

# The Emergence of Economic Regionalism in Asia

## Trends and Prospects

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28 August 2008

Lecture at the GIARI Summer Institute  
Waseda University, Tokyo

# Main messages

- Asian integration is rapid, broad, with global links
- Cooperation is accelerating, but needs more focus
- Distinctive Asian regionalism: open, multi-speed, multi-track, pragmatic, bottom-up
- Need to develop deeper institutional capabilities
  - Asian Financial Stability Dialogue
  - Asian Secretariat for Economic Cooperation
- Asian regionalism is good for Asia, good for the world

# Integrating Asian economies

Integrating Asia (16 economies):

-87% of total Asia's population

-96% of total Asia's output



# Priorities and approaches

- Asian Financial Crisis of 1997/98 as the trigger for the emergence of regional cooperation initiatives
- Four priority areas:
  - i. Trade and investment
  - ii. Financial systems
  - iii. Macroeconomic links
  - iv. Social & environmental issues
- Building regional architecture of cooperation

# All Indicators of Integration are Rising

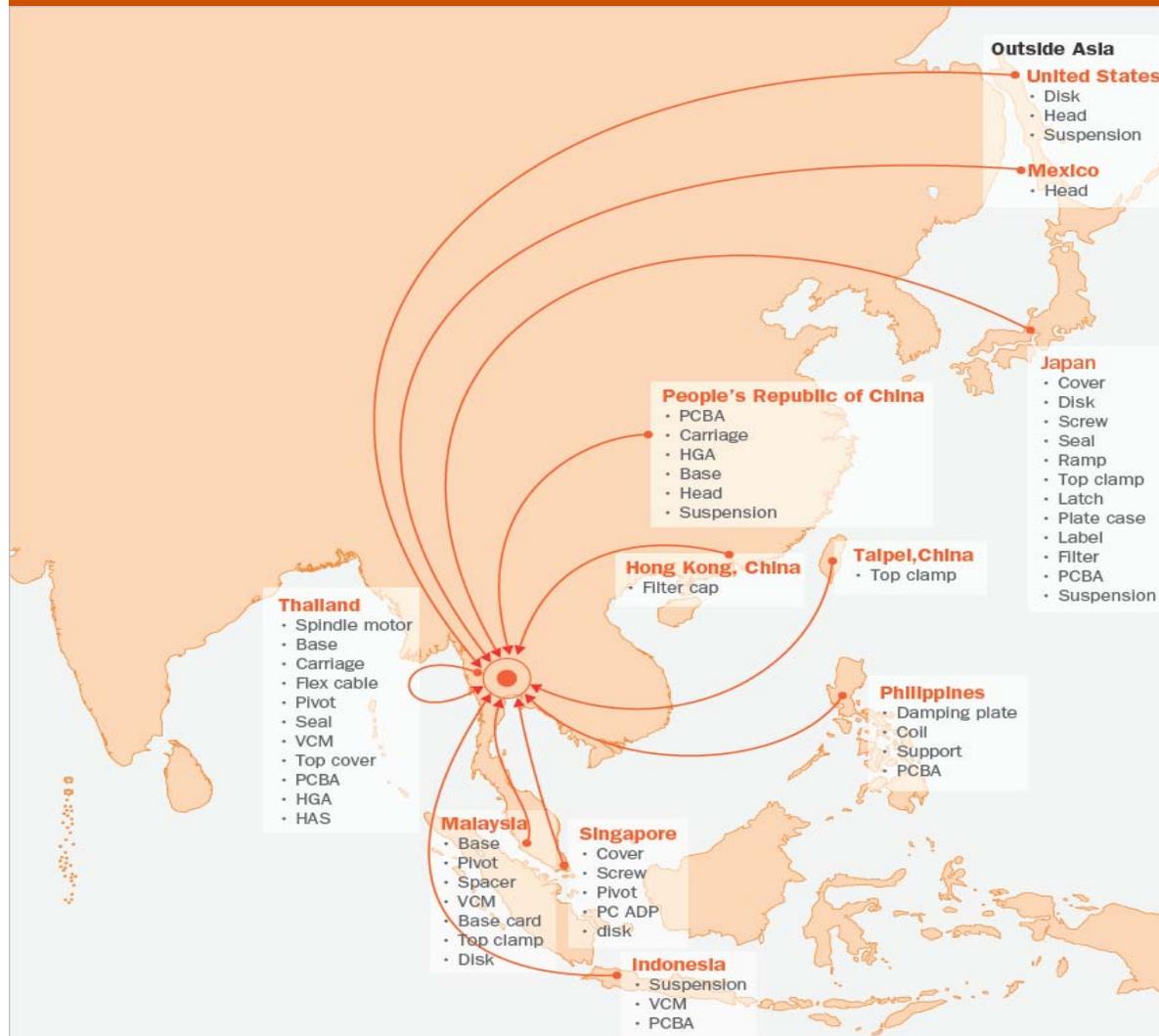
Advancing integration: regional indicators, pre- and post-crisis



# Drivers of Asian regionalism today

- Asia's global economic interests are converging (as demonstrated by the 1997/98 financial crisis)
- Reaction to the progress of regionalism in other parts of the world (Europe, North America, Latin America)
- Exceptional growth makes Asian markets increasingly important to each other
  - Asia's dominance of global manufacturing depends on regional production networks

# How Asia makes a disk-drive



- Assembly production of raw materials, parts, components
- Production and trade fragmentation: location is decided by the cost and availability of inputs, economic infrastructure, local environment
- Technology policy and upgrading is also important

# Integration implies cooperation

- Manage interdependence
  - Reduce regional trade barriers
  - Ensure financial stability and promote financial integration
  - Cooperate on macroeconomic and exchange rate policies
  - Provide public goods in health, security, environment
- Reinforce national policy
  - Support integration against special interests
- Represent shared global interests
  - Champion open, stable global markets
  - Ensure support for development
  - Assume burden of global institutions

# Issues on Regionalism

- Regionalism and discrimination
- Intermediary step towards global integration
- Free riding and reciprocity
- Membership fee and rules of entry
- GATT/WTO Article XXIV
- Open Regionalism

# Logic of regional collective action

- Providing new regional public goods
- Managing spillovers among economies
- Exercising influence in global economic forums
- Liberalizing trade and investment
- Adding value to national policy making

# The Benefits of Regionalism Outweigh its Costs

## Responses of Perception Survey to 600 Asian Opinion Leaders

% of respondents answering 'high' or 'very high'

Percent

0 10 20 30 40 50 60 70 80

**Costs** Greater divide between rich and poor as opportunities are unevenly distributed



Weaker economic linkages with non-Asian countries



Loss of independence of national economic policies



Loss of national culture and identity



**Benefits** Faster and more dynamic economic growth



Stronger Asian voice in international negotiations



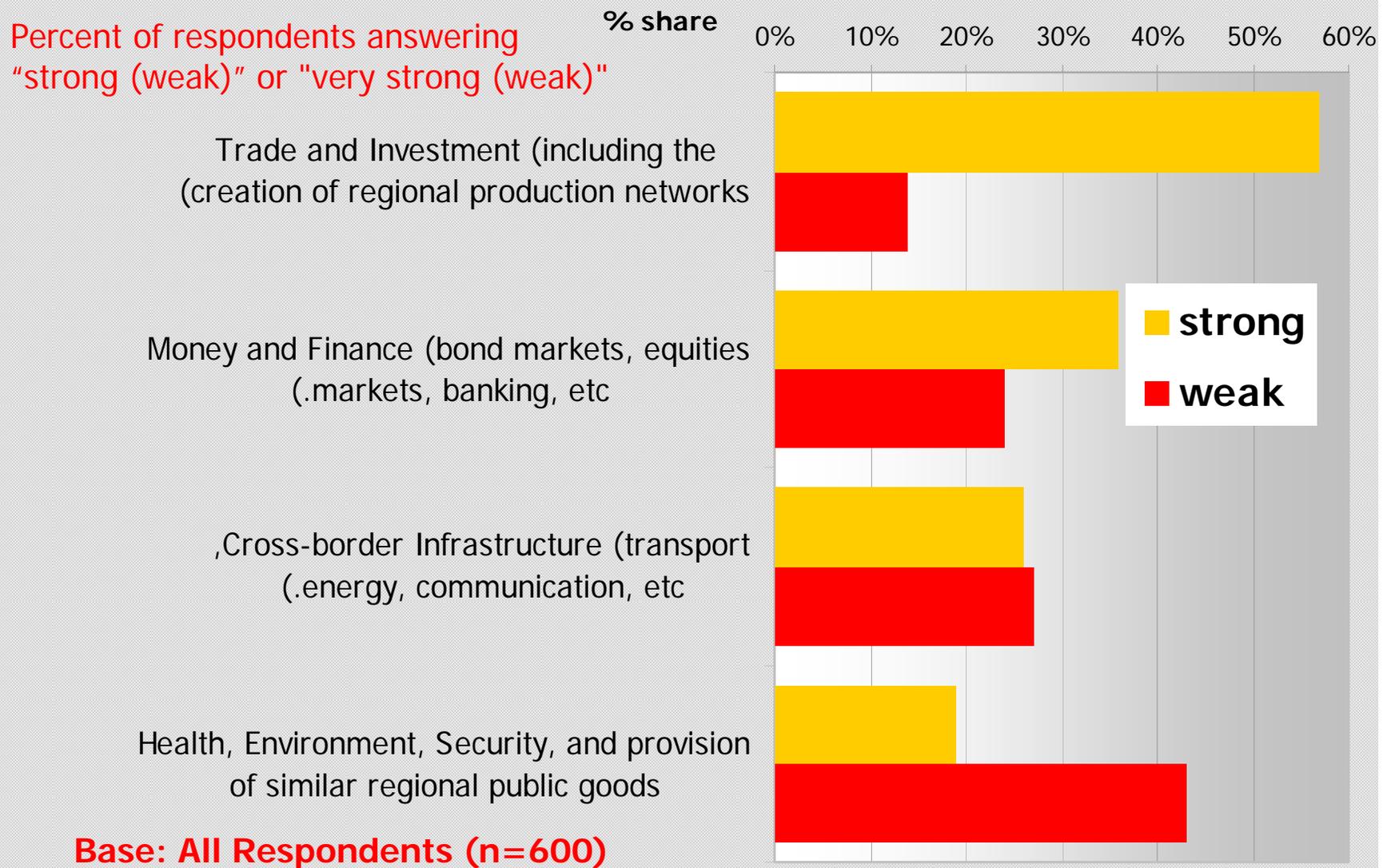
Deeper integration with the global economy



