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Trading places: the 'Commonwealth effect' revisited

Joanna Bennett, Paul Chappell, Howard Reed and Dhananjayan
Sriskandarajah

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About this paper

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Introduction

Today, the Commonwealth is an association of 54 countries, spanning 6 continents with a combined population of over 2 billion people worldwide. Evolving out of the British Empire – a gentle anaesthetic to ease the pain of de-colonisation – the Commonwealth is now a modern voluntary association of equal, sovereign states. But it seems that longstanding questions about the relationship between trade and empire remain relevant even today.

When the modern Commonwealth was born in 1949, the economic ties that linked Britain and its former colonies were strong. Indeed, while there may have been debate at the time about what sort of political association would benefit the changing world order, the trade and investment links across the Commonwealth were taken for granted. Yet, during the 1950s and 1960s, economic links between Commonwealth countries began to weaken, not least because of the winding down of Commonwealth preference in British trade.

The emergence of new engines of economic growth around the world and a new globalised regime of trade preferences followed soon after and the relative importance of the Commonwealth as a trading bloc began to fall away. In recent years, as Commonwealth countries such as India, Nigeria, South Africa, Malaysia and Trinidad and Tobago have developed rapidly, considerably overhauling their trading profiles, it would seem that this trend has continued.

As its economic relevance slipped, so the stature of the modern Commonwealth as a political association began to grow. Although its members were now independent states, the association provided an important vehicle to formalise and underpin the networks, commonalities and shared values that had blossomed in colonial times. In an era of relatively few international associations, the Commonwealth pioneered international cooperation at the political level, promoting democracy, human rights and sustainable development.

Yet, since the late 1980s, changing geopolitical realities and the growth of other multilateral political bodies have led some commentators to argue that the Commonwealth has lost some of its political salience. This was signified most recently at the November 2009 Commonwealth Heads of Government Meeting (CHOGM) in Trinidad and Tobago when leaders called for the creation of an Eminent Persons Group (CHOGM 2009) to explore options for raising the profile of the association and improving its efficacy.

In their relative importance, the economic and political aspects of this association's complex identity appear to have adopted an almost rhythmic ebb and flow. For, in keeping with the patterns of the past, just as the political relevance of the Commonwealth is being questioned, trade and business links are seen once again to be of growing interest.

One of the first concrete indications of this shift came in 1997, when, following the Edinburgh Declaration (CHOGM 1997) Commonwealth leaders agreed to an explicit focus on the economic, financial and business aspects of the association. To this end, the Commonwealth Business Council was established to promote trade and investment and to increase the role of the private sector in national economies.

Despite the changing face of global trade and an apparent decline in the Commonwealth's relevance as a trading bloc, there is considerable evidence that intra-Commonwealth economic links remain strong.

Intra-Commonwealth investment flows have exceeded 180 billion US dollars (CBC, 2008); and its countries have seen over 200 billion US dollars worth of investment over the last ten years (Kaul, 2010). The business-related aspects of Commonwealth membership seem to be increasingly attractive to current and potential member states. For example, it is estimated that an estimated 1 billion US dollars worth of new business and investment deals were done on the fringes of the 2009 CHOGM, yielding a significant windfall to the host country, Trinidad and Tobago.¹

Similarly, in explaining Rwanda's interest in joining the Commonwealth, President Paul Kagame has repeatedly highlighted increased trade, investment and business opportunities as a primary motivation:

“We hope to tap into the trade and investment opportunities that the Commonwealth offers so that Rwanda can expand its economy and effectively participate in the global marketplace.” (Kagame 2010).

It is in the context of this seeming resurgence in the perceived economic importance of Commonwealth membership, and as questions are being raised about the Commonwealth's political identity (see, e.g. Afari-Gayan, Jahangir and Sheehy, 2009; Bennett, Sriskandarajah and Ware, 2010), that this paper seeks to present the facts behind the theory.

