

“Asia’s economic challenges and policy choices”

Molonglo Theatre, The Australian National University

Wednesday, 6 November 2013

Opening remarks

PETER DRYSDALE: Good afternoon. I’m Peter Drysdale from the Crawford School of Public Policy. Welcome to this public forum, which is jointly hosted by the Crawford School and the JEF. Our primary hosts, the JEF Foundation, is associated with the Ministry of Economy Trade and Industry in Japan, and we are very pleased to be collaborating with them and bringing together a group of distinguished economists and analysts from around Asia to talk about Asia’s challenges and policy choices this afternoon. I would now like to introduce Professor Kazumasa Kusaka, who is the Chairman and CEO of JEF. He is also a Professor at the School of Public Policy at Tokyo University. He’s had a distinguished 30 year plus career in Japan’s civil service in trade and energy areas, and has worked closely with policy makers in the region in the development of policies that foster closer economic cooperation among the Asian economies. This has included working with Australia, especially on his work with APEC. In case you didn’t know, today is the 24th birthday of APEC. The first APEC meeting was held here in Canberra on this day in 1989. And Kusaka san among others was very much involved in setting that process up with the Australian government and governments around the region who participated in the first APEC meeting. So welcome to the ANU Professor Kusaka, and may I invite you to say a few words on behalf of JEF.

KAZUMASA KUSAKA: Thank you Peter for the kind introduction. Peter Drysdale, guest speakers from the Asia-Pacific region, Dr. David Gruen, distinguished guests, ladies and gentlemen. My warmest welcome to all you for participating in today’s JEF-ANU international symposium. We have received enormous assistance from the Australian National University in convening today’s forum. We extend our deepest gratitude to Professor Peter Drysdale, Dr. Shiro Armstrong and to all of those who have been involved in organising this forum. Today’s symposium dates back to the Shimoda forum in 1993. Since our own forum in Singapore held in 2002, we began to discuss trade issues and its challenges. Counting from the forum in Singapore, today’s is the 12th Asia-Pacific forum. This Asia-Pacific forum has 13 permanent members including ERIA and ASEAN

secretariat. We have a history that each member has hosted the forum. Australia is the last but most important country among the members to host this forum. Therefore, this event is commemorative in marking a complete circuit of hosting members. Canberra is, as Peter referred to, the venue where the first APEC meeting was hosted by Australia today 24 years ago after Australia and Japan jointly calling on the ASEAN friends. We are so honoured to celebrate this happy 24th birthday here together with APEC's intellectual architect, Dr. Peter Drysdale. And in this regard, this Asia-Pacific forum will be held at the best place to go back to the basics of the establishment of APEC. Looking at recent developments in the global economy, the effects of the Lehman shock are still prevailing and the European debt crisis is still to be resolved. Thus, each country is faced with a challenge of identifying growth strategies and financial and monetary restraints, and all are working on FTAs to promote structural reforms as part of their growth strategies. This year's Asia-Pacific forum is looking at regions where the efforts centre around RCEP, but there are also several bilateral and trilateral movements emerging (as well as TPP) that also involves the United States. In Japan, with the slogan of "Japan is back", efforts are currently underway for the 3 arrows of Abenomics. As a result, Japan, who has been looking inward, is once again looking to the Asia-Pacific region and beyond globally. With these recent developments in mind, this year's Asia-Pacific forum will discuss Asia's economic challenges and policy choices. I hope that discussions will be useful for each of the participants here today. Thank you.

Session 1: Regional trade choices

PETER DRYSDALE: The first session will focus on regional trade policy choices in Asia and try to comprehend different perspectives in the region. A central focus in Asia has always been on external economic policies, especially trade policies as economic prosperity in the region has depended upon industrial and economic transformation through trade, and a framework that contributed to the successes were critical. This still remains at the core and how this framework and economic policy choices are managed will underpin future growth and prosperity. In the past, keeping the global trade system open was absolutely fundamental to Asia's successful industrial and income growth, but the key question now is whether that is still a priority or whether regional trade arrangements will be a vehicle to deliver prosperity.