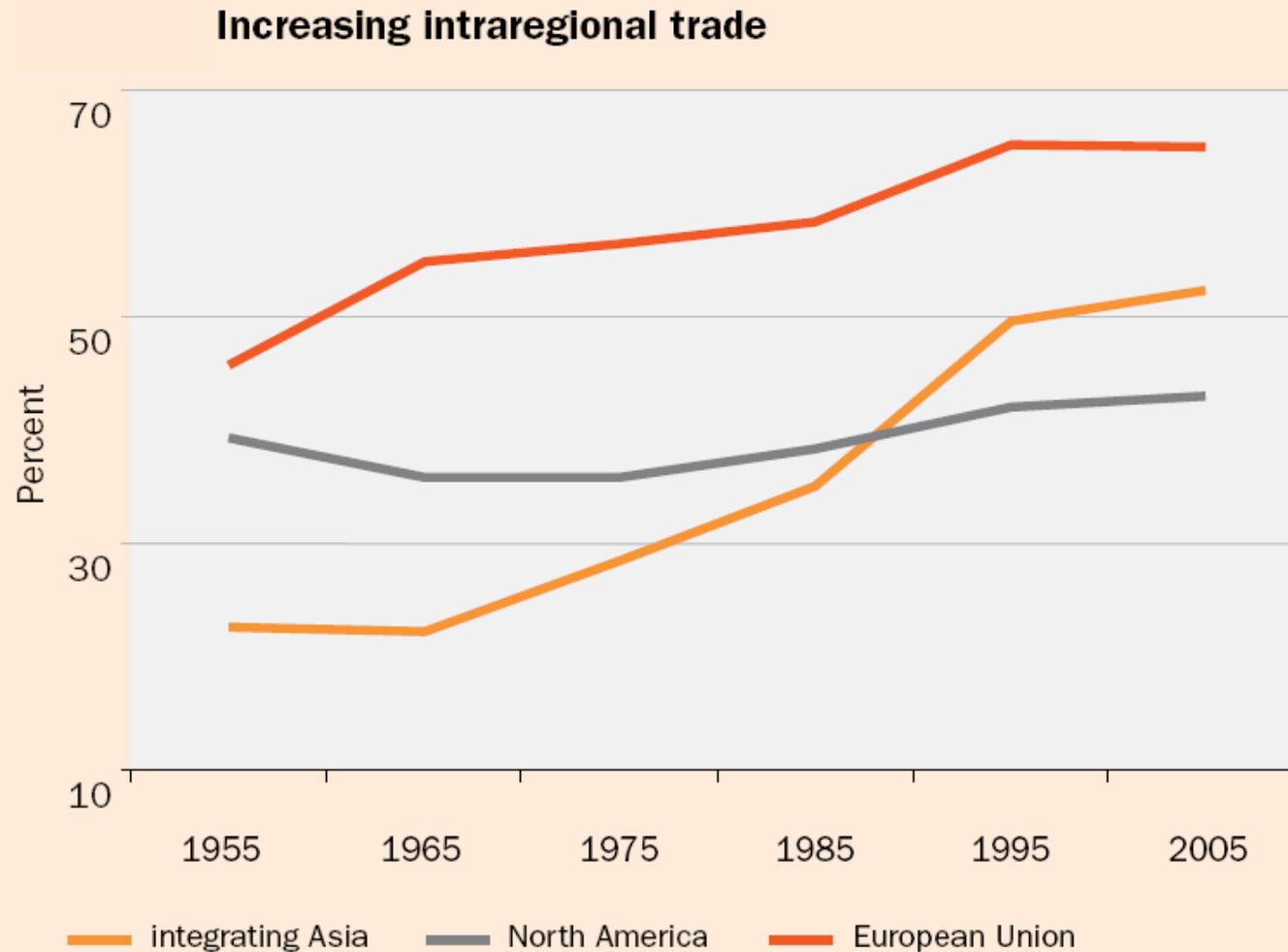
Alternative to global multilateral institutions such as IMF, WTO, etc.



# Assessment of economic relations



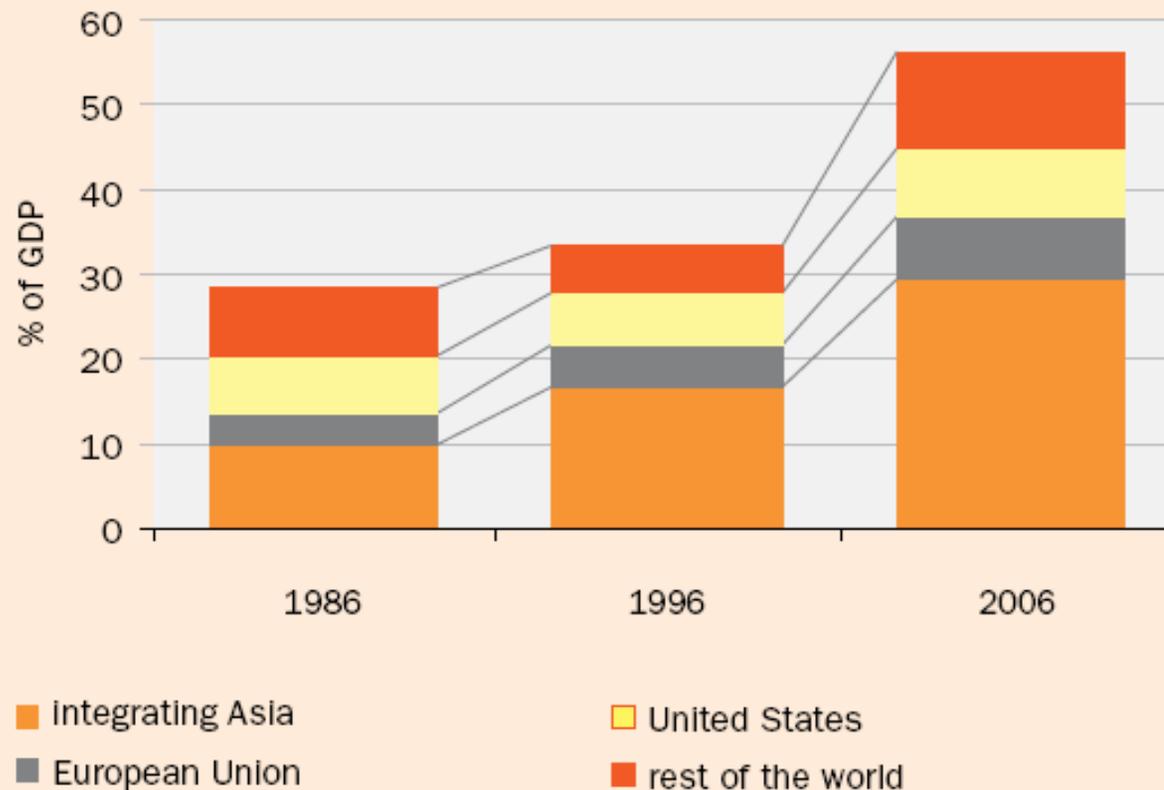
# Growing Trade Integration



# Open Regionalism No Fortress Asia

## Increasing trade links

Trade of Integrating Asia as a share of GDP, by destination



# Trade Policy in a Fractious Global Environment

## Integrating Asia's free trade agreements

Status as of December 2007

Negotiating body	Concluded	Under negotiation	Proposed	Total	of which	
					Inside IA	Outside IA
ASEAN	2	4	0	6	4	2
Brunei Darussalam	3	0	4	7	3	4
Cambodia	1	0	2	3	2	1
China, People's Republic of	7	6	9	22	8	14
Hong Kong, China	1	1	0	2	1	1
India	8	10	12	30	8	22
Indonesia	3	1	6	10	4	6
Japan	8	7	4	19	12	7
Korea, Republic of	6	5	11	22	9	13
Lao People's Dem. Rep.	3	0	2	5	3	2
Malaysia	4	5	4	13	5	8
Myanmar	1	1	2	4	2	2
Philippines	2	0	4	6	3	3
Singapore	11	10	5	26	6	20
Taipei, China	4	2	1	7	0	7
Thailand	6	6	6	18	7	11
Viet Nam	1	1	2	4	3	1
<b>Total</b>	<b>44</b>	<b>49</b>	<b>41</b>	<b>134</b>	<b>30</b>	<b>104</b>
Concluded					14	30
Under negotiation					8	41
Proposed					8	33

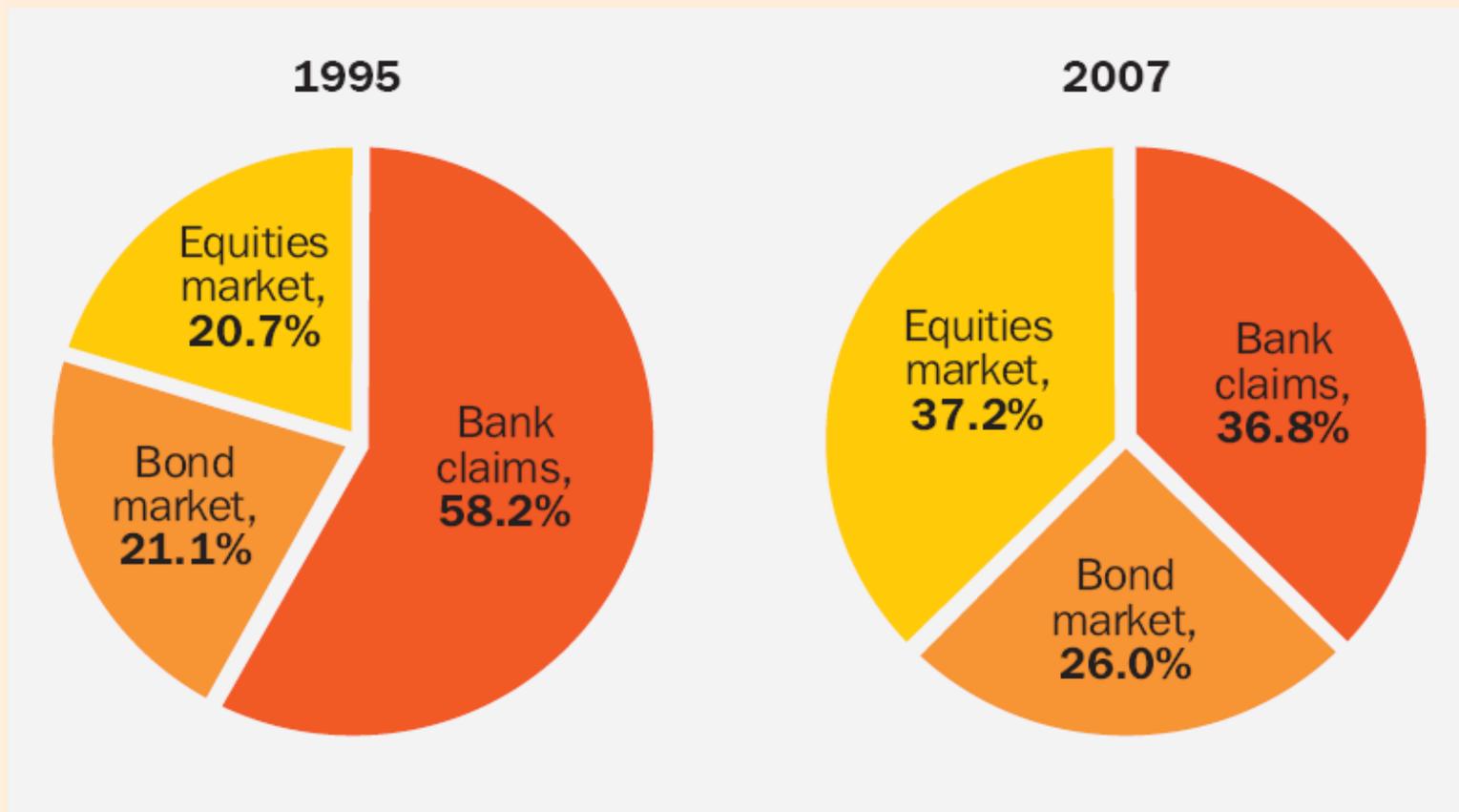
# Priorities for Integrating Production & Trade

- Supporting global trading system
- Maintaining open investment regimes
- Pursuing regional cooperation as widely as possible
- Developing guidelines for best practices in FTAs
- Enhancing regional connectivity
- Improving technological competitiveness

