ASEAN@50
Volume 3

ASEAN and Member States: Transformation and Integration

Edited by Ponciano Intal, Jr. and Lurong Chen

Economic Research Institute for ASEAN and East Asia
I congratulate the Economic Research Institute for ASEAN and East Asia (ERIA), the Permanent Mission of the Philippines to ASEAN and the Philippine ASEAN National Secretariat for publishing this 5-volume publication on perspectives on the making, substance, significance and future of ASEAN. This valuable publication, forming part of the Philippines’ commemorative activities in celebration of ASEAN’s golden anniversary, highlights ASEAN as one of the world’s most successful and enduring regional organizations.

It pleases me to note that this printed work equally supports the development priorities of President Rodrigo Duterte and the Philippine Chairmanship priorities — building a people-oriented and people-centered ASEAN, maintaining peace and stability in the region, cooperating in maritime security, advancing inclusive and innovation-led growth, promoting a resilient ASEAN, and establishing ASEAN as a model of regionalism and a global player. Consistent with President Duterte’s pursuit of an independent foreign policy for the benefit of the Filipino people, the publication also affirms the ASEAN Community Blueprints in raising the profile and awareness on the ASEAN pillars of political-security, economic and socio-cultural communities.

We seek the aid of the Almighty and are hopeful that this publication will provide the reader with greater insights on ASEAN’s history, will be used by decision makers, government officials, analysts, and the people of ASEAN, in charting the future course of the region.

Mabuhay!

Manila, August 2017

Alan Peter S. Cayetano
Secretary of Foreign Affairs
Republic of the Philippines
'The fragmented economies of Southeast Asia [with] each country pursuing its own limited objectives and dissipating its meager resources in the overlapping or even conflicting endeavors of sister states carry the seeds of weakness in their incapacity for growth and their self-perpetuating dependence on the advanced, industrial nations.’ These were the words of Narciso R. Ramos, Foreign Minister of the Philippines, when on 8 August 1967, he and four fellow foreign ministers signed the foundational document for yet another regional body; this time, the Association of Southeast Asian Nations.

How these fragmented economies advanced from such unpromising beginnings to the dynamic region they are today is a history that needs to be recounted, and I am pleased that this volume addresses the questions we all have by reflecting on the keys to ASEAN’s longevity and success.

At the time of its establishment, and noting the recent region’s recent history, the words of the founding charter appeared overly lofty and ambitious, talking of ‘the collective will of the nations of South–East Asia to bind themselves together in friendship and cooperation and, through joint efforts and sacrifices, secure for their peoples and for posterity the blessings of peace, freedom and prosperity’. But with changes of government in the region and wars being fought outside of ASEAN’s then borders, a new political reality was taking shape and for the first time the governments of ASEAN Member States had a common purpose.

Of course, no one could have imagined just what or how such a transformation would bloom in the years to come. Chapter 1 notes how, ‘the first 30 years [of ASEAN] were bookended by economic crises’. With hindsight we see just how economic and political crises can intertwine to bring bursts of renewal and reform. The early years of ASEAN brought stability to the region, allowing for countries to develop their own economies. Changes in the world economy, for example in commodity prices, were skilfully responded to with domestic policy reform and adjustment. Then, in December
1997, at the height of the Asian economic crisis, rather than retreating into isolation and despair, the Leaders of ASEAN came together – in what for some looked like the theatre of the absurd – to sign up to ASEAN Vision 2020. Supported by creating +1 ties to other regional states, this Vision set the framework for ASEAN to become an ever-increasing part of the global value chain.

Importantly, another crucial change took place in the region with the reset of political ideologies in the mid- to late 1960s. The nationalistic ideologies that spurned outside interference and capitalism which dominated some countries gave way to a new embrace of the outside world. Countries of the region were now open to business, accepting the benefits of trade and welcoming outside investment, a key step towards economic transformation.

Economically, the last 50 years have been truly remarkable ones for ASEAN. The next 50 years, with the advent of the Gig economy and Connected Industry, amongst other current buzz terms, will create plenty of challenges for ASEAN and the need to create a people-responsive economy. Lessons for the future can always be discovered from understanding the past. I have no doubt that Volume 3, ASEAN and Member States: Transformation and Integration, gives us cause for measured optimism that ASEAN and the ASEAN Member States could successfully adapt to changes and move forward robustly amidst the challenges of the economic and technological environment in the future.

I would like to thank all those who contributed to this volume, a valuable public memory for us to share with our current and future generations.

May I also express my gratitude to Ambassador Elizabeth Buensuceso of the Philippine Permanent Mission to ASEAN for her strong support and guidance since the start of the ASEAN@50 project.

Jakarta, August 2017

Hidetoshi Nishimura
President
Economic Research Institute for ASEAN and East Asia
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Chapter 1
The Economic Transformation of the ASEAN Region in Comparative Perspective

Ponciano S. Intal, Jr.
Senior Economist, Economic Research Institute for ASEAN and East Asia

ASEAN: an Economic Success Story in the Developing World

Over the course of ASEAN’s 50 years of existence, the ASEAN region has been transformed from a relatively poor region in the 1960s into a robustly growing region of middle-income to high-income countries. The ASEAN Member States (AMSs) have transitioned from being largely exporters of primary products into regional and global exporters of commodities, manufactures, and services. The region has experienced an almost consistently rising share of global output, exports, and imports, and secular but inconsistent global foreign direct investment (FDI) inflows, beating out other prominent regional groupings in the developing world (see Figure 1.1). The pace and consistency of the rise of ASEAN’s shares in global output and international merchandise trade, as well as the secular rise of ASEAN’s share of global FDI inflows, are indicative of ASEAN as an economic success story vis-à-vis other regional associations in the developing world.

ASEAN’s share of global gross domestic product (GDP) rose markedly from 0.8% in 1970 to 1.5% in 1990 and 2.6% by 2015. This contrasts sharply to the near stagnancy in the global shares of Mercosur (Southern Common Market) and the Latin American Integration Association, two major regional integration areas in South America, which both saw significant rises in their global shares from 1970 to 1980 but fell afterwards.

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1 Mercosur comprises Argentina, Brazil, Paraguay, Uruguay, and Venezuela (suspended in December 2016). The Latin American Integration Association is composed of Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Panama, Peru, Uruguay, and Venezuela. Although established in 1980, it superseded the defunct earlier Latin American Free Trade Association established in 1960.
in 1990 before inching up very slowly until 2015 at lower-than-the-1980 shares. Similarly, despite being far less populous, ASEAN’s global GDP share rose to almost the same as the much more populous South Asian Association for Regional Cooperation (SAARC) region by 1980 and kept apace with SAARC during the next 2 decades until 2000. It was only in 2000–2015 that high growth in SAARC, especially for India and Bangladesh, led to a higher global GDP share of the much more populous SAARC than ASEAN by 2015 (see Figure 1.1).

**Figure 1.1. Shares of Selected Regional Economic Cooperation in World GDP, FDI, and Merchandise Trade (%)**

FDI = foreign direct investment; GDP = gross domestic product.

UNCTAD Stat Dataset, [http://unctadstat.unctad.org](http://unctadstat.unctad.org)

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2 The Latin American Integration Association’s global GDP share rose from 5.1% in 1970 to 6.4% in 1980. Mercosur’s global GDP share rose from 2.7% in 1970 to 3.4% in 1980.

3 SAARC is composed of Afghanistan, Bangladesh, Bhutan, India, Nepal, the Maldives, Pakistan, and Sri Lanka.
ASEAN = Association of Southeast Asian Nations, LAIA = Latin American Integration Association, Mercosur = Southern Common Market, SAARC = South Asian Association for Regional Cooperation, SADC = Southern African Development Community.


Figure 1.1 also shows that ASEAN has been the stellar performer in foreign trade among the major regional economic associations in the developing world. In both exports and imports, ASEAN’s global share rose consistently and substantially from 1970 to 2015, overtaking the Latin American Integration Association’s share by 1990 then pulling ahead afterwards into 2015. SAARC, Mercosur, and the Southern African Development Community (SADC) have had global shares that have been significantly lower than ASEAN. In terms of FDI inflow, ASEAN’s global share rose secularly and significantly, highlighted by a nearly 10% share in 2014, reflecting a surge of FDI inflow into ASEAN after the sharp fall in its global share during the crisis years in the late 1990s. Similar to the case of global shares in foreign merchandise trade, and except for the crisis years 1998–2002, ASEAN largely significantly outperformed SAARC, Mercosur, and SADC in global shares of FDI inflows during most of 1970–2015.

The comparatively strong performance of ASEAN in foreign merchandise trade and FDI inflows is echoed in the economic growth performance of the region (see Table 1.1). Table 1.1 shows that the five founding members of ASEAN, together with the future sixth member, Brunei Darussalam, had high growth rates in the 1970s that were much higher than the 5.6% for middle-income countries and 3.2% for industrialised market economies based on the World Bank’s 1982 World Development Report (Estanislao and Aquino, 1983). The other decade of high growth rates in most of ASEAN-6 (the founding five countries plus Brunei) was during the 1986–1996 period before the East Asian crisis of 1997. During the 2000s and early 2010s, it was the new members of ASEAN – i.e. Cambodia, the Lao PDR, Myanmar, and Viet Nam, or the CLMV countries—that consistently topped the growth charts in ASEAN and were among the highest in the developing world.
It is worth noting that ASEAN’s first 30 years were bookended by economic crises, and those crises significantly shaped the course of ASEAN. Specifically, ASEAN was established in 1967 on the heels of a serious economic crisis in Indonesia, ASEAN’s largest member. Indonesia’s annual inflation rate was about 2,285% (Yah, 1976). Such hyperinflation (an indication of serious economic crisis) led to the change in government from President Soekarno to President Suharto. This new government emphasised ending konfrontasi and being at peace with its neighbours, which kick-started with Thailand the establishment of ASEAN in August 1967. The new government succeeded very soon in stabilising the economy: with inflation dropping to an average of 6.2% in 1969–1972, the rupiah becoming stable, and the economy quickly growing at 8.2% during the same period (Yah, 1976).

**Table 1.1. Average Economic Growth of ASEAN Member States**

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<td>1.22</td>
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Similarly, in the 30th year of ASEAN’s existence, the ASEAN region was ground zero of the East Asian crisis that started in Thailand in July 1997 and would engulf all five founding members of ASEAN; the Republic of Korea (henceforth, Korea); and, to a lesser extent, Hong Kong. The marked slowdown in economic growth and the sharp drop in FDI inflow during the latter 1990s are reflective of this economic crisis (Figure 1.1 and Table 1.1). Remarkably, amidst the deepening economic crisis, ASEAN leaders unveiled
the ASEAN Vision 2020 during the Special Summit in Kuala Lumpur in December 1997 that pushed forward regional integration and community building much deeper towards 2020. In addition, during the same Special Summit, the ASEAN leaders held their joint meetings with the three leaders from China, Japan, and Korea in what would become the ASEAN+3 grouping. The crisis gave rise to deeper East Asian economic cooperation, as highlighted by the eventual ASEAN+1 free trade agreements (FTAs) and the Chiang Mai Initiative.

Table 1.1 also shows a significant slowdown in the average growth rates of ASEAN countries in the early 1980s. This proved to be a catalyst for domestic reforms that, together with major developments in East Asia during the latter 1980s, effectively reshaped the trajectory of ASEAN economies into the 1990s and beyond. Behind this was the marked deterioration of the global economic environment, characterised by sharp falls in commodity, energy, and mineral prices and the emergence of a serious debt crisis in the developing world that affected Latin America especially as well as the Philippines. The adverse global environment for primary products and the deepening pressures on trade and fiscal balances have led to significant policy reforms towards greater liberalisation, especially in Indonesia.

The homegrown reforms occurred at the same time as the 1985 Plaza Accord led to a significant appreciation and the concomitant substantial flow of Japanese FDI into ASEAN for manufacturing – and not only in natural resources–based industries. The yen appreciation, followed by the appreciation of the New Taiwan dollar and the Korean won, became a significant catalyst for the development of ASEAN as an export platform for (labour-intensive) manufactures to the world. Thus, the confluence of the domestic reforms that got a push from the sharp falls in commodity prices and the resulting adverse macroeconomic pressures, including some currency depreciation, in ASEAN and the external currency appreciations of the yen, won, and the New Taiwan dollar that gave rise to large FDI inflows into ASEAN led to the robust expansion of export-oriented manufacturing in the region and the eventual integration of ASEAN into the growing regional production networks.

Over the course of the economic booms and a crisis, the ASEAN region has been drastically transformed during the past 50 years (see Table 1.2). In all five founding AMSs, agriculture has drastically declined in economic importance, although the countries are still leading global or regional exporters of several agricultural products, such as palm, coconut, rubber, and bananas. Manufacturing surged in importance and for countries like Singapore, Malaysia, and the Philippines, services – especially modern services like finance, tourism, business, and logistics – have become the largest sector in the economy. For the newer AMSs, robust growth in agriculture and the surge in exports
of highly labour-intensive manufactures like garments as well as tourism have been key drivers of the high economic growth rates during the past 2 decades. As Table 1.2 shows, their economic structures have changed markedly during the period with much higher shares for industry and services.

Table 1.2. Average Economic Growth of ASEAN Member States (%)

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Key Factors of ASEAN Economic Performance and Transformation

Economic growth and transformation is a complex process. Many factors, both economic and non-economic as well as domestic and external, contribute to this growth and transformation process. The decomposition analysis of economic growth in terms of the contributions of capital, labour, and total factor productivity provides a robust common framework for determining the key sources of growth among the AMSs during the past few decades. Table 1.3 consolidates the annual decomposition estimates of the Asian Productivity Organization (2016) for the AMSs.

As the table suggests, (physical) capital or investment has been the most important driver in most cases of economic growth in the region, especially during the very high growth (‘boom’) periods of 1971–1979 and 1986–1995 for the five founding members and the 1990–2010 period for the newer members. The large contribution of capital to economic growth was particularly noteworthy for Singapore and Malaysia in 1971–1985; Viet Nam, in 1996–2014; the Philippines, in 1971–1979; Indonesia, in 1975–1985; and Thailand, in 1991–1995. The growth of capital, or effectively investment, was high in these countries especially during the boom periods, although the growth of capital in the Philippines was more modest. As a useful reference to the ASEAN experience, it is worth noting that the growth rate of capital in China was on average higher and for a longer period than the AMSs (especially during 1986–2014), which partly explains the even more remarkable economic transformation of China during the period. Thus, the results of the growth decomposition analysis of ASEAN countries and China shows the critical importance of the growth of capital in the economic growth (and transformation) process.
Table 1.3. Productivity in ASEAN Countries and China (%)

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<td>-</td>
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<td>Contribution of labour input</td>
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<td>Total factor productivity</td>
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<td>3.28</td>
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<td>3.95</td>
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<td>4.91</td>
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<td></td>
<td>Contribution of labour input</td>
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<td>1.91</td>
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<td>2.87</td>
<td>3.52</td>
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</table>

Note: Data are not available for Brunei Darussalam, Myanmar, or the Lao PDR.
Source: APO Productivity Database 2016 Ver.1.
The strong emphasis on investment as a driver of economic growth in several AMSs is reflected in Figure 1.2. As the figure indicates, the ratio of gross capital formation (or investment) to GDP in Indonesia reached 30% or more during 1979–1987, then rose even higher to more than 40% in 1988–1997 before settling back down to more than 30% in 2000–2015. Similarly, Thailand’s ratio of gross capital formation to GDP was virtually more than 30% in 1970–1989 and then rose further to more than 40% in 1990–1996 before declining to mainly the 20s since then. Singapore’s investment-to-GDP ratio was in the high 30s to more than 40% during 1975–1985, then became largely in the low 30s to mid-30s until 2000, followed by rates largely in the 20s. Malaysia’s ratio rose secularly from the low 20s in early 1970 to the low 30s in the early 1980s, dropped to the mid-20s during 1985–1990. It then surged into the 30s and over 40% by 1997 before settling back to the 20s since 1998. Viet Nam’s ratio secularly rose from the low 20s in the mid-1990s to reach the mid-30s in 2007–2010 and the low 30s by 2015.

Of the major ASEAN economies, the Philippines had an almost consistently low gross capital formation-to-GDP ratio from the 1970s to the early 2010s, mainly in the low 20s, except for when it entered the high 20s in the latter 1970s and the high teens in the mid-1980s (the crisis period) and the latter 2000s (a period of macroeconomic uncertainty). The comparatively low investment-to-GDP ratio partly explains the comparatively lower rate of economic growth of the Philippines for much of the period. Cambodia’s gross capital formation-to-GDP ratio was barely 10% in the mid-1990s but rose secularly to the low 20s by the early 2010s.

Despite its relatively low investment-to-GDP ratio compared to countries like Indonesia or Thailand, Cambodia experienced remarkably high rates of growth during 1999–2008 (see Table 1.1). These are because of high employment growth and robust total factor growth rates, likely as benefits of the successful rebuilding of the country from the ravages of internal conflict. Brunei Darussalam has had the lowest ratio (Figure 1.2), resulting in the continued strong dependence of the economy on energy resources and very low overall economic growth, except largely during periods of higher energy prices (e.g. the 1970s and the early 1990s) (see Table 1.1).
The contribution of labour growth has been largely modest for the ASEAN countries for most of the period. Nonetheless, there were instances where labour growth was robust, noticeably during boom periods, probably reflecting significantly higher labour force participation rates in response to markedly improved employment conditions (e.g. in Thailand in the latter 1970s and Indonesia in the latter 1980s). Singapore is particularly unique because its high economic growth was accompanied by a markedly high growth in labour, reflecting the immigration or labour import response of a country with a very limited domestic labour pool.

For most AMSs, total factor productivity growth also contributed to overall economic growth, albeit relatively modestly for most of the period. Nonetheless, there were several instances of robust productivity growth such as in Thailand during 1986–1990 and 2001–2005; the Philippines during 1986–1990 and 2011–2014; Indonesia during 1971–1975 and 1986–1990; and Malaysia and Singapore during 1986–1990. However, note that most of the sub-periods indicated above were sub-periods after economic crises or growth slowdowns when total factor productivity declined (e.g. during the early 1980s and late 1990s). In short, these sub-periods of significantly higher rates of growth of total factor productivity were for mostly economic recovery periods boosted by markedly improved market conditions.
As a comparison, the growth of total factor productivity in China was significantly higher and consistently positive than that of ASEAN countries that, together with high investment growth, resulted in consistently very high growth rates over at least 3 decades. Thus, China’s productivity growth appears much more anchored on structural factors and efficiency gains, which partly explains the continued competitiveness of China in most manufactures in the export market despite substantially rising real wages. Engendering such robust growth of total factor productivity outside of economic recovery periods from a previous crisis remains a considerable challenge for most of ASEAN, which the grouping takes into account in its ASEAN Economic Community Blueprint for 2025.

The growth of total factor productivity, as shown in Table 1.3, although modest but largely consistent, may reflect many other factors that shaped ASEAN’s economic performance and transformation. Such other factors include the rising quality of human capital in the region, as reflected in the rise of average schooling, especially of the younger population; the quality of institutions; and even of peace itself. Additionally, the high investment rate discussed earlier embodies in it not only machines but also roads, railroads, ports, airports, and other infrastructure facilities that have contributed to the faster movement of people and goods and likely greater efficiencies in production, which itself is contributory to the growth in total factor productivity.

Perhaps more importantly, the embracing of foreign trade and foreign investment by ASEAN countries contributed to the growth of total factor productivity through better allocation of resources within countries, greater pressure for increased firm efficiency, and the transmission and adaptation of foreign technologies, management practices, and market knowledge and linkages that economic openness engenders. Indeed, there has been great synergy among investment, factor productivity, and economic openness. Thus, AMSs’ openness to foreign trade and investment led to the surge in foreign investment, which itself contributed substantially to the significant rise in overall investment rates among ASEAN countries. Similarly, greater trade and higher economic growth have entailed increased demand for better and more accessible infrastructure, which has raised overall investment rates. Meanwhile, the transfer of technologies, management practices, and market knowledge has raised human capital in the host countries of FDI.
Economic openness and the resultant pressure for greater competitiveness increase the demand for better institutions and governance. These contribute to greater investment attractiveness and likely higher foreign investment inflows. It is precisely this virtuous cycle from economic openness that ASEAN countries have increasingly tapped for their economic development. And it is precisely in enhancing further this virtuous cycle that is at the heart of ASEAN’s – and East Asia’s – drive for greater openness and economic integration embodied in the ASEAN Economic Community blueprint and the (future) Regional Comprehensive Economic Partnership (RCEP) that is being negotiated and expected to be signed in 2017.

The next chapter discusses in greater detail foreign trade, investment, and integration in ASEAN, and chapter 3 discusses the implementation of the ASEAN Economic Community blueprint.
Chapter 2
ASEAN Foreign Trade, Investment, and Integration in Comparative Perspective

Economic Research Institute for ASEAN and East Asia

Lurong Chen, Economist
Ponciano S. Intal, Jr., Senior Economist

ASEAN Economic Openness and Globalisation

Most ASEAN Member States (AMSs) have been heavily trade-oriented, especially since the mid-1980s (Figure 2.1). Being small countries, Brunei Darussalam and Singapore could be expected to be trade dependent; the former having its energy exports as its lifeblood, and Singapore, leveraging its vantage point in the international shipping route along the Malacca Strait and its geographic nearness to two major global producers of tropical products into a leading regional and global player in transshipment, processing, and services. Malaysia since the 1970s, Thailand since the early 1990s, and Viet Nam and Cambodia since the turn of the 2000s have had export share-to-gross domestic product (GDP) ratios of at least 30% and rising secularly to reach more than 70% in Malaysia and Thailand and more than 100% in Viet Nam by 2015.\(^1\) Imports have correspondingly expanded strongly, especially since the latter 1980s. Indonesia and the Philippines are the two major ASEAN countries that have been much less trade oriented than the rest of ASEAN. Nonetheless, their shares of exports and imports to GDP have also risen secularly, although more modestly than in other AMSs. As implied in Chapter 1, the strong trade orientation of most AMSs has translated into the rising global share of ASEAN in both exports and imports during the past few decades.

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\(^1\) Malaysia’s export share to GDP reached more than 90% in the late 2000s and then declined to the low 70% by 2015.
Figure 2.1. Share of ASEAN’s Exports plus Imports to Gross Domestic Product

![Share of ASEAN countries' export plus import to GDP (%)](image)

Source: World Bank Dataset: Exports of goods and services (% of GDP), and Imports of goods and services (% of GDP), [http://databank.worldbank.org](http://databank.worldbank.org)

Table 2.1. Foreign Direct Investment as a Share of Gross Fixed Capital Formation (%)

<table>
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<td>5.38</td>
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<td>SADC</td>
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<td>0.15</td>
<td>9.48</td>
<td>7.40</td>
<td>13.82</td>
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</table>

ASEAN = Association of Southeast Asian Nations; ASEAN+3 = ASEAN plus China, Japan, and the Republic of Korea; EU25 = European Union 25; LAIA = Latin American Integration Association; Mercosur = Southern Common Market; NAFTA = North American Free Trade Agreement; SAARC = South Asian Association for Regional Cooperation; SADC = Southern African Development Community.

Source: UNCTAD Stat Dataset: Foreign direct investment as percentage of gross fixed capital formation, [http://unctadstat.unctad.org](http://unctadstat.unctad.org)
ASEAN has been successful in attracting foreign direct investment (FDI); indeed, it has competed with China as the largest FDI investment destination in the developing world in recent years. Thus, for example, ASEAN accounted for 6% of total FDI inflows in 2015 even though it only accounted for 3.3% of global GDP. Table 2.1 shows the ratio of FDI inflows to gross capital formation for ASEAN and other regional economic groupings from the 1970s. As the table indicates, FDI has played a more important role in the region’s capital formation since the 1980s compared to Mercosur (Southern Common Market), North American Free Trade Agreement (NAFTA), South Asian Association for Regional Cooperation (SAARC), and, for much of the period, the European Union (EU). In terms of the ratio of FDI to GDP since the 1970s, most of the AMSs have had ratios that are higher than the average for all developing economies. Singapore stands out for having a large FDI presence vis-à-vis national output since the 1970s, while Cambodia is noteworthy for having the second-highest among the AMSs (second to Singapore) during the past decade.

The liberalisation process of facilitating deeper trade and investment linkages between ASEAN and the world has transpired in the region, especially since the mid-1980s. Thus, for example, there have been large declines in most-favoured-nation (MFN) tariff rates of all manufactured goods, ores, and metals from the late 1980s to the mid-2010s in countries such as Indonesia, the Philippines, and Thailand and to a less extent (the historically less trade restrictive) Malaysia. This is in addition to the historically virtually low-to-zero MFN tariff rate economies of Brunei Darussalam and Singapore. This is indicative of the adoption of trade liberalisation policies in ASEAN in recent decades (see Table 2.2). The MFN tariffs for Cambodia, the Lao PDR, Myanmar, Viet Nam (or CLMV countries) have also declined during the past 2 decades, albeit more moderately. Considering that intra-ASEAN tariff rates declined to virtually zero for 2010 in the ASEAN-6 countries and to nearly zero in most imports for the CLMV countries going into the 2018 deadline, the weighted averages of the MFN and the intra-ASEAN tariff rates have indeed declined dramatically during the past 2–3 decades.
Table 2.1. Foreign Direct Investment as a Share of Gross Fixed Capital Formation (%)

<table>
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<td>Brunei Darussalam</td>
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<td>3.71</td>
<td>3.64</td>
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<td>Viet Nam</td>
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<td>9.34</td>
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Source: http://unctadstat.unctad.org/wds/TableViewer/tableView.aspx?ReportId=122

Figure 2.2. KOF Index of Economic Globalization (weighted by GDP), 1990–2013

ASEAN = Association of Southeast Asian Nations, EU = European Union, NAFTA = North American Free Trade Agreement.

Source: Author’s calculations based on 2016 KOF Index of Globalization.
A measure of the extent of ASEAN’s economic openness and economic integration is the Konjunkturforschungsstelle Index of Globalization (KOF Index), calculated based on a country’s performance in international trade and investment, foreign payments, and measures on trade barriers, including tariff, non-tariff barriers, tax, and capital restrictions. The annual report published by ETH Zurich is based on country-level data; we use the GDP-weighted average of member states’ scores as a proxy for the region’s overall level of economic globalisation for ASEAN, Mercosur, the EU, and NAFTA.

Figure 2.2 presents the pattern of economic globalisation in ASEAN, the EU, NAFTA, and Mercosur since 1970 using the KOF Index of Economic Globalization. ASEAN’s economic globalisation increased gradually from 1970 to 1986, accelerated in 1986–1998 to about 65, and then fluctuated before reaching 68 in 2013. Figure 2.2 shows that ASEAN’s level of globalisation accelerated during the 1990s but stagnated from the late 2000s along with the EU, NAFTA, and Mercosur.

The acceleration of globalisation globally in the 1990s coincided with the establishment of major regional integration areas (the EU, NAFTA, and ASEAN) together with the conclusion and implementation of the Uruguay Round under the General Agreement on Tariffs and Trade/World Trade Organization. The pullback from globalisation since the late 2000s was an after-effect of the Great Recession from the 2008–2009 global financial crisis as well as what seems to be the maturation of the global value chain, which meant lower global trade growth relative to global GDP growth (Pangestu and Armstrong, 2016). This indicates that ASEAN’s performance has been shaped by global trends also, which is what can be expected in a relatively open economy. Nonetheless, Figure 2.2 shows that ASEAN has been much more globalised than Mercosur and even NAFTA, and almost as globalised as the EU.

The significant differences in the extent of globalisation among the AMSs are worth noting. As expected, Singapore has been the most globalised among the AMSs, followed by Malaysia. Thailand and Brunei come next at almost the same level of globalisation, followed by nearly identical scores for Indonesia and the Philippines. Cambodia and Viet Nam follow next with almost the same scores while Myanmar and the Lao PDR bring up the rear. The degree of globalisation accelerated during the 1990s for the five ASEAN founding members, while that of Cambodia and Viet Nam occurred during the past 1–2 decades (see Table 2.3).

---

2 The KOF Index of Globalization is a composite index of economic globalisation, political globalisation, and social globalisation first introduced by Dreher (2006). It conceptualises globalisation as a process of producing/improving mutual interdependence among countries via the integration of their national economies, cultures, technologies, and governance. Higher values of the index denote greater globalisation and vice versa.
Figure 2.2 and Table 2.3 suggest that ASEAN is a product of both globalisation and regional integration, a reflection of the open regionalism that ASEAN followed in its regional integration efforts under the ASEAN Free Trade Agreement (AFTA) and towards the ASEAN Economic Community (AEC). Indeed, Peter Drysdale in his essay in Volume 5 of the ASEAN@50 publication (Drysdale, 2017) emphasises that ASEAN is an experiment in open regionalism that has succeeded. At the same time, the highly varied scoring in globalisation in Table 2.3 suggests that there remain significant challenges to – as well as opportunities from – deeper economic integration of Member States within ASEAN, within East Asia, and with the rest of the world. Such challenges and opportunities from deeper economic linkages regionally and globally, especially with respect to foreign trade and investment, are discussed further in the next sections.

### Table 2.3. Economic Globalisation Scores for ASEAN Member States

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<tbody>
<tr>
<td>(Highest score)</td>
<td>72.81 (Belgium)</td>
<td>80.21 (Canada)</td>
<td>84.19 (Belgium)</td>
<td>92.72 (Belgium)</td>
<td>91.71 (Belgium)</td>
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<tr>
<td>Brunei Darussalam</td>
<td>n.a.</td>
<td>n.a.</td>
<td>51.20 (33)</td>
<td>60.17 (54)</td>
<td>67.38 (51)</td>
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<td>Cambodia</td>
<td>23.89 (114)</td>
<td>22.67 (146)</td>
<td>22.55 (155)</td>
<td>38.16 (137)</td>
<td>50.32 (114)</td>
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<tr>
<td>Indonesia</td>
<td>22.81 (121)</td>
<td>29.09 (114)</td>
<td>34.46 (105)</td>
<td>53.08 (76)</td>
<td>57.75 (84)</td>
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<tr>
<td>Lao PDR</td>
<td>16.65 (134)</td>
<td>17.34 (159)</td>
<td>17.84 (171)</td>
<td>24.11 (188)</td>
<td>30.38 (188)</td>
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<td>46.50 (41)</td>
<td>56.24 (24)</td>
<td>72.65 (27)</td>
<td>79.14 (25)</td>
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<td>Myanmar</td>
<td>19.89 (127)</td>
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<td>21.18 (160)</td>
<td>27.25 (177)</td>
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<td>Philippines</td>
<td>27.61 (94)</td>
<td>33.62 (96)</td>
<td>39.69 (71)</td>
<td>55.26 (68)</td>
<td>57.86 (83)</td>
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<td>57.45 (12)</td>
<td>72.87 (6)</td>
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<td>86.93 (6)</td>
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<td>25.97 (103)</td>
<td>29.98 (111)</td>
<td>36.56 (94)</td>
<td>57.89 (60)</td>
<td>70.45 (42)</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>18.78 (130)</td>
<td>19.87 (153)</td>
<td>24.75 (149)</td>
<td>37.10 (143)</td>
<td>49.91 (116)</td>
</tr>
<tr>
<td>(Lowest score)</td>
<td>14.19 (Lao PDR)</td>
<td>14.00 (Lao PDR)</td>
<td>13.97 (Lao PDR)</td>
<td>19.44 (Lao PDR)</td>
<td>23.44 (Timor-Leste)</td>
</tr>
<tr>
<td>Number of countries</td>
<td>137</td>
<td>160</td>
<td>168</td>
<td>186</td>
<td>187</td>
</tr>
</tbody>
</table>

Deepening Intra-ASEAN and Intra-East Asian Trade

Intra-ASEAN trade deepened during the 1990s and 2000s. Intra-ASEAN trade now comprises a quarter of total trade of ASEAN countries compared to about a fifth in the early 1990s and about 18.6% in the 1980s (see Table 2.4). The share of intra-ASEAN merchandise trade is much higher than trade within Mercosur or SAARC among the developing economy regional integration associations although still significantly lower than NAFTA and the EU. It must be emphasised, however, that the comparatively lower intra-regional trade share in ASEAN than in NAFTA and the EU does not indicate the failure of ASEAN’s regional integration efforts.

Instead, it means that the robust growth of intra-ASEAN merchandise trade has been accompanied by equally robust growth with trade with non-ASEAN trade partners, most importantly with China, Japan, the Republic of Korea (henceforth, Korea), and increasingly India. This reflects the pursuit of ‘open regionalism’ in ASEAN, which essentially means trade discriminatory policies in favour of intra-ASEAN have been minimised, thereby effectively allowing the full play of comparative advantage in ASEAN. It also reflects the growth of regional production networks since the late 1980s in East Asia, with China as the hub. Indeed, a large share of intra-ASEAN trade is in parts and components that are exported also as intermediate products to the rest of East Asia and the world. Hence, the robustness of trade within ASEAN involves also robustness of trade with non-ASEAN countries, especially China.

**Table 2.4. Intra-Regional Trade Shares (Merchandise Trade), 1980–2014 (%)**

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN</td>
<td>18.6</td>
<td>22.5</td>
<td>24.4</td>
<td>25.3</td>
</tr>
<tr>
<td>RCEP</td>
<td>30.0</td>
<td>34.9</td>
<td>38.9</td>
<td>41.2</td>
</tr>
<tr>
<td>EU</td>
<td>61.6</td>
<td>66.5</td>
<td>67.1</td>
<td>62.2</td>
</tr>
<tr>
<td>Mercosur</td>
<td>6.9</td>
<td>17.1</td>
<td>13.4</td>
<td>14.1</td>
</tr>
<tr>
<td>NAFTA</td>
<td>39.5</td>
<td>47.9</td>
<td>53.3</td>
<td>49.2</td>
</tr>
<tr>
<td>SAARC</td>
<td>3.9</td>
<td>4.5</td>
<td>5.8</td>
<td>6.1</td>
</tr>
</tbody>
</table>

ASEAN = Association of Southeast Asian Nations, EU = European Union, Mercosur = Southern Common Market, NAFTA = North American Free Trade Agreement, RCEP = Regional Comprehensive Economic Partnership, SAARC = South Asian Association for Regional Cooperation.

Source: Authors’ calculations based on data from the United Nations COMTRADE database.

Chapter 2: ASEAN Foreign Trade, Investment, and Integration in Comparative Perspective
The pursuit of open regionalism in ASEAN and the growth of regional production networks in East Asia has led to interesting shifts in international trade consistent with the changes in comparative advantage in the increasingly integrating region. Specifically, the 1990s and 2000s saw shifts in comparative advantage in East Asia arising from fast-rising wages coupled by currency appreciations in Japan, Korea, and Taiwan that led to a flood of direct investment from the three economies, Hong Kong, and other parts of the world into export-oriented labour-intensive manufactures to the ASEAN region and China. The surge of such FDI into ASEAN integrated the region into the growing regional production networks in East Asia. At the same time, the surge of investments and concomitant rises in wages led to the changes in the revealed comparative advantage of several AMSs during the past 3 decades. Thus, countries that became export competitive in skilled, labour-intensive manufactures such as electronics and electrical equipment – Malaysia, the Philippines, and Thailand – became less competitive in low-skilled, labour-intensive industries, such as garments. This thereby allowed the low-wage AMSs like Cambodia and Viet Nam to become significant exporters of such products as garments. It is precisely these dynamic shifts in comparative advantage – facilitated by trade and investment – among countries in the region with substantially varying levels of development and wages that characterise the industrialisation and integration process in ASEAN and East Asia in the past 3 decades.

The dictates of comparative advantage, the opportunities from global and regional trade liberalisation, and the dynamics of regional production networks under open regionalism mean that the rise in the aggregate share of intra-ASEAN trade hides interesting country-level developments in the direction of trade (see Table 2.5). Cambodia, the Lao PDR, and Malaysia markedly reduced their reliance on the ASEAN region as an export market while at the same time expanding substantially their import sourcing on ASEAN. On the other hand, five ASEAN countries (Indonesia, Myanmar, the Philippines, Singapore, and Thailand) increased their reliance on the ASEAN region both as an export market and as an import source (most notably, Indonesia and the Philippines). Brunei and Viet Nam marginally reduced their export exposure to ASEAN in tandem with a marginal increase in import sourcing from the region (Brunei) or a marginal decline in imports from ASEAN (Viet Nam).

Thus, for example, Cambodia dramatically shifted its exports away from the ASEAN region towards the EU and the United States (US) while at the same time increasing further its reliance on ASEAN and ASEAN+3 (and away from the EU) as a source of imports. During the period, Cambodia had the sharpest rise in the trade-to-GDP ratio among the AMSs. It effectively leveraged its low labour cost with imported inputs from the ASEAN+3 region to generate exports (mainly of garments) primarily to the West. This smart utilisation of the principle of comparative advantage must have been a big
factor for Cambodia’s growth performance, which was the best in the ASEAN region in the 2000s.

Similarly, the Philippines, hitherto the least engaged in trade among the AMSs in the early 1990s, turned dramatically to the ASEAN and East Asia regions for its export and import expansion in the 1990s and the 2000s. Behind the significant shift in the direction of Philippine trade was the dramatic shift in the composition of the country’s exports towards electronics exports as part of the regional production networks in Southeast and East Asia. The Philippines also indicates the dynamic changes in the direction of imports and exports even within the ASEAN and East Asia regions. Thus, for example, the share of Singapore to Philippine exports dropped by 8.2 percentage points during 2010–2015, whereas the shares of China and Japan to Philippine exports increased by 7 percentage points during the same period.

Table 2.5. Intra-regional ASEAN Trade Shares of Individual ASEAN Countries’ Foreign Trade (%)

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Brunei Darussalam</td>
<td>20.93</td>
<td>41.9</td>
<td>22.21</td>
<td>50.3</td>
<td>23.16</td>
<td>57.66</td>
<td>25.15</td>
<td>64.52</td>
<td>10.53</td>
<td>55.43</td>
<td>18.41</td>
<td>45.52</td>
</tr>
<tr>
<td>Cambodia</td>
<td>74.56</td>
<td>43.27</td>
<td>63.15</td>
<td>75.99</td>
<td>5.578</td>
<td>39.26</td>
<td>4.73</td>
<td>31.06</td>
<td>12.58</td>
<td>34.35</td>
<td>12.65</td>
<td>54.04</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>68.41</td>
<td>60.9</td>
<td>54.98</td>
<td>56.08</td>
<td>42.69</td>
<td>77.7</td>
<td>42.43</td>
<td>76.87</td>
<td>43.78</td>
<td>72.15</td>
<td>48.38</td>
<td>72.04</td>
</tr>
<tr>
<td>Malaysia</td>
<td>29.45</td>
<td>19.07</td>
<td>27.56</td>
<td>17.4</td>
<td>26.56</td>
<td>24.01</td>
<td>26.07</td>
<td>24.87</td>
<td>25.38</td>
<td>27.1</td>
<td>25.28</td>
<td>27.9</td>
</tr>
<tr>
<td>Myanmar</td>
<td>28.21</td>
<td>26.03</td>
<td>30.27</td>
<td>43.63</td>
<td>21.3</td>
<td>45.3</td>
<td>51.14</td>
<td>50.86</td>
<td>46.61</td>
<td>43.56</td>
<td>30.7</td>
<td>37.33</td>
</tr>
<tr>
<td>Philippines</td>
<td>7.265</td>
<td>10.57</td>
<td>13.59</td>
<td>10.58</td>
<td>15.65</td>
<td>15.55</td>
<td>17.34</td>
<td>18.72</td>
<td>22.47</td>
<td>28.05</td>
<td>13.73</td>
<td>23.14</td>
</tr>
<tr>
<td>Singapore</td>
<td>22.35</td>
<td>17.12</td>
<td>30.34</td>
<td>22.27</td>
<td>27.37</td>
<td>24.73</td>
<td>31.38</td>
<td>26.04</td>
<td>30.26</td>
<td>24</td>
<td>29.83</td>
<td>21.5</td>
</tr>
<tr>
<td>Thailand</td>
<td>11.93</td>
<td>13.08</td>
<td>20.31</td>
<td>12</td>
<td>19.34</td>
<td>16.66</td>
<td>21.98</td>
<td>18.3</td>
<td>22.92</td>
<td>16.6</td>
<td>25.72</td>
<td>18.98</td>
</tr>
</tbody>
</table>

Source: Asia Regional Integration Center, Integration Indicators Dataset, https://aric.adb.org/integrationindicators

In addition to the changes in the country-level direction of trade were significant changes in the commodity composition and direction of trade in ASEAN despite the modest increase in the overall intra-ASEAN trade share to total ASEAN trade. Table 2.6 presents the commodity composition of intra-ASEAN trade in 2003 and 2014. The table shows that the shares of intra-ASEAN trade in raw materials and intermediate goods largely remained the same and marginally increased, respectively, between 2003 and 2014. However, the relative importance of capital goods (including parts and components)
and consumer goods drastically changed. Specifically, the share of consumer goods sharply rose and the share of capital goods (including parts and components) drastically declined.

The major restructuring in the commodity composition of intra-ASEAN trade between the early 2000s and the early 2010s appears to be the by-product of ASEAN economic integration itself and the ongoing geographic realignment of the regional product networks, at least with respect to electronics and electronic equipment parts and components, which is the quintessential example of regional production networks in East Asia. With respect to consumer goods, it is interesting to note the increase in the intra-regional trade shares of commodity groups – such as ‘soaps, lubricants, etc.’; ‘essential oils, perfumes, cosmetics, etc.’; and ‘cereal, flour, etc. preparations and products’. These are likely partly a result of the regional production rationalisation strategies of multinational corporations (e.g. Nestle, Procter and Gamble, and Unilever) wherein a specific product is produced in a particular plant in a country for distribution to the rest of, or selected countries in, the region. Such regional production rationalisation programmes have likely been facilitated by the decline and eventual elimination of intra-ASEAN tariffs and the rise in per capita incomes and the middle class in the region with the attendant increased demand in product variety.

**Table 2.6. ASEAN Trade Composition, 2003 and 2014 (%)**

<table>
<thead>
<tr>
<th>Trade Composition, 2003</th>
<th>Trade Composition, 2014</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Intra-ASEAN</td>
</tr>
<tr>
<td>Capital goods</td>
<td>53.5</td>
</tr>
<tr>
<td>Consumer goods</td>
<td>21.3</td>
</tr>
<tr>
<td>Intermediate goods</td>
<td>16.3</td>
</tr>
<tr>
<td>Raw materials</td>
<td>6.2</td>
</tr>
</tbody>
</table>

ASEAN = Association of Southeast Asian Nations, RoW = rest of the world.
Source: Authors’ calculations based on data from the United Nations COMTRADE database.

The encouragement of the full play of comparative advantage and product variety by the elimination of intra-ASEAN tariffs is also reflected in the rise of both intermediate and consumer commodity goods. Some commodity groups that also increased intra-regional trade shares within ASEAN are linked to countries in the region with distinct comparative advantage in natural resources–based products. These products tend to be weighed
down by a relatively high share of transport costs to the unit value of the products. As such, the nearer the market the better is the ex-factory price that producers can receive or the more price competitive they can be in the export market. There are other commodity groups where the intra-regional trade shares have increased but which are not known to be characterised in terms of regional production networks or in relation to regional production rationalisation strategies of multinationals. Examples are ‘plastics and articles’, ‘organic chemicals’, ‘articles of leather, etc. travel goods’, and ‘beverages, spirits, and vinegar’. Intra-ASEAN trade in such products likely benefited from the elimination of tariffs and possibly also of trade facilitation costs arising from improved efficiencies in customs in the region.

It is also worth noting that there has been a marked increase in intra-regional trade shares in commodity groups such as ‘vehicles, other than railway and tramway’ (primarily cars and motorcycles), most likely affected in part by the emergence of Thailand (and to a lesser extent, Indonesia) as ASEAN’s major export hub for automotive products for the ASEAN region and the rest of the world. It is also a result of the regional complementation strategies of multinational companies, where the production of parts is scattered in selected member countries in conjunction with the assembly of specific types of cars in particular member countries for distribution to the whole region or a specified subregion. Such firm-level regional complementation strategies reflect the by-product of ASEAN’s earlier brand-to-brand industrial complementation programme. An example is that of Toyota, for which Indonesia is its hub in producing gasoline engines, the Philippines for transmissions, and Thailand for diesel engines, which are used by the various country assembly plants in ASEAN (ASEAN Secretariat, 2012).

**ASEAN in regional production networks and value chains**

Nonetheless, electronics and electrical equipment parts and components account for the largest share of intra-ASEAN commodity trade, and there is an apparent geographic realignment as part of dynamic changes in the regional production networks in East Asia. For example, Table 2.7 shows the shares of China and ASEAN in the exports and imports of parts and components for electrical and electronic goods in 1995, 2003, and 2015 for the key AMS players in the sector. The table clearly shows the sharp increase in exports to and imports from China during the period for virtually all the ASEAN countries. While most of the increase in trade with China is a redirection away from Japan, the EU, and/or Taiwan, the significant increase in the share of exports to and imports from China is combined with a substantial decline in the share of exports to and imports from ASEAN in Malaysia, Singapore (not in electronic goods), Thailand, Indonesia, and Viet Nam.
In short, ASEAN countries increased their reliance on ASEAN for their imports of electronic goods and substantially shifted their export destination for parts and components of electrical and electronic goods from ASEAN towards China. This shows the emergence of China as the hub of East Asia’s regional production networks in electronic and electrical equipment parts and components. It also shows that ASEAN is very much part of the regional production network.

As indicated above, a significant part of ASEAN trade is the cross-border exchange of parts and components. The importance of regional production sharing is evident when observing the successive waves of industrialisation in East Asia in the post-war era. Production-sharing networks in East Asia were found in various industries, particularly in sectors of machinery and transportation equipment, which are characterised by multilayered vertical production or distribution. Even before the establishment of the AEC, Ng and Yeats (2003) found that regional production sharing in ASEAN and East Asia was ‘a positive factor facilitating regional cooperation and increased interdependence’; and the intensifying trade in parts and components in trade of manufacturing goods could be ‘positive factors in regional trade arrangements’.

<table>
<thead>
<tr>
<th>Table 2.7. Shares of China and ASEAN in AMSs’ Exports and Imports of Parts and Components for Electrical and Electronic Goods (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Reporter</strong></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Indonesia</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Malaysia</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Philippines</td>
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<tr>
<td></td>
</tr>
<tr>
<td>Singapore</td>
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<tr>
<td></td>
</tr>
<tr>
<td>Thailand</td>
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<tr>
<td></td>
</tr>
<tr>
<td>Viet Nam</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

AMS = ASEAN Member State, ASEAN = Association of Southeast Asian Nations.
Source: Authors’ calculation based on data from the United Nations COMTRADE database.
Table 2.8 shows that in the 1980s, about a fifth of the manufacturing goods traded within ASEAN were parts and components. This is very close to that in NAFTA. While the ratio of trade in parts and components to regional trade in NAFTA declined over time, that of ASEAN first increased substantially and reached a peak in the mid-2000s but declined afterwards to the low 20% range, reflecting the redirection of electrical and electronic parts and components trade towards China. Nonetheless, parts and components still comprise a much larger share of manufacturing trade in ASEAN than in other regions, especially Mercosur and SAARC, which have not been part of significant regional production networks in manufactures. Table 2.8 also shows that parts and components account for a much higher share of extra-regional trade in ASEAN than in the other regions, again reflecting ASEAN being strongly embedded in the regional production networks in the wider East Asia region. The participation of individual ASEAN countries in the regional production networks differs tremendously, however. Singapore accounts for a third, while Malaysia and Thailand together account for almost two-fifths of all regional trade in parts and components. The fastest growth in recent years has been for Viet Nam, which more than doubled its share, overtaking the Philippines as the fifth-most important trader in parts and components in ASEAN (see Table 2.9).

Compared with other regions, the regional production networks in East Asia are arguably the most complex and articulated (Ando, 2009). This is in part due to (i) the dominance of machinery that typically requires many parts and components; (ii) the significant
differences in the levels of development and factor prices among the economies in the region, which encourage the profitable fragmentation of production; and (iii) the reduction in trade barriers and transport and trade facilitation costs that allows for the formation of varying layers of networks across production areas. The varying layers of networks stretch from industrial agglomeration clusters within a short distance (for products requiring frequent delivery for just-in-time operations) to farther but networked production areas with relatively more modular inter-firm interfaces (Kimura, 2009). Most of intra-East Asian trade is in parts and components, which, as Obashi (2009a, 2009b) has shown, tend to be more longer-lived, resilient, and less sensitive to trading costs and exchange rate fluctuations than finished goods, thereby allowing for stronger trade relationships, greater learning by doing and technology transfer, and more robust industrial development.

Data from OECD Global Value Chains Indicators (see Table 2.10) further indicates the position of AMSs in the global trading and value chain system. Table 2.10 shows the value of countries’ forward and backward participation indices. The forward indicator – the share of a country’s exporting goods and services that are used by its trade partners as imported inputs to their production for exports – proxies the contribution of a country’s domestic value-added to other countries’ exports. The backward indicator measures the foreign value added embodied in a country’s gross exports. It is expressed as the ratio between the value of imported inputs and a country’s total exports. For both, higher values indicate deeper involvement in global value chains.

Table 2.9. ASEAN Member States’ Shares in Regional Trade in Parts and Components (%)

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Brunei Darussalam</td>
<td>0.8</td>
<td>1.0</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>Indonesia</td>
<td>13.4</td>
<td>14.9</td>
<td>4.0</td>
<td>11.5</td>
</tr>
<tr>
<td>Cambodia</td>
<td>0.5</td>
<td>0.5</td>
<td>0.0</td>
<td>0.1</td>
</tr>
<tr>
<td>Malaysia</td>
<td>22.5</td>
<td>18.4</td>
<td>25.9</td>
<td>22.6</td>
</tr>
<tr>
<td>Philippines</td>
<td>7.5</td>
<td>4.4</td>
<td>19.8</td>
<td>8.1</td>
</tr>
<tr>
<td>Singapore</td>
<td>33.8</td>
<td>32.7</td>
<td>32.9</td>
<td>32.0</td>
</tr>
<tr>
<td>Thailand</td>
<td>17.0</td>
<td>18.2</td>
<td>15.4</td>
<td>19.3</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>4.5</td>
<td>9.3</td>
<td>1.8</td>
<td>6.1</td>
</tr>
</tbody>
</table>

Note: The definition of parts and components is based on Ando, Arndt, and Kimura (2006).
Source: Authors’ calculations based on data from United Nations (2016) COMTRADE database.
The data are available for eight AMSs. The value of the backward participation index is generally higher than that of the forward participation index, except for Brunei and Indonesia. For Malaysia, the Philippines, Singapore, and Thailand, the higher backward participation rate reflects the nature of their stage in the production networks, which is largely to produce parts and components from imported parts, which are then exported as parts and components to the importing countries; hence, the rising forward participation indices of the four countries. Note the significant decline in the backward participation index of Malaysia and the Philippines, suggesting greater localisation and increased value added of the two countries’ exports and/or greater concentration of exports with less imported components.

The participation indices of Cambodia and Viet Nam suggest the dependence of the two countries on imported parts and components (including fabrics for garments) for their major exports of primarily consumer goods (garments for Cambodia and electronic products, especially mobile phones, for Viet Nam). The low backward participation index and higher forward participation index for Brunei and Indonesia show the preponderance of resource- and agriculture-based exports of the two countries, which are then used as inputs for the exports of the importing countries, e.g. energy for Brunei and palm oil for Indonesia.

<table>
<thead>
<tr>
<th>Country</th>
<th>Participation Index, Forward</th>
<th>Participation Index, Backward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brunei Darussalam</td>
<td>19.3</td>
<td>29.9</td>
</tr>
<tr>
<td>Cambodia</td>
<td>17.7</td>
<td>8.7</td>
</tr>
<tr>
<td>Indonesia</td>
<td>18.8</td>
<td>23.7</td>
</tr>
<tr>
<td>Malaysia</td>
<td>15.2</td>
<td>19.6</td>
</tr>
<tr>
<td>Philippines</td>
<td>16.6</td>
<td>17.3</td>
</tr>
<tr>
<td>Singapore</td>
<td>13.8</td>
<td>18.6</td>
</tr>
<tr>
<td>Thailand</td>
<td>12.0</td>
<td>14.3</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>12.6</td>
<td>18.1</td>
</tr>
</tbody>
</table>

Insights

The changing international trade landscape in the region brings the following key insights:

- **Openness to global trade**, and not only regional trade, allows for the full play of comparative advantage. This is best exemplified by the experience of Cambodia, where Generalized System of Preferences privileges in the EU and the US enabled significant market access, leveraging their low labour cost with imported inputs from the region as well as from the major export markets themselves, which has allowed them remarkable growth in exports since the early 2000s.

- Similarly, the near-zero tariff regime in electronics globally allowed for the full flowering of global and regional production networks in the sector. Varying levels of factor prices and factor capabilities concomitant to the varying levels of development of East Asian countries amidst improved and cheaper transportation and communication linkages in East Asia enabled the efficient fragmentation of production processes across various countries in the region. The rise of regional production networks has had major impacts on the volume and direction of intra-regional trade in East Asia. It is not surprising that electronics and electrical equipment and parts have been the key driver of the surge in total exports and intra-regional trade.

- Nonetheless, regional trade liberalisation and integration initiatives have also shaped the changing trade landscape in ASEAN. The substantial reduction in tariffs in the region has encouraged the rise of regional production rationalisation initiatives among multinationals in the region, the growth (in production and trade) of transport cost-sensitive commodities in the region, and the expansion of markets into the region of differentiated products. In effect, the more liberalised trading environment contributed to the deepening of economic interchange in the region in a wide range of industries and products beyond regional production networks per se.

Expanding Investment Linkages

Investment – and especially foreign investment – has been a central driver of economic transformation and integration in ASEAN and East Asia. The spread of regional production networks has been driven by multinational corporations and their SME (small and medium-sized enterprises) suppliers investing in various countries in the region. They invest to minimise costs, maximise access to resources and talent, and be near markets. Nonetheless, they remain seamlessly linked together with the internal
(within firm or group) coordination of the various processes and stages of production. The geographically dispersed but internally coordinated production networks tend to bundle FDI with technology transfer, management, skills training, quality control, and access to markets, etc. At the same time, the host countries are pressured to invest in better infrastructure, logistics, telecommunications, trade-related finance, and other related services to attract more investment from foreign (and domestic) firms involved in more production networks where timeliness in the sourcing, production, and exports within the production networks is a particularly important consideration. Of course, many investments that are not directly linked to production networks are undertaken, for example, to service the domestic market or to tap particular assets or skills. These benefit from, as well as respond positively to, improved infrastructure, services, and trade facilitation, etc. that deep engagement in production networks demands. There is thus a significant virtuous cycle of the trade–investment–services–facilitation nexus. In many ways, the virtuous cycle is one key locomotor of industrial development and transformation of the host countries, including in ASEAN during the past few decades.

Part of the dynamism of ASEAN is due to its success in attracting foreign investment. The level of annual FDI inflows into ASEAN expanded by more than six times between 2000 and 2014, when the region attracted its highest level of US$136.2 billion, higher than what was received that year by China, hitherto the leader in FDI in the developing world. In 2015, ASEAN dropped immediately after outranking China as FDI inflows to ASEAN fell to US$120.8 billion, whereas China’s FDI inflows rose to US$126.3 billion. In the early to mid-2000s, FDI inflows into China were usually more than twice those into ASEAN. That ASEAN now competes with China for the top spot as an FDI destination in the developing world is remarkable indeed because one of the impetus for the acceleration of the target date for the AEC from 2020 to 2015 was for ASEAN to not lag far behind China as an FDI destination. It must be emphasised, though, that ASEAN was in fact the leading FDI destination in the developing world in 1990 (in the middle of ASEAN’s economic boom period) when China was yet to emerge as the major FDI and economic force in the late 1990s and before the sharp drop in FDI inflows to ASEAN in the aftermath of the East Asian economic crisis of 1997–1998. It is also worth highlighting this element of FDI attraction and competition as part of the animus for the deepening of economic linkages and integration in ASEAN.

