

DEVELOPMENT CO-OPERATION DIRECTORATE  
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**AID FOR TRADE AT A GLANCE: CONNECTING TO VALUE CHAINS**  
**CHAPTER 4. BOOSTING VALUE CHAINS VIA REGIONAL AID FOR TRADE**

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## CHAPTER 4. BOOSTING VALUE CHAINS VIA REGIONAL AID FOR TRADE<sup>1</sup>

### 1. Introduction<sup>2</sup>

1. The trade agenda of developing countries is increasingly being pursued through regional economic integration and co-operation efforts, a fact noted at the *Third Global Review of Aid for Trade in 2011*. In this context, regional aid for trade can help boost trade and facilitate movement along value chains. In Asia, regional co-operation is motivated by attendant benefits in regional production networks; fully two-thirds of ASEAN exports can now be traced to participation in these networks (ADB 2013). In Africa, where small, fragmented markets impede trade and competitiveness, regional co-operation is one way in which national markets can be enlarged, specialisation can emerge and risks can be shared. Latin America, which has a long tradition of economic co-operation, is actively using regional fora to lower costs to doing business and trade across the region and with external partners.

2. This chapter shows that regional aid for trade has a critical role to play in boosting the participation of particularly low income countries (LICs) and least developed countries (LDCs) in regional production networks, and in enabling them to move up the value chain. One of the main motivations of the trend towards regional integration, which has become a key component of the international commercial policy landscape, is the need to reduce barriers in regional production networks. Barriers to trade, bureaucratic bottlenecks and infrastructural deficiencies reduce the attractiveness of countries as spokes in the wheel of these production networks.

3. This chapter first considers the links between regionalism and regional integration in the context of production networks (Section 2), followed in Section III by analysis of the role of the current regionalism trend in development strategies and its implications for the development of value chains. Relevant results from the 2013 WTO-AU-UNECA questionnaire regarding regional aid for trade issues and its impact are summarised. Section 4 considers how regional aid for trade can be used as a cost-effective approach to reducing the binding constraints to regional integration and the formation of regional production networks. Section 5 uses case stories to underscore how regional aid for trade has directly and/or indirectly facilitated regional production chains and integration. Section 6 concludes with general assessments.

### 2 Regionalism, Regionalisation and the Role of Value Chains

4. As is underscored in this volume, previous *At a Glance* publications and the considerable literature that has emerged on the topic, trade has played an increasingly important role in successful development strategies and aid for trade has been an instrumental, cost-effective approach to lifting binding constraints to international integration. This section analyses how multi-country and regional aid for trade programmes can support regional integration, or “regionalisation”, and value chains and summarises the policy-relevant implications of bilateral and regional economic co-operation, or “regionalism”, for emerging and developing economies. The section begins with a discussion of regional

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<sup>1</sup> This chapter was written by Michael G. Plummer with contributions from Michael Cornish, Rebecca A. Freeman, and Alissa Tafti.

<sup>2</sup> With financial support from the EU, the OECD is leading a study on regional perspectives on aid for trade, which focuses on not only the potential benefits of regional aid for trade but also the challenges of effective implementation and mainstreaming into national development plans. The study will feature several regional stakeholders’ consultations and will be completed in 2013.

co-operation and development in the context of the multilateral trading system, followed by a topology of economic effects inherent in regional co-operation with relevance to production networks. Next, it considers how regional co-operation can increase prospects for regional integration and production networks. Finally, complementary factors necessary for successful regional economic integration programmes are highlighted.

### ***Regionalism in the Global Context***

5. Some 546 notifications of regional trading arrangements (RTAs, defined by the WTO to be a reciprocal trading agreement between two or more countries) have been made to the WTO, with 354 in force<sup>3</sup>, up from 300 end-2005 and 130 at the beginning of 1995. RTAs have been one of the defining international policy changes in the period since the launch of the Aid-for-Trade Initiative. Developing countries, especially in Africa and Asia, but also in Latin America and elsewhere, have become extremely active in the regionalism movement.<sup>4</sup> Driving much of this process has been the desire to promote regional production networks—as is explicitly the case, for example, in Asia. With no end in sight to this process (despite concerns over the relationship between multilateral and bilateral trade rules' approaches), this trend can likely be a “building bloc” rather than a “stumbling bloc” if production networks prosper via openness and efficiency, not by creating discriminatory blocs (Plummer, 2007).

#### *The Economics of Regional Production Networks*

6. The potential gains to developing and emerging economies of regional co-operation can be large, provided that governments adopt an accommodating policy framework and planning to prepare the economy appropriately. Free-trade areas (FTAs) remove discrimination between partner countries and domestic firms, leading to a positive productive efficiency effect (“trade creation”) and, perhaps, greater investment flows to take advantage of lower barriers to trade among partners and potential synergies (“investment creation”). However, since FTAs grant preferences to partners beyond what is accorded to non-members of the group, they introduce a distortion between partner and non-partner firms, discriminating in favour of the former and to the detriment of the latter (“trade diversion”). Ultimately, trade diversion results in negative terms of trade effects that it may lead to a country's purchasing imports from a higher-cost source, representing a loss to efficiency. Hence, trade diversion is especially problematic for production networks, which depend upon lowest-cost sourcing. This constitutes a key reason why the regionalism movement backed by production networks should remain open and outward-oriented: trade diversion is anathema to the effective organisation of value chains. It also provides a strong incentive to keep rules of origin—which are essential in FTAs to avoid “trade deflection”<sup>5</sup>—liberal, simple, and symmetric.

7. Moreover, the greater the degree of discrimination inherent in an FTA, the greater the potential for “investment diversion” in which FDI flows to a country merely to take advantage of protected regional access. This “tariff hopping” FDI was once promoted extensively in developed and developing economies alike to try to lure increased investment flows. But such an approach is increasingly problematic today for production networks, which thrive when markets are open, not closed. Indeed, the rising importance of production networks might not only explain why FTAs and other forms of regional co-operation are increasingly open in nature but why barriers to trade and investment have been falling globally. The cost of

<sup>3</sup> [http://www.wto.org/english/tratop\\_e/region\\_e/region\\_e.htm](http://www.wto.org/english/tratop_e/region_e/region_e.htm), accessed 11 January, 2013.

<sup>4</sup> For a list of these, updated to 13 January, 2013, see [http://www.wto.org/english/tratop\\_e/region\\_e/region\\_e.htm](http://www.wto.org/english/tratop_e/region_e/region_e.htm).

<sup>5</sup> “Trade deflection” refers to the possibility of non-member economies' diverting exports to the lowest-tariff country in an FTA.

isolating one's economy from the international marketplace was always high, but is increasingly so in a truly globalised economy (OECD, 2012).<sup>6</sup>

8. In addition, value chains amplify the costs of tariff barriers. Even low tariff barriers across a region can inhibit value chains because they are cumulative. Enterprises downstream have to pay tariffs on their inputs as well as on the value of their exports, raising costs of the production network geometrically (OECD, 2013). This magnification of protection along the value chain also holds for non-tariff barriers and behind-the-border impediments (see also chapter X). Hence, the efficiency effect of regional FTAs tends to be greater in the context of production networks. OECD (2013) underscores how various deep provisions in FTAs can significantly increase trade via supply chains. The role of regional aid for trade to facilitate production networks and the goals of regional co-operation are evident in this process.

9. Besides allocative efficiency benefits and greater FDI flows, further benefits to regional co-operation include: (1) potential for greater economies of scale due to access to a larger market; (2) technology transfer via FDI and other aspects of integration; and (3) the potential for a more efficient policy framework due to behind-the-border and trade facilitation measures included in modern FTAs (*e.g.* with respect to quality standards, complex measures specific to the service sector, laws related to corporate and public governance, customs procedures and competition policy). All of these areas are pertinent to creating and enhancing regional production networks along the value chain, discussed at length in Section 4.

#### *Boosting Regional Production Networks*

10. Thus, trade and investment creation resulting from regional co-operation are highly relevant to production networks. By reducing barriers to trade and investment within the region, lead firms are able to organise production according to the respective comparative advantages of member-countries. They create these networks via a number of channels, from FDI to licensing and contracting. These lead firms then engage in fragmented trade along value chains, increasing regionalisation. FDI inflows from within and outside the region rise, and with greater FDI inflows come the myriad potential benefits to host economies, including increased employment, risk-sharing capital, foreign exchange, technological spill-overs and other productivity-enhancing knock-on effects. A regional presence allows lead firms to minimize transport costs and benefit from lower trade costs within a regional co-operation framework. This regional co-operation framework, in turn, is an important gateway to greater multilateral liberalisation.

