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# Achieving the Promise of the ASEAN Economic Community: Less Than You Imagine, More Than You Know

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**EXECUTIVE SUMMARY**

This paper provides a snapshot of the Association for Southeast Asian Nations (ASEAN) as it seeks to promote trade and investment within and outside the region and create an ASEAN Economic Community.

## *Main Argument*

ASEAN and its member states have made considerable progress in developing a rules-based system that promotes trade in goods and services and FDI, and indeed ASEAN's trade and investment performance has been impressive. Measures to create an ASEAN Economic Community (AEC) have contributed to this performance but are not designed to create a European Union–style unified market. While the target date to create the AEC by the end of 2015 should be considered a milestone on a longer journey, the foundations have been laid for deeper and broader integration that could promote productivity and increased, inclusive economic growth to the benefit of all ASEAN member states.

## *Policy Implications*

- Finance ministers should take a larger role in driving ASEAN integration to tap its potential to generate higher economic growth.
- ASEAN should take the next step toward developing regional rules in areas such as customs, investment, and competition policy so firms can more easily implement regional ASEAN strategies.
- The ASEAN secretariat should be empowered to actively monitor effective implementation of ASEAN agreements and should engage with the private sector to facilitate discussions among the member states.

On May 11, 2014, in the Naypyitaw Declaration, the leaders of the Association of Southeast Asian Nations (ASEAN) agreed to intensify efforts to realize the ASEAN Economic Community (AEC) by 2015. This otherwise mundane statement is likely to stoke the lively debate over the AEC. Those who have proclaimed with bold certainty that the AEC will introduce major changes will be encouraged by the leaders' resolve. Those who have offered robust critiques, asserting that the AEC will never be in place by 2015, if at all, are unlikely to be impressed. The commentary will continue to be as pointed and sharp as ever.

In any event, the debate appears to have raised awareness of ASEAN's economic ambitions. A case in point is a recent survey by the Pacific Economic Cooperation Council.[1] Thought leaders in the region were asked about the likelihood of a successful conclusion of the Trans-Pacific Partnership (TPP). The TPP is a high-profile undertaking that has captured attention in the United States, the Pacific region, and the world. Although 18% of the respondents did not know or did not respond to the question, about one-third judged that the negotiations are likely or very likely to be successful over the next three years. By contrast, the AEC has garnered little attention in the United States and much of the rest of the world but has unleashed debate across Asia. Interestingly, the responses to the same question about the AEC were very similar to those about the TPP, with 22% either stating that they did not know or not responding and a remarkable one-third believing that the AEC is likely or very likely to be achieved.

As is its nature, the truth in assertions about the AEC lies in between the extremes. A credible case can be made that ASEAN has constructed a solid base for the AEC. Benefits already are flowing to businesses and consumers, and more are in store. Some will be realized before the end of 2015; more will arrive afterward. However, 2015 should be regarded only as an important

[1] Pacific Economic Cooperation Council, "State of the Region 2013–2014," 2013, 79.

milestone. ASEAN has much to do to integrate and improve the competitiveness of its ten member-state economies. The end is far from near. In fact, the ASEAN Coordinating Council has a working group fashioning a post-2015 vision under the leadership of Myanmar, ASEAN's current chair.

The following brief overview of ASEAN's key achievements in constructing the AEC is drawn from personal observations and recent assessments of progress, most notably the mid-term review by the Economic Research Institute for ASEAN and Southeast Asia (ERIA), issued in October 2012, and the "ASEAN Integration Monitoring Report" by the World Bank and the ASEAN Secretariat released in January 2014.[2]

Before reading on, however, a few words of caution are necessary. If you envisaged ASEAN as a wide open, unified economic entity much like the European Union (EU), relax. The AEC is less than you imagine. But if you steadfastly believe that ASEAN has not made significant progress in economic integration, pay heed. There is more to the story than you know.

## A Progress Report—Of Sorts

As time winds down toward the deadline at the end of 2015 to implement the AEC, it is tempting to report on the distance traveled and what remains. This represents a challenge: some elements of the AEC have clear end points but others do not. Moreover, international experiences suggest that some of the end points are more realistic (such as tariff elimination) than others (such as the elimination of non-tariff measures and open markets for cross-border services).

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[2] See Economic Research Institute for ASEAN and Southeast Asia (ERIA), "Mid-Term Review of the Implementation of AEC Blueprint: Executive Summary," October 2012, http://www.eria.org/publications/key_reports/mid-term-review-of-the-implementation-of-aec-blueprint-executive-summary.html; and ASEAN Secretariat and World Bank, "ASEAN Integration Monitoring Report," 2013, http://www.asean.org/resources/item/association-of-southeast-asian-nations-asean-integration-monitoring-report-a-joint-report-by-the-asean-secretariat-and-the-world-bank-english.

