Regionalism in South East Asia: The Old and the New

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I. Introduction

With mounting North-North and North-South disagreements in various realms creating formidable obstacles in the path of multilateral trade negotiations under the WTO, there is a spurt in the number of regional trade agreements (RTAs) being signed across the globe. RTAs seek to elude the long drawn negotiations of the multilateral route, by agreeing to accelerate the liberalisation process within specific trading blocs through preferential or free trade arrangements. The increased dynamism towards such trading arrangements has perhaps been the strongest in the Asia Pacific region, where countries long in favour of multilateral-only liberalization such as Japan, South Korea and China have whole-heartedly embraced the regional option.[1]

Just as RTA as a general term refers to a whole spectrum of levels of economic integration, the RTAs in the Asia Pacific region vary in the kind and scope of economic cooperation and integration aimed at and achieved. Higgott (1998) has suggested that there are at least four concentric or intersecting understandings of region in the Asia-Pacific – (1) South East Asia (Association of South East Asian Nations-ASEAN, ASEAN Free Trade Area -AFTA and ASEAN Regional Forum -ARF); (2) East Asia (EAEC-East Asian Economic Council, the Asia '10' etc.); (3) the Asia-Pacific Level (principally APEC); and (4) a number of Natural Economic Territories (NETs or growth triangles or sub-regional groupings).[2] The bilateral free trade areas (FTAs) being negotiated by the countries in the region adds the latest dimension to these interlocking levels of regionalism in Asia-Pacific. However, among the 'old' league of RTAs in the region, ASEAN has been the most institutionally developed.

The 'old' type of regional groupings originally involved reducing or removing tariffs in the case of only commodity trade between member countries. As opposed to this shallow integration, new regionalism epitomises 'deep integration' and incorporates services trade liberalisation and several additional elements of harmonizing trade regulatory measures and other national policies.[3] Such deep integration as well as integration

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1 Within Asia-Pacific, only Hong Kong, Macao, Mongolia and Taiwan are not currently party to any RTA, but it has been reported that some of these Members are also engaged in RTA negotiations. Source: WTO Annual Report, 2003.

2 Higgott, Richard, 1998, "The International Political Economy of Regionalism: the Asia-Pacific and Europe Compared", in William D. Coleman and Geoffrey R.D. Underhill, eds. 1998, Regionalism and Global Economic Integration, Europe, Asia and the Americas, Routledge.

3 Beyond improvements of communications and transportation infrastructure to facilitate increased trade and factor mobility in the region; deep integration many involve (in rough order of increasing depth): facilitating financial and foreign direct investment flows; liberalizing movement of labor within the RTA; harmonizing domestic tax policies, especially those affecting production and trade incentives; establishing institutions to manage and facilitate integration (e.g. regional development funds, dispute resolution mechanisms); harmonizing legal

involving developing and developed countries are the two major characteristics of new regionalism.[4]

It is important to contextualise the emergence of this distinction between old and new regionalism in the context of the shift that has occurred in the focus of trade liberalisation globally. As the focus of national policies across countries shifted to export-oriented economic growth from the 1980s, the underlying assumption has been that liberalisation is the single most important key to achieving growth. But, as goods trade liberalisation has advanced substantially[5] and the influence of MNCs in the national and international policymaking spaces has increased further than ever before, the focus of liberalisation has shifted from goods to include not only services and agricultural sector, but also investment liberalisation, and harmonisation of policies in government procurement, competition policy, bankruptcy laws, etc. This has occurred in parallel with the rising spread of the dominant idea that neoliberal economic policies which stress market liberalisation and a greater role for the private sector at the expense of the state sector, are a superior path towards rapid development. This dominant view has undercut the earlier Keynesian/interventionist consensus on development approaches. Simultaneously, multinational capital-driven globalisation has been occurring, both driving the efforts towards liberalization and policy harmonisation, and being driven by the same.

Under such an export-dependent growth paradigm, it is then apparent that the rationale behind old regionalism that convergence among neighbours could (theoretically at least) lead to a more ‘‘introverted collective self-reliance”,[6] will not be on the agenda today. This is why, against the backdrop of the longer time that seems to be required for multilateral negotiations**,** the increasing trend towards RTAs involving both developed and developing countries seems to be driven by the reckoning that these would offer a next-best path towards expanding their trade prospects.

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regulation of product and factor markets (e.g., anti-trust law, commercial law, labor relations, financial institutions); harmonizing fiscal and monetary policies, including coordinated exchange rate policy; and monetary union—establishment of a common currency and completely integrated monetary and exchange rate policy. See Mary E. Burfisher, Sherman Robinson and Karen Thierfelder, 2003, “Regionalism: Old and New, Theory and Practice” Invited paper presented at the International Conference ‘Agricultural Policy Reform and the WTO: Where are We Heading?’, Capri, Italy.

4 Although NAFTA formed way back in 1994 seems to be the first member of this new league, the real trend in RTAs involving developing and developed countries surged only from the late 1990s.

5 However, there is increasing recognition of the fact that the growing use of non-tariff measures (NTMs) by both developed and developing countries are putting new bumps on the road towards “free trade” in goods.

6 This term was used by Hettne, Bjorn, Andras Inotai and Osvaldo Sunkel, eds., 1999, Globalism and the New Regionalism, MacMillan Press Ltd. In association with UNU/WIDER.

Mirroring this global trend of shift in the locus of liberalisation, there has been a growing emphasis in ASEAN's policy focus also. Aimed at achieving rapid region-wide growth, ASEAN's focus has also shifted from goods trade liberalisation towards liberalization of investment and services, as well as trade facilitation and policy harmonisation on a number of fronts, in tandem with the WTO goals. Most of the bilateral FTAs being negotiated by ASEAN members with non-member countries, including developed countries within and without the larger East Asian region, also incorporate several aspects of deep integration.

The underlying rationale driving regional integration (as well as the multilateral trade liberalisation agenda) is that under free trade, member countries would reallocate their factors of production to achieve structures of trade, production, and employment consistent with their comparative advantage, and that the resulting efficiency gains will give rise to increased welfare. Note that the attainment of welfare gains hinges crucially on the assumption being made that factor reallocation enabling economic restructuring will be made. That is, the success and sustainability of any regional integration process (and more fundamentally, any economic restructuring) depends on whether and how effectively the required factor reallocation occurs (both regionally and within the member economies). Whether this will be policy-driven or will occur automatically as a market-driven process (driven by firm-level strategies) is a crucial unanswered question. Again, at the policy level, apart from the policy adjustments that are sought as part of the regional integration initiatives, the role that needs to be played by domestic policy measures to facilitate the factor reallocation domestically are rarely looked into.

Further, the process of economic restructuring in the context of a particular RTA does not occur in isolation from the restructuring processes going on in various other regional groupings and their implications at the global level. The process of regionalisation is therefore a process of regional production and trade restructuring which merges and/or collides with global restructuring. The emergence of the so-called production backyards closer to the large developed country markets like the US and the EU can have substantial impact on traditional backyards like Southeast Asia.

This paper attempts to examine these aspects of the ASEAN integration process through ASEAN Free Trade Area (AFTA) and other associated agreements. Specifically, we will attempt to address the following issues: How far has trade integration taken place in ASEAN? To what extent has this been driven by the policy initiatives under AFTA and to what extent has it been due to synergies between the states and the private sector in the member countries, which evolved out of the dynamics of international production networks created by MNCs? How far has deep integration proceeded in ASEAN? How has the emergence of Chinese dynamism, the consolidation of NAFTA as an FTA, and the EU's expansion towards Eastern European countries impacted the AFTA? Does policy harmonisation under regional integration negate the need for member states to formulate industrial policy at the national levels? (What possibilities remain under AFTA, AIA etc. for such national policy autonomy towards enabling the required domestic restructuring successfully?) Finally, what are the conflicts getting generated between the regional and state policy spaces, particularly in the context of financial stability?

II. The Old Regionalism in ASEAN: Towards Integration in Goods Trade

It is known how the ASEAN originated way back in 1967 out of political and security concerns, with the Vietnam War encouraging regional cooperation among Indonesia, Malaysia, the Philippines, Singapore and Thailand, against the commonly perceived threat of a more widespread communist uprising in the region. The loose arrangements on cooperation encompassed a wide range of cross-national interactions in cultural, health, environmental and other areas. Even though trade was included, economic cooperation really got started only from the 1976 Summit, which was held after the first oil price shock-induced recession and the breakdown of the Bretton Woods system.[7]

Given that during the 1970s most of the members' trading partners were the industrial nations outside the region where trade protectionism was brewing, the economic focus of the 1976 Summit was to consolidate intra-ASEAN trade. Thus, the ASEAN Preferential Trading Agreement (APTA) was initiated in 1978 following a flurry of industrial projects such as ASEAN industrial complementation schemes and ASEAN joint industrial ventures.[8] The ASEAN secretariat was also institutionalised in 1979 to address a number of issues faced by the members.

II.A. Overall Trends in Intra-Regional Trade

Despite the initiation of such measures towards regional cooperation, trade within ASEAN was slow to pick up. The average intra-regional export share during 1980-84 was only 20.8%. Further, despite the fact that export-oriented growth by these countries, particularly Malaysia and Thailand, had accelerated from 1986 onwards, intra-bloc export share declined to about 19% on average during 1985-89.[9] This was because of the fact that these countries had mainly expanded trade with non-members at the expense of intra-bloc trade.

Against the backdrop of the apparent failure of initial ASEAN economic cooperation initiatives to achieve the targeted level of success, the Fourth ASEAN summit in Singapore in 1992 set the pace for the realisation of an ASEAN Free Trade Area (AFTA). This was expected to be a decisive turn in the growth of ASEAN as a regional grouping.

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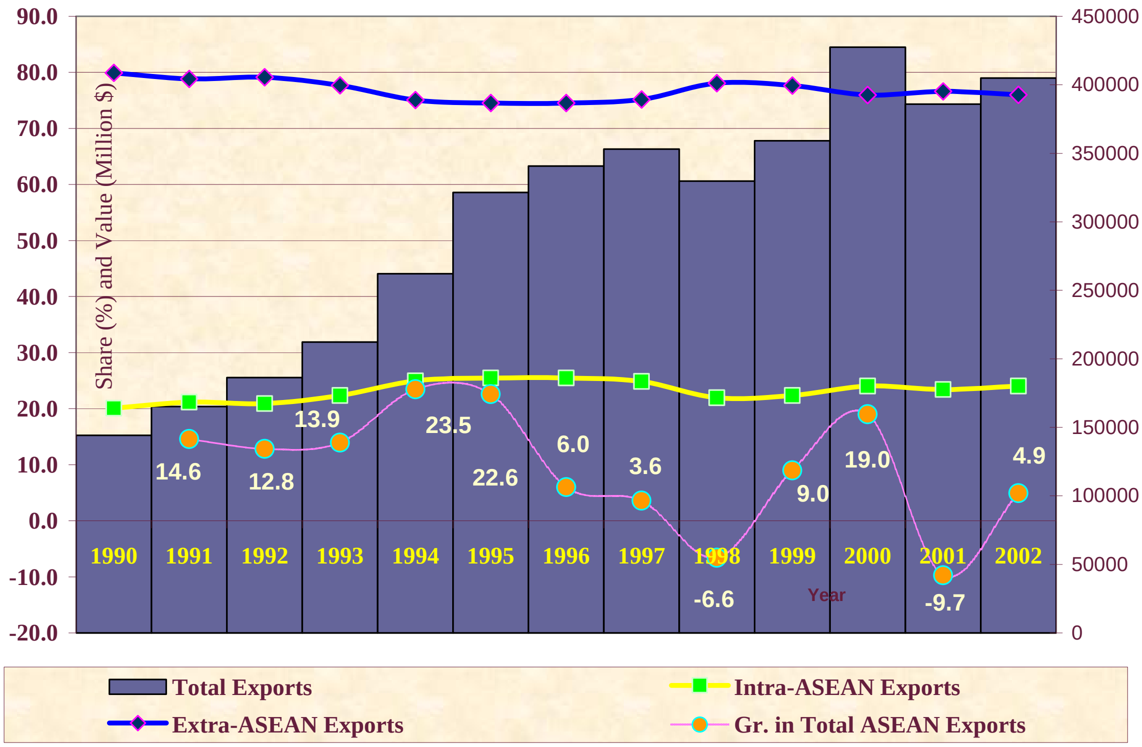
[7] Low, Linda, 2000a, "ASEAN as a Model for Economic Cooperation or the Art of Muddling Through?", National University of Singapore.

