Executive Summary

By coming together, Asia’s economies have grown much stronger. The region’s world-beating economic growth owes much to its success in developing the intricate web of regional supply chains and production networks often known as “Factory Asia.” This exceptional cross-border collaboration involves shipments of raw materials and manufacturing parts and components that crisscross the region, along with foreign investment and—increasingly—businesspeople, managers and other skilled workers. This emerging Asian regionalism offers a new platform for economic development that is, as the predecessor to this report, *Emerging Asian Regionalism: A Partnership for Shared Prosperity*, put it, “good for individual economies, good for Asia, and good for the world.”

These developments are mostly a result of market forces allied with liberalizing national policies, rather than of a grand European-style scheme to create a single market for the region. But while Asia’s integration has mostly been market driven, in recent years it has increasingly been complemented by government-led initiatives, notably in financial cooperation—such as the Chiang Mai Initiative—as well as in trade, investment, and other areas.

Asia has developed a dense and elaborate web of institutions for regional integration (IRIs) that seek to advance regional economic integration and cooperation. IRIs in Asia and the Pacific now number 40 and are classified into several categories¹ (Chapter 4), resulting in a

¹ *Overarching*—umbrella arrangements with comprehensive purviews—such as ASEAN, SAARC, PIF, ASEAN+3 and the EAS; *functional*—specialized institutions with a narrower, often technical agenda—such as Central Asia Regional Economic Cooperation (CAREC); *facilitating*—institutions that bolster regional integration by providing advisory, administrative and technical, and financial support—such as ADB and ESCAP. Their geographical reach is *subregional*—covering all or part of Central Asia, South Asia, Northeast Asia, Southeast Asia, or the Pacific; *intraregional*—covering at least two but not all of these five subregions; *pan-Asian*—covering all of Asia’s subregions; *transregional*—linking Asia to other regions of the world.
tangled web with overlapping agendas and memberships reflecting the region’s diversity. Given this, Asian regionalism remains “institution-light,” characterized by few delegated powers, a lack of permanent secretariats, and a lack of formal rules and legal structures.

The current institutional base needs to become stronger and needs to reform to enable policy makers to address four big challenges.

- **Cementing recent gains.** The region’s openness is a strength, but it also has its downsides, not least a vulnerability to external shocks. The 2008–2009 global financial crisis underscores the need to buttress economic and financial stability to consolidate recent gains. Moreover, while regional economic cooperation has progressed in recent years, existing obligations and commitments have yet to be implemented uniformly across Asia and the Pacific.

- **Broadening the process.** Asian economic integration remains uneven across subregions and sectors. Until now, it has mostly focused on trade in intermediate goods within East Asia. While trade between South and East Asia—notably between India and the People’s Republic of China (PRC)—is growing, not all parts of those regions, and not all sectors and activities, are equally involved. Whereas almost 60% of East Asia’s trade in parts and components takes place within the region, intraregional trade shares are very low in Central and South Asia, and in the Pacific. Since intraregional trade—in intermediate goods, in particular—can be an important driver of growth, its benefits now need to be extended throughout those three subregions.

- **Deepening integration.** The next steps in regional integration involve: moving from integrated trade and production networks to more deeply integrated goods markets by lifting behind-the-border barriers to trade and competition; removing obstacles to interregional trade in services; allowing a freer movement of labor, especially skilled labor, across the region; developing deeper, wider, and more crisis-resilient financial markets in Asia that are able to allocate the region’s vast (often externally invested) savings more efficiently to its huge investment needs and thus facilitate global rebalancing; and coordinating monetary and fiscal policies more closely in order to enhance macroeconomic and exchange-rate stability. Last but not least, they involve reducing poverty, shrinking income disparities, and boosting investment and growth in the less dynamic economies across Asia and the Pacific. The end result would be the creation of an “Asian economic community,” complete with
a new regional architecture that would include fully integrated markets and stronger regional institutions.

**Ensuring the compatibility of regional and global integration.** Since Asia is highly integrated globally as well as regionally, it is crucial that measures to cement the region’s integration complement rather than jeopardize its links with the rest of the world.

These four challenges cannot be met by relying on market processes and national action alone—Asian countries will also have to work together effectively.

Asia’s growing importance in the global economy also demands more ambitious and coherent regional cooperation. To play a greater role in addressing global economic issues, the region must increasingly act together—not only out of self-interest but also to help maintain global economic prosperity. Asia has a large stake in bolstering global economic stability and promoting open international markets. By pooling its strengths, it can have more influence on global economic institutions, such as the World Trade Organization (WTO) and the International Monetary Fund (IMF), to Asia’s benefit and that of the world.

