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Center for the Pacific Rim
2130 Fulton St, LM202
San Francisco, CA
94117-1080

Tel: (415) 422-6357
Fax: (415) 422-5933
perspectives@usfca.edu

Asia Pacific: Perspectives is a peer-reviewed journal published at least once a year, usually in April/May. It welcomes submissions from all fields of the social sciences and the humanities with relevance to the Asia Pacific region.* In keeping with the Jesuit traditions of the University of San Francisco, *Asia Pacific: Perspectives* commits itself to the highest standards of learning and scholarship.

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* 'Asia Pacific region' as used here includes East Asia, Southeast Asia, South Asia, Oceania, and the Russian Far East.

ASEAN Regionalism: Growth Through Integration

by Richard Payne, M.A., M.A.P.S.

Abstract

With the rise of China and India, Southeast Asia risks turning into a backwater and its economies becoming marginalized by dominant regional powers. GDP growth and foreign direct investment are two economic indicators that show how far ASEAN is falling behind. Analysts argue that greater cooperation and economic integration could improve the economics of investment in ASEAN. Despite the formation of the ASEAN Free Trade Area in 1993, progress toward economic integration remains slow and intra-regional trade, as a percentage of the region's total trade, has even declined from 1994 to 2001. Adjustments need to be made. ASEAN should build economic integration by: 1) promoting regionalization and supporting private sector initiatives; 2) pursuing a multipolar strategy to integration; and 3) utilizing voluntarism as a core strategy in promoting integration.

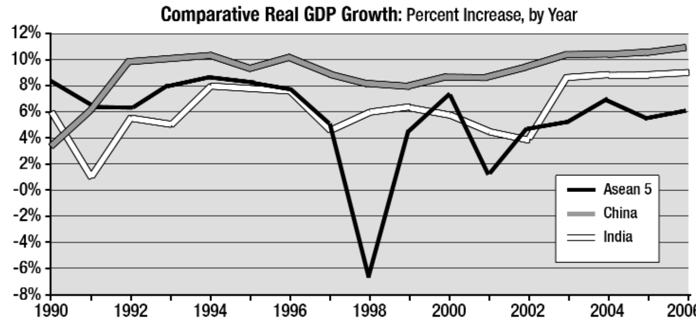
With the rise of China Southeast Asia increasingly risks turning into a backwater and its economies becoming dominated by stronger regional powers.[1] Free trade agreements are increasingly seen as the panacea to the risk of ASEAN[2] marginalization. A *Financial Times* article reports that "China on Sunday signed an agreement with the Association of Southeast Asian Nations that promises to open up key service sectors as the two partners move towards creating what could be the world's biggest free-trade zone. The deal is seen as a vital step towards the establishment by 2015 of a China-ASEAN free trade area. Such a zone would bring together China's 1.2 billion people and Southeast Asia's 500 million citizens into a single market."[3]

Is such a free trade area possible and would it indeed fulfill the lofty expectations of its promoters? The realization of economic integration and its expected benefits are far from certain. This article looks at Southeast Asia's economic performance and the role that economic integration has and can play. It reviews proposals for greater economic integration and offers its own perspective to greater economic growth through economic integration.

ASEAN Economic Performance

The average annual real GDP growth rate for the original five ASEAN countries[4] has lagged behind China and India for most of the last 15 years. From 1990 to 2006, the "ASEAN 5" countries on average have grown just over five per cent per annum, while India has increased over six percent and China over nine percent, during the same period. The economic crisis of 1997 was a critical turning point. While ASEAN growth plummeted and took many years to recover, China continued its robust growth and India emerged as a new force within the region.

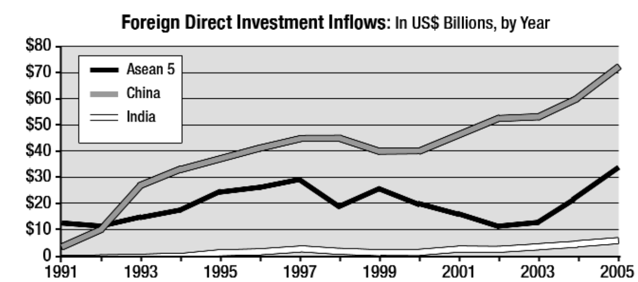
Since 2003, the economies of India and China have overshadowed those of ASEAN. From 2003 to 2006 China experienced growth of 10.2% per annum and India achieved 8.5%



annual growth. The ASEAN 5 secured a 5.7% average annual growth during the same period.