SHUJIRO URATA: Japan's economic growth until the 1970s was closely related to an

open global trade framework. Japan and other countries joined General Agreement on Tariffs and Trade (GATT) and Organization for Economic Co-operation and Development (OECD), and through its membership, benefitted from an open market. While many countries liberalized their trade within the GATT framework, when World Trade Organization (WTO) was established in 1995, it took 6 years to initiate the Doha Round of negotiations. Since 2001, there have been little progress and given the stalemate, other possibilities like the Free Trade Agreements (FTAs) are now explored. But what is important is to understand that these FTAs are alternatives and lead them to multilateral trade liberalization.

PETER DRYSDALE: India experienced significant trade reform over the last 20 years, enjoying above average growth rates, does India still see the global framework being central to its long term reform and development?

BISHWAJIT DHAR: When India opened its market 22 years ago, the critical impact was on its foreign policy, and India began engaging more with the partners in the East and began a strategic dialogue with Association of South East Asian Nations (ASEAN) in 1992. India has since been actively engaging and negotiating free trade agreements. While India is conservative with the WTO process, it is far advanced in its bilateral processes with the East Asian partners with trade agreements in place. Imports from East Asia increased significantly with production networks of parts and components, and India is also laying the groundwork for deeper engagement and connectivity. India has no formal trade agreements with China yet, but the regional market is leading India to greater engagement and integration with China, India's largest trading partner in 2012.

THOMAS G. AQUINO: The Philippines believes in the multilateral trading system and has been active in GATT as one of the original members of WTO. ASEAN 10 countries are trying to share the philosophy of open regionalism in the WTO. The ASEAN Free Trade Agreement has no common external tariff structure among its members. Forming a regional institution like ASEAN provides benefits for smaller member countries engaged in international trade. For a time, ASEAN did not actively seek bilateral trade agreements. However, ASEAN has since identified the importance of seeking partnerships with its big neighboring countries like China, Japan, Korea, India, and Australia. Official meetings held regularly at ASEAN serve as peer pressure to commit moving forward in trade and investment liberalization. ASEAN moves forward when it

believes the time is right and its experience should be shared with the bigger partners in the region.

PETER DRYSDALE: Asia is now central to the global trade system and many argue for Asia to step up to its role. But since WTO negotiations are not moving forward, should the alternative be to move towards more narrow regional agreements?

ANDREW ELEK: GATT and WTO are often talked about as obsolete for its lack of progress in trade liberalization, but its fundamental objective was not to abolish tariffs, but to make the environment predictable and confident. The successes of East Asia depended on establishing confidence and while there were loopholes in the GATT, it was very broad adherence to non-discrimination that contributed to the growth of the region. There is now a danger of losing this framework, and at a time when global influence is shifting rapidly, it is crucial to remember that trade partners need to be treated equally and with respect. The FTAs are not serving the original expectations of fairness, as the protected areas remain protected. Today, electronics and information technology is where the big value-added comes in, and the problems in these areas are not tariffs, but standards. It takes a long time to get across borders not because of tariffs, but because of sheer bureaucratic inefficiency, and regulatory convergence cannot be achieved just by setting rules. Negotiations are not the only way to make progress, and while getting rid of tariffs and trade barriers have certainly made positive impact to the region, it is time to shift to where the bigger gains are in capacity building through mutual learning process guided by trust, not through negotiations.

PETER DRYSDALE: The key question is identifying the best framework to provide those guarantees that will underpin confidence in an international business environment and to foster development of trade and growth in the region. How are Trans-Pacific Strategic Economic Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP) viewed from these perspectives?

SHUJIRO URATA: Multilateral trade liberalization is the best for establishing free and open trading environment. But implementing multilateral trade liberalization is difficult. GATT began with 20 countries and the agreement process was not so difficult, but there are now 159 WTO countries with diverse interests, levels of development, and all the more complex. Be as it may, alternative processes with the same goal should be sought, and TPP and RCEP, the two large regional frameworks that are different in nature but

complementary, can serve as alternative processes. TPP negotiations so far have tried to achieve high level of liberalization and be very comprehensive. RCEP, on the other hand, is also trying to liberalize trade and investment, but its key objective is to provide economic cooperation and assistance to less developed countries in the region. There are a number of countries involved in both negotiations, and the leadership of these countries should join efforts.

