Free Trade Area in Asia

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The formation of trade groupings in Europe has created serious problems for the foreign trade of third countries, particularly under-developed countries.

A proposal to establish an Asian trade bloc was made at the sixteenth session of the ECAEE in March last.

As a defensive step the case for an Asian free trade area can be established if it improves the countries' bargaining strength vis-a-vis the EEC preferential system.

While the enventual formation of a regional trading system in Asia may take a long time, redress of the adverse trade impact of the EEC may be sought through negotiations under the GATT.

PROPOSALS for a customs union or a slight variants of it have been discussed of late in several countries as a policy measure against economic stagnation, especially after the establishment of the European Economic Community in 1958. These proposals have been made with a view to avail of the advantages of free trade — in terms of competition and, hence, the efficient use of resources — over an enlarged market as a result of the widening of 'economic boundaries'. This approach concedes generally the principle of locating industry on the basis of comparative costs. In practice, however, the majority of the schemes now being mooted for regional free trade have emerged from the primary consideration of safeguarding the. countries' trading interests *vis-a-vis* the European Economic Community. So much so, the regional trade arrangements are discussed now as an acceptable mode of policy; trade negotiations of tomorrow, therefore, may not be merely between two countries but between two organised sets of countries. Let us, to begin with, review some of the current trade groupings. It is suggested that possibilities should be explored of a free trade area in South-East Asia comprising Burma, Ceylon, India, Indonesia, Malaya, Nepal and Thailand.

EUROPEAN TRADE GROUPINGS

The European Economic Community (the EEC) became effective on January 1, 1958. It consists of six countries, namely, Belgium, France, West Germany, Italy, Luxembourg and Netherlands. It aims to achieve (a) intra-regional free trade, (b) uniform external tariff and (c) a common agricultural policy. The first stage of trade liberalisation began on January 1, 1959- Most notable, the EEC is a preferential trading bloc insofar as it has extended mutual trade preference to its overseas Associated Territories; this feature of the Community perhaps needs further spelling out since it affects the so-called 'third' countries. The Overseas Territories of the Community fall under two types: (a) those with a colonial status and (b) independent territories; it is the former that are especially associated with the EEC. With the latter the 'Six' are ready to negotiate on the extent of association. A few Asian countries namely Indonesia, Vietnam, Laos and Cambodia are also included in the 'independent' group. The Associated Territories are made up of French Africa, Oceania, Togo and Cameroon, Belgian Congo, Ruanda-Urundi, Italian Somaliland and Netherland New Guinea. One of the important EEC institutions is the Development Fund, 88 per cent of whose resources are to be invested in the social and economic development of the Associated Territories. These Territories, moreover, enjoy special treatment in the application of the EEC external tariff inasmuch as (a) the uniform external tariff of the Community provides them with a preferential market within the region and (b) the associated partners are free to varv their individual tariffs in their trade with third countries.

The European Fre Trade Association (EFTA) was formed after the breakdown of negotiations for setting up a Europe-wide free trade area with E E C at the core. It became effective on Mav 3, 1960. It comprises seven countries, namely, Austria, Denmark, Norway, Portucal, Sweden, Switzerland and the United Kingdom. It aims at free trade within the region for industrial products onlv, to be achieved through elimination by stages of tariffs and quotas. The first cuts were announced on Julv 1, 1960. The Association permits its members to retain their own external tariffs. lt provides for seperate agreements to cover agricultural and fishery products; this is how Britain reconiled her Commonwealth obligations with a trade association with Europe. The EFTA is a preferential bloc insofar as the United Kingdom retains her Commonwealth preferences; the question of origin has been overcome by the '50 per cent rule'. (For instance, in the case of products involving the use of raw materials or other elements originating in a third country, the rule would be that any product in whose case the value added by the national industry or commerce represents 50 per cent of the total value would be considered as produced by the member country.)

THE "SIX" AND THE "SEVEN"

Of the two preferential trade blocs in Europe, only the Community is a customs union in the true sense of the word in that it enjoins internal free trade and uniform external tariffs. It, however, marks an improvement over the pre-World War II variety of customs union in Europe which in the words of a League of Nations study, "tended to abolish internal trade barriers in order to erect on the boundary of the whole community a stiffer barrier, that is to say, in order to create, in practice, a weapon against (trade with) the outside States". That is why the phrase 'common market' has been adopted; 'customs union' had a bad odour about it. Common market does not aim at regional autarky by raising external tariff; the E E C regulation, for example, complies with the GATT principle that the new tariff docs not exceed the average of those it replaces. The first steps towards the introduction of the reduced common external tariff for the Community were taken on January 1. 1961. To recall the beginning of the common market movement in

