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Report of the Multi-year Expert Meeting on Promoting Economic Integration and Cooperation on its third session

Held at the Palais des Nations, Geneva, on 2 and 3 July 2015

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Contents

I. Chair's summary

1. The third session of the Multi-year Expert Meeting on Promoting Economic Integration and Cooperation was held at the Palais des Nations in Geneva on 2 and 3 July 2015 as per the terms agreed by the Trade and Development Board at its fifty-seventh executive session on 26–28 June 2013.

A. Opening statement

2. The Deputy Secretary-General of UNCTAD, in his opening remarks, emphasized that the sustainable development goals involved an entirely new, comprehensive and coherent blueprint for development. To achieve the world we want by 2030 would require a profound transformation of the way we produce and consume, and in that process an important role would be played by a closer subregional, regional and interregional cooperation.

3. The speaker noted that international trade in the two decades prior to the crisis of 2008 expanded more than twice as fast as global output, and hundreds of millions of people were lifted out of poverty. But since the crisis, international trade had barely kept up with the world economy's new, slower pace of growth. Data for the first quarter of 2015 showed trade values declining for many countries. Given this sluggish global environment, regional markets were even more important than in the past. Regional integration, with the goal of boosting trade growth, was increasingly central to many countries' development strategies. Regional integration could also structurally transform economies to improve the lives of everyday people.

4. Given that there was a need to scale up regional cooperation among developing countries, the crucial question was how this could be accomplished. Too many regional initiatives had so far been top-down in nature, and so the main challenge they had faced was implementation. A lot of processes and activities had often had little outcome. A bottom-up approach may be needed to include all stakeholders, from villages, districts, provinces and cities to promote a meaningful regional integration. Concerted small steps towards integration were critical in building momentum.

5. The Deputy Secretary-General said that a closely related issue was how to mobilize finance for increased regional cooperation. The global investment landscape had been changing rapidly and tectonic shifts were underway. Developing Asia was now the largest source and destination of foreign direct investment. Additionally, foreign direct investment flows to developing economies had reached their highest level in 2014, and at $680 billion were $200 billion higher than those to developed economies. The foreign direct investment stock had tripled in least developed countries and small island developing States, and quadrupled in landlocked developing countries. This growing tide of investment in and from developing countries had to be harnessed for regional cooperation and integration, for example through investment in physical infrastructure and regional technology hubs. It had been calculated by UNCTAD that developing countries faced a current investment gap of $2.5 trillion annually for the fulfilment of the sustainable development goals.

6. The speaker said that one possible way to finance this gap would be to involve private investors more closely. With a low-interest environment, profit-seeking private firms and institutional investors had more incentive than before to invest in infrastructure. However, that would not be enough. Development banks, especially regional ones, would also have to contribute to filling the important financing gap for developing regional infrastructure. Recently, initiatives had appeared to set up regional development banks such as the New Development Bank, the Asian Infrastructure Investment Bank, and the Bank of the South.

B. Strengthening subregional, regional and interregional dialogue and cooperation and their contributions to economic integration and development

(Agenda item 3)

Under what conditions could trade become a growth engine in a process of regional integration?

7. In the first part of the meeting, the experts discussed the role of international trade in the post-2008 crisis period. They made reference to UNCTAD's analytical considerations on the state of the global economy and the need to rebalance growth towards domestic and regional demand. This global framework was then analysed regionally, with specific reference to Asia, the newly formed Eurasian Economic Union, and Africa, as well as established industrial economies. Industrialization was highlighted as the key to the success of regional processes. Trade agreements were considered to be an essential component and had resulted in certain new industries coming into existence in regions where they had been previously absent. In this context, the concept of development integration was discussed as an alternative to the traditional, linear model of integration. This concept, introduced in Africa, sought to foster the development of regional value chains combining market opening with cross-border infrastructure development and rehabilitation, and inter-governmental coordination, notably on industrial policy.

