Recent Reports

World Development Report 1993
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Investing in health

Eleven thousand children die each day from malnutrition; infant and child mortality in Africa are increasing, and throughout the continent diseases like cholera, measles and tuberculosis are on the rise again.[1] At the same time the region spends four times more on debt servicing than on health care.[2] In a crisis such as this, the focus on international public health in the World Bank's *Development Report* is certainly welcome if long overdue.

This is the World Bank's 16th *Development Report.* The Reports are produced through a process of drafting and consultations with short-term consultants, and increasingly, prestigious international academics. They tend to influence the formulation of operational directives governing the Bank's own practice, and they play a part in shaping national and global policies on major themes, not least of course, through conditionalities attached to the Bank's lending. It is clearly in the interests of development practitioners, particularly those concerned with health services, to seriously consider the Report and its recommendations.

At the outset, the Report identifies four main problems in the health sector; (1) misallocation, i.e. inappropriate government funding of cost-ineffective interventions such as teaching hospitals; (2) inequity in health services; (3) inefficiency and (4) "exploding costs". The Report goes on to propose a three pronged approach to improving health: (1) foster an environment that enables households to improve health; (2) inequity in health services; (3) promote diversity and competition.

The key recommendations for households are welcome: expand investment in schooling, particularly for girls, and empower women by removing discrimination in the labour market, in access to credit and property ownership. There is a belated recognition that violence against women in the home is a major health problem. (The Bank notes that in the US domestic violence is the leading case of injury among women of reproductive age.)

The Report also makes valuable comments on the connection between poverty and health: "Latin America's recession in 1983 is estimated to have caused 12,000 additional deaths of babies, or 2 per cent of all infant deaths that year." There is a welcome analysis of the crucial issue of distribution of wealth, within countries, and within households. The Report recommends measures to control the use of tobacco and alcohol – an appreciated

departure from years of the softly-softly approach towards these giant industries.

The news on AIDS is shattering: in Sub-Saharan Africa an average of one in forty adults has the virus; in certain cities the rate is one in three. Further, more than 90 per cent of the infected individuals are in their economically most productive years, between ages 15–45. Conservative estimates from the World Health Organisation are that by the year 2000, 26 million individuals will be HIV-infected and 1.8 million a year will die of AIDS.

To improve government spending the Bank proposes the application of a cost effective interventions package – with the aim of delivering the most health for money invested. The approach is not new, but builds on work begun in the 1960s which was accelerated through epidemiological studies during the 1980s. Quality adjusted life years (QALYs) now appear as disability adjusted life years (DALYs), as the unit to measure the effective allocation of funds.

The DALY, which is also used to estimate the "global burden of disease", is reached by combining (a) the loss of life due to premature death (defined as the difference between actual age at death and life expectancy at that age in a low mortality population) and (b) the loss of healthy life due to disability. These measurements allow comparisons to be drawn between regions, risk factors, disease groups (communicable, non-communicable and injuries) and sex. Thus, Sub-Saharan Africa loses 550 DALYs for every 4,000 people, more than twiee the global average. Further, over 80% of the DALYs lost due to diarrhoea are due to infections in children under five years of age.

Crucial to the relevance of the DALY estimations are the data used to support them. Unfortunately, the Bank has been criticised for using poor data, and compounding the problem by extrapolating and making predictions from inferior information. It is clear that the DALY methodology, to be of significance, requires further refinement and well substantiated epidemiological data behind it to make it the cornerstone of the Report and the recommendations seem premature at best.

Finally, the Report recommends a combination of public and private funding to provide the most health for the least money. Governments are encouraged to invest in essential clinical packages (the components of which are identified using the DALY) and to encourage private investment in that this package will be inexpensive because it is directed at a minority in society – the poor. A viable package also includes a minimnm number of components to be effective (immunisations, school based health services, family planning and nutrition etc).

