

ADB Working Paper Series on Regional Economic Integration



ASEAN Economic Integration: Features, Fulfillments, Failures and the Future

Hal Hill and Jayant Menon
No. 69 | December 2010



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For helpful comments on earlier drafts, we are grateful to Max Kreinin, Michael Plummer, and seminar participants at the Australian National University, the Cambodia Development Research Institute, the Centre for Strategic and International Studies (Jakarta), and the Institute for Strategic and International Studies (Kuala Lumpur). Anna Cassandra Melendez provided excellent research assistance. Any remaining errors are our own.

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Asian Development Bank

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Abstract

The 10-member Association of Southeast Asian Nations, ASEAN, is arguably the most durable and successful regional grouping in the developing world. Established in 1967, it has contributed greatly to regional harmony and prosperity. ASEAN is characterized by great internal diversity, generally high economic growth, and a reluctance to establish a strong supranational structure. Beginning in 1976—with its five original members—ASEAN began to move toward economic cooperation and integration, initially with a focus on merchandise trade. In the 1990s, it added focus on services, investment, and labor. And in the past decade—now including all of Southeast Asia—ASEAN broadened cooperation on macroeconomic and financial issues, many of these together with its Northeast Asian neighbors—the “Plus 3” of the People’s Republic of China, Japan, and the Republic of Korea. Members adopted what may appear to be formal preferential trade arrangements. But in practice these are usually multilateralized. ASEAN informally embraces what is sometimes termed “open regionalism.” However, there is little likelihood in the foreseeable future that this will evolve into a deep EU-style economic integration behind a common external trade regime, despite a commitment to forming an ASEAN Economic Community beginning 2015.

Keywords: ASEAN economies, ASEAN economic development, economic integration, regional trade agreements

JEL Classification: F15, F59, O53

1. Introduction

The 10-member Association of Southeast Asian Nations, ASEAN, was established in August 1967. It is arguably the most durable and successful regional association in the developing world. In a region that had been plagued by conflict and divided by a diverse colonial past, ASEAN has first and foremost forged diplomatic cohesion among its population of almost 600 million people. Formed initially by leaders of five member countries,¹ the 1967 Bangkok Declaration was broad and general in its seven objectives. These included, among others

To accelerate the economic growth, social progress and cultural development in the region ... To promote regional peace and stability...
To promote active collaboration and mutual assistance ... in the economic, social, cultural, technical, and administrative spheres.

Subsequently, it has evolved into a close-knit group holding around 700 meetings each year on economic, political, cultural, educational, and security matters. ASEAN has also been able to effectively project itself regionally and internationally through a wide range of initiatives.

Four broad characteristics define ASEAN.

First, it is a region of great diversity, probably more so than any other group in the world. Indeed, its economic, political, cultural, and linguistic diversity is greater than that of the European Union, for example. This diversity was accentuated by colonial experiences, with Brunei Darussalam, Malaysia, Myanmar, and Singapore part of the British empire; Cambodia, the Lao People's Democratic Republic (Lao PDR), and Viet Nam annexed by the French; Indonesia ruled by the Dutch; the Philippines under first Spanish then American rule; while Thailand was never formally colonized.² Political structures are equally diverse, including freewheeling democracies (Cambodia, Indonesia, Philippines), communist states (Lao PDR and Viet Nam), a constitutional democracy with a highly influential monarchy (Thailand), heavily managed democracies with one party in continuous rule since independence (Malaysia and Singapore), a military-dominated authoritarian state (Myanmar), and an all-powerful sultanate (Brunei Darussalam).

ASEAN includes one very wealthy nation (Singapore) alongside some of the world's poorest. The per capita income of the richest is about 80 times that of the (imperfectly measured) poorest. It includes the world's two largest archipelagic states (Indonesia and the Philippines) together with Singapore's city-state, and the tiny oil sultanate of Brunei Darussalam. It includes the world's fourth most populous nation (Indonesia), three states with populations between 60 and 90 million people (Philippines, Thailand, and Viet Nam), while Singapore and Lao PDR have less than five million people; Brunei Darussalam less than half a million.

¹ Indonesia, Malaysia, Philippines, Singapore, and Thailand.

² A word on country names is relevant here: Myanmar is also referred to as Burma, especially by those who do not recognize the legitimacy of the current regime, while Laos is officially known as the Lao PDR (Peoples' Democratic Republic), and Brunei is short for Brunei Darussalam.

Second, most of the countries have achieved rapid economic development for most of the past 25 years, and longer in some cases. Four of them – Indonesia, Malaysia, Singapore, and Thailand – were classified by the World Bank (1993) as “miracle” economies. Since the late 1980s, Cambodia, Lao PDR, and Viet Nam have successfully engineered a transition from planned to market economies with significantly increased growth rates and sharp reductions in poverty. The region’s economic dynamism and steadily expanding cooperation created a virtuous circle, with increased ASEAN’s regional harmony providing an enabling and more conducive business environment. Nevertheless, ASEAN membership has been no guarantee of economic success. Myanmar and the Philippines, for example, were touted in early development economics literature as being prime for rapid economic development, yet they have underperformed, the former disastrously so.

Third, ASEAN diplomacy and cooperation have been characterized by caution, pragmatism, and consensus-based decision-making. The so-called “ASEAN Way” is enshrined in noninterference in others internal affairs and can be characterized by lowest-common-denominator decision-making. ASEAN leaders have deliberately avoided creating a strong supranational regional institution, and the ASEAN Secretariat has been deliberately underpowered, serving more as a diplomatic facilitator and conference organizer rather than a strong EU-type agency. These characteristics are both strengths and weaknesses: they explain ASEAN’s durability, but also limit effectiveness and capacity for strong and decisive action.

Fourth—related to the third observation—ASEAN has never been, and probably will never be, an EU type organization, nor even a NAFTA-type economic bloc. That is, in the foreseeable future it is unlikely to adopt a common external trade regime, with completely free commerce among member states.. In fact, although it appears in a formal sense to be a quasi-preferential trading bloc, in practice, most of trade liberalization have been multilateralized as part of unilateral domestic reforms individually. Moreover, ASEAN is even less likely to develop formal mechanisms for macroeconomic policy coordination, leading for example to a common currency or central bank. ASEAN’s key challenge has from birth been to define a role for itself, especially since Asia’s two giants, the People’s Republic of China (PRC) and India, are now growing faster than ASEAN in aggregate. Will it, as some pundits suggest, be forever at the crossroads, institutionally unable to establish a stronger variant of economic cooperation, and therefore confined to a loose association, a forum for leaders only to discuss issues of regional interest?

This paper introduces ASEAN, and traces its evolution—focussing on programs for economic integration. It also critically evaluates past performance and, based on this, examines prospects for the future.

Section 2 provides an overview of the 10 ASEAN economies, and the development of the group as an institution. Section 3 examines ASEAN economic cooperation and integration with reference to merchandise trade, which was the principal focus of initiatives for its first quarter century. Section 4 then investigates a range of “trade plus” measures, including efforts to develop a broader range of closer economic relations both within and beyond the region—against the backdrop of ASEAN’s expanded membership, the 1997/98 Asian financial crisis, the rise of the PRC, and the rapidly evolving regional commercial architecture. Concluding observations are presented in section 5.

2. ASEAN and ASEAN Economic Development

2.1. The Evolution of ASEAN

There are four more or less distinct phases in the evolution of ASEAN (Table 1). The *first phase* commenced with its establishment in 1967, in a highly uncertain regional and global environment over-shadowed by conflict. This was at the height of the cold war, conflict in Viet Nam, Lao PDR, and Cambodia was at its peak, and the PRC was in the throes of its cultural revolution. Indonesia had only recently renounced its intention to “crush” Malaysia, Malaysia and Singapore had separated after a brief union, Malaysia and the Philippines were in dispute over Sabah, and there were (or had been recently) significant leftist insurgencies in all but Singapore. Thailand was widely regarded in the West as a likely next “domino” to fall to the communist advance. Earlier attempts at establishing a regional association, such as the Association of Southeast Asia (ASA), and a possible three-nation “Malay” group, Maphilindo, had not progressed. A major facilitating factor in the 1967 meeting and declaration was regime change in Indonesia in early 1966, with the Suharto administration signaling its intention to rejoin the international community, to focus on economic development, and to seek better relations with its neighbors. Then, as now, ASEAN was only able to progress as fast as its dominant power.

Table 1: ASEAN - Major Dates

Date	Event
8 August 1967	Bangkok Declaration establishes ASEAN.
23-24 February 1976	Major Bali Summit.
8 January 1984	Brunei Darussalam joins.
28 January 1992	AFTA/CEPT launched.
28 July 1995	Viet Nam joins.
23 July 1997	Lao PDR and Myanmar join.
15 December 1997	Vision 2020 to accelerate economic integration.
30 April 1999	Cambodia joins.
6-8 May 2000	ASEAN+3 announce Chiang Mai Initiative.
7 October 2003	ASEAN Economic Community launched.
22 February 2009	Expanded CMI launched.

