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ASEAN-U.S. ECONOMIC RELATIONS

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ASEAN-U.S. ECONOMIC RELATIONS

Changes in the Economic Environment and Opportunities

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Foreword

The ASEAN Economic Research Unit (AERU) of the Institute of Southeast Asian Studies (ISEAS) was formed in 1979 to promote research and critical thinking and debate on the economics and related political issues of ASEAN. Priority areas identified for research and discussion include investment, industry, and trade; finance and monetary aspects; food, energy, and commodities; transportation/shipping; and political factors in ASEAN economic co-operation. Within these, work relating to ASEAN economic relations with its main trading partners and sources of investment has been most prominent, including the project on "ASEAN-U.S. Economic Relations".

This project has been designed as a three-year undertaking with each year focusing on a distinct but related aspect of the economic links between ASEAN and the United States. The theme for the first year was "The Current State of ASEAN-U.S. Economic Relations". For this, eight papers were commissioned and presented at a workshop on 22-24 April 1985 in Singapore. They covered patterns of trade between ASEAN and the United States; U.S. investment in ASEAN; transfer of technology by U.S. transnational corporations and contractual arrangements; ASEAN manufactured exports to the United States; U.S. exports of goods and services to ASEAN; the impact of U.S. policy mix on the ASEAN economies.

Summaries of these papers were published as a monograph, *ASEAN-U.S. Economic Relations: An Overview* edited by Agustin Kintanar, Jr. and Tan Loong-Hoe. The revised papers themselves were subsequently published in full in the November 1986, March 1987, and November 1987 issues of the Institute's journal, *ASEAN Economic Bulletin*.

The research during the second year of the project focused on "Changes in ASEAN-U.S. Economic Environment: Constraints and Opportunities". Eight papers again were prepared. They examined the following topics: economic trends in the United States and their implications for ASEAN; increasing protectionism and its implications for ASEAN-U.S. trade and investment in services; U.S.-Thai relations: selected case studies in agribusiness; and, the role of U.S. official development assistance in ASEAN.

These papers were discussed at a workshop in San Francisco jointly organized by the Institute and The Asia Foundation's Center for Asian Pacific Affairs (CAPA). The Asia Foundation established the Center in its San Francisco headquarters in 1985 with the goal of promoting communication and strengthening relations between the United States and nations of Asia and the Pacific. This volume is based on the papers discussed at this workshop.

The Institute and CAPA received assistance from several institutions during the workshop and the preparation of this volume. Both the Institute and CAPA would like to acknowledge their appreciation of such help. They are grateful to The Asia Foundation for the financial support for the project as a whole, as well as to the researchers and editors for their contributions and *co-operation* in expediting the publication process. Responsibility for the accuracy of statements made rests exclusively with the editors and the individual authors.

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Changes in the ASEAN-U.S. Economic Environment and Opportunities: An Introductory Overview

*Tan Loong-Hoe and
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Addressing the 20th ASEAN Ministerial Meeting on 15 June 1987 in Singapore, Singapore's Premier Lee Kuan Yew outlined the major changes ASEAN countries were undergoing against a backdrop of four Pacific powers — the United States, Japan, China, and the Soviet Union — and made two observations which are particularly pertinent to the discussion here. First, on the optimism in ASEAN's economic future, he said "sooner or later, the world economy will enter a new cycle of growth and prosperity. We would do well to restructure our economies and prepare ourselves for this next surge of high economic activities . . ." Second, with reference to the United States, Mr Lee added that it was in ASEAN's interest to have the U.S. quickly regain its competitiveness and become once again a creditor rather than a debtor nation. The challenge for the United States is to muster the political will to resolve the root causes of its huge budget and trade deficits (*Straits Times*, 16 June 1987).