This package may be possible for middle income countries, and in countries where the poor *are* the minority. However, for low income countries, or highly indebted countries with over half the population living in poverty, it is almost impossible to imagine government funding of such packages. With the encouragement of private investment to cater for the

wealthy, the real danger is of further fragmentation of health services at a time when integration is crucial, and deeper discrepancies in the quality and type of care available to rich and poor.

The authors boldly state: "By adopting the packages of public health measures and essential clinical care described in the Report, developing countries could reduce their burden of disease by 25%." It goes on to promise "millions of lives . . . could be saved." *The Lancet* cautioned against just such confidence in a recent editorial: ". . . there is a risk that a report from such an influential and well-funded organisation will be used uncritically as the basis for decision on policy and resource allocation."[3]

While structural reform of health care systems may well be necessary, the problems in health care in the "Third World" owe much to the economic crisis which grips these countries. The Working Group on Health and Development in the Netherlands recently called on the Bank to recognise the critical issues influencing health care: "Structural adjustment programmes, imposed by the self same World Bank . . . have given recipients little choice but to cut their health services. After inspecting the debris on the battlefields, donors now emphasise the importance of protecting vulnerable sectors such as health care and education".[4]

The *World Development Report* does acknowledge the close link between poverty and health. What it fails to do is make the direct link between poverty and the failure of the World Bank's economic prescriptions and policies for developing countries. The Bank is prescribing an overhaul of the health care system; the advice would be more appreciated, and realistic, if an analysis were included of the macroeconomic policies that have contributed to the current health care crisis, and if an overhaul in *those* policies were begun.

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Footnotes

1. D. Logie, and E. Woodroffe, "Structural adjustment: the wrong prescription for Africa?" *British Medical Journal*, vol. 301, p.4144.
2. Oxfam, *Africa Make or Break*, Oxfam Publications.
3. Editorial, *The Lancet*, vol. 342, p.63
4. G. De Wildt, et al, WEMOS, *The Lancet*, vol. 342, p.440

A Report on Regionalism

Alan Murray

This paper begins by outlining recent trends in regionalism, and the risks potentially raised for the world economy. It then discusses the four characteristics which are required for a trading bloc to endure and be, in some sense, successful. The paper traces the development of regional trading blocs in Europe, North America and East Asia and assesses the likelihood of success for these blocs on the basis of the four criteria.

Introduction

Since the 1980s there has been a remarkable resurgence of regionalism in the world economy as evident in Europe,[1] North America,[2] and East Asia.[3] Livesey (Dictionary of Economics, Pitman 1993) defines regionalism as, in this context, "a tendency to form regional trade groupings".

One can define a trading bloc as an association of countries that reduces intra-regional barriers to trade in goods and services, investment and capital. The grouping of countries into regional trading communities, customs unions (nations that levy common external tariffs while freeing internal trade are said to have formed a customs union), or full free trade areas (if external tariffs against outside countries differ among member nations while internal trade is free, the nations are said to have formed a free trade area) is allowed under article 24 of GATT, provided that: (i) other GATT members are notified of the details; (ii) such arrangements do not raise new trade barriers on the whole against other contracting parties to the GATT; and (iii) such arrangements cover "substantially all trade" between partners and commit them to reduce barriers to intra-regional trade, possibly by means of a definite schedule and certainly within a "reasonable length of time".

Regionalism of this sort is not new, but its present incarnation is distinctive. A first distinguishing feature of the renewed interest in regionalism is that it has taken place within the context of a potential weakening of the multilateral trading system. Major difficulties were encountered in launching the Uruguay Round of GATT negotiations in 1986; it took four years (from 1982-86) for agreement to be reached for a new round of talks, and progress in completing the round was painfully slow.

A second new element is that far-reaching and successful regional initiatives by major industrial countries have created the feeling that preferential trading arrangements on a regional basis are here to stay. The agreement between the EU and EFTA, and between the US, Canada and Mexico stand out in this regard.

