United Nations

TD/B/C.II/MEM.2/2

# United Nations Conference on Trade and Development

Distr.: General
26 November 2008

Original: English

**Trade and Development Board**
**Investment, Enterprise and Development Commission**
**Multi-year expert meeting on international cooperation: South–South cooperation and regional integration**
Geneva, 4–5 February 2009
Item 3 of the provisional agenda

## South–South cooperation and regional integration: Where we stand and future directions

**Note by the UNCTAD secretariat**

*Executive summary*

This note addresses some of the implications of the current global financial crisis on South–South cooperation and regional integration. It presents an overview of the potential implications of the current crisis in the areas of capital flows and finance, investment and trade. The note surveys South–South and triangular cooperation schemes with respect to (a) South–South and regional financial and monetary cooperation; (b) regional cooperation and South–South investment agreements; and (c) South–South cooperation in trade and trade-related issues. It notes that South–South regional and interregional cooperation could complement and reinforce global efforts to mitigate the negative impacts of the current crisis, as cooperative approaches may provide better results than separate national actions in the face of a crisis. It includes numerous examples of South–South and regional cooperation in the areas of finance, investment and trade, where lessons may be drawn for policymakers.

GE.08-

# I. The present crisis and its impact on developing countries

1. The current financial crisis is one of unprecedented magnitude, which has brought the interplay between macroeconomic policies, financial innovation and regulation to centre stage. The widespread use of opaque financial instruments, mispricing of risk, and excessive leveraging, combined with lax regulation and the questionable use of ample liquidity, have been at the root of the largest financial crisis since the Great Depression. In times of crisis, a considerable degree of public policy is required, in order to avoid a systemic crisis in the financial sector and a severe slowdown of real economic activity. Governments and central banks are the only actors that can stabilize markets when confidence has been lost and all other actors are trying to increase their holdings of liquid assets.

2. Initially, analysts contended that since developing countries have continued to experience buoyant growth, they had been successful in decoupling their economies from those of developed economies. However, the crisis is now spreading to developing countries through both finance and trade channels. In the first case, this is evidenced by the recent increase in emerging market sovereign spreads, particularly for countries that combine high current-account deficits with a substantial stock of foreign liabilities incurred by the private sector. In terms of trade, the crisis is already leading to lower export earnings in developing countries. This is the combined effect of slower demand for these countries' exports, and lower prices for the commodities that account for the bulk of many developing countries' exports. A more detailed discussion follows, which deals with the impact of the current crisis in the areas of finance, investment and trade, and its implications for South–South cooperation and regional/interregional integration.

## A. Implications for the financial sector and the real economy

3. Considerable uncertainty remains with regard to the scale and extent of the financial crisis, and its attendant effects for the real economy. The economic slowdown has been most pronounced in developed countries, which are now sliding into recession. Despite the recent slowdown in growth rates across the developing world, developing country growth rates are widely expected to remain above historical averages. Nonetheless, the emerging recession in the developed world will eventually affect all sectors, in all countries around the world, due to the increased degree of global financial and trade integration.

4. The financial contagion in developing countries and emerging markets was initially confined mainly to the stock market. Equity markets have plunged across the world, but in most countries this decline essentially represents a correction of the steep increase that occurred during the first half of 2007.[1] More recently, however, the financial crisis has also had important implications on resource flows to developing countries. Yield spreads between emerging market economy bonds and US treasury bills have increased. The recent spike in financial market spreads could be a sign that investors are changing their risk perception of emerging markets and reducing their investments. The current crisis may also entail a decline in the growth rate of workers' remittances, which over the last few years has become the main source of foreign exchange for many poor countries. Recent estimates by the World Bank indicate that remittances are expected to decline by 0.2 per cent from 2007 to 2008, and by 0.9 per cent to 6 percent in 2009, in real terms as a share of gross domestic product (GDP). However, the decline in remittances is

[1] UNCTAD. Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus. Trade and Development Board. TD/B/EX(45)/2. 27 October 2008.

expected to be smaller than that of other private or official capital flows to developing countries.[2]

5. Indeed, concern remains that levels of official development assistance (ODA) may decline as donor countries are confronted with financing bail-out packages that may substantially weigh on their fiscal budgets. An assessment of previous crises in developed countries indicates that in some instances, financial crises have led to significantly lower aid disbursements.[3] Given the likely negative consequences of the crisis on developing countries' trade, capital and resource flows, maintaining a sustainable debt and external position in such an economic climate will prove to be a difficult task for many of these countries. Therefore, the international community must live up to its aid commitments.

