

Enhancing ASEAN Connectivity

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ASEAN leaders proclaimed to create an ASEAN Economic Community (AEC) by 2015. The AEC, along with two other pillars - the ASEAN Security Community and the ASEAN Socio-cultural Community – make up the ASEAN Community as declared in the Bali Concord II. The last five years have witnessed various steps taken to speed up and strengthen community building: (a) bringing forward the date for meeting goals of Vision 2020 to 2015, (b) ratifying the ASEAN Charter, (c) implementing the AEC Blueprint and (d) adopting blueprints for Socio-Cultural Community and Political -Security Community.

While the fundamentals for the single market are a work in progress, it is also crucial for ASEAN to facilitate the realisation of ASEAN community through “connectivity”. This is because community building through physical, institutional and personal connectivity is not only expected to reduce business transaction cost, time and travel cost, but is also expected to connect the “core” and the “periphery” in ASEAN, thus distributing the benefits of multi-faceted growth wider in the region and reducing the development divide in ASEAN.

Better connectivity is also expected to maintain ASEAN’s centrality in the evolving and dynamic regional architecture. ASEAN is situated at the heart of an economically vibrant and growing region bounded by India in the West; China, Japan and South Korea in the Northeast; and Australia and New Zealand in the South. Enhanced connectivity can potentially place ASEAN at the centre of growth and development.

Currently, the physical infrastructure, such as highway and rail networks, power grids, and gas pipelines, particularly in the less developed ASEAN countries, is characterised by structural weaknesses - low responsiveness to users, organisational inefficiencies, insufficient funding, and heavy dependence on official development assistance, low foreign direct investments, and lack of environmental awareness. Most ASEAN countries are also short of the ‘soft’ infrastructure (information and communication technology), which are important

prerequisites for the next stage of development. Hence, it is a crucial time for ASEAN to enhance regional connectivity.

During the 15th ASEAN Summit in Cha-am, Hua Hin, Thailand, the ASEAN leaders agreed to develop a Master Plan on ASEAN Connectivity. An ASEAN High Level Task Force was set up to develop the Master Plan, which, during the Hanoi Summit in October 2010, was adopted by the Leaders. The Master Plan on ASEAN Connectivity aims to provide a framework for regional cooperation on connectivity and a foundation for further connectivity with other regions, such as East Asia and South Asia.

Keeping these developments in mind, the ASEAN Studies Centre (ASC) at the Institute of Southeast Asian Studies (ISEAS), along with the Konrad Adenauer Stiftung (KAS) organised a roundtable discussion on May 5, 2011 at the Shangri-La Hotel, Singapore. The theme of the roundtable was: “Enhancing ASEAN Connectivity”, which examined the current state and gaps of infrastructure development across ASEAN. The roundtable gave some concrete policy recommendations and suggested approaches to resource mobilisation for this purpose.

Transportation

Road and Rail Infrastructure: The two flagship projects – the ASEAN Highway Network (AHN) and the Singapore-Kunming Rail Link (SKRL) – suffer from several missing links and substandard work quality. AHN is targeted for completion in 2015, while the completion of SKRL is likely to be extended to 2020. Once these links are built, it will connect both the mainland ASEAN and ASEAN with China and India.

Maritime Network: Although ASEAN has 47 designated ports, there are a number of challenges in providing an efficient shipping network service in the region. According to the UNCTAD Liner Shipping Connectivity Index, except for Singapore and Malaysia, ASEAN countries rank poorly relative to China and Hong Kong. Most of the gateway ports of the ASEAN Member States are “fairly full”, implying investment needs for capacity expansion.

Air Transport: The connectivity through air is the most developed in the region. The airports of ASEAN capital cities are sufficient in terms of runway lengths to accommodate the existing operation of aircraft. However, some of these airports still face problems in providing airport facilities, particularly warehouses.

Telecommunications

Mobile and Broadband Connectivity: In seven out of 10 ASEAN states, mobile connectivity is above 80 percent and in many cases, one person may own more than one mobile phone. On home broadband, Singapore, Brunei and Malaysia are the leading countries and one-third of the people are connected. However, real connectivity of the ASEAN people is much higher than the figure realised by regulators. This is because many people go to internet cafés or surf the internet from the office. Hence there is lot of opportunity for local companies to do business in the digital world. Although telecommunications is a very capital intensive industry, there are lot of benefits for an economy as it brings in foreign direct investment (FDI) and generates direct employment.