The first and most notable attempt to assemble a comprehensive data set on trade and investment relationships within the Commonwealth was made in the late 1990s by Lundan and Jones (2001). In a paper entitled 'The "Commonwealth Effect" and the Process of Internationalisation', they set out to analyse the significance of a 'Commonwealth effect' on trade and investment.

They concluded that there is an overall tendency for high levels of intra-Commonwealth trade and investment, even when factors such as regional trade agreements or geographical proximity are taken into account. They did

¹ Figure quoted by Dr Mohan Kaul, Director General of the Commonwealth Business Council, in interview with Commonwealth Secretariat website, <http://www.thecommonwealth.org/news/34580/212269/218481/110110mohankaulprofile.htm>

however note that simple linear predictions of future trade shares showed a gradual decline in intra-Commonwealth trade in the decade ahead.

This paper sets out to update the Lundan and Jones research; to establish whether the 'Commonwealth effect' still exists; and to find out what might lie behind it.

Methodology

Our analysis of trade patterns uses data from the UN's COMTRADE database for the years 1990 to 2008 inclusive. COMTRADE contains data on trade between pairs of countries.

In our analysis, we use a regression model where the dependent variable is trade (measured in US dollars) in a calendar year between each pair of countries. The dataset is thus made up of country *pairs*. For a given pair of countries, *a* and *b*, there are two trade flows: the flow of commodities from *a* to *b*, and the flow from *b* to *a*. However, COMTRADE reports *four* trade values for each country pair: (1) exports from *a* to *b*, (2) exports from *b* to *a*, (3) imports from *b* to *a* and (4) imports from *a* to *b*. If measured in a completely consistent manner, (1) and (3) would be the same and (2) and (4) would also be the same. However, differences in accounting and measurement mean that exports from *a* to *b* do not always equal imports into *b* from *a*. Because of the measurement differences, we divide the COMTRADE data into two, using the import data and the export data separately.

We estimate an OLS regression model where for the 'home' country (*a*) the dependent variable is trade with the partner country (*b*), which is either an import or an export measure, depending on the dataset used. This is expressed as a share of the home country's GDP in the relevant year. This is regressed on a 'Commonwealth dummy' set equal to 1 where countries *a* and *b* are both members of the Commonwealth, and 0 otherwise².

The model also includes a range of control variables to control for other factors which might affect trade. We estimate two different specifications of the model. Specification 1 contains a skeletal set of control variables, while Specification 2 contains a fuller set. Table 1 gives full details. The basic set of regressors includes the most obvious control variables that would need to be in any sensible regression specification: GDP per head in the home and partner countries, the distance between the countries³, a dummy variable for whether the countries share a land border, and a dummy for each year of the dataset. Specification 2 contains additional variables relating to shared languages in both countries and also a variable for whether the two countries were ever in a colonial relationship *other than* the Commonwealth; this is meant to allow us to examine whether the trade effect for the Commonwealth is stronger than for countries that are (for example) former French or Dutch

² Normally, with a panel dataset like this it would be advisable to take advantage of the data structure by using a more robust panel data estimation technique like a country fixed effects model or Generalised Method of Moments (GMM) regression. However, in this case the variable of interest (the Commonwealth dummy) is time-invariant in the vast majority of cases and so most panel data techniques will not provide useful estimates.

³ The distance data was sourced from CEPII (www.cepii.fr). In the regressions reported here, the square root of distance was used rather than a linear or log measure because this transformation performed better in post-regression specification tests while preserving the monotonicity of the data (full specification results are available from the authors on request).

colonies. We also include a variable for whether two countries are in a *current* colonial relationship.

Table 1. Details of control variables used in specifications

Variables in both specifications	<ul style="list-style-type: none"> • Commonwealth dummy (equals 1 if both countries are in the Commonwealth) • Log GDP per head (measured in US dollars) in home country • Log GDP per head (measured in US dollars) in partner country • Square root of 'as the crow flies' distance between the countries • Dummy variable for countries sharing a land border • Year dummies (1990-2008)
Additional variables in specification 2	<ul style="list-style-type: none"> • Common official language in both countries • Shared language among a minimum proportion of the population in both countries (9%) • Whether countries have ever had a colonial link (except for Commonwealth countries) • Whether countries are still in a colonial relationship

Results

Between them the Commonwealth countries contained in the COMTRADE database imported some 2.3 trillion US dollars worth of goods, and exported some 2.1 trillion US dollars worth of goods in 2008. We have found that trade with other Commonwealth members is certainly important for many Commonwealth countries.

