

# ASEAN is building a common market



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On the south-eastern edge of Asia emerges a strong economic community, which has been built for decades. On 1st of January 2016 state members of Association of Southeast Asian Nations (ASEAN) will form a ground for Common Market for over 630 million consumers. In coming decades a whole integration process will continue but it is important to note that nowadays in these 10 country members of ASEAN lives every 11th inhabitant of the globe, and that in the last decade their economy grew annually by 13.5 percent. With a similar surface as the European Union and with 20 percent bigger population, ASEAN Economic Community becomes one of the largest economically integrated world markets.

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Signs of continued integration of Southeast Asia are clearly visible, especially if we remember the region from many years ago. Over the past two decades the mobility, trade and investment in Indochina greatly improved. Tendency of the South Asian countries to perceive themselves as a whole region, a diverse but connected community sharing common experience and challenges, increased as well. This is the result of the Southeast Asia's consistent efforts striving for closer relations that leads to commercial and political benefits. This processing economic integration and close political cooperation are also the result of global economy networking, competitive and cooperative approach.

Association of Southeast Asian Nations is now one of the fastest growing integration initiatives in the world. For years the process has included wide range of topics, grouped into three pillars: political and security oriented; economic and socio-cultural. Such an approach is a result of desire for comprehensive integration of the region and readiness to face many differences standing behind its individual states. This makes ASEAN a unique case in Asia, where regional cooperation tends to focus on a narrow ground or covers a wide geographical range.

The importance attached to joint initiatives in security and socio-cultural fields distinguishes ASEAN from the European Union, where these issues are basically handled through intergovernmental activities. However, an intention to build in Asia the ASEAN free trade zone, as proposed in the early 90s by Thailand, is similar to the European Union project – EU Single Market. In Poland ASEAN community is not that recognizable. **But the single market, which is to be built in these countries, gives quite huge expansion opportunities for Polish entrepreneurs.**

### From the search for peace to the search for development

ASEAN was established in 1967. The declaration for the founding of the association was signed in Bangkok by foreign ministers of five countries: the Philippines, Indonesia, Malaysia, Singapore and Thailand. Sharing the same experience of the Japanese occupation during the Second World War, the founding members were guided by the desire to secure long-term peace in the region which was ravaged at that time by the Cold War confrontation. Despite significant differences in interests, the leaders of these countries realized that only by acting

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together they could balance the influence of China, the USA and Japan, and ensure the long-term development of their nations.

**Therefore, the reason for establishing ASEAN was the same as for the European communities: the wish to avoid conflicts and fear of war.** The political changes taking place in the next decades were reflected in the expanding membership of the organization. ASEAN was joined sequentially by Brunei, Vietnam, Laos and Myanmar and Cambodia (1995). Today, ten member countries of ASEAN are inhabited nearly by 630 million people (forecast for the beginning of 2016), who in 2014 have produced goods and services worth nearly USD 6.64 trillion (measured by purchasing power parity), which accounted for 6.1 percent of global GDP. The same rate *per capita* was measured in 2014 and reached USD 10,677, placing itself on the top 2/3 of the global level (in 2014 World Bank noted GDP *per capita* at the level of USD 15,189). The combined economies of all ASEAN countries in 2014 were equal to 15 percent of the American economy; by comparison in 2004 it was only 7 percent. Thus this market is quite large, significant, and with growing importance in the global economy.

During the early 90s ASEAN's motives were primarily political and military (joint actions in case of emergency, policy initiatives concerning the region); it was in 1995 when accession of Vietnam and Cambodia, actually changed the most important motives of ASEAN, which began to focus on the economy. At that time one of the main priorities of ASEAN was cooperation with the most successful countries of the Asia-Pacific region (China, India, Australia, and Japan) and also with other regional organizations such as European Union. **This vision of the close economic cooperation and the creation of a Common Market is a driving force for ASEAN today.**

At the same time ASEAN countries are steadily watching the position and actions of China in the region (disputes over islands on South China Sea, *One Belt, One Road* initiative, creation of the Asian Infrastructure Investment Bank), fearing the domination of China. ASEAN region has already experienced moments of disagreements and inability to work out a unified position towards China after the annual summits (the most important fracture was observed during the presidency of Cambodia in 2012). At the same time, each country has bilateral relations with China. Philippines are waiting for the decision of the International Court of

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Justice which will decide on the status of South China Sea islands. Expected verdict will shed new light on relationships in the region.