Figure 3.2.3 presents the composition of FDI inflows to ASEAN by source in 2004 and 2015; note that it was in 2004 that total FDI inflows into ASEAN overtook their pre-crisis level of 1997. The EU-28 has been the largest foreign investor in ASEAN for most of the 2000s and early 2010s, followed by Japan. The US has also been a consistent significant foreign investor in the region; indeed, US direct investment in ASEAN is greater than the combined total of US investment in China, Japan, and Korea (ASEAN
China has grown in importance as a source of FDI into ASEAN in recent years. It is worth noting that the foreign investors tend to focus on certain preferred sectors. Thus, for example, Japanese FDI in ASEAN tends to concentrate in manufacturing, which partly explains the strong Japanese presence in regional production networks. On the other hand, US and EU FDI in ASEAN in recent years has concentrated in services, and much of it is poured into Singapore given the latter’s regional (and even global) strong presence in services, including being the regional hub for Southeast Asia.

However, the most interesting development has been the marked rise in the importance of intra-ASEAN FDI during the 2000s. The share of intra-ASEAN FDI in ASEAN’s total FDI inflows rose from 8.9% in 2004 to 18.4% in 2015, becoming the top source of FDI in that year followed by the usual leader, the EU-28. This is an important development because it reflects the growing regionalisation of ASEAN-based firms (indeed, many have internationalised beyond ASEAN) as well as the implied growing business relationships among ASEAN firms. The ASEAN Investment Reports indicate the growing numbers of ASEAN firms expanding to the rest of ASEAN and the large magnitude of FDI outflows from ASEAN, which reflect the internationalisation efforts of ASEAN firms as they invest or purchase assets in the rest of the world.

Figure 2.4 shows the distribution of FDI by host country for 2004 and 2015. The figure shows the dominance of Singapore as the FDI recipient, but the share has declined from more than three-fifths in 2004 to one half in 2015. The distribution of FDI inflows has become far less concentrated: whereas the comparative richer and large AMSs, Malaysia, Singapore, and Thailand, cornered close to 90% of all FDI inflows in 2004, the trio accounted for only two-thirds in 2015. Instead, the next two largest FDI recipients after Singapore in 2015 were Indonesia and Viet Nam. It is also worth noting that the other AMSs sharply increased their share from just 3.3% in 2004 to 9.5% in 2015. The apparent growing dispersion of FDI inflows into ASEAN is salutary as it likely reflects the following: (i) the positive investment response to almost simultaneous domestic reforms in most AMSs during the period, consistent with the growing integration efforts towards the AEC in 2015; (ii) the growing competitiveness of countries with low-labour cost as

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3 For example, ASEAN Investment Reports 2012, 2015, 2016.

4 A dominant source of ASEAN FDI outflows is Singapore. There is a likelihood that a portion of FDI inflows into Singapore end up as FDI outflows to be used for mergers and acquisitions deals, etc. reflecting the role of Singapore as a regional hub of multinationals and as a regional financial centre.

5 The share of Indonesia was low in 2004 as it was still reeling from the aftermath of the 1998 financial and economic crisis which saw net investment outflows from Indonesia in the first years of the 2000s.
export bases for low-skilled, labour-intensive manufactures in the face of rising labour cost in China; (iii) the widening geographic reach of regional production networks; and (iv) the sheer growing investment attractiveness of serving the demands of the growing middle class, especially in the most populous member states of Indonesia, the Philippines, and Viet Nam.

*Figure 2.3. Foreign Direct Investment Flows into ASEAN, by Source Country (%)*

ASEAN = Association of Southeast Asian Nations.
Source: Data 2004: ASEAN Secretariat (2015a); Data 2015: ASEAN Secretariat (2016b).

*Figure 2.4. Foreign Direct Investment Flows into ASEAN, by Host Country (%)*

Source: Data 2004: ASEAN Secretariat (2015a); Data 2015: ASEAN Secretariat (2016b).

There is a great likelihood of even greater shares of FDI inflows into the low-middle-income Member States (i.e. outside of Brunei, Malaysia, Singapore, and Thailand) in the future as labour-intensive manufacturing activities shift from the upper-middle and high-income countries in Asia to the lower middle-income countries of ASEAN. The infrastructure investment needs and opportunities are great and gathering momentum in these countries. And the countries offer robustly growing large consumer markets as they are the fastest-growing AMSs. Nonetheless, the more advanced Member States are themselves improving their competitiveness and investment attractiveness regionally.
and globally in selected industries, such as in automotive manufacturing for Thailand and the life sciences for Singapore.

Behind the scene is ASEAN’s progress in improving the regional investment environment. To encourage foreign investment to support development, AMSs have taken actions both nationally and internationally. Some typical domestic actions include national investment policy reforms, incentive tax treatment, infrastructure development, and investment facilitation, as well as transparency of investment procedures and institutional support for investors (ASEAN Secretariat, 2015b). In addition, there have been international efforts through the negotiation, signing, and implementation of investment treaties and FTAs, such as the ASEAN Comprehensive Investment Agreement, the Regional Comprehensive Economic Partnership, and so on.

The World Bank Doing Business index shows that ASEAN has significantly improved the regional business environment. In 10 years, ASEAN has narrowed its gap with NAFTA and the EU regarding the ease of doing business. Singapore, Malaysia, and Thailand rank as the top three AMSs for ease of doing business. There has also been significant progress in the CLMV countries. Regional integration, the improvement of the business environment, and the promotion of foreign investment have reinforced one another. Market integration and region-wide regulatory harmonisation can facilitate business activities and encourage foreign investment. The inflow of foreign capital will further improve the efficiency of the market by introducing advanced know-how and best practices of doing business to the region.

Thus, the whole ASEAN region remains a very attractive FDI destination for foreign businesses, being the sixth-largest economy (if ASEAN is viewed as one economy) in the world at present and one of the fastest-growing regions in the world. ASEAN and the United Nations Conference on Trade and Development (UNCTAD) observe that since the implementation of the AEC, investors’ perceptions of the region have been on the rise. Testaments from the private sector reflect strong optimism for the future prospects of the region, drawing from the messages and essays in Investing in ASEAN 2017 (Allurentis Limited and ASEAN, 2017). While foreign companies have continued to strengthen their footprint in the region in manufacturing, finance, infrastructure, and other services, local players are also active in expanding existing business or investing in new projects in the region. Thus, higher FDI flows in ASEAN are foreseeable in the

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6 The World Bank Doing Business index measures a country’s overall business regulations from 10 aspects – starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts, and resolving insolvency. A higher value of the indicator means a more investment-friendly business environment. The simple average of the AMSs’ scores is used to proxy the whole region’s general ease of doing business.
future. Perhaps the best expression of the business optimism for ASEAN is the tag made by Deutsche Bank in its advertisement in the publication *Investing in ASEAN 2017*: ‘Half a century on: ASEAN is only getting better with age.’ (Allurentis Limited and ASEAN, 2017: 26).
Chapter 3
Building the ASEAN Economic Community: Progression and Progress

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Introduction

The ASEAN Economic Community (AEC) was formally established on 31 December 2015. It was the culmination of nearly a quarter century of progression and progress in regional economic integration efforts in ASEAN. At the same time, it is the formal affirmation of the beginning of the drive towards deeper integration and community building in ASEAN. There is thus both continuity and progression as well as an implicit commitment to ensuring progress towards deeper regional economic integration, best encapsulated in the AEC blueprint.

A companion volume to this publication, Volume 1 entitled *The ASEAN Journey: Reflections of ASEAN Leaders and Officials*, describes the evolution of ASEAN and the road to the ASEAN leaders’ decision to establish the AEC and the approval of the AEC Blueprint 2009–2015. From the First ASEAN Summit in Bali in 1976 up to the momentous Fourth Summit in Singapore in 1992, ASEAN focused largely on regional economic cooperation primarily through the preferential trading agreement and industrial cooperation initiatives (e.g. ASEAN Industrial Projects, ASEAN Industrial Ventures, and ASEAN Industrial Joint Ventures). On 28 January 1992, on the occasion of the Fourth ASEAN Summit, the ASEAN leaders decided to move ASEAN political and economic cooperation to a higher level in view of the profound political and economic changes in the world since the end of the Cold War. In the economic arena, the leaders signed the Framework Agreement on Enhancing ASEAN Economic Cooperation. This was highlighted by the signing on the same day by the ASEAN ministers of trade of the Agreement on the Common Effective Preferential Tariff Scheme for the ASEAN Free Trade Area.
The framework agreement on enhanced economic cooperation and the CEPT for AFTA agreement on that fateful day of 28 January 1992 were the signal of the shift from pure economic cooperation towards economic integration, hitherto a taboo word in ASEAN. ASEAN started a slew of major regional initiatives in the 1990s that became the foundation of the AEC – i.e. work on non-tariff barriers; customs cooperation; standards and conformance with the establishment of the ASEAN Consultative Committee on Standards and Quality (ACCSQ); services, with the signing of the ASEAN Framework Agreement on Services (AFAS) and the start of rounds of negotiations on services liberalisation; investment, with the agreement to establish an ASEAN Investment Area; and other initiatives, such as for transport facilitation. The ASEAN initiatives in the aftermath of the 1992 ASEAN Summit were apparently far more than for a standard free trade area.

The ASEAN Vision 2020 – adopted during the Second ASEAN Informal Summit in Kuala Lumpur in December 1997, a few months after the outbreak of the East Asian financial crisis in Thailand and amidst depreciating ASEAN currencies – provided the first cohesive framework of the enhanced cooperation efforts since the early 1990s. The ASEAN Vision 2020 envisages ASEAN as a concert of outward-looking Southeast Asian nations living in peace, stability, and prosperity bonded together in partnership in dynamic development and in a community of a caring society. The vision for 2020 is for a region that is a zone of peace, freedom, and neutrality as well as a highly competitive economic region where there is free flow of goods, services, and investment; a freer flow of capital; equitable economic development; and reduced poverty and socio-economic disparities.

The core elements and key strategies of what would become the AEC Blueprint 2009–2015 were apparently drawn from the ASEAN Vision 2020. The Hanoi Plan of Action of 1998 provided implementation details for the ASEAN Vision 2020, thereby becoming an important building block to the eventual AEC Blueprint 2009–2015. At the turn of the 21st century, former Prime Minister Goh Chok Tong of Singapore suggested that ASEAN move towards an economic community. The High-Level Task Force on ASEAN Economic Integration was assigned to study it and make recommendations drawing from the ASEAN Vision 2020 and the Hanoi Plan of Action, among others. The decision to establish an ASEAN economic community snowballed into the Bali Concord II of 2003 setting out the establishment of the ASEAN Community by 2020 consisting of the ASEAN Economic Community (AEC), ASEAN Security Community (eventually the ASEAN Political–Security Community) and the ASEAN Socio-Cultural Community. The recommendations of the task force on economic integration became an appendix to the Bali Concord II, thereby becoming mandates to ministers and senior officials to formulate the specific commitments and plans of action to implement the
recommendations. These eventually fed into the blueprint to realise the AEC by 2020. Noting progress in the implementation of the AEC action plans and in the face of tighter competition for foreign investment from countries like China, the ASEAN leaders decided in 2007 to accelerate the realisation of the AEC from 2020 to 2015.

In conclusion, a review of the road to the AEC raises two remarkable points:

- **Progression and progress.** The story of the road to the AEC is one of progressive expansion and deepening of cooperation and integration initiatives. This is no doubt facilitated largely by the progress in implementing the continuous expansion and deepening of the tariff reductions under the CEPT scheme. The success of the CEPT scheme and the widening CEPT Plus initiatives lead almost naturally to the proposal for the next level of economic integration – an economic community such as the European Economic Community (one of the earliest partners of ASEAN).

- **Forward-looking leadership.** It is remarkable that the ASEAN leaders responded to significant global and regional challenges by pushing further the drive for regional economic integration. They decided in 1992 to move towards an ASEAN free trade area in response to the threat of a possible ‘Fortress Europe’ with the planned European Union and the impending start of the North American Free Trade Agreement, two major developments that signalled less-than-open major export markets for ASEAN Member States (AMSs). Similarly, the ASEAN leaders in 1997 pushed ahead with the ambitious ASEAN Vision 2020, mandated at the height of an economic boom a year earlier, despite the ASEAN region being in the midst of an economic and financial crisis. The decision to move towards an ASEAN economic community in the early 2000s and the decision in 2007 to accelerate the timeline from 2020 to 2015 were made amidst relatively poor foreign direct investment (FDI) inflows into ASEAN and the surging Chinese economy and rising Indian economy, ASEAN’s two large neighbours and competitors for FDI. All the above shows forward-looking leadership and commitment to the ideals of the 1967 Bangkok Declaration that gave rise to ASEAN.

### The ASEAN Economic Community Blueprint 2015

The AEC Blueprint 2009–2015 consists of a large number of measures aimed at realising an outward-oriented ASEAN Community that has the following interrelated and mutually reinforcing key characteristics: (i) a single market and production base, (ii) a highly competitive economic region, (iii) a region of equitable development, and (iv) a
region fully integrated into the global economy (see Figure 3.1). The AEC with these key characteristics is essentially the end goal of regional economic integration in ASEAN.

### Figure 3.1. The Pillars of the ASEAN Economic Community

- **Pillar 1** Single Market and Production Base
  - Free flow of goods
  - Free flow of services
  - Free flow of investment
  - Free flow of capital
  - Free flow of skilled labour
  - Priority integration sectors
  - Food, agriculture, and forestry

- **Pillar 2** Single Market and Production Base
  - Competition policy
  - Consumer protection
  - Intellectual property rights
  - Infrastructure development
  - Taxation
  - E-commerce

- **Pillar 3** Equitable Economic Development
  - Development of SMEs
  - Initiative for ASEAN integration

- **Pillar 4** Integration into the Global Economy
  - Coherent approach towards external economic relations
  - Enhanced participation in global supply networks

SMEs = small and medium-sized enterprises.

Source: ASEAN Secretariat (2015b).

### Single market and production base

Achieving a single market and production base is the central theme of the regional economic integration initiative towards a regime of free flow of goods, services, investment, skilled labour, and freer flow of capital. To a large extent, the aim is to have an ASEAN region as if it were a single economy.

**Free flow of goods.** Towards a free flow of goods within ASEAN, the AEC blueprint measures include (i) the elimination of tariffs and non-tariff barriers; (ii) putting in place rules of origin that are responsive to and facilitative of a dynamic trading environment with simplified certification processes; (iii) having simple, harmonised, transparent, and standardised trade and customs processes that are regionally integrated and with a well-performing ASEAN Single Window (ASW); and (iv) establishing a regime of harmonised standards, technical regulations, and conformity assessments aligned with international practices, if applicable, together with mutual recognition arrangements (MRAs) and enhanced technical infrastructure and competency.
The implementation of the AEC blueprint measures towards a free flow of goods has seen substantial progress, but much remains to be done especially involving institutions and processes. For the most part, the implementation of the measures can be characterised by gradual progression but significant cumulative progress, which is almost like the ASEAN DNA. Arguably, it is unrealistic to expect the institutional underpinnings of the free flow of goods to be well established in less than a decade of the AEC Blueprint 2009–2015 in light of the vast differences in the levels of development and the varied political-legal systems of the AMSs. Institutional development and regulatory change facilitative of the free flow of goods is a long-term process. The successor AEC Blueprint 2016–2025 continues the progressive implementation of the still incompletely implemented AEC 2015 measures towards the free flow of goods in ASEAN.

**Tariffs.** This is one of the most important achievements of the AEC 2015. As of mid-2016, 99.2% of all intra-ASEAN tariffs in Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, and Thailand have been eliminated. Similarly, 90.9% of intra-ASEAN tariffs in Cambodia, the Lao PDR, Myanmar, and Viet Nam (CLMV) have been eliminated. The 48th ASEAN Economic Ministers’ (AEM) Meeting Joint Media Statement reports that by 2018, 97.8% of intra-ASEAN tariff rates in CLMV will be zero, making 98.6% of intra-ASEAN tariffs in all of ASEAN zero (ASEAN, 2016: 3–4). The ASEAN Secretariat reports that the average CEPT rate for the ASEAN-6 countries declined from 11.44% in 1993 to 0.03% in 2015; that of the CLMV countries fell from 6.31% in 1999 to 0.55% in 2015. An ERIA report indicates that intra-ASEAN trade in several products responded positively to the reduction or elimination of intra-ASEAN tariffs (ERIA, 2015).

It should be noted, however, that the reduction of intra-ASEAN tariffs started in the early 1990s. Indeed, it was the success of the reduction (to a range of 0%–5%) of the intra-ASEAN tariffs (called CEPT rates under AFTA) in ASEAN-6 by the early 2000s that encouraged ASEAN leaders and officials to go beyond AFTA and move towards an ASEAN economic community. The tariff case exemplifies ASEAN’s apparent approach of gradual progression for substantive progress towards meeting the AEC’s goals.

**Non-tariff measures (NTMs)/non-tariff barriers (NTBs).** Whereas ASEAN has been successful in eliminating tariffs, it has continued to be largely concerned about NTMs and NTBs. Indeed, with tariffs nearly eliminated, the issue of NTMs and NTBs has loomed larger among the ASEAN business sector and ASEAN officials. The recent ERIA-UNCTAD study shows that NTMs increased in the ASEAN region in the past decade just as tariffs declined (see Ing and Cadot, 2017) (see Figure 3.2).
ASEAN has been attempting to address the issue of NTMs and NTBs since the latter 1990s. Initially, the focus was on understanding and classifying NTMs (then viewed almost synonymously with NTBs) and generating information on NTMs in ASEAN following UNCTAD classification. In the AEC Blueprint 2009–2015, the approach to eliminating or addressing NTBs was voluntary (the result being minimal).

Although there were a few successful cases, the Ing and Cadot study (2017) and voices from the private business sector indicate that addressing the NTBs or the NTB effects of NTMs remains a significant concern in the region.

The Ing and Cadot study highlights that NTMs are usually imposed for worthwhile non-economic reasons like food safety and environmental purposes. In addition, a large number of NTMs do not necessarily translate into a more burdensome regime as a comparison among AMSs indicates. In short, how the NTMs are implemented has a large bearing on the level of burden of the NTMs. This is especially the case for sanitary and phytosanitary measures and technical barriers to trade, which tend to form the largest shares of NTMs. Thus, Ing and Cadot recommend that the best way to deal with the NTMs is to look at them from the perspective of regulatory improvement in a country rather than from a trade negotiations point of view.
ASEAN is addressing the issue of NTB effects of NTMs through five mechanisms. The first, negotiating down NTBs, has so far had a minimal impact. The second is the resolution of specific cases, initially through the ASEAN Trade in Goods Agreement body, but which is meant to be strengthened via ASEAN Solutions for Investments, Services and Trade. Launched in 2016 and initially focused on trade in goods, ASEAN Solutions for Investments, Services and Trade is an Internet-based facility for receiving and responding to complaints submitted by ASEAN-based businesses (ASEAN, 2016). Two other mechanisms are also very important parts of the AEC blueprint. The third is standards and conformance, an important mechanism to help address technical barriers to trade. To the extent that trade and customs processes are burdensome to importers and exporters, and can potentially be used to discriminate foreign goods in the domestic market, the drive towards efficient customs and trade processes could be considered as another mechanism to temper the trade barrier effect of NTMs (now to include excessive administrative costs). Both are important initiatives in their own right. The last mechanism is captured in the AEC Blueprint 2016–2025, which is the promotion of good regulatory practice. This is consistent with the Ing and Cadot perspective on NTMs discussed earlier. The companion Volume 5, The ASEAN Economic Community into 2025 and Beyond, discusses good regulatory practice and international regulatory cooperation for the AEC towards 2025 and beyond.

- **Trade facilitation.** In a 2011 survey conducted by ERIA, the private business sector in ASEAN considered trade facilitation measures for efficient customs administration and facilitative rules of origin to be the top priority for AEC measures to be implemented by 2015. ASEAN is cognisant of the importance of trade facilitation for the region, with AEC measures focusing on rules of origin, customs modernisation and integration, transparency especially through the national and ASEAN trade repositories, and the national and ASEAN single windows. Progress on the initiatives has been considerable.

  o All AMSs have established their national trade repositories. The ASEAN Trade Repository was launched in November 2015, to which the national trade repositories are being linked. The trade repositories are one-stop online databases of national and ASEAN trade and customs-related information, including NTMs. The repositories enhance transparency and the business sector’s access to information (ASEAN, 2016).

  o National single windows (NSWs) are operational in at least seven AMSs, albeit at varying levels of efficiency, with Singapore’s being one of the world’s pioneers and one of the best. The ASW has successfully tested the electronic
exchange of e-Form D among five exchange-ready AMSs, and there is now the live exchange of e-Form D among Malaysia, Singapore, and Thailand. The important protocol on the legal framework to implement the ASW has been signed and being ratified by Member States. Live implementation of the ASW could be commenced thereafter (ASEAN, 2016).

- Customs modernisation and integration is ongoing, with e-customs in all member states and the ‘pilot project on ASEAN Customs Transit System (ACTS) including the establishment of the ACTS Central Management Team within the ASEAN Secretariat’ (ASEAN, 2015: 3). Other key achievements include the implementation of the ASEAN Harmonized Tariff Nomenclature and the development of best practice documents to support customs modernisation and reform in ASEAN (ASEAN, 2013).

- Rules of origin for the ASEAN Trade in Goods Agreement have been refined over time to be more business friendly, drawing partly from the experiences in the ASEAN negotiations of the bilateral free trade agreements with the ASEAN+6 partners.

The implementation of the trade facilitation initiatives in ASEAN coincided with the improvement in the indicators for Member States’ ease of doing business and trade across borders. A survey conducted by ERIA (2012) of the private sector in all AMSs in 2012 also indicated positive feedback of improvements in the customs and trade processes in many Member States. Nonetheless, gaps in the trade facilitation environment remain large, and an ERIA survey in 2013 (Intal, 2013) focusing on the agricultural trade facilitation environment in ASEAN showed significant complaints related to the efficacy, transparency, and burdensome paperwork in several AMSs. In addition, Ing and Cadot in the companion ASEAN@50 Volume 5 highlight that the ASEAN rules of origin remain complicated in practice with significant ad valorem equivalent (implicit tariffs) in products like footwear, textile and garments, and vehicles.

Given the still substantial gaps and challenges in several AMSs and the region towards a world-class customs and trade facilitation environment in ASEAN in the light of dynamic changes in East Asia, ASEAN has decided to reinvigorate the ASEAN Trade Facilitation Joint Consultative Committee. The association is also exploring the development of an ASEAN Trade Facilitation Indicators system as an important monitoring tool of the state of the trade facilitation environment in the region and the implementation of the ASEAN trade facilitation initiatives. The system is also expected to be consistent with, and useful for, the monitoring of
the implementation of the World Trade Organization (WTO) Trade Facilitation Agreement, which Member States have signed.

**Standards and conformance.** ASEAN established the ASEAN Consultative Committee for Standards and Quality (ACCSQ) in 1992, the same year the decision to establish AFTA was made. The main aim of the standards and conformance initiatives in ASEAN is to eliminate technical barriers to trade for the realisation of a highly integrated and unified ASEAN economy, or the so-called single market and production base. The results of a 2012 ERIA survey on private sector perception on AEC measures in ASEAN (ERIA, 2012) point out that varying standards and technical requirements and difficulties in conformity assessments are a serious deterrent to a more integrated AEC. The ACCSQ’s main approach, through its working groups and product groups, has been to set out the key policy documents of ASEAN guidelines governing standards and conformance initiatives in the region and to focus on the agreed-upon priority integration sectors that have a substantial bearing on intra-ASEAN trade.

The achievements of the ACCSQ have been considerable. In addition to the four major ASEAN policy guidelines, it has succeeded in harmonising many standards and technical requirements and agreed on several sector-specific guidelines in the identified priority sectors, such as electrical and electronic equipment, automotive, pharmaceutical, medical devices, processed food, rubber, and traditional medicines and health supplements. It has developed sectoral MRAs for electrical and electronic equipment and the Good Manufacturing Practice inspection of manufacturers of medicinal products. It has also succeeded in harmonising technical regulations in cosmetics, electrical and electronic equipment, and medical devices. Many of the agreements are recent, suggesting an intensification of efforts of the various working and product groups under the ACCSQ in the run-up to the realisation of the AEC in 2015.

The approach of establishing working and product groups and tapping the expertise of the private sector (including international institutions) has contributed to the ACCSQ’s considerable achievements. Nonetheless, the deepening economic integration in the region means more and more products are potentially tradable.

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1 The key policy documents are the ASEAN Guidelines on Standards, Technical Regulations and Conformity Assessment Procedures; ASEAN Guideline on Accreditation and Conformity Assessment; ASEAN Guideline on the Development of Mutual Recognition Agreements; and ASEAN Guideline on Harmonization of Standards.

2 See Annex 1 of the ASEAN Standards and Conformance Strategic Plan 2016–2025 for the list of the major achievements.
within the region, thereby raising the standards and conformance issues in those not-yet-prioritised sectors and products. Moreover, implementation is the key to ensuring that the ASEAN standards and conformance initiatives bring benefits to the business sector and the public. For example, the results of the AEC Scorecard Study conducted by ERIA in 2015 (ERIA, 2015) indicate several implementation issues and concerns in several AMSs as regards the ASEAN Cosmetic Directive. The results suggest that monitoring of the standards and conformance initiatives would need to include the actual implementation of the agreements.

**Free flow of services.** Services, and with them the free flow of services, are important for ASEAN. Except for Brunei where industry remains the most dominant, the services sector is now the largest economic sector in all AMSs, accounting for more than 50% of GDP in Malaysia, the Philippines, Thailand, and especially Singapore. Services exports and imports of ASEAN grew robustly at double digits during 2009–2014 before dipping somewhat in 2015 to account for about 13% of GDP for either exports or imports in that year. ASEAN is a net importer of services, although the Philippines stands out as having the largest net service export surplus among the Member States. Travel, business services, and transport dominate services exports and imports in the region, both intra-ASEAN and overall. In addition, services value added accounts for a large share of manufacturing exports for a number of AMSs, accounting for more than 30% of the value of the manufactured exports of Brunei, the Philippines, and Singapore in 2009; more than 25% for Malaysia and Viet Nam; and between 17% and 23% for Indonesia and Thailand (Pasadilla and Wirjo, 2014/2015). FDI in services now accounts for at least 40%, and at times more than 50%, of all FDI into ASEAN.

Christopher Findlay highlights in the companion Volume 5 that services, especially modern services, can contribute to productivity growth through several channels. At the same time, they are undergoing a ‘service revolution’, owing to greater tradability, technological changes, the ‘servicification’ of manufacturing, and the growth of service value chains. This offers significant opportunities for the AMSs to improve and expand trade in services directly and indirectly through the service content of goods exports. Capturing the opportunity, however, calls for more liberalised and competitive services markets, the freer flow of specialist service providers, and good infrastructure. Service liberalisation in ASEAN is one key way by which ASEAN can be a service hub in the region and the world. At the same time, a study by Dee (2012) shows that the liberalisation of key services sectors, such as banking, transport, and logistics, can substantially boost productivity and growth.

ASEAN has been pursuing the liberalisation of trade in services since the signing of the ASEAN Framework Agreement on Services (AFAS) in 1995, a year after the
WTO General Agreement on Trade in Services (GATS). Heavily influenced by GATS, AFAS aimed to go beyond GATS in liberalisation; i.e. GATS Plus. Indeed, AFAS went substantially beyond GATS, innovating in its approach in a series of rounds, shifting from pure ‘request and offer’, similar to GATS, to a subsectoral approach bringing in for the AFAS sectors of interest to at least four – and then reduced to three – AMSs. It then became more progressive with the scheduling of several new subsectors while deepening commitments on previous subsectors at successive rounds, until obtaining an expected liberalised free trade regime in services after the completion of the 10th round. Likely as a means to move the AFAS rounds forward, ASEAN in 2009 allowed overall flexibilities up to 15%. The flexibilities include enabling a Member State to catch up in the next round if it cannot meet the parameters of commitments set for the previous round; or allowing a Member State to substitute those subsectors agreed upon for liberalisation though it cannot make a commitment with subsectors outside of the agreed subsectors; or allowing liberalisation through the ASEAN minus X formula. These institutional innovations of liberalisation formulas, frequent rounds, and flexibilities have proven to be successful in moving service liberalisation commitments far more than in GATS, even if the commitments tend to be short of what the actual reality on the ground is.

AFAS negotiations have been undertaken through the Coordinating Committee on Services under the AEM. The Coordinating Committee on Services and AEM also oversaw the negotiations on MRAs on professional services and, eventually, also on the movement of natural persons. Later on, the ASEAN Working Committee on Financial Services Liberalization under the ASEAN Finance Ministers Meeting tackled the negotiations on financial services liberalisation while the ASEAN Transport Ministers Meeting supervised air transport liberalisation. This is likely because financial liberalisation needs to be tackled in conjunction with macro-prudential and other financial sector development issues, while air services liberalisation follows an air transport–specific approach that is very different from the AFAS approach.

The results from the institutional innovations, including the series of rounds, have been considerable given the sensitivity of many services sectors that have bedevilled services liberalisation negotiations everywhere, including the WTO. Nonetheless, services liberalisation under AFAS remained incomplete by the target year of 2015, with the difficult subsector liberalisation challenges postponed by the flexibility rule to the 10th and final round post-2015. Remarkably, it is in the financial services and air service sectors where the most cohesive (financial services) and most far-reaching (air transport) liberalisation initiatives in ASEAN have been undertaken so far.
Figure 3.3 and Table 3.1 provide a good snapshot of the progression and progress of AFAS from AFAS 5 to AFAS 9. (While there is already AFAS 9, the commitments of Indonesia and Singapore are still not publicly available at the time of writing this paper and therefore could not be included.) The figure shows the expansion in the number of subsectors over the years. Member States differ in the round in which they offered the most number of additional subsectors. This is expected because the design of the rounds includes the addition of new subsectors over the minimum required for the previous round. Cambodia is noteworthy for offering the most number of subsectors in AFAS 5; Indonesia, the Lao PDR, Philippines, and Viet Nam offered the most additional subsectors in AFAS 7; and Thailand is noteworthy for its expansion in AFAS 8.\(^3\)\(^4\)

What is equally important is the growing number of subsectors where the AMSs committed more than 51% foreign equity. It is interesting to note that for many AMSs, it is in AFAS 8 where the number and percentage – indeed preponderance – of subsectors with foreign equity of more than 51% allowable foreign equity sharply increased. This is especially true for Brunei, Cambodia, the Lao PDR, and Singapore. It is also worth noting that the new ASEAN members have been far more aggressive in services liberalisation, with the Lao PDR, Myanmar, and Viet Nam having most of their subsectors committed at more than 50% allowable foreign equity.

Table 3.3.1 gives the liberalisation rates for Modes 1, 2, and 3 and the overall liberalisation rate under AFAS 8 and AFAS 9. AMSs are most liberal with Mode 2 as is expected; i.e. there is virtually no restriction to consumption abroad. For Mode 1 – i.e. cross-border consumption – the liberalisation rate varies among the AMSs, with marked increase in liberalisation rates between AFAS 8 and AFAS 9 for Malaysia, Myanmar, and Viet Nam. Myanmar and the Lao PDR stand out as the most liberal; the Philippines has a particularly low liberalisation rate, reflecting the unwillingness to bind commitments (i.e. ‘unbound’). In Mode 3, or commercial presence, the liberalisation commitments between AFAS 8 and AFAS 9 for Brunei Darussalam, the Lao PDR, Malaysia, Myanmar, and, to a less extent, Viet Nam sharply improved. As the table shows, the Philippines and Thailand have much lower liberalisation commitments than the rest of the AMSs.

\(^3\) It should be noted though that the numbers are not always comparable across countries because a commitment is considered one no matter what the disaggregated level of the subsector is. Thus, a country can have very high numbers if its offers are at a much more disaggregated level than another country that has commitments at a more aggregated level.

\(^4\) The sharp increase in the number of commitments for Thailand (and to some extent Malaysia) in AFAS 8 arose from highly disaggregated and specific subsectors with different commitments, even if they are all under the same customs procedure code. In the figure, they are estimated as separate subsector commitments.
(no publicly available data yet for Indonesia and Singapore for AFAS 9). The Lao PDR and Myanmar lead the AMSs in terms of overall liberalisation commitments in AFAS 9, followed by Cambodia and then Brunei Darussalam and Malaysia.

As Figure 3.3 and Table 3.1 suggest, it is primarily in Indonesia, the Philippines, and Thailand where the challenges of further services liberalisation in ASEAN lie. AFAS 10, when finished, will be the last round that will define the outcome of the whole AFAS process. This is because the flexibility rule benefits of delaying implementation for the next round and substitution with non-agreed subsectors for liberalisation will no longer apply in principle given that AFAS 10 is the last and all subsectors are meant to be covered by it.

**Figure 3.3. Progress and Progression of AFAS**

AFAS = ASEAN Framework Agreement on Services, FE = foreign equity liberalisation.

Note: One major reason for the sharp spike in the number of subsectors in AFAS 8 is due to much greater disaggregation and industry specificity because of different foreign equity restrictions despite being with the same customs procedure code at the four-digit level.

Source: Estimated by Jaysa Prana (ERIA) based on AFAS submissions.
Table 3.1. AFAS Liberalisation Rates
(%)  

<table>
<thead>
<tr>
<th>Country</th>
<th>Mode 1</th>
<th>Mode 2</th>
<th>Mode 3</th>
<th>Overall Liberalisation Score</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>AFAS 8</td>
<td>AFAS 9</td>
<td>AFAS 8</td>
<td>AFAS 9</td>
</tr>
<tr>
<td>Brunei</td>
<td>68</td>
<td>68</td>
<td>98</td>
<td>98</td>
</tr>
<tr>
<td>Cambodia</td>
<td>68</td>
<td>71</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Indonesia</td>
<td>72</td>
<td></td>
<td>98</td>
<td></td>
</tr>
<tr>
<td>Lao PDR</td>
<td>95</td>
<td>96</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Malaysia</td>
<td>56</td>
<td>71</td>
<td>99</td>
<td>99</td>
</tr>
<tr>
<td>Myanmar</td>
<td>84</td>
<td>99</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Philippines</td>
<td>47</td>
<td>45</td>
<td>99</td>
<td>100</td>
</tr>
<tr>
<td>Singapore</td>
<td>87</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Thailand</td>
<td>66</td>
<td>65</td>
<td>98</td>
<td>97</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>47</td>
<td>59</td>
<td>99</td>
<td>100</td>
</tr>
<tr>
<td>Average</td>
<td>69</td>
<td>72</td>
<td>99</td>
<td>99</td>
</tr>
</tbody>
</table>

AFAS = ASEAN Framework Agreement on Services.
Source: ERIA.

AFAS 10 is effectively under the purview of the new ASEAN Trade in Services Agreement in the AEC Blueprint 2016–2025. The strategic action plan for services under the AEC Blueprint 2016–2025 includes the assessment of the ‘existing flexibilities, limitations, thresholds and carve-outs’ under AFAS’ (ASEAN Secretariat, 2015c: 6). This is one mechanism that would likely impact on AFAS 10. The other is the exploration of ‘alternative approaches for further liberalisation of services’ (ASEAN Secretariat, 2015c: 6). This is likely essentially a code phrase for exploring a shift from a positive approach – which AFAS is – to a negative approach to services liberalisation moving forward into 2025.

The progressive liberalisation of financial services under AFAS is built on a cohesive ASEAN Financial Integration Framework that aims towards a semi-integrated financial region by 2020. This framework was adopted in 2011 by the ASEAN Central Bank Governors and ASEAN Finance Ministers. It includes frameworks for ASEAN banking and insurance integration, initiatives for capital market development and for interoperable cross-border payments and settlements systems, cooperation in the management of capital account liberalisation, and capacity building.
As banking dominates the financial sector in ASEAN, and banking integration is low in the region, the ASEAN Banking Integration Framework is of particular interest. Banking liberalisation under the framework is specifically ASEAN-biased in contrast to much of AFAS, which tends to be MFN (most favoured nation) even if it is under AFAS. The framework relies on reciprocal bilateral arrangements to give qualified ASEAN banks greater market access and grant them national treatment. The bias for ASEAN banks instead of MFN liberalisation stems partly from the fact that non-ASEAN multinational banks have a much larger presence in ASEAN countries than banks from other ASEAN countries. Other financial industries given special focus for liberalisation are insurance with high priority given to the liberalisation of the cross-border supply of marine, aviation, and goods in international transit insurance as well as natural catastrophe insurance; reinsurance and retrocession for risk diversification; and financial leasing to help firms when acquiring equipment.

Liberalisation initiatives are being undertaken alongside initiatives to improve the institutional and related policy and prudential environments. This includes the agreement to adopt ISO20022 as a common standard for fund transfers in ASEAN, following the readiness of individual countries to have interoperability and greater efficiency in cross-border payments. It also includes several initiatives to develop the capital markets in the region. Such initiatives include (i) the electronic ASEAN Trading Link, initially among the stock exchanges of Malaysia, Singapore, and Thailand; (ii) the adoption of ASEAN disclosure standards to facilitate the multi-jurisdictional offering of equity and debt; (iii) the memorandum of understanding for the expedited entry of secondary listings among regulators and exchanges from Malaysia, Singapore, and Thailand; (iv) efforts to raise corporate governance standards and practices such as the ASEAN Corporate Governance Scorecard; and many more. Improved macroeconomic coordination initiatives to manage capital account liberalisation include the Policy Dialogue Process on Capital Flows and Safeguard Mechanisms for Capital Account Liberalisation, as well as the monitoring tool on the progress of capital market liberalisation through the ASEAN Capital Account Liberalisation Heatmap⁵.

With respect to the liberalisation of air transport services, it is best to view the AFAS liberalisation packages (ninth package as of 2015) of primarily air transport ancillary services together with the ASEAN multilateral agreements on air transport outlined in the Roadmap for Integration of Air Travel Sector. These multilateral agreements are the ASEAN Multilateral Agreement on the Full Liberalisation of Air Freight Services, the ASEAN Multilateral Agreement on Air Services, and the ASEAN Multilateral Agreement

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on the Full Liberalisation of Passenger Air Services, together with their respective protocols. All these agreements aim to establish ‘open skies’ in the region and eventually the ASEAN Single Aviation Market with its open skies policy.

The multilateral agreements and their protocols have all been fully ratified since May 2016. Thus, ASEAN open skies for the so-called third, fourth, and fifth freedoms are now in force. This means that an airline of one Member State can land at an international airport of another with unlimited seat capacity.⁶ It is worth noting that the multilateral air agreements in ASEAN eschew the issue of cabotage (i.e. domestic air transport is reserved for domestic carriers) nor do they address the extent of allowable foreign ownership of airlines. (The AFAS air transport services packages are primarily for the liberalisation of ancillary air transport services.) Nonetheless, the full liberalisation of air traffic rights (i.e. third, fourth, and fifth freedoms) ensures great potential contestability in the air services markets in the region. Although all 10 AMSs fully ratified these agreements and protocols in May 2016, the agreements have been in force before that date. Arguably, the sharp increase in air traffic and the rapid increase in sea capacity, especially of low-cost carriers in ASEAN, have been a by-product of the more liberalised air transport in the region in tandem with lower airfares and the marked improvement in per capita incomes of the AMSs that are generating large increases in demand for travel within the region. And that is what liberalisation and enhanced competition in a dynamic economic environment are expected to bring.

**Free movement of skilled labour.** Linked closely with services, and indeed the key initiatives mainly undertaken by the Coordinating Committee on Services, are the initiatives towards the free movement of skilled people. The main measures are the MRAs on a few professional services, the ASEAN Agreement on the Movement of Natural Persons (MNP), and the ASEAN Qualifications Reference Framework (AQRF).

The MRAs are for the ‘mutual recognition of authorisation, licensing, or certification of professional service suppliers in one ASEAN Member State by other ASEAN Member States’ (ASEAN Secretariat, 2015a: 27). Negotiations since 2003 have produced MRAs in engineering, architectural, and accountancy services, and a framework arrangement for the mutual recognition of surveying qualifications, all in the field of business services. A similar MRA is for tourism professionals. The other ASEAN MRAs for which negotiations started in 2004 are medical services, specifically medical, nursing, and dental services.

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⁶ Indonesia, the Lao PDR, and the Philippines imposed some conditions in their ratification of the agreements. Specifically, Indonesia allowed open skies in only five (major) international airports; the Lao PDR excludes open skies privileges to Thai airlines in Vientiane and Luang Prabang; and the Philippines limits access to Manila International Airport due to capacity constraints and overcrowding concerns. Note that complete open skies includes allowing an airline of one Member State to operate between domestic airports of another Member State – the so-called seventh freedom; this is not in the cards for ASEAN. See J. Jordan (2016).
The template is similar among the MRAs involving business services: establish an ASEAN-wide registration system allowing professional engineers, architects, or accountants to be certified as ASEAN-chartered professional engineers, ASEAN architects, or ASEAN certified professional accountants, after meeting the agreed criteria and receiving approval from an ASEAN technical coordinating body overseeing the certification process (e.g., the ASEAN Architect Council). The ASEAN certified professional can then work as a registered foreign professional engineer, a registered foreign architect, or a registered foreign professional accountant in other Member States. Work for registered foreign professional engineers is in collaboration with other professional engineers in the host country, while registered foreign architects and registered foreign professional accountants can work independently or in collaboration with other licensed architects or accountants in the host country. Registered foreign professional accountants cannot sign off on independent auditor reports or other accountancy services requiring licensing in the host country (ASEAN Secretariat, 2015a: 27–34).

The MRA on Tourism Professionals is somewhat similar to the MRAs in business services, except that tourism professionals tend not to be as regulated as engineers, accountants, or architects. Eligibility to work in a host country requires possession of a valid certificate in a job specified in the ASEAN Common Competency Standards for Tourism Professionals issued by a tourism professional certification board in a Member State. Toolboxes consistent with the competency standards are being developed and so is the registry system of the successful certificate holders, the ASEAN Tourism Professionals Registration System. To a large extent, for largely unregulated or far less regulated professions like tourism professionals, the certification system becomes a quality-signalling device for, and a contributor to, improved efficiency of the labour market in the whole region (ASEAN Secretariat, 2015a: 27–34).

The MRAs on health services do not have a system of ASEAN-certified health professionals nor an ASEAN-wide registration system. A registered nurse in one country can apply in another as a foreign nurse if he or she meets the conditions stipulated in the MRA. Much of the work of the coordinating committees on medical, nursing, and dental practitioners has focused on (i) the exchange of information on laws, practices, and developments in healthcare practice; (ii) procedures for the registration and licensing of domestic and foreign practitioners; and (iii) the required qualifications, etc. These initiatives are nonetheless supportive of facilitating the mobility of professionals within the region, the promotion of best practices on standards and qualifications, and enhancement of cooperation with respect to mutual recognition and capacity building. This cautious approach is likely a recognition that healthcare services are more sensitive.
and in culturally shaped sectors (e.g. language requirements so that health service providers can communicate directly with patients) (ASEAN Secretariat, 2015a: 27–34).

The results on the ground have been less than overwhelming for the MRAs so far if the MRAs are evaluated in terms of the number of professionals involved. As of October 2015, only six out of 1,483 ASEAN-chartered professional engineers had been registered as foreign professional engineers; ASEAN architects were only 284 (ERIA, 2015). The low numbers suggest that the MRAs do not contribute much to the intra-regional mobility of skilled professionals. While the low numbers may be because of the newness of the schemes, they are more likely the result of the presence of alternative legal schemes that allow foreigners to practise in the host countries. An example is the temporary registration or temporary permits for architects or engineers in countries like Malaysia, the Philippines, and Thailand. Labour market conditions in host countries influence unilateral host country policies on foreign providers of professional services. Thus, for example, about 15% of nurses in Brunei in 2015 were from overseas and around 3,000 foreigners were enrolled as nurses at the Singapore Nursing Board in 2013. Many Member State professionals, such as engineers, architects, or accountants, work in other Member States as corporate employees rather than as independent professionals (ERIA, 2015).

In short, in a region of dynamic economies with varying labour market conditions, unilateral policies and market arrangements have so far played a much greater role in facilitating the flow of skilled workers and professionals within the region than the MRAs. Perhaps it is best to view the MRAs on regulated professions, such as those on business services, as managed liberalisation initiatives towards greater contestability of professional services markets in host countries rather than as important means of increasing the mobility of skilled labour and professionals in ASEAN.

The MRAs similar to the MRA on Tourism Professionals, the AQRF, and the MNP agreement probably will have a greater impact on the mobility of skilled labour and professionals within ASEAN. As indicated earlier, the MRA on Tourism Professionals can be a good signalling device because of the clear standards set for the region for the certification. Therefore, it expands the employability potential of a certificate holder to the whole region instead of only the home country. At the same time, the regional registry allows labour demanders a potential regional supply of qualified professionals. This labour market enhancing function of such an MRA is useful for largely unregulated or lightly regulated professions or skills, as those in the tourism industry. The AQRF provides a similar signalling device to the regional labour market by providing a common reference for comparing national qualifications (in education and training) among AMSs according to specified levels of complexity of learning outcomes. This is voluntary at the
moment and does not require changes in national qualification systems. Nonetheless, when fully operationalised, it could provide pressure for transparency and improved quality assurance systems and standards in Member States (ASEAN Secretariat, 2015a: 33–34).

The MNP agreement, signed in 2012, supersedes the earlier AFAS negotiations on Mode 4, which tended to focus on intra-corporate transfers. The agreement also covers business visitors, contractual service suppliers, and other categories that may be specified in the commitment schedules of AMSs. The MNP agreement is on the temporary movement of natural persons to other AMSs to provide services, whereas the MRAs on professional services include the long-term movement of professionals. The agreement aims to establish streamlined and transparent immigration procedures to facilitate the cross-border movement of temporary service providers. An ERIA analysis in 2015 of the Member States’ commitments to the MNP agreement showed improvement over the commitments under AFAS 8; namely, wider sectoral coverage (i.e. 72% vis-à-vis AFAS 8’s 53%); expanded scope of providers to include business visitors (at least six AMSs) and short-term contractual service providers (Cambodia, the Philippines, and Viet Nam); and expanded sectoral coverage in intra-corporate transfers (nine AMSs) (ERIA, 2015: 136–137).

In summary, ASEAN has been improving the institutional mechanisms to facilitate the movement of skilled labour and professionals in the region. Nonetheless, it is likely that the more important facilitators are not the MRAs in professional services that ASEAN focused on at first since the early 2000s. Rather these would be the more recent initiatives that serve more as signalling devices to harmonise skills standards (MRA on Tourism Professionals and the AQRF) and to widen the scope and sectoral reach (and preferably depth) of commitments for the temporary movement of skilled people as well as the promise of more streamlined and transparent immigration procedures. All these would substantially contribute to the labour market impulses towards the freer movement of skilled labour in ASEAN.

**Investment liberalisation and the free flow of investments.** As put strongly in the Roadmap for an ASEAN Community 2009–2015 (p. 27), a ‘free and open investment regime is key to enhancing ASEAN’s competitiveness in attracting foreign direct investment (FDI) as well as intra-ASEAN investment. Sustained inflows of new investments and reinvestments will promote and ensure dynamic development of ASEAN economies.’ Investment liberalisation is central to attaining a free and open investment regime in the region.

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7 This section is largely taken from ERIA (2015: 109–121).
FDI is important to ASEAN. Indeed, ASEAN relies more on foreign investment for its capital formation than do China and India. Moreover, in the context of the so-called second unbundling phenomenon of production networks and global value chains, FDI that is increasingly bundled with technology, management and quality control, and market linkages has been a critical factor in ASEAN’s success of embedding itself firmly in East Asia’s regional production and global value chains. ASEAN’s industrial and technological upgrading imperatives are better served by new investments and reinvestments.

Experiences in the European Union and the North American Free Trade Agreement area show that FDI inflows surged into these regions at the start of their formation. It is worth noting that the surges of FDI into ASEAN occurred during the period of the announcement of the formation of the AEC (2003–2004) and the years coinciding with the Roadmap for an ASEAN Community (2009–2015) going into AEC 2015. No comprehensive analysis of the link between FDI inflows into ASEAN and the impending establishment of the AEC has been undertaken. However, recent surveys of multinational firms suggest that the formation of the AEC has been an increasingly important factor in their investment decisions in the region. Thus, there appear to be good indications that the AEC has already been delivering in one aspect: it has eased the concerns of the ASEAN leaders expressed in the early 2000s that AMSs were losing out to China in terms of FDI. Indeed, ASEAN surpassed China as the leading FDI destination in the developing world and was a very close second to China in 2015. With labour costs in China rising substantially, making the lower-wage AMSs increasingly attractive for more labour-intensive manufacturing companies, ASEAN has recently become a growing global investment hotspot. Firms from within and outside the ASEAN region appear to be increasingly taking note of the growing middle class in ASEAN, creating another source of impetus for FDI inflows into the region.

Under the AEC Blueprint 2009–2015, investment liberalisation in services is covered by AFAS which, as discussed earlier in the chapter, shows the predominance of the services sector where majority foreign ownership is allowed in most AMSs. Investment liberalisation in the goods sector, including services incidental to agriculture, mining, and manufacturing, is covered by the ASEAN Comprehensive Investment Agreement.

To determine the degree of foreign investment liberalisation in the goods sector in ASEAN, ERIA estimated in 2015 the percentage of subsectors in agriculture, mining, and manufacturing (including services incidental to the sectors) where at least 70% of
foreign equity is allowed. The choice of at least 70% allowable foreign equity is based on the presumption that effective control of a corporation (that allows the change in the nature and organisation of a corporation, for example) would generally require a two-thirds majority of the voting rights of the corporation. Although the 70% cut-off is less stringent than the usual 100% foreign equity benchmark, the implied assumption of the 70% threshold as ‘liberalised’ is that it is not difficult to find local partners. Also, such joint ventures may have positive societal benefits through technology and managerial transfers as well as market linkage opportunities. Nonetheless, it is worth noting that countries that allow at least 51% foreign equity tend to allow 70% foreign equity and, in most cases, also up to 100% foreign equity, except in some cases of legal or constitutional constraints or sociopolitical objectives.

Figure 3.3.4 presents the investment liberalisation rate for the case of 70% allowable foreign equity. The figure differentiates the investment liberalisation rate for the combined agriculture and mining sectors from that for the manufacturing sector. The figure shows that the majority of AMSs allow at least 70% foreign equity in at least 90% of all manufacturing subsectors, and virtually all allow at least 70% foreign equity in at least 80% of all manufacturing subsectors. The figure suggests that AMSs have relatively liberal investment regimes in terms of foreign equity in the manufacturing sector. Note that regional production networks are mainly in the manufacturing sector.

**Figure 3.4. Foreign Investment Liberalisation Rate (ACIA, 70% Foreign Equity)**

ACIA = ASEAN Comprehensive Investment Agreement.
It is in the agriculture and natural resource sector where, as Figure 3.4 indicates, a significant divide exists among AMSs in terms of the degree of openness to foreign equity majority control. The figure seems to suggest that the more land-abundant AMSs tend to be more open to foreign majority control of their agriculture and mining subsectors. Country reports in the ERIA study indicate that there are indeed complex non-economic sensitivities or constitutional restrictions to foreign equity control in some subsectors, especially in the agriculture and natural resources sectors.

**Pillars two, three, and four**

**Pillar one: a single market and production base.** This is the most articulated of the four pillars of the AEC Blueprint 2009–2015. To a large extent, pillar one is the core of the AEC, and the AEC is defined in people’s minds in terms of the phrase ‘single market and production base’. Nonetheless, the three other pillars are also important because they complement pillar one and help ensure that the liberalisation and facilitation measures in pillar one benefit more people and keep ASEAN well engaged globally or at least within the broader East Asia and Asia-Pacific region.

**Pillar two: towards a competitive economic region.** The AEC measures geared towards making ASEAN a competitive region are infrastructure development, competition policy, consumer protection, intellectual property rights, taxation, and e-commerce. No cohesive framework weaves all the above together in the same vein as in pillar one; indeed, it may be difficult to make one such a framework to pull them all together. Nonetheless, the list points to at least three major factors that contribute to improved efficiency and productivity growth. These factors are (i) infrastructure and connectivity, (ii) the promotion of a competitive domestic business environment through a competition policy consistent with consumer protection, and (iii) the promotion of innovation and technological adaptation through a facilitative intellectual property rights regime. The three major factors above were the primary emphasis of the implementation of the AEC Blueprint 2009–2015.

Taxation, focusing on bilateral agreements to eliminate double taxation, does not seem as compelling as a factor towards a competitive region. However, it may contribute to an improved FDI climate within the region and thereby improve the competitiveness of the region. A more important role of taxation, not captured in the AEC blueprint, is its centrality in improving the domestic fiscal resources of several AMSs for infrastructure investment because Member States cannot just rely on public–private partnerships for infrastructure development. However, this is the province of macroeconomic policy rather than trade and integration per se. E-commerce is emerging as an important
innovation for trade and development of small and medium-sized enterprises (SMEs) and has a greater emphasis in the AEC Blueprint 2016–2025.

Connectivity, transport facilitation, and infrastructure development are central to the competitive economic region pillar because they not only contribute to improved productivity and a more efficient geographically spread-out production base but also engender the sense of a ‘One ASEAN’ community. ASEAN adopted the Master Plan on ASEAN Connectivity, which envisions physical connectivity, institutional connectivity, and people-to-people connectivity and gives the spatial-economic expression of ASEAN economic integration and community building. It complements and presents a different and complementary perspective to the AEC blueprint.

On physical connectivity, the emphasis on land transport was on the ASEAN Highway Network and the Singapore–Kunming railway link. The ASEAN Highway Network provides links (primarily continental) between AMSs and with neighbouring countries. It also includes priority transit transport routes. The progress of the network has been considerable, with no more missing links and with nearly a 50% reduction in the roads below class III from 2010 to 2015. Work on the Singapore–Kunming (China) Railway Link is ongoing albeit delayed. The section from Phnom Penh to the Viet Nam border as well as the spurs into the Lao PDR are awaiting funding; the line between Thailand and Myanmar has been modified; and upgrading of railroad tracks is being undertaken (ASEAN Secretariat, 2015a).

Transport facilitation is critical as institutional connectivity complements efficient land physical connectivity. Member States have signed three major transport facilitation agreements. They are the ASEAN Framework Agreement on the Facilitation of Goods in Transit, the ASEAN Framework Agreement on the Facilitation of Inter-State Transport, and the ASEAN Framework Agreement on Multimodal Transport, with their corresponding protocols. They are all in force, but only in those countries that ratified the protocols or whole agreements; that is, until 2015, the agreements were not yet fully operational. In addition to these agreements, the AMSs are in negotiations on an ASEAN Framework Agreement on the Facilitation of Cross-Border Transport Passenger by Road Vehicles for seamless cross-border mobility of passengers between and among Member States by simplifying and harmonising transport, customs, immigration, and quarantine procedures and requirements (ASEAN Secretariat, 2015a).

With respect to air connectivity, as discussed in the section on the free flow of services, ASEAN has undertaken significant liberalisation measures, best exemplified by the ratification of all multilateral agreements on air services, air freight, and passengers leading to an open skies regime (except without seventh freedom) and the finalisation
of the ninth package of liberalisation of air transport ancillary services. With respect to maritime transport, the significant initiatives have been in the development of roll-on/roll-off services between identified points in Indonesia, Malaysia, the Philippines, and Thailand; the improvement of selected ports in the region; and efforts to liberalise shipping services (albeit given cabotage rules), etc. towards the ultimate goal of an ASEAN Single Shipping Market.