High growth, a huge market, supportive government economic policies and an increasingly competitive manufacturing base have made China extremely attractive to foreign investors. In 1992 the ASEAN 5 and China attracted similar amounts of foreign direct investment (FDI).[5] From 1992 until 1997, FDI inflows rose rapidly in both ASEAN and China, although China's growth in FDI inflows outstripped the ASEAN 5. In 1997, FDI inflows into China reached US $45 billion while the ASEAN 5 attracted US $30 billion in FDI inflows.[6]

Since 1997, the situation has changed dramatically. ASEAN's 1997 economic crisis and its slow recovery made foreign investors wary of putting more funds into the region. Meanwhile, China's continued economic resurgence made it highly attractive to foreign investors. By 2002 annual FDI inflows into China reached US $52.7 billion while FDI inflows into the ASEAN 5 slid from nearly US $30 billion in 1997 to US $12 billion in 2002 (coincidentally, the same level as in 1992). Since 2002, FDI inflows have recovered to US $34 billion in 2005,[7] but FDI in China has also continued its remarkable rise. FDI inflows into China in 2005 reached nearly US $72 billion.



While foreign direct investment in India has remained modest as compared to ASEAN and China, the increase in FDI inflows has been significant in recent years. In the 1990s foreign direct investment started to grow in fits and starts. From 1992 to 1995 FDI inflows grew by over 130% per annum from a small base of US $75 million in 1991. This growth was short-lived. A slowdown and then net outflow occurred in the late 1990s. The new century brought greater stability. From 2002 to 2005 foreign direct investment to India rose 24% per annum and reached US $6.6 billion in

2005. This is considerably more than any single ASEAN country, other than Singapore.

Is ASEAN Under-Performing?

The economic and investment growth in Asia's two giants combined with ASEAN's 1997 economic crisis and slow recovery have sparked concern that its much larger neighbors will dwarf the region and marginalize its economies.[8] The world's focus seems to be on China and India with little attention being paid to the disparate, fractious and smaller economies of Southeast Asia.

Yet, the facts show otherwise. ASEAN is by no means destined to low growth and marginalization. While growth in ASEAN has not matched the spectacular levels of China and India, the ASEAN economies have performed reasonably well, especially since 2003. Singapore stands out at the top with nearly 8% annual growth from 2004 to 2006. The city-state's impressive economic growth and rise in foreign direct investment is the result of its efforts to identify and capitalize on niches where it has a competitive advantage. The other four original ASEAN members achieved GDP growths of 5-6% in the same period. While these growth rates are down from the boom years of the 1980s and early 1990s, they are still quite respectable.

Opportunities abound for ASEAN to capitalize on growth in China and India. Investors in China, both from the West and from Southeast Asia, have for many years used skilled and experienced executives from Southeast Asia to jump-start their operations in China. In addition, these companies have identified areas of complementarity in manufacturing between Chinese and ASEAN factories. Plants in Southeast Asia now supply components to Chinese factories where they have a competitive advantage.

Tourism and business services are two more areas where Southeast Asia can benefit from China's increased prosperity. Thailand in particular has put out the welcome mat and has enticed more and more visitors from China, Korea and Japan to its many tourist attractions. Singapore also has seen tourism rise, with 2006 setting records virtually every month for number of overseas visitors. Chinese visitors already account for the second highest number of any nationality to Singapore. With the construction and opening of new convention centers and casinos, Singapore is on course to build on its position as a top tourist destination in Asia.

Some analysts argue that greater cooperation and economic integration could improve the economics of investment in the region.[9] Removal of barriers to the free flow of goods, services and people would improve efficiency within the region and open new opportunities in a host of areas beyond just manufacturing. Coordination of policies on investment and greater cooperation in education could improve the attractiveness of the region as a whole to investors.

Economic Regionalism

Theory of Economic Integration

Béla Balassa, a professor at the Johns Hopkins University, first proposed the "Theory of Economic Integration" in 1961.[10] He described economic integration as a continuum that falls into six stages:

1. **Preferential Trading Agreement** (PTA). Preferential trading areas are often between neighboring countries and frequently cover only a single product category (e.g. the Canada-United States Automotive Agreement).
2. **Free Trade Area** (FTA). Preferential trading areas (PTAs) often evolve into wider free trade areas (FTAs) that eliminate tariffs and non-tariff barriers across most product categories. The North American Free Trade Agreement (NAFTA) is at this stage on the continuum.
3. A **Customs Union** eliminates tariffs among member states and establishes common tariffs on imports from the rest of the world. The Gulf Cooperation Council[11] (GCC) and Mercosur[12] are examples of customs unions.
4. A **Common Market** "establishes free trade in goods and services, sets common external tariffs among members and also allows for the free mobility of capital and labor across countries."[13] The European Union would be an example of Balassa's definition of a common market.
5. An **Economic and Monetary Union** is a common or "single" market with a common currency. The only existing economic and monetary union is the Eurozone within the European Union.
6. **Complete Economic Integration** entails centralized economic and monetary control where the individual states within the union have little control over economic policy. The former Soviet Union is an example of this stage of economic integration.

The theory of economic integration argues that economic integration will stimulate increased intra-regional investment and trade. A free trade area has more impact on economic activity than does a narrow preferential trade agreement. In turn, a common market, or better yet, a single market with a common currency has much greater economic benefits than does a free trade area. The more firmly integrated a region becomes, the greater the benefits accruing to businesses in that region.

