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# AFTA

## *The Way Ahead*

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# AFTA

## *The Way Ahead*

*edited by*  
**Pearl Imada and Seiji Naya**

**SEAS** ASEAN Economic Research Unit  
INSTITUTE OF SOUTHEAST ASIAN STUDIES

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## ***Preface***

This volume of collected writings on ASEAN is in honour of Professor Kernial Singh Sandhu, *Director of ISEAS for 20 years since 1972*. His sudden death on 2 December 1992 was truly a great loss to all of us. A few days before his demise, Professor Sandhu, Dr M. Sadli and I attended an IDRC conference, which Kernial helped organize, in New Delhi and Bombay to look at how India can learn from the success stories of the Newly Industrialized Economies (NIEs) and member countries of the Association of Southeast Asian Nations (ASEAN). He is remembered as a person with incredible energy and enthusiasm, bringing together technocrats, government officials, and scholars to promote and foster regional consciousness, an outlook captured aptly in the phrase "Southeast Asian studies for Southeast Asians". He is a key figure in linking the Asian intellectual community with their counterparts all over the world.

Professor Sandhu devoted his professional life to working tirelessly to propel greater ASEAN co-operation. His dream was to see active regional co-operation and economic integration in ASEAN. Through annual ASEAN Roundtables, he gathered together officials, scholars and business people to examine the problems and prospects for ASEAN co-operation. His efforts were not in vain; in January 1992, ASEAN countries agreed to form an ASEAN Free Trade Area (AFTA). The papers in this volume were presented at the ASEAN Roundtable "25 Years of ASEAN — AFTA: The Way Ahead" that was held in Singapore, 3–5

September 1992. This volume — unlike past volumes where the concern was on what ASEAN should do to achieve greater economic cooperation — is most appropriate and timely for it deals with how ASEAN should proceed to achieve the goals of AFTA in 15 years.

Professor Sandhu led the Institute of Southeast Asian Studies (ISEAS) for 20 years and was the first Asian director of the institute since its inception in 1968. I knew him for 15 years as he often invited a few outsiders like myself to work with him on ASEAN-related issues. I am honoured to have worked jointly with him in urging ASEAN to take the steps toward greater economic integration. AFTA came into being not by accident, but through the hard work and sheer determination of men like Professor Sandhu, who are always giving it the needed push to move forward. In the process, he has turned ISEAS into a world-recognized institution, attracting technocrats, scholars, and officials not only from Asia but also North America, Europe, Latin America, and Africa.

Finally, on behalf of my co-editor, Dr Pearl Imada, I would like to thank all the writers and participants in the Roundtable who contributed to this volume to chronicle the compelling issues facing ASEAN countries as they meet the challenges of the 1990s and beyond. The generous financial support of the Konrad Adenauer Foundation is gratefully acknowledged. We would also like to extend our appreciation to Joseph Tan for his substantial contribution, and Janis Togashi for her excellent editorial assistance.

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18 December 1992

## ***Introduction: In Search of Success for AFTA***

The Association of Southeast Asian Nations (ASEAN) has announced that it will create a free trade area in 15 years. This decision, made in January 1992 at the Fourth ASEAN Summit, is seen as a bold decision, despite the fact that ASEAN is regarded as one of the most successful regional groupings among developing countries. All of the papers in this volume agree that although ASEAN's accomplishments in the political arena have been significant, its achievements in the area of economic co-operation have been limited. Neither its preferential trading arrangements nor its attempt at industrial co-operation have done much to increase intraregional trade and investment. In fact, until a few years ago, open discussion of the possibility of a free trade area was discouraged by ASEAN leaders.

What are the factors responsible for the remarkable transformation? And will ASEAN be able to integrate their economies although other developing countries generally have not? Are there any changes in the institutional structure of ASEAN that will contribute to the success of the ASEAN Free Trade Area (AFTA)? What actual mechanisms are being used and are these appropriate and workable? These questions are discussed in the papers in this volume and at the annual ASEAN Roundtable where they were first presented.