# Integrating Financial Markets

## Increasing share of capital markets

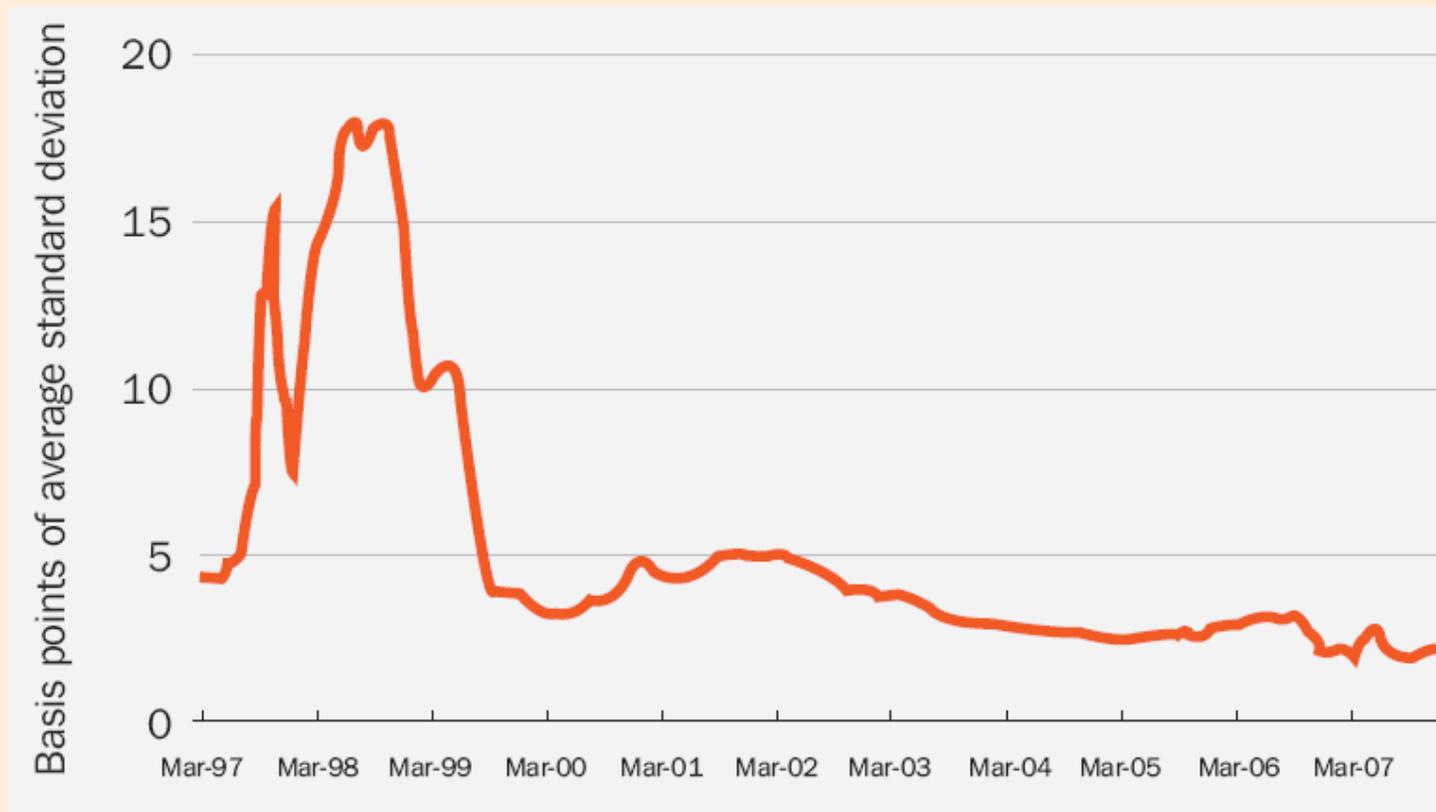
Share in total financial assets in Integrating Asia



# Financial integration is less advanced, but under way: Price indicators

## Declining interbank rate differentials

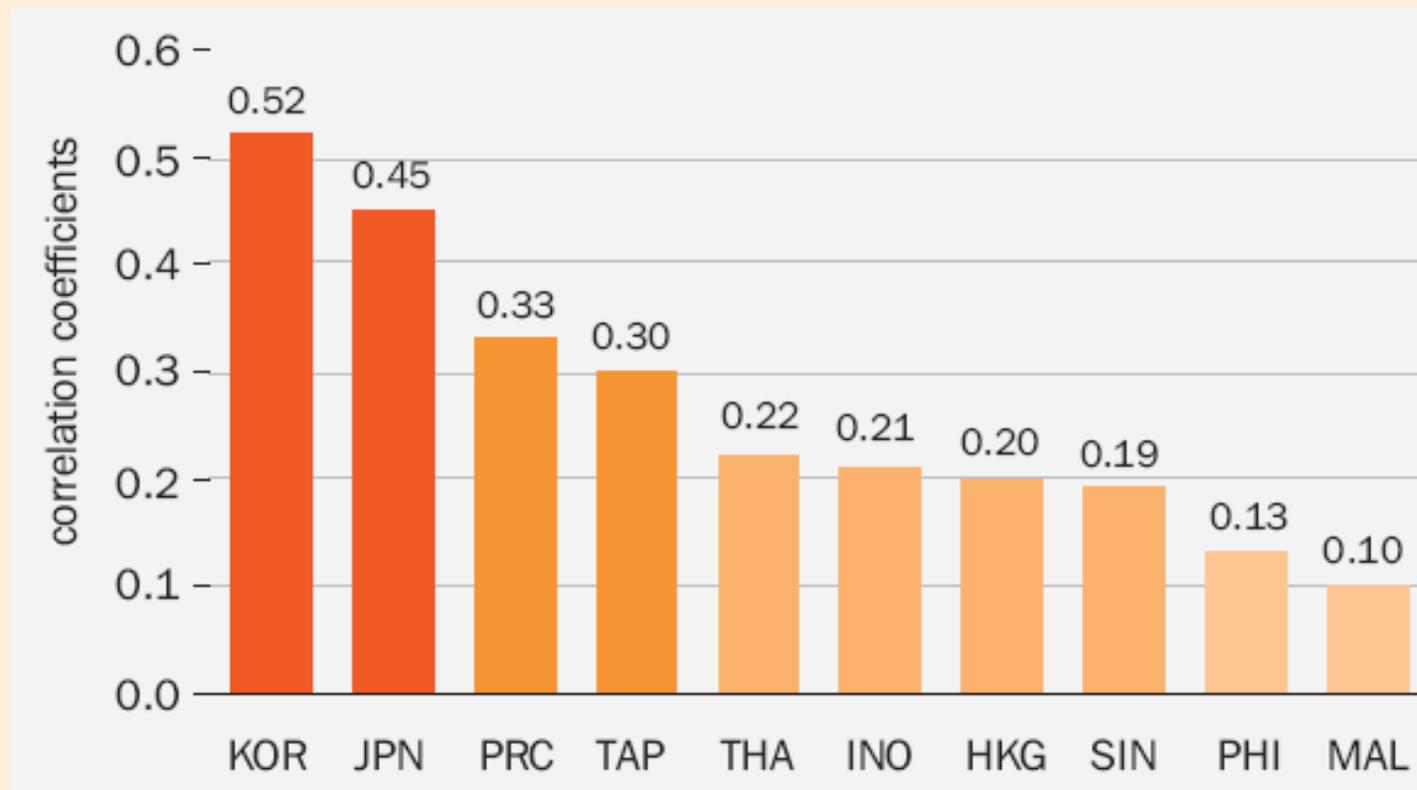
(Standard deviation of cross-market overnight interbank rate differentials)



# Stock Price Correlation

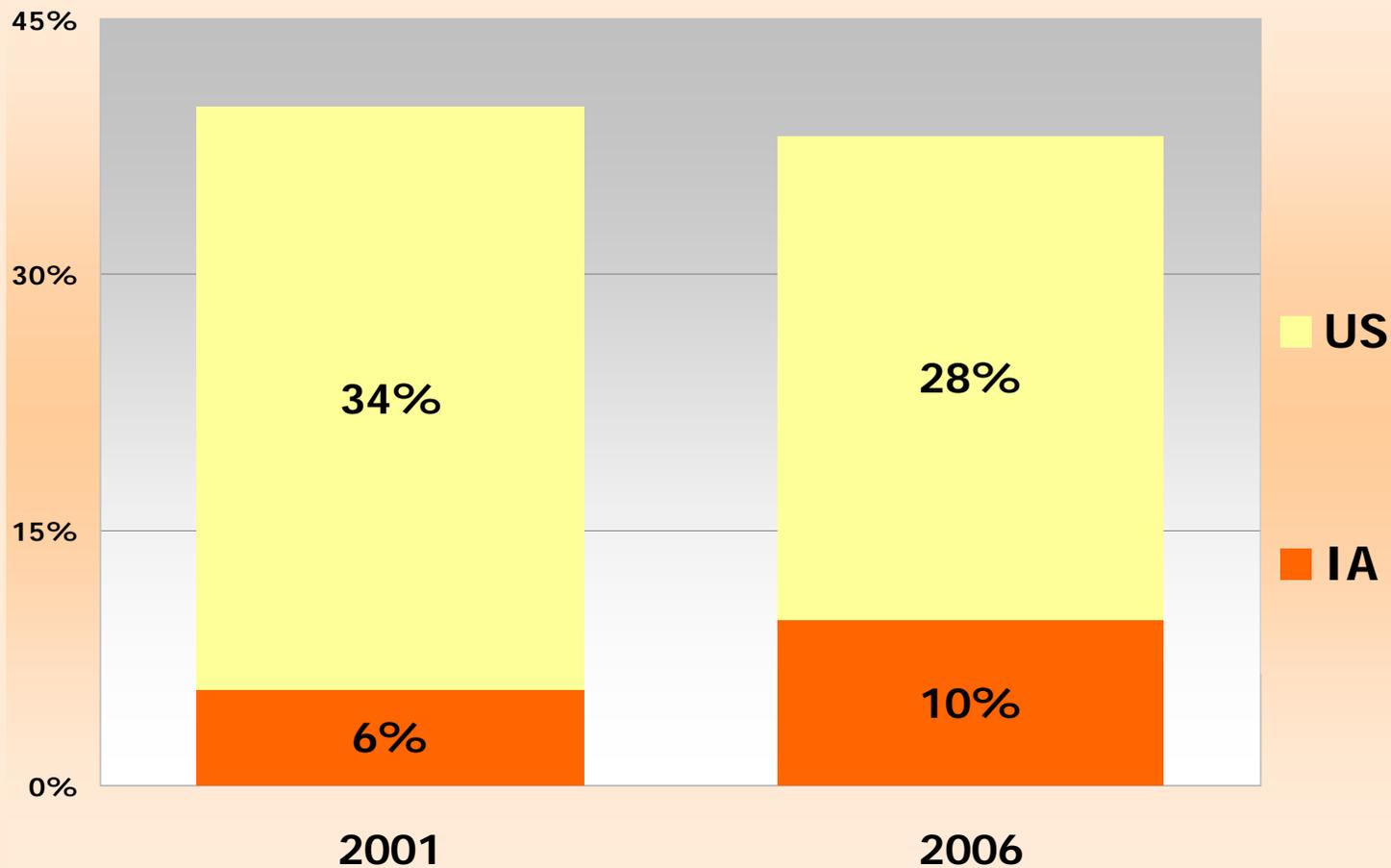
## Correlation of stock price indexes in Integrating Asia

