



Economic Integration in South East Asia  
and the Impact on the EU

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## Executive summary

South East Asia region has seen a wave of bilateral and regional free trade agreements in recent years. The near future is likely to see a continuation of this trend. This report aims at (1) describing and analysing the patterns of regional trade integration involving South East Asia, including the outlook for the future and (2) identifying the possible impacts on the EU arising from the main trade integration initiatives in the region.

In this report South East Asia is taken to mean all the ASEAN countries and the focus is on the effects on the EU from changes in market access conditions arising from closer economic integration between the ASEAN region and other key economies. While we note the potential importance also of the impact on the EU's exports to other Asian markets (such as China, Japan, India, etc.) resulting from these integration processes involving ASEAN, the focus of this study is intentionally more specifically on the impact on exports to ASEAN.

The EU trades heavily with the region with exports to ASEAN countries (EUR 50 billion in 2009) accounting for 4.6% of total extra-EU exports. Singapore is by far the most important ASEAN destination for the EU. Machinery and transport equipment and chemicals are key product groupings in the EU's exports to ASEAN. The combined size of ASEAN and its key FTA partners (China, Japan, India, South Korea, and Australia) in the EU's exports was around 22% in 2009.

ASEAN is becoming a regional FTA hub, having concluded agreements with all key regional players: China, South Korea, Japan, India and Australia and New Zealand. Some ASEAN members actively pursue a policy of engaging in bilateral FTAs with several partners in Asia-Oceania and beyond. Despite some attempts, notably the talks on the EU-ASEAN FTA that are currently on hold, so far the EU has remained little engaged in the Asian integration process.

With regard to the characteristics of South East Asian FTAs, the key findings of this report include:

- The large majority of FTAs in the region are very recent implying that they are at the early stage of their implementation processes. While tariff reductions are generally introduced as planned, progress in implementation of deep integration provisions face more obstacles.
- In view of this, it is not surprising that evidence on utilisation of FTA preferences is scarce and gives mixed messages. While there is evidence that at least for some products preferences are meaningful and are widely utilised, there is also a large heterogeneity in utilisation rates between products, and import and export partners, reflecting different preference margins, stringency of rules of origin, and other factors. Further progress in the FTA implementation process could lead to rising utilisation of preferences (in the form of lower tariff and especially non-tariff barriers) and larger scope for potential adverse impact on non-members, including the EU.
- Intra-ASEAN integration has been gradually proceeding and by 2010, at least for the original six ASEAN members (ASEAN6, i.e. Brunei Darussalam, Indonesia, Malaysia, Philippines, Singapore and Thailand), the task of abolishing internal tariff barriers was almost complete. Cambodia, Lao PDR, Myanmar and Vietnam (CLMV) have also made substantial progress in removing tariffs to intra-ASEAN trade.

- Progress in the liberalisation of trade between ASEAN and ASEAN's partners varies considerably. ASEAN does not have a common external tariff and agreements of the ASEAN+1 format (ASEAN's FTAs with China, Korea, Japan, India, and Australia and New Zealand) contain separate tariff reduction schemes for each ASEAN member. ASEAN6 tariffs on non-sensitive imports from China have already been removed as of 2010. This applies to around 90% of tariff lines and similar magnitude of trade flows. Progress in tariff liberalisation for imports from South Korea and Japan is also advanced. Abolishing of remaining tariffs for non-sensitive imports from South Korea, Japan, India and Australia and New Zealand is expected to be take place over 2010-2013. In CLMV non-sensitive tariff reduction schedules are generally delayed by around 3 years, implying that the process should be mostly completed after 2016. The tariff provisions for sensitive products differ substantially between FTAs and countries.
- There is a large heterogeneity across the FTAs in terms of their treatment of regulatory issues. Broadly speaking, plurilateral ASEAN+1 agreements appear less ambitious than the bilateral agreements analysed in this report, i.e. the FTAs between Japan and individual ASEAN countries and the three agreements Singapore has signed with key trading partners: the US, China and Japan. Japan's agreements are found to have the broadest scope given that they include provisions covering investment, competition and government procurement more frequently than other FTAs. The Singapore-US agreement is the most comprehensive in that its regulatory provisions are most ambitious.
- All analysed bilateral agreements, ASEAN-China, ASEAN-Korea and ASEAN-Australia and New Zealand contain provisions on services, although the extent to which they go beyond GATS commitments varies significantly between FTAs. Among the plurilateral agreements only the agreement with Australia and New Zealand includes binding commitments on investment and intellectual property rights. Only the ASEAN-Korea FTA includes provisions to promote cooperation between the parties to protect intellectual property rights and to protect the environment.
- All the analysed bilateral agreements of Singapore and Japan include provisions on services and investment, all but one on competition and intellectual property, and all but two on government procurement. Provisions related to environmental standards appear in more than half of the analysed bilateral agreements, while labour standard issues can only be found in Singapore-US and Philippines-Japan FTAs.
- We are sceptical as to the medium-term prospects of the very ambitious initiatives to create unified regional FTAs covering a large part of East and South Asia or even the entire Asia-Pacific region – ASEAN Plus Three, ASEAN Plus Six or the Trans-Pacific Partnership. Their progress will be hindered by a combination of political and economic interests. Nevertheless, continued attempts to bring more order and transparency to the current FTA network and to engage new partners, notably the US may also lead to successful implementation of other initiatives that are currently not considered. It is instructive to bear in mind that barely a decade ago most of the FTAs currently in force were hardly conceivable.
- It is difficult to predict to what extent current FTA provisions on regulatory issues and non-tariff barriers will be effectively implemented. Limited capacity especially on the side of less developed ASEAN countries and conflicting interest of various stakeholders are likely to hinder progress. At the same time, the declared general political ambitions of countries sometimes go further than is provided by the current

format of FTAs and the agreements may further evolve incorporating new provisions. It is possible that over time the capacity to act and real commitment to deep economic integration could increase.

We use different methods to identify products and sectors where the potential adverse effects of integration processes involving ASEAN on the EU are most likely to materialise and attempt to quantify these results. The three complementary analytical approaches are (1) the Sussex Framework based on diagnostic indicators constructed from trade and tariff data, (2) partial equilibrium modelling applied to a range of key products exported by the EU to the ASEAN region and (3) a computable general equilibrium model. This analysis takes into account reductions or elimination of tariff barriers and is carried using actual FTA provisions for individual products (6-digit Harmonized Commodity Description and Coding System - HS). The key findings are as follows:

- The magnitude of effects on the EU's production and exports is found to be very small at the aggregate level even under the most comprehensive prospective integration scenarios.
- These small aggregate effects mask potentially non-negligible impacts which could occur in several sectors and products, which together account for a significant part of EU exports to ASEAN. The findings from the partial and general equilibrium models as well as the analysis based on the Sussex Framework indicators consistently point to products in HS chapter 87 (vehicles and parts and accessories thereof) as the ones where current EU exports are sizeable and where particularly significant export market losses could materialise.
- The agreement between ASEAN and Japan is likely to be the most detrimental for the EU's export prospects in ASEAN. All other ASEAN+1 FTAs are associated with much weaker negative impacts for the EU, although some specific sectors or products may experience losses. This differentiated impact reflects a combination of factors, notably the (dis)similarity of export structures between the EU and ASEAN's FTA partners and the patterns of tariff preferences incorporated in the FTAs.

The importance of the successful completion of the Doha Round negotiations for the EU is evident. Assuming a realistic outcome of the Doha Round significantly limits or in some cases completely removes the potential detrimental effects of being excluded from South East Asian integration initiatives.