

LESSONS FROM ASEAN's ECONOMIC INTEGRATION

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Abstract

ASEAN has been a fast growing economic region during the last decade. However, it was not founded as an economic body as such but as a means to stopping the spread of Communism within South East Asia. This article looks at those factors, which have supported this economic cooperation such as the emergence of regionalism, the emergence of Foreign Direct Investment host countries, even the Asian economic crisis that have all contributed to this economic cooperation between the member countries of ASEAN. In addition, factors that have worked against this economic cooperation are also looked at in this article. These include factors such as the early objectives of ASEAN itself, economic dependence on other external economies, ASEAN's lack of an anchor country, the inadequacy of

institutions with member countries, as well as the differences between ASEAN member countries themselves. It concludes by suggesting lessons that can be learned for other developing countries.

Even though not founded primarily and fundamentally as an economic region, the Association of Southeast Asian Nations (ASEAN) has in fact been a fast-growing economic region during the last decade. No doubt a significant factor in this economic success has been the economic cooperation that has occurred between the countries of the region. After its founding in 1967 and for the next two decades there was slight growth only in the economies of ASEAN's member countries. However, during the 1990's, before the region entered into its economic crisis in 1997, this regional economic cooperation expanded considerably as demonstrated

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by its liberalization of trade, service, and investment, sub-regional economic cooperation, and other collaborations in terms of information technology.

This paper endeavors to study lessons derived from this economic cooperation within ASEAN. Factors that have contributed to or hindered the success and failure of regional cooperation will be discussed in the paper, which will conclude with recommendations aimed to help policymakers of regional development for other developing countries. All these recommendations aim to promote a sustainable development for each nation in the shape of new economic and political surroundings.

Factors that supported ASEAN's economic cooperation

Economic cooperation between Southeast Asian Nations was not the main impetus for this bloc during the first two decades after its establishment (Gramegna, 1997). In fact, other internal factors and strategies within the individual nations drove this regional economy. Abundance of natural resources, particularly in terms of minerals and forests, as well as cheap, quality, and hard working labor, which supported intensive-labor based industries ensured low costs of production (Daquila, 2002). Other factors such as infrastructure, developed with United States support during the Cold War; foreign trade,

brought about by a change from import substitution to export-oriented industrialization; stabilized politics, which allowed national leaders to stay in their position for a longer period of time; as well as the economic strength of each country itself also reinforced the economic stability of the region (Daquila, 2002).

However, after the signing of the Singapore Declaration in 1992, economic cooperation within ASEAN increased greatly. This change seems to have occurred partly as the result of the institutionalization of the ASEAN summit meetings once every three years, the holding of informal summits, and the adoption of trade and investment liberalization measures towards the achievement of the ASEAN Free Trade Area (AFTA). AFTA was a developing concept arrived at by consensus. The tariff reduction process is carried out through the Common Effective Preferential Tariff (CEPT), which is reviewed regularly by the AFTA Council (Beng, 1997). All ASEAN member countries are compelled to participate in the CEPT scheme.

Key supportive factors attributed to the expansion of ASEAN's economic cooperation

1) *Emergence of regionalism*

In the past, economic growth within ASEAN countries was caused by global economic conditions that had no

serious competition as well as the support of powerful countries in the world (Kelly, 2002). At present however, developed countries have begun to build economic blocs that in fact have compelled ASEAN to build more regional cooperation in order to compete with other regions (Nishiguchi, 2002).

2) *Emergence of alternative Foreign Direct Investment (FDI) host countries*

The emergence of alternative FDI host countries has brought about more competition to try to attract FDI (Akraseranee and Stifel, 1992). Such competition became more intense after China's entry into the World Trade Organization, which attracted about 70% of FDI into China and a mere 30% into the ASEAN countries (Daquila, 2002). This situation forced ASEAN to develop more cooperation in order to attract more investment and also to expand the scope of this regional cooperation by accepting membership of countries such as Vietnam, Myanmar, Laos, and Cambodia.

3) *Regional economic relationships*

Members of ASEAN have had more increasing economic relationships with a stronger network of cross border operations and cross border inter-firm transactions. Private sectors of ASEAN have a greater potential to invest in the region, particularly large-sized businesses in Singapore and Malaysia (Freeman, 2001). ASEAN therefore demands a decrease in the cost of these transactions (Nishiguchi, 2002).