Absolute changes in the average of bilateral correlation coefficients precrisis (1990:Q2–1996:Q4); postcrisis (2000:Q1–2006:Q2)



# Financial Integration is Under Way: Quantity Indicators

Integrating Asia's portfolio investment in IA and the US  
% share on total assets invested abroad



# Asia's National, Regional, and Global Financial Centers



## Asia's Financial Centers

3 Global

5 Regional

18 National

Growing regional and global integration

Increasing competition

Developing infrastructure

Domestic financial reforms

Harmonizing regulations

Regional cooperation

# Financial Cooperation Forums

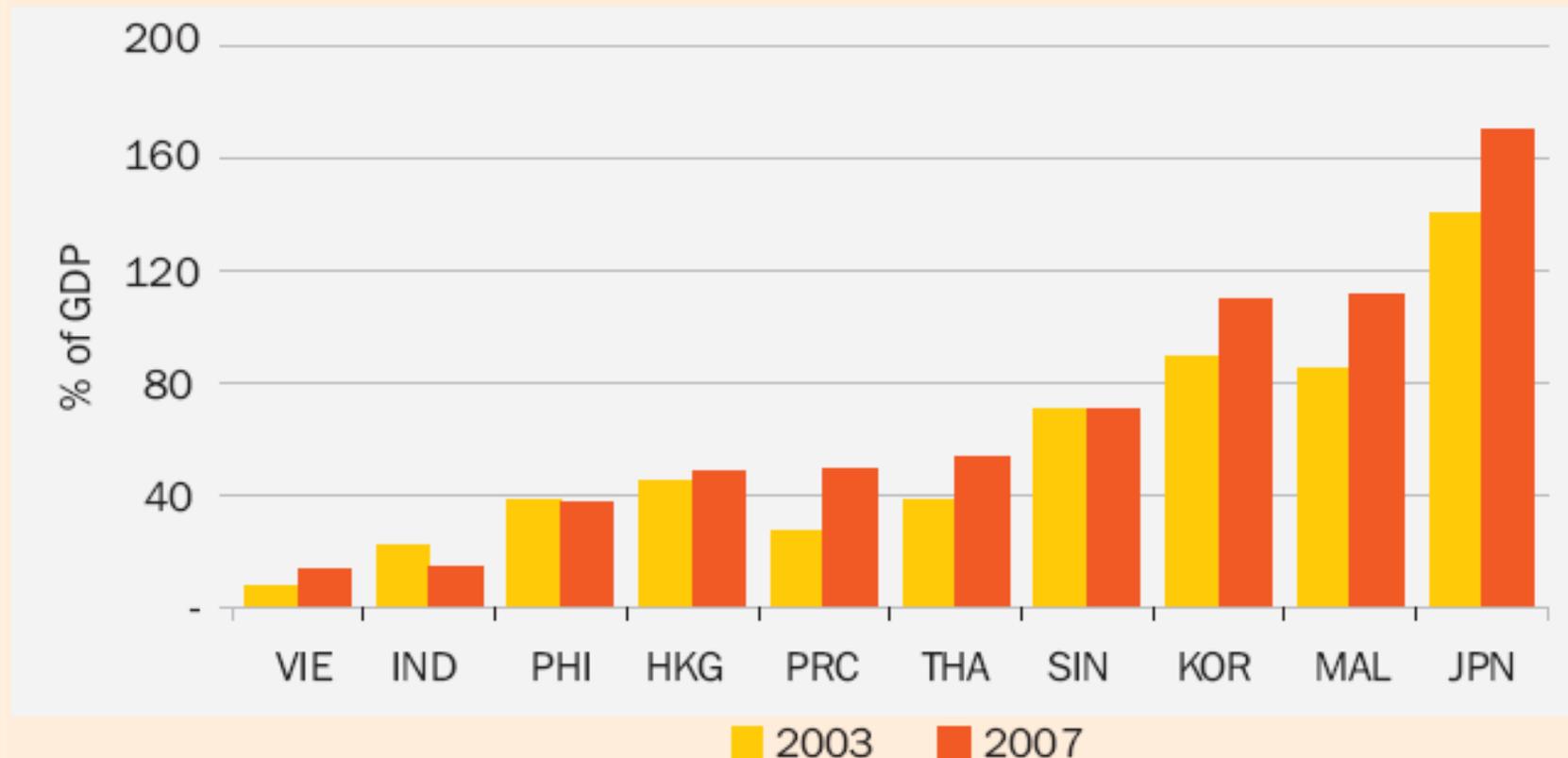
## . Emerging monetary and financial cooperation

Forum	Finance ministry-led cooperation				Central bank-led cooperation			Others	
	APEC	ASEAN	ASEAN+3	ASEM	EMEAP	SEACEN	SEANZA	ACD	EAS
Year established	1989	1967	1999	1996	1991	1966	1956	2002	2005
Number of members	21	10	13	45	11	16	20	28	16
Function	Policy dialogue/information exchange	√	√	√	√	√	√	√	√
	Surveillance/peer review		√	√		√			
	Regional financing arrangements		√	√		√			
	Regional capital-market development	√	√	√		√			
	Capacity building	√	√	√	√	√	√	√	
	Research	√	√	√	√	√	√		

# Effects of Financial Cooperation

## Growing local-currency denominated bond markets

Share of total issuances in GDP, 2003 and 2007



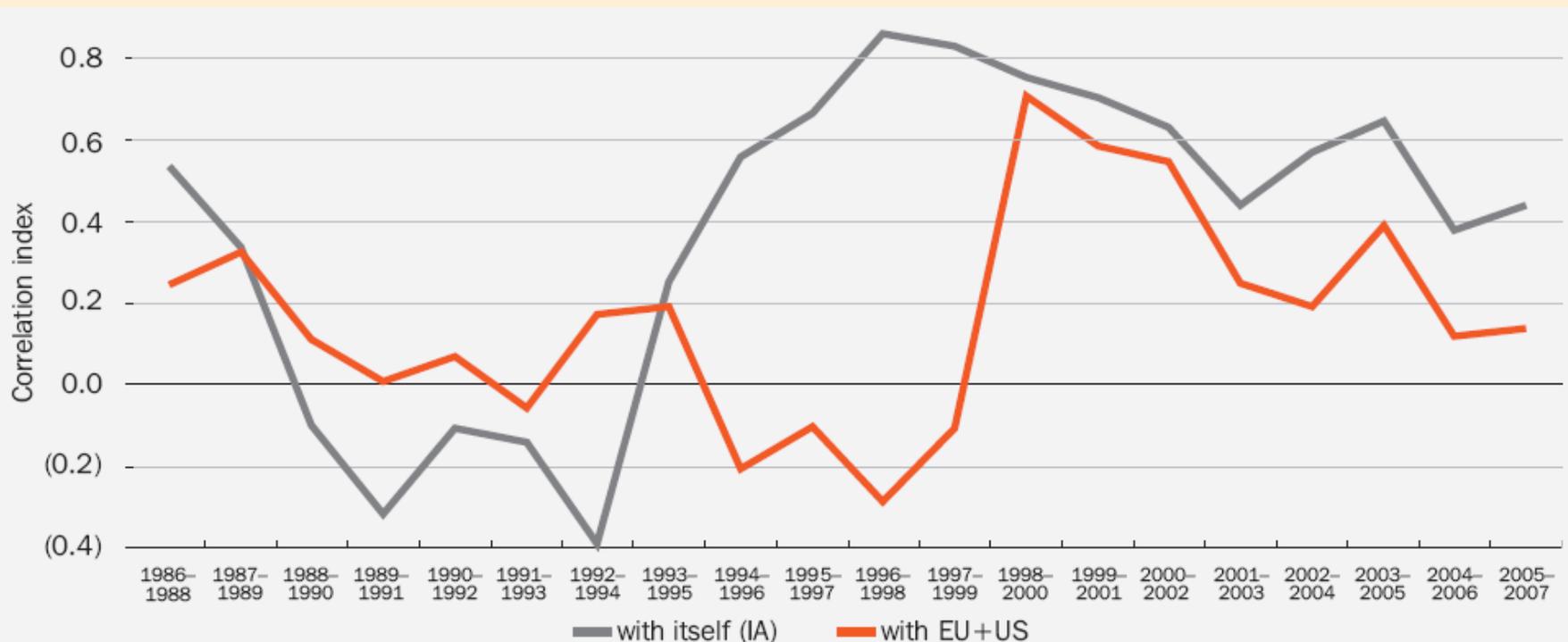
# Priorities for Integrating Financial Markets

- Improving financial market surveillance
  - Asian Financial Stability Dialogue
- Promoting harmonization and mutual recognition
- Strengthening financial markets & infrastructure
  - Develop local currency bond markets
- Liberalizing capital accounts and cross-border financial services prudently

