Chapter 1

Emerging Economic Architecture in Indo-Pacific: Asia and the Pacific at the Center of Trade, GVC Integration, and Economic Cooperation of Future

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Emerging Economic Architecture in Indo-Pacific: Asia and the Pacific at the Center of Trade, GVC Integration, and Economic Cooperation of Future

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The evolving economic architecture in the Indo-Pacific rests squarely on the post-war construct of the Asia-Pacific, which has been in existence for 6 decades but is undergoing changes in the established patterns of economic integration and supply chain linkages. There are without doubt opportunities and challenges in the new policy alignments for institutional support, and (different levels of) willingness amongst governments over such changes in the supply chain linkages and investments – both in Asia and outside Asia – to materialise a newer construct of trade and economic cooperation. The raison d’être of building a new construct lies in the re-evaluation of the existing trade and investment linkages – in Asia, between Asia and the Pacific, between Asia and Europe, and between Asia and Africa – and in the re-calibration of these linkages, along with economic and technical cooperation activities, to reflect the emergent economic and strategic alignments amongst countries and regions. The economic dynamism of Southeast and East Asia, and now increasingly of South Asia, has been at the centre of all economic and strategic cooperation plans, both bilateral and plurilateral, amongst countries in the region and with interregional partners such as the United States (US), the European Union (EU), the United Kingdom (UK), Canada, and even some parts of Africa. Added to this is the opportunity of including the Pacific Island states in the economic linkages in a more vibrant and inclusive manner. To understand the emergent economic architecture in the Indo-Pacific, it is important to evaluate the current state of trade and investment in the wider region from a growth perspective, as well as the strategic importance of regional value chains and global competitiveness for dominating the new technologies that influence both the existing and new centres for the production and consumption of goods and services.

1. Indo-Pacific: A Long Way from the Far East, East Asia, and Asia-Pacific

In Urata et al. (2019) in the seminal research study *ASEAN Vision 2040* (Tay et al., 2019), the authors described in great detail the evolution of trade and supply chain linkages in the Asia-Pacific, which are based on the trade and investment policies of the major economic players and reflect changes in the strategic interests of the countries in Southeast and East Asia.

In the post-war period, when leadership of world affairs rested in the North Atlantic region, the countries of Southeast Asia were often seen simply as part of the ‘Far East’. In the third quarter of the 20th century, the Association of Southeast Asian Nations (ASEAN), then with six members, played a key role in making familiar the concept of the ‘Asia-Pacific’ (Urata et al., 2019). The Asia-Pacific was understood in different combinations of countries and regions. Urata et al. (2019) elaborated on the different understandings of the geography of the Asia-Pacific in terms of economic linkages, trade and investment, and movement of people, although political history and strategic interests prevail upon these linkages to varying degrees. The Japanese word order was ‘Pacific Asia’, which included the
eastern and south-eastern edge of Asia, Australia and New Zealand, and the US, due to the importance of its security relationship with the region. Canada was also included, by analogy with the US, and Mexico and South America came later, mostly as a by-product of the North American Free Trade Agreement and the subsequent trade agreement with Chile. The American understanding of ‘Asia-Pacific’ was similar, along with the identification of the US as a Pacific power after World War II. The British and European understanding of the Asia-Pacific was more likely to include India, while in Australia and New Zealand it was usually read as ‘Asia and the Pacific’ to include the Pacific islands.

The Asia-Pacific, however, was more than a geographical understanding (which is also true for the current theme of economic cooperation in the Indo-Pacific – a concept that lacks geographical continuity but professes cooperation over trade and investment, and infrastructure and institutional connectivity). The Japanese-led economic integration in the region was characterised by business leadership and diplomatic and official processes ensuring several trade and investment facilitation measures, followed by business decisions on investment and the location of operations. Japan’s experience with export-led growth was quite unlike the prevailing policies in most Asian economies, which favoured import substitution. This growth model was soon followed in the Republic of Korea (henceforth, Korea), Taiwan, Singapore, and Hong Kong in the renowned ‘flying geese’ formation.1 Thailand, Indonesia, and other Southeast Asian countries followed. China was too big to be a single goose in a flock, and its opening to international integration after 1978 ushered in a new phase of regional growth. This growth experience was located in the ‘Asia-Pacific’.