Rather than a progress report on the AEC, this paper highlights accomplishments of ASEAN and its members in promoting trade and investment in the region by establishing rules and reducing barriers largely as is embodied in the ASEAN Economic Community Blueprint. This is not to argue that a large part of the region's impressive performance can be attributed to measures to implement the AEC. But it can be argued that AEC rules have influenced policies in many member states. Moreover, ASEAN's rules and performance have laid the foundation for broader and deeper integration in the future.

## The AEC: The Goal

The AEC's overall objective is to "transform ASEAN into a region with the free movement of goods, services, investment, skilled labor, and freer flow of capital."[3] This goal is ambitious by any measure. So is the potential reward. An AEC that realized this vision would lift ASEAN's collective GDP by more than five percentage points, according to Michael Plummer and Chia Siow Yue.[4]

It has taken the EU more than four decades to construct a relatively seamless economic region. This is more than double the time ASEAN has been working in earnest on economic issues. For much of ASEAN's first two and a half decades, its attention was devoted to political issues. And even now, ASEAN is seeking to build political/security and sociocultural communities as well as the economic community. Thus, ASEAN's energies cover a wide spectrum of issues,

[3] Association of Southeast Asian Nations (ASEAN), *Roadmap for an ASEAN Community 2009–2015* (Jakarta: ASEAN Secretariat, 2009), 21.

[4] Michael G. Plummer and Chia Siow Yue, "Introduction," in *Realizing the ASEAN Economic Community: A Comprehensive Assessment*, ed. Michael G. Plummer and Chia Siow Yue (Singapore: Institute of Southeast Asian Studies, 2009), 35–36.

ranging from a new defense ministers process to human rights, food security, climate change, and education.

More to the point, in contrast to the EU, ASEAN comprises a much wider diversity of economic governance systems and levels of economic development, a significantly weaker secretariat (in terms of authority and resources), more modest involvement by finance ministries, and a business community that until recently had been content to carry on at national levels rather than envision the growth opportunities of an integrated regional market. The latter two dynamics may change if finance ministers in ASEAN member states and the business community recognize that ASEAN integration could be a driver of economic growth at a time when previous drivers of growth—China, the EU, and the United States—are less dynamic.

The AEC rests on four pillars, the first being a "single market and production base."[5] Despite the slow start and myriad challenges, several of the basic components of this pillar are in place. These include regional agreements on tariffs, non-tariff measures, and trade facilitation; services; and investment. The second pillar of the AEC consists of a highly competitive region supported by competition policies, consumer protection, intellectual property rights, infrastructure development, no double taxation, and greater connectivity through e-commerce. A third pillar is equitable economic development in which small and medium-sized enterprises, particularly those that are owned by women, can thrive and benefit from the AEC and in which the lesser-developed ASEAN member states (Cambodia, Laos, Myanmar, and Vietnam, known collectively as CLMV) can further narrow the development gap with the ASEAN-6 (Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand). The fourth pillar is a region fully integrated into the global economy. To some extent, the second and third pillars address "behind the border" measures that

[5] ASEAN, *Roadmap for an ASEAN Community 2009–2015*, 22.

ASEAN has traditionally shied away from, respecting its ironclad principle of noninterference in member states' domestic affairs. This, however, is changing as ASEAN has begun to realize the importance of structural policies to strengthen productivity and competitiveness.

ASEAN's integration into the global economy is worth emphasizing: 75% of ASEAN's trade is with non-ASEAN countries.[6] Rather than creating a "fortress ASEAN," AEC's imperative is to be an "open, outward-looking, inclusive, and market driven economy consistent with multilateral rules as well as adherence to rules-based systems for effective compliance and implementation of economic commitments."[7] Recent politically driven inward-looking policies in Indonesia would appear to be contrary to this broad ASEAN principle. The implications of these policies are likely to attract the scrutiny of other ASEAN member states.

### *The Core of AEC: A Single Market and Production Base*

*Tariffs, non-tariff barriers, and trade facilitation*. To liberalize trade in goods, the AEC Blueprint calls for the elimination of tariffs and non-tariff barriers (NTB) and the adoption of measures to facilitate trade. The latter include clear and simple rules of origin, streamlined customs procedures, and standards harmonized with international standards through a transparent process that includes input from the private sector. ASEAN has done well on tariff elimination, poorly on NTB elimination, and credibly on trade facilitation. Much of the progress is due to the ASEAN Trade in Goods Agreement (ATIGA), which took effect in 2010, and its predecessor, the ASEAN Free Trade Agreement. Conceived after the AEC Blueprint, the ATIGA is more detailed than the blueprint, legally binding, and has been ratified by all ASEAN member states.

[6] ASEAN, "Intra- and Extra-ASEAN Trade, 2012," ASEAN Merchandise Trade Statistics Database, December 20, 2013, http://www.asean.org/images/resources/2014/Jan/StatisticUpdate28Jan/table18_as20Dec13.pdf.
[7] ASEAN, *Roadmap for an ASEAN Community 2009–2015*, 21.