[8] Low, 2000a, opcit.

[9] Intra-bloc trade shares for the 1980s are based on Clarete et al., 2002, Table 1. Dobson and Yue (1997) has quoted the share of intra-ASEAN trade in ASEAN's total trade for 1970 as 17.1%.

In fact, during the 1990s, there was a perceptible increase in intra-regional trade share. As ASEAN-10's share in total world merchandise exports rose from 4.2% in 1990 to 6.2% in 1995, intra-bloc export share of ASEAN-10 increased from 20% to almost 26%. Thus, the formation of AFTA was seen to have had an impact in energising intra-regional trade.

Chart 1: Trends in ASEAN's Intra- and Extra Regional Exports



Source: Based on data from WTO Online Statistics Database.

But, a part of this increase in intra-bloc export share in the mid-1990s clearly came from the expansion in the membership of AFTA, as Viet Nam had joined ASEAN in 1995. However, subsequently, AFTA's intra-bloc export share declined to 24% by 2002**,** even though Laos and Myanmar had joined the group in 1997 and Cambodia had done so in 1999 (See Chart 1). Meanwhile, the region's share in world exports too increased only marginally (from 6.2% in 1995 to 6.4% in 2002).[10] That is, even as the growth rate in total ASEAN exports dropped from an average of 17% during 1990-95 to just 3% during

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10 Source: WTO International Trade Statistics, 2003.

1995-2002,[11] extra-ASEAN exports grew more rapidly (3.7%) than intra-ASEAN exports (2.5%) between 1995-2002.[12]

The difference in the effect of AFTA expansion on intra-bloc exports in the two different phases may be partly explained by the very low contribution of Lao, Myanmar and Cambodia both in total ASEAN exports as well as in intra-ASEAN exports, when compared to Vietnam. While the share of ASEAN's total exports attributable to Vietnam was 1.5% in 1995, those of Lao, Cambodia and Myanmar were all just about 0.2% to 0.3% of the total during 1997-99.[13] This was too insignificant for the introduction of these countries into the group to make an impact on intra-bloc trade shares.

Even so, it is also evident that for some among the remaining seven members, there must have been a drop in the share of their respective total exports going to the regional market. Singapore (with 33% of total ASEAN exports in 2001) and Malaysia (24%) have been the largest ASEAN exporters, followed by Thailand (18%) and Indonesia (15%). These countries' shares in intra-ASEAN exports were also 39%, 25%, 17% and 11% respectively.[14] Although it has increased its share, the Philippines is still a relatively small exporter, accounting for only 9% and 6% of total and intra-ASEAN exports in 2001.[15]

When we look at the share of intra-ASEAN trade in each country's total trade in the case of the five larger economies, it is seen that intra-ASEAN export share in its total exports has declined consistently for Malaysia (See Table 1). Additionally, between 1995 and 2002, these shares declined for Singapore and Thailand as well. Thus, the drop in ASEAN-10's intra-bloc export share between 1995 and 2002 can be explained by the increased outward orientation of these three economies. Specifically, between 1995 and 2002, these top three ASEAN exporters increased their exports to Asia much faster (compared to 'Other regions' also).

Table 1: Intra-and Extra Regional Trade of Selected ASEAN Countries, 1990-2002.

[11] Total ASEAN exports had declined by 10% in 2001, with all except the four new members registering negative growth. In 1998 too total ASEAN export growth had declined by about 8%, but then, all countries except the Philippines (+17%) registered export growth declines.

[12] During 1990-95, on the other hand, growing at 23% intra-ASEAN exports had expanded faster than extra-ASEAN exports (16%).

[13] The shares of Vietnam and Lao are based on data from WTO Online Statistics Database. Based on data from ASEAN Secretariat, it is seen that Cambodia and Myanmar's shares in intra-ASEAN exports were also only 0.1% and 1% respectively, even in 2001. Lao and Vietnam's contributions to intra-regional trade are not available separately from either data source.

[14] But, Singapore's and Malaysia's shares in intra-ASEAN trade have dropped since 1995.

[15] The share of Brunei (which had joined ASEAN in 1984) in exports was also still only about 1%.

(Percentage share)

Origin	Dest.	Share in Ctry's Total Exports					Dest.	Orig.	Share in Ctry's Total Imports			
Exports		Intra-ASEAN	Asia	Other reg.s	Extra-ASEAN		**Imports**		Intra-ASEAN	Asia	Other reg.s	Extra-ASEAN
Indonesia	1990	10.0	59.6	30.4	90.0		**Indonesia**	1990	8.6	46.3	45.0	91.4
	1995	14.3	48.8	36.9	85.7			1995	10.4	44.6	45.0	89.6
	2002	17.4	46.5	36.1	82.6			2002	21.6	39.4	39.0	78.4
Malaysia	1990	29.3	32.8	38.0	70.7		**Malaysia**	1990	19.3	41.4	39.3	80.7
	1995	27.6	30.9	41.5	72.4			1995	17.4	44.9	37.7	82.6
	2002	26.0	35.1	38.9	74.0			2002	22.9	42.5	34.6	77.1
Philippines	1990	7.2	31.7	61.0	92.8		**Philippines**	1990	10.5	40.0	49.5	89.5
	1995	13.5	28.8	57.7	86.5			1995	11.9	44.6	43.5	88.1
	2002	15.2	36.8	47.9	84.8			2002	16.3	45.1	38.6	83.7
Singapore	1990	25.7	28.8	45.5	74.3		**Singapore**	1990	20.5	34.2	45.3	79.5
	1995	32.3	29.4	38.2	67.7			1995	25.3	35.6	39.1	74.7
	2002	30.4	34.8	34.7	69.6			2002	30.8	29.4	39.8	69.2
Thailand	1990	11.9	29.4	58.7	88.1		**Thailand**	1990	13.2	47.9	38.9	86.8
	1995	21.8	32.2	46.0	78.2			1995	13.4	46.1	40.5	86.6
	2002	19.7	35.4	44.9	80.3			2002	16.7	45.3	38.0	83.3
ASEAN (10)	1990	20.1			79.9		**ASEAN (10)**	1990	16.2			83.8
	1995	**25.5**			74.5			**1995**	**18.8**			81.2
	2002	**24.0**			76.0			**2002**	**23.6**			76.4

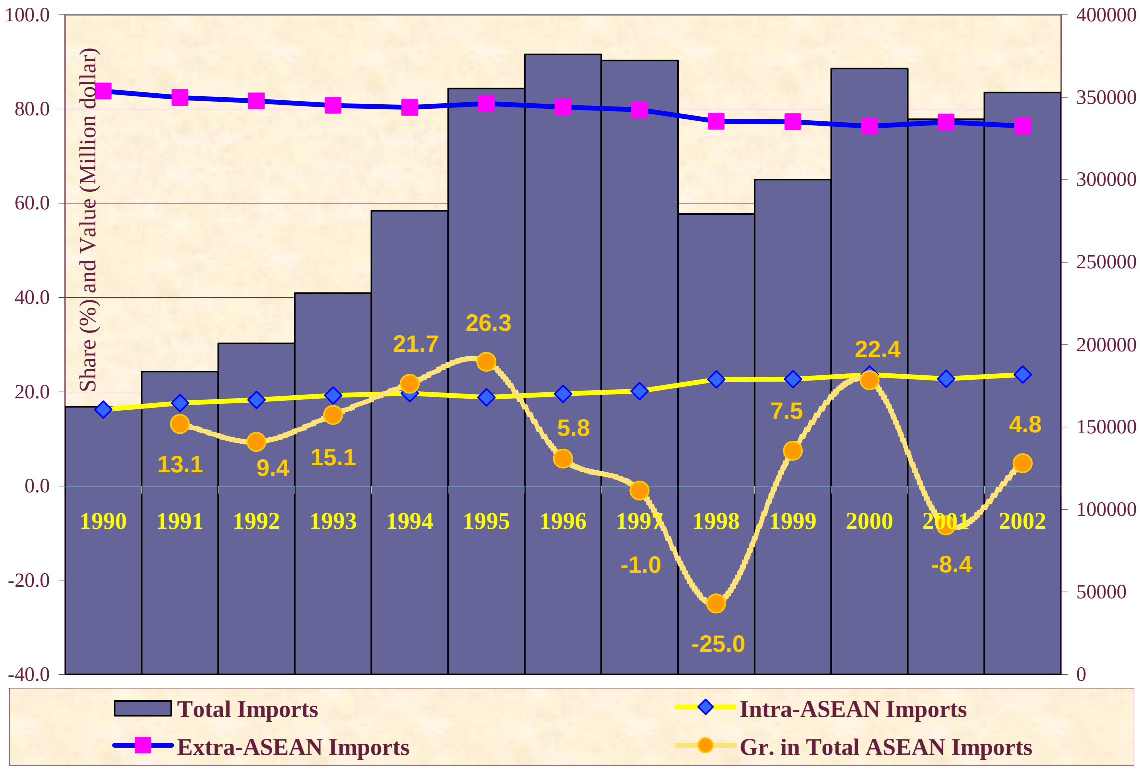
Note: Singapore's data includes significant re-exports.
Source: Based on data from WTO International Trade Statistics, 2003.

Similar to ASEAN's total exports, ASEAN (10)'s aggregate imports also expanded by 17% on average during 1990-95. By contrast, subsequently, they grew by just -0.1% during 1995-2002. But, during both phases, intra-ASEAN imports grew much faster than extra-ASEAN imports.[16] Thus, ASEAN's intra-bloc import share has risen consistently from 16% in 1990 to 19% in 1995 and further to about 24% since 2000, and has hovered around the same since then (See Chart 2). Its share in world merchandise imports, meanwhile increased from 4.6% in 1990 to 6.7% in 1995, but was followed by a decline to 5.4% in 2002.[17]

Chart 2: Trends in ASEAN's Intra- and Extra Regional Imports

[16] During 1990-95, intra-ASEAN and extra-ASEAN imports had grown at 21% and 16% respectively. During 1995-2002, on the other hand, while extra-ASEAN imports grew by only -0.1%, intra-ASEAN imports grew by a positive 3.2%.

[17] Source: Ibid.



Source: Based on data from WTO Online Statistics Database.

Once again, Singapore was the single largest ASEAN importer (37% of total ASEAN imports in 2001), followed by Malaysia (23%). While the share of total ASEAN imports attributable to Thailand has declined from about 23% in 1995 to 20% in 2001, it remains the third largest importer. While Indonesia's share has also fallen from 13% to 10% over the same period, that of the Philippines has increased from about 8% in 1993 to around 10% since 1997. In 2001, the shares of intra-ASEAN imports attributable to these countries were 43% for Singapore, 23% for Malaysia, 15% for Thailand, 9% for Indonesia and 7% for the Philippines.

Table 1 clearly shows that overall there has been an increase in the intra-regional trade shares for all these five large economies when compared to 1990,[18] both in the case of exports as well as imports. This increase in both intra-regional imports and exports follows the implementation of AFTA and thus seems to point towards a traditional trade creation effect due to the formation of the free trade area. But, it is clear that this effect flattened out after the mid-1990s, particularly in the case of exports. On the other hand,

[18] Except in the case of Malaysia, for exports, which show a decline in the share of intra-bloc exports between 1990 and 2002, as we saw already.

growth in intra-ASEAN import trade was faster than that in intra-ASEAN exports in the latter phase (1995-2002).

Trade concentration ratios or trade intensity indices, obtained by dividing the intra-regional trade share by the share of the region in total world trade, (which overcome the limitations of intra-bloc trade shares), give us a clearer picture. AFTA's overall trade intensity index fell from 4.1 in 1990 to 3.4 in 1995, but increased again to 4 in 2002. But, if we look at exports and imports separately, it is observed that while the export trade intensity index for AFTA fell steadily in the nineties from 4.8 in 1990 to 3.7 in 2002, the import trade intensity index, which declined from 3.5 in 1990 to 2.8 in 1995, increased drastically after that to 4.4 in 2002.

These divergent trends in AFTA's intra-regional exports and imports relative to the region's share in world trade in the post-crisis scenario, with ASEAN members exporting more to non-members along with a simultaneous increase in intra-regional imports (despite the accelerated AFTA tariff liberalisation post-crisis), emphasises the continued overwhelming presence of AFTA's trade with non-members and the presence of a triangular trade pattern. In particular, it suggests the presence of a regional production platform, whereby ASEAN members import relatively more from each other (due to the lower intra-regional tariffs when compared to MFN levels), while exporting more to third countries**.** The role played by some of these countries as an international export production base for Japanese, American, European and the East Asian Newly Industrialised Counties (NICs) companies, have been well established in the literature.