Model for Economic Integration

The European Union is the model case study for the continuum of economic integration. The European Coal and Steel Community (ECSC) was established in 1951 as a preferential trade agreement to pool the steel and coal resources of member countries. The ECSC served as the foundation of the European Economic Community (EEC), which was formed in 1957. Over the next 35 years, the EEC gradually evolved from a free trade area into a common market with a strong centralized administration. The Maastricht Treaty signed in 1993 further strengthened ties among member states and set out an ambitious goal for an all-encompassing European

Union (EU). The next phase of economic integration, an economic and monetary union, was reached with the formation of the European Central Bank and the adoption of the euro in 1999. Complete economic integration remains an aspiration, despite the many obstacles that still remain in its the path.[14]

Both the EU and NAFTA must be considered a success of economic integration. The two agreements have led to sharply increased investment and trade. Over time, the ties among the countries in both groupings have strengthened enormously. Plus, accession to the grouping has proven to be a big lift to the economies of new entrants. NAFTA stimulated investment, helped boost exports and led to much greater economic stability for Mexico soon after it became a member. Similarly, the economies of Eastern Europe have benefited greatly from their accession into the EU. Poland, Estonia and the Czech Republic have achieved some of the highest economic growth in Europe since becoming members of the Union.

Based on these two examples, the evolution of economic integration from preferential trading agreements to complete economic integration would appear to be a recipe for high growth and economic prosperity. Other examples, though, seem to put this conclusion in doubt.

Attempts at economic integration among developing countries have not had nearly as positive an impact as those among developed economies and the path toward economic integration is not nearly as clear. NAFTA and the EU brought expanded access to huge new markets for new entrants. Free trade agreements among developing economies were not able to offer a similar stimulus to growth. Mercosur, the Andean Community, the Central American Common Market (CACM) and the Greater Arab Free Trade Area all were formed to stimulate greater intra-regional trade and to promote economic cooperation among members. None of these agreements has had a major impact on trade flows or economic growth.

The key to the success of the EU and NAFTA has been the complementarity of trade and investment of members and the opportunities to access the large developed markets made available to new developing members. If the products and services of member-states are narrowly based and uncompetitive then the benefits offered by economic integration are much less pronounced. The free trade agreements of Latin America suffer from this constraint. The profile of exports among members of the Andean Community and the CACM is similar and trade volume among members is modest. Economic integration under these circumstances has proven to be a poor source of growth stimulus.

ASEAN falls somewhere in between these two extremes noted above. The composition of exports among ASEAN countries is more diverse and less dependent on a few product categories than their Latin American counterparts. Greater cooperation and integration should bring the benefit of more investment to serve a larger market. Still, ASEAN countries often compete in exports and in encouraging foreign investment in a few critical sectors (e.g. electronics). Influential domestic manufacturers remain wary of wider market access and coordinated investment policies. Thus, ASEAN would gain from making progress toward economic integration; however, it would not see the huge benefits offered by membership in the EU or NAFTA.

ASEAN Progress Toward Economic Integration

ASEAN[15] has embarked slowly down the path of economic integration. Since the Bali Summit in 1976, the nations of Southeast Asia have promoted the ideal of economic cooperation. Nevertheless, in the first 15 years after the summit, only lip service was paid to reducing trade barriers and most of the moves toward regionalism were confined to paper only.

In 1992, progress toward trade liberalization and economic integration received a boost with the creation of the ASEAN Free Trade Area (AFTA). Since then, tariffs have significantly declined between the ASEAN 6 (the ASEAN 5 plus Brunei); however, progress toward freer trade overall has been slow, with many fits and starts.[16]

According to a recent McKinsey study,[17] intra-regional trade, as a percentage of the region's total trade, declined by 19% from 1994 to 2001, despite the formation of the ASEAN Free Trade Area in 1993. Although intra-regional trade has declined, AFTA cannot be written off as a failure. Full economic integration, akin to stages five or six of Balassa's continuum was not an ASEAN objective when it created AFTA. According to Narine[18], ASEAN pursued AFTA for four reasons: [1] To provide ASEAN with a new purpose and ensure that the organization remained relevant; [2] To provide greater leverage and a louder voice in international economic negotiations; [3] To make it easier for multinational companies to establish themselves on a regional basis; [4] To make foreign investment in ASEAN countries more attractive and offset the possibility of investment being diverted to China.

AFTA was primarily a *defensive strategy* for ASEAN. Members wanted to protect their share of foreign investment in the face of increased interest in China. Furthermore, they wanted to counter the increased influence of other trade blocks in international trade negotiations. Increased intra-regional trade might have been a welcomed by-product of AFTA, but it was not a primary objective. Rather, AFTA focused on encouraging foreign investment, which had been a primary stimulant of growth over the previous decade.