BISHWAJIT DHAR: There is great discussion and unease in India regarding TPP because so much is a US led with the US agenda seen in the background, and it is quite clear that TPP is about harmonization of rules, not tariffs. India already has a free trade agreement on goods with ASEAN, and India has also agreed to extend this framework to investment and services. Therefore the ASEAN centrality that underpins RCEP is very good for India and will continue to engage actively with ASEAN. India has done a two-step process with ASEAN: an umbrella agreement with the member countries and separate bilateral agreements with individual countries. Regardless of the RCEP process, India is headed towards liberalization, and RCEP negotiations will add the extra push the domestic reform process.

ZHANG YUNLING: The new leadership in China is interested in using TPP as a tool to promote domestic reform, but China cannot accept TPP's harmonization of rules, and Chinese leaders had put more emphasis on RCEP and close cooperation with ASEAN. But RCEP has three fundamental challenges for China: the level of liberalization of trade in goods, the higher level of liberalization in services and investment with no specialist treatment, and the cooperation element of the framework on how, where, and what fits into it. RCEP should be different from TPP but there are expectations of it being at a comparable level, and China still has mixed feelings towards that aspect. The commitment will depend on the China-US relationship, but China is generally very active in terms of attitude and policy towards RCEP, and while China will not lead the negotiation process, if China, Korea, and Japan can quickly agree upon the general principles, it will be easier for China to commit more. The Chinese Roundtable Experts organized by the Economic Research Institute for ASEAN and East Asia (ERIA) tried to provide that general framework as a vehicle to move the process forward, and things are now up to the leaders.

THOMAS G. AQUINO: ASEAN has sufficient experience with the development and enhancement in the integration of the ASEAN Economic Community (AEC). As ASEAN

builds partnerships with the big players in the region, there is a natural tendency to share ways and means of domestic processes. The structure of RCEP is in place, and confidence is building up in trade and investment liberalization as well as on gaining productivity and competitiveness. These experiences are already embedded in the RCEP process and provide great learning opportunities.

PETER DRYSDALE: Does Japan have a powerful incentive to engage in RCEP actively, especially when it involves not only trade but building infrastructure connectivity?

SHUJIRO URATA: Compared to previous administrations, the current Abe administration is eager to expand external relationships. Growth strategy is the third arrow of the “three arrow strategy” of Abenomics, and an important component of that is FTAs, particularly TPP providing an important momentum. The absence of US President Obama at the TPP meeting was disappointing to Prime Minister Abe, but Japan is very eager to move the TPP negotiations forward. But more attention towards RCEP should be given, and to do so, China Japan Korea FTA is important. A bilateral FTA between China and Korea will perhaps come first, to which Japan may join and move the RCEP negotiations forward.

BISHWAJIT DHAR: Incentives for India to become an active participant in the RCEP process is huge given the increase in India’s economic engagement with the East Asian partners, and it is only logical to have clear and predictable rules through trade agreements. The WTO process has not gone far in terms of rule-making, and has become the most problematic issue. This is where regional agreements can have an advantage, discussing these issues in a smaller setting to achieve an agreement more easily. WTO negotiations have shown that even non-controversial issues such as trade facilitation can fall apart, the moment a negotiating approach is taken. Thus it is important to look at what issues should be brought to RCEP and not repeat the past mistakes.

PETER DRYSDALE: One aspect that distinguishes RCEP from the TPP process is the way it encompasses a range of issues, and the fundamental philosophy is different, resembling the philosophy of ASEAN Economic Community. The new government in Australia is actively pursuing the Australian trade agenda, both in the regional and global framework: what can Australia bring into the RCEP process?

ANDREW ELEK: The RCEP vision should follow ASEAN’s example of deep integration

which is not easy, but ASEAN has shown that it can be readily widened. Australia can present its vision of RCEP evolving beyond the traditional trade negotiations into a broader version of an AEC where other countries can join in freely. But it is very important not to mix different problems. A big contribution Australia can make is to propose for RCEP to have a negotiating element that can serve as a capacity building or an institution building process. It has the potential for connectivity, which goes beyond just being a trade agreement to harmonizing policies and connecting people.

