

Regionalism in the Asia-Pacific Region: How Wide, How Deep?*

Richard Pomfret**

The Asia Pacific region was characterized in the second half of the twentieth century by an absence of regional trading arrangements. The situations changed after 2000, raising questions of sequencing and of the boundaries of the region. This paper argues that the proliferation of regional and bilateral agreements has been driven by the rapid emergence of regional value chains and centres on trade facilitation measures. These create deep regionalism and variable boundaries, depending upon which countries integrate into the regional value chains.

JEL Classification: F15

Keywords: regionalism – Asia

* Received July 10, 2009. Accepted October 30, 2009. Paper presented at a plenary session of the Korea and World Economy VIII Conference, to be held at Hong Kong Baptist University on 9-10 July 2009. I am grateful to Hyun-Hoon Lee, Sven Arndt, Eduardo Pedrosa and other conference participants for helpful comments. This paper draws on papers prepared for the Asian Development Bank project *Institutions for Regionalism: Enhancing economic cooperation and integration in Asia and the Pacific*, presented at a workshop in Jakarta on 9-10 June 2009.

** Professor of Economics, University of Adelaide, Adelaide SA 5005, Australia, E-mail: richard.pomfret@adelaide.edu.au

1. INTRODUCTION

Until 1995, when the World Trade Organization (WTO) was established, regionalism was conspicuously absent from East Asia. During the GATT era it was common to contrast the situation in East Asia with the waves of regional trading arrangements (RTAs) occurring in Europe, the Americas and Africa. Korea and Japan were the only countries among the charter members of the WTO not party to any RTAs. China was busy negotiating accession to the WTO and pursued a multilateral trade policy.¹⁾ The only RTA in East Asia was the Association of Southeast Asian Nations (ASEAN), and by common consent ASEAN had had little impact on trade flows since its inception in 1967.

In sharp contrast, the twenty-first century has seen East Asia in the vanguard of a new wave of regional and bilateral trade agreements. What explains this sharp change of direction? If East Asian regionalism is thriving, this raises two further questions: how wide is the region that it covers and what is the content of, or how deep is, the regional integration?

This paper argues that regionalism in East Asia is now a substantial phenomenon. Regionalism did not flourish in the second half of the twentieth century because Asian countries pursued inward-oriented development strategies or, when they pursued outward-oriented strategies, their trade was overwhelmingly with countries outside the region. Intra-Asian preferential trading arrangements held no attraction and when countries liberalized trade policies it was on a non-discriminatory basis (section 2). Several catalysts encouraged monetary integration after 1997 and talk of an Asian sequence of monetary integration preceding trade integration, but actual steps in the monetary sphere have been small (section 3.1). In contrast, since 2000 there has been an explosion of bilateral and plurilateral trade agreements, targeting non-tariff or regulatory impediments to trade. The proliferation of agreements has raised concerns about how to

¹⁾ Mongolia, which joined the WTO in 1997, and Taiwan also had non-discriminatory trade policies.

simplify the noodle bowl and consolidate regional arrangements, which in turn raises questions about which countries to include in consolidated Asian regional arrangements (section 3.2). The driving force behind East Asian regionalism is identified in section 4 as the rapid growth of intra-regional trade centred on regional value chains. In a region of low most-favoured nation tariffs, the functioning of regional value chains can be facilitated by bilateral or plurilateral agreements. The concluding section argues that East Asian regionalism will continue to deepen because trade facilitation addresses “beyond trade” issues of harmonization, mutual recognition of regulations and so forth, and its width will be related to the geographical reach of the regional value chains.

2. REGIONALISM IN EAST ASIA 1950-2000

During the 1960s many observers saw the global trading system caught in a headlong rush to regionalism.²⁾ Following the example of Western Europe, an alphabet soup of regional trading arrangements was created in Latin America, the Caribbean and Africa. These non-European RTAs had little economic impact and the wave ebbed. In the 1980s and early 1990s a second wave of RTAs included negotiations leading to formation of the North American Free Trade Area and discussion of a Free Trade Area of the Americas, leading commentators to fear a collapse of the global system into three blocs centred on Europe, the Western Hemisphere and Asia. In both waves Asia was the missing link, with no serious RTA formation or creation of a regional bloc.

The only significant regional arrangement in East Asia was ASEAN, whose political origins lay in links between the anti-Communist regimes of the region and in confidence-building between Malaysia and Indonesia (Severino, 2009). Attempts in the 1970s to provide an economic impetus to ASEAN through coordination of industrial projects or other measures

²⁾ Pomfret (1997) substantiates the generalizations made in this paragraph.

grounded in import-substituting industrialization had minimal impact. Members wanted to support their own import competing industries, but were unwilling to support their partners' uncompetitive industries. As the five original ASEAN members shifted towards more outward-oriented economic development strategies in the 1980s, their exports went to markets outside the region and intra-regional trade remained small.

ASEAN finally moved towards becoming an RTA with the 1992 announcement that an ASEAN Free Trade Area (AFTA) would be established by 2008. Even this was a hesitant step. Internal tariffs would be reduced to five percent or less rather than full tariff-free intra-ASEAN trade, preferential tariff reductions were back-loaded to take effect as late in the transition period as possible, and lengthy lists of commodities were excluded. Moreover the paperwork was often sufficient disincentive that traders did not claim the preferential tariff rate even if they were eligible. At the same time, ASEAN countries (Philippines and Thailand in particular) unilaterally cut tariffs on a large range of goods, reducing the margin of preference (Ando and Kimura, 2005). The net result was that AFTA's preferential tariffs had a very small impact on trade in the 1990s (Manchin and Pelkmans-Balaoing, 2008).