The left side of Table 2 below shows total imports from other Commonwealth member states; total imports from non-member states; and imports from the Commonwealth as a percentage of total imports, using figures for 2008. The right side of Table 2 gives the same information, but for exports rather than imports.

Table 2 shows that imports from other Commonwealth countries account for 15% of *total* imports of all Commonwealth members (as a proportion of the total volume of trade in US dollars across all Commonwealth countries). However, Commonwealth imports *average* 33% of total imports for each member state (that is for any given Commonwealth country, the average share of imports coming from another member state is around a third). Table 2 also shows that exports to Commonwealth countries average 17% of total trade (weighting by volume of trade in US dollars) but 36% of trade (as an unweighted average across countries).

Table 2. Imports and exports from/to other Commonwealth countries, 2008

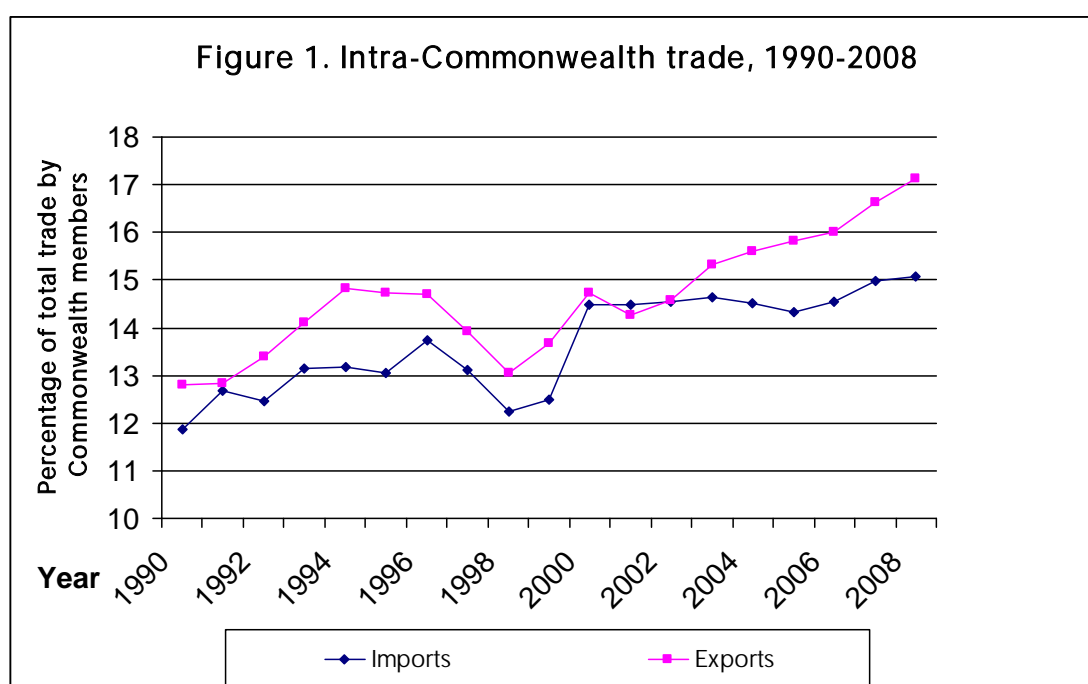
Country	Imports from CW (\$bn)	Imports from non-CW (\$bn)	% imports from CW	Exports to CW (\$bn)	Exports to non-CW (\$bn)	% exports to CW
Australia	46.09	145.49	24.1	42.18	144.68	22.6
Bahamas	0.07	3.16	2.2	0.07	0.63	10.0
Barbados	0.60	1.15	34.2	0.21	0.25	45.9
Belize	0.04	0.80	4.6	0.07	0.22	25.2
Botswana	4.42	0.68	86.8	3.82	1.02	79.0
Canada	27.30	381.44	6.7	22.02	433.69	4.8
