

The enterprise for ASEAN initiative in the emerging Asia-Pacific context: a politico-economic assessment*

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Abstract

Although economic integration under the rubric of the Asia-Pacific Economic Cooperation (APEC) has been relatively lackluster, bilateral and regional accords in the Asia-Pacific region have been proceeding at an unprecedented pace. This paper considers the economics and political economy of the US-ASEAN Enterprise for ASEAN Initiative (EAI) in the context of the rapidly changing policy environment in Asia. The paper gives an extensive review of the ASEAN Economic Integration and "ASEAN Plus Three" Initiatives, in addition to a statistical and econometric treatment of the US-ASEAN economic relationship and the implications of the EAI. It concludes that the EAI makes sense for the United States and ASEAN from both economic and politico-economic perspectives.

JEL classification: F15

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1. Introduction

At the APEC Annual Summit in October 2002, US President Bush announced his desire to pursue a series of bilateral free trade areas (FTAs) under the rubric of the Enterprise for ASEAN Initiative (EAI). There were only two conditions included in the EAI: (1) ASEAN members must be a World Trade Organization (WTO) member, and (2) they had to have in place a trade and investment facilitation liberalization (TIFL) agreement with the United States. While this posed no problem for the original ASEAN member-states and Brunei Darussalam, it could impede negotiations with the new members—Cambodia, Laos, Myanmar, and Vietnam—of which are transitional economies.¹

In many ways, the EAI did not come as a surprise to most observers for a number of reasons. First, the Bush administration had been actively pursuing FTAs with partners throughout the developing world. The US policy of uniquely supporting multilateral liberalization under the GATT/WTO framework changed in the 1980s, first with an FTA (in manufacturing) with Israel and followed by an FTA-like agreement with the Caribbean Basin (1986), the US-Canada FTA (1989), and NAFTA (1994). When the Bush administration received Trade Promotion Authority in 2002, it immediately began negotiating a number of bilateral FTAs with countries throughout the world.

One of these FTAs was with Singapore, which leads us to the second reason why the EAI was expected: Singapore is a key member of ASEAN, and it was believed that after cementing an agreement with Singapore, it would only make sense—from both the US and ASEAN points of view—to consider an accord with other ASEAN member-states. While the EAI framework would no doubt require diversity of substance given the diversity of ASEAN and the fact that Singapore was an “easy partner in that it is rich, developed, has no agricultural sector, and is uncompetitive in other sensitive areas, the US-Singapore FTA did mark which areas and sectors would be included in the EAI FTAs.

Third, given the regionalism zeitgeist, ASEAN is a natural priority target. While ASEAN countries differ considerably in terms of per capita income, most are growing trading partners of the United States. If one controls for their size, the trade with these countries is several times more than one would expect if they were randomly selected countries. Also, the ASEAN countries play host to a more than proportionate share of US multinational investments and have become key to the trade and investment strategies of many American companies. The major push toward greater economic integration in ASEAN over the past decade and a half, from the ASEAN Free Trade Area (AFTA) to the decision in October 2003 to create an ASEAN Economic Community, makes it an even more attractive region.

¹Of this group, only Cambodia is a WTO member-state (as of June 2005). Vietnam has normal trade relations and bilateral trade agreement (BTA) with the United States, and is likely to join the WTO in 2005 or 2006. A Laos-US BTA, styled on the US-Vietnam BTA, came into effect in early 2005 when the US Congress granted normal trade relation status to Laos. Only Myanmar is likely to be left on the sidelines in the short and medium term.

Finally, the United States has long pondered a series of FTAs with the ASEAN countries. For example, in the late 1980s, the US and ASEAN governments, with the United Nations Development Program (UNDP), initiated a collaborative study including both ASEAN and American scholars to explore new means of bilateral cooperation. It was published by the Institute for South East Asian Studies (ISEAS) in Singapore in 1989 [Naya et al. 1989] and concluded that before an FTA could be negotiated, ASEAN needed to deepen its economic integration significantly, which it subsequently did. Coupled with the new US interest in bilateralism, supply and demand appears to be in place, making the moment propitious. A salient contribution of this study was the recommendation that, to promote closer relations, a framework agreement should be developed under which the United States and ASEAN could eventually form a free trade area.

As the proposal to form a series of bilateral FTAs between the United States and ASEAN countries has become a reality, the goal of this study is to consider the economics and political economy of the EAI. The rest of this paper is organized as follows: first, we give an analytical overview of the evolution and significance of ASEAN and Asian economic integration, and consider its significance to the role of the United States in the region (section 2). Next, we give a statistical (section 3) and econometric (section 4) treatment of the US-ASEAN economic relationship, focusing mostly on trade in goods but also considering trade in services and foreign direct investment (FDI). Section 5 gives some concluding remarks.

2. ASEAN and East Asian integration

Intra-ASEAN trade has been rising (marginally) and currently comprises 22 percent of total trade. But ASEAN trade with advanced developing Asian countries such as China and Korea (not including Japan) has been growing faster than intra-ASEAN trade, comprising more than 40 percent of total trade. In other words, intraregional economic integration in East Asia has been increasing substantially. Moreover, this trend is market driven rather than policy driven, as was arguably the case in the early years of the European Union integration. The many new FTAs being proposed in the region, if implemented, could compound the existing trend. This would suggest that the United States could find itself losing market share in the world's fastest-growing market.

