

Regional integration: the ASEAN vision in 2020

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I. Introduction

Regionalism has become a prominent feature of the global trading system for several years now, partly because of the relatively slower pace by which multilateral trade negotiations have been conducted under the General Agreement on Tariffs and Trade (GATT)/World Trade Organization (WTO). The recent proliferation of regional trade agreements (RTAs) and other forms of regional cooperation, triggered by the European Union (EU) market integration which has so far been the most successful example of regional economic integration, has drawn attention to the need of countries to strengthen their ties with other countries given the economic benefits that regional integration brings.

This paper looks into initiatives and the challenges faced by the Association of South East Asian Nations (ASEAN)² to pursue comprehensive integration towards the realization of an open, dynamic and resilient ASEAN Community by 2020. Focus is on the creation of an ASEAN Economic Community where there is a free flow of goods, services, investment, and freer flow of capital, equitable economic development, and reduced poverty and socio-economic disparities in year 2020.

The paper is organized as follows. Section II briefly reviews the economic implications of regional integration. Section III presents the evolution of ASEAN economic integration in a regional context. Section IV discusses the monitoring system introduced to measure the progress towards realizing the ASEAN Community objective. Finally, Section V outlines the challenges of integration in the ASEAN context.

II. Economic implications of regional integration

The most widely recognized argument in favor of regional integration is the benefit of expanding markets and promoting competition by eliminating barriers to trade among member-countries. Economic welfare increases as resources previously engaged in costly domestic production are efficiently reallocated to the direction of a country's comparative advantage and to that which generates greater productivity ("trade creation effect"). An expanded regional market may also be seen by countries outside the region as an increase in trade opportunity.

However, regional integration also has potential risks. First, it may give rise to welfare losses if the "trade creation effect" is overshadowed by a "trade diversion effect", i.e., if the elimination of barriers to trade among member-countries causes trade with more efficient non-member countries to be diverted to the less efficient member-country. Second, it may lead to an "investment diversion effect" where limited investment resources are diverted to

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² Includes the original ASEAN-5, namely, Indonesia, Malaysia, Philippines, Singapore and Thailand, as well as Brunei Darussalam, Cambodia, Lao PDR, Myanmar and Vietnam.

the larger-scale integrated market. Third, there are concerns on the “noodle bowl effect”, referring to the potential problems that may arise as a result of lack of coherence among different overlapping agreements. Tumbarello (2007) cites bilateral agreements being negotiated by some individual member-countries of the ASEAN with non-ASEAN countries even as ASEAN itself is negotiating with the same country. Since there is little effort to achieve consistency and harmonization in the agreements being negotiated, there arises restrictive and inconsistent rules of origin that complicates the trading system. An example given on differences on rules of origin is that of the New Zealand-Singapore and the ASEAN Free Trade Area (AFTA) which uses the 40 percent value-added criteria, while ASEAN-India, Singapore-India and Japan-Singapore include multiple-change-of-tariff-heading criteria or other more complex provisions.

III. The evolution of ASEAN economic integration in a regional context

ASEAN was established on 8 August 1967 by the five original member countries (ASEAN-5), namely, Indonesia, Malaysia, Philippines, Singapore and Thailand. Brunei Darussalam joined on 8 January 1984, Vietnam on 28 July 1995, Lao PDR and Myanmar on 23 July 1997, and Cambodia on 30 April 1999. Its purposes, as stated in the ASEAN Declaration, are: (i) to accelerate economic growth, social progress and cultural development in the region, and (ii) to promote regional peace and stability through abiding respect for justice and the rule of law in the relationship among countries in the region and adherence to the principles of the United Nations Charter.

AFTA: the first major step

Prompted by the rise of regionalism globally with its potential inherent benefits and the generally pessimistic outlook on the multilateral trade initiatives under the WTO, ASEAN embarked on several initiatives towards regional economic convergence. The ASEAN Free Trade Agreement (AFTA) put in place in 1992 was the first major move. AFTA aims to promote the region’s competitive advantage as a single production unit. It commits members to free trade within a 15-year timeframe through the elimination of tariff and non-tariff barriers with the end in view of promoting greater economic efficiency, productivity and competitiveness. Free trade, in this respect, was not strictly defined, as it allows tariffs within the range of 0–5 percent and excludes certain sensitive products. At the start of 2004, AFTA was technically in full effect for the ASEAN-5 and Brunei Darussalam, although some country-specific implementation concerns in certain areas have yet to be addressed. The original target for full implementation was 2006 for Vietnam, 2008 for Lao PDR and Myanmar, and 2010 for Cambodia. In addition, ASEAN agreed to accelerate industrial cooperation through such endeavors as the ASEAN “one-stop investment centers” and the ASEAN Investment Area (AIA) which also offers tariff (0–5 percent) and non-tariff incentives.