A second reason for the slow progress towards economic integration has roots in the method of diplomacy used in ASEAN. In its efforts to promote greater cooperation, the association has strived to follow the "ASEAN Way".[19] Based on the principal of governance in a Malay village, the ASEAN Way emphasizes consensus, consultation and "voluntarism." ASEAN tries to avoid violating any of the member's basic interests and often sets aside contentious issues or develops vaguely worded statements that can be open to interpretation. Numerous committees and working groups seem to characterize every aspect of ASEAN's activities.[20] Yet, for all the discussion, ASEAN does not impose any rules or regulations on its members. Members are *not* required to implement policies and ASEAN relies on the voluntary implementation of all joint declarations and decisions.

Similarly, ASEAN has resisted creating a strong secretariat for the organization that might infringe on the sovereignty and authority of individual members. While the secretariat has grown in size over the past decade, its role is primarily one of logistics and administrative support. It has virtually no oversight authority and does not have the capacity for analysis or recommendation, let alone decision-making.

This approach to decision making means that progress is often slow and halting. Furthermore, the differing stages of economic development and differing economic policies of members inhibit consensus. It is difficult to imagine Indonesia and Singapore having a more different economic profile. Malaysia, The Philippines and Thailand also have their own views on economic policy, which frequently are at odds with each other. Viewed from this perspective, the consensus and cooperation that has been achieved is truly remarkable.

The Price of Fragmentation

Some analysts argue that the slow progress on economic integration is threatening the region's competitiveness and leading to marginalization. A study conducted by McKinsey consultants Adam Schwarz and Roland Villinger for ASEAN's ministers argues that the price of fragmentation has been high. They point to three main concerns about the lack of economic integration in ASEAN:

1. **Subscale Markets**: Manufacturers are forced to produce and market goods for smaller domestic markets. Consequently, manufacturers often cannot reach production levels that are economically efficient or on a globally competitive scale.
2. **Unnecessary Costs**: Different product standards across member countries prevent businesses from standardizing products, which in turn leads to higher production costs.
3. **Unpredictable Policy Implementation**: Policies are implemented inconsistently and regulations are often enforced arbitrarily. The lack of reliable or consistent policies and regulations increases risk and consequently costs.

In addition to these three economic concerns cited by McKinsey, can be added a fourth consequence: dislocation of labor markets. The lack of economic integration has led to higher personnel costs, disparate skills availability and widely varying labor market profiles across the region.

Subscale Markets

The small size and unconnected borders of the Southeast Asian countries create obstacles to building large-scale manufacturing operations. Automotive manufacturing is a case in point. In the past 10 years, automotive manufacturing in China and India has boomed, fueled by a large domestic population and seemingly insatiable demand. The world's largest motor vehicle manufacturers have moved quickly to capitalize on this growth and the number of automotive factories in both countries has mushroomed. Now, some multinational automotive manufacturers are expanding their plants to create capacity for export.[21]

Meanwhile, the automotive industry in Southeast Asia is in the doldrums even though multinational automotive manufacturers have long experience and established operations in the region. Proton, Malaysia's principal automotive manufacturer with 41% of the domestic market, has watched its sales wither and are now looking for foreign partners.[22] Astra International, Indonesia's largest automotive manufacturer, reported a drop of 36% in unit sales in 2006.[23] Thailand's automotive industry has had to scale back its ambitious expansion plans in the face of lower sales in 2006.[24]

Thailand with 1.1 million unit sales in 2005 has perhaps the healthiest automotive industry in Southeast Asia, but it pales in comparison with China's 8 million unit sales[25] or India's 10 million unit sales.[26] The small size of individual ASEAN markets makes it next to impossible for automotive manufacturers to build plants that can compete with those of its northern neighbor.

Unnecessary Costs

ASEAN has made little progress in harmonizing regulations. The multiplicity of regulations and inconsistency in enforcement certainly add to the cost of doing business across Southeast Asia. This is clearly shown through an annual World Bank report, which investigates the regulations that enhance business activity and those that constrain it.[27] The report analyzes and measures ten areas of everyday business: starting a business, dealing with licenses, employing workers, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts and closing a business. Analyzing these factors, the report ranks 175 countries in terms of their ease of doing business.

The results clearly demonstrate the disparity of policies and practices across the region and show how inconsistent regulation adds costs to operating region-wide. According to the World Bank study, Singapore is number one globally in terms of ease of doing business (Hong Kong is the only other territory in all of Asia to rank in the top 10). Thailand is 18th while Malaysia is not far behind at number 25. In contrast, Indonesia ranks 135th and the Philippines 126th in the worldwide ranking of 175 countries. Perhaps equally disappointing, the 2007 ranking of the Philippines and Indonesia has gone down by five and four places respectively as compared to the 2006 ranking.