Questions and answers / open discussion

[Q] PAUL HUBBARD, Australian Treasury: Rather than creating a separate process for RCEP, can existing institutions like the East Asia Summit handle the other non-trade-negotiating functions?

[A] ANDREW ELEK: Indonesia showed great leadership in 2013 and there is the APEC connectivity framework, but it will not go anywhere unless the Finance Ministers get involved understand the capital markets and financial integration problems, and translate it to a domestic reform agenda. This is a greater task than the trade policy agenda, but without this, nothing much will happen in APEC, and if APEC cannot respond, perhaps RCEP can.

[Q] LIGANG SONG, ANU: Trade liberalization and domestic reform goes hand in hand, and there are compromises being made between different sectors and politics. But if the domestic reform agenda is lacking in the negotiations, how can reform be promoted?

[A] BISHWAJIT DHAR: The challenge perhaps is unique to India. Domestic reform is lacking in agriculture, and in looking back at India's past trade negotiations, agriculture has always been an issue. History shows that pre-condition for any negotiation on trade liberalization is domestic reform, and efforts to coordinate the different ministries will be needed.

[A] ZHANG YUNLING: There are two factors that will push China. One is environmental and energy problems that China accumulated through its trade led growth, and therefore needs to change. Another is the level of economic development compared to other countries in the region like Japan, Korea, and Taiwan. The time has come for China to change and reduce the role of government and further liberalize the market. In the

past, liberalization was more focused on growth and trade, but now it is more about institutional reform and formulating new rules that are efficient. China will be actively participating in multilateral framework.

[A] HANK LIM: China seems to be eager for domestic reform. Although China is trying to get growth out of increasing domestic demand, it is not enough to keep up with the excess industrial capacity, and China needs to align domestic reform with regionalization. For India, the reform process is different and more difficult as the Indian policymakers still think that India has the ability to grow domestically without the international agreements.

Conclusion

PETER DRYSDALE: There is from this discussion a strong sense that a number of the major players in the region are at a point where they're grasping for new ways to tackle their national reform agendas. This could provide an important momentum for growth in the region and an international framework for constructive policy development. But the region is yet to actually define the way forward, and get traction in one of the important negotiation processes.

Session 2: Asia and the global trading system

NAOYUKI HARAOKA: This session will try to determine whether regionalism can substitute or complement the multilateral trading system. We will also look at whether regionalism can be a catalyst or a building block for a multilateral trading system. The first question to ask is the current status of the global trading system, WTO. The 9th ministerial meeting is going to take place in December 2013 in Bali which will be a very important milestone. What is the collective role of Indonesia and ASEAN in promoting regional interests?

HANK LIM: The multilateral system has contributed very significantly to the dynamic growth, economic prosperity, and political stability of the region, and the role of ASEAN and East Asia after the Doha Round of WTO has been crucial. The stumbling block for the Doha Round seems to be both in the substance, and more importantly the process, and this is where the regional architecture can play a role. The process would see

innovative regional integration contributing to a new architecture for Most-favored-nation (MFN) which is non-discriminatory, transparent and predictive. It will be convenient for business transactions and facilitates trade and investment flows in the region. Once the process is identified, ASEAN, for example, can play an important role in TPP by reaffirming its importance and its validity, even in a changing global environment. The WTO Bali conference can see the new realities of global trade and instead of just negotiating on tariffs, look at issues such as capacity building and regionalization. This would be a great contribution in terms of keeping the spirit as well as the fundamental principles of a multilateral trading system alive.

GARY HAWKE: WTO is important globally and regionally. The most important aspect of the WTO is the dispute settlement mechanism, and the WTO needs to preserve this mechanism. It is unrealistic to expect any great achievement at the Bali Conference such as trade facilitation or ITA extension, and it is impossible to get agreement on reconciling the safeguards rules. But the leadership change of the WTO is important here and WTO is now led by someone from Brazil. He has already displayed his commitment to reform through his staff appointments, and it will be important for Asia to give support to him and align its willingness to change. The future role of the WTO will need to include a negotiating forum - maintaining the disputes resolution system alone would be very difficult - but familiar rounds are unlikely to survive, and countries need to rethink the traditional ways of ensuring national interests. Plurilateral agreements are growing because economic integration requires confidence in the regulatory systems, and the role of WTO will, then, be maintaining consistency between the rules, and this should be the important rationale to continue participating in WTO.

