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## The facilitation of trade by the rule of law: the cases of Singapore and ASEAN

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### 9.1 Introduction

Geography is unkind. This could be a result of historical accident, wars or colonial boundaries but the results are the same. The classical definition of the factors of production is land, labour and capital.<sup>1</sup> It is a fact of life that some countries have a limited supply of all three.

Soon after independence in the 1960s, this truth was evident to a small nation with a land area of 582 square kilometres, a population of 1.6 million, a literacy rate of 53 per cent, an unemployment rate of 13.5 per cent and a GDP per capita of US\$ 511 per annum.<sup>2</sup> The situation looked even bleaker because of the significant racial and social unrest, the complete lack of natural resources, limited agriculture and insufficient water supply. Government revenues were low and, because of the economic over-reliance on entrepot trade, revenue could not be raised by increasing customs duties. Few would have predicted survival, much less economic progress.

However, geography is not destiny. Fifty years later, that country has a GDP per capita of US\$ 52,051 per annum, a population of 5.3 million, a literacy rate of 96 per cent, an unemployment rate of 2 per cent and, through land reclamations, a land area of 723 square kilometres.<sup>3</sup> This is Singapore today. How did Singapore achieve this?

One clue lies in the data on the contribution of merchandise trade to the GDP of this country. While this contribution has fluctuated from 367.7 per cent just before the recent financial crisis began in 2008, to 265.6 per cent in the depths of the crisis in 2009, the merchandise trade contribution to GDP has been well over 250 per cent for a very long time.<sup>4</sup> Geography had bestowed one blessing on this country, in that it was fairly centrally located and had a deep sea port. This helped the growth of its entrepot trade but other, nearby ports could easily have competed in this regard if

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Singapore had only relied on its strategic location. From its colonial foundation, Singapore had the advantage of an essentially free trade port but this, by definition, does not bring in tax revenue because the imposition of any tariffs would undermine its trade. Thus, something else had to be done to capture other sources of revenue and encourage the relocation of industrial activities so as to provide more jobs than the trans-shipment of goods alone could provide.

After independence, this country adopted a three-pronged strategy to maximize its one advantage, its location. First, existing advantages were enhanced to facilitate entrepot trade, the expansion of the marine sector and the building of large oil refineries, while attendant services, such as logistics, transportation and tourism, were also developed. Secondly, new capabilities were created by incentivizing the use of technology and establishing procedures to review and reduce regulation and taxes. Finally, complementary policies were enabled by training bureaucrats to be strategically pro-enterprise and efficient, as well as developing education and labour policies in consultation with industry. Yet, despite the well-thought-out strategy and the impressive coordination between the various actors, these efforts would not have borne fruit without one necessary (though not, of itself, sufficient) trade reform – strengthening the rule of law.

## 9.2 The rule of law

Nobel Prize-winning economist F. A. Hayek, commenting on the value of the rule of law to economic development, said that individuals (including corporations) would be able to make wise investments and future plans with some confidence of a profitable return on investment if “under the Rule of Law the government is prevented from stultifying individual efforts by ad hoc action [so that] [w]ithin the known rules of the game the individual is free to pursue his personal ends and desires, certain that the powers of government will not be used deliberately to frustrate his efforts” (Hayek, 1994). Hayek contrasted the rule of law with arbitrary government but did not provide a specific definition of it.

There are many definitions of the rule of law, and there is much debate about its core elements. The World Justice Project (WJP) definition of the rule of law is probably one of the most persuasive when considering how a system may be created in order to avoid arbitrary governance.<sup>5</sup> The WJP suggests that the rule of law is a system in which four universal principles are upheld:

- The government and its officials and agents as well as individuals and private entities are accountable under the law.

- The laws are clear, publicized, stable and just, are applied evenly, and protect fundamental rights, including the security of persons and property.
- The process by which the laws are enacted, administered and enforced is accessible, fair and efficient.
- Justice is delivered [in a] timely [manner] by competent, ethical, and independent representatives and neutrals who are of sufficient number, have adequate resources, and reflect the makeup of the communities they serve.

Singapore scores well on perceived absence of corruption, order and security, regulatory enforcement, civil justice and criminal justice. There may be room for improvement with regard to limited government powers, fundamental rights and open government. Arguably, there may be an over-reliance on the presence of a pro-business and long-time incumbent government as an assurance for investors that there is a firm commitment to the rule of law despite the relatively lower levels of perceived checks and balances to the actions of the government.<sup>6</sup>

In any event, its high rankings in regional terms, even for those areas coupled with the strong scores in other areas, makes Singapore an attractive base and hub for the region. With limited endowments of the factors of production and a small domestic market, Singapore has managed to use the rule of law to facilitate its trade and increase its connectivity to the region. This was critical in order to attract foreign multinational corporations (MNCs) to invest in Singapore, set up factories and provide jobs for the local population. With severe supply-side constraints, Singapore attracted investors by assuring them of their legal rights. This led to Singapore's growth as a hub for production and trade facilitation in the region.