The papers in this volume address the changes in the ASEAN-U.S. economic environment and opportunities. To explore this theme in a more focused and systematic way, the volume is divided into four parts. Part I considers the broad trends of recent economic performance of the United States and the problem of increasing protectionism. The implications and consequences of these trends on ASEAN or ASEAN-U.S. economic relations are also examined. Part II analyses the structural adjustments both in the developed country, i.e., the United States, and in the developing countries in ASEAN. It examines the comparative advantage of ASEAN countries and how they should respond to likely changes of industrial and trade policies in general, and those of the U.S. in particular. Part III provides analyses of U.S.-ASEAN trade in services, both from the U.S. and ASEAN viewpoints, and includes discussions of past experience in the light of future directions. Similarly, Part IV examines the role of private enterprise in the development of U.S.-ASEAN economic relations, with illustrations of selected American and Thai agribusiness firms operating in Thailand.

Economic Trends

In Chapter 1, Lawrence Krause's study identifies and analyses the main trends

of structural changes which have had an impact on the performance of the U.S. economy during the 1980s, namely: the shift in the composition of consumption, the decline in the overall growth of productivity, and the evolution of the U.S. comparative advantage. This unfolding of events over the 1980-85 period had ramifications in the ASEAN countries. The most salient event was the rapid expansion of demand in the U.S. when the rest of the world was stagnating. During the 1980-85 period, U.S. imports from ASEAN increased by more than 20 per cent in value terms. Indeed, the notable performance of several ASEAN countries in the export of manufactures was largely because of increased sales to the United States.

Because of their outward orientation, ASEAN countries have a large stake in seeing the United States solve its trade deficit difficulties. The solution of choice, from an ASEAN viewpoint, would be the expansion of U.S. exports. Exchange rate adjustment leading to a further devaluation of the dollar would be the second best solution. Dollar devaluation would facilitate the recovery of the dollar-price of commodities which ASEAN countries export; and would speed up the substitution of American products for Japanese and European goods in ASEAN and other markets. ASEAN countries should also attempt to replace European and Japanese products in the U.S. market. They should also redirect their marketing efforts to other countries to achieve increasing market diversification.

A third and clearly less desirable solution to the U.S. trade deficit would be a U.S. recession — the expenditure reduction approach instead of the expenditure switching method of adjustment. Reduced imports would have depressing effects on ASEAN and other countries. Besides, a U.S. recession would intensify protectionist pressures in the United States and might possibly lead to comprehensive import restraints.

Finally, Krause makes the observation that it is most improbable the United States will continue to be the defender of the international trade and monetary regimes. The far-reaching, but uncertain consequences of these regime changes can stimulate the most productive efforts in turning them into developmental opportunities.

Burnham Campbell and Dean DeRosa's contribution in Chapter Two is a comprehensive examination of the nature and extent of the trend of increasing protectionism and its implications for ASEAN-U.S. economic relations. Their analyses of the evidence of changes in protection both in ASEAN and in the United States and their effects on ASEAN-U.S. trade also contain thorough account of why protectionism may be on the rise in the United States and ASEAN. Their findings and conclusions are discussed very extensively with reference to the larger key issues and problems including the U.S. government deficit, the debt problem, U.S.-EEC agricultural subsidy conflict, demographic transition, and the rapid technological changes — all of which bear importantly in diverse ways on the problem of increasing protectionism and its impact on ASEAN-U.S. relations in trade and beyond trade.

Based on the analyses of data (compiled from sources including UNCTAD, USTR, and ADB) mainly for the 1970 to 1982 (or 1984) period, Campbell and DeRosa arrived at two major conclusions: first, increased U.S. protection against

ASEAN exports is modest when compared with increased U.S. protection against South Korea, Taiwan, and Japan. Second, increased protectionism, either enforced by the United States or the ASEAN countries, has not had an obviously measurable effect on U.S.-ASEAN trade.

With regard to the optimal or desirable current policies in response to increased protection, Campbell and DeRosa suggest that ASEAN can choose any or all of the following options in response to increased U.S. protection:

- Option 1. borrow more;
- Option 2. encourage direct foreign investment;
- Option 3. cut imports by (a) reducing income, (b) raising trade barriers;
- Option 4. expand exports by (a) depreciation, (b) subsidies, (c) block trading;
- Option 5. increase regional trade by forming a customs union (diverting trade from U.S.);
- Option 6. bargain for a roll-back by
 - (a) offering option (2), (b) offering not to do option (3b),
 - (c) opening up the service sector,
 - (d) recognizing patent and copyright rights.