Thus, it is important to understand how much of this seemingly higher trade integration within ASEAN has been driven by the regional trade liberalization initiatives and how much of it already existed prior to the formulation of a formal institutional framework as 7reflected in AFTA**.** Towards this, we undertake an analysis of FDI flows in the region, in order to understand the type and extent of production distribution among the member countries. We will then look at the major commodities involved in ASEAN's export and import trade with its major investing countries and/or trading partners.

II.B. FDI and the Development of Production Networks in ASEAN

With rapidly expanding market, abundant natural resources and labour supply, the ASEAN region had emerged as one of the most attractive investment locations in the developing world in the 1980s itself, and attracted a disproportionately large amount of FDI, particularly in the 1987-91 period.[19] In particular, Singapore, Malaysia and Thailand were among the ten largest recipient developing countries in the 1980s. While investments targeted at the host market characterised the first wave of manufacturing

[19] See Yue, Chia Siow, 1993, "Foreign Direct Investment in ASEAN Economies", Asian Development Review, Vol. 11.

FDI into ASEAN, investments to produce manufactures for export had become increasingly important in the 1980s, particularly following liberalisation of policies after 1985. In fact, until the mid-1990s, South East Asia's growth pattern has been described to follow the 'flying geese' model, following on the heels of the East Asian I-tier economies of South Korea, Taiwan province of China, and Hong Kong.

The 'flying geese' theory envisaged the relocation of production across countries, through FDI from a lead economy to other countries typically at lower stages of development, in search of lower costs. The Southeast Asian economies came under major influence of this, as this paradigm was used to argue that rather than attempting to domestically generate and accumulate the technology and managerial resources required for catching-up industrialisation, late industrialising countries can hasten their catching-up development through inward FDI, which brings in capital, technology, external market access, and managerial and marketing techniques in a packaged form. Thus, as Japan and the first-tier newly industrialised economies of East Asia (particularly, Taiwan province of China, South Korea and Singapore)[20] advanced steadily through the successive development of their light, medium and high-technology industries, Malaysia and Thailand began attracting substantial FDI inflows, utilizing their labour cost advantage fully. By the late 1980s, direct investments almost totally completed the shift away from resource processing sectors towards labour-intensive textiles and garments and electrical/electronic industries.

It can be seen from the table below that during 1984-89, which is the period of the shift to export-oriented growth policies by most of these countries, the six ASEAN members of the time accounted for an average of about 4% of world FDI inflows. Apart from Singapore, which accounted for half of the total FDI inflows into ASEAN during 1984-89, the other major ASEAN host countries were Malaysia and Thailand. Indonesia and the Philippines accounted for 9% and 7% respectively of FDI inflows into ASEAN during the second half of the eighties. Brunei attracted hardly any FDI inflows during this phase. This trend continued more or less in 1990.

While the United States, European Community (EC) and Japan were the three leading investors in ASEAN countries up to 1987 (except in Malaysia, where Singapore ranked third ahead of the US), along with a dramatic growth in Japanese investments, the Asian NIEs had also emerged as major investors in the post-1987 period. Intra-ASEAN investments accounted for only a small share of ASEAN's total inflows of FDI in this phase and were significant only in the case of Malaysia.

FDI from the leading EC investors such as the UK, Netherlands and Germany were concentrated in petroleum-related activities, chemicals and pharmaceuticals, processed

[20] The city-state of Singapore, an ASEAN member, was also included among these I-tier economies due to the much more developed state of its economic structure.

foods, electrical and electronic products, automobile assembly, and banking and finance. US FDI in ASEAN were found in manufacturing, as well as in resource development dominated by oil & gas exploration & development, and also services dominated by banking & finance, trade and restaurants. US manufacturing sector MNCs also invested in industries similar to that of the EU.

But, during 1986-91, Japanese investments dominated manufacturing sector FDI in ASEAN, especially Malaysia, Thailand and the Philippines. Half of Japanese FDI in Indonesia and one-fourth in Philippines went into mining. On the other hand, Japanese FDI in Singapore was concentrated in services, dominated by banking, finance & insurance, commerce and transportation. Within manufacturing, the emphasis was on electrical & electronic products, chemicals, metal products and transport equipment in both Malaysia and the Philippines; electrical & electronic products, machinery, metal products and textiles in Thailand; chemicals, electrical & electronic products, food processing and machinery in Singapore;. and on resource processing, labour-intensive industries and domestic market-oriented industries in Indonesia.

The NICs' investments in ASEAN were also concentrated in the manufacturing sector. South Korea and Taiwan province of China had major investments in ASEAN's textiles and clothing, electrical/electronics products and chemicals. Additionally, South Korea's FDI also went into footwear, wood products and toys, and FDI from Taiwan province of China went into pulp and paper products. Hong Kong's investments were more diversified and went into real estate, services, in addition to labour-intensive manufacturing industries.[21]

The above discussion clearly reveals that FDI inflows into the major Southeast Asian countries were substantial prior to the introduction of AFTA as part of the East Asian regional production networks developed by MNCs. Further, they were also concentrated in certain specific manufacturing sectors, which were increasingly crowded into electrical & electronics products, transport equipment, chemicals, petrochemical products, etc., apart from food processing, footwear, paper & paper products.

The discussion on the structure of exports and imports in a following section will clearly reveal that these were also the industry categories which dominated ASEAN members' exports and imports in 1993, before the effect of AFTA could have materialised. Thus, the 20% share of intra-regional trade flows in ASEAN in 1990, which was already higher than the typical intra-bloc trade share for South-South RTAs, can be clearly attributed to the intra-industry trade within these broad product categories created through the leading MNCs' production distribution or division of labour strategies in the region.

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[21] The discussion for the period 1986-91 is based on information provided in Yue, 1993, opcit.

By the early 1990s, in addition to Singapore that has been an export-oriented economy historically; large FDI-dependent export-oriented domestic private sectors had emerged in all the larger ASEAN members. At the same time, the member governments' increased attraction to continue the rapid export-led growth of the late 1980s (which was due to a combination of favourable factors including the fact that world trade in those industries was growing the fastest during this phase), against the backdrop of the emergence of China as a major FDI attraction and exporter, led them to believe that liberalization of intra-regional trade will enable ASEAN to consolidate their existing trade-investment links and compete with the diversion of investments towards China whose share in developing country FDI was rising dramatically following the removal of several restrictions in 1992. Meanwhile, these governments also had to meet the investment competition being thrown up by the drive towards the formation of a North American Free Trade Agreement (NAFTA) by 1994.

The combination of the interests of these three dominant actors in the region- namely, the state, export-oriented FDI and export-oriented FDI-dependent domestic private sectors in respective countries- became the driving force behind the AFTA regional integration project.

II.C. The Institutional Framework for ASEAN Free Trade Area

It was the Framework Agreement on Enhancing Economic Cooperation signed by ASEAN members at its 1992 Summit, which set the timetable for a complete removal of trade barriers among member countries for establishing an ASEAN Free Trade Area (AFTA) by 2008. The Agreement on the Common Effective Preferential Tariff (CEPT) Scheme has been the main mechanism towards its realisation.

The CEPT sought to reduce intra-regional tariffs on all manufactured items of ASEAN countries to 5% or less and to remove quantitative restrictions (QRs) and non-tariff barriers, over a 15-year period commencing 1 January 1993. In 1994, the time frame for the realisation of AFTA was brought forward to 1 January 2003 instead of 2008. The ASEAN countries were to reduce tariff levels at varying speeds and the traded commodities were categorized into various categories subject to different rates of liberalization, namely, Inclusion List (IL) with fast track and normal track liberalisation, and temporary exclusion and sensitive lists.

The fast track program was to:

(1) reduce tariffs at 20% and below to 0-5% within 5 years (by 1 January 1998); and
(2) reduce tariffs above 20% to 0-5% within 7 years (by 1 January 2000). [22]

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[22] Industries included in the fast track list were for example, vegetable oils, chemicals, fertilisers, rubber products, paper, ceramics and glass products, cement, wooden furniture, pharmaceutical products, plastics, leather products,

The normal track program was to:

a) reduce tariffs above 20% in two stages- first to 20% by 1 January 1998, and then to reduce them to 0-5% by 1 January 2000; and

b) reduce tariffs at 20% and below to 0-5% by 1 January 2000.

Sensitive products not ready to be included in the CEPT could be excluded temporarily, but they were required to be transferred into the Inclusion List (IL) 20% annually. Thus, by 1 January 2003, all these products were to be in the 0-5% range (that is, IL). Unprocessed agricultural products, except for those in the Sensitive list, were also introduced into the CEPT scheme. However, 734 tariff lines in the General Exception List, representing about 1.7% of all tariff lines in ASEAN, are permanently excluded from the FTA for reasons of national security, protection of human, animal or plant life and health, and of artistic, historic and archaeological value. It is important to note that this exclusion of about 2% of tariff lines from the ambit of AFTA tariff reduction cannot be interpreted to represent a minor segment of intra-regional total, unless and until the corresponding share of this exclusion list in the region's total exports and imports is taken account of.

While all products that are wholly produced or obtained in the exporting member state are eligible for the CEPT Scheme's preferential concessions, products not wholly produced or obtained within ASEAN have to satisfy the 40% rules of origin requirements to be eligible for preferential treatment by the importing member country.

Following the financial crisis in December 1998, in an attempt to regain business confidence, enhance economic recovery and to promote growth in ASEAN, it was agreed to advance the implementation of AFTA by one year from 2003 to 2002, in stages. The CEPT Scheme was modified to further reduce intra-regional tariffs (for all products in the IL) from 5% to zero by 2002 for the six original ASEAN nations, by 2003 for Vietnam, and by 2005 for Laos and Myanmar. The 1999 AFTA Council meeting further set the target date for removing tariffs on all goods by 2010 for the original six, and 2015 for the remaining countries.

Apart from these tariff reduction targets to be met, ASEAN also initiated projects towards retaining the region's attraction for foreign investors. Upon realizing that some of the parameters upon which its existing industrial cooperation programs were designed were no longer valid, ASEAN also implemented a new form of industrial cooperation scheme in 1996 to replace the ASEAN Industrial Joint Ventures (AIJV-1983) and the earlier Brand-to-Brand Complementation (BBC) Schemes.

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textiles, gems and jewellery products, copper cathodes, and electronics. Note that this included nearly all the available existing manufacturing product categories.

ASEAN Industrial Cooperation Scheme (AICO) applies the preferential CEPT rate of tariffs (0 to 5%) on approved AICO products, so as to strengthen industrial cooperation within the region by promoting joint manufacturing activities between ASEAN-based companies. AICO Scheme aims to promote resource-sharing and to increase the competitive position of ASEAN's manufacturing industries by means of production integration across borders facilitated by preferential tariff rates.

A manufacturing activity undertaken by a minimum of two companies in two different ASEAN countries, involving not only the physical movement of products between them but also resource sharing/pooling and/or industrial complementation is required to form an "AICO Arrangement". An AICO Product shall meet the Rules of Origin of the CEPT Scheme. The participating companies should also have a minimum national equity of 30%. Since two companies are required to form an AICO Arrangement, each company must meet this national equity holding requirement; but, national equity holding of one ASEAN member country in each of the participating company is sufficient. (In electronics and automobile industries, it is imaginable that an MNC with one or two joint ventures producing related parts & components will be able to make use of the preferential tariff rates). For companies that cannot meet the equity condition, a waiver is possible if the proposing company meets other criteria imposed by the participating country in lieu of the 30% national equity. Other incentives include local content accreditation where applicable and other non-tariff incentives such as investment incentives offered by the participating members.

In any AICO Arrangement, products are categorized as AICO Final Products; AICO Intermediate Products and/or AICO Raw Materials. The Final Products which represents the final output of a specific AICO Arrangement shall have unlimited market access in the participating countries. On the other hand, although the Intermediate Products and/or Raw Materials can enjoy the same 0-5% preferential tariff rate, they have limited market access. These may be imported and used as inputs in the manufacture of approved AICO Final Products in a particular AICO Arrangement only.