**Table 1** World Justice Project scores and rankings for Singapore

Factors	Scores	Global rankings	Regional rankings	Income group rankings
Limited government powers	0.73	21/97	4/14	19/29
Absence of corruption	0.91	7/97	2/14	7/29
Order and security	0.93	1/97	1/14	1/29
Fundamental rights	0.73	26/97	5/14	23/29
Open government	0.67	19/97	6/14	18/29
Regulatory enforcement	0.80	10/97	4/14	10/29
Civil justice	0.79	4/97	1/14	4/29
Criminal justice	0.87	3/97	1/14	3/29

Source: World Justice Project (<http://worldjusticeproject.org/country/singapore>).

9.3 The domestic facilitation of trade by the rule of law

But what is the most important rule-of-law factor for economic development through trade facilitation? Ikenson has charted the relationship between the perception of corruption and logistics performance. As Figure 1 shows, he concluded that, “There appears to be a fairly strong relationship between levels of corruption (as measured in Transparency International’s Corruption Perceptions Index [CPI]<sup>7</sup>) and logistics performance (as measured in the [Logistics Performance Index]<sup>8</sup>). Countries where the perception of corruption is lower are more likely to perform better on logistics perceptions; and countries where corruption is more pronounced appear to have greater frictions in their logistics environments” (Ikenson, 2008).

While both indices are based on perception, there seems a fairly strong correlation between the perception of high levels of corruption and the perception of less effective logistic performance. This is not to say that the absence of corruption is the only important factor of the rule of law. It is not. However, when one looks at Table 2, also compiled by Ikenson (2008), the effects on the financial calculus can be clearly

**Figure 1** Relationship between perceived corruption and logistics performance



**Source:** World Bank and Turku School of Economics (Finland), Logistics Performance Index, <http://info.worldbank.org/etools/tradesurvey/mode1.b.asp>, and Transparency International, Corruption Perceptions Index, <http://www.transparency.org/>.

Note: Each point is a country’s set of scores for both indices.

**Table 2** Various trade facilitation metrics by region or country, 2008

Region or Economy	Documents for export (number)	Time for export (days)	Cost to export (US\$ per container)	Documents for import (number)	Time for import (days)	Cost to import (US\$ per container)
East Asia and Pacific	6.9	24.5	885	7.5	25.8	1,015
Eastern Europe and Central Asia	7.0	29.3	1,393	8.3	30.8	1,551
Latin America and Caribbean	6.7	22.6	1,096	7.7	24.0	1,208
Middle East and North Africa	7.1	24.8	992	8.0	28.7	1,129
OECD	4.5	9.8	905	5.0	10.4	986
South Asia	8.6	32.5	1,180	9.1	32.1	1,418
Sub-Saharan Africa	8.1	35.6	1,660	9.0	43.7	1,986
<b>All countries</b>	<b>7.0</b>	<b>26.1</b>	<b>1,230</b>	<b>7.8</b>	<b>29.7</b>	<b>1,412</b>
United States	4.0	6.0	960	5.0	5.0	1,160
Singapore (best)	4.0	5.0	416	4.0	3.0	367
Kazakhstan (worst)	12.0	89.0	2,730	14.0	76.0	2,780

Source: International Finance Corporation and the World Bank, *Doing Business*, "Trading Across Borders" (<http://www.doingbusiness.org/ExploreTopics/TradingAcrossBorders/>).

seen. A businessperson, when trying to decide where to ship goods to and from, will have three main costs to consider – the financial, time and transactional costs – for each container he or she ships. The lower these costs are, the more attractive a port or hub will be. Singapore makes the businessperson's decision relatively easy. This is the moral of the Singapore story – if you lower the costs for business through the rule of law, traders (and investors) find you more attractive.

Many developing countries today face significant supply-side constraints such as inadequate infrastructure, unavailability of a skilled workforce and insufficient capital for businesses to expand. These problems require a large investment of time and financial resources to address and often do not produce the hoped-for results. One reason for this is that attempting to address these concerns without first addressing the need for improvement in the rule of law is akin to trying to fill a sieve – all the

money, effort and time leaks out. For example, improving trade facilitation may require some coordination but the steps that need to be taken are relatively straightforward – apply international procedures, reduce paperwork, incorporate more technology and keep looking for ways to be more efficient. Many countries have received grants and expert advice and have embarked on projects to do just that, and indeed many have implemented various strategies in this regard. The World Bank reports that in 2006 it took, on average, 26 days to export and 30.4 days to import a standardized cargo of goods by ocean transport (with every official procedure recorded but actual time on the ocean excluded), whereas it now takes, on average, 22.2 days to export and 25 days to import (World Bank, 2013). There has been some improvement but it still takes a lot of time in some countries. The resistance to change can in part be attributed to vested interests and corruption, as every form that is made obsolete represents the reduction of an opportunity for customs officials to engage in rent-seeking behaviour. This underscores the importance of the rule of law for maximizing both trade and investment opportunities.