**Long-Term Vision**

This study’s long-term vision for regional economic integration in Asia and the Pacific is of a strong, prosperous, and outward-looking economic community, regionally integrated yet connected with global markets, and with responsibility and influence to match its economic importance. This implies:

- an integrated market free of restrictions on flows of goods and services;
- deeper and more liquid financial markets open to cross-border financial flows, with high standards of oversight and strong protection for national and foreign investors;
- effective frameworks for coordinating macroeconomic and exchange-rate policies, taking into account global challenges and differing national circumstances;
- regional forums and dialogues to address vital social issues, such as poverty, exclusion, income insecurity, migration, aging, health, and environmental threats; and
- a consistent voice to project regional concerns in global policy forums and enhance responsible global governance.
The creation of such an economic community requires Asia to evolve toward new regional architecture made up of stronger IRIs with greater powers delegated from their member countries and closer links with each other. While an Asian economic community cannot and should not be achieved overnight, it is a long-term goal which can inspire and guide leaders and policy makers as they craft responses to the region’s short- and medium-term needs and challenges.

Anatomy of Existing Institutions

This report offers recommendations for strengthening Asia’s IRIs with the goal of sustaining and broadening regional integration and eventually achieving an Asian economic community. In doing so, it builds on a set of observations about Asia’s institutional architecture and how this compares with other regions.

• Asia’s approach to regional integration is pragmatic and flexible, resulting in a multitrack and multispeed process. It has adapted its cooperative structures to the varied priorities of Asia’s diverse economies and subgroups thereof. Regional cooperation and integration in Asia has tended to follow a bottom–up approach that supports subregional cooperation efforts as building blocks for an eventual broader and more unified regional architecture. However, following a model based only on flexibility and pragmatism has limitations. More effective and efficient institutions for regional integration are increasingly needed to manage Asia’s expanding challenges and opportunities.

• Asia’s existing IRIs are firmly established. They are the starting point for any attempt to create an institutional architecture capable of meeting the new challenges for regional integration. As the survey of Asian opinion leaders conducted for this study shows, there is more support for strengthening the region’s existing institutions than for creating new ones.

• Most of Asia’s IRIs are intergovernmental in structure, take decisions by consensus, and involve the delegation of only limited powers to independent secretariats and other extra-governmental bodies. However, governments are willing to embrace different institutional arrangements when they realize that the advantages of doing so are great. Some IRIs, such as the Association of Southeast Asian Nations (ASEAN), have expressed interest in building stronger secretariats to which member governments may be prepared to delegate more
Institutions for Regional Integration

effective authority to handle some aspects of common regional policies; others are moving toward making decisions through qualified-majority voting as well as by consensus, as in the case of the Chiang Mai Initiative Multilateralization (CMIM).

• Asia’s distinctive institutional architecture reflects its political, economic, and social characteristics. The pronounced diversity of Asia’s economies and societies represents a major challenge for institution building. Moreover, Asian countries that were created only a few decades ago following a period of colonization understandably tend to give regional issues a much lower priority than building national identity and domestic institutions. However, although Asian governments are wary that strengthened regional institutions would intrude into their domestic political space and policy autonomy, regional comparisons and Asia’s engagement with global institutions suggest that sovereignty costs are not insurmountable. Concerns over relinquishing policy autonomy can be met through the design of delegation mechanisms and adequate representation for national governments.

• Regional and global integration are not alternatives. Asia’s economies are continuing to integrate globally as well as regionally. Asia’s regional architecture should remain compatible with global integration and a strengthening of global governance. Unfortunately, Asian countries’ obligations to regional and global institutions are not always implemented and interpreted uniformly across the region. Asia’s exceptional economic and political diversity makes for enormous variation in governments’ capacity to bring national practice in line with those obligations.

• While integration in Asia and the Pacific has been heavily driven by economic logic, there is a broad preference in the region for deepening political and security cooperation and elaborating its corresponding institutional architecture. A large-membership regional institution that combines economic, foreign policy, and security agendas would also permit programs of political reconciliation and possibly military confidence-building that have been instrumental in furthering regional economic cooperation elsewhere.

General Principles for Reform

Using these observations as points of departure, this report identifies two general principles for strengthening Asia’s IRIs—openness and transparency—and three sets of recommendations for reform:
strengthen overarching institutions, develop functional ones, and establish new pan-Asian institutions.

**Openness.** Asia’s idea of “open regionalism,” which does not discriminate against non-members, implies that Asia should make the most of global institutions and conventions. These provide a basis for liberalizing and harmonizing arrangements where there is no strong presumption that regional ones should differ from those in the rest of the world. This is an effective way of ensuring that measures to cement Asian integration also foster the region’s links with the global economy.

In many key areas, however, such as macroeconomic stability, development finance, trade liberalization, and financial stability, Asian institutions can complement the activities of their global counterparts.