In 1998, further special incentives and privileges were also agreed upon to attract FDI into the region. The ASEAN investment climate was improved by extending special privileges to qualified and non-ASEAN investors in manufacturing, including 100% foreign equity ownership, three-years' tax holiday and waiving the 30% national equity for ASEAN Industrial Cooperation Scheme (AICO). The Framework Agreement on the ASEAN Investment Area that came into force in 1998 called for opening up all industries in the region to ASEAN investors and granting national treatment to them (except those on temporary exemption lists).

The objective of the AIA was to encourage investors to think increasingly in regional terms and adopt a regional investment strategy and network of operations. The scheme aims to promote a more efficient division of labour and industrial activities across the region, creating opportunities for greater industrial productivity and cost competitiveness.

II.D. Post-AFTA Trade and Investment Patterns

During 1991-97, there were several important shifts in the pattern of FDI inflows in ASEAN. Overall, FDI inflows into ASEAN increased steadily and remained above 7% of world FDI inflows during 1991-97.[23] But even as FDI flows into all the member countries increased in value terms, the share of ASEAN-6 (within ASEAN-10) dropped from 99% in 1990 to 89% in 1997. While the shares of Singapore, Thailand and the Philippines show major drops, those of Malaysia and Indonesia increased significantly. While Singapore still represented some 34% of total inflows into ASEAN on average during this period, Malaysia followed closely.

Meanwhile, Vietnam had emerged as a significant host country in the first half of the 1990s itself, even though its entry into ASEAN happened only in 1995. FDI inflows into Vietnam, which began rising from 1990 itself, came to account for as much as 8.3% of total inflows into ASEAN in 1995 and overtook both Thailand's and Philippines' shares in that year. From 1991-92 onwards, the shares of Lao, Myanmar and Cambodia also became noticeable. While Lao still did not account for even one per cent of total inflows into the region, Cambodia's share peaked at 1% during 1998-2001 and Myanmar's share peaked during 1997-98 at 3% (soon after it joined ASEAN in 1997), before declining again.

But, subsequent to the East Asian crisis and the ensuing region-wide recession, the share of ASEAN-6 failed to recover beyond the level it achieved in 1999. Net FDI inflows into Indonesia, which had turned negative from 1998 onwards, still did not recover in 2002. This became a major factor in the decline in FDI inflows into ASEAN in absolute terms and a decline in the region's share in world FDI inflows to 3.3% in 1998 and further to just 2% in 2002. In comparison, FDI flows to China have been on a rising trend and reached 8.1 per cent of the total in 2002.[24] Since 1993, China has been accounting for about half of total FDI flows to Asia, including intra-Asian FDI. Meanwhile, ASEAN-5's share of Asia-bound FDI has declined from 51% in 1990 to only 11% in 2001.

The next largest fall in absolute terms was registered by Singapore, followed by Malaysia, although they remained the top two largest hosts within ASEAN despite this. This was due to the fact that except for Thailand and Philippines during 1998-99, inflows into all

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[23] The rise occurred during 1993-97, after sharp declines in flows during 1991-92.

[24] China is now the largest recipient of FDI among all developing countries and, for many years, has been the second largest FDI recipient in the world.

major ASEAN members declined after 1998. Brunei showed a sudden jump in its share to 2% of total ASEAN inflows in 1996 and this increased continuously after that. Overall, the share of ASEAN-4 new members remained around 10%, mainly due to flows into Vietnam and Myanmar.[25]

Table 2: Country-wise Distribution of FDI Inflows in, 1984-2002. (Per cent)

Countries/Year	1984-89 (Ann. Aver.)	1990	1991-97	1995	1996	1997	1998	1999	2000	2001	2002
Share in ASEAN's Total FDI Inflows											
Brunei (1)	-	0.02	0.6	0.0	2.2	2.1	2.6	3.0	2.9	3.5	7.4
Cambodia (2)	..	..	0.7	0.6	2.0	0.5	1.1	0.9	0.8	1.0	0.4
Indonesia	9.1	8.9	13.0	18.0	21.1	13.7	-1.6	-11	-24	-22	-11
Lao PDR (3)	0.02	0.05	0.2	0.4	0.4	0.3	0.2	0.2	0.2	0.2	0.2
Malaysia (4)	17.9	19.0	29.0	24.0	24.8	18.5	12.1	15.6	20.3	3.6	22.9
Myanmar (5)	0.02	0.5	1.3	0.5	1.1	2.6	3.1	1.2	1.1	1.3	0.9
Philippines (6)	7.3	4.5	5.4	6.0	5.2	3.7	7.7	6.9	7.2	6.5	8.0
Singapore (7)	50.3	45.4	33.6	33.9	29.3	39.7	33.9	52.9	66.9	72.0	54.8
Thailand	15.2	20.7	11.4	8.3	7.7	11.4	33.4	24.3	18.0	25.1	7.7
ASEAN-6	**99.9**	**98.5**	**93.0**	**90.2**	**90.4**	**89.1**	**88.1**	**91.7**	**91.0**	**89.1**	**89.9**
Vietnam	0.0	1.0	4.9	8.3	6.1	7.6	7.6	5.9	6.9	8.5	8.6
ASEAN-New 4	**0.1**	**1.5**	**7.0**	**9.8**	**9.6**	**10.9**	**11.9**	**8.3**	**9.0**	**10.9**	**10.1**
ASEAN-10 (Billion $)	4.4	12.3	21.0	24.2	29.4	34.1	22.4	25.0	18.6	15.2	14.0
Share in World FDI Inflows											
ASEAN-10 Total	3.9	6.0	7.2	7.3	7.6	7.1	3.3	2.3	1.3	1.8	2.1
China	2.0	1.7	8.5	10.8	10.4	9.2	6.4	3.7	2.9	5.7	8.1
India	0.1	0.1	0.4	0.6	0.7	0.8	0.4	0.2	0.2	0.4	0.5
Mexico	2.1	1.3	2.7	2.9	2.6	2.9	1.8	1.2	1.1	3.1	2.1
Asia	10.0	10.9	19.7	20.3	24.2	22.6	14.6	10.1	10.2	13.0	14.6
Developing Ctries	19.2	16.6	32.0	31.9	39.5	40.1	27.9	21.2	17.7	25.4	24.9
World Total (Billion $)	115	204	275	331	386	482	686	1079	1393	824	651

Notes: Dash denotes zero or negligible and two dotes indicate that data is not available separately. Negative figures reflect disinvestment.
Source: UNCTAD WIR, 1996, 1998 & 2003.

It is important to understand whether these changes in the distribution of FDI inflows in ASEAN were followed by changes in the source countries.

[25] Thus, between 1985 and 2001, while Indonesia's share of inward FDI stock in ASEAN declined from almost half of the total to just 20%, the shares of all the other members (except also Myanmar) increased significantly. Among others, it is Thailand which has increased its FDI stock the maximum, as Malaysia and the Philippines have maintained their shares. In 2001, Singapore had the largest share (40%) of inward FDI stock in ASEAN.

During 1995-97, Japan was the single largest investor in ASEAN,[26] and was followed by the US. The next two single largest investors were the UK (11%) and Singapore (8%). However, accounting for a 24% share in 1995, the EU as a whole was an equally or more important investor than Japan. Netherlands followed by France and Germany were important investors, as was 'Other Europe' (non-EU). Total intra-ASEAN FDI was also as significant as that from the US (13%), the dominant investor being Singapore, as already seen. Malaysia, Thailand and Indonesia were the other intra-ASEAN investors. East Asian I-tier NIEs (Hong Kong, Taiwan province of China and South Korea) accounted for some 9% of inflows in this phase, dominated by the first two. With 6% of the total, 'Other countries' (that is, non-specified) as well as Canada (4%) constituted a significant share of the boom in FDI inflows in this phase.

During 1998-2001, Japan's share as a host country for ASEAN dropped to just 8%. Meanwhile, intra-ASEAN investment also dropped to only 8% of the total. On the other hand, the share of the US shot up to 24%, and the EU became the largest investor group representing 32% of total inflows at a time when inflows into ASEAN had declined in value terms. Singularly, UK's share went up to 17%. While Germany's share of investments declined, that of Netherlands, France and Belgium increased manifold. NICs' share dropped to 7%, mainly due to the decline in FDI by South Korea after the crisis, while there was some drop in Hong Kong's investments as well. There was a notable increase in the shares of Bermuda and Cayman Islands, with the share of 'unspecified others' dropping. Notably, apart from South Korea and Hong Kong, other countries with significant disinvestments from ASEAN in this period were Australia, Canada, and 'Unspecified Others', as well as Thailand and Malaysia.

In 1995, for the largest host country Singapore, the UK and Canada were the single largest investors, followed by Japan, Malaysia, US and Taiwan province of China. Other EU countries (Germany, France, Ireland and Netherlands) also contributed hugely, followed by 'Other Unspecified countries'. In 2001, the UK, US, Netherlands and Japan were the largest investors.

For Malaysia, Singapore and the US were the single largest investors in 1995, each accounting for more than a quarter of total investment. Japan was the third largest source country. UK, Taiwan province of China, Germany, Hong Kong, Netherlands and South Korea were the other significant investors. Brunei, Indonesia and the Philippines also had significant investments. Investments routed through Bermuda were also significant. In 2001, Singapore's share shot up to 42%, followed by Japan, Netherlands and Hong Kong. With Bermuda showing heavy disinvestment, 'Other Unspecified countries' showed a big increase. Remarkably, South Korean and Australian investments in Malaysia increased in 2001, while the US and some of the European countries undertook heavy disinvestment in Malaysia.

[26] These figures are period averages.

For Thailand, Japan, US, Hong Kong, followed by Singapore, Taiwan province of China, Netherlands, France, and the UK were the largest investors. 'Unspecified' countries' share was also significant. In 2001, Singapore became the single largest investor (41%), followed by Japan (36%). UK, Hong Kong, Bermuda and France were the other major investors. The US contributed just 2% of total FDI into Thailand in 2001 and there's a significant disinvestment by Netherlands.

In the case of Indonesia, with a 40% share, Japan was the single most important investor in 1995. Singapore, Netherlands & the US, followed by Korea, Hong Kong, UK and Australia were the next most important investors. In 2001, all these countries undertook large disinvestments; dominated by Japan and the US, followed by Korea, Singapore, Hong Kong, France, Germany, Netherlands etc.

For the Philippines, Japan (43%) was the single largest investor in 1995, followed by Singapore and Hong Kong. South Korea, France, US, UK, Portugal etc. were also significant. In 2001, on the other hand, the US became the dominant investor, followed by Singapore and Japan. While NICs' investment dropped sharply, France became a significant investor, just next to Japan. Other Central and South America as well as 'Unclassified (including banking sector) became significant in 2001.

For Vietnam, the three I-tier NIEs, Taiwan province of China, Hong Kong and Korea as well as Singapore were the single largest investors in 1995. Japan followed by the EU (dominated by the UK, Netherlands and Sweden) were the next largest investors. Malaysia and Thailand also had significant investment in Vietnam. 'Unspecified other countries' also had a large contribution. In 2001, Taiwanprovince of China followed by Singapore, Netherlands, UK and Japan remained the largest investors.

In the case of Brunei, Singapore and the UK were the single largest investors. Malaysia was also a major investor, followed by US, Australia and Thailand. In 2001, more than 95% of the FDI inflows in Brunei was accounted for by just Netherlands and the UK. With Singapore's investment falling below 1%, Malaysia was the only ASEAN investor in Brunei in 2001.

II.E. ASEAN's Major Markets

Now, an analysis of the distribution of ASEAN (8)'s total exports by destination[27] for 1993 shows that with a share of 21%, the regional market[28] was already the largest market for ASEAN. And as we discussed earlier, this share increased until the crisis and peaked at 25% in 1997. But, with its share maintained around 20%, the US was the

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[27] Source: ASEAN Statistical Yearbook, 2003. Destination/origin wise break-ups of Lao and Vietnam's trade data are unavailable.

[28] This refers to ASEAN-10, including ASEAN-8's exports going to Lao and Vietnam.

single largest market for ASEAN between 1993 and 1997. Japan and the EU followed, each accounting for 15% of ASEAN's total exports in 1993.

Within the EU, the UK with an individual share of 6% of the total was the largest destination, followed by Germany and the Netherlands. But, the shares of both Japan and the UK declined to 12% and 3% respectively by 1997. The shares of most other top export destinations, namely, Taiwan province of China, South Korea, China, Australia, and India showed either an increase in share or maintained their shares between 1993 and 1997. Additionally, Hong Kong became an important export market during 1996-97. Thus, the rise in ASEAN's intra-bloc exports between 1993 and 1997 can be seen to have occurred mainly at the expense of ASEAN's exports to Japan and the UK.

