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Is there an Asian Pacific Model of Regional Agreements?

Prof. Dr. Helen E.S. Nesadurai

Institute of Defence and Strategic Studies

Nanyang Technological University, Singapore

Introduction

Until 1989, the Asia-Pacific region lacked any formal or inter-governmental arrangement for regional economic cooperation. Thirteen years on, the situation has altered dramatically. Today, the Asia-Pacific is a region where a bewildering array of regional agreements is in place, with more anticipated over the next few years. These arrangements range from the ‘minilateral’ Asia Pacific Economic Cooperation (APEC) forum established in 1989 and the ASEAN Free Trade Area initiated in 1992. While the former at present includes 21 members from both sides of the Pacific Ocean, the latter is regarded as a sub-regional economic cooperation arrangement amongst the ten member states of the Association of Southeast Asian Nations (ASEAN). Until 2000, these two regional projects were the sole economic cooperation arrangements in the Asia-Pacific region. Since 2000, a number of new regional economic arrangements has emerged, among them the ASEAN-China free trade area (FTA) and a variety of bilateral FTAs. New proposals for more bilateral and plurilateral FTAs have been announced as well.

These trends raise a number of questions that this paper aims to address. First, how do we explain the proliferation and variety of regional agreements in this part of the world, particularly since most, if not all, regional governments have explicitly expressed their interest both in remaining engaged with the global economy and in the multilateral process centred on the World Trade Organisation (WTO)? Second, what kinds of substantive issues are addressed in these various arrangements? Third, do these various regional agreements share common modalities or procedural approaches to cooperation? Fourth, to what extent do these regional agreements compel regulatory changes in the domestic economy of their respective members? Through these questions, the paper explores the forms of regional economic governance in the Asia Pacific, and how regional governance might relate to national and global economic governance. Although the focus of the paper is on Asia Pacific regional agreements, the paper approaches these questions from the point of view of the Southeast Asian or ASEAN states given their centrality in virtually all the key regional agreements in the Asia-Pacific to date and in those planned for the future. Their governments have played a significant role in shaping the regional architecture of the Asia-Pacific, though they are, of course, not the only actors.

Following this brief introduction, Section 2 outlines the paper's central argument that it is the *interplay* between external pressures associated with economic globalisation and dynamics of the domestic political economy that is key in explaining the emergence and evolution of regional arrangements in the Asia-Pacific. Regional agreements, in short, cannot be understood in isolation from their domestic foundations. The next three sections apply this general argument to the specific cases of APEC, AFTA and the 'newer' regional arrangements. More specifically, the discussion in Sections 3 to 5 shows that economic concerns in many countries of the Asia Pacific with maintaining access to export markets and global capital prompted the turn to regionalism since 1989. Attention to domestic politics is, however, necessary to account for the institutional forms taken by these regional agreements. They reflect domestic pressures arising from the need to secure broad domestic social agendas as well as to protect the more particularistic interests of politically important domestic coalitions formed between political and business elites. The concluding section asks whether we may meaningfully speak of an 'Asian-Pacific model of regional agreements,' and their implications for global economic governance through the multilateral WTO process.

The Globalisation-Domestic Politics Nexus

Contemporary regionalism is generally conceived of as a response to economic globalisation (Gamble and Payne, 1996). The literature to date generally posits this relationship as one of two types. On the one hand, regional projects may emphasise accommodation or acquiescence to global market forces, in which regionalism is but a means to globalisation. This is said to be the most common form of regionalist project in the contemporary world economy (Mittelman, 2000: 126). On the other hand, the resistance approach to regionalism aims at insulation from the effects of global market forces in an attempt to preserve domestic social and economic arrangements that are, arguably, threatened by the forces of globalisation (Hveem, 2000). While offering useful insights, these models may be too stark in their interpretation of the globalisation-regionalism relationship.

A more nuanced approach to understanding this relationship is to focus on how regional projects address the issue of sovereignty, or more precisely, national policy autonomy in a context given by economic globalisation. This suggests three possible ways regionalism may be related to globalisation.[1] First, regionalism potentially offers national governments a means to *retain*, if only partially, control over policy choices in the face of pressures to adopt increasingly neoliberal policies. An extreme version of this argument would see regionalism aimed at resisting globalisation (Hveem, 2000). Second, regionalism is potentially a means through which governments *regain* some control over national policy choices. This formulation sees regionalism providing individual states a collective capacity over the forces of globalisation that they may not have had individually. Third, regionalism may well represent a *renunciation* of domestic policy autonomy, with governments fully committed to globalisation and to its associated policies of liberalisation, deregulation, and privatisation. In this liberal political economy interpretation of the globalisation-regionalism relationship, governments fully accept outcomes associated with market forces and subscribe to the ideal of market competition.

By emphasising concern with domestic policy autonomy as central to explaining regional forms, this approach at once directs attention to the domestic level. Which of these three approaches to regionalism is adopted depends not only on the specific kinds of pressures arising from economic globalisation but more importantly, on the nature of domestic politics, which will influence the degree of importance national governments place on maintaining control over domestic policy choices. Political/state elites who make policy decisions on external matters generally do so on the basis of domestically derived interests and priorities, which helps shape how they interpret external events, including globalisation, and their responses to these events and pressures. This is not the same as saying their choices are solely dictated by the demands of powerful domestic constituencies. Nevertheless, the degree of domestic support enjoyed by political elites and their domestic political legitimacy depends on how they meet the needs of a variety of domestic groups, including social and ethnic groups, business actors and citizens more broadly. In short, international forces only acquire 'political significance' through domestic politics (Jacobsen, 1996: 94).

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[1] See the REMARIN proposal submitted by the LSE to the European Union Sixth Framework

A general model of domestic politics would emphasise how political actors everywhere are usually confronted by the choice of adopting policies that maximise wealth in society as a whole or that benefit particularistic interests; in other words, between concern over growth or over domestic distributive priorities. To the extent that growth for policymakers is achieved through participation in global market activities and the adoption of neoliberal policies, then they would be willing to accede control over domestic policy to regional arrangements that are adopted as a means to engaging with globalisation. When domestic distributive imperatives operate, departures from this posture are likely. Distribution involves the conscious allocation by governments of income, rents and other economic benefits to particular individuals, groups or firms who would otherwise not have received these gains through the workings of the free market. In such instances, policymakers are likely to want to retain as much policy autonomy as is possible under conditions of globalisation, and their approach to regionalism will reflect that imperative. A closer examination of the Southeast Asian case shows more clearly the tensions between growth and domestic distribution that policymakers are confronted with and that is likely to shape their preferences towards both globalisation and regionalism.

The Southeast Asian political setting

The political elite in Southeast Asia where elite governance political systems operate[2] generally needs to respond to two sets of pressures arising from domestic society in order to maintain elite rule and its legitimacy, which remains fragile to date. On the one hand, political elites need the support of citizens to maintain their right to rule and

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Programme.

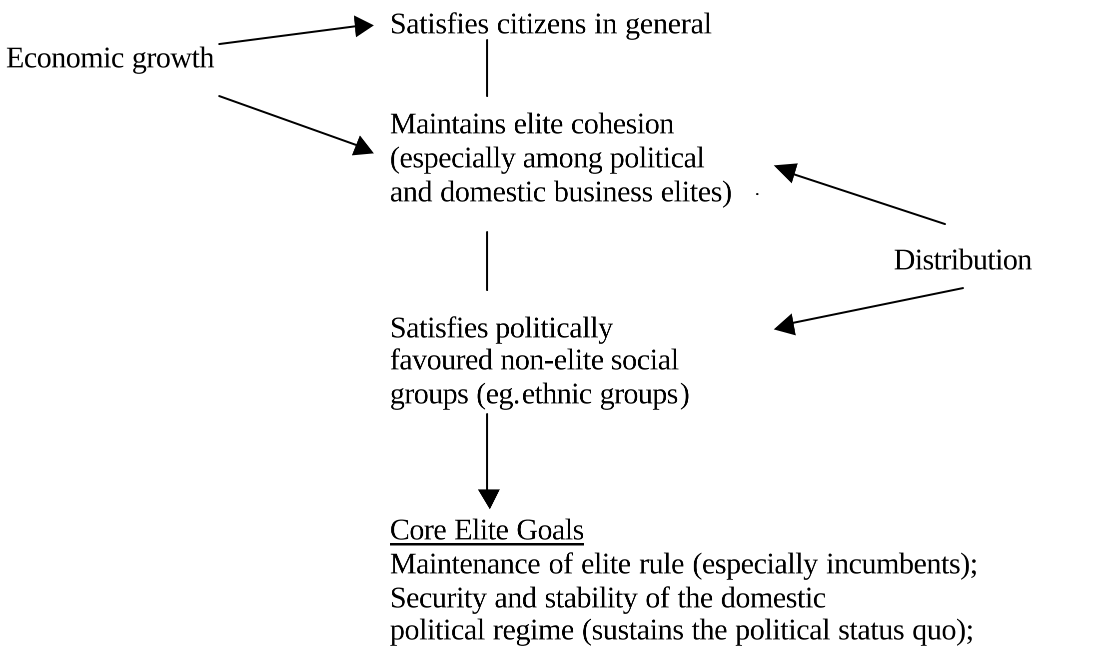
to ensure political order, and this is largely achieved through creating material wealth for citizens – the notion of performance legitimacy, which remains salient in Southeast Asia (Alagappa 1995: 330; Stubbs 2001). This explains the preoccupation of political leaders with securing and maintaining key sources of growth in the economy, of which FDI is pre-eminent, while access to export markets is equally vital given the export-centred growth policies of these governments.

