

Regional Economic Integration: The Challenges Ahead

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Beyond AFTA: Facing the Challenge of Closer
Economic Integration

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I should like, together with you, to trace the evolution of regional economic integration in ASEAN, examine its nature, define its current status, and put forward some views on what else needs to be done to advance its essential purposes; that is, as the title of this workshop suggests, what are today's challenges for closer economic integration in Southeast Asia.

In 1967, in this very city, ASEAN was founded for three interlocking and ambitious objectives — regional peace, stability and prosperity. From the beginning, economic co-operation was to be a key to achieving these goals. At the time, the Indochina war was raging. The Cold War was threatening to wipe out the hopes of Southeast Asia's people for a better life. Disputes among the nations of the region continued to unsettle it.

In these unpromising circumstances, the countries of Southeast Asia set their minds, their labours and their resources on the development of their economies. At the same time, it became increasingly clear that their national programmes for development and prosperity would be strengthened and made more effective by openness to and co-operation with the rest of the world, particularly and above all within the region. Economic co-operation would give each member of the new association a stake in the economic well-being of the others and thus serve as a potent force for regional peace. This was the logic of the European Communities and the European Common Market. Firmly locking their economies together would bind together the core nations of Europe so closely that the wars that had so ravaged the continent for centuries would be unthinkable in the future. At the same time, peace among nations and economic progress for their peoples would bring about a measure of stability that would make further development possible.

Thus, ASEAN laid down programmes of co-operation in industry, minerals and energy, in finance and banking, in transport and communications, in food, agriculture and forestry. The ASEAN countries

devised schemes like the ASEAN Industrial Projects and the ASEAN Industrial Joint Ventures. They set up the Preferential Trading Arrangements.

They used such programmes, schemes and arrangements not only to help their own national development efforts but also to build confidence among themselves, develop personal relationships among their leaders, and cultivate a sense of regional identity among their peoples.

AFTA is Born

After many years, they realized and decided that these tentative and modest measures for regional economic co-operation — nobody dared talk of economic integration in those days — were not enough. Looking to the future, the ASEAN leaders knew that these measures would not be enough to bring about the economic efficiencies and attract the investments essential for their countries' continued development.

At their fourth summit, in Singapore in 1992, ASEAN's leaders decided to move ASEAN to an entirely new stage in their countries' economic relations, to make the leap from co-operation to integration, by resolving to transform the region into a free trade area. In fifteen years, tariffs on goods traded within ASEAN, with some exceptions, would be eliminated or reduced to a maximum of 5 per cent. This commitment would be subject to legally binding schedules of tariff reductions. Most exceptions would be phased out according to fixed timetables.

The objective was to create an integrated ASEAN market for trade in goods. Such an enlarged market would attract investments much more effectively than the much smaller national domestic markets. It would thus be a further stimulus for growth. It would also raise, for ASEAN members, the stakes in one another's purchasing power and economic progress.

In four years, from 1993 to 1997, the value of intra-ASEAN trade almost doubled, from less than US\$44 billion to more than US\$85 billion, from less than 21 per cent to almost 25 per cent of total trade. Largely on account of the financial crisis, these figures dropped to US\$71 billion and 22 per cent in 1998, rising again in 1999. They are still well above pre-AFTA levels. This dramatic rise in intra-ASEAN trade cannot be attributed entirely to AFTA, of course, but AFTA's significance is such that many of the world's largest companies have displayed extraordinary interest in AFTA's progress.

If AFTA is good for ASEAN in economic and other terms, why wait for 2008 for its completion? Asking themselves this question, ASEAN's leaders, meeting in this city in December 1995, decided to advance AFTA's completion date to the beginning of 2003. A few months later, ASEAN adopted the ASEAN Industrial Co-operation scheme, or AICO, in which products of companies operating in two or more ASEAN countries would enjoy the full AFTA treatment immediately.

In 1997, the international financial crisis struck Southeast Asia particularly hard. Immediately, the usual instant commentaries predicted that, as a result of the crisis, ASEAN countries would retreat into isolation, that ASEAN would fall into disarray, that AFTA was dead. Such speculations, some of it evidently arising from herd instinct, were made in defiance of logic and without waiting for the facts to unfold.

AFTA Speeds Up

What ASEAN needed at a time of economic contraction and diminished investor confidence was to regain that confidence and bring investments back in. In the face of this reality, the logical thing to do was to deepen and expand and accelerate regional economic integration instead of hollowing it out, constricting it, or slowing it down. That was the logic. The fact was that, in 1998, at their summit in Ha Noi, the ASEAN leaders again advanced the completion date of AFTA, this time by one year, to the beginning of 2002 for the six original signatories to the AFTA agreement, with the later signatories given a few more years to adjust to regional free trade.

The beginning of 2002 is just a little over a year from now. Already, more than 85 per cent of tariff lines for goods traded under AFTA are in the minimal 0-to-5 per cent zone, representing more than 90 per cent of the value of intra-ASEAN trade. Next year fully 90 per cent of tariff lines will drop to that zone. By 2010, all tariffs among the original six are to be abolished. ASEAN countries are also committed to removing non-tariff barriers among them. Even today, average tariff rates for goods traded within AFTA are down to a low 4.4 per cent and should be less than 4 per cent next year.

To be sure, the financial crisis has brought particular difficulty for some specific industries in individual ASEAN countries. ASEAN is ready to make allowances for the relief of such industries, but these are strictly circumscribed as to scope, timeframe and other conditions.