In the past, the United States did not have to compete with other Asian powerhouses for policy influence in the region. Japan and South Korea were committed multilateralists, and China had not yet emerged as a major economic player. In the 21st century, however, the policy situation has changed considerably. China is now a regional powerhouse and has become active in proposing new FTAs in Asia. China and ASEAN began their Early Harvest Program as a sort of down payment in the FTA negotiation process in 2004, and it was completed at the end of 2004. The agreement is not nearly as comprehensive and "hard" as US FTAs typically

are, but it is interesting that China and ASEAN were able to come to an agreement so quickly. Spurred by China's initiative, Japan and, to a lesser extent, South Korea have also become very active in pursuing FTA agreements with ASEAN. In fact, Japan and Singapore signed an FTA agreement in 2002. Japan has also initiated financial cooperation in the region. Obviously there are strong political as well as economic motivations. Japan-ASEAN will take more time and, we suspect, will be even watered down.

Thus, the United States is finding that major powers are now competing for influence in some of its most lucrative and promising markets. In many ways, the ASEAN plus Three (ASEAN, Japan, China, South Korea) is merely a repackaging of the East Asian Economic Bloc proposal articulated by Prime Minister Mahathir in December 1990. Fearing that a bloc excluding the United States in the region could have severe consequences for US competitiveness in the region, the Clinton administration forcefully voiced its disapproval of such an arrangement and was upset that it was suggested at a time when APEC was getting off the ground. As a result, the US agreed to a watered-down and nonthreatening version of the proposal, i.e., the Asian Economic Caucus.

What is behind this resurgence in East Asian regionalism? First, we identify several factors that stem directly from the Asian financial crisis: (1) obvious contagion relationships, which demonstrated the policy externalities across countries in ASEAN; (2) major disappointment with respect to the US reaction to the crisis, leaving the feeling of "being in it together"; (3) disappointment with APEC progress in trade and financial cooperation, as well as development assistance cooperation (ECOTECH); (4) Japan's offer to create an Asian Monetary Fund during the crisis—opposed by the International Monetary Fund (IMF) and the United States—whatever its inherent merits, which gave the impression that Japan was not to be proactive; (5) arguably, China's decision not to devalue during this period, which also created a sense of solidarity; and (6) the IMF's solution, which was viewed as inappropriate.

The financial crisis itself set the stage for the emergence of serious East Asian regionalism. There are many other internal and external forces at work, such as the rise of regionalism globally and its potential negative effects on the region; the successful implementation of the Single Market Program in Europe and, eventually, a monetary union; questions regarding what can be achieved at the WTO in light of the Seattle and Cancun agreements; and the potential inherent benefits of FTAs. It is ironic that since the establishment of the WTO, there has been a rapid increase in regional trade arrangements, more than 250 as of 2005.²

One might have expected a full retreat in the face of the crisis and the many problems it created. Instead, two important policy decisions have emerged from the crisis. First, ASEAN economic cooperation has been increasing in depth and breadth, including the ASEAN Vision 2020 and, particularly, the ASEAN Economic Community (AEC) initiative, which would create a "common market minus" in which goods

²See <http://www.wto.org>.

services, capital, and skilled labor would flow more freely. It is not certain exactly what the AEC will look like, as its dimensions are currently being developed. Still, it is now a priority in ASEAN.

It is likely that ASEAN sees the AEC as critical in order to ensure that an ASEAN identity is not lost when it integrates with its larger partners. The main priority of the Hanoi Plan of Action in December 1998 was to develop a framework for the Vision 2020. Out of this process came recommendations to (1) speed up the AFTA process and ancillary integration initiatives (e.g., the ASEAN Investment Area, services trade liberalization); (2) further strengthen the technical capacity of the ASEAN Secretariat, raising the number of staff from 64 to 99;³ and (3) implement the ASEAN Surveillance Process (ASP) and ultimately the Bali and Vientiane ASEAN Summits in 2003 and 2004, which began to put meat on the bones of the AEC.

Second, the crisis gave impetus to the creation of the "ASEAN plus Three" or APT (of course, the creation of APT may be traced back to Europe's wanting ASEAN to bring East Asia to the negotiating table in Asia-Europe Meeting [ASEM]). After the crisis, Korean Prime Minister Kim Dae Jung proposed the East Asian Vision Group, with a goal of creating an East Asian FTA. The group proposed such an accord at the 5th APT Summit in 2001, at which an East Asian Summit was also slated for 2005 in Kuala Lumpur. Also, Japan proposed that an Asian Monetary Fund be created to assist Asia in future times of need. The proposal, facing the objection of the US government and the IMF, eventually led to the creation of the Chiang Mai Initiative, which was a financial arrangement in the form of bilateral currency swaps.

It would be difficult to comprehend the recent regionalism drive in ASEAN without recognizing the new roles being played by China and Japan. Intraregional trade between APT countries comes to over 40 percent and is now being driven by China. Interestingly, when Japan and South Korea took off industrially, their external accounts tended to be biased toward a trade surplus, i.e., there was a great focus on exports (and intentional biases against imports). China has emerged as a key exporter and importer; its trade surplus with the United States is large, but its overall trade surplus is fairly modest. Moreover, China continues to grow at more than 9 percent (9.5 percent in 2004, although growth may have slowed marginally in 2005), while Japan has been in economic doldrums for over a decade. Hence, this trajectory will likely continue through the medium term. No doubt this is another reason why the China-ASEAN agreement was reached so quickly. And it is also an important factor in pushing the AEC.