On the other hand, elite rule is also sustained by unity and accommodation between members of the elite/governing coalition (Haggard and Kaufman 1997). In a number of Southeast Asian countries, political elites often selectively distribute economic benefits to their elite partners as a primary means to achieve elite unity, and through that to sustain elite rule. By the 1990s, it was the accommodation between the political elite and an emerging domestic business class that was crucial. The material and other forms of political support provided by domestic businesses help incumbent political elites maintain their power base, while the former in turn receive economic privileges through preferential policies instituted by the latter. In addition, domestic businesses are often privileged because they help political actors fulfil broader social equity goals in society.[3] There is also a wider distributive agenda in parts of Southeast Asia that may lead policymakers to privilege non-elite or broad social groups in policy choices, ethnic groups for instance in Malaysia, provided these represent key constituencies for ruling elites and are regarded as vital to sustaining elite rule and regime stability (Figure 1).

[2] See McCargo (1998).
[3] In Malaysia and Indonesia for instance, political legitimacy also rests on the capacity of the state to develop respectively an ethnic Malay and indigenous Indonesian domestic capital class, particularly to offset the dominance of ethnic Chinese capital.

The importance of the distributive agenda in maintaining elite unity does not imply that economic growth is unimportant. Politically important domestic distributional coalitions are, in fact, sustained by a set of bargains between political and business elites that ultimately depend on economic growth generated through export industries (Jayasuriya 2000: 34). During much of the 1990s, the competitive export-oriented sectors in Southeast Asia, often driven by FDI, helped to maintain the viability of sectors, usually in the service-related or non-tradeable sectors, in which politically connected domestic business actors were dominant. The precise nature of these domestic distributional coalitions and their economic efficiency in the areas they operate differ across the ASEAN countries. The crucial point, however, is that political elites often have to engage in difficult balancing acts in their policy choices, particularly when these involve significant trade-offs between the growth and distributive imperatives, or between maximising wealth and efficiency in society as a whole and maximising the wealth of a segment of society.

Figure 1: Growth and distribution in Southeast Asian political economies



Source: Nesadurai (2003)

This basic model of domestic-level dynamics not only characterises domestic politics in Southeast Asia, it is equally salient to other regional states such as Japan and South Korea, for instance, which have been described as incorporating a distributive or clientalist element within their broadly developmental political orientations (Jayasuriya, 2000: 32). In these settings, as in Southeast Asia, the 'selective allocation of distributive benefits by public sector elites in exchange for promise of solidarity' from private actors have helped sustain competitive export industries that were the mainstay of the Japanese and South Korean economic miracles (Moore, 1987; Woodall, 1996: 9-10).

The rest of the paper use the general argument developed in this section to help explain the emergence and evolution of regional arrangements in the Asia-Pacific region. In summary, the paper argues that economic concerns in many countries of the

Asia Pacific, particularly in Southeast Asia with maintaining access to export markets and global capital prompted the turn to regionalism since 1989. The precise form taken by these regional arrangements in terms of their substantive content/agenda and particularly their modality of cooperation reflects domestic pressures arising from the need for political elites to secure broad domestic social agendas as well as to protect the more particularistic interests of politically important domestic coalitions formed between political and business elites.

The Asia-Pacific Economic Cooperation (APEC) Forum

Currently grouping 21 members, APEC was formed in 1989 as a ministerial-level meeting of 12 member countries, an initiative of the Australian and Japanese governments although officially, APEC is regarded as an Australian proposal (Ravenhill, 2001: 82).[4] Not only does this regional grouping include the three largest economies in the world – the US, Japan and China – it also includes both advanced and developing countries. In addition, there is considerable diversity amongst the 21 members of APEC both in terms of politics and in systems of national economic governance. The latter especially has had a significant influence on the institutional evolution of APEC.

Driving forces behind the formation of APEC

The decision to establish APEC as a formal or inter-governmental cooperative arrangement in 1989 came as something of a surprise, given the long and unsuccessful

[4] The founding members of APEC in 1989 were the then six member states of ASEAN (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand), Australia, Canada, Japan, New Zealand, South Korea and the United States. In 1991, the 'three Chinas' were admitted to the grouping – the Peoples' Republic of China, Hong Kong and Taiwan. Papua New Guinea became a member in 1993,

struggle by trade economists and business actors to push regional governments to create such an arrangement over the previous two decades. The decision to establish APEC was precipitated by growing worry among regional governments from Japan to Australia and in Southeast Asia that the world economy was headed into protectionism through its fragmentation into rival blocs.

These governments viewed with alarm the growing willingness by Washington to enter into regional trade agreements since the mid-1980s, first with Canada (the US-Canada FTA), then Mexico (NAFTA) and later with Latin America (Free Trade Area of the Americas, FTAA). They were not comforted by official US pronouncements that the US was actually attempting to strengthen the multilateral trading system through pursuing trade liberalisation on multiple fronts – multilateral, bilateral and minilateral arrangements. The Southeast Asian governments were also worried by the increasing unilateralism in US trade policy. Washington had turned to using domestic trade bills to pry open markets in Northeast Asia, principally Japan and South Korea, and to reform what the US perceived to be 'unfair' trading practices that gave Northeast Asian exporters an edge in the American and world market during the 1980s. The Southeast Asian governments feared that US unilateralism would hinder Southeast Asian access to the important US market. Moreover, the European Community's decision to form a Single European Market coupled with the slow progress of the Uruguay Round negotiations of the GATT, particularly the 1988 failure in Montreal of the Round's mid-term review, led to a sense of crisis in both Southeast and Northeast Asia. These developments were considered especially threatening to the future growth prospects of the Southeast Asian countries, Japan and

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Chile in 1994 and Peru, Russia and Vietnam formally joined APEC in 1998. Since then, a moratorium

South Korea given their overwhelming reliance in the late 1980s on the US market. For the Southeast Asian states in particular, economic reform programmes adopted since the mid-1980s recession were centred on export-oriented industrialisation, which made access to export markets a vital imperative.

Consequently, Australian Prime Minister Bob Hawke's proposal for an Asia Pacific ministerial conference found a receptive audience in the region.[5] Although Hawke outlined APEC's initial objective as helping to generate a successful conclusion to the Uruguay Round negotiations, the organisation's more fundamental goal was to embed the US within a regional arrangement as a means to ensuring its market remained open to regional exports and to try and constrain US unilateralism in trade policy (Ravenhill, 2001: 83). Despite initial reservations about the domestic implications of APEC from the Southeast Asian side, particularly Malaysia, these governments came on board the project in view of shared interests in a successful Uruguay Round and as a means of ensuring access to the crucial US market as well as maintain US engagement in the region after the Cold War.

While these external pressures, some of them more perceived than real, were responsible for the initial decision to form APEC in 1989, they cannot fully account for the manner in which APEC evolved in the years since its inception. It is here that we see the influence of the domestic political economy in shaping the procedural modalities of the organisation and the substantive content of its economic cooperation programme.

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has been placed on APEC membership.

