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Globalisation and the Competitiveness of Regional Blocs

Both globalisation and regionalisation have gained momentum in the last two decades in every part of the world, involving economies at all levels of development. The following article examines the major determinants affecting the competitive position of selected regional blocs and suggests some policy stances which promise to support both further regional integration and improved competitiveness at a global level.

It is a widespread fashion these days to make globalisation either responsible for all types of national challenges[1] or to stress the opportunities arising from globalisation for exploiting significant welfare gains around the world.[2] In fact, as long as people have exchanged goods and services in different currencies, and factors of production have crossed national borders, has been there a process of internationalisation or globalisation. Indeed, on several economic measures – such as the share of foreign capital in domestic investment, cross-border flows of investment in relation to national output, flows of people in relation to population – the world was more closely integrated before 1914 than it is now.[3] The critical question is whether there is a new dimension in this process, quantitatively and/or qualitatively. A brief look at the statistics demonstrates that the speed of globalisation has indeed accelerated, already mobile factors of production (capital) have become even more mobile, and formerly rather immobile factors of production (services, labour) have become increasingly mobile. Private actors have become more and more the driving forces in this process, while at the same time it has become less and less controllable by national governments.

Mainly driven by progress in multilateral trade liberalisation efforts, which culminated in the successful completion of the Uruguay Round in December 1993, world trade growth doubled from 4 per cent per annum between 1980 and 1993 to 8 per cent 1994-96, outpacing world output growth by a widening margin.[4] Technological innovation, particularly in communication and information processing, has expanded the borders for tradable services significantly. Trade in commercial services grew at double the rate of merchandise trade between 1980 and 1997 (8.7 per cent versus 4.5 per cent). In 1995 it amounted to 23 per cent of total world trade.

Reductions in transport and communication costs (Table 1), capital account opening, financial market deregulation and privatisation of state enterprises have combined to create a favourable environment for increased capital mobility. From 1990 to 1995, borrowing on international capital markets rose by one-fourth, to US$ 1.3 trillion. Net resource flows from OECD to non-member countries amounted to US$ 252 billion in 1995, twice their 1990 level. The trend towards a dominant role for private flows has significantly accelerated in recent years. Their share in the total has risen from one-third in 1990 to two-thirds in 1995. Foreign direct investment represents more than half of private financing from OECD to non-member economies.

Taking into account that about 50 per cent of trade in goods and services is intra-firm trade and two-

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[1] Dani Rodrik: Has Globalization Gone Too Far?, Institute for International Economics, Washington D.C. 1997.

[2] See, for example, World Bank: Global Economic Prospects and the Developing Countries, Washington D.C. 1997.

[3] The Economist, September 20th, 1997.

[4] OECD: The World in 2020. Towards a Global Age, Paris 1997.

Abbreviations

APEC	Asia Pacific Economic Co-operation	NAFTA	North American Free Trade Area
ASEAN	Association of South-East Asian Nations	OECS	Organisation of Eastern Caribbean States
CACM	Central American Common Market	PTA	Preferential Trade Area for Eastern and Southern African States
CARICOM	Caribbean Community		
CEPGL	Economic Community of the Great Lakes Countries	SAARC	South Asian Association for Regional Co-operation
ECCAS	Economic Community of Central African States	SADC	Southern African Development Community
ECO	Economic Co-operation Organisation	UDEAC	Customs and Economic Union of Central Africa
ECOWAS	Economic Community of West African States	UDEAC	Central African Customs and Economic Union
EFTA	European Free Trade Association		
EU	European Union	UEMOA	West African Economic and Monetary Union
GCC	Gulf Co-operation Council		
LAIA	Latin American Integration Association	UMA	Arab Maghreb Union
MERCOSUR	Southern Common Market	UNCTAD	United Nations Conference on Trade and Development
MRU	Mano River Union		

thirds of international capital flows are managed by private actors it becomes evident that the private sector, in particular multinational firms and institutional investors, is the major player in this globalisation process.

The globalisation of markets mainly concerns the integration of product and capital markets.[5] Labour markets remain highly segmented by immigration policies and by language, cultural and other barriers to the international movement of labour. Although residents born abroad, as a share of total population, have been increasing in many advanced countries, their number is still below 5 per cent in most countries and exceeds 10 per cent in only four.[6] It does not appear that labour markets have become more integrated in recent decades.