The founding of ASEAN in 1967 helped shape the conception of the region from being the ‘Far East’ – far away from the global centre (the North Atlantic) – to the more familiar ‘East Asia’, which is increasingly seen as the global centre of manufacturing, and consumption of goods and services. The institutional basis for the Asia-Pacific was supported to varying degrees by the non-official Pacific Economic Cooperation Council (founded in 1980) and the Asia-Pacific Economic Cooperation (APEC) process, which was established in 1989 and extended to leader-level summits in the early 1990s.

ASEAN played an important role in the early history of APEC. Its members were crucial in the endeavour to develop a governmental process from the Track II processes of the Pacific Economic Cooperation Council. The six ASEAN Member States (AMS), which represented half the membership of APEC, initially staged half the annual meetings, and generally provided one of two co-chairs for all significant APEC committees. The inclusion of China, Hong Kong, Taiwan, and Latin American members diluted the role of ASEAN and, although Viet Nam became a member of APEC, other new members of ASEAN – i.e. Cambodia, the Lao People’s Democratic Republic, and Myanmar – did not (Urata et al., 2017).

The Asian financial crisis in 1997 reshaped the intra-regional relations to a great degree. The dissatisfaction of ASEAN with financial agencies such as the International Monetary Fund and the World Bank extended to institutional platforms such as APEC, even though financial issues were not central to the role of APEC. The Asian members found the cooperative principles and assistance from

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1 ‘Fishing geese pattern of development’ was coined by Kaname Akamatsu in 1930s articles in Japanese, and presented to world academia after World War II in 1961 and 1962 articles in English. The fishing geese model explains the catching-up process of the industrialisation of latecomer economies from the intra-industry aspect (product development within a particular developing country, with a single industry growing over three time-series curves, i.e. import (M), production (P), and export (E)); inter-industry aspect (sequential appearance and development of industries in a particular developing country, with industries being diversified and upgraded from consumer goods to capital goods and/or from simple to more sophisticated products); and international aspect (subsequent relocation process of industries from advanced to developing countries during the latters’ catching-up process).
other members missing during the crisis. APEC soon ceased to be the unrivalled institutional platform for economic cooperation in the Asia-Pacific, as ASEAN created its own regional trade and economic cooperation mechanisms for strengthening its own economic community objectives, as well as driving the regional economic integration process in Southeast and East Asia region from a position widely known as ‘ASEAN centrality’ in the post-crisis years.

ASEAN and the three North Asian economies – China, Japan, and Korea – explored the potential of an ASEAN+3 grouping in December 1997 and institutionalised it in 1999 when the leaders issued a Joint Statement on East Asia Cooperation at the Third ASEAN+3 Summit in Manila (ASEAN, 2012). Besides the consensus on economic cooperation, social and human development, and development cooperation, this grouping was the basis for monetary and financial cooperation in what eventually became the Chiang Mai Initiative Multilateralisation. The Chiang Mai Initiative Multilateralisation was implemented with a total of $120 billion by the end of 2009 and set up an independent regional surveillance unit – the ASEAN+3 Macroeconomic Research Office. The 12th ASEAN+3 Summit in Chonburi, Hua Hin, Thailand in October 2009 established the Credit Guarantee and Investment Mechanism with initial capital of $500 million under the Asian Bond Markets Initiative to support the local currency-denominated corporate bond in the region (ASEAN, 2021).