6. A decline in capital inflows – for example, in connection with an unwinding of carry trade positions – has in some countries led to sharp currency depreciations and strains in the domestic financial sector. This has been the case for Brazil, Hungary, Iceland and the Republic of Korea. Bilateral and/or regional swap agreements among participating countries have served to mitigate pressure on their exchange rates.

7. Another big challenge for developing countries is to avoid spillover effects from the current crisis to their real sector. The fact that real economic activity has remained relatively strong in developing countries is due mainly to two factors: (i) domestic demand in several key developing countries has assumed a more important role in their growth performance; and (ii) the continued relatively high prices of certain primary commodities (even after sharp declines in recent months) has strengthened their external account and reduced their dependence on foreign capital.

8. As highlighted in UNCTAD's 2008 executive session, the strong economic performance of China has been a key factor behind the increasing importance of developing countries in global economic growth and in global trade flows. The economic future of China is in many respects crucial for how the repercussions of the financial market crisis will affect other developing countries. While a slowdown in China's exports will reduce its growth rate, domestic demand growth and investment activity are likely to remain steady and strong. Continued robust demand for commodity imports by China would attenuate the negative impact on commodity-exporting countries of what would otherwise be a global economic downturn.

## B. Developments in South–South foreign direct investment

9. UNCTAD estimates suggest that South–South foreign direct investment (FDI) has grown particularly fast since the early 1990s. Total FDI from developing countries and transition economies has increased significantly, from $4 billion in 1985 to $304 billion in 2007. Most of these investments went to other developing countries, often to neighbouring countries, thereby making them regional in nature. FDI by firms in developing countries to other developing countries rose from less than $4 billion in 1990 to $174 billion in 2006. This corresponds to about 12 per cent of global FDI outflows in 2006, compared with only 5 per cent in 1990. Some developing countries have become very important sources of FDI to other developing countries. Host countries with the highest share of South–South FDI, as

[2] World Bank. Outlook for Remittance Flows 2008–2010: Growth expected to moderate significantly, but flows to remain resilient. 11 November 2008. http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1110315015165/MD_Brief8.pdf

[3] Roodman D. History says financial crisis will suppress aid. 13 October 2008. http://blogs.cgdev.org/globaldevelopment/2008/10/history_says_financial_crisis.php

a proportion of total inward FDI, include Bangladesh, Cambodia, Ethiopia, Kyrgyzstan, Thailand, the United Republic of Tanzania and some countries in Latin America. The rise in South–South FDI is strengthening South–South cooperation, and it poses a number of important development issues, such as production and business linkages within the South–South context. However, in view of the current global financial crisis, it is important to address how South–South FDI flows will be affected, and the repercussions. At the structural level, it is equally important to examine how South–South FDI will enhance South–South cooperation and influence the international investment landscape in the future.

10. Many factors drive and motivate developing-country firms to invest beyond their national boundaries, in particular in other developing countries – thereby strengthening South–South cooperation. They invest abroad to access markets, technology and natural resources, to build brand names and to survive. Geo-cultural proximity and affinity – which continue to develop as greater familiarity is created by operating in a region – play an important part in determining developing countries' investments in neighbouring countries. At the same time, regional integration processes, such as those enhancing business linkages or facilitating trade flows, further accentuate intraregional investment and production networks. Intraregional and interregional investments among developing countries are particularly strong in manufacturing, finance, telecommunications, the extractive industries, infrastructure and real estate.[4] The factors underlying these drivers, motivations and processes have not changed since the start of the crisis, and in the short run there is little to suggest that South–South FDI will fall markedly. Transnational corporations (TNCs) from the South in the industries listed above mostly invest through retained profits – not so much through debt – and are therefore less affected by the financial crisis. The same applies to sovereign wealth funds, which are increasingly involved in FDI from the South. However, South–South FDI could fall markedly if the current financial crisis evolves into a protracted global recession that affects the capacity of TNCs from developing countries to invest in other developing countries. In addition, efforts to tighten international regulations on investment in offshore financial centres, following the financial crisis, would affect FDI flows to such centres and the magnitude of South–South FDI flows.

