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RESEARCHERS AT SINGAPORE'S *INSTITUTE OF SOUTHEAST ASIAN STUDIES* SHARE THEIR UNDERSTANDING OF CURRENT EVENTS

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## **Goods to Flow Slow and Steady within the ASEAN Economic Community**

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### EXECUTIVE SUMMARY

- The idea of a 'single market and production base' in the ASEAN Economic Community (AEC) is to provide ASEAN consumers with more choices of goods at lower prices and offer regional producers more space for production activities.
- ASEAN Member Countries (AMCs) have made progress in reducing average tariffs to less than one percent for regional trade. Indeed, the tariff-related AEC deadlines were met in 2012, when 99.1 per cent of the tariff lines of the ASEAN-6 carried zero per cent duty.
- However, issues remain over the utilisation rate of Common Effective Preferential Tariff (CEPT) preferences. In 2005-2010, this rate ranged from a low of 0.5 per cent for Myanmar to a modest 22.6 per cent for Thailand and a high of 47 per cent for the Philippines.
- In addition, while tariffs have come down, non-tariff barriers (NTBs) continue to prevail in the region. The industries most affected by NTBs are

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the chemical, machinery, and electrical sectors. These barriers, both at the border and behind-the-border, are used as policy tools by AMCs to protect domestic interest groups. NTBs are most prevalent in Indonesia, followed by Vietnam. The ineffectiveness of NTB reform can be attributed to ASEAN's way of dealing with the issue – voluntary declaration and the absence of mechanisms of verification.

- As a whole, AMCs have collectively benefitted, albeit in a limited way, from its action of tariff reduction and regular discussions on NTBs. In addition, AMCs' 'open regionalism' has helped integration by creating trade rather than diverting it. As such, ASEAN's economic regionalism is viewed as a 'building block' rather than a 'stumbling block' towards the multilateral world trading system.
- Going forward, key policy recommendations are: generating and maintaining political will for economic integration; generating greater awareness about the pervasiveness and impact of NTBs; streamlining NTBs and harmonising them with existing international databases; increasing public AMC outreach activities with respect to AEC and its benefits; and pushing for domestic reforms in smaller economies such as Cambodia, Laos, Myanmar, and Vietnam.

## INTRODUCTION

ASEAN member countries (AMCs) have made considerable progress towards economic integration since they decided to create an ASEAN Free Trade Area (AFTA) in 1992. Building on this base, they progressively launched other initiatives like the ASEAN Investment Area and the ASEAN Framework Agreement on Services. The process soon became wider in scope with the aim to create an ASEAN Economic Community (AEC). This is because, in its bid to make the region more globally competitive, ASEAN was no longer solely geared towards increasing intra-regional trade and investment, but was also concerned about reducing transaction costs, building soft infrastructure, lowering poverty, and pursuing economic development on a sustainable basis. At its core, AMCs have continued to maintain an outward-looking policy of 'open regionalism'.

In October 2003, as ASEAN Leaders elaborated on their initiative of AEC, the goals were laid out as below:

The ASEAN Economic Community is the realisation of the end-goal of economic integration as outlined in the ASEAN Vision 2020, to create a stable, prosperous and highly competitive ASEAN economic region in which there is a free flow of goods, services, investment and a freer flow of capital, equitable economic development and reduced poverty and socio-economic disparities in year 2020...The ASEAN Economic Community shall establish ASEAN as a single market and production base, turning the diversity that characterises the region into opportunities for business complementation making the ASEAN a more dynamic and stronger segment of the global supply chain.

The target implementation date for the AEC was subsequently brought forward to 2015. In November 2007, AMCs endorsed the AEC Blueprint that outlined specific strategies, actions and timelines needed to create the Economic Community.<sup>2</sup> A Scorecard was developed to track the implementation of measures and achievement of milestones committed in the AEC Strategic Schedule. As announced at the 22<sup>nd</sup> ASEAN Summit in April 2013, 77.5 per cent of the measures in the AEC Blueprint have been implemented by the AMCs<sup>3</sup>. Despite such a noteworthy number, analysts and researchers have reservations regarding the feasibility of full and effective ASEAN regional economic integration<sup>4</sup>.

This ISEAS Perspective examines the *free flow of goods* aspect of the AEC

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<sup>2</sup> AEC is one of three pillars in the process of development of an 'ASEAN Community'. The other two pillars are ASEAN Political-Security Community and ASEAN Socio-Cultural Community.

<sup>3</sup> A more updated figure is 81.7 per cent as of December 2013, though this is not publically announced during the 24<sup>th</sup> ASEAN Summit of May 2014.

<sup>4</sup> Severino, Rodolfo and Jayant Menon. (2013). 'Overview' in Sanchita Basu Das, Jayant Menon, Omkar L. Shrestha and Rodolfo Severino (Eds.), *The ASEAN Economic Community: A Work in Progress*, Singapore: ISEAS, pp. 1-30.

