

APEC Yokohama: Beyond Traditional Trade

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Two Decades of Enormous Change

In its two decades of existence, APEC has witnessed the two sides of the Pacific and the world at large going through dramatic changes. Not long after the launching of APEC, China rose out of a hibernation of over 500 years in perhaps the single most important event of the last quarter of the 20th century. By 2010, the rise of China has redrawn the world's economic geography. China has become the world's largest trader, with huge financial resources, able to compete in both unskilled-labor manufacturing and knowledge-intensive fields. The flying-geese pattern of East Asia's economic transformation continues, offering hope to later developers that they, too, could have their chance, if managed properly. With China's miraculous growth, East Asia as the center of economic growth shifts to a region where several other countries are also performing impressively, including India, Indonesia and Vietnam. This new geography will somehow have to be factored into the APEC agenda if it is to remain of relevance to the struggle for a better life of its member economies.

The history of APEC is by no means one of perfect success. Only three years since the announcement of the very ambitious Bogor Goals of free trade and investment, a deep crisis erupted in East Asia, creating enormous costs in Indonesia, Thailand, the Philippines and Malaysia. The crisis inspired East Asia to see the necessity of a regional mechanism of macroeconomic stabilization along the lines of the European stability pact. The idea of an Asian Monetary Fund (AMF) was floated. However, it stumbled on enigmatic opposition from the United States and ended up as the much more modest Chiang Mai Initiative (CMI) on bilateral currency swaps. It was later multilateralized on a bigger scale when the global economic crisis of 2008-2009 indicated the need for prompt and more sizable mutual support in times of crisis. The initiative can be seen as a fruit of East Asian integration, a process that APEC seeks to encourage without itself getting involved in negotiations.

Rendezvous with Regional Economic Integration

Another stream of large-scale changes that have swept over the Asia-Pacific during the APEC era relates to regional trading arrangements (RTAs). Not so long ago, East Asia was an outsider in regard to regional economic integration (REI). Even ASEAN did not feel comfortable with REI prior to the early 1990s. Yet, East Asia has joined the bandwagon of REI with great enthusiasm. ASEAN is being transformed into an ASEAN Economic Community. Through ASEAN, a network of free trade agreements (FTAs) has emerged involving China, Japan, South Korea, India, Australia and New Zealand. Consolidation of these FTAs into an East Asia-wide FTA has been studied, though governments have so far refrained from making such a choice. Besides, individual countries in East Asia have ven-

ured to all corners of the globe in pursuit of FTAs. In short, East Asia has turned in a short period from a desert of REI into a lush oasis. Perhaps the development is partly attributable to APEC, which in 1994 set a time line of 2010 at an APEC summit in Bogor, Indonesia, for free trade and investment for its developed member economies and 2020 for the less developed ones. The goals were said to be attained through open unilateral and plurilateral initiatives, of which a great many are currently evolving in the Asia-Pacific.