It is submitted, therefore, that the rule of law has the potential to assist supply-side-constrained countries by granting them a comparative advantage and a strong basis to attract investment in order to supplement areas in which they are, by reasons of geography or history, found to be lacking.

## 9.4 Regional trade facilitation by the rule of law: the case of ASEAN

Moving from the situation of a single country to the developmental needs of a region, in this case the South East Asian region, similar supply-side constraints for most of the regional economies can be seen. Some countries may have been blessed with natural resources and others with populations large enough for the domestic market to develop significant contributions to development, but all (perhaps with the exception of current-day Singapore) have limited capital. Moving from the particular to the more general, could the rule of law also alleviate the supply-side constraints of countries in this region?

The forum for economic activity in the region is now the Association of South East Asian Nations (ASEAN). ASEAN was established on 8 August 1967 in Bangkok, Thailand, with the signing of the Bangkok Declaration<sup>9</sup> by Indonesia, Malaysia, the Philippines, Singapore and Thailand. Brunei Darussalam joined on 8 January 1984, Viet Nam on 28 July 1995, Lao People's Democratic Republic and Myanmar on 23 July 1997, and Cambodia on 30 April 1999, making up what are today the ten member states of ASEAN.

ASEAN was conceived as a political enterprise aimed at building trust among the largely post-colonial regional states, which were wary of each other. ASEAN did this well through the “ASEAN Way” of cooperation and dispute resolution in which members do not interfere with the internal affairs of other members and decision-making (as well as dispute resolution) is done only by consensus. While this has enabled ASEAN to reduce regional conflicts (albeit as a relatively “informal” organization), ASEAN has often been criticized for its “ASEAN Way” and its seeming adherence to the principle of non-interference. Many commentators suggest that this adherence to non-interference and consensus undermines the rule of law and ASEAN’s seriousness to integrate (Goh, 2003).<sup>10</sup>

However, the adoption of the ASEAN Charter in 2007 and its ratification by all ten ASEAN states in 2008 marked the beginning of a new self-understanding for ASEAN. The Charter declares that member states will act in accordance with the rule of law, international law and ASEAN rules. The law was for the first time laid as a foundation for ASEAN integration. At the same time, the ASEAN member states also issued a Declaration on the ASEAN Economic Community (AEC) Blueprint<sup>11</sup> which adopted the AEC Blueprint<sup>12</sup> for the implementation of the AEC by 2015. The Declaration states that “[t]he AEC Blueprint will transform ASEAN into a single market<sup>13</sup> and production base, a highly competitive economic region, a region of equitable economic development, and a region fully integrated into the global economy” (note 6, para 1). Article 1(5) of the Charter sets out the purposes of ASEAN, one of which is “to create a single market<sup>14</sup> and production base”. ASEAN declared that it was going to integrate economically and that one major strategy for that integration would be the rule of law.

The integration of ASEAN will be challenging. The combined population of ASEAN, at approximately 600 million,<sup>15</sup> may compare favourably with that of the European Union (EU), at 500 million.<sup>16</sup> However, even with the financial crisis in Europe, in 2011 the combined GDP of ASEAN was only US\$ 2.3 trillion<sup>17</sup> compared with the EU’s US\$ 17 trillion.<sup>18</sup> Thus, any impressionistic understanding of ASEAN integration revolving around a marketplace for ASEAN goods will have to be moderated by the short-term reality that the consumers in ASEAN at the moment are not wealthy enough to buy many of the goods ASEAN produces. Intra-ASEAN trade, which, on average, comprises only one-quarter of total annual ASEAN trade<sup>19</sup> (compared with intra-European Community trade which comprised nearly half of members’ trading activity from 1958-1972 [Mongelli, Dorrucci and Agur, 2005]) is currently not a driving force in ASEAN integration. This current limitation in the buying power of ASEAN consumers is obviously illustrated by the fact that in 2011 the GDP per capita for ASEAN as a whole was only about US\$ 3,600.<sup>20</sup> This partially explains why the contribution of intra-ASEAN trade to total ASEAN trade has been stuck at 25 per cent for the last 10 years.

