non-members free of tariffs or other trade barriers. This very liberal approach to trade relations may not occur easily.

REGIONAL COOPERATION IN THE ASIA PACIFIC

Throughout history, in between political upheavals, there has always been reconciliation and progress in the building of bilateral and later, multilateral relationships such as the EU. Nations that have chosen not to build friendly relationships or to trade freely, have been left behind in terms of growth, wealth and personal freedom. North Korea is a good example.

The following are the major regional cooperations in the Asia Pacific region:

Pacific Free Trade Area (PAFTA)

In the mid-1960s, Japan floated the idea of a PAFTA to incorporate the five developed countries of the area: Australia, Canada, Japan, New Zealand and the USA. However, a free trade area did not emerge*, but from the meetings came the Organisation for Pacific Trade and Development (OPTAD). OPTAD's focus was on increasing the region's voice in global affairs through discussing, planning, resolving problems and allying economically.

Pacific Basin Economic Council (PBEC).

Following Australia's loss of British markets, when that country joined the European Economic Community (EEC), Australia joined Japan and fostered the Pacific Basin Economic Council. PBEC was formed in 1967. It operates from a secretariat in Hawaii and focuses on private sector cooperation.

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* Basically the US was not at that time in favour of regional trade arrangements. Rather it favoured multilateral trade agreements such as GATT, as was seen in the case of the 1960s UK proposal for a North Atlantic Free Trade Area. This was rejected by the US.

Association of South East Asian Nations, (ASEAN)

The ASEAN was formed in 1967. Its five founder nations, Indonesia, Malaysia, the Philippines, Singapore and Thailand, were joined in 1984 by the Sultanate of Brunei when it gained its independence from Great Britain. ASEAN's objectives were to promote peace and security in the region and to enhance collective regional economic growth.

Pacific Economic Cooperation Conference (PECC)

PECC was formed in 1980 and it is an informal tribunal consisting of government, academic and commercial personnel. It has been significant in developing a broader perspective on trade and in facilitating communication and economic issues in the Pacific region.

Australia and New Zealand Closer Economic Relations (CER)

CER, a bilateral preferential trading treaty involving Australia and New Zealand, was instituted in 1983 to accommodate trade between the two nations. This replaced the New Zealand Australia Free Trade Agreement, which was considered ineffective and did not have a proper time-frame for instituting trade changes.

Canada-US Free Trade Agreement (Canada-US FTA)

In 1989, the Canada-US FTA came into being. It was a bilateral agreement instituted to augment trade by lessening tariffs and promoting uniform standards between Canada and the US. In 1992 the concept was expanded into the North American Free Trade Agreement (NAFTA) with the inclusion of Mexico.

East Asia Economic Caucus (EAEC)

After APEC was founded in 1990, the Malaysian Prime Minister Datuk Seri Dr Mahathir Mohamad, expressed fears that APEC would benefit the US to the detriment of the Asian economies. He sought to establish an all Asian group called the East Asia Economic Group (EAEG) as an alternative to APEC. After pressure from the US and guarded resistance from Japan and China, EAEG was reformed into East Asia Economic Caucus (EAEC), which now operates as a forum within APEC.

Overall, the emphasis has clearly moved away from the abject nationalism that was evident in earlier years, and the protectionism that it invariably brings. The trend is now clearly towards regional assistance and partnership.

ASIA PACIFIC ECONOMIC COOPERATION

APEC was formed in 1989 at the initiative of Australia and South Korea. Australia's then Prime Minister, Mr Bob Hawke, is generally credited with its founding. It was not set up as a trade bloc, nor is it a bureaucracy. Only in January 1993 was a small secretariat established in Singapore. APEC was set up as a consultative forum for government ministers and officials to work towards inter-governmental economic cooperation in the region. Its anticipated focus is multilateral and policy oriented.

The APEC geographical coverage extends from North East Asia to Australasia and across the Pacific Ocean to include nations of North and South America. APEC currently has 18 nations as follows:

Australia	Brunei Darussalam	Canada
China	Chile	Hong Kong
Indonesia	South Korea	Japan
Malaysia	Mexico	New Zealand
Papua New Guinea	Philippines	Singapore
Chinese Taipei (Taiwan)	Thailand	USA

Table 5. 9: APEC Timeline

Year	Event
1960-1967	**Phase 1.** *Proposal Phase* Proposal for a Pacific Free Trade Area (PAFTA). OPTAD - The Organisations for Pacific Trade and Development emerged.
1967-1989	**Phase 2.** *Active Movements* PAFTAD - The Pacific Trade and Development Conference. ASEAN formed in 1967. PBEC - The Pacific Basin Economic Council formed in 1967 - Australian/Japanese cooperation. PECC - the Pacific Economic Cooperation Conference formed in 1980. CER - Australia/New Zealand Closer Economic Relations Trade Agreement in 1983. SPARTECA - The South Pacific Trade and Economic Cooperation Agreement formed. The Canada/US Free Trade Agreement signed.
1989-1994	**Phase 3.** *APEC Formation* APEC formed in 1989 by 12 countries; Australia, Brunei, Canada, Indonesia, South Korea, Japan, Malaysia, New Zealand, Philippines, Singapore, Thailand and US. EAEC - The East Asia Economic Caucus was formed. China, Hong Kong and Taiwan joined APEC in 1991. NAFTA - the North American Free Trade Agreement was signed in 1992. Mexico and Papua New Guinea joined APEC in 1993. Chile joined APEC in 1993 bringing the total member countries to 18.
1995-2010	**Phase 4.** *Free Trade* 1995-2010 - Developed economies of APEC (Australia, Canada, Japan, New Zealand and the US) to remove all barriers to trade. 1995-2020 - Developing economies of APEC to remove all barriers to trade.

The original APEC idea did not include any North American nations. However, the US refused to endorse or in any way support any initiative of this nature if they did not take part. Consequently, the North American nations that bordered the Pacific Ocean were invited to join the forum, and Chile formally joined the APEC fold in November 1994. For details of APEC formation and development see APEC timeline in Table 5.9.

THE REGIONAL EXPERIMENT

In some ways, APEC was formed for similar reasons as the European Union: to allow nations to develop economies of scale without the hindrance of tariff duties and quotas. The economic principle of free trade is embraced world-wide as the most effective policy to encourage growth and create wealth. In the case of the EU, this movement towards free trade is the first between a group of countries.

At an early stage however, the EU nations developed a protectionist and isolationist stance. Huge subsidies have kept inefficient sheep and beef farmers employed, while at the same time tariffs and quotas keep cheaper goods, often of better quality, out of Europe. In reflection of this inward trade focus, as we have seen in chapter 3, the mass media aptly has termed Europe as 'Fortress Europe'.

When a nation follows free market policies, politicians have to give up a little control as financial markets will invariably influence government policies. This loss of control is further exacerbated when nations join together to increase market size and efficiencies. Governments may face a transition period between losing control of policy creation and the actual creation of wealth that such an alliance brings.

For this reason, nations normally promote small trade associations with only their close neighbours, as a way of minimising the apprehension of their people.

APEC governments, however, have shown more than a little bravery in attempting such a large grouping of nations. The innate anxiety they have overcome is indeed a sign that a global realignment is taking place, this time with the inclusion of Asia. Nevertheless, the crux of APEC's policy does not start until 2020 when the region becomes totally a free trade area, with an interim step in 2010 when the developed countries of APEC remove all barriers to trade, giving nations a long lead time to prepare for the pact. The Pacific Business Forum (PBF), a private sector group, has already called on APEC to bring the trade liberalisation date forward to 2010 (Bergsten, 1994). There will undoubtedly be continuing pressure applied for fast changes, especially by the western nations of APEC.