For various reasons, there has not been extensive formal East Asian integration, but instead "ASEAN+3" cooperation has moved away from regionwide efforts in favor of "ASEAN+1" agreements. Coupled with the fact that some partners are more interested in bilateral arrangements than regional ones (the United States would fall into this category as well), the incentive to expedite the AEC is clearly there.

³In a project for the ASEAN Secretariat, which we undertook jointly with Cesar Virata in 1991 [Naya 1992], we recommended that the Secretariat be improved in this way as a *quid pro quo* for effective integration. While the Secretariat had been beefed up significantly in the 1990s, this initiative came closer to what we had envisioned.

If APT succeeds in advancing regional integration, through FTAs and/or financial cooperation, it is likely that these accords will be open, as the economic motivation to create a closed bloc simply does not exist (and declarations all stress open regionalism). We would suggest that the United States does not to fear Fortress Asia.

At the latest ASEAN Summit in November 2004, held in Vientiane, ASEAN accelerated the completion of AFTA from 2010 to 2007. More important, extraregional deals dominated the summary. China, after only two years of negotiation over the Early Harvest Agreement, signed an FTA with ASEAN to be completed by 2005 but this excludes a number of sensitive goods, such as automobiles, sugar, iron and steel. It also lacks agreements on services and dispute settlement. Japan and the Philippines also signed an agreement. The Japan-ASEAN FTA will commence negotiations in 2006; these are set for completion by 2012. In addition, negotiations with India, South Korea, Australia, and New Zealand are in the works. The summit might be construed as a reflection of China's desire to expedite trade liberalization with ASEAN and its East Asian partners toward the formation of an East Asian trading bloc. Malaysia's proposal to hold the first East Asian Summit was adopted. The United States has not been invited to this summit.

There have been many complications and difficulties in advancing East Asian integration, and words have frankly exceeded deeds. However, the United States should not underestimate the potential of East Asian regionalism. It could be negatively affected by trade diversion and could find itself losing influence if it does not act proactively in cementing closer relationships with the ASEAN countries which, after all, form the core of the APT. Moreover, the EAI has merits well beyond the mere economics of the initiative. The proposed East Asian Summit could well become a regular event, laying the foundation for a future East Asian economic community. The nature and participation are important, as these will influence the direction of East Asian integration. When Prime Minister Mahathir, who initially proposed the idea of a special summit, tabled his plan, it included only the current APT countries; it was somewhat inward looking. In fact, it was reported that Malaysia and China supported the participation of only APT countries in the upcoming summit. But Indonesia, Singapore, and Vietnam supported the involvement of a wider grouping, including Australia, New Zealand, and India. Hence, there was a considerable degree of division among ASEAN countries, and there were even fears of the summit being cancelled because of this disagreement. But as it has often done in the past to its credit, ASEAN came up with an amicable solution in Cebu at a meeting of ASEAN foreign ministers in December 2004, allowing the participation of other countries by signing the ASEAN Treaty of Amity and Cooperation, meeting two other conditions. This has opened the door for India, Australia, and New Zealand if they meet the three conditions.

This will distinguish the upcoming Asian Summit from the regular APT meetings. The United States has tried not to influence the course of discussion of the summit for various reasons and so far it has not shown any interest in attending. This is due most likely to the fact that the countries will remain outward looking, as well as to the US pursuance of EAI and, possibly, APEC.

3. US-ASEAN trade and investment links

Trade between the United States and ASEAN has grown substantially in recent years. Two-way trade from 1990 to 2003 rose from US\$ 48 billion to US\$ 122 billion (Tables 1 and 2). The United States is the largest export market for ASEAN as a whole and for most individual countries, with the notable exception of Indonesia. Exports to the United States comprised 16 percent of total ASEAN exports in 2003, although this share declined from 20 percent in 1990. In 2003, ASEAN's share of exports to Japan was 12 percent, down from 18 percent in 1990, and exports to China, 6.7 percent, rising from 1.8 percent in 1990. Intra-ASEAN trade as a percentage of the region's total trade rose to 20.4 percent from 19 percent during the same period. ASEAN imports from the United States comprised 12.3 percent of the total, down marginally from 14.7 percent in 1990.

The ASEAN countries do constitute an important market for certain US exports, although obviously a fairly even distribution of the US global trade between Europe, the Americas, and Asia, and the relatively small size of the ASEAN markets, naturally result in relatively low trade shares. Nevertheless, the ASEAN share of US exports has gone up to 6.1 percent in 2003 from 4.8 percent in 1990, while ASEAN's share of US imports also rose from 5.6 percent to 6.0 percent during the same period. The United States traditionally also has a substantial trade in services surplus with ASEAN; in 2002, the surplus in trade in private services totaled US\$ 5.6 billion (Table 3).

Rapid economic growth in ASEAN—pre- and post-crisis—has provided a plethora of new market opportunities for US exports and investors abroad. ASEAN countries have not yet reverted to the pre-crisis growth trend, but the economic expansion over the past five years has been far greater than the global average, and future prospects are bright, although rising oil prices over 2004-2005 are worrisome for some countries. In fact, the average global economic growth in 2004 is estimated to have been at its highest level in two decades, and trade growth has followed. These trends suggest that ASEAN will play an increasing role in US global economic interaction in the future. Moreover, as ASEAN lies in the heart of one of the most dynamic regions of the world, it will continue to be an attractive place for US multinationals.