The onset of the study on an East Asia Free Trade Agreement under the aegis of ASEAN+3 soon intensified the setting up of the ASEAN+6 grouping – the East Asia Summit (EAS) – which included the original ASEAN+3 and India, Australia, and New Zealand. The first EAS meeting in 2005 was convened within the ASEAN Summit mechanism, and the EAS remains within the ASEAN Summit process. This new regional formation was the institutional response to balance the trade and economic cooperation and supply chain linkages, initially in East Asia but soon extending to the US. Since Australia and New Zealand were some of the oldest Dialogue Partners of ASEAN in the region, and India was a major emerging market, the EAS became a more useful platform for trade, economic, and technical cooperation in the region. The EAS was also the first response mechanism where China centrality in regional value chains, new markets for production and consumption, and the strategic interests of several important economies in the Asia-Pacific were underlying to varying degrees in its subsequent meetings. The inclusion of the US and Russia in the EAS membership in 2010 under Viet Nam’s chairmanship of ASEAN was a none-too-subtle pointer in this direction. In 2006, the Japanese leadership promoted a study on an ASEAN+6 Comprehensive Economic Partnership for East Asia, extending membership to India, Australia, and New Zealand. This became the basis for EAS-led trade and economic cooperation in the region. After several rounds of competing presentations on the East Asia Free Trade Agreement and the Comprehensive Economic Partnership for East Asia in the ASEAN+6 Economic Ministers’ Meetings, the amalgamation of the two studies and the streamlining of ASEAN+1 free trade agreements (FTAs) became the basis for initiating the Regional Comprehensive Economic Partnership (RCEP) in 2011.

The EAS remains an extension of the ASEAN ministerial and leaders’ meetings with ASEAN Dialogue Partners. The dichotomy between trade and investment and regional cooperation issues on one side and strategic and security issues on the other in the EAS was made visible by US leaders who made repeated attempts to characterise the EAS as a ‘political and security’ institution and APEC as the ‘premier regional economic institution’, though there was/is no such distinction in the thinking of the original members of the ASEAN+6 EAS. The EAS and its associated economic cooperation agreements have made ‘East Asia’ rival the ‘Asia-Pacific’ as a component of international affairs.

Japanese leadership is once again seen in bringing the parallel narratives of the Asia-Pacific and East Asia closer to address the changing economic and strategic landscapes in the region. Exploring new markets and centres of production, investments in new supply chains, and securing strategic interests
through increased cooperation with friendly partners was in the background of Prime Minister Shinzo Abe’s speech at the United Nations General Assembly in October 2017. Even till as late as 2018, when the Economic Research Institute for ASEAN and East Asia (ERIA) was writing *ASEAN Vision 2040*, most contributing authors agreed that the Asia-Pacific cannot sufficiently represent the current economic linkages in East Asia. Still, the Indo-Pacific was not generally acceptable to many writers of *ASEAN Vision 2040*, as they believed it to represent security connotations, primarily led by the US. Therefore, *ASEAN Vision 2040* settled for the term ‘Indo-Asia-Pacific’ instead. In 2018, Prime Minister Abe’s speech at the United Nations General Assembly brought the focus on economic linkages and cooperation in this region, albeit aligned with strategic interests. He emphasised that a ‘Free and Open Indo-Pacific’ would be the platform for all economic cooperation and connectivity in the region, between Asia and Africa, and between Asia and Europe. He separately revived the Quadrilateral Security Dialogue, commonly known as the Quad, bringing in the US as a major economic partner in the region – underplaying the security partnerships of the US and actively engaging with Australia and India, with ASEAN playing an important link in between though not at the table.

ASEAN lost no time since then in bringing out the ASEAN Outlook on the Indo-Pacific at the 34th ASEAN Summit in Bangkok, Thailand in June 2019 (*ASEAN, 2019*). The ASEAN Outlook on the Indo-Pacific was endorsed by the EAS in 2019. It recognises ASEAN’s centrality in the new architecture of the Indo-Pacific, just as ASEAN had driven the ASEAN+1, ASEAN+3, and EAS meeting process. In practice however, ASEAN’s centrality in the Indo-Pacific requires greater scrutiny, given that the ASEAN-led EAS could not balance the strategic interests of either the AMS or the Dialogue Partners.