Table 1
Transport and Communication Costs, 1920-1990
(in 1990 US dollars)

Year	Sea freight[1]	Air transport[2]	Telecommunication[3]
1920	95	n.a.	n.a.
1930	60	0.68	244.7
1940	63	0.46	180.5
1950	34	0.30	53.2
1960	27	0.24	45.9
1970	27	0.16	31.6
1980	24	0.10	4.8
1990	29	0.11	3.3

[1] Average ocean freight and port charges per short ton of import and export cargo.
[2] Average air transport per passenger mile.
[3] Cost of a 3 minute telephone call New York to London.
n.a. = not available.

Source: Georg Hufbauer: World Economic Integration: The Long View, in: Economic Insights, Vol. 30 (1991), pp. 26-27.

One measure of the extent of product market integration is provided by the ratio of trade to output. By this measure, product market integration has doubled since 1950 and has risen significantly in the past decade (Figure 1). This measure obviously understates the degree of integration because an increasing share of output in advanced countries consists of services, a large proportion of which are non-tradable.

Another way of assessing the degree of product market integration is to examine the extent to which prices for internationally traded products converge across countries. Empirical studies have consistently found large and persistent deviations from the law of one price for a wide range of traded goods, except for some highly homogeneous commodities, such as gold.[7] This may be attributed to various adjustment costs and trading frictions, including transportation

[5] Thomas Straubhaar: Standortbedingungen im globalen Wettbewerb, in: Reinhold Biskup (ed.): Globalisierung und Wettbewerb, Bonn 1996.

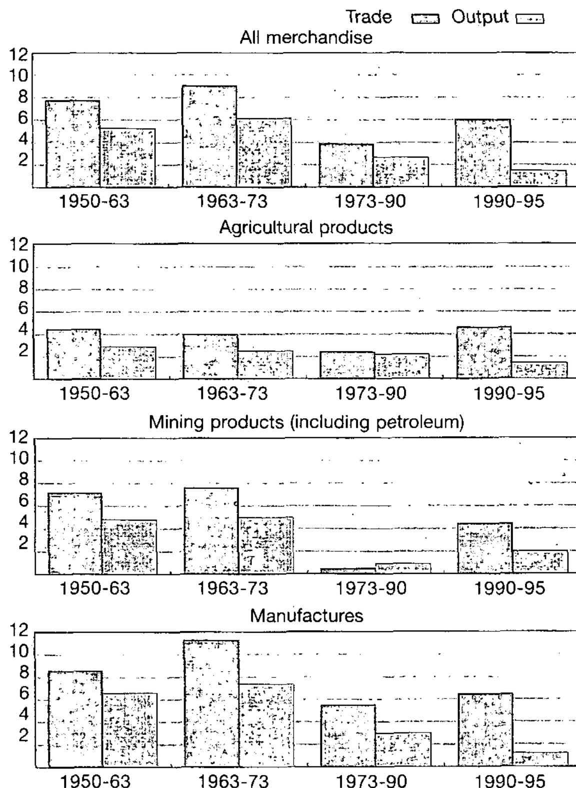
[6] IMF: Direction of Trade Statistics, Washington D.C. 1997.

costs, tariff and non-tariff barriers and transaction costs. Thus, even though international goods markets are becoming increasingly integrated they are clearly not yet as integrated as domestic goods markets.

Capital markets have also become more integrated especially over the past two decades. However, despite the phenomenal growth of cross-border flows and the rapid progress toward the integration of financial markets, financial globalisation seems to be confined to heavily traded, highly liquid financial assets, while countries' overall investment performance continues to be determined predominantly by their domestic savings rates rather than by net capital inflows. But the highly integrated segment of the capital market is large enough to exercise higher constraints than in the past on the conduct and effectiveness of macroeconomic policies.

In the past 30 years, and particularly since the mid-1980s, the environment for FDI and trade has changed significantly.[8] The most important changes relate to the reduction of technological and policy-related barriers to the movement of goods, services, capital, professional and skilled workers, and firms. More specifically, technological developments have greatly enhanced the ease with which goods, services, intangible assets and people can be transported, and tasks related to the organisation and management of firms implemented over distances. As a result, international production has grown substantially, as many firms have become transnational corporations. For example, the number of parent firms headquartered in major developed home countries nearly quadrupled between 1968/69 and 1993, from 7,000 to 27,000. Thus there is a substantial presence of foreign affiliates in the world economy today. The principal effect of the new environment is that firms are freer to choose how to serve foreign markets: by producing at home and exporting, by producing in a foreign country for local sale, or by producing in a foreign country for export. They also have greater freedom to obtain foreign resources and inputs for producing raw, intermediate or financial products for use elsewhere in national, regional or global markets.