11. Regional production networks boost trade performance of the country, and create a demand for trade-enhancing measures to boost efficiency through, for example, trade facilitation and better soft and hard infrastructure. Participating in these regional networks allows for ready-made external markets for local production and has a "learning-by-doing" effect on local firms as the economy opens up to regional and global markets. FDI inflows and other forms of interaction with lead firms generate important spillovers to the economy that tend to accelerate moving up the value chain. In other words, production networks make use of each economy's comparative advantages to boost productivity and cut costs, while bolstering investment and technology transfer, plugging developing economies into the global economy in ways that would have been impossible two decades ago. Via production fragmentation, lead firms allocate labour intensive segments to low-wage economies, resulting in rapidly growing intra-industry trade in parts and components along the value chain.

12. Regional co-operation holds especially significant opportunities for small LICs, which, as mentioned earlier, in the past have been generally excluded from the FDI-trade link. As such, regional co-operation serves as a stepping-stone for deeper integration into wider regional and global markets and

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<sup>6</sup> A formal approach to this changing reality was developed in the "endogenous tariff" literature.

facilitates moving up value chains. Vietnam, for example, benefitted from its accession to ASEAN in 1995 by adopting an increasingly liberal trade and investment regime through the ASEAN Free-trade Area (AFTA) and the ASEAN Investment Area programmes, allowing it to participate along with its more developed partners in various production networks – a process further encouraged by WTO accession in 2007. This led to increased globalization of the economy, higher inflows of FDI, technology spill-overs, increased employment of its labour force and decreased poverty. Over time, it began to move up the value chain, becoming a middle-income country in 2012. It hopes to replicate these successes via participation in mega-regional economic co-operation accords in the Asia-Pacific region, discussed below. The Vietnamese success in this regard has had an important demonstration effect on other transitional economies in the region; Cambodia has been imitating Vietnam’s success in recent years and Myanmar, whose political opening in 2012 has been followed by an enthusiastic embrace of outward-oriented economic reforms, is counting on integration into production networks as a critical future source of FDI, employment and poverty reduction in natural-resource and manufacturing sectors.

13. Indeed, Southeast Asia has been particularly successful in attracting regional production networks due to its differences in wage and labour productivity levels across member-states, which facilitates benefits from value chains; regional trade and investment liberalisation through such initiatives as AFTA and the ASEAN Economic Community (AEC); increasingly-competitive soft and hard trade infrastructure, such as efficient maritime ports, national “single windows” for customs under the ASEAN Single Window programme, and several industrial “growth triangles” (in many ways similar to export processing zones); and increasingly-strong intra-regional and international links that result in lower production and logistics costs.<sup>7</sup>

14. For example, ASEAN began to create a dynamic trade sector in the early 1980s, via trade and FDI liberalization and investments in trade-related infrastructure. The reform programme led to major changes in the structure of trade, from a dominance of natural resource and agricultural products to manufactures. In this latter sector, the most significant changes took place in machinery and transport equipment (SITC 7). Within this sector, by far the biggest change has been for thermionic valves (SITC 776), whose export value rose from USD 12 billion in 1990 to USD 120 billion in 2006, accounting for 16% of ASEAN’s total exports of USD 759 billion.<sup>8</sup> ASEAN exports nearly one-third of the world’s thermionic valves (USD 379 billion), which include television picture tubes; other electrical valves and tubes; diodes, transistors, and similar semiconductors; electronic microcircuits; and Piezo-electric crystals. In other words, these exports are part of an electronics value-chain in which ASEAN is the key link. A main goal of the AEC is to repeat this success in attracting value chains in other areas as well.

#### *Complementary Factors in Fostering Regional Economic Integration*

15. In order for regional co-operation—or any trade policy innovation—to spur successfully regional integration, some essential pre-conditions need to be in place. First, the impact will depend on the soundness of its member countries’ domestic economic policies. Few firms will be able to benefit from regional trade if there is macroeconomic instability, weak property rights, corruption, or opaque tax laws and business regulations. An FTA typically spurs reform in domestic economic policy; given that FTAs tend to be much deeper than what has been the case in a multilateral context, this underscores an important advantage of regionalism as a complementary trade policy strategy. For example, Mexico was able to use its commitments under the North American Free-trade Area (NAFTA) as part of a pervasive domestic economic reform programme, and the associated liberalisation of behind-the-border measures was “first best”.

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<sup>7</sup>Plummer and Chia (2009) and Athukorala (2010).

<sup>8</sup> Plummer and Chia (2009).

16. Second, success in attracting production networks via an FTA will also depend on the efficiency of transportation and other infrastructure, trade facilitation, and other policy-related measures. For example, to realise benefits from the FTA, the transportation and logistics networks between member countries need to have enough capacity to handle increased trade volumes. Landlocked countries in particular depend critically on the quality of the infrastructure in neighbouring countries.

17. Hence, in order for trade liberalisation to be successful, developing economies often require improvements in a variety of areas that have traditionally fallen under the central themes of the aid-for-trade initiative: trade-related infrastructure, trade facilitation and creating a trade-enabling environment are essential for developing countries to benefit from trade liberalisation, regardless of the context. Regional trade agreements facilitate progress in these areas, as it is easier to address these (often politically sensitive) issues in the context of a small group of like-minded economies in the region than in, say, the multilateral context. Below, these complementary policies that help to determine the success of trade liberalisation and facilitation are surveyed, before proceeding to analysis of how the emerging regionalism in the global economy is spurring production networks and fragmented trade along the value chain.

#### *Transit/Transport Corridors*

18. Transit/transport corridors constitute excellent examples of the advantages FTAs and other forms of regional economic co-operation offer to developing member economies, as by their very nature they are regional in scope. They are generally understood to be physical routes that connect two or more areas and allow for the flow of people and goods between or along the route. These corridors can serve to connect different areas of a single country, or they can connect sub-regions and regions. They are composed of roads, railways, bridges and port access. They can be developed to increase trade within a region, provide access to landlocked countries and create international access to trade in goods by connecting a region to ports. Transit/transport corridors are particularly important to the trade and growth prospects of landlocked countries.

19. High transport costs undermine potential gains from trade liberalisation and can negate the price effects of reductions in tariffs and non-tariff barriers via FTAs. As such, they limit the ability of economies to participate in production networks. Their significance in impeding trade resonates throughout the trade literature. For example, Limao and Venables (2001) estimate that the quality of infrastructure in developing economies account for 40-60% of the variation in transport costs, and a 10% drop in transport costs subsequently increases trade by nearly 25%. Thus, attention to transit corridors in aid-for-trade programmes in particular is well-merited.

20. Early attention to transport issues was most heavily focused on the development and improvement of physical infrastructure such as roads, railways and bridges. More recently, projects and programmes aiming to improve transport corridors have expanded to include measures that serve to remove bottlenecks at border crossings and decrease transit time and costs directly and indirectly via, e.g., harmonisation of border controls, improvements in technology and communication, reduction in required paperwork and improved efficiency of government agencies and border agents.

21. Taking a regional approach to developing transit corridors is efficient, but is often politically challenging (OECD 2009). Countries bear different shares of the corridor and its project costs, so there exist asymmetric incentives to expend limited funds and resources on the corridor over other domestic projects, particularly when projecting which country “gains the most” is often highly disputed. In this sense, the role of an “honest broker”, such as a multilateral or regional development bank, can help overcome this problem. Some examples of this include the role of the Asian Development Bank in the Greater Mekong Subregion (GMS) and the Central Asian Regional Economic Cooperation (CAREC), discussed below, in which it has invested heavily and plays the role of honest broker.

22. Tangible benefits of using a regional approach in place of a series of national approaches can range from standardisation of construction of rail lines, which would allow rail cars from each of the countries within the region to use the rail lines along the corridor, to the development of regional weight standards. OECD (2009, Chapter 2) illustrates how regional co-operation organisations have worked with donor and partner governments to improve cross-border transport links as a strategic plan to boost regional economic integration. Further, as noted by Kuroda, *et al.* (2007), “No matter how good roads are, they are of little use if traffic is held up at the borders.”<sup>9</sup> In order to maximise the impact that infrastructure has on trade, there must also be harmonisation of regulations and systems and co-operation among governments to ensure swift access across borders.

### *Trade Facilitation*

23. As it involves tackling many complicated and sometimes politically sensitive behind-the-border measures, trade facilitation tends to be more easily handled at the regional level than in multilateral negotiations. Trade facilitation is distinct from other issues in international trade because of its focus on *efficient* processes (UNDP, 2007). Measures geared towards enhancing trade facilitation are vital to countries’ trade and development strategies: they allow for a realisation of trade expansion that would otherwise be stunted because of non-tariff and behind-the-border barriers. Indeed, such impediments to trade reduce potential efficiency gains, productivity improvements, and subsequent growth possibilities that derive from increased exports and imports. They are also detrimental to the creation of production networks and often are responsible for countries being excluded from value chains.