It may be worthwhile considering the role of India in the East Asia narrative and its growing importance in the Indo-Pacific construct, both from an economic and a strategic perspective. India’s participation in the EAS highlights the looseness of the term ‘East Asia’ and was indeed used by some EAS members, both in ASEAN and the plus 6, to question India’s inclusion in the economic construct of East Asia and the EAS. Despite deep historical and cultural linkages with Southeast and East Asia, and a dialogue partnership with ASEAN since 1999, India’s trade integration with this region was weak. With a growing economy and its then ‘Look East’ policy, however, India was ready to join regional institutional arrangements and the EAS fulfilled this objective. The Framework Agreement on Comprehensive Economic Cooperation Between India and ASEAN had been concluded in 2005, and the ASEAN–India Free Trade Area negotiations commenced the same year. In view of its huge negative balance of trade with China and close trade integration between ASEAN and China, and considering its domestic market and industries, India negotiated and concluded a conservative rule of origin and tariff elimination schedule for trade in goods with ASEAN in 2009. India’s rate of growth remained impressive in the following years, attracting the interest of East Asia, especially that of Japan, Korea, Indonesia, Singapore, and Thailand, which had closer trade and bilateral relations with India. The increasing trade imbalance with China, and India’s unresolved strategic interests, gave India the impetus to participate actively in regional dialogue on economic and strategic cooperation, first in the EAS and now in the Indo-Pacific. India has also promoted its bilateral relations with Japan, Indonesia, Singapore, and Viet Nam, amongst others, to forge a layered trade integration that actively supports its strategic interests in the region. While most members of East Asia share oceanic distance, India is the only country that shares a land border with China with a history of border conflicts. India’s inclusion in the East Asia group and its leading role in the Indo-Pacific (and the Quad) is therefore more complex than the tick boxes of contiguous geographical or oceanic region and the extent of trade integration. This complexity is further deepened by the US’s strategic interests in South and West Asia and the Indian Ocean.

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2. Framing the Shift in Economic and Strategic Outlook

Before the Indo-Pacific captured the imagination of observers from across the globe, policy researchers covering this region had explained the essence of the EAS as a first political attempt to balance China centrality in the supply chains of Southeast and East Asia and to forge a rules-based partnership in the East Asia region. ASEAN centrality and the ASEAN Summit, as the drivers of the EAS, were a conscious decision by all members of the EAS to create this balance in an inclusive manner – where no member country could claim exclusion or be singled out. Between 2005 and 2010 – the year the US and Russia became EAS members during Viet Nam’s chairmanship of ASEAN – the cooperation element was predominant in the EAS.

The following years of the EAS witnessed three important features. First, China’s economy grew at an average of 10% during this decade as it rapidly climbed the value chains of production. Several AMS, as well as Japan, the US, Korea, and the EU, were closely integrated with supply chains in China. The Australian economy thrived largely due to commodities exports to China. These economic linkages were, however, being tested by the strategic interests (and intents) of China in the South and East China Sea through unilateral measures of infrastructure development and economic activities.

Second, the US had returned its attention to this region after its prolonged engagement and preoccupation with West Asia. The renaming of its US Pacific Command to the US Indo-Pacific Command in 2018 was a significant signal of its intent for the region, although its strategy was as yet un-delineated. From a trade and economic cooperation perspective, this gave policy watchers an opportunity to link the Indo-Pacific with US security interests in the region, and as a potential threat to the existing economic dynamism of East Asia. It has taken the US a decade to arrive at a more nuanced version of the Indo-Pacific, served by its huge foreign direct investment in the region. The US is now more integrated with the region than before. Japan’s efforts to link the Indo-Pacific with economic cooperation in East Asia and with partners outside Asia notwithstanding, the US’s participation in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (eventually pulling out from the final agreement during the Trump presidency), and the launch of the Indo-Pacific Economic Framework for Prosperity negotiations signify the alignment of the US’s economic and strategic interests in the region. The arrival of the digital economy and technology platforms has made the US’s presence in East Asia more keenly felt than ever before. Third, the unravelling of globalisation since 2016, when ‘Brexit’ and ‘America First’ echoed in other economies, has affected policy sentiment in most countries. The US–China trade tensions, which were initially confined to tariffs, have escalated to control of the technologies that underlie the manufacturing value chains. This narrative was compounded in recent years by the onset of the coronavirus disease (COVID-19) pandemic, which originated in China and created severe supply chain disruptions, at least in the initial few months of the pandemic in 2020. Social and health measures in most countries sustained these disruptions for longer. The existing supply chain dependency and efficiency are therefore being re-examined and sometimes rebuilt with bilateral and trusted partners. New policy watch words such as ‘re-shoring’ and ‘friend-shoring’ are used extensively, and bilateral and trilateral relations are being explored to alter supply chains and investments in favour of friendly countries. In its inception phase, the emergent economic architecture of the Indo-Pacific reflects some or all these phenomena in varying measures.