Modalities of cooperation: 'open regionalism' and the salience of domestic politics

APEC is defined by 'open regionalism', a procedural approach to trade liberalisation that is based on unilateral liberalisation offers by APEC members, which may be extended to non-APEC members on a most-favoured-nation (MFN) basis without the need for reciprocity from the other party.[6] Reciprocity is also not required for APEC members making trade liberalisation offers. The economic rationale put forward by its proponents for adopting this modality of cooperation was that it would generate freer global trade by minimising trade diversion and generating incentives for liberalising trade in other regions outside APEC, ultimately leading to lower trade barriers across the international economic system. In this, APEC is distinct from other regional trading arrangements such as the EU, NAFTA, and even the Southeast Asian states' own regional scheme, AFTA. APEC has also rejected legally binding trade agreements, opting for a voluntary process of liberalisation, which allows each member government substantial discretion in determining the substantive concessions it is willing to make and its schedule of liberalisation, particularly since reciprocity is eschewed. The adoption of the principle of open regionalism in APEC reflected the preferences of its Asian members, especially the Southeast Asian states (Plummer, 1998: 309).

In addition to shaping its modus operandi, the Southeast Asian states also attempted to control the APEC agenda. In 1991, they had successfully pushed for the adoption of a

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[5] Ravenhill (2001) provides an insightful and theoretically informed analysis of the formation and evolution of APEC.

[6] This is the original definition of open regionalism, articulated most clearly by Drysdale and Garnaut (1993: 187-88). The term is now used in a more general sense to characterise regionalist schemes that are fundamentally about engaging with globalisation and the global market, usually specified to mean projects where the exchange of preferences among regional partners is not accompanied by the imposition of new barriers to non-partners (Gamble and Payne 1996: 251). For this paper, the term is employed in its original sense meaning unilateralism and non-reciprocity in trade liberalisation.

statement that APEC should be a purely consultative forum. By 1994, however, APEC had adopted the goal of regional trade and investment liberalisation, much to the disquiet of a number of its members, notably Malaysia. Nevertheless, the ambiguity engendered by the open regionalist mode of cooperation in APEC allowed its members considerable discretion in the specific tariff concessions they would offer and in their liberalisation schedules (Plummer, 1998: 308). Open regionalism effectively institutionalises complete domestic latitude in regional liberalisation. This mode of cooperation has, therefore, helped to sustain prevailing domestic distributional coalitions by allowing national governments almost full flexibility in deciding which sectors would be subject to trade liberalisation (Jayasuriya, 2000: 39). In fact, it was because of these domestic political imperatives that the Asian members of APEC pushed the notion of open regionalism as the preferred modality of regional cooperation in APEC. Thus, even the adoption of a more substantive programme for regional trade and investment liberalisation in 1994 did not lead to a shift in the modality of cooperation in APEC.

To Beeson and Jayasuriya (1998: 323-31), APEC represents a site of contestation between two approaches to regional economic governance that have their roots in distinct national approaches to economic management endorsed by 'western' and 'Asian' governments.[7] The former approach to economic governance, idealised in the Anglo-American capitalist model of the minimalist state, the self-regulating market and (seemingly) arms-length relationships between state and business and amongst businesses, is rather at odds with the interventionist approach to economic governance found in the Southeast and Northeast Asian states and in their close state-business links. The latter group of governments has pushed for open regionalism precisely because it is this particular mode of cooperation that is most likely to allow the continuation of preferred interventionist approaches to economic governance that in turn help to sustain politically vital domestic distributional coalitions. The US, on the other hand, has long preferred a rules-based approach to APEC liberalisation that would impose increasingly binding commitments on members on a reciprocal basis, which was seen as a way to structure national economic systems in Southeast and Northeast Asia in line with a neoliberal economic order. Open regionalism, however, prevailed as the latter group of countries have refused to compromise on this point. Nevertheless, the practice of open regionalism has helped to accommodate both sets of interests in APEC, principally due to the ambiguity it introduces into the game of regional liberalisation.

The financial crisis in East Asia and the economic reforms adopted in response to crisis have not fundamentally transformed Asian economic systems nor weakened previously dominant domestic coalitions. Despite specific areas of economic reform, particularly in the financial sector, pre-crisis business and political interests have managed to regroup in the aftermath of the crisis around new institutional forms associated with freer and more deregulated markets (Robison *et al*, 2002). Hence, its members have not sought a change to the modality of cooperation in APEC, although a growing degree of bargaining and negotiations over members' respective liberalisation concessions has become the norm, driven largely by the US (Ravenhill, 2001: 189).

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[7] This is not to deny the diversity of national systems of political economy among APEC's Asian or

Those member states that have endorsed open regionalism have clearly sought to introduce a degree of ambiguity into the functioning of APEC, which allows them substantial latitude in addressing domestic imperatives. The declining salience throughout the 1990s of the external threats that initially prompted the decision to form APEC has made it possible for its members to live with the ambiguity that is now in-built into the grouping. It has, however, made APEC an ineffective mechanism for trade liberalisation compared with the WTO or even with other arrangements such as AFTA. While the WTO combines flexibility with rigidity, the APEC modus operandi 'is all flexibility and no rigidity', which many scholars argue has reduced its capacity to offer a predictable environment and an effective mechanism for regional trade liberalisation (Ravenhill, 2001: 165).

The substantive content of APEC

When APEC was first formed, it was meant to be a purely consultative forum on key economic issues of the day and as a confidence-building mechanism among highly diverse states with long-standing historical animosities amongst some of them. In 1993, trade and investment liberalisation became the central item on the APEC agenda, with APEC itself given a boost by the first APEC Leaders' Summit hosted by President Bill Clinton. Although the liberalisation agenda proposed by the Eminent Persons Group (EPG, 1994: 5)[8] was supported by APEC's 'western' governments – the US, Canada, Australia, and New Zealand – and by trade economists and globally oriented businesses, the Asian governments were rather hesitant, preferring to

western members. Nevertheless, there are key features that distinguish 'Asian' from 'western' approaches to economic governance. See Stubbs (1998).

[8] The EPG was a group largely made up of academic economists and political scientists from the member countries of APEC, many of them heads of think-tanks and research institutes. They had been appointed by the APEC member governments in 1993 to develop a plan of action for APEC. The EPG

emphasise trade facilitation and economic/technical cooperation instead. They were not in favour of trade liberalisation forming the central agenda item in APEC from fear that the regional organisation would become another instrument through which the US would attempt to open their markets before they were ready to do so. Instead of rejecting the trade liberalisation agenda outright, which could have jeopardised continued US participation in APEC, these governments sought a compromise by stressing adherence to APEC's modus operandi – open regionalism.

Trade liberalisation

Trade liberalisation was mainly focused on the reduction of tariff barriers, which was to be undertaken in accordance with the principle of open regionalism whereby APEC members would unilaterally determine through Individual Action Plans (IAP) their own timetable for liberalisation and the specific sectors/products in which tariff concessions would be offered. They would, however aim to reach the APEC goal of free trade by 2010 for advanced country members and by 2020 for its developing country members. In short, negotiation and bargaining amongst members over their tariff offers was eschewed in favour of what came to be termed 'concerted unilateralism'. Open regionalism was, in fact, a means of ensuring that governments did not face pressure from their APEC counterparts to liberalise politically sensitive domestic sectors. Thus, it was not surprising that the IAPs not only lacked transparency and specificity, they were also inadequate in substantive terms, failing to go beyond members' offers in the Uruguay Round (Yamazawa and Urata, 1999). Domestic political sensitivities over the impact of regional liberalisation clearly

submitted three reports to the APEC Ministerial Meeting in 1993, 1994 and 1995, after which the group was dissolved.

prevented most of APEC's Asian members from making credible offers that went beyond their GATT/WTO commitments.

Similarly, a subsequent plan adopted in 1997 for 'early voluntary sector liberalisation' (EVSL) of 15 selected sectors was jeopardised by Japan's refusal to participate in two of the sectors APEC members had endorsed – fish and fish products, and forestry products – due to domestic political pressure. South Korea, with similar domestic political sensitivities centred on the agriculture sector adopted a similar position as the Japanese, as did China and Taiwan (Ravenhill, 2001: 184). In the end, Indonesia, Malaysia and Thailand too failed to support the EVSL package at the Kuala Lumpur Ministerial in 1998. APEC members then submitted the EVSL package to the WTO. APEC's modus operandi, while ill suited to deal with such problems, may itself have contributed to the EVSL debacle (Ravenhill, 2001: 185).[9] Clearly, there were governments that were prepared to sacrifice APEC at the altar of the domestic political economy, particularly as APEC's procedural form, which they had helped design, ensured they maintained considerable discretion over their regional obligations.