Table 1. Exports of ASEAN, Japan, and the United States
(in % of world total)

To	Exports of				
	ASEAN	JA	CH	US	DA
<i>Japan</i>					
1990	18.5	-	14.1	12.4	14.4
2003	12.1	-	13.6	7.2	10.1
<i>US</i>					
1990	20.0	32.0	11.0	-	22.0
2003	16.0	25.0	21.0	-	18.0
<i>China</i>					
1990	1.8	2.1	-	1.2	5.1
2003	6.7	12.1	-	3.9	12.0
<i>ASEAN-5</i>					
1990	19.1	11.5	5.8	4.8	10.9
2003	20.4	12.3	6.0	6.1	10.7
<i>Dev. Asia</i>					
1990	35.1	31.3	48.3	15.5	33.3
2003	36.3	39.7	42.8	16.4	42.1
<i>World*</i>					
1990	138,813.0	287,678.0	69,478.0	393,106.0	451,900.0
2003	426,636.0	473,911.0	438,250.0	723,611.0	1,562,727.0

Source: IMF [2004].

*In US\$ million

Table 2. Imports of ASEAN, Japan, and the United States
(in % of world total)

From	Imports of				
	ASEAN	JA	CH	US	DA
<i>Japan</i>					
1990	23.6	-	13.4	18.0	21.0
2003	16.1	-	18.4	9.3	16.4
<i>US</i>					
1990	14.7	22.5	10.7	-	15.2
2003	12.3	15.6	8.2	-	9.9
<i>China</i>					
1990	2.9	5.1	-	3.2	7.7
2003	8.1	19.7	-	12.5	12.1
<i>ASEAN-5</i>					
1990	15.4	11.9	5.5	5.6	9.8
2003	23.5	13.9	11.0	6.0	13.9
<i>Dev. Asia</i>					
1990	29.9	28.9	35.1	20.2	30.7
2003	40.9	40.4	26.3	24.4	42.7
<i>World*</i>					
1990	158,870	235,307	58,632	517,020	467,800
2003	393,621	382,922	412,836	1,305,220	1,455,220

Source: IMF [2004].

*in US\$ million

Table 3. US trade in private services, 2002
(in million US\$)

	<i>Exports</i>	<i>Imports</i>	<i>Balance</i>
World	279,495	205,234	74,261
Japan	29,688	17,312	12,376
Indonesia	1,021	285	737
Malaysia	1,142	498	644
Philippines	1,514	1274	240
Singapore	5,766	2070	3,697
Thailand	1,139	810	329
ASEAN-5	10,583	4,936	5,647
China	6,073	4136	1,937

Source: Department of Commerce, Bureau of Economic Analysis.

However, we might also note that in addition to potential "growth effect", ASEAN could easily become an even more attractive destination for US FDI in the short and medium term for other reasons, such as AFTA, which considerably reduces transaction costs associated with using ASEAN as a production hub, as well as outward-oriented economic reforms in general.

Over the years, American firms have invested a substantial amount, second only to Japan, in ASEAN countries. The US FDI stock in ASEAN countries was about US\$ 81 billion in 2003, substantially higher than the US FDI stock of US\$ 12 billion in China (Table 4). However, total FDI inflow into ASEAN from the United States as well as other investing countries has declined sharply from US\$ 23 billion in 1997 to US\$ 5.7 billion in 2002 (Table 5). Indonesia, in particular, has had a substantial and continuous negative inflow of FDI since 1998. It is easy to understand why many countries in the region see this trend as alarming, as China has absorbed FDI that might have gone to ASEAN. For example, it received eight times as much FDI as the ASEAN-5 in 2002.

4. Capturing the US-ASEAN economic relationship

From the above review, it is clear that the United States and the EAI are important trading partners. But relative to other countries, how does the relationship fare? To what extent is the US-EAI economic relationship "special" in a global context? Do the United States and ASEAN form a "natural economic bloc"?⁴ In other words, is

⁴For a review of the economics of what constitutes a natural economic bloc, see Frankel [1997]. We note here several possible measures that have emerged in the literature: (1) trade shares greater than 50 percent [Krugman 1991]; (2) double-density measures greater than 1 (Frankel [1992]; Petri [1993]); (3) an arrangement that preserves comparative advantage [Kreinin and Plummer 1994]; and (4) statistically significant binary coefficients on bilateral trade, which is what we focus on here.

US-EAI economic interaction in the order of what one would expect from countries with the economic characteristics of the United States and EAI? We attempt to address this question by using a gravity model of international trade flows. This is an econometric procedure in which trade in a certain year is posited as a function of the GDP of the source and partner country (or their product) as a proxy for size, per capita income of the source and partner country (or their product) as a proxy for wealth, distance between the two countries as a proxy for transportation and other costs, and an adjacency binary (dummy) variable to control for whether or not the trading countries have a common border. To test the hypothesis that a natural trade bias does exist, we add a regional dummy variable.