However, in the immediate post-crisis period, 1998-99, intra-bloc export share dropped from 25% in 1997 to 22% in 1998-99. Evidently, the 1997-98 financial and economic crises and the subsequent recession across the region had led to a fall in the demand originating from member countries. Meanwhile, although Japan showed a continued fall in share, ASEAN's exports to the US, the EU (a recovery in UK's share and rise in exports to other 'Unspecified EU'), India, and Others showed a relative rise.

But, during 2000-2001 on the other hand, while the shares of intra-ASEAN exports (23%) and Japan (13%) staged a recovery and the EU maintained its total share (15%), the share of ASEAN exports going to the US declined significantly to 17% in 2001.

A significant change in the market composition occurred due to the consistent increase in the share of China as a market for ASEAN exports, which went up from 2% in 1993 to 7% in 2001. There were also constant marginal increases in the case of India (from less than 1% to 2%) and Australia (less than 2% to more than 2%). South Korea and Taiwan province of China more or less maintained their shares, while Hong Kong has also remained among the top ten destinations. Overall, there is a rise in concentration among these top ten markets for ASEAN, with their cumulative share going up from 83% of all ASEAN exports in 1993 to about 87% in 2001.

II.F. ASEAN's Import Suppliers

On the other hand, providing 25% of total ASEAN imports, Japan was the single largest source country for ASEAN in 1993. But its share declined steadily from 1996 onwards and stood at 17% in 2001.

The share of ASEAN's imports originating from within ASEAN was the second largest in 1993 and expanded steadily from 17% in 1993 to 21% in 2001. The US was the third largest supplier in 1993, providing 15% of ASEAN's total imports during 1993-97. It peaked at 20% in 1998 before declining to 14% in 2001. Barring the post-crisis period (which it showed a rise and then a fall), the share of the EU remained around 13%-14%. The shares of the UK and Germany, which were the single largest EU suppliers to

ASEAN in 1993, had declined. But, as can be seen in the case of exports to the EU, the sudden appearance and rise in the share of 'Unspecified EU' suggests that from 1998 onwards there is some un/under-reporting of ASEAN's imports (&exports) from the individual EU member countries also.

Among the NIC suppliers, South Korea (4%) and Hong Kong (1%) have increased their shares in total ASEAN imports, while Taiwanprovince of China's share declined from 4% to 2% in 2001. While Australia's share increased from (to 3% in 2001), India's share has remained at 1% during 1993-2001. Again, ASEAN's imports from China showed a remarkable increase from 1996, with its share rising to 6% in 2001 compared to 2% in 1993. Thus, ASEAN's trade with China has gone up significantly for both exports and imports, and point towards the incorporation of China into the region's trading and possibly production networks.

Remarkably, within ASEAN, the share of 'Unspecified ASEAN', which consists of the combined intra-ASEAN imports of Singapore during 1998-2001 and Thailand during 2000-2001, has registered a sharp rise in share. It is evident that stricter rules of origin in the RTAs (high value addition criteria to claim preferential benefits) are leading to a situation wherein countries and firms involved in imports (from non-ASEAN countries for re-exports to third countries with very low value addition, may manifest these figures in terms of 'unspecified' trade, whose volume has increased significantly. This could be being done to benefit either from AFTA's lower tariff rates or from other preferential benefits under various bilateral FTAs signed by AFTA members with non-members.

II.G. Major Commodities in ASEAN Trade

Analysis of ASEAN-6's exports at the 2 digit HS code reveals clearly that the concentration of ASEAN's exports within the top ten categories has been increasing, with its share in total ASEAN (6) exports going up from 70% in 1993 to 75% in 2001. The export commodity with the largest share has been electrical machinery & parts, (HS code 85). Its share has increased from 23% to more than 30% between 1993 and 2001. The second largest export commodity has been computer machinery & parts (HS code 84), whose share also has risen from 15% in 1993 to 20% in 2001. The third largest category has been mineral fuels (HS code 27), but its share has shown a decline from close to 12% in 1993 to 10% in 2001. In fact, this composition of the top three exports has remained the same for total ASEAN exports since the early 1990s (before the introduction of AFTA).

Among the other top ten export commodities of ASEAN-6, wood and wood products, apparel & accessories (not knitted), apparel & accessories (knitted) and rubber and rubber products, which were the most prominent categories initially, show a continuous decline in their shares. The shares of animal fats & vegetable oils, fish as well as footwear have also declined. Meanwhile, the share of plastics & plastic products has increased to some 2.3% of total ASEAN exports in 2001. While jewellery & semiprecious stones also became a significant export commodity. In addition to vehicle parts & accessories (HS 87), two categories which have increased their shares particularly since 1996 are organic chemicals and optical/medical instruments (HS 90). It is clear from the table below that the composition of top-20 categories among ASEAN's total exports has hardly changed since the early 90s. The increase in concentration among top-ten export categories has come principally from increased concentration into the electrical and computer machinery categories.

Table : Share of Top-20 Products in ASEAN's Total Exports, 1993-2001.

	1993			1995		2001	
Sl.no.	Chap.	Sector	Share	Sector	Share	Sector	Share
1	85	Electrical Equipment	23.1	Electrical Equipment	27.1	Electrical Equipment	30.5
2	84	Computer/Machinery	15.1	Computer/Machinery	17.1	Computer/Machinery	20.0
3	27	Lubricants/Fuels/Oil	11.5	Lubricants/Fuels/Oil	9.0	Lubricants/Fuels/Oil	10.3
4	44	Wood	5.5	Wood	3.5	Plastics	2.3
5	62	Apparel, not Knitted	3.4	Rubber	3.1	Wood	2.0
6	40	Rubber	2.6	Fats & Oils	2.6	Apparel, not Knitted	2.0
7	61	Apparel, Knitted	2.4	Apparel, not Knitted	2.5	Optical/Medical Instruments	2.0
8	15	Fats & Oils	2.3	Jewelry	2.5	Apparel, Knitted	1.9
9	03	Fish	2.1	Plastics	2.0	Organic Chemicals	1.9
10	39	Plastics	1.9	Fish	1.8	Rubber	1.7
		Cumulative Top-10	**69.9**	**Cumulative Top-10**	**71.1**	**Cumulative Top-10**	**74.5**
11	71	Jewelry	1.7	Apparel, Knitted	1.7	Postal Packages & Special Transactions	1.5
12	64	Footwear	1.5	Footwear	1.6	Fats & Oils	1.4
13	98	Postal Packages & Special Transactions	1.5	Optical/Medical Instruments	1.3	Cars, Trucks, Autos	1.4
14	90	Optical/Medical Instruments	1.4	Postal Packages & Special Transactions	1.1	Fish	1.2
15	94	Furniture	1.2	Organic Chemicals	1.1	Furniture	1.2
16	87	Cars, Trucks, Autos	1.1	Articles of Iron or Steel	1.1	Jewelry	1.2
17	29	Organic Chemicals	1.0	Furniture	1.0	**Paper & Paper Board**	1.0
18	55	Man-made Staple Fibers	0.9	Cars, Trucks, Autos	0.9	Articles of Iron or Steel	0.8
19	73	Articles of Iron or Steel	0.9	Man-made Staple Fibers	0.8	Preparations of Meat/Fish	0.7
20	16	Preparations of Meat/Fish	0.8	Toys	0.7	Footwear	0.7
		Cumulative Top-20	**81.9**	**Cumulative Top-20**	**82.6**	**Cumulative Top-20**	**85.5**

Notes: Figures cover only Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand (1993 - 1998). 1999 Figures include Myanmar also and figures for 2000-01 include Cambodia as well.
Source: Based on ASEAN Trade Statistics, ASEAN Secretariat available at www.aseansec.org.

In the case of intra-ASEAN exports, it is seen that the commodity groups with the top three largest shares are the same as in the case of total ASEAN exports. The single largest share is accounted for by electrical machinery & parts. However, accounting for a 27% share in 1993, its share in intra-ASEAN exports was already higher than its share in total ASEAN exports in the early 90s. Further, this has increased continuously through the mid-1990s and was much higher than its in total ASEAN exports in 2001. Similarly, the share of computer machinery & parts has also increased continuously. On the other hand, in the case of mineral fuels & oil, the shares in total ASEAN exports and intra-ASEAN exports have been similar.

With a share of 3%, plastics & plastic products have remained the fourth largest export commodity in intra-ASEAN exports. However, wood & wood products, and fats & oils were of lesser importance in the case of intra-ASEAN exports in comparison to total ASEAN exports, and they also declined in share over the years. On the contrary, vehicle parts & accessories, jewellery & precious stones, followed by iron & steel and articles of iron & steel, none of which were present among the top ten export commodities for ASEAN's total exports in the early 1990s, already had a significant presence in intra-ASEAN exports in 1993. While jewellery and iron & steel dropped out from the top ten later, rubber & rubber products and paper & paper products have both become significant in intra-ASEAN exports since 2000.

Table : Share of Top-20 Products in Total Intra-ASEAN Exports, 1993-2001.

(Percentage)

	1993			1995		2001	
Sl.no.	HS code	Sector	Share	Sector	Share	Sector	Share
1	85	Electrical Equipment	26.8	Electrical Equipment	34.2	Electrical Equipment	35.8
2	84	Computer/Machinery	15.4	Computer/Machinery	17.4	Computer/Machinery	18.3
3	27	Lubricants/Fuels/Oil	13.7	Lubricants/Fuels/Oil	8.6	Lubricants/Fuels/Oil	10.8
4	39	Plastics	3.6	Plastics	3.6	Plastics	3.0
5	71	Jewelry	2.0	Jewelry	1.7	Organic Chemicals	2.1
6	87	Cars, Trucks, Autos	2.0	Cars, Trucks, Autos	1.5	Optical/Medical Instruments	1.5
7	44	Wood	1.9	Rubber	1.5	Cars, Trucks, Autos	1.5
8	15	Fats & Oils	1.7	Fats & Oils	1.5	Rubber	1.4
9	73	Articles of Iron or Steel	1.5	Organic Chemicals	1.4	Wood	1.2
10	72	Iron and Steel	1.5	Optical/Medical Instruments	1.4	Paper & Paper Board	1.2
		Cumulative Top-10	**70.0**	**Cumulative Top-10**	**72.7**	**Cumulative Top-10**	**76.7**
11	90	Optical/Medical Instruments	1.4	Articles of Iron or Steel	1.3	Articles of Iron or Steel	1.2
12	29	Organic Chemicals	1.3	Wood	1.3	Postal Packages & Special Trans.	1.1
13	40	Rubber	1.2	Postal Packages & Special Trans.	1.2	Misc. Chemical Products	1.0
14	48	Paper & Paper Board	1.2	Iron and Steel	1.2	Tobacco	1.0
15	55	Man-made Staple Fibers	1.1	Paper & Paper Board	1.2	Jewelry	**0.9**
16	98	Postal Packages & Special Trans.	1.1	Copper	1.0	Fats & Oils	**0.8**
17	62	Apparel, not Knitted	1.1	Tobacco	0.9	Copper	**0.7**
18	03	Fish	1.0	Tanning/Dyeing Extracts/Ink	0.9	Other	**0.7**
19	74	Copper	0.9	Man-made Staple Fibers	0.8	Iron and Steel	**0.7**
20	54	Man-made Filaments	0.9	Ships, Boats	0.8	Aluminum	**0.6**

		Cumulative Top-20	**81.2**	**Cumulative Top-20**	**83.3**	**Cumulative Top-20**	**85.5**

Source: Same as above.

By contrast, neither textiles nor clothing were significant in intra-ASEAN trade (because of the fact that all these countries are major textile & clothing exporters to the developed markets under the quota system and also had high intra-regional tariffs on these items). From 1996 onwards, organic chemicals and optical/medical instruments became important export commodities within ASEAN.

When we look at ASEAN-6's import structure, it is again seen that there has not been much change in ASEAN's import structure also since 1993. Electrical machinery, computer machinery and mineral fuels & oils have been the three top most import categories throughout, with their shares rising from 24%, 19% and 8% in 1993 to 30%, 18% and 11% respectively in 2001. Vehicles & parts as well as iron & steel, which were the next largest import categories, remain within the top ten still, but has shown a slight decline in their shares.

Table : Share of Top-20 Products in ASEAN's Total Imports, 1993-2001.

