Emergent Trilateralism in Developing Asia

Long Term Scenarios for Regional Growth and Trade

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presented at the
ADB Dissemination Seminar
Ministry of Finance, PRC
July 21, 2005
Beijing
1. Introduction
2. Overview of Initial Conditions
3. Globalism, Regionalism, and Asian Trade and Growth
4. What Makes Regionalism Work?
1. Introduction

• Regional events of the last decade have fundamentally changed the economic landscape of Asia and its relation to the global economy.

• While uncertainties remain and cycles will be inevitable, the Asian region has demonstrated its resilience.

• Ideology and rivalry are giving way to pragmatism and new opportunities for mutual prosperity.
Motivation

• Given the complexities of the modern global economy, policy makers relying on intuition alone are at a disadvantage.
• To improve both public and private sector visibility, ADB developed long term projections for Asian regional growth and trade linkages.
• Our goal is to promote policy coherence, empirical standards, and evidence-based policy dialogue.
• Here we present work in progress.
Overview of Conclusions

• Regional trade and integration offer Asia great potential for more rapid and sustained growth. Indeed, much of Asia’s benefits from global trade liberalization can be realized by regional initiative alone.
• Structural barriers to trade are now more important than tariffs. Policies and investments that facilitate trade can accelerate regional growth dramatically.
• Regional integration can promote Asian economic convergence, raising average growth rates and benefiting poorer countries.
2. Overview of Initial Conditions

• Economic dynamism is well established in Asia and continues to spread.
• Trade has been a primary driver in most regions, but heavy reliance remains on demand outside the region.
• Regional living standards remain uneven and many areas have yet to enjoy significant benefits.
Asian Trade and Growth Patterns

A Schematic View of ADB Developing Member Countries

- East and Central Asia
  - People’s Rep. of China
  - Hong Kong, China
  - Republic of Korea
  - Taipei, China
  - Central Asia
  - Mongolia

- South Asia
  - India
  - Nepal
  - Pakistan
  - Sri Lanka
  - Bangladesh

- Southeast Asia
  - ASEAN
  - Oceana
Macro Conditions, 2005

- GDP
  - East and Central Asia
  - Southeast Asia
  - South Asia

- Trade
  - East and Central Asia
  - Southeast Asia
  - South Asia

- Population
  - East and Central Asia
  - Southeast Asia
  - South Asia

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Extra-regional demand remains a primary economic driver.

Intra-Asian trade is far from reaching its potential.
On a global basis, Asia continues to represent superior growth.

Sources: DRI, Oxford Econometrics, IMF.
Three Virtues of Asian Regionalism

Asian regional integration offers three essential opportunities:
1. Geographic diversification/new markets
2. Superior growth rates
3. Structural differentiation – more rapid evolution from established North-South patterns of trade and specialization
3. Regionalism, Globalism, and Asian Growth

To project regional trade and growth under alternative scenarios, we have developed the Scenario-based ADB General Equilibrium (SAGE) model, adapted from the World Bank LINKAGE model, calibrated to the GTAP 6 database:

- 18 countries/regions
- 10-50 sectors

Currently in prototype form, SAGE is benchmarked for projections to 2025.
1. **Baseline**: Baseline scenario
   - including admission of China in the WTO
   - removal of quotas on textile to the US and the EU

2. **GBL0**: Global Trade Liberalization
   - removal of all import tariffs and export subsidies

3. **GBL2**: Global Trade Liberalization with Trade Facilitation
   - GBL0 with trade facilitating policies simulated by 2 percent annual increases in intra-Asian trade efficiency

4. **AFTA2**: Asia Trade Liberalization with Trade Facilitation
   - remove all import tariffs and export subsidies within Asia
   - trade facilitating policies simulated by 2 percent annual increases in intra-Asian trade efficiency
Equivalent Variation Aggregate Income
(percentage change from Baseline in 2025)