East Asian Integration at Crossroads

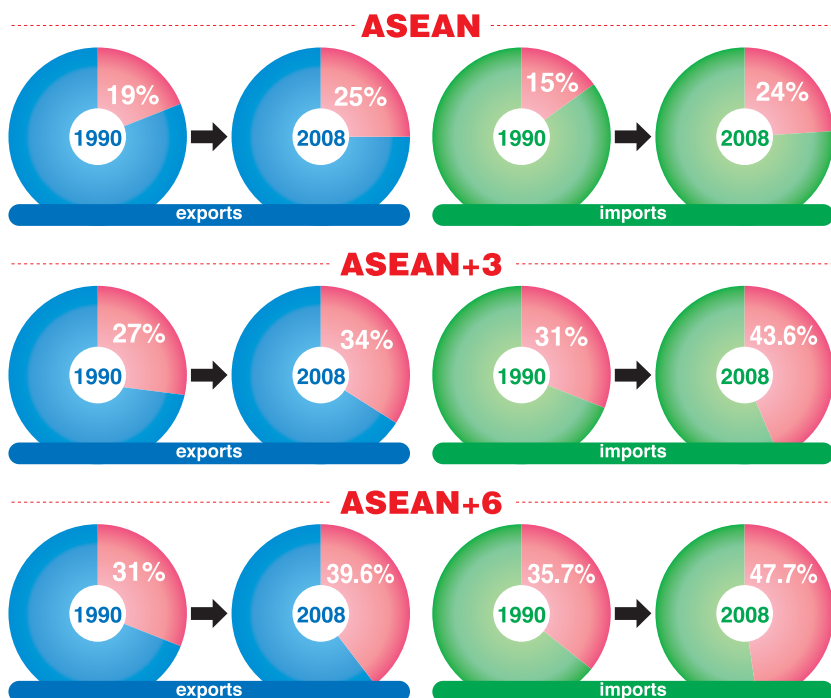
Amplified partly by the very active pursuit of REI by governments, economies in East Asia are deepening their de facto integration. As shown in *Chart 1*, intra-ASEAN exports and imports rose from 19% to 25% and from 15% to 24% of total exports and imports, respectively, between 1990 and 2008. In the case of ASEAN+3, they rose from 27% to 34% and from 31% to 43.6%, respectively. For ASEAN+6, the increases were from 31% to 39.6% and from 35.7% to 47.7%, respectively. In other words, East Asia is no longer a dwarf when it comes to the share of intraregional trade in total trade. Obviously, a few footnotes to these statistics are in order. The level of integration does differ across economies as well as across sectors. What is more, the figures also imply the continued reliance of East Asia on the rest of the world, particularly North America. The trans-Pacific connection makes the openness of East Asian REI a necessity. The underlying principles of the Bogor Goals remain relevant.

While busy negotiating an ever-widening network of FTAs, governments would be well advised to weigh the risks inherent in the current proliferation of REI schemes. Unchecked, such proliferation is bound to end up in disintegration. The risks can be mitigated somewhat by multilateralizing rules of origin (ROO). However, such multilateralization is partially by way of necessity. Attempts can also be made to get rid of highly restrictive elements in ROO. Some studies suggest that FTAs do differ indeed in their restrictiveness. East Asia is less restrictive than Europe. Detrimental effects of REI such as trade diversion and trade suppression can be reduced a great deal under a more pro-trade ROO. However, governments of East Asia should go beyond simply tinkering with ROO.

Consolidation to East Asia-wide FTA

As East Asia is increasingly immersed in REI, the incompleteness of the process in terms of geographical coverage is puzzling. China, Japan and South Korea have individually entered into free trade with ASEAN as a group and with its individual members. Yet the three countries have made no progress in forging such ties among themselves. There is no sign that a China-Japan free trade agreement will soon be announced. The same basically applies to Japan-South

CHART 1

ASEAN's intra-trade share of total trade

Source: United Nations "COMTRADE"

Korea free trade. The three countries seem to have become trapped in endless studies while their governments lack the determination to act. This fact of the lack of FTAs between China, Japan and South Korea has created very little noise as if people find it natural. Yet free trade in East Asia will remain highly incomplete as long as the triangular trade between China, Japan and South Korea remains beyond its reach.

The road to an East Asia-wide FTA has been explored. Governments have tasked a group of economists to study the feasibility of an East Asia Free Trade Area (EAFTA) under the ASEAN+3 framework. The same governments have also established an expert group on a Comprehensive Economic Partnership for East Asia (CEPEA), using the framework of the East Asia Summit (EAS) or ASEAN+6. Membership of this latter group overlaps a great deal

with that of the group on EAFTA. In the meantime, a Trans-Pacific Partnership (TPP) has also been set in motion, where some members of ASEAN participate actively. The issue of consolidation into a larger, more comprehensive framework has gotten more urgent (Chart 2).

East Asians are typically pragmatic in approaching REI. They allow the process to evolve under an agreement that is open to different interpretations. A pre-commitment to a grand design is avoided. Even the ASEAN Charter is less than "grand" as a design of regionalism. Criteria that one can use to judge options like the extent of geographical coverage are not in place. Governments are helpless when challenged to choose from the different options for consolidation. If history is of any value to guide future development, East Asians may benefit from learning that the European Union started off from a core which was large enough to serve as an attractor, but also not so large as to become too diverse for members to share a common set of goals. Such a core appears to be badly needed in East Asian integration. Otherwise, the region could face the danger of disintegration as a result of unchecked bilateral and plurilateral subregional initiatives on integration.