In short, there has been an improvement in the region’s connectivity, transport facilitation, and infrastructure development, although it has been slow in many cases, except notably in air transport. The Kuala Lumpur Transport Strategic Plan or ASEAN Transport Strategic Plan 2016–2025 (ASEAN Secretariat, 2015d) aims for accelerated implementation. The companion volume, Volume 5 of ASEAN@50 entitled The ASEAN Economic Community into 2015 and Beyond, discusses the connectivity issue in greater detail.

The AEC Blueprint 2009–2015 measures for competition policy aim at fostering a culture of fair competition in the region. The focus of the initiatives was to introduce competition policy in each Member State, create a network of competition agencies, undertake capacity building, and develop regional guidelines on competition policy. Achievement of the AEC measures has been reasonably high. To date, 9 out of 10 have enacted competition policy laws and established competition agencies. An ASEAN Experts Group on Competition has been established and has been instrumental in driving the activities on competition policy, including several capacity-building activities and the development of regional guidelines on competition policy in ASEAN. A comparison of the competition laws of a number AMSs shows significant differences in their provisions, e.g. the threshold for dominance and merger controls. The implementation experiences of the competition agencies also differ significantly, with Indonesia’s competition policy agency (KPPU Komisi Pengawas Persaingan Usaha/The Indonesian Competition Authority) being the most mature (Lee and Fukunaga, 2013). To some extent, these experiences and the regional capacity-building initiatives can contribute towards the convergence of competition policy regimes as well as to greater cooperation among the region’s competition agencies in the future. This is needed as deeper economic integration would mean deeper business relationships among firms in the region and, therefore, a greater chance of cross-border anti-competitive behaviour.

ASEAN has long acknowledged the important role of intellectual property in technological, economic, and social progress. In fact, ASEAN formed the ASEAN Working Group on Intellectual Property Cooperation early on in 1996, a year after the signing of the ASEAN Framework Agreement on Intellectual Property Cooperation in 1995. Note that the focus of the working group has been on regional cooperation and
coordination and not on designing a single harmonised regional intellectual property system. This is in cognisance of the wide difference in levels of development of the Member States with their own intellectual property–related laws, rules, and practices as well as institutions.

The ASEAN Intellectual Property Rights Action Plan provides a wide and long set of cooperation and coordination initiatives. The strategic goals are (i) the improvement of the efficiency of the administration and protection of intellectual property rights, (ii) the development of national or regional legal and policy infrastructure responsive to the dynamic changes in the intellectual property landscape, (iii) systematic promotion of intellectual property, (iv) active regional participation in the international community, and (v) intensified regional cooperation and collaboration on capacity building. Of interest is the ASEAN Patent Examination Cooperation, built on the principle of mutual recognition, wherein patent examination in one AMS may build on the results of examination in another, in effect a mechanism for work-sharing to ease patent workloads in the region (Degelsegger, Remoe and Trienes, 2016). Also of note are the capacity-building initiatives with the support of AMSs’ dialogue partners, most especially the European Union.

Despite the lofty goals of the ASEAN Intellectual Property Rights Action Plan, however, there are major challenges towards a well-performing system in the region. The results of the study by Degelsegger, Remoe, and Trienes (2016) show a wide variation in the capacities of the intellectual property offices of AMSs. This has constrained the effectiveness of the ASEAN Patent Examination Cooperation because of differentiated levels of trust among the intellectual property offices of Member States. For example, patent applications with available search reports from Singapore may be fast-tracked compared to patent application from another AMS with a known weak intellectual property office. Some intellectual property offices are understaffed and/or staff are inexperienced and not well trained. The patent filing and granting process can sometimes take more than a decade in one Member State compared to only a few years in another, like Singapore. Thus, much is to be done to have a well-performing system that is supportive of ASEAN’s drive towards an innovative region. Indeed, the patenting activity in ASEAN is low and dominated by non-resident filing, although the filing for utility models is predominantly by residents. There are also major challenges in the ecosystem for generating intellectual property in many Member States; nonetheless, there is a growing trend of filings by residents, although from a level, especially in comparison with neighbouring countries like China (Degelsegger, Remoe, and Trienes, 2016). The ASEAN Intellectual Property Rights Action Plan 2016–2025 presents a wider set of initiatives going into 2025 that builds on the initiatives of the earlier Intellectual Property Rights Action Plan. It also attempts to address major challenges facing the intellectual
property rights regime in the region, with the ultimate goal of transforming ASEAN into an innovative and competitive region through the use of intellectual property. The issue of innovation and intellectual property rights regimes is discussed further in Volume 5.

**Pillar three: region of equitable development.** Narrowing the development gap between AMSs (most specifically, the gap between the ‘older’ ASEAN-6 and the ‘newer’ ASEAN-4 [CLMV] countries) and engendering more inclusive growth through the growth and development of ASEAN SMEs are the focus of AEC pillar three towards a region of equitable development. The centrepiece AEC measures are the Initiative for ASEAN Integration (IAI) for narrowing the development gap and the ASEAN strategies and plans of action for SME development.

The IAI is essentially a mechanism for the ASEAN-6 countries to help the CLMV countries meet the ASEAN-wide targets and commitments towards the realisation of the ASEAN Community. The activities are primarily of a capacity-building nature. A survey of government officials in the CLMV countries by ERIA in 2012 (Intal, 2012) indicated that the IAI activities have generally been beneficial to the CLMV countries and have been largely well received there. The respondents indicated the programme can be improved through the tailoring of the training programmes to the specific needs and concerns of the CLMV countries, more realistic objectives for the specific projects, greater attention to institutional issues as well as to newer and emerging issues of interest to the CLMV countries, improved prioritisation of projects, greater coordination with the projects in CLMV of the dialogue partners, and greater CLMV ownership of the IAI projects (ERIA, 2012). Similarly, the report of the official midterm review of the IAI voiced concerns for the need to fine-tune the prioritisation process to be more attuned to the needs of the CLMV countries, the need for improving the coordination mechanisms internally and with the donor community involved in the Mekong Basin, and the need to enhance the ownership of IAI projects. The report also recommended the expansion of the project coverage of the IAI programme.

It is worth noting that the IAI, while relatively low budget and focused primarily on capacity building, may have had a salutary effect of signalling to the donor community the special bias of ASEAN for the CLMV countries to narrow the development gap with ASEAN-6. There has indeed been significant donor community support, including infrastructural support, to the CLMV countries, oftentimes in the context of the Mekong River basin development.

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It may be arguable whether the IAI has been a critical facilitating factor, but the CLMV countries (especially Cambodia, the Lao PDR, and Viet Nam) have been the more enthusiastic reformers for implementing the mandates of the AEC measures. They have been more enthusiastic liberalisers than several older AMSs. They have also been working hard on the facilitation initiatives, although they face constraints on financing for some initiatives, such as the National Single Window (NSW). While some facilitation environments are less favourable, such as in trading across borders, there have been substantial improvements.

Domestic reforms, improved institutional capacity, and better infrastructure have led to remarkable increases in FDI. Each CLMV country has registered higher growth rates than ASEAN-6 since the early 2000s. The CLMV story is certainly a success story for ASEAN and a great example for the developing world, especially Africa.

The other important AEC measure towards a region of equitable development is SME development. SME development has received nearly constant emphasis by the country hosts of the ASEAN summits. This reflects the high importance that ASEAN leaders give to SME development in their own countries and the region. This is not surprising because about 89% to nearly 100% of firms in ASEAN countries are SMEs. They also account for the predominant share of total employment, although their shares to national output and exports are decidedly less. Because of their centrality in creating jobs and the sheer numbers, SME development is a strategic measure towards a more inclusive growth and development in an integrating ASEAN region.

The ASEAN Strategic Plan for SME Development 2010–2015 focused on enhancing the internationalisation of SMEs, improving their access to finance, achieving human resource development, encouraging incubators for SMEs, establishing SME service centres, and establishing the ASEAN SME Development Fund. While the goals were noteworthy, the action plan was not cohesive. However, the successor action plan, the ASEAN Strategic Action Plan for SME Development 2016–2025, effectively addressed this issue. Nonetheless, several significant initiatives have brought the cause of SME development forward in recent years. Perhaps the most important are the series of SME trade/business fairs that have been undertaken by the Member States or business groups themselves in support of the ASEAN community-building and integration efforts.

The other significant initiatives include the development of the ASEAN SME Policy Index jointly with ERIA and the Organisation for Economic Co-operation and Development (OECD) that is meant to be a tool for generating a better policy
environment for SME development, the development of the methodology for an ASEAN benchmark for SME credit rating, and the study on the strengthening of the SME business and technology incubators. ASEAN has also started putting together the outstanding and innovative SMEs in the region. These initiatives are a good foundation for implementing the ASEAN Strategic Action Plan for SME Development 2016–2025, arguably a much better document than the previous one. This is discussed further in Volume 5, which focuses on the AEC into 2025.

**Pillar four: integration into the global economy.** The AEC Blueprint 2009–2015 is very thin with respect to pillar four, with the stated measures being a coherent approach to international economic relations and enhanced participation in global supply networks. Despite this, ASEAN has been strengthening its economic relations with its partners especially the ‘+6 partners’ (Australia, China, India, Japan, New Zealand, and the Republic of Korea [henceforth, Korea]) through the ASEAN+1 FTAs. ASEAN is also at the centre of current negotiations for the Regional Comprehensive Economic Partnership (RCEP), which is hoped to be finalised and signed in November 2017 during the ASEAN Summit. The issue of the ASEAN FTAs and RCEP is discussed further in Volume 5. Nonetheless, it is worth concluding the discussion on pillar four and concluding this chapter by highlighting what Figure 3.3.5 suggests: AMSs would benefit a lot more by integrating with ASEAN+3 (China, Japan, and Korea) and with RCEP than with the AEC solely.

![Figure 3.5. Economic Impact of ASEAN’s FTA and Five ASEAN+1 FTAs](image)

**Figure 3.5. Economic Impact of ASEAN’s FTA and Five ASEAN+1 FTAs**

(percentage points, accumulated from 2011 to 2015)

ASEAN = Association of Southeast Asian Nations, CJK = China, Japan, and the Republic of Korea, FTA = free trade agreement.

Chapter 4
The ASEAN Member States and ASEAN Economic Integration

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The pace and success of the ASEAN economic integration ultimately lie in the willingness, pace, and success of ASEAN Member States (AMSs) in opening up, undertaking domestic policies consistent with deepening economic linkages with the rest of ASEAN and the world, and benefiting from the integration process. As the country essays in this volume bear out, the ASEAN economic integration story contributed to and benefited from the remarkable economic transformation of ASEAN’s newest members while at the same time gradually shaped and is being shaped by the more measured and halting opening up and integration efforts of its original members. How the regional initiatives and the domestic imperatives interact and weave together in the context of a fast-changing international economic and technological environment would likely largely determine the pace and future of ASEAN economic integration.

ASEAN’s New Members: Remarkable Success Story

A significant part of the diplomatic and economic glow of ASEAN during the past 2.5 decades stems in part from the remarkable political–security and economic transformation of ASEAN’s newest four members, namely, Cambodia, the Lao PDR, Myanmar, and Viet Nam – or the CLMV countries. Once the principal theatre of conflict in Southeast Asia in the 1970s and 1980s, and for Cambodia’s internal discord into most of the 1990s, the CLMV countries would become the economic growth leaders of ASEAN from the late 1990s to the present. In addition, they would become the more aggressive economic liberalisers and integrators in the region. In this remarkable economic transformation and success story, ASEAN has been both a co-driver and
a handmaiden, highlighting the interplay of regional integration initiatives and the domestic policy imperatives that characterise ASEAN economic integration.

Cambodia. ASEAN’s newest member, Cambodia, is also one of ASEAN’s most remarkable transformations. Chap Sotharith, in his essay in the volume, puts it well: ‘… once a failed state with civil war, genocide, and political turmoil … [Cambodia] has been transformed from a centrally planned economy into a free market economy … and from a battlefield on the verge of destruction into a country of emerging development [that is] increasingly … becoming integrated into the regional and global community.’

ASEAN played a key role in Cambodia’s transformation. ASEAN helped bring peace and stability to Cambodia, highlighted by the 1991 Paris Peace Accords and ASEAN’s backroom efforts supporting domestic political reconciliation within Cambodia in the 1990s. The 1991 Paris Peace Accords raised significantly the international diplomatic standing of ASEAN. They also arguably helped ASEAN get the support of the Big Powers in the region to take the central facilitating role in the regional security architecture through initially the ASEAN Regional Forum since the mid-1990s and the subsequent institutions like the East Asia Summit since the mid-2000s. Cambodia’s membership in ASEAN effectively erased the country’s international isolation. Its participation in the ASEAN Free Trade Agreement (AFTA) and the ASEAN Economic Community (AEC), together with its accession to the World Trade Organization (WTO) in 2004, would cement Cambodia’s outward-oriented structural reforms and drive for integration into the regional and international economies.

According to Sotharith, Cambodia accelerated domestic institutional and legal reforms in many fields to prepare for WTO admission and in line with ASEAN, e.g. public administration reform, economic management, judicial reform, financial reform, good governance and promotion of transparency, public–private partnership. Investment and trade reforms were noteworthy as trade became an important instrument for economic development. Cambodia has become one of the most aggressive liberalisers in ASEAN. The country has virtually become the most open AMS in terms of foreign equity in both manufacturing and services. On trade policy, Cambodia reduced dramatically its intra-ASEAN tariffs consistent with AFTA/AEC, streamlined the structure of most-favoured-nation (MFN) tariff rates and gradually reduced the average MFN rate, and established a national committee on non-tariff measures (NTMs). Cambodia is also in the process of implementing the trade facilitation initiatives under the AEC blueprint such as the National Trade Repository but more slowly the National Single Window (NSW) because of the inadequacy of financial resources and trained personnel to undertake well such initiatives. Cambodia has one of the most open investment regimes, with more than 90% of all manufacturing, agriculture, and mining sectors open to 70% or more of foreign
equity (see Figure 3.4). Similarly in the services sector, Cambodia's overall liberalisation rate for ASEAN Framework Agreement on Services (AFAS) 9 commitments is among the highest, second only to those of the Lao PDR and Myanmar. Cambodia is benefiting from the various subregional and regional programmes on enhancing physical connectivity in the Mekong Region that the donor community and ASEAN dialogue partners – like Japan, China, and the Asian Development Bank – substantially fund. Cambodia is also benefiting from various capacity-building programmes for the CLMV countries that the donor community and ASEAN support.

The result of peace, domestic structural reforms that led to great openness to trade and foreign investments, improved infrastructure and physical connectivity with its neighbours, and strengthened institutional capacity has been tremendously positive for Cambodia. The annual net inflow of foreign direct investment (FDI) increased from about US$54 million in 1993 to about US$1.9 billion in 2015, or from 2.3% of GDP in 1993–1994 to about 9.7% in 2014–2015. Indeed, the FDI inflow per population ratio is much higher than the ASEAN regional average. As much of this FDI is also export oriented, total trade as a percentage of Cambodia’s GDP increased substantially from 56% in 1995 to 106% in 2015. Cambodia is slowly becoming part of the regional production networks.

An important aspect of Cambodia’s trade performance is the sharp redirection of its export flows, with a greater percentage of exports going to non-ASEAN countries as implied in the marked decline in the share of ASEAN in Cambodia’s exports (see Table 2.5) because the country’s main exports of garments are primarily geared for the United States (US) and European Union markets where the country has Generalized System of Preferences (GSP) privileges¹. Thus, interestingly, Cambodia’s liberalisation drive as part of the AEC resulted in the country being more integrated with the rest of the world, a reflection of the ‘open regionalism’ espoused in ASEAN.

In addition to the surge in exports of manufactures, Cambodia’s tourism boomed. International tourist arrivals rose dramatically from 220,000 in 1995 to 4.77 million in 2015. Estimated tourism receipts grew from US$100 million in 1995 to US$3.0 billion in 2015. Exports of agricultural products, specifically rice and rubber, also expanded robustly in recent years.

¹ The data are official figures. It is known that substantial informal, unofficial trade occurs between Cambodia and Thailand. Thus, the share of ASEAN to total Cambodia trade is underestimated.
Not surprisingly, Cambodia has experienced one of the fastest economic growth rates in the world of more than 7% per year since 1986. Cambodia has turned from a poor and troubled least-developed country to a robustly growing and transforming lower middle-income country. Despite such remarkable success, Chap Sotharith highlights several significant challenges that the country faces. These include the large development gap between Phnom Penh, provincial capitals, and rural areas; the pervasiveness of NTMs; low productivity and product quality amidst intensifying market competition; poor logistic and transport system; and the limited capacity, human capital, and entrepreneurship to propel the country towards a much more diversified economic structure than what it is at present.

Nonetheless, the challenges above are themselves seeds of opportunity. Arguably, just as ASEAN was an important catalyst and facilitator of the political stabilisation and economic reforms in the country, the implementation of the AEC Blueprint 2025 and the Master Plan on ASEAN Connectivity 2025 – with their special focus on good governance, regulatory excellence, and institutional connectivity, among others – could provide the environment for the private sector and the government to undertake complementary efforts to address the challenges stated above. And as Chap Sotharith indicates, addressing those challenges would enable Cambodia to maximise the benefits from regional integration.

Lao PDR. ASEAN has also been important in the transition of the Lao PDR from a relatively closed and planned economy to an open market economy. Before it became a member of ASEAN in 1997, the Lao PDR had a centrally planned economy under the ambit of the former Soviet Union in 1975–1986, followed by a transition towards a market economy in 1986–1997. ASEAN’s admission of the Lao PDR accelerated the process of warming relations with its ASEAN neighbours and the process of economic liberalisation under AFTA and eventually the AEC. As a small and landlocked country surrounded by four AMSs and China, the Lao PDR’s economic fortune is necessarily affected by the stability and economic fortunes of its four ASEAN neighbours and China. As Leebuoapao and Sayasenh in their essay in this volume points out, ASEAN is the ‘golden opportunity’, the nearest and biggest market for the Lao PDR both for export and import, in particular Thailand and Viet Nam. Thus, not surprisingly, the Lao PDR sees ASEAN membership as a safeguard to ensure peace, security, and economic opportunities for its development.

Leebuoapao and Sayasenh highlight that the Lao PDR has been adjusting its economic policy in accordance with the AEC blueprint, with emphasis on trade liberalisation and facilitation, as well as with the requirements for WTO accession. Among the policy actions are the adoption of the ASEAN Harmonized Tariff Nomenclature 2012,
together with the other AMSs; reduction and near elimination of intra-ASEAN tariffs following its commitments under the ASEAN Trade in Goods Agreement; granting of preferential tariffs under the ASEAN+1 FTAs, etc. As in Cambodia, implementation of trade facilitation measures has been challenging due to limited financial resources and inadequate institutional capability. Also, the Lao PDR’s commitments to the ASEAN investment and services liberalisation agreements (under the ASEAN Comprehensive Investment Agreement and AFAS, respectively) are among the most liberal among the AMSs. Indeed, for the latest AFAS 9 commitments, the Lao PDR and Myanmar share the highest liberalisation rate among the AMSs (see Table 3.1).

The result of the openness to trade and FDI can be seen in the sharp increase in both trade and foreign investment over time. The value of total trade exploded from US$213 million in 1990 to US$10.35 billion in 2015; the total trade-to-GDP ratio increased from 23% in 1990 to about 83% in 2015, using World Bank estimates. Most of Lao exports are in electricity and minerals, with the latter vulnerable to global price fluctuations. Not surprisingly, the share of trade to GDP has fluctuated significantly during 2011–2015 for example. Among the AMSs, the Lao PDR is the most dependent on ASEAN for its international trade, with ASEAN accounting for about 70% of its exports. ASEAN, essentially Thailand and Viet Nam, is also the main channel for the robustly growing tourism sector.

Electricity generation and mining are capital intensive. The capital-intensive nature of the Lao PDR’s main exports shows the critical importance of the country’s liberalised investment regime. FDI into the country increased markedly in recent years, raising the ratio of FDI to GDP from about 4.7% in 2010 to around 8.5% in 2015. The high growth of FDI, tourism, and international trade translated into a very robust economic growth rate, with the Lao PDR having the highest economic growth on average among the AMSs in the latter 2000s and into early 2010s.

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2 There is substantial difference in the estimates of the foreign trade-to-GDP ratio for the Lao PDR. The ASEAN Secretariat, in its ‘ASEAN Community in Figures 2016’, estimates the trade-to-GDP ratio for the Lao PDR in 2015 to be 53.5%, which is much smaller than the World Bank’s 82.9%. Behind this large difference is the estimate of imports into the Lao PDR. The ASEAN Secretariat relies on the official submissions of the AMSs whereas the World Bank estimates (and those of the International Monetary Fund [IMF]) include information from partner countries of the Lao PDR (mainly Thailand, China, and Viet Nam), i.e. export data to the Lao PDR from these countries. The gap between the two estimates arises primarily from the import estimates, with the World Bank/IMF estimates much higher than the official import data. This suggests that there is either large under-declaration of imports in the Lao PDR (i.e. technical smuggling) or there are large informal (from the Lao PDR’s perspective) imports into the Lao PDR (outright smuggling) or informal export and import trade between the Lao PDR and its neighbours (which is probable given that the border is mainly a river between Thailand and the Lao PDR, for example, and the people in northern Thailand are culturally close to the Lao people).
**Myanmar.** Myanmar is a recent significant diplomatic success for ASEAN. Instead of sanctions against Myanmar that many Western countries resorted to, ASEAN engaged and quietly encouraged the former military rulers of Myanmar over the years to democratise the country. The ascension of the neo-civilian government under President U Thein Sein led to major and wide-ranging reforms in the country, complemented by the lifting of the sanctions against investments in and trade with Myanmar. The successor civilian government, led by State Counsellor Daw Aung San Suu Kyi and President U Hin Kyaw, is continuing the reform process. The wide-ranging reforms were shaped partly in the context of ASEAN, especially the AEC Blueprint 2015, but have been strongly facilitated and supported by major international multilateral institutions such as the World Bank, the International Monetary Fund (IMF), and the Organisation for Economic Co-operation and Development (OECD) as well as by major bilateral donors like Japan. The successful hosting by Myanmar of the ASEAN Summit in 2014 is an affirmation of the dramatic political, diplomatic, and economic reforms in the country consistent with the overall regional thrusts of the ASEAN integration and community-building efforts.

In terms of commitments, Myanmar is indeed one of the leading liberalisers in ASEAN as shown in Figures 3.3 and 3.4 for services and investment. Similarly, intra-ASEAN tariff reduction and eventual elimination have been moving apace. Myanmar also agreed on other AEC measures including, for example, trade facilitation measures. The challenge is in the implementation. Some domestic reforms are related to the implementation of the measures. For example, the country’s customs law since the late 1940s was updated to be consistent with the World Customs Organization Kyoto Convention provisions that are the backbone of modern customs administration and which underpin the ASEAN customs modernisation and single window initiatives. Implementation also entails improvement in the capacity of institutions tasked to implement the domestic measures consistent with and supportive of ASEAN measures and other domestic policy imperatives. Domestic reforms and capacity building are ongoing.

The end result so far has been sharply expanding FDI inflow, robustly growing foreign trade, and surging foreign tourist inflow. Myanmar is now the fastest-growing economy in ASEAN.³

**Viet Nam.** Viet Nam has the enviable achievement of having the highest average growth rate in ASEAN since the mid-1990s. Indeed, the country has one of the highest average growth rates in the world during 1996–2015. This meant a remarkable economic

³ Note that the country essay on Myanmar is not included in the volume because the country author could not finish it due to health reasons.
transformation into a major global exporter of agricultural products such as rice, coffee, and fish as well as an emerging manufacturing hub in East Asia. The country experienced one of the sharpest declines in poverty rate in the world, arguably only second to China. Underpinning this remarkable success story is the positive interplay of aggressive domestic reform and proactive international economic integration efforts backed by solid human capital and infrastructure investments. Like the other new members of ASEAN, and indeed much more so, the sharp rise in foreign trade (with Viet Nam now having the second-highest trade-to-GDP ratio in ASEAN) and FDI has been central to Viet Nam’s economic dynamism.

ASEAN contributed to Viet Nam’s economic dynamism even as the country’s domestic reform efforts have gone on earnest since the mid-1980s under Doi Moi (renovation). As Vo Tri Thanh highlights in his essay in this volume, ‘…ASEAN integration has marked an essential first step towards international economic integration’ for Viet Nam. Viet Nam joined ASEAN in 1995, and joined AFTA in 1996. The next decade would see the country signing the Viet Nam–US bilateral agreement in 2000 and joining the WTO in 2007. These two landmark events had a major impact on Viet Nam. The first led to a sharp rise in trade with the US; the latter forced Viet Nam to undertake amendments or promulgate many laws, ordinances, and decrees to meet WTO commitments. The next decade would find Viet Nam even more aggressive in regional and bilateral trade agreements, both signed and under negotiations: (i) under ASEAN, through the ASEAN+1 FTAs, the AEC and the ASEAN Community, and the Regional Comprehensive Economic Partnership (RCEP); (ii) under bilateral agreements like the Japan–Viet Nam Economic Partnership Agreement, Viet Nam–Eurasian Economic Union FTA, and the EU–Viet Nam FTA; and (iii) under regional agreements like the Trans-Pacific Partnership. Thus, ASEAN integration paved the way for the wide range of integration agreements that Viet Nam signed with many other countries.

Vo Tri Thanh observes that ASEAN integration induced institutional reforms in Viet Nam, particularly in the areas related to trade and investment. For instance, in line with the implementation of the AEC Blueprint, the country developed the NSW in 2005 under the ASEAN integration framework and got it connected to the ASEAN Single Window (ASW) in 2015. The progress in customs modernisation mirrors the government’s strong political willingness to foster economic integration. This reaffirms international donors to support its reform. Learning from advanced AMSs, Viet Nam also launched a policy package (Resolution 19) to improve its business environment aiming for the standards of ASEAN.

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4 This paragraph and the next draw heavily from Vo Tri Thanh’s essay in this volume.
Vo asserts that ASEAN holds the highest importance for Viet Nam, despite the many FTAs it has signed with other countries. This is because the gradualist nature of ASEAN integration is more consistent with Viet Nam’s development level; ASEAN initiatives are more comprehensive as they involve the three ASEAN communities; and ASEAN has a growing role in international and regional initiatives, such as the East Asia Summit. Nonetheless, a key challenge for Viet Nam is to ensure that the various FTAs it has signed are harmonised and do not conflict with the interest of the country.

**ASEAN and the Older ASEAN Six: Concerted Goading and Facilitation**

If the role of ASEAN in the newer CLMV countries is relatively straightforward, the interaction between ASEAN and the six older AMSs\(^5\), especially in the economic field, is more complex. Included among the factors behind this complexity are more assertive parliaments of most ASEAN-6 countries and more complicated political economy considerations for losers and winners from liberalisation. The ASEAN-6 are a highly varied lot, ranging from an active globalist and international pacesetter on the one hand and a reluctant regional integrationist despite robust regional diplomatic leadership on the other. In short, the AEC is as much shaped by, as it is shaping, the AMSs.

**Singapore.** The quintessential globalist, Singapore nonetheless shows us an example where ASEAN’s goals are in line with an AMS’s national interests; and the country can eventually gain from what it contributes to regional integration. As a small country lacking natural resources, Singapore needs ASEAN to foster regional political and security stability. Different from the CLMV countries, it is concerned more with vulnerability from an unfavourable external political and security environment.

Hank Lim discusses in his essay the importance of ASEAN to Singapore by dividing the country’s development into four phases. The Singapore story shows us how a small city-state managed to link domestic growth via its efforts of pushing forward the process of ASEAN integration and achieving economic success. To countries like Singapore, it seems clear that an open and competitive economy works as the base for its development and prosperity. For that reason, deregulation and trade liberalisation seldom see domestic resistance. The country has been actively accelerating and deepening the process of ASEAN integration, advocating and promoting ASEAN internationally, and providing technical and financial assistance to CLMV on capacity.

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\(^5\) These are Singapore, Brunei Darussalam, Indonesia, the Philippines, Malaysia, and Thailand.
building. On the other hand, ASEAN integration provides Singapore (i) a safeguard on regional security and stability, (ii) a regional single market as an external wing for its economy, and (iii) a strengthened position as a regional hub for multinational corporations and FDI.

Singapore has a two-pronged approach to its external economic policy. In addition to actively promoting closer economic integration in ASEAN, Singapore has also been emphasising closer economic relations with many non-ASEAN countries. In fact, it has been the most active among AMSs in negotiating FTAs with many non-ASEAN countries because Singapore, being a tiny city-state, is driven by foreign trade (in goods and services). Hank Lim provides a positive spillover effect to ASEAN of Singapore’s deep economic engagement with the rest of the world; and it could:

...spur other ASEAN economies to liberalise and deregulate their economies in the global marketplace [as]...Singapore’s proven success in its bilateral and plurilateral FTAs with non-ASEAN economies has given a strong impetus for other ASEAN countries to emulate Singapore’s FTA policies. In turn, the more open and successful other ASEAN economies become, the more receptive and likely they are to accept Singapore’s initiative for wider and deeper ASEAN economic integration.

For Singapore (with its tiny domestic market and no natural resources) to compete well with such deep economic linkages with so many countries worldwide, it must have top-flight infrastructure and global connectivity, a global pacesetting trade facilitation environment, effective governance and ease of doing business, and forward-looking human capital investments. And indeed, tiny Singapore has become, as one well-known business network puts it, a global trade colossus. Arguably, more than Singapore’s success with its FTAs, as Hank Lim avers, are the domestic measures Singapore has been undertaking to succeed in international competition that have been the important learnings to emulate as a spillover effect to ASEAN countries. A reading of the AEC Blueprint 2025 and national programmes of several AMSs suggests the growing emphasis on improving governance and ease of doing business, trade facilitation, infrastructure, regulatory institutions, etc. All these are consistent with the direction towards the Singapore experience, albeit considering the resource constraints the AMSs face.
**Brunei Darussalam.** As the smallest AMS of about 400,000 people, Brunei Darussalam has embraced ASEAN fully – from its long-serving Sultan Bolkiah (ASEAN’s longest serving leader) to its citizens – as the results of the survey on what ASEAN means to ASEAN peoples\(^6\) indicate. Joyce Teo, in her essay on Brunei Darussalam in this volume, shows that Bruneian small and medium-sized enterprises (SMEs) have benefited from their access to a much larger regional market. She also indicated the domestic and policy reforms undertaken with regional initiatives, such as on competition policy and consumer protection. She further pointed out that ASEAN’s emphasis on SME development initiatives also benefited Brunei’s SMEs.

Just as Brunei Darussalam benefited and will benefit from ASEAN, Joyce Teo also highlights the actual and potential contribution of the country to ASEAN. Perhaps foremost is the constructive role of Brunei for its neutral position that allows the country to undertake trust and confidence-building measures as exemplified by the South China Sea issue during its most recent ASEAN chairmanship. Another is the essential congruence of AEC initiatives and Brunei’s outward-oriented strategies, the country being a small and open economy with pro-progress policies. Another possible contribution of Brunei to ASEAN is as a bridge between ASEAN and the Commonwealth group of nations, of which Brunei Darussalam is a member; similarly, as a leader in the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA).

Finally, while Brunei has embraced ASEAN, it has not yet fully embraced the potentials of the association for the country. Specifically, although Brunei is the second-richest in ASEAN country, it has been the slowest growing among the AMSs for some time. This reflects the overdependence of the economy on oil and gas whose global prices have been volatile and low in recent years. The fact that the domestic market is extremely small means that an effective diversification of the economy would call for Bruneian firms, large and small, to be more deeply integrated into the ASEAN economy and business milieu. This means Brunei and its firms should know their niches and work with ASEAN firms and institutions to provide services and goods for the regional market, not just for the Brunei market. This clearly calls for the Brunei business sector to have an ASEAN market perspective rather than one focused on Brunei Darussalam’s tiny domestic market. The results of the face-to-face interviews reported in Joyce Teo’s essay suggest that there are ASEAN-oriented members in the business sector. It may well be that Brunei Darussalam needs to encourage more of them as a way forward for the country’s diversification growth strategy.

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Indonesia. As the largest economy and most populous country in ASEAN, it is not surprising that Indonesia has greatly impacted the pace of the ASEAN economic integration project. Nonetheless, the ASEAN integration initiatives have also helped shape Indonesia’s domestic policies. This interplay of the design and implementation of ASEAN initiatives and the domestic policy environments in the AMSs can be considered as at the heart of the essential characteristic of the ASEAN integration agenda. This is a much more measured (although criticised as slow) liberalisation and integration process against which there is no significant backlash.

Thus, early proposals in the mid-1970s for ASEAN economic integration were nixed in favour of industrial economic cooperation and preferential tariffs. At that time, Indonesia preferred an import substitution policy and a more inward-looking development strategy as Yose Rizal Damuri notes in his essay on Indonesia in this volume. Indeed, the word ‘integration’ was deemed taboo in ASEAN until the 1980s. As noted in Volume 1 of ASEAN@50: The ASEAN Journey: Reflections of ASEAN Leaders and Officials (Pitsuwan et al., 2017), the ASEAN industrial cooperation programme largely failed and the preferential tariffs were inconsequential. Necessarily, as Damuri highlights, Indonesia’s early initiatives towards economic openness were unilateral. Those were in response to adverse external developments, most importantly the fall in the global price of oil in the early 1980s, Indonesia’s main export product during the 1970s and 1980s. Those early liberalisation initiatives – such as reduction in tariffs and non-tariff barriers (NTBs) especially in labour-intensive manufacturing together with customs reforms – have facilitated the surge in Indonesia’s exports of labour-intensive manufactures since the latter 1980s. During the ASEAN Economic Ministers Meeting in December 1989 in Bandar Seri Begawan, Indonesian economic officials agreed that it was time for ASEAN to explore deeper economic cooperation in ASEAN in response to the growing regionalism worldwide. In the next 2 years, ASEAN would agree on an integration project, AFTA, anchored on the Indonesian Common Preferential Tariff (CEPT) proposal, and launched it in 1992.

AFTA, the WTO’s Uruguay Round, the Asia-Pacific Economic Cooperation (APEC) forum, and the structural adjustment programme in the aftermath of the 1997–1998 Asian financial crisis have all contributed to the furthering of liberalisation efforts of Indonesia. Damuri shows the strong correlation between the tariff reductions under CEPT and MFN rates, which he surmises as suggestive of the AFTA CEPT programme influencing the overall tariff reduction programme of the country in the late 1990s and early 2000s. Indonesia’s commitments in the WTO on bindings on tariffs and selected service sectors, reduction of NTBs, and elimination of quantitative restrictions, among

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7 Based on personal interview with Ambassador Delia Albert of the Philippines.
others, were all complementary to the AFTA initiatives. Similarly, the tariff reductions and/or removal of NTBs in sensitive products and industries, and services liberalisation under the IMF structural adjustment programme were also all complementary to the AFTA initiatives. Through AFTA, and eventually the AEC, ASEAN would deepen its facilitating role to Indonesia’s domestic reform programme to include ASEAN trade facilitation initiatives like the NSW, the National Trade Repository, and air transport liberalisation initiatives under the Roadmap for Integration of Air Travel Sector. The AEC Blueprint 2025 can be expected to continue the facilitating role of ASEAN in Indonesia’s domestic reform programme with deepening commitments on a large range of liberalisation and facilitation areas and to even wider areas of cooperation such as good regulatory practice. Thus, on the whole, the concert of ASEAN, the WTO, APEC, and the IMF provided the external driving force for Indonesia to move further in its economic opening up in the 1990s and early 2000s. Since then, ASEAN has been largely a goad for reform, as part of a concerted regional programme, in areas that Indonesia itself (and similarly, other AMSs) has been wont to undertake in the face of tight global competition for markets and investments.

Indonesia’s trade with the rest of ASEAN has been expanding robustly. As Table 2.5 shows, ASEAN’s share to total Indonesian merchandise exports rose from 10% in 1990 to 17.5% in 2000 and 22.3% in 2015. The share of ASEAN to total Indonesian merchandise imports rose from 8.4% in 1990 to 19.4% in 2000 and 27.5% in 2015. This apparent trade imbalance for Indonesia vis-à-vis ASEAN has led to, as Damuri notes in his essay, ‘…[a] general suspicion that AFTA was less beneficial to Indonesia, at least in terms of trade’. Damuri explains the trade deficit in terms of low ASEAN Trade in Goods Agreement utilisation rate by Indonesian firms and the growth of ASEAN-sourced inputs to Indonesia’s manufactured exports as part of the production networks in the region. Possibly two other factors would complement and strengthen Damuri’s explanations. The first is the rise of ASEAN-sourced inputs for manufactures sold in the domestic market (e.g. parts for cars assembled and sold in Indonesia). The second is the composition of Indonesia’s exports, which remains substantially consisting of commodities geared primarily for non-ASEAN markets.

Sound explanations notwithstanding, there is such a ‘general suspicion’ of AFTA being less beneficial to Indonesia. And it is likely the presence of such general suspicion that appears to have made Indonesia more cautious and less willing to push further on deeper liberalisation initiatives in ASEAN, especially as they increasingly touch on more sensitive sectors of the economy. It is worth noting that the negative trade imbalance vis-à-vis ASEAN is even worse for countries like the Philippines and Cambodia than Indonesia, but without apparent public push for protection against imports from ASEAN. Perhaps by emphasising more what Damuri asserts in his essays that ‘protectionist policies
have cost Indonesian society very dearly’, would Indonesia become more engaged in implementing the deeper integration and cooperation programme embodied in the AEC 2025.

**Philippines.** The Philippines underwent wrenching domestic macroeconomic, trade, and industrial policy reforms and adjustments under a series of IMF and World Bank programmes for about 2 decades in the aftermath of the economic crisis in the country in the early to mid-1980s. No other AMS experienced such wrenching adjustments for so long. The structural adjustments of the transition economies of Cambodia, the Lao PDR, and Viet Nam in the latter 1980s and 1990s were largely efficiency enhancing and foreign investment attracting. In contrast, opening up the Philippine economy with comparatively high wage costs from long decades of industrial protection and in a fragile macroeconomic environment proved far more disruptive to the Philippine manufacturing sector and the overall economy during most of the latter 1980s until the early 2000s. Only in the last decade or so has the Philippines righted itself macroeconomically, and its underlying comparative advantage has shone and become potent. As a result, the mediocre economic performance of the 1980s through the early 2000s changed to sustained robust growth with markedly rising foreign investments in recent years. And the contentious debates in the latter 1980s between protectionism and openness have now been transformed into a nationally agreed industrial strategy ('Manufacturing Resurgence Program'): an open manufacturing sector is a given to compete better in an integrated ASEAN and more open East Asia.

In his essay in this volume on the Philippines, Gilbert Llanto presents the evolution of Philippine trade policies from the protectionist, inward-looking policy of the 1950s–1970s towards the increasingly outward-looking and more open trade regime from the latter 1980s onwards. While the liberalisation initiatives were initially unilateral under the IMF/World Bank programmes, AFTA, the WTO Uruguay Round, and APEC all played a part in the trade and industrial reforms of the 1990s. ASEAN, through AFTA and then the AEC and facilitated by APEC, has deepened its influence on the domestic policies of the countries since the early 2000s. Llanto presents several examples where ‘... ASEAN has influenced and provided impetus to the crafting of better policies, programmes, and regulations’. Examples include the (i) establishment of the NSW (and relatedly, the National Trade Repository); (ii) services liberalisation and the mutual recognition arrangements (MRAs) on several professional services as well as the ASEAN (and Philippines) Qualifications Reference Framework; (iii) liberalisation of banking services; (iv) alignment of quarantine and inspection procedures of Philippine fisheries with ASEAN and international standards; and (v) reduction in regulatory burden on firms. Indeed, many more are not cited in Llanto’s paper, e.g. signing on ASEAN’s open skies policy, standards and conformance measures such as MRAs in priority goods.
sectors like electronic and electrical machinery, and harmonised technical regulations and requirements as in cosmetics.

The role of ASEAN for the Philippines appears like a mirror image for Indonesia, i.e. as a driver of trade reform together with the WTO and APEC in the 1990s and early 2000s, and as a facilitator and goader for the broader set of domestic reforms consistent with the measures in the AEC blueprints. ASEAN integration has impacted the direction of Philippine merchandise trade primarily in the sourcing of inputs because Philippine exports have become more geared to Northeast Asia, as Llanto’s essay shows. Like Indonesia, the Philippines has a trade deficit with ASEAN. Unlike Damuri’s observation for Indonesia, there does not appear to be any general suspicion that ASEAN has been less beneficial to the Philippines with a pressure for increased protection against imports. Instead, the increased pressure has been for improvement in infrastructure, governance and processes, and regulatory regime in the country for it to be more attractive to investors, and for domestic firms to be more competitive in both domestic and foreign markets, and thereby reap the benefits from economic integration.

**Malaysia and Thailand.** Malaysia and Thailand are the two upper middle-income countries in ASEAN, with Malaysia very close to being a high-income country. In contrast to ASEAN’s high-income city-states, both Malaysia and Thailand have a considerable domestic market to build on and grow outward into the region. The essays on Malaysia and Thailand in this volume bring out a key rationale for the AEC agenda; that is, to provide the private sector the supportive environment to adjust and grow, meet the challenges of, and reap the benefits from deeper economic linkages and integration in the region. After all, an integrated regional market brings about larger market potential, more job opportunities, greater economic attraction to foreign investment, and therefore more space for development. Ideally, reaping the benefits of economic integration has a greater chance if national policies and the ASEAN regional initiatives are congruent.

Saowaruj Rattanakhamfu shows the impact of ASEAN on Thailand through the increased trade, investment, and labour flows. Thailand increased its import sourcing from ASEAN; the region is now the second-largest import source after China. Thailand also expanded tremendously its exports to ASEAN; indeed, ASEAN has been Thailand’s largest export market, replacing the United States, since 2003. Thailand now has a large merchandise trade surplus vis-à-vis ASEAN. The reduction and eventual elimination of intra-ASEAN tariffs and ASEAN’s rules of origin facilitated the marked rise in Thailand’s trade with its ASEAN neighbours.
Although not discussed in Rattanakhamfu’s essay, the rise of Thailand as the automotive hub of ASEAN exemplifies how economic integration helps an industry grow. Thailand was the primary beneficiary of the export-oriented foreign investment flow from Japan to ASEAN in the aftermath of the yen appreciation in the mid-1980s that was induced by the Plaza Accord. The resulting high growth rate meant a surge in domestic demand for vehicles which, together with massive infrastructure investments especially in the Eastern Seaboard, enticed Japanese, American, and other multinational corporation assemblers and suppliers to set up plants in Thailand for the domestic and foreign markets. This ‘first mover advantage’ with a robust domestic supply chain became even more important as intra-ASEAN tariffs on automotive products were drastically reduced for enhanced market access to a robustly growing market. With economies of scale and increasingly more extensive regional production networks, the Thailand automotive industry has become export competitive not just regionally but also globally. It is now a major industry of Thailand.

ASEAN is also important in Thailand’s direct investment inflow and outflow. Rattanakhamfu notes that the region has been the second-largest source of FDI after Japan during 2005–2015. She also notes the surge in Thailand’s outward direct investment to ASEAN since the Bank of Thailand eliminated in late 2010 the ceiling on Thai investment abroad. The investments have gone primarily to Singapore and to the CLMV countries. The investment in the CLMV countries is noteworthy because the liberal investment regimes in these countries (discussed in the previous chapter) are enabling the Thai private sector to develop supply chains in the Mekong subregion, with Thailand as the hub. This is similar to the ‘Thailand Plus’ strategy that multinational corporations seem to be developing in the area, with their Thailand plants as the hub. Such a process has evolved partly because of the regional integration initiatives in ASEAN.

Labour flows, overwhelmingly unskilled, are also an important pillar of Thailand’s linkage with ASEAN. Of 1.33 million workers, only about 23,000 of them are semi-skilled and skilled. Given Thailand’s ageing population, the foreign labour force has been important for the country’s many industries, especially the tourism and food-related industries. Rattanakhamfu notes that there is no ASEAN-wide agreement on the movement of unskilled labour in ASEAN, yet a huge number, primarily from neighbouring Myanmar, Cambodia, and the Lao PDR, are working in Thailand. In contrast, despite several ASEAN MRAs on professionals, there are comparatively few semi-skilled and skilled workers in Thailand, and most of them were not hired under the ASEAN MRA process. Indeed, implementation of the MRAs in Thailand faces many problems. This issue of constraints to the implementation of the ASEAN agreements is discussed further in the next subsection. What the contrasting cases of foreign unskilled versus skilled labour in
Thailand suggest is that the imperatives of the market sometimes trump official regional agreements, and bilateral agreements may be sufficient.

Nonetheless, economic integration is better managed if the national policies and programmes of the AMSs and the regional integration programme under the AEC are congruent.

Nambiar highlights that Malaysia’s strategies and programmes in the Eleventh Malaysia Plan and the New Economic Model are indeed very much aligned with the AEC blueprints. This is because trade and investment have been the cornerstone of Malaysia’s economic development and continual economic transformation towards becoming a high-income country. As Nambiar emphasises, the various transformation programmes are meant to strengthen the national foundations that can take advantage of the external environment facing the country. At the same time, as a small, open economy, Malaysia manages its external environment largely through FTAs and the AEC. Malaysia gives high importance to ASEAN and the AEC, as reflected by the fact that the ASEAN division of the Ministry for International Trade and Industry is the largest. More importantly, Malaysia sees ASEAN and the AEC as one collective entity, which now ranks as the sixth-largest economy and the third-most populous in the world.

An example of the congruence of Malaysia’s strategy and the AEC is the liberalisation of services under AFAS. As Figure 3.3 and Table 3.1 show, and as Nambiar details in his essay, Malaysia has liberalised more of its services sector compared to Indonesia, the Philippines, and Thailand. This reflects a growing appreciation that its rising comparative advantage is in higher-value services industries such as tertiary health services, private higher education, and international schools to which the country is enticing more international patients and students. Another example of this congruence is Malaysia’s leadership in institutionalising good regulatory practice in ASEAN under the AEC Blueprint 2025, an initiative that Malaysia has been assiduous in undertaking for the past decade as exemplified by the Pemudah Task Force and the National Plan on Good Regulatory Practice.

Nonetheless, Nambiar notes that there are limits to Malaysia’s liberalisation drive, such as limits on the mobility of skilled workers and on foreign ownership of hotels ranked below four stars. What this brings out is the challenge of balancing national interests and imperatives on the one hand and the regional integration goals on the other. There lies at the core of the challenge the implementation and design of the AEC integration programme moving forward.
Challenges

Implementation is key to the success of ASEAN community building. However, there are significant challenges, as the country essays in this volume bring out. The NSW serves as an illustrative example. As Llanto cites in the case of the Philippines, ‘… implementation of the NSW has been hampered by turf issues among government agencies, a lack of understanding of stakeholders of the value of NSW, and disjointed supply chains’ (Ibrahim, 2011).

Similarly, the commitments on the liberalisation of the services sector of a few AMSs are relatively low due to political economy considerations, the constraints from the country’s domestic regulatory environment, or, in the case of the Philippines, constitutional restrictions. Thus, for example, as Nambiar tells us, despite Malaysia’s progress in liberalising its financial sector, until now there are still domestic restrictions on the operations of foreign banks, which are not ‘in keeping with the liberalisation of the banking sector’. The slow progress of liberalisation in services has negative impacts on development. As Yose Rizal Damuri notes for Indonesia, ‘[d]espite being framed to protect national interest, protectionist policies have cost Indonesian society dearly … ASEAN initiatives for services have, unfortunately, yet to lead to a better and more open regulatory environment for Indonesia’s services sector’.

NTMs, the reduction of the tariff barrier effects, and the elimination of NTBs stay on top of the to-do list for ASEAN as well. The ERIA–UNDP study shows increasing NTMs in ASEAN, as is the experience in most of the rest of the world also. The majority are technical barriers to trade, with largely non-economic reasons for their imposition in Member States. Making them less of a trade barrier would call for greater regional efforts to harmonise rules, standards, and procedures and increase the transparency of the related administration. At the national level, the establishment of good testing and standards processes would help, as the experience of Malaysia’s SIRIM Berhad® indicates. Nonetheless, even for SIRIM, the SMEs still call for further simplification of documents and procedures as well as more skilled personnel, as Nambiar points out. The AMSs, in several ERIA monitoring studies on the implementation of AEC 2015, raised the inadequacy of good testing facility and complex certification processes. As a first step, greater transparency on NTMs region-wide through the ASEAN and national trade repositories could be pursued more assiduously.

Formally known as the Scientific and Industrial Research Institute of Malaysia.
Deepening regional integration requires at-the-border liberalisation and behind-the-border actions. Fulfilling the commitments to the regional blueprint demands AMS’s individual actions that involve coordination and collaboration among government agencies, cooperation and synchronisation among countries, public–private partnership, and the involvement of stakeholders from various backgrounds. Moreover, the beneficial effects from the implementation of AEC commitments would also need complementary efforts under the socio-cultural community blueprint.

Infrastructure, including logistics, transportation, market mechanism, and others, is still the bottleneck in many countries. Especially for the CLMV countries, poor infrastructure and logistics limit the benefits they get from the regional single market and constrains them in hooking up more to the regional production networks and global value chains. Equally important, Leebuoapao and Sotharith highlight the inadequacy of human capital in the Lao PDR and Cambodia, respectively, that limits their economies’ competitiveness and, in principle, their growth potential. In this regard, it becomes more relevant to enhance the existing regional mechanism, such as the Singapore Cooperation Programme that Hank Lim introduces in this volume, and the establishment of additional means of technical assistance and capacity building to the poorer AMSs. A related common concern by ASEAN countries is how to improve the global value chain–regional integration–sustaining growth nexus. Thus, for example, Thailand and Malaysia are challenging themselves to graduate from high middle-income to high-income countries by further integrating their domestic economies with the regional market and then upgrading the capability of higher value-added activities.

Last but not the least, ASEAN needs more effort to increase the awareness of ASEAN. Vo Tri Thanh mentions that for countries like Viet Nam, building awareness of and consensus on regional integration for domestic reform is important. In the case of Thailand, Rattanakhamfu suggests ASEAN integration to be ‘a catalyst for [the country’s] domestic institutional and regulatory reforms’. As the progress of ASEAN integration tends to increase the awareness of ASEAN, wider public support tends to facilitate the further movement towards the ASEAN Community. This calls for multilayered actions, including education, cultural exchanges, and various media, to get people in the region to know more about ASEAN and better understand the pros and cons of regional integration.
Concluding Remarks

ASEAN has been both a co-driver and a handmaiden of domestic reform and adjustment of the AMSs. ASEAN as a co-driver (together with the WTO and bilateral FTAs) is most evident in the case of the newer ASEAN members largely because they had to transition from relatively closed, planned economies to market and outward-oriented economies. For the older AMSs, ASEAN, specifically AFTA and the AEC, provided further impetus to their reform and institution-building efforts, in part together with the WTO and APEC in their liberalisation efforts in the 1990s. The design and pace of implementation of the AEC measures were also shaped by the varied institutional capacity and political economy environments of the member economies. Overall, ASEAN has been a positive force for the development of and improved policy regimes in the AMSs.

Moving forward, the fundamental challenge is to ensure greater congruence between national and regional policies; indeed, to embed ASEAN into the national strategies and policies, as Malaysia's approach, while each AMS attempts to influence regional policies to be consistent with national imperatives; thus, for the regional to be national in the same way that the national informs deeply the regional. This is clearly a tough task in a region consisting of members with varied levels of development and priorities. Nonetheless, AFTA and the AEC have shown that the interests and concerns of the AMSs are congruent to a large degree, and that the experiences and policy innovations of individual member countries are good sources of learning. In the end, this is a matter of degree, and the challenge is to widen and deepen further the areas of congruence. This is necessary as the countries move deeper into the goals of the AEC – a region that is deeply integrated and economically cohesive; dynamic, competitive, and innovative; resilient and inclusive; and globally connected. Such goals demand greater coherence at both the border and behind-the-border levels while at the same time allowing flexibility to accommodate the unique specificities of each AMS.

Such goals need to be ultimately in the service of the ASEAN people. For this reason, ASEAN community building requires some further strengthening of the integration–domestic reform–FDI encouragement–job creation nexus. For that, as Vo and Rattanakhamfu emphasise, there is a need to build awareness of and consensus on regional integration for domestic reform as well as domestic reform for regional integration.

One of ASEAN’s jobs is to provide its members the best development-friendly regional conditions feasible, and encourage everyone to adopt outward-looking economic policies that favour openness and inclusiveness. This is certainly not an easy task,
given the changing domestic, regional, and international political and socio-economic conditions. The solution may come from some joint or concerted actions from the AEC, ASEAN Political-Security Community, and ASEAN Socio-Cultural Community. It would be ideal to have a self-reinforcing cycle where ASEAN integration encourages cooperation and collaboration among the AMSs. The consequent regional cohesion in turn reinforces ASEAN’s capacity in facilitating domestic transition, and thereby increases AMSs’ willingness to further regional cooperation and coordination for smoother adjustment and transition and for dynamic development. In short, ASEAN’s success is built on all AMSs’ common interests. As Hank Lim states, ‘a more developed and richer ASEAN … provides wider and deeper opportunities and benefits [to all AMSs] through a more open and competitive economic environment’.

The companion Volume 5, *The ASEAN Economic Community into 2025 and Beyond*, elaborates the key elements of moving the AEC into 2025 and beyond.
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COUNTRY ESSAYS
AND PAPERS
Introduction

The Association of Southeast Asian Nations (ASEAN), which started out as a group of countries in Southeast Asia trying to overcome significant political and security challenges when ASEAN was created in 1967, has slowly evolved into a movement to transform the region into an economic powerhouse. Today, if ASEAN were considered as a single country, it would be the seventh-largest economy in the world, with a population of 622 million people. Data have also shown that the region’s gross domestic product (GDP) has nearly doubled since 2007 (Borneo Bulletin, 2016).

Now ASEAN is a grouping of 10 Member States in Southeast Asia that fosters regional cooperation and facilitates economic integration among its members. ASEAN was formed on 8 August 1967 with Indonesia, Malaysia, the Philippines, Singapore, and Thailand as founding members. The association has expanded over the years with the joining of Brunei Darussalam, Cambodia, the Lao PDR, Myanmar, and Viet Nam. Brunei Darussalam joined ASEAN as its sixth member on 7 January 1984, a week after the country gained independence.

Based on the Bangkok Declaration of 1967 (ASEAN, 2016), ASEAN aims to (i) promote economic growth and social and cultural progress in the region through joint endeavours; (ii) foster regional peace and security; (iii) encourage active collaboration and mutual assistance in the economic, social, cultural, technical, and scientific fields; (iv) promote partnerships in the development of agriculture and industries, trade, and transportation and communication facilities in the region; (v) promote Southeast Asian studies; and (vi) maintain ‘close and beneficial cooperation with existing international and regional organisations with similar aims and purposes, and explore all avenues for even closer cooperation among themselves’.
A few key highlights have shaped ASEAN in different ways from other associations, to name a few, the ASEAN Way, the ASEAN Charter, and the ASEAN Community.

As this paper discusses and relates more to deeper economic integration, hence it is worthwhile to elaborate a little more on the ASEAN Economic Community (AEC) in this section. The AEC is set to allow the free flow of goods, services, investments, and skilled labour, while facilitating the movement of capital across the region. Formally established on 31 December 2015, the community is built on a series of agreements and pillars that establish a stable foundation for liberalised trade and economic expansion in the region. The four key pillars include the creation of a single market and production base, the development of a competitive economic region, the realisation of equitable economic growth and integration with the global economy. As a single regional market and production base, ASEAN’s combined GDP in 2014 was US$2.5 trillion, making it the seventh-largest economy and third-largest population in the world, according to a 2015 ASEAN report (Oxford Business Group, 2016b).