In the area of macroeconomic stability, the IMF’s Article IV has led to procedures on which Asia’s own nascent surveillance activities can usefully draw. ASEAN+3 countries recognized the IMF’s experience in structuring emergency financial assistance and conditionality when developing the CMIM.

In future, regional organizations—alongside the IMF—could act as “first responders” in the case of regional threats. This could avert the criticism that the IMF reacts too slowly because it represents the interests of countries outside the region, and it could better internalize spillovers among closely linked economies. The CMIM provides an especially opportune foundation for such complementary responsibilities. This could also allow the emergence of a new model of Asian collaboration with the IMF, drawing on Europe’s example.

In the area of development finance, the World Bank provides technical assistance and finance for development projects not just on a self-standing basis but also in cooperation with Asia’s IRIs. Where their agendas overlap, ensuring the coherence of the efforts of Asia’s IRIs and global institutions is an essential element of shaping a new regional institutional architecture.

Ideally, the World Bank should focus on global objectives and externalities, and regional development banks should focus on regional ones, such as infrastructure connectivity and regional environmental protection. They could also support projects funded and managed by the countries most interested in them. A good example is the creation of the Credit Guarantee and Investment Facility (CGIF) as ADB’s trust fund to promote local-currency bond markets in ASEAN+3 countries.

In the area of trade liberalization, trade policies could be harmonized across Asia in a manner that strengthens the region’s integration with the rest of the world by bringing national law and
practice in line with WTO protocols, a strategy that has worked well previously.

Unfortunately, the WTO’s Doha Round negotiations have stalled, while regional agreements continue to proliferate. A link between regional and global processes could address the challenge of making regional free trade agreements (FTAs) more multilateral-friendly, for example, by using standard approaches to address vexing issues, such as rules of origin.

In the area of financial stability, bringing national regulation and practice into compliance with Basel Committee and Financial Stability Board (FSB) standards, supervision and regulation within Asia could be harmonized so as to promote the integration of regional financial markets while strengthening their links to global ones.

The recent global financial crisis has highlighted the need for an international framework to monitor, regulate, and supervise cross-border transactions, including the activities of systemically important financial firms and products. At a global level, the FSB has been tasked with establishing such a framework and coordinating the authorities charged with implementing it. It is also charged, in collaboration with the IMF, with providing early warning of macroeconomic and financial risks and proposing actions to remedy them. The same issues are being addressed in Europe by a new European Systemic Risk Board and European System of Financial Supervisors. A similar structure should be developed in Asia, starting with the creation of an Asian Financial Stability Dialogue (AFSD) to promote financial stability, assist in long-term financial market development, and establish standards for governance and transparency in the region. Such an institution could play a valuable role by translating FSB initiatives into a regional context and then helping to implement them.

**Transparency.** Asia should enhance the governance of its IRIs by providing more information about their activities and more civil-society input into their deliberations. Regional leaders are aware of the need to improve the governing principles and decision-making structures of Asia’s IRIs, as the perception survey conducted for this report makes clear. Transparency is one mechanism for enhancing accountability and strengthening governance. One suggestion along these lines is for Asia’s IRIs to establish compliance boards: independent entities composed of business and academic members to assess progress. More generally, it would be desirable to encourage greater participation in Asia’s IRIs by civil society members sympathetic to the goals of regional integration.
Specific Recommendations

This report offers three sets of specific recommendations consonant with these overarching principles.

**Strengthen and rationalize overarching institutions.** Overarching IRIs play a key role in the Asian integration process. Both subregional and intraregional ones need to be strengthened, while intraregional ones also need to be rationalized. They need to create more effective, autonomous secretariats, equipped with stronger agenda-setting and surveillance powers, adequate financial and human resources, and clear legal mandates; establish clearer and more objective membership rules; develop enhanced decision-making rules; and build stronger links both with each other and with national agencies in order to promote closer integration among Asia’s subregions. At the intraregional level, ASEAN+3 and the East Asia Summit (EAS) both need to establish a secretariat.

**Develop functional institutions.** Subregional initiatives that have worked well in specific parts of the region ought to be replicated elsewhere. For example, the Cross-Border Transport Agreement of the Greater Mekong Subregion, the Asian Bond Fund (ABF) of the Executives’ Meeting of East Asia Pacific Central Banks (EMEAP), and the ASEAN Agreement on Transboundary Haze Pollution. Newly established IRIs such as the CGIF of ASEAN+3 could also bolster regional economic integration by facilitating the development of Asia’s bond markets. Wide-ranging discussions are also under way concerning the formation of a region-wide FTA, possibly by connecting complex, overlapping FTAs into one simplified agreement.