Limits to ASEAN Leadership

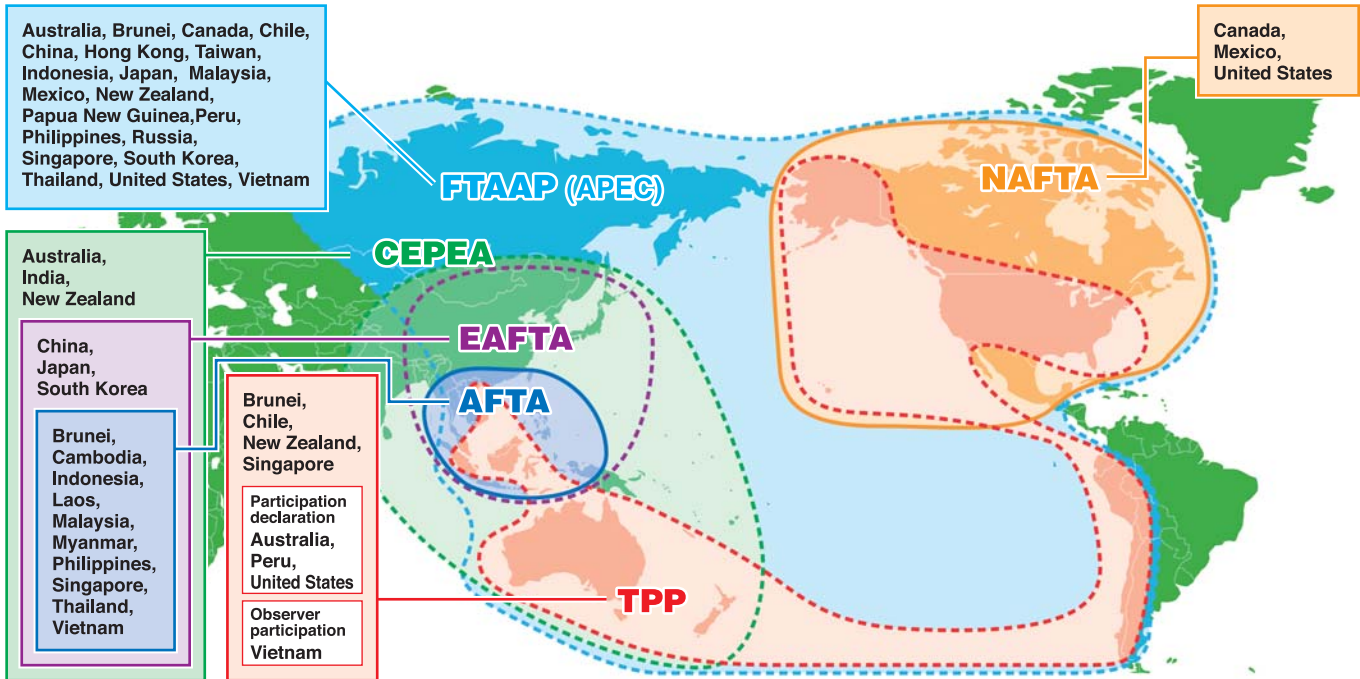
ASEAN cannot assume such a role. It is too small to be able to attract the larger economies of the region together. ASEAN is also not as cohesive as it appears at first glance. Although it has deepened, intra-ASEAN trade has remained small relative to total trade. ASEAN is also home to an immense income gap. Social indicators such as life expectancy, health-adjusted life expectancy (HALE), educational attainment, poverty and poor employment differ greatly between the members, making the stitching of a common position