AFTA was the only RTA in East Asia in the second half of the twentieth century. Sub-regional trading zones emerged in the Pearl River Delta (the PRD involved Hong Kong, Macau and Guangdong Province of China) and around Singapore (Sijori, or Singapore, Johor and Riau), but these were market-driven, with some public policy measures to facilitate cross-border trade and investment (Pomfret, 1996). Other sub-regional zones or "growth triangles" tried to replicate the success of the PRD or Sijori, with more state involvement and less economic impact. In Northeast Asia the Tumen River Project, a state-driven sub-regional zone involving the Koreas, China, Japan and Mongolia, had little economic effect.

Although AFTA had little impact as a conventional RTA with preferential tariffs, cooperation among ASEAN members did have economic effects during the 1990s. Singapore already had liberal and efficient trade

arrangements, but Indonesia, Malaysia, Thailand and, to a lesser extent, the Philippines all began to streamline their border facilities. Much of this trade facilitation could be done unilaterally, but there were benefits from coordination and standardization between neighbours and on a regional basis. Coordination among customs officials and initiatives such as the ASEAN Single Window were aimed at reducing the time and cost of trading across ASEAN borders. Individual steps can be listed, but their impact is hard to measure. At the aggregate level, however, trade costs of the five countries declined substantially, converging on the best practice of Singapore.³⁾

In sum, regionalism in the Asia-Pacific region was characterized by its absence. The open (i.e. non-preferential) regionalism of Asia-Pacific Economic Cooperation (APEC), which was established in 1989, was not regionalism in the normal sense of RTAs and the membership encompassed a range of countries with no common features beyond a Pacific coastline.⁴⁾ Politically, APEC was driven by US opposition to and Australian fear of being sidelined by an Asian RTA, such as the East Asia Economic Caucus (EAEC) proposed by Malaysia. Open regionalism was popular in the context of many Asian countries seeking to liberalize their own trade policies and hoping for reciprocal multilateral liberalization on the part of other countries beyond what was being achieved in multilateral trade negotiations (the Uruguay Round) which seemed stalled at the end of the 1980s. The declaration at the 1994 Bogor Summit that APEC members would remove their tariffs by 2010, with extensions for developing countries to 2020, was the high-point of open regionalism.⁵⁾ When the USA tried to push trade liberalization further in 1996 with the Early Voluntary Sectoral Liberalisation (EVSL) initiative, it ran into opposition led by Japan. APEC members were

³⁾ Pomfret and Sourdin (2009) provide evidence that trade costs of the ASEAN countries fell substantially during the 1990s and significantly faster than other countries' trade costs, suggesting that national policies as well as technical change were responsible.

⁴⁾ APEC now includes Australia, Brunei, Canada, Chile, China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, the Philippines, Russia, Singapore, Taiwan, Thailand, the USA and Vietnam.

⁵⁾ APEC may have also had a less direct impact on trade by encouraging transparency, which Helble, Shepherd and Wilson (2009) found to significantly increased trade flows.

unwilling to accept pressure to liberalize beyond what they would have done unilaterally, and the scope for concerted unilateral liberalization had narrowed by the late 1990s. Although APEC remains active in areas such as trade facilitation and APEC summits provide a useful meeting place for world leaders, open regionalism lost the significance that it attained in the mid-1990s. APEC's inability to find any response to the 1997 Asian Crisis underlined its limited relevance as a regional institution.

3. ASIAN REGIONALISM IN THE TWENTY-FIRST CENTURY

The 1997/1998 Asian Crisis provided a catalyst for change. Many Asians felt that the global institutions provided too little assistance too late, and contrasted the generous support that had been given in the recent past to Latin American countries or Russia. The main culprit was the IMF and Japan latched on to this to propose the creation of an Asian Monetary Fund. Following the momentum gathering in Western Europe towards the creation of the euro, there was even talk of an Asian currency. However, none of these grand plans attracted serious support.

China was relatively little affected by the Asian Crisis and in 1997 was a staunch supporter of the multilateral institutions, willing to follow the US lead in matters of global economic architecture. This support started to flag as China perceived itself receiving little credit for its position and for self-effacing measures such as not joining the competitive devaluations of 1997-8. The US bombing of the Chinese embassy in Belgrade in May 1999 was a catalyst for re-evaluation of China's position and a decision to shift China's support in favour of regional institutions.

In the 2000 Chiang Mai Initiative (CMI) the ten ASEAN countries, China, Japan and Korea agreed on currency swap arrangements in the case of a balance of payments crisis. The CMI was the first East Asian regional agreement in banking and finance; although there had been informal

arrangements, such as the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP), none had the formal status or explicit regionalism focus of the CMI.⁶⁾ The CMI's ASEAN+3 membership recalled the EAEC proposal, and was in stark contrast to the pan-Pacific composition of APEC. The Asia-Europe Meeting (ASEM) which began to hold biennial summits in 1996 may also have contributed to a sense of Asian-only regionalism encapsulated in ASEAN+3, although the EU was more concerned about its own exclusion from groups like APEC than in promoting Asian solidarity.⁷⁾

In the financial sphere The Asian Bond Market Initiative (ABMI) was launched at the EMEAP central banks forum and endorsed by ASEAN+3 finance ministers in 2003. The ABMI is intended to mobilise the region's currency reserves for the region's own needs, but the value of bonds issued remains small. The first Asian Bond Fund pooled one billion US dollars from the eleven EMEAP members for investment in US-dollar denominated bonds issued by sovereign or quasi-sovereign borrowers from eight of the EMEAP economies. In June 2005 the second Asian Bond Fund invested \$2 billion in local currency denominated sovereign and quasi-sovereign bonds from the same eight economies. The ABMI's main role has been to highlight both cross-border and domestic market impediments (e.g. capital controls and variations in withholding and other taxes) to bond market development in the region.