Investment

In addition to trade liberalisation, investment liberalisation was also placed on the APEC agenda in 1993 through a proposal to adopt an APEC Investment Code. Among the key principles to be incorporated within the Code were transparency, non-discrimination, and crucially, national treatment and the right of establishment (or market access). This move potentially placed APEC in line with the OECD, which was negotiating the Multilateral Agreement on Investment, and ahead of the WTO, which has yet to incorporate investment within the WTO framework.

Most of the Asian member governments insisted, however, that the set of principles was non-binding on members. The original investment code was thus altered to a set of Non-Binding Investment Principles (NBIP). These governments also watered down the final set of principles so substantially that fully half of the principles failed to reach best international practice according to assessments conducted by the Eminent Persons Group. The principles deemed inadequate were those relating to national treatment, market access, performance requirements, investment incentives, transfer of funds and capital movements (Urata, 1998: 108). These governments also introduced loopholes into the NBIP, particularly to the national treatment principle, by allowing for exceptions provided for in domestic laws, regulations and policies (APEC, 1994). From starting out as a Code that would go beyond existing multilateral initiatives on investment, the NBIP soon became, in the words of one private sector actor, 'mere principles, unsigned, unratified, unenforceable, unincorporated into national law, and lacking meaningful clauses on national treatment' (Messing, 1995: 59).

The Asian member governments, possibly with the exception of Singapore and Hong Kong, were clearly hesitant about adopting a strong set of investment principles, although non-binding, in an association that also included the advanced countries, particularly the US. They were concerned that they would be compelled by these governments to make those principles mandatory, which the Asian governments were

[9] The Japanese and South Korean governments had interpreted the principle of open regionalism to

not prepared to do in order to protect domestic interests. Although FDI was a crucial source of growth for the Southeast Asian economies especially and national FDI regimes had been liberalised substantially since the mid-1980s, investment restrictions were maintained in much of Southeast Asia with regard to market access (the right to establishment) and national treatment in certain sectors (Nesadurai, 2003). Investment policy was employed extensively to attain domestic social and political objectives more broadly, as well as in a more particularistic way to distribute economic gains to politically important businesses and individuals.

The future of APEC

Since the EVSL debacle in 1998, APEC has turned away from its ambitious goal of regional trade and investment liberalisation to focus on the other 'pillars' of APEC – trade facilitation and economic/technical cooperation (ECOTECH). Trade and investment liberalisation is clearly off the APEC agenda. Moreover, despite the 1999 adoption by APEC leaders of a set of competition principles, flexibility of implementation of these principles was once again emphasised by leaders, as was their non-binding nature (Ravenhill, 2001: 192). In short, APEC will have little impact on regulatory structures in member economies. It will also remain marginal as a vehicle for liberalisation, although its utility as a political and security forum and as a venue where heads of governments meet annually is in itself valuable, particularly in the present uncertain global and regional environment.

APEC stands in marked contrast to the ASEAN Free Trade Area (AFTA). Unlike their position in APEC, the Southeast Asian governments not only endorsed an

mean that they did not need to make tariff offers in all fifteen sectors identified for early liberalisation.

extensive agenda for AFTA they also adopted an approach to AFTA that was not in the style of 'open regionalism'. Instead, a typical trade negotiation approach was adopted that involved bargaining, negotiations and diffuse reciprocity; binding commitments that were ratified; increasing resort to rules-based institutionalisation; and firm timetables. The next section turns to a discussion of why the Southeast Asian governments privileged AFTA over APEC as a vehicle for trade liberalisation, while also inscribing a modality of cooperation in AFTA that was quite distinct from the approach they endorsed for APEC.

The ASEAN Free Trade Area (AFTA)[10]

The core members of ASEAN[11] adopted the decision to form AFTA in 1992. The project was originally designed to lower tariffs on manufactured goods and processed agricultural products to between 0-5 per cent by 2008 over a fifteen year period beginning in January 1993. Despite considerable setbacks to the project during its early years, these governments agreed in 1995 to accelerate the project's pace and substantially extend its agenda from what had been planned initially. The six original or core members[12] of ASEAN agreed to bring forward the date of AFTA's completion to 2003 when tariffs on all manufactured products and processed agricultural products are to be at the 0-5 per cent level. In addition, they also added new issue areas to the AFTA agenda, namely the liberalisation of trade in unprocessed agricultural products, services, and in investment flows, all potentially contentious issue areas that member

[10] The material presented in this section is drawn from Nesadurai (2003).
[11] ASEAN was formed in 1967 by Indonesia, Malaysia, the Philippines, Singapore, and Thailand. Brunei joined the grouping in 1984 on its independence from Britain. Vietnam joined in 1995, Laos and Myanmar in 1997, while Cambodia joined the Association in April 1999, bringing ASEAN's total membership to ten.
[12] The core or founding members of AFTA are Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand. New members of ASEAN acceded to AFTA on joining the Association.

governments had initially excluded from AFTA. Later in 1998-99, member governments agreed to bring forward to 2002, where it was possible, the deadline when tariffs would reach the 0-5 per cent target although the formal deadline remained 2003. They also decided at this time to reduce tariffs to zero percent for the six original signatories by 2010.

Thus, AFTA has now become a composite project of ASEAN economic regionalism comprising three component programmes. The Common Effective Preferential Tariff (CEPT) scheme governs liberalisation of goods trade, the ASEAN Framework Agreement on Services (AFAS) governs liberalisation of services trade, and the ASEAN Investment Area (AIA) scheme governs investment liberalisation. While the services agreement commits members to make offers that go beyond their WTO commitments, the investment agreement incorporates the principles of national treatment and market access to govern investment liberalisation. A wide range of commitments in these different component programmes was subsequently negotiated, timetables and rules governing liberalisation were firmed up, and additional programmes in trade facilitation[13] to support these primary liberalisation agreements were adopted. All agreements governing liberalisation programmes in AFTA are legally binding, requiring domestic ratification.

Although AFTA is often unfairly dismissed as a vehicle for regional liberalisation, it has, in fact, registered significant progress on the tariff front. Tariff reductions on manufactured goods are essentially on schedule, with almost 96 per cent of total tariffs already in the 0-5 per cent band in 2002. Average tariffs have fallen to 2.89 per

[13] The latter include customs initiatives, standards harmonisation and mutual recognition programmes.

cent in 2002, down from 12.8 per cent in 1993. Moreover, there is a significant difference of between 5-15 percentage points between average MFN tariff rates applicable to all parties and AFTA preferential tariff rates applicable to ASEAN members. This point challenges the oft-made charge against AFTA that it is a redundant exercise, merely replicating tariff reductions already offered unilaterally.

Other developments qualify this sense of progress in AFTA. Despite an otherwise excellent track record in lowering tariffs under AFTA, Malaysia chose to exclude automobiles from the AFTA schedule of tariff liberalisation for two years until 2005. Moreover, the deadline for trade liberalisation in key unprocessed agricultural products has been pushed back to 2010 from the original 2003 while a number of exceptions to the end tariff rate of 0-5 per cent were allowed for so-called 'highly sensitive' agricultural items, essentially rice. Negotiations in services liberalisation have been slow, especially in the financial services and telecommunications sectors. Although a substantial portion of non-tariff barriers that had been prevalent in ASEAN have been removed, notably customs surcharges and barriers arising from domestic monopoly arrangements in agriculture, new forms of NTBs are now prominent. Antidumping duties especially are on the increase. Apart from these, the other curious development in AFTA was the distinction initially made in the investment liberalisation programme between ASEAN and non-ASEAN or foreign investors. The ASEAN member governments pledged to remove all exemptions to national treatment and market access for ASEAN investors by 2003 in the manufacturing sector and 2010 in other sectors while offering these concessions to foreign (non-ASEAN) investors only in 2020 (ASEAN, 1998).

Three questions emerge from this survey of AFTA. First, how do we explain what were clearly very significant advances made in the regional project since its initial days, both in terms of commitments made and in implementing tariff liberalisation, particularly given quite the opposite sentiments of these same governments in APEC? Second, why despite considerable success in implementing tariff reduction in manufactures, were setbacks experienced in sectors like agriculture, automobiles and services? Third, why was a distinction between ASEAN and foreign investors made in the investment programme? As in the case of APEC, these puzzles are best explained in terms of the *interaction* between external pressures associated with globalisation *and* domestic political economic dynamics.

