11

The Regulation of South-South RTAs: An Analysis of AFTA and COMESA

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The recent rise in regional and bilateral preferential trade agreements (PTAs) highlights the need for further analysis of the "spaghetti bowl" of agreements and regulations that integrate global markets. This article gives specific attention to the regulation of South-South regional trade agreements (RTAs) and these agreements' capacity to generate new flows of intra-regional trade. The author uses an interdisciplinary approach to examine both the legal frameworks and economic impacts of different South-South RTAs. Case studies of AFTA and COMESA offer insight into the inadequacies of the multilateral trading system's current regulations, which promote trade in blocs of industrializing member-states. The article concludes with various recommendations to improve South-South RTAs' ability to foster intra-regional trade and encourage liberal trade practices between emerging market economies.

Introduction

Since the Doha Round of trade negotiations stalled, many states have neglected multilateral negotiations and refocused on regional and bilateral preferential trade agreements (PTAs) in order to further liberalize trade regimes beyond the World Trade Association (WTO) agreement.

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The current rise in regional and bilateral PTAs highlights the need for further analysis of the "spaghetti bowl" of agreements and regulations that integrate global markets. In particular, the ability of North-South trade relations to foster economic development and expand trade flows has been examined extensively. PTAs between developed countries are also being actively researched by academics, government officials and private firms. In contrast, growth in South-South PTAs has received much less attention. This article contends that South-South PTAs' smaller contributions to global trade flows should not diminish their significance in the progression of international trade liberalization. Increasingly, developing countries are liberalizing their economies in order to offer a larger and stronger market to foreign investors. Examining the progress of these regions' trade arrangements can inform present liberal trade strategies related to emerging markets.

To conduct this examination, the following question is proposed: How do trade regulations respond to the development of emerging markets in the global economy, and how does this response affect developing states in the international community? This article argues that trade regulations respond to the development of emerging markets by offering weak legal frameworks to South-South regional trade agreements (RTAs) that are not enforced or applied. This response has limited intra-regional trade between developing states. In support of this argument, this article will offer a case study comparison and analysis of AFTA (the Free Trade Area of ASEAN, the Association of Southeast Asian Nations) and COMESA (the Common Market for Eastern and Southern Africa). AFTA and COMESA both include a mixture of least-developed countries (LDCs) and developed member-states. Thus, case studies of these two agreements will allow for a comprehensive evaluation of intra-regional trade between markets at various levels of development. In addition, an analysis of these agreements' legal frameworks—followed by an evaluation of their economic impact—will demonstrate the inadequacy of trade regulations in the multilateral trading system's development agenda. To complement the case study comparison, this article also includes a general discussion of trade regulation and economic impacts regarding all South-South trade. The economic impact of free trade agreements will be investigated through an analysis of trade flows, trade creation and trade diversion.

This article will not attempt to evaluate whether free trade is an appropriate mechanism for development. Much literature has been written on this topic and opposing camps continually shore up new evidence to support their positions. Instead, it considers the ability of multilateral trade

regulations to foster strong international trade regimes between developing member-states. If the WTO promotes a trade development agenda, it is important to examine whether it has encouraged trade in developing countries by means of multilateral legal frameworks, or whether its attempts to cultivate intra-regional trade have proven largely inadequate.

The Regulation of South-South RTAS

Under the multilateral trading system, there are diverse positions regarding the ability of regional agreements to further trade liberalization. In practice, opponents to RTAs have largely lost out against the promoters of regional integration. A legal framework has been established for the creation of RTAs under the General Agreement on Tariffs and Trade (GATT). Specifically, there are several levels at which RTAs and the multilateral trading systems cross paths. Firstly, the multilateral trading system establishes the margin of preference for the most-favored nation (MFN) market access of South-South RTAs and provides a negotiation framework that determines the conduct of developing members' trade policy. Secondly, the "Enabling Clause" of the GATT, negotiated in the Tokyo Round, provides the legal backing for the creation of South-South RTAs (Davidson 2005, 11). The waiver states:

> 1. Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favorable treatment to developing countries, without according such treatment to other contracting parties.
>
> 2. The provisions of paragraph 1 apply to the following:
> ...(c) Regional or global arrangements entered into amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the CONTRACTING PARTIES, for the mutual reduction or elimination of non-tariff measures, on products imported from one another (Davidson 2005, 11).