Currently there are several barriers in adopting broadband technology in ASEAN. It is not easy to build the hard infrastructure in some countries as there is poor electricity infrastructure or copper theft. Getting a license is often cumbersome and expensive. Mobile broadband is still a negative proposition for companies, as wireless networks require significant investment to support high mobile data traffic. ASEAN countries also suffer from the unavailability of good quality, affordable smartphones, which are prerequisites for mobile broadband connectivity.

Information and Communication Technology (ICT)

Internet penetration is at very different stages of development in the ASEAN member states. While Singapore and Malaysia have more than a 50 percent penetration rate, Laos and Cambodia are below two percent. This disparity shows that a large segment of the ASEAN population is not ‘connected’.

ASEAN is also challenged by the ICT divide between “youth” and “official” ASEAN. The youth of ASEAN are at the forefront of the global social network revolution. Indonesia is among the top five countries in Asia in terms of Facebook users. Against this, “official” ASEAN is still struggling with ICT. In the ASEAN ICT Master Plan 2010-2015, ASEAN ICT initiatives seem to be focused on infrastructure development. However, it should be noted that applications and capacity developments are an integral part of ICT development in the region. A failure to address these three aspects of ICT equally will lead to sub-optimal use of ICT for development.

Energy infrastructure

Under the ASEAN Connectivity initiative, there are two major energy infrastructure projects, the ASEAN Power Grid (APG) and the Trans-ASEAN Gas Pipeline (TAGP). APG is a flagship program mandated in 1997 by the ASEAN Leaders and aims to help member states to meet increasing demand for electricity and improve access to energy services. But there are several challenges. ASEAN countries are at different stages in the reform of their respective power markets. While at one end there is the vertically integrated power market with monopoly utility model (Brunei, Cambodia, Laos, Myanmar), at the other, there is the privatised/ market friendly model (Singapore, the Philippines). Again, there is a tremendous spread across electricity tariffs with Laos very cheap (US4.5 cents/ kWh) and Cambodia most expensive (US14.4 cents/ kWh). The difference is mainly due to various generation mixes that the countries draw their electricity from as well as installed capacity. Moreover, the countries are very different from each other in terms of legal and financial matters.

TAGP aims to develop a regional gas grid by 2020, by interconnecting existing and planned gas pipelines of member states and enabling gas to be transported across borders. The realisation of TAGP is expected to encounter substantial financial and legal complexities, most of which are easier to handle on bilateral basis rather than multilateral. One special challenge for TAGP is that the regional gas supply is dwindling. Countries like Indonesia and Malaysia, who were once significant LNG exporters, are now looking at ways to supply in their own countries. This is because, in recent times, there have not been any new discoveries of large gas fields.

Resource Mobilisation

To realise ASEAN connectivity, ASEAN needs huge resources and a lot of coordination among ASEAN stakeholders and dialogue partners.

Implementation Arrangement

The overall implementation plan of ASEAN connectivity will be overseen by the Connectivity Coordinating Committee (CCC). The CCC is expected to work closely with respective national coordinators for implementation and with relevant ASEAN sectoral bodies. ASEAN CCC is also expected to engage ASEAN stakeholders in this process through communication and exchange of information. As far as the ASEAN Secretariat is concerned, a separate secretariat unit will be established to support the CCC in coordinating and monitoring the process. It will also be responsible for connectivity progress reports from time-to-time.

For the coordination mechanism, various stakeholders will be involved i.e. the private sector, various sub-regional groups such as the Greater Mekong Subregion (GMS), the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EGA), dialogue partners, multilateral development banks etc.

Resource mobilisation

The Asian Development Bank (ADB) estimates that ASEAN countries will require infrastructure investment amounting to US\$596 billion during 2006-2015, with an average investment of US\$60 billion per year. Meeting this financing requirement will pose tremendous challenge in realising full ASEAN connectivity by 2015.