Globalisation and global capital: explaining the ambitious AFTA agenda

Officials preparing for the 1992 Singapore Summit at which the decision to establish AFTA was formally adopted admitted that one of the most compelling arguments advanced for AFTA, and which convinced the leaders of its necessity, was its purported capacity to attract FDI to the region (Akrasanee and Stifel, 1992: 36). Although a range of factors stimulated the ASEAN decision, including the need to keep ASEAN relevant as a regional organisation in a post-Cold War world and in the face of competition from APEC, these strategic motivations behind the decision to establish AFTA were initial goals that were soon overtaken by the FDI imperative. The idea mooted by Thai Prime Minister Anand Panyarachun in 1991 quickly found support in all the ASEAN capitals when it became apparent that economic growth in the ASEAN countries was under threat due to declining FDI inflows in the early 1990s. By this time, the ASEAN countries had grown highly dependent on FDI to fuel economic growth, which made these governments highly vulnerable to any slowdown in FDI.

The concerns over declining FDI inflows in the early 1990s do not, however, explain what prompted the *regional* response since ASEAN governments could well have adopted further unilateral reforms or used incentives at the national level to make individual economies more attractive to FDI without engaging in regionalism. It was, in fact, the awareness, or at least perceptions on the part of ASEAN leaders and policymakers that FDI was attracted to large and/or regional markets – NAFTA, the Single European Market (SEM) and especially China – that demonstrated to ASEAN leaders the potential utility of a similar project in ASEAN. It was, in short, the contagion effect at work.

By 1993, China had become far more threatening as a competing investment location to ASEAN despite initial fears centred on NAFTA and the SEM. The call in January 1992 by Chinese leader Deng Xiaoping for faster and deeper economic reforms in China sparked off an investment boom in that country. The sharp rise in FDI flows to China since then was seen as being increasingly at the expense of the ASEAN countries (Table 1). Since 1992, the surge of FDI from the Asian newly industrialising economies (NIEs) to ASEAN moderated, with an increasing proportion of Japanese, Taiwanese and Hong Kong investment flowing to China instead (Parker, 1993: 61). Investments from OECD sources, including North American and European sources to ASEAN similarly weakened (Thomsen, 1999: 16). Thus, by the end of 1992, the FDI situation in the core ASEAN countries had become extremely worrying to policymakers and political leaders.

Table 1: Flows of FDI to host region/economy, 1983-1998 (US$ million)

Host region or economy	Total Flows	Developed countries	All Developing countries	ASEAN countries [a]	China
1983-88	91,554	71,779	19,757	3,708 (5.2%)	1,823 (2.5%)
1988	159,101	131,313	27,772	6,991 (25.2%)	3,194 (11.5%)
1989	200,612	171,722	28,622	7,591(26.5%)	3,393 (11.9%)
1990	211,425	176,436	34,689	12,158 (35.0%)	3,487 (10.1%)
1991	158,936	114,792	41,696	13,400 (32.1%)	4,366 (10.5%)
1992	173,761	119,692	49,625	12,074 (24.3%)	11,156 (22.5%)
1993	219,421	133,850	78,813	15, 994 (20.3%)	27,515 (34.9%)
1994	253,506	146,379	101,196	19,681 (19.4%)	33,787 (33.4%)
1995	328,862	208,372	106,224	21,643 (20.4%)	35,849 (33.7%)
1996	358,869	211,120	135,343	25,980 (19.2%)	40,180 (29.7%)
1997	464,341	273,276	172,533	27,813 (16.1%)	44,236 (25.6%)
1998	643,879	460,431	165,936	21,400 (12.9%)	45,460 (27.4%)

[a] Includes all ten ASEAN member economies
Figures in parentheses refer to investment flows as a proportion of total flows to developing countries

Sources: UNCTAD, World Investment Report, 1999
ASEAN Investment Database as reported in ASEAN Secretariat (1999:131-32).

The ASEAN member governments believed that the large market potential of AFTA would act as a carrot to attract FDI flows to the region, given the keen interest shown by investors flocking to large markets elsewhere, or at least expressing an interest in doing so. In this, the ASEAN governments were aided by the changing 'regional' logic of global capital. By the early 1990s, foreign investors had begun to show increasing interest in regional divisions of labour (Oman, 1994; Dicken, 1998). Under globalisation, capital was paradoxically not aiming for a global division of labour but was instead expanding in the global market through distinct regional strategies (Mittelman, 2000). While the aim of transnational corporations was to operate business globally, that goal was being increasingly achieved through the development of 'complete and integrated production and management systems within definable regions' (Rodan, 1993: 234). China by itself offered investors a potentially competing 'regional' investment site in the Asia-Pacific region, particularly in view of its (potential) market size (Baldwin, 1997: 3). What the ASEAN governments attempted to offer to foreign investors through AFTA, specifically through its CEPT tariff liberalisation component programme, was an alternate single regional space of investment and production, in effect exploiting the 'regional' logic of global capital.

Their interest in attracting FDI to the region more broadly and to counter its perceived diversion to China partly explains the initial decision by the ASEAN governments to establish AFTA. As already noted, other strategic goals were also influential. The FDI imperative has, since then, became paramount, however, and explains why the project was sustained, its pace accelerated and its agenda expanded despite growing domestic business opposition to it. Political leaders found the potential threat to economic growth from slowing FDI inflows sufficiently overwhelming to decide in 1995 to accelerate the completion of AFTA, introduce new rules to govern tariff reductions through annual packages, as well as to adopt programmes in trade facilitation. They also placed agriculture, services and investment on the AFTA agenda in 1995 to keep AFTA relevant to foreign investors, especially since the GATT, NAFTA and even APEC had addressed, or were planning to address these concerns (Hay, 1996: 266-68).

The further acceleration of AFTA during 1998-99 and the decision to aim for a zero tariff AFTA by 2010 were also aimed at convincing foreign investors that despite the turmoil of the Asian financial crisis, AFTA remained on track (Bowles, 2000: 444). The core ASEAN governments had to make sure that their respective economies remained attractive to FDI amidst the economic turmoil of the regional financial crisis, and they attempted to partly accomplish this through regionalism. As huge amounts of portfolio capital began flowing out of these economies, the imperative of maintaining direct investment became paramount, especially since domestic investments had also suffered a sharp contraction in the region (OECD, 1999: 120). AFTA became one tool in the process of maintaining foreign investor interest in the region, particularly as China still loomed as an alternative investment site. Although tariff barriers were employed to shield domestic industries during the financial crisis, many of these import restrictions were temporary, for a one to two year period, and were generally part of a set of short-term fiscal measures designed to reduce immediate pressure on countries' external accounts through restricting big-ticket and luxury items (Shimizu, 2000: 83).

While the global capital/FDI explanation provides a plausible account for the driving forces behind AFTA, it remains a partial explanation. As in the case of APEC, the domestic level offers additional insights. Most importantly, it explains the modality of cooperation adopted in AFTA, which may be characterised as 'negotiated flexibility'. Negotiated flexibility combines rigidity of project targets and schedules with a degree of flexibility that allows member governments to address domestic political economic imperatives. Although flexibility is a key feature of the modus operandi of AFTA, this is not the same as 'open regionalism' that effectively institutionalised complete domestic autonomy in APEC.

Negotiated flexibility and domestic political economic considerations

There were two approaches to negotiated flexibility in AFTA. The first saw flexibility institutionalised at the outset, or very early on in the project, as an approach to implementing AFTA commitments. The second saw flexibility as the outcome of a political bargaining process that was set in motion when implementation problems arose. This process led to both a downward re-negotiation of original commitments and institutional strengthening involving additional procedures and rules to govern the revised programme. Both approaches to negotiated flexibility were important as they enabled member governments to reconcile their FDI concerns with their domestic distributive priorities. Although those parties for whom the original commitments had been superior in effect lost out in the short run as a result of the downward revisions to AFTA targets, they were prepared to compromise in order to preserve the regional arrangement.

Flexible implementation procedures

To ensure flexibility for member governments in implementing their AFTA commitments, particularly in the CEPT tariff liberalisation programme, three key mechanisms were adopted: the normal and fast track schedules, the temporary exclusion list and the specialised programme on industrial cooperation termed the ASEAN Industrial Cooperation Scheme (AICO).

The normal and fast track programmes offered governments a choice of the speed at which tariffs on different categories of products would be liberalised. The temporary exclusion list allowed further flexibility in that governments could opt to exclude certain products from the AFTA/CEPT tariff liberalisation schedules for a limited period of time. Although initially there had been no rules to govern the treatment of temporary exclusions, by 1995, new procedures had been instituted that stipulated a firm schedule for subjecting excluded items to AFTA disciplines and the deadline for complete elimination of the exclusion list. Finally, the AICO programme effectively fast-tracked tariff liberalisation under the CEPT by allowing firms to enjoy the full benefits of a regional free trade area for particular approved products well before the

2003 deadline. Tariffs on these products, largely in the automotive sector, were immediately set at 0-5 per cent.