Tariffs among ASEAN member states have been virtually eliminated. The simple average of tariff rates among the ASEAN-6 is 0.05%, with 99.10% of the tariff lines at zero.[8] Tariff rates in the less-developed CLMV countries are higher because these states enjoy a longer phase-out period. They boast an average tariff rate of 2.4%, with 67.6% of the tariff lines at zero (up from 50% in 2011).[9] Critics point out that ASEAN members still impose tariffs on sensitive items, such as rice, and therefore are not completely free from tariffs. This is true. But it is also true of other free trade agreements (FTA). World Bank figures show that ASEAN's average tariff rate, including those on sensitive items, of 0.05% compares favorably with the 0.03% average tariff in the North American Free Trade Agreement (NAFTA).[10]

Elimination of tariffs among ASEAN members has had a positive knock-on effect, according to the World Bank. Member states' most-favored-nation (MFN) tariff rates have declined. The result is that the margin of preference between ASEAN and the MFN tariff rates is a slight 4–6 percentage points for the ASEAN-5 (Singapore has no tariffs so has zero margin of preference) and 3–7 percentage points for the CLMV countries.[11] Detractors, on the other hand, note that ASEAN preferential tariff rates are not widely used. Part of the explanation is that such a low margin of preference provides little incentive for traders to bother with the extra paperwork and requirements to apply for preferential rates. However, an Asian Development Bank survey of firms in Singapore, Thailand, and the Philippines showed that 28% of the respondents do use preferential

[8] Aladdin Rillo, Pitchaya Sirivunnabood, Ahmad Ahsan, and Jean-Christophe Maur, "ASEAN Integration Monitoring Report," ASEAN Secretariat and World Bank, Working Paper, no. 83914, January 1, 2014, 3, http://documents.worldbank.org/curated/en/2013/01/18780456/association-southeast-asian-nations-asean-integration-monitoring-report-joint-report-asean-secretariat-world-bank.

[9] Rillo et al., "ASEAN Integration," 4.

[10] Rillo et al., "ASEAN Integration," 3.

[11] Rillo et al., "ASEAN Integration," 8.

tariffs in FTAs and that another 25% plan to do so.[12] Even a slight preference can mean a competitive edge.

Progress on the elimination of NTBs has been decidedly sparse. ATIGA calls for notification and review of non-tariff measures (NTM) and elimination of those that constitute barriers to trade between 2010 and 2018. ASEAN has taken the first step of creating an NTM database. The database shows that about a third of the NTMs consist of non-automatic licensing and another third of technical regulations and quality standards.[13] Outright import prohibitions account for another 20%. The product groups most affected are chemicals, machinery, foodstuffs, and vegetable products. ASEAN, however, has not taken the next step to identify NTMs that are really NTBs and set a schedule for phasing them out.

ASEAN has made progress on trade-facilitation measures. ATIGA contains clear, relatively simple rules of origin. ERIA's mid-term review notes that ASEAN rules of origin in ATIGA have become "more liberal and business friendly."[14] For example, ASEAN now provides an option to use rules of origin most advantageous to the trader, either the regional value-added or the change in tariff classification rule, and is installing procedures for traders to self-certify origin, reducing time and paperwork. Agreement on the ASEAN harmonized tariff nomenclature for customs classification, based on the World Customs Organization nomenclature, has given a measure of uniformity in nomenclature, although classification and valuation practices may differ among member states.

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[12] Masahiro Kawai and Geneshan Wignaraja, eds., *Asia's Free Trade Agreements: How Is Business Responding?* (Cheltenham and Northampton: Asian Development Bank and ADB Institute with Edward Elgar Publishing, 2011), 34.

[13] Rillo et al., "ASEAN Integration," 13.

[14] ERIA, "Mid-Term Review of the Implementation of AEC Blueprint: Executive Summary," October 2012, 12.

ATIGA devotes a chapter to trade facilitation, reflecting many of the features that were subsequently incorporated into the 2013 World Trade Organization (WTO) Agreement on Trade Facilitation. Such features include the "single window" (single submission and synchronous processing of all information required for border clearance), risk management and authorized economic operators or trusted traders, advanced rulings, and post-entry audit. While implementation of each of these varies from state to state, ASEAN rules are clear and the working groups provide support. ASEAN would benefit from active monitoring of implementation—for example, by reactivating the Joint Committee of Trade and Customs Officials to monitor implementation of ATIGA's trade facilitation agenda.

Of particular note is progress on the ASEAN single window. ASEAN is making the first serious attempt at a regional single window that links together ten national single windows. ERIA reports that five ASEAN member states have live implementation of their national single windows and two more are at an advanced stage.[15] A pilot project in 2013 with seven ASEAN members proved the concept of a regional single window by accurately and efficiently exchanging technical customs information among the participants. ERIA surmises that full implementation of the ASEAN single window by 2015 is "not quite farfetched" and could be an "emerging success story" for ASEAN.[16] Since ERIA's report, Vietnam, Laos, Cambodia, and Myanmar have stepped up their efforts to create national single windows.