At the same time a new wave of RTAs centred on bilateral agreements and focussing on non-tariff barriers to trade originated in East Asia (and was taken up energetically by the Bush Administration in the USA). In the final months of 2000 the leaders of China and Japan individually approached ASEAN with proposals for a free trade agreement, and in the following year China, Japan and Korea discussed a coordinated ASEAN+3 FTA.⁸⁾ However,

⁶⁾ The Executives' Meeting of East Asia-Pacific Central Banks was established in 1991 and currently has eleven members (the original ASEAN5, Australia, China, Hong Kong, Japan, Korea and New Zealand).

⁷⁾ The ASEM summits in Bangkok (1996), London (1998) and Seoul (2000) were attended by leaders of the fifteen EU countries, seven ASEAN countries, China, Japan and Korea.

⁸⁾ Lee, Koo and Park (2008) describe the dramatic change in the three countries' positions on trade agreements. Using a gravity model, they conclude that the Three have not been

China became impatient with the slow progress and negotiated a bilateral FTA with ASEAN in 2002.⁹⁾ Apart from this major ASEAN+1 agreement, dozens of bilateral trade agreements were concluded by East Asian countries.

3.1. Money before Trade: Is there an Asian Sequence?

Bela Balassa (1961) set out a five-stage taxonomy of economic integration from simple preferential tariffs to a free trade area (preferential tariffs equal zero) to a customs union (FTA plus common external trade policy) to a common market (customs union plus free movement of capital and labour) to economic union. Although Balassa viewed this as a taxonomy from shallow to deeper economic integration, his stages have often been interpreted as a chronological sequence, capturing Western European regional integration, which broadly followed a trade-first sequence. The customs union established in the 1960s was followed by reductions in the restrictions to labour and capital movement, and finally by monetary union at least among some European Union members.

The slow progress on intra-Asian trade liberalization combined with the establishment of the CMI encouraged some observers to identify a distinctive Asian sequence of monetary integration preceding trade integration. There is some logic to the idea that monetary integration will facilitate intra-regional trade (Dieter and Higgott, 2003). However, the empirical support for the Asian sequence remains slight (Pomfret, 2005). The CMI played a minimal role in the 2008-2009 global crisis because Asian countries' own reserves were more than adequate, i.e. governments had learned national rather than regional lessons from the 1997-1998 Asian crisis. Both the CMI and the

adversely affected by the existence of major regional RTAs, which implies that the post-2000 increase in RTAs in East Asia is internally driven rather than a defensive response to developments elsewhere.

⁹⁾ China turned to bilateral trade agreements after completing its WTO accession negotiations. China had an advantage over Japan and Korea insofar as its FTA with ASEAN could obtain a WTO waiver of most-favoured nation treatment under the Enabling Clause which governs preferential arrangements among developing countries, whereas any Japanese or Korean FTAs have to gain waivers under the stricter conditions of Article XXIV.

Asian Bond Market Initiative (ABMI) are minor contributions to Asian monetary integration, even with the vaunted Chiang Mai Initiative Multilateralization (CMIM) in early 2009.¹⁰⁾

More substantive steps, such as the proposal for an Asian Monetary Unit (AMU), have made no progress, and an Asian Monetary Fund (AMF) or Asian currency remain distant.¹¹⁾ The key obstacle is lack of political will. There is disagreement about which currencies should be included in an AMU and with what weights. There would be disagreement about relative voting weights in an AMF, and about who should run monetary policy in a currency union. With the multilateralization of the CMI in early 2009 came agreement on contributions and voting rights, by which equal weights for Japan and China were achieved by a fudge: the share of China plus Hong Kong is equal to that of Japan, although Hong Kong is in many respects a separate economic entity and was not party to the CMI.¹²⁾ Even beyond the tensions between the established and rising economic power for supremacy, it is uncertain what the weight should be of the mid-rank economic powers, led by Korea but also including the larger ASEAN economies.

In the twenty-first century, East Asian regional agreements have primarily concerned trade. The spread of trade agreements in Asia has been

¹⁰⁾ The ASEAN+3 finance ministers decided to multilateralize the CMI swap arrangements, so that a country with balance-of-payments problems can access the entire pool, which the ministers agreed should amount to a total of US\$120 billion. However, issues such as economic surveillance before release of CMIM funds and monitoring to ensure due diligence after disbursement remain unresolved.

¹¹⁾ Dieter (2007, p. 139) similarly concludes that “monetary regionalism in Asia will both be a complex endeavour and will — if at all — only be achieved in the long run”. Grimes (2009) takes a slightly more upbeat position on the process, but from an international relations perspective of how the CMI, ABMI etc affect interaction between Japan, China and the USA rather than from a perspective of enhanced regional financial market integration or monetary coordination.

