Chapter 5

What Kind of Trade Integration Would the SCO’s Further FTA Be?

Engin Sorhun
University of Strasbourg, France

ABSTRACT

The Shanghai Cooperation Organization (SCO), whose the history dates back to “Shanghai five,” was founded in 1996 in order to deal with security and border issues. However, in the course of time, the organization has expanded the cooperation ground: the vision of the organisation has been recently enlarged so as to intensively emphasise economic issues such as forming a free trade area and initiating an economic integration. Since the potential economic effect is ambiguous and initially depends on the actual trade structure among the member countries, it is crucial for policymakers to have the right tools to evaluate the economic effect of such an initiative. The aim of this study is to provide practical guidance to policymakers for determining the potential economic effect of a further Free Trade Area (FTA) to be founded within the SCO. For this purpose, a set of indicators are used to determine the potential effect at regional and industrial levels that a possible regional trade arrangement may yield for the participating countries. It is concluded that there is a geographical bias towards trading among the members. To overcome this, there are two possible solutions for the SCO if it attempts a FTA: It should generate inter-industry and intra-industry trades and initiate new members.

INTRODUCTION

The security concerns in Post-Soviet period were initially the main motivation for the SCO. However, economic cooperation gradually became an area of growing interest for its members. Though economic cooperation has always been on the agenda of the SCO since its foundation it has only come to fore following the completion of the SCO’s institution-building and agenda expansion phase. In 2006 an Action Plan for the realization of the SCO Programme of Multilateral Trade and
Economic cooperation was initiated. It has been observed since a decade that the expectations of the member countries from the Organization have evolved. Since they reached a consensus on the initial concerns like security and border issues the economic cooperation has gradually gotten more importance. Especially, the global financial crisis engendered an accelerating impact on the economic ambitions of the SCO to cope with its negative effects as well as to enhance economic cooperation. During the discussion in the recent submits the Chinese leadership proposed the removal of tariff barriers and to opening-up of its market to the other members. Additionally, the Russian leadership proposed the introduction of a common unit of currency among the SCO members (Aris, 2011). Intention of forming a regional economic community on the basis of a free trade area (and further a customs union) has gained ground.

The growth in intra-regional trade is one of the dominant features of the world economy. Establishment of a free-trade area is thought to have a power of facilitating the realization of potential trade, translating into a more rapid growth of trade than. Although the net welfare effect of a FTA is ambiguous (Frankel, 1997; Panagaria, 2000; Iapadre, 2004) it is important for the countries to form one of it to understand the nature of trade relation with the other members and analyse analytically how much the proposed FTA is worth. For this purpose the international trade literature suggests two empirical a priori solutions for policymakers: (i) econometric solution which uses the Gravity Equation or Computable General Equilibrium (CGE) to predict the future gain from integration; and (ii) statistical solution which uses sophisticated trade indices and indicators to assess trade patterns and characteristics of a group of countries as well as change in trade patterns of individual countries in this group. There is a large literature for both of them.

However, indicator-based policymaking that focuses on tracking, monitoring and evaluation of the results of implemented policies consist of using statistical techniques to be employed in the consultative process. Considering the phases that the SCO has passed and the recent expansion of perspective of the Organization this study aims at analysing the nature and opportunity of a possible FTA within the SCO and suggests a set of statistical methods to evaluate the nature of a future formation of a FTA by the SCO. In this respect Cheong’s (2010) set of indicators is adopted in this study to analyse the SCO-case.

In the next section the technical information is given about the suggested indicators and the results are assessed. Subsequently, the conclusion and remarks are presented.

TRADE INDICATORS TO EVALUATE THE POTENTIAL ECONOMIC EFFECTS OF A POSSIBLE FTA OF THE SCO

To address the problem Cheong (2010) regroup trade indicators that can be used at initial stage before the formation of a FTA under two levels: regional level indicators that measure regional trade interdependence; and industrial level indicators that measure which sectors are efficient (or inefficient) and whether they are complementary (or similar).

REGIONAL LEVEL INDICATORS

There is an understandable linkage between the nature of the actual trade (trade volume, structure, bilateral relations, trade costs, etc.) and the further potential trade following the formation of a FTA. It is important to know how much volume of trade the participating countries already have.