ASEAN is looking at both traditional and new ways of resource mobilisation. There are commitments for funding and loans from international institutions and several dialogue partners. The international community and international financial institutions are encouraged to actively contribute in the implementation of projects under ASEAN Connectivity. Member countries are also trying to increase the role of private sector participation in the physical

connectivity of ASEAN. Public-Private Partnership (PPP) is one of the key approaches for funding infrastructure projects.

One new way of generating funds is to set up a regional and domestic capital market. This is something ongoing such as establishing the Credit Guarantee Investment Facility (CGIF), which is a US\$700 million of trust fund among ASEAN +3 countries, managed by the ADB. The objective of CGIF is to support the issuance of local currency-denominated corporate bonds in Asia, so as to give financial support to regional companies for capital mobilisation. The first pilot project under CGIF will be started in 2011.

ASEAN member states along with the ADB are in the process of setting up the ASEAN Infrastructure Fund (AIF) by September 2011. A series of meetings since 2009 have settled issues like capital structure, governance and domicile of the AIF. Under capital structure, a total equity of US\$485 million has been decided, of which ASEAN will contribute US\$335 million and the rest by the ADB. There is also an arrangement for hybrid capital, which is a financial instrument of both debt and equity, and will be issued under the AIF (US\$162 million). Regarding governance issues, the AIF will be a corporate entity and there will be a board (Chair and members), who will take the key decisions of selection of projects and implementation. Malaysia will be the domicile of AIF and it will be administered by ADB on behalf of ASEAN member countries. While some indicative project pipelines (transport and energy) have already been listed by the ADB, it is subject to review by the member states.

ASEAN Connectivity with China and India

Enhanced physical connectivity in ASEAN is an instrument for better cooperation between the ASEAN region and China and India. Since the 2008 financial crisis, there have been some medium-term challenges for Asia-Pacific such as boosting demand within the region, complementing the sluggish demand and uncertain recovery in developed countries. This demand can be boosted in some regional countries by increasing the consumption of the poor and in others by increasing investment, especially in infrastructure. Exporting countries in ASEAN should be able to take advantage of this growing demand in the major regional countries – India and China.

However, for ASEAN, China and India should be seen in different ways:

First, in short to medium term, China is a potential net exporter to ASEAN and India is a potential net importer. In this limited sense, India's contribution to ASEAN's GDP will be higher. Second, transport connectivity with China can be comprehensive (road, rail, sea and air links) because of geophysical location of the ASEAN countries. Similarly, energy connectivity with China can be comprehensive (oil, gas, coal, electricity); while with India, oil and gas are likely to dominate in the near-term. ICT connectivity with China will be more infrastructure and hardware oriented, while with India, services will be more important. Third, there are not many differences for people-to-people connectivity or regional financial cooperation (although China's role will be more significant due to the size of its foreign reserve holdings). Lastly, a number of these trends will shift over the long term, e.g., China's growing middle class can create demand for ASEAN's services sector, and India's relative younger work force can play a larger role in ASEAN production systems.

Policy Recommendations

As infrastructure needs are not uniform in the region, harmonious infrastructure development is crucial. Governments have to identify the infrastructure gaps and then plug them accordingly. While the Master Plan has ascertained the stretches of road for regional connectivity, it has missed the smaller details. For example, it did not consider rural connectivity, which is essential to eliminate the rural-urban divide and to distribute the benefits of economic integration to all. Similarly, intra-country integration via gas and power grids can be as important as cross-border grid and pipeline interconnections.

The policies related to legal and regulatory frameworks should be harmonised and synergised among ASEAN member countries. For example, the legal and policy framework on cross-border power trading in ASEAN remains weak. Although Laos' electricity laws address cross-border power trading, they have insufficient and unclear provisions. Conversely, some countries like Malaysia, Thailand, and the Philippines do not have any existing laws or policies on cross-border power trading. Hence, the importance of "legal connectivity", i.e. being on the same page in terms of the existing legal frameworks, common specifications and standards in implementing the various components of the Master Plan, should be highlighted to each member country.