Blueprint—which comes under the first pillar of the Blueprint in transforming the region into a “single market and production base”<sup>5</sup> and, in particular, assesses the progress made to remove tariff and the non-tariff barriers (NTBs). In doing so, it analyses the gains available to AMCs and suggests what the AMCs should bear in mind in the future.

## THE IDEA OF A ‘SINGLE MARKET AND PRODUCTION BASE’

The single market and production base is expected to provide ASEAN consumers with more choices of goods at lower prices and offer regional producers an expanded space so that they can undertake production activities seamlessly over national boundaries<sup>6</sup>. Economies of scale and other efficiencies have also been used as justification for an integrated region characterised by varied comparative advantage of member economies. The pursuit of these benefits were particularly relevant to AMCs since the 1980s when international trade became increasingly driven by the development of cross-border production networks with each country specialising in a particular stage of the production sequence<sup>7</sup>. To reap the benefits of a single market, ASEAN must enhance its collective capacity to not only participate in the global supply chain of production but also strive to become a hub for such a production network in Asia.

However, the barriers to trade and investment have to be removed to create such a market space. This prompted ASEAN governments to agree on the AFTA and, subsequently, the AEC by 2015. To support AFTA’s objective of creating an internal market and making the region competitive for foreign direct investment (FDI), the agreement was supplemented with other measures such as free flow of services and investment, development of a regional competition policy, regional cooperation on the protection of intellectual property rights, and infrastructure development.

### *The Goal of the Free Flow of Goods in AEC*

To be sure, the lineage of a unified ASEAN market and production base via a free flow of goods can be traced back to 1992 with the signing of the Agreement on the Common Effective Preferential Tariff Scheme (CEPT) under AFTA. The scheme included a schedule of preferential tariff reductions which was to be implemented progressively<sup>8</sup>. In 2003, leaders decided to eliminate import duties to

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<sup>5</sup> The first pillar of ‘single market and production base’ also includes free flow of services, free flow of investment, freer flow of capital, free flow of skilled labour, priority integration sectors and food, agriculture and forestry

<sup>6</sup> Soesastro, Hadi. (2008). ‘Implementing the ASEAN Economic Community Blueprint’, in *The ASEAN Community: Unblocking the Roadblocks*, ASEAN Studies Centre, Report No. 1, ISEAS.

<sup>7</sup> Athukorala, Prema-chandra and Yamashita, Nobuaki. (2006). ‘Production fragmentation and trade integration: East Asia in a global context’, *North American Journal of Economics and Finance*, 17(3): 233–256.

<sup>8</sup> CEPT-AFTA consisted of five classes: Inclusion List (IL) required AMCs to reduce tariffs to 0-5

deepen the integration further. While the ASEAN-6<sup>9</sup> countries had a deadline of 2010 to reduce their intra-ASEAN tariffs to zero, the CLMV (Cambodia, Laos, Myanmar and Vietnam)<sup>10</sup> countries were given a longer time frame until 2018 to meet this target, with the flexibility of seven per cent of their tariff lines. In 2009, the AMCs adopted a more holistic approach to ensure the free flow of goods in the region. They signed the ASEAN Trade in Goods Agreement (ATIGA) that consolidated and streamlined all provisions in CEPT-AFTA and other protocols related to trade in goods into one single legal instrument<sup>11</sup>. It entered into force in 2010 and superseded CEPT-AFTA.

Besides tariff elimination, AMCs are expected to undertake the following measures to eliminate the NTBs that impede smooth flow of merchandise trade in the region: (a) to enhance transparency by abiding to the protocol on Notification Procedure and setting up an effective Surveillance Mechanism; (b) to abide by the commitment of a standstill and roll-back on NTBs; (c) to remove all NTBs by 2010 for the ASEAN-5 countries, by 2012 for the Philippines and by 2015 with flexibilities to 2018 for CLMV; (d) to enhance transparency of non-tariff measures (NTMs); and (e) to work where possible towards having regional rules and regulations consistent with international best practices.

## TOWARDS FREE FLOW OF GOODS

### *Intra-ASEAN AFTA Tariffs*

ASEAN's pursuit of the AEC has shown measurable advancement in encouraging member countries to participate in the regional and global trade in goods. The member economies have made commendable progress by reducing average tariffs to less than one per cent for regional trade (Figure 1). The ASEAN-6 countries have eliminated tariffs since 2010 as scheduled under the ATIGA<sup>12</sup>. Tariffs on agriculture goods (especially for Indonesia, Malaysia, the Philippines and Thailand) are maintained at 0-5 per cent, again as recommended in ATIGA<sup>13</sup>. For CLMV countries, the average CEPT tariff declined from 7.3 per cent in 2000 to 1.8 per cent in 2013.