Areas where Indonesia ranks poorly in the worldwide ranking are the cost and time of starting a new business, enforcing contracts, and dealing with licenses. Restrictions on hiring and firing and the complexities of paying taxes also are relatively onerous in Indonesia.[28] The Philippines scores lowest in protecting investors due to limited disclosure requirements and investor protection. Hiring and firing as well as dealing with licenses are also problematic.[29]

Unpredictable Policy Implementation

Policies toward foreign investment and trade vary widely across the region. Singapore, on one extreme, has the most open economy in the world and aggressively promotes foreign investment. It has successfully attracted the largest amount of foreign investors' funds despite its small size. Only China and Hong Kong surpass Singapore's inflows of foreign direct investment in all of Asia.[30]

On the other extreme is The Philippines, where FDI inflows in 2004 amounted only to US $469 million. The Philippines has long been ambivalent towards foreign investment and free trade. Restrictions on foreign ownership are written into the Philippine constitution and non-tariff barriers have risen recently, along with a resurgence of protectionism.[31] Political turmoil and domestic issues in Thailand and Indonesia have preoccupied policymakers in those countries for most of the past decade. The populism of Thaksin Shinawatra thwarted efforts to open up the Thai economy and no meaningful liberalization occurred under his administration.[32] The recent flip-flop of Thailand's new administration on portfolio foreign investment controls has scarred investors and raised concern about the reliability of Thai financial policy.[33]

While President Susilo Bambang Yudhoyono has brought greater stability to Indonesia, the country has faced a series of natural disasters and terrorist attacks that have taken priority over economic issues. Strict labor market regulations, undependable enforcement of property rights and contracts, corruption and weak public administration remain the primary obstacles to foreign direct investment and economic growth.[34]

Dislocation of Labor Markets

In addition to the three economic issues cited above, lack of cooperation and coordination on labor issues threatens ASEAN's competitiveness. Rigidities in the labor force and labor laws put Southeast Asia at a distinct disadvantage when compared to China, plus personnel costs are relatively high.

A great strength of the Chinese economy is the depth and flexibility of its labor force. Chinese workers are highly mobile, as witnessed by the massive migration home every year at Chinese New Year. Variance in wages and salaries across the country are relatively modest. While salaries are rising rapidly for professional level staff, wages for unskilled workers are kept in check by the continuous flow of labor from the countryside to the cities. At the same time, labor unrest is almost unheard of.

In contrast, labor rigidities, disparate costs and rising industrial unrest are major constraints to growth and inhibit competitiveness across Southeast Asia. Resistance to intra-regional immigration or employment has created labor rigidities. Even in labor-short countries, such as Singapore, the preference is for workers from distant locations, such as Bangladesh and China, rather than close ASEAN neighbors, such as Indonesia or Thailand. Restrictions on immigration plus differences in culture and language inhibit companies from treating ASEAN as a single pool of talent. Ironically, ASEAN expatriate workers and professionals alike are more likely to be found in jobs outside the region than jobs within. The end result of restrictions on labor movement is that shortages and surpluses occur across the region for similar skill sets.

The labor rigidities have a knock effect on costs. Unlike China, the cost of personnel varies widely across the region. Ironically, the smaller countries of Singapore and Malaysia have greater availability of many technical skills than do the larger economies of Indonesia and Thailand. Low investment in education in Indonesia and Thailand further compound the problem of skills availability and leads to disproportionately high costs for professional and managerial positions.[35]

Rising industrial unrest and declining productivity have been a growing problem in Indonesia. Indonesia's new labor law, enacted in 2003, has made the situation worse by increasing mandatory severance payments and allowing local governments to set minimum pay increases for workers.[36] Labor laws in The Philippines are also onerous.[37] Plus, the large number of Filipinos employed as foreign workers are leading to serious social issues at home that have been characterized as "a recipe for stagnation."[38]

Steps Needed for Integration

Economic integration would help address the concerns mentioned above and improve the prospects for higher economic growth in ASEAN. Many analysts have encouraged ASEAN to take more assertive action towards integration. The rise of China and India has re-enforced and made more urgent the call for action on integration.

The McKinsey report cited previously believes that the foremost factor behind the slow progress towards integration is "a lack of political will … because of widespread uncertainty among policy makers and business executives about the end goal of economic integration and its benefits for individual countries."[39] The report recommends a two-pronged integration plan: 1) a sector-based approach to focus the region's integration efforts and, 2) a set of reforms to create stronger regional institutions to manage the integration.

McKinsey would accelerate an integration program for consumer goods and electronics through four initiatives: [1] Eliminate non-tariff barriers by harmonizing regulations; [2] Enhance tariff reform by eliminating tariffs that bring in relatively little revenue while creating an administrative burden; [3] Create a level playing field for capital by eliminating restrictions on cross-border investment; [4] Improve regional collaboration by cooperating in testing for product certification, automating customs and enforcing intellectual property rights.

At the same time, McKinsey urges ASEAN to develop a much stronger institutional framework that would support integration. According to McKinsey, ASEAN should state explicit economic goals and develop a plan for achieving them. ASEAN should move toward "qualified majority voting and strengthen its secretariat and entrust it to analyzing issues and developing recommendations. McKinsey would also have ASEAN establish a mechanism "to handle any failure of member countries to implement their integration commitments." [40]

Using the experience of the EU as a model, the McKinsey consultants have identified lofty goals and a roadmap for achieving them. Unfortunately, their recommendations appear to be unrealistic and divorced from political realities. The principal obstacles in the way of adopting ambitious goals and plans for economic integration are a vacuum in regional leadership, a lack of consensus on ASEAN objectives and a reluctance to abandon the "ASEAN Way."