NAOYUKI HARAOKA: The future of WTO will involve thinking about the future of Asian regionalism, and the focus of Asian regional trade agreements have shifted to economic integration. There must be economic and political challenges for this process, how can market based supply chain connectivity be ensured with these challenges in mind?

MIGNONNE MAN-JUNG CHAN: The impasse of the Doha development agenda has led like-minded regional economies to flock together in order to move forward as path finders, the cases in point include RCEP and TPP. However, this does not mean that the world has to give up WTO. WTO cannot be substituted in its own merit. In the past, The Asia-Pacific region had the track record of serving as a catalyst for the WTO agenda, today,

APEC, RCEP and TPP should continue to shape inspiring agenda. There was APEC success in putting forth proposition such as The Information Technology Agreement in WTO, although there was also APEC failure in promoting the initiative of Early Voluntary Sectoral Liberalization (EVSL) in the name Advanced Tariff Initiative. Currently, the governments in the Asia-pacific region could focus on the bottom-up, market-based supply chain connectivity, which is crucial for regional growth and mutual prosperity.

TADAYUKI NAGASHIMA: Institute of Developing Economies, Japan External Trade Organization (IDE-JETRO) and WTO conducted a joint study on analyzing supply chain connectivity through measuring trade in value added and to investigate the real structure of trade. WTO's interest in this area in itself indicates a change in WTO's thinking towards trade issues. In looking at trade between China and Japan, China is Japan's top gross export partner, followed by the US. But when the real value added is accumulated, the top partner is the US, followed by China. For Japan and Korea, Japan has great surplus with Korea, but the balance of trade in value added is equal, because Korea import parts and components from Japan and exports the products to China or the US. Hence there is now global value chain making international trade complex.

NAOYUKI HARAOKA: What is the role of Indonesia at the Bali Ministerial Conference, and when economic integration or regionalism faces question of geopolitics, how can the RCEP members strengthen institutional connectivity, not supply chain connectivity?

DJISMAN SIMANDJUNTAK: Indonesia should try to persuade major parties of the WTO on restatement of their commitment to the principles of the WTO. Until the early 1990s, ASEAN only discussed cooperation, and not integration. But with the ASEAN Free Trade Agreement (AFTA) in 1992, Indonesia was persuaded of the merits to participate in the globalization process. For Indonesia, AFTA was originally conceived as a training ground for engagement in global trade, and this process may be useful in thinking about regionalism. Asia, including ASEAN and RCEP, has somehow always managed to find pragmatic ways to live with a rule based system, however evolutionary in nature. Regional grouping is a cooperative undertaking with regional commons such as the maritime common, air space common, biodiversity common, energy security, and food security. Cooperation in Asia often tends to relate itself primarily to providing extra support to the less developing members, but it can learn from the experiences from the EU as well in pooling resources to produce and maintain regional commons such as the

pooling of research and development (R&D) resources as part of endeavours to create a balance in science and technology capability. East Asia is now resourceful enough to play a responsible and positive role in providing regional commons, and will need to continue building better relations both within and outside Asia as the region requires conducive a global framework while it seeks to climb up the development ladder.

NAOYUKI HARAOKA: Regional politics is a sensitive issue and apart from whether WTO is still valid or not, there is a need for a global trading system which would be fitting even with the realists. In that sense, there should be a way to think about how regionalism can expand to a multilateral system, and how accession to regional groupings can be managed.

GARY HAWKE: An alternative to the basic presupposition that accession to any grouping depends on unanimous agreement of all the existing members needs to be identified. The basic idea that membership should be open to anybody who accepts the rules of the group is sensible, but there are always differences between economies and exactly what the rules mean for individual applicant becomes a significant question. The way forward will likely take the politics as far away as possible, to make the process a technical decision. The decision should be based on economic principles and not on politics. That would be helped by using an independent institution; governments cannot be excluded entirely and there are other ways of providing guidance to a technocratic process for deciding on membership obligations. For RCEP where economic development levels differ between its members, accession may be assessed accordingly, and guidance to a technocratic process may be worth exploring.