There is growing pressure within APEC to make it a Free Trade bloc. However, for the present free trade is based on the concept of open regionalism and is promoted as the platform for global growth and globalisation. A free trade bloc on the other hand, is a course of action that enables the gains accrued to be kept within the group. The heads of government of the democratic nations of APEC have their constituents to appease, and it takes time for the general populous to lose their feelings of xenophobia.

THE MEMBER NATIONS

The founding members are Australia, Brunei, Canada, Indonesia, Japan, Malaysia, New Zealand, the Philippines, Singapore, South Korea, Thailand and the US. The third meeting of APEC held in Seoul in November 1991 served to demonstrate the goodwill that exists in the region. The three Chinas, The Peoples Republic of China, The Republic of China (Taiwan) and Hong Kong, were all accepted as members. Taiwan's concession to entry was that it be called Chinese Taipei

(Bergsten and Noland, 1993). Also from this meeting came the 'Seoul Declaration'. This announced APEC's commitment to regional free trade and economic conformity. Mexico and Papua New Guinea joined in 1993 at the Seattle meeting and Chile was accepted as a member in 1994.

The Ministerial Meeting in Indonesia in November 1994 placed a moratorium on new members, with the exception of Chile, whose membership was put forward at the 1993 meeting Bergsten, 1994b). New entrants, therefore, will not be accepted into APEC until after the 1996 ministerial meeting. Prospective members of APEC are Vietnam, Russia and Colombia (Caplen, 1994b). Interest has also been expressed from the Indian subcontinent, from both India and Sri Lanka. The dynamic growth that is apparent in the region will serve as a magnet to other prospective members.

The member countries are markedly diverse, from China with a population of 1.2 billion to Brunei Darussalam which has 260,000 people. The size of the countries also vary: Canada extends over 10 million square kilometres while Singapore's area is just 6412 square kilometres.

The economic statistics are equally far ranging (see Table 5.1). In terms of growth, Chile is the only nation that matches the growth of the booming East Asian nations. Averaged over the years from 1985 to 1992, GNP per capita has increased 8.5 per cent in South Korea, 8.3 per cent in Thailand, 7.7 per cent in Taiwan, and 6.1 per cent in Chile. This contrasts with the industrialised countries where Canada's figure is 0.3 per cent, New Zealand 0.4 per cent, Australia 0.7 per cent, and US 1.1 per cent per annum.

The members of APEC collectively account for 38.5 per cent of the world's population, 54 per cent of the global gross product, and 41 per cent of total world trade (See table 5.1).

The assortment of nations is unique. APEC combines the manpower of China, Indonesia, Mexico and the Philippines with the wealth of the financial markets of Taiwan, Japan, Hong Kong and the US. Also included is the manufacturing capability of the industrialised countries and of the NICs, connected with the natural resources of Canada, Papua New Guinea, China and Australia. Infrastructure is being established in Malaysia, and to a lesser extent, Thailand, to rival that already in place in Singapore. APEC merges the rapidly expanding influence of Asia, particularly the ASEAN countries, with the developed, but under-utilised, Western style economies.

WILL APEC BECOME A TRADE BLOC?

APEC's current mandate is based on the consolidation of decisions made at the previously held six annual ministerial meetings and its two annual leaders summits. It continues to be a mere forum, regardless of the global power base which makes up its constituency. Therefore, for the present APEC is an 'experiment' in open regionalism.

However, APEC's future purpose is unclear. Some members wish it to be more than a forum, others seem content with its current purpose, and a third group have not yet made public an opinion. 'The fundamental difference......centers on whether APEC should develop primarily as an organisation for reducing trade barriers, or as a club for promoting regional growth through more diversified means' (Smith M, 1993:77).

As a result of the EPG's report, APEC leader at the 1994 Leaders Summit in Jakarta accepted the open regionalism vision and a timetable for implementation of that vision. This timetable sought an elimination of trade barriers by APEC's developed nations by the year 2010 while APEC's developing nations worked towards the year 2020 (Kwang, 1995). However, this recommendation, although accepted as a policy, failed to achieve unanimous endorsement and the debate is therefore continuing.

The debate centres, on one side, on nations who are strongly in favour of the development of APEC into a formal group working towards free trade and open regionalism. This group includes the US, Mexico, Canada, Australia, New Zealand, Indonesia and Singapore; with Thailand and the Philippines favouring a slower pace. On the other side the debate is primarily and most vocally led by the Malaysian Prime Minister, Datuk Seri Dr Mahathir Mohamad, who states that 'APEC should not be a structured organisation'. Mahathir is concerned that APEC will become a trade bloc, used by North America and Japan to counter-balance the European Union. The third group, particularly Japan and China 'are difficult to gauge, in large part because of what is happening behind the scenes in trade talks with the US' (McBeth, 1994:32).

Whether the Asia Pacific region develops into a trade bloc has become an issue of concern in the region and of great interest to the world economy. Some trade blocs already exist. ASEAN formed AFTA (ASEAN Free Trade Area) in 1994. The EAEC (East Asia Economic Caucus), a forum, was created within APEC in 1993 and is supported by most East Asian nations and the USA to prevent further blocs being set up. The EAEC exists within APEC to help its members learn about each other and to generate understanding, goodwill and trust. It gives its members an opportunity to talk about economic issues of particular relevance to East Asia. The EU has insisted that APEC's plans for regional trade expansion are fine, but the region has to remain committed to a policy of open regionalism (*Tokyo Business Today*, November 1994).

As an institution, APEC is neither an economic union like the European Union nor a free trade area like NAFTA. APEC promotes free trade within the context of open regionalism in preference to a free trade area or a trade bloc.

THE ROLE OF APEC

APEC plays an important role in world economics because in terms of population and trade it stands for almost half the world. It also has a strong influence in world economics and in other international organisations such as WTO. The development also balances the world economic order, counteracting the power of the EU. The stable and high percentage of intra-APEC trade (see Table 5.10) makes APEC important globally. The effort of APEC through economic cooperation should ensure regional growth.

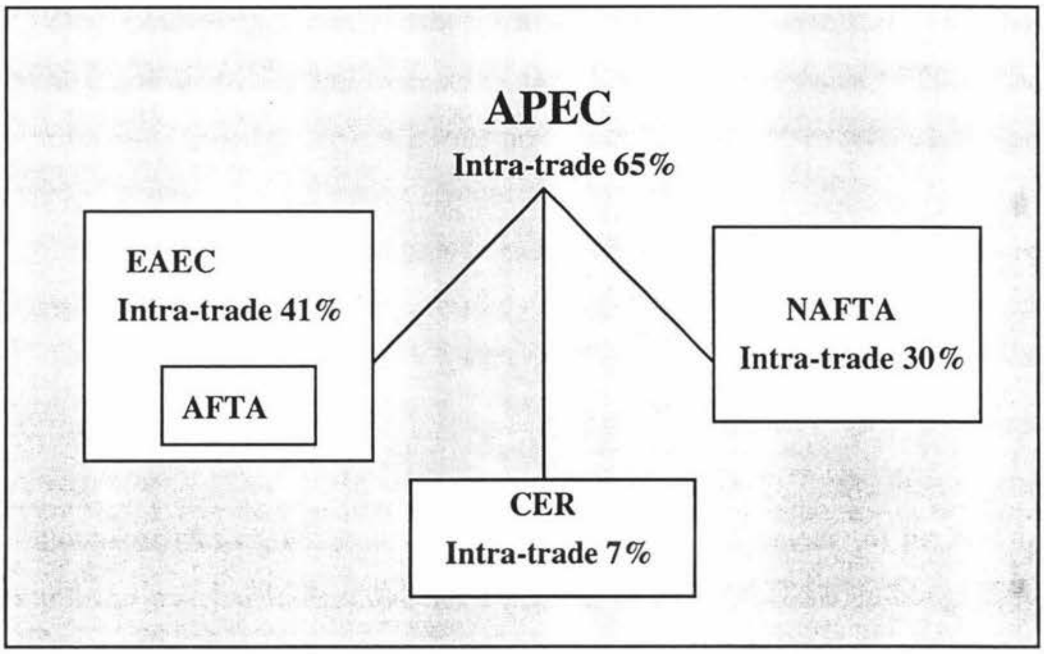
Table 5.10: The intra-APEC trade (billion US$)