11. Such a decline could have significant effects, especially for some countries or regions. For example, FDI from developing countries is a significant source of investment for many least developed countries (LDCs). More than 40 per cent of FDI from developing countries goes to LDCs.[5] Regionally, in Africa, more than 50 per cent of all FDI inflows into Botswana, the Democratic Republic of the Congo, Lesotho, Malawi and Swaziland have come from South Africa. In Asia, more than 50 per cent of all FDI flows to Cambodia, the Lao People's Democratic Republic and Myanmar between 2002 and 2007 were from other developing countries in Asia. Investors from Argentina, Brazil, Chile and Mexico have become significant regional players in Latin America, partly because of regional integration and trans-Latin TNCs' strategies of establishing a stronger foothold in their region. Partly because of economic integration, firms from Malaysia, Singapore and Thailand are becoming significant regional players in the countries of the Association of South-

[4] UNCTAD. World Investment Report, 2007: Transnational Corporations, Extractive Industries and Development. United Nations publication. New York and Geneva. 2007.
UNCTAD. World Investment Report, 2008: Transnational Corporations and the Infrastructure Challenge. United Nations publication. New York and Geneva. 2008.
[5] UNCTAD. *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development.* United Nations publication. New York and Geneva. 2006.

East Asian Nations (ASEAN).[6] A prolonged financial and economic crisis will reduce all these activities, as profitability and the export orders of TNCs from developing countries are affected, and as they downsize or rationalize their overseas operations. Nonetheless, over the medium term, as the world recovers from the crisis, South–South FDI to particular developing regions and industries could increase in sectors such as finance, the extractive industries and infrastructure.

## C. Consequences for South–South trade

12. South–South trade is at risk of being hit by the global financial crisis. South–South merchandised trade in 2007 amounted to US$2.4 trillion in 2007 – or 20 per cent of world trade. South–South trade has grown with significant speed during the period since 1995, on average by 13 per cent per year, compared to the average annual 9 per cent growth in world trade, and the 10 per cent growth in trade among developed countries. During this period, the weight of South–South exports in total exports went up by 7 percentage points in developing Africa, by 4 percentage points in Asia, and by 2 percentage points in the developing countries of the Americas.

**Destinations for exports from developing countries in 2007 (as a percentage of total exports)**

| 2007 | **To the North** | **To the South** | Developing Africa | Developing Americas | Developing Asia |
|---|---|---|---|---|---|
| Developing Africa | 70.1 | 29.9 | 9.7 | 2.9 | 17.2 |
| Developing Americas | 70.0 | 30.0 | 1.8 | 18.8 | 9.3 |
| Developing Asia | 50.9 | 49.1 | 2.4 | 2.8 | 43.9 |
| 1995 | | | | | |
| Developing Africa | 77.6 | 22.4 | 10.5 | 1.8 | 10.2 |
| Developing Americas | 71.8 | 28.3 | 1.4 | 19.8 | 7.1 |
| Developing Asia | 54.9 | 45.1 | 2.0 | 2.2 | 40.9 |

*Source:* UNCTAD.

13. In the years between 2005 and 2007, over a third of the goods traded within the South were from the high-skill manufacturing sectors, namely electrical/electronic goods (including parts and components), and machinery and mechanical appliances. Exports of fuels also accounted for a high share. These are the sectors that have exhibited the most dynamic growth since 1995: the share of high-skill manufactured exports in total South–South exports has increased by 8 percentage points to 34 per cent, and fuels by 8 percentage points to 21 per cent. The increase in manufactured exports within the South came from an increase in the trade of manufacturing parts and components, as a result of regional production-sharing schemes, particularly in East Asia (e.g. ASEAN plus China), in addition to a rise in exports of final goods.

[6] UNCTAD. *Global Players from Emerging Markets: Strengthening Enterprise Competitiveness through Outward Investment.* United Nations publication. New York and Geneva. 2007.