NAOYUKI HARAOKA: Turning to the business aspect, JETRO is working hard to attract business interests to FTA or trade liberalization efforts. What is JETRO's analysis on this "spaghetti bowl syndrome" with different Rules of Origin (ROO) in different regional integrations?

TADAYUKI NAGASHIMA: FTA or RTA should be business friendly so that the complication of the ROO should not hinder trade. Japanese companies located in Asia not only use the FTA and EPA that Japan has with ASEAN member countries, but as 30% of the companies are located in ASEAN, these companies are using AFTA. Japanese businesses consider FTA as the second best, or an alternative to multilateral agreement, and are expecting progress at the Bali meeting, progress in RCEP, or the conclusion of

TPP. Looking at the Japanese automobile industry for example, the strategy has changed dramatically in the past few years, and more companies are now producing locally in overseas markets. This means that the companies are now expanding their production where there's great market demand. The currency risk is also gearing the companies to produce locally and hence there is a global value chain.

NAOYUKI HARAOKA: Will TPP or RCEP contribute to the multilateral global trading system?

MIGNONNE MAN-JUNG CHAN: TPP claims the high-quality platinum FTA, whereas RCEP emphasizes an incremental building-block approach. Ideally, TPP can discuss "market access" first without neglecting "capacity building" later, and vice-versa for RCEP. As long as both TPP and RCEP are comprehensive and address mutual interests which in turn will contribute to the global system, they could all work.

HANK LIM: TPP and RCEP are different but each has a certain role to play with different structure, negotiations process, the elements of the MFN, and non-discriminatory dispute settlement mechanism.

DJISMAN SIMANDJUNTAK: Perhaps it is not entirely unrealistic to expect some convergence between TPP and RCEP given the overlapping participation of the members, like Japan, Australia, New Zealand, Malaysia and Vietnam. RCEP may somehow be able to raise its ambitions from the current level and perhaps TPP can somehow lower its expectations, and by doing so, both can become a building block for multilateral systems.

GARY HAWKE: WTO has never been perfect and will not be in the future, but it should be preserved, and maintaining compatibility, not necessarily identity, between the provisions of different regions and agreements is important. This would be from a business stand point where individual companies can choose to move between regional agreements.

Questions and answers / open discussion

[Q] Audience from Department of Industry: At what level can countries discuss harmonization of regulations, liberalization, and domestic reform, given it is very specific to each country and region?

[A] **HANK LIM:** The priority should be on the ease of doing business, connectivity and coherence that would facilitate expediency of the flow of goods, services, investment and capital. But it is just the initial impetus towards the new approach of regulatory coherence rather than just talking about trade negotiation.

[A] **TADAYUKI NAGASHIMA:** Safety standards and emission standards for cars is a very important issue in the FTA negotiations, whether the negotiation is between Japan and EU, or South Korea and EU or South Korea and US.

[Q] The discussion have to be at the very micro level as standards are run by different organizations in different countries.

[A] **GARY HAWKE:** It is tempting to say that discussions should be as general as possible. Most of the productive discussions that are taking place are very high level, and are dealing with questions like transparency and what that means. Translating transparency into publishing rules, making sure that decision making processes are bound by regulations are where regulatory coherence is being advanced, but beyond that, harmonization should be avoided. Setting up a standard and making everybody identical guarantees failure. The process should be achieving regulatory coherence, and should not be an attempt to make the regulations identical. Specific issues like consumer safety will be interesting to watch, whether EU and the US can discover common basis for standards in various fields. Work on standards needs to be done at a sectoral level as different industries require different rules. But again there are certain ways in which one can work gradually from the abstract to the specific issues, and the discussions will always go forwards and backwards. The most important development at the moment is getting the regulators involved in these discussions and getting a regional approach. This is where progress is being made, although slow, and regional elements are sewn into the decision making process which have traditionally been very domestically focused.