To attain a politically acceptable open economy, a "wise" ASEAN government would choose option (4a) and option (6); option (5) would be second best.

Structural Adjustments

Chapters 3 and 4 present two different views on the issues of structural adjustments in ASEAN and the United States, and to a much lesser extent the interactions between them. While Jesus P. Estanislao examines the structural adjustment in ASEAN, Wing Thye Woo poses the theme-question: What kind of structural adjustment policies are needed to remedy the U.S. trade difficulties?

"Structural Adjustment", according to Estanislao, refers to the shifting of factors of production to alternative uses in response to changes in technology, consumer preferences, and international competitiveness. It is not only a principle for trade policy but also an inevitable and necessary part of the process of economic growth. However, as a result of external shocks or inappropriate domestic policies, structural adjustment may be made urgent.

Over the past decade, the external shock waves jolting the ASEAN economies have been: world inflation, two sharp oil price increases, and subsequent recessions in the industrialized countries (particularly in the United States). These extra-regional shocks generated two notable effects on the economies of ASEAN:

1. Serious deterioration of their terms of trade: higher oil prices substantially raised the import bills of oil-importing countries (the Philippines and Thailand). Simultaneously, prices of primary commodity exports of developing countries fell more markedly than the prices of capital and manufactured goods of the industrialized countries.
2. The volume of ASEAN exports declined as a consequence of recession-induced falling incomes and the reduction of aggregate demand in the

industrialized countries because of both recession and heightened protectionism especially in the United States.

The ASEAN countries have used four types of structural adjustment (as defined above) policy-responses to the difficult, if not challenging, external economic environment, i.e., the external shocks:

- (a) export market penetration, which involves efforts to increase and diversify a country's exports to pay for a higher import bill;
- (b) import substitution, involving the replacement of a significant amount of imports with domestic products;
- (c) reduction of demand and imports by lowering overall economic growth rate through monetary and fiscal policies;
- (d) expansion of net external borrowing.

Theoretically, these options of structural adjustment can possibly be pursued independently; in practice most governments implement programmes which combine these four approaches. However, the extent of structural adjustment achieved through (a), (b), and (c) determines the last form of adjustment (d).

Another observation underlined by Estanislao is that for the ASEAN countries, rising protectionism (especially originating from the United States) impedes efforts to undertake effective structural adjustments. However, he sounds a warning note that "the greatest danger to ASEAN's structural adjustment efforts is not protectionism from outside but protectionism from within ASEAN". He calls for trade liberalization within the region, which can stimulate competition and development of new structures of comparative advantage bringing benefit to the region in the long term. He stresses that ASEAN economic co-operation and integration will lead to intra-ASEAN trade expansion and possibly the emergence of a more efficient international division of labour.

The future growth and prosperity of ASEAN will continue to be largely dependent on the role and performance of the OECD countries (especially the United States) not only as suppliers of capital and technology for ASEAN industries but more importantly as major markets of ASEAN exports. This hinges upon the nature of structural changes and adjustments in the OECD in general and the United States in particular. And on this matter we turn to Wing Thy Woo's contribution.

Woo's contribution examines: the displacement of labour by free trade and the performance of U.S. Trade Adjustment Assistance programmes; the effects of foreign industrial targeting on the growth and competitiveness of U.S. high-tech industries; the role of exchange rate in trade deficits; and the policy alternatives to industrial policies.

The major observations or conclusions drawn from Woo's studies are the following:

1. Evidence suggest that labour is *not* increasingly concentrated in industries with low productivity growth potential. Foreign trade generated growing employment opportunities in the high-tech industries in the 1970s. The fear that trade has contributed to create a sectoral distribution of labour threaten-

ing improvement in living standards is unfounded. Hence, undoubtedly, the United States is capable of maintaining comparative advantage in activities that can pay high wages.