Article I, paragraph 2c is established only for the benefit of global and regional agreements between less-developed countries. According to this clause and Article V of the General Agreement on Trade in Services (GATS), developing countries face less stringent requirements than those governing developed countries in Article XXIV of GATT. In effect, South-South RTAs under the Enabling Clause (including COMESA and AFTA) are not obligated to cover "substantially all trade," do not have a specific time

frame for implementation, do not have to eliminate all duties, and are not subject to periodic examinations (Esteevadeordal 2004, 22). South-South RTAs are only required to notify the WTO Committee on Trade and Development when they have been implemented, provide the WTO with full access to information if a mutual change of preferences occurs, and allow for WTO consultation regarding problematic issues (Esteevadeordal 2004, 39). These provisions have remained unchanged since their formulation. Only recently has the Enabling Clause been considered renegotiable, as a result of the growing discussion regarding the provisions' effectiveness in creating trade.

The Enabling Clause Today

Presently, developing countries have avoided making the Enabling Clause a topical issue on the Doha Development Agenda (DDA). In the Doha Round of negotiations, the African, Caribbean and Pacific (ACP) Group of States proposed that special and differential treatment (SDT) be included as a waiver to Article XXIV, but the group has urged that the Enabling Clause remain untouched in the DDA (Crawford 2005, 26). Adding SDT under Article XXIV is argued to be a key way for South-South RTA member-states to influence the WTO to adopt their development concerns (Crawford 2005, 27). According to some developed countries, however, further concessions under Article XXIV for developing countries are not necessarily the best way to foster trade creation. For example, the Enabling Clause has allowed South-South RTAs, such as COMESA and AFTA, to lower barriers to trade in an unsystematic and delayed fashion.

In contrast to the stance of developing countries and the ACP, the European Community (EC) and Australia have proposed a re-evaluation of the Enabling Clause. An EC submission to the WTO emphasizes that South-South RTAs should deepen their economic integration agreements (Onguglo 2005, 23). To encourage better integration, the EC recommends realigning the substantive commitments in the Enabling Clause with the obligations stated in Article XXIV (Onguglo 2005, 23). This demonstrates that even though the ACP regards the Enabling Clause as an *acquis* to the WTO, the EC clearly views the waiver as open to review and modification (Onguglo 2005, 23). The EC believes alterations to the waiver are long overdue because most South-South RTAs have only partially liberalized under current regulations (Onguglo 2005, 23). Modifying the Enabling Clause could pressure South-South RTAs to continue liberalization at a more regimented pace.

In addition to the above matter, the EC is concerned with the fairness

of the Enabling Clause between developing countries (Onguglo 2005, 26). EC member-states question whether large South-South RTAs should be grouped with RTAs that do not represent a substantial amount of world trade. Should smaller South-South RTAs be subject to the same trade regulations as larger RTAs that trade massive amounts of goods with developed countries? In response to this question, the EC has recommended equal treatment between developed country RTAs and South-South RTAs with large external trade flows (Onguglo 2005, 26).

Overall, the EC is concerned with differential treatment under the Enabling Clause. Given what it views as unnecessarily lax regulations for South-South RTAs and a lack of distinction between fundamentally different South-South RTAs, the EC suggests that change is needed. At the very least, the EC and Australia are willing to put the waiver issue up for debate. This may lead to modifications that could improve the enforcement and application of multilateral trade regulations. To date, the current level of enforcement has not induced South-South RTAs to develop legitimate legal frameworks that compel member-states to consistently lower barriers to intra-regional trade. An analysis of AFTA's and COMESA's legal frameworks displays this trend.

AFTA'S Legal Framework

The WTO was notified of AFTA under the Enabling Clause. Therefore, it is not mandatory that AFTA member-states follow all of the standards outlined in Article XXIV. Particularly, tariffs in the region do not have to focus substantially on all trade within a specific time frame, and each member-state may assign its own preferential tariffs to various product lines (Baldwin 2003, 9). Moreover, there is presently no mechanism within the WTO to enforce a systematic lowering of AFTA's tariffs. As a consequence, protectionist domestic actors within AFTA member-states can encourage neglect of a structured schedule of trade barrier reductions. The political economy of the region, not unlike other regions with RTAs, is rooted in national politics. Thus, member-state governments not bound by strict multilateral obligations may succumb to pressures from local producers opposed to South-South trade liberalization; these producers wish to promote their less competitive domestic industries.