ASEAN also faces integration challenges because of the great diversity in the application of the rule of law among the ASEAN member states.<sup>21</sup> The European model of integration was built on the somewhat more established rule-of-law systems of its members whereas the post-colonial legal systems of many ASEAN members still remain less developed. One indicator of this is that, despite the current financial crisis and the exposure of bureaucratic and parliamentary failures, EU member states all rank in the top half of Transparency International's CPI rankings for 2012, with Italy and Bulgaria the lowest ranked at 72 and 75 respectively. By contrast, as illustrated in Table 3, seven out of the 10 ASEAN members rank in the bottom half of the index, with Myanmar almost at the bottom with a ranking of 172 (Transparency International, 2012).

This perception of corruption (even if unjustified) undermines investors' confidence and poses a real problem for ASEAN economic integration, for the following reason. With the relatively less affluent domestic market of ASEAN, in the short term, the main economic objective for ASEAN should be the development of the production base referred to in the ASEAN Charter through the facilitation of integrated production networks (IPNs) created by MNCs. When an IPN becomes transnational, it faces several challenges. The main challenge beyond the cost of transport and logistics planning is ensuring that the rules applicable to each actor in the network remain predictable and certain. Where the IPN operates in countries where the rule of law is weaker, guarantees against arbitrary intervention and discrimination become more critical for the continued effective functioning of the IPN. If investors

**Table 3** Transparency International's Corruption Perceptions Index, 2012

Country	Country ranking		CPI score	Score
	2011 <sup>1</sup>	2012 <sup>2</sup>	2011	2012
Singapore	5	5	9.3	87
Brunei Darussalam	44	46	5.5	55
Malaysia	60	54	4.4	49
Thailand	80	88	3.5	37
Philippines	129	105	2.4	34
Indonesia	100	118	2.8	32
Viet Nam	112	123	2.7	31
Cambodia	164	157	2.1	22
Lao PDR	154	160	2.1	21
Myanmar	180	172	1.4	15

Source: Transparency International, Corruption Perceptions Index 2012.

Notes: 1. 2011 surveyed 183 countries and territories.

2. 2012 surveyed 176 countries and territories.



do not trust the strength of the rule of law in the region, less investment will flow in and this will limit the development of regional IPNs.

The automotive industry is frequently put forward as one of the best examples of IPNs in Europe, and that may well be true. Direct production of cars accounts for 2.2 million jobs and another 9.8 million jobs in closely related sectors (ACEA, 2010). While the creation of the European single market indirectly created the environment for new networks of businesses and production, in ASEAN, counter-intuitively, these networks already exist, despite some trade barriers. Rather than lobbying to change the legal environment to create a climate for such networks, Asian businesses often took advantage of the less-than-transparent discretion provided to policy-makers at all levels in many ASEAN countries and, instead, obtained specific solutions to the trade barriers they faced without insisting on formal obligations.

This increased regional trade and, since the 1980s, subject to the changing players and gravitational forces, much of the intra-ASEAN trade consists of components which are part of the production chains of “Factory Asia”, with one state being part of a process that culminates in a final product for export to developed countries. In 1985 there were only four major trade-in-goods players in the Asian region: Malaysia, Indonesia, Japan and Singapore. Resource-rich states Malaysia and Indonesia would supply resources to Japan, while Singapore manufactured component parts for assembly in Japan which would then be exported to the West (WTO and IDE-JETRO, 2011).

The gravitational forces changed when, in 2001, China joined the WTO and began to access Japan’s current supply chain of component parts. By 2005 the centre of gravity had shifted to China, with it being the main market for all component products from the Asian region. The competitiveness of China’s export trade is not only attributable to its cheap labour but also to the intermediate, high-quality goods/products it receives from the other Asian countries (and in particular ASEAN member states) which are part of the IPN or, as referred to in the WTO and IDE-JETRO report, the global value chain (GVC) structure. ASEAN countries today produce parts, accessories and components and export them to China which, copying the previously successful Japanese model, then assembles the products and exports the finished products principally to the West. Thus, unrestricted regional trade is “an important building block for the region’s economic strength, and consequently disruptions – whether political or administrative – put this competitiveness at risk” (Dieter, 2007).

But if “Factory Asia” already exists, what gains may be made with the ASEAN Charter and its emphasis on the rule of law? To answer this, a closer look into the state of “Factory Asia” is required.