2. Foreign industrial policies, already pursued by U.S. competitors since the 1950s, are not responsible for the present U.S. trade problems. Woo's findings indicate that secular forces did not cause the U.S. trade deficits of the 1980s. As of 1980, there is no significant evidence that labour has been increasingly shifted to low-wage industries, or that the composition of U.S. efforts has become more low-tech compared to the other major developing countries. Indeed, there is no systematic decline in U.S. competitiveness.
3. The most prominent of the many factors influencing the U.S. trade account balance include changes in domestic and foreign trade barriers; the difference between U.S. income growth rate and that of foreign countries, and real exchange rate. Woo's analysis demonstrates that U.S. trade problems of the 1980s are caused primarily by appreciation of the dollar and not foreign industrial targeting policies.

As to the appropriate structural adjustment policies to alleviate U.S. trade difficulties, Woo offers three recommendations

- (i) Eliminate the structural budget deficits through a macro-economic policy mix. Cut back public borrowing, which would lead to an easing of monetary policy to replace the fiscal stimulus causing the exchange rate to depreciate.
- (ii) Concentrate on lowering the foreign trade barriers to the exports of America's most productive sector — agriculture. The Pacific Rim (including ASEAN) countries are experiencing a substantial increase in the demand for food in consequence of rapidly growing population and the surge in incomes. The overvalued exchange rate should be dealt with to enhance the promotional effectiveness of U.S. agricultural products in the ASEAN and the Pacific Rim markets.
- (iii) Seek bilateral reduction of trade barriers rather than multilateral trade negotiations within GATT. The quid-pro-quo approach could be encouraged as ASEAN and the Pacific Rim developing countries are most concerned with greater access to the U.S. market, and the two main trade priorities of the U.S. are the reduction/elimination of trade barriers to agricultural and service exports. From the ASEAN viewpoint, this idea of quid-pro-quo in ASEAN-U.S. trade relations is also suggested by Lee (Tsao) Yuan's study on trade in services (as discussed below).

Trade and Investment in Services

The two contributions in Chapters 5 and 6 complement one another, by providing different perspectives, one from the ASEAN side and the other from the American side, to this "surge of interest in services and services trade" in the 1980s.

In the context of ASEAN-U.S. relations, Lee (Tsao) Yuan's contribution assesses the U.S. position in the international transactions in services, and the ASEAN position as enunciated in the GATT meeting at Punta del Este in September 1986. However, Chung H. Lee & Seiji Naya's paper is more concerned with issues relating to the internationalization of U.S. service industries and ASEAN's place in that process; the service transactions (trade and investment) between the U.S. and the ASEAN countries; and highlighting the barriers to these transactions encountered in ASEAN by U.S. service industries.

In reporting the findings and conclusions of their studies, Lee (Tsao) Yuan and Chung H. Lee & Seiji Naya underscore the point of serious data constraints in the study of trade and investment in services in general and ASEAN-U.S. bilateral relations in particular.

The empirical analyses from both contributions provide the following findings:

1. that U.S. direct investment in services in ASEAN in 1979 was US\$4 billion, but by 1983 it had grown two times to US\$8 billion. Even then it amounted to only 4 per cent of total U.S. investment in 1983.
2. ASEAN countries are not a major market for U.S. services exports and direct investment in services. Except for Singapore, the other ASEAN countries are net importers of services and probably have a balance of services deficit *vis-à-vis* the United States. Singapore enjoyed a significant increase in service export during the 1979-83 period.
3. For Indonesia, Malaysia and Thailand, tourism may be the most important services export. But there may still be a net deficit with respect to the United States.
4. Investment income flows to the United States are probably large relative to the rest of the other items in the balance of services.
5. Regarding the important issue of barriers to trade and investment in services, Chung & Naya's study in particular noted that most barriers are investment-related and constituted serious obstacles or difficulties in establishing and operating U.S. affiliates in ASEAN especially in the banking, insurance, and advertising industries. But some of these barriers are trade-related as in the case of quotas on film imports affecting the motion-picture industry.

The conclusions then are that services exports are more important to the United States than to the ASEAN countries (Indonesia, Malaysia, the Philippines, and Thailand except Singapore); and that the pattern of the service trade of the ASEAN 4 appears to be roughly similar to that of developing countries in general, i.e., services trade deficit with respect to the United States with a sizeable proportion of investment income payments also flowing into the United States.