Private sector participation is a key component in the development of ASEAN connectivity. While Public-Private Partnership (PPP) has huge potential, it does not seem to be fully utilised at this point. PPPs bring together the best of the knowledge and expertise of the private sector, and the funds and institutional reach of the public sector. In this vein, it should be beneficial for ASEAN to involve more industrial heads and entrepreneurs during project and financial decision making processes under ASEAN connectivity.

It should also be noted that the investment needs of ASEAN such as physical infrastructure have to be translated into commercially viable projects for private investors to take an interest. In this regard, there has to be a higher quality of information on investment opportunities in the ASEAN countries that are made available to the public. In addition, governments must create an enabling environment that assures investors of predictability, a level playing field, low transaction costs and fair rates of return commensurate with the risks they take.

Finally ASEAN must ensure good governance. The regulatory framework has to be strengthened to make sure that capital is used appropriately for infrastructure development.

Sector-specific recommendations:

ASEAN countries must cooperate on both national and regional levels. While ASEAN has made a good start with cross border projects, like the ASEAN Highway Network, and the Singapore-Kunming Rail Link, it has to continue and expand effective cooperation at all levels of government and with multiple stakeholders (central government, local government, the private sector, and civil society). The member countries with the means, expertise and technology should assist the countries who do not have these resources.

As ASEAN is endowed with approx 51,000 kilometres of navigable inland waterways, waterways transport has enormous potential in reducing freight costs in ASEAN. But the current utilisation rate is very low due to the underdeveloped waterways network, poor river ports and facilities, and poor inter-port connectivity. These infrastructure issues

need to be addressed, together with improving rules and governance for managing the connected inland waterway transport systems.

ASEAN is not able to turn the demand for the internet into companies that can take benefit from it. Currently, Google takes the lion's share of the search market in ASEAN countries. ASEAN needs to create local champions in the digital industry. In doing so, the public sector can co-invest to encourage private investment in telecom infrastructure. Governments can increase internet connectivity by pushing more e-services and connecting educational institutions. It must realise that for rural areas with moderate throughput, mobile broadband is the only affordable solution.

As ASEAN faces the challenge of evolving into a more institutionalised organisation, ICT can help ASEAN achieve this goal more effectively. ASEAN can adopt appropriate and cost efficient conferencing software to be used by various ASEAN bodies or at meetings. ASEAN, through the Secretariat, can also develop appropriate eParticipation tools to enhance the engagement with all ASEAN stakeholders.

Regarding energy infrastructure, reducing power and gas subsidies is critical for many ASEAN countries. It is important to capture economic benefits from market-based pricing in key natural resources, infrastructure and energy sectors. Market oriented reforms are necessary to ensure fiscal stability in countries which subsidise gas and power, to alleviate shortages of natural gas for domestic demand and to maintain a stable policy environment for private sector investments, which require predictability and transparency. While this is a difficult task as it may hurt constituencies, countries need to move from subsidies to appropriate social safety nets. Flexibility is one of the important criteria for energy security for example exercising small scale LNG options where viable, exposure to spot and short term LNG contracts form part of a broader supply portfolio.

Concluding Remarks

The ASEAN Connectivity Master Plan is one of the important solutions to the problems obstructing the process of ASEAN community building by 2015. Road, rail, water

and aviation corridors are indeed the most visible face of connectivity due to their importance for the movement of goods and people. However, given the ubiquitous role of the internet and mobile telephony in business and other economic and social development, it is crucial to promote the utilisation of ICT. The absence of such linkages will threaten to accentuate the already existing gaps between different countries both within ASEAN and around the world. Finally, integrated power grids and gas pipelines for ASEAN countries are also important as they aim to improve energy efficiency and develop indigenous energy resources.

Enhanced ASEAN connectivity is a means to reduce development gaps in ASEAN, thus helping the less developed countries reap the benefits of integration in parallel to their more advanced counterparts. It is also to raise the competitiveness of the ASEAN region with the rest of the world and participate more effectively in the production network that is developing in the eastern part of the world.

In the next few years, what is needed is for the multiple ASEAN stakeholders to work together with various sources of funding. Besides, the investment and technology, what is also crucial is good governance as all this together will finally lead to rise in flows and volumes of goods, services, people and information across the ASEAN region.