The reality, however, is that the Indo-Pacific region is an economic construct along the Indian Ocean, in which several alternative plans and groups of countries are working on their mutual relations and combined strengths. The new plans aim to create new or alternative supply chains or to strengthen existing ones – in order to address changing political and economic needs in Asia, incorporate the opportunities arising from the digital economy and Industry 4.0, expand the location of the global...
value chains (GVCs) and new markets, ensure inclusive growth, bridge the fault lines in supply chains exposed during the pandemic, and accommodate partners’ interests from within and outside Asia. The presence of the US as the largest economic and strategic partner is meant to be a guarantor of these objectives and consensus-based changes in the region.

3. Imperatives for Indo-Pacific Coming from Outside of East Asia

Japan’s efforts to draw the economic landscape of the Indo-Pacific were complementary, and even necessary, to address the unilateral changes in the status quo in the South and East China Sea by a rising China. Abe’s call for a Free and Open Indo-Pacific struck a chord with several major trading partners of China, whose reliance on Chinese imports and their greater trade integration (and value chain dependency) with China were being challenged in the political realm, if not by the businesses themselves. As stated above, after the general recovery from the global financial crisis, and especially since 2015 when China announced the Belt and Road Initiative for infrastructure development, the political and public discourse on China centrality in regional supply chains, principles of reciprocity and fair competition, market access, problems of overcapacity, and protection of intellectual property were uppermost in the policy platforms of major economies in Asia and Europe, and in the US, including those in Southeast and East Asia. The EU’s current approach towards China, set out in the ‘Strategic Outlook’ Joint Communication of 12 March 2019 remains valid (EEAS, 2022). The EU continues to deal with China simultaneously as a partner for cooperation and negotiation, an economic competitor, and a systemic rival.

With the EU, the changing nature of China’s supply chains and China’s ascent of GVCs also affected EU member states’ integration with each other in terms of trade in intermediate goods. In fact, while the size of the intra-EU value chain has shrunk (countries are more loosely bound to each other in their exports of intermediate goods), EU member states were increasingly linked to China for intermediate goods (EU, 2020). The EU, therefore, has shown open support for the new policy discourses in East Asia and has stopped using the term Asia-Pacific in its leadership statements. Ursula von der Leyen, President of the European Commission, attended the Asia–Europe Meeting in Cambodia in November 2021. She referred to the region only as Indo-Pacific in her speech. The leaders of all the EU member countries addressed the summit using the same nomenclature. The EU has also put in place its Global Gateway programme, which is covered in the chapter on Supply Chain Connectivities in Indo-Pacific in this volume.

Indo-Pacific is a well-established term in discussions on international security in venues such as the ASEAN Regional Forum and its Council for Security Cooperation in the Asia Pacific. The significance of the Strait of Malacca and its role as a fulcrum between the Indian Ocean, the South China Sea, and the Pacific Ocean make Indo-Pacific a natural term of discussion in Southeast Asia. This is especially true for Indonesia, but also for other AMS that have territorial issues in the South China Sea, with contestations of free movement of goods in the oceans surrounding the ASEAN region. A school of thought regards the current use of Indo-Pacific as a rather transparent effort to create a forum for the promotion of leadership in Asia, excluding China. This study evaluates this claim in the context of the evolution of the Asia-Pacific; the expansion of East Asia; the robust supply chains in East Asia, and between East Asia and the EU and the US; and the balancing of economic and strategic interests amongst these economic partners. In a real sense, the Indo-Pacific is the quest for more inclusive and rules-oriented trade and economic cooperation where places of production and consumption are diversified and advantageous for all stakeholders.
4. Trade and Investment: Hallmarks of Indo-Pacific Economic Architecture