The binary variable is rising (falling) over time, meaning that the trade bias is increasing (decreasing). We ran our entire gravity model for US trade with ASEAN, as well as for EU trade with ASEAN as a "control country". Our model is based on a database made publicly available at Andrew Rose's website at the University of California, and includes US and EU trade with 178 countries.

Presented in Figure 1 are the estimated coefficients on the ASEAN binary variables for the United States and the European Union, denoting those statistically significant as a "dot". As expected, given the results of the pooled data above, the estimated coefficients are larger for the US market than for the EU market. Moreover, prior to 1970, there were no statistically significant ASEAN binaries for Europe, whereas they were statistically significant for most of the period 1948-1970 for the United States, albeit with considerable volatility. Since the mid-1980s, i.e., when ASEAN countries began to embrace an aggressive outward-oriented development policy, the magnitudes of the ASEAN binary coefficients have been rising for both the United States and the European Union, peaking just before the Asian crisis. Estimated coefficients for the European Union and the United States tend to move together over time.

Table 4. US FDI outward position in and outflows to ASEAN and China
(million US\$)

	US FDI Stock				
	1990	1993	2001	2002	2003
Indonesia	3,207	4,864	10,551	10,341	10,387
Malaysia	1,466	1,975	7,489	6,954	7,580
Philippines	1,355	1,953	5,436	4,642	4,700
Singapore*	3,975	8,875	40,746	52,449	57,589
Thailand	1,790	2,943	6,176	7,608	7,393
ASEAN-5	11,793	20,610	70,398	81,994	87,649
China	354	916	12,081	10,499	11,877

*Singapore 2002 figure is from 2001 data.

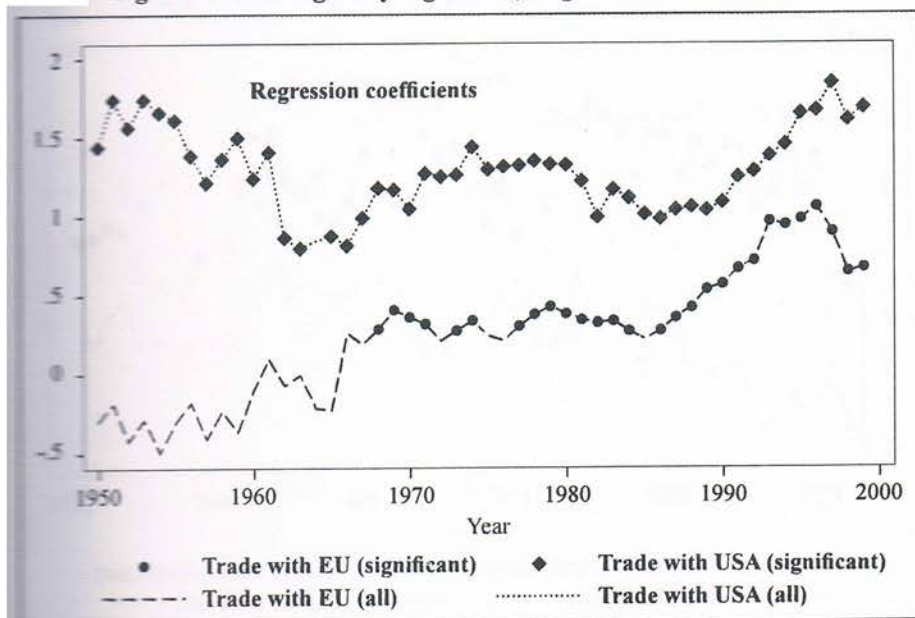
Source: US Department of Commerce, Bureau of Economic Analysis
website: <http://www.bea.doc.gov/bea/di/1001serv/intlserv.htm>.

Table 5. OECD FDI outflows to ASEAN, selected years (1985-2000)

	1995	1997	1998	1999	2000	2001	2002
<i>ASEAN-5</i>							
Indonesia	4,346.0	4,677.0	(356.0)	(2,745.0)	(4,550.0)	(3,278.0)	(1,513.4)
Malaysia	4,178.2	5,136.5	2,163.4	3,895.3	3,787.6	553.9	3,203.4
Philippines	1,478.0	1,222.0	2,287.0	1,725.0	1,345.0	982.0	1,111.0
Singapore	7,206.4	8,085.2	5,492.9	8,550.6	11,919.1	(2,025.1)	2,030.5
Thailand	2,068.0	3,894.7	7,315.0	6,102.7	3,366.0	3,820.1	900.2
ASEAN-5 Total	19,276.5	23,015.4	16,902.3	17,528.6	15,867.7	52.9	5,731.7
<i>New ASEAN</i>							
Cambodia	150.8	204.0	242.9	230.3	148.5	148.1	53.8
Lao PDR	95.1	-	-	-	33.9	23.9	25.4
Myanmar	279.2	390.8	317.8	255.6	258.3	210.3	128.7
Vietnam	1,780.4	2,220.0	1,671.0	1,412.0	1,298.0	1,300.0	1,400.0
New ASEAN Total	2,305.5	2,814.8	2,231.7	1,897.9	1,738.7	1,682.3	1,607.9
ASEAN-10 Total	21,582.0	25,830.2	19,134.0	19,426.5	17,606.4	1,735.2	7,339.6
China	35,849.2	44,237.0	43,751.0	38,753.0	38,399.0	44,241.0	49,308.0

Source: Asian Development Bank, Key Economic Indicators, Table 33, www.adb.org.