¹²⁾ Japan will contribute \$38.4 billion, or 32% of the \$120 billion total, while China will contribute \$34.2 billion and Hong Kong \$4.2 billion. Thus Japan is the largest single contributor and China and Hong Kong are the biggest co-equal contributors. These shares contrast to earlier arrangements such as funding of the Asian Development Bank, in which China’s share is less than half of Japan’s. Korea’s contribution to the CMIM is \$24 billion and other contributions less than \$5 billion per country. As a reference point, Korea’s bilateral swap agreement with the US Federal Reserve is for up to \$30 billion; Japan’s liquidity swap agreement with the US Fed is unlimited.

documented by Menon (2007), Kawai and Wignaraja (2007), Lee *et al.* (2009) and ADB (2008). However, it is difficult to generalize about the agreements' content. Many of the agreements lack much serious content, and address specific, sometimes apparently minor, issues (Pomfret, 2007). The agreements are not primarily about tariff barriers, but more often about reducing border and behind-the-border trade costs.

Reflecting the accelerated pace of regional integration, an initiative to establish an ASEAN Economic Community was launched at the 2003 ASEAN summit in Bali, and at the January 2007 summit the target date for creation of a single ASEAN market was brought forward to 2015. The ASEAN Economic Community project is an attempt to unify and extend the ASEAN Free Trade Area, the ASEAN Investment Area and the ASEAN Framework Agreement on Services, and is clearly aimed at facilitating trade.

At the same time as ASEAN was deepening its own regional integration, it looked for new institutional arrangements with its northeast Asian trading partners. ASEAN had been considering in 2000 a proposal for integration among ASEAN+3, but foot-dragging by Japan and Korea (Munakata, 2006, pp. 117-118) led to ASEAN and China moving swiftly in 2001 towards negotiating a trade agreement. In November 2002 ASEAN and China signed the framework agreement on Comprehensive Economic Cooperation, which foreshadowed establishment of an ASEAN-China Free Trade Area within ten years. In June 2003 China and Thailand signed an "early harvest" agreement to eliminate tariffs on 108 edible vegetables and 80 edible fruits and nuts from 1 October 2003, and early harvest measures involving other ASEAN members were introduced on 1 January 2004. In November 2004 the formal Agreement on Trade in Goods between ASEAN and China was signed; it envisaged establishment of a free-trade area by 2010 for six ASEAN members and by 2015 for the four newest ASEAN members. In addition, the framework agreement foresaw more comprehensive liberalization, with agriculture, human resource development, information and communication technology, investment, and development of the Mekong River Basin identified as priority areas (Sen, 2004, p. 76) and collaboration on illegal

immigration, drug smuggling, counterterrorism and other security concerns also on the agenda (Kwei, 2006, p. 121).

In sum, despite the stimulus of regional dissatisfaction with international monetary institutions during the 1997-1998 Asian Crisis and the CMI, regionalism in East Asia has been primarily in trade. This is consistent with the observation by Estevadeordal and Suominen (2008, pp. 129-130) based on analysis of cooperation agreements at the global level that “states cooperate disproportionately more in the domain of trade than in other domains. This may suggest that trade has properties that render it particularly amenable to formal as well as bilateral cooperation”. The distinctive feature of Asian agreements is not a novel sequencing, but the focus on trade facilitation rather than preferential trade policies

3.2. Variable Geometry: Who belongs in the Asian Region?

Intertwined with the struggle for regional hegemony is the question of how the region should be defined. ASEAN expanded in the second half of the 1990s to include Laos, Myanmar, Vietnam and Cambodia. ASEAN+3 emerged as a broader grouping in the late 1990s, but by the turn of the century Japan was becoming concerned about China’s weight in this grouping and neighbouring countries were concerned about being excluded.

At the eighth ASEAN+3 summit in 2004, it was agreed to convene a regular East Asia Summit (EAS). The First East Asia Summit, held in Kuala Lumpur on 14 December 2005, was preceded by arguments about whom to invite, with China favouring a guest list limited to ASEAN+3. Japan argued successfully for Australia, India and New Zealand to be included, so that the East Asia Summit configuration is sometimes referred to as ASEAN+6. At the summit China argued for Russia’s inclusion, but no agreement was reached and the second East Asia Summit held in Cebu in January 2007 had the same participants as the first.¹³⁾ There was also no clarification of the

¹³⁾ Russia participated in the first EAS as an observer at the invitation of 2005 host Malaysia and its request to become a future member seems to be supported by China and India, but

relative roles of the East Asia summits and the ASEAN+3 summits in the evolving regional architecture.

It is not essential that all functions of regional institutions be met by organizations with a common membership, and Australia in particular has pushed for “variable geometry” as a practical way forward. However, if there is a core membership, there will inevitably be competition to be included in the core and for pre-eminence within the core. One consequence of the East Asia Summit was to highlight the competition for regional leadership. Even though China gave way to Japan on the invitation list, the summit was a Chinese initiative and Japan felt a need to respond. The Japanese proposal of a Comprehensive Economic Partnership in East Asia among the 16 East Asia Summit participants was controversial, especially because it seems even more than the EAEC to be an RTA that excludes the USA. The various forums reflect Great Power competition, with Japan using the broader East Asia Summit membership to counterbalance China’s success with a more functional approach towards relations with ASEAN and in various bilateral agreements.¹⁴⁾

The East Asia Summit (EAS) provided an alternative grouping of ASEAN+3 plus Australia, India and New Zealand.¹⁵⁾ FTAs between ASEAN and the Closer Economic Relations (CER) countries (Australia and

no formal progress has been made. Timor-Leste is seeking ASEAN membership and became a member of the ASEAN Regional Forum in July 2005; presumably any new member of ASEAN would also join the EAS.