Since the WTO provides loose regulations for South-South RTAs, the unsubstantial legal framework of AFTA itself is also allowed. For example, nowhere in the AFTA framework is there a provision for national treatment (Hafez 2004, 210). National treatment is an essential requirement of FTAs under Article XXIV of the GATT because it insures that regula-

tory procedures and internal taxes are not levied as protectionist measures (Hafez 2004, 211). Some countries within AFTA are also members of the WTO and therefore can apply Article III of the GATT (Hafez 2004, 211). However, several member-states of AFTA are not members of the WTO and thus have no obligation to apply national treatment to regional trading partners (Hafez 2004, 211). These countries—namely Cambodia, Laos, and Vietnam—are not restricted under any international trade laws from applying domestic tax and regulatory policies for protectionist purposes (Hafez 2004, 211). Therefore, AFTA does not provide uniform conditions for imported goods that must compete with similar domestic products (Hafez 2004, 211). This absence of a legal infrastructure for non-WTO members increases the potential for internal barriers to trade, weakens the free flow of intra-regional trade within AFTA, and thus allows protectionist measures to outweigh fundamental principles of free trade agreements.

Article 9 of the CEPT-AFTA Agreement is another legality that can serve protectionist purposes. Under Article 9, member-states are able to implement regulations for the protection of public morals, national security, human, animal or plant life, or health (Hafez 2004, 213). These exceptions are similar to those outlined in Article XX of the GATT and several exceptions in the Sanitary and Phytosanitary Measures (SPS). Yet, national treatment under the WTO can counter any protectionist manipulations of WTO exceptions. In contrast, since national treatment is not an obligation for several CEPT-AFTA signatories, the potential for abuse of Article 9 is enhanced by AFTA's weak legal framework. The WTO does not stipulate that WTO members in South-South RTAs must impose GATT rules on non-member states. This lack of enforcement and direction by the WTO permits South-South RTAs to construct incomplete legal frameworks that permit barriers to intra-regional trade.

Another flaw of the CEPT-AFTA Agreement, which persists under multilateral regulations, is its poor enforcement of non-tariff barrier (NTB) reductions. This is a key defect of the legal framework because removing tariffs can encourage the free flow of goods only to the extent that NTBs are limited. Article 5 obligates member-states to gradually remove NTBs and quantitative restrictions (Hafez 2004, 213). However, Article 5 has not been implemented with much success. A 1999 survey of private firms in ASEAN, conducted by the ASEAN Secretariat, concluded that several types of NTBs still exist in the region (e.g. length procedures for import licenses, non-publicized frequent regulatory changes, inconsistent customs valuation, quota restrictions and privileges provided to selected compa-

nies) (Hafez 2004, 215). With a stronger legal framework, the proper enforcement of Article 5 could eliminate many of these NTBs. However, the WTO has not provided AFTA with the legal fortitude necessary to remove NTBs. The current moderate GATT requirements for South-South RTAs allow member-states to succumb to domestic political pressures that support enacting NTBs.

South-South RTA regulations under the GATT have also failed to include a strict provision concerning transparency. Nontransparent regulation of trade in South-South RTAs encourages deceptive practices, which eventually restrict flows of intra-regional trade and deters foreign direct investment (FDI). The WTO maintains its transparency through various provisions, but does not require South-South RTAs to follow suit. For example, AFTA's transparency, when compared to that of the WTO, has not been properly established. Under Article X of the GATT, regulations must be made readily available to traders and laws must be uniformly administered (Hafez 2004, 217). AFTA does not have an article outlining practices for publishing and administering laws (Hafez 2004, 217). This disregard for transparent regulation has led to the development of bureaucratic red tape, heightened corruption, and discouraged investors (Hafez 2004, 218). Unfortunately, flows of both intra-regional trade and foreign investment rely on the efficiency and reliability afforded by transparent regulation. For potential investors, AFTA's exclusion of rules on transparency limits the credibility of its mandate (Hafez 2004, 218). Thus, AFTA's underdeveloped legal infrastructure for trade regulations hinders its ability to achieve its goals of attracting FDI (Kaplan 1995, 148) and reducing barriers to intra-regional trade.

Clearly, barriers to trade have not been steadily removed through the unstructured, less transparent and more personalized "ASEAN way" of conducting negotiations (Davidson 1996, 596). Consistent tariff-reduction and the uniform removal of barriers to trade have also been constrained by AFTA's haphazard method of resolving disputes between member-states. Since its inception, ASEAN has been unable to develop an apolitical dispute settlement mechanism to enforce specific schedules of trade liberalization or restrict the creation of barriers to trade. A supra-national law-making or decision-making organ that could implement AFTA protocols, solve disputes, and implement community law could limit the hesitancy of individual countries to abide by the terms of agreements (Tan 2004, 949). To create such an enforcement body, ASEAN would have to overcome the past unwillingness of its member countries to form community law for the region (Tan 2004, 952). Moreover, international lawmakers would have to

deal with the region's immense diversity of legal systems. Civil law, common law, and hybrids of both are found in the region (Tan 2004, 952).