	1993			**1995**		**2001**	
Sl. no.	Chap.	**Sector**	Share	Sector	Share	Sector	Share
1	85	Electrical Equipment	24.0	Electrical Equipment	26.6	Electrical Equipment	30.1
2	84	Computer/Machinery	18.5	Computer/Machinery	18.9	Computer/Machinery	17.6
3	27	Lubricants/Fuels/Oil	8.4	Lubricants/Fuels/Oil	6.4	Lubricants/Fuels/Oil	11.2
4	87	Cars, Trucks, Autos	4.2	Cars, Trucks, Autos	4.6	Cars, Trucks, Autos	2.9
5	72	Iron and Steel	4.2	Iron and Steel	4.1	Plastics	2.7
6	39	Plastics	2.9	Plastics	2.8	Organic Chemicals	2.4
7	88	Aircraft, Spacecraft	2.4	Aircraft, Spacecraft	2.7	Optical/Medical Instruments	2.4
8	90	Optical/Medical Instruments	2.3	Organic Chemicals	2.7	Iron and Steel	2.2
9	29	Organic Chemicals	2.2	Optical/Medical Instruments	2.2	Aircraft, Spacecraft	1.9
10	73	Articles of Iron or Steel	2.1	Articles of Iron or Steel	1.7	Articles of Iron or Steel	1.6
		Cumulative Top-10	**71.1**	**Cumulative Top-10**	**72.7**	**Cumulative Top-10**	**75.2**
11	71	Jewelry	1.5	Jewelry	1.7	Jewelry	1.5
12	38	Misc. Chemical Products	1.5	Paper & Paper Board	1.2	Misc. Chemical Products	1.0
13	48	Paper & Paper Board	1.2	Misc. Chemical Products	1.1	Paper & Paper Board	1.0
14	52	Cotton	1.1	Copper	1.1	Aluminum	1.0
15	89	Ships, Boats	1.0	Cotton	1.0	Cotton	0.9
16	74	Copper	0.9	Aluminum	1.0	Postal Packages & Special Transactions	0.8
17	55	Man-made Staple Fibers	0.8	Ships, Boats	0.9	Rubber	0.7
18	40	Rubber	0.8	Cereals	0.9	Tanning/Dyeing Extracts/Ink	0.7
19	98	Postal Packages & Special Transactions	0.8	Postal Packages & Special Transactions	0.9	Copper	0.7

20	32	Tanning/Dyeing Extracts/Ink	0.8	Rubber	0.8	Cereals	0.7
		Cumulative Top-20	**81.9**	**Cumulative Top-20**	**81.9**	**Cumulative Top-20**	**81.9**

Source: Based on ASEAN Trade Statistics, ASEAN Secretariat.

On the other hand, plastics & plastic products, organic chemicals, articles of iron & steel, aircraft, spacecraft & parts, and optical/medical instruments have remained the other major top-ten import commodities throughout. Overall, there is an increase in concentration within the top-ten, which is again attributable to the large increase in shares of electrical machinery imports, followed by imports of mineral fuels & oils.

Among ASEAN's imports from within ASEAN also, electrical machinery again dominates throughout, with a much higher share in intra-ASEAN imports than its share in total ASEAN imports. Its share rose from 34% in 1993 to 36% in 2001. However, the second largest intra-ASEAN import commodity in 1993 was mineral fuels & oils, whose share has however declined from 15% in 1993 to 12% in 2001. Meanwhile, since the mid-1990s, computer machinery has become the second largest intra-ASEAN import, with its share going up from 15% in 1993 to 19% in 2001.

Table : Share of Top-20 Products in Total Intra-ASEAN Imports, 1993-2001.

(Percentage)

	1993			**1995**		**2001**	
Sl. no.	HS code	**Sector**	Share	Sector	Share	Sector	Share
1	85	Electrical Equipment	33.7	Electrical Equipment	36.3	Electrical Equipment	35.1
2	27	Lubricants/Fuels/Oil	15.2	Computer/Machinery	17.2	Computer/Machinery	18.0
3	84	Computer/Machinery	13.8	Lubricants/Fuels/Oil	11.2	Lubricants/Fuels/Oil	12.3
4	39	Plastics	2.7	Plastics	2.7	Plastics	3.0
5	44	Wood	2.3	Wood	2.2	Organic Chemicals	2.5
6	15	Fats & Oils	1.8	Articles of Iron or Steel	1.5	Paper & Paper Board	1.4
7	73	Articles of Iron or Steel	1.6	Rubber	1.5	Articles of Iron or Steel	1.3
8	72	Iron and Steel	1.6	Jewelry	1.4	Optical/Medical Instruments	1.2
9	40	Rubber	1.4	Cereals	1.3	Cars, Trucks, Autos	1.2
10	61	Apparel, Knitted	1.4	Fats & Oils	1.2	Jewelry	1.1
		Cumulative Top-10	**75.7**	**Cumulative Top-10**	**76.5**	**Cumulative Top-10**	**77.1**
11	71	Jewelry	1.3	Organic Chemicals	1.2	Rubber	1.1
12	90	Optical/Medical Instruments	1.1	Paper & Paper Board	1.1	Wood	1.0
13	48	Paper & Paper Board	1.1	Iron and Steel	1.0	Apparel, Knitted	1.0
14	87	Cars, Trucks, Autos	1.0	Apparel, Knitted	1.0	Aluminum	0.9
15	62	Apparel, not Knitted	0.9	Optical/Medical Instruments	1.0	Man-made Staple Fibers	0.8
16	03	Fish	0.8	Postal Packages & Special Transactions	0.9	Copper	0.8
17	38	Misc. Chemical Products	0.8	Copper	0.9	Iron and Steel	0.7
18	89	Ships, Boats	0.8	Aluminum	0.8	Misc. Chemical Products	0.7
19	74	Copper	0.7	Fish	0.8	Cereals	0.7
20	29	Organic Chemicals	0.7	Cars, Trucks, Autos	0.7	Ships, Boats	0.7

		Cumulative Top-20	84.8	**Cumulative Top-20**	**85.8**	**Cumulative Top-20**	**85.5**

While plastics & plastic products has remained the fourth largest intra-ASEAN import category, fats & oils and wood & wood products have declined in share after 1996. Rubber & rubber products, jewellery, and apparel articles & accessories (stitched), articles of iron & steel have been among major imports. From 2000 onwards, organic chemicals, paper & paper products, optical/medical instruments and vehicles & parts (from 2001 onwards) have become significant as well.

In the case of ASEAN's exports to the US (the 'single' largest market throughout, although it has declined in share) also, HS codes 85 and 84 were the two largest export commodities since the early 1990s and much higher than their respective shares in ASEAN's exports to the world. This clearly signified that for ASEAN's electrical and computer machinery exports, the US has been one of the pre-dominant markets since the early 1990s.

Although textiles and clothing showed a significant drop in their respective shares in ASEAN's exports to the US in 1996, they recorded a rise again and have been the third and fourth largest export commodities of ASEAN to the US market throughout. Two other commodities which remain significant among exports to the US are mineral fuels & oils, and fish etc. Two new commodities which have become significant among top ten exports to the US since 1996 are rubber & rubber products and optical/medical instruments. While the category furniture, bedding, lights & light fittings, etc. also records a steady rise in share, footwear & parts show a decline in share from the 1993 levels.

In the case of ASEAN's imports from the US, electrical machinery has been the single largest import commodity and its share rose from less than 30% in 1993 to as much as 36% in 2001. The second largest import of ASEAN from the US has been HS 84. However, after a rise in the mid-1990s, its share has shown a decline in 2001. The third largest import category has been aircraft & parts (88), whose share in ASEAN's imports from the US was at 10% in 2001. The other major imports are optical/medical instruments, plastics & products, organic chemicals, miscellaneous chemical products, and articles of iron and steel. Interestingly, during 2000-01, mineral fuels & oils, cereals, and food industry residues & prepared animal feed became important as ASEAN's imports from the US.

In the case of ASEAN's exports to the EU, the shares and trends with respect to the two largest export commodities (85, followed by 84) are similar to those of ASEAN's exports to the US. However, in 2001, ASEAN's electrical machinery exports to the EU overtook that to the US in value terms for the first time. On the other hand, although they have remained among the top six exports to the EU, textiles and clothing show a steady decline in their shares. Other commodities which ASEAN continue to export significantly to the EU include animal and vegetable fats & oils, rubber & rubber products, furniture, bedding & lighting, etc. Interestingly, vehicle parts & accessories (and also optical/medical instruments) have made a presence among ASEAN's top ten export commodities to the EU during 2000-01.

Among ASEAN's imports from the EU too, HS codes 85 ad 84 were the two largest categories, pointing towards the significant amount of intra-industry trade occurring between the EU and ASEAN countries in these industries. The third largest import commodity from the EU has been vehicles, parts & accessories. But, its share has been much lower at around 4% of the total. The major imports from the EU are observed to be iron & steel, articles of iron & steel, organic chemicals, plastics & plastic products, and also optical/medical instruments, miscellaneous chemical products, etc. In 2001, pharmaceutical products also were important imports of ASEAN from the EU.

The other second most important market for ASEAN in the early 1990s was Japan. In the case of ASEAN's exports to Japan, mineral fuels & oils was the single largest export commodity in 1993 (28%) and 1996. However, it has dropped to the second position since 2000, while electrical machinery has become the single largest export item with a share of 27% since 2000. Computer machinery almost doubled its share and became the third largest export commodity from ASEAN since 1996. Although wood & wood products have remained among the top five ranks, its share has dropped drastically since 1996. On the other hand, ASEAN's textile exports to Japan were significant only till 1996 or so, whereas fish & crustaceans, furniture & lighting, etc., rubber & rubber products, and ores, slag & ash, along with optical/medical instruments remain significant throughout. Plastic & plastic products also have become important exports from 2000 onwards.

From the early 1990s, ASEAN's imports from Japan are dominated by electrical and computer machinery categories, followed by vehicle parts & accessories. The fourth largest ASEAN import from Japan has also been constant, iron & steel. In fact, there has been hardly any change in the commodity structure of ASEAN's imports from Japan. The other major import categories have been optical/medical instruments, plastics & plastic products, articles of iron & steel, organic chemicals and rubber & rubber products.

Mineral fuels & oils, followed by wood & wood products and animal and vegetable fats & oils were the three most important ASEAN exports to China in the early 1990s. However, their shares dropped drastically by the mid-1990s. Simultaneously, by the mid-1990s, there has been a dramatic increase in the shares of computer machinery initially and of electrical machinery. By 2001, electrical machinery accounted for as much as 28% and computer machinery accounted for 20% of ASEAN's exports to China. The other top export commodities by 2000-01 are organic chemicals, plastics & plastic products, rubber & rubber products, postal packages & transactions, and optical/medical instruments, etc.

Again, electrical machinery, computer machinery and mineral fuels & oils showed significant intra-industry trade between ASEAN and China, with the imports of electrical and computer machineries showing rapid increases from the mid-1990s onwards. The other major imports of ASEAN from China have been cotton & cotton fabric, iron & steel, inorganic chemicals, precious metals & radio active elements, and optical/medical instruments, etc.

For ASEAN exports to South Korea too, mineral fuels & oils followed by wood & wood products constituted the two largest export commodities in 1993. However, the share of both dropped drastically to 28% and to 2% respectively in 2001, although mineral fuels & oils still remained the second largest ASEAN exports to Korea. But, by the mid-1990s, ASEAN was exporting significant volumes of electrical machinery and computer machinery products. By 2001, electrical machinery products accounted for 36% of total ASEAN exports to South Korea. Organic chemicals, ores, slag & ash, man-made staple fibres (incl. yarn & fabrics) have been the other important exports to Korea.

In the case of ASEAN's imports from South Korea too, the same pattern of intra-industry trade is observed in electrical and computer machineries, mineral fuels & oils, and organic chemicals. In particular, the share of electrical machinery in total ASEAN imports from South Korea has become as high as 43% since 2000. The other major imports of ASEAN from South Korea have been iron & steel, plastics & plastic products, man-made filaments, yarn & fabrics (54), vehicle parts & accessories, articles of iron & steel (73)

On the other hand, ASEAN's exports to Australia have increased significantly in the case of mineral fuels & oils, which has become the largest export category in 2001 with a share of 26%. Meanwhile, computer machinery, which was the single largest export category in 1993, declined to the second rank with a share of 16%. At the same time, the share of electrical machinery has hovered around 14%. Exports of wood & wood products were significant till 2000. But, increasingly, plastic & plastic products, paper & paper board, jewellery & precious stones, organic chemicals, as well as vehicle parts & accessories have become more important ASEAN exports to Australia.