#### Ambitious plans: the single market

What mostly binds the Member States of ASEAN is economy. Creation of a community based on open market and industrial base, with free movement of goods, services, investments, skilled workers and liberalized capital market could ensure faster and more balanced development to the South-East Asia, based on a high level of competitiveness and full integration with a global economy.

One of the most significant projects leading to the market integration is an agreement on lowering tariffs under the ASEAN free trade zone. Almost complete abolition of tariff barriers between the six state members (Brunei, Indonesia, Malaysia, Singapore, Thailand and the Philippines) and reducing tariffs to only 2.6% for the remaining four countries, intensified trade within the organization. In 2004-2011 trade value increased by 129 percent: from 260.9 to 598.2 billion dollars. In 2014 the further increase was recorded up to USD 607 billion.

The reduction of tariffs undoubtedly remains a key achievement of ASEAN; internal trade increased, but still represents less than 1/4 of the turnover. The remaining 3/4 is the trade with the rest of the world, in which case ASEAN countries apply different rates and import procedures.

Another step towards improving the movement of goods and services within ASEAN is removing non-tariff barriers. Efforts to harmonize custom procedures will eventually allow the flow of goods within ASEAN, by completing only one set of standardized documents (this goal is intended to be completed by 2025 for the most developed countries in ASEAN). Member States also strive to develop common standards which will lead to elimination of duplication of certification and testing processes. To achieve that, twelve priority sectors were designated, including among others: electronics, health care, automotive, agricultural processing, the timber sector, ICT, textiles and clothing.

An essential element in building the ASEAN cohesion are infrastructure projects, whose implementation is to provide better access to markets, reduce transport costs and also engage the state members in regional and global supply chains. In this context one of the flagship investments is

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certainly completing the TransAsia bus station in Kunming - Singapore, which will connect the south-western provinces of China with ASEAN countries.

#### New initiatives

In the last 12 months, two important economic initiatives for the ASEAN area were launched. On the one hand it is an initiative supervised by China Asian Infrastructure Investment Bank (AIIB). Their goal is to invest annually USD 100 billion in Asia. On the other hand, in opposition to China initiative, stands the assistance offered by the Government of Japan (Tokyo and the US are the two main countries that have not joined the AIIB) with the same amount of money. ASEAN countries will become therefore an object of increased investment activity which will come together with tug-of-war activities.

Recently we can observe a race of promises, foreign travels and billions in contracts signed between Chinese President and Prime Minister of Japan.

The implementation of key importance investments is to be supported by ASEAN Infrastructure Fund, whose budget over the next three years will reach a billion dollars. According to the estimates, in order to make

up for many years of backlog in this field, infrastructure investments of transnational importance in the years 2010-2020 should reach 60 billion dollars annually. In this case, the role of said capital from China and Japan will be crucial for geopolitical stability in the region.

Conscious of their advantage in the form of low costs and increasing labor productivity, ASEAN states are now the driving force behind the liberalization of trade in Asia. In the perspective of the changes in the labor market in China (rising wages and an aging population) **goal of the ASEAN is to take over the role of the largest factory of the world.** The growing attractiveness of ASEAN countries provides a strong inflow of foreign investment in recent years. As a result, their level is flushing with capital involved in China. In 2014 FDI in ASEAN amounted to USD 136 billion – this is the highest figure in the history of the group.