**Top export sectors from developing countries**

| | | Share in total exports from the South, as percentages; (average 2005–2007) | Percentage point change from 1995 |
|---|---|---|---|
| | **To the South** | | |
| 1 | Electrical/electronic goods | 24.1 | 6.6 |
| 2 | Fuels | 21.1 | 7.7 |
| 3 | Machines and mechanical appliances | 10.1 | 1.3 |
| 4 | Base metals and products | 7.4 | -0.3 |
| 5 | Agriculture | 5.7 | -4.1 |
| 6 | Chemicals and allied industries | 5.3 | -0.4 |
| | Other sectors | 32.0 | -15.2 |
| | **To the North** | | |
| 1 | Fuels | 23.4 | 6.2 |
| 2 | Electrical/electronic goods | 16.1 | -0.1 |
| 3 | Machines and mechanical appliances | 12.0 | 1.6 |
| 4 | Textiles and textile articles | 8.9 | -3.2 |
| 5 | Base metals and products | 6.1 | 0.7 |
| 5 | Agriculture | 6.1 | -4.3 |
| | Other sectors | 33.6 | -5.2 |

*Source:* UNCTAD.

14. Such a rapid expansion of South–South trade, however, may be slowed down by the current global financial crisis and the subsequent economic slowdown in major developed countries. This is because the current economic crisis risks negatively affecting the factors that have been the engine of South–South trade growth, identified by UNCTAD as: (i) the rapid economic growth of a number of emerging markets in the South (e.g. Brazil, China and India); (ii) the increase in production-sharing schemes within the South; and (iii) improvement in trade facilitation and transport among developing countries.[7]

15. Firstly, "dynamic" exports from the emerging economies of the South – i.e. high-growth exports in goods and services – were directly hit by the economic slowdown in markets such as the European Union countries and the United States of America, due to a drastic cut in consumer demand from these countries. Dynamic exports – which include consumer electrical and electronic goods, ICT products, textiles and clothing, and other light manufactured goods – account for over 40 per cent of exports from the South to the North. Secondly, the demand shock in the North is quickly transmitted from emerging economies to other developing countries via the South–South trade linkages that were strengthened in the past decade through – among other things – new production-sharing schemes among countries in the South. For example, a fall in US demand for exports of final goods from China will reduce Chinese demand for parts and components imported from neighbouring Asian countries. If, as a consequence, a cooling of Chinese domestic activity occurs, this will likely lead to a lower level of imports of raw materials and commodities.

[7] These factors were identified as the major drivers in "Emergence of a new South and South–South trade as a vehicle for regional and interregional integration for development", a note by the UNCTAD secretariat for Roundtable 4, UNCTAD XII, April 2008 (TD/425).

16. Commodity prices have already plunged from their peak in June 2008. As shown by the UNCTAD commodity price index, global commodity prices decreased by 11.5 per cent in United States dollar terms in the period between June and September 2008.[8] Lower-income developing countries, particularly LDCs, would suffer from a global financial crisis. As these countries are heavily dependent on commodity exports, they will be affected very directly by an immediate reduction in export earnings. They do not have a sizable domestic market that can serve as a leverage to tide over their shrinking external trade prospects. Nor are they equipped with sufficient foreign reserves to cover the loss in export revenues.

17. Thirdly, a global financial crisis creates turbulence in trade facilitation and logistics, such as transport and trade finance. As far as transport is concerned, lower global demand and the subsequent slowdown in world trade significantly reduces transport costs, which should in principle be a plus for developing countries. However, the number of shipping lines is being cut back due to excess capacity and a decline in trade, particularly those connecting developing-country markets. This, in turn, reduces their access to foreign markets.[9] The global liquidity crunch created dire consequences for the terms and availability of trade credit and project finance: currently the bond market and syndicated loans are effectively non-existent. Obtaining finance has become costly, including to South–South trade. Interest rates on export credits are climbing far above bank refinancing rates, and export insurance premiums are rising fast, while the terms of repayment (e.g. the repayment period) or the liability coverage are becoming more restrictive. Export credit solutions (financing backed by export credit agencies) and other financing structures, such as barters, have regained prominence as key financing resources. Efforts to pump up the fund for trade finance are made at national or international level.[10] But further cross-border coordination among banks (including multilateral and development finance institutions, and central banks) or credit agencies is required, in order to create a tangible impact that is capable of mitigating the current problem and maintaining the growth momentum of South–South trade.