8. Rising incomes depended on rising productivity, which in turn depended on establishing industries and reinvestment of profits that led not only to specialization but diversification based on intra-industry trade. The strategic role of intra-industrial trade was emphasized by two of the panellists. This required industrial policy at the national level for countries throughout a given region. Western Europe and developing Asia, mainly East Asia, had succeeded in industrial development over the last fifty years and also had high intraregional trade.

9. Participants noted that intraregional trade represented only 14 per cent of the total trade of African countries. However, if informal intra-African trade was accounted for by the statistics, it would equal that of Latin America, at 22 per cent. In contrast, regions that had succeeded in industrial development had recorded much higher figures. Intraregional trade in East Asia was around 52 per cent of the total trade of these countries, and in the European Union that figure was around 65 per cent. Nevertheless participants also noted that, despite being relatively low, intra-African trade was composed by higher value added products as compared with extra-African flows. This in turn suggested that regional integration in Africa was of crucial importance to achieve economic diversification.

10. In the absence of industrialization in Africa, several panellists discussed the unlikelihood of establishing strong regional economic ties that could lead to virtuous cycles of trade and growth. Africa's fragmentation was considered to be a barrier to economic development, and it was stressed that there needed to be capacity to benefit from open regional arrangements. The Chair considered that UNCTAD's *Economic Development in Africa Report 2013. Intra-African Trade: Unlocking Private Sector Dynamism* continued to have pertinent messages in this area. Most notably, weak productive capacity meant that there was not much to trade, therefore building productive capacity was a precondition for a more robust intra-African trade. Numerous African free trade agreements were acknowledged as commendable by one discussant, with customs unions and ease of movement of goods and labour mobility already achieved in some subregions. Progress in transport and infrastructure had also been made, but low growth rates persisted.

11. One of the panellists presented the Eurasian Economic Union as an important new experience that was founded partially on the European Union model, but emphasizing, in addition to a free trade zone and customs union, a trade integration with the aim of achieving regional integration for development. Important gains in trade had been made with the newly formed customs union and the elimination of border controls. Intraregional trade had doubled over the course of two years, while subsequent declines mostly reflected changes in oil prices. What was considered more serious for intraregional trade was the slowdown in economic growth in 2015.

12. The key to the political success of the Eurasian Economic Union was its foundation on equal representation of countries in the union, regardless of size, as well as the consensus-oriented basis upon which it took decisions and the one-vote-per-country arrangement. One of the panellists cited UNCTAD's methodology for eliminating trade barriers as very useful for the establishment of the Union, which aimed to achieve a single economic space for goods and services without barriers by 2025. A step-by-step sectoral approach would be pursued to achieve this aim for both identified strategic manufacturing sectors and in the financial sector.

13. Regional financing institutions were considered to be a vital component for growth and trade by all panellists in order to provide necessary long-term financing for development strategies. Scaling up these institutions was a key challenge. The remarkable size of the European and Brazilian development banks was mentioned by one panellist, particularly as they dwarfed disbursements of the World Bank in investments in infrastructure.

14. The issue of trust between members of the regional integration process was raised by two discussants and further addressed by the panellists. There was an inherent trade-off involved in regional cooperation that relinquished to a certain degree national autonomy and curtailed the policy space of national policymakers. Two panellists considered that this relationship required strategic thinking and assessment to set a good balance between external and internal integration: while development by definition implied building up national capacity, this required policies that extended beyond national boundaries.

Productive integration as the basis of development-oriented regional integration

15. In the second part of the meeting, the experts discussed the role of regional productive integration as a key driver of development and catch-up growth. The experts emphasized the importance of the manufacturing sector and of industrialization for economic growth. They suggested that advanced economies had all relied on a significant expansion of manufacturing output and employment during their initial economic phases, and that growth in manufacturing employment in particular was one of the best predictors of future income growth. Participants also suggested, however, that industrialization and manufacturing sector expansion had become harder today; in the last two decades many fast-growing developing economies had in fact experienced marked manufacturing output growth without any significant expansion of the workforce in the sector. It was observed that this was partly explained by the nature of technological progress, which was less labour intensive than in the past and allowed for footloose investment.