Writing about the development of the automotive market in Europe, Dieter points out that “without the creation of a single regulatory sphere, the integration processes could not have taken place” (Dieter, 2007). He suggests that the expansion of the EU itself enlarged the space for business while the PANEURO scheme (that allowed for the cumulation of origin) increased the area available for sourcing of components without having to consider the local content requirements of the EU. By contrast, writing in 2006, Baldwin characterizes East Asian regionalism as being “a mess”, in that, while there is a high level of regional division of labour in the production process, there has been limited legalization of the process. He suggests that the problem with “Factory Asia” is not a plan but the management of the plan, highlighting that the unilateral tariff-cutting that created “Factory Asia” is not subject to the WTO discipline (binding) or any alternative legal disciplines (Baldwin, 2006). This has resulted in a business environment which is less transparent and less certain than that of Europe, but one which is no less productive. Dieter (2007) further shows that the production of automobiles and electronics in East Asia is relatively integrated in practice but is facing headwinds of protectionism and inconsistent governmental policies.<sup>22</sup> The strengthening of the rule of law would reassure investors worried about arbitrary practices and regional backsliding towards protectionism.

## 9.5 The value of international investment agreements

How can the rule of law be strengthened regionally? It begins with international commitments between the ASEAN members. While much has been said about the value of ASEAN’s commitments to lower tariffs, creating a single window for customs clearances and increasing intra-ASEAN connectivity, the rule of law will be foundational for all these endeavours.

Some economies with low natural endowments and relatively small markets, such as Costa Rica, Hong Kong (China) and Singapore, have succeeded in attracting substantial amounts of foreign direct investment (FDI). Investors are attracted to their investor-friendly tax regimes, good infrastructure and high quality human resources, as well as their strong rule of law built on an effective domestic legal, administrative and judicial infrastructure. Unfortunately, the domestic legal infrastructure is often inherently quite resistant to change due to interest capture and the need to build human resource capacity. An extra-domestic system is therefore (at least in the short term) easier and quicker to implement. It could also act as a governance facilitator for the domestic system by introducing more transparency and accountability and, potentially, remedies for domestic system failures. In addition to assuring investors by creating an international obligation, the state would also create incentives for domestic reform.

Many studies have been conducted to analyse the efficiency of international investment agreements (IIAs) in attracting FDI (UNCTAD, 2009). Some point to China and Brazil as countries with few, if any, IIAs but which have been successful in attracting significant FDI. Nevertheless, China and Brazil are exceptions because both have large markets and, in the case of Brazil, significant natural endowments. Other countries may be less fortunate. In comparing the effectiveness of IIAs, often the difficulty is establishing the counterfactual.

Indeed, the Executive Directors of the International Bank for Reconstruction and Development (World Bank), in their 1965 report on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) stated that, while they thought that “private capital will continue to flow to countries offering a favorable climate for attractive and sound investments, even if such countries did not become parties to the Convention [...] adherence to the Convention by a country would provide additional inducement and stimulate a larger flow of private international investment into its territories” (IBRD, 1965). The ICSID Convention ensures access to third-party dispute settlement mechanisms for an investor investing in another country, provided the country and the investor’s country of nationality are parties to the Convention. This assures investors who may not trust a domestic legal system.

ASEAN has recognised the significant role that an IIA can play in attracting FDIs. In 2009, they concluded the ASEAN Comprehensive Investment Agreement and, soon after, the ASEAN–Australia–New Zealand Free Trade Agreement, with an investment chapter, as well as agreements on investment under the Framework Agreement on Comprehensive Economic Cooperation, with the Republic of Korea and the People’s Republic of China respectively.<sup>23</sup>

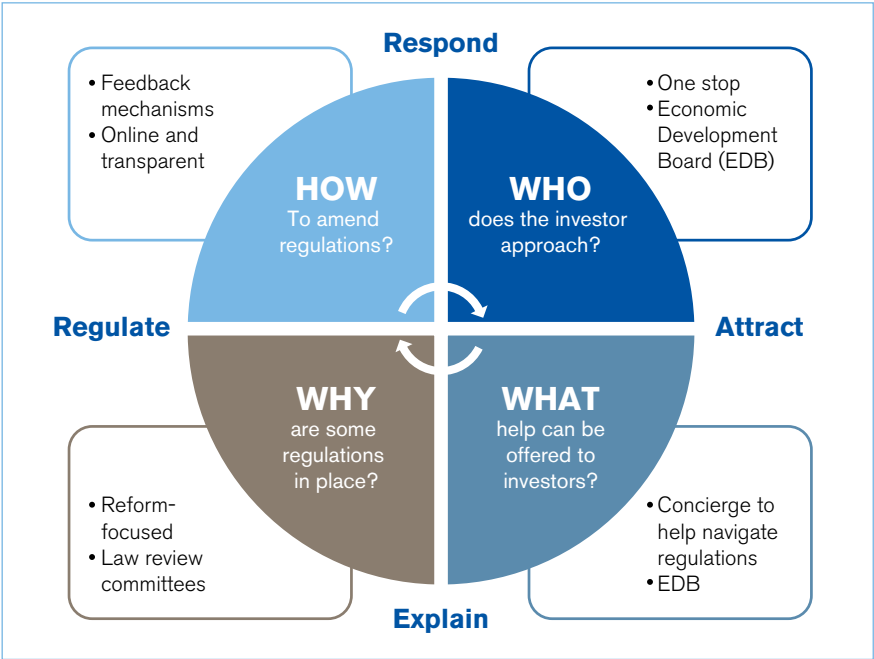
These IIAs require ASEAN members to provide clear rules and procedures, and that disputes be settled by independent adjudicative means. It should be noted that the provisions of these IIAs have been refined from being purely pro-investor to demonstrating understanding of the current investment context in which all the countries involved are capital-importing and capital-exporting countries. They attempt to strike a balance between preserving policy space for a government to regulate matters which are critical to the country and legal rules which provide foreign investors with confidence. This includes the matter of ensuring sustainable development of the country with sound environmental policies.