In answering these questions, it is appropriate to start with Rolf J. Langhammer's contribution entitled, "Shaping Factors and Business

Conditions in the Post-Fourth ASEAN Summit Period". The paper provides a comprehensive panorama of the international political economy and ongoing developments — exogenous and endogenous "shaping factors" — that are impinging on rapid economic changes within the ASEAN region. Global and social economic issues including the increasing trend toward regional rather than multilateral trading systems, world-wide disarmament, capital shortages in the world economy, new markets in Eastern Europe and former Socialist Asia, international migration, environmental problems, and technological innovations in communication industries, have all had an effect on ASEAN. Regional economic and political issues include a systematic consideration of China's economic liberalization, changes to ASEAN's internal cohesion, and the equity and efficiency dilemma facing ASEAN policy-makers. Langhammer's major conclusion is that the ASEAN private sector, as well as the government, should take the lead in dealing with these shaping factors. He adds that regional co-operation and integration policies within the ASEAN framework should provoke pragmatic innovations from private sector efforts. The performance, indeed the very survival and prosperity of the private sector, are dependent upon their adept and efficient response to the opportunities within the international market.

While Langhammer describes the broadest picture of the shaping factors and challenges confronting the ASEAN region, Narongchai Akrasanee and David Stifel concentrate more narrowly on "The Political Economy of the ASEAN Free Trade Area". They briefly discuss the emergence of a new environment in Southeast Asia, and the changing perceptions of the governments and private sectors of the costs and benefits of regional economic co-operation and integration in ASEAN. Like Langhammer, they recognize the crucial role of foreign direct investment (FDI) and the globalization of production by multinational firms, and of the pressures upon ASEAN arising from the emerging Single Singapore European Market 1992 and the North American Free Trade Area (NAFTA) in stimulating the adoption of economic liberalization policies and growth strategies amongst the ASEAN countries. Their key question, however, is a politico-economic one: is AFTA an aberration from the slow and reluctant progress of ASEAN economic co-operation over the past 25 years? In answering the question, they suggest that economic co-operation and integration is becoming less of a political burden or constraint to ASEAN leaders and therefore may attenuate problems relating to weak political will which has slowed

ASEAN economic co-operation in the past. Using an argument based on the politico-economic dynamics of interests groups and lobbies, they depict ASEAN leaders as being engaged in a “situation in which all can gain through co-operation; if one party pursues its narrow national interests outside of a regional context, however, the others may lose relatively and absolutely”. At the micro level, they find diminishing resistance from many urban-based industrialist coalitions supporting AFTA because they have benefited from freer access to international markets and gained confidence in their abilities to compete in AFTA. Indeed, there has been a general shift in thinking, with the private sector making tangible moves away from import substitution. However, the strong agro-industrialist lobbies continue to fight to exclude their products from tariff reductions. Under this framework, Narongchai and Stifel conclude that effective implementation and the success of AFTA will depend on a few ASEAN countries — more specifically, they suggest Thailand and Malaysia — taking the initiative and leadership role.

Our paper, “The Long and Winding Road Ahead for AFTA”, concentrates on the mechanics of regional integration. The paper first examines the vision of AFTA and the diverse essential rules and measures that need to be considered in a free trade area, such as rules of origin and content; rules of competition and tariff reduction; the exclusionist and safeguard measure; dispute settlement; and AFTA. Then, we pose critical questions: what are the internal and external changing circumstances leading to the momentous breakthrough in the agreement to establish AFTA (and with a clear 15-year timetable)? What are the major obstacles that need to be cleared and issues that need to be resolved in the successful implementation of AFTA? We believe that the ASEAN nations have indeed taken an impressive step forward in strengthening their economic bonding with the commitment to establish AFTA. However, there are many substantive and technical matters that require immediate and careful attention, although these problems and difficulties are solvable. Among other things, we explicitly call for the creation of an “ASEAN Experts’ Convention” to be organized to promote consensus and adopt the necessary agreements to implement ASEAN’s “Free Trade Area Plus”, thereby enhancing ASEAN’s movement toward a higher level of regional co-operation and integration. In addition, we believe that AFTA will render ASEAN a greater cohesive force in its negotiations with other regional groupings and trading blocs as well as strengthen ASEAN’s collective position in its negotiations in the

ongoing Uruguay Round of GATT, given the fact that preservation of the multilateral system of international trade is precious to ASEAN.