PRC, Korea, Hong Kong, China, Taipei, China, Indonesia, Thailand, Viet Nam, Rest of ASEAN, Bangladesh, India, Sri Lanka
EV Income Growth: East and Central Asia
(incremental percentage change from Baseline in 2025)
EV Income Growth: East and Central Asia
(incremental percentage change from Baseline in 2025)
### Regionalism and Trade Facilitation Increase
Most Trade, but Intensify Asia’s Linkages

#### Regional Trade Flows (percent change from 2005 in 2025)

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<tr>
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#### Regional Trade Shares (percent change from 2005 in 2025)

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General Conclusions

1. Growth prospects for the region are quite positive, and trade can play a central role.

2. Regionalism and trade facilitation should be very high priorities for the region. Combined gains from removing tariff and structural barriers to Asian trade far outweigh those of simple tariff abolition.

3. Asian trade liberalization will increase trade in nearly all directions, but significantly intensify intra-Asian trade linkages.

4. ASEAN generally, and the Greater Mekong Sub-region in particular, will contribute to Asian regional convergence for two reasons:
   - because of geography this region can act as a “growth bridge” between South and East Asia, facilitating regional trade
   - GMS includes some of Asia’s lowest income economies, and these are among the most appropriate for infrastructure to promote regional integration. Myanmar, Laos, Cambodia, and Vietnam could all be “pillars” of the Asian growth bridge.
What Makes Regionalism Work?

- Historic trade patterns were driven by traditional comparative advantage, emphasizing national differentiation.

- As economies advance and diversify internally, trade is increasingly driven by shared characteristics:
  - Economies of Scale
  - Multinational marketing
  - Supply chains

- The main impetus for modern integration is to expand networks and capture value added through domestic and international diversification
• Greater regional integration will propagate commercial linkages and transfer the stimulus of Asia’s rapid growth economies to their neighbors

• Coherent administrative, regulatory, and technical standards are essential ("soft infrastructure" – an Asian OECD)

• Focused policies to promote growth spillovers:
  - Integrated infrastructure development
  - Regional capital market coherence
  - Trade negotiation and facilitation
Infrastructure Investment

• Infrastructure commitments will be an essential guarantor of regional integration and growth.

• Public investment needs to extend its development leadership, increasing returns to market participation and private investment across the region.

• Public and private capital commitments must be complementary, particularly if the former is to be effective.
We live in an age of complementarity.
Asian FDI – Top Ten Destinations

FDI is very unequally distributed.

Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics).
1 Ranked on the basis of the magnitude of 2003 FDI inflows.
• Along with export demand, private capital formation has been an essential growth agent in Asia.
• International investment flows have helped many emerging economies overcome savings constraints to stimulate and sustain development.
• FDI is now an essential feature of regionalism and a forceful integration mechanism.
• Policy can facilitate FDI through standard setting and public investments that extend the profitable investment horizon across the region.
Bilateral and multilateral trade facilitation are essential for regional integration and growth:

• Geographically, ASEAN’s role as the growth bridge is critical. Unless this succeeds, intra-Asian trade and growth benefits will be much smaller.

• This project will be evaluating regional and national implications of a variety of trade agreements, including:
  – WTO and Doha global negotiations
  – ASEAN plus China and others
  – Northeast Asian FTA
  – Deepening APEC
  – various bilateral agreements
Economic Convergence and Sustainability

- Disparities in regional growth characteristics pose a challenge for equitable development and weaken the basis for overall progress.
- The Asian region still relies heavily on external demand, awaiting emergence of middle income consumer majorities.
- Meanwhile, expansion and diversification of regional demand are essential to stability and sustained growth.
To promote convergence at higher growth trajectories, regional commitments can be focused in two areas:

1. Infrastructure and other policies to increase market participation - distribution costs undermine market access, and more so for less developed regions

2. Investment promotion - let private capital do more of the work.

3. Human capital development – a huge public and private challenge; initial conditions vary greatly
• Institutional Change
• Demographic Transition
• Environment and Public Health
• Natural Disturbances
• Primary products (energy, food, etc.)
Discussion
A Snapshot of Regional Growth Drivers:
Regional Import Demand Composition (2005)