For regional stakeholders, these IIAs enable investors from the region to expand regionally. In the past, only MNCs or strong interest groups possessed the power to influence the policy-making process. However, with these IIAs, for the first time, all

investors, under the shadow of compulsory investor-to-state adjudication, have access to tools of persuasion based on legal obligations.

In this context, it should be noted that the WJP's four universal principles upheld by the rule of law, stated above, also correspond to the concept of legalization of international obligations between states. This has been defined as obligation, precision and delegation, meaning that states and other actors are legally bound by the rules, that the rules are clear and compliance is monitored, and that disputes are adjudicated by independent parties (Abbott et al., 2000). The WJP adds to this a focus on the administration and enforcement of the law. This is useful, since relying on litigation is a poor alternative to efficient and effective administration. Litigation is not a good system for policy-making and governance. It is episodic and expensive and usually only results in binary decisions. It acts as a useful last resort which encourages more reasonable negotiation and better governance. Regional governments could, therefore, also introduce processes to obtain feedback from investors (both domestic and foreign) and mechanisms to incorporate that feedback into their policy-making. Figure 2 illustrates one such process based on Singapore's experience.

**Figure 2** Investor-centric feedback loop



Source: Prepared by the authors.

Rather than waiting for investors to complain about policies and regulations, Singapore instituted proactive procedures to attract investors by creating a one-stop entity to manage foreign investors – the Economic Development Board (EDB). The EDB was tasked with helping investors navigate regulations and, at the same time, fed back to relevant governmental bodies information about the obstacles faced by investors. Steps were then taken in a relatively transparent manner to see how these laws and policies could be fine-tuned. By making it easy for investors through a process of explanation, facilitation and reform, Singapore was able to make itself more attractive and, at the same time, reduce the legal risks associated with the binding commitments created by the IIAs.

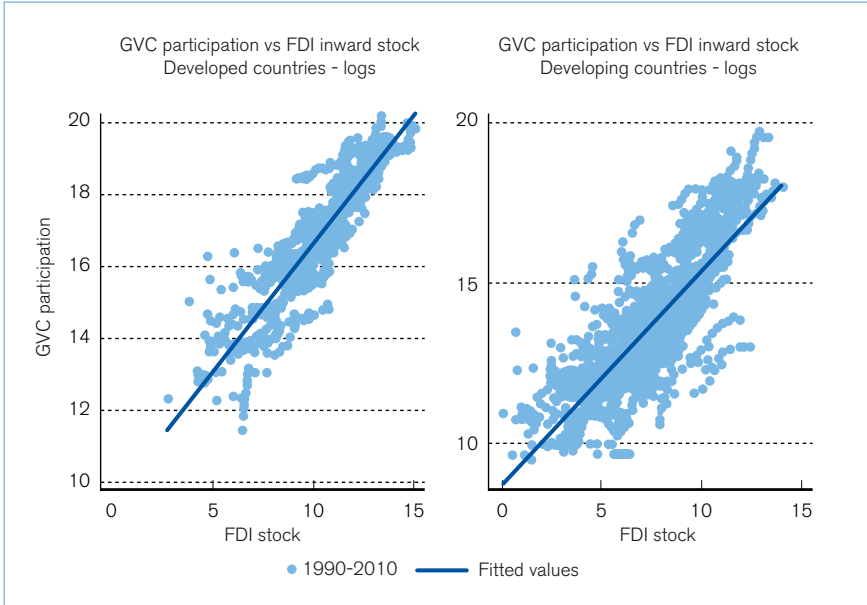
## 9.6 Conclusions

Singapore built on its colonial free trade policies by joining the General Agreement on Tariffs and Trade (GATT) in 1973 and, later, the WTO, thereby adding binding legal obligations to its already liberal trade policies. Together with commitments made in a number of IIAs and an effort to embed a domestic rule-of-law system, these assurances provided investors with the confidence to invest in a country with otherwise very limited factors of production and an insignificant internal market. These investors initially invested in factories which produced goods. But even today, when the high cost of production has made Singapore less competitive for the production of goods, the country enjoys a status as a hub for high-premium services such as banking, finance and logistics for many of the GVCs in Asia, because of this commitment to the rule of law.