Problematic implementation and re-negotiating commitments

The second approach to flexibility was in effect triggered by implementation problems, and it was most evident in the case of agriculture and automobiles. Problems over implementation in these two sectors had emerged as Indonesia and Malaysia respectively refused to comply with their original commitments. Inter-governmental bargaining was set in motion as a result of these disputes, which although protracted, eventually allowed the problem to be addressed.

As a compromise, the ASEAN members allowed downward revisions to the original commitments in these two areas from those previously agreed. This was absolutely necessary, as otherwise Indonesia and Malaysia had threatened to withdraw from AFTA. For Indonesia, adhering to its AFTA commitments in agriculture would have hurt domestic coalitional arrangements, particularly the domestic monopoly arrangements of politically well-connected individuals and firms prevalent in sectors like sugar, wheat flour milling and cloves. For Malaysia, implementing its AFTA obligations in automobiles would have jeopardised the country's national car project, and thus, the political and economic objectives the project was designed to meet. Aside from helping to stimulate and nurture an indigenous capability in technological development, engineering design and industrial production, the national car project, the favoured project of the Malaysian Prime Minister, was also aimed at meeting ethnic development goals in Malaysia. The project formed the nucleus for nurturing an ethnic Malay business class in the automotive components industry through guaranteed purchase by the national car firm.

To offset the fallout from re-negotiating the original commitments, the ASEAN governments adopted new rules and procedures to govern implementation of the revised targets. This was important not only to convince other governments in the project to continue cooperation they were also useful as signalling devices aimed at convincing investors that the regional project remained viable despite the re-negotiation of commitments. In the two cases outlined above, these rules took the form of two protocols. The *Protocol on Sensitive and Highly Sensitive Agricultural Products* (ASEAN 1999) adopted in September 1999 focused both on procedural matters as well as outlined revised policy targets for agricultural trade liberalisation. It provided clarification on how exemptions from agricultural trade liberalisation were to be treated, while also setting new deadlines and tariff targets, including when exemptions were to end. Likewise, members adopted a *Protocol Regarding the Implementation of the CEPT Scheme Temporary Exclusion List* (ASEAN 2000) in November 2000 to govern the temporary withdrawal of concessions in AFTA. This protocol, based on Article XXVIII (Modification of Schedule) of the GATT 1994, also provides for compensatory adjustment from the offending party to other members on a most-favoured nation (MFN) basis.

The ‘negotiated flexibility’ approach to AFTA clearly prevented the need by member governments to alter domestic arrangements in the two sectors concerned. Instead, it allowed these governments the leeway to maintain them for a longer period than would have been the case if the original commitments had been implemented.

Whether the governments concerned would have respected their revised commitments is difficult to assess. In any case, this point is moot in the Indonesian case since IMF restructuring programmes adopted during the financial crisis have dismantled virtually all the monopoly arrangements in agriculture (with the exception of rice), facilitating Indonesian compliance with its AFTA commitments in this sector. It is also apparent that the Malaysian government is preparing for eventual regional liberalisation of the automobile industry despite delaying its AFTA commitments in this sector. Additional steps are being taken to improve the efficiency of the national car firms through global sourcing of component parts, departing from the previous policy of obtaining high-cost supplies from domestic vendors. Moreover, the decision to sell an equity stake in the company to foreign automobile firms, a departure from the Prime Minister's previous position, was adopted in recognition that foreign engineering expertise and technology was invaluable for the viability of the national car project.

Services, investment and the domestic political economy

The crucial importance of domestic priorities is also seen in the slow progress in the services negotiations. The ASEAN governments found it especially difficult to advance their negotiations to obtain specific commitments to liberalise trade in the financial and telecommunications sectors. Malaysia was especially unwilling to consider liberalising foreign equity and market access conditions for financial services, which Singapore and Thailand favoured. This is unsurprising since domestic banks were key players in the Malaysian political economy and liberalisation would have reduced the space for patronage-based manoeuvring to take place (Gomez and

Jomo, 1997). As in the case of automobiles, steps are, however, being taken to prepare the Malaysian financial sector for eventual liberalisation.[14]

The ambitious attempt at targeting all four modes of service supply, namely cross-border supply (Mode 1), consumption abroad (Mode 2), commercial presence (Mode 3), and the presence of natural persons (Mode 4) in services negotiations has contributed to the slow progress. Initial commitments were forthcoming only in Modes 1 and 2. Negotiations to obtain offers for Modes 3 and 4 were protracted, as it was very difficult to get agreement on commitments that would allow non-national service firms to establish a market presence in the domestic economy, particularly in very sensitive sectors like financial services and telecommunications. To help the process along, the ASEAN economic ministers adopted in September 2002 the 'ASEAN minus X' formula under which concessions may be exchanged among a subset of members within ASEAN, rather than requiring a consensus of all ten members.

The importance of domestic priorities is also evident in the way investment liberalisation was designed. While many of the ASEAN countries were highly dependent on FDI, and thus keenly interested in ensuring continued access to global capital, a few governments were also troubled by the impact of global competition on the future of domestic-owned capital. More specifically, they were worried by the prospect that new multilateral rules on investment that emphasised national treatment and market access for all investors would soon become incorporated in the WTO,

[14] Consolidation of the domestic financial sector through merger of 54 local banks and finance companies to 10 banking groups, with further mergers in the pipeline, is part of the government's strategy to improve the capacity of the financial sector to survive liberalisation.

which would effectively allow TNCs maximum freedom of operation worldwide. This, they feared, would especially jeopardise emerging domestic-owned capital.

Although domestic capital was important in all the core ASEAN countries, it was especially important in Malaysia and Indonesia, often enjoying close political relationships with incumbent political elites and thereby helping to sustain elite coalitions and the stability of the prevailing regime. Domestic-owned firms were also important in fulfilling wider socio-economic and ultimately political goals in these two countries. Malaysia, therefore, spearheaded the idea of using regionalism as a developmental tool to secure the future of domestic firms amidst impending global market competition, to which idea Indonesia gave its support. The idea of developmental regionalism was especially salient in sectors outside manufacturing, particularly in the category termed 'services incidental to manufacturing'.

Thus, the ASEAN member countries endorsed the privileging of ASEAN investors over foreign investors in the investment programme, intending the investment preferences to stimulate the growth through regional expansion of domestic firms into larger enterprises able to compete with TNCs, including through forming ASEAN multinationals. All the core ASEAN governments were broadly united on the importance of domestic firms becoming large and/or multinational as a means for them to survive global market competition. While the idea of developmental regionalism is theoretically plausible, underpinned by insights from strategic trade theory, whether the idea was a workable one in practice is a separate issue and beyond the focus of this paper.[15]

The point to note is that proponents of developmental regionalism did not fully accept the hegemonic position of foreign/global firms associated with globalisation, and attempted to nurture domestic firms in an environment that was considered to be harshly competitive to developing country capital. The growth imperative was infused with a need to accommodate to domestic distributive priorities centred on elements of domestic capital that were considered to be important to the political elite. Despite these concerns over domestic capital, the growth and FDI imperative became overwhelming by the middle of 2001 in the face of an expected slowdown in the global economy and the decline in FDI flows to regional economies. Member governments, consequently, gave up their attempt at developmental regionalism and extended the offer of national treatment and market access privileges in non-manufacturing sectors to foreign investors at the same time as ASEAN investors, by 2010. Although the differential treatment of FDI was not the main reason for the slowdown in FDI inflows to regional economies, the ASEAN governments were nevertheless concerned that the ASEAN-foreign distinction could send the wrong signals to foreign investors at a time when ASEAN was under severe scrutiny by foreign investors and was facing a rather precarious FDI/growth situation.

The future of AFTA

The first, and perhaps, easier phase of liberalisation – in manufactured goods – is clearly over. AFTA has not, however, become irrelevant for the ASEAN member governments, and indeed key foreign and domestic business groups continue to push for its full implementation (amidst pressures from other domestic sources to delay particular aspects of AFTA). Although ASEAN will continue to work towards full

[15] The theoretical basis of developmental regionalism is discussed in Nesadurai (2003).

implementation of AFTA, progress in liberalising services trade, the next phase of AFTA, is likely to be slow because this will affect entrenched domestic interests. While AFTA will remain a key feature of the regional economic architecture, it will increasingly be in competition with some of the newly emerging regional configurations.