24. Many aspects of trade facilitation when addressed at the regional level do not lend themselves to discrimination across trading partners and, hence, lead to greater efficiencies in global trade rather than just regional trade. Indeed, the Asia-Pacific Economic Cooperation (APEC) organisation has made significant progress in trade facilitation on a completely voluntary, non-discriminatory basis, including a set of trade facilitation principles devised in close consultation with the private sector (discussed in Section 5).

25. Perhaps the most obvious argument in favour of regional trade facilitation initiatives relates to geography, as regional proximity allows for better information flows between traders, shared cultural practices and common systems developed over time (Maur, 2008). As many non-tariff and behind-the-border barriers to trade are geographically located, regional solutions are logical. Specific regional trade facilitation initiatives related to geography might include sharing of border facilities or regional harmonisation and co-operation to address duplication (arising because of differing standards across countries) and friction costs (for example, inefficient time usage because of repeated loading and unloading of commodities).

26. Second, regional trade facilitation can create efficiency gains through the elimination of costly procedures and services. Here, regional solutions can sometimes be easier than multilateral approaches because of: (1) the complexity of trade facilitation deals; and (2) the fact that implementation of measures to decrease costs often necessitates regional co-operation on the ground. Eradicating costly procedures enables efficiency gains for firms and allows smaller scale operators to access export markets, a key problem in developing countries. Regional solutions include harmonisation, mutual assistance among authorities for customs valuation, and mutual recognition of rulings and of certification and testing (OECD, 2009).

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<sup>9</sup> Haruhiko Kuroda, Masahiro Kawai, Rita Nangia, “Infrastructure and Regional Cooperation” in *Rethinking Infrastructure for Development*, François Bourguignon and Boris Pleskovic, eds, The World Bank: Washington, DC, 2007: p. 246

27. Third, regional trade facilitation can also engender competition in trade-related activities. Regional agreements that generate increased transparency in regulations can, in turn, stimulate more efficient border management. Trade-related services that are dependent on regulatory co-operation benefit as well.

28. In short, experience suggests that transit corridors and trade facilitation are important to the success of any trade policy strategy, and addressing associated issues tends to be easier and more efficient in the context of regional economic co-operation than in other approaches.

### **3 Regionalism and Production Networks in Developing Economies**

29. The above analysis highlighted the importance of regional co-operation in facilitating the participation of developing economies in value chains, as well as the necessary complementary policies to support the process. Lowering trade and investment barriers via regional trading arrangements reduces transactions costs associated with fragmented trade and, hence, enables the creation of regional value chains (OECD, 2013). WTO (2011), for example, uses a gravity model to capture the effects of deeper economic co-operation accords on production-network-related trade, and estimates that they increase trade among partner countries by almost 35 percentage points. It is also easier to promote deep reforms in the context of regional agreements, as they are typically composed of a smaller set of like-minded countries and they tend to preclude “free-riding”. Even “special and differential” treatment in FTAs is increasingly expressing itself in the form of longer transition periods rather than derogations from policy reform exigencies.

30. This section considers briefly the respective experiences of the most successful region in establishing value chains, Asia, and the least successful, Africa. In addition, it includes a review of efforts in the Caribbean, which has been an especially active sub-region in trying to promote value chains. It also considers inputs regarding “revealed” strengths and weaknesses of regional aid for trade as a catalyst for regional integration via results from: (1) the 2013 WTO-AU-UNECA surveys of donors and partner countries in Africa; and (2) the 2010 OECD-WTO regional aid-for-trade monitoring and evaluation exercise. The next section discusses how regional aid-for-trade constitutes an effective means to promote value chains and contribute to the success of these regional agreements.

#### ***Regional Co-operation in Asia as a Successful Vehicle to Promote Value Chains***

31. East Asia has been by far the most active—and successful—region in mobilising regional co-operation as a means of promoting fragmented trade and production networks. Most Asian FTAs have been bilateral in nature, which tend to be easier to negotiate than, say, larger memberships or deeper accords such as customs unions. Moreover, a majority of these FTAs are with economies outside of Asia. For example, ASEAN as a regional organisation has six FTAs in place (with China, South Korea, Japan, Australia, New Zealand and India), and its member-countries have ten separate agreements with East Asian economies outside of ASEAN and nine outside of East Asia entirely, with several of latter accords being more comprehensive than even intra-ASEAN cooperation (Petri, *et al.*, 2012). A great deal of empirical work has been done on production networks and fragmented trade in the region and with external partners.<sup>10</sup>

32. The driving force behind regional co-operation in East Asia is market-based; FTAs are being sought in large part as a means to increase FDI flows to deepen existing production chains and promote new ones. As noted above, the region has been very successful in this regard; intra-regional trade and investment flows have been rising significantly over time, to the point that regional trade now constitutes

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<sup>10</sup> Kimura and Obashi (2011) offer an extensive survey of the literature.

more than half of total trade. However, if one computes trade on a value-added basis, intra-regional trade comes to significantly less than half (ADB 2008). In other words, the growing role of regional production networks leads to “double counting” of (nominal) intra-regional trade flows. This conclusion can also be gleaned from the OECD-WTO TiVA database for selected countries; for example, in nominal terms, China became Japan’s most important trading partner in 2007, but in part this is because of the rising importance of China in Japanese-led production networks. According to TiVA, in value-added terms, the United States continues to be Japan’s most important trading partner.

33. While the vast majority of empirical studies on bilateral FTAs in Asia would suggest that these accords have had (or will have) a positive effect on welfare of their member-states, they have important shortcomings: since the driving force behind Asian regionalism pertains to fostering regional production networks, bilateral FTAs will always tend to fall well short of potential. Regional FTAs would be needed to optimise value chains and lower costs associated with, for example, rules of origin (via “cumulation”), create regional intellectual property standards, adopt regional trade facilitation measures, and so forth. It is important to note that these policies are “first best”, as all countries benefit, not merely partner countries.

34. Recognising these constraints, Asian governments have now launched negotiations to create mega-regional accords, namely, the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP), a trend that has been called the “new regionalism” in Asia (Petri, *et al.*, 2012). As each would constitute approximately 40% of global trade, they will be highly significant new institutions in the global economy and will serve to undo many of the much-maligned inefficiencies associated with the FTA “Asian noodle bowl”.

35. The TPP agreement negotiations were launched in 2008 and the 17<sup>th</sup> round of negotiations took place in May 2013. The TPP builds on a high-quality FTA between four small, open economies (Brunei Darussalam, Singapore, New Zealand and Chile), known as the “P4,” and in addition to these negotiating parties the TPP includes the United States, Australia, Malaysia, Vietnam and Peru, and more recently Canada and Mexico. Japan confirmed its intentions of joining in March 2013 and will likely begin to participate as a full member in July.

36. The TPP is distinct in terms of not only large differences in levels of development but also its ambitions to become a modern, “21<sup>st</sup> Century” agreement that would embrace a wide-variety of areas, including border and non-border barriers to trade in goods and services, FDI, intellectual property protection, trade facilitation, competition policy, and even sections on science and technology and small- and medium-sized enterprises. All of these areas are pertinent to production networks.

37. The RCEP is a much more recent initiative which was launched in November 2012. It is the first major initiative that has been spearheaded by ASEAN as part of its strategy of “ASEAN Centrality”; the RCEP is to be initially negotiated only by ASEAN and its existing FTA partners, which are China, Japan, South Korea, Australia, New Zealand, and India. However, the Guiding Principles for Negotiating the RCEP, which were endorsed by ASEAN and its FTA partners’ leaders, would allow the region’s economic partners to eventually accede into the agreement. The RCEP is intended to be a “high quality” agreement, though its focus on being more “flexible” than the TPP, as well as its membership, suggests that it will be less comprehensive. The RCEP leaders finished their first negotiating round in May 2013, at which scope and methodology were discussed, with a second meeting planned for September. The leaders of RCEP have targeted completion of the agreement by the end of 2015.<sup>11</sup>

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<sup>11</sup> See the “Joint Declaration on the Launch of Negotiations for the Regional Comprehensive Economic Partnership,” available at: <http://www.meti.go.jp/press/2012/11/20121120003/20121120003-2.pdf>.

38. Empirical studies suggest that these regional accords will have large effects on regional economic growth to no small degree due to the effect that the TPP and RCEP will have on FDI inflows and outflows, that is, in enhancing production networks. For example; Petri, *et al.* (2012) uses an advanced CGE modelling approach to estimate the economic impact of the RCEP and the TPP as pathways to the FTAAP in 2025.<sup>12</sup> They estimate large gains for both tracks: the effects on the world economy would be small initially but by 2025 the annual welfare gains would rise to USD 223 billion on the TPP track, USD 499 billion on both tracks, and USD 1.9 trillion with the Free Trade Area of the Asia-Pacific (FTAAP), or almost 2% of global GDP. Interestingly, the biggest gains accrue when the two tracks are consolidated; in effect, this results from both China and the United States being included in the same agreement.