#### ASEAN plus...

ASEAN's activity is not limited only to the relationship between the ten Member States. Bitter experience of the economic crisis in 1997 pushed ASEAN states to cooperate with China, Japan, South Korea and Hong Kong in order to build the Asian financial crisis prevention mechanism. The fund,

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created on the basis of the so-called Chiang Mai initiative provides the measures to maintain the stability of exchange rates in the amount of USD 240 billion. But, as some economists say, firewall cannot be strong enough in the face of a crisis, although its value as a symbol of the determination of states to defend regional economic stability gives no doubt.

Besides the "ASEAN+3" initiative, it is possible to observe the coordinated inter-governmental cooperation with China, Japan and South Korea. It includes, among others, energy and food security, natural disasters, financial cooperation, stimulating trade and sustainable development. In an even broader group, "ASEAN+6", undertaken initiatives also include: Australia, India and New Zealand. Free trade agreements signed by ASEAN with the entire "six", that is, with Australia and New Zealand, China, India, Japan and South Korea, contribute to the strengthening of the trade relations across the region. At stake is the creation of a resilient and regional free-trade zone covering all these countries - and therefore more than 3.36 billion people - 49 percent of the world's population that produce 25% of the global wealth. At the moment the perspective of forming this zone is in 2050. Analytics claim that if the current

ASEAN growth continues, all country states will cumulate the potential that will locate them on a 4th place in the world's economy ranking (today ASEAN gains 7th place in that ranking).

ASEAN region resisted the excessive deficit of national budgets and today shows the average debt at the level of 50% of GDP. By comparison, in the UK it amounts to 90% and in the USA 105%. ASEAN represents a very impressive pace of a middle class growth. It is estimated that the current 67 million households with annual incomes of at least 7,500 dollars is expected to double by 2025, reaching more than 125 million. ASEAN with its common market economy has a great potential to become the consumer center of the whole world. The variety of 10 markets is so large that you cannot talk about the typical customer of the ASEAN area, but it also creates additional opportunities for Polish companies.

ASEAN region is also undergoing a strong urbanization. By 2025, 54 million residents will move to the cities. 40% of the area GDP will be produced in the 142 largest cities. Great potential lays also in computerization - Singapore is the leader in this regard, with 3/4 of the population having access to the network, but for comparison

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Myanmar records only 1% of people connected to the Internet.

#### Interior challenges

Apart from promising prospects there are also several challenges. In opposition to the European Union countries, the countries of ASEAN are profoundly different in terms of level of development, culture and political systems. They are also divided over territorial claims (eg. between Thailand and Cambodia) and huge social disproportions. The main axis of the divide runs between the much more developed ASEAN founding countries and Brunei and four less developed countries that joined the organization in the 90s: Myanmar, Cambodia, Laos and Vietnam.

The scale of inequality is illustrated by the fact that the national income *per capita* of Singapore is more than forty times higher than GDP *per capita* in Myanmar. Huge differences also manifest themselves in doing business. In the 2016 *Doing Business* ranking leaders like Singapore or Malaysia occupy the 1st (Singapore), and the 18th position (Malaysia). There has been considerable decline in the position of Thailand in the ranking. Today Thailand occupies the 49th position instead of 18th (according to 2013), while the worst in this regard are

Cambodia, Laos, and Myanmar, on the 127th, 134th and 167th positions accordingly. The scale of disproportions is much larger than the one that occurred in integrating Europe.

In turn, the territorial disputes between some ASEAN countries make it difficult to build a security community in the region. At the same time, the fact that for almost half a century association members were able to prevent escalation of emerging conflicts (and solved some of them), should be treated as equally important achievement as its progress in economic integration.

**Certainly, a model of the relationship within associated countries, so-called "ASEAN way", contributed to this success, a model based on the principle of non-intervention in the internal affairs of others and making joint decisions by consensus.** What in the past allowed the neutralization of numerous tensions, today is increasingly seen as a barrier preventing the deepening of the integration process. It will inevitably disclose divergent political and economic interests, primarily between more and less developed countries. All this makes the existence of several "integration speeds" within the framework of ASEAN not seen as controversial, unlike the situation in the EU.