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percent by 2000 and 2003; Temporary Exclusion List (TEL) were expected to be phased into the IL by 2000 for most manufactured products, and by 2003 for unprocessed agricultural products. Sensitive List (SL) goods constituted unprocessed agricultural products while Highly Sensitive List (HSL) constituted rice and it was granted a more flexible arrangement for phasing into the Inclusion List. Finally, General Exceptions (GE) products were permanently excluded from the agreement.

<sup>9</sup> ASEAN-6 countries include Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand

<sup>10</sup> CLMV countries, also known as newer members, constitute Cambodia, Laos, Myanmar and Vietnam

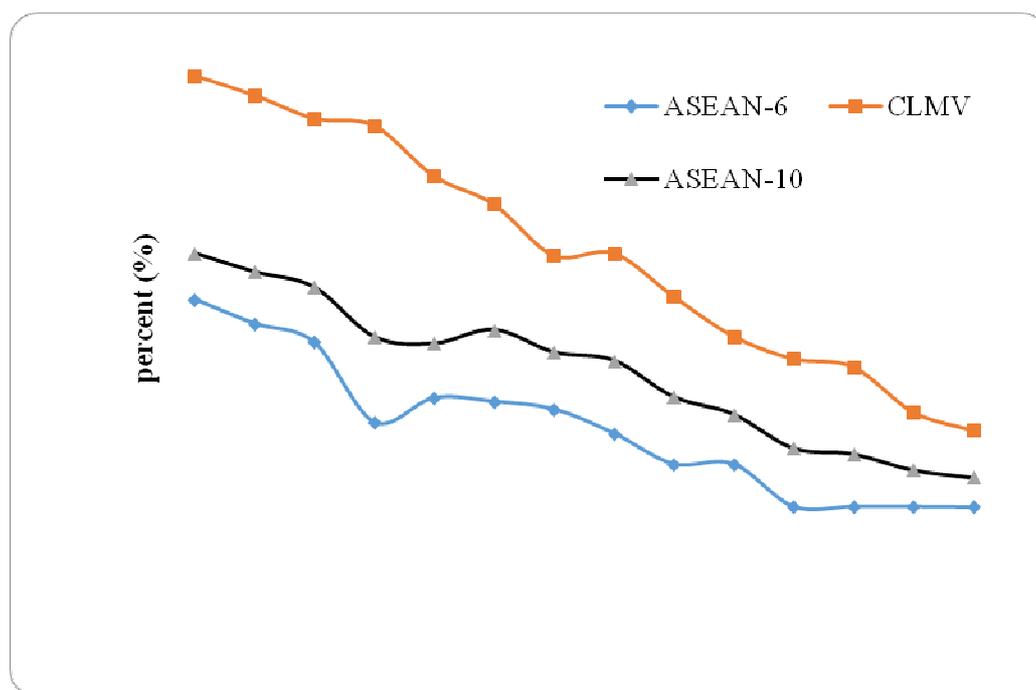
<sup>11</sup> ASEAN Secretariat. ASEAN Trade in Goods Agreement. 2011a.

<sup>12</sup> Singapore and Brunei have completely eliminated their tariff protection on intra-ASEAN trade.

<sup>13</sup> The ASEAN-6 countries' simple average CEPT tariff is around 0.05 per cent that compares well with other FTAs like the North American Free Trade Area (NAFTA), whose average tariff is approximately 0.03 per cent.

Looking at the share with zero percent duty, 99.1 per cent of ASEAN-6 tariff lines were duty-free as of May 2012, thus meeting the AEC 2015 tariff-related targets (Table 1). For CLMV countries, the share stood at 67.6 per cent.

**Figure 1: Intra-ASEAN Preferential Tariffs (Average CEPT Rates), 2000-2013**



Source: Author's compilation from ASEAN Secretariat Statistical Database

**Table 1: Share of Tariff Lines at Zero Per Cent CEPT Preferential Duty**

	% Share in 2012			2012 ATIGA Schedule
	0% duty	>0% duty	Other	
Brunei	99.07		0.93	99.1
Indonesia	98.72	0.18	1.10	98.7
Malaysia	98.69	0.54	0.78	98.7
Philippines	98.63	1.06	0.31	98.6
Singapore	100.0		0.00	100.0
Thailand	99.84	0.16	0.00	99.8
<b>ASEAN-6</b>	<b>99.11</b>	<b>0.35</b>	<b>0.54</b>	<b>99.16</b>
Cambodia	40.29	59.71	0.00	93.0
Laos	78.87	21.13	0.00	93.0
Myanmar	79.42	19.87	0.71	93.0
Vietnam	71.75	26.22	2.04	93.0
<b>CLMV</b>	<b>67.58</b>	<b>31.73</b>	<b>0.39</b>	<b>93.00</b>
<b>ASEAN</b>	<b>87.24</b>	<b>12.17</b>	<b>0.60</b>	<b>96.70</b>

Source: ASEAN Secretariat (as of May 2012)

Despite these achievements, the low utilisation rate of the CEPT preferences (Table 2) remains an issue. This is with regard to the operational procedures on the issuance and verification of the Certificate of Origin (CEPT Form D).<sup>14</sup> While the value of imports using CEPT Form D increased from US\$9.2 billion to US\$26 billion during 2005-2010, the preference utilization rate ranged from a low of 0.5 per cent for Myanmar to a modest 22.6 per cent for Thailand and a high of 47 per cent for the Philippines. It also appears that the utilisation rate for each AMC varies depending on its ASEAN partner country<sup>15</sup>.