Have these trade measures made a difference? The World Bank estimates that trade costs in ASEAN have dropped by as much as 15% over the past decade.[17] The result is that ASEAN trade

[15] ERIA, "Mid-Term Review of the Implementation of AEC Blueprint," 12.

[16] ERIA, "Mid-Term Review of the Implementation of AEC Blueprint," 12.

[17] Rillo et al., "ASEAN Integration."

costs are now comparable to those in NAFTA. The World Bank further suggests that the reduction in trade costs has contributed to the increase in ASEAN's trade.[18] Total ASEAN trade has soared from around $800 billion in 2000 to just over $2,500 billion in 2012.[19] During this same period, intra-ASEAN trade has hovered around 25%, demonstrating that ASEAN firmly remains outward-oriented. Some point to the flat-lining of the intra-ASEAN share of trade as evidence that integration has stalled. The World Bank, to the contrary, points out that as measured by an intraregional merchandise trade openness index (which measures intraregional imports as a share of regional GDP), ASEAN's 16% compares favorably with the EU's 17 %.[20]

*Services*. ASEAN has enshrined the approach of the WTO's General Agreement on Trade in Services (GATS) to liberalization of services in the ASEAN Framework Agreement on Services (AFAS). Commitments to open services trade are made through "scheduling" commitments, the so-called positive list approach. Through eight negotiating rounds, ASEAN members' services experts have scheduled commitments on services sectors based on the GATS "modes of delivery": (1) cross border supply, (2) consumption abroad, (3) commercial presence, and (4) presence of natural persons. Financial and air-transport services (see the section on infrastructure below) are handled by separate groups.

In early rounds, commitments were uneven in sector coverage and commitments to liberalize. ASEAN sought to instill discipline by incorporating deadlines and expectations for commitments in the AEC Blueprint. By 2015, the plan was that there would be no restrictions for the first two

[18] Rillo et al., "ASEAN Integration."

[19] "ASEAN Trade, 2012."

[20] Rillo et al., "ASEAN Integration," 32.

modes except for *bona fide* regulatory reasons; mode three should allow for 70% foreign-equity participation; and procedures for liberalizing mode four should be agreed on.

The World Bank's review finds that while the ASEAN members are still behind schedule, they have made "significant commitments to liberalize regional trade."[21] Commitments under AFAS now exceed commitments made by ASEAN member states under the GATS. This has been confirmed in studies by Hikari Ishido that have been published in ERIA discussion papers. Using the Hoekman Index (1=open, 0.5=limited, 0=closed) for 55 subsectors, ASEAN's average commitments under the GATS registered 0.14 compared with 0.42 under AFAS.[22] The World Bank observes, however, that commitments under AFAS reflect less openness than is actually the case according to the World Bank's 2007–8 services database.[23] This suggests that ASEAN states' commitments under AFAS have not provided an impetus to further liberalization. Rather, they serve more as a "ceiling binding," an obligation not to become more restrictive.

Among the most challenging issues regarding foreign investment in services is the level of foreign equity participation. The World Bank assessment declares that the "most significant difficulties have arisen" on this issue.[24] Allowing 49% foreign equity is generally within the realm of possibility, but 51% or greater presents a significant challenge. In some instances the limitations are embedded in the national constitutions or have strong backing by domestic interests.

[21] Rillo et al., "ASEAN Integration," 97.

[22] Hikari Ishido, "Harmonization of Trade in Services by APEC members," Institute of Developing Economics, March 2013, 6, 8, http://www.ide.go.jp/English/Publish/Download/Dp/410.html.

[23] Rillo et al., "ASEAN Integration," 98.

[24] Rillo et al., "ASEAN Integration," 96.

Financial services are particularly sensitive, given the degree of national prudential regulations, and are pursued on a separate track by finance experts. A sixth package of commitments to liberalize financial services is to be signed in the near future. The Task Force on ASEAN Banking Integration Framework and the ASEAN Capital Markets Forum have made modest steps toward integration of banking and securities markets, respectively, at the urging of private industry, and work has been taken up recently with insurance regulators. ASEAN +3 (China, South Korea, and Japan) have progressed toward institutionalizing the ASEAN Macroeconomic Research Office as an international organization that will help support the operationalization of the Chiang Mai Initiative Multilateralization, a swap arrangement that was expanded to $240 billion in 2012.

So where does this put ASEAN on services? As measured by the World Bank's Services Trade Restrictiveness Index (STRI), the average of the six ASEAN member states for which there is data (Cambodia, Indonesia, Malaysia, the Philippines, Thailand, and Vietnam) is 44, compared with an East Asian average of 41 and world average of 29 (with 0 being the least restrictive and 100 the most restrictive).[25] Restrictiveness varies among sectors and countries. Nonetheless, even with a modestly restrictive reading on the STRI, ASEAN services trade has more than doubled from $118 billion in 2005 to $253 billion in 2011.[26] The share of intra-ASEAN service trading is holding steady at 8%.