Leadership Vacuum

As McKinsey rightly points out, the principal factor behind AFTA's slow progress is the lack of political will. But each of the ASEAN countries except Singapore is engrossed in domestic political issues that preclude an assertive international role. Singapore itself is unable to exert a regional leadership role due to its small size and unique economic character (i.e. a fully open and developed economy).

Indonesia would seem to be the natural candidate for the primary leadership role in the region. It is by far the largest ASEAN nation and has gone through major political reforms since the days of President Suharto. Unfortunately, Indonesia also has been beset by natural disasters and terrorist attacks that have required the administration of President Yudhoyono to focus its attention internally. President Yudoyono has shown little interest or concern for promoting regional integration. The other most likely candidate is Thailand. Thailand has demonstrated support for ASEAN integration and strong leadership within the Association. It was through a Thai initiative that AFTA was originally created. But it is unlikely that Thailand will re-exert a leadership role any time soon. With the overthrow of Thaksin Shinawatra in 2006, the new regime has become preoccupied with returning the country to civilian rule. It will be many years before Thailand can take a lead within ASEAN.

Similarly, the leaders of Malaysia and The Philippines are in no position to take a central international role due to domestic weakness brought about by strong opposition leaders; for example, Malaysian Prime Minister Abdullah Ahmad Badawi is beset by continuous sniping from former Prime Minister Mahathir Mohamad. The administration of President Gloria Macapagal-Arroyo is quite fragile as she battles demands for her resignation and impeachment as well as threats of a coup and allegations of vote rigging. Strengthening ASEAN through economic integration is perhaps the last thing on her mind.

Leadership is unlikely to emerge from within ASEAN until considerable time has past and current political issues have been resolved. Some analysts have called on China, Japan or the US to provide greater support for ASEAN economic integration. In fact, in 2003 China signed a pact with ASEAN that called for a free trade area among the countries by 2010. "ASEAN + 3" (ASEAN plus China, Japan and South Korea), represents another attempt to extend ASEAN beyond Southeast Asia.

Lack of Consensus

As McKinsey rightly points out, ASEAN suffers from no clear economic goals or a plan to achieve them. The difficulty is that no consensus exists, nor is one likely to emerge for the ultimate economic objectives of the Association. Each ASEAN state has a different perspective on its own economic interests. With its open economy, Singapore is unlikely to embrace any regional economic integration that entails a common customs union. Singapore has advocated "open regionalism" where any tariff reductions apply equally to all trading partners, whether or not they are part of ASEAN. Malaysia, on the other hand, backs the "ASEAN + 3" initiative that looks toward a free trade area encompassing ASEAN plus China, Japan and South Korea. Indonesia and The Philippines are the most cautious, claiming that reduced tariffs in many product categories would damage domestic manufacturers.

The lack of consensus extends beyond trade matters. ASEAN initiatives to reduce and reform regulations have met with resistance in many quarters. Consistent regulations on product labeling are at odds with domestic insistence on labels in the local language. This is especially the case for Thailand since Thai uses its own written script, which is unique within ASEAN. Demands for consistent ASEAN regulation often are seen as an encroachment on national sovereignty. Even these small attempts at consistency are sometimes met with hostility.

Reluctance to Abandon the "ASEAN Way"

McKinsey argues that there needs to be greater clarity in objectives and greater detail for a plan to reach those objectives. Furthermore, it argues a strengthened secretariat is essential to monitor and police the commitments that members make.

As was mentioned earlier, ASEAN has been built on consensus, voluntarism and avoidance of conflict. Insistences on clarity, demands for compliance rather than voluntarism, and policing of the agreement are directly at odds with the ASEAN Way. The next step in economic integration requires greater clarity and cooperation. The ASEAN Way has served the region well in advancing the limited goals of the Association. Few ASEAN leaders would be willing to give up their authority to a regional body.

The Way Forward

For these reasons, it is highly unlikely that ASEAN will adopt the recommendations of consultants to aggressively pursue the path of increased regional economic integration and stronger supra-national regional authority. The model of the European Union has limited relevance for ASEAN and a full economic and monetary union should not be considered as an ASEAN aspiration. In fact, ASEAN may never advance to the next stage according to the theory of economic integration.

Singapore's former Prime Minister and current Senior Minister Goh Chok Tong put it succinctly, "The trend toward greater economic integration in Asia will gather speed. East

Asian regionalism will, however, be far less institutionalized than in Europe. New patterns of trade and investment, business decisions, production chains and webs of FTAs will draw the region together. Such a looser and less bureaucratized structure will be more appropriate to East Asia than the EU model."[41]

The way forward for ASEAN is to build on past successes and pursue economic cooperation using its own unique approach. The critical elements of a successful strategy of economic integration is one which encompasses:

The ASEAN Way: As pointed out by Goh Chok Tong, "Southeast Asia enjoys no natural coherence. Rather it is characterized by deep political, ethnic, cultural and religious diversity." The ASEAN Way is designed to deal with the challenges of diversity. ASEAN cannot impose majority will on all members. It must look for areas of agreement and all agreements need not apply to all members. Through patience and persistence, the ASEAN Way of diplomacy is best suited to this region.