ASEAN's imports from Australia are less concentrated among the top ten commodities. The import structure again points to significant degree of intra-industry trade taking place in mineral fuels & oils, electrical machinery, computer machinery, jewellery & precious stones. Additionally, cereals, cotton & and cotton fabric, aluminium & products, dairy products & other edible animal products, iron & steel, sugar & sugar confectionary, copper & copper products, etc. have also been important imports of ASEAN from Australia.

In the case of ASEAN's exports to India, with a share of 21%, mineral fuels & oils were the single most important export category in 1993. This declined sharply to some 14% by 2001. Meanwhile, the share of computer machinery has increased from 10% in 1993 to

18% and has been the top most export category since 2000. The share of electrical machinery also increased from 9% to some 14% by 2001. On the other hand, from only 5% in 1993, the share of animal and vegetable oils & fats has increased dramatically from the mid-1990s onwards and stood at 15% in 2001. The share of organic chemicals has also increased significantly, while plastic & plastic products, jewellery & precious stones, man-made filaments, yarn & fabric, optical/medical instruments, etc. have also become important during 2000-01. (India is one of the few export destinations to which ASEAN's exports have not really increased in concentration.)

ASEAN's imports from India was dominated by food residues & prepared animal feed, computer machinery and jewellery & precious stones, apart from electrical machinery, cotton & cotton fabric, etc. But, imports of aluminium & aluminium products, organic chemicals, mineral fuels & oils, meat and edible meat offal, iron & steel, and cereals have also been significant. Thus, ASEAN's trade with India show a significant degree of intra-industry trade in electrical and computer machineries, jewellery, organic chemicals, mineral fuels & oils.

The above analysis of the pattern of trade flows in South East Asia with growing levels of intra-industry trade (to members and non-members) clearly points to a high degree of horizontal division of labour in the region, arising from production distribution carried out by MNCs in these industries.

II.H. AFTA's Contribution to Trade and Investment Integration

The logic underlying AFTA has been that the elimination of tariff and non-tariff barriers would lead to greater efficiencies and competitiveness and eventually bring about the creation of a unified production hub to serve the world market. A larger market would support greater economies of scale, which would in turn make the region more attractive to FDI and lead to a higher level of industrialisation for the region as a whole.

Indeed, the AFTA now covers all manufactured and agricultural products and the current average tariff on goods traded under the AFTA scheme is about 3.8%.[29] 38% (20,701 tariff lines) of the Inclusion List already have zero duties. The Secretariat also states that by the beginning of 2002, only 3.8% of products in the Inclusion List of the original six members (or 1,683 items out of total of 44,060 tariff lines) would have tariffs above 5%. By 2003, the first six members were to each have at least 60% of their Inclusion Lists with zero duties. Vietnam will have 35.4% of its Inclusion List with no tariffs in 2006 while Laos and Myanmar will abolish import duties on 87.6% and 3.9%, respectively, of their IL products by 2008. Cambodia will eliminate duties on 7.6% of its IL in 2010.

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[29] ASEAN Secretariat, 2002, opcit.

According to the AFTA Council, the AFTA has been virtually realized after ten years, since regional tariffs on 99.6% of products in the CEPT Inclusion List (IL) of ASEAN 6 – Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore and Thailand – are now within the 0-5% range, compared to 96.24% in 2002. The Ministers noted that with the completion of the transfer of products from the Sensitive Lists to the IL by 2004, only 247 tariff lines or 0.5% of all products traded in the region would remain out of the CEPT Scheme. The average CEPT rate for ASEAN 6 has gone down from 12.76% in 1993 to 2.39% in 2003.[30]

Brunei Darussalam, Malaysia and Singapore have already reached their 2003 targets and that Thailand will achieve its target within the year. Indonesia, which currently has more than 56% of items in their CEPT Inclusion List with zero tariffs, will complete their 60% target by 2004. The Philippines is facing some legal constraint in implementing this commitment, although majority of the items in their CEPT Inclusion List are levied 1% tariff.

CLMV (Cambodia, Lao PDR, Myanmar and Viet Nam) are also keeping pace with the older members in implementing their CEPT commitments. Their Inclusion Lists now comprise 72.22% of their total number of tariff lines, in contrast to 64.27% in 2002. The CLMV countries will continue to transfer products that were previously excluded from tariff reductions to their IL and by 2004, the IL of CLMV would cover 76.81% of all their tariff lines. In terms of tariffs, CEPT rates on 60.64% of products they trade in the region are already within the 0-5% tariff band and this would go up to 66.74% by 2004. The average CEPT rate for CLMV now stands at 6.22% from 6.77% in 2002. Overall, the inclusion list of ASEAN-10 would be 92.07% of the tariff lines and within these, 91.10% would have tariffs ranging from 0-5%.

Clearly, AFTA's tariff reduction schedule has been very ambitious, particularly in terms of the targets set for the original ASEAN members. However, crucially, it is not known how significant the shares of the various members' Inclusion List products in their respective trade in terms of value terms are. Thus, the reality in tariff reduction and harmonisation across members may not have been as simple as these projections based on tariff lines seem to suggest.

It has been estimated that only around 1 per cent of total ASEAN trade, or less than 5 per cent of intra-ASEAN trade, falls under the Common Effective preferential Tariff of AFTA.[31] This rather limited ratio is attributable to the high costs of compliance with rules of origin and the fact that most members of ASEAN have reduced most-favoured-nation (MFN) tariff rates along with the AFTA rates. While tariffs on intra-ASEAN trade

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[30] Source: The Joint Media Statement of the Seventeenth Meeting of the ASEAN Free Trade Area (AFTA) Council, held on 1 September 2003 in Phnom Penh, Cambodia, available at www.aseansec.org

[31] See 'The Proposed ASEAN Economic Community', Box II.4 , Economic and Social Survey of Asia and the Pacific 2004, UNESCAP, New York.

were being lowered, multilateral tariffs have also been falling as part of the Uruguay Round commitments. With much of the products traded in the region now having CEPT rates that are equal to the MFN rates, separating the effects of AFTA from the broader process of global trade liberalisation will prove to be difficult.[32]

On the other hand, the higher foreign direct investment flows and transfers of production by multinational companies, which have contributed to a greater role for intra-industry division of labor in the region &beyond), can be argued to have played a larger role in the apparently increasing trade and investment integration in the region. We have seen that intraregional trade in Southeast Asia is increasingly characterised by the dynamics of the production networks being developed by MNCs, which have been extensively present in the electrical machinery and computer machinery industries. Increasingly, trade in segments like automobiles, chemicals, and many other products are now being driven by internationally dispersed production patterns. The increased participation of these countries in the growing networks of production has been driven mostly by specialisation in mostly low and medium value added stages of the production process rather than in entire product segments, resulting in high degree of intra-industry trade in the related broad product categories.

This also means that it is the internal and external factors which influence the regional FDI pattern and in turn, the scope and pattern of production restructuring in the individual member countries that will help explain the rise and fall of intra-regional trade shares within ASEAN. This is precisely why, while it is tempting to attribute the rise in intra-bloc trade shares during 1990-95 to the introduction of AFTA from 1993 onwards, the even more rapid tariff reduction further on fails to capture the trends in intra-regional trade flows.

This expansion of IPNs and intra-industry trade can be a major factor contributing to the rapid expansion in intra-regional trade. Since trade among countries linked through international production networks tends to be double-counted, an expansion of such networks gets reflected in a faster growth of international trade in the goods concerned than of their total global production and consumption. TDR (2003) has pointed out that such double-counting was another reason why the data show rapid increases in manufactured exports and imports relative to value added in countries that are heavily involved in IPNs.

It is well known that although production disintegration enables more countries to take part in the production networks, even small variations in costs in the host country can lead to large shifts in locational advantages from the point of view of the parent firm,

[32] As pointed out by Singapore Prime Minister Goh Chok Tong, the original proponent of the ASEAN Economic Community (AEC), only 18 per cent of personal care products and 5 per cent of food are currently sourced within ASEAN, whereas the corresponding figures for the EU are 50 and 25 per cent. See UNESCAP, 2004, opcit.

which then shifts production out to somewhere else. Such footloose nature of the investment involved in production networks requires large and sudden domestic structural adjustments in the host country, to enable its successful transition/upgradation to other higher value-added industries/segments. The required domestic production adjustment and the costs associated with it will be as severe as the extent of production concentration in particular segments.

However, as Dhar and Murali (2002) established so vividly while analysing the Southeast Asian crisis economies, under liberalised financial markets, the credit allocation needs of the real sector for production restructuring may get hijacked by market-determined investment activities, which promote high-return sectors (generally, the FIRE sectors- finance, insurance, real estate and entertainment) with shorter gestations against the longer gestation low-return manufacturing sector.[33] This can seriously jeopardize the structural adjustment needs of their real economies with serious consequences.

Meanwhile, the table below shows that the export dependence of their economies has increased tremendously across the South East Asian region.

Dependence on Exports in ASEAN and Other Selected Countries
(Exports of goods and services as percentage of GDP) #

Country	1970-80	1981-86	1987-92	1993-96	1997-99	2000-01
Brunei	..	..	..	..	..	..
Cambodia	5.8	..	8.4	22.9	34.3	51.8
Indonesia	23.4	24.9	25.1	26.4	38.8	41.7
Lao PDR	..	3.5	12.2	23.1	30.1	..
Malaysia	45.3	52.5	71.5	88.4	110.1	120.6
Myanmar	6.2	6.2	2.3	1.3	0.6	..
Philippines	21.7	23.4	28.3	35.5	50.9	52.8
Singapore	..	..	176.0	172.5	163.6	176.2
Thailand	19.5	22.9	34.0	39.5	55.1	66.7
Vietnam	..	6.6	22.6	34.1	45.6	54.9
ASEAN-5	**27.5**	**30.9**	**53.2**	**72.5**	**83.7**	**91.6**
CLMV*	**6.3**	**6.0**	**11.2**	**20.3**	**27.5**	**53.3**
Hong Kong, China	88.4	100.9	134.0	142.9	131.8	147.0
Korea, Rep.	25.7	34.4	32.2	28.8	42.3	43.8
Australia	14.7	15.1	16.7	19.2	19.7	22.9
New Zealand	25.4	29.3	27.8	29.8	30.0	36.7
India	5.3	6.1	7.5	10.6	11.5	13.8
China	4.1	9.5	16.0	21.9	22.4	25.9
Japan	**11.9**	**13.8**	**10.1**	**9.2**	**10.5**	**10.6**

[33] For a detailed analysis of the pre-crisis credit allocation behaviour in the crisis economies and the links between financial liberalisation and real sector investments, see Dhar, Biswajit and Murali Kallummal, 2002, Capital Inflows and Effects of Market-Driven Investments: A Focus on Southeast Asian Crisis, RIS Occasional Paper No. 66, New Delhi.

Notes: * CLMV- Cambodia, Laos, Myanmar and Vietnam. Two dots denote that data are not available.
All ratios are averages for the given periods.
Source: # World Development Indicators, 2003.

Even though these export figures provide only an imperfect measure of the contribution of the external sector to the members' GDP (which would more appropriately be measured by the domestic value-added contained in exports), they illustrate the increased exposure of ASEAN to fluctuations in export market demand. It is amply evident that across the region, dependence of the countries on exports has increased tremendously. This makes the region extremely vulnerable to country-specific developments in its dominant markets for these industries. Further, high intra-regional dependence can lead to region-wide transmission of such effects.

In a country like Thailand, the implications of such high dependence on particular product segments where expanding export shares in these so called 'high-tech' exports are completely driven by export-oriented FDI production bases and do not reflect the actual domestic production capabilities of the indigenous technological capabilities, have been seen to be severe in the event of shift in global demand trends.[34]

ASEAN's challenges are thus numerous, especially in the context of the severe competition these countries face from China. China has taken great strides in technology absorption and improvements in industrial capacity, and has been moving not only into production areas the ASEAN has left behind, but also into newer areas ASEAN has not so long ago entered. As Chavez (2002) has rightly pointed out, the biggest threat of China is in light of its advance to newer production areas in which ASEAN still has huge production capacities, faster than ASEAN itself can move into higher value-added production areas.