## II. South–South and triangular cooperation schemes

18. The core principle of interdependence is that no country can act in isolation in an interconnected world. In November 2008, the Group of 20 met to address appropriate responses to the ongoing financial crisis. It identified actions taken and to be taken, with regard to the following core areas of reform: strengthening transparency and accountability; prudential oversight; risk management; enhancing sound regulation and prudential oversight; promoting integrity in financial markets; and reforming international financial institutions. Given the truly global nature of the crisis, solutions need to be found in a truly inclusive global organization such as the United Nations – in what has also been termed the “G192”. These global efforts,

[8] The trend has been global among commodities, and specific commodities or commodity groups have been more affected than others: vegetable oils and oilseeds (-28 per cent), crude oil (-24.5 per cent), and food prices (-11.5 per cent), which includes rice (-28 per cent) (May-September), maize (-20 per cent) (June-September) and wheat (-16 per cent) (June-September). Source: UNCTAD commodity price bulletin.

[9] On 30 October 2008, the world’s biggest ocean carrier, Maersk Line, confirmed that it is to cut an entire nine-vessel Asia–Europe loop, removing approximately 7,600 twenty-foot equivalent units (TEU) a week from the trade. The Danish carrier was just three days behind an announcement from American President Lines (APL), which said that because of “increasingly challenging conditions”, it was carving 25 per cent from its Asia–Europe and 20 per cent from its transpacific trade lanes. Containerization International online. 30 October 2008.

[10] Brazil, the United States and other countries injected liquidity to ease the export credit drought faced by their exporters. The International Finance Corporation of the World Bank Group is planning to increase its global trade finance programme for developing countries, to triple the programme’s ceiling to reach US$3 billion, as stated in an international meeting on export finance organized by the World Trade Organization on 12 November 2008.

in the form of North–South and triangular cooperation, may be complemented by South–South and regional cooperation.

19. Small and open developing countries have limited choices for dealing with external shocks. One option for small open economies is to join forces, through South–South and regional cooperation, to protect their economies from the adverse external shocks from international capital markets. Cooperative approaches may provide better results than separate national actions in the face of a crisis. In addition, developing countries now have more resources than they did in the past (e.g. in terms of foreign reserves, outward FDI, their domestic markets), which increases the range and scope of possible collaboration. Some examples of financial cooperation include swap agreements, pooling of reserves among central banks, exchange rate coordination mechanisms, regional supervisory institutions, regional payments agreements, and the expansion or creation of regional development banks and regional bond markets to boost access to long-term financing. Monetary coordination may take the form of a regional exchange rate mechanism, common-bloc floating or a monetary union.

20. There are certain benefits associated with these forms of cooperation. South–South and regional cooperation can play a useful role, particularly in the design and provision of instruments to assist and enable Governments. Countries may also gain greater degrees of freedom in designing national strategies and identifying national priorities, in contrast to other forms of assistance that may be subject to conditionality. There are already pre-existing instruments from which lessons may be drawn. Some examples of how South–South cooperation has been effective in facilitating financial flows and monetary cooperation, investment and intraregional trade and are presented below.

## A. South–South and regional financial and monetary cooperation

21. Monetary and financial cooperation have gained an increasingly prominent role in regional integration processes, from which many lessons may be drawn. South–South and regional monetary and financial cooperation and arrangements can serve to reduce developing countries' vulnerabilities to the vagaries of the international financial markets, by developing regional payments systems and mutual financing, enforcing the use of national currencies and establishing regional mechanisms for policy coordination and macroeconomic surveillance.

22. The UNCTAD Trade and Development Report 2007[11] surveys some recent examples of regional financial and monetary cooperation.[12] Such cooperation may take several broad forms. These include payment facilities and credit agreements, regional cooperation for development financing, and exchange rate mechanisms and monetary unions. An analysis follows:

*(a) Payment facilities and credit agreements:* Payment and credit agreements among central banks are aimed at facilitating intraregional trade and at providing liquidity financing to member countries of a trade agreement. Through this facility, central banks can compensate cross-payments owed to each other for balance of payments transactions carried out during a given period, and then settle the remaining debt in hard currency on an established date. This provides a mechanism to facilitate international transactions between countries. Participation

[11] UNCTAD. *Trade and Development Report 2007: Regional Cooperation for Development.* United Nations publication. New York and Geneva. 2007. http://www.unctad.org/en/docs/tdr2007ch5_en.pdf

[12] For a more general discussion, see: UNCTAD. *Global and Regional Approaches to Trade and Finance.* UNCTAD/GDS/2007/1, United Nations publication. New York and Geneva. 2007.

in such arrangements allows countries to require less international liquidity for their engagement in intraregional trade.