Figure 1. ASEAN gravity regression, original ASEAN countries



Given that the gravity models are loglinear in general but the binaries cannot be logged, the meanings of the coefficients have to be treated with care. For example, an estimated coefficient equal to 1.5 would suggest that US trade with the ASEAN countries is 165 percent higher than one would expect, given the effects of all the other variables controlled for in the model.

After controlling for the usual factors, such as size, wealth, and distance, Figure 1 reveals that there exists a bias toward bilateral trade in US-ASEAN trade patterns. Indeed, we find that the US-ASEAN relationship is special, in that the partnership adds extra explanatory power to the determinants of trade flows.

However, upon separating individual ASEAN countries (Figures 2-6), this special relationship does not quite materialize in the case of Indonesia (except for a few years); exists only to some degree in the case of Malaysia but appears to be declining over time and with a good deal of volatility; and is most notable in the cases of Thailand and the Philippines but, again, the magnitude and, in the case of the Philippines, statistical significance decrease over time. We suggest that this decrease in bias toward bilateral trade could be a result of the fact that the United States—as well as the European Union—has been creating FTAs and other bilateral accords with ASEAN's competitors. Or it could be that ASEAN countries have been losing competitiveness for other reasons, e.g., the emergence of China and India as major competitors, or local structural factors. In any event, the EAI would certainly help remove any associated trade diversion from regional agreements, give the region a level playing field in the US market, and even give it a competitive edge over such formidable competitors as China.