The Asian crisis provided impetus to address major structural weaknesses in regional economies -- especially in the financial and corporate sectors. It also prompted economies in the region to take historic initiatives in regional monetary and financial integration to enhance resilience to external shocks. But, clearly, it is moving towards full-fledged trade and financial liberalisation that in the first place creates the instability and tendency towards regional contagion of financial or real economic instability, thus, giving rise to the need for thinking of regional financial cooperation. But, the fact of the matter is that even with cooperation on the latter front, the vulnerabilities associated with greater and deeper integration will remain (as they are systemic to the system operating under a neoliberal paradigm). Looking at RTAs without examining the working of the financial markets' role in that region will provide only a partial understanding of the dynamics operating there. While this is especially crucial given the

[34] See Francis, Smitha, 2003, Foreign Direct Investment Flows and Industrial Restructuring in South East Asia: A Case Study of Thailand 1987-98, Jawaharlal Nehru University, New Delhi, Unpublished Ph. D. thesis.

widespread liberalization of financial markets in the region, this is beyond the scope of the present paper and will need to be looked at separately.

Under AFTA, the original six members are now committed to implementing zero tariffs by 2010 and the newer ASEAN members have advanced their deadline for doing so from 2018 to 2015 for most products.[35] ASEAN members of Asia-Pacific Economic Cooperation (APEC) will implement zero MFN tariffs also by 2020.

In the absence of the prospect for major tariff preferences, the ongoing initiatives in AFTA are thus focussed towards removing some 'invisible' trade barriers. These include factors that add cost to trade such as transport and communication, infrastructure, harmonization and simplification of custom procedures, trade facilitation measures for transit goods, etc. ASEAN Framework Agreement on the Facilitation of Goods in Transit (signed at the 1998) promotes simplification of procedures (exemption of customs checks, tariffs, etc.) concerning movement of goods within the region. ASEAN has now adopted an ASEAN Harmonized Tariff Nomenclature.

In addition, technical or health standards and other non-tariff barriers may also impose significant costs. ASEAN has devoted attention to trade facilitation in the area of customs and through the elimination of technical barriers to trade (TBTs) with a view to lowering the cost of doing business in the region. In the AFTA Council Meeting held at Cambodia in September 2003, the ASEAN Economic Ministers expressed their serious concern over the slow progress in the work on the elimination of unnecessary and unjustifiable non-tariff measures (NTMs).[36]

At the same time, further investment liberalisation is driven by liberalization of intra-regional flows of investment and harmonisation of investment policies of countries, focused towards attracting MNCs to invest in a range of production capacities covering the region. ASEAN investment cooperation has remained focused on the implementation of the Framework Agreement on the ASEAN Investment Area (AIA) and on engaging major dialogue partners on investment consultations. As of 1 January 2003, the Temporary Exclusion Lists (TEL) for the manufacturing sector of Brunei, Indonesia, Myanmar, Philippines, and Thailand have been phased out thereby broadening the scope of economic activities where ASEAN investors are given national treatment. Malaysia and Singapore have no temporary exclusion list. The ASEAN Investment Area (AIA)

[35] Besides the acceleration of AFTA, the 6th ASEAN Summit in Hanoi in December 1998 pronounced two other bold measures to enhance the investment climate and liberalise trade in services. Vision 2020 as proposed by the Eminent Persons' Group (EPG) at the Hanoi summit is to have ASEAN achieve peace and stability, a regional identity, socially cohesive and caring community of societies and technologically competent ASEAN as in electronic-ASEAN (e-ASEAN).

[36] It has been pointed out that to bring a new pharmaceutical drug to market in ASEAN, a manufacturer needs the approval of 10 health authorities and a bewildering array of non-tariff barriers and product standards impede the freer flow of trade. See UNESCAP, 2004, opcit.

came into force in 2003. By 2010, full national treatment has to be extended to ASEAN investors, which will be extended to all (non-ASEAN) investors by 2020. It has allowance for safeguard measures, a dispute settlement mechanism and contains the most-favoured-nation (MFN) treatment principle.

Member countries have also taken individual policy measures to improve their investment climates. Such measures include signing of bilateral investment treaties, double taxation agreements, further opening-up of sectors for FDI, strengthening institutional arrangement to facilitate the investment process, relaxation of equity ownership, simplification of investment procedures and provision of incentives. The Ministers agreed that the scope of the AIA Agreement include services incidental to manufacturing and those services under the 11 priority sectors (i.e. tourism, air travel, e-ASEAN and healthcare).

The Protocol to Amend the Basic Agreement on the ASEAN Industrial Cooperation Scheme (AICO) to maintain the relevance of the AICO Scheme until 2010 has also been signed. The Protocol provided for new preferential rates to be given to new approved AICO projects: zero percent for Brunei, Cambodia, Indonesia, Lao PDR, Malaysia and Singapore; 0-1 percent for the Philippines; 0-3 percent for Thailand; and maximum of 5 percent for Myanmar and Vietnam. As of 20 January 2004, 172 applications were received, of which 118 applications have been approved, expected to generate an estimated value of US$ 1,236 million of transactions per year.

In October 2003, the ASEAN members signed a landmark accord[37] to turn their vastly disparate states into an integrated, tariff-free trading and economic community by 2020, which would resemble the early embodiment of the European Union. They also agreed to complete deals with China, India and Japan by 2012. The pact with Beijing would create the world's largest free trade zone by far. The ASEAN 2020 vision, dubbed the Bali Concord II, would eliminate tariff and non-tariff barriers, standardise customs procedures, gradually reduce capital controls and abolish visas in a region that is home to 500 million people. Eleven sectors, including electronics, tourism and air travel will be on fast-track integration by 2010 and some nations, particularly Singapore and Thailand, are keen to liberalise everything as quickly as possible.

The High-Level Task force on ASEAN Economic Integration issued its recommendations at the same time as Bali Concord II, setting out numerous, time-bound initiatives. These include improvements in the rules of origin to be completed by 2004 and the removal of non-tariff measures judged to be barriers to trade by 2005. Customs procedures are to be unified and mutual recognition arrangements completed by 2004-2005 in five priority sectors, electrical and electronic equipment, cosmetics, pharmaceuticals,

[37] The Declaration of ASEAN Concord II (also known as Bali Concord II) was signed at the Ninth ASEAN Summit held in Bali, Indonesia.

telecommunications equipment and prepared foodstuffs, with more general harmonization of product standards at a later date. Mutual recognition arrangements in major professional services are to be completed by 2008, and the implementation of AFS and AIA speeded up and given greater priority. Cooperation on, and enforcement of, intellectual property rights will be extended by 2004 and capital mobility facilitated by the implementation of the Road map for the Integration of ASEAN in Finance. Eleven priority sectors, wood-based products, automotives, rubber-based products, textiles and apparel, agro-based products, fisheries, electronics, e-ASEAN, health care, air travel and tourism, are to be fast-tracked for vertical integration and a network of free-trade zones is to be established. Visa requirements will also be liberalized and harmonized.[38] Draft roadmaps for the integration of the 11 priority sectors (as well as a draft roadmap for the horizontal issues cutting across these 11 sectors) have already been submitted.[39]

III. Conclusion

Within a general neo-liberal framework, policy communities in all the major regions of the world have seen a convergence of thinking about how to respond to globalisation. Regional groupings are described as responses to four aspects of globalisation: The replacement of national markets by world markets; the internationalisation of the division of labour; the decline of geographical determinants of financial location and; the continued strengthening of multinational and private policymaking structures vis-à-vis the public authority of the state (Susan Strange, 1995 quoted by Higgott (1998)).

The last point however, seems problematic (in the sense that it covers only the second part of the causal relationship that has developed between regionalism and MNCs). Regional cooperation cannot be seen purely as a response of nation states to deal with the policy problems associated with the increased overtaking of public policymaking space by MNCs. In fact, ASEAN’s integration ideas may be seen as having gone through four stages of evolution. The first phase is the period since the inception of ASEAN as a regional grouping up to the late 1980s, the second refers to the period from the early 1990s up till the East Asian crisis, and the third is the post-crisis period. My argument is that the internationalisation of the division of labour that was already emerging in the region under the globalized corporate strategies mainly of Japanese firms (along with the US, East Asian NICs, and European firms) particularly since the mid-1980s, well before the emergence of the idea of regionalism began to actualise in the 1990s, led to the emergence of MNCs and the private sector elites in Southeast Asia as the core of the policymaking community in the region.

Even though ASEAN existed prior to the emergence of regional production networks, it is clearly seen that the efforts towards economic integration accelerated only from the

[38] Source: UN ESCAP, 2004, Economic and Social Survey of Asia and the Pacific 2004.

[39] The media statement of Tenth ASEAN Economic Ministers Retreat, 1 April 2004, Singapore.

early 1990s. Surely, by then there was the emergence of strong interest groups towards making ASEAN an integrated market for goods and services, with potential benefits of regional economic cooperation relating to lower risk and uncertainty for investors. Indeed, it is not surprising that Japanese and other businesses have been among the most enthusiastic proponents of the ASEAN Free Trade Area (AFTA) and ASEAN Investment Area.

Along side, at the level of the government policymaking community, there was also the recognition of the need to fight the competition from the emerging China, NAFTA and East Europe in the case of investment, by putting forth ASEAN as a unified region offering both a suitable platform for production allocation as well as an integrated market.

On the other hand, what Susan Strange (quoted by Higgott 1998) describes will pertain to the post-crisis period. Following the East Asian crisis, there has been a growing desire on the part of a wide range of policy makers in the region to establish a more cohesive regional vision. Following the crisis, two things have happened. At first, it was the purely reactionary in that there was the (re)awakening of the idea of 'East Asianness' and the need to come together to fight an 'external common enemy'. But, gradually but surely, there was the growing and widespread recognition of the problem of the erosion in the capacity of nation states to deal with the policy coordination issues requiring transnational attention.

This can be observed to be particularly true of attempts in ensuring regional financial stability and security – link to the discussion on the regional bond market, as well as of the need to liberalise to increase competitiveness in the face of enhanced challenges from other countries/regions retain the attraction of the region for the MNCs who had already managed to get the countries in the region in a race-to-the-bottom in investment incentives and tax concessions. In this sense, any attempts in policy harmonisation can be seen as a response to the challenge of continued strengthening of multinational and private policymaking structures vis-à-vis the public authority of the state/s in the region, as Strange (1995) pointed out. However, regional initiatives cannot advance in a context where nation states abdicate the responsibilities for policymaking at the country level, as domestic level adjustments towards the international dimensions of adjustment become crucial.

The large integrated markets offered by China, AFTA, India etc. pose challenges for ASEAN, which cannot be addressed effectively with further tariff or non-tariff liberalization. We have clearly seen that regional integration efforts that lower the costs of cross-border transactions to help advance the locational advantages of the member countries in the international production system context, will not even succeed in that purpose.[40] Continuous production restructuring and upgradation through indigenous technological capability development is a necessary pre-condition for a sustainable shift to export-led growth. The pace of progress in expanding higher value-added manufacturing will be crucial for the more developed ASEAN members.

A fourth and the latest phase clearly go beyond the traditional parameters that define RTAs, in particular, geographical proximity. The US and the EU are making a series of separate trade agreements with member countries of ASEAN to gain access to their markets, without having to make serious concessions themselves. The various bilateral FTAs coming into being can be seen essentially as the emergence of various negotiating alliances (hoping to protect the perceived national interests of member elites). At a deeper level, does the emergence of these FTAs point to the resurgence of the neoliberal ideology in the Asian region, while some analysts had earlier hoped that the new Asian discourse (of the late 1990s) would help resist the ideological hegemony of the USA within the context of an 'Asia-Pacific' (in the APEC context) discursive strategy of the USA and its acolytes such as Australia?

In fact, there are certain other questions that need to be answered in this context as well: Does the emergence of the fourth phase mean contradiction with the resurgence of a 'regional identity' in the earlier phases? How will the region reconcile the identity question in the face of bilateral FTAs whose underpinning characteristics obviously lie beyond geography?

In the final analysis, it is evident that without effective strategies for industrial transformation at the national levels, ASEAN's attempts to attract investment through AIA or other initiatives for an export-oriented growth strategy will fail to be effective beyond the short-term. This is so since the strength and stability of the ASEAN economies will be dependent on their national strategies to a larger extent, and on regional and multilateral initiatives to a smaller extent. National strategies will become all the more crucial in building strong bargaining positions in trade negotiations, particularly in the context of the burgeoning bilateral trade deals involving ASEAN countries.

1st July, 2004.

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40 This is evident from the decline in the region's share in world FDI inflows to 3.3% in 1998 and further to just 2% in 2002.