As ASEAN approaches its 50th founding anniversary in August 2017, it is timely to ascertain the public’s perception of the association to determine the gaps and areas for improvement. The region and the world when ASEAN was born 50 years ago were very much different to how they are now. For instance, Southeast Asia is no longer the divided region that it was in the 1960s and 1970s. ASEAN must evolve with and adapt to the times and must remain relevant and responsive to the needs of its peoples.

In a Titah by His Majesty Sultan Haji Hassanal Bolkiah Mu’izzaddin Waddaulah ibni Al-Marhum Sultan Haji Omar ‘Ali Saifuddien Sa’adul Khairi Waddien, Sultan and Yang Di-Pertuan of Brunei Darussalam at the 27th ASEAN Summit in Kuala Lumpur said (Borneo Bulletin, 2015a):

> ASEAN needs to be more economically integrated and interdependent. This is possible by improving on what has accomplished [sic] to facilitate trade and investment. Businesses, especially micro, small, and medium enterprises, should continuously be made aware of opportunities and be able to take advantage of ASEAN’s integration efforts.

His Majesty highlighted the importance of raising awareness of ASEAN, especially among the youth as they play an integral part in fostering a people-centred, people-oriented ASEAN. There is also the need to keep the youth informed of ASEAN’s vision because they are the ones who will inherit its work.
His Majesty Sultan and Yang Di-Pertuan of Brunei Darussalam also said (Borneo Bulletin, 2015a):

It is hoped that ASEAN can continue to develop into a community that is more dynamic, based on the principles that have shaped the region today… ASEAN economies have enjoyed growth, the peoples of ASEAN have become closer and most importantly, they have benefitted from the efforts of ASEAN leaders.

The Potential Impact of ASEAN on Brunei

Brunei is the smallest country in Southeast Asia with a population of about 400,000 people. It is at the centre of ASEAN, and this is where the opportunities, especially for our small and medium-sized enterprises (SMEs), await. In this section, we frame the impact around the four important and mutually reinforcing pillars of the AEC.

Single market and production base

Under the first pillar, ASEAN has worked hard to improve trade and investment in the region. The achievements of local Bruneian companies, such as Sabli Foods, BMC, KTM, Tri-Sun, and Hasmit Roofing, are some of the many success stories made possible through the AEC. Local companies can benefit from the lowering of production costs, for example, through accumulation and access to cheaper raw materials, and subsequently export their goods more competitively to other ASEAN Member States like Malaysia, Singapore, the Philippines, and even beyond. The focus for ASEAN now is to further improve customs procedures and ensure that all rules and regulations are clearly published to facilitate the import and export of goods.

Competitive economic region

ASEAN’s efforts under Pillar 2 are aimed at improving the competitiveness not only of each ASEAN Member State but also of the region as a whole. As a result of ASEAN’s target and commitments under this pillar, efforts have also been focused at developing the capabilities of each ASEAN Member State, including Brunei, in other areas that were targeted at improving the region’s attractiveness for trade and investment. At the same time, Brunei has introduced several laws, including the Competition Order 2015 and
the Consumer Protection Order 2011, to make the country an attractive destination for foreign direct investment.

A region with equitable economic development

Under the third pillar, efforts have been concentrated towards ensuring that the benefits of improved trade and investment in the region would also be equitably shared and enjoyed by the lesser developed economies, as well as SMEs, whose active contribution provides for up to 90% of total employment in the region. Brunei has been able to benefit from the programmes provided for SMEs; in particular, it has collaborated with the expertise available through the various trade and investment promotion centres, such as the ASEAN-Japan and the ASEAN-Korea centres based in Tokyo and Seoul, respectively. In the past, some Brunei companies, such as IBIC Sdn Bhd and Mustaqim Enterprise, benefitted from the product design and packaging techniques, giving them an edge in marketing their goods abroad.

A region that is fully integrated into the global economy

The work under the fourth pillar aims to ensure that the AEC will not be isolated, but will instead be a relevant and key player in the global economy. To achieve this objective, ASEAN has established free trade agreements (FTAs) with several countries including China, Japan, the Republic of Korea (henceforth Korea), India, Australia, and New Zealand. As a result, ASEAN Member States including Brunei were able to open markets abroad and it enabled Bruneian companies, such as Golden Corporation, to access overseas markets like Australia, New Zealand, and Korea.

A lot of anticipation now is on the mega trade agreement between ASEAN Member States and the existing FTA partners of ASEAN, through the Regional Comprehensive Economic Partnership (RCEP). This can potentially lead to the creation of one of the world’s largest free trade areas, establishing an integrated market comprising of over 3 billion people. This is beneficial for small countries such as Brunei whose local businesses and investors do not only deal with a small domestic market but also have access to a much larger regional and global market. In addition, with the AEC now established, the next stage of integration for ASEAN beyond 2015 is the AEC 2025 Blueprint. For the next 10 years, the focus for ASEAN economic integration is very likely to be set through five key characteristics: (i) an integrated and highly cohesive market; (ii) a competitive, innovative, and dynamic ASEAN economy; (iii) a resilient, people-oriented, and people-centred ASEAN; (iv) improved connectivity and sectoral cooperation to improve efficiency and ASEAN’s effectiveness; and (v) a global ASEAN.
Brunei’s Role in ASEAN

Brunei’s GDP per capita as of 2011 was US$38,703 (ASEAN Secretariat, 2013). It was the second-highest in ASEAN (Singapore’s GDP per capita was US$52,888 while Malaysia’s was US$9766 in the same year). More than half of Brunei’s population has Internet subscriptions. The cell phone-to-person ratio is more than 1:1; 92% of its roads are paved (ASEAN Secretariat, 2013). Almost all country targets under the Millennium Development Goals were already achieved. The new Secretary-General of ASEAN in 2018 is set to be from Brunei Darussalam and such appointment will see that the country plays a key role in opening a new chapter for ASEAN.

Brunei’s commitment to continued prosperity and stable macroeconomics is underscored by Wawasan 2035, the National Vision. It provides for the promotion of investments both in downstream industries and economic clusters beyond the oil and gas industry. Under this vision, Brunei is also to implement national strategies in education, political stability and security, institutional development, local business development, infrastructure, social security, and the environment.

Being a small country has its inherent advantages that make it possible to ride the ascent of ASEAN successfully. The first advantage is that the country is easily manageable due to its small population and general stability. These conditions give greater room to carry out regional policymaking at the local level. The second advantage is that Brunei is in a great position to adopt global, pro-progress policies. Brunei has made great progress, for example, in the education sector; the country has the second-highest literacy rate in ASEAN in 2013 according to the ASEAN Annual Report 2012–2013 (ASEAN Secretariat, 2013). The success in the education sector will help drive the development of industries such as finance, real estate, and logistics trade.

Since joining ASEAN on 7 January 1984, Brunei has played a constructive role by maintaining a neutral position. Brunei’s constructive role in ASEAN was highly applauded particularly on the effort to help build confidence between ASEAN and Chinese leaders throughout the ASEAN chairmanship in 2013. For example, one important development regarding the South China Sea disputes in 2013 was the agreement between China and ASEAN to actively work towards a binding code of conduct. Three months after ASEAN leaders initiated discussions on ways to handle the South China Sea territorial disputes at a meeting in Brunei in April 2013, China agreed to start consultations with ASEAN on a binding code of conduct at the ASEAN Regional Forum. The joint communiqué issued by Chinese and Southeast Asian foreign ministers in July 2013 emphasised the need to peacefully resolve competing claims in the South China Sea.
In addition, Brunei’s ability in managing meeting agendas and stakeholders’ concerns during the ASEAN chairmanship in 2013 have helped ensure the integrity of ASEAN-hosted meetings as venues for constructive dialogue in the Asia-Pacific, while affirming Brunei’s image as a credible player in ASEAN and in the region.

Furthermore, Brunei has also encouraged other ASEAN Member States to expedite the AEC blueprint; this was an important initiative as Southeast Asia becomes more important to various regional trade integration efforts. At the East Asia Summit in November 2013, only 79.7% or 279 measures of the AEC blueprint had been completed (ASEAN Business Advisory Council, 2014). Brunei had indicated to the other ASEAN leaders to further intensify the efforts in the remaining areas to meet the common goal by the end of 2015.

In a 2015 seminar titled ‘ASEAN Media: Opportunities and Challenges’ held by the Ministry of Foreign Affairs and Trade, in collaboration with the Thai Journalists Association, former Secretary-General of the ASEAN Secretariat Surin Pitsuwan delivered a special keynote address on ‘The ASEAN Community and the New Geopolitics in the Region’. He shared that Brunei did well with the ASEAN chairmanship in 2013 and that the country would definitely continue to be a valued member of ASEAN. When he was asked about the role of Brunei in ASEAN, Dr Pitsuwan highlighted Brunei’s important role in raising the proficiency of other ASEAN Member States in the English language. He added that ‘Brunei is doing what it can as a small member but it has contributed a lot of resources both financial and intellectual’ (Borneo Bulletin, 2015b).

**Brunei’s Scorecard in ASEAN**

The AEC could open an array of business opportunities both for Brunei’s large construction firms and SMEs despite the country’s small labour market and relatively small number of SMEs. In 2015, the Oxford Business Group report stated that smaller businesses accounted for only 22% of total employment in the country, compared to 70% for Singapore and 65.5% for Malaysia. Brunei is preparing its human resources professionally for the open competition.

Reducing tariff and non-tariff barriers falls under the AEC pillar of creating a single market and production base. To date, tariffs on all building and construction goods and products have been eliminated for Brunei, Indonesia, Malaysia, Thailand, and the Philippines since 2010. Viet Nam, Cambodia, the Lao PDR, and Myanmar are set to become tariff-free by 2018. There are plans to completely remove the tariffs. The ASEAN-6 Member States – Brunei, Indonesia, Malaysia, the Philippines, Singapore,
and Thailand – are signatories to the ASEAN Trade in Goods Agreement (ATIGA), which came into force in 2010. ATIGA eliminates import duties for ASEAN-6 Member States, which is useful for exporters of building and construction materials and products. Indeed, the ASEAN-6 have almost fully eliminated intra-regional tariffs, with 99.2% of tariff lines at 0%, according to the ASEAN Annual Report 2012–2013 (ASEAN Secretariat, 2013).

ATIGA ensures not only tariff reduction but also most-favoured-nation (MFN) treatment and national treatment on internal taxation and regulation, both of which can be leveraged by Member States’ construction sectors to ensure favourable treatment. MFN gives ASEAN the right to request any Member State that gives a non-Member State more favourable commitments to incorporate that commitment into ATIGA. National treatment prohibits any ASEAN Member State from treating imported goods less favourably than its own domestically produced goods in terms of internal taxation or regulation.

The ASEAN Framework Agreement on Services (AFAS) aims to eliminate restrictions on trade in services and enhance cooperation within ASEAN. AFAS benefits companies providing services, including construction services, in the ASEAN region by ensuring national treatment, market access, and recognition of professions under mutual recognition arrangements (MRAs). MRAs have been agreed for engineering, architecture, and land surveying professionals, facilitating free movement and access to opportunities within ASEAN, while at the same time maintaining high standards of accreditation. The construction-related agreements are among the various packages signed by ASEAN economic ministers. These agreements include eliminating restrictions on activities such as construction of commercial buildings, installation works, rental of construction equipment, and civil engineering. Other agreements in the planning stage will see MRAs tabled for the construction and building sectors, among others.

The ASEAN Comprehensive Investment Agreement (ACIA) protects existing investments and prospective investors. This could benefit any construction project requiring foreign investment and could ultimately create a larger marketplace for mega projects along the line of the Temburong Bridge in Brunei. Along the same lines as ACIA, the Investor–State Dispute Settlement (ISDS) mechanism gives investors the right to use dispute settlement proceedings when they are unable to obtain compensation after unlawful direct or indirect expropriation. The ISDS also allows for improved transparency in investment regulations, calling for ASEAN Member States to make information on laws, regulations, administrative guidelines, or policy changes relating to investments publicly available. These policies will safeguard and further promote foreign direct investments in the ASEAN region.
Brunei, along with the Philippines and Myanmar, is a ‘Country Champion’ for the ASEAN Strategic Action Plan for SMEs Development 2016–2025 goal to promote entrepreneurship and human capital development in the community. This goal puts the country in the position of driving human capital development to enable MSMEs\(^1\) to succeed. The desired outcomes include instituting entrepreneurial education and learning programmes, enhancing human capital development for microenterprises, and promoting women’s participation in MSMEs. To achieve the entrepreneurship goal, the focus for Brunei is to ensure that the creation of effective entrepreneurial human resource development can be achieved quickly. The Ministry of Education introduced in 2014 the National Entrepreneurship Agenda, which established an entrepreneurship village in the national university, Universiti Brunei Darussalam. This village aims to inculcate the entrepreneurial mindset in creating the entrepreneurship ecosystem for the country.

Furthermore, in January 2016, the Energy and Industry Department under the Prime Minister’s Office announced the formation of a new statutory body that will be responsible for the growth of local SMEs. Darussalam Enterprises (DARe) was set up to encourage and manage the growth and development of local enterprises, including SMEs. With 85% of DARe’s board of directors being drawn from the private sector, the body will be a mix of representatives comprising entrepreneurs and veteran industry players from the country’s construction, logistics, and consultancy sectors. With the necessary rules and regulations in place, and with the positive determination of entrepreneurs matched by the experience of business people, Brunei looks well placed to move its economy in the direction of ASEAN integration with a focus on how the construction and logistic sectors can contribute to this direction.

**Brunei’s Further Contribution to ASEAN**

Brunei has opportunities to play a key role in ASEAN. Even though by population base it is the smallest country in ASEAN, Brunei’s potentials are there. Since Brunei is a member of the Commonwealth, it has a good connection globally and has close relations to many countries in every continent. It could then play a key role in enhancing or further maintaining good relations between ASEAN and Commonwealth countries.

Another potential is Brunei becoming an education hub in the region. This is also in line with the country’s 2020 Higher Education Strategic Plan. The basic literacy rate in Brunei

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\(^1\) MSMEs stand for micro-, small, and medium-sized enterprises. Microenterprises are firms with 1–5 employees.
is almost 100%; people are mostly bilingual (Malay and English) and have access to free education. Moreover, Brunei has liberal trade policies, relatively lower corporation tax, excellent investment incentives, a clean environment, and a life of harmony and peace that can make the country an ideal destination for further education and eventually a hub of education. Additionally, Brunei has strengths in several niche areas—such as in the teaching of English and in the study of medicine, energy, and biodiversity—that can help the country attract institutions from abroad to establish themselves in Brunei, and for international students to study at local institutions.

Brunei could also greatly improve its role in the region as a major transport hub in the Brunei Darussalam-Indonesia-Malaysia-Philippines–East ASEAN Growth Area (BIMP-EAGA) region if current developments continue. First, Brunei is part of four major projects, with total investments of up to B$20 billion in the region (Brunei Times, 2013), that include the Trans Borneo Railway, a 4,440-kilometre network that will stretch across Borneo Island and will connect Bandar Seri Begawan with major cities in Malaysia and Indonesia. Then there is the proposed ASEAN Halal Park, an integrated project that will set up many halal-certified manufacturing companies and is aimed at becoming the strongest manufacturing centre for premium halal products in the global market. The Trans-Borneo Railway will connect Sarawak, Sabah, Kalimantan, and Brunei with major sea ports and airports; it will also make Borneo’s vast commodity resources, such as coal, timber, and minerals, easily accessible, with Brunei expected to become an important shipping hub for these commodities in the region and beyond. Brunei, together with Sarawak and Sabah, can vastly benefit from such a project because it already has active port industries that are being upgraded and added to in efforts to reach some of the fastest-growing consumer markets in the world.

The Oxford Business Group Report (2015) said that Brunei’s position next to the South China Sea’s sea lanes made its 160-kilometre coastline strategically significant. Under the Kuala Lumpur Transport Strategic Plan 2016–2025, Brunei has agreed to contribute to the establishment of an ASEAN single shipping market and to promote maritime safety, security, and strategic economic corridors in ASEAN. The report said the strategic plan would enable Brunei to engage in regional maritime transport cooperation in developing the ASEAN strategic-logistics corridors.
Results of the Face-to-Face Interviews

A total of 56 respondents participated in the face-to-face interviews.

<table>
<thead>
<tr>
<th>Age Group</th>
<th>Number</th>
<th>Share of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>15–30</td>
<td>15</td>
<td>26.79</td>
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<tr>
<td>31–49</td>
<td>39</td>
<td>69.64</td>
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<tr>
<td>50+</td>
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<td><strong>Total</strong></td>
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<td><strong>100.00</strong></td>
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<table>
<thead>
<tr>
<th>Gender</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Male</td>
<td>16</td>
<td>28.57</td>
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<tr>
<td>Female</td>
<td>40</td>
<td>71.43</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>56</strong></td>
<td><strong>100.00</strong></td>
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<table>
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<tr>
<th>Sectoral</th>
<th>Number</th>
<th>Share of Respondents</th>
</tr>
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<td>Public Sector</td>
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<td>73.21</td>
</tr>
<tr>
<td>Private Sector</td>
<td>15</td>
<td>26.79</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>56</strong></td>
<td><strong>100.00</strong></td>
</tr>
</tbody>
</table>

Source: Author’s compilation from the interviews.

This is a follow-up to the 103 emails our research team sent. We invited various public and private sector agencies, and 56 accepted an appointment for a face-to-face interview. Each interview took about 45 minutes. Beside questions on personal details such as age, highest educational attainment, occupation, and the sector where the respondents work, we asked five questions on their understanding, knowledge, and perspectives of the future of ASEAN. The five questions concentrated around (i) the importance of ASEAN integration, (ii) regional FTAs, (iii) RCEP and its possible impact, (iv) key 2030 challenges for ASEAN, and (v) the world facing ASEAN in 2050 and beyond.

The largest age group was composed of those aged 31–49. More females (71%) were interviewed using this random method; 41 of the respondents were from the public sector, and 15 from the private sector. All of them have at least a post-secondary education, with the majority having a bachelor’s degree.
We performed a linear regression on the data sets with responses from the 56 respondents. We found this technique more suitable than a simple correlation coefficient to understand the association between the dependent variable (familiarity with ASEAN) and independent variables (age, gender, private sector employment, occupation, and highest educational attainment). No missing data were detected when coding was carried out. The data were processed using the Analysis ToolPak in Excel. Table 2 shows that the R squared and the adjusted R squared values of the regression results for predicting the familiarity with ASEAN (0.2917 and 0.2504, respectively) show a medium/weak correlation between the independent variables and the dependent variable. Usually, we must also consider the statistically significant values to improve the validity of the results, in this case p < 0.05 in almost all cases or 0.01 (education variable). Hence, we can conclude the findings are statistically significant because a smaller p value represents a more significant impact.

<table>
<thead>
<tr>
<th>Model</th>
<th>Coefficient</th>
<th>Standard Error</th>
<th>P Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>Age</td>
<td>0.0024</td>
<td>0.0063</td>
<td>0.000</td>
</tr>
<tr>
<td>Gender</td>
<td>0.1446</td>
<td>0.0043</td>
<td>0.000</td>
</tr>
<tr>
<td>Public Sector</td>
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<td>0.0321</td>
<td>0.000</td>
</tr>
<tr>
<td>Occupation</td>
<td>0.2525</td>
<td>0.021</td>
<td>0.000</td>
</tr>
<tr>
<td>Education</td>
<td>0.0005</td>
<td>0.0001</td>
<td>0.010</td>
</tr>
</tbody>
</table>

R-squared: 0.2917; adjusted R sqr: 0.2504
Dependent variable: Familiarity on ASEAN
Source: Author’s computation.

The results have identified that those working in the public sector, in administrative services, have a better understanding of and are more familiar with ASEAN and its activities compared to those in the private sector. The association between age and gender is not strong in comparison. The surprising finding is that the education variable, which has a coefficient of 0.0005, indicates that education does not have much productive impact on familiarity with ASEAN. Nevertheless, the result for this variable is not as statistically significant as the other variables.
Importance of ASEAN integration

The vast majority (75%) of survey respondents believe that ASEAN integration is important in helping businesses and SMEs in the region. Some phrases (permission given to quote) given during the face-to-face interviews include: (i) ‘An integrated ASEAN provides increased opportunities to our prospects to expand the small domestic demand’; (ii) ‘Hopefully, it will help to facilitate and expedite the paperwork process’; (iii) ‘We see opportunities for Brunei to leverage on ASEAN integration to capitalist in niche sectors such as logistics, halal industry, and medical technology (MedTech)’.

Less than half (36%) of respondents indicated that their companies have an ASEAN regional strategy based on the goals of the AEC blueprint. Of the respondents who did not, many commented that they are still developing their strategy, that they focus only on a single country in ASEAN, or that they are unsure or uncertain about the timeline and feasibility of the AEC blueprint.

Respondents cited that non-tariff barriers to trade (51%) and transparency (40%) are areas of work that deserve attention to further enhance regional economic integration. Respondents from the private sector emphasised the need for effective communication between different offices or the setting up of one-stop facilitation centres to improve the ease of doing business.

Regional free trade agreements

The majority of the respondents expressed that they are not too familiar with regional agreements. However, they believe that FTAs are important to the overall trade activities of the country and the region. The few respondents who are familiar with FTAs considered AFAS to be most important (60%).

The Regional Comprehensive Economic Partnership

RCEP is a trade initiative proposed by the 10 ASEAN Member States and six FTA partners: Australia, China, India, Japan, Korea, and New Zealand.

It aims to consolidate the various ‘ASEAN +’ agreements listed in the previous section into one broader regional free trade network. Probably due to media coverage, 50% of respondents were more familiar with RCEP compared to the FTAs mentioned earlier. About 19% believe that RCEP will not impact trade and investment, while 17%
believe that it will lead to business expansion prospects in ASEAN and increase overall satisfaction in the local business environment.

A lot of anticipation has been on whether the two regional trade agreements, the Trans-Pacific Partnership (TPP) and RCEP, will both be implemented in the Asia-Pacific region. Furthermore, the wave of adjustment to international trade and investment rules, stirred up by the Transatlantic Trade and Investment Partnership and the Trade in Services Agreement, is becoming yet another major external factor that impacts the economic development of Asia-Pacific countries. Hence, it has become critical to optimally balance the relationship between the TPP and RCEP. However, compared to the TPP, RCEP seems more feasible now. The respondents believe that the early completion of RCEP may provide a new path and platform for promoting trade, facilitating investment, fine-tuning industry, and facilitating the resulting spillover effects that will further improve the manufacturing network, expand the value chain, and optimise the allocation of trade and production factors in the Asia-Pacific region. This will create new opportunities for every country in the region.

**Key challenges in 2030**

Respondents were asked what they perceive are the key challenges for ASEAN in 2030. This question received one of the most positive responses as 80% of the respondents described ASEAN in 2030 as resilient, inclusive, competitive, harmonious, and united. In addition, about 91% of respondents unanimously shared that Asian countries are likely to be ‘leading actors’ on the global trade stage.

Among many issues discussed, the majority of respondents also forecasted that the number of elderly people in Asia will increase. The Asia Pacific Risk Center (2016) also reported that the number of elderly people will increase by 200 million by 2030. Almost all respondents also revealed their views that they expect greater life expectancy in the next 13 years with the increase in non-communicable diseases, such as diabetes and dementia. Increasing life expectancy and falling fertility rates result in the growing number and proportion of the elderly population. This in turn implies an increase in healthcare services such as long-term care facilities and trained workers to run them. For the workforce, it will also mean a labour shortage. One solution being tried in Japan is to make up for workforce shortages by using robotic technology to assist elderly people. The confluence of societal ageing leads to the risk of exponential growth in elderly healthcare expenditure and a rising trend of medical technology. According to the International Labour Organization, some three in five jobs in ASEAN-5 (Cambodia,
Indonesia, the Philippines, Thailand, and Viet Nam) face a high risk of being replaced by automation in ASEAN in 2030.

**The world facing ASEAN in 2050 and beyond**

All respondents predicted that by 2050, there will be more people over 65 than under 15, presenting the ASEAN Member States with a whole new range of challenges. All respondents expected older people to continue living and working longer. This percentage is projected to jump to nearly 17% of the world’s population by 2050, i.e. 1.6 billion (Cire, 2016). This in turn means that ASEAN’s social protection mechanisms such as healthcare and pension schemes will need to be strengthened. Forty-nine percent of the respondents also shared that they expected the ASEAN region to become more integrated with open labour migration policies, so that workers from a labour surplus region can work where there is demand for their skills.

Highlighting the rapid technological advances being experienced by Asian youth, even in rural areas, ASEAN Member States would need to harness their knowledge and skills. Forty-nine percent of the respondents revealed that many jobs in 2050 might not even exist now. Repetitive jobs would likely be made redundant. Hence, it is crucial to look now into the new directions of artificial intelligence, robotics, and telecommunication. These implications were not only for education and skills policies but also be reflected in how ASEAN can use technological advances in designing cities, public transportation networks, logistics, and building codes for the future.

Although the education variable does not have a high coefficient in the regression results as shown in Table 2, the results reveal that the respondents generally felt that by 2050, workers with only a primary degree or lower have a higher chance of losing their jobs to automatons than secondary school graduates. For those with a tertiary education, the risk is substantially lower. These trends support the notion that higher education and training are vital to developing the competencies needed for complicated tasks that are difficult for machines to do.

The majority of respondents also shared that another likely scenario of the 2050 economy is that the economic growth in the ASEAN Community will face the issue of the middle-income trap. A growing population combined with financial prosperity and a heightened consumption mentality will provide a fertile environment for the consumer market. However, this may cause further economic divide in ASEAN-10 Member States. Generally, countries in a middle-income trap situation do not suffer from desperate poverty; nevertheless, they are not able to afford the luxuries enjoyed in more developed
nations. In recent years, some economists have already raised the unsettling possibility that while most countries can climb into the ranks of middle income, it might be much harder to climb up to the top level.

Summary and Conclusion

This year on 8 August, ASEAN celebrates an important anniversary. It is the 50th year since the signing of the Bangkok Declaration, which established the association.

According to the McKinsey Report (Vinayak et al., 2014), if ASEAN were a single country, it would already be the seventh-largest economy in the world, with a combined GDP of US$2.4 trillion in 2013. It is projected to rank as the fourth-largest economy by 2050. Nevertheless, to capitalise on these trends, the region must develop its human capital and workforce skills. For people outside ASEAN, the memories of the 1997 Asian financial crisis linger, leading many outsiders to expect that volatility comes with the territory. However, the region proved to be remarkably resilient in the aftermath of the 2008 global financial crisis. Today it is in a much stronger fiscal position where the savings levels have also remained steady since 2005 (at about a third of GDP), albeit with large differences between high-saving economies – such as Brunei, Malaysia, and Singapore – and low-saving ones – such as Cambodia, the Lao PDR, and the Philippines. Furthermore, despite their distinct cultures, histories, and languages, the 10 Member States of ASEAN share a focus on development and prosperity. Household purchasing power is rising, transforming the region into the next frontier of consumer growth. To maintain the current trajectory will require enormous investment in infrastructure and human capital development, which is a challenge for any emerging region but a necessary step towards ASEAN’s goal of becoming globally competitive in a wide range of industries. In addition, it must tackle challenging questions on how to navigate the accelerating pace of technological change and digital disruption. On the one hand, the Fourth Industrial Revolution could bring huge benefits to the region, driving financial inclusion and the creation of new companies and service sector jobs.

From an economic perspective, the AEC offers an opportunity to create a seamless regional market and production base. If the implementation of the ASEAN Community Vision 2025 is successful, ASEAN could prove to be a case in which the whole does exceed the sum of its parts. Not only will this help ensure equal economic development but also it will further integration into the global economy.


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Cambodia

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Introduction

Cambodia, once a failed state with civil war, genocide, and political turmoil, has achieved national reconciliation and political stability. After overcoming hardship, including a protracted civil war, political genocide, and international isolation, the country has been transformed from a centrally planned economy into a free market economy whose main tasks are to implement macroeconomic and structural reforms and to alleviate poverty. As a result, Cambodia has achieved significant success in stabilising its macroeconomic foundation with rapid economic growth and low inflation. In line with peace, political stability, and social order, the country has been transformed from a battlefield on the verge of destruction into one of emerging development, and now increasingly it is becoming integrated into the regional and global community.

After the new coalition government was established following the first democratic general election in 1993, the Royal Government of Cambodia started implementing macroeconomic and structural reforms to reconstruct and develop the country. To ensure success for such reforms, the government strongly committed to be part of regional and global economic integration.

It is recognised worldwide that free trade significantly helps reduce poverty and improve people’s living standards. Thus, the Royal Government continued to liberalise trade and ensure the free flow of goods and services both within the country and between Cambodia and key regional and global partners. Such would provide Cambodia with the economies of scale and opportunities that attract investment, create employment,
increase incomes, and accelerate economic growth, thus reducing poverty. Indeed, Cambodia’s participation in ASEAN in 1999 and in the World Trade Organization (WTO) in 2004 constitutes strategic and historical steps towards its miracles of national rehabilitation and development.

The Royal Government recognises that Cambodia’s membership in ASEAN requires great efforts in the formulation, adoption, and implementation of laws, regulations, and procedures, and increases the country’s capability in production and competitiveness to reap maximum benefit from ASEAN membership.

As ASEAN celebrates its 50th anniversary in 2017, Cambodia also celebrates its 18th anniversary as an ASEAN Member State. It is an appropriate time to assess achievements, opportunities, and challenges for ASEAN.

This paper describes and analyses the impact of ASEAN membership on Cambodia’s political–security, economic, and socio-cultural aspects. It also highlights Cambodia’s role in contributing to building the ASEAN Community, and the challenges ahead for the country.

**Political and Security Impacts**

Cambodia undoubtedly has been able to get the most benefit out of its membership in ASEAN since its admission into this regional grouping in April 1999, after several years of intensive preparation and negotiation. The public has always questioned the benefits and costs of the country’s membership in ASEAN; and it is very difficult to answer. In other words, people want to know if the country is benefiting from ASEAN at all; and if so, what the actual, tangible gains are. This is very hard or almost impossible to explain. Clearly, there are both tangible and intangible benefits. Cambodia has certainly benefited from its membership in ASEAN in many ways and in many aspects.

First, ASEAN contributed to political change and helped bring peace and stability to Cambodia. The country adopted democracy and national reconciliation under the Paris Peace Accords, in which ASEAN, especially Indonesia, played an important role. One could argue that the United Nations peacekeeping operations in Cambodia, through the UN Transitional Authority in Cambodia, could have contributed towards ending the country’s international isolation. Yet, Cambodia’s admission into ASEAN could have also played a crucial role in accomplishing its integration in the region. In this context, ending Cambodia’s isolation positively contributed to the political reconciliation and development in the region. In other words, the region was no longer
divided, as it had been. With strong interest and commitment, the country was given ASEAN observer status in 1995 and was to be admitted to ASEAN in 1997, along with the Lao PDR and Myanmar. However, due to internal problems, the membership was delayed. The country’s legitimacy and political situation encountered problems. The ASEAN Troika was established to help solve the crisis in Cambodia. Some conditions were also proposed, such as requiring Cambodia to restore democracy, create a peaceful environment for the elections, and establish a Senate. Cambodia followed the recommendations and successfully fulfilled all conditions. It was finally admitted to ASEAN in 1999.

Secondly, its ASEAN membership contributed to promoting Cambodia’s image and prestige in the regional and international arena. As the youngest member of ASEAN, Cambodia has been undoubtedly given an equal footing in this regional grouping, with its rights and obligations. Therefore, the country has been active in all areas of cooperation—from international politics to security, and from economic to functional cooperation. Cambodia has been strongly committed in participating in regional and global platforms to shape common values and serve common interests. For instance, it has contributed more than 1,000 peacekeepers to different parts of the world with ASEAN identity under the United Nations. This action has promoted Cambodia’s image in international relations and diplomacy.

ASEAN membership has helped strengthen Cambodia’s role in regional and international affairs over the past years on bilateral and multilateral diplomacy. Through ASEAN multilateral diplomacy, the country has been able to engage and participate actively in other important forums, such as the WTO, Asia Cooperation Dialogue, the Asia–Europe Meeting, and the Forum for East Asia–Latin America Cooperation. While ASEAN covers a wide range of areas of cooperation, it is important that each Member cooperate more closely with one another, both collectively and individually, to ensure that regional cooperation equally benefits all Member States. ASEAN, as a dynamic and open regional organisation, plays an essential role in both regional and global affairs at present and in the future. Without ASEAN, small and medium-sized states in Southeast Asia would have little influence or role in international affairs, given the growth of regionalism in other parts of the world and the full swing of globalisation. In addition, the small states in Southeast Asia are vulnerable to the external influences of the major powers. Therefore, to maintain the central role of ASEAN, these small states in the region should fully participate in realising an ASEAN Community.

1 The ASEAN Troika, formed to deal with the Cambodian crisis, comprised the former chair (Indonesia), the current chair (Philippines), and the incoming chair (Thailand) of the ASEAN Standing Committee. The Troika was designed to allow ASEAN some flexibility in dealing with potential crises; however, it could not make decisions on its own. It was only an arm of ASEAN’s foreign ministers to represent them in a particular crisis.
Thirdly, ASEAN helps provide security and peace to Cambodia. From its inception, ASEAN has always emphasised the spirit of equality and partnership towards peace and non-interference. This effectively means that membership in ASEAN bolsters overall security, especially along the borders of individual countries. In further fostering security and safety for the peoples of ASEAN, law enforcement agencies of Member States have played a key role in engaging in dialogue – either through conferences, workshops, trainings, and meetings – which allows each agency to exchange experiences and establish channels of communication to assist their daily operations. A good example of this cooperation includes the combat against terrorism. All agencies in the region have coordinated with one another in sharing information and intelligence, leading to the arrest of some members of, and disruption to, terrorist organisations. Another is on humanitarian assistance and disaster relief; ASEAN Member States have effectively cooperated and supported each other in coping with natural disasters.

Fourthly, ASEAN promotes the defence and security capacity of Cambodia. The ASEAN Defence Ministers’ Meeting (ADMM), established in 2005, and ADMM Plus, created in 2010, have significantly promoted practical security cooperation among Member States and the Plus Eight countries – namely Australia, China, India, the Republic of Korea (henceforth Korea), Japan, New Zealand, the Russian Federation, and the United States. The current five areas of security cooperation within the framework of ADMM Plus are (i) maritime security, (ii) humanitarian assistance and disaster relief, (iii) counter-terrorism, (iv) peacekeeping operations, and (v) military relief. In such a cooperation framework, Cambodia has sent its security officers to participate in training workshops, capacity-building programmes, and joint exercises. Skills and expertise among the Cambodian officers and armed forces have been gradually strengthened to meet the new challenges, especially coming from the nontraditional security threats. The ASEAN Chiefs of Police (ASEANAPOL) Conference is an additional platform of which Cambodia’s national police has been a part. The forum has provided law enforcement agencies of ASEAN Member States the opportunity to review their cooperation, address crime situations that impact the region and beyond, and come up with better and more effective joint strategies to combat them. The forum has discussed the whole range of transnational crime issues such as terrorism, drugs, arms smuggling, trafficking in persons, piracy, cybercrime, money laundering, and economic crimes. These exercises not only make law enforcement a well-informed body but also expand the operating network, which is the critical qualification to fight transnational crimes in this modern age. The emergence of transnational crimes, including terrorism, has not escaped the attention of law enforcement agencies of ASEAN Member States. The Senior Officials Meeting on Transnational Crime (SOMTC) was established to annually discuss and share intelligence information on these crimes. Through this meeting, Cambodian law
enforcement has learned a great deal about the nature and situation of transnational crimes, enabling them to prepare better to combat such crimes.

**Economic Impacts**

**Economic development**

Along with Cambodia’s effort to develop its economy, membership in ASEAN can be one of the stimuli contributing to economic development. The country has seen considerable economic and social achievements, with robust and steady growth of about 7% over the past 2 decades. At present, Cambodia has one of the fastest economic growth rates in the world. With a low inflation rate of less than 5% and a stable local currency (riel), the country presents a stable macroeconomic prospect in the medium and long term (Figure 1).

Gross domestic product (GDP) increased from US$7.27 billion in 2006 to US$18.05 billion in 2015 and US$20.23 billion in 2016 (Figure 2). GDP per capita also increased from US$666.5 to reach US$1,020.9 in 2015 and US$1,325 in 2016, promoting Cambodia from the status of least-developed country to a lower middle-income country.2

The leading sectors for growth are the garment and apparel industries, construction, tourism, and agriculture.

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Figure 2. Cambodia’s GDP, 2007–2015


Figure 3. Cambodia’s Per Capita Income, 2007–2015


Trade promotion

ASEAN is one of the main factors to promote trade. In addition to its own bilateral approach, Cambodia has been working through the regional framework to promote trade in goods and services. Within the framework of the ASEAN Free Trade Agreement, Cambodia can access a market of about 600 million people in the whole of Southeast Asia. This is the reason cooperation with ASEAN has become even more important in recent years, given the current process of ASEAN integration and the deepening and growing cooperation that Cambodia has with all dialogue partners of ASEAN, particularly with the Plus Three countries (China, Japan, and Korea) and India.
As result, Cambodia’s trade volume remarkably increased from US$7.2 billion in 2005 to US$26.36 billion in 2015; exports increased from US$3.09 billion to US$11.96 billion and import increased from US$ 3.93 billion to US$14.4 billion (Table 1). In 2015, Cambodia exported clothing, timber, rubber, rice, fish, tobacco, and footwear to its main export partners. These are the United States (23.1%), United Kingdom (8.8%), Germany (8.2%), Japan (7.3%), Canada (6.7%), China (5.1%), Viet Nam (5%), and Thailand (4.9%). Cambodia imported petroleum products, cigarettes, gold, construction materials, machinery, motor vehicles, and pharmaceutical products from its main import partners. These are Thailand (28.5%), China (22%), Viet Nam (16.3%), Hong Kong (6%), and Singapore (5.6%). Cambodia has transformed from an import-oriented into an export-oriented country. From 2003 to 2016, its exports covered an average rate of 63.62% of GDP, indicating that the country is export oriented.4

### Table 1. Cambodia’s Trade Data, 2005–2015 (US$ billion)

<table>
<thead>
<tr>
<th>Year</th>
<th>Export</th>
<th>Import</th>
<th>Total Trade</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>3.09</td>
<td>3.93</td>
<td>7.02</td>
<td>-0.84</td>
</tr>
<tr>
<td>2006</td>
<td>3.69</td>
<td>4.77</td>
<td>8.46</td>
<td>-1.08</td>
</tr>
<tr>
<td>2007</td>
<td>4.09</td>
<td>5.44</td>
<td>9.53</td>
<td>-1.35</td>
</tr>
<tr>
<td>2008</td>
<td>4.71</td>
<td>6.51</td>
<td>11.22</td>
<td>-1.80</td>
</tr>
<tr>
<td>2009</td>
<td>4.20</td>
<td>5.83</td>
<td>10.03</td>
<td>-1.63</td>
</tr>
<tr>
<td>2010</td>
<td>5.14</td>
<td>6.79</td>
<td>11.93</td>
<td>-1.65</td>
</tr>
<tr>
<td>2011</td>
<td>6.70</td>
<td>9.30</td>
<td>16.00</td>
<td>-2.60</td>
</tr>
<tr>
<td>2012</td>
<td>7.84</td>
<td>11.35</td>
<td>19.19</td>
<td>-3.51</td>
</tr>
<tr>
<td>2013</td>
<td>9.25</td>
<td>12.80</td>
<td>22.05</td>
<td>-3.55</td>
</tr>
<tr>
<td>2014</td>
<td>10.86</td>
<td>13.50</td>
<td>24.36</td>
<td>-2.64</td>
</tr>
<tr>
<td>2015</td>
<td>11.96</td>
<td>14.40</td>
<td>26.36</td>
<td>-2.44</td>
</tr>
</tbody>
</table>

Source: Statista.com at
http://www.statista.com/statistics/438746/export-of-goods-to-cambodia/ and


4 According to the World Bank, a country whose exports are greater than 60% of GDP indicates an export-oriented economy. In contrast, values lower than 15% of GDP indicate a relatively closed economy.
To be in harmony with ASEAN and the WTO, Cambodia reformed its tariff structure by reducing the number of tariff bands from 12 to only 4, and abolishing the high tariff rates of 40%, 50%, 90%, and 120%. Tariff comprises four tiers: 0%, 7%, 15%, and 35%. The tariff rate of 35% protects several semi-processed goods and consumer goods, such as processed meat and dairy products, processed vegetables and fruits, beverages and tobacco, footwear, and motor vehicles. Over 53.4% of tariff lines are duty free or subject to the minimum 7% tariff rate, compared with 44% in 2001. A standard deviation of 9.2% in 2011 indicates that there is still some dispersion of tariff rates.

The average MFN (most favoured nation) applied rate on agricultural products (WTO definition), at 14.5%, remains higher than that for industrial goods (11.3%). Cambodia has an escalating tariff structure with rates increasing with each stage of processing. Overall tariff lines were reduced from 10,700 to 8,314 from 2007 to 2011, based on the Harmonization System of 2007 nomenclature (International Trade Centre, 2011). At present, Cambodia has an 8-digit HS with a total of 9,574 tariff lines (see Table 2) (General Department of Customs and Excises, 2016).

### Table 2. Cambodia’s Customs Tariff and Development of HS Classification

<table>
<thead>
<tr>
<th>Year</th>
<th>Harmonization System</th>
<th>No. Digit</th>
<th>No. of Tariff Lines</th>
</tr>
</thead>
<tbody>
<tr>
<td>Before 1993</td>
<td>Not yet implemented Harmonization System</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1993</td>
<td>HS 1993</td>
<td>6</td>
<td>2,200</td>
</tr>
<tr>
<td>2000</td>
<td>HS 1997 &amp; AHTN 2000</td>
<td>8</td>
<td>6,822</td>
</tr>
<tr>
<td>2004</td>
<td>HS 2002 &amp; AHTN 2004</td>
<td>8</td>
<td>10,689</td>
</tr>
<tr>
<td>2007</td>
<td>HS 2007 &amp; AHTN 2007</td>
<td>8</td>
<td>8,314</td>
</tr>
<tr>
<td>2008</td>
<td>HS 2007 &amp; AHTN 2007</td>
<td>8</td>
<td>8,314</td>
</tr>
<tr>
<td>2010</td>
<td>HS 2007 &amp; AHTN 2007</td>
<td>8</td>
<td>8,314</td>
</tr>
<tr>
<td>2012</td>
<td>HS 2012 &amp; AHTN 2012</td>
<td>8</td>
<td>9,574</td>
</tr>
</tbody>
</table>

Source: Ministry of Economy and Finance (2016).

**Foreign direct investment**

To compete with ASEAN Member States that have better infrastructure, bigger population, and more attractive conditions, Cambodia has implemented many reforms in the policy and legal framework to attract foreign direct investment (FDI). Presently, the country has an open and liberal foreign investment regime with a pro-investor and pro-business legal and policy framework. Investment incentives available to foreign investors include 100% foreign ownership of companies, corporate tax holidays of up to
8 years, a 20% corporate tax rate after the incentive period, duty-free import of capital goods, and no restrictions on capital repatriation.

According to Index Mundi, net FDI inflow to Cambodia increased from US$54.12 million in 1993 to US$1.9 billion in 2015. The main projects focused on textile production in the special economic zone, construction, mining, manufacturing mainly concentrated on spare parts and food products, and tourism. FDI inflow as a percentage of GDP varied from year to year. FDI was the highest in 2014, with FDI covering 10.31% of GDP, considered high compared with regional and global rates (Index Mundi, 2016). From 2006 to 2015, FDI inflow per GDP averaged 8.1% of GDP indicating that Cambodia is an FDI-attracting country (see Table 3).5

Table 3. FDI Data in Cambodia, 1993–2015

<table>
<thead>
<tr>
<th>Year</th>
<th>FDI Net Inflow</th>
<th>FDI as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>$54,124,000</td>
<td>2.14</td>
</tr>
<tr>
<td>1994</td>
<td>$68,900,000</td>
<td>2.47</td>
</tr>
<tr>
<td>1995</td>
<td>$150,800,000</td>
<td>4.38</td>
</tr>
<tr>
<td>1996</td>
<td>$293,600,000</td>
<td>8.37</td>
</tr>
<tr>
<td>1997</td>
<td>$203,700,000</td>
<td>5.92</td>
</tr>
<tr>
<td>1998</td>
<td>$242,823,000</td>
<td>7.78</td>
</tr>
<tr>
<td>1999</td>
<td>$232,238,700</td>
<td>6.60</td>
</tr>
<tr>
<td>2000</td>
<td>$148,503,600</td>
<td>3.24</td>
</tr>
<tr>
<td>2001</td>
<td>$149,397,500</td>
<td>3.68</td>
</tr>
<tr>
<td>2002</td>
<td>$145,106,400</td>
<td>3.06</td>
</tr>
<tr>
<td>2003</td>
<td>$83,980,650</td>
<td>1.75</td>
</tr>
<tr>
<td>2004</td>
<td>$131,416,200</td>
<td>2.46</td>
</tr>
<tr>
<td>2005</td>
<td>$277,180,200</td>
<td>5.99</td>
</tr>
<tr>
<td>2006</td>
<td>$483,209,400</td>
<td>6.64</td>
</tr>
<tr>
<td>2007</td>
<td>$867,288,500</td>
<td>10.04</td>
</tr>
<tr>
<td>2008</td>
<td>$815,180,200</td>
<td>7.87</td>
</tr>
<tr>
<td>2009</td>
<td>$511,114,500</td>
<td>4.91</td>
</tr>
<tr>
<td>2010</td>
<td>$739,199,200</td>
<td>6.54</td>
</tr>
<tr>
<td>2011</td>
<td>$795,460,500</td>
<td>6.20</td>
</tr>
<tr>
<td>2012</td>
<td>$1,440,978,000</td>
<td>10.26</td>
</tr>
<tr>
<td>2013</td>
<td>$1,345,044,000</td>
<td>8.71</td>
</tr>
<tr>
<td>2014</td>
<td>$1,730,356,000</td>
<td>10.31</td>
</tr>
<tr>
<td>2015</td>
<td>$1,915,525,841</td>
<td>9.42</td>
</tr>
</tbody>
</table>

Sources: Index Mundi: http://www.indexmundi.com/facts/cambodia/foreign-direct-investment;

According to the World Bank, values of FDI above 4%–5% of GDP suggest that the country is an attractive foreign investment destination.
Tourism promotion

ASEAN membership is a main factor to promote tourism. The Open Skies Policy, also known as the ASEAN Single Aviation Market, aims to increase regional and domestic connectivity, integrate production networks, and enhance regional trade by allowing airlines from ASEAN Member States to fly freely throughout the region via the liberalisation of air services under a single, unified air transport market. As a member of ASEAN, Cambodia’s tourist market is integrated with other ASEAN tourist destinations. With strong commitment to implement the framework of the ASEAN Open Skies Policy and related protocols, Cambodia has increased connectivity, tourist marketing, and air transport remarkably.

Tourism is a key area where Cambodia has been able to work with ASEAN over the years. The regional cooperation and integration process has contributed to the growth of the tourism industry because the ASEAN connectivity plan creates a favourable condition for air, maritime, and land transport connections and for the movement of tourists across the region. ASEAN tourism products have also been marketed better. Cambodia, like other ASEAN Member States, has teamed up and worked closely with ASEAN dialogue partners to promote tourism to benefit all countries. Cambodia has benefited much in pro-poor tourism, which is a key to reducing the development gap in the country and in the region.

Tourist arrivals in Cambodia increased from only 367,743 in 1999 (the year Cambodia was admitted to ASEAN) to 5.01 million in 2016 (Figure 4).

In 2016, the top 10 tourist markets for Cambodia were Viet Nam, China, Thailand, the Lao PDR, Korea, United States, Japan, United Kingdom, Malaysia, and France (Figure 5). During the year, 2,121,220 tourists (or 42.3% of total) were from ASEAN. At the same time, 1,434,030 Cambodian tourists travelled abroad (Ministry of Tourism, 2016).
At the heart of the ASEAN Socio-Cultural Community (ASCC) is the commitment to lift the quality of life of its peoples through cooperative activities that are people oriented, people centred, environment friendly, and geared towards the promotion of sustainable development (ASEAN Secretariat, 2016).

The ASCC Blueprint was substantially implemented from 2009 to 2015 and was found effective in developing and strengthening the coherence of policy frameworks and institutions to advance human development, social justice and rights, social
protection and welfare, environmental sustainability, ASEAN awareness, and narrowing development gaps. More concretely, the ASCC has helped heighten commitment in the form of policy and legal frameworks, such as the Declaration on Non-communicable Diseases in ASEAN and the Declaration on the Elimination of Violence Against Women and Elimination of Violence Against Children in ASEAN. The region has also shown collective will, for example, in offering quick and tangible action in humanitarian assistance through the ASEAN Coordinating Centre for Humanitarian Assistance.

Cambodia’s benefit from the ASCC is huge but difficult to calculate. The country has received positive impact from ASCC participation. Underlying ASCC’s initiatives are important development outcomes pushing social changes in the country: the rate of poverty (people living on less than US$1.25 per day) fell about 1% per year from 53% in 2004 to 20% in 2011; life expectancy rose from 54.9 years in 1999 to 71.6 years in 2012; the net enrolment rate for children of primary school age rose from 78% in 1999 to 85% in 2012; the proportion of seats held by women in parliament increased from 10.6% in 1998 to 19.5% in 2013; and maternal mortality per 100,000 live births fell from 830 in 1990 to 206 in 2010.\(^6\)

Other Impacts

Acceleration of reforms

In preparing to be admitted and to work within ASEAN, Cambodia had to introduce many reform programmes to improve institutional and legal frameworks affecting economic management, public administration, and the judicial system, among others, to be consistent with ASEAN. Membership in ASEAN has been the pushing factor for Cambodia to have a trajectory for sustainable and inclusive economic development, together with regional economic integration. To benefit from such a dynamic regional integration process, Cambodia has no choice but to improve its capacity both in the public and the private sectors to narrow the gap, and compete at the regional level to maximise the benefit from regional integration. Providing better and favourable conditions for production, trade, investment, and promotion of competitiveness in all fields are the most important tasks for the country’s economic survival.

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\(^6\) Data obtained from many sources such as the Cambodia National Assembly, United Nations Children’s Fund (UNICEF), and the World Bank.
Human resource development

In the Initiative for ASEAN Integration framework, Cambodia has benefited from assistance in human resource development. Every year, Cambodia sends many of its officials and students to various training programmes and workshops in Member States or in dialogue partner countries of ASEAN. Training and human resource development are important for Cambodia since the country has been struggling to train and develop its human resources in many fields.

Assistance through the ASEAN framework

This means that Cambodia could directly benefit from bilateral or multilateral projects, funded by ASEAN dialogue partners, such the Plus Three countries. For example, the projects under the Initiative for ASEAN Integration have been important to support the new Member States of ASEAN, thus strengthening ASEAN integration, especially in providing training and study tours in many fields to Cambodian government officials. The recent creation of the ASEAN Infrastructure Fund is another important milestone in linking ASEAN infrastructure, especially in the least developed countries of ASEAN.

Promotion of other regional and subregional cooperation

As a Member State of ASEAN, Cambodia has opportunities to participate in other related regional and subregional cooperation such as in the Greater Mekong Subregion (GMS), ASEAN Mekong Basin Development Cooperation, CLMV (Cambodia, Lao PDR, Myanmar, Viet Nam) cooperation, the development triangles, and the Ayeyawady-Chao Phraya-Mekong Economic Cooperation Strategy, and Lower Mekong Initiative.

Cambodia’s Contribution to ASEAN

Since accession to ASEAN, Cambodia has actively participated in summits, ministerial meetings, conferences, working groups, and other forums. It has successfully hosted various summits and meetings that provided opportunities to expose the country to the world and to change the negative mindset towards Cambodia into a positive one.

Cambodia hosted two ASEAN summits and related ones in 2002 and 2012. In both years, it also hosted the ASEAN+3 Summit, the ASEAN+1 Summits with China, Japan,
and Korea, the first ASEAN–India Summit, the ASEAN Ministerial Meeting, ASEAN Regional Forum, the post-ministerial conferences, East Asia Summit, ASEAN Defence Ministers’ Meeting, and other related sectoral meetings. It also chaired the ASEAN Standing Committee. In addition, Cambodia successfully hosted the ASEAN Inter-Parliamentary Organization in 2004 and the ASEAN Inter-Parliamentary Assembly in 2011 aimed at strengthening the role of the legislature in promoting a people-centred and rules-based ASEAN.

Cambodia successfully chaired the Eighth ASEAN Summit in Phnom Penh on 4 November 2002 and achieved remarkable results. It was a historic and proud moment for Cambodians. At the opening of the ASEAN Summit, the Chair outlined the Phnom Penh Agenda Towards a Community of Southeast Asian Nations. The initiative has four themes:

- collaboration with the Greater Mekong Subregion programme to accelerate ASEAN integration;
- ASEAN as a single tourist destination;
- ASEAN solidarity for peace and security, especially in the fight against terrorism; and
- bold steps in sustainable natural resources management, including ratification of the Kyoto Protocol by all ASEAN Member States. Leaders considered the idea of an ASEAN Economic Community as an end goal for the Roadmap for the Integration of ASEAN and Vision 2020 (ASEAN Secretariat, 2012).

At the summit, the leaders also witnessed the signing of the Declaration on the Conduct of Parties in the South China Sea that provided for confidence-building activities between ASEAN and China. In addition, the two sides adopted the Joint Declaration of ASEAN and China on Cooperation in the Field of Non-traditional Security Issues and tasked the ministers to expeditiously specify mechanisms for such cooperation. China expressed its interest to accede to the Treaty of Amity and Cooperation in Southeast Asia and stated its willingness to work with ASEAN to push for the early accession to the Southeast Asia Nuclear Weapon-Free Zone.

On 18 November 2012, Cambodia proudly hosted the 21st ASEAN Summit in Phnom Penh. The ASEAN heads of state/government discussed the Progress of the Implementation of the ASEAN Charter and Roadmap for an ASEAN Community as a follow-up to the 20th ASEAN Summit’s Progress Report on the Implementation of the Master Plan on ASEAN Connectivity. They then signed the Phnom Penh Statement on the Adoption of the ASEAN Human Rights Declaration, Exchange of View on Regional and International Issues, and issued the Leaders’ Statement on the Establishment of an ASEAN Regional Mine Action Centre.
ASEAN Leaders agreed to sign, adopt, and note the following outcome documents:

- Phnom Penh Statement on the Adoption of the ASEAN Human Rights Declaration,
- ASEAN Human Rights Declaration,
- ASEAN Leaders’ Joint Statement on the Establishment of an ASEAN Regional Mine Action Centre, and
- Concept Paper on the Establishment of an ASEAN Regional Mine Action Centre.

**Challenges**

**Development gaps**

As a country of lower income compared to other members, Cambodia needs to implement further reform in many fields, especially in the economic sector, to catch up with the older members. The development gap between Cambodia and the rest of ASEAN must be narrowed down gradually and consistently. This, however, is difficult to achieve.

More efforts are needed to continue to focus on ASEAN integration, particularly through the projects of the Initiative for ASEAN Integration, the Vientiane Action Programme, and the subregional development projects, to ensure that the least developed members of ASEAN can fully integrate their economies into the regional and the global economic system. In this regard, the dialogue partner countries, as well as other interested third parties and institutions, can assist ASEAN to further advance its integration, especially in reducing the development gaps within the region.

For Cambodia, the internal development gap between its capital city, Phnom Penh, provincial capitals, and rural areas are huge, presenting big disparity in public utilities, wealth, and infrastructure. Most economic development projects are concentrated in Phnom Penh, causing urbanisation, migration, traffic, and pollution problems.