# Deepening macroeconomic interdependence

## Output Correlation of Integrating Asia with itself and EU+US

Correlation of de-trended quarterly growth rates of GDP

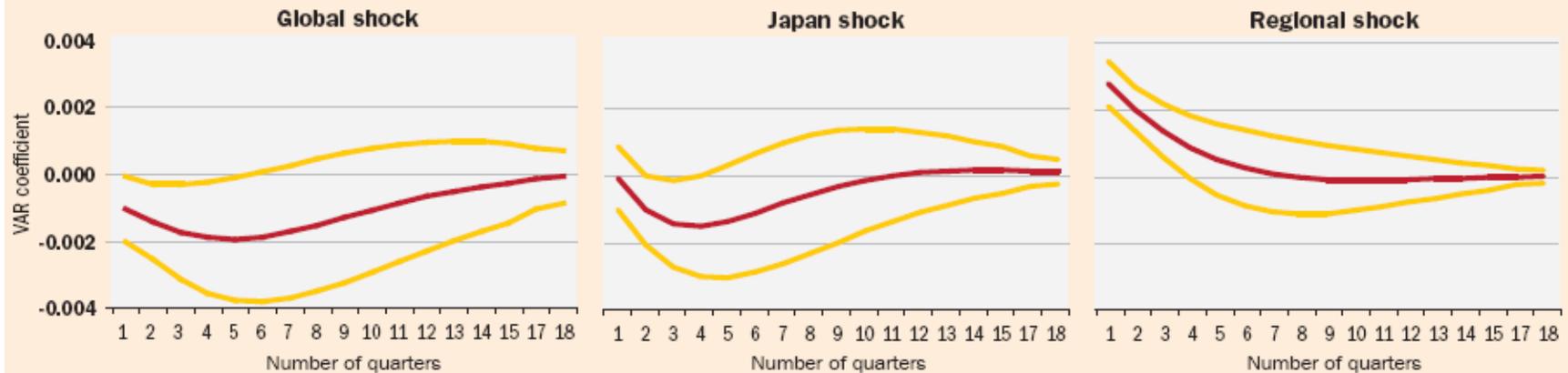


# Transmission of Shocks

## Global and regional shocks have greater impact on Asian economies

Reactions by type of shock per month pre- and post-crisis

### a. Precrisis



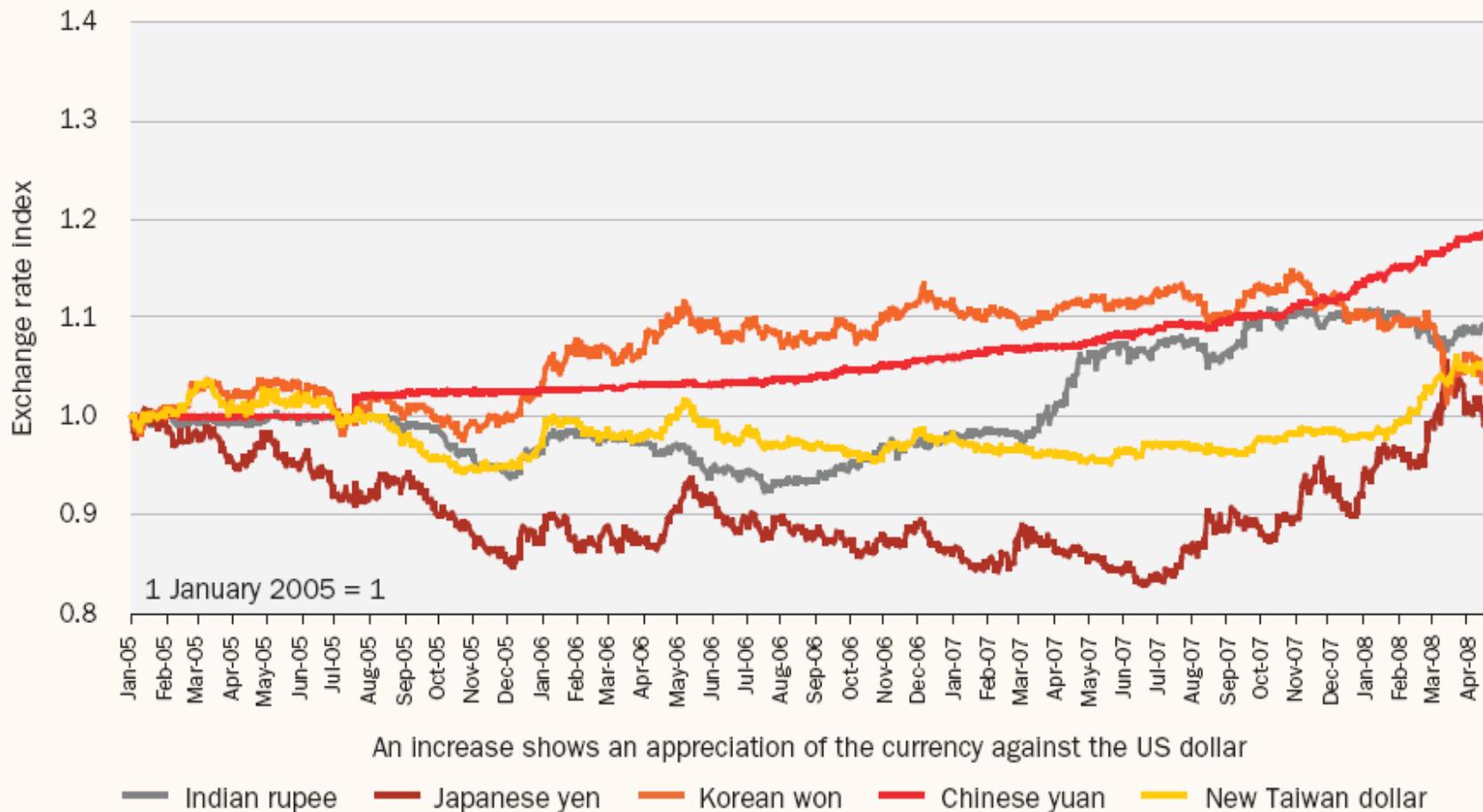
### b. Post-crisis



# Trend of Asian Exchange Rates

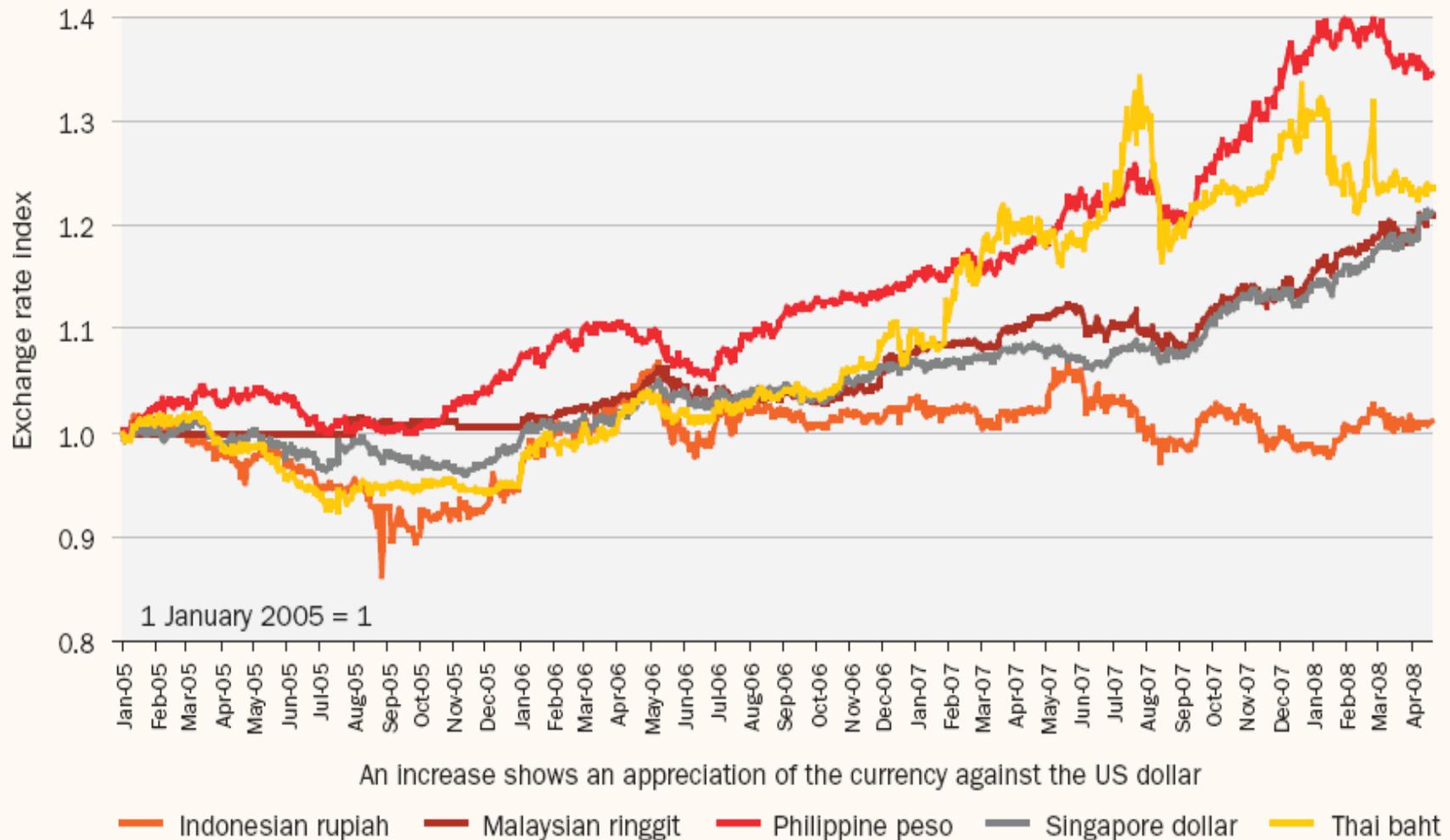
## Trend of Asian currencies against the US dollar

### a. Major Asian currencies



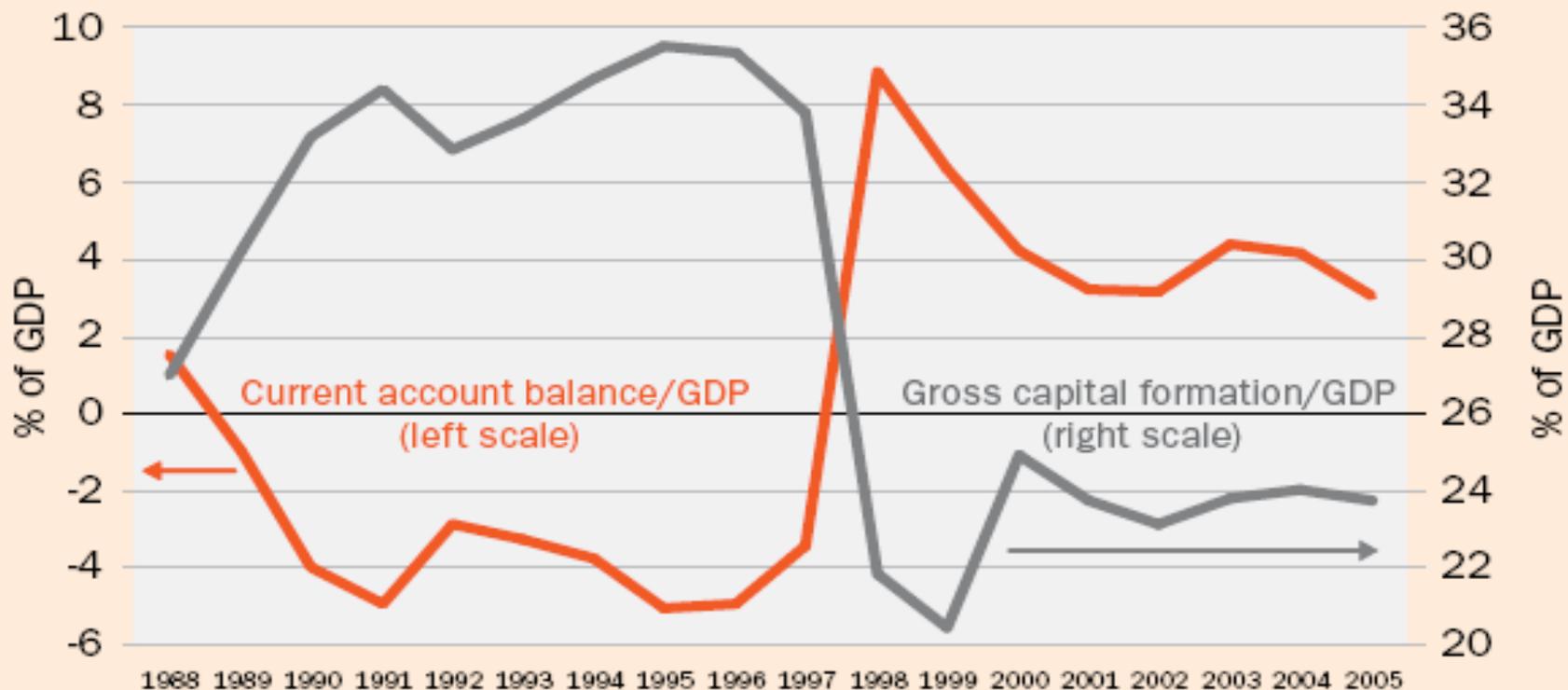
# Trend of Asian Exchange Rates ./.