There are a number of examples of these types of arrangements, one of which is the Chiang Mai Initiative (CMI), launched by ASEAN+China, Japan and the Republic of Korea (ASEAN+3) in 2000, in response to the 1997–1998 Asian financial crisis. The CMI was the most prominent bilateral swap arrangement to include developing countries. Three of the main areas of dialogue and cooperation are capital flow monitoring, self-help support mechanisms, and international financial reforms.[13] The CMI is geared both towards crisis management and towards crisis prevention by providing participating countries with international financial liquidity. In October 2008, the ASEAN+3 finance ministers agreed to expand the financing facility under the Chiang Mai Initiative from $6 billion to $80 billion. The ministers further agreed to extend the plan, to include multilateral swaps as well as bilateral swaps, and to advance the implementation date to the first half of 2009.[14]

Another example is the Latin American Reserve Fund, which was established in 1978 to support the stability of member countries in the Andean region. The stated objectives of this fund are: (i) to provide member countries with balance of payments assistance through the provision of credits and loans to third parties; (ii) to contribute to the harmonization of member countries' monetary, exchange rate and fiscal policies; and (iii) to improve the conditions of international reserve investments made by member countries.[15]

In October 2008, Brazil and Argentina announced the launch of the Brazil–Argentina Local Currency Payments System (SML), which aims to simplify and enhance the efficiency of intraregional transactions, by facilitating the flow of trade transactions and by lowering costs. Under the agreement, importers and exporters operate in their domestic currency through the local currency payments system. The SML will serve to reduce the transaction costs associated with international payments, and eliminate the use of a third currency in direct company transactions.

*(b) South–South and regional financial cooperation:* Regional financial cooperation in the form of a regional investment fund based on hard currencies, or in the form of already existing regional financial institutions, potentially offers investment alternatives that would not only increase the financial returns on foreign reserve holdings, but would also enhance regional development. In addition, an increasingly important feature of regional development banks is their local currency exposure and portfolio. One example of this is the Andean Development Corporation (CAF), which is a multilateral financial institution that provides financing to the Andean region, with the objective of supporting regional integration and sustainable development among its member countries. The CAF constitutes the main source of multilateral financing for the Andean region. Another example is the Asian Development Bank (ADB), which strengthens local and regional financial markets both in its function as a borrower and in its function as a lender, by using local currency denominated instruments. The ADB has introduced a local currency loan product, with the aim of reducing currency mismatches and supporting local capital market development.

[13] See: The Joint Ministerial Statement of ASEAN+3 Finance Ministers' Meeting. Chiang Mai, Thailand. 6 May 2000.
[14] Aglionby J. Currency swap scheme to be expanded. Financial Times. 16 October 2008.
[15] Article 3 of the Constitutive Agreement.

*(c) Exchange rate mechanisms and monetary unions*: Regional exchange rate mechanisms and monetary unions can serve to preserve regional markets from exchange rate volatility. Monetary cooperation is a useful tool for achieving stability of the internal and the external value of their money, while also avoiding volatile short-term capital flows, arbitrage, and frequent overvaluation and undervaluation of the currency. Developing countries, particularly those bound together by openness and close trade ties, stand to benefit from monetary arrangements that seek to strengthen both export competitiveness and external monetary stability. Three of the four monetary unions in the world are established among developing countries, namely the Eastern Caribbean Currency Union, the Common Monetary Area in Southern Africa, and the Zone franc in Africa, which comprises – in particular – the West African Economic and Monetary Union and the Economic and Monetary Community of Central Africa. The world's other currency union is the European Monetary Union. The members of the Gulf Cooperation Council aim at forming a currency union by 2010.