**Non-tariff barriers and non-tariff measures**

Non-tariff barriers and non-tariff measures (NTMs) still impede trade in ASEAN. Though the country has implemented many reforms, the problem still exists due to many reasons, such as poor law enforcement and corruption. A study conducted by the Economic Research Institute for ASEAN and East Asia found that from 52 regulations, 243 NTMs affected 9,558 Cambodian products (HS codes). This is 100% of the total...
products traded in Cambodia (Chap, Tobing, and Widiana, 2015). Not only Cambodia but also other ASEAN Member States have NTM problems. So far, some Cambodian products are difficult to export due to NTMs, especially sanitary and phytosanitary (SPS) measures and technical barriers to trade (TBT) imposed by importing countries.

**Competition**

ASEAN membership also brings negative impacts to Cambodia. Its weak position in regional competition is one of the country’s biggest challenges. With its low production base, poor skilled labour, and weak infrastructure, Cambodia’s productivity is still low and its products of poor quality and costly compared with regional norms. The poor marketing mechanism and high cost of electricity, logistics, and transport make it difficult for Cambodian products to compete with imported products sold locally and with local products of exporting markets. The regional free trade in goods and services seriously affect Cambodia’s local small and medium-sized enterprises (SMEs).

**Lack of resources**

To benefit from regional integration and the reduced regional development gap, Cambodia must build its capacity in all sectors, especially in those related to the free market environment. So far, the public sector still needs to build expertise in strategic planning, legal regulations, and leadership. The private sector still lacks professionals, skilled labour, and entrepreneurs who can conduct research and development (R&D), create innovation, and drive their business to the higher level. Cambodia also lacks other resources such as technology and investment capital.

**Diversification of economic sectors**

Cambodia’s economy is driven by a few sectors, and its concentrated garment and apparel manufacturing makes the economy vulnerable.
Poor logistics and transport system

Trade, especially cross-border trade, cannot be promoted without a long-term plan and a proper logistics system. Logistics connectivity can be measured both in terms of cost and time. Cambodia’s transport modes, including railways and waterways, are outmoded due to the lack of long-term planning and regional logistics and transport system. Most bulk cargo and containers use the road transport system, resulting in quick deterioration of road networks, which is costly for the government to repair and maintain.

Railways usually offer an efficient interface between maritime and land transport systems, especially since container shipping became prevalent. Rail logistics is, however, complex as it requires management of capacity, schedule, shipment, characteristics, origin, and destinations. Cambodia’s rail transport is considered the weakest link in the regional logistics infrastructure. The railway system was built in the 1960s. Due to war and lack of maintenance, the railways have deteriorated and their rehabilitation has been very slow. The only two railways lines are in single tracks. At present, the operation of Cambodia Railways is privatised but it is inefficient. So far, transport of passengers and cargo by train is limited due to many reasons such as poor condition of railways, lack of logistics hubs, lack of train stations, high cost, slow speed, and lack of reliability.

On the other hand, despite the country’s good waterway system in the Mekong River, waterway transport is also limited. There is no link in logistics between ports, airports, railways, and waterway and maritime transport.

The other bottleneck in trade facilitation is the weak system in handling and clearing cargo and containers at main international border checkpoints. Though the Automated System for Customs Data (ASYCUDA) has been installed and fully implemented at all border checkpoints, the problems of long waiting time and disorder and traffic jams at the clearing areas still remain.

Poor awareness of ASEAN

According to surveys, both the public and the private sectors in Cambodia still have limited awareness of ASEAN. It is important to bring all sectors to join regional integration. Without awareness, they would not participate and prepare, especially to meet changes in the business environment.
Conclusion

Starting as an observer in 1995 to become a full member of ASEAN in 1999, Cambodia worked hard and achieved remarkable results. It was very hard at the beginning for a country that recently emerged from destruction from war, political strife, and isolation to change from a centrally planned economy to a market economy to prepare for membership in ASEAN. However, after many years of membership, Cambodia could overcome all hardship and has been successful in reforming both its institutional and legal systems to be consistent with ASEAN.

Since 1999, ASEAN has impacted Cambodia’s political, security, economic, and socio-cultural aspects and has driven reforms. From being deeply engaged in war, isolation, and destruction, Cambodia has transformed into a peaceful, stable, and developed country. It has also advanced from a low-income or least-developed country to a lower middle-income economy.

Despite the huge benefits Cambodia has gained from being an ASEAN member, it still faces many challenges for regional integration. Such challenges are (i) the development gaps still existing among old and new members (Cambodia, the Lao PDR, Myanmar, and Viet Nam); (ii) non-tariff barriers and NTMs still existing among ASEAN Member States; (iii) weak position in competition; (iv) lack of resources; (v) poor logistics and transport system; and (vi) low awareness of ASEAN. To maximise the benefits of regional integration, Cambodia should address all these challenges, exert more effort to further its reforms, and engage more in implementing all ASEAN agreements and protocols.

ASEAN integration needs to be fully realised to effectively address the imbalance of development in the region on the one hand, and to enhance and deepen East Asia cooperation on the other. The disparity in ASEAN today constitutes the major challenge that must be overcome at any cost. A fully integrated ASEAN will sustain its relevance, boost its competitiveness in the face of increasing challenges of regional integration and globalisation as well as be a catalyst for strengthening East Asia. Moreover, an economically strong ASEAN will benefit not only its Member States but also its partners as well. Therefore, its integration remains a critical factor to the progress of East Asia and to its other partners.

While ASEAN positively impacts and greatly benefits Cambodia, in return, Cambodia also tirelessly works to help build the ASEAN Community in all aspects. Cambodia has been an active member and has provided important inputs for ASEAN strategic and development policies. Its participation in ASEAN can change the image of Southeast Asia into a united region of peace and development.
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Indonesia

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Introduction

With an estimated population of 250 million and per capita gross domestic product (GDP) of around US$900 billion, Indonesia is the fourth most populous country in the world and the 16th largest economy. It is the largest economy in Southeast Asia and ranks sixth among other Asian countries. The current state of Indonesia is the result of a long transformation that has been taking place for 50 years. While it obtained formal independence in 1949, the first 25 years of the history of the nation was marked with an independence war, military conflicts, and regional uprisings that led to economic disaster. It was not until the late 1960s that the process of economic development started.

A stable political situation was finally achieved when President Suharto took over the country’s administration from President Soekarno in 1967, following political turmoil that lasted for almost 2 years. Political and economic stability were crucial elements for the Government of Indonesia to pay more attention to economic development. The government of the New Order under President Suharto (1967–1998) immediately implemented macroeconomic stabilisation policies, such as reducing inflation from almost 600% to less than 10% within 5 years, that remarkably created a favourable situation for economic development (Hill, 2000).

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1 It started with a failed coup attempt by the Indonesian Communist Party (Partai Komunis Indonesia, PKI) in September 1965, which later shifted against Soekarno’s leadership for not taking necessary action towards PKI. General Suharto, who emerged as a leader in stopping the coup, was authorised by President Soekarno in 1966 to stabilise the situation, but ended up taking actions that stripped Soekarno of his power with the help of Parliament. He was sworn in as President in March 1968, after having been appointed Acting President the year before (Vatikiotis, 1998).
Development was also marked with the transformation of policies and institutions, and the country’s policy and attitude towards openness significantly shaped its economic performance. The New Order relied heavily on capital and investment from abroad to finance government projects and to promote business activities. While trade made only a small contribution to the economy, it was an important source of efficiency improvement (Soesastro and Basri, 2005). However, Indonesia’s attitude towards trade and openness has changed frequently over the last 50 years. The country has tended to embrace openness and promote outward-looking policies to support economic reforms during difficult times but become more protective and inward-looking during economic boom periods.

Along with the development process came regional integration, particularly with other countries of Southeast Asia and East Asia. After receiving power to lead the country in 1966, Suharto decided to stop the Indonesia–Malaysia Confrontation – a series of military actions under the command of the previous president, Soekarno, against the creation of Malaysia – which lasted for 4 years. Realising that the stability of the region was an important factor in supporting development, Indonesia, together with Malaysia, Singapore, the Philippines, and Thailand, established the Association of Southeast Asian Nations (ASEAN) on 8 August 1967. Intended as a regional organisation to ensure peace and security during the Cold War, ASEAN has grown to also cover various aspects of integration during its later years, including in economic areas.

The two simultaneous processes of economic development in Indonesia and integration in the region have certainly affected each other. Indonesia pursued an agenda to promote its interests in as early as the 1970s when ASEAN came up with the idea of having several joint industrial projects. The country became the location for some industries – e.g. fertiliser production, pulp, and paper – deemed to be important for Indonesia at that time. In the 1990s and 2000s, Indonesia’s liberalisation process could not be separated from the trade liberalisation and integration process in ASEAN. As the largest country in the region, Indonesia’s role and attitudes towards regional integration had shaped economic integration in Southeast Asia and East Asia and would determine the future direction of this process.

This paper looks at the various elements of the interaction between Indonesia and ASEAN, particularly the economic policy formulation and the economic development processes. The next section examines Indonesia’s perspective and approach towards openness and integration, and proceeds to discuss how ASEAN integration has affected Indonesia’s economic situation, policy formulation, and economic performance. Finally, this paper discusses Indonesia’s current and future role in ASEAN integration.
Indonesia’s Trade Policy and Integration Efforts

Unilateral initiatives towards openness

Indonesia’s development process can be characterised by several distinct periods. One of the most important early policies to support economic development was the introduction of the open-door policy on foreign investment in 1967 to finance economic activities. The policy towards economic openness was in line with the New Order’s strategy for economic development, considering that the country had no financial resources to support the development. The government also began to simplify trade regulations quite quickly, introducing a series of major liberalising reforms over 1966 to 1969, while introducing capital account liberalisation and unifying the exchange rate of the rupiah (Hill, 2000).

However, this open policy was short-lived. By the early 1970s, it became apparent that Indonesia preferred import substitution and a more inward-looking development strategy, supported by the increase in international oil prices, which quadrupled in the mid-1970s. The oil boom that had taken place since 1973 made the country rich enough to afford many government-led economic projects. With huge state revenues from state oil company Pertamina, the government set up factories and increased production capacity in both oil-related and non-related sectors, such as oil refineries, fertiliser plants, cement, and iron and steel/aluminium.

The development of heavy industries was the highlight of this period for supporting the import substitution policy. Exports were dominated by the primary sectors, most prominently by oil products. The export base of manufactured goods was tiny, comprising only a little more than 1% of total exports in 1970–1975. Furthermore, despite rapid GDP growth, Indonesia’s pattern of structural transformation seems to have been unsatisfactory as the share of industry in GDP slightly declined from 12% to 11%.

Initial efforts for openness and integration with the global and regional economy were unilateral responses to external developments, namely the decline in oil prices in the early 1980s. They began with limited economic policy deregulation complemented with tariff reductions and the removal of some non-tariff barriers (NTBs) in the manufacturing sector, especially in labour-intensive industries. By 1992, the average tariff had been reduced to 20% from 26% in 1986, while the incidence of NTBs fell to 5% from 32% (Pangestu and Feridhanusetyawan, 2003). The progress slowed in the early 1990s as most of the ‘low-hanging’ trade barriers had been eliminated. It became
increasingly difficult to reduce protection since most of the barriers were in politically sensitive sectors, such as agriculture, heavy industries, and motor vehicles.

Further trade reforms took place in 1997–1998, the period of the Asian financial crisis, to comply with the structural adjustment programme attached to the International Monetary Fund’s lending package. The package included a gradual reduction of import tariffs, including those on sensitive products of heavy industries; the removal of NTBs and licensing for imports of many agriculture products; and the liberalisation in several services sectors. These unilateral efforts, however, were put on hold and even reversed as forms of protectionism when economic recovery took place. Imports of agricultural products were prohibited except under certain conditions. Various policies were introduced in a revival of the import substitution strategy. Despite the need for investment in the services sector, various limitations were imposed on foreign providers, including those in finance, marine transport, and telecommunications.

**Indonesia’s trade policy in a multilateral and regional context**

Reversal of the unilateral open policy, which happened several times during Indonesia’s development period, signifies the importance of international commitments in economic and trade areas. Indonesia had been involved in the multilateral General Agreement on Tariffs and Trade (GATT) since 1950 and was one of the founding members of the World Trade Organization. Indonesia’s involvement in this forum helped shape the formulation of its trade policy.

World Trade Organization agreements set maximum tariff rates for most of Indonesia’s imported products and placed binding requirements on existing market access–related regulations in various services sectors. The commitments also reduced the incidence of NTBs and eliminated quantitative restrictions on trade while at the same time removing local content requirements, which were common for supporting import substitution (Pangestu and Stephenson, 1996). While many of these commitments had little impact on actual trade liberalisation, they placed limitations on policy reversal.

Another important regional initiative is the Asia-Pacific Economic Cooperation (APEC) forum. While this remains informal and commitments are not formally binding or made through a process of negotiations, APEC has also influenced Indonesia’s trade and investment policy, particularly on commitments to provide facilitation to economic activities. One example is the APEC investment principles, which call for equal treatment between domestic and foreign investors. Indonesia has accepted these principles and adopted them in its investment policy. While APEC’s voluntary approach
to trade liberalisation seems to be less demanding than preferential trade agreements, it provides more confidence for the unilateral approach. Commitments in APEC have often provided starting points for more formal and detailed commitments in various trade agreements.

**ASEAN as the driver of regional integration**

As mentioned earlier, ASEAN was not intended to be a driver of economic integration in the region. However, several factors pushed the Member States to turn ASEAN into an economic integration vehicle. One important motivation was the de facto economic and business integration that has been taking place in the region for quite a while, mostly driven by foreign investors and multinational companies. As regional business arrangements have become more complex, they have required facilitation from authorities to ensure cross-border economic activities in the region. Another reason was to provide fresh motives and purposes for the ASEAN Member States in the post-Cold War period.

The ASEAN Free Trade Area (AFTA) in 1992 was not the first ASEAN initiative on economic integration, but it was the first formal and binding commitment to reduce trade barriers in a detailed and comprehensive way. AFTA set the deadline of the Common Effective Preferential Tariff (CEPT) to be 5% or less in 2003 and to cover more than 90% of imported items. This was then extended to cover most traded items by 2010. The ASEAN Member States also agreed to liberalise services and investment and to facilitate economic and business activities. The commitment to form an ASEAN Economic Community (AEC) promoted the integration initiative to a higher level. As a member of ASEAN, all these initiatives affected Indonesia's perception on economic integration and openness not only towards other Member States but also to the rest of the world.

**ASEAN’s Influence on Indonesian Policy**

How do ASEAN economic initiatives affect Indonesia’s economy? To answer this question, this section discusses the extent to which ASEAN integration initiatives have influenced Indonesia's policies by looking at some of the commitments and their implementation.
AFTA and Indonesian trade policy

One major initiative of ASEAN is to promote free trade in the region, which has been described broadly since the inception of AFTA, particularly under the CEPT. In this area, Indonesia's commitment is quite significant. Indonesia is committed to reducing preferential tariff rates to zero within the agreed timeline. By 2010, less than 1.3% of Indonesia’s imports from other ASEAN Member States remained subject to tariffs while the rest enjoyed duty-free tariffs. The implementation of the ASEAN Trade in Goods Agreement has reduced the tariff rates even further.

One interesting aspect to examine is how the CEPT rates have affected Indonesia's trade policy, particularly in the formation of the most-favoured-nation (MFN) rate. Table 1 shows the influence of the ASEAN preferential rate on Indonesia's MFN tariff rate. As expected, ASEAN's CEPT rate decreased significantly during the period 1995–2010 from 14.2% to 2.1%. However, Indonesia’s MFN tariff rate also followed a similar pattern. The average MFN tariff decreased substantially from 16.5% to 7.1%.

<table>
<thead>
<tr>
<th>Table 1. Average Indonesia’s Tariff Rates and the Number of Tariff Lines</th>
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<tbody>
<tr>
<td><strong>1995</strong></td>
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<tr>
<td>Average CEPT rate (%)</td>
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<tr>
<td>Average MFN rate (%)</td>
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<tr>
<td>Number of duty-free MFN tariff lines</td>
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<tr>
<td>Number of CEPT tariff lines</td>
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<tr>
<td>Number of tariffs with MoP less than 5%</td>
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</table>

Note: CEPT = common effective preferential tariff, MFN = most-favoured nation, MoP = margin of preference (the difference between the MFN and the preferential rate).

Source: Calculated by the author from Indonesia’s tariff schedule and CEPT.

The number of MFN lines with zero tariff also followed the same pattern as the CEPT. In 2010, 98% of tariff lines for imports from other ASEAN Member States was set to zero, a significant increase from only 68% during the first 3 years of CEPT implementation. But Indonesia also increased the number of its duty-free tariff lines for imports from other countries. For many tariff lines, the MFN rates were eliminated to zero just several years after their CEPT rates. Moreover, the reduction of MFN rates was also in line with the CEPT. While in 1995 only less than 30% of tariff lines had 5% differences between their MFN and CEPT rates, in 2010 this increased to 57% of tariff lines. That indicates that more MFN tariff rates are not significantly higher than the
CEPT rates. While more rigorous examination is needed, this indicates that the ASEAN CEPT rate might have had a positive effect on Indonesia’s MFN tariff.

However, ASEAN initiatives on trade barriers have marginal effects on certain sectors, notably agriculture. Indonesia maintains a list of sensitive products in its CEPT schedule that includes rice, sugar, soybeans, and wheat flour. This allows Indonesia to exclude these products from the trade commitments with other ASEAN Member States. Until recently, imports of various agricultural products were still prohibited except for certain situations where the government considered them to be necessary. However, the country agreed to phase out import duties on several unprocessed agricultural products to 0%–5% under the ASEAN Trade in Goods Agreement.

**Trade facilitation**

Another important element of commitments in ASEAN is the promotion of trade facilitation and customs modernisation. Indonesia began its customs modernisation when import inspection authority was given back to Indonesia’s Customs Office in 1997. Previously, since 1985, the government had asked a survey company, Société Générale de Surveillance, to conduct pre-shipment inspections and be in charge of trade procedures. This was then followed by a series of customs reforms and improvements to infrastructure, institutions, and procedures.

ASEAN introduced programmes to facilitate trade in 1997 in view of AFTA, by calling for greater harmonisation of trade procedures under the ASEAN Customs Policy Implementation and Work Programme, including the harmonisation of tariff classifications. Indonesia agreed to carry out these efforts as part of its modernisation of customs and trade procedures (Damuri, 2006). The next main agenda of trade facilitation in ASEAN was the creation of an ASEAN Single Window, which required the establishment of the Indonesia National Single Window.

Indonesia has been quite successful in implementing trade facilitation measures, particularly with regard to the Indonesia National Single Window. Seventeen major ports, accounting for more than 98% of the value of Indonesia’s foreign trade, have been connected to the system (Damuri et al., 2015). Although the system still has a lot of room for improvement, it has facilitated Indonesia’s private sector in dealing with trade procedures.
Services reform

Recognising the importance of services trade, ASEAN Member States have initiated negotiations concerning the services sector since 1995, when the countries first decided to negotiate the ASEAN Framework Agreement on Services (AFAS). This services agreement among ASEAN Member States focuses on liberalisation efforts, particularly in Mode 1 and Mode 3.

While the agreement has been in place for more than 2 decades, Indonesia seems to have encountered difficulties in carrying out its commitments under the AFAS. The country committed to liberalising 104 subsectors in the latest AFAS Package 9 with a foreign equity limitation of more than 70% by the end of 2015. Indonesia only managed to follow the commitment for 81 subsectors and seems to be lagging behind in following the commitments in health-related services, communications, and logistics, despite these being priority sectors. Under the current regulatory environment, many subsectors still limit foreign participation to less than 70%. Indonesia also faces issues related to national treatment principles in AFAS, especially regarding taxation policy, land use, and professional qualification requirements, which dictate different treatment for foreign and domestic firms (Damuri, 2015).

Despite being framed to protect national interests, protectionist policies have cost Indonesian society dearly. For example, the lack of openness in the healthcare sector has led to deficient healthcare facilities in several regions and low-quality service delivery. In another instance, the protectionist regulatory regime in the maritime sector has imposed high transport and logistics costs on the users of these services, as support for infrastructure and efficient cargo-handling processes remains highly insufficient. The lack of competitiveness in the telecommunications sector has also led to the Internet fixed broadband penetration rate in Indonesia being among the lowest in the region.

ASEAN initiatives for services have, unfortunately, yet to lead to a better and more open regulatory environment for Indonesia’s services sector.

Investment liberalisation and facilitation

Investment liberalisation and facilitation have always been vital to deepening economic integration in ASEAN and East Asia. In 2009, the Member States introduced the ASEAN Comprehensive Investment Agreement (ACIA) to enhance and integrate previous agreements on investment. As a country in which growth relies on foreign direct investment (FDI), Indonesia is anticipated to support these commitments. Results
show that there have been some progress and successful implementation of investment liberalisation and facilitation in Indonesia.

In 2007, the government promulgated a new investment law, Law No. 25 on Capital Investment. The law provides, among others, national treatment to foreign investors and investments, standard protection for investors, and a list of obligations and responsibilities of investors. It also specifies that in principle, all lines of business are open to foreign investment, except for those sectors specifically mentioned in the so-called ‘negative list’ (Daftar Negatif Investasi, DNI) and in other laws and regulations. The negative list is also subject to change every 2–3 years to accommodate new developments. All these features were adopted following various principles laid down in investment agreements in ASEAN and other regional initiatives, such as APEC.

The DNI has been reviewed and revised three times since 2007, with the latest being launched in 2016. The new DNI tends to be more open than the previous one. It also pays more attention to the commitments Indonesia specified in the ACIA. This is an improvement from the last DNI, which placed higher restrictions on several subsectors than in their ACIA descriptions.

Indonesia has made some progress in investment facilitation. It has introduced a one-stop service centre for investment to serve in a more rapid, simple, transparent, and integrated fashion. The service also integrates all licensing and non-licensing services related to investments, which used to be scattered across 22 ministries and government agencies. This progress is in line with the AEC blueprint (ASEAN Secretariat, 2015), which calls for more transparent, consistent, and predictable investment rules, regulations, policies, and procedures (Atje and Sasmito, 2015).

**ASEAN in the Indonesian Economy**

The other ASEAN Member States were traditionally not important partners for Indonesia, except for Singapore, which serves as a hub of economic activities in the region. However, through economic integration, the economic links between Indonesia and ASEAN have become more important.

**Benefits of ASEAN integration for the economy**

A large proportion of studies on the impact of ASEAN integration on the regional economy is conducted using the computable general equilibrium (CGE) model.
The CGE model is an ex ante simulation model that uses a general equilibrium setting to analyse the potential costs and benefits of a trade agreement before implementation.

An early study by Pangestu and Feridhanusetyawan (2005) looks at the impact of Indonesia’s liberalisation efforts, including those conducted under AFTA. It concludes that the welfare gain from AFTA alone was negligible in comparison to liberalisation under the GATT/Uruguay Round. It added a welfare gain of only 4% to the impact of the GATT. One reason for this small benefit comes from the fact that agriculture has remained quite restrictive in the early arrangement of AFTA. The study also concludes that incorporating agricultural liberalisation into AFTA would have increased its benefits.

A more recent study by Plummer, Petri, and Zhai (2012) found that full implementation of the AEC would have raised ASEAN real incomes by US$69.4 billion, or 5.3% over the 2004 baseline income by 2015. Based on the study, Indonesia would be one of the countries to benefit most from the integration, with a 6.2% increase in real income. Additionally, simulations by Plummer, Petri, and Zhai show that raw materials output will mostly shrink relative to the baseline, while manufacturing and services output is likely to rise relative from the baseline. The increase in the services sector reflects the sector’s linkages with and importance to the manufacturing sector as a result of more integrated regional production.

Using a dynamic CGE model, a study by Plummer and Lee (2011) suggests that reducing administrative and technical barriers (e.g. streamlining customs procedures and the mutual recognition of product standards) and lowering the trade and transport margins (e.g. through increased competition and improvements in infrastructure) are significant for enlarging the benefits of the AEC. The study finds that reductions in frictional trade costs, as well as the trade and transport margins, have significant effects on economic welfare, as deviations in equivalent variations, while allowing for endogenously determined productivity levels, have a small impact. The estimated welfare gains for 2015 were 1.1% for Indonesia, much lower than for Thailand at 9.4%.

Several studies have also estimated the impact of the AEC on the growth and shifts of sector employment. A study from the International Labour Organization and the Asian Development Bank (2014) estimated a net increase of 14 million jobs in Cambodia, Indonesia, the Lao PDR, the Philippines, Thailand, and Viet Nam. The largest demand was estimated for low- and medium-skilled jobs. This is consistent with the findings in the study by Plummer, Petri, and Zhai (2014), in which the CGE model shows that the rise in sector employment tends to be dominated by increasing jobs in the informal sectors, with the exception of the Philippines.
Nevertheless, the study by the International Labour Organization and the Asian Development Bank also projects high-skilled occupations to grow in some economies. High-skilled employment growth between 2010–2025 in Indonesia, Cambodia, the Lao PDR, the Philippines, Thailand, and Viet Nam is estimated to be 41%, with half of the gain taking place in Indonesia.

**Indonesia’s trade with ASEAN Member States**

Figure 1 shows the general trend of Indonesia’s trade relations with other ASEAN Member States. Indonesia’s total trade with ASEAN increased throughout 1990–2015. The trade intensity index – an indicator of whether trade between two economies is greater or smaller than would be expected based on their importance in world trade – was bigger than 1 and was increasing, signifying the increasing importance of ASEAN to Indonesia.

![Figure 1. Total Trade with ASEAN, Trade Intensity Index and Export Intensity Index of Indonesia with ASEAN, 1990–2015](image)

There are two turning points, namely in 1993 and 2003, during which Indonesia’s total trade with ASEAN increased at a faster rate than in the previous period. Trade grew by more than 16% after the inception of AFTA in 1992 and got stronger when AFTA was almost fully implemented in 2003.

Few changes are observed in terms of trade with Indonesia’s partners within ASEAN. More than 90% of Indonesia’s trade with ASEAN was conducted with ASEAN-4 (Singapore, Thailand, Malaysia, and the Philippines). Singapore is Indonesia’s largest trade partner. Until 2015, Singapore’s share in Indonesia’s trade with ASEAN was still
larger than 40%. Nevertheless, this is much less than in 1993 when the share of trade with Singapore was 67.47%.

Along with the decline in trade with Singapore, trade with Malaysia and Thailand picked up to double from their respective amounts in 1993. Trade with Malaysia rose to 25.39% in 2013 from the 14.41% in 1993. A similar pattern occurred with Thailand, for which trade nearly doubled to 17.74% in 2013 from 9.18% in 1993. In the case of Thailand, the increase in trade share was driven by the increase in the share of imports from Thailand. As for Malaysia, it was driven by the increase in the share of exports to Malaysia.

It should be noted that the increasing trade came more importantly from imports, as indicated by the lower export intensity index. The value of imports overtook exports in 2005, not long after the implementation of AFTA. This has led to a general suspicion that AFTA was less beneficial to Indonesia, at least in trade. One explanation for this situation is the low utilisation of AFTA by Indonesian exporters. In order to receive the ASEAN preferential rate when exporting to other ASEAN Member States, exporters need to show that their products are eligible to be considered ‘ASEAN products’ according to the specified rules of origin. Only less than 7% of exports made use of the CEPT rate until 2007, although the figure increased to 50% in 2012 (CSIS, 2013). This caused exports from other ASEAN Member States to grow slower than imports.

**Development of the production network**

Another explanation comes from the emergence of the international production network (IPN) in the region. In this business model, domestic and foreign firms utilise comparative advantage by slicing up production into finer stages and sourcing inputs from different locations according to factor intensity and the abundance of factors of production. This means trade in intermediate inputs becomes more important in trade and economic activities.
Trade in value added statistics indicates the importance of this regional network, which might explain increasing imports from ASEAN. Table 2 shows the intensity of foreign value added in Indonesia’s exports, an indicator of the importance of the international network in exports and production. We can deduce two points. First is the increasing share of foreign value added in Indonesia’s exports, which indicates a greater involvement of Indonesian industries in the international network. This is even more obvious in the case of manufacturing industries. Second is the increasing proportion of foreign value added coming from other ASEAN Member States. These two factors indicate the development of a production network among ASEAN Member States and the importance of ASEAN not only as a market for Indonesia’s exports but also as a source of production inputs.

Greater participation in the IPN has enabled Indonesian industries to develop further. The IPN promotes higher specialisation, which allows firms and industries to improve their efficiency and productivity. Even during the earlier stages of the production network in the late 1980s and early 1990s, Indonesian industries gained from sourcing their intermediate inputs from foreign countries and specialising in the final stage of production (Amiti and Konings, 2007). Participation also increased the transfer of technology since foreign companies need to ensure that their domestic partners can produce to international standards. This creates an opportunity for the domestic industry to upgrade its performance and reach higher stages of production. In addition, greater participation in IPN also brings investment and provides job opportunities, which the economy needs.

Table 2. Share of Foreign Value Added in Exports (%)

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<tbody>
<tr>
<td>Share of foreign value added in Indonesia’s exports</td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>12.5</td>
<td>17.3</td>
<td>16.5</td>
<td>14.6</td>
<td>16.5</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>19.6</td>
<td>24.3</td>
<td>22.3</td>
<td>21.5</td>
<td>26.7</td>
</tr>
<tr>
<td>Share of foreign value added originating from ASEAN</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>8.3</td>
<td>13.0</td>
<td>18.0</td>
<td>19.2</td>
<td>38.6</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>7.7</td>
<td>12.4</td>
<td>17.3</td>
<td>18.3</td>
<td>40.8</td>
</tr>
</tbody>
</table>

Source: Calculated by the author from the OECD-TIVA database.
FDI in Indonesia

The emergence of the IPN and participation in it also suggest that ASEAN initiatives in investment are not merely interested in promoting intra-regional investment but also in making ASEAN as a whole more attractive to FDI. Indeed, there has been increasing FDI into ASEAN Member States in recent years, including Indonesia. Nevertheless, the FDI contribution to gross fixed capital formation in Indonesia has been relatively small compared to its ASEAN peers. In 2014, FDI accounted for only 8% of the gross fixed capital formation in Indonesia, compared to 12.5% in Malaysia, 10.5% in the Philippines, 13.5% in Thailand, and 21.8% in Viet Nam (UNCTAD and ASEAN Secretariat, 2016).

As Figure 2 shows, there is an increasing trend of FDI coming to Indonesia. However, as a percentage of GDP, FDI remains relatively small. Before the Asian financial crisis, almost 70% of FDI went to the manufacturing sector, attracted by Indonesia’s comparative advantage in labour-intensive industries. Investment shifted towards the services sector after the crisis and later to the primary sector, such as mining and agricultural plantation, when the commodity boom took place in the mid-2000s, although investment in the secondary sector has been gaining more importance lately. The largest proportion of FDI comes from Singapore, Japan, European countries, and the Republic of Korea.

**Figure 2. FDI Inflows to Indonesia by Sector, 1990–2015**

FDI from ASEAN has always been important to Indonesia. Around 44% of Indonesia’s foreign investment during the last 10 years came from its neighbouring countries. However, 94% of the investment actually came from Singapore. The importance of Singapore in Indonesia shows that the city state plays an important role as a financial and
investment hub in the region, where part of the FDI inflow to Singapore does not add to the productive assets of the country but flows through to other countries.

**Conclusion: Indonesia’s Future in ASEAN Economic Integration**

This paper highlights the role of Indonesia in ASEAN integration, especially in the economic area. Indonesia’s participation has shaped ASEAN integration into the current form. As the largest economy in Southeast Asia, Indonesia would also determine the future direction of economic integration in the region. It is then important to examine whether Indonesia would still play an active role in shaping the future of regional integration, especially among Southeast Asian countries.

While Indonesia has been enthusiastic to pursue greater market access for its exported products, and in return to open up its market, deeper and broader economic integration under more recent initiatives such as AEC 2015 has attracted strong resistance. Indonesian businesses, for example, are among those who fear the implementation of AEC\(^2\). This fear is coupled by lack of credible information on the integration process and how it would affect the economy and business\(^3\). Indonesia’s current political-economic aspirations that focus mostly on domestic issues, such as infrastructure development and logistic costs reduction, have also shifted the country’s attention to and involvement in regional integration. The general perception is that by solving these domestic issues, Indonesia would improve its economic competitiveness.

That does not mean the country neglects its economic integration initiatives with its major partners. However, it is more selective in pursuing integration. Currently Indonesia is negotiating bilateral trade agreements with two major partners, namely Australia and the European Union. President Joko Widodo also expressed interest in joining the Trans-Pacific Partnership, eyeing the market of the United States. It seems that the country is willing to sign an agreement with partners that can offer tangible benefits, either from market access or from economic cooperation and capacity building opportunities.

\(^2\) In one survey of companies’ perceptions, Indonesian companies indicated greatest concerns regarding ASEAN integration. Around 42% of the respondents regard the integration as a threat, compared to only 10% in other ASEAN Member States (see the results of the survey at [https://www.bcgperspectives.com/content/articles/growth_globalization_winning_asean_how_companies_are_preparing_economic_integration/?chapter=3#chapter3](https://www.bcgperspectives.com/content/articles/growth_globalization_winning_asean_how_companies_are_preparing_economic_integration/?chapter=3#chapter3)). While the survey has many weaknesses, it gives an indication of how the business community in Indonesia sees the process.

\(^3\) One of the biggest concerns among Indonesians regarding the implementation of AEC 2015 was the invasion of foreign labour from other ASEAN Member States. That had never happened because the AEC did not aim for free movement of labour. However, false information has led to opposition against ASEAN economic integration.
On whether Indonesia plays an active role in ASEAN’s future integration depends on whether the initiatives are perceived to benefit Indonesia or not. It is then important for ASEAN to come up with some tangible initiatives to increase its attractiveness among Member States, including Indonesia. But it is even more important for Indonesia to know its interests in regional integration and to know the benefits it would bring.

The availability of credible information is crucial in getting political support and to obtain domestic consensus on the country’s interests in ASEAN integration. The Government of Indonesia should convey detailed and sincere information about the benefits and consequences of the integration. This can be done only with more research and evidence-based information on the impact of economic integration. Failure to facilitate such activities would lead to misunderstanding that eventually would evolve into opposition.

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Lao PDR

National Institute for Economic Research (NIER), Lao PDR

Leeber Leebouapao, Vice President

Amphaphone Sayasenh, Researcher

Introduction: Historical Background

The history of present-day Lao PDR dates to the 14th century with Fa Ngum, the first king who successfully united numerous small states and subsequently founded the Kingdom of Lan Xang. The Lan Xang Kingdom was one of the largest states in the region, whose territory encompassed the Mekong River in the middle from north to south. Due to its central geographical location in Southeast Asia, the kingdom became an important centre of trade, becoming wealthy economically and culturally. Lan Xang’s territory and power continued to grow until the end of the 17th century. Its rise culminated in the long reign of King Souligna Vongsa, between 1637 and 1694, at times called the ‘Golden Age’ in the country. After a period of internal conflict, the kingdom disintegrated in the 18th century into three separate kingdoms – Luang Prabang, Vientiane, and Champasak.

In 1983, it became a French protectorate, with the three territories uniting to form the country of Laos; this altered the borders of the country. Anti-imperialist movements were organised in many parts of the country. Since the 1930s, the battles of the Lao people have been closely connected to the battles of the three countries in Indochina. In 1945, at the end of World War II, Laos briefly gained independence, only to be re-occupied by French troops in early 1946. In 1949, it was granted autonomy by the Government of France; in 1953, it gained full sovereignty, with a constitutional monarchy. Shortly after independence, in late 1955, the United States (US) Department of Defense created a special Programs Evaluation Office to replace French support of
the Royal Lao Army against the Pathet Lao, the communist-supported movement. This marked the beginning of a long civil war, which ended in 1975 with a victorious Pathet Lao. The monarchy was abolished and the Lao People’s Democratic Republic (Lao PDR) was established on 2 December 1975.

After the establishment of the Lao PDR, its government adopted a centrally planned economy. Such an economic system is characterised by a high degree of centralisation of economic decisions, strict control, and limited reliance on market forces. What to produce, by whom, and for what uses were subject to administrative decisions. During the first Five-Year Plan 1981–1985, the state continued to control the economy in order to (i) support agriculture–forestry production to ensure food self-sufficiency, (ii) repair existing factories and create a number of new industrial facilities, and (iii) construct basic infrastructure. At the end of the first Five-Year Plan, the Lao PDR achieved some progress towards economic development especially in rice production. However, growth was accompanied by high inflation, large budget deficits, increasing trade deficits, overvalued and multiple exchange rates, and increasing foreign debts. It was against this backdrop that the government reappraised its development strategies and began a series of reform processes.

In November 1986, the Fourth Party Congress approved the New Economic Mechanism (NEM). The reform programme under the NEM includes measures to (i) reform the economic system to allow market forces; (ii) open up the economy; and (iii) stabilise, deregulate, and improve its performance. Although the NEM was endorsed in 1986, reforms started very slowly. The initial reforms in 1986–1988 were limited mainly to improving the structure and performance of state-owned enterprises, selective deregulation of agricultural marketing management, and private sector development and trade reform. Since 1988, the reform process gathered momentum and major measures have been undertaken to improve macroeconomic management, including for fiscal, monetary, and trade policies and state-owned enterprises. At the micro level, price liberalisation, enterprise reform, and improvement of the legal framework were carried out. The first foreign investment law was promulgated in 1988. Price liberalisation, agriculture, and enterprise reforms have been intense. Reforms in fiscal, monetary, and trade policies were considered moderate whereas those of the legal framework were the weakest.

As a result of the reforms, economic performance improved substantially as annual gross domestic product (GDP) growth rates averaged 6%–7% between 1989 and 1994, exchange rates unified and stabilised, and the inflation rate fell from more than 60% in 1989 to 6.8% in 1994 (Than and Tan, 1996: 8). Significantly, most prices are now market-determined, economic decision-making decentralised to a great extent, and
many macroeconomic management instruments have been put in place. In addition, the Lao PDR’s economy has become more integrated internationally and regionally because of border agreements with neighbouring countries and the promulgation of the foreign investment law. The major step in international integration was in July 1992 when the country signed the Bali Treaty of Amity and Cooperation in Southeast Asia. With this official action, the Lao PDR won observer status in ASEAN in the same year. This event marked the beginning of the new era in the Lao PDR’s regional economic cooperation with its neighbours, particularly with then six countries of ASEAN. Following Viet Nam’s membership in ASEAN in 1995, the Lao PDR became a full member in July 1997. The year 2017 marks the 30th anniversary of the Lao PDR’s membership in ASEAN and the 50th anniversary of ASEAN. For these special occasions, this paper aims to provide insights on the relationship between the Lao PDR and ASEAN by recounting the historical background of ASEAN–Lao PDR relations over time, analysing the impact of ASEAN integration on the Lao PDR, and assessing the opportunities and constraints of ASEAN from the perspective of the Lao PDR.

ASEAN–Lao PDR Relations since 1967

1967–1986: Difficult times for ASEAN–Lao PDR relations

ASEAN was established in August 1967 when five Southeast Asian countries – Indonesia, Malaysia, the Philippines, Singapore, and Thailand – signed the ASEAN Declaration. Its establishment was amidst rising regional tension and conflicts in Indochina, which needed a regional framework that would promote economic growth, safeguard regional peace and security, and display solidarity against communist insurgency and expansion in Indochina.

In 1967, Laos was undergoing an intense civil war that started in 1955 between the Royal Lao Government, who received support from the US, and the Pathet Lao communist movement under the leadership of the Lao People’s Revolutionary Party, who won and founded the Lao PDR in 1975. The communist party negatively viewed ASEAN as a tool of US imperialism.

The period 1975–1986 was characterised by the Cold War. It was an ideological war between socialism led by the Soviet Union and capitalism led by the United States. As mentioned earlier, after the establishment of the Lao PDR in December 1975, the Lao People’s Revolutionary Party, the sole leading party, adopted the socialist-oriented political regime and centrally planned economy. As a result, the government emphasised its political and trade relationships mainly with socialist countries, namely the Soviet
Union, Eastern European countries (East Germany, Poland, Czechoslovakia, Bulgaria, Hungary, Rumania), Viet Nam, China, North Korea, and Cuba.

The Lao PDR communist party’s view of ASEAN did not improve. Trade relations with Thailand, one of ASEAN’s founding members, deteriorated as Thailand strongly supported the US during the civil war era. The Lao PDR’s economy remained closed until 1986, when worsened economic conditions and the external environment called for alternative economic policies, resulting in the launch of the NEM in 1986. As a result, the period between 1967 and 1986 is considered a difficult time for ASEAN–Lao PDR relations.

1986–1997: Shifting from political isolation to cooperative relation

In the mid-1980s, the global Cold War was relaxing and gradually ended in most regions. Economic reforms significantly took place in Eastern European countries, led by the Soviet Union, and in East Asian countries, particularly China and Viet Nam. The Lao PDR, with its centrally planned economy, saw a steadily worsening economic situation, declining living standards, and increasing external debts. Concerned about the worsening economic condition and encouraged by the global reform process, the Government of the Lao PDR launched the NEM to shift from a centrally planned economy to a market-oriented system in 1986. Measures to improve macroeconomic management were implemented; these included reforms in fiscal, monetary, and trade policies. At the micro level, price liberalisation and agricultural and non-agricultural enterprise reforms were undertaken.

Those reforms improved economic conditions and people’s living standards. In addition, the Lao PDR’s foreign relations expanded – from a closed political relationship mainly with socialist countries to a more open one. Its economy became more integrated with the world, especially with Southeast Asian countries, because of border agreements with neighbouring countries and the promulgation of the first foreign investment law in 1988. The political and ideological differences of ASEAN–Lao PDR relations were significantly relaxed and normalised. Driven by economic imperatives, its open-door policy, and improved view of ASEAN, the Lao PDR, in July 1992, signed the Bali Treaty of Amity and Cooperation in Southeast Asia, along with Viet Nam, and acquired observer status. Motivated by Viet Nam’s full membership in ASEAN in 1995, the Lao PDR applied for ASEAN membership in March 1996 and became a full member on 23 July 1997. This officially marked its shift from political isolation to cooperative relations with ASEAN. In addition to joining ASEAN, the government also applied for membership in the World Trade Organization (WTO) in July 1997.
1997 to present: From cooperative relations to regional integration

The Lao PDR had several reasons and motivations to join ASEAN, foremost of which is the potential benefits in socio-economic development and cooperation, and in political-security affairs. Specifically, it hopes to transform the disadvantage of being a small landlocked country into the advantage of being the land linking ASEAN neighbouring countries with China, where there are bigger markets. Also, by joining ASEAN and applying for WTO membership, the Lao PDR expected to raise its role at regional and international platforms, attract more official development assistance and foreign investment, and expand its trade. The government has, therefore, attached great importance to and supported the deepening and expanding regional and international integration. It has also been greatly responsible for fulfilling commitments under ASEAN and beyond. These have been well evidenced in many policy documents. For example, the 7th Five-Year National Socio-Economic Development Plan (7th NSEDP) for 2011–2015 (GOL, 2011) clearly set the goal for the Lao PDR to help achieve the establishment of the ASEAN Economic Community by 2015. To achieve this goal, the 7th NSEDP listed tasks to be implemented, including developing a legal system to support the establishment of a common market: (i) improving the effectiveness of ASEAN coordination; (ii) creating an enabling and favourable environment for competition especially improving human resources in professional skills and foreign languages; (iii) promoting and protecting intellectual property rights; building transport infrastructure; (iv) improving tax collection; and (v) strengthening e-commerce. The 10-Year Socio-Economic Development Strategy until 2020 and the 8th National Socio-Economic Development Plan (2016–2020) (GOL, 2016a) continue to highlight the importance of regional and international integration for the Lao PDR. These also encourage participation of integration processes with strong ownership and great responsibility. These policy documents clearly show that the country is on the journey towards regional and international integration.

Impact of ASEAN Integration on the Lao PDR

After a long period of civil war and a decade of centrally planned economic regime, joining ASEAN was an important milestone for the Lao PDR’s open-door policy and a major step towards a market-oriented economy. As a member of ASEAN, the Lao PDR must adjust its national policy frameworks, including for security, socio-cultural, and economic development, to be consistent with ASEAN frameworks. The roadmap for an ASEAN Community 2009–2015 – comprising the ASEAN Political-Security Community Blueprint, ASEAN Economic Community Blueprint, and ASEAN Socio-Cultural Blueprint – has improved the policy frameworks of the country in the last
decade. However, it is worth recognising that for trade and investment, the country has not benefited solely from ASEAN’s framework but, to a great extent, from the WTO accession process. The Lao PDR submitted its application for WTO membership in July 1997 at the same time it officially became a member of ASEAN. Since then the country has drawn a lot of technical assistance from donors to support its domestic reform and institutional building, and strengthen human resource capacity and coordination mechanism. This improvement in soft infrastructure has been complementary to the implementation of ASEAN commitments. Therefore, when analysing the impact of ASEAN on the Lao PDR, the impact of the WTO accession process should be mentioned.

**Impact on the Lao PDR’s national policies**

Since its membership in ASEAN, the Lao PDR has been actively cooperating with Member States to make the region one of peace, stability, and prosperity. In building the ASEAN Community, the country has attached great importance and attention to this and has implemented the blueprints of the ASEAN Political-Security Community, ASEAN Economic Community, and ASEAN Socio-Cultural Community. By doing so, the Lao PDR has improved and adjusted its national policies accordingly. The government exerted genuine effort to improve the rule of law and transparency by reforming its legal system. The effort has been reinforced by the WTO accession process. For example, since 2000 more than 90 new and amended regulations have been issued, including 26 new laws and 18 decrees. In addition, there is also an effort to increase transparency and public participation by launching a web-based official gazette in 2013. The Lao Official Gazette is an electronic source of all laws and regulations and a platform where the public can provide comments on draft legislations.

In the area of political–security, the country has fostered mutual understanding on the political system, culture, and history among ASEAN Member States through increased cooperation and relation on regional political and security matters, including regular exchange of information at the governmental level. Moreover, the implementation of the ASEAN visa exemption framework, coupled with tourism promotion efforts, has helped boost the number of ASEAN visitors to the Lao PDR and that of Lao visitors to other ASEAN Member States. To a great extent, this has promoted a better understanding among ASEAN peoples of Member States’ political systems, culture, and history, especially creating more understanding of the Lao PDR. ASEAN frameworks on other important areas – namely anti-corruption, human rights, traditional and nontraditional security – under this pillar have helped the country improve its policies and legal frameworks. For example, to facilitate the implementation of the ASEAN Convention
Against Trafficking in Persons, especially Women and Children, the Lao government promulgated the new Law on Anti–Human Trafficking.

Within the framework of the ASEAN Economic Community, the country has implemented various measures. On trade in goods, it has made great progress in reducing tariffs and setting up institutions and physical infrastructure to improve trade facilitation. To meet the commitments under the ASEAN Trade in Goods Agreement, the Lao PDR adopted the ASEAN Harmonized Tariff Nomenclature (AHTN) for its tariff classification and reduced its import tariff rates from ASEAN Member States. By the end of 2015, the zero import tariff rate covered 89% of the total 9,558 tariff lines under AHTN version 2012 and will be increased to 96% in 2018. The zero rate is also applied to car import. This is considered an important step in promoting regional trade as tariff rates in the Lao PDR were previously high, including a 40% rate for car import. Although the Lao National Single Window has not yet been operationalised, preparation works taken towards it has greatly improved customs procedures. In 2011, the country launched the electronic customs clearance system, ASYCUDA (Automated System for Customs Data), in two pilot sites and rolled out the system in 10 customs checkpoints by the end of 2015. The ASYCUDA system now operates in all 21 checkpoints, replacing the outdated legacy C-2000. The new system allows for risk-based selectivity, which in turn allows the shift away from 100% physical inspection. The amended Customs Law was approved in December 2011; new articles included provisions for the use of e-transactions and electronic signatures and approvals; the application of administrative appeals; and basis for risk management approaches, advance rulings, post-clearance audit, and measures for infringement.

Another achievement is the launch of the Lao Trade Portal in June 2012. The portal was developed to increase transparency of trade-related regulatory information in compliance with the requirements of the WTO and the National Trade Repository under the ASEAN Trade in Goods Agreement (ATIGA). Since its launch, the Lao Trade Portal has improved its coverage of information by adding more types of trade-related information. Currently, the portal contains all types of information specified in Article 13 of ATIGA, except a list of authorised traders. Under trade in goods, the Lao PDR has to improve implementation of standards and conformance, where it has limited legal and institutional foundation. Thanks to the ASEAN Economic Community framework, the Lao PDR has started building legal and institutional ground and gradually implementing the commitment.

As to trade in services, liberalisation continues to be undertaken progressively under the ASEAN Framework Agreement on Services (AFAS). To deepen the level and widen the coverage of its commitment, the country has revised various domestic regulations for
implementation. It also set up institutional bodies and amended domestic regulations to support the implementation of the Mutual Recognition Arrangements on Professional Services. Other important policy measures taken as a result of ASEAN economic integration include the issuance of the Law on Business Competition and deepening SME promotion.

**Impact on human resource development**

As a least developed country and a new member of ASEAN, the Lao PDR has received a tremendous amount of support from development partners and the aid community for its international and regional integration process. Such support is in the form of technical assistance, financial assistance, and, most importantly, capacity-building activities. With the entry of the latter four ASEAN Member States (Viet Nam, the Lao PDR, Myanmar, and Cambodia [CLMV]), there have been concerns about the development gap between the six older ASEAN Member States and the newer four. Against this backdrop, the ASEAN adopted a special programme to narrow the development gap, naming it ‘Initiative for ASEAN Integration’ or IAI. The IAI is a policy framework aimed at providing special support and technical assistance to the CLMV countries to enhance their capacity in implementing ASEAN commitments and agreements. So far, three work plans have been adopted for 2002–2008, 2009–2015, and 2016–2020. Although the first two work plans have low implementation rates, they have benefited CLMV to a certain extent. Under the IAI, the Singapore Cooperation Programme have provided scholarships for CLMV nationals to study in Singapore and have established four training centres in the four countries. To date, the Singapore Cooperation Programme has more than 12,500 Lao alumni. The Trade Development Facility (TDF), a multi-donor trust fund, has also played a very important role in capacity building in areas related to trade and economic integration. The initial TDF1 covered the period August 2008–March 2013, with TDF2 introduced for the period April 2008–2016 with a 1-year extension. TDF1 addresses the key institutional and operational bottlenecks and capacity gaps that hinder cross-border trade, whereas TDF2 focuses on trade policy, trade facilitation, competitiveness, and diversification. In capacity building, the TDF has supported various training related to trade and economic integration, workshops, and platforms to strengthen coordination mechanisms. For example, it has supported the establishment of the working group on non-tariff measures and provided training on data collection, classification, and impact assessment of such measures. It also provided support in training the public and the private sectors at the provincial level. Still on integration, the Lao PDR received support from the Government of the United States through the implementation of the LUNA projects. These projects support effective and equitable implementation of trade agreements, new laws and regulations at both the national level.
and subnational levels, including institutional development and building competitive capacities in both the public and the private sectors. Many development partners and communities also provide various types of support for capacity building, including collaboration with the ASEAN Secretariat, and training programmes.

**Impact on economic relations**

The Lao PDR started its open-door policy in the late 1980s under the NEM. Since then it has entered into various bilateral and multilateral economic cooperation agreements and partnerships; joining ASEAN is one of them. Yet despite attempts to diversify its economy, the Lao PDR’s main economic partners remain its neighbouring countries – Thailand, Viet Nam, and China – because of its landlocked location in the heart of Southeast Asia. Thailand and Viet Nam are ASEAN Member States; and ASEAN frameworks to broaden and deepen regional integration play an important role for the economic development of the Lao PDR, particularly in trade, investment, and tourism.

**Cross-border trade**

Since the implementation of its open-door policy, the Lao PDR’s international trade has continuously increased, except for a few interruptions during regional and global crises. According to Lao official data submitted to the ASEAN Secretariat, the value of the Lao PDR’s total export increased from US$144 million in 2003 to US$3,714 million in 2015, an average annual growth rate of 38%. Similarly, the value of total import rose from US$338 million to US$3,049 million during the same period, which translated into an average annual growth rate of 27% (Figure 1). Despite impressive growth rates of import and export, the extent of trade openness remains low. The trade-to-GDP ratio was 23.7% in 2003 and increased to 53.85% in 2015, with an average value of 40.82% between 2003 and 2015.

In 2003, the value of Lao export to ASEAN was US$253 million and accounted for 71% of total export. The value then grew at an average rate of 40% per year and reached US$2,646 million in 2015. Since the export to ASEAN grew at a similar average rate as total export, its share in total export remains high at 70% on the average. When looking at the disaggregate level, almost all of Lao’s export to ASEAN goes to Thailand and Viet Nam. Exports to Thailand on average accounted for 72% of total export to ASEAN or 51% of the total export in 2003–2015, while those to Viet Nam accounted for 21% of total export to ASEAN and 15% of the total export.
Similar to exports, the value of Lao imports from ASEAN also grew remarkably. Expectedly, Lao import from Thailand accounted for the largest proportion in total Lao import from ASEAN; i.e. it accounted for 83% of total Lao import from ASEAN and 61% of total Lao import, on average between 2003 and 2015.

Interestingly, when using the data from the Direction of Trade Statistics of the International Monetary Fund (IMF), which compiled data from the Lao PDR’s trading partners, the degree of trade openness of the Lao PDR has been higher, with the trade-to-GDP ratio at 53.78% in 2003 and 87.92% in 2015. Sources of discrepancy come from differences in values of both import and export. Figures 2.A and 2.B show that values of import and export from the Lao official source have been lower than those from the IMF’s Direction of Trade Statistics. The discrepancy of import values has been much higher than the discrepancy of export values; and the discrepancy of import has increased over time. Phaydanglobriayao (2017) uses data of import from China and Thailand in 2009 and 2011 from the Lao customs authority and mirrored data from the International Trade Centre’s Trade Map to find evidence of tax evasion. The study finds strong evidence of tax evasion both in the values and quantities of Lao import from these two top main trading partners; tax evasion also increased over time. Unit values of Lao imports from Thailand were under-reported for 2009 and 2011, and mislabelled for 2009. Lao imports from China was under-reported for both years. On the contrary, no study has been linked to the discrepancy of Lao export data. However, there have been documentaries, news, and concerns of illegal logging and illegal log exports in the country over the last decade; this could be a source of the export data discrepancy.
Despite discrepancy of import and export data, the mirrored data from the IMF’s Direction of Trade Statistics show similar results in terms of ASEAN’s role in Lao international trade. The share of Lao import from ASEAN accounted for 73% on average during 2005–2015, and import from Thailand accounted for 88% of total import from ASEAN and 64% of total import during the same period. The share of Lao export to ASEAN in total export averaged at 56.33% in 2005–2015, of which export to Thailand accounted for two-thirds and export to Viet Nam accounted for one-third of total Lao export to ASEAN.

China, the European Union (EU), and the United Kingdom (UK) are major non-ASEAN export markets. Before the mining boom, the share of EU export was 21.55% and that of UK export was 7.2% of total export in 2005, whereas export to China was only 4.3%. After large values of minerals began to be exported to China, the share of export to China dramatically increased to 10.65% in 2008 and to 32.11% in 2015. However, the share of export to the EU declined to 8.74% in 2008 and 4.17% in 2015. This makes China the second-largest export market for the Lao PDR after Thailand.