**Table 2: ATIGA Preference Utilization (Usage of CEPT Form D)**

	2005	2006	2007	2008	2009	2010
Brunei	0.9	1.3	--	2.6	--	3.3
Indonesia	3.0	--	0.3	--	--	19.0
Malaysia	5.4	2.7	3.5	--	12.5	11.1
Philippines	19.5	18.2	20.6	--	38.6	41.2
Thailand	16.4	12.3	12.2	8.3	15.2	22.6
Cambodia	--	--	--	--	--	47.1
Laos	--	--	--	2.6	2.8	3.4
Myanmar	--	0.3	0.34	0.34	0.37	0.5
Vietnam	8.8	19.1	10.7	9.9	16.1	13.4

Source: ASEAN Secretariat and the World Bank, 2013

There could be two key reasons for this. First, importers may not find it cost-effective to comply with the CEPT-ATIGA's Rules of Origin (ROO) even though ASEAN has a simple ROO requirement of minimum regional value-added (RVA) of 40 per cent or a change in tariff classification at the 4-digit level.<sup>16</sup> Second, low most-favoured-nation (MFN) status tariffs offered little incentive for ASEAN members to use the CEPT preferential rates. While the average preference margins between MFN and CEPT tariffs are four to six per cent for the ASEAN-5 countries, it is three to seven per cent for CLMV countries. It has been observed that, since 2000, AMCs have simultaneously lowered their MFN and CEPT tariffs. Other than Singapore which has zero MFN tariffs, during 2000-2011, the ASEAN-5 countries lowered their applied MFN tariffs from 9.1 per cent to 6.4 per cent.

<sup>14</sup> Form D: The exporter must obtain a 'Form D' certification from its national government attesting that the good has met the 40 per cent requirement of Rules-of-Origin. The Form D must be presented to the customs authority of the importing government to qualify for the CEPT rate.

<sup>15</sup> For example, in 2010, in the case of Indonesian imports, CEPT utilisation rate was 56 per cent from Thailand, 20.6 per cent from Laos, 33 per cent from the Philippines, 19 per cent from Malaysia, 10 per cent from Cambodia, 4.9 per cent from Singapore and 86.2 per cent from Myanmar.

<sup>16</sup> The Harmonised System of Classification categorises products into Chapters (2-digit), headings, (4-digit) and sub-headings (6-digit). A Chapter change would require a change at the 2-digit level, a heading change, at the 4-digit level, and a sub-heading change, at the 6-digit level. The focus is on the transformation of the imported inputs into the finished product. A substantial transformation is expected to have occurred if there is a change in tariff classification.

Among the CLMV group, Cambodia and Vietnam reduced their MFN rates from 16 to 14.2 and 9.8 per cent, respectively, over the same period with their accession to the WTO. Surveys conducted by the Asian Development Bank Institute (ADBI)<sup>17</sup> and ADB-ISEAS<sup>18</sup> have also attributed the low utilisation of AFTA tariffs to the lack of information, low margin of preference, the prevalence of NTBs, as well as the cost effectiveness of ROOs and its related administrative procedures.

### *Non-tariff Barriers*

In contrast to the progress made on tariff reduction, NTBs—both on imports<sup>19</sup> and exports<sup>20</sup>—continue to prevail in the ASEAN region and appear to have replaced tariffs as measures to protect domestic industries<sup>21</sup>. This is not unusual given the ongoing rising uncertainties in the global economy since the 2008 crisis. Hence, the bigger challenge for raising intra-ASEAN trade lies in eliminating diverse and abundant non-tariff measures (NTMs)<sup>22</sup> that, though set in line with domestic policy objectives, have the potential to discriminate against imports or foreign firms.