## b. Major ASEAN currencies



# Needing Adjustment Ahead

**Declining investment and rising current account surpluses**  
(simple average of the 5 most crisis-affected Asian countries)



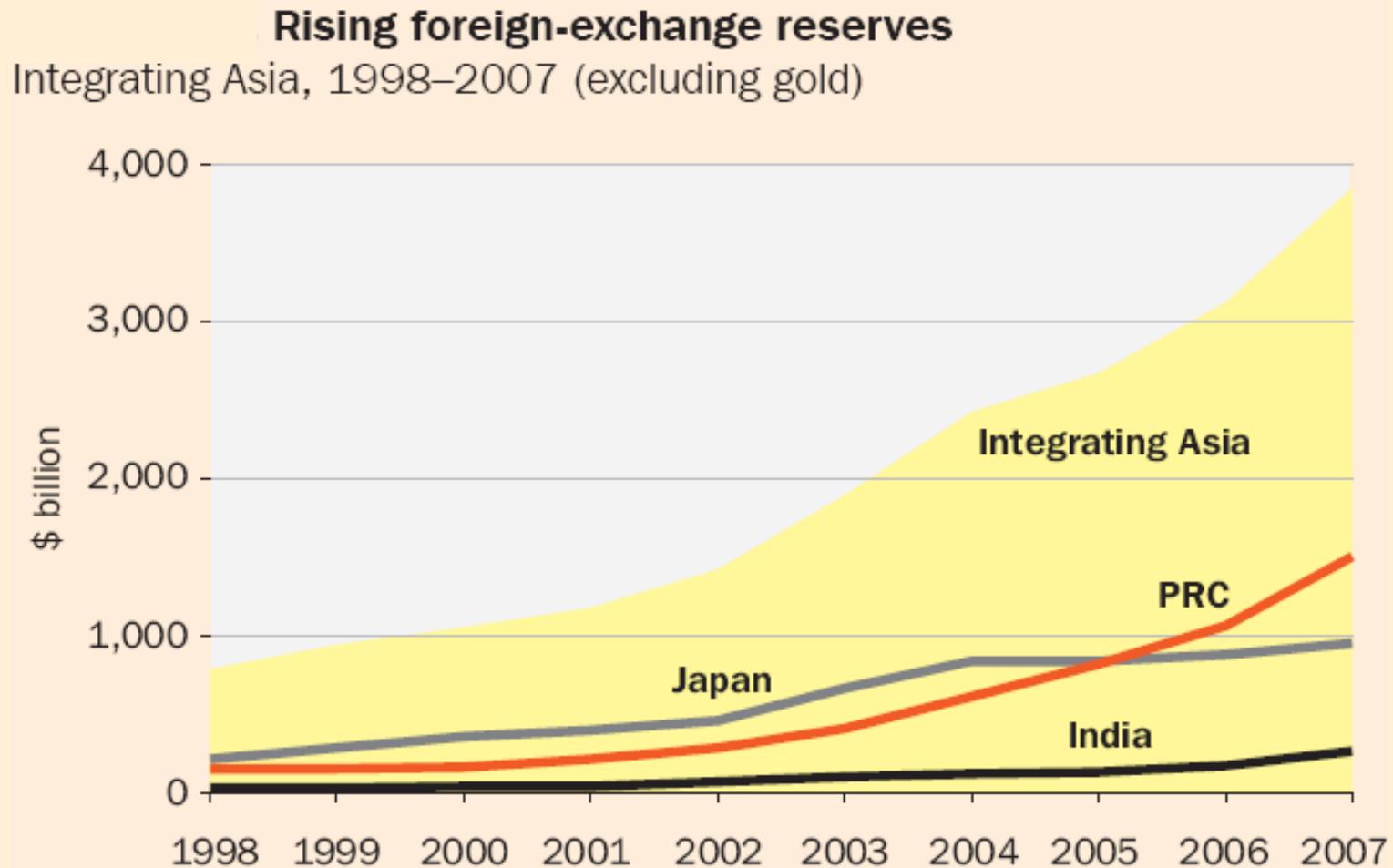
# CMI Swap Arrangements

## Swap arrangements under the Chiang Mai Initiative

\$ billions as of January 2008

From \ To	PRC	Japan	Rep. of Korea	Indonesia	Malaysia	Philippines	Singapore	Thailand	Total
PRC		3.0	4.0	4.0	1.5	2.0		2.0	16.5
Japan	3.0		13.0	6.0	1.0	6.0	3.0	6.0	38.0
Korea, Rep. of	4.0	8.0		2.0	1.5	2.0		1.0	18.0
Indonesia			2.0					18.5	2.0
Malaysia			1.5						1.5
Philippines		0.5	1.5						2.0
Singapore		1.0							1.0
Thailand		3.0	1.0						4.0
<b>Subtotal</b>	<b>7.0</b>	<b>15.5</b>	<b>23.0</b>	<b>12.0</b>	<b>4.0</b>	<b>10.0</b>	<b>3.0</b>	<b>9.0</b>	<b>84.0</b>
ASEAN Swap Arrangements									2.0
<b>Total</b>	<b>7.0</b>	<b>15.5</b>	<b>23.0</b>	<b>12.0</b>	<b>4.0</b>	<b>10.0</b>	<b>3.0</b>	<b>9.0</b>	<b>86.0</b>

# Managing Foreign Reserves: New Challenges Ahead



# Agenda for Macroeconomic Cooperation

- Making macroeconomic dialogue and surveillance more effective
  - Asian Secretariat for Economic Cooperation
- Strengthening Asia's short-term financing facility
  - Chiang Mai Initiative
- Enhancing regional demand and maintaining robust growth
- Cooperating in exchange rate management

# Many are still left behind

## Gains In the battle against poverty

Economy	Poverty index				Survey year	
	\$1-a-day		\$2-a-day		Initial	Final
	Initial	Final	Initial	Final		
China, People's Rep. of	28.3	10.8	64.5	37.8	(1993)	(2004)
Cambodia	25.5	18.5	76.5	61.6	(1993)	(2004)
India	41.8	35.1	85.1	79.6	(1993)	(2004)
Indonesia	17.4	7.7	64.2	52.9	(1993)	(2002)
Lao PDR	47.8	28.8	89.9	74.4	(1992)	(2002)
Malaysia	0.0	0.0	19.2	9.8	(1993)	(2004)
Philippines	18.1	13.2	52.7	43.6	(1994)	(2003)
Thailand	6.0	0.0	37.5	25.8	(1992)	(2002)
Viet Nam	27.3	8.4	73.5	43.2	(1993)	(2004)

Several major groups have been left behind

Labor market and investment policies can help alleviate poverty and exclusion

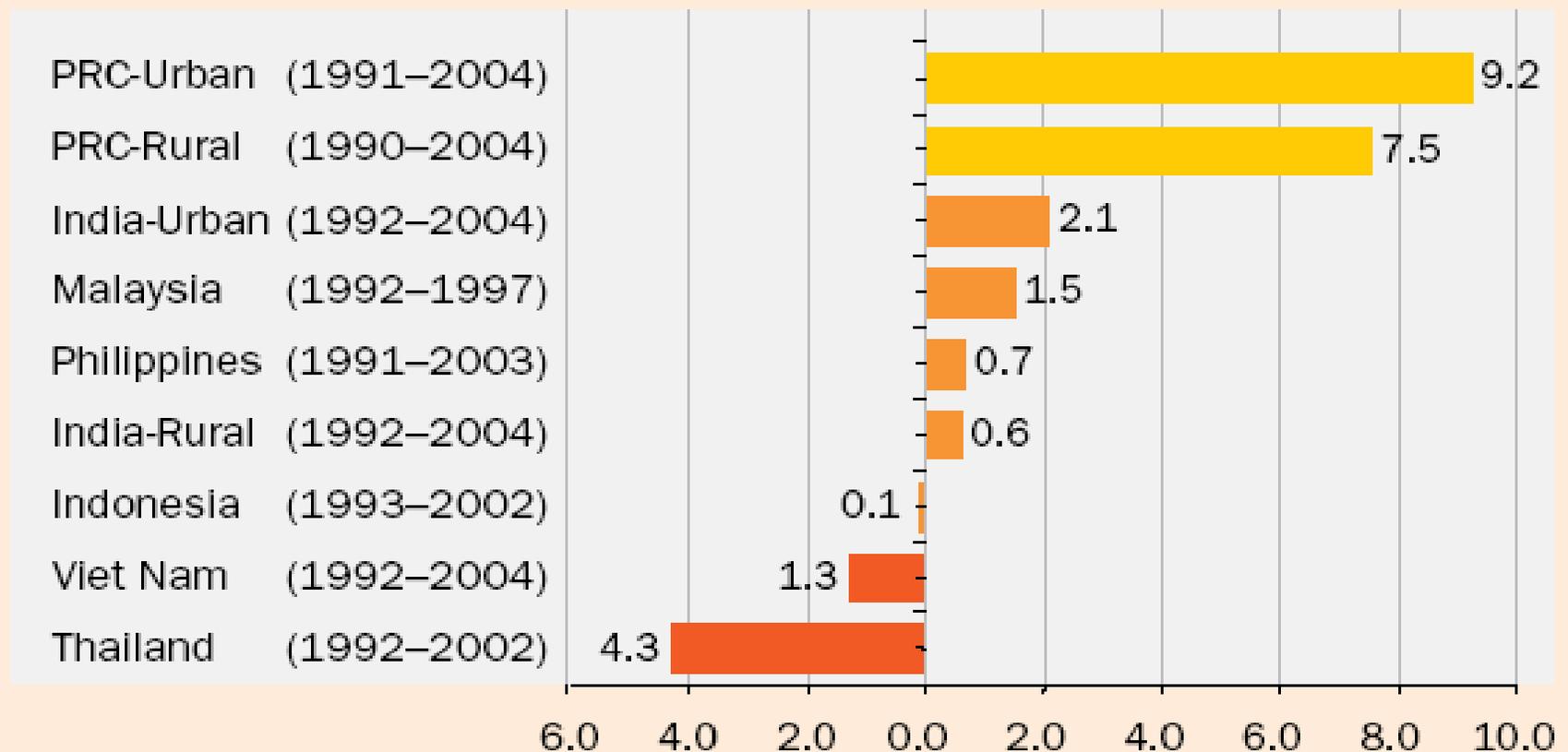
Increased migration can produce large social benefits

Managing threats to health and safety is a priority

# Fighting poverty and exclusion

## Growing inequality

(changes in the Gini index)