Source: ASEAN Website, www.aseansec.org

The vision of the leaders therefore focused primarily on establishing regional harmony. While all were strongly anti-communist in outlook, they explicitly emphasized socio-economic cooperation and development rather than defense and security. In 1969 the ASEAN Foreign Ministers commissioned a study on ASEAN economic cooperation to be conducted by the United Nations. The resulting report, known as the Kansu Report (after its leader, Professor G. Kansu), was completed in 1972. But it was not widely circulated, and was not formally published until 1974 (as United Nations, 1974). Its recommendations on economic cooperation reflected both popular thinking at the time as well as the inclination of ASEAN member countries. Specifically, it proposed trade liberalization through selective, or product-by-product

tariff negotiations, package deal arrangements for large industrial projects, and financial cooperation.

Meanwhile, various cooperation activities had begun, including reports by various committees covering commerce and industry, agriculture, tourism, transport, and telecommunications. As early as 1971, for example, the commerce and industry committee was exploring the possibility of trade fairs and cooperation, trade liberalization, harmonization of trade statistics, and industrial complementation projects. The spirit of the Kansu report was broadly accepted, including in principle the notions of joint industrial projects and of reciprocity among relevant parties.

The *second phase* began with the Bali Summit of the five leaders in February 1976. This marked the beginning of a formal set of regional cooperation measures. These comprised the ASEAN Preferential Trading Agreement (APTA), the ASEAN Industrial Projects (AIPs), the ASEAN Industrial Complementation (AIC), and the ASEAN Industrial Joint Ventures (AIJVs). APTA, the most significant of the four, represented the first attempt to promote intra-ASEAN trade through institutional integration and regional trade preferences. The AIPs, on the other hand, were designed to establish in each member country a large-scale, inter-governmental project. The AIC and the AIJVs were aimed at promoting specialization in complementary products and to facilitate resource pooling.

These initiatives were broadly consistent with the Kansu and other reports. They reflected the desire on the part of leaders to “put some flesh on the bones” of regional cooperation, at least in a minimal, non-threatening sense. They were generally similar to other regional initiatives being promoted in the developing world—notably in Latin America, the Caribbean, and East Africa. A major trigger was the reunification of Viet Nam in April 1975 and communist take-overs in Cambodia and Lao PDR. ASEAN meanwhile became a more active organization in international affairs. It began to caucus as a group, for example in the United Nations and on issues of common concern, such as market access for its labor-intensive manufactures and tropical cash crops. Dialogue-partner relationships with a wide array of countries and regions were established, and some of these formed the basis for subsequent regional architecture initiatives. ASEAN also began to be active diplomatically, especially its attempt to isolate Viet Nam for its role in the removal of the murderous Khmer Rouge regime in Cambodia.

However, none of the four economic cooperation programs had any significant impact on regional economic relations (Imada and Naya, 1992). Indeed, they were explicitly designed to have minimal effect. In spite of the early enthusiasm, the APTA had little impact on intra-regional trade. The tariff cuts were not implemented on an across-the-board basis but rather on product-by-product basis. Hence the commodity coverage was narrow, the tariff cuts were too small to have any discernible effect on trade,³ and implementation was half-hearted.⁴ Moreover, APTA failed to deal with

³ Until 1981, most of the items on the list had tariff reductions of just 10%. In that year, the size of the tariff cuts for products already listed was increased to 20%–25%. But this was still regarded as too low by the business community, which argued that cuts of 30%–50% would be needed to have a perceptible effect (Saw, 1982). More generally, as Ariff (1991) points out, a major problem with APTA was the failure to consult and involve the business community.

⁴ The first list, presented to the Fifth ASEAN Economic Ministers (AEM) meeting in Singapore in July 1977, contained only 71 products (15 from Indonesia, 14 from each of the other four) for the 10%

non-tariff barriers (NTBs), which were generally a more serious impediment to trade than tariffs. The AIP, AIC and AIJVs also had limited success. In the case of the AIJVs, for example, the Philippines and Thailand were in dispute over wanting to produce the same automotive parts (Ajanant, 1997). More generally, the failure of these initiatives was symptomatic of the members' unwillingness and unpreparedness to pursue either trade liberalization or regional integration at the time. Notions of infant industry were still popular.

There was little further progress during the 1980s. Brunei Darussalam's accession in 1984 occurred upon independence. During 1984–87, the Philippines was engulfed in economic and political crisis, and effectively disengaged from ASEAN. The collapse in commodity prices in the mid-1980s pushed both Indonesia and Malaysia—and by extension Singapore—into recession, in turn prompting swift and effective reforms, but lessening interest in the broader regional agenda.

The *third phase* started in 1992 with another leaders' Summit at which the ASEAN Free Trade Area (AFTA), was announced. This marked a clear break with the past. The emphasis was on stronger economic cooperation: for the first time, "free trade" was the regional objective, there was a clear timetable for implementation, and a "negative list" approach was adopted, in that all goods trade was to be included within AFTA unless explicitly excluded. The six leaders agreed to reduce the common effective preferential tariff (CEPT) rates to 0%–5% by 2008, with an interim target of 20% by 1998–2000. This deadline was subsequently advanced to 2005 at the Fifth ASEAN Summit in 1995, and later to 2003. The leaders also agreed that each country would have at least 85% of its tariff lines in the "Inclusion List" by 2000, and 90% by 2001.

Here, too, a range of regional and external drivers was at work. First, there was general recognition that the 1976 measures were cosmetic and ineffective. Second, there was increased self-confidence in the region. Indonesia in particular had weathered the mid-1980s debt crisis effectively, and introduced sweeping policy reforms. Third, substantive regional associations were coming into vogue elsewhere, especially with the signing in 1991 of the EU Maastricht Accord and the imminent extension of the North America Free Trade Agreement (NAFTA) to Mexico, a middle-income competitor in the crucial US export market. Fourth, the PRC was now growing very fast, and attracting large foreign direct investment (FDI) inflows. ASEAN leaders felt they had to present the region as a competitive single-market alternative to the PRC. Fifth, other changes in the regional and global commercial architecture were gathering momentum and threatened to overshadow slow-moving ASEAN. Notable here were the establishment of the Asia Pacific Economic Cooperation (APEC) process in 1989 and the promulgation of the Uruguay trade round in 1995.

ASEAN leaders built on this renewed vigor by seeking to extend its geographic spread and commercial depth. By the early 1990s, Viet Nam had clearly signaled its intention to adopt market-oriented reforms and to look outwards. The earlier

reduction in tariffs. These products constituted just 2.5% of intra-ASEAN trade in 1975 (Saw, 1982). Although the number of items grew quickly, the scheme still only covered 5% of intra-ASEAN trade in 1986 (Edwards and Wong, 1996). The right of members to exclude "sensitive" items from the list was so widely exploited that only minimally traded goods were included. Moreover, some of the "concessions" were memorable, including snow ploughs and specially created but fictitious trade categories.

antipathy toward the communist regime gave way to pragmatism, fuelled in both cases by a common apprehension toward the PRC. Thus Viet Nam joined in 1995, followed by Lao PDR and (with a delay owing to its domestic political instability) Cambodia. Despite some reservations, ASEAN also invited Myanmar to join, partly for geopolitical reasons and partly in an effort to engage one of the world's most isolated states economically and politically.

ASEAN has played a constructive role in its commercial engagement with the three reforming states in mainland Southeast Asia. ASEAN membership has reinforced their outward orientation, built confidence in their reform momentum, and enabled them to learn from their more advanced neighbors. The four mainland states negotiated phased-in arrangements for accession to AFTA and other agreements. Thus Viet Nam was given until 2006 to bring down tariffs on products in its Inclusion List to no more than 5%. For Lao PDR and Myanmar it was 2008, while owing to its delayed accession Cambodia had until 2010. As of 2009, almost 80% of the products of the new member countries had been moved into their respective Inclusion Lists, and of these about two-thirds have tariffs within the 0%–5% range. Thus the implementation of the AFTA accords for this group is on track.

By the mid-1990s, and consistent with the global trend in preferential trade agreements (PTAs), ASEAN began to cautiously develop arrangements for trade in services, investment, harmonization of customs, and in other fields. The ASEAN Framework Agreement on Services (AFAS) was signed 15 December 1995 at the Fifth ASEAN Summit Meeting in Bangkok. This was an ambitious agreement with two main objectives: to substantially eliminate all restrictions (both discriminatory and market access measures) to trade in services among member countries, and to liberalize trade in services by expanding the depth and scope of liberalization beyond those undertaken by member states under the General Agreement on Trade in Services (GATS).