If one includes Cambodia, which entered ASEAN in 2004, Viet Nam, which entered in 2007 and Laos, which entered in 2013, all ASEAN members have now committed themselves to the rules of the WTO and the dispute settlement process for the enforcement of such rules. As discussed above, ASEAN members have also committed themselves to various WTO-plus rules in IIAs, both between themselves and with major regional trade partners. Despite the poor rankings of most ASEAN members with regard to perceived corruption, this makes the region more attractive to investors, who should feel more reassured by having such binding international rules and the attendant international processes for the enforcement of the rules.

A recent UNCTAD study (illustrated in Figure 3) shows that the expansion of the operations of MNCs through FDI has been a major driver of growth of GVCs, as illustrated by the close correlation between FDI stocks in countries and their GVC participation (UNCTAD, 2013). Therefore, ASEAN members with supply-side constraints benefit significantly from the development of the rule of law regionally, as this makes the region more attractive to major investors seeking to set up IPNs.

**Figure 3** Foreign direct investment and participation in global value chains, 1990–2010



**Source:** UNCTAD-Eora GVC Database, UNCTAD FDI Database, UNCTAD analysis.

**Note:** Data for 187 countries over 20 years. The regression of the annual GVC participation growth on the annual FDI inward (stock) growth yields a positive and significant correlation (at the 5 per cent level) both for developed and developing countries ( $R^2 = 0.77$  and  $0.44$ , respectively). The correlation remains significant considering the two time periods 1990–2000 and 2001–2010 separately. Regressions use lagged (one year) inward FDI (stock) growth rates and include year fixed effects to account for unobserved heterogeneity.

This has the twin advantages of increasing trade and attracting much-needed capital for the development of those ASEAN countries.

This chapter has focused on the example of one country, Singapore, and one region, as represented by ASEAN, and the way in which the rule of law could maximize their potential for economic growth in the face of supply-side constraints. It is suggested here that the strategy of committing to international trade and investment rules as well as international dispute resolution helps to reassure investors. If this is coupled with a domestic system based in the rule of law that supports trade facilitation, even countries with severe supply-side constraints may be able attract FDI from MNCs and thereby gain more opportunities to participate in GVCs. This capital and technology inflow could result in improvements in infrastructure and increased capacity and productivity of the labour force, with the consequent technology transfer allowing that country to more actively participate in global trade.

However, there is no “one-size-fits-all” approach which would see the implementation of specific solutions for all situations. While some basic principles can be drawn from the “Singapore story”, it is idiosyncratic. ASEAN itself is only gradually finding common ground amongst its 10 very disparate members on the advancement of regional integration through the promotion of common principles of the rule of law.<sup>24</sup> It is, therefore, worth remembering the words of former Brazilian Minister Luiz Carlos Bresser Pereira: “Institutions can at most be imported, never exported” (Przeworski, 2004). Locally grounded solutions are required to ensure that the commitment to the rule of law is sustainable over time.

## Endnotes

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1. See “Factors of production”, “Capital”, “Human capital” and “Land” under the Glossary of Terms in Samuelson, P. A. and W. D. Nordhaus (2005), *Economics*, New York, McGraw-Hill (18th ed.). Some scholars argue that energy, human capital and entrepreneurship may be added to the picture but they can also be incorporated into the classical factors.
2. See historical data at: [www.singstat.gov.sg](http://www.singstat.gov.sg)
3. See 2012 data at: [www.singstat.gov.sg](http://www.singstat.gov.sg)
4. See: <http://data.worldbank.org/indicator/TG.VAL.TOTL.GD.ZS>
5. See: <http://worldjusticeproject.org/what-rule-law>. See also: Ginsberg, T. (2011), “Pitfalls of measuring the rule of law”, *Hague Journal on the Rule of Law* 3(2): 269-280.
6. Academic studies have suggested that central to economic growth is the perceived commitment of a government to the rule of law. While this is often achieved via the existence of institutional checks on government, arguably other factors could support strong commitment levels, including the stability and duration of the political system, the existence of credible challenges to authority or the extent to which the executive’s own support base would be harmed by an adverse shift in policy. See: Haggard, S., A. MacIntyre and L. Tiede (2008), “Rule of law and economic development”, *Annual Review of Political Science* 11: 205-234.
7. The Corruption Perceptions Index is developed by Transparency International. Higher rankings indicate the country is perceived to be less corrupt. The Index basically scores countries based on how corrupt the public sectors are seen to be. The data is sourced from independent institutions specializing in governance and business climate analysis. The index captures perceptions of the extent of corruption in the public sector, mainly from the perspective of business people and country experts.
8. The Logistics Performance Index is developed by the World Bank. Higher rankings indicate better logistics performance based on the performance along the logistics supply chain within a country. The Index is based on a survey of operators on the ground (global freight forwarders and express carriers), providing feedback on the logistics “friendliness” of the countries in which they operate and those with which they trade. The operators combine in-depth knowledge of the countries in which they operate with informed qualitative assessments of other countries with which they trade and experience of the global logistics environment.