vis-à-vis the rest of the world extremely difficult. Some of its members interact only very marginally with the outside world. ASEAN+3 is obviously larger, being home to both China, the world's largest trader, and Japan, another leading player in world trade. ASEAN trades in fact more with China, Japan and South Korea than internally among its members. On the question of cohesion, ASEAN+3 is certainly no better than ASEAN. What China thinks about Japan's leadership in East Asia and what Japan thinks about China's leadership in the same region are largely unknown to outsiders. Nevertheless, both China and Japan have unmistakably demonstrated their capability of climbing the ladder of development through trade. They have a lot to say about weaving success in world trade. What is more, ASEAN, China, Japan and South Korea have dealt intensively with one another as regards trade and investment. ASEAN+6 is even larger, but even less cohesive. Interactions between India and ASEAN, China, Japan and South Korea are more limited, though they may accelerate at a high speed in the wake of India's rapid economic growth. Under the current circumstances, ASEAN+3 or East Asia 13 appears to be in the best shape to serve as a core for East Asia-wide integration. Under East Asia 13, the strategic intent of regional integration can be laid down and the sequences for their attainment mapped in a way that will attract other countries from East Asia to join at a later stage.

APEC is not directly responsible for the proliferation of RTAs in East Asia, nor is it obliged to show the position on the path that East Asia should follow in its attempts to consolidate REI in the region. Nevertheless, APEC may assist by helping create a favorable environment for consolidation. By waiving the right to most-favored-nation treatment, APEC members from outside East Asia would provide consolidation with a tailwind.

CHART 2

Multilayered frameworks of regional economic integration in Asia-Pacific



Source: Ministry of Economy, Trade & Industry (METI)

Wider Agenda

The world at large and East Asia in particular have gone through a dramatic period of cumulative policy changes in the form of deregulation, liberalization, corporatization and privatization over the last 30 years or so. East Asians have benefited a great deal from this tireless reform. The fact that the health of the world economy now depends considerably on East Asian growth is a clear sign that the changes that are championed by governments in East Asia are highly opportune. Yet it is also true that the serial crises that hit the world almost regularly in the wake of the breathtaking changes, of which the Asian financial crisis of 1997-1998 is only one, are clear evidence that numerous imperfections in the policy environment are waiting to be addressed. APEC may continue to be seen primarily as a mechanism to advance trade, investment and related areas of policy-making. However, trade stretches over a very long sequence of processes: sourcing of inputs, production, distribution, retailing and cleaning up of all the myriad of wastes that emerge out of the entire chain. The processes are often distinguished between border processes and behind-border processes. Furthermore, burning trade issues do shift from one sector to another, depending on the specific problems of scarcity that confront mankind. To stay relevant, APEC may also have to venture to address new issues, paying the greatest attention to trade and trade-related aspects while doing so.

Food and energy crises have afflicted humans time and time again. Violence breaks out every day as competition for fresh water heightens. Scientists tirelessly seek to draw attention to the imbalance between the supply of and demand for basic materials. Every time prices skyrocket, adjustments usually follow, mitigating or even removing the imbalance. Scientists also warn of the dangers inherent

in the stock of greenhouse gases (GHG) and their continuous emissions into the atmosphere. Many of them even argue in favor of “de-growth.” Faced with these very difficult fundamental choices, governments will need some time to decide what to do. Countless debates will have to be staged before informed decisions are made. But putting decisions off to the indefinite future is also unwise. In some areas, immediate actions are badly needed.

There is no panacea to the issues of sustainability. The recurring material crisis is simply part of the human predicament. The APEC Economic Leaders’ Meeting in Yokohama in November 2010 is also not expected to produce miracles. Years and decades are needed to fix problems that have been cumulating over hundreds of years. However, APEC 2010 in Yokohama can contribute a great deal by setting the right agenda with the right focus. Drawing up such an agenda is necessarily difficult. In times of a phase transition or changes of a qualitative nature, such as the transition from solid to liquid or liquid to gas, core issues are hard to pinpoint.

APEC 2010 may decide to include in its agenda issues of sustainable growth, food and energy security, climate change, short-term economic recovery and related public debts in addition to trade and trade-related issues. Given the very technical nature of many of these issues, a question arises on the extent to which the annual leaders’ meeting is appropriate to deal with them. Perhaps the time has come for a less frequent leaders’ meeting, leaving the work of APEC more and more to ministers and senior officials. In other words, issues of an institutional setting may also have to be taken up at APEC 2010, noting that consensus typically takes time to filter through. **JS**

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