

Designing an East Asian FTA

By Zhang Yunling

New Economic Convergence

East Asian economic convergence is increasing. This process, started by a “flying-geese model,” is being led by Japan. It has helped to build up a “vertical” chain through capital flow, technological transfer and the supply of manufacturing parts, formulating a high level intra-regional integration based on market exchange. Until the mid-1990s, intra-regional trade in East Asia was as high as 50%. The financial crisis of 1997 changed the environment and structure of East Asian economic growth and integration. As a result, intra-regional economic activities slowed down. But following the recovery of the economies, East Asian intra-regional trade has been strengthening again. This trend has become even more evident since the intra-regional exports of East Asia have risen faster than exports to the rest of the world. Exports by these economies to East Asia contributed two-thirds of their total export increase in 2002. This intra-regional trade is increasingly based on the exchange of parts, components and other intermediate products, reflecting the development of intricate intra-regional production networks, in which production processes are subdivided among many different countries.¹ Foreign direct investment (FDI) flow plays a key role in creating this network. The network based on the exchange of trade and capital will have a profound impact on East Asian economic development since it will create a kind of “parallel development.” This is different from the traditional vertical and hierarchical transfer of technology.² This FDI-driven supply chain has created diverse and vibrant local industries around the East Asian region. The further supply chains are decomposed and extended geographically, the faster and more profuse will be the proliferation of new enterprises.³

However, compared with other

regions, East Asia is late in forging regional trade arrangements (RTA) and other institutional establishments. East Asian market-based integration shows its vulnerability. The new initiative for regional cooperation will certainly help to enhance and facilitate the further integration of the East Asian region.

East Asian RTAs

East Asian RTAs are currently being developed in a multi-layered process. They include both sub-regional agreements, like the ASEAN Free Trade Area (AFTA), the China-ASEAN free trade agreement (FTA) and bilateral (Japan-Singapore) arrangements. The question is how to consolidate all these different efforts into an integrated process.

East Asian market liberalization used to be based on a mostly multilateral approach. Real RTAs only appeared by the early 1990s when ASEAN launched its AFTA in 1992. Japan and South Korea began with a proposal for a bilateral FTA in 1999. Since then, several other initiatives have been made. Japan and Singapore concluded their negotiations and signed an agreement for a closer economic partnership (CEP) in early 2002 and China signed a framework document for a CEP in late 2002. Japan and ASEAN signed an economic partnership document in the same year. China, Japan and South Korea issued a declaration for economic cooperation in 2003.

The concern is how to move from the current multi-layered efforts into an integrated process, and finally toward an East Asian FTA (EAFTA). There may be three options:

- **Option 1:** To encourage the three “10 plus one” (ASEAN plus China, ASEAN plus South Korea and ASEAN plus Japan) FTA formula and merge the three into one EAFTA at a later date.
- **Option 2:** North East Asian countries

develop their own FTA and then integrate this with an AFTA to form an EAFTA.

- **Option 3:** To launch an EAFTA early on. This is parallel to the other multi-layered arrangements in the early stage.

It seems that “option 3” is more feasible than the other two, which means it is necessary to start early preparations for an EAFTA.

While encouraging the existing multi-layered efforts, it is important to incorporate the various cooperative mechanisms into a framework and organizational setup for long-term cooperation in East Asia.

If we envisage that these multi-layered arrangements can be finalized within five years, then it is reasonable to expect a “convergence process” after launching a new EAFTA (or an East Asian Closer Economic Partnership, EACEP). The research work for this should be started right now, and hopefully the negotiations can be concluded at an early date. As for the implementation, it would be ideal if an EAFTA could be realized by 2020 (by 2015 for most members, and 2020 for less developed economies).⁴