Financial cooperation is a particularly important area. East Asia is leading the way through ASEAN+3 and EMEAP, and other parts of Asia could learn from its experience. The new ASEAN+3 Macroeconomic Research Office (AMRO), established to conduct regional financial surveillance, needs to be endowed with appropriate financial and human resources and authorized to prepare comprehensive analyses to support the operation of the CMIM and ASEAN+3’s Economic Review and Policy Dialogue (ERPD). By organizing frank peer reviews of members’ policies, AMRO would strengthen the CMIM, since more effective surveillance would encourage governments to undertake necessary policy reforms and hence increase their partners’ willingness to lend.

**Establish new pan-Asian institutions and strengthen existing ones.** Some issues are best addressed at the level of Asia and the Pacific as a whole. While strengthening existing institutions such as
Institutions for Regional Integration

ADB and the Economic and Social Commission for Asia and the Pacific (ESCAP) can help in this process, there is a need for establishing new ones which play important roles as facilitating IRIs. In particular, new pan-regional institutions could include:

- a Pan-Asian Infrastructure Forum (PAIF) to address the increasing needs of regional infrastructure development;
- an Asia-Wide Free Trade Area (Asia-FTA) to facilitate trade and investment integration by consolidating existing bilateral and plurilateral FTAs;
- an Asian Monetary Fund (AMF) to conduct regional macroeconomic surveillance and provide financial assistance in case of crises;
- an Asian Financial Stability Dialogue (AFSD) to address regional financial stability and regulatory issues, while promoting the development of Asia’s financial markets;
- an Asian Legal Advisory Council (ALAC) to improve the predictability of legal obligations by ensuring that international agreements are implemented and interpreted uniformly across the region;
- several regional public goods’ forums (RPGF) to promote regional cooperation in dealing with issues such as natural calamities, climate change, and health concerns; and
- a Council of Asian Economic Cooperation (CAEC), a coordinating body governed at the highest political level, to ensure that all Asian countries are represented and have a voice in regional integration, provide a mechanism for coordinating the various subregions’ initiatives, capture synergies and spillovers between economic and security cooperation, and enable Asian countries to coordinate their positions in global venues and forums more effectively.

Toward an Asian Economic Community

Goals are one thing; strategies for achieving them another. Since Asia’s policy making tends to be pragmatic and cautious, efforts to strengthen its regional architecture should proceed in this mold. At the same time, formulating a proper strategy to strengthen Asia’s IRIs and move toward an Asian economic community requires a strong commitment from political leadership, adequate financial resources, and a knowledge community of scholars, businesspeople, government officials, and other parties with a shared commitment to Asian regionalism.
Theory and experience, in both Asia and other regions, underscores the critical role that can be played by national leaders to advance this agenda. Given the region’s diversity, building Asian regionalism will require collective leadership that achieves an adequate balance of power among the participants. The shared leadership of established, emerging, and middling powers will provide the backbone for building an economic community in Asia.

Proposals for reforming existing or creating new ones must weigh the benefits against costs—not least, the financial expense of staffing an organization and its administering operations. But estimating the costs of creating new institutions designed to serve the long-term vision of forming an Asian economic community is more speculative, as it depends on various factors, including what the organization would be expected to do, and how effective member governments would want it to be. A starting point may be to extrapolate from costs associated with existing IRI s such as Asia-Pacific Economic Cooperation (APEC), ASEAN, and the European Commission (EC)—though these vary widely.

A knowledge community can also provide an impetus for regional integration, serving as mechanisms for communication, socialization, and information sharing.

Building robust institutional architecture to further Asian integration is highly challenging. However, the prize is huge: a more integrated Asia, free of poverty and conflict, prosperous and confident, and well-equipped to shape its destiny—and that of the world—for the better.
Institutions for Regional Integration: Toward an Asian Economic Community

In continuation of the work on Asian economic integration done by the Asian Development Bank (ADB) and the ADB Institute, this book takes stock of existing institutions for regional integration in Asia and the Pacific and discusses the need for institutional innovation and reform in moving toward the creation of an Asian economic community. The study draws its strength and insights from a team of authors including ADB staff, scholars, and advisers to regional policy makers. Consultation workshops to finalize the study involved leading experts in several countries in Asia, Europe, and North America.

www.aric.adb.org/iri

“Regionalism creates a new platform for economic growth and can be a stabilizing factor when shocks arise. It carries the responsibility of proper management, effective communication, and policy coordination. To make regional cooperation effective and enable the region to speak with a more prominent common voice, Asia needs to enhance its institutional capabilities for regional integration.”

— Haruhiko Kuroda, President, Asian Development Bank

About the Asian Development Bank

ADB’s vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries substantially reduce poverty and improve the quality of life of their people. Despite the region’s many successes, it remains home to two-thirds of the world’s poor: 1.8 billion people who live on less than $2 a day, with 903 million struggling on less than $1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

Asian Development Bank
6 ADB Avenue, Mandaluyong City
1550 Metro Manila, Philippines
www.adb.org/publications
Publication Stock No. RPT113047