APEC's exports	'88	'89	'90	'91	'92
Member countries	712.1	784.3	839.9	914.6	1,002.6
Outside APEC	367.3	395.7	436.8	480.6	515.4
Total exports	1,079.4	1,180.0	1,276.7	1,395.2	1,518.0
% of intra-APEC exports	66.0	66.5	65.8	65.6	66.0
APEC's imports					
Member countries	737.5	814.9	862.3	934.8	1,020.9
Outside APEC	384.6	425.7	480.0	468.9	498.5
Total imports	1,122.1	1,240.6	1,342.3	1,403.7	1,519.4
% of intra-APEC imports	65.7	65.7	64.2	66.6	67.2

Source: Australian Government (adapted from Awanohara & Chanda, *Far East Economic Review*, 18/11/93, p.17)

The objectives of APEC are to strengthen economic link and the multilateral trading system; to reduce barriers to trade and investment; and to specify opportunities for regional cooperation. APEC has become the primary regional organisation for improving trade liberalisation and economic cooperation in the Asia-Pacific region. It is the single largest forum promoting trade liberalisation. APEC was not designed to be a regional economic bloc. On the contrary, it is seeking to overcome barriers and inefficiencies in the region without any discrimination against other countries. It improves cooperation through groups within the region lowering barriers among the participants in WTO, and by increasing efficiency and expanding markets for others.

Figure 5.2: APEC and subregion arrangement



The Asia-Pacific region is geographically vast, and this is one reason why APEC is still a loose forum. Within APEC, subregional economic arrangements, such as NAFTA, EAEC, AFTA and CER have been established or proposed at the same time. Figure 5.2 illustrates the relations between them and APEC. All these subregional economic arrangement seem to support APEC. Intra-EAEC trade is around 41 per cent, intra-NAFTA trade around 30 per cent, intra-CER trade around 7 per cent and intra-APEC trade around 65 per cent, which is almost as large as the share of Western European trade. Thus the role of APEC in the Asia-Pacific region is important. Rising intra-regional trade and investment results in the growth of economic interdependence, and this growth makes regional economic cooperation more and more important. As the only formal forum in the Asia-Pacific region, APEC seems to be the best vehicle to improve regional economic cooperation.

APEC STRUCTURE

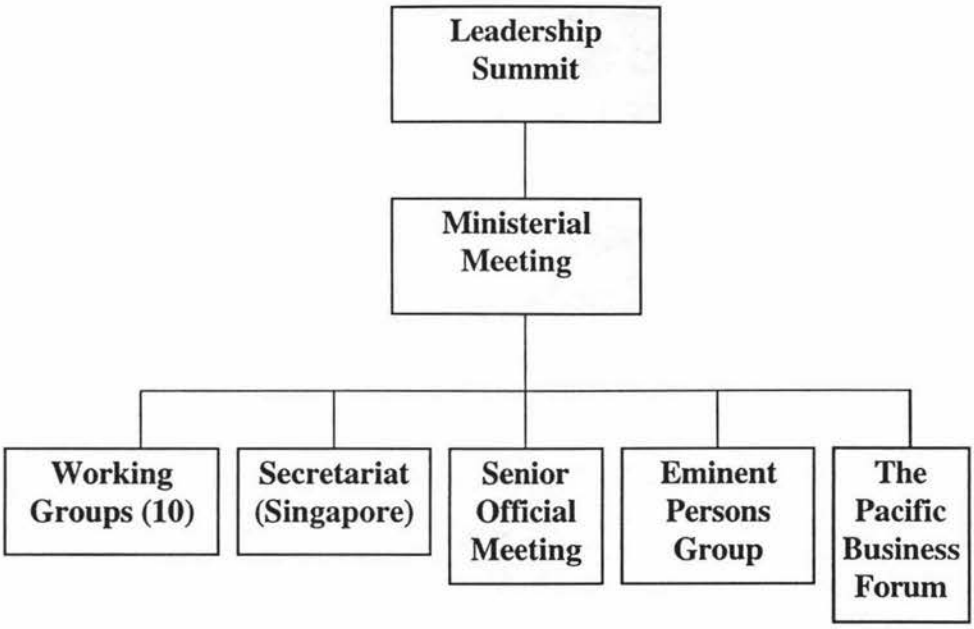
APEC started out as a loose forum but it has become more than that in the last two years. With the Leaders Summit an annual event and the vision of 2020, the loose forum is transforming into a structured grouping of countries with a common purpose. The operational structure is illustrated in Figure 5.3.

LEADERSHIP SUMMIT

The first leadership summit was held in Seattle in 1993 and has became an annual meeting where nation leaders are given the opportunity to meet, discuss and develop directives for administrators and politicians in the region. At the Seattle summit the national leaders did not reach any solid conclusions, although they approved the creation of a business forum and an education foundation (Cung, 1993a). To pacify China, Hong Kong's Governor Chris Patten and Taiwan's President Lee Teng Hui were not allowed to attend the summit: only lower-level officials from the two countries took part in the leadership meeting. As a reaction to the US's objection to the EAEC, Malaysia's Prime Minister, Dato Mahathir Mohamad, did not attend the Seattle Summit either.

The 1994 Jakarta Summit and Ministerial meeting concluded in November. Apart from Hong Kong's Governor and Taiwan's President, all heads of state attended this summit. The decision was taken to make the region a free trade area by the year 2020, and this is expected to be achieved in two stages: by 2010 the developed countries and by 2020 for the remaining countries of APEC.

Figure 5.3: The structure of APEC



MINISTERIAL MEETING

A high-level Ministerial Meeting is held once a year, and five annual ministerial meetings have been held since 1989. The most significant activity of APEC after the Leaders Summit, it is during this meeting that the region's government ministers review APEC's progress. APEC's senior officials also meet periodically to raise and develop issues for the ministers to consider and to give guidance to the working groups to co-ordinate APEC's activities and deal with specific issues.

TEN WORKING GROUPS

In an endeavour to keep all members up-to-date with ever changing business markets, ten working groups are in place to monitor change, to set standards and for consultation. These working groups cover such areas as (Garnaut and Drysdale, 1994):

- Trade/Investment issues and data
- Trade Promotion: Programmes and mechanisms for cooperation
- Expansion of investment and technical transfer
- Human resource development
- Regional Energy cooperation
- Marine resources conservation
- Telecommunications
- Fisheries
- Transportation
- Tourism

APEC SECRETARIAT

The APEC Secretariat, located in Singapore, is a permanent secretariat intended to institutionalise the grouping and to provide logistical support for APEC meetings and the activities of its working groups.