Given the importance of FDI in the region, ASEAN was one of the first regional groups in the “South” to adopt formal instruments to try to promote and protect cross-border investment among its members. A number of agreements were signed, the most significant of which was the Framework Agreement on the ASEAN Investment Area (AIA) in October 1998, which was subsequently expanded and consolidated into the ASEAN Comprehensive Investment Agreement (ACIA) in February 2009.

However, just as the original leaders' dream of “one Southeast Asia” was being realized, in mid-1997 the Asian financial crisis suddenly erupted. What transpired in its aftermath is now well known. Notwithstanding its ferocity, the direct crisis impact was surprisingly short-lived. Most crisis economies experienced a V-shaped recovery, although they have generally returned to somewhat lower growth trajectories, putting aside the 2008-09 global financial crisis (GFC).. For ASEAN as an institution, the crisis had two principal effects. First, the region as a whole lost some of its commercial attractiveness, especially as the PRC and India were largely unaffected by the crisis. Moreover, ASEAN was seen by many as an ineffective and feeble institution, unable to respond decisively at a time of crisis. This was despite attempts to be responsive, such as decisions taken at the ASEAN summit in Ha Noi in 1998 to (i) accelerate AFTA implementation; and (ii) expand ASEAN cooperation to include PRC, Japan, and Korea (ASEAN+3). In addition to its crisis reaction, it was unable to play any role in two other major regional flashpoints of that period, the

1998/99 Timor crisis and the forest fires and ensuing regional haze pollution of 1997/98.⁵

Second, the crisis led to a general rethink about the future of economic cooperation, and the need for some sort of coordinated macroeconomic response capacity to avert such future events. This led to the current *fourth phase* in the evolution of ASEAN, dominated by two key features. These are the return to growth (despite the immediate effects of the GFC), and the struggle to define its rationale and identity against the backdrop of a fast-changing regional and global environment, including a plethora of initiatives affecting commercial policy architecture.

Four features have dominated the commercial policy architecture in the first decade of the 21st century, and all have posed new and difficult challenges for ASEAN. These developments, and their implications for ASEAN, are discussed in more detail in section 4 below.

The first is the spread of PTAs. Singapore in particular, frustrated with slow pace of ASEAN, began to break ranks and embark on a bold strategy of PTAs. Although causing strain within the group, this had momentum or a domino effect with other ASEAN countries, especially Thailand, feeling compelled to follow.

Second, there has been recognition that ASEAN is too small to address some of the broader, post-crisis macroeconomic coordination issues. For example, ASEAN is too small to seriously contemplate coordinated macroeconomic policy, such as a common exchange rate regime. As for emergency or crisis prevention measures—including currency swaps and fiscal standby agreements—the huge international reserves accumulated in North Asia dictate that these economies will be the major players in any regional and international agreements on emergency finance.

Third, ASEAN has now largely completed the “easy phase” of intra-regional trade liberalization. As of 2009, zero tariffs applied to 64% of products in the Inclusion List of the East Asia Summit process, or ASEAN-6 (ASEAN+3 plus India, Australia, and New Zealand). The average tariff for ASEAN-6 under the CEPT scheme is down to 1.5%, from 12.8% when tariff cutting began in 1993.

What remains are the politically more sensitive areas, heavy industry and food crops in particular. An unstated tenet of ASEAN trade liberalization is that the concessions would be “multilateralized” as long as it was politically acceptable domestically for the signatories to do so. But for more contentious liberalization, progress has been slower and exemptions have proliferated. For example, Indonesia periodically bans rice imports. As food prices rose sharply in 2008, there was a free-for-all in the regional rice markets, with talk of a “Mekong rice cartel” among exporters, and the then president of the Philippines (now the world’s largest rice importer) announcing that her country would buy rice “at any price”. Each country has sought to protect its steel industry. Malaysia has been reluctant to liberalize its auto trade barriers for fear of competition from Thailand, the regional leader in the industry. In addition to these

⁵ Writing at this time, the late Hadi Soesastro (1999, 158–9), one of the leading thinkers in ASEAN on regional cooperation, observed: “The public has been largely disappointed with ASEAN. Its perception is that of a helpless ASEAN, an ASEAN that cannot move decisively, an ASEAN that is trapped under its organizational and bureaucratic weight, and an ASEAN that fails to respond to real, current problems and challenges.”

barriers at the border, a further obstacle to the notion of “ASEAN as a single market” has been the proliferation of sub-national barriers, particularly in Indonesia, where many provincial and *kabupaten* (county) governments have introduced illegal levies on cross-border transport (McCulloch, 2009).⁶

Fourth, the rise of fragmentation trade called into question the viability of all forms of PTA’s that do not multilateralize concessions. East Asia has been the dominant player in this fast-growing segment of international trade, which involves the physical relocation of stages of the production process that can be transferred to lower-cost sites.⁷ Parts and components in the electronics and automotive industries have been the major segment of this trade, although it is now spreading rapidly to (poorly measured) services trade through Build-Operate-Transfer (BOT) facilities. Within East Asia, ASEAN countries stand out for their heavy dependence on production fragmentation trade. In 2005–06, for example, parts and components accounted for 44% of ASEAN manufactured exports, up from 29% in 1992–93. The shares are higher still for some countries: 64% for the Philippines in 2005–06 (up from 24% in 1992–93), 53% in Singapore (from 32%) and 51% in Malaysia (from 37%). Over this period, ASEAN’s share of world trade in parts and components also rose significantly, from 7.8% to 10.9% (Athukorala and Menon, 2009).

Clearly, the management of global production facilities, sourcing inputs to the final product from many countries, is fundamentally incompatible with PTAs: some countries may be signatories to various PTAs, and these agreements are unlikely to be mutually compatible. The response of governments and multinational enterprises (MNEs) in these industries has been to locate such activities in free trade zones, thus placing their operations on a free trade footing. More recently, governments have come to recognize the impracticality of any form of trade barriers—unilateral or preferential—in this segment, through the establishment of the International Technology Agreement (Bhagwati, 2008), to which the major Southeast Asian electronics exporters are signatories.

2.2. The ASEAN Economies: An Overview

Table 2 summarizes the key socio-economic features of ASEAN’s 10 member countries, which are diverse in practically every respect. The richest country, Singapore, has a per capita income of about 50 times the poorest, Cambodia.⁸ In purchase power parity (PPP) terms, the range is narrower, but is still more than 25:1, larger than for any other regional association in the world. Of course, the range is exaggerated by Singapore, whose per capita income is 5 and 3.5 times that of third ranked Malaysia. But even excluding Singapore (and Brunei Darussalam), the range

⁶ In addition to these formal and informal trade barriers, studies of the region’s logistics have drawn attention to the high trade costs in some of the lower income ASEAN economies, resulting from poor infrastructure, limited competition, and regulatory impediments in the customs agencies. See Brooks and Hummels (2009) and Shepherd and Wilson (2009).

⁷ See Athukorala (2006), Athukorala and Menon (2009), and Kimura (2006) for detailed examinations of this trade.

⁸ Data are not always available for Brunei Darussalam and Myanmar, the former because it is so small as to not always be included in comparative international statistics, and the latter because its statistical system is considered unreliable. In the rankings, Brunei Darussalam’s per capita income can safely be assumed to be similar to Singapore’s, and Myanmar’s probably a little below that of Cambodia. So assertions about the range of incomes are unaffected by their exclusion.

Table 2: ASEAN - Key Socio-Economic Indicators

Country	GDP, 2008		GDP per capita, 2008		Population, 2008		Percent of GDP (value added), 2007				Human Development Index, 2008		Poverty headcount ratio at \$2/day, PPP (% population)
	Current \$ bil	PPP \$ bil	Current \$	PPP \$	Total (mil)	Density (per sqm)	Agri	Ind	Man	Ser	Value	Rank	
Brunei Darussalam ^{/1}	14.6	19.7	37,053	50,199	0.4	75	1	71	10	28	0.9	30	...
Cambodia	9.6	28.0	651	1,905	14.7	83	32	27	19	41	0.6	131	68 ^{/2}
Indonesia	514.4	907.3	2,254	3,975	228.3	126	14	47	27	39	0.7	107	54 ^{/3}
Lao PDR	5.2	13.2	837	2,134	6.2	27	40	31	20	29	0.6	130	77 ^{/4}
Malaysia	194.9	383.7	7,221	14,215	27.0	82	10	48	28	42	0.8	63	8 ^{/2}
Myanmar ^{/1}	26.2	68.0	446	1,156	58.8	75	0.6	132	..
Philippines	166.9	317.1	1,847	3,510	90.3	303	14	32	22	54	0.8	90	45 ^{/5}
Singapore	181.9	238.5	37,597	49,284	4.8	7,024	0	31	25	69	0.9	25	..
Thailand	260.7	519.1	3,869	7,703	67.4	132	12	46	36	43	0.8	78	12 ^{/2}
Viet Nam	90.7	240.1	1,052	2,785	86.2	278	20	42	21	38	0.7	105	48 ^{/5}

Notes:

bil = billion, mil = million, Agri = agriculture, Ind = industry, Man = manufacturing, and Ser = services.

