

A sian Economic Integration & The Role of Japan

By Harald MALMGREN

AEEC: Beyond the Scope of FTA/EPA

In May, 2008 Japan's Ministry of Economy, Trade and Industry (METI) issued an important proposal for an Asian Economic and Environmental Community (AEEC). Accompanying this proposal was a detailed analysis of the Asian economic region as it has evolved in recent years not only into "a factory of the world," but into "a growth center of the world."

The METI report identifies bottlenecks to further integration and correctly observes that such bottlenecks are restricting the sustainable economic growth of Asia. The report also suggests that Japan itself is facing great challenges to maintaining a leading regional role as Japan's economy matures, with a falling birthrate and aging society. To enable Japan to continue to grow alongside its geographic neighbors, new policy initiatives are needed.

In this challenging context, METI proposes that Japan take a leadership role to develop an AEEC. This new framework of cooperation in the Asian region would focus on a variety of environmental, technological and human-resource challenges to further growth. The AEEC concept goes far beyond the scope of the many FTA and EPA proposals for strengthened regional economic integration that have been suggested since the middle or late 1960s. Some of these proposals even involved participation of the advanced economies of the Pacific Rim in a region-wide free trade area.

Since the 1960s, I personally had been an advocate of efforts to enhance interaction of countries in the Asian-Pacific region with the objective of promoting economic and social integration. In the spring of 1972, in my then formal position of Deputy US Trade Representative, I made an address in Sydney calling for establishment of a formal multilateral institution to consider and negotiate agreements among governments of the region to enhance social and economic development. My 1972 Sydney address was the first official US government expression of interest in and support for Asian regional integration initiatives. Since that time, US government support for Asian integration has varied between hot and cold, as the attention of America's leaders was drawn from one global economic or security challenge to another.

Disparities Impede Asian Integration

Although the Asian economies have experienced dramatic growth in recent years, political consideration of greater economic or trade integration has been impeded by large economic, social, political, religious, population and cultural disparities among the Asian coun-

tries. Moreover, some of the Asian economies leaped ahead in terms of economic growth while others faltered. As a result of these continuing disparities, the pace of economic, social and political change has varied greatly within Asia. Many of these disparities also exist inside several of these nations, posing domestic economic, social, and political tensions between central governments and local communities, ethnic groups, and a variety of dissident movements. Thus, in spite of a plethora of ideas for strengthening Asian economic integration, governments have continued to find it politically and commercially difficult to develop a common institutional framework for cooperation.

In 1997, the Asian financial crisis came like an earthquake to virtually all the Asian economies. In the following 10 years, Asian governments seemed to have learned lessons from the Asian financial crises as they built up substantial currency reserves and reduced dependence on short-term foreign borrowing. However, in spite of the financial and fiscal reforms of the last decade, in 2008 Asian nations once again found themselves confronted with triple crises of worldwide food inflation, fuel inflation and financial market breakdown. Inflationary super spikes in food and fuel prices collided with elaborate price controls in several Asian countries, disrupting supplies of food and fuel to ordinary people and businesses in their daily life. The breakdown in global financial markets has brought about a continuous unwinding of credit and global financial flows, and widening of spreads for borrowing by weaker governments and enterprises.

The year 2008 also seems to be showing signs of the start of a decline in world economic growth. Instead of surging growth, the Asian region is now faced with likelihood of economic slump alongside the faltering US and European "engines" of global growth. The emerging global strains in financial markets that first became apparent in 2007 in North America and Western Europe are now spreading indiscriminately across national borders, bringing credit contraction and higher costs of capital everywhere. This has resulted in a spreading credit contraction throughout much of the international capital market. Credit contractions historically are one of the most powerful causes of recession and deflation.

As 2008 draws to a close, US and European economic slowdowns are resulting in declines in export orders for many export-dependent economies. World trade growth has stagnated and it appears highly likely that the growth rate of most emerging markets, including those in Asia, will fall. As export demand dries up, many export-dependent countries will find that servicing their external debt will become far more difficult and costly, in the context of world credit contraction.