Finally, the most recent regional arrangements among industrial and developing countries involve reciprocal trade concessions. This is illustrated by the negotiations between Canada, Mexico and the US on the North American Free Trade Agreement. Previous arrangements with developing countries generally took the form of one-way trade preferences granted by industrial countries in favour of selected

developing countries – for example, the EU trade preferences extended to certain developing countries under the Lomé convention.

Regionalism's risks

There are risks as well as possibilities associated with regionalism: these include the possible diversion of scarce skills from multilateral to regional negotiations and the increased threat of tension between regional groups. Regional and multilateral negotiations are time consuming and skill-intensive; they therefore compete for scarce human and administrative resources. The main concern in this period is that the current proliferation of regional trading arrangements that have high priority in governments' agendas may be diverting these scarce resources away from multilateral negotiations. Some analysts suggested that the EU was more preoccupied with its Single European Market programme than with the Uruguay Round of GATT talks.

An excessive number of preferential regional trading arrangements can also lead to significant frictions, political pressures, and practical problems. Each new arrangement inevitably undermines the value of the preferential access granted to some countries under existing arrangements. Schott notes that this type of problem has already occurred in the case of the US-Israel Free Trade Agreement, with Israel arguing that Canada obtained better terms in its subsequent deal with the US, especially regarding the provisions on trade in services and the dispute settlement mechanism.

Non-participating countries have at least two additional reasons to be wary of regional agreements. One is that the integrating countries may be tempted to raise trade barriers against third countries at the same time that they lower them between themselves. This, ironically, can result in the integrating countries doing themselves at least as much damage as they inflict on others, because they, in effect, cut themselves off from world competition. The disastrous performance of the former Comecon countries was due, in part, to the barriers erected against imports from the West, while trade amongst themselves was encouraged by the Comecon system.

The second reason is that even when trade barriers against third countries are not raised, regional agreements can inflict damage on other countries. In 1950, the Canadian economist Viner showed that a selective and limited lowering of trade barriers will lead to trade distortions. When tariffs are uniform, each country will import from the lowest-cost source (although paying a higher price than with totally tariff-free trade). When tariffs on imports from some countries are lower than others, the importers will buy from the country that supplies at the lowest price, which might not necessarily be the country that can produce at the lowest price. "Trade diversion" of this sort is an inevitable consequence of regional trade agreements, and it is important to establish whether or not it is more than offset by "trade creation" – the extra trade and prosperity generated within the

region by the selective lowering of barriers.

It is worth noting that, in some senses, the traditional trade creation/ trade diversion debate is becoming less relevant. Tariffs on trade in goods between OECD countries are very low so lowering them further will have little overall effect. The sort of regional agreements now being engaged in go well beyond the common agreements to lower tariffs on trade in goods. The North American Free Trade Agreement (NAFTA), for example, deals with non-tariff barriers to trade in agriculture and textiles, with trade in services, with investment flows, even with contentious environmental regulations.

Criteria for Success

Successful trading blocs, i.e. those that have held together over time and have increased the welfare of their members (whatever their implications for non-participants), tend to exhibit the following four characteristics. These are:

* similar levels of per capita gross national product (GNP);
* geographic proximity;
* similar or compatible trading regimes;
* political commitmeut to regional organisation.

Blocs with wide income differences face difficulties because producers in rich countries are often seen as swamping those in poorer regions. Geographic proximity is a key factor because of the importance, technological progress notwithstanding, of transportation and communications costs. The third and fourth characteristics relate to the durability of the trading bloc. Similar trading regimes involve similar laws and regulations governing trade flows among members and between members and third countries. For a regional trade bloc to work, it requires a political commitment that dilutes national sovereignty in favour of broader regional policies.

The European Trading Bloc

A European regional trading bloc has been in existence since 1957 when Belgium, the Netherlands, Luxembourg, West Germany, France and Italy signed the Treaty of Rome. Since then the community has been enlarged to 12 countries, and, in 1991, an agreement was reached on the creation of a European Economic Area, a zone of free trade incorporating the 12 community members and the seven countries of the European Free Trade Agreement (EFTA). This is intended as a preparatory stage to membership of the community for some EFTA states, currently being negotiated. The EFTA states present major advantages for the community. They boost community average GNP considerably, provide an important contribution to community finances and allow for a logical integration of the West European aid effort in Eastern Europe and the developing world.