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#### Anxious times

In the XXI century, the center of gravity of the world politics inevitably shifts to Asia, with ASEAN Member States in the center. Malacca Strait separating Malaysia and Indonesia is one of the most important sea routes, where one-third of world trade flows. At the same time South China Sea became an arena of territorial disputes. New tensions emerging in the region and a growing threat of international terrorism reinforce the meaning of close political and military relations. Information about the possibility of suicide bombing attacks during the ASEAN summit in November this year in Kuala Lumpur was based on information about terrorist group meetings in the Philippines. There are evidences that extremists from Malaysia, Indonesia and the Philippines are trained in Syria, Iraq and Afghanistan, and that ASEAN can be the target of terrorist attacks. The proof that the situation of a so far bomb attack free region has changed, is a bomb attack in Bangkok in July this year. Important for the stabilization of the region is US military and diplomatic support. US Navy is for Vietnam (guarantees of military assistance and diplomatic contacts revival of the 20th anniversary of the establishment of diplomatic relations celebrated this year) and the Phi-

ippines (reactivation Base Subic Bay after more than 2 decades) main guarantor of the security. ASEAN countries are uniting also through bilateral alliances; one of them was signed in November 2015 between Vietnam and the Philippines.

#### What about China?

China – in the early nineties mainly a source of concern – has grown after the financial crisis in 1997 into the most important trading partner of the ASEAN and the regional center of economic network. Starting 2010 under the Law on Free Trade more than 90 percent of trade goods between China and Brunei, the Philippines, Indonesia, Malaysia, Thailand and Singapore are exempt from customs duties. In 2015 similar rules will come into force in trade between China and the other four members of ASEAN, namely Vietnam, Laos, Cambodia and Myanmar. What proves how important these agreements are for the ASEAN economy is the fact that only during two years since the implementation of the agreement, ASEAN exports to China soared by almost a third.

If the importance of economic ties with China is highlighted by every single analysis on the situation in the region, the activity of another Asian power - Japan - is often not

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given a proper place in the studies. Japan is in the second place after the European Union among foreign investors in ASEAN countries (the value of Japanese investments in 2011 was almost three times higher than the Chinese) and one of the largest trading partners in the region. In a perspective of the escalation of Beijing-Tokyo tensions, the meaning of ASEAN and its existence in Japanese politics, both as an alternative for investment and geopolitical counterweight towards China, will definitely grow.

#### Other players

India, concerned about the growing power of China, plays an active role in the region. India is mostly concerned about freedom of navigation in the South China Sea and the development of economic relations with ASEAN members, as proved by their participation in the free trade zone of "ASEAN+3". More than a billion-dollar domestic market in India is seen by the producers from South-East Asia as an excellent alternative for China's market. The government of the Prime Minister, Narendra Modi, strongly promotes the strategy of encouraging foreign countries to shift production directly to India - a plan conducted since 2014 under the slogan "Make in India".

Geopolitical picture of the region is complemented by the now famous return of the US "towards Asia" - which is one of the key elements of President Obama foreign policy. Among the main objectives of American construction of the "Asian axle" is to strengthen relations with the ASEAN countries - not only in the military sphere, but also, as mentioned less often, in the field of economy. Initiated in 2012 Expanded Economic Engagement between the US and ASEAN is poised to become the nucleus of a future free trade zone. Already, the United States are at the forefront of the most important foreign investors and trading partners of ASEAN.