### ***Regional Co-operation in Africa: Attempts to Develop New Networks of Integration***

39. Africa has been just as busy as Asia in formulating FTAs and even deeper forms of integration, such as customs unions (*e.g.*, the Southern African Customs Union, SADC, and the Economic Community of West African States, ECOWAS) and even monetary unions (*e.g.*, West African Economic and Monetary Union, known by its French acronym, UEMOA). Extensive surveys of these initiatives and plans for the future can be found in the African Development Bank's *Regional Integration Strategy Papers* for various regions.<sup>13</sup> Like Asia, Africa has considered integrating its many FTAs in a "continental" or "pan-African" FTA, which began to be actively discussed at the 6<sup>th</sup> Ordinary Session of the AU Ministers of Trade in 2010. However, a major difference between the Asian and African experience is that the former has been far more effective in boosting intra-regional trade: intra-regional trade in Africa comes to only about 10% of total trade.

40. The superior performance of Asia in increasing intra-regional trade relates in part to the structure of production: African economies tend to engage more in inter-commodity trade (*e.g.*, natural resource exports for imports of manufactures) whereas Asia's export structure is much more diversified and is increasingly characterised by intra-industry trade, including fragmented trade via production networks. But at early stages of development, most Asian economies also began with inter-industry trade; diversification proceeds as countries develop and move up value chains. In addition, like Africa, intra-regional trade in Asia has been hampered in the past by connectivity issues; Southeast Asian nations have been prioritising and placing significant resources into enhancing cross-border road and rail links, bridges and "soft" infrastructure in order to lower the cost of intra-regional interchange through transit corridors and other initiatives, with considerable success.

41. For example, to this end the ASEAN Infrastructure Fund was created in 2012, and the Greater Mekong Subregion (GMS), with its secretariat at the ADB, has been highly successful in addressing key bottlenecks to trade in the Mekong region since its inception in 1992. It is important to note that these initiatives are often framed in the context of the need to reduce the costs of intra-regional interchange *not* as a means of raising intra-regional trade shares as a goal in itself but rather to attract production networks, which in turn usually have the effect of raising intra-regional trade, though not in all cases (intra-regional trade in ASEAN has only risen from 20% of total trade when AFTA was signed to about 25% today). But, success in this regard should be measured by the effects on lowering costs, rising competitiveness and attracting FDI, all of which have been a hallmark of the ASEAN success story over the past generation.

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<sup>12</sup> In the actual Petri, *et al.*, (2012) publication, the RCEP calculations only include the "ASEAN+3" economies, that is, ASEAN, China, Japan, and South Korea; and the TPP simulations do not include the three members that have joined over the past year, *i.e.*, Canada, Mexico and Japan. However, the website supporting the book ([www.asiapacifictrade.org](http://www.asiapacifictrade.org)) includes numbers for RCEP ("ASEAN+6") and the TPP 12.

<sup>13</sup> Available at: <http://www.afdb.org/en/>

42. Moreover, “deep” regional co-operation that includes removing border and non-border impediments to trade has supported the integration process across East Asia, motivated by production networks. Further, the stress placed on services liberalisation in the context of the AEC and RCEP is indicative of this priority to attract value chains; as is clear from the TiVA database, international trade in services is much larger in terms of value added (50%) than seemed to be the case in terms of nominal trade (around 30%). This difference is explained in large part by the prominent role that the services sector plays in supporting international production networks. East Asian policy makers are now prioritising services.

43. Thus, the fact that Africa has not been able to create regional production chains has been an important factor behind this underperformance in terms of regional integration. The lack of intra-industry trade and insufficient development of production networks as impediments to closer regional integration were underscored in the AfDB’s *Regional Integration Strategy Papers*.

44. Clearly, African leaders are cognizant of these problems and have sought means to rectify them. For example, the African Union’s *Action Plan for Boosting Intra-Regional Trade* (African Union, 2012) identifies the constraints limiting intra-regional trade and proposes specific projects to remove them. *Inter alia*, it notes that, “African countries will trade more with each other if they upgrade their productive capacities in dynamic sectors of the economy and support the development of regional enterprises and value chains.” (p. 8). It also prioritises programmes to increase FDI and develop regional enterprises and value chains.

45. Donors have also been addressing these core binding constraints to intra-regional trade in Africa. The 2013 WTO-AU-UNECA surveys were undertaken as part of the monitoring and evaluation preparations for the Fourth Global Review of Aid for Trade. The WTO, in collaboration with the African Union (AU) and the Economic Commission for Africa (ECA), designed an online questionnaire aiming at assessing how aid for trade can best support the AU objective of increasing intra-African trade. The questionnaire was circulated by the AU and ECA to African countries and Regional Economic Cooperation organisations (RECs), as well as donors and Southern partners. Overall, 51 responses to the questionnaire were received, including 30 responses from African countries, 5 from the RECs and 16 from donors (8 bilateral and 8 multilateral).

46. With respect to regional co-operation and integration, the donor survey revealed that:

- Three-fourths of donor respondents were investing in transit corridors in Africa, and three-fourths of these indicated that their activities were based on both regional and corridor strategies.
- More than three-fourths said that the demand for assistance for regional trade programmes by partners had increased significantly since 2005, suggesting the perception of a rise in interest in developing regional co-operation programmes with donors (“triangular co-operation”). Almost all donors note that their support has been aligned with various AU trade initiatives, especially the African Productive Capacity Initiative (approximately 90%) and the Programme for Infrastructure Development in Africa (two-thirds).
- Over 80% of donors have participated in pan-African projects to promote regional trade co-operation and integration, and over half of these reported involvement in various sub-regional initiatives as well, including EAC (63%), ECOWAS (56%) and SADC (50%).
- Evaluations of donor programmes on regional trade co-operation suggest that these programmes have been highly successful: about two-thirds found that these programmes lead to increased exports and trade, over two-fifths found that they led to increased economic growth and reduced

poverty, and slightly over one-third noted that the programmes had helped with export diversification.

47. The results of the donor survey, therefore, would suggest that regional aid for trade has been: (1) focused on removing the binding constraints to regional integration and improving regional economic co-operation via improved hard and soft infrastructure; (2) directed at sub-regional and regional initiatives and developed in close co-operation with development partners; and (3) successful in spurring growth, reducing poverty, and diversifying the economy, *i.e.*, the essential goals of regional co-operation.

48. The accompanying 2013 WTO-AU-UNECA partner survey corroborated many of these themes.<sup>14</sup> According to this survey, trade-related infrastructure and transport constitute key sectors in regional trade strategies, as do agriculture, trade in services and services to support exports. Respondents also reported that their regional co-operation strategies were developed via consultation with donor-partners, regional partners and needs assessment, but added consultation with the private sector (domestic and foreign) as an important participant in the process. The EU was cited as by far the most important source of assistance for regional trade integration.<sup>15</sup> However, the notion that backing for regional trade programmes since 2005 increased significantly was only supported by less than 10% of the respondents, with less than half noting that it had increased somewhat. This finding may be suggestive of unmet demand for regional assistance.

49. Priority sectors for regional co-operation were similar to those cited by the donors, but recipient countries appear to believe that donor support is less aligned with their own strategies, with only one-tenth saying they were well-aligned and only two-thirds saying they were moderately aligned. Two-thirds maintain that they had not requested help for AU initiatives. The most important difficulties in implementing regional and/or sectoral trade strategies cited were the lack of implementation by regional partner countries—underscoring problems associated with regional public goods—and capacity constraints of the implementing ministry.

50. Evaluations of the programmes revealed similar results as in the donor survey, with increased economic growth, trade and poverty reduction among the greatest successes. However, increasing aid for trade for regional funds was also listed as an important outcome of evaluations, with half saying that regional aid for trade increased as a result, whereas less than 20% of the donors believed this to be the case.

51. In short, while regional co-operation can be an important protagonist of regional trade in Africa, as noted in Section II, supporting “soft” and “hard” infrastructure and other complementary policies need to be in place in order to achieve results. This is an important reason why the many attempts at formal economic co-operation have yet to have an important effect on regional integration. Hence, regional aid for trade is particularly effective in creating a better environment for value chains. The 2013 UNECA surveys suggest that regional aid for trade has been effective but much more can be done.

### ***The Caribbean: Using regional aid for trade to promote integration***

52. The Caribbean Community (CARICOM) is an organisation made up of 15 member states and dependencies. The Caribbean has a long tradition of economic co-operation; CARICOM evolved from the Caribbean Community and Common Market (1973) into the CARICOM Single Market and Economy, which went into effect in 2006. While the sub-region is small, with only about 17 million people, its integration objectives have been ambitious: the CARICOM Single Market and Economy is essentially a

<sup>14</sup> While the response rate to the partner questionnaire was fairly good with 30 countries responding, many of the questions only included a fraction of the total, with most questions having only about five respondents.