Regionalization: Economic integration in Southeast Asia needs to be characterized by "regionalization" as much as "regionalism." The distinction between the two is quite important. According to T. J. Pempel, "regionalism has three key elements: it is top down, it is biased toward formal (usually governmental) agreements; and it involves semi-permanent structures in which governments or their representatives are the main participants. Regionalization, in contrast, develops from the bottom up through societally driven processes. The most important driving forces in regionalization come from markets, from private trade and investment flows, and from the policies and decisions of companies."[42]

The private sector has always had a critical role in economic policymaking in Southeast Asia. Private sector involvement in the process of economic integration is essential to its success. Unlike in Europe, governments need not spearhead economic integration in all matters. The benefits of integration are clear to many in the private sector and numerous global, as well as regional companies have already embarked on integrating their East Asian operations. Close private-public cooperation will help ensure that barriers to this integration are dealt with on a practical and case-by-case basis.

Multipolarism: The diversity of Southeast Asia dictates a multipolar approach towards economic integration. A web of agreements and relationships among member and non-member states and groups is likely to characterize closer economic integration in the future. In the past decades, ASEAN and its members have concluded numerous free trade agreements. This trend is likely to continue since no single approach is agreeable or will work for all ASEAN members. Rather than pursue a single approach such as AFTA, ASEAN + 3, or the Free Trade Area of Asia Pacific; ASEAN and its members will identify opportunities that advance growth through increased trade and investment.

ASEAN ties increasingly will extend beyond Southeast Asia. The growing importance of India and China to the world economy will encourage ASEAN to forge ties of cooperation with these two countries. China has already reached agreement on a free trade area with ASEAN, while negotiations with India are underway. At the same time, it is unlikely that members will turn their backs on long-established links to the US, Japan and the EU. ASEAN and its members have numerous trading agreements with all three regions and discussions are underway as to how to make these agreements stronger.

Voluntarism and Informality: Voluntarism and informality are distinctions that have characterized ASEAN since its inception. Members can "opt-in" to agreements and full compliance is rarely necessary before an agreement comes into force. For example, AFTA currently only applies to the ASEAN 6. Voluntarism is highly practical for such a diverse grouping as ASEAN. Rarely is it possible to have full consensus and agreement from all 10 members. Similarly, informality works well for the organization. Discussions often do not lead to a formal, binding agreement among members. Members identify points of commonality during the discussions and those that can agree to a common approach may go forward. This enables progress on contentious issues without enforcing majority will or demanding unanimity.

ASEAN should build on its unique approach to economic integration through regionalization, multipolarism and voluntarism. It should:

Promote regionalization and support private sector initiatives: Working closely with the private sector, the governments of ASEAN can identify and address specific obstacles to greater integration of business across the region. ASEAN sector-specific, public-private working groups should identify critical areas of regulatory reform. ASEAN members can help each other by relying on best practices and pooled resources to reform and coordinate regulatory practices across the region.

Pursue a multi-polar strategy to integration: ASEAN and its members should continue to build and strengthen a network of ties among its members and with its major trading partners. The increased web of trade liberalization and regulatory cooperation will boost economic growth and hasten regional economic integration.

Utilize voluntarism as a core strategy in promoting integration: The AFTA approach to economic integration is the most appropriate for ASEAN. Members accede to the terms of a free trade agreement when they are ready, but benefits accrue to members only when they accede to the agreement. Members are encouraged to adopt regulatory reform and trade liberalization in order to gain the benefits gained by those that have already done so.

The way forward for ASEAN is clear – to build on past achievements and pursue the unique approach that has characterized the grouping since it's founding. ASEAN can gain from the advantages of increased regional cooperation. While Southeast Asia cannot aspire to overtake China as the economic powerhouse of Asia, greater economic integration will increase growth in the region and provide greater opportunities for investors. ASEAN and its members, acting alone and in concert, should take steps to ensure economic integration happens.