Trade in services is notoriously complex. Two areas in ASEAN are especially challenging: one concerns delivering services in person, and the other concerns delivering services through a commercial presence (i.e. investment), discussed in the section on investment below.

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[25] Rillo et al., "ASEAN Integration," 101.

[26] World Trade Organization, *International Trade Statistics 2012* (Geneva: World Trade Organization, 2012).

Delivering services in person is a key component of the AEC—i.e., creating a free flow of skilled labor. Thus, there is a section dedicated to it in the blueprint, in addition to this area being covered in AFAS. A host of issues arise for individuals to work in foreign countries, including visas, work permits, and technical qualifications. ASEAN has adopted several approaches to address these issues.

ASEAN has created eight mutual recognition arrangements on major professional services (engineering, nursing, architecture, surveying, tourism, medicine, dentistry, and accountancy) that provide a basis to work toward mutual acceptance of professional qualifications. Supplementing these is the 2012 Agreement on the Movement of Natural Persons, under which commitments can be scheduled for professionals in specific service sectors. In addition, ASEAN has embarked on developing an ASEAN Qualifications Reference Framework that will enable comparisons of qualifications across participating members. The ASEAN University Network (AUN) also has created the AUN–Quality Assessment Network that works toward the harmonization of educational standards. These long-term efforts speak to ASEAN's determination to create mechanisms that will allow a freer flow of skilled labor in the region.

*Investment*. The AEC Blueprint declares that a "free and open investment regime is key to enhancing ASEAN's competitiveness in attracting foreign and intra-ASEAN investment."[27] At the time the blueprint was drafted, ASEAN investment obligations were governed by two instruments: the Framework Agreement on the ASEAN Investment Area (focusing on liberalization and cooperation) and the ASEAN Agreement for the Promotion and Protection of Investment (covering investment protection). Subsequently, ASEAN member states agreed to and ratified a new, legally binding ASEAN Comprehensive Investment Agreement (ACIA), which took effect

[27] ASEAN, *Roadmap for an ASEAN Community 2009–2015*, 27.

in 2012. The ACIA contains obligations as envisaged in the blueprint—namely, on investment cooperation, protection, facilitation, and liberalization—as well as reflects international norms. The ACIA's coverage is the same as under the previous investment agreements: manufacturing, mining, agriculture, fisheries, forestry, and services incidental to these sectors.

While the ACIA sets broad rules, investors still face ten different investment regimes in ASEAN. National competition and vested interests tend to trump efforts to harmonize rules in order to create a truly single production base for investors. However, harmonization could yield greater benefits, allowing firms to "think ASEAN" by going beyond their national markets to a regional one.

Where does ASEAN stand on having open investment regimes? An ERIA study examined ASEAN member states' investment rules in six areas: market access, national treatment, screening and approval procedures, board of directors and management composition, movement of investors, and performance requirements. Using a variation of an Organisation for Economic Co-operation and Development (OECD) methodology, different restrictions were given different weights, with scores ranging from 1 to 0 and lower scores indicating more market openness. In the agriculture, forestry, fishing, mining, and manufacturing sectors covered by the ACIA, ASEAN's average score was a decent 0.267, aided by a solid market access score of 0.197.[28]

But there remains room for further improvement. States are able to submit sector-specific reservations to the ACIA, the so-called negative list. According to the World Bank's calculations,

[28] Shujiro Urata and Mitsuyo Ando, "Investment Climate Study of ASEAN Member Countries," in "Tracing the Progress toward the ASEAN Economic Community," ed. Shujiro Urata and Misa Okabe, ERIA, ERIA Research Project Report 2009, no. 3, March 2010, Table A3.1, 224–27.

there are 130 such reservations.[29] These are to be subject to a peer-review mechanism with a view to their reduction and elimination.

Investment facilitation is another area where ASEAN could strengthen its efforts. According to the World Bank's Doing Business survey, ASEAN as a whole is about on par with the average in East Asia and the Pacific and slightly under the Asia-Pacific Economic Cooperation (APEC) average. So as a group, ASEAN is not performing badly. As in most other areas, however, this average hides substantial divergences among the states, with Singapore generally turning in some of the best performances in the world.

Some ASEAN member states are stepping up their game. The seven ASEAN states in APEC are participating in APEC's Doing Business initiative to reduce the number of procedures, time, and cost of doing business by 25% by 2015. Indeed, the ASEAN participants in this initiative have kept pace with APEC's improvement level overall. More broadly, in an increasingly competitive marketplace for investment, there is growing interest in ASEAN to strengthen investment facilitation.