## B. Regional cooperation and South–South investment agreements

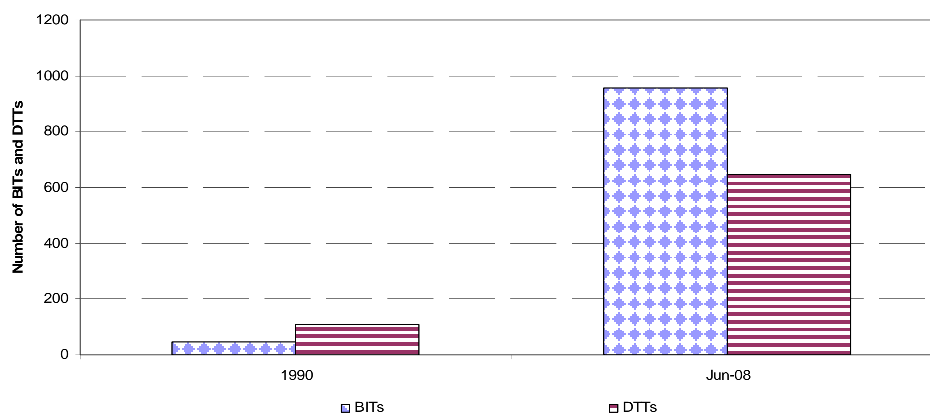
23. A particularly important reason for the rapid rise in FDI and TNCs from developing countries, including South–South FDI, is the increasing number of investment opportunities in other developing countries and the relaxation of home-country policies towards outward FDI. Some developing countries such as China, India, Malaysia, the Republic of Korea and Singapore are encouraging their firms to invest abroad. As a result of this development, there has been a substantial increase in the number of South–South international investment agreements.[16] For example, the number of South–South bilateral investment treaties (BITs) leaped from 42 in 1990 to over 950 by June 2008 (fig. 1). The number of double taxation treaties (DTTs) rose from 110 in 1990 to 645 by June 2008.[17] More than 100 economic cooperation agreements with investment provisions between developing countries had been concluded by June 2008.[18] These trends will continue in the future and will bolster South–South cooperation and regional FDI, irrespective of any short- or medium-term declines as a consequence of the financial crisis.

[16] UNCTAD. *South–South Cooperation in International Investment Arrangements.* United Nations publication. Sales No. E.05.II.D.26. New York and Geneva. 2005.
UNCTAD. Forthcoming. *International Investment Rule-Making: Stocktaking, Challenges and the Way Forward,* United Nations publication. New York and Geneva. Sales No. E.08.II.D.1

[17] These numbers include economies in transition.

[18] Other bilateral and regional free trade area (FTA) agreements which also cover investment issues are making the contracting countries or regions attractive to FDI. Such arrangements include the ASEAN–China FTA, ASEAN–India FTA, China–India FTA, China–Republic of Korea FTA, Chile–China FTA, China–Pakistan FTA, and South Asia FTA.

**Figure 1. Increasing number of South–South BITs and DTTs, 1990 and June 2008**




24. Regional integration in Africa, Asia and Latin America has contributed to an increase in the attractiveness of these regions for FDI, partly as a result of the benefits from economies of scale offered by an enlarged regional market, easier sourcing of production inputs, freer movement of goods and services, and a more efficient production structure made possible by a regional division of labour. ASEAN economic integration through – for instance – the ASEAN Free Trade Area and the ASEAN Investment Area, has increased the region's attractiveness for FDI and as a competitive production platform. Similarly, regional integration in the Southern African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA) is making these regions more attractive for FDI too. In Latin America, intraregional investment has become significant, and has contributed to South–South investment in industries such as food and beverages, engineering, electricity, the extractive industries, telecommunications and retail. South–South FDI and its interrelationship with regional integration will remain an important component of development for many countries and regional groupings.

## C. South–South cooperation in trade and trade-related issues

25. South–South trade linkages can become viable channels for mitigating the negative impact of the current crisis on South–South trade. Instruments may include the General System of Trade Preferences, regional trade agreements, and cooperation in other trade-enhancing areas and institutions.

26. South–South regional and interregional integration schemes have become key instruments of regional cooperation and development of member States. Over the years – and especially in recent years with the emergence of dynamic growth in some developing countries – such schemes have evolved innovative cooperation strategies and mechanisms in such areas as trade, finance, money, and the related macroeconomic areas, to further strengthen the process of regional economic integration as a building block for beneficial participation in the international trading system. For example, Latin American countries created the South Bank in 2007 to finance development in the region. Such novel arrangements can build up the resilience of economies in the region and strengthen South–South trade.