Figure 2. ASEAN gravity regression, trade with the Philippines

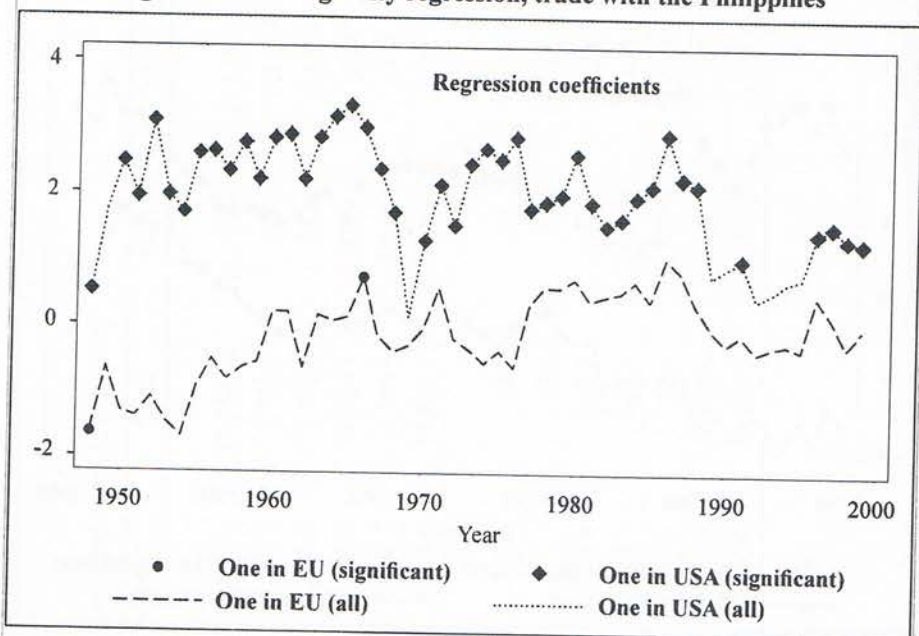


Figure 3. ASEAN gravity regression, trade with Malaysia

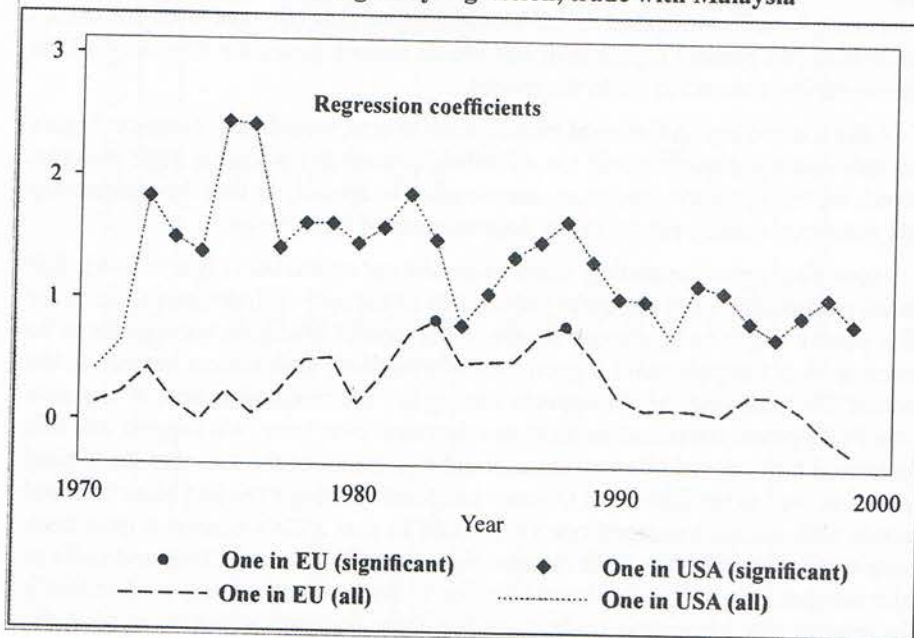


Figure 4. ASEAN gravity regression, trade with Indonesia

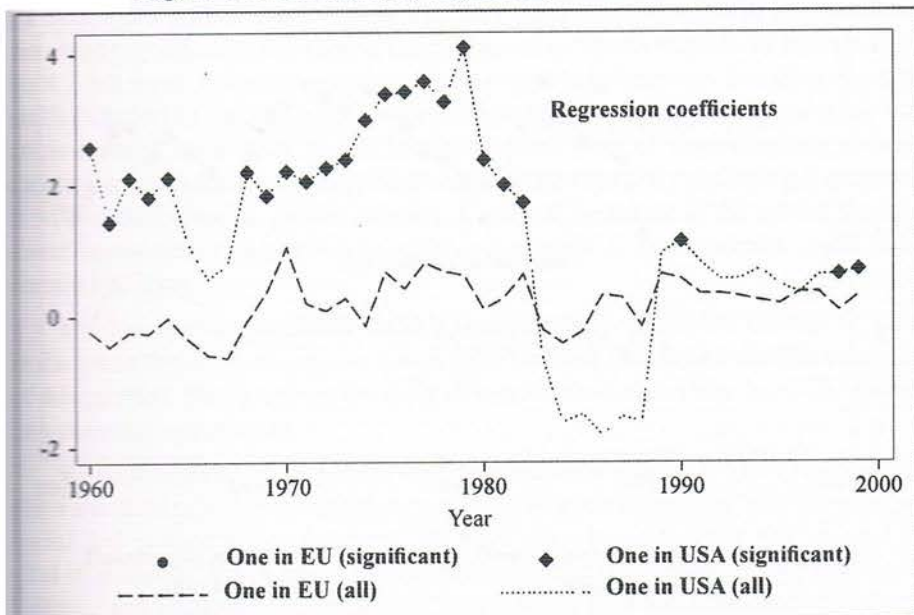


Figure 5. ASEAN gravity regression, trade with Thailand

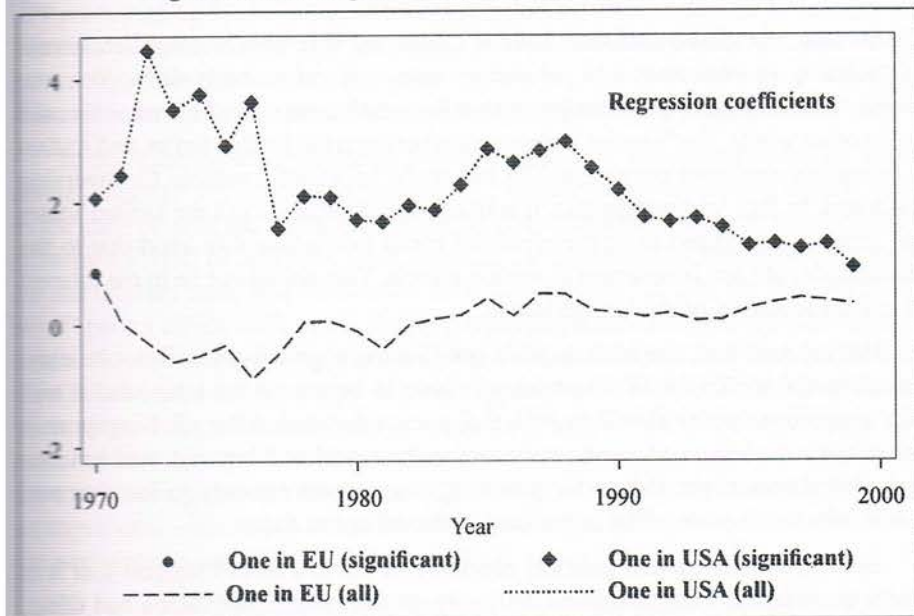
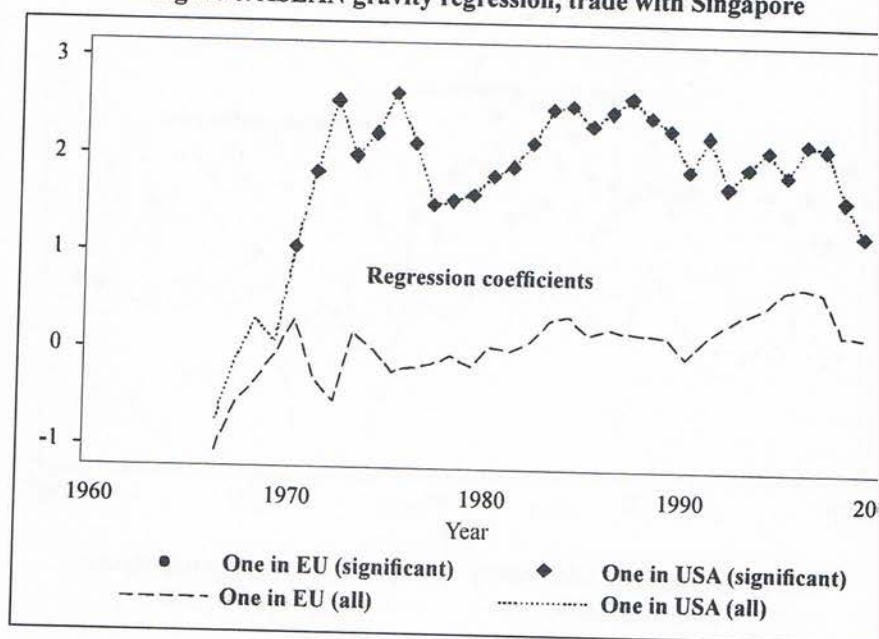