It would be a challenge for AFTA members to establish a strong legal framework to support their agreement. The current Protocol of Dispute Settlement Mechanism is highly politicized. Under the protocol, parties in a dispute face a diplomatic-political body called the ASEAN Senior Economic Officials Meeting, which has the final decision in any AFTA dispute (Hafez 2004, 240). This body does not represent diverse legal traditions and appears to focus on domestic political concerns instead of making consistent supra-national decisions. These politicized facets of dispute resolution have developed because the multilateral trading system has not made dispute settlement an imperative element in the South-South integrative processes. The WTO does not provide South-South RTAs with stipulations requiring dispute settlements or a working supra-national legal system which could enforce tariff reductions.

A legal framework with a dispute settlement body is also effective for continued integration. As AFTA pursues further integration, the absence of a dispute settlement mechanism could limit the transparency of the integration process and exacerbate domestic political insecurities. Most recently, ASEAN has proposed a European-style single market by 2015 (Lingga 2006). A notable characteristic of the EC is their well-established legal framework. The WTO could encourage South-South integration projects, such as AFTA's single market, by promoting strong legal frameworks. These frameworks could include schedules of tariff reductions enforced by dispute settlement bodies within South-South trading blocs or through the WTO.

In the future, AFTA's integration process may be challenged by the Enabling Clause's inability to manage contemporary aspects of South-South RTAs. Currently, the Enabling Clause only sanctions unregimented schedules of tariff reductions for developing countries. However, several ASEAN member-states have approached or are approaching a stage of economic development which is above the level of a "newly industrializing country." The WTO has never obligated developed countries in ASEAN to graduate from their initial status under the Enabling Clause (Davidson 1993, 598). Yet countries who are developed and not part of AFTA must accept the MFN obligations under GATT 1994 in full. For example, Singapore, as a developed member of AFTA, does have to award MFN treatment. This poses the question: Is the AFTA scheme compatible with the GATT obligations for all parties? The provisions of the Enabling Clause are only available to global or regional arrangements "entered into amongst less-developed

contraction parties" (Davidson 1993, 607). Certainly, developed countries can award preferential treatment to goods from developing countries, but the reverse is not permissible (Davidson 1993, 607). Therefore, one can reason that Singapore should not be permitted to be a member of AFTA under the Enabling Clause (Davidson 1993, 607).

If AFTA is to continue under GATT rulings, the WTO will have to consider how to transfer Singapore out of the agreement without harming the level of trade that has been achieved thus far. Currently, AFTA is stalling on the issue of further liberalization. Thus, Singapore has opted to move beyond AFTA and engage in multiple bilateral agreements (Hafez 2004, 603). The WTO's inability to offer a proper mode of transition for Singapore could cost AFTA its most developed member-state. As Singapore pursues trade policies suited for small open state bilateralism, ethnically diverse and complex ASEAN economies could be left to establish more South-South integration without Singapore as a flagship (Low 2004, 15).

The WTO's unclear requirements for South-South RTAs jeopardize AFTA's leadership, institutions, dispute settlement mechanisms, transparency and ability to reduce NTBs. Combined, these characteristics create a restrictive trading environment in which intra-regional trade is limited. However, AFTA is not the only region with a flawed legal framework. An examination of COMESA's legal framework points out similar problems.

COMESA'S Legal Framework

In order for COMESA to operate as envisioned, it requires a well functioning legal framework. Unfortunately, COMESA has to integrate a conflicting mixture of legal traditions and contend with a political culture that favors municipal law (Kiplagat 1994, 284). Not unlike AFTA, several legal systems are found within the member-states of the region—including civil law, Anglo-Dutch, common law, Amharic Law and Islamic law. In addition, the linguistic diversity between these systems complicates the creation of a well-functioning legal framework for the region (Kiplagat 1994, 284). A stable and credible legal structure for COMESA also depends on the willingness of domestic political actors to grant power to regional institutions so that municipal law does not interfere with regional law (Kiplagat 1994, 286).

To construct a legal framework that facilitates international trade and avoids the complexities of domestic legal systems, COMESA has developed a legal architecture mirroring the WTO. For example, the COMESA Treaty is based upon two key principles underlined in the GATT (Oduor 2005, 192). Article 57 highlights the principle of non-discrimination and

Article 56(1) of the COMESA treaty outlines MFN treatment (Oduor 2005, 192). Similar to GATT Articles I and III, Article 57 states that the members of COMESA must "refrain from enacting legislation or applying administrative measures which directly or indirectly discriminate against the same or like products of member-states" (Oduor 2005, 192). Moreover, Article 56(1) typifies GATT language by requiring member-states to "accord one another the most favored nation treatment" (Oduor 2005, 192). This language demonstrates that COMESA has chosen to reproduce key content from the WTO's legal framework for trade in goods.