Southeast Asia and East Asia are at the centre of the Indo-Pacific’s economic vibrancy. This region has, over the years, provided buoyancy to international trade and has been the largest recipient of investment (Table 1.1). The RCEP agreement estimates that the 15 member countries\(^3\) of Southeast and East Asia contribute $26.3 trillion to global gross domestic product (GDP). If India were added, this region would account for nearly one-third of global GDP. It is no surprise, then, that important global economies such as the US and the EU (and the post-Brexit UK) are keen on an Indo-Pacific partnership that allows for sharing the economic dynamism of the region through its production facilities, markets, and vast human resources capacity. The Indo-Pacific emerges as a plurilateral component of the international economy. Nobody is thinking in terms of a ‘bloc’. The development of production networks, including the third unbundling, likely makes the blocs of earlier eras impossible. A plurilateral Indo-Pacific would simply be a region that finds it mutually advantageous to work cooperatively.

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\(^3\) The RCEP consists of 15 member countries: the ASEAN 10, Australia, China, Japan, Korea, and New Zealand. India’s participation in the RCEP is on hold until certain demands from India and the rest of the members are resolved to their mutual satisfaction.
### Table 1.1: Trade in Goods amongst the Major Economies of Indo-Pacific (USD Billion)

<table>
<thead>
<tr>
<th></th>
<th>ASEAN</th>
<th>China</th>
<th>Japan</th>
<th>Korea</th>
<th>India</th>
<th>Australia</th>
<th>NZL</th>
<th>EU</th>
<th>US</th>
<th>UK</th>
<th>EAC</th>
<th>South Africa</th>
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<tbody>
<tr>
<td>ASEAN</td>
<td>417.81</td>
<td>238.91</td>
<td>191.25</td>
<td>91.83</td>
<td>80.96</td>
<td>11.15</td>
<td>282.01</td>
<td>373.79</td>
<td>32.27</td>
<td>3.67</td>
<td>10.66</td>
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<tr>
<td>China</td>
<td>417.81</td>
<td>371.35</td>
<td>362.29</td>
<td>125.65</td>
<td>230.11</td>
<td>24.72</td>
<td>828.48</td>
<td>758.10</td>
<td>112.68</td>
<td>15.27</td>
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<tr>
<td>Japan</td>
<td>238.91</td>
<td>371.35</td>
<td>84.69</td>
<td>19.01</td>
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<td>5.70</td>
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<td>219.06</td>
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<td>1.87</td>
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<tr>
<td>Korea</td>
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<td>84.69</td>
<td>23.66</td>
<td>42.66</td>
<td>3.46</td>
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<td>EU</td>
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ASEAN = Association of Southeast Asian Nations, Korea = Republic of Korea, EAC = East Africa Community, EU = European Union, NZL = New Zealand, UK = United Kingdom, US = United States.

As with trade, the supply chains in the Indo-Pacific are equally vibrant and the China centrality in the supply chains is visible in most sectors of production. Countries’ participation in GVCs, as measured by the value added generated in a country that crosses at least two borders in international trade relative to gross exports, reached a peak at the global level in 2008 and declined progressively afterwards. This feature also included Asian economies and the ASEAN region (Figures 1.1 and 1.2). The ASEAN example is particularly important as it provides a snapshot of trade integration between the largest economy in Asia and an economic community of member states that have differently sized economies, industrial bases, and levels of participation in the regional value chains. Moreover, ASEAN has been the fulcrum of trade and investment linkages from partners within and outside Asia. It is one of the most open economic regions in the world, and its economies are growing faster than the rest of the world and are converging in terms of production capacity as well as purchasing power.