^{/1} GDP, GDP per capita and total population data are from the IMF World Economic Outlook Database, October 2009

^{/2} 2004

^{/3} 2005

^{/4} 2002

^{/5} 2006

Source: World Bank, 2009 World Development Indicators; IMF, World Economic Outlook Database, October 2009; UN, 2009 Human Development Indicators.

is very large, about 11-fold. In terms of economic size, however, Indonesia is the dominant economy—with over 35% of ASEAN GDP—almost double that of second-ranked Thailand. There follows three intermediate ranked economies, Malaysia Singapore, and the Philippines (with relative sizes depending on which GDP series is used), followed by the four small mainland states, of which Viet Nam is by far the largest. Cambodia and Lao PDR are still officially regarded as “least developed states”, reflecting their poverty and (along with Viet Nam) the historical legacy of deep conflict.

The demographics of the 10 countries also vary considerably. Here also, Indonesia is by far the largest, with 39% of ASEAN’s population, followed by three mid-sized populations, in order the Philippines, Viet Nam, and Thailand. Myanmar’s 50 million is a very approximate estimate. Malaysia is approaching 30 million people, while the remaining four states are considerably smaller. Population densities provide a clue to comparative advantage in land-intensive activities. Apart from the special case of Singapore, the Philippines and Viet Nam have the highest population densities, with the three poor mainland states much less heavily settled. Indonesia’s average density of course obscures its huge demographic imbalance, with the main island of Java containing regions ranking among the highest population densities in the world.

There are also large differences in economic structure, reflecting both levels of development and relative resource endowments. Cambodia and Lao PDR (and almost certainly Myanmar) are still heavily agrarian economies, with one-third or more of GDP derived from agriculture, while the richer economies have largely shifted out of agriculture. Several of the economies have experienced rapid industrialization over the recent decades, with industry accounting for at least one-quarter of GDP in Indonesia, Malaysia, Singapore, and Thailand. Services as expected dominate the Singapore economy. For a complex set of reasons, they also account for more than half of the still low-income Philippine economy.

Welfare indicators correlate closely with per capita income. Thus human development indicator (HDI) indexes for Singapore and Brunei Darussalam are well above that of the others (although internationally their HDI rankings are well below their per capita income rankings), with Malaysia and Thailand a good deal higher than the other six economies. Those for the three poorest mainland states are among the lowest in the world. Poverty incidence, as measured by the percentage of the population living below \$2/day, is still very high in these three (again with accurate estimates for Myanmar unavailable), and still over 40% in Indonesia, the Philippines, and Viet Nam. Poverty incidence has however fallen rapidly in all cases of sustained rapid growth in the region.

These socio-economic indicators highlight several distinctive features of the ASEAN group, and they have important implications for how it operates. ASEAN is unlike any other regional group with respect to its balance of economic power. Singapore—by far the richest economy—has less than 1% of the population, and it is ethnically distinct. By contrast, the largest economy, Indonesia, is barely in the middle-income developing group, and its per capita GDP is below the ASEAN average. This contrasts with NAFTA, dominated by one rich economy, and with the European Union, with its four major economies together with a diverse group of member countries on average considerably richer than that of ASEAN. ASEAN also differs from SARC, SADC, and Mercosur in this respect, with India, South Africa, and Brazil

respectively the dominant economies (though not the richest in the first and third case).

Moreover, owing to its unique historical, political, economic, and cultural characteristics, Singapore is unable to provide the leadership that might otherwise have been expected of a country that is the richest and has historically been the most economically dynamic, except by example, in the high quality of economic policy, legal and other institutions, and its superb infrastructure. Indeed, leading security analysts sometimes characterize its principal challenge as “dealing with vulnerability”. Although referring primarily to defense and foreign policies, the sentiment also has broader implications for the country’s policies, ranging from large defense expenditures to an extraordinarily high savings rates and huge foreign exchange reserves.⁹

There is also greater diversity in economic structure—and hence scope for intra-regional specialization and commerce—than is commonly recognized. There are net food exporters (most of the mainland states) and importers (most of archipelagic Southeast Asia); resource-poor and resource-rich nations (the latter Brunei Darussalam and Malaysia, especially on a per capita basis); net labor importers (the four higher income states) and net labor exporters; while Singapore and to a lesser extent Malaysia have advanced research and development (R&D) capacity and higher education resources, compared with their neighbors’ much weaker human capital bases.

ASEAN economies are diverse not only with respect to levels of development but also institutional and commercial policy environments. Three of the economies, Singapore, Malaysia, and Thailand, were classified by Sachs-Warner as “always open”. Singapore has never deviated from this open borders approach, apart from a very mild and brief period of import substitution as part of its short-lived union with Malaysia. By contrast, the four poorer economies of mainland Southeast Asia have been largely closed to the international economy, in the case of Cambodia, Lao PDR, and Viet Nam until they began their historic and increasingly decisive reorientation from planned to market economies. Indonesia and the Philippines have for extended periods erected high barriers to international trade and investment, but since the mid-1980s have become increasingly open.

Various estimates of openness and the summary indicators of commercial policy regimes in the 10 countries presented in Table 3 confirm these generalizations. With respect to trade/GDP ratios, Singapore is one of the most open economies in the world, with Malaysia, Viet Nam, Thailand, and Cambodia also having figures above 100%. The tariff data show a broadly similar picture, with weighted averages below 10% for most of the economies, and only marginally higher for Cambodia and Viet Nam. The higher figures for the latter two economies in part illustrate their success in converting opaque trade barriers into transparent tariffs. Smuggling remains extensive in those economies with remaining trade barriers, long porous borders and weak administrative capacity. Myanmar, Lao PDR, and Indonesia stand out in this respect. The dispersions in tariffs across sectors are generally declining, with a

⁹ These features also have implications for Singapore’s role within ASEAN. As a senior official once caustically noted in private, the other ASEAN members not infrequently tell it to “provide the funds and then shut up”.

switch from above- to below-average protection for manufactures observable in several countries. Like tariffs, non-tariff barriers (NTBs) are generally declining, but they remain significant in some cases for the usual political economy reasons. Highly protected sectors are often those dominated by state-owned enterprises in the former command economies and in Indonesia.¹⁰

Table 3: ASEAN Trade and Commercial Policy Regimes

Country	Trade/GDP, 2007 (%)	FDI Stock/GDP, 2007 (%) ^{1/1}	Average Tariff, 2006 (wtd, %)	Index of Economic Freedom ^{1/2} Rank	Regulatory Quality ^{1/3} Rank	Ease of Doing Business ^{1/4} Rank
Brunei Darussalam	95	82	na (v low)	..	75.8	14
Cambodia	138	49	10.8	106	34.3	22
Indonesia	55	14	4.3	131	45.4	19
Lao PDR	87	28	9.3	150	9.7	24
Malaysia	200	43	3.4	58	60.4	4
Myanmar	..	29	3.9	176	1	..
Philippines	85	13	3.2	104	51.7	21
Singapore	429	160	0	2	99.5	1
Thailand	144	35	4.7	67	59.9	3
Viet Nam	167	60	13.3	145	32.4	13

Notes:

na = not available

^{1/1} FDI data are estimates for 2007.

^{1/2} Measures ten components of economic freedom, assigning a grade in each using a scale from 0 to 100, where 100 represents the maximum freedom. The ten component scores are then averaged to give an overall economic freedom score for each country.

^{1/3} One of the six dimensions of governance captured by the World Bank's *Worldwide Governance Indicators*. Reflects the ability of the government to provide sound policies and regulations that enable and promote private sector development.

^{1/4} This index averages the country's percentile rankings on 10 topics, made up of a variety of indicators, giving equal weight to each topic. A high ranking on the index means the regulatory environment is conducive to the operation of business.

Source: World Bank, 2009 *World Development Indicators*; UNCTAD, 2009 *Foreign Direct Investment Database*; The Heritage Foundation and Wall Street Journal, 2009 *Index of Economic Freedom*; World Bank, 2009 *Worldwide Governance Indicators*; World Bank, 2009 *Doing Business*.