Figure 6. ASEAN gravity regression, trade with Singapore



5. The EAI in the emerging Asia-Pacific context

In sum, the above statistical review confirmed that the US-ASEAN economic relationship is important and, in some cases, critical to both sides. Yet, econometric estimates would suggest that the relationship is not all what it could be. In other words, the "special" relationship between the United States and ASEAN is ostensibly declining over time. The EAI could be a useful vehicle for reversing this trend. In fact, without the EAI, it is likely that the many FTAs the United States has recently negotiated or in the pipelines could exacerbate this trend due to associated trade and investment diversion effects. This would not be in the interest of either the ASEAN or the United States.

Having said that, we wish to point out that the negotiations will not be easy. Controversial topics for all countries will have to be put on the table, and it will take tremendous political will to push the process forward. After all, Singapore is one of the most advanced, open economies in the world and does not even have a significant agricultural sector; yet, the US-Singapore agreement was not easy to hammer out. It will take much more effort in the case of the other EAI FTAs.

But the economics and political economy of the EAI would suggest that it is worth the effort. Putting controversial issues on the table is not such a bad thing, after all. If the EAI forces the United States to open up its agricultural and textile and clothing markets, so much the better. The same is true of the Malaysian, Philippin

and, of course, Thai auto industry. Moreover, most ASEAN countries do not have a competition policy, yet it is clear that they need one; the EAI will help produce domestic regulation in this regard. IPR protection in ASEAN tends to be strong in the books, but weak in implementation. The EAI will help here, too. It will also assist modernization of the financial sectors of the region—an important point, as the crisis-induced reforms in ASEAN lost momentum with economic recovery—and create greater transparency in government procurement and corporate governance. It will no doubt lead to greater degrees of national treatment in the area of foreign direct investment (FDI), which is widely recognized as an important obstacle to certain FDI flows.

The “conflict management” field is based on the premise that conflict is good in the sense that it allows serious issues to be tackled. This is an excellent example of this process. We do not see the difficult negotiations ahead as a “con” but rather as a potential opportunity.

We have shown how important the United States is to ASEAN. The United States plays a critical role in the maintenance of regional security, helping to achieve rapid social and economic development. We have also shown that the APT process is vital in assessing Asia’s future. Frequent meetings at the highest official levels are building and creating better relations. This leads to trust and confidence building. However, we feel that these results are better achieved with active US participation. Also, there is a subtle perception that the United States is losing influence in Asia. For example, in many ways scholars in Asia are becoming active in the analysis of APT processes, and the United States is being left out. It is important for the United States to become more active through such means as the EAI and other initiatives. Integrating dialogue not only between officials but also between ASEAN and other Asian scholars and their American counterparts should be a priority.

In the East Asian integration process, ASEAN is the cornerstone; as noted above, “ASEAN+1”, rather than “ASEAN+3”, initiatives are emerging. Hence, even in the case of APT, the focus is bilateral; it is not surprising that the EAI would be bilateral as well. Economists often criticize the bilateral FTA movement not only for the implicit trade and investment diversion effects, but also for the “spaghetti bowl” policy effect, such as overlapping regulations and different types of rules of origin. But the reality is that it is extremely difficult to have a regionwide FTA with the United States. In pursuing a bilateral approach, the United States should keep track of the unique arrangements made in each agreement, in order that they can be consolidated in the later stage of regionwide trade arrangements. In this sense, the EAI is taking the correct approach, in that it recognizes the need for bilateral arrangements—the ASEAN countries are quite diverse, after all—while undertaking the negotiations under a regional framework.

In the past, Asians felt that the United States would oppose Asia-wide integration through the APT or its equivalent, for various reasons. First, the United States opposed the establishment of the East Asian Economic Grouping proposed

by Prime Minister Mahathir with considerable vigor, mainly because it seemed that the proposal was for an inward-looking trade bloc. Second, the United States opposed the establishment of the Asian Monetary Fund, suggesting unease with such a regional initiative. Nevertheless, we would argue that this is not the case and is based on a misconception of the APT process itself in the 21st century. As previously discussed, we believe that the United States should not oppose the APT process as long as there is no move toward a Fortress East Asia, and there is no indication that this is in the cards. In fact, we would suggest that the United States consider giving even more positive support for the APT, for example, by possibly participating at APT summits. All major countries, including China, Korea, Japan, and Australia, now do so.

It is also important for the United States to preserve the trans-Pacific trade liberalization movement that includes not only APT countries but also Taiwan, Hong Kong, Australia, and New Zealand—in short, APEC. For its part, APEC faces some serious challenges in restoring and maintaining itself as an effective organization. But APEC liberalization comes closest to the concept of open regionalism and the WTO approach to multilateral liberalization. Most empirical studies indicate that APEC liberalization provides more economic gains for the region as a whole than any configuration of an East Asian bloc. Here again, the role of the United States is crucial in truly strengthening the role of APEC.

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