<sup>15</sup> OECD (2009), Chapter 2, gives a good overview of EU assistance to African countries in implementing EPAs.

unified market with a common external tariff, free flow of goods, services, labour and capital.<sup>16</sup> Together with the Dominican Republic CARICOM is linked to the EU via an Economic Partnership Agreement, which began in 2013. It also has a special FTA with the United States (the Caribbean Basin Initiative, CBI).

53. The CARICOM has already been active in using regional aid for trade in order to foster regional integration and strengthen co-operation. In December 2012, it launched the Caribbean Community Regional Aid for Trade Strategy 2013-2015, which outlines its regional aid for trade priorities and objectives over the next few years. It notes that, despite the best of intentions in terms of economic co-operation, its intra-regional economic interaction is operating at less than 50% of what it could—and should—be. It notes that, “the Region’s efforts to carve out a trade-led economic growth path have been beset by poor economic infrastructure, low and declining competitiveness, weak institutions, fragmented production systems and limited productive capacity,” that is, many of measures noted above that can be addressed by effectively-targeted aid for trade. Indeed, using regional aid for trade to increase value-added in production is a salient priority in the Strategy.

***What do partners report as the main challenges?***

54. Responses from regional organisations to the 2011 OECD/WTO monitoring survey highlighted what they believe to be the most important impediments to trade, both in intra- and extra-regional contexts. The results are summarised in Table 1. In general, the survey revealed that competitiveness, limited export diversification and inadequate transport links are deemed to be the most important impediments to intra- and extra-regional trade, with significant overlap across the two categories. Soft and hard infrastructure-related issues appeared across all regions, with trade finance and limited export diversification also being significant constraints for several regions. Standards and compliance issues also appeared frequently, especially in the external trade of most African sub-regional organisations and CARICOM.

55. In addition, their responses highlight differences in perception between organisations even in the same region. For example, the three regional economic communities whose membership spans West African states answered quite differently regarding the most important constraints to intra-regional trade. The regulatory environment is a key constraint to intra-regional trade according to ECOWAS and external trade for TTCA-NC, but this is not the case for SADC (or OECS). Limited access to trade finance was significant for intra-regional trade of SADC and OECS and external trade of the latter. Competitiveness figured highly everywhere except ECOWAS. In addition, the cost of transport services was important according to ECOWAS but not to the other regional groupings. It is difficult to explain these differences in perception, but perhaps it is an interpretation problem; for example, the costs of transport services raises costs and reduces competitiveness.

56. In any event, according to the questionnaire the most important constraints affecting intra- and extra-regional trade pertain to trade-related policies and trade facilitation, trade finance, transport links, limited export diversification, and low regional demand. As is clear from the 2013 WTO-AU-UNECA surveys and the regional case stories (Section 5), regional aid for trade has proven to be effective in addressing all these issues, with the exception of trade finance.

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<sup>16</sup> For details on the Single Market and Economic, see:  
[http://www.caricom.org/jsp/single\\_market/single\\_market\\_index.jsp?menu=csme](http://www.caricom.org/jsp/single_market/single_market_index.jsp?menu=csme)

Table 4.1. Overview of constraints to intra- and extra-regional trade

Regional Organisation	Most important constraints to intra-regional trade	Most important constraints to extra-regional trade
CARICOM	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Limited export diversification</li> </ul>	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Limited export diversification</li> <li>• Inadequate transport links</li> <li>• Standards compliance</li> </ul>
CEN-SAD	<ul style="list-style-type: none"> <li>• Low regional demand</li> <li>• Competitiveness</li> <li>• Limited export diversification</li> </ul>	<ul style="list-style-type: none"> <li>• Low regional demand</li> <li>• Competitiveness</li> <li>• Cost of export</li> </ul>
ECOWAS	<ul style="list-style-type: none"> <li>• Regulatory environment of doing business</li> <li>• Inadequate transport links</li> <li>• Cost of transport services</li> <li>• Limited access to trade finance</li> </ul>	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Limited export diversification</li> <li>• Standards compliance</li> </ul>
OECS	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Inadequate transport links</li> <li>• Limited access to trade finance</li> <li>• Standards compliance</li> </ul>	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Inadequate transport links</li> <li>• Limited access to trade finance</li> <li>• Standards compliance</li> </ul>
SADC	<ul style="list-style-type: none"> <li>• Low regional demand</li> <li>• Competitiveness</li> <li>• Limited export diversification</li> <li>• Inadequate transport links</li> <li>• Customs and border procedures</li> <li>• Informal restrictions</li> </ul>	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Limited export diversification</li> <li>• Cost of export</li> <li>• Customs and border procedures</li> <li>• Informal restrictions</li> </ul>
TTCA-NC	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Regulatory environment for doing business</li> <li>• Inadequate transport links</li> <li>• Standards compliance</li> <li>• Customs and border procedures</li> <li>• Informal restrictions</li> </ul>	<ul style="list-style-type: none"> <li>• Competitiveness</li> <li>• Limited export diversification</li> <li>• Inadequate transport links</li> <li>• Cost of export</li> <li>• Access to trade finance</li> <li>• Standards compliance</li> <li>• Customs and border procedures</li> <li>• Informal restrictions</li> </ul>

Source: 2011 OECD/WTO questionnaire

#### 4 Regional Aid for Trade as an Efficient Catalyst of Value Chains

57. For developing economies to attain the benefits of regional integration and co-operation, they must address a variety of market failures and constraints. This is where multi-country and regional aid for trade can play an important role. As is evident in the regional aid for trade case stories (OECD/WTO, 2013) and the 2013 WTO-AU-UNECA Survey, there are many areas in which regional aid for trade is efficiently and effectively addressing bottlenecks to closer bilateral and regional integration, be it in the context of a formal regional accord or otherwise.

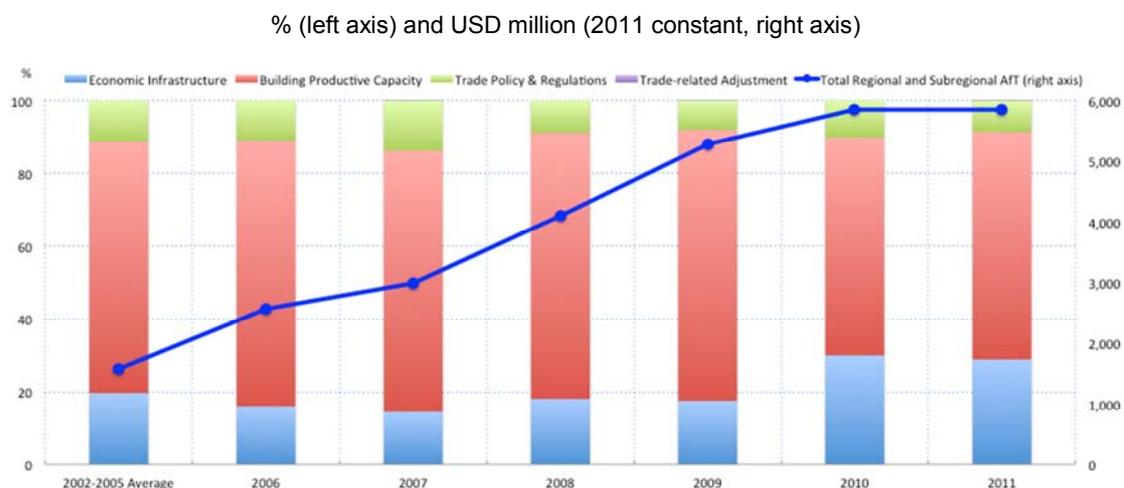
58. Regional aid for trade can play a cost-effective role in supporting regional integration and co-operation. It constitutes a critical area in which donor and recipient countries can get the “biggest bang for the buck”. This begs the question as to the extent to which recipient and donor countries have thus far responded to the evident need for regional aid for trade. How has regional aid-for-trade fared in terms of growth in aggregate flows? How do they compare to overall aid-for-trade flows? Which sectors are receiving the most regional aid-for-trade flows? And, have there been significant regional differences in the distribution of regional aid for trade flows at the regional level?

59. Chapter 2 notes that, while aid-for-trade commitments continue to be strong relative to the 2002-05 baseline, they have been declining of late, concomitant with overall development assistance. While aid for trade has fared reasonably well during this difficult period, some cutbacks were, perhaps inevitable. This highlights the importance of ensuring that aid for trade is as efficient and effective as possible. The remainder of this section considers trends in multi-country and regional aid for trade at the sectoral level and the next section provides examples of regional aid for trade in action. These experiences underscore the beneficial role of regional aid for trade in supporting the economic co-operation process.