THE EMINENT PERSONS GROUP

An Eminent Persons' Group (EPG), made up of a group of key individuals nominated by APEC economies, was formed in 1992 (NZMFAT, 1995:13). was set up at the 1993 Seattle meeting at Australia's behest. Their brief was to develop a trade policy vision for the Asia Pacific region for the twenty-first century. In order to help achieve this vision, the group held meetings to develop proposals and recommend them to the organisation. In 1992 the EPG met in Tokyo to frame guidelines on financing global environment and development. It was decided that developing nations should contribute most of the money needed to fund environmental protection and development in their countries (Sugio, 1992). The Group issued its first report in October 1993. The main recommendations related to the desirability of APEC setting the goal of free trade. The Group issued its second report in August 1994.

The second report recommended that leaders and Ministers of APEC should (NZMAFT, 1995:14):

- Adopt a long-term goal of free and open trade and investment in the region.
- Aim to begin implementing APEC's programme of trade liberalisation to achieve that goal by the year 2000.
- Aim to complete the liberalisation process by 2020, with the more economically developed nations eliminating their barriers more quickly than the newly industrialised countries.

This EPG report provided a particular focus for the Leaders' and Ministerial Meetings in 1994 in Bogor, Indonesia. Guided by these visionary statements, an agreement to establish a free trade region by 2020 was agreed upon at the 1994 Leaders Summit in Bogor. Based on the EPG report, the Meeting accepted an interim step where developed countries of the region would reduce tariffs by the year 2010. Significantly, the proposal has been accepted before the detail has been worked through. This laissez faire attitude indicates a commitment on the part of members not to get too bogged down in detail.

THE PACIFIC BUSINESS FORUM

The APEC economic leaders at their Summit Meeting on Blake Island in November 1993, asked business leaders to establish a Pacific Business Forum

(PBF) to 'identify issues APEC should address to facilitate regional trade and investment and encourage the further development of business networks throughout the region' (NZMAFT, 1995:32).

The establishment of the PBF is a recognition by APEC leaders of the importance of private sector involvement in APEC. The PBF has served to draw senior business leaders into discussions on the region's economic future. The forum has greatly assisted in under-scoring the priorities of APEC business communities and the role of governments in advancing those priorities.

The PBF includes representatives from both large and small scale industries and it gives high priority in its 1994 report to further trade and investment liberalisation, business facilitation through deregulation, easier border procedures and progress on standards and conformance, and human resource development (APEC, 1994).

PACIFIC ECONOMIC COOPERATION COUNCIL

The Pacific Economic Cooperation Conference is APEC's non-government sister organisation that has been doing much of APEC's work and helping APEC to succeed. PECC (Pacific Economic Cooperation Council) has the same objectives as APEC: strengthening economic ties primarily through liberalised trade (Smith M, 1993). At its ninth General Meeting in 1992, the PECC chose 'Open Regionalism: A Pacific Model for Global Economic Cooperation' as its theme. In support of this theme, representatives of the twenty Pacific economies that make up the Council prepared and signed an unusual declaration. It set forth the conditions essential for an open region and committed the council to support these conditions (Cheit, 1992).

THE BENEFITS

APEC offers its members something positive by providing opportunities to support regional economic transactions among members, and by playing a consultative role for members.

Besides reducing tariffs the benefits include (Garnaut and Drysdale, 1994):

1. Forming working groups for better communication among members
2. Helping intra-regional trade by reducing tariffs and cutting non-tariff barriers
3. Speeding up trade liberalisation and facilitation
4. Working on standardisation throughout the region
5. Assisting investment liberalisation
6. Providing more opportunities for small countries
7. Insuring better cultural understanding and acceptance
8. Offering the possibility to reach a group agreement or cooperate in an approach to other international forums.

APEC CONCERNS

The formation of APEC, bringing together nations of the West and the East, the developed with the developing, and overcoming obstacles placed by cultural, political and economic differences, has by no means been a simple exercise. Concerns, apprehensions and suspicions still remain. In the following section, some of these concerns are discussed.

PROBLEMS FOR THE US

The United States' trade with APEC's members has been large - in 1994 it stood at 40 per cent of its total trade (see Table 5.3). Although Asian countries within APEC have tried to divert part of their trade to other areas, the US, being a large market for Asian products, has held great influence over APEC members.

However, this influence has waned somewhat. Intra-Asia trade has been growing four times more rapidly than trade between the US and Asia (see Table 5.3). Yet America's exports to Asia are growing faster than its exports to any other part of the world. Asia is becoming more important to the US but not vice versa. In May 1994, US President Clinton disassociated the issue of renewal of China's most favoured nation trading status from human rights as this issue had worsened relations with China (CNN Live, 28 June 1995). The United States' relationship with Japan also hit a low point in February 1994 when talks between the two leaders Bill Clinton and Morihiro Hosokawa broke down in Washington.

In the issue of trade liberalisation, some protected countries, such as Indonesia and China, have sacrifices to make. Their tariffs are at the highest level, while the US's tariffs are amongst the lowest in the region (Dobbs-Higginson, 1993). This point of view can postpone trade liberalisation though the US may extol the virtues of free trade within APEC.

Some ASEAN leaders have been afraid that the US would dominate every issue within the region even though their behaviour tends to be more protectionist. According to the US, the Asia-Pacific region consists of two important dialogue institutions, APEC and the newly created ASEAN Regional Forum. The former will be the main vehicle for building economic cooperation, while the latter will be used to enhance regional security (Holloway, 1994a:29).

JAPAN'S NEEDS

Japan recognises the danger of being discriminated against by powerful economic groupings in Europe and in the Americas. Although trade within Asia has increased, Japan still accounts for around 30 per cent of total foreign trade with the United States and around 15 per cent with Europe (Rowley, 1992). Access to these markets is very important, and APEC appears to provide Japan with a good opportunity to operate within a multilateral trade system which includes both Asia and the US. Also, APEC's character of trade liberalisation and non-discrimination will favour Japan's economic needs. It is therefore in Japan's interest to support the APEC model for free trade within an open regionalism concept (Chandra, 1993). In this sense, it is not in Japan's interest to commit itself to any discriminatory regional integration such as the first proposal of EAEC, the East Asia Economic Grouping (EAEG).

ASEAN'S CONCERN

When the annual brainstorming meeting of economic ministers from the six ASEAN states (before Vietnam joined) was held on September 22-23, 1994, the ASEAN Free Trade Area received a resounding vote of support, but did not give similar enthusiastic support to the 17 member APEC forum (Chile was not then a member). They were reluctant to see the organisation expand beyond its current informal role (Schwarz, 1994). The ASEAN economic ministers were particularly concerned about the recommendations of a report by APEC's EPG who drew up a blueprint for APEC's future. One of the ministers commented 'The EPG report is a big provocative document. But EPG members did not think of the feasibility of what they were suggesting' and it could lead to 'excessive institutionalisation of APEC'. It has failed to find endorsement from the ASEAN ministers (Schwarz, 1994:14).

INFLUENCE OF CHINA

APEC is an economic forum with its main objective being trade and investment liberalisation, but it does not take a stand as a stoutly independent organisation when a large political member exerts its influence. In order to pacify China, Hong Kong's Governor and Taiwan's President were not allowed to attend the annual leadership meeting both in Seattle 1993 and in Jakarta 1994. Hong Kong and Taiwan are welcome to contribute in economic aspects but are not given the same opportunity to discuss matters at the highest summit. APEC's growth will be marred by this fact.