Cyprus	1.39	9.46	12.8	0.23	1.48	13.5
Dominica	0.09	0.14	38.3	0.03	0.01	73.2
Gambia	0.05	0.27	15.4	0.00	0.01	34.2
Ghana	2.47	6.06	29.0	2.26	1.55	59.4
Grenada	0.14	0.22	38.6	0.02	0.01	62.4
Guyana	0.44	0.90	32.9	0.49	0.34	59.0
India	53.15	262.56	16.8	39.65	142.21	21.8
Jamaica	1.97	6.49	23.3	0.57	1.87	23.3
Kenya	3.34	7.79	30.0	2.38	2.62	47.6
Malawi	1.51	0.69	68.6	0.27	0.60	31.2
Malaysia	29.47	126.73	18.9	54.32	144.53	27.3
Maldives	0.76	0.62	55.1	0.02	0.10	19.0
Malta	1.11	4.04	21.5	0.75	2.28	24.7
Mauritius	2.09	2.58	44.8	0.89	1.51	37.0
Mozambique	1.57	2.44	39.1	0.38	2.27	14.5
Namibia	3.80	0.89	81.1	2.77	1.96	58.6
New Zealand	11.51	22.86	33.5	11.57	19.00	37.8
Nigeria	6.18	22.01	21.9	16.76	65.06	20.5
Pakistan	7.03	35.30	16.6	3.21	17.07	15.8
Rwanda	0.57	0.58	49.6	0.20	0.20	49.8
Saint Lucia	0.25	0.41	37.6	0.10	0.06	61.1
Saint Vincent & Grenadines	0.14	0.23	37.3	0.05	0.00	92.3
Samoa	0.17	0.12	58.1	0.07	0.01	92.4
Seychelles	0.34	0.69	32.8	0.05	0.29	15.5
Singapore	60.20	259.58	18.8	87.34	250.83	25.8
South Africa	14.45	73.14	16.5	18.07	55.90	24.4
Sri Lanka	6.12	7.51	44.9	2.02	6.15	24.8
Trinidad & Tobago	1.04	8.55	10.8	3.69	14.96	19.8
Tuvalu	0.01	0.02	37.1	-	-	-
Uganda	1.82	2.71	40.2	0.52	1.21	30.0
United Kingdom	54.55	579.90	8.6	40.18	417.57	8.8
United Rep. of Tanzania	3.25	4.84	40.2	1.07	2.06	34.1
Zambia	2.87	2.19	56.7	0.89	4.21	17.5
Total	352.37	1985.24	15.1	359.21	1738.42	17.1