ASEAN economic community: the ultimate goal in 2020

In November 2002, the ASEAN Heads of Government recommended the creation of an ASEAN Economic Community (AEC) by 2020. This proposal was underpinned by various considerations, including: (i) the desire to create a post-AFTA agenda, (ii) the need to deepen economic integration within the region in light of the increasing dominance of free trade areas (FTAs), (iii) the possibility that bilateral FTAs, which members are free to engage in, would jeopardize ASEAN integration, and (iv) post-1997 Asian financial crisis lessons that recognized the importance of cooperation in both real and financial sectors, and the free flow of skilled labor to be able to achieve this cooperative endeavor (Plummer, 2006).

The following year, in 2003, ASEAN resolved to pursue comprehensive integration towards the establishment of an ASEAN Community by 2020, founded on the three pillars of political and security community, economic integration, and socio-cultural cooperation, to form the ASEAN Security Community (ASC), the ASEAN Economic Community (AEC) and the ASEAN Socio-Cultural Community (ASCC). The ASC aims to ensure that countries in the region live at peace with one another and with the world at large in a just, democratic and harmonious environment. The AEC is the realization of the ultimate goal of economic integration to create a stable, prosperous and highly competitive ASEAN economic region in which there is a free flow of goods, services, investment and freer flow of capital, equitable economic development and reduced poverty and socio-economic disparities in year 2020. The ASCC is envisioned to create a region bonded together in partnership as a community of caring societies. The Vientiane Action Programme (November 2004) describes how these three pillars are closely intertwined:

“Since economic growth could be threatened by social inequities that could in turn undermine political stability, the ASEAN socio-cultural action programme is linked inextricably with the economic and security pillars of the ASEAN Community. The establishment of the ASCC stems from the premise that economic integration and security alone will not be sufficient to realize the vision of an ASEAN Community.”

A fourth dimension can be added to the three pillars en route to the attainment of the goal of realizing the ASEAN Community in 2020. While recognizing that regional economic integration can enhance the convergence of incomes across countries in the region, ASEAN is concerned about its potential risk given the existing wide disparities in income and other human development dimensions among its member countries. The narrowing the development gap (NDG) concern was, in fact, introduced in July 2001 when ASEAN issued the Hanoi Declaration on Narrowing Development Gap for Closer ASEAN Integration, and was reaffirmed in the Bali Concord II in 2003.

The AEC shall establish ASEAN as a single market and production base, turning the diversity that characterizes the region into opportunities for business complementation and making the ASEAN a more dynamic and stronger segment of the global supply chain. ASEAN has agreed on the following: (i) institute new mechanisms and measures to strengthen the implementation of its existing economic initiatives such as the AFTA, ASEAN Framework Agreement on Services (AFAS) and AIA; (ii) accelerate regional integration by 2010 in priority sectors, namely, air travel, agro-based products, automotives, e-commerce, electronics, fisheries, healthcare, rubber-based products, textiles and apparels, tourism, and wood-based products; (iii) facilitate movement of business persons, skilled labor and talents; and (iv) strengthen the institutional mechanisms of ASEAN, including the improvement of the existing ASEAN Dispute Settlement Mechanism to ensure expeditious and legally-binding resolution of any economic disputes.

It is still not clear, however, what form the AEC will take. One form could be an “FTA-plus” arrangement, which includes some elements of a common market, e.g., free flow of capital, free flow of skilled labor, zero tariffs on intraregional trade, but does not include a common external tariff. The other form is that of a “common market minus” arrangement that aims to create a fully integrated market but has areas where members of ASEAN will reserve deeper integration for a later stage.

What is clear is the fact that unlike European economic integration which started as an inward-looking approach to regionalism, ASEAN economic integration has been mainly geared toward “open regionalism” given that its important economic partners are outside the region. This is evident in the recent proliferation of FTAs in the region, particularly with China, Japan and the Republic of Korea, which collectively has been called ASEAN+3.

Monetary and financial integration

Following the Asian financial crisis, ASEAN has sought to promote closer monetary and financial cooperation by way of the conduct of an economic review and policy dialogue as well as the establishment of regional financing arrangements.