ASEAN has detailed several measures to eliminate NTBs such as: elimination of import surcharges, mutual recognition or harmonisation of product standards, adoption of pro-competition policies, introduction of market access measures, and elimination of quantitative restrictions. However, the effectiveness of such NTB reforms is very much open to question and the lack of success can be attributed to ASEAN's way of dealing with the issue: while AMCs have to voluntarily declare their list of NTMs (both trade restrictive ones and not) that will form part of the ASEAN Trade Repository System, there is no mechanism for verification<sup>23</sup>. Moreover, there is no common definition or understanding of NTBs that arise from the NTMs which have evolved over time in response to political imperatives of

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<sup>17</sup> Kawai, M. and G. Wignaraja (ed.), *Asia's Free Trade Agreements: How is Business Responding?* Asian Development Bank, the ADB Institute with Edward Elgar Publishing, 2011

<sup>18</sup> Hu, Albert G. (2013), 'ASEAN Economic Community Business Survey', in Sanchita Basu Das, Jayant Menon, Omkar L. Shrestha and Rodolfo Severino (Eds.), *The ASEAN Economic Community: A Work in Progress*, Singapore: ISEAS, pp. 442-481.

<sup>19</sup> Import restrictions have been adopted to meet objectives of public health, infant industry protection or consumer health.

<sup>20</sup> Most AMCs need export licensing (except for the Philippines) or impose export taxes (except for Brunei, the Philippines and Singapore) for selected products, including on intra-ASEAN trade.

<sup>21</sup> World Bank. *A Survey of Non-Tariff Measures in the East Asia and Pacific Region*. Washington DC: World Bank, 2008.

<sup>22</sup> Often, the terms NTMs and NTBs (core NTMs) are used interchangeably. However, a distinction can be made. Conceptually, NTMs are behind-the-border measures that arise from government regulatory policies, procedures and administrative requirements which are imposed to serve a particular national purpose (like safety, environmental or social). They have the potential to become barriers to trade, i.e. NTBs.

<sup>23</sup> The ASEAN NTM Database is available at (<http://www.asean.org/communities/asean-economic-community/item/non-tariff-measures-database>)

particular member states<sup>24</sup>. Each of the member economies has to develop their own work programme to eliminate their trade-restricting NTMs (or NTBs). More recently, ASEAN is working with its automotive, electronics and textile industry groups to determine the NTMs that are raising the cost of their business, thereby exploring ways to reduce their trade-restricting effect. So far little progress has been made in eliminating NTBs from intra-ASEAN trade. Other than removing a few NTBs offered by Malaysia and Thailand, ASEAN has adopted a mutual recognition agreement (MRA) on cosmetics.

Some observations can be made on the nature and characteristics of NTBs in ASEAN. First, NTBs are most prevalent in Indonesia with 48 measures affecting 388 tariff lines, followed by Vietnam with 15 measures affecting 927 tariff lines (Table 3). Second, NTBs, both at the border<sup>25</sup> and behind-the-border<sup>26</sup>, are used as policy tools by AMCs (Figure 2).

**Table 3: Non-tariff Measures by Type**

	Indonesia	Malaysia	Philippines	Singapore	Thailand	Vietnam
Total number of measures	57	8	11	7	18	26
Number of measures classified (green)	9	2	7	0	9	11
Number of measures in database classified (amber)	18	3	3	3	5	0
Number of measures in database classified (red)	30	3	1	4	4	15
Number of tariff lines affected by red measures	388	29	1	0	28	927

Notes: the criteria for identifying NTBs were established by the 19<sup>th</sup> AFTA Council on 27 September 2005 as: Green – indicates the measure is either: a) Announced and involves liberalisation on a non-discriminatory (i.e. MFN) basis; or b) The measure has been implemented and is found (upon investigation) not to be discriminatory; or c) The measure has been implemented, involves no further discrimination, and improves the transparency of a jurisdiction’s trade-related policies. Red – indicates the measure is implemented and almost certainly discriminates against commercial interests. Amber – indicates the measure is either: a) Implemented and may involve discrimination against foreign commercial interests; OR b)

<sup>24</sup> Austria, Myrna. (2013). ‘Non-tariff Barriers: A Challenge to Achieving the ASEAN Economic Community’, in Sanchita Basu Das, Jayant Menon, Omkar L. Shrestha and Rodolfo Severino (Eds.), *The ASEAN Economic Community: A Work in Progress*, Singapore: ISEAS, pp. 31-94