4) *Asian economic crisis*

The economic predicament in 1997 was yet another impetus that forced ASEAN to liberalize quickly so as to attract investment and thereby aid the recovery of the regional economy. Policies centered on trade and investment liberalization were made by many member countries (Lane, et al., 1999). For example, the allowance provided to foreigners to be domestic entrepreneurs (business ownership) was raised to 100%, particularly in the export industry, banking business, and financial institutes (due to the effects of the crisis in Thailand, Indonesia, and the Philippines). Moreover, the crisis also triggered ideas of expanding cooperation to other countries outside the group, for example, Japan, China, and Korea, entitled ASEAN+3, as well as building regional financial cooperation.

Obstacles to the development of economic cooperation within ASEAN

Development of ASEAN in the first 20 years after 1967 was not as successful as that experienced by other economic blocs, especially The European Union (EU) and The North American Free Trade Association (NAFTA). There were significant factors that interfered with the development of ASEAN's economic cooperation such as:

1) *The early objectives of ASEAN*

ASEAN does not in fact function as an economic bloc (Frankel

and Wei, 1996). When founded, its main objective was to be a political cooperation to restrain the expansion of communism in Southeast Asia, which at that time was threatening Vietnam, Laos, and Cambodia. Leaders of more liberalized countries believed in the 'domino effect', that is, if Thailand had become communist, this would cause the region to become communist as well. The five pioneer countries of ASEAN therefore founded it with this in mind and consequently, during the embryonic period of its establishment, they did not pay attention to the co-development of each of their own economies.

2) Dependence on external economies

ASEAN countries have demonstrated a high degree of dependence on external technology, foreign direct investment (FDI), and international financial flows and subsequently the economic structure of ASEAN's member countries was highly dependent on other countries outside the region (Harianto, 1994). Such a situation is reflected in the value of domestic trade in the region that is quite low compared to the value of total trade for member countries. Most industries in ASEAN are export-based industries, established by the FDI of developed countries and New Industrialized Economies (NIE) (Nishiguchi, 2002) and as a result most production aims to penetrate large markets outside the region. In addition, most export-based businesses import from mother companies and foreign producers of

capital goods that are not located in the region (Ariff, 1997).

Economic relationships within ASEAN itself are also quite poor compared to internal relationships within NAFTA and the EU. Regional trade is promoted more by Singapore and other neighbouring countries with the exports of Singapore and Malaysia accounting for two-thirds of the total exports in the region (Nishiguchi, 2002). Without trade with Singapore, regional commerce would be 2-5% only of the total trade of ASEAN. As a result, the Common Effective Preferential Tariff (CEPT) appears not to have had much impact on the expansion of exports and economies within ASEAN. After the declaration of CEPT, regional exports expanded by 2.9% only, while regional income expanded by just 3.1% (Daquila, 2002). As Harianto (1994) suggested, the ASEAN Free Trade Area appears to be only an integrated production base for standardized and mature products and not a conventional free trade area.

3) Other external impetus

Most factors supportive of the development of ASEAN's economic cooperation however, are external. These include the expansion of Communism, the trade and investment policies of Japan, the emergence of China all of which brought about a redrawing of the map of industrialization in East Asia, as well as the Asian economic crisis (Atsurou, 2001). However, most of these factors

were external to the region, and consequently the development of ASEAN has not only been slow but it also lacks clear direction. In fact changes within ASEAN may be seen as response to these external factors only. On the other hand, unlike ASEAN, the establishment of the EU was rapid with a clear direction. It was driven by internal factors that were aimed to cope with regional competition and to use the economy as a tool to solve conflicts between Germany and France. In addition, all of these external factors are not meant to underestimate the impact of the Asian economic crisis itself (Atsurou, 2001).

4) *Lack of the anchor country*

ASEAN lacks an anchor leader, a large country that can lead member countries (Ethier, 1998; van der Geest, 2002). Unlike ASEAN, NAFTA is led by the USA and the EU by Germany. Member countries of ASEAN have equal status and therefore it is difficult to conclude negotiations and conditions since there is no one country that has adequate bargaining power to force every country to follow that condition.

5) *Lack of adequate institutional strength*

The institutes of ASEAN lack strength and power, unlike the institutes of the EU, independent high authorities, whose roles are paramount (Chino, 2003). For the time being, ASEAN does not have an independent, supranational body and therefore the common positions can only mature through

consensus with the lowest common denominator. Representatives of ASEAN are usually ministers from the member countries and so its role has been limited to ad hoc dispute settlement. In the EU however, the heads of state or government normally meet twice a year together, with the president of the commission, as the European Council. On the other hand the council of ministers of ASEAN normally meets once a year only and even though this council shapes common positions amongst member states, it does not have a legislative function (Gramegna, 1997).