Endnotes

1. Lee Kuan Yew. “ASEAN Must Balance China in Asia.” *New Perspectives Quarterly* V18 no3 (Summer, 2001) p21 and Adam Schwarz and Roland Villinger. “Integrating Southeast Asia’s economies” *McKinsey Quarterly*, 2004, No. 1, p35-47
2. The Association of Southeast Asian Nations (ASEAN) was originally formed in 1967 and comprises 10 countries: Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam.
3. Roel Landingin and John Burton. “China in key deal with ASEAN on services.” *The Financial Times*. London: January 14, 2007.
4. The original five ASEAN members were Indonesia, Malaysia, the Philippines, Singapore, and Thailand. The average GDP growth figures cited in the text are “unweighted”, i.e. each country has an equivalent weight.
5. FDI inflows into China in 1992 were US$11 billion while FDI inflows into the ASEAN 5 were US$12 billion.
6. All statistics on foreign direct investment have been taken from *World Investment Report*. United Nations. UNCTAD. *World Investment Report 2005*. New York and Geneva: July 2005.
7. Singapore alone accounted for US$20.1 billion up from US$13.5 billion in 2003.
8. Schwarz and Villinger. “Integrating Southeast Asia’s economies”.
9. Schwarz and Villinger, p43.
10. Béla Balassa. *The Theory of Economic Integration*. Homewood, IL: R.D. Irwin, 1961
11. Members of the GCC are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.
12. The Mercosur members are Brazil, Argentina, Uruguay, Venezuela, and Paraguay.
13. Steve Suranovic. “International Trade Theory and Policy: Special Topics and Issues.” 4 Jan 1998. The International Economics Study Center. 5 Jan. 2007. internationalecon.com/v1.0/ch110/ch110.html.
14. The economic challenges posed by the expansion of the EU into less-developed Eastern Europe and the United Kingdom’s continuing resistance to adopting the euro are two examples of obstacles in the way of complete economic integration.
15. ASEAN is currently comprised of 10 countries: Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam.
16. Shaune Narine. *Explaining ASEAN: Regionalism in Southeast Asia*. Lynne Rienner Publishers, Inc (Boulder, CO: 2002) 237 pages.
17. Schwarz and Villinger, p40.
18. Shaune Narine, p126.
19. For a full discussion of the “ASEAN Way”, see Explaining ASEAN, p31-33.
20. ASEAN has over 100 official working groups. See “Committees Under the Purview of AMM (Foreign Ministers)” - www.aseansec.org/14422.htm.
21. “China expects to beat US as world’s No. 1 auto market.” *Shanghai Daily*, 31 October 2006.
22. “Corporate News: Malaysia’s Proton to review goals amid ‘tough’ automobile market.” *The Wall Street Journal Asia*, 11 September 2006.
23. “General Motors Exec: No Plans To Merge With Rival Ford.” *Dow Jones Newswire*, 8 November 2006.
24. “Thailand’s automobile industry .. It is now time to adjust strategy and revise the Eco Car project” *Thai News Service*, 6 November 2006.
25. “China 2007 auto sales to exceed 8 mln units, up 15 pct yr-on-yr - state media.” *Xinhua Financial Network (XFN) News*, 22 December 2006.
26. “India yr to March auto sales up 13 pct; output tops 10 mln units for 1st time.” *AFX Asia*, 13 April 2006.
27. The International Bank for Reconstruction and Development. *Doing Business 2007: How to Reform*. Office of the Publisher: Washington DC 2006,
28. The World Bank Group, “Doing Business: Explore Economies: Indonesia,” World Bank, www.doingbusiness.org/ExploreEconomies/?economyid=90. (accessed January 9, 2007)
29. The World Bank Group, “Doing Business: Explore Economies: Philippines,” World Bank, www.doingbusiness.org/ExploreEconomies/?economyid=153.
30. Note that a large proportion of foreign direct investment into Hong Kong is actually destined for China.
31. Razeen Sally; Rahul Sen “Whither Trade Policies in Southeast Asia? The Wider Asian and Global Context” *ASEAN Economic Bulletin*; Apr 2005; 22, 1: 106.
32. Sally and Sen, 104.
33. “Experts warn of ripple effects.” *The Nation* (Thailand), 26 December 2006.
34. Sally and Sen, 105.
35. *2006/2007 Asia Pacific Human Resource Atlas*. Mercer Human Resource Consulting, Singapore: 2006.
36. Tom Wright “Indonesia’s Labor Laws Deter Investment” *Wall Street Journal*, New York: December 7, 2006, p A8.
37. Jeffrey O. Valisno, “RP labor laws uncompetitive: *BusinessWorld*. Manila: Feb 23, 2006. pg. 1
38. Richard C. Paddock, “The New Foreign Aid: Philippines” *The Los Angeles Times*, April 20, 2006, pA22.
39. Schwarz and Villinger, p43.
40. Schwarz and Villinger, p46.
41. Goh Chok Tong, “The New Shape of Asia” *The Wall Street Journal Asia*, June 10, 2005, pA7.
42. T. J. Pempel, “Introduction: Emerging Webs of Regional Connectedness”. *Remapping East Asia: The Construction of a Region*. Cornell University Press (Ithaca, NY: 2005), p19.

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Richard Payne is an international strategic management consultant helping organizations build successful businesses in Asia. He advices corporate leaders on how best to lead, motivate, and reward employees throughout Asia by utilizing 25 years of experience creating an Asian-wide consulting business and writing about business issues in the region. Richard is the author of numerous articles and books, including: *The Asian Manager: Recruiting, Training and Retaining Executives* and T*he Asian Expatriate: Strategies for Recruitment, Training and Re- entry*. Mr. Payne has a Master of Arts in Asia Pacific Studies from the University of San Francisco and a Master of Arts in International Relations from Johns Hopkins University School for Advanced International Studies.