Investments by service providers are not covered by the ACIA. When the ACIA was being designed, ASEAN investment experts debated whether investment in services should be moved from AFAS to the new investment agreement. Under AFAS, each state commits to discipline sector by sector or makes "horizontal" commitments for several sectors. This implies that the treatment of services investment can vary by sector and by country. The decision, regrettably, was not to move obligations on services investment to the ACIA. This was a missed opportunity.

As a consequence, investment by foreign service providers in ASEAN does not benefit from the general uniform obligations of the ACIA. These include fair and equitable treatment, the right

[29] Rillo et al., "ASEAN Integration," 145.

to make transfers, protections against expropriation, requirements for prompt and adequate compensation should expropriation occur, and recourse to dispute settlement. Moreover, ASEAN has more restrictions on services investments that could be diminished through the ACIA. Using the modified OECD method of measuring investment restrictions explained above, ERIA studies show that the average for all ASEAN sectors was 0.337, suggesting that investment rules are more restrictive in services than in the sectors covered by the ACIA (0.267). The average ASEAN score on market access for investment in services was 0.323, considerably higher than the 0.197 for those sectors covered by the ACIA.[30]

Still, the overall ASEAN investment numbers have been impressive. Net FDI flows into ASEAN rose to a record level of $110 billion in 2012.[31] According to the most recent *ASEAN Investment Report 2012*, inward FDI stock reached an all-time high of $1.1 trillion, a mighty rise from $266 billion in 2000.[32] Factors driving the rise include the region's growth potential, role in production networks and value chains, and consolidation through mergers and acquisitions. The share of intra-ASEAN FDI to total FDI in ASEAN has jumped from 8% to 20%. While Singapore has accounted for the bulk of the FDI inflows to ASEAN (50%), it also was the primary source of intra-ASEAN FDI (50%), suggesting that Singapore is being used as a turntable for FDI throughout ASEAN.[33]

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[30] Urata and Ando, "Investment Climate Study," Table A3.1, 224–27.

[31] ASEAN, "Foreign Direct Investment Net Inflows, Intra- and Extra-ASEAN," ASEAN Foreign Direct Investment Statistics Database, October 30, 2013, http://www.asean.org/images/resources/2014/Jan/StatisticUpdate28Jan/Table%2025.pdf.

[32] ASEAN, *Investment Report 2012: The Changing FDI Landscape* (Jakarta: ASEAN Secretariat, 2013), 3.

[33] ASEAN, *Investment Report 2012*, 55.

Overall, the trend for FDI in ASEAN is positive. A survey of businesses by the U.S. Chamber of Commerce and American Chambers of Commerce based in the region revealed that 80% of those surveyed have stepped up their trade and investment in ASEAN over the last two years and 90% expect to do so in the coming five years.[34]

*Highly Competitive Region*

All the areas included in the AEC Blueprint to make ASEAN a more competitive region have work plans underway. Rather than reviewing all these areas, this section highlights progress in two important areas: competition policy and transport.

*Competition policy*. Theory suggests that competition can help drive productivity and increase real incomes. According to one estimate an effective competition policy in ASEAN could boost per capita GDP in Indonesia, Malaysia, Thailand, and the Philippines by 3%–15% over ten years.[35] Recognizing these potential gains, ASEAN has made significant progress. Fifteen years ago, no ASEAN economy had a competition law; now five states have one—Indonesia (1999), Malaysia (2012), Singapore (2004), Thailand (1999), and Vietnam (2005). At the urging of ASEAN ministers, the other five members have pledged to put a competition law in place by 2015 as a part of the AEC. Two states (Myanmar and the Philippines) are actively discussing draft legislation.

[34] "ASEAN Business Outlook Survey 2014," AmCham Singapore and U.S. Chamber of Commerce International Affairs, August 2013, 6.

[35] Wisarn Pupphavesa, Santi Chaisrisawatsuk, Sasatra Sudsawasd, and Sumet Ongkittikul, "Competition Policy, Infrastructure, and Intellectual Property Rights," in *Realizing the ASEAN Economic Community: A Comprehensive Assessment*, ed. Michael G. Plummer and Chia Siow Yue (Singapore: Institute of Southeast Asian Studies, 2009), 78.

The ASEAN Experts Group on Competition drafted the ASEAN Regional Guidelines on Competition Policy and launched an official website in an effort to bolster advocacy efforts on the benefits of competition policy and laws.[36] The goal is not to create a single ASEAN competition regime but rather to establish a common platform for cooperation and collaboration in competition cases.

*Infrastructure*. The ASEAN Strategic Transport Plan covers land, air, and marine transport and transport facilitation, providing more depth to the AEC Blueprint. ERIA's mid-term review of the AEC highlighted progress in air transport following the ASEAN-X formula, under which an agreement can enter into force when ratified by fewer than all ASEAN member states (typically ASEAN agreements enter into force only after being ratified by all ten member states). The Multilateral Agreement on the Full Liberalization of Air Freight Services has entered into force in nine member states, the Multilateral Agreement on Air Services in eight states, and the Multilateral Agreement on the Full Liberalizing of Passenger Air Service in five states. Experts have completed eight rounds of scheduling commitments on aviation services (e.g., maintenance and repairs, computer reservation systems, leasing, and catering). Work is underway on an ASEAN Single Aviation Market that would cover such issues as air traffic management, aviation safety, aviation security, and institutional arrangements.