However, COMESA's replication of the WTO's legal framework has not ensured a steady reduction of barriers to trade and the continuous liberalization of its trade regime. For instance, WTO-type provisions on subsidies, anti-dumping and countervailing duties have not been supported with the proper enforcement (Oduor 2005, 193). The WTO has demonstrated that a legitimate dispute settlement body is an effective way of enforcing trade regulations. COMESA offers a dispute settlement mechanism designed to gain domestic political approval by granting non-state and private actors procedural and substantive rights (Oduor 2005, 202). This mechanism has yet to effectively enforce the various WTO-style obligations in the COMESA treaty.

COMESA does not have to provide a legitimate mechanism to solve disputes among member-states on its own. WTO jurisprudence under Article XXIV (e.g. the Turkey Textiles Case) conveys that the WTO is capable of intervening in disputes involving RTAs (Oduor 2005, 206). However, in the case of South-South RTAs such as COMESA, the WTO has not made key interventions in such disputes. As developing states liberalize their trade regimes and overcome domestic political influence, they must be supported by legitimate regional laws and regulatory bodies. Current multilateral regulations of South-South RTAs have not made these institutions and laws an imperative aspect of FTAs under the GATT.

Legal Framworks' Ability to Meet FTA Requirements

Both AFTA and COMESA are exempt from many Article XXIV obligations under the Enabling Clause. However, it is still important to discern whether they could conform to requirements currently faced by developed countries, given that industrialized countries have suggested aligning the Enabling Clause with North-North FTA obligations. Moreover, examining these RTAs' ability to meet the same requirements faced by North-North RTAs is another way to conceptualize AFTA and COMESA's levels of integration. The following examination

will demonstrate that AFTA and COMESA have not integrated sufficiently to comply with WTO standards. However, this article will also demonstrate that the WTO does not adequately enforce its standards, thus permitting RTAs to limit flows to intra-regional trade.

Article XXIV of the GATT stipulates RTA requirements, but much of the article has not been defined. Consequently, little is known about the precise requirements for WTO-approved FTAs. Future interpretations of Article XXIV may stipulate that COMESA and AFTA do not meet all the conditions for FTAs. This uncertainty further demonstrates the WTO's inability to offer enforceable trade regulations for RTAs. A lack of evaluation and enforcement allows protectionist measures to embed themselves within South-South RTAs, thus preventing trade creation within the multilateral system.

It should also be noted that many other RTAs, both North-North and North-South, are arguably infringing upon future interpretations of Article XXIV. For example, the Appellate body decision on the *Turkey-Textiles* case notes that:

> [N]either the GATT Contracting Parties nor the WTO Members have ever reached an agreement on the interpretation of the term 'substantially' in this provision. It is clear, though, that 'substantially all the trade' is not the same as *all* the trade, and also that 'substantially all the trade' is something considerably more than merely *some* of the trade (Anonymous WTO Analytical Index).

The Appellate body explains that the WTO has not identified the extent to which customs unions must liberalize their trade regime under Article XXIV, paragraph 8(a). Thus, one can conclude that a future WTO panel will have to decide the meaning of "substantially all trade" in paragraph 8(b), which points out the degree to which FTAs must reduce barriers to trade (Mathis 2002, 217). Should a panel judge "substantially all trade" in an FTA to mean a high percentage of liberalization, many RTAs—both North-North and South-South—could be in jeopardy of violating Article XXIV.

In addition to the ill-explained paragraph 8(b), AFTA and COMESA could also be in violation of Article XXIV, paragraph 5(c). The obligation on schedules of integration states:

> [A]ny interim agreement referred to in subparagraphs (*a*) and (*b*) shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time (Anonymous WTO Analytical Index).

AFTA and COMESA both have outlined timelines for their trade liberalization process, but delays have occurred in the implementation of agreements. Consequently, extensions are frequently granted for stages of liberalization. Paragraph 5 maintains that FTAs must be formed within a "reasonable length of time." If the WTO were to outline definite schedules of integration, South-South RTAs such as AFTA and COMESA would likely struggle to meet specific WTO deadlines.

While COMESA and AFTA may be deemed inconsistent with Article XXIV at a future date, there are other obligations that both agreements have fulfilled. Paragraph 5(b) of the article states:

> [W]ith respect to a free-trade area, or an interim agreement leading to the formation of a free-trade area, the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement *shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area, or interim agreement as the case may be* (Anonymous WTO Analytical Index).