16. It also emerged from the discussion that services could not be expected to deliver rapid growth and good jobs in the way that manufacturing had done in the past. Services tended to be technology and capital intensive and could therefore absorb only a fraction of the labour supply. Furthermore, most services were closely linked to manufacturing activity (for example, banking and logistics) and could not be expected to grow in isolation. For developing economies today it would be, therefore, relatively more difficult than in the past to take off and catch up with present industrial leaders. This would require a constant upgrade of the production structure towards products with high value added and high income elasticities of demand, which would be possible only if developing economies could find market niches based on product innovation.

17. According to the experts, regional value chains could play a critical role in raising competitiveness and upgrading production in developing countries. While global supply chains had facilitated entry into manufacturing, they had also reduced the gains in terms of value added that accrued to the developing economies. Regional value chains, on the contrary, provided higher per unit returns (as they did not entail high fixed costs) and offered more possibilities for branding and capturing value. The experts presented the estimates of a dynamic gravity trade model applied to the leather sector in Africa and South Asia; they showed how regional trade could be doubled in both regions and, if tariff and other barriers to trade were removed, gains could be even bigger.

18. The question of what kinds of policy intervention were needed to fully exploit the potential benefits offered by regional trade and regional value chains was discussed. The experts focused their attention on three key areas for policy action: financial cooperation and integration; physical integration; and trade facilitation. In terms of financial cooperation, discussants highlighted the importance of reducing regional financial transaction costs, enhancing regional information systems and tailoring the financial instruments towards the different types of value chains in place (buyer driven, producer driven or integrated through the lead firm). It was also suggested that regional financial institutions should provide funds to overcome capacity constraints, through, for example, the implementation of regional training/skill-development facilities, should encourage the harmonization of financial regulation at the regional level, and favour regional branding.

19. Experts also insisted on the importance of physical infrastructures which went beyond transport and also involved telecommunications, energy, and a vast array of systems and facilities that housed and transported people and goods, as well as provided services. The case of Latin America was analysed with particular attention. Building infrastructure in the region posed several challenges related to externalities, to asymmetry of returns and of access to finance across different countries, and to intergovernmental coordination. Furthermore, Latin America had an extremely low population density and therefore faced high costs to build regional infrastructures relative to other regions of the world. The experts discussed the main initiatives undertaken in the region to close the infrastructure gap in the framework of the most important regional economic partnerships. The initiative launched by MERCOSUR in the previous decade was considered to be of particular importance as it involved a redistributive component. In fact, MERCOSUR created a structural convergence fund (the FOCEM) designed to reduce disparities among member countries through financing physical infrastructures. The experts concluded that the key lesson learnt from this and other Latin American initiatives was that infrastructural decisions could not be detached from an overall trade and integration strategy.

20. Finally, during this session the experts also devoted attention to trade facilitation as a key enabler of regional integration. Trade facilitation had gained relevance since the volume of traded goods had markedly increased in the last two decades and its composition had become more complex. It was observed that the share of intermediate goods and of intra-company trade were in fact on the rise in the wake of the internationalization of production, and that the traditional North–North trade flows had now been overshadowed by the rising South–South connections. These important novelties had fostered a renewed demand for simplicity, standardization and transparency of international rules and procedures governing the movement of goods across national borders. The experts suggested that priorities should be set on the trade facilitation agenda and reported recent empirical results that found that increasing transparency and reducing formalities were of critical importance to improve logistics performance.

21. Questions and issues raised by the floor concerned: the critical role of China and of its development cooperation strategy to raise capacities in other developing countries and least developed countries; the difficulties encountered to adopt common policies and rules at regional level across countries at different levels of development; the role of education for production upgrade; and the critical situation of Burundi, which was seriously lacking infrastructures, especially energy.

Financing for development-oriented regional integration

22. The third part of the meeting considered the policy lessons for development-oriented regional integration and particularly the financing aspects. In order to foster regional integration, building up infrastructure was considered to be a key element for economic development. However, some regions, including in the developed world, suffered from an investment gap in infrastructures that had been exacerbated by the crisis.

23. Experts addressed this challenge in the context of Europe by discussing the role of the European Investment Bank (EIB) in support of European integration.