East Asian Identity

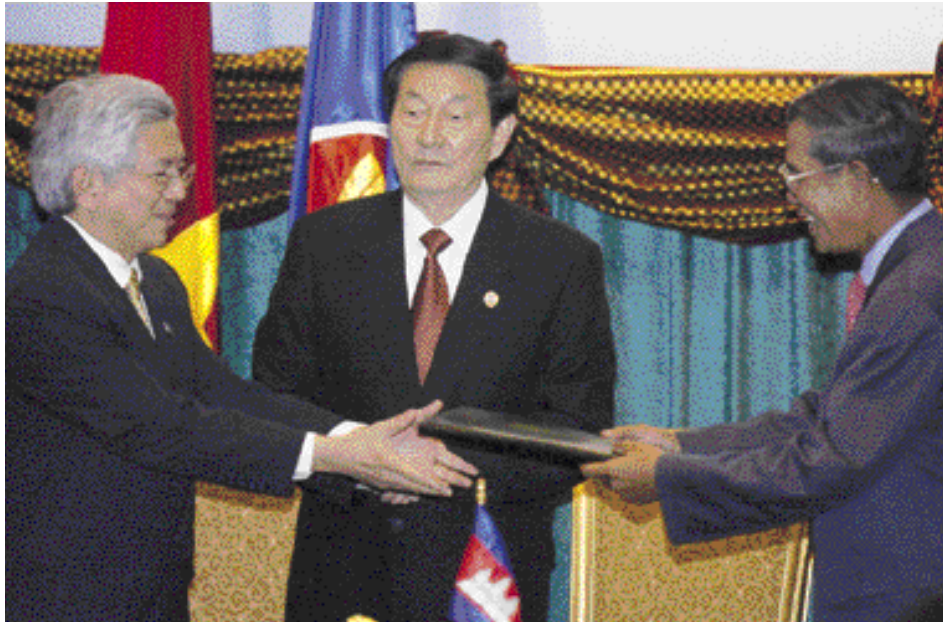
The long-term objective of East Asian cooperation is to recognize itself as an integrated region with shared common interests and regional institutions. Viewed from a geographical position, economic focus and practical angle, three large regions exist in the world today: The European Union (EU), North America and East Asia. In comparison, cooperation in the East Asian region lags behind. Although progress has been made in starting such cooperation, East Asia still lacks a clear long-term vision. The “East Asia Vision Group” (EAVG) called for an East Asian community, but no consensus has been reached yet.

Institutional building is crucial for the process of East Asian cooperation. Although the institutional building starts from a low level and on a multi-layered structure, progress must be achieved in developing a convergent institution for East Asia. As an important step, it is necessary to consider moving from the current "10 plus three" (ASEAN plus China, South Korea and Japan) structure to a regional organization, for example the Organization of East Asian Cooperation (OEAC) or the East Asian Economic Organization (EAEO) by 2010. The OEAC or the EAEO should have its secretariat and functional committees. It will not only continue the current activities, but will also develop new functions. The OEAC or the EAEO will not be replaced by or merged with other multi-layered arrangements in the region in the near future. However, efforts should be made to develop a framework and institutions on the regional level, such as an EAFTA, financial arrangements and sub-regional development projects. Political and security cooperation should also be finally integrated into the cooperation process. The OEAC or EAEO should extend its membership to all East Asian countries eventually.

There is a long way to go before East Asia can become a fully integrated region. But the efforts must be made from now on to bring about this goal.

China's Role

Following the economic success and World Trade Organization (WTO) accession, China has become very active in forming and promoting RTAs, especially in East Asia. In 2002, China and ASEAN signed the framework agreement for comprehensive economic coopera-



Former Chinese Premier Zhu Rongji (center), Cambodian Prime Minister Hun Sen (right) and former ASEAN Secretary-General Rodolfo Severino at the ASEAN summit meeting in Phnom Penh

tion, including the conclusion of an FTA within 10 years.

However, China will not just stop at this arrangement. Its larger interest lies in an EAFTA and hopefully an OEAC or EAEO. China proposed a Northeast Asian FTA (NEAFTA) in 2002 based on the joint studies of three official research institutions. China also supports Thailand's proposal for an early study and preparations for an EAFTA.

China insists that East Asian cooperation should not be limited to economic areas. East Asia needs a strong political built-up. East Asian community building will cover comprehensive areas of cooperation.

China understands that as a developing country, it needs strong capacity building to accommodate the quick process of globalization on the one hand, and regionalization on the other. China does not intend to be a leader of East Asian cooperation, but it is certainly preparing to play an active role. **JS**

Notes

- 1) The World Bank, "East Asia Update: Looking Beyond Short-term Shocks," April 2003, p.15
- 2) Chen Yu-shi, "A New Paradigm Shift in East Asian Economic Studies," *Ritsumeikan Journal of Asia-Pacific Studies*, vol.10, December 2002, P. 10
- 3) David Roland-Holst, Iwan Azis and Li-Gang Liu, "Regionalism and Globalism: East and Southeast Asian Trade Relations in the Wake of China's WTO Accession," Asian Development Bank Institute Discussion Paper Series, January 2003, P.16
- 4) As proposed by the East Asia Vision Group's report, the establishment of an EAFTA will be well ahead of the Asia-Pacific Economic Cooperation's goal declared in Bogor, Indonesia, in 1994, i.e. 2020 for developing countries, and will surely help to realize it.

Zhang Yunling is a professor and the director of the Institute of Asia-Pacific Studies at the Chinese Academy of Social Sciences in Beijing.