Japan in Unique Position to Display Leadership

At this moment in world history, Japan is in a unique position to demonstrate leadership in pursuing Asian economic integration. Preoccupied with cleaning up lending excesses of the 1980s, Japan's banking system was not caught up in the financial innovations in debt markets in North America and Europe. As the major financial institutions of North America and Europe are paralyzed by the "Great Unwind," Japan's banks are in a position to expand their role in global finance. Japan's domestic interest rates, having long been held down by deflation tendencies and slow GDP growth, now provide a unique base for lending to other countries eager to build up their domestic infrastructure and replace sagging exports with domestically driven growth. The Japan Bank for International Cooperation (JBIC) is in a strong position to support projects aimed at improved infrastructure in the emerging Asian economies.

At the same time, world trade liberalization has run out of momentum. The Doha Round world trade negotiations are struggling. Agreement seems to be eluding the grasp of negotiators, and even if an agreement could be reached, the US Congress would likely fail to support it. The United States, for decades a leader in promoting liberalization of trade and finance, finds itself with growing domestic political doubts about whether and how to continue on this path. European governments are also confronted by growing worries among their citizens about the pace of European integration and the extent to which EU borders should be thrown open further to competition from the rest of the world. There is no longer world consensus on whether or how to proceed internationally.

In 2008, the United States is experiencing a transition in political leadership. National elections in November 2008 will produce a new president and a new Congress, and in 2009 we shall see the establishment of a new US administration. New policies will appear only gradually, influenced heavily by the differing political priorities of the new president and of the Congress. In 2009, American political priorities will initially focus on domestic economic challenges from an economic downturn, including rising unemployment, and the legislated expiration of tax reductions initiated by President George Bush. World challenges to the new president early in 2009 may include new Russian assertiveness in world affairs, continued uncertainties in the Middle East, and a potential insistence by Congress that the United States take a more aggressive stance towards China.

At least in the near future, it is likely that American foreign economic policy will assign lower priority to trade negotiations and other trade initiatives. Preoccupied with domestic economic, fiscal

and regulatory issues, and under pressure from labor unions, Congress will likely want to "postpone" or delay consideration of trade liberalization initiatives. There will be growing pressures to undertake a "rethinking" of the objectives and modalities of American trade policy, and to take a "pause" in US trade policy.

AEEC: Historically Timely Idea

At this moment in history, there is opportunity for stepped-up efforts among the Asian nations by themselves to consider strengthening the economic workings of the Asian region. The METI proposal for an AEEC is the kind of new initiative that should be given serious attention. By moving beyond traditional issues of trade relations that arise in negotiation of FTAs, the AEEC concept poses suggestions for regional cooperation that transcend the current strains in world economic relations, focusing instead on the environment, human-resource development, infrastructure constraints, and building the foundations for a greater Asian open economy.

This way of looking into the future, beyond the Doha Round, was also recently suggested by Singapore's senior minister of state for finance, Lim Hwee Hwa. She argued in September 2008 the need for a new effort to promote "open regionalism" for Asia to create "an environment where companies can operate across Asian countries and beyond in a borderless manner...where goods, funds and information flow at minimal cost." In this way, she suggested, Asia could sustain the momentum for trade liberalization in spite of the faltering of the Doha Round and the inability of the WTO to move forward with global liberalization of trade and commerce.

Looking back over my own experience of the last several decades, I personally believe this moment in history offers both the opportunity and the need for strengthened efforts by Asian governments to seek ways to build upon past economic successes and secure sustainability of economic and social advancement at a time of worldwide economic, financial, food and climate change challenges. Such ideas as METI's AEEC and the suggestions of Singapore's Lim are historically timely, and deserve close attention by politicians, business people and strategists throughout the Asian region. **JS**

Harald Malmgren served Presidents Kennedy, Johnson, Nixon and Ford where he held a leadership role in devising US trade policy and served as chief US trade negotiator with the rank of ambassador. Since 1975 he has been adviser to many world corporations, financial institutions and sovereign wealth funds, and has been highly active in economic, financial and political relations between the United States and Japan.