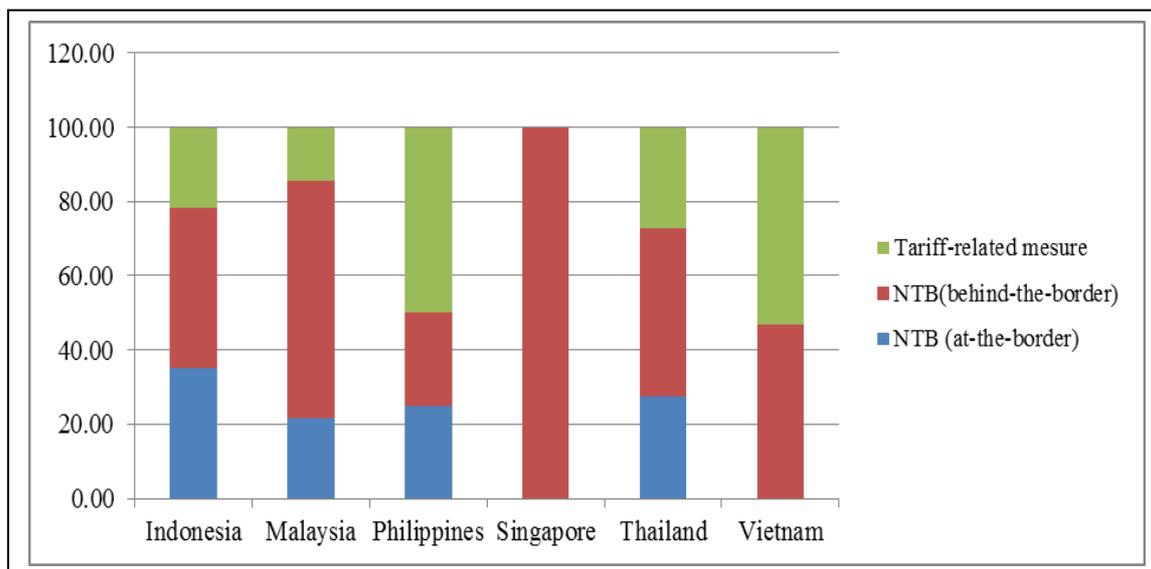
<sup>25</sup> NTBs at the border include import bans, import subsidies, non-automatic import licensing, new procedures for importation, additional requirements for importation, quotas, sanitary and phytosanitary measures, and technical barriers to trade.

<sup>26</sup> NTBs behind the border include state aid measures, public procurement requirements, trade finance, export taxes and restrictions and investment measures

Announced or under consideration and would (if implemented) almost certainly involve discrimination against foreign interests.

Source: Austria, Myrna (2013) (calculated using [www.globaltradealeert.org](http://www.globaltradealeert.org), downloaded 10 March 2012)

**Figure 2: Discriminatory Non-tariff Measures**



Source: Austria, Myrna (2013) (calculated using [www.globaltradealeert.org](http://www.globaltradealeert.org))

Third, the most common NTMs are non-automatic licensing and technical regulations and quality standards (both at 31.8 per cent of total ASEAN NTMs; see Table 4). Fourth, chemical and allied industries account for 20.9 per cent of the total NTMs, followed by the machinery and electrical industry with 17.9 per cent (Table 4).

**Table 4: NTMs in ASEAN**

By type	Percent of the total NTMs	By Industry	Percent of the total NTMs
Tariff Rate Quotas	0.6	Transportation	6.5
Internal Taxes and Charges	1.7	Machinery/ Electrical	17.9
Automatic Licensing	7.1	Metals	5.4
Discretionary Import Licensing	1.3	Stone/ Glass	0.9
Import ban on certain goods	0.0	Footwear/ Headgear	0.3
Non-automatic licensing	31.8	Textiles	5.8
Quota	0.7	Wood & wood products	2.5

<b>By type</b>	<b>Percent of the total NTMs</b>	<b>By Industry</b>	<b>Percent of the total NTMs</b>
Prohibition	21.4	Raw hides, skins, Leather and Fur	0.4
Selective approval importers	0.8	Plastics/ Rubber	1.7
State Trading Administration	1.4	Chemical & allied Industries	20.9
Import ban due to hazardous components	0.0	Mineral Products	2.6
Technical Regulation – Quality Standards	31.8	Foodstuffs	12.2
Technical Regulation – Preshipment inspection	0.9	Vegetable products	11.1
Technical measures	0.4	Animal & animal products	7.1
		Miscellaneous	4.8

Source: ASEAN Integration Monitoring Report, ASEC and WB<sup>27</sup>

## GAINS FOR ASEAN MEMBER COUNTRIES

As a whole, AMCs have collectively benefitted, albeit in a limited way, from its action of tariff reduction and regular discussions on NTBs<sup>28</sup>. The intra-ASEAN trade share has gradually increased from 19 per cent in 1993 to 22 per cent in 2000; it rose further to 26 per cent in 2008, and has remained at around 24 per cent in the last two years. The share of intra-ASEAN trade has also gone up for the Philippines, Indonesia and Cambodia, but this has been offset by a reduced share for Brunei, Singapore and Myanmar (Table 5). Among the industries, a rising intra-ASEAN trade share in motor vehicles, soaps, lubricants, essential oils, perfumes and cosmetics has been equalized by declining shares in ASEAN's key export sectors like electrical machinery, equipment and parts<sup>29</sup>.

<sup>27</sup> ASEAN Integration Monitoring Report (AIMR), The ASEAN Secretariat and the World Bank, 2013

<sup>28</sup> Economic Research Institute for ASEAN and East Asia (ERIA), 2012, *Mid-term Review of the ASEAN Economic Community Blueprint* and AIMR (2013)

<sup>29</sup> According to ERIA's mid-term review of AEC, the decline in intra-ASEAN trade share of ASEAN's top ten exports is due to the rise of China at the centre of the electronics and electrical equipment production networks in East Asia.