Duties and tariffs have been lowered to some degree in several sectors of AFTA and COMESA. While their level of integration may not cover substantially all trade, neither agreement was created to increase barriers to trade between member-states. Paragraph 7(a) is another provision that both RTAs have followed. It states:

> [A]ny contracting party deciding to enter into a customs union or free-trade area, or an interim agreement leading to the formation of such a union or area, *shall promptly notify the contracting parties and shall make available to them such information regarding the proposed union or area as will enable them to make such reports and recommendations to contracting parties as they may deem appropriate (Anonymous WTO Analytical Index).*

COMESA and AFTA have notified the WTO of their existence under the Enabling Clause, but no formal evaluation of the RTAs has been conducted by the WTO. Most major RTAs have been notified to the WTO under Article XXIV or the Enabling Clause. However, none has been examined for conformity by the Committee on Regional Trade Agree-

ments (Lamy 2002, 1411) or the Committee on Trade and Development. This inadequate review and regulation of trade policy allows developing countries to establish RTAs, but these RTAs only generate limited levels of intra-regional trade and economic integration.

Economic Analysis

An economic analysis of South-South RTAs demonstrates these agreements' insubstantial levels of intra-regional trade. The case studies of COMESA and AFTA display this trend well. Both regions defend the economic theory behind RTAs in their agreements, but insufficient enforcement of these RTAs' regulations has rendered their economic rationales irrelevant.

Economic Rationale and Theory

It is well-recognized in economic literature that dynamic and static gains can be made from regional integration (Esteevadeordal 2004, 5). Trade theory contends that under perfect competition, a simple "partial equilibrium model" can increase trade between members of a regional agreement by forcing the least efficient producers out of the market. If domestic producers' competitiveness increases, there is an opportunity to create trade. However, if foreign producers are damaged by a South-South PTA, costly trade diversion can occur (Esteevadeordal 2004, 5). Therefore, welfare can grow only if trade creation is larger than trade diversion (Esteevadeordal 2004, 5). Many developing countries have joined RTAs to generate the potential gains from establishing a market of increased scale and competitiveness (Esteevadeordal 2004, 5).

Economic Gains from South-South Trade

Some data have indicated that worldwide South-South trade agreements have the capacity to accelerate developing countries into prominent positions within the global economy (Esteevadeordal 2004, 16). Today, 42 percent of developing countries' exports come from integrated South-South trade blocs (Esteevadeordal 2004, 16). South-South trade in the world economy has almost doubled in the last decade (Esteevadeordal 2004, 16). This is in part a result of export expansion in new sectors such as telemarketing services (Esteevadeordal 2004, 17). However, the doubling effect is more likely attributable to the rise of large liberalizing markets in East Asia such as China (Trade and Development Report 2005, 6). Trade growth has not been as substantial in other South-South RTAs such as COMESA and AFTA.

Economic Gains from South-South Trade in AFTA

AFTA has been in place for thirteen years and has failed to produce significant levels of intra-regional trade (Baldwin 2006, 4). Any gains that have occurred have been momentary and have been offset by periods of declining trade flows (*The Economist* 2004, 35). Between 1995 and 2001, intra-AFTA merchandise exports declined from 25.4 percent to 23.3 percent of total exports (Hafez 2004, 208). The protracted flows of intra-regional trade can be attributed to AFTA's high administrative costs and tariffs.

AFTA's administrative costs derive from several inefficiencies. The trade agreement continues to have costly rules of origin (ROOs), which can be considered disproportionately high in comparison to the gap between preferential Common Effective Preferential Tariff (CEPT) and MFN tariffs rates (Tumbarello 2006, 12). In addition, procedural red tape, inconsistent product standards between countries and non-tariff barriers (e.g. stringent quality and performance standards and complex inspections procedures) have all limited intra-regional trade to less than 35 percent of total foreign trade (Nesadurai 2003, 71).

AFTA's low levels of intra-regional trade also result from tariffs in key sectors. These tariffs are the result of member-states' lackluster commitment to the agreement's common tariff structure. The CEPT is continually abused in prominent sectors because individual member-states can develop their own product category lists for preferential treatment (Tan 2004, 941). For instance, Malaysia did not comply with AFTA on automobile tariffs until 2006. Although Malaysia has finally cut auto import tariffs to 5 percent, it imposed another barrier to trade by forcing car manufacturers to register for government approval (Theparat 2006). This demonstrates the reluctance of AFTA member-states to further trade liberalization within their South-South RTA.