Session 3: Asian growth - prospects and risks

SHIRO ARMOSTRONG: This session will look more broadly at Asian growth for both individual economies and the region. Australia has just gone through a national conversation in crafting “Australia in the Asian Century” White Paper which focused on where Australia is in the world and how much of Australia’s prosperity depends on Asia.

The White Paper projected that by 2020, Asian economies will account for nearly 50% of global output, and by 2030, more than 3 billion people will be middle class in Asia. Hence Australia is trying to understand the issues, perspectives, and challenges in East Asia, Southeast Asia, and South Asia.

ZHANG YUNLING: After more than thirty years of continuous high economic growth, China has accumulated many problems that policymakers have to tackle, and the leadership as well as the entire Chinese society as a whole, understands the need to change and to liberalize the market. The question is how, and there are high expectations towards the forthcoming Plenary Session of the Party Congress where the leaders are committed to providing a package of reform agendas. China has followed the traditional East Asia model of government-led, export-led growth, but this must be readjusted so that the market plays a more important and independent role. For external trade also, China cannot continue even with the changes in the global market. For change to occur, China must meet several basic requirements. First is continuous economic growth which is debated by many outside observers. Second is reduction in income gaps between the different people across regions, which is not just an economic process, but more related to China's unique economic and social system calling for a new urbanization process. Third is the ability of the legal and political system to cater the change. How to meet these requirements and the high expectations is a huge challenge. China is committed to liberalization and leaders understand the need to further liberalize, but structural reform in the political system in China is difficult, but the direction is very clear and both internal and external factors will press China to change. China may not join TPP, but will nevertheless discuss the principles so that China is not excluded, and this will be the same for RCEP, and these processes will acts as positive forces for China to change.

KAZUMUSA KUSAKA: There are high expectations on the Japanese economy for the first time in a long time. A healthy Japanese economy is critical to robust economic growth of the region. But the change in mind-set is needed to become outward looking to the Asia Pacific region, and this change will lead to a new situation where Japan, both the public and the private sector, will assume greater role in providing public goods to the region. This is where Abenomics can contribute to the region with its third arrow being the growth strategy, where the FTAs are given the role of achieving higher productivity and higher wages through structural reform, to be accelerated through FTA negotiations and increase in trade and investment. Hence Japan is very forthcoming in regional FTAs. Japanese productivity in the service industry and agriculture is low and

needs competition. These are domestic issues, but any democratic government needs some kind of peer pressure from other countries, through the process of FTA negotiations achieving domestic agenda becomes easier.

CHULSU KIM: Korean economy has not been doing very well in recent years. In 2012, growth went down to 2%, which is very low given the South Korean growth trajectory in the recent years. The major causes are dwindling external demand, and domestic demand has not been able to do make up for that due to high and increasing household debt dampening private consumption. The economy seems to be picking up a little in 2013 on the back of improvements in overseas market demand, but South Korea is still faced with a challenge of North Korea with its unpredictable behavior, and other economic factors. The household debt situation is deteriorating quite rapidly, and there is still an ongoing social welfare debate concerning old age pension, a very controversial issue throughout the Korean society. External demand is a key factor for the future of the Korean economy. As for trade policy issues, the new government will continue to be actively pursuing FTAs with both large and regional trading partners, and would seek to become the lynchpin of regional trade integration initiatives such as the TPP and RCEP. South Korea is negotiating FTA with China and has also begun China-Japan-Korea FTA, and all of these regional initiatives will be the focus of the Korean policymakers.

ANITA PRAKESH: South Asia is one of the least economically integrated regions in the world, and there is recognition within South Asia that the region needs connectivity and to develop a system to replicate the South East Asian model. The accidents of geography and history have so far not allowed much progress on this front, and for India, it is easier to talk about the connectivity with the South East Asian countries and East Asia, where efforts are more predictable and visible. India's "Look East" policy came in the early 1990's when the relationship was more at a policy level, and the India-ASEAN framework for FTA negotiations began in the early 2000s. Since then, trade between India and ASEAN has taken quantum leaps, and trade with China has also increased enormously. The important issue is how to balance the trade relationship, and now that Myanmar has opened up, the last missing link between India and ASEAN has been established, and the future of physical connectivity to the production networks into South East Asia is looking up.