Furthermore, the notion of constructive engagement encourages member countries of ASEAN not to meddle in the domestic affairs of other member countries. As a result, ASEAN countries lack sufficient power to coerce other member countries to follow group opinion or even to be supportive of other countries. The military government of Myanmar, for example, limits the political right and freedom of Aung San Suu Kyi, a situation that makes ASEAN look weak since it has not been able to pressure Myanmar about this issue. However, after many other countries in the world approached ASEAN, it was compelled to form a resolution aimed at forcing Myanmar to free Aung San Suu Kyi. Such an event had never happened before in the history of ASEAN when member countries intruded into the national issues of another member country.

6) Differences amongst member countries themselves

Unlike the fifteen member states of the EU, which are all Christian and pluralistic democracies, members of ASEAN have differences in both religions and political systems. Members of the EU are all developed countries even though the GDP per capita of the richest member is more than three times that of the poorest. Another difference between ASEAN and the EU lies in the ASEAN economies having differences in tariff structures that instigated the Common Effective Preferential Tariff (CEPT) scheme in 1993. Although this has led to a significant increase in absolute terms, intra-regional trade has remained at around 25% of ASEAN's global trade (Thongpakde, 2001).

Moreover, it is very difficult to make ASEAN+3 into a currency area. Despite member countries of ASEAN+3 having many differences, guidelines and criteria on just how they should adjust their national identities to get along well with other member countries are not mentioned before membership of the currency area begins. By way of contrast however, EU countries have fewer differences than the ASEAN countries, yet new members have to meet convergence criteria before joining with the EU currency area (Ethier, 1998; van der Geest, 2002).

7) Competition between member countries

Some believe that groups of countries that are able to carry out a lot of international trade with adjacent national locations should be "natural trading partners" (Wonnacott and Lutz, 1989; Summers, 1991; Krugman, 1991). Such an idea suggests that this grouping fits the idea of a free trade zone since distant locations can increase the cost of transportation and consequently bring about less international trade. However, even though countries in ASEAN are located adjacent to each other, the proportion of their trade is low – unlike in the EU that has a high rate of international trade within the European region.

More significantly though, ASEAN countries have seen themselves as economic rivals with each other. Although they have similar structures of production, member countries of ASEAN are in serious competition to attract foreign investment, which prevents them from becoming natural trading partners totally. Compared to other external trading from the region, ASEAN has a lower trade transaction level. This may be due to the distortion of the trade barrier amongst member countries, and the privilege of tariff, which causes a high proportion of trade between ASEAN and developed countries. After the liberalization of AFTA, these distortions decreased but with a proportionate increase in some of ASEAN's regional trade.

8) *Stream of bilateral negotiation*

Trade liberalization, favoured by a World Trade Organization agreement, has been delayed since such a resolution is difficult to conclude. This is due to the large number of participant countries that argue against such a move thereby preventing successful negotiations. ASEAN's member countries were pushed to liberalize their trade according to the AFTA agreement, but this eventually proved unsuccessful because of the low cost of their withdrawal according to the AFTA agreement. As a result, some member countries did not liberalize some of their industries as they were expected to do. As a result of the ineffectiveness of multi-lateral negotiations on trade, some ASEAN member countries preferred to negotiate bilateral trade, that is, to set the mutual free trade zone between two parties (Chua Lee Hong, 2001). Undoubtedly, member countries have not paid much attention to developing cooperation for the benefit of ASEAN itself.

9) *Internal resistance from member countries*

Another key obstacle against the building of economic cooperation within ASEAN is internal resistance from member countries themselves. Since some advantages are lost because of ASEAN's trade liberalization policy, groups of people who have been

disadvantaged resist the development of ASEAN cooperation. These groups can include governments who have lost income from the collection of tariffs; entrepreneurs of domestic industry, as well as governments that endeavor to protect domestic industries they consider to be strategic points or the stability of their nation.

CONCLUSION

The achievements and failures that have occurred in the development of ASEAN's economic cooperation should provide lessons for other developing countries. In developing economic cooperation between any group of countries, every member country needs to have a clear intention of developing relationships with other member countries by every means possible. They need to have an active goal to expand this relationship and to go further than the scope of just their region. The whole operation should be a well-organized process with appropriate criteria for each member country that may in fact be different for each country. Distinguishing several levels of policy targets may speed up the integration process in a more stable manner and may also help to reduce the adjustment costs for the different member countries (van der Geest, 2002).

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