Figure 1
World Merchandise Trade and Output by Major Product Group 1950-95
(average annual percentage change in volume terms)



Source: WTO: Annual Report 1996, Vol. II, Geneva 1996.

One important consequence of the rapid progress in globalisation is that margins of competitive advantages have become thinner: a small shift in costs somewhere can seriously affect a nation's competitiveness, which means that comparative advantage has become increasingly volatile.[9] This is partly reflected in industrial countries by increased pressures on the labour markets. In the USA the problem takes the form of poverty wages and in Europe of unemployment, in particular of unskilled workers. The underlying cause appears the same: the developing countries' comparative advantage in unskilled labour. The serious challenge for industrial countries is that globalisation is tending to reduce the capacity of the state when it comes to taxes and spending while at the same time it is enlarging the demands on the state when it comes to the labour market. This implies a big threat to national social consensus and income disparities within countries, a phenomenon which can be observed in both industrial and developing economies.

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[7] Kenneth Rogoff: The Purchasing Power Parity Puzzle, in: Journal of Economic Literature, Vol. 34 (1996), pp. 647-688.

[8] United Nations: World Investment Report 1996. Investment, Trade and International Policy Agreements, New York and Geneva 1996.

[9] Jagdish Bhagwati: The Global Age: From a Sceptical South to a Fearful North, in: The World Economy, Vol. 20 (1997), No. 3, pp. 259-283.

Trends in Regionalisation

Together with the acceleration of the process of globalisation regional trade agreements have gained momentum in the 1980s and 1990s in all parts of the world,[10] involving economies at all levels of development (Table 2). This means that the world has seen at least as much fracturing as merging. With the emergence of APEC, virtually all members of the World Trade Organisation (WTO) now participate in at least one agreement to advance regional trade liberalisation in goods and/or services. In the context of the newly established Committee on Regional Trade Agreements, the WTO Secretariat has identified 88 individual regional agreements currently in force.[11] These agreements and initiatives vary substantially in coverage, scope and completeness: the European Community, the only entity with a fully fledged single market and a supranational authority; MERCOSUR, the Andean Group and CARICOM designed as "classic" custom unions with a common external tariff; EFTA and NAFTA as free trade areas; APEC as an example of a looser association of trading partners with the long-term aim of free trade; the Free Trade Area of the Americas, a grand design but still only at a conceptual stage. Whether regional and multilateral trade liberalisation are compatible or whether there is the possibility of fragmentation of the international trading system through the development of different sets of rules is a question which causes concern. As regional trading arrangements (RTAs) have spread, enlarged and deepened over the last decade the discussion has intensified whether RTAs stimulate growth and investment, facilitate technology transfer, shift comparative advantage towards high value-added activities, provide credibility to reform programs, or induce political stability and co-operation. There is also the proposition that RTAs are a useful vehicle for countries to employ for improving their international competitiveness. In this context it is claimed that trading blocs can serve as a testing ground for eventual global integration as they allow firms to gradually develop internationalisation skills. This argument reminds one of the infant industry protectionist argument in which barriers are used to protect domestic industries until they develop the skills necessary to compete internationally: as history has proven, such policies have a fairly poor record.

Although conclusive evidence on the significance of trade diversion induced by regional integration schemes is almost impossible to produce, recent trends in intra-regional and extra-regional trade allow for some tentative conclusions on whether regional rather than global networking was the dominant feature in the world economy during the 1980s and early 1990s. It is not surprising that intra-regional trade linkages are clearly most developed in Europe, considering the EU's long tradition and advanced stage of economic integration.[12] More than two-thirds of total EU exports go to neighbouring countries (other EU Members, EFTA countries, and central and eastern Europe). However, the share of extra-regional exports has not declined further since 1980. The