Although the European Union was referred to as a unique economic entity and the most economically integrated region of the world, it had a diverse economy with significant disparities between and within its members in terms of life expectancy, human development index, standard of living, and the like. In recent years, most European Union countries had been growing below their potential, and as a result the gap in real gross domestic product (GDP) per capita between the European Union and the United States had widened.

24. To address this problem, the EIB had identified a number of shortfalls in competitiveness, most notably a large investment gap. For instance, the annual shortfall in research and development was estimated at €130 billion, while that of human capital development amounted to about €100 billion. The combined infrastructure investment shortfall was estimated to be close to €300 billion. In this regard, the EIB had tried to bridge the gap by supporting physical integration. The EIB had the mandate to develop the internal market and support regional development in conjunction with the structural funds administered by the European Union commission. To this end, approximately half of EIB loans concerned physical infrastructure in collaboration with sovereign and local entities, the latter being key actors for public investment projects. Nevertheless, a speaker noted that physical infrastructure was not enough for integration. There were still institutional gaps that could act as obstacles to full cross-border integration.

25. In order to promote a balanced economic development, the EIB also supported projects in the area of health, education, water, sewage, and the like. These investments were particularly directed towards the poorest members of the European Union. The EIB also tended to play a counter-cyclical and stabilizing role in order to support broad-based GDP growth during recession times. To improve competitiveness, the European Union had planned to unlock €315 billion of additional investment (the Investment Plan for Europe) within three years in growth-enhancing areas: research and development, innovation, education, health and infrastructure. This extra funding aimed at improving European Union competitiveness, restore confidence and improve the investment environment.

26. In addition, to ensure the financial and economic viability of the different projects of the Investment Plan for Europe, the EIB in conjunction with the European Commission, had created the European Investment Advisory Hub. The Hub aimed at providing a unique portal for all stakeholders, including project promoters, public authorities, member States and the private sector. It was a single access point to a wide range of advisory services and a cooperation platform. The Investment Plan for Europe would certainly bring about direct and indirect positive spillovers.

27. Experts also focused on the activity of infrastructure financing in Africa carried out mostly with the help of the African Development Bank (AfDB). A participant observed that in the case of Africa, the lack of suitable infrastructure reduced productivity by as much as 40 per cent and lessened national economic growth by two percentage points every year. The cost of inadequate infrastructure was therefore significant. The infrastructure development in Africa had several objectives: to create the economic conditions needed for longer term growth enshrined in the goals of the African Union and the New Partnership for Africa’s Development; to promote socioeconomic development in Africa through improved

access to integrated regional and continental infrastructure networks and services; and to foster poverty alleviation.

28. Participants noted that the AfDB had identified four significant infrastructure gaps in Africa. First, the growth of the population would substantially increase the demand for energy and electric power. Second, transport volume demand was projected to increase by a factor of 6 to 8 by 2040. Third, surging water demand would remain an economic and environmental challenge in the future. Fourth, information and communications technology (ICT) demand was expected to rise considerably, in particular, for wider bandwidth. To meet these challenges, a number of institutions focused on Africa, such as the AfDB, the New Partnership for Africa’s Development and the African Union Commission, had established a Priority Action Plan which had identified 51 infrastructure programmes to be implemented by 2020 in four key sectors (energy, transportation, water and ICT).

29. The total cost of these projects had been estimated at $68 billion through 2020. However, the domestic resources, private and public jointly, amounted to only $30 billion. The remaining $38 billion would have to be covered through external financing sources. These included: official development finance; private participation in infrastructure; and official investments from China. To scale up its funds, the AfDB had become one of the most active investors in African private equity funds, particularly those investing in public–private partnership investments. In addition, the AfDB was also active in developing and promoting innovative instruments to finance African infrastructure, for instance by promoting and deepening domestic debt markets and by promoting the use of project bonds to attract domestic investors to participate in the development of Africa's infrastructure. Also, the Bank ensured that projects were consistent with its green growth strategic objective to help the continent to transition towards the development of cleaner energy. Finally, by promoting an enabling legal, policy and regulatory environment, the AfDB aimed at enhancing infrastructure projects bankability and investment.