Lao PDR’s cross-border trade is not only concentrated in terms of trading partners but also in terms of export products. Its main export products are copper, electricity, garments, wood and wood products, and agricultural products. Export of these products accounted for almost 80% of total export in 2015.
**Foreign direct investment**

At the beginning of the Lao PDR’s economic reform and the promulgation of the first foreign investment promotion law in 1989, inflows of foreign direct investment (FDI) were small. Figure 3 shows that FDI in 1988 was US$2 million; in 1989, US$4 million; and in 1990, US$6 million. After the amendment of its investment law and the global economic boom in 1994, FDI in the Lao PDR dramatically increased – from US$59 million in 1994 to US$160 million in 1996. FDI then started to decline due to the Asian financial crisis, went down to US$4 million in 2002 and remained until 2005. When resource sectors, specifically mining and hydropower, started to attract large amounts of FDI. The recent increase has been associated mostly with an increase of investment in the hydropower sector.

**Figure 3. Net Inflows of Foreign Direct Investment, from Balance of Payments**

![Graph showing inflows of FDI from 1988 to 2005.](image)


Before the resources sector boom, Thailand had been the dominant foreign investor in the Lao PDR. Because of the large amount of investment in the hydropower and mining sectors, in 2011 China became the largest investor in the Lao PDR, followed by Viet Nam, and Thailand in third place. As a result, the share of ASEAN FDI in the Lao PDR dropped from 40.7% in 2010 to 20.56% in 2015. The FDI from the balance of payments captures foreign investment using the banking system. Supplementing the balance-of-payments data, the values of FDI approved by the Ministry of Planning and Investment were used to identify countries that are potentially interested in investing in the Lao PDR. Table 1 shows that in 2010–2015, foreign investors from ASEAN who applied for...
investment approval in the Lao PDR include those from Viet Nam, Thailand, Singapore, Malaysia, Indonesia, and Cambodia. On average, investors from Viet Nam, Thailand, and Singapore applied for investment projects worth more than US$10 million, whereas investors from Malaysia, Indonesia, and Cambodia applied for investment approval with values less than US$600,000 on average.

Table 2 shows that in 2005–2010, the mining sector attracted the largest value of FDI application, followed by electricity generation, services\(^2\), and agriculture. During 2011–2015, the top values of approved FDI is in electricity generation, followed by mining, and agriculture. Table 2 reflects that over the last decade, foreign investment was concentrated mainly in the natural resource sectors which are capital intensive and generate limited employment opportunities.

### Table 1. Value of Approved FDI from ASEAN Member States, 2010–2015

<table>
<thead>
<tr>
<th>Country</th>
<th>Number of Projects</th>
<th>Value of Investment (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Viet Nam</td>
<td>88</td>
<td>1,132,246,387</td>
</tr>
<tr>
<td>Thailand</td>
<td>95</td>
<td>1,038,885,515</td>
</tr>
<tr>
<td>Singapore</td>
<td>4</td>
<td>45,720,000</td>
</tr>
<tr>
<td>Malaysia</td>
<td>22</td>
<td>6,692,022</td>
</tr>
<tr>
<td>Indonesia</td>
<td>1</td>
<td>550,000</td>
</tr>
<tr>
<td>Cambodia</td>
<td>2</td>
<td>250,000</td>
</tr>
</tbody>
</table>

FDI = foreign direct investment.


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\(^2\) Excluding construction, hotel and restaurant, banking, wholesale and retail trade, public health, healthcare, telecommunications, consultation, and education. A large portion of investment in this sector is in shopping centres.
Table 2. Values of Approved FDI, by Sector

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<tr>
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<tbody>
<tr>
<td></td>
<td>Number of Projects</td>
<td>Value of Investment (US$)</td>
</tr>
<tr>
<td>Electricity Generation</td>
<td>14</td>
<td>2,048,429,828</td>
</tr>
<tr>
<td>Mining</td>
<td>118</td>
<td>2,109,371,391</td>
</tr>
<tr>
<td>Agriculture</td>
<td>681</td>
<td>1,531,473,828</td>
</tr>
<tr>
<td>Industry and Handicraft</td>
<td>575</td>
<td>815,478,232</td>
</tr>
<tr>
<td>Services</td>
<td>394</td>
<td>1,598,584,611</td>
</tr>
<tr>
<td>Construction</td>
<td>73</td>
<td>295,533,369</td>
</tr>
<tr>
<td>Hotel and Restaurant</td>
<td>297</td>
<td>260,316,118</td>
</tr>
<tr>
<td>Banking</td>
<td>14</td>
<td>122,460,347</td>
</tr>
<tr>
<td>Wholesale and Retail Trade</td>
<td>14</td>
<td>122,460,347</td>
</tr>
<tr>
<td>Healthcare</td>
<td>8</td>
<td>9,760,000</td>
</tr>
<tr>
<td>Telecommunication</td>
<td>4</td>
<td>44,779,749</td>
</tr>
<tr>
<td>Wood Industry</td>
<td>146</td>
<td>133,647,481</td>
</tr>
<tr>
<td>Garment</td>
<td>32</td>
<td>18,210,030</td>
</tr>
<tr>
<td>Consultant</td>
<td>101</td>
<td>36,266,832</td>
</tr>
<tr>
<td>Education</td>
<td>554</td>
<td>11,285,976</td>
</tr>
</tbody>
</table>

FDI = foreign direct investment.

Tourism

Over the last decade, tourist arrivals continuously increased. In 2003, about 636,000 tourists arrived; with an average annual growth of 18.51%, they increased to 4,684,429 in 2015. Visitors from ASEAN represented the largest number of tourist arrivals with an average share of more than 75% during 2003–2015. Overall, tourist arrivals in the Lao PDR from all geographical regions have increased, with those from ASEAN and non-ASEAN Asia-Pacific region showing exceptional growth rates (Figure 4). The rapid rise in the number of tourist arrivals from the Asia-Pacific region was associated with the large increase of visitors from the Republic of Korea and China.
Table 3 shows that the number of tourist arrivals in the Lao PDR from all ASEAN Member States increased in 2010–2015, except for tourist arrivals from Singapore and Malaysia which declined in 2014 and 2015. The table also shows that tourists from Thailand and Viet Nam outnumbered those from the rest of the region. The Lao PDR’s effort to promote tourism, the ASEAN visa exemption scheme, and the country’s participation at regional and international stages have contributed to this increase.

### Table 3. Values of Approved FDI, by Sector

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
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<tbody>
<tr>
<td>Brunei</td>
<td>197</td>
<td>354</td>
<td>533</td>
<td>730</td>
<td>564</td>
<td>865</td>
</tr>
<tr>
<td>Cambodia</td>
<td>6,908</td>
<td>7,561</td>
<td>15,140</td>
<td>12,301</td>
<td>15,342</td>
<td>20,625</td>
</tr>
<tr>
<td>Indonesia</td>
<td>2,245</td>
<td>3,338</td>
<td>4,265</td>
<td>5,530</td>
<td>4,812</td>
<td>6,019</td>
</tr>
<tr>
<td>Malaysia</td>
<td>15,427</td>
<td>17,702</td>
<td>22,785</td>
<td>29,739</td>
<td>24,312</td>
<td>24,095</td>
</tr>
<tr>
<td>Myanmar</td>
<td>1,652</td>
<td>1,765</td>
<td>1,730</td>
<td>2,073</td>
<td>2,157</td>
<td>2,661</td>
</tr>
<tr>
<td>Philippines</td>
<td>10,341</td>
<td>11,847</td>
<td>14,281</td>
<td>17,759</td>
<td>15,179</td>
<td>16,709</td>
</tr>
<tr>
<td>Singapore</td>
<td>6,087</td>
<td>7,130</td>
<td>10,545</td>
<td>12,571</td>
<td>9,621</td>
<td>8,258</td>
</tr>
<tr>
<td>Thailand</td>
<td>1,517,064</td>
<td>1,579,941</td>
<td>1,937,612</td>
<td>2,108,566</td>
<td>2,043,761</td>
<td>2,321,352</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>431,011</td>
<td>561,586</td>
<td>705,596</td>
<td>868,450</td>
<td>1,108,332</td>
<td>1,187,954</td>
</tr>
</tbody>
</table>

Source: Ministry of Information, Culture and Tourism (2016).
The Role of the Lao PDR in Regional Integration

The Lao PDR joined ASEAN in 1997 as part of ASEAN enlargement. At the initial stage of enlargement, there have been concerns on roles of new members in region building. However, the Lao PDR, along with other new and founding members, has seen that the 10 ASEAN Member States have fostered regional integration. Already in the pipeline are agendas for deepening integration and making ASEAN a dynamic, rules-based, people-oriented, and people-centred region. As a member of ASEAN, the Lao PDR has attached great importance to fulfilling its commitments and actively engaging in regional activities. Since its membership, the country has been given opportunities to assume the chairmanship of ASEAN in 2004–2005 and 2016. Under its chairmanship, two ASEAN Summits, the 28th and 29th ASEAN Summits, were held in Vientiane back-to-back in September 2016. These are the first two ASEAN Summits following the formal establishment of the ASEAN Community on 31 December 2015 and held in the first year of implementation of the ASEAN Community Vision 2025. During these summits, ASEAN Member States adopted and noted various frameworks and declarations across the three pillars of the ASEAN Community as well as cooperation frameworks between ASEAN and its dialogue partners aiming at ‘Turning Vision into Reality for a Dynamic ASEAN Community’3. The outcomes are a total of 57 documents, including IAI Work Plan III and the Master Plan on ASEAN Connectivity 2025, which are integral parts of the ASEAN Community Vision 2025, and other frameworks and declarations to implement the eight priorities of the Lao PDR’s ASEAN Chairmanship in 2016 and three ASEAN Community Blueprints 2025.

The country’s landlocked location bordered by four ASEAN Member States (Cambodia, Myanmar, Thailand, and Viet Nam) and China can be turned and developed into an advantage – as a strategic ‘land bridge’ physically connecting ASEAN Member States and linking the ASEAN region with a big market, like China. For example, a highway and a railway through the Lao PDR could provide the shortest route from the ASEAN region to China.

With its large hydropower potential, the Lao PDR could also supply the region with electricity. Moreover, the country could potentially leapfrog and plug in to regional value chains to enhance ASEAN’s production base.

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3 This is the theme of the 28th and 29th ASEAN Summits.
Opportunities and Challenges under ASEAN Integration: the Lao PDR’s Perspective

The year 2017 marks the 50th anniversary of the founding of ASEAN. Over the past 5 decades, ASEAN has evolved and overcome various challenges, with steady achievements made in various fronts leading to the formal establishment of the ASEAN Community on 31 December 2015. ASEAN has become a single market and production base with a combined GDP of US$2.43 trillion in 2015, ranking as the seventh largest economy in the world. Building on the achievements in the implementation of the Roadmap for an ASEAN Community (2009–2015), the post-2015 agendas and ASEAN Community Vision 2025 continue to enhance and consolidate the ASEAN Community through a deeper and more comprehensive integration process to realise a dynamic, rules-based, people-oriented, and people-centred ASEAN Community, with vibrant, sustained, and highly integrated economies. ASEAN integration has contributed to Lao PDR’s socio-economic development, to a certain extent, over the country’s 20 years of membership. The ASEAN Community and post-2015 agendas will continue to offer great opportunities for the Lao PDR. However, opportunities will not come automatically; they have to be seized by overcoming challenges and constraints. The section below highlights key opportunities and challenges and constraints that the country could face under post-2015 ASEAN integration.

**Enhanced domestic reform**

Regional efforts to advance towards the ASEAN Vision 2025 – by completing the implementation of measures unfinished under the 2015 blueprints and implementing new commitments – imply that the Lao PDR would have an anchor to further domestic reform. For example, the rules-based characteristic that has been envisioned would require the country to improve its governance, enhance the rule of law, and combat corruption. Being ‘people-oriented and people-centred’ would call for the Lao PDR to ensure that its development process and policy are inclusive and sustainable. In addition, the agendas under the ASEAN Economic Community – such as the ASEAN Single Window; trade facilitation; non-tariff measures; investment environment; financial integration; and promotion of micro, small, and medium-sized enterprises (MSMEs) – would all require the Lao PDR to further improve its institutional and regulatory frameworks. These would potentially bring its rules and regulations closer to other more developed members and eventually contribute to its socio-economic development.
However, to push forward the reform and implement commitments would require financial and human resources and good coordination and understanding among stakeholders. On financial resources, fiscal space has been quite limited over the last decade as revenue collection, despite its growth, cannot catch up with expenditure. The fiscal deficit stood at 7.9% (6.2% with grant) of GDP in FY2015–2016 and averaged at 7.8% (3.5%) between FY2004/05 and FY2014/15. The continued leakage of revenue collection and decline in commodity prices have made expansion of revenue challenging. Limited fiscal space would hinder the reform progress and implementation of commitments. For example, implementing trade facilitation measures and the National Single Window would require a large amount of financial resources to put in place both soft and hard infrastructure. Ensuring that relevant officials attend all working group meetings is also challenging under the current situation. On human resources, limited human resource capacity has been a major problem for both the public and the private sectors because of the low quality of education and its limited coverage. The inefficient recruitment system and non-competitive remuneration in the public sector fail to attract many talents and create mismatches in the system. There is also the weak coordination mechanism and knowledge and understanding gaps among line ministries and between the central and local levels.

**Enhanced support for capacity building**

As ASEAN integration becomes deeper, broader, and more complex, ASEAN Member States and dialogue partners have attached greater importance to assisting the CLMV countries to meet ASEAN-wide targets and commitments and close the development gaps in the region. IAI Work Plan III, adopted during the 28th and 29th ASEAN Summits in Vientiane, is a policy framework that aims to provide special support and technical assistance to the CLMV countries to enhance their capacity in implementing the commitments. It comprises five strategic areas – food and agriculture; trade facilitation; micro, small, and medium-sized enterprises (MSMEs); education; and health and well-being. It also highlights the low rate of implementation of IAI Work Plan II, and thus sets measures to the ensure effective and efficient implementation of IAI Work Plan III. Given the many commitments under ASEAN and the WTO, development partners will likely continue providing support to the Lao PDR in this area.

Over the past decades, support from development partners have contributed substantially to the Lao PDR’s capacity development although the scale and the

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4 Since the mining boom, the mining sector has contributed substantially to revenue collection. According to World Bank estimates, revenue from the mining sector accounted for 14% of total revenue in FY2011/12 and continuously declined to 7% in FY2014/15 and estimated to reach 5.3% in FY2015/16.
coverage have been limited. For example, the majority of government officials have limited English skills, especially those in the provinces, and they are among the most in need of capacity enhancement. However, some training programmes require participants to have a certain level of English ability, eventually leaving out those most in need of training. Also, coordination between government and development partners and among development partners, though it has improved, remains ineffective. This results in overlapping of capacity-building programmes and discontinued participation of government officials. Furthermore, there is a lack of national ownership. In various programmes, the government counterpart is in charge only of administrative arrangements and leaves the technical aspects to international or local consultants, resulting in limited transfer of knowledge and capacity building.

Cross-border trade

With the formal establishment of the ASEAN Economic Community, the Lao PDR now has inexpensive access to a regional market of more than 600 million people. Given the ASEAN frameworks of trade facilitation and ASEAN connectivity, regional and national infrastructure development, and the economic potential of the country, there are opportunities for the country to increase trade diversification. The Lao PDR, Thailand, Malaysia, and Singapore Power Integration Project is, for example, an opportunity for the Lao PDR to broaden its market to export electricity beyond its existing market of Thailand. In addition, there are potential opportunities to plug into regional value chains. The Lao PDR could join regional value chains in certain sectors such as agro-processing, and mechanical and electrical assembly. Potentially, these would boost production and export of agricultural products as well as mechanical and electrical parts, in addition to electricity and its traditional export products. On the import side, consumers would be able to enjoy lower-cost imported goods and increased varieties of choices. Domestic producers would also benefit from cheaper and convenient import of raw materials.

As a least developed country, the Lao PDR has been granted duty-free market access by 38 countries under the Generalized System of Preferences. However, experience has suggested that market access does not guarantee an increase in export as evidenced by limited utilisation of its available trade preferences. Enterprises lack capacity to increase their production, enhance product quality, and identify niche products to export and to penetrate new markets. The Lao PDR also has similar potentials and endowment as its neighbouring ASEAN Member States; but on many fronts, it still lags behind in
such areas as productivity and cost of transportation. Thus, since other countries would also exert effort to grab opportunities, Lao enterprises would find it even harder to compete. On import, reducing tariffs and eliminating non-tariff barriers for import from ASEAN Member States will create competition for domestic producers. Furthermore, if regulatory capacity and infrastructure are not well in place, there will be risks of influx of low quality and harmful imported products.

**Investment**

The Lao investment regime has been quite liberalised and the government has attached great importance to investment promotion. By fulfilling ASEAN commitments, the Lao PDR would be able to increase its international reputation and gain more confidence from potential investors. The ASEAN connectivity plan and regional infrastructure development would increase the country’s attractiveness for investment.

Due to its natural resource endowment, the Lao PDR has attracted large amounts of foreign investment in mining, hydropower, and agricultural land concession, and these are expected to continue playing important roles. However, experience has suggested that there is weak regulatory capacity and a lack of transparency in screening for quality investment and monitoring to ensure compliance. In non-resource sectors, which can potentially generate jobs, the Lao PDR has many challenges to address to attract foreign investment. Its business environment remains limitedly supportive. According to the World Bank (2017a), the country is 136th in the Ease of Doing Business Index in 2016. In 10 areas under Ease of Doing Business, it is ranked 169th in resolving insolvency, 168th in starting business, 166th in protecting minority investors, 158th in getting electricity, 143rd in paying taxes, and 116th in trading across borders. It also does not perform well in logistics. The World Bank (2017b) ranks the Lao PDR 152th in the Logistics Performance Index. Lack of skills and capacity of its labour force is another discouraging factor in attracting foreign investment. The Lao Development Report 2014 by the World Bank (2014) reveals that the skills problem in the country is deeper and more severe than is generally recognised. The report highlights the very low levels of literacy as the main problem. The adult literacy assessment carried out in six countries, including Viet Nam, China, and the Lao PDR, found that Lao adults had the poorest literacy skills; post-secondary graduates performed almost on par with people with only primary education in Viet Nam. Despite international and regional integration processes driving domestic reform and thus resulting in improved regulatory and institutional improvement, there remains large room for further improvement and urgency to accelerate the reform to make the Lao PDR competitive.
Movement of skilled labour

Given the limited supply of skilled labour in the country, the last few years saw an increase in skilled labour from ASEAN Member States to the Lao PDR. Some professionals, such as interior designers and architects, take advantage of visa-free tourism visits to perform short-term services. The ASEAN framework on free flow of skilled labour would potentially provide a reference for the Lao PDR to develop its regulatory and institutional foundation to facilitate, promote, and regulate such movement. More high-quality skilled labour could create spillover effects in knowledge transfer. At the same time, it will also push for an improved education system and skills development through regional cooperation.

More skilled labour, preferred by large companies and international organisations, would increase competition against Lao workers who generally have lower quality of education and limited English skills.

The Way Forward

Deeper and strengthened regional integration will bring opportunities for the Lao PDR to further improve its socio-economic development. However, opportunities are not automatic but need to be grabbed by overcoming challenges and constraints. The following are recommendations to enable the country to do so:

- There must be political will to drive and accelerate domestic reform as required by regulatory and institutional frameworks to fulfil ASEAN commitments, improve the business environment, and enhance the capacity of the public and the private sectors. The Lao PDR also needs to enhance governance and fight corruption.
- Enhance fiscal space by continuing good initiatives to improve revenue collection and reduce unnecessary spending. Fiscal space is essential to support domestic reform, fulfil commitments, and enhance human capacity and development.
- Provide a clear framework to improve effectiveness of support for training and capacity building. This includes clearly identifying areas for assistance and capacity building; strengthening coordination between government and development partners as well as among development partners; taking strong ownership of all activities, especially capacity building for both the public and the private sectors.
- Improve the coverage and quality of the education system. The focus should be beyond primary education and towards the professional level. The Lao PDR needs to look for opportunities for regional cooperation on educational exchanges and learning from ASEAN’s best practices.
In addition to improving the ‘doing business environment’ and enhancing human resource capacity, improve dialogue between relevant government agencies and potential trading partners to identify products for export. Enterprise development and integration policymaking should promote engagement of research institutions and participation of the private sector.

References


GOL (2016b), National Socioeconomic Development Strategy up to Year 2025 and 2030 Vision. Vientiane: Ministry of Planning and Investment.


Malaysia

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Introduction

Malaysia is an active trading nation that is among the largest importers and exporters of goods and among the top 30 trading nations of commercial services. The country’s total trade to gross domestic product ratio is about 200%. Malaysia’s growth, development, and employment have gained, in no small measure, from trade and foreign direct investment (FDI). Since trade and investment are the cornerstone of Malaysia’s economic development, it has adopted a market-oriented foreign trade policy. It is strongly committed to the liberalisation of the economy and has been a strong supporter of the multilateral trading system.

However, the World Trade Organization (WTO) has not evolved rapidly enough, and with the bottlenecks that the WTO has experienced, Malaysia has found it expedient to engage in several regional and bilateral free trade agreements (FTAs). Thus, Malaysia has signed regional FTAs with China, Japan, the Republic of Korea (henceforth, Korea), India, Australia, and New Zealand. It also has bilateral FTAs with Chile, Pakistan, Turkey, India, Australia, and New Zealand. In addition, the Trans-Pacific Partnership agreement has been concluded though not ratified by the United States. The progress of the agreement lies in the balance. Much depends on how the administration of President-elect Donald Trump will view the agreement, though it is generally thought that the agreement has little favour from Trump. Other FTAs that are under negotiation include one with the Gulf Cooperation Council, the European Union, and possibly with Korea and Bangladesh.

Malaysia’s trade policy is aligned with its overall strategy of national transformation. The country’s economic transformation process has been continual. Broadly, it has moved from being based on a policy of import substitution in the 1960s to an economy that was
export oriented and labour intensive in the 1970s. In the 1980s, the emphasis was on resource-based and heavy industries, with a shift to technology-intensive strategies in the 1990s. The evolution in Malaysia’s development journey was marked in 2011 by an emphasis on key growth areas, or so-called National Key Economic Areas. These areas are oil, gas, and energy; palm oil and rubber; wholesale and retail; financial services; tourism; electronics and electrical products; business services; communications, content, and infrastructure; education; agriculture; healthcare; and Greater Kuala Lumpur. These National Key Economic Areas are meant to propel Malaysia’s growth so the country can transform into a high-income nation characterised by innovation and creativity.

Alongside its economic transformation, Malaysia has also attempted to undertake political transformation and the Government Transformation Programme. The latter was initiated in 2010 and was meant to improve the effective delivery of government services. Since 2010, and as part of the attempt to transform Malaysia into a high-income nation, the various transformation programmes have acted as part of a concerted effort to set the domestic foundation for national transformation to take advantage of the external environment. This is where the importance of Malaysia as a small, open economy becomes a compelling force in determining its national economic strategy.

Indeed, the relevance and importance of the ASEAN Economic Community (AEC) should be seen in this context. In other words, the domestic transformation programmes were being undertaken domestically while simultaneously attempting to better manage the global trading environment. The latter was accomplished through the FTAs that were (and are) being negotiated and signed. ASEAN plays an important part in this strategy because the bid to improve domestic conditions and Malaysia’s trading capabilities via FTAs is carried out to position Malaysia in the global economic environment. ASEAN is integral to Malaysia’s development strategy in view of the fact that ASEAN can occupy a place as a key player in the global hub.

ASEAN has always held a special place in Malaysia’s foreign and trade policy. Malaysia’s Minister of International Trade and Industry pointed out that the fact that the ASEAN division is the largest division in the Ministry of International Trade and Industry is testimony to the importance that the ministry accords to ASEAN. ASEAN has been evolving and Malaysia has been an active partner in this process. However, the conceptualisation of the AEC has happened at a critical juncture in Malaysia’s own development path because the country’s goals and aspirations find strong resonance with those articulated by the AEC.
The Government of Malaysia has continually emphasised several issues on the importance of ASEAN integration and Malaysia’s role in it. First, the government has stressed that ASEAN should be looked at as a collective entity (Mustapa, 2015). The points that the government has continually raised in this context include the fact that ASEAN is the seventh-largest economy in the world; it has the third-largest market (in terms of population); a rising per capita income; total trade amounting to about US$3 trillion; and total FDI flows worth about US$136 billion. Second, by virtue of the high direct investments by Malaysia in ASEAN and by ASEAN Member States (AMSs) in Malaysia, huge benefits could be obtained if there were greater regional integration. Third, Malaysia has been pursuing a development strategy aimed at driving its growth through the development of the services sector. Obviously, the country’s growing services sector, which is spreading its wings within ASEAN, would gain from a more deeply integrated ASEAN.

The ASEAN Economic Community and National Strategies

The main policy documents that define and outline the philosophy and approach to Malaysia’s economic development are the New Economic Model (NEM) and the Eleventh Malaysia Plan (11MP). The country’s national economic strategies are largely defined by its economic transformation and government transformation programmes.

NEM was published as a two-volume document that seeks to achieve a high-income status for Malaysia while also addressing sustainability concerns and distributional issues. Thus, the model has a three-pronged approach with attention on income, sustainability, and social inclusiveness. It envisions that Malaysia, aside from achieving other characteristics, will be a market-led and regionally integrated economy, these being among NEM’s objectives. The 11MP acts in unison with NEM in working towards making Malaysia an advanced economy by 2020. The plan places great importance on trade and investment as mechanisms for achieving this objective. The macroeconomic strategies that have been earmarked to bring about the success of the 11MP include improving the productivity of the economy, promoting investment, increasing Malaysia’s export potential and trade balance, and enhancing fiscal flexibility. Obviously, these goals can be achieved through trade liberalisation. Indeed, the plan does specify initiatives that would increase growth through liberalisation, trade facilitation, and regulatory reform. These mechanisms are in line with the thrusts of the AEC.
Many strategies and programmes outlined in the 11MP would, indeed, be facilitated by the AEC’s four pillars: a single market and production base, a competitive region, equitable economic development, and linkages with the global economy. Before going into more detail on the two-way relationship between the AEC and the national development policy, it is worth stating that the AEC’s goals are not contradictory to Malaysia’s own long-term plans. This is firmly held by the government, senior government representatives, and a large section of the private sector. Although some sections of society who think that conforming to the AEC’s plans would be to Malaysia’s detriment, it is a minority view that does not have the support of the government or the business sector.

Indeed, the AEC’s intention to pursue trade in goods has not met with any opposition from any sections of Malaysia’s stakeholders. That is because Malaysia has almost completely eliminated all tariffs. That does not mean that attendant issues do not have to be resolved. One particular case in point is trade facilitation, where much is to be done. While trade in goods is at an optimal level under existing circumstances, the boundaries of efficiency can be moved forward if the supporting services are improved. This is precisely how improving trade facilitation will help the export-oriented industries in Malaysia. The government is aware of this and has been taking positive steps in this direction since the last decade. This has raised expectations among logistics companies, which are now benchmarking Malaysian standards against the highest standards in the world. Thus, firms are now comparing trade facilitation practices in Malaysia against those in Hong Kong and Singapore. The demand for greater openness and the simplification of practices as required by the AEC requires the government to push for the required reforms. In fact, the AEC does provide added impetus for government agencies to undertake the necessary changes.

Trade in services is a more complicated matter since the AEC expects deeper reforms to be undertaken. The government’s response is, again, clear on this area because, as pointed out earlier, the reforms are necessary if the services sector were to grow and add substantially to gross domestic product. From the business side, the feedback is mixed. Some sectors see and anticipate greater liberalisation of the services sector, whereas others are less keen on liberalisation. The banking sector in Malaysia is undoubtedly deeply interested in the liberalisation of services in ASEAN. Nevertheless, this may not be the majority view outside of certain sectors. The banking sector, which is already poised to be a regional player, is obviously interested in the AEC’s liberalisation moves. Similarly, the higher education industry will be interested because it is competitive as it is. But those in the professional services sector have several concerns. There are fears that given the differences in culture and educational systems, allowing the inflow of foreign professionals, such as doctors and nurses, might jeopardise standards and safety.
The question of those providing professional services, such as accounting and legal services, seems distant because of widely differing traditions and language barriers.

The national development strategy agrees with the need for the free flow of investment and the freer flow of skilled labour. In fact, the national strategies as articulated in the development plans (NEM and 11MP) are in agreement with the AEC strategies with respect to the freer flow of skilled labour. It is hard to see Malaysia’s development goals being realised if there are restrictions to the free flow of skilled labour. Nevertheless, investigations reveal that the movement of skilled labour has its constraints. This applies to the banking, insurance, and tourism sectors, more so when it comes to skilled expatriate workers for multinational corporations. The free flow of investment has been considerably relaxed and many equity conditions have been relaxed. But more can be done to liberalise investment, especially in the services sector. The liberalisation of investment in financial services and telecommunications are cases in point. Thus, by subscribing to the AEC, Malaysia will obviously expedite its own national development strategies.

Challenges with the AEC

Non-tariff measures and non-tariff barriers

Tariff barriers have been successfully resolved in ASEAN. This has facilitated trade in goods. However, there has been less progress with non-tariff measures (NTMs) and non-tariff barriers. These remain issues for ASEAN that demand attention to further remove the restrictions to free trade in goods, since NTMs raise the costs of sourcing and enforcement. High sourcing and enforcement costs can affect the market structure, resulting in the loss of productivity, raising the cost of the output, and even driving smaller firms that cannot bear these costs out of the market.

The incidence of NTMs is high for some AMSs. The core NTMs, which have the potential to be non-tariff barriers, are high for Myanmar, Brunei Darussalam, Viet Nam, Malaysia, and Indonesia. On an index of a maximum of 1.0, the core NTM restrictive index is very high for Malaysia (0.52) and Indonesia (0.67) (see Narjoko, 2015). The restrictiveness index of non-core NTMs, referring most likely to technical barriers to trade or TBTs, have been noted to be moderately high for Brunei, Viet Nam, and the Philippines; it is very high for Malaysia (0.53) and Indonesia (0.59).

NTMs, as has been observed in ASEAN, do have an impact on production costs, and this varies by company size (Narjoko, 2015). NTMs affect medium-sized companies
the most. Large firms are least affected, while small firms are moderately affected. Large firms can absorb the cost of NTMs; small companies, on the other hand, are not much worse off despite the higher costs because many of them do not export their products. The policy implications are clear for ASEAN. The AEC blueprint places special emphasis on small and medium-sized enterprises (SMEs). This, therefore, calls for a more concerted attempt at improving testing procedures as well as simplifying them. It is also necessary to reduce the bureaucratic procedures relating to NTMs so that firms do not have to bear the burden of allocating more staff or more staff time for these purposes. In part, this requires more investment in laboratories and testing facilities that need heavy investment. However, unless the costs involved in servicing NTMs are reduced, SMEs will be adversely affected.

With a low-tariff environment, non-tariff measures assume greater importance. NTMs can (and are often) used as a regulatory trade policy and protectionist tool. Malaysian manufacturers and traders are aware of the importance of NTMs in this context as NTMs affect the import of raw materials, intermediate inputs, and final products. Various reasons, including safety, health, and sanitary reasons, can be used to restrict trade if NTMs are used negatively. This is especially the case for SMEs.

These issues have serious implications for Malaysian SMEs. Malaysia seeks to develop its SMEs and this is more pressing now since the country wants to increase its aggregate demand, primarily through domestic demand. SMEs have an important role to play in this scheme. NTMs must be reduced to encourage the growth of SMEs and allow them to become more export oriented. The AEC goals of reducing NTMs are, thus, in line with Malaysia’s own intention of encouraging the growth of SMEs.

The Royal Malaysian Customs (Prohibition of Import) Order has a list of NTMs. Four schedules in this list classify imports based on the purpose of the NTM. The first schedule lists the goods for which imports are totally prohibited. The second schedule lists imports that are allowed only with import licences for health, sanitary, security, environmental, and intellectual property protection. The third schedule records imports imposed with licences to protect local industries, while the fourth schedule records goods for which imports are only allowed according to the manner of importation specified.

Over the years, non-tariff protection on automobiles and parts have been maintained or even increased. The World Trade Organization (2006) has stated that the automotive industry is protected by high import duties and by the import licensing system. The high excise tax structure is a major barrier to the import of foreign-manufactured automobiles. This, combined with the tax exemptions given to local cars based on local
content, effectively acts as a barrier for foreign cars. The issuance of import permits to Bumiputera businesses are also perceived as discriminatory (Ministry of Trade, Economy and Industry of Japan, 2007).

In the third schedule, temporary protection from imported goods was granted to domestic producers through import licences. Several reviews in the number of products listed in this schedule were made throughout the period of analysis, which resulted in more products being included. In the fourth schedule, only safety seat belts, electrical apparatus, and electrical luminaries for fluorescent lamps were found listed in 1979 and 1981. A majority of the products in the schedule were included only since the late 1980s. Since 2000, that is, after the financial and economic crisis of 1997, the number of products imposed with NTMs from the fourth schedule has declined. Devadason (2006) points out that the proportion of import licences in the country’s manufacturing industry has increased from 8% to 14%. Nonetheless, NTMs or non-tariff barriers are generally prevalent in the country’s manufacturing sector (Hanif et al., 2011). The Malaysian government imposes quotas on the quantity of foreign rice that is imported into the country in the interests of local paddy farmers. It is with this aim in mind that the government set up BERNAS (Padiberas Nasional Bhd).

There are still outstanding issues with respect to NTMs, but there are areas where perceivable progress is apparent. One such instance is the case of the establishment of good testing and standards processes. The Standards and Industrial Research Institute of Malaysia has good facilities to ensure that standards are measured according to international benchmarks. However, interviews with SMEs suggest that more can be done to simplify documentation and procedures. Besides, the limited number of well-trained personnel at the Standards and Industrial Research Institute of Malaysia is quoted as a reason for delays in approval.

Services

A key goal of the AEC blueprint is to achieve the free flow of services. However, the free flow of services is inextricably bound with domestic regulatory reform and is further complicated with prudential concerns, particularly in the financial services sector. As such, the free flow of services is a difficult goal to achieve, but ASEAN is committed to removing restrictions in the trade of services. Towards this end, it has been engaged in negotiations to remove the impediments through the ASEAN Framework Agreement on Services (AFAS).
Examining the progress of liberalisation in AFAS, Narjoko (2015) observes that while services liberalisation substantially improved between the fifth and seventh package negotiations, this was not the case in the changes from the seventh to the eighth packages. In the case of the latter, there was an increase of about 1% between both packages, while for the earlier it is about 12%. Narjoko argues that the liberalisation rate has increased for Mode 3 under AFAS 8 by close to 2 percentage points, with a marginal decrease in the liberalisation rate for Mode 1. A significant contribution to the increase in Mode 3 liberalisation comes from priority integration sectors (i.e. medical and health, communications, and tourism and hospitality services), which more than compensate the declines registered in logistics and other services. It is significant that there is little progress being made on foreign equity liberalisation rates. The fact that there is little intent to allow foreign investors a majority role in many services subsectors is cause for concern on ASEAN’s progress towards achieving a free flow of services.

As an economy with well-developed financial markets, good regulation, and adequate reserves, Malaysia serves as a good example of how financial market development can work as a good buffer against external shocks. The domestic reforms that were taken in Malaysia following the 1997 economic and financial crisis are illustrative of domestic reform that can prepare an economy for integration within larger financial markets. Thus, domestic reform can and should take place along with regional financial integration. Almekinders et al. (2015) argue that banking integration requires a sound institutional and legislative framework. This can be implemented through a planned approach in order to achieve a single market for ASEAN banking that includes the specification of minimum regulatory requirements for entry, permissible banking activities, regional arrangements for cross-border bank supervision and resolution, and new regional standards and rules with enforcement mechanisms to ensure that there is national compliance to regional rules. In line with this goal, ASEAN capital account integration is intended to take a gradual, correctly sequenced approach, with the necessary safeguards put in place first.

While Malaysia is ahead of many other AMSs on the issue of preparing the right regulatory framework for banking and financial services, this cannot be said for some of the less-developed Member States. This is a source of some discontent among some banking companies in Malaysia, especially those that are already poised to be ASEAN-wide banks. Although Malaysia can take advantage of developments with regard to the AEC in this respect, it lags behind in the case of labour.

The flow of services demands a concomitant flow of labour, particularly skilled labour. However, AMSs have a strong interest in protecting domestic professionals. Singapore is, perhaps, the exception to this policy position since it views the free flow
of skilled labour as adding to the stock of high-quality human capital, which increases Singapore’s competitiveness. The harmonisation of standards is one obstacle to the movement of skilled labour, and more attention must be directed to resolving this issue. Notwithstanding the ongoing process on the harmonisation of standards, there is a reluctance to allow the free flow of professional labour. Malaysia allows the flow of expatriate staff, but only after various needs tests are cleared. Bank Negara Malaysia allows foreign staff to work in financial institutions in Malaysia on the request of multinational companies based in the country, provided they are for short-term purposes. A limited number of senior staff are permitted in foreign-owned financial institutions and on boards of directors. These strict measures can be a constraint to the efficient functioning of banks, particularly foreign-owned banks. Cross-border trade for the banking sector also has more scope for improvement. The ability of foreign banks abroad to lend in Malaysia remains limited. They are also not allowed to raise funds in Malaysia. If these restrictions are lowered, then there will be an expansion of cross-border clearing and settlement services, as well as more securities and foreign-exchange business. A more liberal policy for the establishment of the commercial presence of foreign-invested banks in Malaysia is also necessary. Under the current uncertain global environment, such initiatives will likely be restricted. Also, banks with foreign-invested banks are still not allowed to open branches without the approval of Bank Negara Malaysia. This restriction is not in keeping with the liberalisation of the banking sector.

The tourism industry is another sector where the free flow of services is not permitted. This is not in keeping with the AEC vision. Thus, steps should be taken in a phased manner to liberalise the tourism industry. At present, only four- and five-star hotels with foreign ownership are permitted to be set up. Further, foreign tourism providers can only represent the head office and cannot undertake commercial activities in Malaysia in their own capacity. In addition, the representative offices must be completely funded from sources outside Malaysia. This is a constraint to the functioning of foreign tourism service providers. In the interests of greater liberalisation of services, a freer movement of service providers should be introduced. As a step towards this goal, the paid-up capital that is required by foreign-invested tourism firms should be relaxed. In other words, the foreign equity requirements should be removed to expedite the AEC’s goal regarding the liberalisation of services in ASEAN.

**Investment Liberalisation**

Investment liberalisation is crucial to ASEAN because ASEAN leaders have been concerned about the flow of FDI in favour of China rather than ASEAN. This was felt as early as 2003 during the ASEAN Summit in Bali that year; and this was the driving
force behind the ASEAN leaders’ decision to establish the AEC. In fact, following the declaration to form the AEC, FDI into the region increased. In 2013, China was second to the United States as a destination for FDI. But if ASEAN were to be viewed as a single entity, it would have been the second-largest investment destination rather than China. This highlights ASEAN’s potential as an attractor of FDI in the world.

Within ASEAN, Singapore has undeniably been the most attractive Member State for attracting FDI. Malaysia, Brunei, and Thailand have performed above the ASEAN average in drawing FDI into their economies. There is much disparity between AMSs as far as investment inflows into their respective countries are concerned. This emphasises the need to undertake liberalisation measures to reduce these differences. The fact that Indonesia restricted foreign equity in some sectors while liberalising further equity restrictions in others suggests that it does not support indiscriminate investment liberalisation, but will place restrictions judiciously based on its national interest (Intal, 2015).

The same can be said for many AMSs, Malaysia being another such country with an independent view on investment liberalisation. Malaysia has a fairly long ASEAN Comprehensive Investment Agreement (ACIA) reservation list on goods, but has been making bold efforts to liberalise its services sector. While it has provided preferential treatment to local car makers, it is easing the automotive sector selectively in respect to energy efficient vehicles. This indicates the priority given to a national champion while also attempting to incorporate strategic industrial goals.

The government has long upheld its interest in investment liberalisation. A significant step in this direction was taken in 2009, when various policies were announced in the 2009 Budget Speech by Prime Minister Najib Razak. Among the steps taken was the rationalisation of the investment guidelines as administered by the Foreign Investment Committee, which allowed for greater liberalisation of foreign investment. More path-breaking was the announcement to liberalise 27 sub-sectors within the services sector. The equity condition was relaxed, with the government declaring that the 30% Bumiputera equity condition would not be imposed on these sectors. The exempted sectors included the health and services, tourism, transport, business, computer and related products, and sporting and other recreational services sectors.

Further announcements were made in the 2012 budget, which included proposals to liberalise telecommunication licences. It was also announced that 100% ownership of accounting and tax and courier services would be allowed. The same budget speech further declared that private higher education, international schools, and technical and vocational secondary education services would be liberalised.
The financial sector has long been slotted for liberalisation, and major commitments were made in 2009. The financial liberalisation package included relaxing the issuance of licences to allow more foreign companies to operate in the Malaysian financial services sector. Other policy changes included measures to increase foreign equity ownership limits and relax operational restrictions.

There is clear evidence that the government is serious about liberalising investment. It has taken important steps to liberalise investment, particularly in the services sector. This is necessary in the context of Malaysia’s development because of the various economic corridors that have been launched. Secondly, Malaysia wants to spur national economic growth through the growth of the services sector. Finally, the country is pursuing several FTAs that cannot progress without liberalising investment. There is no doubt that the government is serious in carrying out its goal of liberalising investment, but more can be done. This includes consistency in rules and regulations, benchmarking procedures, and rules that are in accordance with international standards.

**Malaysia and ASEAN**

Malaysia’s relations with its ASEAN neighbours have been improving over the years. Malaysia’s ties with Singapore have improved tremendously in recent times. In the case of Myanmar, Malaysia has had a deep relationship with the country and has played a key role in assisting with Myanmar’s transition into one that is based on the principles of democracy and the aspirations of its people. Not only has Malaysia worked on bilateral ties, but it has also contributed to ASEAN as an entity. A more significant step that Malaysia has taken is to deepen its relationship with China and India, two significant economies that have a long history of economic, political, and social engagement in the region.

For more than 20 years, Malaysia and Singapore were caught in an imbroglio that revolved around disputes regarding land and water. Various issues have plagued relations between the two countries; water has been a particularly point of discord. Three separate agreements were signed between the two countries in 1961, 1962, and 1990 for Singapore to receive fresh water from Johor daily. The 1961 pact expired in 2011; however, the agreements signed in 1962 and 1990 will remain in force until 2061. Singapore is developing its domestic water supplies and can be expected to be self-sufficient in water before the agreements expire.

There have also been disputes regarding the sovereign ownership of islands off Malaysia and Singapore. During colonial times, the British took possession of Pedra
Branca (referred to as Pulau Batu Putih in Malaysia), which remained undisputed until 1979. In 1979, in a map published by Malaysia, Pedra Branca was claimed to be a part of Malaysian territory. Following the disagreement, the issue was submitted to the International Court of Justice, which, in its judgement of 2008, upheld that the island belonged to Singapore. The court awarded sovereignty over Middle Rocks to Malaysia, but ‘refrained from awarding South Ledge to either country, ruling that ‘sovereignty over the low-tide elevation belongs to the State in whose territorial sea it is located’ (The Hague Justice Portal, 2008).

Another issue that has plagued relations between Singapore and Malaysia has been the bridge that links the two countries. Then Prime Minister Mahathir Mohamad proposed to his counterpart, Lee Kuan Yew, in 2000 that the causeway be demolished and replaced with a bridge. Since there was no response from Singapore, Mahathir, impatient with Singapore, decided that Malaysia unilaterally build a short bridge to the midpoint of the causeway, after which the Malaysian half of the causeway would be demolished.

In August 2003, the Malaysian government ordered a private company to start work on the crooked bridge, but Abdullah Badawi, who took over as prime minister just 2 months later, considered it untenable for Malaysia to initiate any unilateral action on the causeway and halted work on the bridge. Not only was the bridge not built, it also led to the worsening of relations between Mahathir and Badawi.

In recent years, under Prime Ministers Najib Razak and Lee Hsien Loong, Malaysia–Singapore relations have improved considerably. Najib has gone on record as having spoken before the Economic Society of Singapore’s annual dinner on 5 May 2015 that Malaysia–Singapore relations have ‘never been better’. He voiced the sentiment, after concluding the Annual Malaysia–Singapore Leaders’ Retreat with Lee, that it would be no exaggeration to say they have never been better in their countries’ histories. The acceptance of the Malaysia–Singapore Points of Agreement of 1990 clearly indicated that Malaysia’s relations with Singapore had improved.

Malaysia has enjoyed cordial relations with Myanmar. Malaysia was keen that Myanmar should return to democracy during the days of its military regime. However, Malaysia strongly felt that this should be done in a non-disruptive fashion. Accordingly, it sought the services of Tan Sri Razali Ismail to foster the transition from the military junta. Tan Sri Razali, as the United Nations’ Secretary-General’s special envoy to Myanmar, played a pivotal role in securing the release of Aung San Suu Kyi from house arrest in 2002.

The present exodus of migrants, particularly with respect to the Rohingyas, is a more delicate problem and one that puts Malaysia in a predicament. This is because although
Malaysia is sympathetic to the plight of the Rohingya Muslim ‘boat people’, it felt that it cannot address their deplorable condition. The initial reluctance in directly assisting the Rohingyas is because of the thousands of people that are trying to flee the country. Malaysia could not absorb the large number of refugees who, if allowed to enter the country, could lead to the cascading inflow of Rohingya refugees totalling hundreds of thousands. The Malaysian government felt that this would cause social problems and, thus, although sympathetic to Muslims, has refused to grant entry to the Rohingyas. However, recently, the government reversed its position on the issue and severely condemned Myanmar’s handling of this minority group. Nevertheless, it must be accepted that holding street demonstrations to protest Myanmar’s position against the Rohingyas is not in line with the ASEAN process, and more diplomatically acceptable channels could have been chosen to communicate Malaysia’s concern for the ethnic group.

In 2015, as Chair of ASEAN, Malaysia adopted the theme ‘Our People, Our Community, Our Vision’. This theme aimed to emphasise that 2015 was meant to focus on people-centred initiatives. The political–security, economic, and socio-cultural pillars of the ASEAN Community are meant to benefit the people of the region, and accordingly, the people-centred dimension was supposed to receive special attention. Malaysia was committed to the process of community building during its chairmanship in 2015. In that context, Malaysia formally established the ASEAN Community, developed the post-2015 vision, helped steer ASEAN closer to its people, worked towards strengthening SMEs, and sought to expand intra-ASEAN trade and investment. Malaysia also strove to strengthen ASEAN’s institutions, promoted regional peace and security, and attempted to enhance ASEAN’s role as a global player.

Looking beyond ASEAN, Malaysia has been building its ties with India. The Prime Minister of India, Narendra Modi, came to Malaysia in a highly publicised visit. Both the bilateral trade agreement with India and the multilateral arrangement through ASEAN have brought the two countries closer in terms of trade and investment. Malaysia is an active investor in India. The investments are in projects such as power, oil refineries, telecommunications and electrical equipment industries, besides highway and other infrastructure development projects. There is also Indian investment in Malaysia in banking, insurance, information technology and software engineering, education, electrical equipment, and railways. Following the improved relations, there has been more trade and investment between the two countries, although they are far from optimal.

Malaysia’s economic and political ties with China have progressed rapidly. On the economic front, China’s trade and investment with Malaysia dominate the picture,
with China being Malaysia’s top trade and investment partner. Chinese investment in Malaysia has been increasing in a wide range of areas, including bridges, ports, and mega infrastructure projects. China has extended its connectivity to Malaysia and there is potentially more investment to be directed to Malaysia in this area. China has also established a university in Malaysia and will extend its technical expertise in the areas of transportation and information technology to Malaysia. Prime Minister Najib Razak’s visit to China in November 2016 contributed to ushering more economic, political, and security cooperation between the two countries.

Moving Ahead

Malaysia is committed to ASEAN’s vision and roadmap. Indeed, Malaysia can gain much from the development of ASEAN as a region. In addition, some of Malaysia’s national strategies are in consonance with ASEAN’s broader goals. The AEC depends crucially on the liberalisation of trade and investment, without which the attempt to connect with the global economy will not work.

Malaysia has been moving ahead in many areas to establish itself as a desirable centre for trade and investment. This includes Malaysia’s strong performance in the World Bank’s Ease of Doing Business Index, its attractiveness as a destination for foreign investors (Baseline Profitability Index), and well as its outstanding performance in the Global Competitiveness Report. All these reports and indices are based on scores that reflect Malaysia’s efforts at liberalisation and openness to the private sector and foreign investors. Many of these criteria are in line with the aspirations of the AEC. Some government agencies, such as the Malaysia Productivity Corporation and Pemudah, are dedicated to creating improvements in efficiency and enhancing the regulatory framework, as well as the government’s responsiveness to the private sector and foreign investors.

Although significant progress has been made in many areas, progress has been slow in others. One area in which more openness is possible is in the movement of workers, especially skilled workers. There is still some reluctance to allow the freer movement of skilled workers and expatriate staff, an area that requires a less restrictive environment. Mutual recognition of awards and qualifications must also be more flexible; but in the first instance, there should be more discussions on these issues.

The Regional Comprehensive Economic Partnership (RCEP) will be an excellent arrangement to overcome many of the obstacles that stand in the way of achieving the required level of liberalisation. It will give Malaysia an opportunity to undertake some of
the necessary behind-the-border reforms and to ensure that the regulatory framework is coherent and supports a more liberalised regional trading environment. Abiding by the RCEP will require Malaysia to work on those areas in which it currently has shortcomings while also overcoming any reluctance on the part of certain groups. It is imperative that Malaysia extend its greatest efforts towards the accomplishment of the RCEP now that the Trans-Pacific Partnership agreement seems to have been laid aside.

The government, with the Ministry of International Trade and Industry at the forefront, has been undertaking constant efforts to increase public awareness of the AEC, its challenges, and how Malaysia can benefit from it. Two obstacles have to be resolved. The first relates to the utilisation of FTAs. Existing FTAs appear to have an unsatisfactory utilisation pattern. This is so for several reasons. First, the utilisation level is less than optimal. Some studies indicate that the average utilisation of FTAs is about 16% on average. There are indications that larger firms and those based in industrial areas use FTAs. Another problem is the lack of knowledge of certificates of origin, FTAs, and the benefits that can be derived from FTAs. These issues will impede the RCEP once it is implemented and so must be addressed systematically, even now.

**Conclusion**

Malaysia has been an active member of ASEAN. It has pursued ASEAN’s objectives assiduously, and has sought to contribute to the development of ASEAN as a strong and vibrant regional entity. As this paper has shown, Malaysia supports the notion of regionalism and sees value in the idea of ASEAN centrality, the latter being very much based on achieving liberalisation.

Malaysia is committed to the ASEAN process of liberalisation. Consequently, the country has been undertaking the necessary reforms to open its markets for trade and investment. While tariffs on goods are not a constraint any longer, more work needs to be done on other areas. Some of the outstanding areas that need to be prepared for greater liberalisation include trade in services and all that it entails, including issues such as the harmonisation of standards. In accordance with the timelines suggested by the AEC, efforts are being undertaken to initiate reform regarding the restrictions arising from NTMs and non-tariff barriers.

On the broader front, Malaysia has maintained good relations with its neighbours. In particular, it has expanded efforts in improving its relations with Singapore. It has also contributed towards the political transitioning of Myanmar. This is an example of Malaysia’s interest in the welfare of individual Member States. But beyond that, Malaysia
also successfully contributed to the ASEAN process when it held the chairmanship. Malaysia made many notable achievements as chair, most significant being the formal declaration on the establishment of the AEC. That aside, it pushed for many initiatives that were directed at accomplishing a people-oriented ASEAN. Malaysia’s interest in ASEAN is a robust and enduring one that includes sustained efforts towards reaching the AEC 2025 goals.

References


Introduction

The establishment of the Association of Southeast Asian Nations (ASEAN) on 8 August 1967 ushered a new development era for the region. Fifty years since its establishment, the ASEAN development journey shows remarkable achievements and economic structural transformations in the 10 Member States. Despite the 1997 Asian financial crisis and the recent global financial crisis, ASEAN occupies centre stage in the global community with its relative share of world gross domestic product (GDP) expanding from 2.6% in 2009 to 3.2% in 2014 (Figure 1). It has achieved a pronounced reduction in poverty and the poverty gap, and significant improvements in health outcomes and literacy (Intal et al., 2014).

Figure 1. Share of ASEAN GDP to World GDP, 2009 and 2014

Source: World Bank World Development Indicators (for 2009); ASEAN Secretariat (for 2014).

1 This is an essay commissioned by and written for the Economic Research Institute for ASEAN and East Asia (ERIA), Jakarta for its ASEAN at 50 publication (volume 3). Permission has been granted by ERIA through Dr Ponciano Intal, Jr., Project Director, to share this essay with the National Economic and Development Authority and the Department of Foreign Affairs.
ASEAN has metamorphosed into a regional bloc moving towards economic integration that finds substance in the establishment of the ASEAN Economic Community (AEC) in December 2015. ASEAN has three pillars: (i) the ASEAN political-security community, (ii) the ASEAN socio-cultural community, and (iii) the ASEAN economic community. The agreement to develop an ASEAN Socio-Cultural Community Blueprint was made on 20 November 2007 at the 13th ASEAN Summit in Singapore (ASEAN Secretariat, 2015b). Philippine advocacies in this area include the following: migrant workers’ protection, social protection, disaster management, climate change, and biodiversity conservation (Philippine ASCC Secretariat, 2015). The third pillar relates to the establishment of a cohesive political-security community. Compared with the other two pillars of the ASEAN Community – the ASEAN economic community and the ASEAN socio-cultural community – this goal may be the most difficult to attain (Baviera, 2013). This will be a long work in progress, but it is important to underscore that political security is the most critical element of any community because it concerns peace and order in local communities as well as stability in the national and regional order. Political instability will chase away and put at risk any gains made in building a regional economic and socio-cultural community. Notwithstanding many difficulties, ASEAN has become an important institution for regional security, peace, solidarity, and communication over potentially disruptive political issues, such as terrorism and border disputes. This paper focuses on the third pillar, more specifically, the impact of ASEAN on Philippine policies and strategies. It examines the challenges and provides some policy recommendations on embedding ASEAN in Philippine policies and strategies.

**ASEAN and Philippine Policies and Programmes**

Since the founding of ASEAN, the region has undergone critical economic structural transformation. The AEC blueprint has four interrelated goals serving as a foundation for the region’s economic integration (Figure 2): (i) a single market and production base, (ii) a competitive economic region, (iii) equitable economic development, and (iv) integration into the global economy. Various agreements that are geared for economic integration have driven the ASEAN Member States’ (AMs) policies, regulations, and strategic thrusts. The AMs have committed to adjust and harmonise existing policies and regulations, formulate new ones, and revoke policies and regulations that hinder economic integration. The AMs’ responsiveness depends on their respective socio-economic and political conditions and political commitment to the AEC vision.

The ASEAN Preferential Trade Agreement was signed in 1977 and by the late 1990s economic integration initiatives had emerged (ASEAN Secretariat, 2015a). In 1993,
the ASEAN Free Trade Area (AFTA) came into effect, while the ASEAN Framework Agreement on Services (AFAS) was signed in 1995. This was followed by the ASEAN Vision 2020 in 2003 that guided the crafting of the overall objective of the Bali Concord II, the establishment of the ASEAN Community. Major agreements include the ASEAN Investment Guarantee Agreement, the Framework Agreement on ASEAN Investment Area, the ASEAN Trade in Goods Agreement in 2010, and the ASEAN Comprehensive Investment Agreement implemented in 2012 (ASEAN Secretariat, 2015a).

Figure 2. The ASEAN Economic Community’s Interrelated Goals

![Diagram](image)

GPN = global production network, IPR = intellectual property rights, SMEs = small and medium-sized enterprises.