Table 2
Intra-trade of Regional Arrangements, 1970-1993

Region	Intra-trade of group as percentage of total exports of each group			
	1970	1980	1990	1993
Developed and Developing Countries and Territories				
APEC	57.1	57.5	60.0	67.2
EFTA	18.1	14.7	13.5	11.4
EU (12)	53.2	55.7	60.6	56.0
EU (15)	59.5	61.0	66.0	61.2
NAFTA	36.0	33.6	41.4	45.4
Developing Countries				
America				
Andean Group	1.8	3.8	4.1	9.2
CACM	26.0	24.4	15.4	14.2
CARICOM	4.6	4.3	7.8	8.5
LAIA	9.9	13.7	10.8	15.9
MERCOSUR	9.4	11.6	8.9	17.5
OECS	-	19.7	8.2	9.4
Asia				
ASEAN	21.1	16.9	18.7	20.0
Bangkok Agreement	1.5	2.2	1.7	2.5
ECO	3.3	18.4	3.0	1.4
GCC	6.0	3.0	7.9	7.6
SAARC	4.6	5.0	3.0	3.5
Africa				
CEPGL	0.4	0.1	0.5	1.1
ECCAS	2.4	1.5	2.2	2.5
ECOWAS	3.0	10.2	7.9	8.6
MRU	0.2	0.8	0.1	0.0
PTA	9.6	12.1	7.6	7.0
SADC	5.2	5.1	5.2	5.1
UDEAC	4.9	1.8	2.3	2.3
UEMOA	6.4	9.9	12.0	10.4
UMA	1.4	0.3	2.8	3.2

Source: UNCTAD: Handbook of International Trade and Development Statistics 1994, New York and Geneva 1995.

[10] See, for example, Axel Borrmann, Bernhard Fischer et al.: Regionalismustendenzen im Welthandel. Erscheinungsformen, Ursachen und Bedeutung für Richtung und Struktur des internationalen Handels, Baden-Baden 1995.

[11] World Trade Organisation (WTO): Annual Report 1996, Vol. 2, Geneva 1996, Table III.2

[12] Peter Nunnenkamp: Winners and Losers in the Global Economy. Recent Trends in the International Division of Labour and Policy Challenges, Kiel Discussion Papers, No. 281, Kiel 1996.

process of completing the internal market had little impact on the relative importance of intra-EU trade until 1993. Intra-regional trade has traditionally been less significant for the United States than for Europe (even if US exports to Latin American countries are considered as part of regional trade relations). But there are nevertheless two important similarities: intra- and extra-regional trade increased at similar rates in 1980-93 and total US export growth was in line with world export growth. Most surprisingly, NAFTA has been estimated to have only marginal trade diversion effects on non-member countries in Latin America. Regional networking in Asia, which was mainly market-driven, in contrast to institutionalised regionalism elsewhere, is also highly unlikely to have retarded the globalisation of Asia's trade relations. There are also indications that the regionalism in ASEAN will continue to take the form of "open regionalism".[13]

There are at least two indications that the regional integration schemes in Latin America may be labelled open regionalism. First, when comparing the periods 1986-90 and 1991-95 changes in the growth rates of imports in Latin America have been less pronounced for intra-regional imports in Latin America than for their imports from the rest of the world (Table 3). For example, while growth of intra-regional imports in the MERCOSUR was 24.6 per cent in the period 1991-95 vis-à-vis 18.5 per cent in 1986-90, the growth rates of imports from the rest of the world were 19.7 per cent and 7.9 per cent respectively. Secondly, as MERCOSUR has demonstrated with its association agreement in the cases of Chile and, recently, Bolivia, the integration schemes offer access for potential new members. Evidence for the potential adverse effects of RTAs on members and on third countries was recently provided by a World Bank study for MERCOSUR,[14] but this analysis only captures static, and not dynamic, effects from integration. Although trade regimes may constitute an important element of a competitive strategy, in the following the focus will be placed on the meaning of competitiveness in a global context, and the extent to which it makes sense to speak of competitiveness among regional blocs will then be discussed.

Table 3
Growth of Intraregional Imports in Latin America, 1986-1995
(Growth rates of the import value in US$, c.i.f., per cent)

Regional Integration Schemes	1986-90		1991-95	
	Intra	RoW	Intra	RoW
MERCOSUR	18.5	7.9	24.6	19.7
Andean Community	9.8	34.6	2.7	16.0
CACM	3.0	5.7	20.8	15.6
CARICOM	6.7	0.4	6.2	6.3

RoW = Rest of the World.

Source: IMF: Direction of Trade Statistics, Washington D.C.