30. Expanding on the African experience, the experts highlighted the challenges faced by developing countries in financing their infrastructures. The gap in the financing for infrastructure development was estimated to amount to over $1 trillion in developing countries and currently most of the financing came from government budgets (about 60 per cent). However, developing countries faced the issue of a limited fiscal space because of the weak revenue collection capacity. Typically, countries with lower GDP per capita tended to have less government revenues.

31. In this context, an expert noted that development banks could fill this gap by providing long-term financing. In order to bridge the investment gap, however, these banks needed to fulfil a number of conditions. They needed a clear mandate to support developmentally oriented projects, a solid funding base, a capital base owned by highly rated sovereigns allowing them to borrow at lower costs, and in-house expertise to take decisions in terms of technology, project design, scale and location. Subregional development banks played in this regard a critical role by their unique expertise of the region where they operated.

32. To move forward on these issues, the developing countries had created a number of new entities characterized by new financial and monetary arrangements

and institutions, such as the Bank of the South, the New Development Bank, and the Asian Infrastructure Investment Bank. Experts also highlighted that a successful financing for regional integration required an integrated approach, involving different financing sources and mechanisms. The recently established southern institutions could contribute to the emergence of a new, reformed international financial architecture which would be more apt to provide financial stability and prosperity worldwide.

33. The ensuing discussion highlighted the stabilizing and counter-cyclical role that development banks can play during recessionary times. Also by playing this role, the development banks ensured that productive capacities remain intact while the economy recovered. Finally, greater cooperation among development banks at the national, regional and international levels allowed scaling up projects and ensured sustainability.

34. Several delegates thanked UNCTAD for organizing the expert meeting on a timely and important topic. Most delegates also thanked experts for their fascinating presentations which informed them about the regional integration processes in different parts of the world. Two delegates thanked UNCTAD for preparing a very useful and thought-provoking background note which served as a basis for discussion during the meeting.

II. Organizational matters

A. Election of officers
(Agenda item 1)

35. At its opening plenary, on 2 July 2015, the multi-year expert meeting elected the following officers:

Chair: Mr. Xavier Amelio Carim (South Africa)

Vice-Chair-cum-Rapporteur: Ms. Jeannette Mariño Castro (Ecuador)

B. Adoption of the agenda and organization of work
(Agenda item 2)

36. Also at its opening plenary, the multi-year expert meeting adopted the provisional agenda for the session (contained in document TD/B/C.I/MEM.6/7). The agenda was thus as follows:

1. Election of officers
2. Adoption of the agenda and organization of work
3. Strengthening subregional, regional and interregional dialogue and cooperation and their contributions to economic integration and development
4. Adoption of the report of the meeting

C. Outcome of the session

37. At its closing plenary, on 3 July 2015, the multi-year expert meeting agreed that the Chair should summarize the discussions.

D. Adoption of the report of the meeting
(Agenda item 4)

38. At its closing plenary on 3 July 2015 the multi-year expert meeting authorized the Vice-Chair-cum-Rapporteur to finalize the report after the conclusion of the meeting.

Annex

Attendance[1]

1. Representatives from the following States members of UNCTAD attended the session:

Algeria	Greece
Angola	Japan
Argentina	Mexico
Bhutan	Nigeria
Bolivia (Plurinational State of)	Poland
Burundi	Saudi Arabia
China	Seychelles
Ecuador	South Africa
Ethiopia	Sudan
	Uganda

2. The following intergovernmental organizations were represented at the session:

African, Caribbean and Pacific Group of States
African Development Bank
Commonwealth Secretariat
Eurasian Economic Commission
European Union
Permanent Secretariat of the General Treaty on Central American Economic Integration
South Centre

3. The following United Nations organs, bodies or programmes were represented at the session:

Economic Commission for Africa
International Trade Centre

4. The following specialized agencies and related organizations were represented at the session:

Universal Postal Union

[1] This attendance list contains registered participants. For the list of participants, see TD/B/C.I/MEM.6/INF.3.