The ASEAN Trade in Goods Agreement governs AFTA for intra-ASEAN trade in goods. It covers the elimination of tariff barriers under a tariff reduction program, the elimination of quantity restrictions and non-tariff barriers, and rules of origin wherein only ASEAN products directly produced within the region qualify for benefits of AFTA. As of now, 99% of ASEAN-6 (Brunei Darussalam, Indonesia, Malaysia, Thailand, Singapore, and the Philippines) tariffs are zero.²

Under AFAS, qualified service professionals will have greater mobility within the region, governed by common professional standards based on mutual recognition arrangements.

² Only 68% of tariffs of Cambodia, the Lao PDR, Myanmar, and Viet Nam are zero, but most of these will be zero in 2018.
MRAs seek the mutual recognition of the education, training, licences, and experiences of the region's professionals and skilled workers. Ratification and signing of protocols are necessary to make the MRAs a useful instrument for skilled workers' mobility across the region (Figure 3). Under AFAS Article V: Recognition, AMSs should recognise the education or experience obtained, requirements met, and licences or certifications granted in other AMSs for the licensing or certification of service suppliers. In 2011, the ASEAN Central Bank Governors adopted the ASEAN Financial Integration Framework as a general approach to the integration initiatives under the AEC. The ASEAN Financial Integration Framework aims to have a semi-integrated financial market by 2020.

**Figure 3. ASEAN Mutual Recognition Arrangements**

![Diagram](source: Manzala (2013a).

The Philippine experience shows how a country equipped with the right economic policy and institutional reforms can literally rise from the ashes like a proverbial phoenix. Once dubbed the ‘sick man of Asia’, the Philippines has now outperformed other ASEAN countries (Figure 4). It has leveraged the policy and institutional reforms that have been instituted over the years to achieve substantial economic gains by the start of the third millennium. Table 1 summarises the dramatic economic recovery of the Philippines from the severe trauma of the lost decade of the 1980s, principally brought about by authoritarian rule, to its remarkable performance in the 2000s, even as the global economy was reeling from the impact of the global financial crisis.
Figure 4. GDP Growth Rate of ASEAN-5, 2006–2015 (%)

Source: World Bank’s World Development Indicators.

Table 1. Growth and Employment in the Philippines, 1980–2015

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<th>Value Added</th>
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<td>Average Share</td>
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<tr>
<td>Services</td>
<td>3.3</td>
<td>3.6</td>
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Note: 2000s statistics cover data from 2000 up to 2015 (updated by the author).

Source: Philippine Statistics Authority.
The economic turnaround was underpinned by strong economic fundamentals: (i) improvements in the fiscal space (fiscal deficit at 0.9% of GDP in 2015) (Bureau of the Treasury, 2016a); (ii) manageable inflation (1.4%) (Bangko Sentral ng Pilipinas, 2016a); (iii) a reduction in debt (44.7% of GDP in 2015; the average ratio for the period 2005–2014 was 54.3%); (iv) a growing stock of foreign exchange reserves (US$85.9 billion, equivalent to 10 months’ imports and payments of income and services); (v) investment grade ratings (BBB by Standard and Poor’s, April 2015; Baa2 by Moody’s, December 2015; and BBB+ by Fitch, September 2015); and (vi) political stability (strong democratic governance). Strong consumption and public and private investments, a revitalising manufacturing sector, a surging services sector led by the information and business process management industry, and substantial remittances from overseas Filipino workers (Bangko Sentral ng Pilipinas, 2016b) continue to power the economy. With a young and relatively well-educated labour force, the Philippines can use its demographic dividends and continuing policy and institutional reforms for stronger growth. At the beginning of the third millennium, the Philippines is a rising economic star amidst a raft of economies facing deep political and economic challenges and wide-ranging global risks and uncertainties.

From the 1950s to the 1970s, the Government of the Philippines adopted import substitution policy as its primary vehicle towards industrialisation. The inward-looking import substitution strategy initially worked for the economy, but the protectionist policies and foreign exchange controls eventually took a toll on the economy. A balance of payments crisis in the mid-1980s, large external debt, inefficient manufacturing industries, and an export industry with weak backward linkages eventually stymied growth (Aldaba, 1994; Austria, 2002).

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3 As of September 2016. The stock of foreign reserves is six times the short-term external debt based on original maturity, a better ratio than those of other countries in East Asia and ASEAN.

4 The Philippine Information Technology and Business Process Management (IT-BPM) Roadmap 2012–2016 suggests that the annual revenues for the IT-BPM industry could more than double from US$9 billion in 2010 to US$25 billion in 2016 – equivalent to a 10% share of the global market. The industry expects to employ up to 1.3 million Filipinos and account for 9% of GDP (IT and Business Process Association of the Philippines, 2016).


6 The 10-point economic agenda of the current administration implies a continuation of the market-oriented economic policy reforms pursued by former President Benigno Aquino III. Rodrigo Duterte, elected president on May 2016, will serve a 6-year term with no re-election as stipulated in the 1987 Philippine Constitution. The economy seems to be on a sustained growth path but faces the challenge of making growth more inclusive.
After the trauma of martial rule in the 1970s and 1980s, the Philippine economy recovered slowly at first but picked up with strong growth momentum later. Behind this performance were policy reforms, a transition to a more open economy, and improved governance that boosted economic performance. Trade and industrial policies were geared towards openness, trade liberalisation, privatisation, and deregulation (Llanto and Ortiz, 2015). Medalla (2002) categorised the trade policy reforms into five stages: (i) a pre-reform era of a highly restrictive trade and protectionist policy regime in the post-war period up to the 1970s; (ii) the first major trade reform era during the first half of the 1980s; (iii) a major import liberalisation period during 1986–1988; (iv) the second phase of the Tariff Reform Program, which narrowed the tariff range to mostly within 30%; and (v) the third phase of the Tariff Reform Program under Executive Order 264, which was implemented from 1996 to 2000. In the 1980s, the Philippines undertook initial efforts to reduce tariffs as part of a broader-based industrial restructuring programme (Medalla et al., 1996; Canlas, 2007).

ASEAN’s main point of entry to Philippine policies, regulations, and strategies was the trade sector. The Agreement on the Common Effective Preferential Tariff (CEPT) Scheme for AFTA was signed in Singapore on 28 January 1992. It did not require ratification and entered into force on the same date. AFTA is the primary trade agreement for the Philippines and it has significantly motivated tariff reduction, but other factors have also played an important role in trade liberalisation. Azarcon (1997) noted that shifts in tariff policy in ASEAN have responded to developments on three fronts: (i) multilateral trade negotiations, which resulted in the General Agreement on Tariffs and Trade/World Trade Organization Agreement; (ii) unilateral tariff reforms undertaken by most AMSs; and (iii) the accelerated pace in intra-ASEAN trade liberalisation under the CEPT.

Thus, while the Philippines unilaterally reduced tariffs, it also adhered to commitments to reduce CEPT rates in tandem with the reduction in most-favoured-nation rates. The story of the Philippine Tariff Reforms of 1995 and the subsequent tariff reduction is one of a confluence of unilateral action under the General Agreement on Tariffs and Trade/World Trade Organization Agreement and compliance to the ASEAN-led tariff reduction within the AFTA framework. As Azarcon (1997) puts it, consensus was building within ASEAN towards the adoption of a free trade area as envisioned under the AFTA Agreement in 1992.

Since the trade liberalisation programme of the 1980s and 1990s, ASEAN has informed and strongly influenced the Philippines’ policies, strategies, and regulations. The Philippines has ratified important protocols. Some of those protocols are being implemented, while others, such as consultations, are in the preparation stage for
ratification (Aldaba et al., 2013). The Philippines has ratified the ASEAN Framework Agreement on Multimodal Transport and ASEAN Framework Agreement on the Facilitation of the Inter-State Transport, which are currently being implemented (ASEAN Secretariat, 2015a). On 13 January 2016, former President Aquino ratified Protocol 7 of the ASEAN Customs Transit System of the ASEAN Framework Agreement on Facilitation of Goods in Transit, which was signed on 17 February 2015 in Bangkok, Thailand.

Being part of ASEAN has helped keep the country open, especially when the tendency to waver became intense following the 1997 Asian financial crisis (Aldaba et al., 2013). Executive Order 850 (December 2009) reduced tariffs on imports from ASEAN to zero in 2010, except for a short list of sensitive products. The Philippines CEPT rates are now zero except for sugar at 5%, and rice at 35%.

Philippine trade has shifted away from the United States and the European Union to Asia in the past 30 years. The share of Philippine imports from ASEAN has grown from 15.5% in 2001 to 21.7% in 2013, and 25.3% in 2015, while exports to ASEAN have been at around 15%, with export trade shifting overall to East Asia (Table 2). The country’s main imports from Thailand are motor vehicles, electronics, petroleum products, and chemicals, whereas its main exports consist of motor vehicle parts, electronics and electrical machinery, and minerals. With Singapore, the Philippines’ main imports are electronics, machinery, and petroleum products, while its main exports are electronics and electrical machinery and petroleum products. The top imports from Malaysia are electronics, petroleum, and chemicals, while the top exports are electronics, coconut oil, and petroleum products. Growing intra-industry trade with AMSs is due mainly to the rise of regional production networks, which has shaped the production and distribution of goods and services in the region. Intra-industry trade in ASEAN is complementary rather than competitive, with trade in intermediate goods dominating as AMSs participate in regional value chains that exploit economies of scale, specialisation, and coordination to produce goods and services of higher value (Stephenson, 2013).

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7 Certain products are permanently excluded from the free trade area for reasons of protection of national security, public morals; human, animal, or plant life; and health and articles of artistic, historic, and archaeological value.
### Table 2. Direction of Philippine Trade, Exports and Imports (%)

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2003</th>
<th>2005</th>
<th>2007</th>
<th>2009</th>
<th>2011</th>
<th>2013</th>
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<tr>
<td><strong>Imports</strong></td>
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<td></td>
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<td>71.5</td>
<td>72.5</td>
<td>68.6</td>
<td>73.9</td>
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<td>ASEAN</td>
<td>15.5</td>
<td>39.3</td>
<td>18.7</td>
<td>23.2</td>
<td>25.5</td>
<td>23.7</td>
<td>21.7</td>
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</tr>
<tr>
<td>East Asia</td>
<td>39.3</td>
<td>39.3</td>
<td>39.7</td>
<td>36.7</td>
<td>38.6</td>
<td>37.6</td>
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<td>42.5</td>
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<td>0.8</td>
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<td>1.3</td>
<td>1.3</td>
<td>1.3</td>
<td>1.6</td>
</tr>
<tr>
<td>Middle East</td>
<td>8.1</td>
<td>6.2</td>
<td>7.6</td>
<td>9.5</td>
<td>6.1</td>
<td>10</td>
<td>6.7</td>
<td>4.5</td>
</tr>
<tr>
<td>America</td>
<td>20.9</td>
<td>23.7</td>
<td>20.8</td>
<td>15.9</td>
<td>14</td>
<td>12.6</td>
<td>13.1</td>
<td>12.2</td>
</tr>
<tr>
<td>Europe</td>
<td>10.3</td>
<td>9.6</td>
<td>9.1</td>
<td>9.9</td>
<td>8.4</td>
<td>10.2</td>
<td>12.4</td>
<td>10.1</td>
</tr>
<tr>
<td>Oceania</td>
<td>2.8</td>
<td>2</td>
<td>1.9</td>
<td>2.1</td>
<td>2.9</td>
<td>3</td>
<td>2.6</td>
<td>2.0</td>
</tr>
<tr>
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<td>0.1</td>
<td>0.1</td>
<td>0.1</td>
<td>0.2</td>
<td>0.3</td>
<td>0.2</td>
<td>0.1</td>
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<td>Others</td>
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<td>3</td>
<td>1.4</td>
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<td>100</td>
<td>100</td>
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<th>2011</th>
<th>2013</th>
<th>2015</th>
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<td><strong>Exports</strong></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td>67.7</td>
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<tr>
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<td>18.2</td>
<td>17.3</td>
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<td>18</td>
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<td>40.3</td>
<td>47.7</td>
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<td>South Asia</td>
<td>0.3</td>
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<td>0.4</td>
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<td>1</td>
<td>0.6</td>
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<tr>
<td>Middle East</td>
<td>0.6</td>
<td>0.5</td>
<td>0.6</td>
<td>0.9</td>
<td>1.1</td>
<td>0.9</td>
<td>1</td>
<td>0.9</td>
</tr>
<tr>
<td>America</td>
<td>29.5</td>
<td>21.3</td>
<td>19.2</td>
<td>18.1</td>
<td>19</td>
<td>16.8</td>
<td>16.5</td>
<td>17.4</td>
</tr>
<tr>
<td>Europe</td>
<td>19.5</td>
<td>16.4</td>
<td>16.6</td>
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<td>11.6</td>
<td>11.5</td>
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<tr>
<td>Oceania</td>
<td>0.8</td>
<td>1.3</td>
<td>1.3</td>
<td>1.3</td>
<td>0.9</td>
<td>1</td>
<td>1.1</td>
<td>0.9</td>
</tr>
<tr>
<td>Africa</td>
<td>0.1</td>
<td>0.2</td>
<td>0.1</td>
<td>0.3</td>
<td>0.3</td>
<td>0.4</td>
<td>0.5</td>
<td>0.3</td>
</tr>
<tr>
<td>Others</td>
<td>0.7</td>
<td>0.9</td>
<td>1.1</td>
<td>1.3</td>
<td>1.8</td>
<td>2</td>
<td>1.9</td>
<td>3.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Philippine Statistical Yearbook (various years).
The Philippines has been working to have a fully functional national single window (NSW) that will be part of the ASEAN single window. This is a critical measure for effective trade facilitation. The number of government agencies connected to the NSW portal has risen significantly (from 10 to 26 agencies providing electronic licences, permits, and certificates) in the last 5 years. Government agencies also use the system to standardise their processes and decentralise operations, thus improving customer service throughout the Philippines. Electronic viewing and tagging of cargo import/export permits and clearances were initially rolled out in the Manila International Container Port and Port of Manila (Llanto et al., 2015). The recent enactment into law of the Customs Modernization and Tariff Act will strengthen trade facilitation efforts. Its goal is to modernise customs laws, rules, and administration in accordance with the mandatory standards of the Revised Kyoto Convention (Tamayo, 2016) and international agreements.

With respect to the free flow of investments, the Philippines established a National Competitiveness Council composed of key government agencies and private representatives that oversee efforts to reduce the cost of doing business through regulatory reform and improvement in governance. The National Competitiveness Council has recently unveiled Project Repeal, which seeks to revoke regulations that cause an unnecessary burden on private firms. Project Repeal has been motivated by ASEAN-wide efforts to reduce regulatory burden on private businesses. The AMSs are committed to aligning and harmonising regulatory frameworks and fundamentally to reducing regulatory burden and improving regulatory quality and coherence (Llanto, 2015).

Regulatory quality and coherence are critical in stimulating investments and improving the overall investment climate in the region. Regulatory reform has largely been a government effort, but with ample democratic space in the Philippines, dialogues and consultations with private businesses and civil society have now become an indispensable process in regulatory reform. The enormous challenge in regulatory reform in the Philippines is illustrated in Figure 5.

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8 The NSW was implemented under EO No. 482. The executive order created the NSW Task Force 14 for Cargo Clearance on 27 December 2005 to ensure an effective formulation, coordination, implementation, and monitoring of the NSW.

9 The Revised Kyoto Convention is the blueprint for modern and efficient customs procedures of the World Customs Organization, to which the Philippines is a signatory.
In the agriculture sector, the government has aligned the quarantine and inspection procedures of Philippine fisheries to ASEAN and international standards (Clarete and Villamil, 2015). In the case of sanitary and phytosanitary requirements, the country has passed a food safety law (Republic Act 10611). The Department of Agriculture implements regulations in line with the requirements set for the AEC. For example, the regulation of harmful chemicals for aquaculture and the use of environmentally safe chemicals and pesticides are in accordance with regional standards. Overall, the country’s fisheries sector has been compliant with the AEC blueprint except for the application of quality and safety standards for small firms and establishing networks and linkages between fisheries cooperatives.

The Philippines is signatory to the AFAS, which seeks to provide market access and national treatment to ASEAN services suppliers. With respect to skilled labour, Republic Act 8981 already allows the entry of foreigners, e.g. ASEAN nationals, subject to foreign reciprocity provisions. In the case of MRAs, the Philippine Professional Regulation Commission (PRC) has developed roadmaps for medicine, dentistry, and nursing (Manzala, 2013b). During 2005–2009, the Philippines signed seven MRAs for engineering, nursing, architecture, land surveying, medical practice, dental practice, and accountancy. The Philippines has a Qualifications Framework (PQF) that the PRC will harmonise with the ASEAN Qualifications Reference Framework (AQRF), which is presently being done by an ASEAN team chaired by the PRC.

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10 Through the Bureau of Fisheries and Aquatic Resources, Bureau of Plant Industry, Bureau of Agriculture and Fisheries Product Standards, and Bureau of Animal Industries.
Manzala (2013a) described the AQRF as a common reference framework that functions as a translation device in comparing qualifications across participating AMSs. It addresses the education and training sectors and incorporates informal, non-formal, and formal learning. Formal learning includes post-compulsory schooling, adult and community education, technical and vocational training, higher education, and lifelong learning. Developing and harmonising the PQF with the AQRF is a long process. The AQRF is still a work in progress. But the important thing is that the PRC and its regional counterparts are conducting regular consultations to prepare their respective qualifications framework and that a regional team headed by the PRC is working on the AQRF.

With respect to financial services, the Philippines enacted Republic Act No. 10641 on 15 July 2015 to liberalise the entry of foreign banks into the country. This is part of its commitment to make the financial and banking industry more competitive and able to address the varying financial services needs of a growing economy. It is a significant step towards financial integration. Bangko Sentral ng Pilipinas (or the Central Bank of the Philippines) and the Department of Finance, the main agencies involved in financial integration, focus on the following: (i) financial services liberalisation, (ii) capital account liberalisation, and (iii) capital market development. They work with their ASEAN counterparts to formulate consistent rules and regulations that conform to the requirements of financial integration and international financial standards.

Among the recent accomplishments of the working group for financial integration are (i) the harmonisation of prospectuses for cross-border primary offerings of securities under the ASEAN Equity Disclosure Standards and ASEAN Debt Disclosure Standards (‘ASEAN Disclosure Standards’), where issuers offering equity and plain debt securities in multiple jurisdictions within ASEAN will only need to comply with ASEAN Disclosure Standards; (ii) completion of framework to reduce the review time frame of secondary listing application; and (iii) launching of the ASEAN Corporate Governance Scorecard and development of the Bond Market Development Scorecard (Bangko Sentral ng Pilipinas, 2016c). The disclosure standards for Philippine corporations will be important for improving corporate governance and public trust in those corporations. The bond development scorecard tracks gaps or barriers to ASEAN bond market development to help widen and deepen ASEAN financial and capital markets. More recently, Bangko Sentral ng Pilipinas relaxed its rules on foreign exchange to facilitate access to foreign exchange by corporates and individuals for legitimate non-trade current account transactions (Bangko Sentral ng Pilipinas, 2016d).
Challenges

Table 3 shows the broad status of Philippine commitments to the free flow of goods, investment, skilled labour, and services. In the case of trade in goods, the main remaining issues are trade facilitation measures and non-tariff measures that can act as barriers to trade. Non-tariff measures, such as technical, sanitary, and phytosanitary requirements, are imposed for reasons of health, safety, and environmental protection. To address this type of barrier to trade, the Philippines must work with other AMSs to harmonise procedures and make their administration transparent. For a more efficient NSW, the Philippines should work further on manifest processing, declaration processing, simplification, and harmonisation, and have all concerned government agencies prioritise the establishment of a fully functional NSW. Ibrahim (2011) notes that implementation of the NSW has been hampered by turf issues among government agencies, a lack of understanding of stakeholders of the value of NSW, and disjointed supply chains. A fully functional NSW should include computerised risk management and documents clearance with post-audit as a tool for trade facilitation (Banomyong, Cook, and Kent, 2008).

<table>
<thead>
<tr>
<th>Free Flow Type</th>
<th>Status</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods</td>
<td>Advanced</td>
<td>0% tariff by 2010 except sugar, 5%; rice, 35%</td>
</tr>
<tr>
<td>Investment</td>
<td>Commenced</td>
<td>Review case of having four investment promotion agencies; investment promotion and facilitation; foreign equity restrictions due to constitutional limitations</td>
</tr>
<tr>
<td>Skilled labour</td>
<td>Commenced</td>
<td>Republic Act No. 8981 allows foreign skilled workers subject to foreign reciprocity provisions; accounting; bilateral negotiations commenced; PRC and DOLE facilitate MRA implementation</td>
</tr>
<tr>
<td>Services</td>
<td>Behind</td>
<td>Philippines has the lowest level of commitment; many sectors unbound under Modes 3 and 4; foreign equity restrictions due to constitutional limitations</td>
</tr>
</tbody>
</table>

DOLE = Department of Labor and Employment, MRA = mutual recognition arrangement, PRC = Philippine Professional Regulation Commission.

Source: Aldaba (2014); author.
With respect to the free flow of investments, while substantial progress has been made in liberalising the country’s foreign direct investment policy, certain significant barriers to foreign direct investment entry remain. The sectors with foreign ownership restriction include mass media (no foreign equity), land ownership (foreign ownership limited to 40%), natural resources, firms that supply to government-owned corporations or agencies (40%), public utilities (40%), and build-operate-transfer projects (40%) (Aldaba, 2012). The Philippines must work on lifting constitutional restrictions limiting foreign equity participation to 40%. A window of opportunity now exists in the current congress, which has expressed interest in improving the economic governance framework to attract investments and create jobs.

While the Philippines has made significant progress in embedding ASEAN into policies and regulations in the goods sector, it seems to face the biggest challenge in services. The Philippines is behind in its services commitments due to foreign equity restrictions under the 1987 Constitution. In an examination of the services restrictiveness index covering the AFAS and ASEAN+1 free trade agreements, Ishido and Fukunaga (2012) show that AMSs have relatively low levels of commitment. The ASEAN average for the AFAS Seventh Package was 0.36, with Thailand at 0.50, Cambodia at 0.41, Indonesia at 0.36, and the Philippines at only 0.33.

With respect to MRAs, there is a need to (i) develop research capabilities in developing labour market information that will guide the development of qualifications and core competencies, and (ii) improve the governance of higher educational institutions through the PQF and AQRF that will increase the transparency and readability of PQF vis-à-vis higher education institutions in ASEAN (Manzala, 2013a).

The government must address the remaining restrictive regulations in the services sector that affect domestic and interregional connectivity. A recent amendment to the cabotage law, Republic Act No. 10668 (21 July 2105), augurs well for full liberalisation of shipping in the future. Before this amendment, only domestic shipping companies could engage in coastwise trade. Now, foreign-flagged vessels are allowed to call at Philippine ports, which enables importers and exporters to load cargoes in foreign ships going in and out of the country. The AEC is about allowing the free movement of goods, services, and people across the region.
Conclusion and Policy Recommendations

The Philippines and ASEAN have a mutually beneficial, symbiotic relationship. ASEAN has influenced and provided impetus to the crafting of better policies, programmes, and regulations. The Philippines has contributed as well to shape ASEAN policies that have led to deeper economic integration among the AMSs, and it has acted in solidarity with other AMSs to achieve the goals of ASEAN. This has been demonstrated in policies, programmes, and regulations that uphold ASEAN’s vision, mission, and goals.

Fully embedding the ASEAN framework into the country’s policies, programmes, and regulations faces certain challenges. It will be to the Philippines’ advantage to address these challenges to have an economic policy and regulatory framework that is coherent, consistent, and harmonised with those of other AMSs in the emerging AEC. With each AMS participating in the policy and regulatory reform journey, at the end, the overall regional benefit from a more cohesive and consistent economic framework will be greater than the sum of the benefits accruing to individual Member States.

In addressing the challenges enumerated in this paper, the Philippines must undertake certain complementary actions: (i) improve industry competitiveness, (ii) address binding constraints to services trade and investment liberalisation, (iii) invest in physical infrastructure and efficient telecommunications systems, and (iv) reduce the cost of power.

In this light, the following are recommended:

- Review the regulatory framework affecting investments, skilled labour, and services to identify and revoke the rules and regulations that impede full implementation of signed ASEAN agreements and protocols.
- Address the constitutional limitations in terms of foreign ownership of land, and the ownership and operation of public utilities and services, which tend to constrain foreign direct investments.
- Continue with efforts to improve governance, such as judicial reform, and elimination and control of corruption, for an environment that is more conducive for business.
- Reduce the cost of doing business through investments in physical infrastructure, power, and logistics. Increase local government investment in infrastructure, especially all-weather roads, bridges, and ports.
- Continue with investment and trade reforms in line with the ASEAN Comprehensive Investment Agreement together with reforming ‘behind-the-border’ policies and regulations, such as economic regulations, corporate governance, and labour laws.
Review non-tariff measures to revoke those that hinder the free flow of goods and services, and work for the full implementation of the NSW.

Assess the costs and benefits of embedding ASEAN agreements in domestic policies and regulations and disseminate the information to concerned stakeholders.

Continue with reforms in basic and higher education as well as in technical-vocational education and training programmes with a view to implement MRAs and facilitate the mobility of professionals and skilled labour across ASEAN.

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Singapore

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Introduction: Historical Background

The Republic of Singapore was established on 9 August 1965. Prior to independence, Singapore had been a British colony since 1824. In 1963, Singapore gained independence from the British when it joined the Federation of Malaya, Sabah, and Sarawak to form the Federation of Malaysia. However, political, economic, and ideological differences led to Singapore’s separation from the rest of Malaysia, and it became a sovereign, democratic, and independent nation on 9 August 1965. The People’s Action Party dominates Singapore’s political scene and has held power since 1959.

Under the British colonial government, Singapore served as a free port for the region. As a regional trading hub, Singapore capitalised on its strategic geographic position at the heart of Southeast Asia. It also served as a service hub for the region in finance, logistics, and shipping. During the colonial period, manufacturing was not developed, but there were a number of indigenous manufacturing firms. These were mostly in light industries, such as food, beverages, and raw material processing. The raw materials were imported from neighbouring countries, especially from Malaysia and Indonesia.

Singapore’s production structure and trade pattern started to change after 1959, following self-governing status granted by the British. The ruling People’s Action Party decided to shift away from its heavy dependence on entrepôts, or transit trade. It was clear to the government then that trading activities alone could not provide enough employment for the workforce, nor could it offer a base for sustainable economic development. This policy conclusion was quite evident to the government when, after gaining independence, neighbouring countries tried to bypass Singapore and develop
direct trade routes with their trading partners. Initially, the industrialisation programme was carried out along an import-substitution approach, with Malaysia providing the domestic market for Singapore’s industrial output. This import-substitution strategy was given a much greater emphasis during the 2 years when Singapore was part of the Malaysia Federation from 15 September 1963 to 9 August 1965. However, the strategy became untenable when Singapore was forced out of Malaysia in 1965 (Low, 1998).

Following separation from Malaysia, the government decided to shift its industrialisation strategy from import substitution to export orientation. To jump-start industrialisation, Singapore had to rely on multinational companies (MNCs), as these wholly owned foreign companies had the critical elements of technology, capital, and market, to produce industrial output for the region and the world. Singapore’s successful experience of export-oriented strategy in industrialisation and its liberal trade and investment policies had great impacts on other countries of the Association of Southeast Asian Nations (ASEAN) in subsequent years. Practically all other ASEAN Member States (AMSs) have followed export-oriented industrialisation strategies and relied heavily on MNCs in various forms to develop their respective economies. As a result of this deliberate large-scale reliance on MNCs, due to Singapore’s limited domestic market, its relative export share to its neighbouring countries gradually declined. By 1980, Singapore’s total trade volume with the United States, Japan, and Western Europe amounted to over 40% of Singapore’s total global trade. In contrast, Singapore’s economic reliance on other AMSs declined throughout the late 1960s and 1970s; in the 1980s, Singapore’s trade with extra-ASEAN markets grew, in relative terms, to dwarf Singapore–ASEAN trade.

Singapore is one of the five original signatories of the ASEAN Declaration, which was signed in Bangkok for the establishment of ASEAN in 1967. The importance, character, nuances, and perception of Singapore’s membership in ASEAN have changed over the years. Nonetheless, membership of ASEAN has been the cornerstone of Singapore’s economic strategy and foreign policy. The Government of Singapore sees active membership of ASEAN as a means to enhance the country’s security, political stature, economic development, and competitiveness, and to provide the region with a strong platform to engage key regional and international players.

ASEAN was established primarily as a political entity aimed at safeguarding regional security and maintaining peace among its members. During that period, the five founding member countries – Indonesia, Malaysia, Thailand, Singapore, and the Philippines – seriously feared that communism would spread from Indo-China to the rest of Southeast Asia. There were also concerns that territorial disputes among neighbouring countries would escalate to become region-wide conflicts. In the words
of Singapore’s first Prime Minister, Lee Kuan Yew, ASEAN’s main achievements in the 1970s were ‘tearing down the psychological barriers or distrust among member nations’ and helping to ‘lubricate relationships which could otherwise have generated friction’ (Lee, 1972). Although the ASEAN Declaration in Bangkok listed economic cooperation as one of the objectives, it was not in ASEAN’s main agenda in the first 10 years following its formation. The levels of trade protection and economic nationalism among AMSs were high throughout the 1970s and early 1980s. Rapid economic development and structural transformation in Malaysia, Thailand, and later in Indonesia, and the increasing use of protectionist trade policies by Western industrialised countries in the late 1970s compelled these Member States to re-examine their strategy and to put more emphasis on economic cooperation. Increased trust and confidence among Member helped facilitate such political and economic transition. Broadly speaking, the importance of ASEAN to Singapore can be divided into four phases: the first phase from 1967 to 1975; the second phase from 1976 to 1991; the third phase from 1992 to 1997; and the fourth phase from 1998 to the present. Singapore’s perception and interpretation of the importance of ASEAN to Singapore vary in the four different periods due to changes in internal and external dynamics within Singapore and among AMSs.


Following Singapore’s forced separation from Malaysia, the country became a sovereign, independent, and democratic on 9 August 1965. Obviously, Singapore’s basic priority was to survive politically and economically amid the heightened regional conflict in Southeast Asia due to the Viet Nam War and Indonesia’s confrontation policy against the formation of Malaysia (Acharya, 2008). In fact, the political and economic survival of Singapore was widely considered as unlikely as it was a small city-state of diverse and non-homogenous ethnic groups of Chinese, Malays, and Indians, without any hinterland of natural resources and industrial capacity. It was against these overwhelming odds that Singapore chartered its nation-building process in a region of political instability and economic uncertainty. Therefore, when the five Southeast Asian nations of Indonesia, Malaysia, Singapore, Thailand, and the Philippines agreed to form ASEAN through the signing of the ASEAN Declaration, Singapore strongly supported the initiative. The formation of ASEAN provided a regional framework for the five Southeast Asian nations to foster regional, political, and security stability amid rising tension and conflict due to the war in Viet Nam and territorial claims among neighbouring countries. At the same time, Singapore embarked on a comprehensive and long-term industrialisation
programme to diversify its economy from overdependence on entrepôt trade. Singapore’s industrial policy is based on an export-oriented strategy through a liberal foreign direct investment (FDI) policy to attract MNCs.

Although the ASEAN Declaration provides agreements on economic cooperation, the underlying objective among AMSs is to provide regional security and domestic political stability. This is particularly true for Singapore as a small city-state as it is vulnerable to an unfavourable external political and security environment. Even with the most liberal FDI policy, good infrastructure, and administrative efficiency, it would have been difficult for Singapore to attract FDI without a semblance of regional security that, in turn, would have negative domestic political implications. Without a large inflow of FDI, it is unlikely that Singapore would have been able to reduce its massive unemployment or sustain the inflow of FDI in its industrialisation programme. Such is the definitive statement on the importance of ASEAN to Singapore’s precarious nation-building process in the early years of its independence.


After the signing of the ASEAN Declaration in Bangkok in 1967, ASEAN heads of government did not meet. The external event that prompted a major change in ASEAN’s orientation among its member states was the fall of South Viet Nam and the subsequent unification of Viet Nam under Communist rule. Initiated by Indonesia, the First ASEAN Summit was hosted in February 1976 in Bali by then President Suharto of Indonesia. During the summit, Member States discussed ways to increase intra-regional trade for the first time. The result was the signing of the ASEAN Preferential Trading Arrangement (PTA) in February 1977. The agreement stipulated a cut of 10% in tariff rates on bilateral trade among all ASEAN countries. The group of products affected was to be selected by each Member State through product-by-product negotiations.

The PTA provided an important framework for trade promotion and economic cooperation among AMSs. However, progress in trade liberalisation was slow in the late 1970s and throughout the 1980s despite two more rounds of tariff reductions in 1981 and 1987. The reason was that the economic interests of individual countries remained strong and entrenched, despite much improved political relationships among Member States. In addition, the scope for economic cooperation was also limited by almost similar stages of economic development and by the different economic strategies adopted by different ASEAN countries. For example, Singapore adopted global free
trade, Thailand and Malaysia adopted export promotion, and Indonesia and the Philippines used import substitution. To protect their own domestic industries, many Member States exploited the advantage of the product-by-product approach in PTA negotiations to exclude sensitive items from the list of negotiation, i.e. product items that would disadvantage their own domestic industries. Many of the items offered for preferential tariffs were in fact irrelevant for AMSs (Wong, 1985).

During this second phase, Singapore progressed substantially in its industrialisation programme through sustained rapid economic growth and structural transformation. From 1985, Singapore moved from mere export promotion of goods to an all-out global free trade approach; from manufacturing to finance and other services; from labour-intensive to capital-intensive activities; and subsequently to technology-intensive activities and innovation to propel its economic growth. During this stage, Singapore moved to middle-income status, then to the lower-upper-income status category. In terms of its gross domestic product and industrial structure, Singapore was far ahead of the other ASEAN Member States. Naturally, to sustain its economic growth, Singapore had to pursue global trade and investment outreach and therefore required a different set of strategies and policies compared to the rest of ASEAN. This can be seen from the much more rapid growth in Singapore’s exports compared to exports to neighbouring AMSs. It is worth noting that Malaysia is more connected and interlinked economically and politically with Singapore but economically with Indonesia.

During the second phase, the importance of ASEAN to Singapore continued to grow and expand as the country considered ASEAN as its base and one of the main pillars of regional security and a source of economic growth. Politically, Singapore was an active member of ASEAN in advocating and promoting ASEAN to the United Nations and to the world’s major powers, such as the United States, China, Japan, and European major powers. Specifically, Singapore played a major role in initiating a nuclear-free zone for Southeast Asia, the ASEAN Regional Forum, and the Paris Accord, which maintained Cambodia’s national integrity and sovereignty. Without ASEAN and its political gravity, Singapore and the other AMSs would have had difficulty in galvanising regional and global attention and support on major issues relevant and important to all the Member States.

Economically, although Singapore is increasingly relying on markets and export destinations outside ASEAN based on its relative export growth and FDI flows, ASEAN, particularly Malaysia and to a lesser extent Indonesia, provides the base sources of growth and economic interdependence for Singapore (the forerunner of the regional production network). During the period, Singapore started investing directly and indirectly in Malaysia, Thailand, Indonesia, and the Philippines. The objective was to
create Singapore’s ‘external wing’ to supplement its limited domestic market and at the same time to be an important economic stakeholder to the process of economic development in ASEAN economies. For example, the formation of the Growth Triangle of Singapore-Johor-Riau among Singapore, Malaysia, and Indonesia was based on mutual respect and mutual interest. Such a ‘win–win’ concept of subregional development promoted the initial concept of regional stakeholders or community that developed further in the successive phase to the ASEAN Free Trade Area (AFTA) and subsequently to the ASEAN Economic Community.

The Importance of ASEAN to Singapore: The Third Phase, 1992–1997

The pace of economic integration accelerated in the early 1990s, when most ASEAN economies started to adopt a more consistent economic development strategy based on FDI-sponsored and export-orientation industrialisation. The incentive to accelerate ASEAN economic cooperation was also due to China’s rapidly emerging economy, which attracted FDI at the expense of FDI flows to ASEAN. Effective economic integration was an important part of the efforts to maintain ASEAN’s attractiveness as an investment destination for MNCs. The grouping reached a new economic milestone during the Fourth ASEAN Summit in 1992 when it agreed to establish AFTA, the first regional FTA in East Asia. AFTA was officially launched in the following year, with the Common Effective Preferential Tariff (CEPT) as the core trade liberalisation programme.

The CEPT spelt out an ambitious timeline for the elimination of duties on all products in intra-ASEAN trade, except those listed as sensitive or highly sensitive unprocessed agricultural products. ASEAN-6 countries (Brunei Darussalam, Indonesia, Malaysia, Thailand, Singapore, and the Philippines) had to eliminate all tariffs by 2010, while the deadline for ASEAN-4 countries (Cambodia, the Lao PDR, Myanmar, and Viet Nam) was extended to 2015. In addition to liberalisation in trade in goods, Member States also set up other mechanisms to liberalise trade in services and investment flows within ASEAN. The ASEAN Framework Agreement on Services was agreed in 1995 with the aim of completely liberalising trade in services among ASEAN Member States in sectors such as air transport, business services, construction, financial services, maritime transport, logistics, and e-commerce.

Notwithstanding the increasingly pro-integration stance and rhetoric taken by ASEAN countries during this period, the reality remained quite different. The strong policy announcements and various agreements were not matched by actual trade or economic...
integration. During this period, the export-oriented growth strategies adopted by almost all ASEAN Member States were successful in accelerating high growth in the individual ASEAN economies through the rapid expansion of export markets to highly developed non-ASEAN markets. They were doing so well in export growth that they saw no urgency to accelerate intra-ASEAN trade. However, the unexpected Asian financial crisis devastated the economies of Thailand, Malaysia, and Indonesia in 1997. Following the financial and economic crisis, a major change in policy and mindset with respect to regional cooperation occurred. The financial and economic crisis taught ASEAN policymakers that rapid economic growth and structural changes urgently required close mutual monitoring and cooperation to prevent future external shocks from adversely affecting individual economies and regional economic stability. Another important lesson learned was that ASEAN needed to bring along major regional economies into the process of regional economic cooperation and integration. Such realisation brought the ASEAN Plus Three concept – namely, ASEAN plus China, Japan, and the Republic of Korea (hereafter, Korea) – as important regional partners to widen ASEAN’s scope and increase its flexibility in forging regional cooperation. A wider and more diversified economic area was hoped to facilitate policy choice and leverage the benefits and costs of economic cooperation and integration.

Some argue that Singapore prospers and derives benefit from its relatively less-developed neighbouring countries. This argument is not supported when examining Singapore’s official economic policy. As a small city-state without natural resources, Singapore’s development and prosperity must always be based on an open and competitive economy. This strictly implies that it must maximise whatever comparative advantage it possesses at any given point of its development stage and ahead of the curve of its competitors. Such a policy objective is possible through long-term, comprehensive, consistent policies that cut across the broad range of government policy supported by efficient bureaucrats and world-class hardware infrastructure and software. In fact, as Singapore develops further economically and socially, it would prefer to deal with more developed and confident neighbouring ASEAN Member States. As a logical corollary to this argument, Singapore strongly supports the acceleration and deepening of ASEAN’s integration process. At the same time, Singapore readily provides substantive economic and technical assistance to the less-developed ASEAN-4 on a bilateral basis and collectively through the ASEAN Development Fund. Naturally, as ASEAN becomes more developed, Singapore faces stronger competition from the other Member States. However, Singapore perceives ASEAN and the economic development process in a dynamic context. A more developed and richer ASEAN also provides wider and deeper opportunities and benefits through a more open and competitive economic environment.
The Importance of ASEAN to Singapore: The Fourth Phase, 1998–Present

Following the Asian financial crisis in 1997, ASEAN’s share of FDI in the developing economies decreased from an annual average of 22.8% in 1990–1995 to only 6.5% in 2001. The difficulty ASEAN faced in the late 1990s was further worsened by the rapidly growing Chinese economy. As China was less affected by the crisis, it was able to attract investment away from ASEAN. In 1990, China accounted for less than 20% of total FDI in developing Asia, while ASEAN took 60%. After the Asian financial crisis, the numbers were reversed.

In the face of the crisis, ASEAN decided to speed up economic integration. Generally, the integration process was divided into three levels. First, to strengthen ASEAN’s competitive position, the grouping agreed to rectify the ASEAN Vision 2020 plan in 1998. The plan called for the creation of the ASEAN Economic Community, which would allow the free flow of goods, services, investment, and freer capital movement within the community. The vision was built on previous agreements, including AFTA of 1992 and the ASEAN Framework Agreement on Services of 1995. To support the implementation of ASEAN Vision 2020, new agreements were signed in subsequent years, including the setting up of the ASEAN Investment Area in 1998 to encourage the free flow of investment in the region, as well as the Hanoi Action Plan (1998) and the Vientiane Action Plan (2004), both of which provide roadmaps to show how ASEAN should progress towards the creation of an economic community.

Recognising that the development gap between the more developed and the less developed ASEAN member countries, mainly Cambodia, the Lao PDR, Myanmar, and Viet Nam (CLMV), needed to be substantially narrowed to achieve effective economic integration, ASEAN introduced the Initiative for ASEAN Integration in 2001. The initiative provides a platform for more developed ASEAN Member States to invest in CLMV and in the Greater Mekong Subregion countries, either through various subregional development projects or on a bilateral basis in areas ranging from infrastructure development to human resource training.

The second initiative of ASEAN’s response to the Asian financial crisis was its decision to strengthen the grouping’s economic links with other economies. The decision came about as it became clear that the costs of an inward-looking economic strategy far outweighed the benefits they conferred on member economies. At the ASEAN Summit in 1999, former Singapore Prime Minister Goh Chok Tong urged ASEAN Member
States to broaden and deepen economic integration internally while at the same time strengthening their links with major economies externally (Goh, 1999).

To this end, ASEAN set up an ASEAN Plus framework, which brought regional major powers, such as China, Japan, and Korea, into ASEAN as official dialogue partners. This opened ASEAN up to more market and investment opportunities. Indeed, economic initiatives, such as the agreement to formalise the ASEAN-China FTA, ASEAN-Japan Comprehensive Partnership Agreement, and ASEAN-Korea FTA, proved to be effective in promoting growth in ASEAN. These efforts led to the emergence of another major regional framework, the ASEAN+3 grouping, which consists of the 10 ASEAN Member States as well as China, Japan, and Korea. Although these three countries have economic importance and leverage that are far greater than what ASEAN can project at the global stage, ASEAN is still widely considered as the hub or core that pulls all the 13 economies together. As part of its efforts to expand beyond its member countries, ASEAN also tried to strengthen economic linkages on a global basis through the setting up of the East Asia Summit and the establishment of cooperative linkages with the European Union and the United States, including the Asia-Pacific Economic Cooperation Forum and Asia-Europe Meeting.

The third aspect of the ASEAN response to the financial crisis was a concerted attempt by member countries to build on the region’s capability to handle future financial crises through region-wide financial cooperation. In this regard, ASEAN worked closely with the three economies within the ASEAN+3 framework. The Chiang Mai Initiative, which provides for a series of swap arrangements to strengthen each member country’s ability to defend its currency during a crisis, as well as the various surveillance mechanisms and attempts at policy consultations and coordination among the 13 economies, are some of the visible results of ASEAN’s post-crisis integration approach. As a result of this wider and more intensive cooperation approach, intra-ASEAN trade increased considerably from about US$58 billion in 1991 to nearly US$300 billion by the end of 2006.

Impact of ASEAN Integration on Singapore

Impact on Singapore’s trade patterns

The various phases of ASEAN economic cooperation and integration over the years had some positive effects on Singapore’s trade patterns in Southeast Asia. Significant growth was not evident in the second phase (1976–1991). From 1977 to 1985, Singapore’s trade with ASEAN increased only from US$5.8 billion to about US$9.5 billion. The slow
growth continued even after ASEAN raised the preferential level of the PTA from 10% in 1977 to 50% in 1988. Visible growth in Singapore’s trade with ASEAN was seen in the third phase (1992–1997) when ASEAN adopted AFTA and the CEPT scheme in 1993. During this period, Singapore-ASEAN trade increased from US$22 billion in 1990 to nearly US$70 billion by the end of 1996. The growth of Singapore-ASEAN trade in the 1990s established ASEAN as a major market for Singapore’s external trade. The share of Singapore-ASEAN trade in Singapore’s total global trade increased from about 20% in 1985 to nearly 30% in 1996. However, this increase did not signify that Singapore’s trade was more oriented towards the ASEAN region in the 1990s. In fact, the trade intensity of Singapore’s trade with ASEAN declined from 1990 to 1996, even though the share of Singapore-ASEAN trade in Singapore’s total global trade increased during this period.

Significant growth of Singapore’s trade with ASEAN occurred only during the fourth phase (1998–present). This was demonstrated in the 170% increase of Singapore-ASEAN trade from US$67 billion in 1997 to US$182 billion by the end of 2015, accounting for nearly 33% of Singapore’s total global trade. The trade intensity of Singapore-ASEAN trade also started to rise during this period, continuing up to the present. Singapore’s trade relations are concentrated with Malaysia, Indonesia, and Thailand, and more recently with Viet Nam. Singapore’s total merchandise trade with those four countries by end of 2015 was US$72 billion, US$43 billion, US$22 billion, and US$16 billion, respectively. Total merchandise trade with the Philippines stood at US$11 billion at the end of 2015.

**Impact on Singapore’s investment patterns**

Through phases two to four, ASEAN has become more integrated; not only has trade with ASEAN expanded but Singapore’s overseas investment has also become regionalised. Singapore’s FDI has grown considerably since the 1990s. The growth of the total value of Singapore’s investment abroad reached some US$173 billion by the end of 2007, before the global financial crisis. A large amount of Singapore’s investment had been allocated to ASEAN, particularly to Malaysia, Indonesia, and Thailand, and to the East Asia region, particularly China and India. By 2014, Singapore’s FDI to ASEAN was US$84 billion, or S$117 billion.

Singapore companies are also showing greater interest in investing in development projects in the Greater Mekong Subregion countries, such as Viet Nam and Myanmar, and to a lesser extent Cambodia. Singapore has been a major participant in the programme since its inception in 2001. Most of the projects involve improving transport and energy infrastructure as well as human resource development in the CMLV countries.
and the Greater Mekong Subregion region. Singapore’s direct investment has been concentrated in Malaysia, Indonesia, Thailand, and Viet Nam, and the FDI value in the four countries was US$29 billion, US$34.3 billion, US$14 billion, and US$3.5 billion at end of 2014, respectively.

**Impact on Singapore’s economic policy**

Despite being the smallest AMS in terms of territorial size and having a small domestic market, Singapore has played a leading role in pushing for trade and investment liberalisation in ASEAN. After the First ASEAN Summit in Bali in 1976, Singapore took the lead in liberalising its intra-ASEAN trade ahead of the signing of the PTA by introducing a 10% across-the-board tariff reduction on its bilateral trade with the Philippines and Thailand in January 1977. When Thailand called for an adjustment on the preferential level set by the PTA in 1987, Singapore set the pace by being the first ASEAN Member State to increase the PTA level to 50% and implement an across-the-board tariff cut on all trade items entering the country. Singapore is also the first ASEAN Member State to comply with AFTA’s timeline by completely removing tariffs for all goods in its ASEAN bilateral trade and imposing almost no restrictions on the flow of ASEAN investment into Singapore (Panagariya, 1999).

Singapore has been so proactive in promoting economic integration in ASEAN for several reasons. Firstly, economic integration helps ensure Singapore’s survival and security. As one of the smallest countries in the region in terms of population and geographical size, and without hinterland or a domestic market, Singapore is both economically and politically more vulnerable than many other ASEAN Member States. Being a predominantly ethnic Chinese state in a region of non-Chinese states, Singapore’s position is particularly precarious. It therefore perceives closer economic linkage with ASEAN countries as an effective way to foster good political relationships with its neighbours and believes an economically prosperous ASEAN will help ensure political stability in the region. Efforts to establish some subregional economic groupings, such as the Singapore-Johor-Riau Growth Triangle, were partly aimed at fostering political cooperation with Singapore’s neighbouring states.

Secondly, Singapore hopes to leverage on ASEAN to build an external wing for its economy. Without any significant natural resources, hinterland, or a domestic market, Singapore’s ability to attract MNCs and build its own domestic industries depends to a large extent on its ability to capitalise on and synergise with the various comparative advantages that its neighbouring countries offer. In fact, one important component of Singapore’s economic strategy has been to serve as operation headquarters for MNCs
to maintain production operations in the region by offering tax incentives and other benefits to MNCs. In the past, Singapore served as an entrepôt in the region. This intermediary business service continues to be used by Singapore by offering its position as an efficient service provider in the region. Wider and deeper economic integration in ASEAN not only enhances market opportunities but also increases investment flows to the region.

Thirdly, Singapore’s need to leverage on ASEAN as an economic hinterland to attract foreign investment became more evident with the rapid emergence of major economic powers, like China and India, and the formation of regional free trade groupings in other parts of the world, such as the North American Free Trade Agreement. Individually, Singapore cannot offer a sufficiently attractive base for MNCs. However, as part of a larger ASEAN economy with a combined population of about 600 million, Singapore’s position as a base for MNCs is significantly strengthened. As a testament to Singapore’s strong commitment to the ASEAN integration process, Singapore was one of the first members to ratify the ASEAN Charter and the ASEAN Economic Community Blueprint.

As a small country whose only resource is its people, Singapore believes that human resource development is vital for economic and social progress. It has benefitted from the technical assistance extended by several developed countries and international organisations. This helped transform Singapore from a Third World country to a modern, developed city-state. Through the Singapore Cooperation Programme of the Ministry of Foreign Affairs, Singapore is committed to share its development experience and knowledge with others as a responsible global citizen to help other countries achieve their development goals. The Singapore Cooperation Program (SCP) was established in 1992 to serve as the primary platform through which Singapore offers technical assistance to other countries.

Although the SCP provides training to countries around the world, its primary focus is on the ASEAN region. Singapore offers training courses to ASEAN Member States in a diverse range of subjects, such as public governance and administration, trade and economic development, environment and urban planning, civil aviation, land transport, port management, education, healthcare, and information and communications technology. The courses are conducted both in-country and in Singapore, and the courses are reviewed regularly to ensure they are relevant to recipient countries’ development needs.

In addition, Singapore offers significant technical assistance to the newer members of ASEAN, CLMV, through the Initiative for ASEAN Integration. This initiative was launched at the Fourth ASEAN Informal Summit in November 2000 to strengthen
ASEAN and promote ASEAN integration. It has established in-country training centres in the CLMV countries. These in-country Initiative for ASEAN Integration centres allow more participants to benefit from the training courses. In this context, Singapore also collaborates with over 40 key countries and international organisations to pool expertise in providing technical assistance to other countries under the Third Country Training Programme framework.

The SCP has been successful, and Singapore’s experience is a powerful example of how a small country without natural resources can survive and thrive as long as it has good leadership, political stability, rule of law, and well-run and forward-looking institutions, as well as sustained investment in its people. The programme is a concrete and an excellent example of Singapore’s strong commitment to sharing its development experience with ASEAN, and particularly with the CLMV countries, to provide financial and technical assistance that aims to narrow the development gap in ASEAN.

Singapore’s active role in promoting closer cooperation and economic integration is part of its two-pronged approach in its external economic policy. While emphasising the importance of ASEAN integration, Singapore continues to maintain closer trade relations with other non-ASEAN countries. First, Singapore actively pursues bilateral FTAs with countries outside ASEAN, despite expanding integration within ASEAN. Compared to other ASEAN Member States, Singapore has been the most active in concluding FTAs. The obvious reason is that the total value of its trade is about three times its gross domestic product. To maintain its economic growth, the growth must come from expanding trade with all its major trading partners, particularly the United States, China, the European Union, and Japan. The share of intra-ASEAN trade has been growing but is not adequate to drive its ever-growing economic growth. In turn, expanding the country’s successful economic links with non-ASEAN economies demonstrates positive spill-over effects to spur other ASEAN economies to liberalise and deregulate their economies in the global marketplace. Singapore’s proven success in its bilateral and plurilateral FTAs with non-ASEAN economies has given a strong impetus for other ASEAN countries to emulate Singapore’s FTA policies. In turn, the more open and successful other ASEAN economies become, the more receptive and likely they are to accept Singapore’s initiative for wider and deeper ASEAN economic integration. For example, Singapore was the first to initiate bilateral FTAs with Australia, New Zealand, the United States, China, and Korea, as well as smaller economies such as Jordan, Panama, and the Gulf Cooperation Council. In addition, Singapore is also actively promoting the Asia-Pacific Economic Cooperation, World Trade Organization, Asia-Europe Meeting, Forum for East Asia-Latin America Cooperation, and Asia-Middle East Dialogue to establish dialogue and strengthen cooperation between Singapore, Asia, and the respective regions.
Singapore is deepening its bilateral relations with emerging economies, particularly with China and India. After Singapore established official diplomatic relations with China in 1990, Singapore’s trade volume with China increased significantly from US$2.9 billion in 1990 to US$7.8 billion by the end of 1996. From 1997 to the end of 2007, Singapore’s trade with China grew from US$9.8 billion to US$60.5 billion, and by the end of 2015, Singapore’s total merchandise with China reached US$91 billion. Singapore’s direct investment in China grew from US$5 billion in 2008 to US$14.4 billion in 2014.

Singapore’s trade and investment relationship with India has also strengthened in recent years. Bilateral trade and investment relations started when India started the liberalisation of its domestic policy, particularly when the two countries agreed to establish the India–Singapore Software Technology Park in Bangalore. This bilateral relation was accelerated further when the two countries agreed to establish a Comprehensive Economic Cooperation Agreement (Singapore–India bilateral FTA) in 2003. As a result, Singapore’s total trade volume with India registered significant growth of nearly 300%, from US$4.5 billion in 2003 to US$16.7 billion in 2007, and reached $17 billion by the end of 2015. At the same time, Singapore’s total direct investment in India increased from about US$600 million in 2003 to US$3 billion in 2007, and reached US$16.7 billion by the end of 2014.

Singapore’s rapid trade and investment expansion to China and India is an integral part of its fundamental policy to establish an ‘external wing’ policy to provide a sustainable economic booster and sources of economic growth. Nonetheless, during this period, ASEAN remains as Singapore’s political and economic anchor for regional economic integration and regional political stability. In this context, the Singapore government has actively encouraged local companies to invest overseas, especially in East Asia and ASEAN economies, with a view that these companies can leverage on their own comparative advantage with neighbouring ASEAN Member States. The charge was led by large government–linked companies, which started to invest actively in the ASEAN countries, China, and India. Large government–linked companies, such as Sembawang Corporation, Keppel Corporation, and Singapore Technology, have invested and built a number of industrial parks in Indonesia, Viet Nam, China, and India. Since the Asian financial crisis, Singapore’s external wing has still been largely confined to East Asia due to the region’s geographical proximity and Singapore’s overall development strategy to establish itself as a regional headquarters. An increasingly protectionist global economic environment, brought about by the formation of regional blocs in different parts of the world, has also made it more compelling and pragmatic for Singapore to focus on the region.
Opportunities and Constraints for ASEAN: Singapore’s Perspectives

Singapore’s geographical position at the heart of Southeast Asia provided unique opportunities and challenges when Singapore became a sovereign and independent nation on 8 August 1965. Its independence was not sought but was forced out of its status for 3 years as part of the Federation of Malaysia. As an independent nation without any natural resources and hinterland, Singapore had to chart its nation building and economic development based on very different policies and strategies from its Southeast Asian neighbours. Being a small city-state, the government right from the start had to be pragmatic and have a strategic vision for steering and managing its political and economic policies, particularly with its immediate neighbours. To survive and prosper politically and economically, Singapore must always be able to leverage external resources to its full benefit. Singapore’s noted success in transforming from a Third World to a First World country in 50 years is a clear testimony to its success in minimising the negative elements of its limited size and vulnerabilities through maximising external opportunities and resources. To successfully carry out such strategies and policies, Singapore has instituted strong, clean, visionary leaders and effective and efficient public administration to sustain rapid economic and social development. In this context, the establishment of ASEAN in 1967 played an important and strategic role in creating an external environment necessary for the success of Singapore in its national transformation.