**Table 5: Share of Intra-ASEAN Trade as a Percentage of Total Trade**

	1993	1996	2000	2005	2010	2012
ASEAN-10	19.2	21.5	22.0	25.7	25.4	24.3
Brunei	-	47.6	36.3	28.8	20.6	19.8
Indonesia	11.8	13.8	18.5	23.1	27.4	25.1
Malaysia	24.1	25.0	22.7	25.8	26.2	27.4
Philippines	9.2	14.6	15.7	18.1	25.4	21.1
Singapore	23.3	25.7	26.0	28.9	27.2	26.6
Thailand	13.8	17.0	17.4	20.0	22.5	20.9
Cambodia	-	-	22.6	19.8	22.8	27.6
Laos	-	-	-	58.2	57.1	37.9
Myanmar	-	-	44.1	87.7	48.6	39.3
Vietnam	-	-	-	22.8	17.0	16.8

Source: author's calculation, ASEAN Secretariat Statistics Publications (various issues)

Another indicator for ASEAN's progress towards increased cooperation is intra-ASEAN merchandise trade openness (i.e. intra-ASEAN imports as a share of GDP). During the pre-crisis years of 1997 and 2008, the simple average value of this indicator peaked at 22 per cent and 16 per cent respectively for ASEAN-10, after which it fell to hover around 14-16 per cent.

**Table 6: Intra-ASEAN Merchandise Trade Openness**

	1993	1996	2000	2005	2010	2012
Brunei	22	55	12	8	10	10
Indonesia	--	--	5	6	7	6
Malaysia	13	15	18	21	18	18
Philippines	3	5	7	9	8	6
Singapore	31	30	36	42	35	29
Thailand	5	5	8	12	13	12
<b>ASEAN-6</b>	<b>11</b>	<b>22</b>	<b>14</b>	<b>16</b>	<b>15</b>	<b>13</b>
Cambodia	--	--	15	16	15	29
Laos	--	--	--	13	21	13
Myanmar	--	--	12	8	5	5
Vietnam	--	--	--	17	15	15
<b>ASEAN-4</b>	<b>--</b>	<b>--</b>	<b>--</b>	<b>14</b>	<b>14</b>	<b>16</b>
<b>ASEAN-10</b>	<b>13</b>	<b>22</b>	<b>13</b>	<b>16</b>	<b>13</b>	<b>12</b>

Source: author's calculation, ASEAN Secretariat Statistics Publications (various issues)

A relative measure of trade, the intra-regional trade intensity index (TII)<sup>30</sup>—though it shows a declining trend for ASEAN from 3.8 in 1990 to 3.6 in 2012—remains higher than that for the European Union which was at 2.0 in 2012 (Table 7). This

<sup>30</sup> Intra-regional trade intensity index is the ratio of intra-regional trade share to the share of world trade with the region. An index of more than one indicates that the trade flow within the region is larger than expected given the importance of the region in world trade.

implies that ASEAN trades relatively more within its region when compared to the EU. It should also be noted that ASEAN's declining trend of intra-regional TII is matched by a rising trend of TII with China, which may indicate that ASEAN's efforts with regard to AFTA are being carried out simultaneously with ASEAN-China FTA.

**Table 7: Intra-regional Trade Intensity Index**

	1993	1996	2000	2005	2010	2012
ASEAN-10	3.29	3.12	3.71	4.26	3.72	3.59
European Union	1.61	1.62	1.73	1.67	1.93	2.04

Source: ADB-ARIC website (<http://aric.adb.org/integrationindicators>)

**Table 8: Trade Intensity Index of ASEAN with East Asian Countries**

	1993	1996	2000	2005	2010	2012
China	0.71	0.78	0.94	1.23	1.20	1.27
Japan	2.52	2.54	2.45	2.35	2.34	2.36
South Korea	1.87	1.80	1.69	1.64	1.76	1.81

Source: ADB-ARIC website (<http://aric.adb.org/integrationindicators>)

Other AEC studies have used the Computable General Equilibrium (CGE)<sup>31</sup> modelling to evaluate the effect of trade policy. One such study analysed the key AEC blueprint initiatives<sup>32</sup> and concluded that “AEC could yield benefits amounting to 5.3 per cent of the region’s GDP and more than twice of that if the AEC leads to FTAs with key external partners.”<sup>33</sup>

## CONCLUSION AND POLICY RECOMMENDATIONS

Although the deadline of 2015 for AEC is fast approaching, ASEAN is not yet a ‘single market and production base’. While the member countries have achieved their goal of progressive tariff reduction or elimination, much more needs to be done as discrimination against imported goods continues to persist with ‘at the border’ and ‘beyond the border’ NTBs. The elimination of NTBs needs strong political will. The increased level of global uncertainties, diverse country

<sup>31</sup> CGE models provide an empirical foundation to trade policies that can quantify the magnitude of the effects identified in the theory of net welfare gain from trade creation and trade diversion.