Dismantling trade barriers is, of course, not enough. Trade must be made easier as well as freer. Thus, ASEAN has been working on the harmonization of tariff nomenclatures, the compatibility of product standards, mutual recognition arrangements, and the streamlining of customs procedures. Nor is it sufficient to free up and facilitate trade in goods. Services are becoming a larger and larger part of ASEAN's economy. Services are also a much more complex area to deal with than merchandise trade. But they, too, are now subject to liberalization negotiations, sector by sector.

ASEAN is seeking to increase its attractiveness to investments by integrating itself as a market for goods and services. It is also doing this by directly allowing investments to move freely within ASEAN. Under the ASEAN Investment Area agreement, each ASEAN country opens itself up to investments from other ASEAN countries and extends national treatment to those investments. The few exclusions are to be phased out according to an agreed, binding and short timetable. Impediments to investments are being removed. ASEAN has also begun to promote itself jointly as one investment area in Japan, the United States and Europe.

ASEAN's economies are being bound closer together through infrastructure linkages. ASEAN is planning the consolidated expansion of the already extensive road network on mainland Southeast Asia covering a total of 33,480 kilometres. It is working out the protocols for the implementation of the agreement to facilitate the treatment of goods in transit. Agreements on multi-modal transport and interstate transport are in the works. The feasibility study on the completion of a railway from Singapore to Kunming in southern China has been completed, and a decision on the precise route out of several alternatives should be made soon. For the power grid on the mainland, two out of the fourteen projected interconnections are already in operation. The trans-ASEAN gas pipeline network should, as it moves to completion, progressively help to ensure the region's energy security. Co-operative measures are being taken to make possible telecommunications interconnectivity in ASEAN and the standardization of telecommunications equipment. The question now is how to package these infrastructure projects as attractive opportunities for investment.

Into the Information Age

ASEAN is taking economic integration into the information age, while using information and communications technology to strengthen regional economic integration. A combined private-sector and public-sector task force is working on a programme to create e-ASEAN. It would recommend the facilities and policy environment required to encourage the private sector and the people in general to make use of and develop technology for progress and profit. The work covers such key areas as an ASEAN information infrastructure, the facilitation of e-commerce, the legal and policy environment for the development and use of information technology, the liberalization of the trade in goods and services related to such technology. It is expected to identify the requirements for human resources and ways to meet those requirements. It also addresses the use of information and communications technology for improved governance and for social uses like health and education and even rural development.

The impact of the financial crisis on the region, with its strong characteristics of contagion, demonstrated, if further proof was needed, how integrated the ASEAN economy had become. If that was so, then not only must the market for goods and services be more deeply and more rapidly integrated, not only must ASEAN investments flow more freely in the region; co-operation in financial matters needed to be pursued much more intensively.

Thus, ASEAN's finance ministers have set up a surveillance mechanism through which the ASEAN governments would monitor macroeconomic developments in the region and encourage one another, through a process of peer review, to strengthen their economic fundamentals and to push forward the necessary economic reforms. Last week, the ministers conducted, in Prague, the fourth such review. The ministers also decided to enlarge the currency swap arrangement through which ASEAN countries could help one another in case of balance-of-payments difficulties.

Analyses within ASEAN, however, have highlighted the fact that market integration and financial co-operation, essential as they are, are today not enough to shore up investor confidence in ASEAN and enhance ASEAN's strength in the global competition for investment capital. Attention must be paid to the domestic investment climate in each ASEAN member. Here we enter into the area beyond AFTA, beyond market integration, beyond strictly economic and financial co-operation, in order to face the challenges of the future.

The domestic investment climate of each ASEAN country has to be constantly burnished. Each government has to put in place the necessary national laws and policies. The rule of law has to be fortified. The competitive field must be levelled. Transparency must be fostered. The integrity of governmental and corporate institutions and processes must be upheld. The people's skills have to be upgraded to ensure their competitiveness. Security and order have to prevail — and be perceived to prevail.

The Next Step

This is the next important stage in ASEAN's integration, a broader stage than dismantling international barriers to trade and investment. This may require ASEAN countries to concern themselves more with issues of governance without, of course, interfering in one another's internal affairs or imposing policies on one another.

This is not without precedent in ASEAN. After all, tariff policy and other trade restrictions are a matter of sovereign right on the part of states. But AFTA obligates ASEAN members to make commitments to one another in bringing down, through domestic legislation, barriers to regional trade. They are doing so with respect to obstacles to intra-regional investments. They are about to do so in the case of services. In the peer review that the finance ministers frequently conduct, they look into one another's national economic policies and reform measures. Other ministers and officials have been discussing national policies and practices that have a serious impact on the atmospheric pollution levels in other parts of the region.

ASEAN governments should be able to discuss, in a frank but friendly and discreet manner, other elements of the investment climate — governance, the rule of law, the judicial system, transparency and accountability, corruption and integrity, measures to improve people's skills, order and security. After all, the image of disorder in one country affects perceptions of the stability of the region as a whole. Impressions of an inhospitable investment climate in one country deeply influence the regional climate.

ASEAN ministers have begun to conduct such dialogues with increasing frequency and intensity, as they respond to the challenge of regional economic integration beyond free trade areas, investment areas and financial policy co-ordination. This is for them a matter of regional solidarity. And that is what ASEAN is about.

SOURCE: ASEAN Secretariat <<http://www.aseansec.org>>