The EU has substantially succeeded in promoting the integration of its members. The share of intra-regional trade to total exports reached 63% in 1991. Intra-European trade flows of more than $US1 trillion in 1990 and

1991 are unequalled anywhere else in the world. Exports to EFTA countries now account for more than 26% of total shipments to non-EU member countries. In turn, exports to the EU account for almost two-thirds of total EFTA exports to non-EFTA countries.

These figures have resulted in some analysis suggesting that a "Fortress Europe" may be emerging. Three devices in particular have provoked the suspicions of Europe's trading partners: anti-dumping actions, reciprocal deals, and informal quotas.

Under the rules of GATT, if the European Commission can prove that foreign goods are being priced at less than in their home markets, or for less than would be necessary to ensure a reasonable profit, then it can take action. The Commission can force the importer to either pay an import levy or raise its prices. Every year, the Commission receives hundreds of complaints about dumping from European manufacturers. Most actions come from well organised industries such as electronics. These complaints often prompt the Commission to take action and it is this which results in allegations of a "Fortress Europe".

On a wider scale the Commission has been willing to court the disapproval of the world trading system by entering into reciprocal deals. It is an article of faith in world commerce that trading blocs should not do special trade deals with each other. Under the rules of GATT all countries should have equal access to one another's markets. However, the EU has shown a tendency to side-step GATT in favour of reciprocal deals that allow foreign companies access to Europe to the same extent that European companies have access to foreign markets.

The third and most blatant piece in the EU's protectionist armour has been the use of informal quotas. The EU is divided between members that have basically open markets such as Ireland (although not in the case of, say, textile and clothing imports) and Germany, and others such as Italy and France, which have strict quotas in particular industries on non-EU imports. For example, France and Italy have tried desperately hard to keep out imports of Japanese cars.

Whatever the fears raised for other parts of the world, the EU/EFTA region fulfils the four characteristics of a successful trading bloc. Firstly, with the exception of Portugal and Greece, the national incomes of member countries are very similar. Secondly, with the exception of Ireland, the UK and Greece, all members are contiguous; and the Treaty of Rome and the Maastricht Treary have highlighted a willingness to broadly accept the third and fourth requirements.

North American Free Trade Agreement

In 1991 an agreement was reached between Canada, Mexico and the US, labelled the NAFTA which came into force in January 1994, and created the largest single trading bloc outside the EU. The objectives of the agreement are to eliminate barriers to trade, promote conditions of fair competition, increase investment

opportunities, and promote further trilateral, regional and multilateral trade. The NAFTA provides for the gradual elimination of tariff and non-tariff barriers to the movement of goods, services and capital in the zone over a 10-15 year period.

Both Canada and Mexico conduct two-thirds of their trade with the US, and each benefits from substantial US foreign investment in their economies. US trade with its North American neighbours accounts for about 26% of total US trade. However, unlike the EU, intra-regional trade accounted for no more than 40% of the combined exports of the US, Canada and Mexico in the 1980s.

Despite initial enthusiasm Canadians have recently been voicing their fears about the treaty. They fear that stronger US companies will dominate their local markets. They also fear the threat offered by Mexico's low wage economy.

The Mexican authorities, in particular, hope that Mexico's expanded access to the North American market will open up new opportunities in Mexico, and increase wages. In addition, NAFTA is expected to improve Mexico's position in the current international competition for capital. Secure access to the North American market would be an added incentive to potential investors willing to exploit Mexico's comparative advantage. US companies are already reported to be locating south of the border to benefit from Mexico's low wage workers. The resulting capital inflows and imports of modern technology through foreign direct investment will, it is hoped, be an important element of Mexico's modernisation process and will strengthen the country's production capacity and international competitiveness.