Note: CW = Commonwealth

This shows that the proportion of Commonwealth trade tends to be higher in countries where the overall volume of trade is lower. For example, more than four-fifths of Botswana's and Namibia's imports come from other Commonwealth countries. Similarly, for some small island Commonwealth

members in the Caribbean and Pacific a high proportion of their exports go to other Commonwealth members. The evidence also confirms the findings of Lundan and Jones (2001) that smaller and less wealthy Commonwealth nations have a higher propensity to trade within the Commonwealth.

If we look over time, we also find that the relative importance of intra-Commonwealth trade has increased. As Figure 1 shows, the proportion of *total* imports into Commonwealth member states from other Commonwealth members (again a proportion of the total volume of trade in US dollars across all Commonwealth countries) has grown steadily from 11.9 per cent in 1990 to 15.1 per cent in 2008. Similarly, the proportion of the Commonwealth share of exports has grown from 12.8 per cent in 1998 to 17.1 per cent in 2008. In other words, over the last two decades the importance of Commonwealth members to each other as sources of imports and destinations for exports has grown by around a quarter and third respectively.



We now turn from the descriptive statistics to the results of our regressions. Table 3 below gives the results from the import model specification, and table 4 from the export model. A T-statistic with a value of greater than 1.96 indicates that the coefficient is significant at the 5% level. In every case (apart from the effect of an official common language in Specification 2 of the export regression) the effects are significant. We have omitted the year dummy variables from the table to save space – they are jointly (and in most cases individually) significant at the 5 per cent level.

Table 3. Regression results - imports

Dependent variable: (log) share of imports from partner country in home country's GDP

Specification	1		2	
	coefficient	T-stat	coefficient	T-stat
Commonwealth dummy	0.537	23.326	0.421	16.279
Home country: log GDP/head	-0.160	42.995	-0.160	42.647
Partner country: log GDP/head	0.908	255.415	0.905	253.511
Square root of distance between countries	-0.031	147.413	-0.031	144.111
Land border dummy	2.666	65.591	2.584	63.347
Common language (official)			-0.274	-9.561
Shared language (>9%)			0.566	20.697
Ever had a colonial link (except Commonwealth)			0.174	5.583
Still in a colonial relationship			-0.974	5.583
Constant	-9.523	178.914	-9.591	177.586
R-squared	0.241		0.242	
Number of observations	324,852		324,852	

Table 4. Regression results - exports

Dependent variable: (log) share of exports to partner country in home country's GDP

Specification	1		2	
	coefficient	T-stat	coefficient	T-stat
Commonwealth dummy	0.549	23.512	0.318	12.255
Home country: log GDP/head	0.913	241.081	0.919	241.706
Partner country: log GDP/head	-0.186	52.645	-0.188	52.956
Square root of distance between countries	-0.025	116.374	-0.024	110.412
Land border dummy	2.916	75.083	2.791	71.740
Common language (official)			0.041	1.448
Shared language (>9%)			0.460	16.936
Ever had a colonial link (except Commonwealth)			0.365	14.580
Still in a colonial relationship			1.737	10.442
Constant	-9.189	171.389	-9.407	172.483
R-squared	0.232		0.235	
Number of observations	290,243		290,243	

Despite the measurement differences in the import and export variable, the Commonwealth dummy is significant in both versions of the regression and across both specifications in each case. In specification 1 the coefficient is around 0.55; given that the dependent variable is in logs this means that in the case of countries which are both in the Commonwealth, imports (or

exports) from one country to the other are on average around 70-75 per cent higher (in value terms) than when only one country (or neither country) is in the Commonwealth, controlling for other factors. In the export model, log GDP per head of the home country is positive (indicating that countries with higher GDP per head tend to export more, conditional on other factors). In the import model, the reverse is the case. Not surprisingly, countries with a land border between them tend to trade a lot more, as do countries with a shorter distance between them. Overall, the explanatory variables included in the regression appear to explain around a quarter of the variance in trade patterns between countries.

The additional variables in specification 2 are mostly statistically significant but do not change the impact of most of the other variables that much. The Commonwealth dummy has a value of 0.42 in the Specification 2 import model and 0.32 in the export model. In percentage terms this corresponds to a Commonwealth effect of around 50 per cent for imports and around 38 per cent for exports. Countries which were previously (but no longer) in a (non-Commonwealth) colonial arrangement are more likely to trade with each other than country pairs that were never in such an arrangement. Countries with a common official language are less likely to trade with each other given other factors, but countries are more likely to trade with each other where 9 per cent or more of the population in both countries share a common language.

How do these results compare with the previous research on the Commonwealth Effect by Lundan and Jones (2001)? Like them, we find that there are "significant intra-Commonwealth flows of trade". Their methodology differed somewhat from ours, in that they used data for only 53 countries and 18 non-Commonwealth countries and used more detailed comparisons between individual Commonwealth country pairs and Commonwealth/non-Commonwealth country pairs, rather than including all the available country data in as large a sample as possible. The choice of countries to use for the matched comparisons was determined by relative GDP per capita, industrial structure (the proportion of agriculture to manufacturing and services in the economy), and distance between the country pairs (where possible).