The ASEAN Surveillance Process was established in October 1998 to strengthen the policy-making capacity in the region. ASEAN and the ASEAN+3 Finance Ministers, their deputies and central bank deputies meet on separate occasions to review global, regional and individual country developments and monitor exchange rate and macroeconomic aggregates, as well as sectoral and social policies. This review has included the monitoring of short-term capital flows and development of early warning systems of currency and banking crises.

In May 2000 at Chiang Mai, Thailand, the ASEAN+3 Finance Ministers agreed on the Chiang Mai Initiative (CMI) to expand the ASEAN Swap Arrangement (ASA) to all ASEAN members and to set up a network of bilateral swap arrangements. In February this year, ASEAN+3 approved the multilateralization of the CMI in response to a decision in 2006 that “all swap providing countries can simultaneously and promptly provide liquidity support to any parties involved in bilateral swap arrangements at times of emergency”. By turning the CMI into a multilateral facility, ASEAN hopes to send a strong signal of regional cooperation and policy coordination; play a complementary role vis-à-vis international financial institutions in providing liquidity support to crisis economies and conduct surveillance; and facilitate the evolution of the CMI into higher forms of regional monetary and financial cooperation. An independent surveillance unit will monitor and analyze regional economies and support decision-making within the CMI framework.

Other types of financial cooperation that have so far been introduced were, among others, the Asian Bond Fund (ABF) and the Asian Bond Markets Initiative. The ABF consists of ABF1 which are invested in US dollar-denominated bonds issued by Asian sovereign and quasi-sovereign issuers, and the ABF2 which are invested in bonds denominated in regional currencies.

IV. Monitoring progress towards realizing the ASEAN community goal

Rana (2006) presents two measures of trade integration using Direction of Trade Statistics of the International Monetary Fund. Table 1 shows intraregional trade among ASEAN countries increasing from 17.9 percent in 1980 to 24.0 percent in 2005. By member country, Brunei Darussalam had the highest intra-ASEAN trade ratio, followed by the new member countries, such as Myanmar and Lao PDR. A higher share indicates a higher degree of dependency on regional trade.

Table 1
Intraregional trade
 As percent of total world trade¹

	1980	1985	1990	1995	2000	2005
Brunei Darussalam	80.1	77.3	81.7	79.5	74.2	75.0
Cambodia		67.4	68.6	81.5	35.8	46.8
Indonesia	58.3	53.3	51.7	49.5	50.6	54.6
Lao PDR		82.6	85.7	65.3	72.8	74.0
Malaysia	46.7	54.1	49.6	48.2	49.4	54.7
Myanmar	50.6	42.9	58.7	72.5	62.2	74.9
Philippines	33.8	36.0	32.8	37.5	39.7	52.7
Singapore	36.8	40.6	39.5	47.2	46.5	45.4
Thailand	38.1	42.7	42.6	43.7	44.9	49.5
Vietnam		10.5	27.8	57.6	56.4	52.7
ASEAN	17.9	20.3	18.8	23.9	24.5	24.0
Memo items:						
ASEAN+3	30.2	30.2	29.3	37.3	37.0	38.2
ASEAN+3+						
HongKong + Taiwan	34.6	37.1	43.0	51.7	51.9	54.5

¹ For regional grouping, intraregional trade share is calculated using the formula: $X_{ii} / \{(X_{iw} + X_{wi})/2\}$, where X_{ii} is export of region i to region i , X_{iw} is export of region i to the world, and X_{wi} is export of world to region i .

Meanwhile, Table 2 shows data on trade intensity indices which gives a better measure of economic interdependence. An index of more than one indicates that trade flow within the region is larger than expected given the region's importance in world trade. The data show that the total trade intensity index has been broadly steady at about 4.

Table 2
Intraregional trade intensity index¹

	1980	1985	1990	1995	2000	2005
Brunei Darussalam	6.7	5.4	5.3	4.0	3.7	3.5
Cambodia		4.7	4.4	4.1	1.8	2.2
Indonesia	4.9	3.7	3.4	2.5	2.5	2.5
Lao PDR		5.8	5.6	3.3	3.7	3.4
Malaysia	3.9	3.8	3.2	2.4	2.5	2.5
Myanmar	4.2	3.0	3.8	3.6	3.1	3.5
Philippines	2.8	2.5	2.1	1.9	2.0	2.4
Singapore	3.1	2.8	2.6	2.4	2.3	2.1
Thailand	3.2	3.0	2.8	2.2	2.3	2.3

Table 2 (cont)

Intraregional trade intensity index¹

	1980	1985	1990	1995	2000	2005
Vietnam		0.7	1.8	2.9	2.8	2.4
ASEAN	4.8	5.7	4.4	3.7	4.0	4.2
Memo items:						
ASEAN+3	2.4	2.1	1.9	2.0	2.0	1.9
ASEAN+3+						
HongKong + Taiwan	2.5	2.3	2.2	2.1	2.2	2.2

¹ Intraregional trade intensity index is the ratio of intraregional trade share to the share of world's trade with the region. For regional groupings, trade intensity index is calculated using the formula: $[X_{ii} / \{(X_{iw} + X_{wi})/2\}] / \{[(X_{iw} + X_{wi})/2] / X_{ww}\}$, where X_{ii} is export of region i to region i , X_{iw} is export of region i to the world, X_{wi} is export of world to region i , and X_{ww} is total world export.