##### *Trends in Regional Aid-for-trade Flows*

60. Chapter 2 gives a thorough overview of the trends in overall aid-for-trade flows in the context of aggregate official development assistance flows. Regional and sub-regional aid for trade—as defined in the CRS—constitutes a relatively small share of total aid-for-trade flows, but it has been rising. In 2002-2005, total disbursements under regional and sub-regional aid for trade came to slightly over USD 1.5 billion (on average). In 2011 they rose to roughly USD 5.8 billion. Hence, the share of regional and sub-regional aid for trade in total aid for trade has grown from about 9% in 2002-2005 to 12% in 2006 and 18% in 2011. While total aid for trade flows grew by about 50% over the 2006-2011 period, regional and sub-regional aid for trade increased by 2.5 times as much.

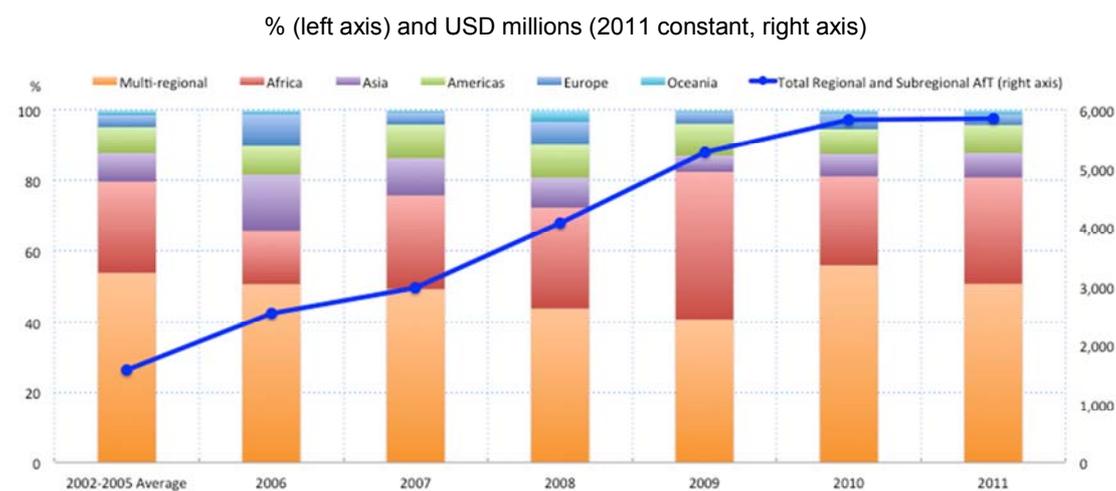
61. At the sectoral level, there are significant differences in regional and sub-regional aid for trade flows compared to overall aid for trade. Since 2002, building productive capacity has consistently been the most important component of regional and sub-regional aid for trade by far. The share of disbursements to this sector remained fairly stable over the period 2002-2009, in the range of 69-74%. However, building productive capacity experienced a decline of roughly 12 percentage points from 2009 to 2011, mostly in favour of economic infrastructure and, to a lesser extent, trade policy and regulations (Figure 4.1).

**Figure 4.1. Share of regional and sub-regional aid for trade disbursements, by sector**

Note: Data extracted 15 April 2013

Source: OECD/DAC Creditor Reporting System (CRS)

62. Figure 4.2 presents data for total and regional and sub-regional aggregates by region. Aggregates for Africa, Asia, the Americas, Europe, Oceania, and a “multi-regional” category are included. The distribution of aid for trade disbursements differs widely across the total and regional and sub-regional categories, as one would expect given the nature of regional and sub-regional flows. The multi-regional category is the largest and reflects projects related to: (1) South-South co-operation, which has been increasing in importance in recent years; and (2) multi-country aid for trade flows allocated to countries with similar needs but not determined by geography.

**Figure 4.2. Share of regional and sub-regional aid for trade disbursements, by region**

Note: Data extracted 15 April 2013

Source: OECD/DAC Creditor Reporting System (CRS)

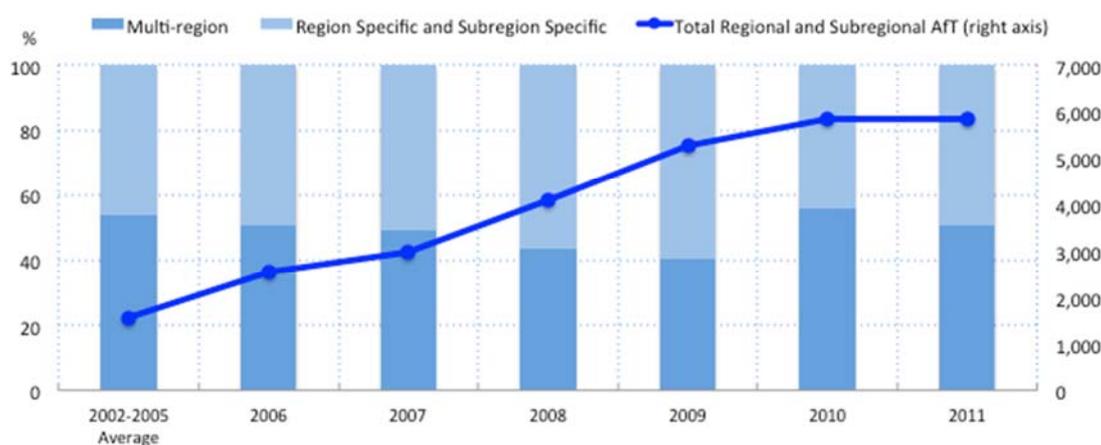
63. At the regional and sub-regional level, the share of aid for trade disbursed to Africa is on average four times that disbursed to Asia (with the exception of 2006, when shares across the two regions were

roughly equal and 2007 when shares in Asia were approximately 2.5 times higher): shares of regional and sub-regional aid for trade disbursements range from 4 to 16% in Asia compared to 25 to 42% in Africa. This is no doubt a reflection of the high priority placed on regional integration by African leaders.

64. Figure 4.3 breaks down regional and sub-regional aid for trade flows into “multi-region” and “region and sub-region specific” categories. In both 2010 and 2011, the distribution was roughly equal. This is consistent with the 2002-2005 benchmark years but in contrast to the 2008-2009 period when region and sub-region specific flows received a greater share, in the range of 56-60%.

**Figure 4.3. Regional and sub-regional aid for trade disbursements, by regional category**

% of total regional and sub-regional AFT (left axis) and USD millions (2011 constant, right axis)



Note: Data extracted 15 April 2013.

Source: OECD/DAC Creditor Reporting System (CRS)

65. In sum, the share of regional and sub-regional aid for trade flows has increased since the 2002-05 baseline, in spite of a slight decrease in dollar amounts of total and regional flows in 2011. Nevertheless, with an aggregate value of slightly less than USD 6 billion in this same year, regional aid for trade continues to be relatively small, particularly given its potential as noted above and its proven effectiveness as described in the next section.

66. Although the composition of these flows has changed somewhat over time, the “building productive capacity” and “economic infrastructure” sectors have consistently dominated regional flows. The literature on “binding constraints to trade” suggests that this focus is well-merited, and case studies reviewed below display a number of successful projects. Still, trade facilitation, more efficient and practical accommodating policies, and facilitating structural change are increasingly important to successful development strategies in general and regional co-operation and integration in particular. As such, they constitute potentially high impact areas for future regional aid for trade programmes.

## 5 Case Stories of Regional Aid for Trade in Promoting Value Chains

67. The above makes a strong case in favour of regional aid for trade as an effective way of lowering barriers to the creation and expansion of production networks and facilitating participation in value chains. However, realising the potential of regional aid for trade requires effective development planning in which regional projects are mainstreamed effectively in national development programmes. Herein lies the crux of the problem; it is often difficult for national governments to devote scarce financial resources to projects

with strong externalities but whose benefits cannot be appropriated nationally. Consequently, much of the focus in the aid-for-trade initiative has been at the national level; instruments to support multi-country and regional programmes are less well-developed. Coupled with declining ODA resources globally, augmenting regional aid for trade poses many challenges. But the above analysis strongly supports the notion that increasing regional aid for trade will pay rich dividends; well-targeted regional aid for trade can go a long way in offering firms in developing countries a stepping-stone towards international production networks, regional integration and competitiveness globally.

68. There is ample empirical evidence that this is the case. In July 2010, the OECD and WTO solicited case stories for the *Global Review of Aid for Trade 2011* from interested stakeholders (OECD/WTO, 2013). About 10% of the case stories submitted could be classified as multi-country or regional aid for trade projects, somewhat less than the share of regional aid for trade in total aid for trade flows. Below, we summarise some of the key case stories and other projects pertinent to how regional aid for trade can contribute to production networks and deepening involvement in value chains.<sup>17</sup>

### *Insights from the Regional Case Stories*

69. In order to organise the case stories systematically, this section divides the projects into several categories: economic infrastructure, trade facilitation, trade-related policies, building productive capacity and value-chain promotion. One should note, however, that this is done for convenience rather than by economic design or priority. Indeed, many projects would comfortably fit under more than one category and all projects below have played an important role in addressing some binding constraint to regional integration and production networks.