The forthcoming presidential elections in the US (November 2016), which may significantly affect the continuation or discontinuation of the current policy of the US "towards Asia" is crucial for the future of the region. The next year will also bring new presidents of Taiwan (January 2016), the Philippines (May 2016) and XII Congress of the Communist Party of Vietnam (also January 2016), which may make a reshuffle at every level of the highest positions. The key is to conduct appropriate recognition in the field of existing alliances, policy strategies, and profiles of candidates running in the elections in these countries. It

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would enable Poland to react quickly and adequately to the needs of newly elected politicians.

#### The European Union and ASEAN

Despite the limited role that Europe plays in the region of Southeast Asia in the political-military field, economic ties between the EU and ASEAN are extremely strong. **ASEAN is among the top three non-European Union's trade partners, and EU remains the most important foreign investor in ASEAN and third largest trading partner.** Between 2004 and 2008, trade between the EU and ASEAN increased by 25 percent, reaching a value of EUR 175 billion. At the same time, the Union's share in the total trade of ASEAN fell from 14.5 percent in 1998 to 10.2 percent in 2010. Promoting liberalization of trade between these two organizations could be one of the best solutions to reverse this trend. However, suspension of talks on a Free Trade Agreement between the EU and ASEAN, because of the lack of common economic instruments for countries associated within FTA, made the center of gravity shift to bilateral agreements. Agreements between EU and Singapore and EU and Vietnam have been achieved but at the

same time talks between EU and Malaysia have been terminated. Currently, there are some difficulties in negotiations with Indonesia (progressive protectionism) and Thailand (political instability). The EU is considering a return to the concept of the framework agreement on free trade, but only as long as the requirement for compliance with its provisions will be achieved by all countries. At the same time four countries from ASEAN (Singapore, Brunei, Malaysia, Vietnam) have recently signed a transpacific agreement (TPP), which strengthened the position of the US and Japan and weakened the EU's position in the region.

The strong European capital for ASEAN countries is high volume of trade and the positive image (*soft power*). However, it is difficult to say that the EU could be exemplary model of integration for ASEAN countries. But at the same time, undoubtedly, its experience remains a valuable inspiration and a reference point. EU financial support for the functioning of ASEAN is not without significance. The European Commission indicated ASEAN in 2006 as a priority market and one of the key economic partners of the European Union. The most important EU countries, with Germany as a leader, have already recognized the huge

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potential of the ASEAN countries. Numerous visits of leading European politicians to the ASEAN region demonstrate the EU return towards Asia. Polish companies should follow this path if they want to seek opportunities in overseas markets.

#### What will change in 2016?

The inauguration of the ASEAN Economic Community does not fundamentally change the way European companies operate in these ten markets. Businesses will still be conducted bilaterally and bureaucracy and permits will still be based on relations with the concerned countries. However, the accessibility to the neighboring markets and the ability to use cheaper labor force of the least prosperous countries of the community, such as Laos and Myanmar, will definitely increase.

In the short term future, there will be facilities enabling to enter the markets of ASEAN partners within the formulas "ASEAN+3" or "ASEAN+6".

By building ASEAN Economic Community, country members have already achieved two substantial successes:

- The abolition of most tariffs (above 99 percent for the six richest economies

and 97 percent for the other four countries);

- The high level of mutual investments (50 percent), of which about half comes from Singapore, a total of nearly 90 percent of the five richest states. At the same time in Laos it is a little over 0 percent and in Vietnam about 6 percent.

However, the lack of standardized regulations governing investments for the entire zone of ASEAN and the lack of common agreement on services and free movement of workers may still be observed. At the same time, monetary and financial integration is under preparation.

If the economic integration of Southeast Asia proceeds according to the plan, tariffs on turnover of almost all goods within the framework of the ASEAN countries will be zero or close to zero, the financial system will be unified, and restrictions on employment will be reduced. This means that every inhabitant of the region will be able to work in any member country of the association. In some key sectors, such as airline flights, *e-commerce*, car manufacturing or textiles, the integration will significantly accelerate. Free movement of labor will also influence the region's economy, creating opportunities for companies that have already invested in

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the region. Combining sustainable development oriented approach, the growth that does not exclude anyone and a green knowledge-based economy, may bring substantial economic acceleration in South-east Asia and raise the importance of the region in the global economy.