CONCLUSION

It is often said that governments follow the lead of their people. In the case of the APEC experiment this is true, but only to a degree. The governments of the region have accepted an economic principle and are endeavouring to put this principle into action on a large scale. The principle followed is that of comparative advantage, where it is accepted that every nation can be self-sufficient only at an enormous cost. Economies of scale are achieved when a group of nations becomes collectively self-sufficient. Rather than impose conditions on their business sectors, APEC governments are putting a medium in place to assist the change from a national to a regional emphasis. For some, this is a brave step as the benefits will not accrue until the future. Forward-thinking nations such as Malaysia are well advanced in establishing a regional infrastructure. Others will undoubtedly follow.

The European Union was the first of the major blocs to become established, but it has deficiencies as a role model for other blocs. It is important, therefore, that

APEC's experiment in open regionalism is a success. The implications for the evolution to globalism are enormous.

The nations of APEC are a unique blend. They are each rich in different ways, be it people, cash, natural resources or intellectual properties. The pooling of such an imposing wealth of resources should, if properly managed, enable APEC to become the symbol of free trade that sets the trend for all others. As Indonesia's President Suharto has said on the 2020 deadline for free trade set by APEC, 'It doesn't matter whether you want it or not, whether you like it or not, or whether you are prepared for it or not: We have to enter the international free-trade system' (*Far Eastern Economic Review*, 1995).

There are conflicting opinions among APEC's members (Garnaut and Drysdale, 1994). While the developed nations such as the United States, Australia and Canada prefer rapid transformation of APEC from a consultative forum into a body for actual negotiation on trade standards and other issues, ASEAN countries continue to oppose such a move. These countries are afraid that their influence would be weakened in an organisation which might be dominated by large members such as the United States and Japan.

US President Bill Clinton wanted to strengthen APEC as a tool to open Asian markets but Japan was not in support of this idea (Cole, 1994b). Japan wants to ensure Asia's stability, both economically and militarily. Japan is also aware of the distaste of neighbouring Asian countries for intervention by the US, with its tendency to dominate (Cole, 1994a). Japan would like to play the role of broker between the US and Asian countries.

There are two alternative paths APEC could take. One is a free trade area operation such as PAFTA, the other is 'ASIAN OECD', a forum for extensive consultation but without a large secretariat. The latter would promote multilateral trade, assist the WTO by issuing supplementary economic policies for the region, and provide a neutral forum for every economy in the region to discuss issues of regional interest.

Before the 1994 APEC summit, APEC's Eminent Persons Group made the key recommendation that APEC launch a free-trade programme by 2000, to be completed by 2020, with more advanced members eliminating trade barriers five or even ten years ahead of that target (Bergsten, 1994b). This means that the developed countries would achieve the free-trade target before 2010 and the other countries by 2020. This recommendation was endorsed by the Leaders Summit in Bogor, Indonesia in November 1994.

In order to prevent APEC from becoming a trade bloc, members have promoted the idea of open regionalism. The US feels that trade privilege should be provided to partners outside APEC on a reciprocal basis but, in contrast, Malaysia and other countries want to be able to offer and receive such benefits unconditionally on a most-favoured-nation basis (Vatikiotis, 1991c).

PART III

CONCLUSION

There are three purposes in this concluding chapter. First the objectives of the thesis are reviewed. Second, the stated hypotheses are considered in relation to the analysis. Finally, there is discussion based on the analysis.

Chapter 6

Results, Discussions and Conclusion

Reviewing the objectives of this research provides a good point at which to start assessing its progress towards a useful conclusion. The objectives were basically to develop a conceptual model for understanding the nature of economic global realignment as a process towards globalisation; to development of a set of hypotheses that addresses the nature and process of the realignment; and to understand the relationship between regional group formations and the global system of which this realignment is a part. The validity of the study and the insights derived from it, must be viewed within a framework that allows an objective appraisal of the globalisation process. This new world order is being achieved by way of different variations in the regionalism concept.

MODEL BUILDING

The Conceptual Model in Figure 1 formed the schematic base for the current study. It provided an overview of the globalisation process where the economic relationship of nations progresses from a relationship based on national interest, as suggested in stage 1, to a more global relationship, as suggested in stage 4. The relationship in stage 1 reflects a relationship based on nationalism and independence, while at the extreme end of the developmental stage, the relationship is toward mutual growth, cooperation and the interdependence of nations within a global free trade framework as supported by WTO/GATT. In this progress toward global free-trade, regional arrangements such as the EU, NAFTA, AFTA and APEC are being supported. In this expanded environment, small nations in the regional groups, such as Brunei Darussalam in APEC and ASEAN, and Luxembourg in the EU, poorer nations such as Mexico in the NAFTA, and Vietnam in ASEAN, are seen to be equal participants within the respective groups.

In the intermediary stages 2 and 3, there is a conscious shift among economies to form regional trade groupings. The European Union is seen as the initiator of this trend toward trade groupings. The EU is now steadily progressing to a monetary and political union in what will be a single Europe. Similarly, the formation of NAFTA in the Americas has prompted the development of other regional trade groups, such as the AFTA in South East Asia and the Mercosur in South America. As a result, trade between regional trade blocs is also growing, and this further enhances the development of regional groups. This is implied in Stage 3. Transatlantic trade negotiations between NAFTA and the EU, and the recent AFTA - EU Summit Meeting held in Bangkok in February 1996 are both examples of this cooperation between regional trade blocs.

APPRAISAL OF THE GLOBALISATION PROCESS

The appraisal of the globalisation process will be presented in the order of the respective hypotheses established in the introductory chapter. This thesis has discussed the process of globalisation as reflected in the qualitative analysis of the developing regions. NAFTA, and more particularly APEC, are recent formations and as such the performances of these groupings, based on quantitative data, may not reflect the true nature of relationships between member countries within the region. For example, it is impossible to quantify the trade performance of APEC as a trade group. The 18 member nations of APEC are yet to realise the impact of a free trade area which is targeted for the year 2020.

Hypothesis 1

> That globally, there is a shift from multilateral trade relationships to trade based on regionalism.

Hypothesis 1 suggests that the interdependence of nations has created a regional awareness as a basis for economic cooperation. One of the major issues of world trade as we move toward the 21st Century is the intensity of trade bloc formations. The free trade advocators, the European nations and the United States (with Canada and Mexico) have grouped to form the two largest trade blocs the world has known. The European Union and the NAFTA have been dealt with in chapters 3 and 4 respectively.

A significant feature of recent decades has been the manner in which the growth of trade has outpaced the growth of production in the global economy. In 1988 total world exports were four times greater than in 1960, while total world output was a little under three times greater than in 1960 (Dixon, 1993). This divergence in the two growth rates is a clear indication of the increasing degree of inter-dependence in the global economy. However, more recently, the world economy is witnessing a move towards more intra-regional trade (see Table 6.1). Countries are now orientating towards a more regional focus as witnessed by the continued integration of the EU, the formation of NAFTA, and a growing Asian regional consciousness.

World trade seem to be dominated by the three regions of Europe, North America and East Asia: 79.8 per cent of world exports were generated by and 79.2 per cent of the world imports received by them in 1992. These three regions contained nearly 80 per cent of the world trade, and generated about 70 per cent of the world output (IMF, 1993). Dixon (1993) described the three regional blocs as the 'triad' which like a modern, three-legged Colossus sits astride the global economy, and absolutely dominates current economy and trade. Kenechi Ohmae (1985, 1995) reflects a similar understanding of global realignment.