Ground transportation facilitation has languished after a promising start. Important protocols, such as customs transit, under the ASEAN Framework Agreement for Transport Facilitation remain unfinished. In addition, the ASEAN Framework Agreement on Multimodal Transport and the ASEAN Framework Agreement on Facilitation of Interstate Transport were concluded in 2005 and 2009, respectively, but have been ratified by only a few countries. While states that have

[36] See the ASEAN Competition Policy and Law website, http://www.aseancompetition.org.

ratified these agreements can implement the agreements among themselves, ratification by all members would provide a more coherent, comprehensive approach.

The AEC Blueprint notes the importance of attracting innovative financing for infrastructure. The Asian Development Bank calculates that the ASEAN region will need around $60 billion a year to meet its infrastructure needs.[37] In 2011, ASEAN finance ministers agreed to create the ASEAN Infrastructure Fund (AIF). The AIF's $485.2 million in equity is held by ASEAN member state governments ($335.2) and the Asian Development Bank. The AFI will issue debt in 2016 with a view to support $12 billion in projects for the period 2012–20.[38] The first loan, made at the end of 2013, was for $25 million as part of a $410 million project to strengthen power transmission in Indonesia from Java to Bali.[39]

### *Equitable Economic Development*

Equitable economic development refers to development among and within ASEAN member states. In ASEAN the development gaps are significant: the CLMV countries' annual per capita income is $1,600 or less. Four other ASEAN states have per capita incomes ranging from $2,600 to $10,000, while Singapore and Brunei are in a league of their own with annual per capita incomes in the range of $42,000 to $54,000.[40] It is little wonder that the CLMV countries seek longer

[37] Asian Development Bank, "Proposed Equity Contribution and Administration of ASEAN Infrastructure Fund," Report and Recommendation of the President to the Board of Directors, August 2011, 1.

[38] Asian Development Bank, "Proposed Equity Contribution," 4–5.

[39] Asian Development Bank, "Indonesia Power Project Marks First Loan of ASEAN Infrastructure Fund," Press Release, December 3, 2013.

[40] ASEAN, "Selected Basic ASEAN Indicators," April 30, 2014, http://www.asean.org/images/resources/Statistics/2014/SelectedKeyIndicatorAsOfApril/table1_as%20of%20Apr14_upload.pdf.

transition periods to implement AEC obligations and also additional capacity building and technical assistance through the Initiative for ASEAN Integration.

A recent study entitled *Narrowing the Development Gap in ASEAN* showed that the difference in gross national income between the ASEAN-6 and the CLMV countries widened by 10% from 2000 to 2011. During the same period, the difference as measured by the United Nations Human Development Index narrowed by 13%. While the trend demonstrated in the Human Development Index is positive, the gap remains substantial. Rough calculations suggest it could take the CLMV countries fifteen to twenty years to reach the ASEAN-6's average in 2011.[41]

*Narrowing the Development Gap* identifies "key drivers" that could help accelerate inclusive economic growth. These include physical capital, openness to trade, human capital, financial sector development, governance, labor mobility, FDI, and external development finance. Most of these drivers are included in the AEC Blueprint and are well on their way to being implemented.

More directly, the AEC Blueprint calls for concentrated effort on the development of small and medium-sized enterprises to promote equitable economic development. This makes good sense. In ASEAN states, small and medium-sized enterprises account for more than 96% of all businesses and contribute between 50% and 95% of domestic employment and between 30% and 53% of GDP.[42] Capacity building, access to finance, women's entrepreneurial networks, links to supply chains, and access to information and innovation are among the many activities underway under the ASEAN strategic plan for small and medium-sized enterprises. At the May 2014 summit, leaders announced that ASEAN is working with the World Bank to develop a monitoring tool to

[41] Mark McGillivray, Simon Feeny, and Sasi Iamsiraroj, "Understanding the ASEAN Development Gap," in *Narrowing the Development Gap in ASEAN: Drivers and Policy Options*, ed. Mark McGillivray and David Carpenter (Oxon: Routledge, 2013), 29–31.

[42] ASEAN, "Small and Medium Enterprises," http://www.asean.org/images/archive/SME/SME-FS.pdf.

track equitable development in the region. This tool promises to lead to more strategic thinking and targeted actions.

*Integration into the Global Economy*

The AEC Blueprint prescribes a "coherent" approach to external economic relations. ASEAN has negotiated FTAs with its major regional dialogue partners: China, South Korea, Japan, New Zealand and Australia (jointly), and India. These agreements vary in quality, with recent agreements, particularly the FTA with New Zealand and Australia, offering greater levels of market access, broader coverage, and more rigorous obligations.