Employing the stock of FDI to GDP as a crude measure of openness, Singapore has one of the highest ratios in the world, with very high figures (over 40%) for Brunei Darussalam, Cambodia, Malaysia, and Viet Nam. Of course, these indicators of openness do not necessarily imply the existence of secure, transparent and low-corruption business environments. Subjective, perceptions-based indicators, for all their limitations, portray a somewhat different story. For illustration, we also include in Table 3 three widely used comparative indicators: the index of economic freedom,

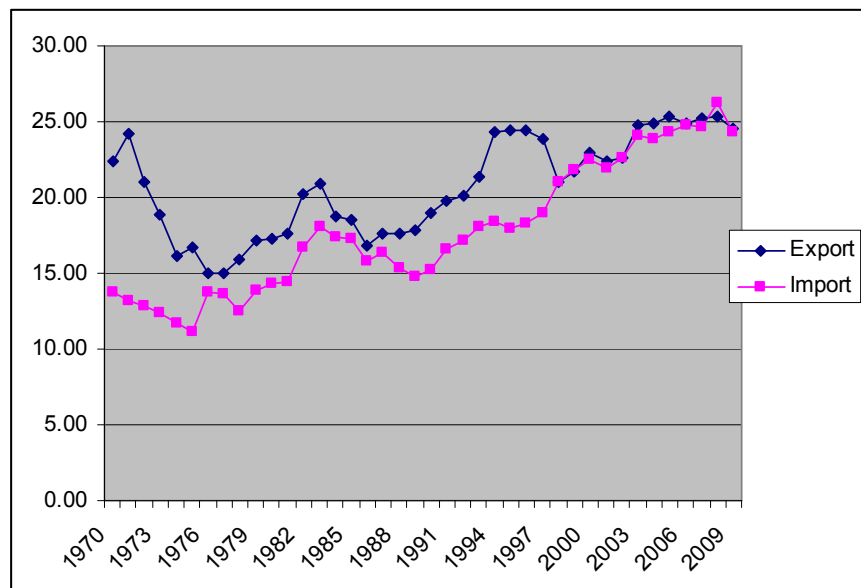
¹⁰ Various trade policy country studies illuminate these NTBs in more detail and examine the trade reform agenda in the respective countries. As illustrations, see for example Athukorala (2006a) on Viet Nam, Bird et al (2008) on Indonesia, and Fane (2006) on Lao PDR. See also the ASEAN Secretariat website for detailed listings of NTBs by country, at www.aseansec.org/16355.htm.

regulatory quality as measured by the World Bank's *Governance Indicators*, and the Bank's *Doing Business* series. On these indicators, the rankings generally correlate quite closely with per capita income. Singapore stands far apart from its neighbors, with rankings at or very close to the top in all three series. Brunei Darussalam follows, with Malaysia and then Thailand some way further behind. Although reforming quickly, the former command economies are still regarded as having uncertain business climates, weak property rights, high-levels of corruption, and in some cases all three. However, in aggregate they do not rank far behind Indonesia and the Philippines, illustrating in turn the slower pace of reform in the latter two. Whereas 15 years ago the original ASEAN-5 group was well advanced on the transition economies, the distinction is now increasingly blurred.

3. “Old Issues”: Merchandise Trade

Two features dominate ASEAN trade. First, ASEAN economies trade predominantly with the rest of the world. That is, extra-regional trade is much larger than intra-regional trade. Since 1970, the latter has generally constituted between 15% and 30% of total ASEAN trade (Figure 1). These seemingly low shares of intra-ASEAN trade have attracted a lot of critical comment, and some have used it to question ASEAN's viability as a regional group. An important point to bear in mind in interpreting these shares is the fact that the ASEAN economies only account for a small share of global trade flows. When adjusted for this scale factor—through the computation of trade intensity measures for instance—the picture that emerges is quite different. For 2006, for example, all intra-ASEAN flows record an index greater than unity, and many are in double-digits and range to a maximum of 53.

There is also a general upward trend in the intra-ASEAN trade shares, reflecting the rising importance of the group in world trade. Earlier, commodities dominated this trade, with Singapore the entrepot for resource-rich Indonesia and Malaysia. This in turn explained the volatility in shares. While still important, intra-regional trade is now considerably more broad-based, with manufactures playing a larger role, increasingly as Singapore-centered global production networks. Note that these statistics refer only to merchandise trade and do not include the fast-growing but poorly measured services trade. It is also important to contrast the much lower intra-ASEAN share with that of the EU figure of around 70%. Since, as will be argued below, most AFTA trade concessions are multilateralized, the observed increase in intra-regional trade shares must be explained by complementarities and market-driven factors rather than deliberate policy measures.

Figure 1: Intra-ASEAN Exports and Imports as a Percent of Total ASEAN Trade

Source: UNCTAD, 2010. *Handbook of Statistics Online*. Data for 2009 from the ASEAN Secretariat.

Second, Singapore dominates intra-ASEAN trade flows, as shown in Table 4.11 The largest single trade flow is between Singapore and Malaysia, as it always has been historically. Singapore's trade with Indonesia and Thailand is also very large. The largest non-Singapore trade flows involve the region's second most open economy, Malaysia—with the two neighbors with which it shares a land boundary, Indonesia and Thailand. The matrix also shows the small scale of official trade of the poorer mainland states, although Viet Nam is rising fast. The countries also differ with respect to the importance of ASEAN within their total trade. For both Singapore and Malaysia, ASEAN markets constitute more than one-quarter of total exports. The share is much lower for Indonesia, where natural resource exports to extra-regional markets are important, and for the Philippines, whose commercial patterns have always been the least ASEAN-centered of the five original member countries.

¹¹ A word of caution is necessary in interpreting these trade shares. While aggregate trade flows are reasonably accurate, as they can be verified from major OECD trading partner statistics, some intra-ASEAN trade flows are at best approximate, owing to widespread physical and technical smuggling. For many years, Singapore has not released its trade statistics with Indonesia, for fear that any discrepancy with the Indonesian statistics may trigger accusations that the island state is complicit in smuggling. Smuggling from Myanmar is known to be extensive, as it was in the communist states of Cambodia, Lao PDR, and Viet Nam until their major trade liberalizations.

**Table 4: Major Intra-ASEAN Trade Flows in 2008
(% of Total Intra-ASEAN Trade)**

ASEAN Country	Partner					
	Indonesia	Malaysia	Philippines	Singapore	Thailand	Viet Nam
Indonesia	0	2.6	0.8	5.1	1.5	0.7
Malaysia	2.5	0	1.2	11.7	3.8	1.0
Philippines	0.2	0.8	0	1.0	0.6	neg
Singapore	14.2	16.3	2.9	0	5.2	3.5
Thailand	2.4	3.9	1.3	3.9	0	2.0
Viet Nam	neg	0.8	0.7	1.1	0.5	0

Notes: top 10 flows in bold; neg = very small, <0.5%.

Source: IMF. 2010. Direction of Trade Statistics.

Two important implications for the governance of regional economic architecture flow from this analysis. First, it does not make sense for ASEAN to contemplate the formation of a customs union, since the major trade is outside the region. That is, the costs of trade diversion would almost certainly exceed the benefits of trade creation. Second, Singapore's dominance of intra-ASEAN trade flows, and the country's non-negotiable commitment to open borders, means that any attempt to set a common external trade regime at anything other than that defined by Singapore is not feasible, since the latter would be a veto player. In other words, a common external ASEAN trade regime would have to be at Singapore levels. This does not necessarily preclude the adoption of free trade within ASEAN alongside differing trade policies for each state. Such an arrangement would imply a two-tier trade policy for all but Singapore, which is technically feasible but would obviously be administratively cumbersome and subject to widespread corruption. In any case, the fact that less than 10% of intra-ASEAN trade avails of AFTA concessions suggests that this approach is virtually irrelevant. The margins of preference between the AFTA and most favored nation (MFN) rates are already very low, and the administrative procedures render the AFTA option unattractive. We return to this issue below.

4. "New Issues": Services, FDI and Regional Economic Architecture

ASEAN—AFTA and related initiatives in particular—has had a deeper regional economic integration objective since the early 1990s. What light does its experience shed on the broader question of whether PTAs can accelerate economic integration? The regional trade liberalization experience was discussed above. In this section we address this question with reference to a range of issues beyond the first-round efforts that focused on merchandise trade.

4.1. Deepening Integration: Services Trade, FDI, Labor

Following AFTA, ASEAN has also signed agreements relating to trade in services, intra-regional investment and labor movements. ASEAN economies are increasingly integrated in all these respects, but they are all market-driven, with little if any formal implementation of regional initiatives.

Under the 1995 ASEAN Framework Agreement on Services (AFAS), negotiations over the liberalization of services have focused on five sectors, namely financial services, transport, telecommunications, tourism, and professional business services. Progress has however been limited, owing to the lack of political commitment to open up the services market, weaknesses in negotiation frameworks, legal restrictions, and institutional limitations (Rajan and Sen, 2002). These problems have been compounded by the global tendency to liberalize services last, whether in the form of general market liberalization or specifically privatization and FDI liberalization.