New Regional Arrangements in the Asia Pacific

Since 1999, at least 20 proposals for new trading arrangements have been put forward in the Asia Pacific, ranging from bilateral FTAs to plurilateral arrangements. Among the latter include proposals for a Northeast Asian FTA grouping China, Japan and South Korea; an ASEAN-China FTA involving 11 countries; as well as an East Asian FTA grouping the 13 countries of Northeast and Southeast Asia. Their prospects remain uncertain, given that many of these remain at the proposal stage. Nevertheless, they may well add to already existing regional trading arrangements in the region, namely APEC and AFTA. A closer examination of the two most concrete forms of new regional agreements already in place – the ASEAN-China FTA and Singapore's bilateral FTAs – reveals that the same dynamics at work in APEC and AFTA are also behind these new regional arrangements.

<u>The ASEAN-China Free Trade Area</u>

The cautious response of all the ASEAN leaders and policymakers to China's proposal made in late 2000 to form a free trade area between China and ASEAN is completely understandable. Market displacement is a key concern of virtually all the ASEAN governments. China by itself potentially offers foreign capital a 'regional' site of production by virtue of its size and internal industrial complementarities.

China's attraction is, of course, magnified when its overall lower cost of production is factored into the equation. China's regional market potential, moreover, is strengthened through the 'Greater China' configuration that includes Hong Kong. In short, China offers a range of complementarities that producers can take advantage of, that smaller countries as in ASEAN are only able to do through pooling their complementarities via regional cooperation. This means that the market displacement effect in ASEAN from cheaper imports from China will likely extend over the value-added chain rather than be confined to labour-intensive industries only.[16]

An ASEAN-China FTA would also tend to blur the distinction between the two regional sites because the FTA would allow producers locating in China to sell at preferential rates in both China and ASEAN and vice versa for those locating in ASEAN. At another level, this could well enhance the attraction China displays relative to ASEAN as a site for investment as it means that an investor preferring to locate in China would be assured of preferential market access to ASEAN, assuming that selling in ASEAN is considered to be important. In short, if AFTA had been salient because it offered an investment site for FDI searching for a *regional* economic space in the Asia Pacific, then an ASEAN-China FTA has the potential to weaken the salience of the AFTA region as a distinct regional space for investment.

These concerns explain the hesitant ASEAN response to the Chinese proposal in November 2000 when they sidestepped the issue by suggesting a one-year feasibility study on the proposal. In the end, the project was formally endorsed by ASEAN in November 2001 and a Framework Agreement signed in November 2002. ASEAN is,

[16] Computer simulations confirm the competitive nature of the ASEAN-China relationship. See Scollay

however, proceeding cautiously on implementation of the proposal, with a fully operational FTA with China scheduled for 2010 at the earliest. This is not to suggest that ASEAN policymakers and leaders are against the idea of closer economic integration with China. On the contrary, all the ASEAN leaders, including those hesitant about the project, recognise the gains to their respective economies from investment opportunities for local firms in China, from preferential market access to the China market and from access to lower priced final products and intermediate inputs from China.

In fact, a China-ASEAN FTA may well provide the ASEAN side with a 'regional space of consumption' to supplement AFTA as a 'regional space of production' given the enormity of the Chinese market. AFTA, at present, is most significant as a region of investment/production, while its capacity as a significant consuming region is limited until such time that economic growth and development raise regional consumption demand for a wider range of goods and services produced within ASEAN. AFTA is, therefore, best seen as a 'partial economic space', with its main markets remaining outside ASEAN, notably in the US, notwithstanding the rise in absolute levels of intra-regional trade since the mid-1990s.[17] As such, global market developments and the prospects for the US economy would have considerable bearing on how ASEAN members calculate the costs and benefits of a free trade area with China. The uncertainties surrounding the global economy in the closing months of 2002, particularly with economists fearing that the US could linger for a few years in

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and Gilbert (2001).
[17] Intra-ASEAN trade accounts for about 20-25 per cent of ASEAN's global trade.

a post-bubble recession[18] may well render the ASEAN-China FTA more attractive to those ASEAN members currently most hesitant about this project.

For the present, however, there is considerable ambivalence about this project in the region as leaders recognise the competitive and cooperative nature of an ASEAN-China free trade area. The ten-year delay is, therefore, seen to be necessary to allow ASEAN to consolidate itself as a regional site for production and for domestic industries to make the transition to competing first in ASEAN.[19] In fact, Malaysia, the Philippines and Indonesia are said to prefer the project to only become fully operational by 2012 or 2014 rather than in 2010 for precisely this reason.[20] Although this is not to suggest that a wider free trade zone with China will never materialise in the future, the argument put forward is that the ASEAN governments will probably proceed cautiously for so long as they regard China as a major rival for FDI and as a competing producer of goods now being manufactured in ASEAN. ASEAN member governments may not concur with liberal expectations that wider regionalism, particularly with China, would necessarily be a good thing on economic grounds.

Thus, the *Framework Agreement on ASEAN-China Comprehensive Economic Cooperation* signed at the ASEAN-China Summit in November 2002 will only flag off negotiations on the FTA, which are scheduled to begin in 2003. Although the idea of an 'early harvest package' has been proposed as a means of accelerating implementation of the project by focusing initially on a limited number of liberalisation commitments, this package is only scheduled to be implemented from

[18] See Paul Krugman, 'The US economy needs leadership', in *The New York Times*, reproduced in *the International Herald Tribune*, 2 October 2002.
[19] Interview with a Malaysian trade official, December 2001.
[20] *Philippine Daily Inquirer*, 'ASEAN wants trade bloc with Japan before China', 18 September 2002.

2004 and then over a three-year period, taking it to 2007. It is clearly with much caution that the ASEAN countries are approaching the ASEAN-China FTA. These sentiments, driven by domestic concerns, could change if there is expectation of a prolonged global economic downturn, a point already alluded to above.

Bilateral Free Trade Areas

Bilateral free trade areas are increasingly the norm in the region, with Singapore the most active proponent of this instrument.[21] At least seven bilateral FTAs involving Singapore have been considered, with the Japan-Singapore FTA[22] agreement already signed and the US-Singapore FTA currently in the final stage of negotiations. Singapore has also concluded agreements with New Zealand and with EFTA (European Free Trade Area), while negotiations are ongoing with Australia, Canada and Mexico. Singapore, New Zealand and Chile have also signalled their intentions to begin negotiations on a trilateral FTA, due to be concluded in 2004. The rush to such bilateral arrangements is clearly an instance of governments aiming to secure market access for domestic exporters and investors in an increasingly uncertain global trading environment.

A plus for global free trade?

Both the Japan-Singapore FTA and the soon-to-be concluded US-Singapore FTA are clearly WTO-plus, covering investment and government procurement in addition to services. Labour and environmental standards are also expected to be part of the deal with the US. In the Japan-Singapore FTA agreement, Singapore has pledged to go beyond its WTO offers in 78 specific service areas while Japan will make WTO-plus offers in 32. Moreover, both parties have agreed to lower the threshold for adhering to WTO rules in government procurement to below the level currently prescribed in the WTO.

Apart from concern over the future of multilateral trade liberalisation (Desker 2002), Singapore's frustration over the slow pace of services liberalisation in AFTA also explains its new preference for bilateralism. Thus, the services component of the Singapore-Japan free trade area is highly significant for Singapore, enabling the country to gain access to Japan's notoriously closed but large services market. In the forthcoming US-Singapore free trade area, all service sectors will be liberalised automatically unless specifically excluded.[23] Singapore's bilateralism in trade policy, which has generated some tensions within ASEAN over its potential to 'dilute AFTA', clearly reflects the kind of economic realism that paradoxically prompted the ASEAN countries to form AFTA in the face of an external threat from China to FDI inflows to the region. Sinagpore's foreign economic policy is based on the search for economic security and achieved at various levels – bilateral, regional and multilateral (Dent 2001). That the bilateral instrument was pursued given the slow pace of regional services liberalisation and the uncertainties in the multilateral process is unsurprising.