27. In the area of transport, ASEAN adopted the Roadmap towards an Integrated and Competitive Maritime Transport. In Latin America and the Caribbean, the Central American Common Market, the Caribbean Community (CARICOM), the Andean Community and the Southern Common Market (MERCOSUR) are linked

by their respective land and sea transport systems, which have their own transport networks, institutional framework, established regulatory schemes, and particular infrastructure development plans. In Africa, COMESA has introduced the Trade and Transit Transport Facilitation Programme, while the SADC has adopted the Protocol on Transport, Communications and Meteorology. Similarly, within the framework of the Transit Transport Framework Agreement (TTFA), the Economic Cooperation Organization (ECO) has embarked on a number of intra-regional initiatives in the regions of Central and West Asia, that involve 10 countries, including Afghanistan, Pakistan, the Islamic Republic of Iran, and others, with a view to promoting South–South cooperation in trade, transport and other areas. For example, a new railway cargo service link has been established, which starts in Almaty (Kazakhstan), passes through the Central Asian republics and the Islamic Republic of Iran, and terminates in Turkey, linking the entire region by rail network.

28. In the area of trade and project finance, the Global Network of Export-Import Banks and Development Finance Institutions (G-NEXID) is a dynamic institutional response to the emerging trends in international trade, where South–South trade has been impressive in quantity and quality. Launched in 2004, G-NEXID, which currently has 25 members, aims at boosting bilateral and multilateral agreements of all kinds among export–import (Exim) banks and development finance institutions based in developing countries. The current financial crisis has reinforced the importance of collaboration, and G-NEXID is well placed to deliver. Members of G-NEXID have increasingly been entering into business cooperation alliances amongst themselves, through co-financing, provision of appropriate and competitive financial instruments and lines of credit. For instance, the Exim Bank of India has entered into a lines of credit relationship with the Eastern and Southern African Trade and Development Bank (PTA Bank), the Nigerian Exim Bank and the African Export–Import Bank (Afrexim Bank). A similar agreement has been finalized between the Exim Bank of Romania and the Industrial Development Bank of Kenya, as well as between the East African Development Bank and the China Development Bank.

# III. Issues for discussion

29. In light of the numerous examples of South–South and regional cooperation in the areas of finance, investment and trade, there are many lessons to be drawn. Experts may wish to address the questions posed here within the context of triangular, regional, and South–South cooperation. The following issues have been identified for the experts to discuss:

## A. Regional integration and South–South cooperation

How are different regions integrating? What are their similarities and effectiveness for regional integration?

What are the long term trends of regional integration across regions? What is its impact on South–South cooperation?

Have cooperative arrangements become more effective in supporting South–South integration and development?

What new opportunities are presented in the areas of finance, investment and trade?

## B. Financial crises: South–South solutions?

How effective have countries' responses been in mitigating risks and addressing and preventing crises? What, if any, mechanisms did they institutionalize?

Have different regions emerged stronger after a financial crisis? If so, what is the empirical evidence supporting this observation? What policy lessons can be learned form these experiences?

What lessons can be drawn from regional integration in enhancing South–South cooperation, especially with respect to capital flows and financial cooperation?

What are the implications of a potential decline in official development assistance for South–South cooperation?

What is the potential of interregional investment funds?

## C. Regional integration and FDI

Will the global financial crisis affect South–South FDI? Will all sectors be affected to the same extent?

What policy lessons can be drawn from the different national and regional experiences in attracting and benefiting from South–South FDI?

How do regional arrangements increase the attractiveness and resilience of a region for investment and production? How will South–South FDI influence the future international investment landscape and South–South cooperation?

## D. South–South trade and the global financial crisis

How has the current financial crisis affected South–South trade, including trade within regional groupings? Are there any sectors that stand to benefit from South–South trade during the current crisis?

What are the different types and degrees of trade-related impact that each regional grouping is experiencing from the current financial crisis? What measures are required to overcome these challenges (e.g. in areas such as trade finance and trade facilitation)?

What is the likelihood that the current financial crisis and the prospect of a global economic downturn will lead to a reassessment of international production-sharing schemes, including among developing countries?

---