ASEAN itself, through the Vientiane Action Programme, had endeavored to develop a system to monitor the progress towards the realization of the vision of an ASEAN Community by 2020. The first step done was the preparation of the ASEAN Baseline Report which included the identification of an initial set of indicators and collection of available data to generate a preliminary analysis of the baseline situations as outlined in the VAP in 2005. In the selection of indicators, the ASEAN project team was guided by the following selection criteria: policy relevance, simplicity, statistical consistency, validity, data availability, and indicator coverage. The indicators were grouped into three, namely: (i) process indicators, which are intended to capture various stages involved in policy/program formulation and implementation; (ii) output indicators or those that result from certain measures being adopted; and (iii) outcome indicators which go beyond output indicators and are usually influenced by many factors. Indices are constructed for each of the identified indicators. Composite indices are also constructed for some indices and for each of the four dimensions of the ASEAN Community.

The ASEAN Socio-Cultural Community has four major thrusts. These include (i) building a community of caring societies, (ii) managing the social impact of economic integration, (iii) promoting environmental sustainability, and (iv) promoting an ASEAN identity. On the other hand, the ASEAN Security Community is focused on the following strategic thrusts: (i) political development, (ii) shaping and sharing norms, (iii) conflict prevention, (iv) conflict resolution, and (v) post-conflict peace building.

In the case of the ASEAN Economic Community, the overall strategy involves deepening and broadening economic integration in the product and factor markets and accelerating the integration process towards a single market and production base. The acceleration of economic integration begins with the 11 priority sectors. The indicator system follows three major areas of integration, as follows: trade in goods and services, investment and skilled labor. Trade in goods and services are facilitated by the removal of barriers to trade, both tariff and non-tariff barriers, and through harmonization of procedures and classifications. In the area of investment, it is limited to direct investment. Finally, with respect to the labor market, integration will focus on skilled labor. Indicators include wage rates and employment of ASEAN workers. Indicators relating to financial services, such as credit markets, bond markets, stock markets and the banking sector, as well as other support sectors including the transport sector, are also taken into consideration.

Taking a cue from the analysis provided by the baseline report, the ASEAN Community Progress Monitoring System (ACPMS) was introduced in 2007. It aims to come up with a

system that will produce periodic reports to monitor the outputs and impact of measures taken by the ASEAN member countries, individually or collectively, towards the attainment of the ASEAN Community vision. It shall establish a system using indicators that are concise, reliable and pointed, and data that are cost-effective to collect, accurate, timely and consistent across jurisdictions. However, the ACPMS is not intended to monitor compliance of specific agreement/activities. The monitoring of the implementation of agreed activities and of compliance to agreed systems/mechanisms/principles will be taken care of by the AEC Scorecard. The Scorecard will assess the completion and/or implementation of processes – negotiations for agreements, capacity building activities, or mechanism setting; production/delivery of immediate outputs of programs; and completion of measures relative to pre-agreed, time-bound targets.

V. Challenges

This paper has presented the initiatives that ASEAN has undertaken towards regional integration. The multi-track system consisting of the trade track and the monetary and finance track appears to be working well. Significant progress has been made with the creation of AFTA, the first major step of ASEAN en route to economic integration. The remaining challenges would be to determine the exact form that the ASEAN Economic Community will take and to address the “noodle bowl” effects associated with the increasing number of FTAs negotiated. Since FTAs impose strict rules of origin and other conditions that increase administrative costs, it is important that FTAs should be carefully reviewed to ensure compatibility with other FTAs. The monetary and finance track requires stronger regional surveillance. ASEAN has identified two tools – the ACPMS and AEC Scorecard – to measure how far or how close it is towards the ASEAN 2020 vision. These tools have so far not been finalized. However, the biggest challenge is not in completing these monitoring tools but in ensuring the commitment of the member countries to move the process forward. This requires the openness and willingness of ASEAN and the political will of its leaders to see through the attainment of its objectives.

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