¹⁴⁾ India is a latecomer to the competition. As well as participating in the East Asia Summits, India promotes the Asia–Pacific Trade Agreement (APTA), a preferential trading arrangement open to all members of the UN Economic and Social Commission for Asia and the Pacific (ESCAP). APTA’s current members are Bangladesh, China, India, South Korea and Sri Lanka. So far APTA has had little impact on regional trade flows.

¹⁵⁾ Australia and New Zealand embraced deep regionalism with their 1983 CER agreement. Several overtures to link the CER and ASEAN were rebuffed in the 1990s and early 2000s. In the late 1980s and early 1990s Australia played a leadership role in arrangements such as APEC or EMEAP, but under the 1996-2007 Liberal governments engaged less actively with Asia at the political level, even as economic ties continued to strengthen. In 2006 Australia’s government publicly stated that “if invited by ASEAN+3 members, Australia would be willing to make a financial and practical contribution to the Chiang Mai Initiative” (Corbett and Fitriani, 2008), but no invitation came and the CMIM remained an ASEAN+3 affair.

New Zealand) and ASEAN and India also highlighted the broader region. However, the EAS raises questions about the trade off between size and efficacy (is 16 countries too many to reach agreements?) and about the position of geographically cognate countries not in these arrangements, such as Bangladesh or Papua New Guinea.

The phenomenon of non-members wanting to be in the club (“the grass always looks greener beyond the fence”) is illustrated by the expansion of EU membership and also by the recent flourishing of G7 Groups. The G7 meetings, which began in 1975 in response to the economic shocks of the early and mid-1970s, brought together the leaders of the seven largest market economies in annual summits. In 1997 Russia was invited to join what became the G8. By the twenty-first century with the economic rise of China, India and Brazil, the G8 seemed anachronistic. The problem was addressed in 2009 by convening a G20 meeting which include not only the G8 countries but also the major Latin American economies, South Africa, Saudi Arabia, Turkey, India and Australia. From East Asia the G20 included Japan, China, Korea and Indonesia. ASEAN was represented by Thailand which held the rotating presidency. However, in future Thailand will not be represented and could legitimately question why Indonesia has a seat and it does not when their GDP is roughly equal. Mid-sized economic powers such as Australia and Korea are vigorous supporters of the G20 grouping, because it represents a number which will just include them; with more exclusive membership Australia and Korea would likely be excluded and in a bigger group each country’s weight would be smaller.¹⁶⁾ Similar tensions surround the composition of the UN Security Council, where the five permanent members are jealous of their position while countries such as Japan, India, Germany or Brazil consider their claim to be at least equal to that of an

¹⁶⁾ Korea and Australia both favour the idea that the Asian G6 from the G20 countries should play a strategic agenda-setting role on Asian regional issues. Australian Prime Minister Rudd’s proposals along these lines in Singapore (speech at the Shangri-La Dialogue summit on 29 May 2009) would not have been popular with his hosts who have seen Singapore as a hub for ASEAN and East Asian regionalization. Korea is devoting much energy to hosting the G20 finance ministers meeting in 2010 and, as G20 chair for the year, is responsible for preparing for the 2010 summit.

existing member. In Asia this plays out in competition between regional organizations. China has greater influence within the UN Economic and Social Commission for Asia and the Pacific (ESCAP). Japan has more influence, because it provides the largest share of funding, in the Asian Development Bank (ADB).

In sum, the geographical extent of Asian regionalism remains in a fluid state. The core in recent years has been ASEAN. In the twenty-first century ASEAN's institutional relations with China have strengthened, and much of the action has centred on the reaction of Japan to the challenge of China's growing economic significance and concerns of other countries such as Korea or in a wider circle Australia and India about their role in regional institutional developments. Such concerns are counter-productive for cooperation and regional integration because power and influence are zero-sum games. They may be even more corrosive in Asia because, in the absence of clear geographical borders defined by mountains or water, the geometry of Asian regionalism is variable.¹⁷⁾ The arena for fighting over influence itself becomes a source of endless manoeuvring with little net benefit.

4. DRIVING FORCES BEHIND ASIAN REGIONALISM

Until the 1990s the trade of Asian countries was largely with countries outside the region. Japan initiated a trend towards integrated production

¹⁷⁾ To the north and west, Central Asia and Mongolia are geographically and culturally closely linked to neighbouring provinces of China, and organizations such as Central Asian Regional Economic Cooperation (CAREC) or the Shanghai Cooperation Organization bridge these countries. To the south west, India and Pakistan are linked by history and institutionally in the South Asian Association for Regional Cooperation (SAARC), while Pakistan, Afghanistan, the Central Asian countries, Azerbaijan, Turkey and Iran are members of the Economic Cooperation Organization (ECO). To the southeast Papua New Guinea and Timor-Leste are contiguous with Indonesia and the three countries are neighbours of Australia, while including New Zealand in this group provides a link across Polynesia. This last link suggests that the Pacific Ocean itself may be a bridge, which is reflected in the concept and composition of APEC.

chains within East Asia when it invested heavily in Southeast Asia after the yen's post-1985 appreciation. Intraregional trade and investment in East Asia began to increase rapidly during the 1990s, and by 1996 intraregional trade accounted for 50% of the East Asian countries' total trade, compared to about a third at the start of the 1980s.¹⁸⁾