Of course, although it is notoriously difficult to measure, intra-ASEAN service trade is intense, driven by proximity (which generally matters more for services than with merchandise) and complimentary. In the majority of ASEAN countries, tourists from within the region dominate. In financial services and telecommunications, Singapore and Malaysia are major investors throughout the region. The flows of intra-regional education and health services are growing rapidly. These are essentially market-driven transactions, which can be facilitated by simplified visa arrangements (such as the current ASEAN-wide visa-free facility) and other harmonization measures that lower transaction costs. However, it would hardly make sense for ASEAN governments to give preferential access to neighboring service providers over the best-practice global alternative.

In the case of FDI, there are a number of sequentially related agreements, starting in 1987 with the ASEAN Agreement for the Promotion and Protection of Investment, commonly known as the ASEAN Investment Guarantee Agreement (IGA). More than a decade later, the Framework Agreement on the ASEAN Investment Area (AIA) was signed in October 1998 at the 30th Meeting of the ASEAN Economics Ministers (AEM). The most significant initiative of the AIA was the preferential, or discriminatory, treatment afforded ASEAN investors in member countries for a fixed period of time. This preferential treatment was to take the form of access to particular industries available only to ASEAN member countries on a reciprocal basis.¹² However, in 2007, the 39th Meeting of the AEM effectively nullified this preferential treatment, when the provisions were extended to foreign-owned ASEAN-based investors. In February 2009, the ASEAN Comprehensive Investment Agreement (ACIA) was signed, intended to be more comprehensive as it deals with liberalization, promotion, facilitation and protection, and adopting also a single negative list approach.

Regional investment flows have risen rapidly over this period. But these are predominantly market-driven, and there is no evidence that they have been induced by the special provisions offered under the AIA and ACIA initiatives. That is, although

¹² Access was to be provided through national treatment provisions within 6 months of the AIA signing. These exclusions were to be progressively phased out by 2003, extended to 2010 in the case of new ASEAN members.

some of ASEAN's investment provisions may represent a medium for regional protectionism or sectoral sheltering rather than liberalization, in practice they appear to have little impact (Jarvis et al, 2009).

Singapore, with its extraordinarily high savings rate and international reserves, and its large government-linked corporate sector, has emerged as a major foreign investor, globally and regionally. Its scale is such that in several ASEAN countries it is among the top three foreign investors. Its investments are broad, including banking, telecoms, hotels, and real estate. As the major regional headquarters for MNEs, it is also a base for these companies investing elsewhere in the region. Malaysia too has become a major investor abroad, with a similar set of drivers at work—high savings rates, loss of comparative advantage in labor-intensive activities, and an activist government-linked company (GLC) sector. For example, both countries have emerged as major investors in Indonesia over the past decade in a diverse range of sectors, including banking, palm oil, hotels, and telecommunications. Thailand is now a major investor in the small neighboring ASEAN economies in a wide range of service, manufacturing, and resource-based activities, and despite occasional Thai-Cambodian hostilities.

Table 5 provides estimates of realized FDI by for each ASEAN economy by source—ASEAN and extra-ASEAN—for 2006–08, which are indicative of longer-term shares. Extra-ASEAN economies dominate these flows, and are typically five to seven times larger than those originating from within ASEAN. This applies to all economies, including the mainland transition economies which, in the early reform phase, received much of their FDI from neighboring ASEAN countries. It also needs to be noted that the intra-ASEAN share in total FDI flows to the region is less than the corresponding share for trade. This is to be expected given that, among the ASEAN-10, only Singapore is an outward investor of any significant scale. The implication is that preferential investment schemes within ASEAN are unlikely to make economic sense for the foreseeable future.

Table 5: ASEAN Shares of FDI and Trade

Country	ASEAN share of inward FDI, 2006-2008 ¹ (%)	ASEAN share of exports, 2009 (%)	ASEAN share of imports, 2009 (%)
Brunei Darussalam	7.8	17.1	51.8
Cambodia	30.8	12.9	37.3
Indonesia	27.4	21.1	28.7
Lao PDR	21.5	80.6	85.8
Malaysia	27.2	25.7	25.4
Myanmar	14.6	50.4	53.7
Philippines	0.1	15.2	25.4
Singapore	3.4	30.3	24.0
Thailand	31.6	21.3	20.0
Viet Nam	17.5	15.1	19.6

Notes:

na = not available

¹Data for 2008 are preliminary.

Sources: ASEAN Secretariat Website, www.aseansec.org

Regional labor markets are becoming increasingly integrated. Here too ASEAN has signed several formal accords since 2000, including the January 2007 ASEAN Declaration on the Protection and Promotion of the Rights of Migrant Workers. Discussions on implementation of this agreement are continuing. However, intra-ASEAN labor flows occur independently of these arrangements and are largely market-driven, dictated by large inter-country wage differentials and open labor markets. Labor flows to, from, and within ASEAN countries are significant. Several lower-income countries are major labor exporters, particularly the Philippines, where remittances are the fourth largest in the developing world. The two richer countries, Singapore and Malaysia, together with tiny Brunei Darussalam, have always had very open labor markets, with 20% or more of their workforces temporary foreign workers. In neither case is there a deliberate preference for workers from other ASEAN countries, but in practice proximity and ethnic/cultural similarities result in the majority of these foreign workers coming from neighboring countries. This is particularly the case with Malaysia, where about 75% of the workers are estimated to be from Indonesia. Given the former's delicate ethnic mix, it is widely believed that the dominant Malay community tacitly supports these large inflows. The Philippines is the second largest source of migrant workers, with particularly large inflows to East Malaysia.

Table 6 provides one set of estimates of the stock of temporary intra-ASEAN migrants in 2006. Recognizing that they are almost certainly a considerable underestimate, they highlight the major flows. The three richer economies, Singapore, Malaysia, and Thailand, all with broadly open international labor markets, are the major recipients, while Indonesia, Malaysia, and Myanmar are major labor sources. Among the 5.5 million recorded workers, three large concentrations stand out, accounting for about two-thirds of the total: migrants from Myanmar working in Thailand, Indonesians in Malaysia, and Malaysians in Singapore. Malaysia is unusual in that it is both a significant recipient and source, with the former predominantly low-skilled workers and the latter higher skilled. Some of the other flows, while small in aggregate, are significant for the countries' concerned. For example, about 10% of the Lao PDR workforce is estimated to work in Thailand, on a permanent or casual basis.

Table 6: Bilateral Estimates of Migrant Stocks in ASEAN, 2006 (in thousands)

Source Country	Destination										
	Brunei	Cambodia	Indonesia	Lao PDR	Malaysia	Myanmar	Philippines	Singapore	Thailand	Viet Nam	ASEAN
Brunei Darussalam	neg	neg	neg	neg	neg	neg	1	neg	neg	neg	1
Cambodia	neg	neg	neg	2	7	neg	neg	neg	232	neg	240
Indonesia	6	neg	neg	neg	1,215	neg	5	96	1	neg	1,323
Lao PDR	neg	1	neg	neg	neg	neg	neg	neg	257	neg	258
Malaysia	68	1	neg	neg	neg	neg	neg	994	3	neg	1,066
Myanmar	neg	neg	neg	neg	92	neg	neg	neg	1,382	neg	1,475
Philippines	23	1	neg	neg	353	neg	neg	136	3	neg	516
Singapore	3	1	neg	neg	87	neg	neg	neg	2	neg	92
Thailand	11	129	neg	3	86	neg	neg	neg	neg	neg	229
Viet Nam	neg	157	neg	15	86	neg	1	neg	20	neg	279
ASEAN	111	290	neg	20	1,925	neg	8	1,226	1900	neg	5,480

Note: Details may not add up to totals due to rounding off errors; neg indicates less than 1,000, or no estimates available.

Source: ILO 2007. Labor and Social Trends in ASEAN 2007: Integration, Challenges and Opportunities. Bangkok.

4.2. The Rise of PTAs

As noted, with the exception of ASEAN itself, the countries of Southeast Asia generally eschewed preferential trading arrangements until the late 1990s, preferring a combination of multilateral and unilateral measures. The former had resulted in a global trading environment that generally supported export expansion with few serious trade barriers, apart from some agricultural and labor-intensive manufactured products. There were meanwhile a series of significant domestic liberalizations in the 1980s and 1990s, most particularly in the three communist states, but also in Indonesia and the Philippines.

Since 2000, there has been little progress with multilateral liberalization, and domestic reform has slowed significantly. Not unrelated to these developments has been the proliferation of various forms of PTAs. Table 7 lists each ASEAN country's participation in PTAs as of January 2010: 91 PTAs have been signed or are under implementation, 32 are under negotiation, and 36 proposed. These numbers include a variety of agreements, ranging from the comprehensive to the so-called "trade-lite", and thus they are not strictly comparable.