Competitiveness in a Global and Regional Context

The rapid process of globalisation and regionalisation of the world economy has serious consequences for our understanding of competitiveness. While competitiveness at the firm level is characterised by a firm's increased market share at the expense of others, competitiveness at the level of nations (and thus regions) has lost its significance with the increased mobility of factors of production. The competition is more and more among (increasingly less) immobile factors to attract internationally mobile resources from the global pool thus raising the incomes of complementary immobile factors within the borders.[15] However, Krugman's notion that "competitiveness is a meaningless word when applied to national economies"[16] is somewhat exaggerated, as competition between nations continues to matter because there are systemic differences in economic performance.[17]

Factors affecting domestic productivity gains are the rate at which capital is accumulated domestically, the rate at which human skills are acquired, and the efficiency of using physical and human capital in producing goods and services. However, competitiveness cannot be reduced to the mere notion of GDP growth and productivity. The success of firms also depends on other economic, institutional, political, socio-cultural, human and educational dimensions of a country. The International Management Forum

[13] Prema-Chandra Athukorala and Jayant Menon: AFTA and the Investment-Trade Nexus in ASEAN, in: The World Economy, Vol. 20 (1997), No. 2, pp. 159-174.

[14] Alexander Yeats: Does Mercosur's Trade Performance Raise Concerns about the Effects of Regional Trade Arrangements?, The World Bank, Policy Research Working Paper No. 1729, Washington D.C. 1997.

[15] Robert Findlay: The Philosophy of Locational Competition, in: Horst Siebert (ed.): Locational Competition in the World Economy, Tübingen 1995, pp. 1-25.

[16] Paul Krugmann: Competitiveness: A Dangerous Obsession, in: Foreign Affairs, Vol. 73 (1994), No. 2, pp. 28-45, here p. 44.

[17] Gary Hufbauer and Sherry Stephenson: Competitive Advantage in the World Economy, in: Horst Siebert (ed.), op.cit., pp. 45-63.

Davos[18] has identified the following national factors which are – according to economic theory and empirical evidence – conducive to the demonstrated social competitiveness of enterprises operating in a country:

☐ macroeconomic stability and predictable policies (domestic economy);

☐ the extent to which a country participates in international trade and investment flows (internationalisation);

☐ the extent to which government policies are conducive to competition (government);

☐ the performance of capital markets and quality of financial services (finance);

☐ the extent to which resources and systems are adequate to serve the basic needs of business (infrastructure);

☐ the extent to which enterprises are managed in an innovative, profitable and responsible manner (management);

☐ scientific and technological capacity, together with the success of basic and applied research (science and technology);

☐ the availability and qualifications of human resources (people).

Based on statistical indicators obtained from international and regional organisations, private institutions and national institutes as well as survey data compiled from an Executive Opinion Survey sent to executives world-wide to obtain their views on the present and future competitiveness of the country, the IMD has calculated a factor ranking and an overall ranking for 46 countries which assesses each country's competitiveness relative to its competitors.[19] A comparison of the relative ranking positions within factors of competitiveness for countries belonging to major regional integration schemes suggests that the countries belonging to a regional co-operation scheme are very heterogeneous with regard to their relative competitive position, which is not just a reflection of their different levels of development. Therefore it does not make much sense to compare the competitive positions of regional blocs as a whole. Comparing the relative competitive position of individual countries belonging, for example, to the EU or MERCOSUR respectively, the biggest competitive disadvantage of Brazil vis-à-vis Germany, for example, can be identified in internationalisation, science & technology, and infrastructure. A comparison between the USA and Germany reveals that Germany lags behind in particular in domestic economy, management, and government. Such isolated comparisons of factors of competitiveness can of course only provide a rough indication of relative competitive positions as the quality of interaction of these indicators also matters but is not easy to quantify.

Conclusions

The main challenge today for both industrial and developing countries is globalisation. The challenge of regionalisation, though significant, is subordinate to the challenge of globalisation. The importance of FDI and inter-firm tie-ups points to the importance of policies to attract such investment; but it also points to a danger of excessive competition among governments seeking to attract it.[20] There is therefore the *need for greater policy co-ordination among potential* competitors for foreign investment which in turn points out a possible role for enhanced regional or sub-regional integration both as a means of achieving such policy co-ordination and as a means of attracting FDI – the latter because of the greater steadiness and credibility which regionalisation can give to member governments' policies as well as the larger market it offers to investors. Another challenge is to resolve the problem of frequently weak price competition among firms in the domestic economy. The pursuing of de jure regionalisation, and/or policies conducive to greater de facto regional integration, can be a means to weaken the power of locally entrenched oligopolies, rent-seekers, and distributional cartels. Regionalisation can, at the same time, work to strengthen the effectiveness and credibility of the state and of economic policies in general, which are required for attaining political stability, macroeconomic stability, and investment growth. In particular, policy-makers in developing countries can thus reduce the risk of exclusion from the growth dynamics of globalisation.