As Asian incomes and demand rose, regional markets became more important.¹⁹⁾ At the same time regional value chains began to emerge, a pattern documented in the "Emerging Asian Regionalism" project (ADB, 2008).²⁰⁾ Regional networks became denser in the 1990s and China played an increasingly central role.²¹⁾ Intra-industry trade (IIT) increased rapidly; Kimura, Takahashi and Hayakawa (2007), Haddad (2007) and Gruenwald and Hori (2008) provide evidence that Asian IIT is vertical intra-industry trade associated with fragmentation of production rather than the horizontal intra-industry trade due to product differentiation observed in Europe.²²⁾ Input-output analysis of the destination of Asian exports of final goods reinforces the conclusion that the region still relies on markets beyond the region.²³⁾

¹⁸⁾ The share of intraregional trade in total exports dipped after the Asian Crisis, but climbed back to 52% in 2004, when the import share was 57% (Munakata, 2006, p. 47). These are higher than equivalent measures for NAFTA and similar to those for the EU in the mid-1980s. Trade intensity indices also show increasing trade within the East Asia region during the 1990s (Sohn, 2002; Ng and Yeats, 2003). This section draws on material analysed in greater depth in Pomfret (forthcoming).

¹⁹⁾ The increased regionalization of the East Asian economy is described in Frankel and Kahler (1993), Hatch and Yamamura (1996), Aggarwal and Morrison (1998, pp. 65-86), Lincoln (2004, pp. 42-113), Munakata (2006, pp. 37-61), Rajan (2006) and Dean and Lovely (2008).

²⁰⁾ Ando and Kimura (2005) calculate very high shares of machinery (HS84-92) in East Asian countries' trade in 1996 and 2000, and conclude that this structure is especially suited to production fragmentation. Pomfret (forthcoming) discusses the emergence of regional value chains in East Asia in greater depth.

²¹⁾ Gaulier, Lemoine and Ünal-Kesenci (2006) and Athukorala (2007) emphasize China's growing role in this process.

²²⁾ Fragmentation is analysed in Arndt and Kierzkowski (2001). Xing (2007) calculates intra-industry trade, IIT (measured at the 3-digit SITC level), to have accounted for 6% of China's bilateral trade with Japan in 1980, 18% in 1992 and 34% in 2004 and finds that Japanese foreign direct investment performed a significant role in enhancing IIT. Zhang *et al.* (2005) have comparable estimates.

²³⁾ Pula and Peltonen (2009) estimate that only 7% of emerging Asia's GDP was ultimately

The emergence and rapid growth of regional value chains created pressures for trade facilitation because fragmentation of the production process is only profitable if the cost of moving components across borders is low in terms of both money and time. In the pre-1990 setting there was no pressure for preferential tariff reductions within an RTA, because East Asian countries were not selling within the region, and indeed the import-competing industries opposed reduction in their protection whether the liberalization was preferential or multilateral. With production fragmentation and the emergence of regional value chains, the pressures were for trade facilitation.²⁴⁾ Small tariffs were irrelevant; what mattered was the absence of delays and unexpected costs when crossing borders.

These pressures were in the 1990s addressed predominantly by national measures such as improved customs administration. Sometimes there was bilateral cooperation as between Singapore and Johor (Malaysia) and between Singapore and Riau (Indonesia) to facilitate trade within the Sijori subregional zone. ASEAN provided a forum for setting regional standards for integrated border management. Although trade facilitation consisted of many discrete measures of unknown individual impact, there is strong evidence that during the 1990s trade costs within ASEAN fell faster than in other parts of the world (Pomfret and Sourdin, 2009; Shepherd and Wilson, 2008). Measures to promote supply chain integration in specific sectors such as information and communications technology and the deepening of

sold as exports to another emerging Asia country, while 22% went to the USA, EU and Japan. Exposure to external markets was highlighted in 2008 when East Asia experienced little financial contagion from the crisis in the USA, UK and elsewhere, but suffered from reduced import demand in the crisis economies.

²⁴⁾ Baldwin (2006) sees the recent Asian trade agreements posing a threat to intra-regional trade. He diagnoses Asian regionalism as suffering from the “Noodle Bowl Syndrome” and argues that these complex and undisciplined trade agreements will disrupt “the smooth functioning of ‘Factory Asia’ ... [which is dependent on] ... the free flow of intra-regional trade”. This argument fails to explain why the agreements have proliferated since the late 1990s. Baldwin ascribes the proliferation to a “big-hearted gesture” from China to assuage ASEAN fears of Chinese competition and the domino effect that followed the China-ASEAN FTA, but China (like most economic powers) is not noted for big-heartedness and freeing up bilateral trade would exacerbate any fears that ASEAN countries might have harboured.

ASEAN integration towards formation of an ASEAN Economic Community by 2015 continues this pattern in the twenty-first century.²⁵⁾

Similarly, the ASEAN-China FTA was a response to the increasingly central role played by China in regional value chains that involved a subset of ASEAN countries. The accelerated pace and broad scope of China-ASEAN negotiations in the early years of the twenty-first century reflected the growth of regional value chains involving China and Southeast Asian nations and the corresponding need to reduce trade costs. The bilateral and plurilateral trade agreements are hard to classify, but preferential tariff rates are not the centrepiece and the terms are more commonly aimed at addressing specific concerns about trade costs. The ASEAN-Australia-New Zealand FTA (AANZFTA) signed in February 2009, for example, has a very short chapter on tariffs, and country-specific schedules for tariff reductions, while the other twelve chapters concern measures to improve the environment in which trade occurs, with improved customs procedures, smoother quarantine processes, more transparent rules and regulations, the alignment of standards and so forth. The bilateral agreements are often scoffed for failure to reduce tariffs and for claiming to be WTO-Plus, but the latter label is accurate insofar as the agreements address trade facilitation measures which have not been part of past rounds of WTO multilateral trade negotiations, and are only weakly represented on the Doha agenda.