# Building Physical Connectivity Corridors in Great Mekong Subregion



Building physical infrastructure

Key for regional connectivity

Role of regional development banks for development financing

Creating development opportunities through trade and services

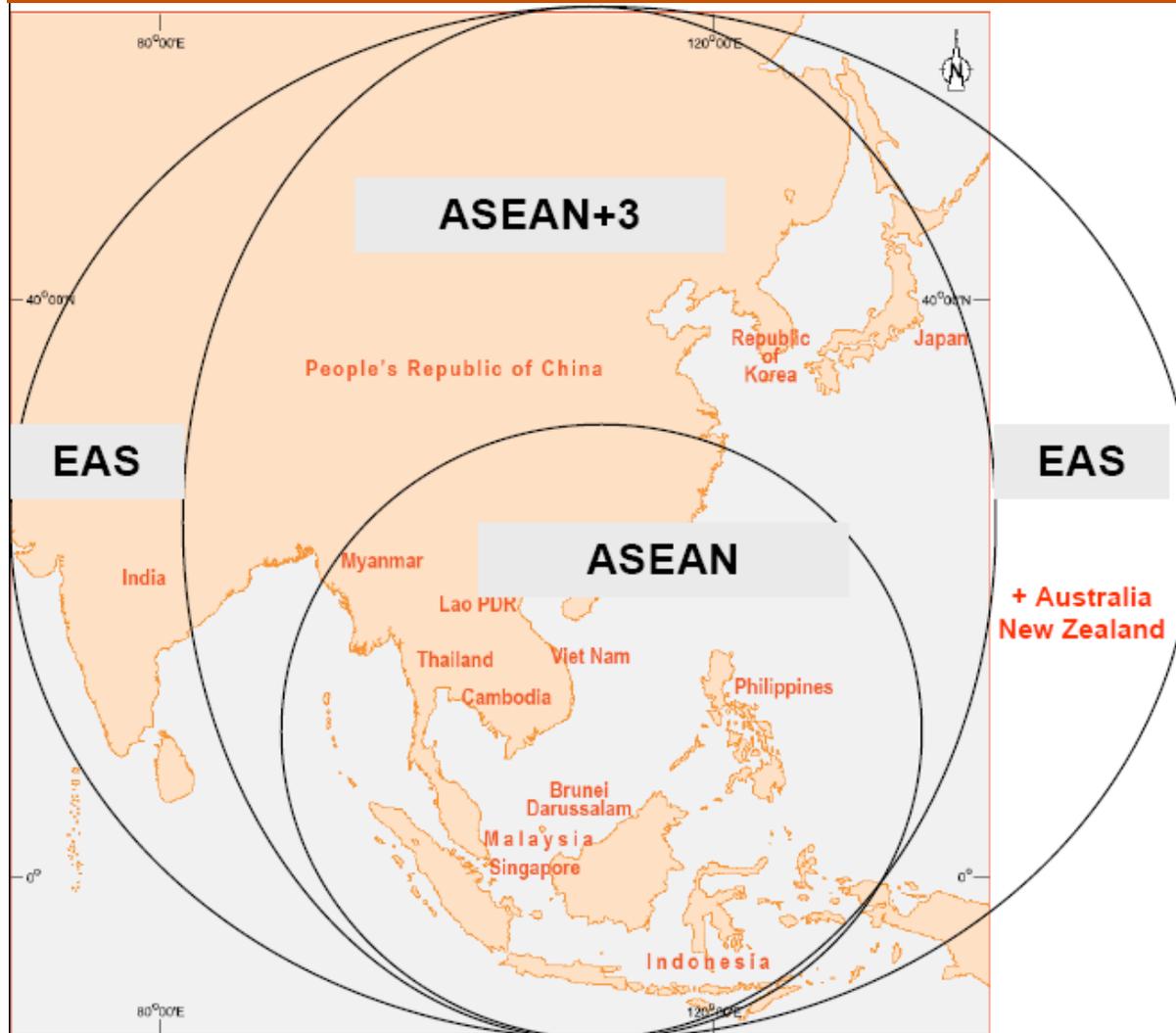
# Agenda for Inclusive, Sustainable Growth

- Connecting the poor to the thriving regional economy
- Developing cost-effective social protection systems
- Facilitating and managing labour migration
- Fighting epidemics and natural disasters
- Limiting environmental degradation

# Building regional architecture with Asian characteristics

- Outward-oriented, flexible, multi-speed, multi-track, pragmatic, bottom-up
- Some streamlining and deepening necessary
- ASEAN, ASEAN+3, and EAS as the strategic regional forums
- Develop deeper institutional capabilities
  - Asian Financial Stability Dialogue
  - Asian Secretariat for Economic Cooperation
- Regionalism as an engine for further global integration

# Strategic Regional Forums



## ASEAN

Economic cooperation; Trade & investment  
Regional Security  
Socio-cultural exchange

## ASEAN + 3

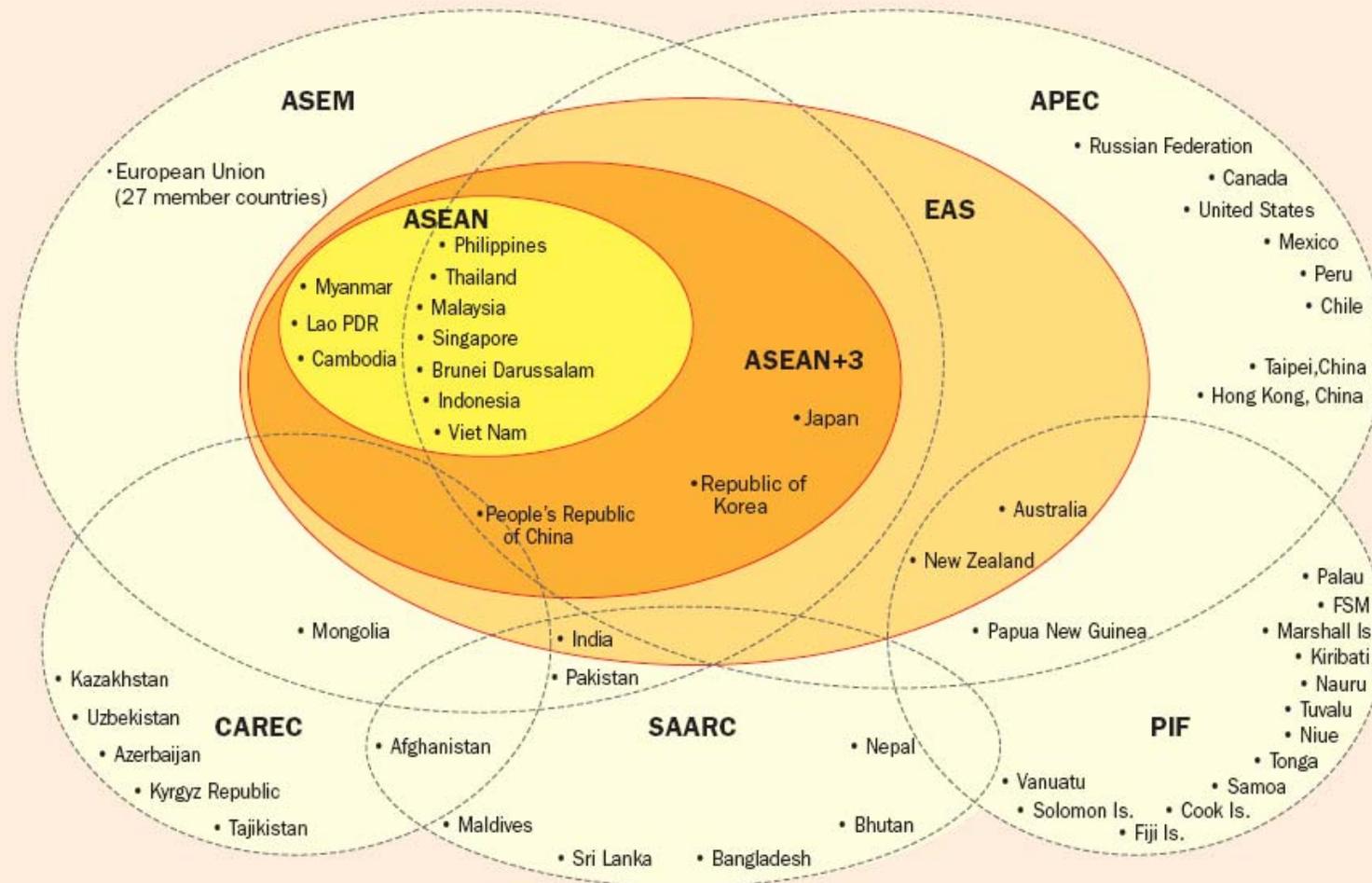
Finance  
Macroeconomics

## EAS

Economic Community;  
Energy & Environment;  
Trade & Finance

# Emerging architecture of cooperation

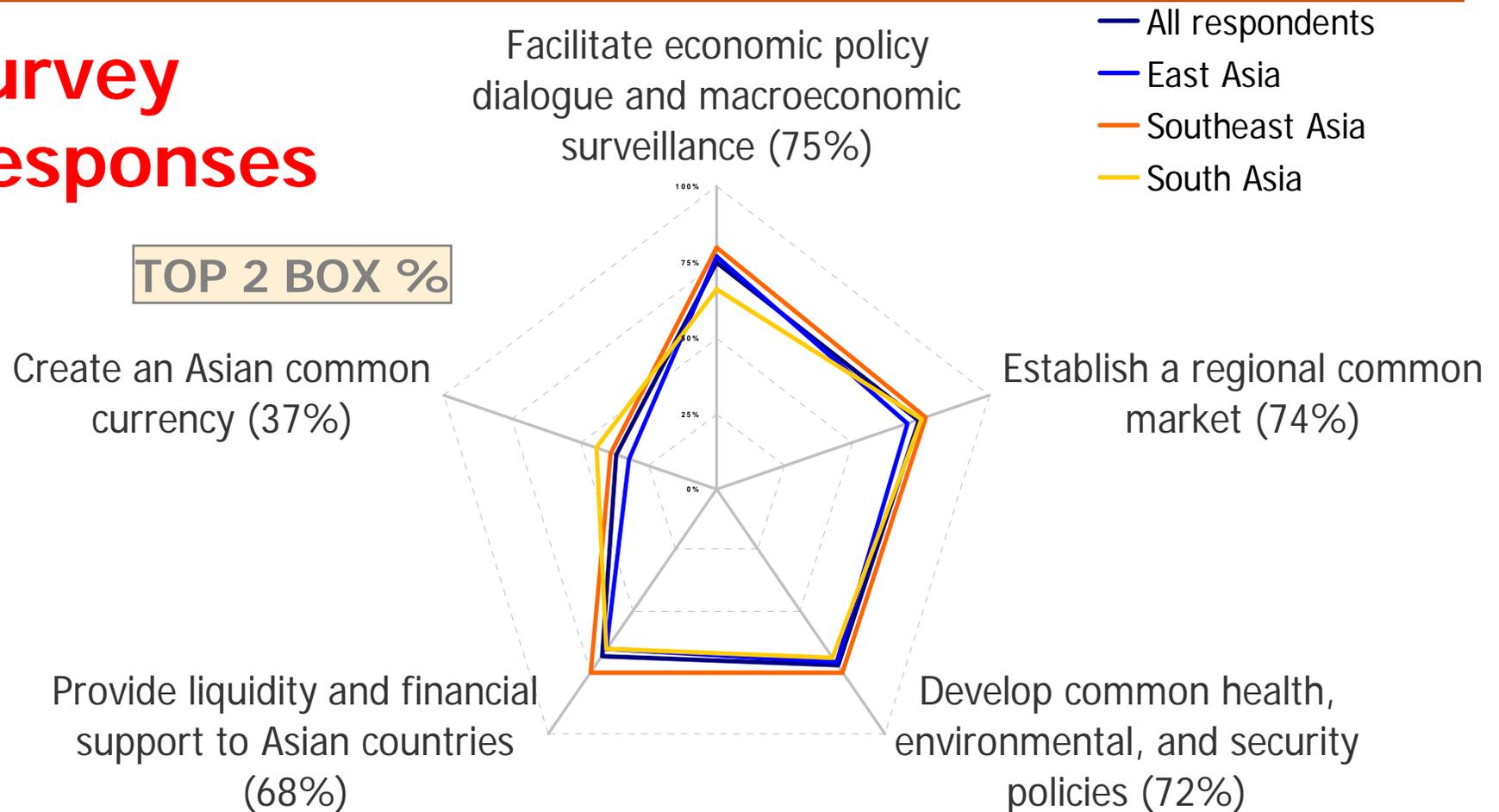
## Economic architecture: regional and transregional forums



# Regional Economic Institutions

## Survey Responses

TOP 2 BOX %



Base: All Respondents (n=600)

East Asia (n=244), Southeast Asia (n=198), South Asia (n=158)