TABLE 6.1: REGIONAL TRADE OF THE THREE LARGEST ECONOMIC REGIONS

World Trade Share %

	Region	1980	1985	1986	1987	1988	1989	1990	1991	1992
Exports	East Asia	14.4	20.1	21.0	21.3	22.3	22.3	21.1	23.0	24.0
	EU	36.5	35.9	40.3	40.7	39.6	38.9	41.2	39.9	39.8
	NAFTA	15.2	16.8	14.4	14.8	16.3	16.6	15.7	16.0	16.0
	Total	66.1	72.8	75.7	76.8	78.2	77.8	77.9	78.9	79.8
Imports	East Asia	14.8	16.8	15.7	16.2	18.5	19.3	19.1	20.3	20.8
	EU	39.7	35.1	37.9	39.2	39.1	38.8	41.3	40.9	40.3
	NAFTA	16.3	23.3	21.5	21.1	20.7	20.4	18.6	17.8	18.1
	Total	70.8	75.2	75.1	76.5	78.3	78.5	79.0	79.1	79.2
Total	East Asia	14.6	18.4	18.3	18.7	20.3	20.8	20.1	21.7	22.3
Trade	EU	38.4	35.5	39.0	39.9	39.4	38.9	41.2	40.4	40.0
	NAFTA	15.8	20.1	18.0	18.0	18.5	18.6	17.1	16.9	17.1
	Total	68.5	74.0	75.3	76.6	78.2	78.3	78.5	79.0	79.5
Trade	East Asia	-0.4	3.3	5.3	5.1	3.8	3.0	2.0	2.7	3.2
Balance	EU	-3.2	0.8	2.4	1.5	0.5	0.1	-0.1	-1.0	-0.5
	NAFTA	-1.1	-6.5	-7.1	-6.3	-4.4	-3.8	-2.9	-1.8	-2.1
	Total	-4.7	-2.4	0.6	0.3	-0.1	-0.7	-1.0	-2.8	0.4

Source: International Monetary Fund, *International Financial Statistics*, (Washington, D. C. 1980-1993)
Note: Countries that are part of East Asia not included are Myanmar, Cambodia, Vietnam and Laos.
The EU data does not include the three newest members - Austria, Finland and Sweden

Hypothesis 2

That there is a fundamental paradigm shift in political thinking and policy making towards interdependence of nations rather than independence.

Table 6.1 summarises the global economic triangle and suggests that the world trade share of East Asia has grown at a steady rate from 14.6 per cent in 1980 to 22.3 per cent in 1992, while in the same period the EU and the NAFTA have grown only from 38.4 per cent to 40.0 per cent and from 15.8 per cent to 17.1 per cent respectively. East Asia has also a large surplus of exports with both North America and Europe and a stable trade surplus averaging 3.55 per cent during this period. The trade balances of the EU and the NAFTA over the same period, however, have averaged 0.46 per cent and -4.36 per cent respectively.

TABLE 6.2: EAST ASIAN EXPORTS DEPENDENCE BY REGION

Share of total exports, %

		1980	1985	1986	1987	1988	1989	1990	1991	1992
East Asia to:	USA	22.3	32.3	34.1	32.1	29.4	28.9	26.4	24.2	24.2
	EU	15.4	11.1	13.8	14.9	12.6	15.2	16.4	16.5	15.6
	Japan	10.3	8.7	7.3	8.1	8.6	8.8	8.6	8.3	7.8
	Asian NIEs (a)	14.7	14.1	14.7	16.5	17.8	18.4	19.7	21.3	21.8
	ASEAN (b)	7.2	5.2	4.4	4.8	5.3	6.1	7.3	7.5	7.3
	China (c)	2.6	5.9	4.5	4.3	4.9	4.7	4.1	5.0	6.2
	(a)+(b)+(c)	24.6	25.1	23.6	25.6	28.0	29.2	31.2	33.8	35.3
	East Asia	34.8	33.8	30.9	33.7	3.6	38.1	39.8	42.0	43.1

Source: Compiled by NRI based on IMP, *Direction of Trade Statistics* and MoF (Taiwan), *Monthly Statistics of Exports and Imports.*
Note: This Table is adopted from Kwan (1994, p102).

Table 6.2 above indicates the emergence of the East Asian region into a more economically integrated regional economy than ever before. The general perception from outside, however, is that the region is not homogeneous and ready for a single united East Asia (*The Economist*, 2 March, 1996:25; 9 March, 1996: 27). Indeed, the social, cultural, political and economic contrasts and conflicts that exist within the region make it one of the most potentially volatile in the world. Though this may be the case, recent trends in East Asia seem to go against this perception. The region is drawing synergy as never before and is forging a new cooperative dynamism as seen in the formation of ARF, AFTA and ASEM.

Globalism based on the concept of open regionalism was formally recognised with the formation of APEC. Asia, especially ASEAN, is the central focus of this regional alignment. At present, Asia holds 25 per cent of international trade and this is expected to grow further at the expanse of the present dominant regions (ibid). This realisation places Asia on a different keel - that before long Asia will be in a key position to influence world politics and economic decisions. This has created the need for a closer understanding of the economies in the region. There is strong evidence of exchange of ideas and views, cooperation in development projects, and greater interdependence between the different countries of the regions in the pursuit of mutual economic development.

This is causing a fundamental shift in political thinking and policy decisions. Formalisation of APEC is a result of this shift, where East Asia is seen as a major global player that can no longer be ignored. In fact it would be in the interest of the developed economies of the Pacific to include the developing nations of this region in a cooperative arrangement. The one time opponent of regional arrangements, the US, moved away from opposition to support of regional trade blocs when it promoted NAFTA.

The movement toward regionalism and a growing consciousness of evolving Asian identity has also brought large trading groups such as the EU to the negotiating tables. The Asia-Europe Summit (ASEM) which ended on March 2, 1996, was said to have been an eye-opener to the Europeans (*The Economist*, 9 March 1996:27). It was reported that the bridging process between the continents showed that the former colonialists now treated Asian countries as equals, and took the economic potential of Asia seriously. The differences between the negotiation methods such as Asia's 'consensus more important than break-through, camaraderie than formality, and process than substance' was for the 'first time' appreciated by the Europeans who were used to 'formal fixed agendas and timetables' and preferred to 'report negotiating triumphs to their parliaments and electorates' (ibid).

Summit meetings are now becoming common within APEC, and between regional groupings, and these will invariably contribute to changes in political thinking and policy decisions as demonstrated above.

Regions will be seeking to achieve the following policy issues:

- establishing of economic frameworks that will reflect the synergy of the region
- moving toward self determination in defence and in world politics
- seeking the security and the operation of multilateral organisations
- playing a greater role on regional and global issues
- pushing for a freer world economy
- widening its sphere of influence to include other nations in the region.

If the interdependence of nations does not emerge, the current level of economic performance of Western nations indicates that the international market place may become more protectionist (Selvarajah, 1994). Nations may impose more trade barriers and, as we have discussed in Chapter 2, imposing protectionist trade barriers may give temporary economic gain to those countries imposing them but in the long term this may lead to the slowing down of the world economy. The risk is, perhaps, even greater now than during the Great Depression of the 1930s as nations are now more global in orientation.

The Asian region has had and continues to have political, economic and social problems. It is clear that the division between socialism and capitalism remains as one important dimension of the regional fragmentation. The capitalist nations have experienced the worst of the communist insurgencies, but pockets of real and potential trouble still exist. Many political hot-spots exist within the region, such as the unresolved stalemate between the two Koreas; the transfer in 1997 of the

British Colony of Hong Kong to socialist China; and the separatist movements in East Timor. These situations can erupt very quickly into violent expressions of dissatisfaction and repression.