A similar sentiment is shared by Sree Kumar in his contribution entitled, "Policy Issues and the Formation of the ASEAN Free Trade Area". Kumar's contribution identifies the various bottlenecks hindering the effective formation of AFTA and possible ways to get around these barriers. His analysis of ASEAN's trade and growth in recent years serves as useful background to evaluate the trade items in the proposed CEPT scheme and the structure of tariffs. Concrete views of the private sector interests in ASEAN on current issues facing intra-ASEAN trade are professed in fifteen corporate interviews. He observes that if ASEAN can surmount its narrow nationalist interests and move to dismantle some of the barriers to cross-border trade and investments, this would be confidence-enhancing for the private sector and improve their ability to take advantage of the opportunities presented by AFTA. Additionally, he recommends three measures which, if adopted, may do much to promote AFTA. First, the CEPT list should be increased considerably to generate more substantive intra-ASEAN impact. Second, non-tariff barriers to trade should be dismantled simultaneously with tariff cuts on a broader range of goods. A sector-by-sector approach should replace the present product-by-product approach to tariff reductions. Third, greater harmonization of investment policies amongst the ASEAN countries should be pursued. This point is consistent with, and reinforces, the advocacy of AFTA-Plus by Seiji Naya and Pearl Imada. Finally, Kumar calls for an effective system, for example institutional mechanisms for addressing the various problems and issues raised by the formation of AFTA, in order to enhance the credibility of the governments' commitment to AFTA in the eyes of the ASEAN private sector.

With the perspective of the next 10 to 15 years, Jacques Pelkmans comprehensively examines the institutional mechanism for ASEAN in general and AFTA in particular. He sets the stage by reviewing the recent institutional decisions of the Singapore ASEAN Summit and the Group of Five proposal concerning the strengthening of the structure and mechanism of ASEAN, with special reference to the ASEAN Secretariat. His cautious yet critical review leads him into a cut-and-thrust debate with the paper by Chng Meng Kng, who was also given fair and equal time to respond with his discussant's comments; this opened up new terrain for mutual clarification and agreement. Drawing from the strength of his expertise on EC integration, Pelkmans next positions

himself more dispassionately and addresses the fundamental question of what "policy functions" ASEAN might be expected to fulfil in the decade of the 1990s and beyond. He identifies eight policy functions which are carefully distinguished at four levels: national, intra-ASEAN, the dialogue partners level, and global. Specific to the institutional aspects of AFTA, he observes that "AFTA will fundamentally change ASEAN, economically, in terms of political economy, administratively and institutionally". For instance, he argues in detail that political economy and bargaining will tax the ASEAN institutions with such "core questions" as credibility with businesses, customs, procedures, legal security, and dispute settlement. In conclusion, he warns that even if ASEAN may be relatively uninterested in establishing a legal mechanism, and even less so in building a "litigation society", unless ASEAN is able to "come up with any other method, or variation of judicial review, to guarantee implementation so as to provide credibility to business the extent to actually realizing AFTA, and its gain, may turn into an anti-climax".

Other contributors agree that much remains to be done. Sree Kumar concludes that ASEAN should "unshackle itself from the pressures imposed by protected domestic industries". Otherwise, AFTA will remain "a fiction". We are more confident and sanguine about "the ASEAN way", which is consultative and less amenable to a legalistic framework. Nevertheless, ASEAN can do better. We also believe that the time has come for ASEAN to develop a formal, transparent, dispute settlement mechanism, so that the obligations of participating members are clear. The road ahead is long and winding, but there is much that ASEAN can do to ensure that the journey is smooth and the final destination is reached.