Combating illegal immigration, by creating incentives for people to stay in Mexico, is one of the reasons the US administration favours the deal. But not all US opinion favours the treaty. The US Labour Advisory Committee notes that NAFTA "will have the effect of prohibiting democratically elected bodies... from enacting measures deemed inconsistent with the provisions of the agreement," including measures on the environment, workers' rights, health and safety.

Despite the significant differences in income between Mexico, Canada and the US, this bloc does exhibit most of the characteristics of a successful trading group. The geographical test is passed, and there is a political commitment to regionalism; and, because of the economic reforms now taking place in Mexico, differences in trade regulatory systems are rapidly fading.

The NAFTA leaves the door open for any other country or free trade bloc/region to apply for membership, providing it meets the NAFTA rules. This could ultimately lead to a link-up with Latin American trading blocs now emerging.[4]

East Asia

In East Asia there is an informal trading bloc which includes Japan and some other Asian countries. This region experienced the strongest

export growth of the three regions discussed here during the 1980s. The region's total trade more than doubled; much of the growth was generated by sales to the North American market. Because of the strong growth in exports to third countries, East Asia was the only region in which the relative share of intra-regional trade to total trade remained basically the same in the 1980s – 34% in 1980, 35% in 1989.

Some commentators see an East Asian trading bloc emerging because the countries of the region seem to be coalescing around the region's dominant trading partner – Japan. *The Economist* cites four reasons for the emergence of a Japan-centred trading bloc:

1. Japanese trade with other Asian countries has grown faster than its trade with the US;
2. Japanese imports of manufactured exports from Asian countries have grown substantially;
3. there is a growing internationalisation of the Yen;
4. Japanese foreign direct investment in the rest of Asia has grown substantially.

While Japanese trade and investment in East Asia has grown significantly over the past decade with investment quadrupling to $8.2 billion between 1985 and 1988 alone so has Japanese trade and investment in North America and Europe.

Also, Bello (1992) is quick to point out that Japanese investment in the region has left countries like Korea and Taiwan highly dependent on Japanese technology. Japan, for its part, has been criticised for transferring only "second class technology" to these countries. For example, the Japanese government has prohibited the transfer of 200 ultra modern high technologies to Korea until the year 1995, by which time the Japanese corporations should have been able to exploit most of the market opportunities of these new technological advances.

Overall, this bloc exhibits the least number of characteristics required for a successful trading bloc. Firstly, the countries in the region are widely dispersed geographically and have different levels of economic development. Secondly, the last two characteristics of successful trading blocs seem to be lacking. Trading policies and regulatory regimes differ markedly from country to country, and there seems to be little commitment to an evolving regional organisation.

Conclusion

There is no doubt about the existence and future development of a European trading bloc; a North American trading bloc is evolving despite tensions caused by wage and income differentials; but the failure of the East Asian region to increase its intra-regional trade during the 1980s suggests that an East Asian trading bloc remains only a remote prospect. Whether these trends are positive or negative for participants, or for those excluded, will be the subject of intense discussion in the coming years.

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Footnotes

1 Europe comprises the twelve members of the EU and the seven members of EFTA.

2 North America comprises the US, Canada and Mexico.

3 This region is comprised of Australia, Hong Kong, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore, Taiwan and Thailand.

4 In 1992, a free trade agreement known as the Andean Pact was reached between Venezuela, Colombia, Bolivia, Peru and Ecuador. There is a tree trade agreement being forged by Argentina, Brazil, Uruguay, and Paraguay – when these four economies become integrated in 1995, they will have established a market of US$500 billion per year, with 195 million inhabitants, in an area of almost 12 million square kilometres. They will produce 13% of the world's meat while Brazil, Argentina and Uruguay will produce 17% of the world's poultry. Two orher pacts are in the offing. Central America is trying to revive its Common Market which was set up in the 1960s and collapsed in 1969. The five members – El Salvador, Honduras, Guatemala, Nicaragua and Costa Rica – decided in July 1992 to re-establish the common market by 1994. And, finally, there is a customs union to be created between the English speaking Caribbean countries.