A global Asian identity, however seems to be emerging as a result of immigration, global commuting, improved communication and the accelerated mobility of capital. The overseas Chinese that have historically settled throughout South East Asia are the best illustration of a trans-national East Asian community and are helping to forge links between South East Asia and North East Asia, especially China, Taiwan and Hong Kong. A similar trend is recognised where overseas Indians are forging links between South East Asian economies such as Singapore and Malaysia and the Indian subcontinent.

Increased protection of the American market and the formation of NAFTA is likely to be accompanied by a general reduction of the American presence in East Asia. The easing of global tension has particularly reduced the significance of American presence and there are clear signs that Japan is ready to replace the US in East Asian economic activity. On the other hand, as discussed earlier, although Japan and the Asian NIEs are the main players, and China is the potential economic giant in the region, East Asian integration cannot emerge without the full participation of ASEAN.

Hypothesis 3

> That the needs of a country are balanced with the needs of the region and where national stability is strengthened by the prospects of regional growth

This hypothesis suggests that through greater regional awareness, nations are balancing their economic, political and social needs with the needs of the region and through the prospects of greater regional economic growth, individual nation's economic and political stability are enhanced.

The effects of the Second World War, the demise of Communism as a global political ideology, and the growing concept of the global village changed ideas on nationalism and the sole importance of the nation state. Countries have formed alliances for purposes of security, stability and economic growth (Baldwin, 1993). History, in both Europe and Asia, has shown that nations have gone to war when traditional alliances have broken down. The two major wars in this century are examples of the result of rivalry. The EU and the ASEAN are good example of regional groupings formed to create regional political stability and to enhance economic growth in both individual member countries and in the region collectively.

The creation of the US-Canada Free Trade Area and subsequent formation of NAFTA was developed out of economic necessity and has been driven by the need for political stability and the ability to expand markets that were previously bilateral.

Integration and cooperation in the EU has had some set-backs. The member states of the European Union are collectively having some difficulty in casting off and ceding sovereignty to European institutions. Member nations, such as Britain, are seeking a balance between maintaining their national sovereignty and identity and becoming part of an expanded Europe. The economic growth of Europe, collectively, is seen as an important contributing factor in the growth of the British economy. To pursue both goals, that is to be part of the EU and to maintain aspects of British sovereignty, Britain has proposed the idea of European Club. Nations such as Switzerland and Norway have based their rejection of the EU membership on national interest - they are not prepared to lose economic gains and neutrality respectively.

Hypothesis 4

> That the concept of national dependence being enhanced by regional interdependence is inevitably leading to global interdependence.

The philosophical thrust of this hypothesis is that regionalism is a route to multilateralism: it would continue to expand, eventually embracing many, preferably all (Bhagwati, 1993:45).

The formations of EU and NAFTA grouped two of the world's largest economic regions and have driven the world to trade more regionally. Their formation has had strong influence on the world economy and trade order, and the trend towards trade regionalism now characterises global trade. The question here then is whether regionalism contributes to global growth more than it retards it.

The premise for the development of regional groupings, as mentioned, has been to increase the degree of economic interdependence among members by creating stable democratic political institutions and market-oriented economic institutions. As far as these objectives go, arguments for trading blocs do have strong merits.

We raised the question in chapter 2 whether a trade bloc promotes free trade or whether it promotes protectionism? The phenomenon of trade blocs may pose a serious threat to the free world trade order and to the World Trade Organisation. Indeed, the WTO has a role in the management of trade blocs. Although all trade blocs claim that they are compatible with WTO's free trade philosophy, it is a fact that a trade bloc will favour its members against those who are not, and will encourage its members to trade within its region rather than outside its bloc. Almost all of the current trade blocs are grouped along geographical locations and the development these world trade blocs has seen some trend towards greater regional insularity.

Bhagwati (1993:45) states that the US vision for regionalism as a clear route to multilateralism was flawed. He quotes 'If American regionalism is not to turn into a piecemeal, world trading system-fragmenting force, it is necessary to give to it a programmatic world trade system unifying format and agenda'. The discriminatory stance taken by the US in rejecting Malaysia's proposal for an Asian trade bloc is he says, 'self-contradictory and self-serving: trade blocs are good for us but not for you'.

Such discouragement by the US in itself implies that regionalism is harmful or if left unchecked may be harmful to international trade and free market operations.

SUMMARY OF RESULTS

The discussions outlined above indicate:

- the emergence of regions more economically integrated;
- a trend towards regional economies with self-sustaining growth supported by intra-regional trade;
- direct foreign investment from countries within the regions, and
- a regional integration which includes the socialist countries with the democratic nations, small countries with the large, poor countries with the rich.

This thesis supports the following hypotheses:

- that globally there is a shift from multilateral trade relationships to trade based on regionalism;

- that there is a fundamental paradigm shift in political thinking and policy making towards interdependence of nations rather than independence;
- that the needs of a country are balanced with the needs of the region and where national stability is strengthened by the prospects of regional growth;

and gives only qualified support to the following hypothesis:

- that the concept of national dependence being replaced by regional interdependence is invariably leading to global interdependence.

DISCUSSIONS

As the world settles into a new economic orbit, caused by the shift in economic power eastwards, the ensuring scramble to retain past economic positions will cause nations to seek new alliances with those that can assure them of their own continued prosperity. This inturn will lead to a trend towards global co-ordination in trade.

While global realignment is viewed mainly as inter-country, it could also be inter-firm, allowing firms as well as countries access to economies of scale and learning as well as access to markets, technology or to a government's requirement for local ownership (Porter, 1990:66). Porter states that 'Alliances are frequently transitional devices. They proliferate in industries undergoing structural change or escalating competition, where managers fear they cannot cope' (ibid). While this quote relates to individual firms, it can also apply to nations and governments facing political and economic crisis.

With the admission of Austria, Sweden and Finland, the EU has probably reached the maximum number of members to make it workable in its present form. The

With the admission of Austria, Sweden and Finland, the EU has probably reached the maximum number of members to make it workable in its present form. The goal of the EU must be to create a democratic, less bureaucratic, integrated economic and political all-or-nothing Union of European countries, governed by a parliament with supernational powers. A deepening of the Union is needed before a widening to the East can take place. This deepening is best achieved with a one-speed Europe, rather than a multi-speed collection of countries that are pulling in different directions and choosing only what is good and convenient for themselves.

To create a united Europe, the EU needs to have common laws, defence, foreign policy and a single currency. These, when achieved, will give the EU unmatched clout in the world in terms of financial, political and military strength.

The trend in the future (and NAFTA is an example) is to move away from the bilateral style of agreements that are discriminatory, and focus on multilateral agreements on regional basis. The preferred agreement is WTO, except that it is now too large (117 members) and, because of the process involved, it is too slow in making decisions. The latest GATT Round took seven years instead of the normal five-year period.

NAFTA is perhaps an example of how first to remove trade barriers within a geographical region and proceed to global trade liberalisation at a later stage. The agreement is innovative in that it addresses environmental and investment issues. If NAFTA is to progress, it will need to develop common understanding on how regulatory laws can be applied within NAFTA and what impact these will have on its trading neighbours.

How big will NAFTA grow in the future, or will it be an alternative trading bloc based on highly competitive countries/industries? This question is being answered by the inclusion of Chile, as NAFTA seeks to expand. Even today, NAFTA is not the final solution as Mexico struggles with economic reforms and the falling value of the peso. Will the US and Canada under NAFTA have to protect their investments in Mexico?

Is NAFTA the US's answer to the EU? It would appear from the analysis above that the US has strategically planned NAFTA to create opportunities that may go missing not only in the EU but also in other regions such as East Asia (for example within the ASEAN grouping). However, with the NAFTA nations becoming part of APEC, the chances are less likely that the US will be denied opportunities in East Asia.