### *Economic Infrastructure*

70. As noted above, insufficient economic infrastructure constitutes a key constraint on regional economic integration and value chain creation in emerging and developing economies, and LICs in particular. The case stories underscore that regional aid for trade for economic infrastructure projects and programmes must unavoidably rely upon close pluri-national coordination, and this creates a veritable web of various government agencies and external stakeholders whose relationships need to be closely managed, requiring a careful balancing of their political and economic interests. Gaining traction with so many stakeholders and maintaining momentum is difficult, increasing the importance of high-level political commitment and support. Economic infrastructure requires some form of on-going funding and accompanying capacity-building measures in order to ensure that they are managed effectively and sustainably into the future, but also to fully realise the potential gain that can be delivered by removing bottlenecks, developing critical transport corridors and strengthening information and communication technology backbones. These are all essential to promoting production networks and moving up the value chain.

71. *The Nacala Corridor Economic Development Strategies* programme, funded by the Japanese International Cooperation Agency (JICA) in close co-operation with the Government of Mozambique and with the financial participation of the African Development Bank, is an example of a successful project that aims to develop soft and hard infrastructure in order to promote extractive value chains and value added through business services.<sup>18</sup> The Nacala Corridor has historically been an important transit corridor in South-eastern Africa, but was disrupted due to the civil war in Mozambique that ended in 1992. With

<sup>17</sup> Before beginning, we might note that these are case *stories* as opposed to case *studies*; that is, they tend to be descriptive and informational rather than analytical. Benefit-cost analysis was not part of the exercise, for example.

<sup>18</sup> See: <http://www.jica.go.jp/project/english/mozambique/002/outline/index.html>

infrastructure in ruins, the corridor became an important priority for international donors. This programme seeks to formulate an integrated development strategy for the Nacala Corridor and create an effective planning framework. It takes both a regional approach, including regions in Mozambique and connections to neighbouring Zambia, Tanzania and Malawi; and a sectoral approach, including logistics, tourism, mining, industry, forestry, agriculture, water resource, electricity, communication, social infrastructure and transport infrastructure, enabling the programme to prioritise and formulate projects in an integrated way. In addition to improving available databases in areas relevant to both social development and business, the programme has reviewed development plans, prioritized development projects and public and private investments, analysed capacity constraints, and identified constraints to development in the Nacala Corridor, with a view to informing project selection and planning.

72. Founded in 2001, the Central Asia Regional Economic Cooperation (CAREC) programme is composed of 10 Central Asian countries (including China) and is supported by 6 multilateral institutions with the goal of enhancing economic development via regional co-operation.<sup>19</sup> It boasts regional projects in transport, economic corridor development, trade facilitation, energy, and trade policy, with 140 projects worth USD 21 billion to date. Arguably the greatest benefits thus far have been in the area of “better connectivity,” reducing the cost of doing business at home and across the CAREC region and stimulating trade.<sup>20</sup>

### ***Trade Facilitation***

73. As noted in Section 2, trade facilitation has an important bearing on the creation of production networks. Lowering costs to economic integration via trade facilitation is frequently cited by the private sector as a top priority in enabling production networks and boosting international trade, as well as ensuring that efficiency improvements in hard infrastructure translate into lower costs. Regional aid for trade can play a catalytic role in reducing these barriers to interchange.

74. Various trade facilitation initiatives under the APEC framework offer excellent examples of how regional co-operation can lower the costs of economic interaction and promote value chains.<sup>21</sup> APEC economies were able to lower business transactions costs across the region by 10% via two Trade Facilitation Action Plans over the 2002-2010 period. It has also promulgated a Single Window Action Plan (2007) for customs and an APEC webpage on tariffs and rules of origin (“WebTR”). In addition, it created an APEC Business Travel Card that reduces costs of business travel by allow travel without visas and special express lanes at airports.

75. In the Americas, the FTA between the United States, Central America and the Dominican Republic stressed the importance of trade facilitation and associated Ministers launched the Trade Facilitation Initiative in 2011, with the goal of identifying key barriers to economic interchange in the region.<sup>22</sup> The three central areas were: customs and trade facilitation; logistics and the supply chain; and technical standards, including SPS. Surveys of stakeholders found that the areas requiring the most improvement were: customs administration, including risk management; logistics and related infrastructure; the need for integrated border management; and heavy bureaucracy at the borders. Such regional co-operation is effective in helping the region prioritize the greatest challenges to regional integration.

<sup>19</sup> See: <http://www.carecprogram.org/index.php?page=carec-development-effectiveness-review>

<sup>20</sup> For a “stock taking” of progress after ten years, see: <http://www.carecprogram.org/uploads/events/2010/9th-MC/Draft-10Year-Commemorative-Study-Main-Text.pdf>

<sup>21</sup> See: <http://www.apec.org/About-Us/About-APEC/Achievements-and-Benefits.aspx>.

<sup>22</sup> See: <http://www.iadb.org/intal/intalcdi/PE/2013/11612.pdf>.

76. In addition, the *International Transit of Goods* programme, launched in 2008 by the Inter-American Development Bank (IADB), created a single electronic document to be used at the El Amatillo border crossing between Honduras and El Salvador, which has the highest volume of trade in Central America, with the goal of simplifying and harmonising border processes.

Another project related trade-facilitation cost reduction has been spearhead by Trademark South Africa (TMSA). At the Chirundu border crossing, Africa's first one-stop border post (OSBP) along the North-South Corridor, trade facilitation improvements are evident in transit cost reductions for the private sector and increases in government tax collection: between June 2010 and June 2012 border crossing time fell by 36% to an average 25 hours, while during the same period, the border post became much busier, with the number of vehicles increasing by 65%. As a result, the private sector was averaging savings due to faster transit times of about USD 20 million per month by mid-2012. Without increasing tax levels, more efficient customs operations lead to a doubling in the Government of Zambia's trade tax from 2009 to 2012.

### ***Trade-related Policies***

77. As noted in Section 4, the trade policy and regulations sector is relatively small compared to economic infrastructure and building productive capacity. It includes projects related to trade policy and administrative management; trade facilitation; regional trading agreements; multilateral trade negotiations; trade education and training; and tourism policy and administrative management.<sup>23</sup> In other words, this sector considers part of the "soft" infrastructure for regional co-operation and integration. Nevertheless, the OECD/WTO UNECA surveys reviewed above stress the importance of improving trade-related policies in order to boost regional integration and competitiveness.

78. Hence, regional aid for trade in the "trade policy and regulations" area can be important in facilitating intra-regional integration and building "soft" capacity in government agencies. While at present the allocation of regional aid for trade to trade policy and regulations is not high, it has great potential for the future, particularly as new configurations of regional trade arrangements emerge, e.g., the proposal for the pan-African FTA and the RCEP noted above. Moreover, the potential gains from greater trade facilitation in multi-country and regional contexts will also render this area increasingly attractive in terms of aid for trade.

79. The Caribbean Aid for Trade and Regional Integration Trust Fund (CARTFund): A Mechanism for Delivering Aid for Trade Support to CARICOM and CARIFORM States (CARICOM) programme, also supported by the UK and administered by the CARICOM and CARIFORUM, started in 2009 as a demand-driven mechanism to support Caribbean implementation of EPAs with Europe and the CARICOM Single Market and Economy. By 2011, 18 projects had been approved in eight CARIFORUM states, of which five were regional and 13 national projects, accounting for approximately 70% of available funding with demand surpassing available resources. The establishment of the fund is especially notable as it is truly a joint effort across donor and recipient regional organisations.

80. The economic literature suggests a clear link between FDI, intellectual property protection (IPR), and moving up the value chain (e.g., Park and Lippoldt, 2008). However, there are often misconceptions regarding the desirability of IPR protection, and this has sometimes led to policies that have reduced the potential for attracting regional production networks. The *OAS Intellectual Property Value Capture Export strategy* project, sponsored by the Organization of American States (OAS), programme endeavours to increase awareness on the part of domestic and regional actors regarding potential increases in export

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<sup>23</sup> In the CRS database, it also includes trade-related adjustment, but this component is negligible in size in terms of regional aid-for-trade flows.

income through the use of intellectual property (IP) strategies. Key to the success of this programme is the involvement of both local and regional stakeholders in selecting the products; the inclusion of the private sector in the process and in the training module; the sequencing of the programme within each of the phases; and the final output of the methodology that can be used within the Caribbean to support additional products, as well as in other regions.