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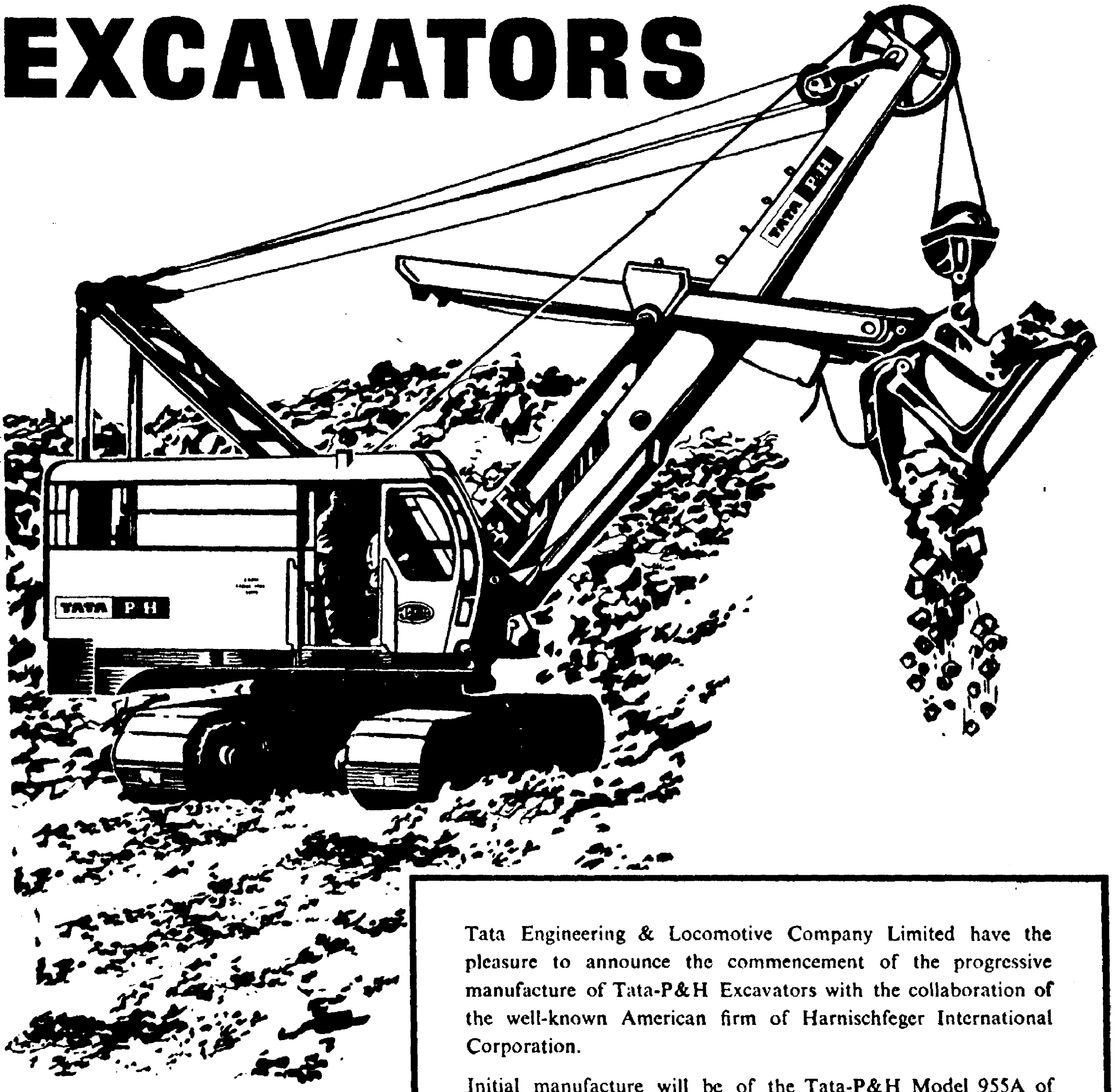

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Europe, it was in May 1930 that the then French Prime Minister M Briand suggested the establishment of a common market since customs unions in the past were "not good". This proposal, however, did not catch on since the United Kingdom was not keen on it. After the Second World War France insisted on pressing its common market scheme without waiting for Britain to fall in. This became clear from the abortive, negotiations through 1958 for setting up a European free trade area, as proposed by Britain, covering all countries of the Organisation for European Economic. Co-operation (OEEC). It was as a retaliatory move that Britain in the following year organised the European Free Trade Association.

