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The Numbers Tell the Story

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Supporters of the ASEAN-China Free Trade Area (ACFTA) argue that numbers tell the story. And indeed, they do. But while those advocates focus on big numbers, such as the billions of consumers in the new market or its combined gross domestic product, the most important figures are much smaller. Forget the billions and trillions: the real significance of the FTA is in the simple “10 plus one” formula or, more accurately, one plus 10, given China's predominant position. For in addition to moving the focus of regional decision making to the north, the new free trade area will change the way Southeast Asia integrates, fundamentally altering the region's organizing principles. Unless ASEAN can effectively transform “10 plus one” into “one plus one,” through greater ASEAN coherence, it will be overwhelmed by China's rise.

The ASEAN-China FTA is designed to create a market of 1.7 billion people with a total GDP of approximately $2 trillion. Under the Framework Agreement on China-ASEAN Comprehensive Economic Cooperation signed in Phnom Penh this week, China will cut import tariffs on ASEAN products a few years before these countries will reciprocate and open their own markets to China's exports. This is intended to give ASEAN an export advantage over Chinese products, and allow Southeast Asian manufacturers time to become more efficient and productive. ASEAN officials also expect China will become a significant importer of ASEAN primary products. Thus, ASEAN's Secretary General Rodolfo Severino has asserted that “the overall impact of (free trade) on China and ASEAN will be beneficial.” A joint study by ASEAN and China found China's exports to ASEAN will increase by $10.6 billion, or 55 percent, while its imports from ASEAN will rise by $13 billion, or 48 percent. By one estimate, the FTA will add one percentage point to annual economic growth in the ASEAN countries and 0.3 percent in China.

This happy outcome is based on several assumptions, none of which are certain. Let's call them “the three competes.” First, there is the competition for capital. Productivity and efficiency gains depend not only on low-cost labor, but require private capital formation and investment in public and social infrastructure as well. Unfortunately, ASEAN is losing the contest for foreign direct investment (FDI) to China. At the beginning of the 1990s, Southeast Asia took 61 percent of all direct investment flows to developing countries in Asia, while China received 18 percent. Within a decade, the proportions had been reversed: China took 61 percent of FDI, while ASEAN states claimed but 17 percent. ASEAN's failure to create a business environment more receptive to foreign investment will undermine its ability to compete with China over the long run.

Second, there is competition for third country markets. ASEAN economies will benefit from the “early harvest” in tariff cuts for exports to China (even though those are proving to be more limited than many Southeast Asian governments had hoped), but Southeast Asia will continue to lose export market share in the U.S., Asia, and elsewhere to China. For example, in 1990 China had a 2 percent share of the U.S. import market for electronics; by 2000, that share reached 9.7 percent, topping those of the ASEAN-4 countries - Malaysia (9.2 percent), Thailand (4.5 percent), Philippines (3 percent) and Indonesia (1.02 percent). Every ASEAN member has increased its share of total Asian exports from 1990-2001, but China's growth has been spectacular - more than doubling in size. China's exports to the U.S. grew 185 percent during that period, while its exports to the European Union increased 49.5 percent. Among the ASEAN-4, only Indonesian exports to those markets increased during the same time, and only 21.5 percent and 17.3 percent, respectively - a mere fraction of China's growth.

Third, ASEAN will have to compete with China for slots on the value-added chain. It is assumed that economic development in the region is linear: production in China will become increasingly sophisticated and ASEAN will stay ahead and profit from supplying the capital goods needed for China's growth. But this “flying geese” model of development is no longer viable - countries can jump the queue. China is large enough, and sophisticated enough, to fill every link on the production chain itself.

While the logic of ACFTA is economic in nature, its impact is political. ACFTA shifts the locus of regional decision-making away from Southeast Asia, and moves it north to China. China, by virtue of its size, becomes the dominant economic power in the region and will enjoy the political benefits that flow from that status. The eventual inclusion of Japan and South Korea in the FTA could help balance China, but that would merely underscore the shift in political competition northward, among the three Northeast Asian states - increasing neither ASEAN's influence nor status. Moreover, relying on Japan to balance China may be a mistake, given Tokyo's inability to match Beijing's recent diplomatic initiatives.

At the same time, the nature of the integrative process in Southeast Asia will change. The region's striking economic success and ASEAN's emergence as a global player (until 1997 at least) have obscured the organization's most essential role: ASEAN is a norm-building institution that was designed to manage change in a volatile region. It has “socialized” emerging economies, and in the process created a community that is more than a market. While the addition of Vietnam, Cambodia, Laos, and Burma has strained the organization, expansion has also been critical to helping those governments better participate in regional and international affairs. ASEAN has been a stepping stone to better citizenship.

An FTA that is dominated by non-Southeast Asian nations could reverse that process. Regional governments will no longer look to each other for answers to political and economic problems, but to China or Japan. Economic considerations will take precedence over the “community” concerns that previously drove decision-making. On both levels, Southeast Asia is the loser.

ASEAN must adjust to China's rise. Southeast Asian governments and businesses need to match - if not anticipate - China's development and modernization, which means increasing their competitiveness and integrating their own markets. A failure to do so will only put them at a greater disadvantage with China. Thus, the ASEAN Free Trade Area (AFTA) needs to move forward in advance of the ACFTA to ensure that ASEAN maintains its own coherence and voice.

The vast discrepancies in the size of ASEAN economies and China mean that that there is only one way to check the drift of power northward. ASEAN needs to become more integrated and more cohesive. An ASEAN that speaks with one voice could pose a credible counterweight to a larger power in East Asia. That may be fantasy, given the vast differences among the ASEAN nations and the history that divides them, but those long odds were only a little shorter when Southeast Asian governments had to negotiate among themselves. The new regional dynamic threatens to turn ASEAN and Southeast Asia into an appendage of the more developed economies of the northeast. ASEAN's future depends on a “one plus one” approach.

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