In 2012 ASEAN launched negotiations for the Regional Comprehensive Economic Partnership (RCEP). The objective is to "achieve a modern, comprehensive, high-quality and mutually beneficial economic partnership agreement among the ASEAN Member States and ASEAN's FTA Partners."[43] The RCEP is intended to cover trade in goods, trade in services, investment, economic and technical cooperation, intellectual property, competition, dispute settlement, and other issues. Ministers ambitiously have targeted the end of 2015 to reach an agreement.

ERIA forecasts that the RCEP will produce more economic growth for all ASEAN member states than the current network of FTAs.[44] Peter Petri and Michael Plummer calculate that the RCEP could lift average real GDP in ASEAN by 2% over baseline estimates by 2025.[45] The RCEP

[43] "Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership," August 30, 2012.

[44] Yoshifumi Fukunaga and Ikumo Isono, "Taking ASEAN+1 FTAs Towards the RCEP: A Mapping Study," ERIA, ERIA Discussion Paper Series, no. 2, January 2013, 22.

[45] Peter A. Petri and Michael G. Plummer, *ASEAN Centrality and the ASEAN-U.S. Economic Relationship*, (Honolulu: East-West Center, 2014), 41.

could also be used to streamline and harmonize provisions in the existing network of ASEAN+ FTAs and allow ASEAN to press for more rigorous rules and broader coverage. Despite the promise of the RCEP, however, progress and enthusiasm are difficult to detect after four negotiating sessions.

Trade rules emerging from the RCEP can be expected to reflect generally accepted international trade and investment practices, since participants broadly ascribe to the same principles. All are members of the WTO, and the ASEAN states have pledged that their agreements should be consistent with international rules. In addition, twelve of the sixteen RCEP participants are members of the APEC forum, which also supports international rules. Moreover, ASEAN members Singapore, Malaysia, Vietnam, and Brunei—as well as Australia, New Zealand, and Japan—are participating in both the RCEP and the more ambitious TPP negotiations that include the United States. The TPP is aiming for high-level standards and maximum coverage, to be a new type of 21st-century trade agreement. In sum, the RCEP participants are broadly like-minded with respect to the use of international trade and investment rules and practices.

The RCEP, however, is presaged to be substantially different from the TPP in important ways. It claims to be willing to recognize countries at different levels of development, making allowances for special and differential treatment. The RCEP is to be based on existing FTAs, which have significant product exclusions, and is decidedly less ambitious regarding the level of commitment and rigor in some of the obligations.

Still, given the points made above, some provisions of the RCEP and the TPP, such as trade facilitation, are likely to be similar. If so, these areas of commonality, coupled with information sharing and transparency, could provide a pathway toward realizing APEC's vision for a free trade area of the Asia Pacific.

## Conclusion

ASEAN has come a long distance in economic integration from its inception as a political group and even from its initial economic agreements. An AEC by 2015 is a bold vision that, as the date approaches, has generated excitement and interest. More businesses have ASEAN strategies than ever before. Yet as with all bold visions, in reality much remains to be done. ASEAN has not constructed a single market; however, it has made more progress than is acknowledged by naysayers.

Building on what has been accomplished to date, this paper suggests five measures that would give more impetus to ASEAN's current efforts and move states in the organization toward broader, deeper integration.

1. Update AFAS to incorporate new approaches to scheduling services—such as negative lists or a hybrid of positive and negative lists to allow more flexibility. The announcement at the May 2014 ASEAN Summit of negotiations regarding an ASEAN Trade in Services Agreement by the end of 2015 is a solid first step in this direction.
2. Amend the ACIA to cover investment in services so that those investments benefit from all ACIA's investor protection provisions.
3. Articulate a vision of an ASEAN Customs Union, at least with respect to a few key sectors, that entails harmonizing and streamlining customs procedures and setting a uniform external tariff. This would promote intra-ASEAN trade and save time and expense with border administration.
4. Establish binding cooperative agreements to investigate and act on cross-border anticompetitive practices.

5. Empower the secretariat to monitor the implementation of ASEAN agreements in member states' domestic laws and regulations and to serve as an enquiry point for the private sector, including as a facilitator of discussions between the private sector and the collected member states.

Most importantly, finance ministers should assume a larger role in driving ASEAN economic integration beyond the financial sector, perhaps by co-chairing the ASEAN Economic Council together with economic ministers. This would be a natural fit, given their responsibilities for customs, financial services, and investment. Moreover, in the absence of any other clear engine for growth in the current global environment, finance ministers from the ASEAN states should tap the growth potential of ASEAN integration. Increased economic growth, stronger budgets, and more resilient economies should be of paramount interest to them. These constitute the real economic promise of ASEAN, for both the organization and the citizens of its member states.