The bilateral instrument is clearly attractive to other countries as well in addition to Singapore, as seen in the rush by countries such as New Zealand, Mexico, Vietnam, Thailand, Chile, Canada, Australia, and South Korea to pursue their own bilateral

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[21] Scollay and Gilbert (2001: 1-2) provide a list of negotiated and proposed bilateral and plurilateral free trade areas in the Asia Pacific region.
[22] The *Japan-Singapore Economic Agreement for a New Age Partnership* was signed in January 2002.
[23] *Sunday Times*, 'FTA customs union to benefit SEAsia' 17 March 2002.

deals with selected partners. Their ambivalence about the prospects of early success in negotiating a new WTO Round, given the very extensive agenda adopted a year ago at Doha, may well be driving these governments to hedge their bets and opt for a surer approach to lock in market access. Moreover, the emphasis on new issue areas – services, investment and government procurement – is extremely significant as it implies that these newer arrangements are taking liberalisation beyond the WTO. In short, the new bilateralism is potentially a building block for global free trade.

The growing trend towards bilateral agreements is likely to alter patterns of trade and investment in the region, and consequently lead to shifts in the regional distribution of economic gains. While bilateral arrangements certainly provide gains for participating countries, economic simulations reveal that those excluded would suffer losses, particularly if these arrangements involve a major economic power such as the US or Japan (Scollay and Gilbert 2001: 115-6). This may, however, prompt excluded countries to either get on board existing bilateral arrangements or to negotiate their own bilateral free trade areas, leading to what economist Richard Baldwin calls the 'domino effect' in regionalism (Baldwin 1999) and, consequently, a push for global free trade. The 'domino' effect is clearly evident in the Asia Pacific, as seen in Washington's latest initiative to negotiate bilateral FTAs with any ASEAN country and the trilateral FTA proposed by Singapore, Chile and New Zealand. Both initiatives were announced on the sidelines of the 2002 APEC Ministerial Meeting and Leaders' Summit held in Los Cabos, Mexico.

Potential drawbacks

There are, however, indications that bilateralism, while not detracting completely from global free trade, could, nevertheless, limit the globalisation agenda by offering an institutional means to both secure market access *as well as* accommodate domestic economic/political sensitivities. There may be better prospects for negotiating bilateral FTAs on an *a la carte* basis than in global or even regional processes, with the cooperating parties opting to exclude particular sectors that are sensitive for one or both parties. This was evident in the Japan-Singapore FTA, when goldfish and cut flowers were excluded due to domestic sensitivities in Japan. The significance of this move becomes clear given the impasse in APEC over Japanese intransigence in liberalising agricultural tariffs. Any new bilateral arrangement involving Japan, South Korea, China and the ASEAN countries could well go down this *a la carte* path, given existing domestic political sensitivities over many aspects of trade liberalisation, particularly in agriculture. The question here is the extent to which the FTA signatories could exclude sensitive products and sectors, or include only selected sectors without contravening GATT Article XXIV and the non-discrimination principle of the multilateral process.

The second source of concern stems from any mushrooming of bilateral arrangements that will lead to what Jagdish Bhagwati and his colleagues call a 'spaghetti bowl' phenomenon, and to the fragmentation of the regional economy (Bhagwati *et al*, 1998). Fragmentation could arise if overlapping arrangements involved mutually inconsistent rules and different liberalisation schedules, which mean that products could be traded under a range of different rules and tariffs. This is especially likely during the period when the free trade area provisions are being implemented. In such instances, firms are likely to suffer directly from the increased costs of complying with distinct trading arrangements. Under these conditions, firms will have to comply with a range of requirements depending on which FTA partner they are trying to do business with. Such effects will be especially pronounced for overlapping free trade areas even if these are designed to be WTO consistent. A mere difference in tariff phasing schedules and in rules of origin could mean that the same product would be subject to quite different treatment, depending on its origins and its destination (Scollay and Gilbert 2001: 17). For these reasons, the bilateral route, while offering a way out of the difficulties in obtaining further progress at the multilateral level or even at the AFTA level, might itself introduce economic inefficiencies and add to the cost of doing business in the region.

Moreover, to the extent that firms are interested in regional divisions of labour, as mentioned earlier in the paper, and are increasingly engaging in regional production networks, then a 'spaghetti bowl' framework of market access arrangements may not be in their best interests. This is why in the US-Singapore free trade area still under negotiation, a provision has been included to extend the juridicial reach of the free trade area to include two Indonesian islands, Batam and Bintan for the category of electronics and information technology items. Because production of final goods in Singapore involves extensive use of components produced in other parts of the region, like on Bintan and Batam islands, strict rules of origin would effectively exclude Singapore-made final products from the US market unless crucial portions of Singapore's hinterland are included within the ambit of the free trade area. While the US-Singapore approach is one way to address this structural issue, the exercise repeated over a number of bilateral FTAs will only raise the costs of negotiating, monitoring and enforcing agreements, while increasing fragmentation in the regional economy. There is, in a sense, a tension or incongruence between the institutional framework for organising economic activity that appears to be increasingly dominating the regional landscape – the bilateral framework – and the logic of capital, which is seeking *regional* spaces for organising production.

Conclusion

The paper's central argument is that the regional trend in the Asia Pacific is best explained in terms of the interaction between concerns stemming from globalisation at the systemic level and domestic political economic priorities. Although the regional arrangements examined here – APEC, AFTA and the bilateral FTAs – are about ensuring continued integration of member economies with global markets, they are not all about governments renouncing national policy autonomy. There are significant domestic political priorities centred on emerging domestic-owned capital, politically important domestic distributional coalitions and wider domestic social agendas that make it imperative for governments to retain domestic policy autonomy and even to regain some degree of control over globalisation outcomes. Thus, open regionalism in APEC, negotiated flexibility in AFTA and the possible adoption of the *a la carte* principle including a WTO-plus agenda in bilateral FTAs are all attempts to secure domestic priorities through procedural approaches. In short, regional agreements are embedded in a context shaped by dominant domestic coalitions, growth strategies that take domestic social/political agendas into account, and prevailing international conditions (Jayasuriya, 2003).

There are clear commonalities in all three major regional forms studied. All three are about *regaining* some measure of control over the outcomes of globalisation, notably access to export markets and to global capital. This is especially clear in the case of the bilateral FTAs and AFTA. In their attempts to use AFTA as an instrument to redirect global investment flows to regional economies, the ASEAN member governments were clearly trying to regain some degree of control over globalisation outcomes – where FDI locates – through regional collective action. The attempt at developmental regionalism, although short-lived, was likewise aimed at collectively securing the future of domestic-owned capital in a world these governments saw as increasingly dominated by TNCs. Nevertheless, these governments were not prepared to completely transfer sovereignty to AFTA.

In fact, the manner in which both AFTA and APEC were structured, notably their modalities for cooperation, also reflected their members' keen interest in retaining *national* policy autonomy. The degree of *regional* policy autonomy transferred to these projects differed, however. APEC was allowed the least degree of regional autonomy since members maximised their domestic policy autonomy through the principle of 'open regionalism'. Open regionalism was the only way for many of APEC's Asian governments to retain policy autonomy in the presence of more powerful, industrial country governments that might have employed APEC to accomplish market opening and economic reform in their economies. AFTA, given its clear role as a regional instrument for the ASEAN governments to gain some control over globalisation was clearly endowed with more regional autonomy than APEC, but continued to permit domestic policy latitude through 'negotiated flexibility'. The bilateral arrangements already concluded to date, notably involving Singapore, have retained the least domestic policy autonomy, although the possibility of *a la carte* approaches allows for some degree of domestic policy autonomy.

The implications of these regional agreements for global governance, particularly the WTO, are mixed. Certainly, these regional agreements are not a direct threat to a liberal trading order since they are all about engaging with the global market. Their underlying dynamics suggest, however, that governments might be hesitant to fully support the multilateral process through the WTO if the latter focuses too much too soon and at too rapid a pace on areas of domestic regulatory control that challenge domestic political and social agendas or the interests of key domestic coalitions. If that happens, governments may well pursue the regional and especially the bilateral option with greater enthusiasm. In fact, the bilateral route might become an extremely attractive option for some states as APEC becomes increasingly marginalized as a vehicle for economic liberalisation and AFTA enters into a more difficult phase of economic cooperation. The danger of bilateralism is that it may impose more costs on businesses, while also creating a disjuncture between the 'regional' logic to global capital and the institutional framework governing economic cooperation. Bilateralism, while it may act as a building block to global free trade, could also divert attention and resources from the multilateral process, particularly if it is able to offer greater flexibility to its negotiating parties, whether it is to retain greater domestic policy autonomy in some areas or to advance beyond the present WTO agenda. The bilateral agreements already negotiated to date have managed to accommodate both these distinct needs. It is perhaps precisely because of this that bilateral agreements will come to dominate the regional economic architecture.

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Helen E S Nesadurai
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