Table 7: FTA Status by Country, as of January 2010

COUNTRY	UNDER NEGOTIATION			CONCLUDED		TOTAL
	Proposed	Framework Agreement Signed/Under Negotiation	Under Negotiation	Signed	Under Implementation	
Brunei Darussalam	4	0	1	0	8	13
Cambodia	2	0	1	0	6	9
Indonesia	6	1	1	1	7	16
Lao PDR	2	0	1	0	8	11
Malaysia	3	1	5	2	8	19
Myanmar	2	1	1	0	6	10
Philippines	4	0	1	0	7	12
Singapore	5	0	9	2	18	34
Thailand	6	4	3	0	11	24
Viet Nam	2	0	2	0	7	11
Total	36	7	25	5	86	159

Notes:

1. Proposed - parties are considering a free trade agreement, establishing joint study groups or joint task force, and conducting feasibility studies to determine the desirability of entering into an FTA.
- 2a. Framework Agreement Signed/Under Negotiation - parties initially negotiate the contents of a framework agreement (FA), which serves as a framework for future negotiations.
- 2b. Under Negotiation - parties begin negotiations without a framework agreement (FA).
- 3a. Signed - parties sign the agreement after negotiations have been completed. Some FTAs would require legislative or executive ratification.
- 3b. Under Implementation - when the provisions of an FTA becomes effective, e.g., when tariff cuts begin. As of January 2010

Source: ADB Asian Regional Integration Center 2010, Free Trade Agreement Database for Asia.

Singapore has adopted the most PTAs in ASEAN, with 20 concluded, and 14 under negotiation or proposed. It accounts for over one-quarter of the regional PTAs under implementation. Its government decided to be proactive in this commercial diplomacy, frustrated with the slow pace of ASEAN and alert to commercial opportunities elsewhere. It might appear puzzling that free-trade Singapore would embark on this route, since it has little to offer by way of reciprocal market access. However, it has made some concessions in its more protected services sector, and it has used PTAs to extract useful concessions from partner countries (for example, extensive access to Indian landing rights for Singapore Airlines). It has also suited other countries to engage with Singapore as a “training exercise” in preparation for negotiations with larger, more complex economies. Singapore is seen as small, non-threatening, and with a nonexistent agricultural sector, traditionally the area of greatest sensitivity in trade negotiations. Singapore’s participation in these PTAs has attracted subdued criticism from its ASEAN partners, but it has not seriously threatened the viability of ASEAN.

Thailand has also been active with PTAs, particularly during 2001–2006, when Thaksin Shinawatra was prime minister. This is somewhat ironic because, although traditionally a relatively open economy, Thailand has achieved little progress with its own trade reform since the 1980s. The governments of Indonesia, Philippines and the other four mainland Southeast Asian states have thus far engaged very little in PTAs, reflecting mainly their concerns with domestic reform and a generally reactive approach to international commercial diplomacy. The smaller transition economies, in particular, have struggled to cope with the demands of formalizing their trade regimes, converting the many implicit and obscure NTBs into tariffs. This is also in the context of securing membership of the World Trade Organization (WTO) (except for Lao PDR, which is still an applicant), then implementing the formal requirements, all in an institutional environment of very limited analytical expertise in their bureaucracies and many competing demands from the international donor community.

Three general observations need to be made about these agreements. First, they vary considerably in their scope, depth, and coverage. The larger economic powers, notably Japan and the US, are able to extract specific requirements, for example, the exclusion of sensitive agricultural products in the case of the former and intellectual property rights in the latter. Where ASEAN rules apply, the agreements are more likely to be multilateralized and have less restrictive rules of origin (ROOs). Some of the agreements are very minor, and have little functional significance.¹³ Second, there is considerable variation in the capacity of ASEAN governments to implement these agreements. Singapore, for example, has a high-quality analytical and negotiating capacity, while Lao PDR has practically none of these resources at its disposal and is struggling to satisfy the requirements for WTO membership. PTAs involving the transition countries are a clear distraction from the more important task of general trade reform.

Thirdly, there is the issue of whether these and the broader regional initiatives discussed in the following section will collapse into a plurilateral, pan-Asian

¹³ For example, out-of-season fruits and vegetables could motivate a PTA, such as in the US-Chile agreement (that also included copper), or the proposed Indonesia-Pakistan agreement related to citrus fruits.

agreement. This approach has gained further impetus from the October 2009 East Asian Summit in Hua Hin, Thailand, where the Japanese and Australian prime ministers put forward proposals for an ASEAN+6 and APEC-wide FTA respectively, and with the former receiving ASEAN support. Both proposals are substantially driven by political and strategic objectives. What if any contribution do they make to clearing up the current, distorted trade policy landscape?

According to one school of thought, these multiple and overlapping PTAs could be consolidated into a single East Asian PTA. However, details of how these PTAs can somehow be folded into a much broader multilateral agreement remain sparse. It is also perplexing that advocates of this approach often argue that bilateral agreements are able to achieve much deeper integration because only two parties are involved, but then inexplicably expect the same results from a consolidated agreement involving many more parties.

Even if the “consolidation approach” may be able to address the proliferation of often overlapping PTAs, and make the best of the current mess, other options could achieve the same outcome without creating yet another FTA. Two such alternatives include the multilateralization of preferential accords, and the dilution of ROOs. The original members of ASEAN have employed the multilateralization approach with success, and today close to 90% of the preferences of their PTA are available to nonmembers on an MFN basis. This is a model of how so-called “open regionalism” can work. As a result, overall tariffs have fallen sharply on trade with all countries, because the PTA liberalization program has been more ambitious and rapid than the WTO alone could have delivered. Consequently, utilization rates of remaining preferences have also fallen to negligible levels. Joining a new East Asian PTA would be a step backward, as it would bring this process of multilateralizing preferences to a halt.¹⁴

If members of the PTA are not yet ready to give up reciprocal preferences, then liberalizing ROOs could be an interim step in preparing the groundwork for that process. This could be done by harmonization, and expanding the so-called “rules of cumulation” (that is, the number of countries whose value-added qualifies). If rules of cumulation are sufficiently expanded and then harmonized across different agreements, the outcome could no longer require formal multilateralization of tariff accords. Here again, a new and larger PTA is not required, and would in fact be a less desirable option.

Both these alternatives could be applied to intra- and extra-regional PTAs. The consolidation approach, on the other hand, is only designed for intra-regional PTAs. But most PTAs are extra-regional. An ASEAN+3 PTA (ASEAN plus PRC, Japan, and Korea) would address only 6% of all PTAs of the countries concerned, while an ASEAN+6 PTA (ASEAN+3 plus India, Australia, and New Zealand) could potentially neutralize a quarter of them. But these figures in turn prompt the question as to why most PTAs are extra-regional to begin with? A common explanation is that they are designed to restore market access in traditional trading partners that may have joined a regional PTA (see Menon, 2007b). If this is true, then a new, consolidated East Asian FTA may itself spark a new wave of extra-regional PTAs. With more countries

¹⁴ For further discussion, see for example the exchange of views in the Far Eastern Economic Review between Kawai and Wignaraja (2008), and Hill and Menon (2008).

outside the region than inside, an East Asian PTA could actually be counter-productive, leading perversely to an increase in the total number of PTAs. “Consolidation” therefore does not appear to provide a solution, and may actually contribute to the problem, by adding another strand to the spaghetti bowl or, worse still, inducing a new wave of extra-regional PTAs.

4.3. From ASEAN to the East Asian Summit, and Beyond?

ASEAN has developed an elaborate set of extra-regional agreements, ranging from general statements about the desirability of closer economic relations to what on paper appears to be firm commitments to economic integration (see for example Plummer and Chia eds, 2009). Until around 2000, the former prevailed, and involved little more than official dialogues and sporadic business cooperation programs. However, in recent years, ASEAN has made significant commercial policy commitments, initially in the form of ASEAN+3 and more recently ASEAN+6. The latter has in turn morphed into the ASEAN Economic Community and the East Asian Summit¹⁵. In addition, there are various formal agreements with other economic communities, such as the AFTA-CER, involving ASEAN and Australia-New Zealand, and ASEAN+1 agreements, where ASEAN may negotiate with a particular country (or bloc) on a specific issue.

ASEAN's regional economic integration efforts are geared toward creating an ASEAN Economic Community (AEC). The ASEAN Leaders had originally intended to create the AEC by 2020, but in early 2007 they advanced the deadline to 2015. The AEC envisions ASEAN as a competitive economic region with a single market and production base. At the 13th ASEAN Summit held in Singapore on 20 November 2007, ASEAN Leaders adopted the ASEAN Economic Blueprint, to serve as a guide for establishing the AEC. The blueprint contains 17 “core elements” and 176 priority actions, to be implemented within a Strategic Schedule of four periods (2008–2009, 2010–2011, 2012–2013, and 2014–2015). Given the diversity within ASEAN, and sensitivities regarding different issues\sectors, it was agreed that liberalization of goods, capital, and (skilled) labor flows proceed at different speeds according to member countries’ readiness, national policy objectives, and levels of economic and financial development. Thus, despite the blueprint and the various priority actions and schedules, it remains to be seen to what extent concrete liberalization will be implemented, or whether it will remain essentially a vision statement.