Figure 1.1: GVC Participation by Economic Area (% of gross exports)

Figure 1.2: GVC Participation by Economic Area and Type, 2015 (% of gross exports)

ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States.

Notes: ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019. Source: OECD (2018).

The ASEAN+3 region – comprising the 10 AMS, China, Japan, and Korea – provides the most vibrant GVC integration in the Indo-Pacific region. Indeed, these economies exemplify what are called regional value chains. ASEAN integration with the main developed economies has declined since its peak in the late 2000s, maintaining a steady negative trend vis-à-vis the US and Japan, but there has been a partial recovery with respect to the EU. On the other hand, ASEAN has become increasingly integrated with

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4 The GVC database used in this chapter covers 2000–2015. Unfortunately, data for the GVC analysis are published with a substantial delay, and the available sample does not allow a thorough analysis of recent trends – particularly the effect of the COVID-19 outbreak. For the latter, higher-frequency but indirect and partial metrics are used in Chapter 5 to provide insights on potential GVC reshuffling originated by the pandemic.
the two largest Asian economies, particularly with China, which has become the main individual partner in GVCs.

ASEAN integration has progressively shifted away from developed to developing economies, particularly reflecting what is known as ‘China centrality’ in GVCs (Figure 1.3). With developed economies, a steady negative trend has been observed for ASEAN integration with the US and Japan since its peak in the late 2000s. In contrast, a partial recovery has taken place in recent years with respect to the EU, which remains the main integration partner for ASEAN amongst developed economies.

Figure 1.3: GVC Participation of ASEAN, by Partner
(% of Gross Exports)

ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, US = United States.
Notes: ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019.

The China centrality in the GVCs was evident during the outbreak of the COVID-19 pandemic in Wuhan, which later spread to the rest of the world. The first instance of supply shocks emerged from China, especially for medical supplies, leading to a breakdown of entire production and consumption lines in Asia and the rest of the world. While the GVC participation rates had slowed since the global financial crisis in 2008, the COVID-19 experience of supply and demand shocks has given impetus to further balancing of GVCs and investments in supply chains in terms of distance, reliability, and vertical integration. These aspects of GVC participation predate the US–China trade tensions and the COVID-19 related shocks to supply chains. The latter two have only intensified policy actions amongst governments to establish a network of trade and investment in the Indo-Pacific which integrates the strategic and economic interests under similar if not the same rules of engagement.

This, effectively, is the antithesis of economic integration with China, and in the larger Indo-Pacific region. When China joined the World Trade Organization in 2001, the labour dividend in China was available to regional economies as well as businesses in developed markets. China’s vertical integration leads to China’s reduced dependence on Asian regional value chains. As discussed in the
previous parts of this chapter, Europe’s value chain became increasingly dependent on China at the expense of its own regional integration. The US encountered rising dependency on Chinese intermediates while facing declining exports of intermediates not only to China but also the rest of the world. Reshuffling of supply chains to Southeast Asia in response to China’s vertical integration has been the intermediate response, as seen in the increased investments of the EU and the US in ASEAN since 2010 (Herrero, 2019).

The Indo-Pacific economic architecture is therefore a longer-term response for the balancing of trade and investment partnerships amongst the major economies of the world, with Southeast Asia, East Asia, and the Pacific at the core. The Indo-Pacific is also differentiated by a larger role of South Asia, especially India, in the alignment of strategic and economic interests with the rest of the major players in the architecture. When seen as an oceanic construct, the Indo-Pacific also envisages trade integration and production sharing with countries along the eastern seaboard of Africa as well as the major economies in East, North, and South Africa (Chaturvedi, Prakash, and Dash, 2020).

5. Raising the Indo-Pacific Architecture on Firm Grounds

The Indo-Pacific economic architecture builds upon existing capacities in manufacturing, innovation, trade, and investment – leading to new policy alignments over strategic interests, new production locations, and markets. COVID-19 and the US–China trade tensions have given a new impetus to the rule-setting process around trade and investment (Figure 1.4).