Along with the first round of tariff and quota reductions on January 1, 1959 for intra-regional trade, the EEC' decided to extend to the other eleven members of the OEEC' and to all other participants in the General Agreement on Tariffs and Trade (GATT) an important share of the trade liberalisation on a reciprocal basis. This was conceded by the EEC with a view to preventing serious trade discrimination within the OEEC. As a result it appeared likely that on the failure of the Eurpean Free Trade Area talks, some OEEC country might enter into negotiations with the EEC'. In the hope of forestalling such a situation and with a view to avoiding the adverse effects on their economies of the gradual implementation of the Common Market programme and eventually with a view to reopening negotiations on a free trade area with the Six, Britain along with six Continental countries, namely, Austria, Denmark, Norway, Portugal, Sweden and Switzerland formed the so-called Stockholm Group. In June-July 1959 this group produced a draft convention for a. European Free Trade Association which was ratified in January 1960 and came into force from May 3, 1960.

TRADERS' MUTUAL DEFENCE SOCIETY

One of the aims of the EFTA, in common with the EEC, is to establish free trade within the region by eliminating tariffs and quotas, though this is limited to industrial products only in order to reconcile the conflicting interests of the members. A point of basic difference between the two is regarding the external tariff: unlike the EEC, the EFTA members retain their individual tariffs against non-member countries. 'The EFTA is not a customs union; it is only a partial free trade area. It is an association with open membership. Moreover, the EFTA, again unlike the EEC, is purely economic, in character; it does not aim at harmonising or integrating social and economic, policies of the countries of the region. Although the stipulated object of the Association is similar to that of the ECM, namely "to strengthen the economies of its members by promoting expansion of economic activity, lull employment, a rising standard of living and financial stability", its basic purpose is to act as an "effective counterweight" to the EEC and thereby to keep the balance in negotiations with the EEC', aiming at the removal of trade barriers in Europe and ultimately, at the establishment of a free trade association including all the OEEC members. Appropriately the EFTA was described by *The Economist* as a "traders' mutual defence society".

Another consideration that should have prompted the United Kingdom to make haste with its trade association plans in Europe, was the imminent Nordic Union which, in the event of materialization, would have left Britain out in the cold. As a matter of fact, discussions regarding the formation of a Nordic Customs Union consisting of Denmark, Finland, Iceland, Norway and Sweden had manifested much disagreement. The Nordic countries had backed Britain during the 1958 negotiations for a European free trade area. After the failure of these negotiations and in the absence of any attractive alternative proposal from the United Kingdom, it was likely that they would readily patch up their differences and launch a customs union in some modified form. Britain lost no time and acted judiciously in setting up the EFTA.

The formation of these trading groups in Europe has created serious problems for the foreign trade of third countries. We discuss these from India's point of view. Insofar as the ECM external tariff does not show preference of entry to products from the Associated Territories, thereby keeping out the products from India and other third countries and insofar as the Commonwealth preferential arrangements remain unaffected due to United Kingdom joining the EFTA. the European movement towards regionalisation is of little material concern to India's trade problems. What has actually disturbed or is likely to disturb India's trade pattern and economic, development is the EEC system of extending preference to the Associated 'Territories in trade and the supply of capital. It is feared that this would injure India's export prospects both in the six Common Market countries and their Associated Territories and would also impede the provision of foreign capital for India's economic development. India is faced with the problem of exploring new export markets other than the EEC' preferential area and new sources of development finance[1]. We do not consider the problem of development finance here; we confine ourselves to the trade problem. It is in order to ensure a secure market for our products that we suggest an examination of the possibilities of forming a free trade area in South-East Asia consisting of Burma, Ceylon, India, Indonesia, Malaya, Nepal and 'Thailand. (In case Indonesia, in view of its independent' status with respect to the EEC, signs a trade treaty with the European Community, she will not participate in an Asian free trade area arrangement).

THREAT TO THIRD COUNTRIES

The threat to the export trade of third countries, especially the under-developed ones was confirmed by the report early in 1959 of a working party which was appointed by the GATT to investigate the likely effects of the establishment of the EEC, as a new preferential area, on the export trade of third countries. The majority view, supported by Brazil, Ceylon, Chile, the Dominican Republic, Ghana, India, Indonesia, Pakistan, Rhodesia and Nyasaland and the United Kingdom, stated that since importers in the member States of the EEC would give priority in their purchases to the products of the Associated Territories, it would divert trade from third-country suppliers, and disrupt traditional trade patterns, so that third countries would be forced to seek markets elsewhere for a considerable part of their present exports to the six Common Market countries and their Associated Territories. The minority view, representing the members of the EEC who were also members of the GATT working party, maintained that the fears expressed by the majority were exaggerated. Expanding production within the ECM would result in increased devand for the goods and commodities of third countries as well.

Important commodities whose export prospects are likely to be affected adversely due to the emergence of the EEC preferential system arv cocoa, coffee, tea, bananas, sugar jute, tobacco, oilseeds and vegetable oils and cotton. India's export trade especially in tea, coffee, tobacco, oilseeds and vegetable oils will be hit by the EEC's trade preference to its African territories.