One should also note that much of the tariff reduction that has occurred in ASEAN has not been the result of AFTA. The CEPT, an indicator of tariff rates within the region, has not been substantially reduced when compared with the MFN rate established at the multilateral level. In the mid-1990s, only 1.5 percent of intra-ASEAN trade utilized CEPT rules of origin certification (Nesadurai 2003, 68). During this period of liberalization, domestic manufacturers had little incentive to apply for concessions under CEPT because the MFN rate was comparable to AFTA's preferential tariff rate (Nesadurai 2003, 68). By 2001, there was still a lack of reliance on the CEPT. Eighty-three percent of tariff lines in Indonesia were based upon MFN rates (Nesadurai 2003, 69). Sixty-three percent of tariff lines in the Philippines and 69 percent of Malaysian tariff

lines followed MFN rates (Nesadurai 2003, 69). These data demonstrate ASEAN's reliance on tariffs established at the multilateral level of trade regulation. It is therefore questionable whether permitting South-South RTAs under the Enabling Clause truly fosters an ASEAN free trade area. AFTA maintains substantial barriers to trade and relies heavily on MFN rates to liberalize its trade in goods.

Those defending AFTA's poor intra-regional trade creation could argue that the region has, at the very least, formed a cohesive trading bloc capable of increasing exports. Although this may eventually occur, achieving higher foreign exports is not part of the short-term or mid-term economic rationale behind creating RTAs (Hafez 2004, 209). Moreover, from 1995 to 2001 the implementation of AFTA did not increase the region's world merchandise exports (Hafez 2004, 209). Therefore, global trade creation under AFTA is not an excuse for its inability to generate trade between member-states.

Economic Gains from South-South trade in COMESA

Since 1994, COMESA has integrated in stages. The first stage, which occurred prior to 1994, entailed the creation of a preferential trade area in which member-states awarded one another privileged treatment when trading specific goods (Trivedi 2006, 63-64). Then in 2000, COMESA implemented an FTA that forced imports from third countries to be exempt from tariff and non-tariff barriers (Trivedi 2006, 63-64). This agreement is still in place today. The next stage for COMESA is the creation of a customs union with a four-band common external tariff (CET) structure of 0-5 to 25-30 percentage points on capital goods, raw materials, intermediate goods and finished products (Trivedi 2006, 63-64). In 2008, countries that are prepared to enter into the customs union will proceed with implementation of the CET (Otieno 2006).

The latest reports on trade within COMESA have been optimistic. Total trade in 2005 was U.S.$87.7 billion and agricultural trade has significantly increased over the past seven years (Latest Report 2006). Combined trade and cross-border investment flows in COMESA have grown by U.S.$7.5 billion since 2000 (Karugaba 2006). However, when compared to long-term reports, these figures are less than promising. Long-term trends have not shown RTAs in Africa to have any effect on intra-regional trade growth (Yang 2005, 14). There are still many barriers to trade within COMESA capable of restricting the formation of new intra-regional trade flows. For example, restrictive ROOs remain in place and external barriers to trade are relatively high (Yang 2005, 10-12). When evaluating COMESA's

economic performance, one must take these restrictive policies into account. A political economy perspective focuses on protectionist practices and helps to explain COMESA's inability to foster lasting increases in intra-regional trade.

Political Economy of COMESA

Member-states of COMESA claim to subscribe to the aforementioned economic theory that regional integration can improve efficiency, stimulate economic activity, and generate healthy competition, which in turn creates jobs and attracts investment (Trivedi 2006, 64). However, member-states' commitment to implementation has been limited by interventionist measures. COMESA maintains that member-states must eliminate non-tariff barriers in order to proceed with the liberalization of trade within the region. Yet import bans, roadblocks, administrative charges and quantitative restrictions still exist (Yang 2005, 10). These barriers to trade operate as regional import substitution policy, reducing incentives to exporters and local industries (Yang 2005, 17).

Comparison of Economic Gains

The above description demonstrates that although some integration has been achieved, several external trade barriers still exist between member-states of AFTA and COMESA. AFTA may have fewer barriers than COMESA, but both have limited levels of intra-regional trade. In 2004, the applied MFN tariff rate in developing countries of Asia-Pacific on average was 12.1 percent (Yang 2005, 12). In COMESA, the average rate was 18.5 percent (Yang 2005, 12). In contrast, industrialized countries maintained an average tariff rate of 5.7 percent (Yang 2005, 12). This demonstrates that neither AFTA nor COMESA has achieved relatively low tariff rates between member-states.