Lundan and Jones's analysis did not control for common languages or attempt any comparison with trade patterns between non-Commonwealth/non-Commonwealth pairs of countries. They were only able to analyse 18 sets of Commonwealth-non Commonwealth countries which they then compared with matched pairs of Commonwealth countries. Thus, their analysis went into greater detail on a much smaller sample of countries than our dataset. Subject to funding, we plan to extend our dataset to breakdown aggregate trade into trade by industrial subsector (ISIC classification) in future work.

Lundan and Jones also look at whether a Commonwealth effect exists in foreign direct investment (FDI) data using the UNCTAD database but this is

much harder to do for trade, since most of the UNCTAD data shows aggregate FDI for each country rather than investment *from one country into another*. This makes it impossible to replicate the same kind of large-sample country pair model that we have used for trade on the FDI sample without a large time investment in data collection from the statistical offices of individual Commonwealth and non-Commonwealth countries. Even in this case we might not be successful; Lundan and Jones were only able to use an aggregated “proportion of investment into Commonwealth countries” variable for 28 countries, which in the context of our model design, is unlikely to yield a sample size large enough to detect a significant Commonwealth effect⁴. Thus, for the moment, we have included only trade in the analysis in this paper.

Lundan and Jones find a significant Commonwealth effect, but, because their empirical work is based on a series of pairwise comparisons rather than cross-country regression, they are unable to pull out a percentage figure for the size of the Commonwealth effect in the way we can. Thus it is not clear whether the effect is increasing or decreasing over time (their data runs from 1970 to 1995). In future work we plan to use a larger sample to assess the size of the Commonwealth effect and whether it is increasing or decreasing between the 1970s and the current decade.

⁴ Lundan and Jones, 2001, p.101: “As regards data on the stock of FDI, in addition to using a wealth of published sources from the United Nations, OECD and IMF... the High Commissions of all Commonwealth countries for which data was not readily available were approached to provide information. Unfortunately, these queries were largely non-productive owing to the dearth of data on direct investment broken down by home and host countries and industrial classification.”

Conclusion

This research has tried to discover how important Commonwealth members are to each other when it comes to trade. Our findings confirm that trade is an important dimension of the Commonwealth and suggest that it is increasingly significant.

The total value of imports into Commonwealth countries was around 2.3 trillion US dollars in 2008 and the total value of exports from Commonwealth countries was around 2.1 trillion US dollars in 2008. About one-sixth of this total trade occurred purely within the Commonwealth, though on average the Commonwealth share of trade for each member state was about a third. The data also suggest that the Commonwealth is particularly important for small states, with the Commonwealth share of total trade value reaching as high as three-quarters in some cases.

More significantly, the relative importance of Commonwealth members to each other is increasing, with the share of intra-Commonwealth trade (within the total trade of Commonwealth members) rising by over a quarter in the last two decades.

Finally, and perhaps most importantly, our findings confirm that there is a considerable trade advantage to be found in the Commonwealth. We have found that the value of trade is likely to be a third to a half more between Commonwealth member states compared to pairs of countries where one or both are not Commonwealth members. This effect can be seen even after controlling for a range of other factors that might also explain trade patterns.

This research provides compelling evidence that Commonwealth membership presents tangible benefits and clearly this is good news for the association. It is also timely news given that questions are being raised about the association's continued relevance.

Of course, our research also raises the wider - and perhaps more interesting question - of what might explain such a large Commonwealth Effect. Lundan and Jones (2001) suggested that the Effect could be partially explained by a reduction in "psychic distance" achieved between Commonwealth member nations. Their basic assertion was that, due to their familiarity with the institutions related to business, member countries might find it easier to internationalise within the Commonwealth before expanding to the global market.

The data collated here shows that there is a clear relationship between Commonwealth membership and increased trade and investment, but explaining causality remains a challenge. While our regressions do account for factors such as language commonalities, they do not control for other factors which may favourably dispose the Commonwealth to trade and investment - for example, the fact that it encourages multi-party democracy, human rights,

the rule of law, good governance, similar legal and administrative systems, an open media and, since 1997, market-orientated economic policies. Without further analysis and a more sophisticated treatment of political, legal and cultural factors, it is impossible to say for sure what impact these factors have. If future research could show that the Commonwealth Effect does not just reflect past relationships, but implies an under-utilised resource which is able to be leveraged, then the possibilities of realising growth potential throughout the Commonwealth could be improved.