# Needed Institutional Development

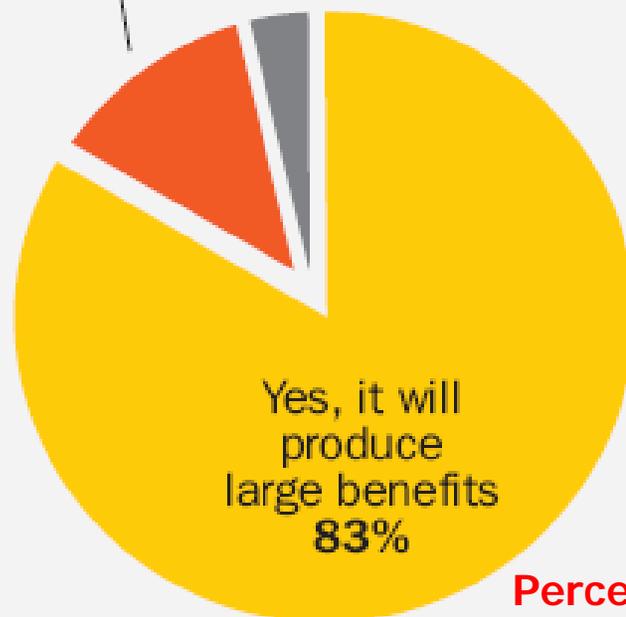
- **Asian Financial Stability Dialogue**  
Forum for all major players in financial market policy (central banks, regulators, supervisors) on issues of financial stability and integration of Asian financial markets.
- **Asian Secretariat for Economic Cooperation**  
Permanent staff to help governments formulate and implement cooperation policies, including:
  - Economic Review and Policy Dialogue
  - Asian Financial Stability Dialogue
  - Chiang Mai Initiative
- Further analysis of institutional options

# Asian Opinion Leaders Support an Asian Economic Community

Will Asia gain from creating an Asian economic community?

No, costs are too high  
13%

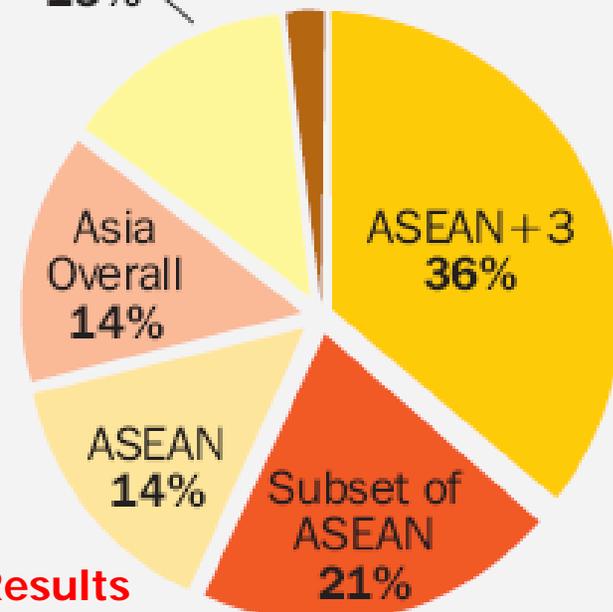
Do not know  
4%



Best regional groupings to build an Asia economic community

East Asian Summit  
13%

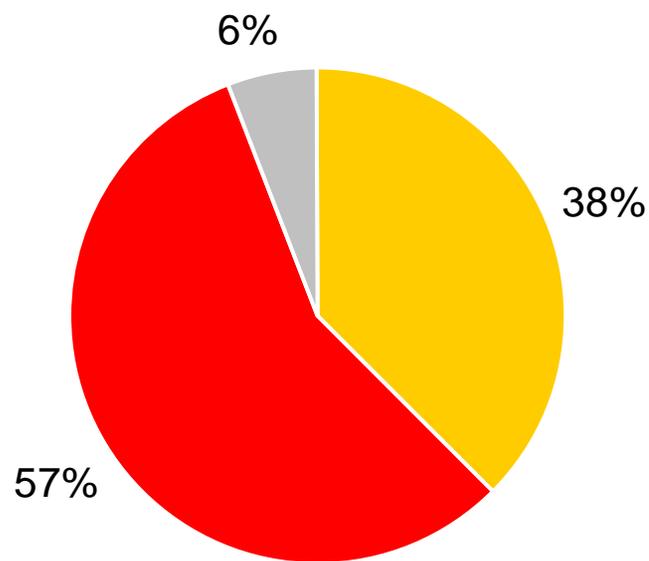
Others  
2%



Perception Survey's Results

# Creation of Asian Common Currency

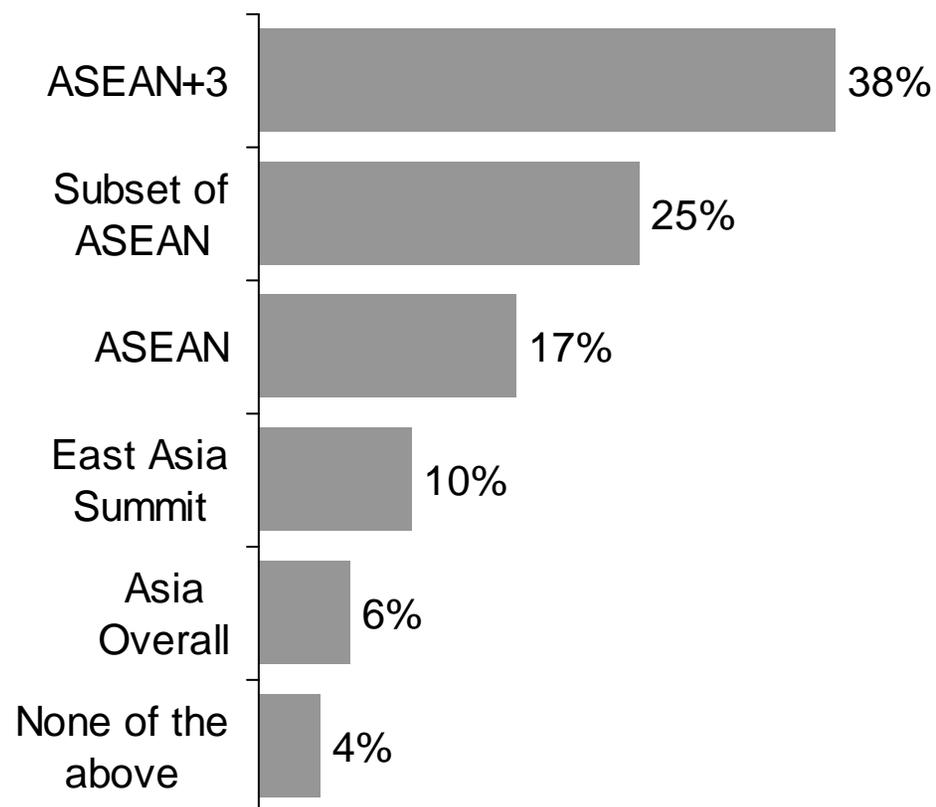
Should Asia create a common currency?



- Yes, some time in the future
- No, Asia's economic gap still too wide
- I don't know

Base: All Respondents (n=600)

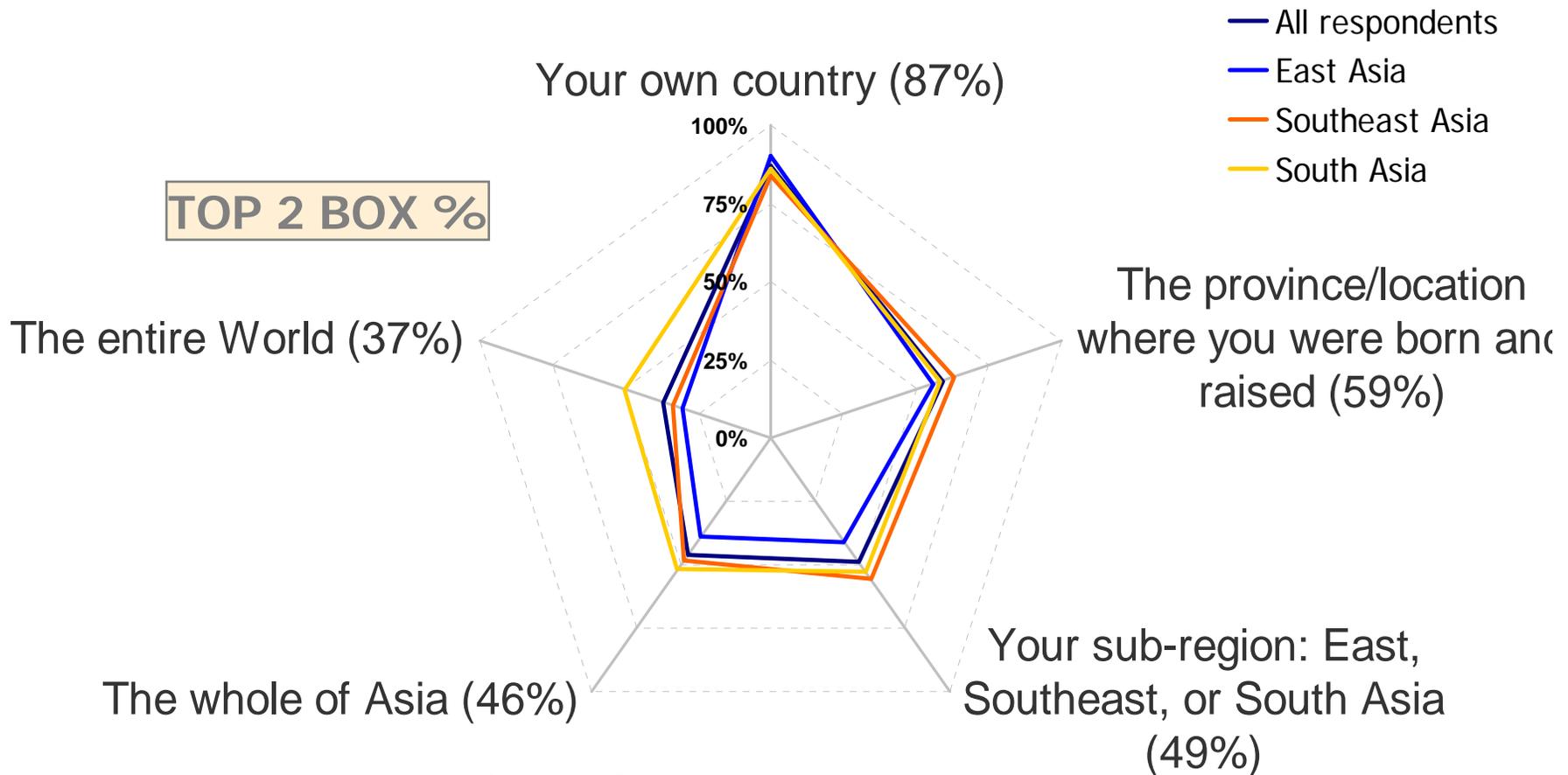
Which is the best positioned group of countries?



Base: Respondents who believed a common currency for Asian will be created (n=226)

# Regional Economic Identity

Q: Thinking about your economic interests and regional identity, rate your sense of belonging to:



**Base: All Respondents (n=600)**

**East Asia (n=244), Southeast Asia (n=198), South Asia (n=158)**

# A Partnership for shared prosperity

**Asian economies in the long-run are likely to have**

- a single market
- deep, liquid and integrated financial markets
- effective macroeconomic policy coordination
- workers moving much more freely than today
- collective efforts to address social issues
- stronger voice in global policy forums
- more regional institutions