**Figure 1.4: Building Blocks for the Indo-Pacific Economic Architecture**


Source: Author.
Supply chains in ASEAN, East Asia, and South Asia are likely to remain intact in the post-COVID-19 period. It is still early to say to what extent GVC integration has been affected by the COVID-19 pandemic, as rigorous data will only be released after a delay of some years (Shepherd and Prakash, 2021). Besides the policy conversation (and agreements) for restructuring of supply chains along elements of distance and reliability, and an increased policy weightage to domestic production centres, the Indo-Pacific economies are now more engaged in rebuilding and rebalancing trade and investment. The region is also aware of the major potential change in conditions facing GVCs in the rise of the digital economy, environmental products, electric vehicles, or goods suited for increasingly carbon-neutral societies. Recovery programmes in high-income markets will favour this shift through incentives and other measures. East and Southeast Asia is well positioned to take advantage of these opportunities, with some important incentives of retooling. Keeping markets relatively open, an effective supplier network, and integrated GVCs could be an important advantage for the Indo-Pacific region in developing the GVCs of the future.

The ASEAN and East Asia region has shown, so far, that supply chains have been able to withstand the supply and demand shocks emanating from the pandemic-induced disruptions and delays. The implications of the pandemic are mainly macroeconomic, with some difference across sectors. From a supply chain integration standpoint, technology (digital, robotics, and automation) has the potential to move production closer to the location of final consumption. The pandemic experience will likely lead to a reassessment of the risks associated with dispersed production and just-in-time management practices. The US–China trade tensions over control of technologies and redistribution of investments, together with new rules of economic engagement, will likely facilitate a rebalancing of GVCs amongst the trading partners, and the Indo-Pacific will represent these changed dynamics of cooperation and change.

Trade and investment policies will assume more significance in the coming months as they determine the ability of firms to contest markets or to source intermediate inputs from foreign suppliers. For ASEAN, East Asia, and South Asia, trade and investment facilitation will be crucial as it can increase backward and forward linkages and deepen trade integration. Nurturing the business environment will also play a role in structuring trade relations in the Indo-Pacific. The trade agreements of the RCEP, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, and the Indo-Pacific Economic Framework for Prosperity will be expected to play a crucial role in trade integration and investments in the Indo-Pacific region.

An Indo-Pacific trade and economic cooperation plan must consider China. In 2019, China became ASEAN’s largest trading partner (surpassing intra-ASEAN trade) and is now the fifth largest investor in the region. Closely integrated value chains between China and ASEAN have cast a shadow on some trade and investment partnerships with ASEAN, e.g. with Japan, the EU, and most noticeably with India. The negotiations on trade in goods in the RCEP reflected these concerns at several points before the conclusion of the FTA. It is also an important reason why India stayed out from the conclusion of the RCEP. The emerging economic architecture in the Indo-Pacific, in which ASEAN has a central role, will also face the inevitability of supply chain integration between ASEAN and China, and the EU and China, amongst others. The lessons from the pandemic and the advent of the digital economy underline both the scope of, and immediate need for, efficient and trusted partners. Equally, value chains of the green economy, high-tech production, research and development, and financial markets are other strong prospects for the Indo-Pacific region. Investments in infrastructure for the digital economy and cybersecurity are the two most pressing needs in the region for it to grow as a digital economy hub. The Indo-Pacific region should be ready and able to fulfil both the capacity needs and trust issues required in these areas of cooperation.
The Indo-Pacific region is home to some of the most open markets for both trade and investment. Its economic dynamism is becoming contemporary and future-ready through the cooperation plans for new GVCs and investments, and rules of engagement.

In the following chapter, readers will find evidence supporting the cooperation plans along several verticals of economic and strategic interests in the Indo-Pacific. The building blocks of the new economic architecture in the Indo-Pacific are already in operation, with the caveat that there are several opportunities, some certainties of success, and a few unknown gaps that will shape progress towards the future.

References