The question is how to take advantage of these opportunities. European Union notice that through greater cooperation with ASEAN countries, European exports could increase, as well as the investments and job opportunities. Polish companies should also benefit from this trend.

At the same time, persistent political tensions in the region and the threat of Islamic fundamentalism may weaken the interest of the European companies into the ASEAN market. This trend can be prevented by the cooperation between the Member States of the European Union and ASEAN, especially in a field of combating international terrorism and solving global challenges such as, among others, climate agreement or the implementation of new development goals for the world (sustainable development goals) adopted by the United Nations in September of 2015.

### What ASEAN mean to Poland?

Polish turnover with the countries of ASEAN is still low, taking into consideration the potential of these economies. In 2014 it was just over 7 billion of which USD 1.6 billion was export and USD 5 billion was import. Trade deficit is mainly caused by high import from Vietnam (\$ 1.2 billion) as well as Malaysia, Indonesia, Singapore and Thailand. Poland has the weakest economic relations with the sultanate of Brunei and Laos. The largest increases were recorded in exports to the Philippines and Myanmar.

From Polish perspective it is certain that Poland should invest in diplomatic presence in ASEAN, make new business contacts and mostly explore potential markets. Sectors of promising opportunities are: infrastructure, green technology, trade, tourism and food industry. Trade missions, participation in international fairs, as well as the export of Polish specialists offering help on a number of infrastructure and IT projects, could be very useful. We should not count on a significant breakthrough in this area, but this should not discourage investors to participate in tenders. In some ASEAN countries there are laws that make it difficult

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or even impossible for foreign companies to compete with domestic companies. Potential capital that could be received through AIIB investments may make this situation last.

To explore the potential of the new common market, it is crucial to establish direct flight connections from Warsaw to ASEAN countries, especially because today the Far East destination is available on two direct routes only: Beijing and Tokyo. According to analysts, by 2025 half the world's consumers open to every kind of goods will live within five hours' flight from Myanmar.

It is worth to act quickly, because every year new international companies establish their headquarters in ASEAN. The growth rate is significant: in 2006, there were 49 ASEAN companies listed in the *Forbes Global 2000* and in 2013 already 74. Currently, ASEAN has 227 global companies with revenues exceeding one billion dollars. In this respect, it is ranked 7th globally – after the US, Japan, China, Germany, Great Britain and France. This involves the foreign direct investments as well: in 2014, Indonesia, Singapore, Thailand and the Philippines recorded more FDI than China (128 to 117 billion dollars). Establishing ASEAN Economic Community will defi-

nately make the region more attractive to the world.

It is worth noting that ASEAN and Economic Community are not just a customs union, but also a declaration of further integration towards creating an economic zone in the selected areas. Basing on today's data it is impossible to predict how deep the integration will continue. Direct sales from Poland will probably remain unchanged due to differences in access to markets and the lack of arrangements and certificates recognition procedures. However, investment attractiveness for Polish companies will increase, as well as transfer of goods, within ASEAN region and with ASEAN countries.

In this way one may see basic assumptions of the ASEAN Economic Community whose goal is to become "the largest factory of the world".

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CSM is an independent, non-government analytical centre established in 1996 and dealing with Polish foreign policy and the most important issues of international politics. CSM is active in research, education and publishing, organises conferences and meetings, and participates in international projects in collaboration with similar institutions in many countries. CSM creates a forum for debate and exchange of ideas in matters of international politics, relations between states and challenges in the global world. CSM's activities are addressed above all to local-government officials and to entrepreneurs, as well as to officials of the central administration, politicians, diplomats, political scientists and the media. In 2009, CSM was recognised as one of the best think-tanks in East-Central Europe in the study "The Leading Public Policy Research Organisations in the World" conducted by the University of Pennsylvania.

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