Basically, these were considerations that led to the emergence, of similar trade groupings in other parts of the world. Let us describe briefly the events in the Middle East and South America.

In January 1959, the Arab league Economic Council decided to establish the Arab Financial Institution for Economic Development and the Temporary Arab Economic Unity Council, the latter to study an agreement for economic unity among the Arab countries and to make recommendations for the establishment of the Arab common market consisting of the following countries: United Arab Republic, Iraq, Saudi Arabia, the Lebanon, Sudan and the Persian Gulf Kingdoms.

In the distant central and south America, there is, first, the Central American common market formed in 1959 with the tiny States of Nicaragua, Costa Rica, El Salvador, Guatemala and Honduras and associating Panama, and second, there, is the Latin American Free Trade Area set up in January 1960 comprising Argentina, Bolivia, Brazil, Chile, Paraguay, Peru ann Uruguay and associating Mexico, The organisation both of the LAFTA and CACM has been inspired, essentially bv defensive motives, by the emergence of another preferential trade area on the European Continent besides the Commonwealth.

PROPOSAL FOR ASIAN BLOC

A proposal for the establishment of an Asian bloc to consist initially of Malaya, the Philippines, Thailand and Vietnam and. possibly, Indonesia (but subsequently to cover the other countries of South-East Asia) was made by Dr Perfecto E Laguio, head of the Philippine delegation at the sixteenth session of the Economic Commission for Asia and the Far East in March 1960. Although it excluded India to begin with, it did manifest the trend of thinking towards trade grouping on this continent. The ECAFE did not set up a studv group to examine the desirability and scope of this scheme. Such examination is, however, contained in a study submitted to the ninth session of the Commission on Asian and Far Eastern Affairs of the International Chamber of Commerce held in Karachi, December 1960 *(Implications of the European Common Market and the European Free Trade Association on Trade and Economies of Asian Countries,* Rapporteurs: P Chentsal Rao and H L Gupta. Federation House, New Delhi: September 1960). Discussing the difficulties in the way of organizing an Asian free trade area, the study concludes, "It is not inconceivable that some selected countries of the region may enter into arrangement on the lines of EFTA". As alternatives, the study discusses other steps that Asian countries may co-operativelv take with a view to safeguarding their economic interests; *vis-a-vis* the EEC. These include intra-regional trade promotion arrangements. mutual exchange of tariff and quota concessioins between underdeveloped countries of the region and corrective action through the GATT forum. The study abstains from suggesting a definite scheme for a regional free trade arrangement.

A factor that any Asian free trade area a proposal must take note of is the form that a likelv raoprochement between the EEC and the EFTA might assume. To the extent this lead to a substantial modification of the EEC's preferential character. the case for organizing a free trade area in Asia purely on defensive grounds is lost. In the event it becomes worthwhile examining how far an Asian free trade area is feasible for other economic reasons. From his survey of the customs union theory, Dr R G Linsev lavs down the conditions under which countries ought to form a customs union. (*Economic journal,* September 1960.) Either the union partners should be doing a high proportion of their foreign trade with one another; or, foreign trade should form a low proportion of the participating countries' total expenditure. Stated in the negative form, it implies that a country should not join a free trade arrangement if its foreign trade constitutes a high proportion of its national income, and especially not if the participating countries account for only a small proportion of its foreign trade.

Proceeding on the basis of these theoretical principles, one can support the case for a free trade area between those Asian countries who either do not trade much abroad, or trade mostly with countries within the area. India's foreign trade as per cent of her national income is low: it is only 7 per cent. Having satisfied one of the two conditions, India should look about for neighbour countries whose foreign trade is onlv a low proportion of their national incomes or whose trade is mostly confined within the region. Looking to the desirability of having a geographically well-knit region, a free trade area covering Burma. Cevlon. Tndia, "Indonesia, Malaya, Nepal and Thailand deserves consideration.

As a defensive step the case for an Asian free trade area can be supported if the union improves the countries bargaining strength *vis-a-vis* the EEC preferential system either because the group is one of the chief buyers from or sellers to the EEC. But its defensive function is satisfied onlv if no member country is free to enter into an individual arrangment with the opposing group. If the members are willing to surrender questions of extra-regional trade also for consideration by a single governing authority the proposed free trade group of South-Fast Asia will become the monopoly seller of tea, tin and rubber and a hie buyer—for this group will account almost for one-fifth of the world population.

The eventual formation of a regional trading system in Asia would take a long time. Meanwhile, re-

the EEC preferential system should be sought generally through GATT portntinns. The impending rap-Kingdom and the EEC is also a hopeful sign in this respect.