ASEAN also participates in a range of broader regional and multilateral initiatives. These include APEC and WTO-based negotiations (for example, the current Doha Round). Its official position is that it regards these processes as consistent with ASEAN objectives and therefore supports them. However, in practice, ASEAN does not appear to have played an effective catalytic role in recent years. One ASEAN country, Indonesia, is a member of the G20, which appears to be morphing into the principal global forum for addressing key development issues, such as the measures to prevent a recurrence of financial crises and climate change. It is too early to judge whether Indonesia attempts to represent ASEAN interests at these meetings. Institutionally, ASEAN also has observer status at the G20. In sum, ASEAN is

¹⁵ Russia and the US were observers at the East Asia summit in Ha Noi on 30 October 2010, and will formally become members in 2011.

moving cautiously and uncertainly toward being at the center of a potentially large, yet still undefined, economic group.

Meanwhile, ASEAN has been an active participant in the ongoing, though still largely inconclusive, discussions concerning broader macroeconomic coordination. Following the 1997/98 Asian financial crisis, East Asia launched several interrelated regional cooperation initiatives, particularly for early detection and management of financial and macroeconomic vulnerabilities, as well as broader macroeconomic coordination. Some of these have developed faster than others, and all have occurred within the framework of ASEAN+3, with the involvement of PRC, Japan and Korea.

The three major initiatives undertaken by ASEAN+3 finance ministers are the introduction of a regional economic review and policy dialogue process (ASEAN+3 ERPD); the establishment of a regional reserve pooling arrangement, the Chiang Mai Initiative (CMI); and the development of local-currency bond markets, the Asian Bond Markets Initiative (ABMI). The first two were launched in May 2000 and the latter, which has progressed at the slowest pace, three years later.

The ASEAN+3 ERPD mechanism is intended to improve information sharing, promote dialogue among policymakers, and foster collaboration on financial, monetary, and fiscal issues of common interest. Initially, the CMI involved an expanded ASEAN Swap Arrangement (ASA) involving all ASEAN members, and a network of bilateral swap agreements (BSA) and repurchase facilities among ASEAN+3. The size of the CMI fund has grown from \$36.5 billion in 2001–2005, to \$84 billion in 2008, and to \$120 billion in May 2009. Since its inception, however, it was clear that the CMI was much more than this, in that it was actually an institutional mechanism to pursue further negotiations, rather than a final agreement on swap arrangements.

The biggest step forward took place in May 2009, when the ASEAN+3 Finance Ministers (AFMM+3) agreed on the governing mechanisms and implementation plan for the CMI multilateralization (CMIM). Japan and the PRC would contribute identical shares of the total reserve pool (32%), together with Korea (16%) and ASEAN (20%). The AFMM+3 also agreed to establish an ancillary institution in the form of an independent regional surveillance unit to monitor and analyze regional economies and support CMIM decision-making—the Asian Macroeconomic Research Office (AMRO), to commence in May 2011 in Singapore. Looking forward, the success and relevance of this fund will depend on boosting its size from its current \$120 billion, an amount that is unlikely to be sufficient in the event of a major regional crisis. Moreover, as long as countries continue their attempts to “self-insure” in the form of accumulating very large (and low return) foreign exchange reserves, it is unlikely to play much of a role. Much will also depend on how AMRO performs, and crucial issues of surveillance and conditionality are operationalized.

5. Retrospect and Prospects

Now in its fifth decade, how should one evaluate ASEAN? To what extent has it contributed to the region’s economic dynamism? Is it a building block or a stumbling block toward greater Southeast Asian and Asia-Pacific economic integration?

ASEAN has significant achievements to its credit. First, it still exists as an effective functioning entity, which is more than can be said for several other past and present regional organizations in the developing world. Second, for a region characterized by great diversity and considerable past tension, Southeast Asia has by and large been free of major conflict since the mid-1980s, as the three communist states progressively re-entered the regional and international mainstream. Of course, border skirmishes persist—the creation of East Timor as an independent nation state was a challenging experience and Myanmar remains an international pariah beyond the reach of ASEAN diplomacy. Third, and most important, ASEAN in aggregate has been a region of rapid economic development and rising living standards. One can debate the direction of causality between this outcome and ASEAN, but undeniably the determination of the region’s leaders to forge more harmonious relations has facilitated economic development. The engagement with and the nurturing of Cambodia, Lao PDR, and Viet Nam in their early stage of economic liberalization, after decades of acrimony and one of the most destructive wars in recent memory, has been a signal achievement.

Fourth, ASEAN has been diplomatically skillful in effectively playing “balance of power” politics (Acharya, 2009). There is no clear economic and political leadership in East Asia, with the economic giants of the past and future—Japan and PRC respectively—engaged in a battle of constant diplomatic rivalry. Courted by both powers, ASEAN has thus been able to advance its own interests considerably, and become either the arbiter or driver of almost every major initiative on regional commercial and security architecture. ASEAN’s pivotal position has been maintained as Asian regionalism has extended to embrace South Asia, and in particular the inclusion of the third major Asian power, India.

Yet, on the other side of the ledger, ASEAN has not progressed very far in terms of becoming a formal economic entity. This proposition can be illustrated with reference to the standard theory of customs unions (Table 8). In over four decades, it has not progressed beyond the first phase, of loosely exchanging trade preferences, while still maintaining their separate, and still quite variable, trade regimes. As noted, it is very unlikely to progress to the next stage, of a customs union with common external tariffs. Deeper integration, affecting factor markets and a common macroeconomic policy regime a la the EU, is even further off the horizon.

Table 8: Indicators of Economic Integration

Indicator	ASEAN	EU	NAFTA	CER	Mercosur
Free trade in goods	part	yes	yes	yes	part
Free trade in services	part	yes	part	yes	part
Capital mobility (FDI)	part	yes	part	yes	part
Labor mobility	no	yes	no	yes	no
Competition law converging	no	yes	no	yes	no
Monetary union	no	yes	no	no	no
Unified fiscal policy	no	part	no	no	no

Source: Authors’ interpretation

Moreover, ASEAN runs the risk of being consigned to the status of diplomatic talkshop. In the words of one its former Secretary Generals, in a frank report to leaders: “regional economic integration seems to have become stuck in framework agreements, work programs and master plans” (Severino, 2006, p. 247). ASEAN has a long history of issuing declarations, action plans and charters, yet with limited capacity—and in some cases arguably intention—for implementation. It has generally prevaricated on whether to become a formal customs union. It has developed a plan for labor market integration, while some of the largest labor movements in the world (relative to the size of the recipient economy) have occurred outside this framework. Even after one of the deepest economic crises in the region’s history, ASEAN was unable to develop a set of emergency support mechanisms. At its root, the “ASEAN Way” is an institutionalized mechanism that renders very unlikely the prospect of a fundamental change in direction. The most likely outcome is that the country’s policy regimes will converge over time, to the point where preferential arrangements become redundant. As the region’s commercial hub, Singapore sets the standard in this respect, and one to which the lower-income members of ASEAN might aspire.

And so it is not surprising that ASEAN’s greatest achievement in the economic sphere has been more to do with what AFTA has indirectly induced rather than mandated. Recognizing that most of the region’s trade is extra-regional, in order to minimize the potential costs of trade diversion the original ASEAN members have been reducing their external tariffs in conjunction with reduced barriers to intra-ASEAN trade. The ASEAN-6 countries have also undertaken several waves of multilateralizing preferences, where they have voluntarily offered their AFTA concessions to nonmembers on a nondiscriminatory basis. When the preferences are fully multilateralized, the margins of preference are zero, as is the potential for trade diversion. This was the case for more than two-thirds of the tariff lines for the ASEAN-6 countries through 2002 (Feridhanusetyawan, 2002), and the proportion has increased since (Menon, 2007a).

Furthermore, because preferential tariff reduction schedules have been ambitious and rapid, AFTA has accelerated the pace of multilateral trade liberalization in ASEAN-6 countries. Instead of jeopardizing multilateralism, it has hastened the speed at which these countries have moved toward their goal of free and open trade. In this way, AFTA’s greatest achievement may have less to do with what it prescribes or mandates, and more to do with what it promotes indirectly through the long-standing commitment of its members to openness.

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ASEAN Economic Integration: Features, Fulfillments, Failures and the Future

Established in 1967, ASEAN is arguably the most durable and successful regional grouping in the developing world. Despite great internal diversity and a reluctance to establish a strong supranational structure, its economic agenda has grown from liberalization of merchandise trade to include services, investment, and labor. More recently through ASEAN+3, it has broadened cooperation to macroeconomic surveillance and financial issues. Nevertheless, there is little likelihood in the foreseeable future that this will evolve into a deep EU-style economic integration behind a common external trade regime, despite a commitment to forming an ASEAN Economic Community beginning 2015.

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