9. See: <http://www.asean.org/news/item/the-asean-declaration-bangkok-declaration>
10. Goh (2003) provides an overview of the criticism and a response that separates the "ASEAN Way" and the principle of non-intervention. For an historical perspective of the "ASEAN Way", see Acharya, A. (2001), *Constructing a security community in Southeast Asia: ASEAN and the problem of regional order*, London and New York, Routledge (2<sup>nd</sup> ed.). Other criticisms of the "ASEAN Way" can be found in books/articles by Shaun Narine.
11. See: <http://www.asean.org/news/item/declaration-on-the-asean-economic-community-blueprint>
12. See: <http://www.asean.org/archive/5187-10.pdf>
13. To most people, a single market is synonymous with a customs union which includes free movement not only of goods but also of labour, services and capital. The most famous single market, the European Union (EU), began life as the European Coal and Steel Community in 1951 (Treaty of Paris, 1951) and went on to become the European Economic Community (EEC) in 1957 (Treaty of Rome, 1957) (when it became known in the United Kingdom and Ireland as "the Common Market"). The abolition of internal tariff barriers was achieved in 1968. The Single European Act was signed in 1986 to establish a Single European Market by 1992, by removing the barriers to free movement of capital, labour, goods and services.
14. The AEC will have free movement of goods, services, *skilled* [our emphasis] labour and *freer* [our emphasis] movement of capital (see para 9 of the AEC Blueprint) but is unlikely to be a customs union. This is because a customs union has to create a common external tariff policy. Singapore has an almost zero tariff policy (only beer, stout, samsu and medicated samsu are subject to tariffs, although a universal excise tax is imposed on goods such as cigarettes, automobiles and wine). This means that Singapore's tariffs will have to go up or that other ASEAN members' tariffs will have to go down significantly to implement a common external tariff policy. Furthermore, Singapore will have to give up many of its FTAs with non-ASEAN partners unless those partners agree with all the other ASEAN partners or the preferential tariff rates are harmonized with the ASEAN common external tariff rates (thus making the FTAs superfluous, at least for goods).
15. ASEAN (2012), *ASEAN Community in Figures 2012* (ACIF 2012) ([http://www.asean.org/images/2013/resources/publication/2013\\_ACIF\\_2012%20Mar.pdf](http://www.asean.org/images/2013/resources/publication/2013_ACIF_2012%20Mar.pdf))
16. EUROSTAT (2011), *Europe in Figures: Eurostat yearbook 2011*, Luxembourg, Publications Office of the European Union, p.109.
17. ASEAN (2012), *ASEAN Community in Figures 2012* (ACIF 2012).
18. *International Monetary Fund, Report for selected country groups and subjects* (<http://www.imf.org/external/pubs/ft/weo/2012/01/weodata/weorept.aspx?sy=2010&ey=2010&scsm=1&ssd=1&sort=country&ds=.&br=1&c=998&s=NGDPD&grp=1&a=1&pr1.x=75&pr1.y=15>)
19. ASEAN (2012), *ASEAN Community in Figures 2012* (ACIF 2012).
20. ASEAN (2012), *ASEAN Community in Figures 2012* (ACIF 2012).
21. See also: Agrast, M. D. et al. (2013), *The World Justice Project: Rule of Law Index 2012-2013*, Washington, DC, World Justice Project. The Index compares Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Viet Nam. It did not gather data for Brunei Darussalam, Lao People's Democratic Republic or Myanmar.
22. Dieter (2007), note 35, p. 41-42



**23.** For a description of these ASEAN IIAs, see: Ewing-Chow, M. and G. R. Fischer (2011), "ASEAN IIAs: Conserving regulatory sovereignty while promoting the rule of law?" *Transnational Dispute Management* (8)5: 1-12.

**24.** For a very detailed study of this, see National University of Singapore, Centre for International Law (2009-), ASEAN Integration Through Law: The ASEAN Way in a Comparative Context Project (<http://cil.nus.edu.sg/research-projects/cil-research-projects/asean/>), from which a series of books is forthcoming, to be published by Cambridge University Press.

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