Concerning the issue of liberalization of services trade and investments, from the ASEAN viewpoint, Lee (Tsao) Yuan makes the following observations:

1. The American initiative in pushing for trade liberalization in the services sector is important and potentially beneficial for all countries concerned. The ASEAN 4 (Indonesia, Malaysia, the Philippines, and Thailand) in particular would probably gain from freer trade in services. However, the

quantum of gains from the United States is a matter of uncertainty.

2. A politically feasible option to stimulate the growth of U.S. trade and investment in the services sector in ASEAN would be for ASEAN countries to negotiate for a quid pro quo in exchange for the lowering of barriers to trade and investment in services in ASEAN countries.

From an American perspective, Chung & Naya offer the following observations:

1. The United States would like barriers in services trade and investment in ASEAN countries to be substantially reduced or even eliminated. The U.S. stand appears to have been very much influenced by certain self-interest of services industries including banking, insurance, and "telematics".
2. Liberalization of ASEAN services industries is likely to have greater impact on ASEAN economies than on the U.S. economy as ASEAN constitutes a relatively small market for U.S. service industries.
3. The benefit to the U.S. will be the probable improvement in allocative efficiency as it permits the expansion of those industries in which the Americans do have comparative advantage.
4. For ASEAN, liberalization will do more than enhance allocative efficiency. The reason is that internationally transacted services, especially those provided by foreign affiliates, tend to be producer services, and liberalization will reduce the prices of producer services industries. Hence, liberalization will reduce absolutely and relatively the prices of service-intensive commodities.
5. In recent years, certain U.S. service industries (e.g., professional and technical services) experienced rapid technological changes. As they embody state-of-the-art technology, their acquisition whether transferred through MNC affiliates or imported, constitutes a type of technology transfer. Indeed, as the continuing technological changes may have profound economic effects, such technology transfer may be more important than any other effect of liberalization of the service industries.

Role of Private Sector

The role of the private sector in ASEAN-U.S. economic relations in general (and U.S.-Thai economic relations in particular) is examined in Chapter 7 by Mingsarn Santikarn Kaosa-ard and Narongchai Akrasanee.

Using the case-study approach of analysis at the firm level, they argue that the U.S.-Thai relationship in the agribusiness "is not merely competitive but is multi-dimensional and this property should be exploited properly", for instance, in the rice industry. Prospectively, it may be fruitful to combine superior U.S. rice-based processing technologies and market development expertise with Thailand's comparative advantage of rice-growing in lower costs of labour and other inputs. However, if U.S. market access is restricted because of narrow protectionist reasons, the ability to purchase technology and repay external debts will be markedly curtailed. Also, the United States will be unable to find effective allies in countering the European Community's common agricultural policy.

Hence, based on their case analyses of six agribusinesses in industries including rice, agro-chemical products, tobacco, tapioca products and corn, canned pineapples, and canned tuna, Mingsarn S. Kaosa-ard & Narongchai suggest that both the United States and Thailand (and ASEAN as a whole) would definitely benefit from freer and fairer agricultural trade as well as from the mutually beneficial combining of comparative advantage of the different techniques of production in the agribusiness.

Indeed, as they put it:

The story of U.S.-Thai economic relations need not be one of a zero-sum game as shown by the tendencies adopted by the U.S. Congress which has turned itself into the world's largest non-tariff barrier to trade.

In conclusion, they raise three points of observation or suggestion with reference to the growing protectionist or "neo-mercantilist" sentiment in the United States. First, ASEAN governments must unceasingly indicate in every possible way to the U.S. Congress and the Administration that such a mercantilist approach is economically short-sighted and will unleash increasingly disruptive effects on the social and political good relations nurtured over many years. Second, both losers in Thailand and in the United States should co-operate and work together to protect their own shared interests. The American population and taxpayers at large should be better informed that they should not mortgage their children's future for the benefit of inefficient American producers. Third, increasing efforts should be given to identify areas of complementarity between the Thai/ASEAN and U.S. agricultural sector, at the same time minimizing the areas of competitiveness or conflict in trade.