Our results are also telling because of the relatively minor importance attributed to economic and trade issues in Commonwealth life at present. Considerable attention is given to the inter-governmental aspects of the Commonwealth (whether it is the suspension of a member or the declarations made by heads of government on one topic or another) and much is made of the Commonwealth's civil society links (from professional associations to pan-Commonwealth campaigns). Yet, the Commonwealth Business Council (CBC) is the only Commonwealth organisation which explicitly devotes itself to promoting trade, investment and business across the association. Indeed, before the creation of the CBC in 1997, there was very little attention given to trade or investment facilitation, and, in contrast to other areas of Commonwealth life, no related Ministerial-level conferences.⁵ This could well suggest that the Commonwealth effect accrues, despite only a relatively recent - and limited - focus on trade amongst Commonwealth institutions. Yet, given the relatively small scale on which Commonwealth business and trade is currently promoted, the potential for the association to nurture these links is significant. If promoted effectively, it could well be the association's economic ties, rather than its political bonds, that become its driving feature in the 21st century.

⁵ The Commonwealth Secretariat does support developing countries in researching, developing and negotiating trade policy as well as convening trade Ministers, but this does not usually involve a direct focus on boosting intra-Commonwealth trade or business links.

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Royal Commonwealth Society

The Royal Commonwealth Society (RCS) is the oldest and largest civil society organisation devoted to the Commonwealth. Founded in 1868, the RCS aims to promote international understanding through its range of events and activities. Headquartered at the Commonwealth Club in London, the RCS has some 5,000 members in the UK and a presence in more than 40 Commonwealth countries through a network of branches and Commonwealth societies.

Royal Commonwealth Society
25 Northumberland Avenue
London WC2N 5AP
United Kingdom
Email: info@thercs.org
Telephone: +44 (0) 20 7766 9200



Commonwealth free trade is the process or proposal of removing barriers of trade between member states of the Commonwealth of Nations. The preferential trade regime within the British Empire continued in some form amongst Commonwealth nations under the Imperial Preference system, until that system was dismantled after World War II due to changes in geopolitics and the pattern of global trade, and the United Kingdom's entry into the European Economic Community. The idea of promoting renewed inter... The 'Commonwealth Effect' Revisited. February 2011. The Round Table 100(412).¹ This article argues that, even as the Commonwealth has been seen by some commentators to have lost some of its political salience, its attractiveness as a trading bloc remains as strong as ever. It draws on recent research that indicates very healthy growth rates in intra-Commonwealth trade, and that reaffirms the continuing relevance of the 'Commonwealth effect' identified by Ludan and Jones in 2001. Discover the world's research. 19+ million members. Lord Howell: 'We want the Commonwealth to play a key role in the unfolding opportunities and challenges that our increasingly networked world brings.' From: Foreign & Commonwealth Office and The Rt Hon Lord Howell of Guildford. Published. 26 July 2011.² The recent Royal Commonwealth Society paper that you will be familiar with, *Trading places: the Commonwealth effect revisited*³, made it clear that there is indeed a *Commonwealth factor*⁴ when it comes to intra-Commonwealth trade. The research found that when both trading partners were Commonwealth members the value of trade was likely to be a third to a half more than when one or both of the trading partners was a non- Commonwealth country. * The Commonwealth dominates trade in some countries; for example more than four-fifths of Botswana's and Namibia's imports come from other Commonwealth countries; and more than 90 per cent of the exports from St Vincent and Samoa go to other Commonwealth countries.⁵ All this leads us to the case for a Commonwealth trading and investment compact. Even if a Free Trade Pact between diverse countries who make up the membership of the Commonwealth seem a difficult and daunting proposition, a move to give a Commonwealth preference to trade and investment flows between member countries could well see respective economies gaining in economic terms.