5. FUTURE PROSPECTS

In sum, there has been considerable activity aimed at reducing trade costs in East Asia. Some of this is in a broad Asia-Pacific context, but most determinedly it has centred on ASEAN since the mid-1990s and

²⁵⁾ In many key sectors tariffs are not an issue. Much of the shipping of electronics components that dominates, for example, Korea-China trade is covered by the multilateral Information Technology Products Agreement signed at the 1996 WTO Ministerial in Singapore. Moreover, import of intermediates is frequently exempt from duties as long as the product is eventually exported.

subsequently included China, and to a lesser extent Japan and Korea. This has coincided with increased regionalization of East Asian trade and the growing importance of regional value chains. The needs of participants in these value chains have driven unilateral, bilateral and regional moves to reduce trade costs.

When regionalism finally arrived in East Asia it centred on trade, but on trade facilitation rather than traditional trade policies. In this sense it is deep integration because it addresses issues of domestic administration and regulation that are beyond the scope of the first four stages of Balassa's taxonomy, but it is unlikely to encompass meaningful monetary integration in the near future. The width of Asian regionalism is likely to be determined by the geographical range of the regional value chains.

Finally, a distinctive feature of the new regionalism in Asia is its openness and essentially non-discriminatory nature. For example, although trade facilitation measures within ASEAN are agreed at a regional level or among a subset of members, improved documentation, port logistics and so forth reduce costs of trade with all partners; a Thai-Malaysian bilateral agreement to reduce border costs, e.g., by simplifying customs forms or having a one-stop process, is likely to benefit all traders crossing the Malaysian or Thai border. Thus the current wave of East Asian regionalism with its plethora of bilateral and plurilateral agreements is not creating an EU or NAFTA style of RTA with clear-cut external borders, but a less well-defined area of trader-friendly conditions centred on ASEAN and China but with malleable outer limits.

REFERENCES

- ADB, *Emerging Asian Regionalism: A partnership for shared prosperity*, Manila: Asian Development Bank, 2008.
- Aggarwal, Vinod and Charles Morrison, *Asia-Pacific Crossroads: Regime Creation and the Future of APEC*, New York: St. Martin's Press,

- 1998.
- Ando, Mitsuyo and Fukunari Kimura, "The Formation of International Production and Distribution Networks in East Asia," in Takatoshi Ito and Andrew Rose, eds., *International Trade in East Asia*, Chicago: University of Chicago Press, 2005, pp. 177-213.
- Athukorala, Prema-chandra, "The Rise of China and East Asian Export Performance: Is the crowding-out fear warranted?," *The World Economy*, 32, 2009, pp. 234-266.
- Balassa, Bela, *The Theory of Economic Integration*, Homewood, IL: Richard D. Irwin, 1961.
- Baldwin, Richard, "Managing the Noodle Bowl: The fragility of East Asian regionalism," CEPR Discussion Paper, No. 5561, London: Centre for Economic Policy Research, 2006.
- Corbett, Jenny and Evi Fitriani, "Australian Perspectives on the Road Map towards East Asian Economic Integration," *APEC Economies Newsletter*, 12(5), June 2008 (available at <http://www.crawford.anu.edu.au>).
- Dean, Judith and Mary Lovely, "Trade Growth, Production Fragmentation, and China's Environment," NBER Working Paper, No. 13860, 2008.
- Dieter, Heribert, ed., *The Evolution of Regionalism in Asia: Economic and Security Issues*, London: Routledge, 2007.
- Dieter, Heribert and Richard Higgott, "Exploring Alternative Theories of Economic Regionalism: From trade to finance in Asian co-operation?," *Review of International Political Economy*, 10(3), 2003, pp. 430-454.
- Estevadeordal, Antoni and Kati Suominen, "Sequencing Regional Trade Integration and Cooperation Agreements," *The World Economy*, 31(1), 2008, pp. 112-140.
- Frankel, Jeffrey and Miles Kahler, *Regionalism and Rivalry: Japan and the United States in Pacific Asia*, Chicago: University of Chicago Press, 1993.
- Gaulier, Guillaume, Françoise Lemoine, and Deniz Ünal-Kesenci, "China's