KAZUMUSA KUSAKA: Economic and geopolitical risk must be managed in the region.

The economic risk is the middle income trap, and provided that rate of increase in CPI is much higher in this region and without the increase in productivity, the increase in CPI will bring the increase of wages resulting in a decline in competitiveness. The geopolitical risk is the perceived decline in US presence in Asia and in the Middle East. This may increase tension within the region, and would also pose a risk in securing energy sources. The global strategic approach to overcome the middle income trap is the focus on human resources. A country has to upgrade the industrial structure leaving behind the low waged, unskilled labor based factories, and globally that means supporting industries as well as small to medium enterprises by providing human resources, financial resources and technologies through foreign direct investment, transfer of technology and training of engineers.

SHIRO ARMSTRONG: The current bilateral relationship between China and Japan is worrying, but the economic relationship has continued to do very well. Should we be worried about the Senkaku islands, and what are the prospects for the economic relationship?

ZHANG YUNLING: In his first speech at a central party organized conference, Xi Jinping repeatedly emphasized the need for China to have good relationships with its neighbors. The end of the Cold War brought different types of conflicts and tensions in East Asia, and fortunately there has not been a war. The question now is whether there will be a war between China and Japan, and although there are different stories in the media, the decision makers on both sides are still constrained. Leaders of both countries feel that the time is not yet ripe to come to an agreement, but should nevertheless try and find a way ease the current tension rather than prepare for the worst scenario that neither is prepared for. If China-US relations can play a positive role, that will also avoid military conflict between China and Japan. China also has various trilateral and regional frameworks that can act as channels to communicate, which in itself is different from the past. The concern now for Asia, rather, is increased military and defense costs associated with becoming stronger against its rivals. South Korea's success in the past was very little military spending, but that is changing and the same holds true for China and Japan. This means resources are transferred away from economic development and innovation, and this is worrisome. China will continue to grow, and will remain a big military power and hence tensions will continue. Therefore, how the regional framework can be utilized to build confidence and reduce the risk is vital, not only in its economic relations but also on cooperation in traditional security. Now may be a time to consider

the traditional security cooperation arrangements in the region to secure stability and peace.

KAZUMUSA KUSAKA: Japan and China does need some sort of a make-up, and political tensions have not deterred the economic relationship between the two countries.

SHIRO ARMSTRONG: It is reassuring that Japan-China bilateral relationship is embedded in a region that is very highly integrated, and regional institution building and cooperation process is therefore all the more important. The question is leadership in providing public goods for cooperation. Australia and Japan led the APEC process, South Korea has been very successful in showing some leadership as a middle power, and all eyes are now on China to provide public goods in the form of infrastructure for the Asian Investment Bank. What is the prospect for leadership in the region?

CHULSU KIM: Given the current tensions, it would be very difficult for China or Japan to assume leadership in the region, and it will have to be a collective leadership. Hence it is important that China, Korea, and Japan to begin talks on trilateral FTA or other economic issues rather than security or political issues. In the long run, these trilateral discussions will help to improve not only the situation amongst the three countries, but also the situation in Northeast Asia.

HANK LIM: ASEAN countries are very worried about security issues. The ASEAN perspective is often aligned with the Western perspective as the legalities of international relations has been set by the West for the past 500 years. But Asia needs to be understood as very pragmatic, not dogmatic and not ideological, and this is very different from the Western mindset. The most important aspect is to avoid any accident in today's world, where intercontinental ballistic can change the scenery immediately. Perhaps a hotline-like mechanism between the leaders may be needed. The Defense Minister's meetings of ASEAN, where there are also territorial issues, and the Shangri-La dialogue in Singapore have certain lessons for Northeast Asia.

Closing remarks

PETER DRYSDALE: What was discussed today is a region at the cusp of significant change in response to a new set of circumstances, reinvigorating their growth prospects.

There are prospects for policy initiatives, particularly international economic diplomacy, and dimensions of the ways to carry forward around what is already in place in regional negotiations. Breathing life into those negotiations and their potential role in the global system remains vital to the health of the Asian economy and polity.