<sup>32</sup> Key AEC Blueprint initiatives include tariff, NTBs, liberalisation of services trade and investment and trade facilitation measures

<sup>33</sup> Petri, Peter. A, Plummer, Michael and Zhai, Fan (2012) ‘The ASEAN Economic Community: A General Equilibrium Analysis’, *Asian Economic Journal*, 26(2): 93-118

development stages and economic structures are prohibiting AMCs from removing their protectionist NTMs.

Nevertheless, the integration indicators (i.e., trade share, openness, intensity index) remain positive. It was also noted that the lower ASEAN tariff has encouraged member countries to reduce their tariffs with partners outside the region<sup>34</sup>. While this could have partially limited the share of intra-ASEAN trade to around 25 per cent, it did not significantly divert trade away from non-ASEAN partners. AMCs' approach of 'open regionalism' helped the region through a trade creation effect rather than a trade diversion effect<sup>35</sup>. As such, ASEAN's economic regionalism should be viewed as a 'building block' rather than a 'stumbling block' in the multilateral world trading system.

Given that this is only a beginning and AMCs will have to continue with their efforts at economic integration, ASEAN policy makers need to be reminded of the following:

- Integration is a continual process and takes time and political commitment<sup>36</sup>. In times of global economic uncertainties, though protectionism in the form of NTMs could be tempting, it would be harmful for the current economic imperatives of regional production networks. Most often, protectionism leads to the erosion of domestic export competitiveness. Economic cooperation is one of the best hedging strategies for sustainable growth and development in the future.
- AMCs should bring their policy makers and private sector together more regularly and all tradable goods sectors should work towards a common understanding and definition of NTBs. It is the businessmen on the ground who can identify the NTBs among the NTMs that are restraining them from recognising the ten AMCs as a single production base. To quicken the process of identification, one easy way is to subject all prevailing NTMs to a review process so as to ensure that they are transparent, non-discriminatory, and do minimise trade restrictiveness.

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<sup>34</sup> Calvo-Pardo, Hector; Caroline Freund and Emanuel Ornelas. (2009). 'The ASEAN Free Trade Agreement: Impact on Trade Flows and External Trade Barriers', *Policy Research Working Paper No. 4960*, The World Bank.

<sup>35</sup> Trade creation is the phenomenon of displacing the less efficient domestic production with more efficient partner country production. This leads to economic gain as now the country's resources are more efficiently utilised. However, it is also possible that preferential treatment is extended to a partner country that replaces a more efficient non-FTA partner. In that case, there will be trade diversion: the importing country is using a less efficiently produced import. Viner, J. (1950) *The Customs Union Issue*, New York: Carnegie Endowment for International Peace

<sup>36</sup> It took forty years before the EU was able to establish a common market. While it is said to be a success, the process face lot of problems, even till today.

- While the elimination of all NTBs is not a realistic goal that can be reached any time soon, AMCs should work towards streamlining them. To facilitate that, establishment of the ASEAN Trade Repository (ATR) should be completed as soon as is practicable. The ASEAN classification of NTMs should be harmonised with existing international databases such as the UNCTAD-TRAINS. Though notification of NTMs can be left to the AMCs, monitoring and verification processes should be carried out by an independent body like the ASEAN Secretariat in consultation with industry groups.
- ROO is not a key reason for the low utilisation rate of the CEPT-AFTA scheme. There are other factors such as limited information-sharing, lack of transparency, and higher transactions cost due to the lack of supporting trade facilitation measures that are hindering the private sector from using ASEAN trade preferences. AMCs need to work on their public outreach activities, involve apex business associations in implementation plans, and provide more targeted technical assistance to businesses.
- Lastly, the divergent development stages among member economies hinder the less developed economies (i.e. CLMV) from moving at the same pace as the other six. Moreover, these countries are likely to incur revenue losses<sup>37</sup> while implementing their commitments as signatories of AFTA. To overcome this issue, CLMV must look for alternative sources of revenue and undertake reforms in the revenue system. The countries should try to minimise illegal trade, as well as improve governance and information systems to ensure greater benefits from ASEAN cooperation measures.

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<sup>37</sup> In 2009, import duties constitute 19.8, 10.3 and 24.2 per cent of tax revenues for Cambodia, Laos and Vietnam respectively. In a 2005 study, 'Options for Managing Revenue Losses and Other Adjustment Costs of CLMV Participation in AFTA' by Jose L. Tongzon, Habibullah Khan and Le Dang Doanh under the Regional Economic Policy Support Facility, it was shown that all CLMV countries, with the exception of Myanmar, stand to lose substantial customs revenue from ASEAN imports due to the implementation of the CEPT scheme.

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