The EU offers no guarantees to the US in terms of access to markets, especially in the area of services. With NAFTA, the US has secured a market the size of the EU and, with the impending admission of Chile and other Latin American nations, in the future that market will be substantially larger than the EU. In order to gain access to NAFTA markets the EU will be forced to ensure that it reciprocates by allowing freer access by the US and other NAFTA nations. One could well say that this is the very reason why NAFTA is the US's response to the EU.

Last but not least, the growing economies of Mexico, Chile and other Latin American countries (potential NAFTA members) offer lucrative markets for US goods and services. These countries with a large young population may eventually create a bigger market for US goods and services than the whole of the EU ever could.

It seems that for now at least, the US has come out with a winning survival strategy.

NAFTA can be said to have both positive and negative elements in its design, function and worth as one of the world's attempts to create a more open and freer trading environment.

Its highlights include (a) being an improved version of the Canada-US Free Trade Agreement, (b) elimination of duty and non-duty barriers on regional trade [a plus for the three members but not for non-member countries], (c) the commitment of freeing up trade and investment, and (d) setting precedents for future regional and multilateral negotiations by substantially opening the financial services market in Mexico to US and Canadian participants by the year 2000.

Its negative elements, include (a) basic energy remains immune to free trade, especially with Mexico's vast oil reserves, (b) labour and environmental issues are moving at a very slow pace and (c) restrictive rules of origin that have been labelled tools of discrimination.

NAFTA is a noteworthy achievement, but its implications for the three member countries can not be exaggerated. By widening the scope of the market and enlarging the range of available labour skills, NAFTA enables the North American companies to compete more effectively against foreign producers, both at home and in the world markets.

Yet NAFTA does not suggest to the world trading market that the Americans are keen to pursue a totally open market. They appear to want to create an extended home market basically to bolster their own economy. Until trade agreements such as NAFTA, EU, AFTA and even CER fully acknowledge that the world needs to be totally borderless, there will never be free trade.

Talks are continually taking place within ASEAN and some East Asian countries for the construction of a European Union-type structure to present a common

The integrationists' case for believing that East Asia can integrate rests on growing economic link and on the idea that the region has a great deal in the way of common heritage.

In conclusion, despite the social, cultural, political and economic contrasts and conflicts faced by the APEC nations, a strong alliance based on cooperation is indeed taking place. Restricted access to the European markets has also increased the intra-US and Asian trade, and regional cooperation.

The two markets that have to remain open for a developing East Asia are Japan and the US. In the past the US interest has been global, but with the formation of NAFTA there is increasing doubt whether this interest will continue. Its position in APEC is important to developing countries in Asia as they still need the US market for their exports. It would be the in US interest to safeguard its current dominant position. Remaining an active and influential member of APEC and being part of the Asian economic sphere is crucial to maintaining this position.

There still exist various opinions among APEC members about free trade and open regionalism. For example, the Japanese outlook seems to be more regional (Cole, 1994a). China thinks APEC should recognise members' different levels of economic development to ensure poorer ones do not lose out if tariffs were to fall progressively faster. While Indonesia and Singapore want to go ahead with free trade, Thailand and the Philippines favour a slower pace. Malaysia's Prime Minister, Datuk Seri Dr Mahathir Mohamad, thought that APEC should not be a structured organisation, it should be a mere forum in which developed nations could help less developed nations with their problems (Hoon, 1993; Kiyokatsu, 1993). APEC officials acknowledge there is still much work to be done to turn the forum into a functioning free-trade area based on the concept of open regionalism. It is said 'What is politically impossible now may not be politically impossible in a few years' time' (McBeth, 1994:29).

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The number of blocs that exist within APEC may be viewed as an evolution - as steps from nationalism to localism to regionalism, before the final step of globalism. It can be argued that the nations of CER, AFTA, NAFTA, and even other groups such as the Arab Common Market and the Andean Common Market, are natural developments towards larger groupings. It is unlikely that APEC will be made redundant as nations interfuse within multiple and overlapping free trade areas. This will effectively leapfrog APEC on to the globalist path. APEC's strength is in the relationships that its member nations have already built.

CONCLUSION

Competition has been a strong motivating force in establishing these regional groupings. As indicated in this thesis, the world is currently witnessing the biggest shift in economic strength for more than a century. The industrial economies at present dominate the globe as they have for the past two decades. Yet within a generation several are likely to be dwarfed by newly emerging economic giants.

Global competition has come about basically to create wealth in a secure environment, and the three triads have been formed in support of this principle. All through the world countries are seeking new alliances to maintain or improve living standards. This has been the underlining theme for the new global realignment.

The emerging poor class of displaced low skilled workers in developed countries and the lack of development in the African continent appear as two black spots in the current global realignment. If these trends cannot be averted in some way these spots could threaten the new world economic order.

An integral part of global realignment is the assumption of global leadership. The former colonial powers, Great Britain, France and the Netherlands, have passed the mantle of global leadership to the United States as their global interests waned. During the late 1980s and 1990s, the US accumulated high levels of debt and trade deficits, and with the ascendancy of Japan the international economic baton is again about to change. Historically, economic strength has gone hand in hand with political strength. This suggests a number of developments over the next few years to determine where the new mantle of leadership will lie. Increasing political stability within the Asia region and the status of a number of Asian countries as creditor nations strengthens this potential claim.

Japan on the other hand has never taken a global leadership role. It has continually avoided any kind of global leadership and it is quite unlikely that it will take a leading political role in international affairs in the near future. However, there are strong indications that, at least on the economic front, the country is entering a new era. Japan has a relatively closed US$4 trillion economy. Its current import of manufactured goods is only 3% to 4%, while the average for the G7 countries is 10% (Holloway, 1994b; Higgott, Cooper, and Bonner, 1991). If Japan becomes an importer of manufactured goods, it alone could restart the depressed world economy.

With the defeat of the Liberal Democratic Party in 1993, after 38 years in power, a fundamental change in thinking is taking place in Japan. The coalition Prime Minister Morihiro Hosokawa promised deregulation and market opening reforms. Politically this is difficult as it would entail shifting the electoral base more to urban Japan, creating a set of policies to free up consumption and to allow imports to rise, policies which are favourable to younger and more cosmopolitan Japanese.

The main obstacle to Japan taking a leading role as international spokesperson has alway been its lack of leadership abilities. In recent years the country has also been dogged b political problems and has recently been preoccupied with recessionary economic trends Most of Japan's energies are being channelled into managing the economic crisis and it domestic political reforms, and this is at the cost of multidimensional global leadership.

Global Asia may yet revolve around ASEAN and not Japan. While Japan may provide th major market when it deregulates its economy, ASEAN leaders may yet forge th structures that will promote East Asia's interests globally. The following factors suppo ASEAN's leadership role in Global Asia (Selvarajah, 1994):

- A strong Western and Eastern orientation
- A multicultural population
- Open attitude to foreign investments and market entry
- More experience in dealing with other cultures internationally than Japan
- The advantage of relative neutrality in a region where age-old mistrust and sensitivitie exists - between Japan and China, between Japan and South East Asia and East Asi and between China and India
- The region's two most charismatic leaders - Malaysia's Prime Minister, Dr Mahathir Mohamad and Singapore's Senior Minister, Lee Kuan Yew.

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	August	September
Owing from previous month	30,000	60,000
Payment with 10%	9,000.00	18,000.00
Payment at net	20,000.00	40,000.00
Total disbursed 1st of month	29,000.00	58,000.00

	July	August
Owing from previous month	50,000	30,000
Total disbursed	45,000.00	27,000.00