81. The lack of harmonisation of standards- and conformance-related policies can impede the functioning of regional production networks as well. The German-financed *Establishing a Regional Quality Infrastructure (QI) in the East African Community (EAC)* project is designed to improve the regional quality infrastructure (QI) in East Africa, which involves standardization, quality assurance, accreditation and testing. The project, which runs from 2004-2013, began working on the establishment of a regional QI that was compatible with the WTO requirements. A Standards, Quality, Metrology, Testing Act was passed in the EAC in 2007 and established the framework for harmonisation of standards and coordination of activities. A regional QI system was created nearly from scratch: 1,100 standards were harmonised, though they have not been fully adopted at national levels; a pool of trained assessors for the accreditation of medical, testing and calibration laboratories was created, and an East African Accreditation Board was established in 2009; capacities for regional harmonisation of inspection procedures and product certification have been developed; and metrology laboratories have improved in all EAC countries.

82. The COMESA-EAC-SADC Tripartite Non-tariff barrier (NTB) notification and resolution system is web-based, but has been made accessible to the entire spectrum of traders through the use of a mobile phone functionality. Furthermore, the system has been embedded solidly in regional economic community, national government and private sector institutional structures and approaches. By the end of March 2013, 73% of NTB complaints had been resolved, often within days or weeks rather than the lengthy periods (months and even years) experienced in the past. The most frequently logged complaints include those related to lengthy and costly customs procedures throughout the Tripartite region; issues related to the application of rules of origin; costly road user charges and issues related to the application of sanitary and phytosanitary standards. Lifting a ban on cross-border buses and heavy vehicles through the Kariba Border Post, has, among other things, boosted small-scale trade; increased the volume of cross-border trade; reduced travel and transit times; and boosted employment and clearing capacity.

### ***Building Productive Capacity***

83. From the case stories, it is clear that engaging and mobilising the private sector constitutes a key but constant challenge when building regional productive capacity.<sup>24</sup> Yet, the private sector constitutes the basic core of international and regional integration and production networks. Regional aid for trade projects are quite effective in addressing some of the greatest difficulties faced by the private sector in developing regions.

84. For example, the EU-sponsored *Caribbean Trade and Private Sector Development Programme (CTPSD) – Phase II Caribbean Export Component* contributed to the Caribbean Export Development Agency (“Caribbean Export”), which is a regional export and trade promotion agency, to support the private sector in the signing of the EU and CARIFORUM Economic Partnership Agreement. The programme’s aim was to work at the regional level to use regional organisations more effectively to achieve the goals of strengthening export capacities within the region. Involving Caribbean Export as a partner was deemed to be a key to the success of the programme, as it was an established regional

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<sup>24</sup> In the CRS database, building productive capacity includes projects related to banking and financial services; business and other services; and agriculture, forestry and fishing.

organisation prior to the programme and already had important partnerships with public and private sector participants at the regional level.

85. An interesting example of a more advanced developing economy sharing its experiences in order to promote best practices at the regional level is the OAS-sponsored *Strengthening the Official Sanitary System of Agricultural Goods for Export Markets in CARICOM Member States* programme. The Government of Chile, through the Secretariat of the OAS, shared its Sanitary and Phytosanitary Standards (SPS) management rules and practices with the CARICOM countries. The success of this programme demonstrates the effectiveness of South-South co-operation.

86. The Canadian-sponsored *Program for Building African Capacity for Trade (PACT)* was a joint project implemented by the ITC, the Trade Facilitation Office Canada and various African organisations, with the objective of expanding and diversifying exports in the recipient African countries and building SME export capacity. The programme focused on offering training in export readiness and information and communications technology-based delivery of market information, expert advice on market readiness and market access missions. The programme resulted in an increase in exports to Europe, which included small farmers in Africa gaining access to European markets and Canada. Additionally, the programme facilitated the introduction and export of the Design Africa brand in home furnishing products to the EU, Canada and the US. Furthermore, Access! African Businesswomen in International Trade provided export training and business counselling for women. At least 100 entrepreneurs completed two years of export preparedness seminars in the initial four countries and were selected to participate in trade missions and/or attend trade fairs. Of those, the study reports 50-60% established business linkages with a distributor in the importing country, and 20% actually received orders or were in the process of doing so.

### ***Value-Chain Promotion***

87. Each of the above case stories had a direct or indirect bearing on improving prospects for integration into value chains. However, there were also several case stories that identified the promotion of value chains as their primary purpose.

88. For example, the *Exports Promotion & Enterprise Competitiveness for Trade (ExPECT) Initiative*, directed by ECOWAS, was launched in 2010 to develop and promote high export potential value chains. The EXPECT programme was designed to ensure the region's ownership and the sustainability of PACT II (*Programme for Building African Capacity for Trade*). The Initiative aims to create and strengthen the technical, managerial and institutional structures and capacities to help achieve the region's trade development agenda in the area of value chains. Thus far, the project has led to a large financial commitment from the ECOWAS Commission and ICT/PACT II for implementation support for 2011-2013; the development of a results-based 2011 workplan developed by ECOWAS-10; and a mango value chain analysis that involved both the private and public sectors from the region in order to develop a regional mango strategy, among others. In 2011, the programme was scaled up to include implementation of clusters to increase SME competitiveness in the EXPECT-selected value chains for mango, cashew and palm oil; validation of the regional mango strategy at the national level and completion of the process for a second good; and the first ECOWAS Export Actors Forum to discuss priorities for export value chain development and competitiveness.

## **6 Conclusions**

89. The above analysis comes to the following general conclusions: (1) regional production networks are becoming increasingly important to the success of the trade agenda of developing economies; (2) in addition to increasing trade performance and generating many of the same gains that accrue from a more open trade and investment environment, participating in regional production networks can serve to reduce

poverty, increase employment and eventually help countries move up the value chain; (3) outward-oriented regional economic co-operation can be used as an effective strategy to promote integration into value chains and enhance regional integration; and (4) regional aid for trade can be an efficient protagonist of regional integration and value chains. The increasing share of regional aid for trade in overall aid for trade flows, coupled with responses to the 2013 WTO-AU-UNECA Survey, underscore the rising awareness among partners and donors about the effectiveness of regional aid for trade in meeting trade and development goals.

90. The OECD/WTO publication *Aid for Trade at a Glance 2009* highlighted the great impact that regional aid for trade projects can have, but also the problems associated with regional projects. In particular, it delineated two major challenges for the future: the need for better coordination at the regional level, and for strengthening human and institutional capacities. Concerning the first challenge, this chapter identified three key problems: (i) weakly articulated demands for regional aid for trade; (ii) lack of coherence between national and regional priorities; and (iii) lack of effective coordination at the regional level. Concerning the need for strengthened capacities, this chapter highlights that RECs have widely varying institutional and human capacities, which has significant ramifications for absorptive capacity for regional aid for trade. Moreover, the existence of multiple and overlapping regional integration arrangements and organisations can make establishing a stable donor-recipient relationship difficult.

91. From the 2013 WTO-AU-UNECA Survey for Africa and the case stories reviewed above, it would appear that there has been substantial progress since 2009 in articulating demands for regional aid for trade and in fostering closer co-operation between donors and partner countries, though there is room for improvement. Strengthening the coherence between national and regional priorities remains a medium/long-term challenge, however. Enhancing the capacity of human and institutional capacities is also a medium/long-term challenge in the development process. However, donors and regional organisations have placed a strong emphasis on relaxing this constraint with considerable success, and the movement toward mega-regional arrangements, especially in Asia and Africa, should reduce problems of overlapping arrangements.

92. It is difficult to generalise regarding the experiences from regional projects and programmes, as they are so diverse in terms of their objectives, contextual situation, country composition and size. However, research and surveys undertaken by the OECD, WTO and other international organisations suggest that the “recipe for success” would be:

- Emphasising *ownership* on the part of stakeholders needs to be a high priority in order for the project to be successful.
- Related to point (1), ensuring active ‘buy-in’ on the part of stakeholders in order to ensure that a project will have support throughout its life. This is particularly important for regional and multi-country projects.
- Consistent and corrective monitoring and evaluating regimes need to be incorporated into project design, allowing comparisons across the regional/national dichotomy. CAREC is an example of best practice in this regard.
- Projects need to have clear, realistic goals. Timing needs to be practical and realistic but not overly conservative. However, there also needs to be sufficient, built-in flexibility to manage unanticipated events.
- While different projects have different goals, sustainability should be an important consideration for most projects, particularly in the economic infrastructure category.

- In regional aid for trade projects, particularly in the economic infrastructure and building productive capacity sectors, it is important to engage the private sector and other non-government-affiliated partners, a point that was underscored in the WTO-AU-UNECA partner survey.

93. While regional aid for trade projects are inherently complex because of the need to involve and coordinate multiple governments, their various agencies and a great multitude of private stakeholders, they constitute a cost-efficient approach to helping developing economies meet their trade and development objectives. At a time when fiscal budgets in donor countries are stretched, regional aid for trade offers an excellent example of producing large benefits for any given outlay.

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