Given the uncertain outcome of regional trade arrangements and given the need for improved international competitiveness due to ongoing globalisation

[18] IMD: The World Competitiveness Report, Lausanne 1997.

[19] For methodological details see Madeleine Linard de Guetechin: Methodology and Principles of Analysis, in: IMD: op.cit., pp. 42-49.

[20] Charles Oman: Globalization and Regionalization: The Challenge for Developing Countries, OECD Development Centre, Paris 1994.

it seems advisable to promote those policies at a national level which might help to enhance integration into both regional and world markets. Prominent candidates for such policies are the development of infrastructure at the national and regional level and human capital formation.[21] According to estimates by the World Bank[22] about US$ 60 billion would have to be invested in infrastructure up to the year 2000 to enable Latin America to continue its export-led growth strategy succcessfully. Presumably the greatest competition between nations, in terms of bidding for a larger share of mobile resources, occurs in the context of the competition among successful multinational enterprises for managerial and technological skills, including the competition for the talents of highly skilled professionals - academic researchers, engineers and other professionals.[23] Therefore human capital development should be a priority on the policy agenda. Finally, the enforcement of institutional competition could be a deliberate strategy in improving the competitiveness of economies.[24] Institutions are the constraints that human beings impose on human interaction including formal rules, informal constraints and enforcement characteristics.

Given the importance of FDI as a driving force of both regional and global integration there is an urgent need to ensure a fair international competitive environment, in particular with regard to foreign direct investment. Investment issues are currently the subject of discussion or negotiation in a number of regional fora. One important initiative was the launching, in May 1995, of negotiations aimed at the conclusion of a multilateral agreement on investment among the members of the OECD. The main aim of these negotiations is to eliminate discrimination between foreign and domestic investors. The agreement is intended to provide a broad framework for international investment, with high standards for the liberalisation of investment regimes and the protection of investment, and with effective dispute management. Other regional and international fora have already addressed investment issues, or are in the process of doing so, including APEC, ASEAN, SADC, NAFTA and MERCOSUR, as well as initiatives pursued in the context of the Free Trade Area.

Other proposals aim at the negotiation of multilateral rules on FDI in the framework of international organisations with global membership. In particular, the WTO has been mentioned as an appropriate forum for such negotiations since the intertwining of investment and trade requires a more integrated approach to international rule-working. The WTO already deals with certain aspects of investment issues in the context of the agreements on trade in services, trade-related investment measures and trade-related aspects of intellectual property rights. In perhaps one of its most important decisions, the WTO Singapore Conference in December, 1996, set up a working group to examine competition policies. Yet the big question is whether trade liberalisation and WTO discipline will be best served by adding to the trading system a global codex, harmonising national competition policies ex ante, or by mutually recognising well-functioning national competition policies. While sound economic arguments support the latter, prevailing country-of-destination principles conjure up concerns that the former will dictate the approach.[25]

The further development of regional and international rules on FDI needs to consider at least the following key issues:[26]

- investment measures that affect entry and operations by foreign investors, particularly relating to admission and establishment, ownership and control, operations, incentives and investment-related measures;
- application of certain standards of treatment, particularly national treatment, most-favoured-nation treatment, and fair and equitable treatment;
- measures dealing with broader concerns, including the proper functioning of the market, particularly related to restrictive business practices, transfer pricing, transfer of technology, employment, the environment, and illicit payments;
- investment protection and the settlement of disputes, relating to expropriations and property taking in general, abrogation of state contracts with investors, transfer of funds, and dispute settlements.

[21] Bernhard Fischer, Albrecht von Gleich and Wolf Grabendorff (eds.): Latin America's Competitive Position in the Enlarged European Market, Baden-Baden 1994.

[22] World Bank: World Development Report, Washington D.C. 1994.

[23] Gary Hufbauer and Sherry Stephenson, op.cit.; Stephane Garelli: What is World Competitiveness?, in: IMD, op. cit., pp. 6-7; and Stephane Garelli: The Fundamentals of World Competitiveness, in: IMD, op. cit., pp. 10-17.

[24] Douglass C. North: Institutional Competition, in: Horst Siebert, op. cit., pp. 27-44.

[25] Dean Spinanger: The WTO after the Singapore Ministerial: Much to Do about What?, Kiel Discussion Papers, No. 304, Kiel 1997.

[26] United Nations, op. cit.