- Emergence and the Reorganisation of Trade Flows in Asia,” CEPII Working Paper, No. 2006-05, 2006, Centre d’Etudes Prospectives et d’Informations Internationales, Paris — revised version published in *China Economic Review*, 18, 2007, pp. 209-243.
- Grimes, William, *Currency and Contest in East Asia: The Great Power Politics of Financial Regionalism*, Ithaca, NY: Cornell University Press, 2009.
- Gruenwald, Paul and Masahiro Hori, “Intraregional Trade Key to Asia’s Export Boom,” *IMF Survey*, March, 45 - summary of chapter 4 of International Monetary Fund, *Asia and Pacific Regional Outlook*, October 2007, 2008.
- Hatch, Walter and Kozo Yamamura, *Asia in Japan’s Embrace: Building a Regional Production Alliance*, Cambridge, UK: Cambridge University Press, 1996.
- Hedi Bchir, Mohamed and Michel Fouquin, “Economic Integration in Asia: Bilateral Free Trade Agreements versus Asian Single Market,” CEPII Working Papers, No. 2006-15, Paris, October 2006.
- Helble, Matthias, Ben Shepherd, and John Wilson, “Transparency and Regional Integration in the Asia Pacific,” *The World Economy*, 32(3), 2009, pp. 479-508.
- Kawai, Masahiro and Ganeshan Wignaraja, “ASEAN+3 or ASEAN+6: Which Way Forward?,” ADB Institute Discussion Paper, No. 77, September 2007.
- Kimura, Fukunari, Yuya Takahashi, and Kazunobu Hayakawa, “Fragmentation and Parts and Components Trade: Comparison between East Asia and Europe,” *North American Journal of Economics and Finance*, 18(1), 2007, pp. 23-40.
- Kwei, Elaine, “Chinese Trade Bilateralism: Politics still in command,” in Vinod Aggarwal and Shujiro Urata, eds., *Bilateral Trade Agreements in the Asia-Pacific: Origins, evolution, and implications*, London: Routledge, 2006, pp. 117-139.
- Lee, Hyun-Hoon, Chung Mo Koo, and Euijeong Park, “Are Exports of China,

- Japan and Korea diverted in the Major Regional Trade Blocs; Why and whither?," *The World Economy*, 31, 2008, pp. 841-860.
- Lee, Jong-Wha, Innwon Park, and Kwanho Shin, "Proliferating Regional Trade Arrangements; Why and whither?," *The World Economy*, 31, 2008, pp. 1525-1557.
- Lincoln, Edward, *East Asian Economic Regionalism*, Washington, D.C.: Brookings Institution Press, 2004.
- Manchin, Miriam and Annette Pelkmans-Balaoing, "Clothes without an Emperor: Analysis of the preferential tariffs in ASEAN," *Journal of Asian Economics*, 19, 2008, pp. 213-223.
- Menon, Jayant, "Bilateral Trade Agreements," *Asian-Pacific Economic Literature*, 21(2), 2007, pp. 29-47.
- Munakata, Naoko, *Transforming East Asia: The evolution of regional economic integration*, Tokyo: Research Institute of Economy, Trade and Industry and Washington, D.C.: Brookings Institution Press, 2006.
- Ng, Francis and Alexander Yeats, "Major Trade Trends in East Asia: What are their implications for regional cooperation and growth?," World Bank Policy Research Working Paper, No. 3084, June 2003.
- Pomfret, Richard, "Sub-Regional Economic Zones," in Bijit Bora and Christopher Findlay, eds., *Regional Integration and the Asia Pacific*, Melbourne: Oxford University Press, 1996, pp. 207-222.
- _____, *The Economics of Regional Trading Arrangements*, Oxford: Clarendon Press, 1997 (paperback edition with new Preface, Oxford: Oxford University Press, 2001).
- _____, "Sequencing Trade and Monetary Integration: Issues and application to Asia," *Journal of Asian Economics*, 16(1), 2005, pp. 105-124.
- _____, "Is Regionalism an Increasing Feature of the World Economy?," *The World Economy*, 30(6), 2007, pp. 923-947.
- _____, "Regional Value Chains and Asian Regionalism" in Christopher Findlay," in Mari Pangestu and David Parsons, eds.,

- Light the Lamp: Papers on world trade and investment in memory of Bijit Bora*, Singapore: World Scientific, forthcoming.
- Pomfret, Richard and Patricia Sourdin, "Have Asian Trade Agreements reduced Trade Costs?," *Journal of Asian Economics*, 20(3), 2009, pp. 255-256.
- Pula, Gabor and Tuomas Peltonen, "Has Emerging Asia Decoupled? An analysis of production and trade linkages using the Asian International Input-Output Table," ECB Working Paper, No. 993, European Central Bank, Frankfurt, 2009.
- Rajan, Ramkishan, "Asian Regionalism: A Symposium," *The North American Journal of Economics and Finance*, 17, 2006, pp. 231-302.
- Sen, Rahul, *Free Trade Agreements in Southeast Asia*, Singapore: Institute of Southeast Asian Studies, 2004.
- Severino, Rodolfo, "Regional Institutions in Southeast Asia: The First Movers and their Challenges, paper prepared for the Asian Development Bank project," *Institutions for Regionalism: Enhancing economic cooperation and integration in Asia and the Pacific*, presented at a workshop in Jakarta on 9-10 June 2009.
- Shepherd, Ben and John Wilson, "Trade Facilitation in Southeast Asia: Measuring progress and assessing priorities," World Bank Policy Research Working Paper, No. 4615 (forthcoming in *Journal of Asian Economics*, 2008).
- Sohn, Byeong Hae, "Regionalization of Trade and Investment in East Asia and Prospects for further Regional Integration," *Journal of the Asia Pacific Economy*, 7(2), 2002, pp. 160-181.
- Xing, Yuqing, "Foreign Direct Investment and China's Bilateral Intra-Industry Trade with Japan and the US," *Journal of Asian Economics*, 18(4), 2007, pp. 685-700.
- Zhang Jianhong, Arjen van Witteloostuijn, and Chaohong Zhou, "Chinese Bilateral Intra-Industry Trade: A Panel Data Study for 50 Countries in the 1992-2001 Period," *Review of World Economics (Weltwirtschaftliches Archiv)*, 141(3), 2005, pp. 510-540.