In a region rich in natural resources, traditionally Singapore served as a vital entrepôt or transshipment centre for Southeast Asian economies. Following independence in 1965, this role gradually shifted from being mainly trade dependent to having a global focus on industrialisation and a wide trade and investment network through MNCs. Nonetheless, the role of its neighbouring countries, such as Malaysia and Indonesia, remained crucial throughout the period. The relative economic gravity may have changed, but in absolute numbers, Singapore’s neighbouring countries and ASEAN constitute the major political and economic pillars of Singapore’s political stability and economic prosperity.

Does ASEAN’s slow and gradual approach to regional integration hurt Singapore? Generally, many analysts argue that Singapore, being the most developed member, would prefer for the ASEAN integration process to be implemented faster so it can extract larger relative mutual benefits from other ASEAN Member States. ASEAN’s principles, or the ASEAN Way, based on consensus, may better serve Singapore and other members, at least in the initial phases of economic cooperation and integration. This is supported by the fact that the ASEAN Member States are at widely different
stages of economic and social development. If the process of integration is prematurely implemented and accelerated, there might be domestic backlash and strong opposition in many Member States. ASEAN’s gradual progress is calibrated based on the consensus that all have agreed to move forward to the next stage of cooperation and integration.

In summary, all AMSs view Singapore favourably. This can be argued from three perspectives. Firstly, Singapore’s success in transforming itself from a Third World to a First World nation has been inspiring, and the country has acted a role model for other ASEAN members. Secondly, Singapore can serve as an effective conduit to connect with major political and economic powers in the world as Singapore is highly respected internationally; despite its small size, Singapore is always invited to attend G–20 meetings as an observer. Thirdly, Singapore has demonstrated its strong commitment to extend technical and financial assistance to less developed ASEAN members to narrow the development gap in the region. Of course, there are bilateral disagreements and frictions between Singapore and other ASEAN Member States, particularly with its immediate neighbours, such as Malaysia and Indonesia, but they are under control. Progress in integration within the ASEAN framework would augur well and provide an enhanced important regional mechanism to ameliorate and minimise bilateral stress, frictions, and conflicts among AMSs.

**Summary and Conclusions**

As a small city-state, Singapore viewed the formation of ASEAN in 1967 with hope and anxiety. This view was seen in the context of turbulence in Southeast Asia amid the war in Viet Nam and a major deficit of trust and simmering conflict arising from Indonesia’s policy of confrontation against the formation of Malaysia in 1963. When a ‘New Order’ was installed by then President Suharto, Indonesia ceased confrontation with Malaysia and Singapore. However, bilateral relations among the three neighbouring countries remained fragile and unsettled. Therefore, when the five Southeast Asian countries of Indonesia, Malaysia, Thailand, and the Philippines agreed to form ASEAN in August 1967, it was seen from Singapore’s perspective as hope that this regional organisation would bring a semblance of peace and regional security. The ASEAN Declaration intended to promote economic, social, and cultural cooperation, as well as act as a mechanism for political and security dialogue and discussion.

As the Viet Nam War continued until 1975, there were few substantive intergovernmental meetings among the five ASEAN Member States, but regional stability among the Southeast Asian nations prevailed. During the period of transition, Singapore did not know what the next step forward for ASEAN would be. Would
ASEAN turn into a passing regional phenomenon or would it be a pretext for larger and more powerful ASEAN Member States to use it to achieve their national objectives? There was certainly a sense of anxiety on the part of Singapore on the possible role of ASEAN during that period. However, the establishment of ASEAN served as a clear and important message to Viet Nam of a regional-inspired grouping that was different from the United States–inspired Southeast Asia Treaty Organization, which had the membership of the Philippines, Thailand, and a group of Western powers. When Viet Nam was finally unified in 1975 and Indonesia has stabilised its domestic political changes, Indonesia initiated the first meeting of the ASEAN Heads of Government in Bali in 1975, which became known as the Bali Concord I.

As a small country in terms of population and territorial size, Singapore is keenly aware that to benefit more from the association, it must be a vibrant nation that is useful to ASEAN. Otherwise, Singapore will have a relatively insignificant voice and political leverage in major decisions taken by ASEAN. Therefore, the importance of ASEAN to Singapore has changed at different phases of ASEAN’s evolution and progress from the Bali Concord I. In political terms, ASEAN has been important to Singapore since the first phase of ASEAN’s establishment to the present. In economic terms, the absolute benefit to Singapore increased when its neighbouring economies opened up and increased economic cooperation through ASEAN. However, the relative benefit as measured in Singapore’s intra-industry trade with ASEAN has been fluctuating, dependent on the rate of growth of global trade as Singapore has become more connected economically with major global economic powers. Nonetheless, the importance and impact of ASEAN to Singapore’s foreign and economic policies are very important and visible. Singapore has proven that it has also contributed much to the development of ASEAN through its well-respected international prestige and leverage. This can be seen through Singapore’s wide network and strategic bilateral relations with the United States, China, Japan, India, and the European Union. Equally, Singapore’s exceptional economic achievement has created a seamless connectivity to all major markets in the world. Such political and economic assets to Singapore can be conveniently adapted and leveraged by other AMSs. The magnitude and extent of ASEAN’s importance and relevance to Singapore will increase as ASEAN becomes more integrated as a community in the future. A more integrated, prosperous, and inclusive ASEAN would enable Singapore individually and ASEAN collectively to project their political and economic power more effectively regionally and globally.

ASEAN’s process is a top-down approach by leaders, ministers, and public officials. As a result, there is not enough public awareness of the importance of ASEAN for average Singaporeans. There is media coverage and school textbooks to provide public understanding of ASEAN of its multifaceted activities. However, the effectiveness is
generally limited to the more educated audience, younger generation, and the public at large is unaware of the many important political, economic, and social implications of ASEAN for Singapore. In the next lap of ASEAN evolution, moving to the ASEAN Economic Community, ASEAN Political–Security Community, and ASEAN Socio–Cultural Community, Singapore and other AMSs must engage in wider and deeper outreach efforts not only from the top–down approach but equally importantly through engaging in bottom–up social dissemination of the meaning, importance, and implications of ASEAN to the common people in the region. Indeed, this is a long–haul process that will require consistent and persistent efforts by AMSs due to diversity in terms of ethnic, religious, and social backgrounds, as well as differences in legal and institutional heritage. As ASEAN becomes more integrated and complex as an organisation, there is a strong case for more resources and capabilities at the ASEAN Secretariat. More authority is needed for the secretariat to allow it to monitor the many ASEAN agreements with a view to implementing them more effectively. Equally important at this stage of its development, some decision–making processes should be made more flexible and innovative, rather than based solely on absolute consensus. In a fast–changing geopolitical landscape in East Asia, ASEAN must be relevant to major global and regional powers and leverage its strategic position as the default hub of East Asian economic integration to advance further its importance amidst a rising China and India. Throughout the ASEAN evolution, Singapore has been directly and indirectly encouraging ASEAN to be more competitive, open, and inclusive through widening and deepening ASEAN economic integration through deliberation and consensus decision–making processes. Specifically, through the Initiative for ASEAN Integration, Singapore’s effort to narrow the development gap among AMSs should not be considered as an act of charity but an act of self–interest. Singapore has long held the view that a prosperous, competitive, and stable ASEAN is to Singapore’s long–term national interest. With the ASEAN Economic Community that came into effect at the end of 2015, Singapore looks forward to a more integrated and competitive market in ASEAN through minimising non–tariff barriers, harmonising standards and procedures, facilitating cross–borders trade in goods and services, and investment and freer capital flows as agreed in the ASEAN Economic Community Blueprint.

With wider and deeper implementation of the ASEAN Economic Community Blueprint beyond 2015, Singapore looks forward to a more competitive, resilient, inclusive, and equitable ASEAN Community. Despite the lack of implementation of many of its agreements and slow progress at times, there has been a clear definitive policy statement in Singapore that the establishment of ASEAN in 1967 has been very positive and beneficial, not only to Singapore but to all AMSs. By 2030, three or four AMSs will likely be high–income countries; several Member States have upper middle–income status and are approaching the enviable high–income category. As ASEAN moves towards its
50th year of establishment in 2017, it is progressing slowly but surely towards the full potential of its political, security, economic, social, and cultural visions and objectives as intended by its founders in Bangkok in 1967.

In short, Singapore’s national interests have been facilitated by the evolving process of ASEAN integration. In the future, its long-term national interests are likely to coincide further with a dynamic and effective ASEAN. This will be especially so as the ASEAN Economic Community becomes a living reality to the 10 AMSs in the foreseeable future.

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Thailand

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Introduction

The Association of Southeast Asian Nations (ASEAN) was established in 1967, with the founding members consisting of Indonesia, Malaysia, the Philippines, Singapore, and Thailand. Later, ASEAN’s membership expanded to include Brunei Darussalam, Cambodia, the Lao PDR, Myanmar, and Viet Nam. The main objectives of ASEAN are to accelerate the economic growth of its Member States, promote social progress and cultural development in the region, and promote regional peace and stability (ASEAN, 2016).

One of ASEAN’s milestones has been the establishment of the ASEAN Economic Community (AEC), which was formally launched at the end of 2015. The four pillars of the AEC are a single market and production base, a competitive economic region, equitable economic development, and integration into the global economy. Since the first pillar has progressed much more than other pillars, this paper will focus on its role in promoting the free flow of goods, services, investment, and skilled labour from the perspective of Thailand.

This paper aims to assess the substance and significance of ASEAN economic integration for the Thai economy, examine the policies and strategies, identify the potential challenges for Thailand, and propose a way forward for further economic integration within ASEAN.

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ASEAN Economic Integration and Thailand’s Economy, Policies, and Strategies

Tariff reduction through ASEAN economic integration has made tangible progress; however, it is still very much a work in progress, especially the elimination of non-tariff barriers (NTBs) and the promotion of the free flow of cross-border services, investment, and skilled labour.

Regarding trade in goods, tariff reduction under ASEAN has brought about higher-value trade among ASEAN Member States, but the existence of NTBs is still a main issue that needs to be addressed. Through the ASEAN Free Trade Area, the Common Effective Preferential Tariff scheme requires ASEAN-6 countries (Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam) to reduce most of their tariff rates to 0% by 2010 and for Cambodia, the Lao PDR, Myanmar, and Viet Nam (CLMV) to do the same by 2015 with the flexibility to postpone the obligation to 2018.

Since 1993, ASEAN-6 have gradually reduced their intra-regional import tariff rates to zero for almost all items, except copra, coffee beans, fresh flowers, and potatoes, which have tariff rates of 5%. CLMV also have 0%–5% rates for over 98% of their tariff lines (ASEAN Secretariat, 2015). With the tariff cuts, intra-regional trade has significantly increased.

For example, the value of imports from ASEAN to Thailand increased from US$10.3 billion in 2000 to US$38.4 billion in 2015, while the country’s import share from ASEAN in total imports increased from 16.6% to 19% over the same period (see Figure 1). ASEAN is currently Thailand’s second-largest import market after China.

Similarly, the value of exports from Thailand to ASEAN increased from US$13.5 billion to US$55.2 billion during 2000–2015, and the export share of Thailand to ASEAN increased from 19.3% to 25.7% over the same period. ASEAN has replaced the United States as Thailand’s largest export market since 2003.
In addition to lower tariff rates, the relatively simple and transparent rules of origin under ASEAN, which require 40% regional value added or a change in the tariff heading, expedite the free flow of goods among ASEAN Member States.

The trade flows between Thailand and ASEAN, especially CLMV, are likely to increase in the future due to two factors. Firstly, during 2016–2020, the annual average gross domestic product growth rates in ASEAN and CLMV are projected to be around 5.2% and more than 6%, respectively (OECD, 2016). Secondly, the Common Effective Preferential Tariff rates for CLMV are scheduled to be reduced further by 2018.

Trade in intermediate goods, which has increased significantly (see Figure 2), dominates intra-regional trade between Thailand and ASEAN. This is because Thailand and ASEAN are increasingly becoming part of the regional and global value chains of many products. This trend is expected to continue given the fact that Thailand and ASEAN are undergoing deeper economic integration.

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1 Goods are classified into capital goods, intermediate goods, and consumption goods based on the Broad Economic Categories scheme.
However, the extensive use of NTBs, also known as core non-tariff measures (NTMs), still hinders the free flow of goods in ASEAN. According to the core NTM restrictiveness index in ASEAN, Indonesia has the greatest restrictions, followed by Malaysia and Viet Nam, while Thailand and the Philippines are less restrictive (ERIA, 2012). A study by the Thailand Development Research Institute (TDRI, 2013) shows that for Thailand, most NTBs are applied to protect consumers and the environment.

The ASEAN Comprehensive Investment Agreement was entered into force in 2012 to create a freer and more open investment regime. It covers five main sectors, namely manufacturing, agriculture, fishery, forestry, and mining and quarrying, as well as services related to these sectors. ASEAN Member States are expected to liberalise investment by phasing out their remaining restrictions by 2015.

Thailand has compiled a temporary investment exclusion lists in four sectors, consisting of (i) the production of flour from rice and field crops; (ii) fishery, especially aquaculture; (iii) plant cultivation, propagation, and breeding; and (iv) forestry from forest plantation. So far, Thailand has liberalised its market in a few subsectors of the first three sectors but has yet to do the same for the last sector, which is still under consideration by the Royal Forest Department (BOI, 2016). The sensitive list is based on Thailand’s Foreign Business Act (1999), which prohibits foreigners from becoming majority shareholders in many sectors, especially the agriculture and services sectors. It is noted that the list of the restricted sectors has not been revised for almost 20 years, reflecting the lack of dynamism in Thailand’s investment liberalisation policy.

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2 Core NTMs include non-automatic licensing; quantitative restrictions; prohibitions; enterprise-specific; single channel for imports; and foreign exchange market restrictions (ERIA, 2012).

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**Figure 2. Trade in Goods between Thailand and ASEAN**

Source: Author, data from the Ministry of Commerce of Thailand.
Despite slow progress in the implementation of the ASEAN Comprehensive Investment Agreement, cross-border investment between Thailand and ASEAN has organically increased. Outward direct investment (ODI) from Thailand to ASEAN Member States has significantly surpassed foreign direct investment (FDI) from these ASEAN Member States to Thailand since 2011 (see Figure 3). The notable surge in outward investment from Thailand in 2011 was mainly because the Bank of Thailand allowed Thai companies to invest abroad freely from October 2010.³

**Figure 3. Investment Flow between ASEAN and Thailand**

ASEAN, especially CLMV, has become Thailand’s main destination for ODI in the past decade. In particular, Thai investment to CLMV has greatly exceeded Thai investment to ASEAN-4 countries (Malaysia, Indonesia, the Philippines, and Brunei) since 2014. Among the ASEAN Member States, Singapore is the top destination for Thailand’s ODI, accounting for 17% of its total ODI.⁴ However, the majority of the investment in Singapore is used to set up holding companies to enjoy tax reliefs on dividends and capital gains. After Singapore, the CLMV countries are major investment destinations for Thailand, with an average share of 9% of Thailand’s total ODI.

Mainly to seek new markets and resources, Thai companies listed on the Stock Exchange of Thailand have rapidly expanded their business in ASEAN, especially CLMV (Rattanakhamfu and Tangkitvanich, 2017). In 2014, among 575 companies,

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³ The Bank of Thailand had continuously increased the limit of the amount of investment abroad for Thai companies. From October 2010, there is no limited amount of investment abroad for Thai companies anymore (Bank of Thailand, 2010).

⁴ The average share of Thailand’s ODI in ASEAN was 33% of its total ODI during 2005–2015.
at least 129 companies had already set up 591 subsidiaries or joint ventures in ASEAN countries. The top five business sectors of Thai firms investing in ASEAN were energy and public utilities (110 subsidiaries or joint ventures); food and beverage (58 subsidiaries or joint ventures); commerce (58 subsidiaries or joint ventures); construction (57 subsidiaries or joint ventures); and material, petrochemical, and chemical products (47 subsidiaries or joint ventures).

ASEAN has become a major source of FDI for Thailand, with an average share of 18% during 2005–2015, second only to Japan (23%). Among ASEAN Member States, Singapore accounted for 13% of Thailand’s FDI, followed by Malaysia (3%) over the same period.

Thailand has also made little progress in services liberalisation. Under the ASEAN Framework Agreement on Services, ASEAN Member States have committed to allowing at least 70% foreign equity participation in all services sectors by 2015. However, Thailand still lags far behind schedule (see Table 1). This is because Thailand’s Foreign Business Act restricts foreign equity participation to be no more than 49% of the registered capital for most major services sectors, such as mobile telephone services, healthcare services, education services, and maritime and road transport services. Unwilling to revise its law, Thailand has committed little to opening its services sectors to ASEAN investors. Some of its specific commitments under the ASEAN Framework Agreement on Services Ninth Package are not meaningful, such as its offers to open up bicycle courier services for food delivery, day-care services for children with disabilities, and space passenger transportation services (excluding the launching and placing of satellites in space).

Although the productivity of Thailand’s services sectors is relatively low, compared to the manufacturing sector (Lee and McKibbin, 2014), Thailand has not shown a strong will to liberalise its services sectors. Restrictions on foreign investment and behind-the-border barriers also prevent effective competition in services sectors. As competition can bring about higher productivity, Thailand should consider liberalising its services sectors by revising its Foreign Business Act.
Table 1. Foreign Equity Participation in Services Sectors

<table>
<thead>
<tr>
<th>Sector/Subsector</th>
<th>Target</th>
<th>E-ASEAN</th>
<th>Thailand</th>
<th>Malaysia</th>
<th>Singapore</th>
<th>Philippines</th>
<th>Indonesia</th>
<th>Brunei Darussalam</th>
<th>Cambodia</th>
<th>Lao DPR</th>
<th>Myanmar</th>
<th>Viet Nam</th>
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<tr>
<td></td>
<td>2015</td>
<td>Framework Agreement on Services Ninth Package (% of allowed foreign equity participation)</td>
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<tr>
<td>E-ASEAN</td>
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<tr>
<td>Mobile phone services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>75.99</td>
<td>40</td>
<td>49</td>
<td>100</td>
<td>100 (with facilities)</td>
<td>100</td>
<td>&lt;45 (non-facilities)</td>
<td>&lt;45 (facilities)</td>
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<tr>
<td>Online data and database services</td>
<td>≥70</td>
<td>49</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>51</td>
<td>100</td>
<td>100 (with facilities)</td>
<td>100</td>
<td>&lt;45 (non-facilities)</td>
<td>&lt;45 (facilities)</td>
<td></td>
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<tr>
<td>Consultancy services on hardware installation</td>
<td>≥70</td>
<td>49</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>49</td>
<td>100</td>
<td>100 (with facilities)</td>
<td>100</td>
<td>100</td>
<td></td>
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<tr>
<td>Healthcare</td>
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<tr>
<td>Hospital services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>100</td>
<td>100</td>
<td>50 (East)</td>
<td>51 (Blitar and Surabaya)</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>70</td>
<td>100</td>
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<td>Medical services</td>
<td>≥70</td>
<td>49</td>
<td>100</td>
<td>100</td>
<td>70 (East)</td>
<td>70 (Makassar and Makassar)</td>
<td>100</td>
<td>100 (except clinics)</td>
<td>70</td>
<td>100</td>
<td></td>
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<tr>
<td>Dental services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>100</td>
<td>70 (East)</td>
<td>70 (Makassar and Makassar)</td>
<td>100</td>
<td>100 (except clinics)</td>
<td>70</td>
<td>100</td>
<td></td>
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<tr>
<td>Tourism</td>
<td>≥70</td>
<td></td>
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<tr>
<td>Hotel lodging services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>100</td>
<td>100</td>
<td>70 (East)</td>
<td>70 (Others)</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td></td>
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<tr>
<td>Catering services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>100</td>
<td>100</td>
<td>70 (East)</td>
<td>70 (East)</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td>100</td>
<td></td>
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<tr>
<td>Tour agent services</td>
<td>≥70</td>
<td>49</td>
<td>70</td>
<td>100</td>
<td>70</td>
<td>&lt;49</td>
<td>70</td>
<td>51</td>
<td>70</td>
<td>100</td>
<td>&lt;100</td>
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<tr>
<td>Construction</td>
<td>≥70</td>
<td>49</td>
<td>51</td>
<td>100</td>
<td>40</td>
<td>&lt;55</td>
<td>55</td>
<td>100</td>
<td>100</td>
<td>100</td>
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</table>

Source: Author.

The ASEAN Mutual Recognition Arrangement (MRA) scheme is designed to promote the free flow of skilled labour by facilitating the cross-border movement of eight types of professionals, namely engineers, architects, medical practitioners, dental practitioners, nurses, accountants, surveyors, and professionals in tourism services. Despite the implementation of the scheme, the cross-border flow of such professionals in ASEAN is still limited. As of October 2016, the total number of ASEAN skilled and semi-skilled workers in Thailand was only 22,942, constituting only 1.7% of the total number of ASEAN workers in Thailand (Department of Employment, 2016).

In particular, only 813 ASEAN architects and engineers are currently permitted to work in Thailand, constituting 11.5% of total foreign architects and engineers in the country. Most of them are from the Philippines (37%), followed by Malaysia (21%) and Myanmar (16%) (Figure 4). It should be noted that these professionals are working in Thailand as skilled workers or experts under the existing frameworks, not as licensed...
professional architects and engineers under ASEAN’s MRA schemes. In fact, ASEAN MRAs for engineering and architect services do not provide significantly easier or simpler movement procedures. For example, meeting the qualifications specified in the MRA for engineering services does not result in automatic recognition to work in other Member States. To do so, ASEAN engineers are also required to meet domestic regulations, as previously required. In addition, the ASEAN MRA does not allow independent practices but requires joint work with local professional engineers in the host countries. For example, Thai law requires skilled foreign engineers to work alongside Thai counterparts. Those who aspire to work independently must pass the examination of the Council of Engineers (in Thai).

**Figure 4. ASEAN Architects and Engineers in Thailand**

![Diagram showing the distribution of ASEAN architects and engineers in Thailand](image)

Note: Data as of October 2016.
Source: Statistics on Foreign Workers Permitted to Work in Thailand, Department of Employment (2016).

For other types of professionals, the picture is even less heartening. Thus far, no foreign nurses have worked in Thailand. The total number of registered nurses in Thailand in 2014 was 187,030, and all were Thai (Thailand Nursing and Midwifery Council, 2016). The main obstacle for foreign nurses to practise in Thailand is the requirement to pass the national licensing examination, which is only available in Thai. As Thailand is facing a shortage of nurses while aspiring to be a major medical hub in Asia, the country should consider allowing foreign nurses to work in Thailand, at least to provide services to foreign patients in the country.

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5 Under the existing frameworks, foreign workers are not allowed to work in engineering and architectural work except for necessary and urgent work for a period not exceeding 15 days under the Law on Investment Promotion. (according to the Alien Working Act B.E. 2551, Occupations and Professions prohibited for foreign workers, the list appended to the Royal Decree B.E.2522, and Engineer Act B.E.2542).
Similarly, foreign medical professionals are required to pass the licensing examination in Thai to work in Thailand. During the past 70 years, there have only been 247 licensed medical doctors with non-Thai nationalities; 26 of them graduated from medical schools in Thailand, and 221 graduated from other countries (Medical Council of Thailand, 2016). These medical doctors with non-Thai nationality likely stayed in Thailand for a long time or had Thai parents, allowing them to have the required Thai language proficiency. Similar constraints exist for dentists. As there is a shortage of medical doctors and dentists in Thailand, allowing foreign professionals to work in Thailand, at least to treat foreign patients, would help support government policy to develop Thailand as a medical hub in the region.

Although no agreement on unskilled workers exists in ASEAN, the number of unskilled workers from ASEAN Member States in Thailand has reached more than 1.33 million workers compared to only 22,942 skilled workers (see Figure 5). The top three nationalities of ASEAN workers in Thailand are those from Myanmar (72%), followed by Cambodia (19%), and the Lao PDR (8%). Due to Thailand’s labour shortages, the flow of ASEAN workers, especially from Cambodia, the Lao PDR, and Myanmar, into Thailand is expected to increase in the future.

**Figure 5. ASEAN Workers in Thailand**

(‘000 workers)
Challenges for Thailand

Thailand’s economy has benefited from ASEAN economic integration. In particular, Thailand has benefited greatly from the increasing cross-border flows of goods, investment, and labour with ASEAN. In the future, ASEAN economic integration will be one of Thailand’s few growth engines as the country faces the challenges of sluggish economic growth and an ageing population.

Due to the global economic slowdown, Thailand’s export growth has declined since 2010 and has had negative growth rates since 2013 with a historically high negative growth rate of −5.8% in 2015. Looking for growth, Thai firms are increasingly investing in ASEAN, especially CLMV. This trend is likely to continue as the economic growth rates of CLMV are projected to be relatively higher at around 6% per year during 2016–2020, whereas that of Thailand is expected to grow only 3.6% per year (OECD, 2016).

On the supply side, Thailand is facing the problem of an ageing population. In 2015, 15.8% of the Thai population were 60 years or older. This share is projected to reach 26.9% (18.4 million people) by 2030 (United Nations, 2015). This demographic factor will be a strong headwind for Thailand to grow in the future.

The Thai government is aware of the opportunities of ASEAN economic integration, as reflected in its national plan (The 12th National Economic and Social Development Plan, 2017–2021) and the new draft constitution. However, its ASEAN economic
agenda is limited to only trade and investment promotion and facilitation, without a focus on liberalisation.

The Government of Thailand must overcome its challenges to reap the full benefits from ASEAN economic integration. Most importantly, it should focus on building the competitiveness of the country by upgrading the skills of Thai labourers to compensate for rising labour costs and solve the problem of skilled labour shortages. In addition, Thai companies should be supported and promoted to upgrade their capabilities to higher value-added activities, such as research and development, design, and marketing, while shifting low value-added activities, such as assembling, to neighbouring countries. It should also improve competitiveness by promoting competition in the services sector. However, it is still questionable how these ambitious policies can be formulated and implemented amidst Thailand’s political instability. In particular, the instability leads to the lack of long-term strategies on trade and investment in the country. In addition, with short-lived governments, Thai government officials tend to maintain the status quo on sensitive issues, such as service liberalisation and the movement of skilled labour. Under this situation, it is crucial for the private sector to take the leading role and provide a united voice on these issues.

Conclusion and the Way Forward

ASEAN economic integration has made tangible progress on tariff reduction; however, it is still very much a work in progress, especially the elimination of NTBs and the promotion of the free flow of cross-border services, investment, and skilled labour.

Thailand’s economy has benefited from ASEAN economic integration despite its limited progress. In particular, Thailand has greatly benefited from the increasing cross-border flow of goods, investment, and labour between itself and ASEAN. In the future, ASEAN economic integration will be one of Thailand’s few growth engines as the country is facing the problems of a sluggish economic growth rate and an ageing population.

Thailand should utilise ASEAN economic integration as a stepping stone to escape from the ‘middle-income trap’ before it becomes a completely aged society by 2025. To reap the full benefits of ASEAN economic integration, Thailand should do the following.

Firstly, ASEAN economic integration should be used as a catalyst for Thailand’s domestic institutional and regulatory reforms to improve its productivity and competitiveness, particularly by lifting restrictions on foreign skilled workers and service operators. It is crucial for Thailand’s trade policy to focus not only on gaining market
access but also on reducing domestic restrictions. Thailand should align its domestic regulatory reforms with regional integration strategies to reap the full benefits from integration. For example, the Foreign Business Act should be revised to be less restrictive and promote more competition and better resource allocation in major services sectors, such as telecommunications, public utilities, and energy.

Secondly, the Thai government should inform the public of the benefits of ASEAN economic integration to gain public support. Moreover, it needs to pay attention to measures to compensate those who receive adverse effects from economic integration as well as improve the competitiveness of small and medium-sized enterprises by enhancing their capacities.

Thirdly, Thailand should improve its physical infrastructure to enhance connectivity with its neighbouring countries, namely Cambodia, the Lao PDR, and Myanmar, in order to utilise its strategic locational advantages. It should also provide financial and technical assistance to improve the hard and soft infrastructure with its neighbours to promote mutually beneficial integration.

Finally, Thai people should be encouraged to have a more international mindset through understanding and respecting the cultural differences among ASEAN Member States. Some Thai people have little interest in learning about and understanding their neighbouring countries even though Thailand is becoming increasingly dependent on them. Recent initiatives by the Ministry of Education to allow schools in the border areas to teach classes to Thai students in the languages of the neighbouring countries is a welcome starting point. However, further efforts in this area are required.

References


Viet Nam

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Introduction

In December 1997, the Association of South East Asian Nations (ASEAN) adopted the ASEAN Vision 2020, aimed at ‘transforming ASEAN into a stable, prosperous, and highly competitive region with equitable economic development and reduced poverty and socio-economic disparities’ (ASEAN, 2007: 1). In October 2003, ASEAN Member States agreed on the establishment of the ASEAN Community by 2020, resting on three pillars as a political-security community, economic community, and socio-cultural community. In August 2006, the ASEAN Economic Ministers agreed in principle to accelerate the establishment of the ASEAN Economic Community (AEC) by 2015 as an intermediate goal towards its vision by 2020. ASEAN declared the establishment of the AEC in December 2015 together with a follow-up blueprint towards 2025.

Even with the AEC already in place, ASEAN Member States still have a sizeable workload. The Member States and the region as a whole face remaining challenges and impediments, the most pressing of which rely on whether the less-developed Member States can catch up with the more advanced ones. Yet ASEAN’s progress so far, particularly in amalgamating itself into a single bloc for negotiating and implementing free trade agreements (FTAs) with other major trading partners, has brought about major hopes for a more meaningful realisation of the AEC’s goal by 2025.

From Viet Nam’s perspective, ASEAN integration has marked an essential first step towards international economic integration. Nevertheless, the country has emphasised the need for broader integration with all partners, not just ASEAN. International economic integration in Viet Nam was initiated in as early as 1986 when the country started to transform itself into a socialist-oriented market economy. By the end of 2000, the country had already signed bilateral trade agreements with all its major partners.
Viet Nam even went on to join the World Trade Organization (WTO) in 2007, after which it further deepened integration attempts by negotiating various new and ambitious agreements, such as an FTA with the European Union, the Trans-Pacific Partnership agreement, and the Regional Comprehensive Economic Partnership.

As part of the dynamic ASEAN region, Viet Nam finds itself attached to regional integration and development. This attachment has been even more meaningful as ASEAN has assumed greater centrality in the East Asian economic integration process while various non-traditional security issues have emerged with commonality to the regional economies. Contributing to deepening the AEC and addressing the non-traditional security issues will require Viet Nam to significantly enhance its institutional capacity, trade facilitation, and connectivity, which will ultimately benefit the country’s own development in all socio-economic aspects. The challenge lies in whether Viet Nam can harmonise ASEAN integration with the other integration tracks it has been pursuing. Active AEC membership should by no means lead to the divergence of economic relations away from other major and traditional partners. In addition, Viet Nam needs to overcome the weaknesses inherent in its socio-economic structure. Otherwise, with the sizeable economic disparity between itself and its more advanced partners, Viet Nam may not fully benefit from the AEC. Overcoming these weaknesses will require a proper and gradual shift in economic structure to accommodate evolution under the regional economic community.

This paper discusses the impacts of ASEAN integration on Viet Nam. It briefly reviews Viet Nam’s economic integration process, in which ASEAN integration plays a pivotal role, and discusses the impacts of ASEAN on Viet Nam’s economy and reforms. The paper then identifies some major issues and challenges facing ASEAN integration until 2025, and finally concludes with how the country can participate more effectively in ASEAN integration by 2025.

**ASEAN in Viet Nam’s Economic Integration Process**

Since the start of Doi Moi (renovation) in 1986, Viet Nam has embarked on gradually opening its economy to foreign trade and investment. The country’s process of economic integration became more rapid from 1995 with four significant milestones. First, Viet Nam joined ASEAN in 1995 and participated in the ASEAN Free Trade Area from 1996. Over the 2 decades until 2016, Viet Nam was also a signatory to an array of FTAs under the ASEAN-plus framework. By the end of 2015, Viet Nam had become a member of the ASEAN Community as well as ASEAN’s Economic Community and Socio-Cultural Community. As of 2016, Viet Nam was active in the negotiation of the
Regional Comprehensive Economic Partnership between ASEAN, China, the Republic of Korea (henceforth, Korea), Japan, Australia, New Zealand, and India; and an FTA between ASEAN and Hong Kong.

Second, Viet Nam negotiated and signed the Viet Nam–United States bilateral trade agreement in 2000. This agreement laid an important foundation that induced preparations for Viet Nam for participating more deeply in regional (FTA-based) integration and WTO processes. Under the agreement, Viet Nam was for the first time exposed to a range of new liberalisation issues, such as intellectual property rights, which later helped shape the new generation of FTAs. The agreement also enhanced Viet Nam’s access to the largest export market, with less discrimination compared with other major exporters.

Third, Viet Nam made huge negotiation attempts to join the WTO and became an official member in January 2007. The largest sources of pressure under the WTO were related to institutional reforms and the services sector (Central Institute for Economic Management, 2013). To fulfil its WTO commitments, Viet Nam had to amend and promulgate many laws, ordinances, and decrees related to domestic regulations (institutions).

Fourth, from 2008, Viet Nam began to focus more on bilateral and plurilateral FTAs. The first among them was the economic partnership agreement with Japan, which was effectively a bilateral FTA. By 2016, Viet Nam had signed various FTAs, including the Trans-Pacific Partnership and others with the European Union, Chile, Korea, and the Eurasian Economic Union (Figure 1).

Figure 1. Viet Nam’s Free Trade Agreements

Source: Authors’ compilation.
Among the discussed milestones, ASEAN integration still remains highly important to Viet Nam for several reasons (Vo, 2012). First, ASEAN was the first playing field for trade and investment liberalisation, which matches the relatively low development level of Viet Nam. The gradual nature of ASEAN integration also permits less costly adjustment in terms of the regulatory and economic aspects. Second, ASEAN integration has become more comprehensive, covering not only trade and investment but also socio-economic issues, foreign affairs, security cooperation aspects, and even non-traditional security issues. Third, ASEAN Member States have been working together to reduce the intra-regional development gap, particularly between Cambodia, the Lao PDR, Myanmar, Viet Nam, and the rest of the Member States. Finally, ASEAN, as a single body, has been emerging in popularity in international and regional initiatives, such as the East Asia Summit and the Asia–Europe Meeting. Thus, being a member of ASEAN has allowed Viet Nam to contribute to the various regional activities and dialogues that have helped promote further economic integration and sustainable development in Southeast Asia.

Acknowledging this importance, Viet Nam actively contributes to the community-building process in ASEAN. Viet Nam has joined and promoted the work of ASEAN for regional integration, including in the aspects of economy, trade, socio-culture, and tourism. In the pioneering Hanoi Plan of Action of 1997, Viet Nam and other ASEAN Member States recognised the need to facilitate regional economic recovery and regional economic integration after the Asian financial crisis. Viet Nam, as Chair of ASEAN in 2010, conducted various initiatives to strengthen relations with ASEAN’s dialogue partners, the most noticeable of which was the engagement of the United States and the Russian Federation in the East Asia Summit.

At the same time, Viet Nam is also keen on respecting ASEAN centrality in regional issues, even those related to non-traditional security. While engaging in strategic partnerships with other ASEAN Member and other sub-ASEAN processes (such as the Cambodia–Lao PDR–Viet Nam Development Triangle), Viet Nam duly supports the role of ASEAN in dialogues and in the identification of measures to address common regional issues. Such support has been reflected in the country’s contribution to ASEAN’s collective efforts for harmonising the agenda for ASEAN-centred East Asian economic integration. In particular, Viet Nam joined other ASEAN Member States to coordinate with dialogue partners the implementation of the Master Plan for ASEAN Connectivity (MPAC), which explicitly acknowledged ownership of ASEAN in regional connectivity initiatives.1

1 Noticeable examples are the public–private partnership-financed infrastructure projects in selected ASEAN countries, including Viet Nam.
Impacts of ASEAN Integration on Viet Nam’s Economy and Reforms

Impacts on Viet Nam’s economy

In terms of economic performance, ASEAN integration has been markedly beneficial for Viet Nam. Its trade with ASEAN has increased drastically, with average growth of 16.8% per annum for exports and 13.0% per annum for imports (Figure 2). The declining share of ASEAN in Viet Nam’s trade simply reflects Viet Nam’s more rapid expansion of trade with its non-ASEAN partners, such as the United States, the European Union, China, and Japan.

Figure 2. Viet Nam’s Trade with ASEAN, 1995–2014
(a) Exports to ASEAN
(b) Imports from ASEAN

As trade expanded, Vietnamese enterprises have become more deeply engaged in the regional supply chain. ASEAN’s share in Viet Nam’s value added from exports has been rather stable (Figure 3). East Asia’s share has tended to increase, reflecting the outcome of integration efforts with East Asian countries, which have induced more imports of intermediate products from those countries. Among the East Asian countries, China stands out as the main source of imports of intermediate goods into Viet Nam. The share of value added from China in Viet Nam’s exports is estimated to have increased from 1.5% in 2000 to 6.1% in 2008. It then fell to 5.8% in 2009 before recovering to 6.3% in 2011. The expanded share of East Asia in Viet Nam’s exports has also been induced by integration efforts under ASEAN framework with these partners, namely through FTAs with China, Korea, and Japan.

In addition, foreign direct investment (FDI) has increased remarkably and has made important contributions to gross domestic product, exports, and job and income creation, etc. Total registered capital decreased significantly during 1997–2000 due to the Asian financial crisis but gradually recovered during 2001–2006. The main reason for the recovery was the adjustment of Viet Nam’s economic policy in preparation for its WTO accession as well as ASEAN’s deepened economic integration. The pace of FDI expansion was, however, uneven throughout the period 2007–2015.

Still, by partner, ASEAN as a whole attained even greater importance than Korea and Japan in terms of registered capital (Table 1). Like other foreign investors, those from ASEAN were driven by the incentives and preferences offered by Viet Nam. FDI flows from ASEAN experienced significant changes. The highest level of FDI from ASEAN was witnessed in 2008 at US$27.9 billion, 42.9 times higher than in 2005 (US$651.9 million), and the highest historical growth rate of 250% per annum was recorded during the period 2005–2008. FDI flows from ASEAN to Viet Nam, nevertheless, dropped sharply in 2009 to only US$1.3 billion, a decrease of 95.3% compared to the previous year. This was the largest drop among major foreign investors in Viet Nam. In 2010, while overall FDI to Viet Nam followed a declining trend until 2011, FDI from ASEAN went the opposite direction, increasing by 3.1 times compared to 2009 to reach US$5.3 billion. During 2011 and 2012, FDI from ASEAN continued to decline by 42.6% and 19.7%, respectively, equalling only US$2.5 billion in 2012, the lowest value since 2007. The situation only improved in 2013 as FDI capital flows from ASEAN to Viet Nam expanded by 110.2% (to US$5.2 billion) before deteriorating again in 2014 (decreasing by 31.4% to US$3.5 billion).

Figure 3. Share of Value Added in Viet Nam’s Gross Exports by Country, 1995–2011 (%)
Table 1. Inward Foreign Direct Investment by Country/Territory
Cumulative 1988-2015

<table>
<thead>
<tr>
<th>Country/Territory</th>
<th>Number of Projects</th>
<th>Registered Capital (US$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASEAN</td>
<td>2,813</td>
<td>59,050</td>
</tr>
<tr>
<td>Korea</td>
<td>4,970</td>
<td>45,191</td>
</tr>
<tr>
<td>Japan</td>
<td>2,914</td>
<td>38,974</td>
</tr>
<tr>
<td>Taiwan</td>
<td>2,478</td>
<td>30,997</td>
</tr>
<tr>
<td>British Virgin Islands</td>
<td>623</td>
<td>19,275</td>
</tr>
<tr>
<td>Others</td>
<td>6,271</td>
<td>88,395</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>20,069</strong></td>
<td><strong>281,882</strong></td>
</tr>
</tbody>
</table>

Source: Ministry of Planning and Investment, Viet Nam.

Table 2 suggests that in the pre- and post-ASEAN Comprehensive Investment Agreement implementation periods, FDI had a weak influence on domestic investment. Realised FDI fell in 2012, the first year of implementation of the ASEAN Comprehensive Investment Agreement. In contrast, state and non-state domestic investment still increased, particularly state investment. In 2013, FDI resumed its growth, while the growth of state investment decelerated and non-state investment growth was moderate. In 2014, non-state investment performed better but FDI growth was slower.

Table 2. Annual Growth Rate of Realised Investment by Ownership (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>Non-state</th>
<th>Foreign Direct Investment</th>
<th>State</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>15.4</td>
<td>21.4</td>
<td>9.4</td>
</tr>
<tr>
<td>2007</td>
<td>27.7</td>
<td>94.5</td>
<td>4.8</td>
</tr>
<tr>
<td>2008</td>
<td>-4.0</td>
<td>35.3</td>
<td>-3.1</td>
</tr>
<tr>
<td>2009</td>
<td>28.2</td>
<td>-19.3</td>
<td>22.6</td>
</tr>
<tr>
<td>2010</td>
<td>20.1</td>
<td>10.0</td>
<td>-0.7</td>
</tr>
<tr>
<td>2011</td>
<td>-0.5</td>
<td>-13.9</td>
<td>-9.2</td>
</tr>
<tr>
<td>2012</td>
<td>3.8</td>
<td>-3.9</td>
<td>13.5</td>
</tr>
<tr>
<td>2013</td>
<td>5.6</td>
<td>8.8</td>
<td>7.3</td>
</tr>
<tr>
<td>2014</td>
<td>9.5</td>
<td>6.4</td>
<td>6.0</td>
</tr>
</tbody>
</table>

Finally, one can also anticipate the positive impacts of connectivity enhancement under the ASEAN framework. This is because better and more comprehensive connectivity under MPAC, if realised, can help facilitate the flow of goods, services, and persons across ASEAN subregions and states. This postulation is supported by some recent empirical attempts to quantify the net impacts on subregions and states in ASEAN. Based on findings from ERIA’s Geographical Simulation Model, MPAC seems to promote ASEAN economic growth and narrow the development gap (Table 3). While the findings are restricted to economic impacts, they still have important implications for enhancing the confidence of Member States and stakeholders in MPAC implementation. By country, Viet Nam ranks second, with a simulated increase in economic benefits of 115%.

Table 3. Geographical Simulation Model: An Illustration

<table>
<thead>
<tr>
<th>Region</th>
<th>Country</th>
<th>Economic Effect</th>
<th>Country</th>
<th>Economic Effect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kota Lhokseumawe</td>
<td>Indonesia</td>
<td>533.7%</td>
<td>Myanmar</td>
<td>145.8</td>
</tr>
<tr>
<td>Asahan</td>
<td>Indonesia</td>
<td>485.8%</td>
<td>Viet Nam</td>
<td>114.6</td>
</tr>
<tr>
<td>Mamuju Utara</td>
<td>Indonesia</td>
<td>480.8%</td>
<td>Lao PDR</td>
<td>99.3</td>
</tr>
<tr>
<td>Kota Pematang Siantar</td>
<td>Indonesia</td>
<td>463.4%</td>
<td>Thailand</td>
<td>98.6</td>
</tr>
<tr>
<td>Rokanhilir</td>
<td>Indonesia</td>
<td>432.8%</td>
<td>Cambodia</td>
<td>97.9</td>
</tr>
<tr>
<td>Indragiri Hilir</td>
<td>Indonesia</td>
<td>419.2%</td>
<td>Indonesia</td>
<td>85.0</td>
</tr>
<tr>
<td>Kota Binjai</td>
<td>Indonesia</td>
<td>411.4%</td>
<td>Philippines</td>
<td>73.4</td>
</tr>
<tr>
<td>Kota Kediri</td>
<td>Indonesia</td>
<td>410.3%</td>
<td>Malaysia</td>
<td>64.4</td>
</tr>
<tr>
<td>Kota Tanjungbalai</td>
<td>Indonesia</td>
<td>408.1%</td>
<td>India</td>
<td>45.6</td>
</tr>
<tr>
<td>Soc Trang</td>
<td>Viet Nam</td>
<td>404.4%</td>
<td>Singapore</td>
<td>29.2</td>
</tr>
<tr>
<td>Number of regions with</td>
<td>100% or more</td>
<td>254</td>
<td>China</td>
<td>25.4</td>
</tr>
<tr>
<td>50% to 100%</td>
<td>239</td>
<td>Bangladesh</td>
<td>23.0</td>
<td></td>
</tr>
<tr>
<td>0% to 50%</td>
<td>446</td>
<td>Hong Kong</td>
<td>8.2</td>
<td></td>
</tr>
</tbody>
</table>

Impacts on Viet Nam’s institutional reforms

ASEAN integration has also helped induce institutional reforms in Viet Nam, particularly in areas directly related to trade and investment (Vo et al., 2015). For instance, trade facilitation received significant attention under the ASEAN integration framework and has been implemented relatively rapidly in the country. The Viet Nam National Single Window (NSW) was developed in 2005 and widely implemented in 2013–2016. An initial achievement of the NSW’s first pilot period was the technical connection between three core governmental agencies, namely the Ministry of Finance (General Department of Customs), the Ministry of Transport, and the Ministry of Industry and Trade, on 26 February 2014. Three other core governmental agencies – the Ministry of Agriculture and Rural Development, the Ministry of Health, and the Ministry of Natural Resources and Environment – were also connected to the NSW in late 2015. In September 2015, Viet Nam was the fifth country to connect to the ASEAN Single Window after Singapore, Indonesia, Malaysia, and Thailand.

The technical infrastructure of the NSW is being implemented, comprising the main functions, such as front-end systems for traders; manifest submissions; goods declarations; and the payment of duties, taxes, and fees. Providing functionality for integrated risk management, electronic connectivity, and international data exchange is currently underway. More investment to expand the NSW Customs Portal has been made to unify administrative procedures, technical plans, and working schedules with various stakeholders (Hai and Bao, 2016).

Customs modernisation has become an essential activity of the General Department of Customs in recent years. The government issued the first initiative on piloting e-customs at Hai Phong Customs Office under Decision 149/2005 on 20 June 2005. After gaining considerable experience, the piloting of e-customs was expanded to 19 other provinces in 2009. In the years until 2017, there have been rapid and significant reforms in customs modernisation. This shows a stronger political willingness to foster economic integration and implement regional and international commitments. It also reaffirms the support from international donors, such as the Government of Japan and the World Bank.

Finally, Viet Nam also aims to catch up with ASEAN (especially ASEAN-6, namely Singapore, Malaysia, Thailand, Indonesia, Brunei Darussalam, and the Philippines) in terms of its business environment. In particular, the various iterations of Resolution 19 (first issued in 2014 then renewed in 2015 and 2016) aim to strengthen national competitiveness and make the domestic business environment more enabling. A new feature in Resolution 19 is that it sets out specific tasks related to improving the business
environment, including (i) simplifying the procedures and reducing the time required to start a business to 6 days or less to shorten the time from business registration to actual business activity; (ii) improving the routines, documents, and procedures related to paying taxes so that the time needed for enterprises to pay taxes is equivalent to or below the average level of ASEAN-6, i.e. 171 hours per annum; (iii) reducing the time for enterprises and investment projects to get electricity to 70 days or less (the average figure for ASEAN-6 is 50.3 days); and (iv) simplifying the routines, documents, and procedures for import and export activities and customs clearance and reducing the time for customs clearance to the average level of ASEAN-6 (i.e. 14 days for exports and 13 days for imports). Along with these tasks are an array of measures identified for each ministry, together with a quarterly reporting mechanism specifically led by the Ministry of Planning and Investment. As these resolutions set out various reference targets in line with the average level of advanced ASEAN Member States, they may signify bolder and more serious attempts by Viet Nam to bring itself closer to the standards of ASEAN.

Key Issues and Challenges

Looking forward, Viet Nam must still address several key issues and challenges for furthering ASEAN integration. First, the country still needs to actively develop itself and contribute to narrowing the development gap between ASEAN-6 and Cambodia, the Lao PDR, Myanmar, and Viet Nam. Despite the attempts to facilitate trade and investment liberalisation and the pledged commitments towards the AEC during 2000–2009, the development gap in ASEAN is still huge (especially between Cambodia, the Lao PDR, Myanmar, Viet Nam, the Philippines, and Indonesia and the rest of ASEAN in terms of purchasing power parity income). Table 4 depicts the purchasing power parity income gap between several ASEAN Member States. With Viet Nam serving as a base, the purchasing power parity income gap in 2000–2008 is evident. Even so, the change in income gap that occurred during 2008–2015 is hardly unambiguous. The Lao PDR and Cambodia still had the lowest income levels, while Singapore remained the richest. In the absence of more meaningful measures for addressing the regional development gap, ASEAN may find the momentum for furthering regional integration has weakened. From Viet Nam’s perspective, similarly, failure to promptly foster sustainable, innovative, and inclusive growth and catch up with ASEAN-6 will undermine the country’s contribution to the ASEAN integration process.
Second, while the need for further ASEAN integration has prevailed, Viet Nam has encountered challenges in building awareness and consensus for domestic reforms (Vo, 2015). Despite having taken a top-down approach towards formulating reforms in past decades, Viet Nam has more recently endeavoured to consult stakeholders as part of the process of implementing its regional economic integration commitments and domestic reforms. The scope of these consultations has gradually been expanding. Various workshops and dialogues have been organised to consult with the business community on integration roadmaps and other related issues. Regarding ASEAN integration, the views of stakeholders have been collected on major issues, such as tariff reductions for sensitive and highly sensitive products, sanitary and phytosanitary measures, and trade facilitation. However, the effectiveness of such consultations has been somewhat limited. As regards international economic integration in general and ASEAN integration in particular, consultation efforts have often been confined to traditional stakeholders, such as government agencies, researchers, and the business community. Non-governmental organisations have thus far raised concerns on behalf of various social groups only with respect to the AEC and other important FTAs, such as the European Union–Viet Nam FTA and the Trans-Pacific Partnership. Even in the case of domestic reforms induced by other international FTAs, the consultation processes have not been effective. Consultations have only been undertaken with respect to major laws, such as the Constitution, Enterprise Law, and Investment Law, not only because of their importance to the public but because significant resources (time and money) were dedicated to

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**Table 4. Purchasing Power Parity Income Gaps between ASEAN Member States**

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cambodia</td>
<td>0.6</td>
<td>0.7</td>
<td>0.7</td>
<td>0.6</td>
</tr>
<tr>
<td>Indonesia</td>
<td>1.6</td>
<td>1.4</td>
<td>1.4</td>
<td>1.8</td>
</tr>
<tr>
<td>Lao PDR</td>
<td>0.8</td>
<td>0.8</td>
<td>0.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Malaysia</td>
<td>6.0</td>
<td>5.3</td>
<td>5.1</td>
<td>4.5</td>
</tr>
<tr>
<td>Philippines</td>
<td>1.7</td>
<td>1.5</td>
<td>1.4</td>
<td>1.2</td>
</tr>
<tr>
<td>Singapore</td>
<td>23.7</td>
<td>19.9</td>
<td>17.8</td>
<td>14.1</td>
</tr>
<tr>
<td>Thailand</td>
<td>3.3</td>
<td>3.1</td>
<td>2.2</td>
<td>2.7</td>
</tr>
<tr>
<td>Viet Nam</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Note: Viet Nam’s purchasing power parity income is set at unity.
Sources: Ministry of Planning and Investment, Viet Nam. The figures for 2015 are the authors’ calculations based on the World Bank’s World Development Indicators statistics.
their drafting processes. Inadequate attention has been paid to various measures of ASEAN integration, such as mutual recognition and services liberalisation. Possible reasons include the lack of a regulatory framework for sharing confidential information and technical details during negotiation processes. Accordingly, various Vietnamese stakeholders did not have the opportunity to make comments during the negotiation and inception of the AEC-related measures and were also not given sufficient information to plan for the implementation of the measures. In addition, stakeholders were hardly consulted formally on the reduction of the policy space for supporting domestic economic activities (due to a phasing out of barriers to trade and investment).

Third, Viet Nam must strive to harmonise its integration tracks and routes. Its WTO commitments have, so far, been the most comprehensive. Trade agreements with other key partners, such as China, India, Japan, and the United States, have been signed either under the umbrella of ASEAN or on a bilateral basis and have already been implemented. More comprehensive and in-depth FTAs are to be signed and/or implemented. However, risks may arise from the discrepancy in commitments that Viet Nam has made under the different agreements. As such, harmonising its integration tracks is important to prevent any unwanted distortions to resource allocation. Furthermore, Viet Nam must align its efforts for liberalisation with development cooperation under ASEAN’s FTAs. With its intermediate level of development, Viet Nam could bridge or contribute to the technical assistance from more advanced ASEAN Member States to Cambodia, the Lao PDR, and Myanmar. In this regard, Viet Nam could promote not only domestic economic reforms but also deeper economic relations with other ASEAN members.

**Conclusion**

In summary, ASEAN has achieved a range of regional integration commitments. The most progress, however, has been made mainly in the liberalisation of merchandise trade. Ample room remains for promoting further liberalisation in other areas, such as investment and services trade. Past experiences in ASEAN have shown that higher economic growth and an advanced economy are by no means automatically attained by having a more liberalised business environment. Future attempts towards ASEAN integration, therefore, might be challenged by institutional inadequacies, the considerable differences among ASEAN Member States, or the emergence of new issues, including non-traditional security issues.

ASEAN integration has played a key role in Viet Nam’s international economic integration process. Since its accession to ASEAN in 1995, the country has worked
to implement its Common Effective Preferential Tariff and ASEAN Free Trade Area commitments while being a signatory to and implementing various trade and investment agreements. Bilateral trade and investment ties between Viet Nam and ASEAN have grown stronger over time. Thus, ASEAN has proved to be vitally important to Viet Nam, and the country has made progressive moves in the integration process to accelerate its transition to market-oriented reforms. However, as Viet Nam becomes more deeply integrated into the regional economy, it must confront the common regional issues facing further ASEAN economic integration while addressing the problems it faces as a lower middle-income economy. These problems have persisted for quite some time and are not new. Yet, in this regard, Viet Nam’s successful integration experience over the past years has marked a profound start. Like other ASEAN Member States, Viet Nam still has room for more meaningful integration into the regional economy.

Experiences of attempts towards an ASEAN community also have significant implications. While a ‘true’ single market remains to be realised, it is crucial that a breakthrough is made for ASEAN economic integration by 2025 and beyond. More importantly, ASEAN as a whole should extend further efforts to consolidate the sense of an economic community. More specifically, ASEAN integration should at least be accompanied by the effective enforcement of commitments, reflected by a shift ‘from action to decisive actions’ rather than just ‘from vision to action’. ASEAN cooperation should be further enhanced in ways that facilitate and strengthen connectivity through regional infrastructure development and service-link cost reduction. For the ASEAN Community to function by the people and for the people, it should also allow for active participation by the public and social and business communities.

From Viet Nam’s perspective, again, effective and deeper integration within the ASEAN framework has proved, and will continue to be, beneficial. Therefore, the country is committed to the process. It should be proactive in undertaking measures to ensure that further ASEAN integration is smooth, not only for itself but also for other ASEAN Member States as well. As a country with an intermediate level of development, Viet Nam has much in common with the more advanced economies as well as the less advanced ones in ASEAN. Therefore, the country can serve as a ‘bridge’ for better mutual understanding between the newer and older Member States in the region. The realisation of the potential for further meaningful ASEAN integration rests crucially on this.
References