Recommendations

AFTA and COMESA have both been neglected by the multilateral trading system. Each region has been allowed to develop non-comprehensive trading regimes that rely on underdeveloped legal frameworks and lack binding schedules. Without a consistent schedule and definite rules, neither region has been able to generate substantial flows of intra-regional trade. If the WTO is intent on using a development strategy that employs trade as a mechanism for promoting economic growth among developing member-states, there are several areas upon which it must improve.

First, the WTO should consider strengthening the interpretation of Article

XXIV or the Enabling Clause. The enforcement of regulations for South-South RTAs would be more effective if concrete regulations were outlined. The Enabling Clause was meant to allow developing members to form FTAs with reduced requirements. However, fewer obligations have resulted in less structure and insufficient scheduling of tariff reductions. To ensure that barriers to trade are removed on a consistent basis, the WTO should clearly define the phrase "substantially all trade" for South-South FTAs. Defining this axiom, either under a new Enabling Clause or under Article XXIV, would allow rule violations to be identified, judged, and limited through enforcement mechanisms. One may argue that "substantially all trade" has been left undefined to allow for flexibility in the negotiation of tariff lines. That is why the Appellate Body ruled that substantially all trade did not indicate *all* trade in the *Turkey-Textiles* dispute (Anonymous WTO Analytical Index). However, the Body also noted that the clause indicates substantially more than *some* trade (Anonymous WTO Analytical Index). AFTA and COMESA can trade beyond *some* amount of intraregional trade if multilateral regulations insist upon it.

In addition to the expression in Article XXIV, paragraph 8(b), the WTO should describe what constitutes a "reasonable length of time" for South-South RTA formations in order to guarantee an unvaried schedule of tariff harmonization. Generous but well-defined schedules could provide a means for the multilateral trading system to regulate the integration of South-South RTAs. Combined, these precise explanations of what the WTO considers sufficient and steady liberalization could prevent barriers to trade between developing member-states.

Secondly, the WTO must derive a strict criterion for determining whether a member is eligible for developing country treatment. As noted, Singapore is not at the same level of industrialization as other AFTA member-states. Singapore has the ability to provide leadership and diversification in the region, but is arguably an illegitimate member of AFTA. A justifiable method of preserving region leaders such as Singapore would be to permit their inclusion under the Enabling Clause. To limit the benefits that North-South RTAs could obtain from this provision, RTAs registered under the Enabling Clause would have to be examined to ensure that new entries do not include developed member-states. For example, a Western state should be prevented from designating itself as the leading member of a South-South RTA in Asia. One may counter this recommendation by asserting that once a country reaches a certain level of economic development, it should no longer receive preferential access to regional markets. Instead, it should renegotiate trade regulations under a framework similar to a North-South RTA negotiated between non-regional parties. Yet this burden of rewriting rules and breaking up regional trade to uphold fair market access could serve as a disincentive to achieving regional economic growth, and could further

complicate regulatory frameworks

Another problem the WTO should address is the poor administration of dispute settlement in South-South RTAs. Since 2000, about 20 percent of WTO disputes settlements have involved developing members (Anonymous WTO Dispute Settlement). However, none of the disputes have involved member-states within either AFTA or COMESA. Indeed, some trade issues are resolved through consultation and thus never reach the process of dispute settlement. Still, many important matters are resolved through highly politicized methods of negotiation. A legitimate and consistent dispute settlement body would add certainty and confidence in regional markets that are regulated by the politics of the day. Stabilizing a trading environment through consistent and transparent enforcement could result in accelerated integration and decreased barriers to intra-regional trade.

In order to foster an effective dispute settlement body, the WTO should encourage the use of its own dispute settlement body. To foment the use of this body, the WTO could provide more funding for technical missions to aid in dispute cases between member-states of South-South RTAs. Also, the WTO could provide non-binding panel reviews of rulings made by dispute settlements in South-South RTAs. Reviews of decisions, while giving guidance to South-South RTAs, would help the WTO gauge whether the RTAs are promoting or discouraging trade creation. Together, these two strategies for improving South-South disputes could further the WTO's pursuit of increased trade within industrializing countries' RTAs.

Conclusions

Case studies of AFTA and COMESA demonstrate that current South-South RTA regulations outlined under the multilateral trading system have not been adequately enforced or applied. As a result, these regulations have not induced significant increases in South-South intra-regional trade. I have offered only a few recommendations to counter this issue, but clearly there are numerous ways in which the regulation of trade could be more conducive to the development of emerging markets in the global economy. Continued analysis of South-South RTAs could produce viable policy prescriptions to improve the WTO's inadequate approach to cultivating intra-regional trade between industrializing countries.

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