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Asean summit: A fragmented forum

By Kevin Brown

Regional leaders hoping to create a trade area to rival China and India must prove the south-east Asian grouping is more than just a talking shop for disparate nations



On a former Royal Air Force base at Seletar, close to Singapore's border with Malaysia, Rolls-Royce is close to completing its first factory outside the UK for manufacturing the Trent 900 and 1000 engines that power the Airbus A380 and Boeing's Dreamliner.

It is exactly the kind of investment on which heads of state and government will be focused as they fly into the Indonesian holiday island of Bali this week for the annual summit of the 10-country Association of Southeast Asian Nations.

Yet there is a paradox. Asked about the appeal of Selatar, Jonathan Asherson, Rolls-Royce's south-east Asia head, says: "We did look at other Asian locations, but once we got down to the detailed analysis Singapore stood out quite clearly." He points to the fast-growing Asian market for engines for wide-bodied jets, an existing relationship with Singapore Airlines and the availability of skilled workers.

Tellingly, however, he does not mention Singapore's membership of Asean – even though together the grouping boasts a population of more than 620m, with forecast gross

domestic product this year of \$1,800bn and is a potential alternative to an increasingly expensive China.

By these measures, Asean is the economic third pillar of emerging Asia – behind China and India, the region's giants – which helps to explain why its leaders will be joined for a series of further summits over the weekend by eight of their counterparts with strategic interests in the Pacific. For presidents Barack Obama of the US and Hu Jintao of China, and prime ministers Vladimir Putin of Russia and Manmohan Singh of India, as well as the leaders of Japan, Australia, New Zealand and South Korea, the annual east Asia summit that follows the Asean meeting is one of the few events in the political calendar that provides a broad forum for discussing increasingly acute regional problems such as overlapping territorial claims in the South China Sea.

For the US, in particular, Asean is an important arena in the battle for influence with China that has followed the Obama administration's decision to reassert American influence across the Pacific.

But Asean's growing political importance is largely a function of its location. Economically, the agglomerated population and GDP numbers are a polite fiction. It remains a fragmented grouping of 10 separate, very different economies. Many people in business see it as a perennially disappointing talking shop that happens to include several countries that offer an attractive alternative to China for manufacturing operations or regional headquarters.

An ocean apart

GDP per head of Asean members at purchasing power parity 2011 (\$)

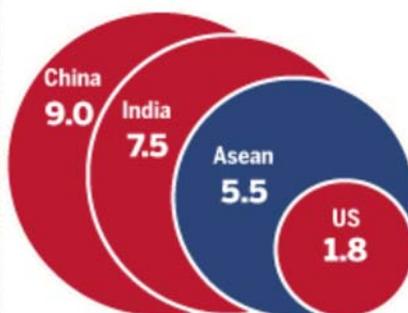


Population forecast 2012



Sources: IMF; US Census Bureau

Forecast GDP growth, 2012 (%)



Bali presents a rare opportunity to change that view, making the meeting a critical moment in the grouping's 44-year history. Asean leaders will review progress on an ambitious plan to create an integrated economic community by 2015. It would build a regional free market in goods and services, with harmonised rules for investment, a common visa regime for professional workers and skilled labour, and liberalisation of capital movements.

"If they could pull off that integration it would be the icing on the cake, [because] it would allow companies to operate more seamlessly across countries," says Grant Powell, head of Accenture's Management Consulting Innovation Centre in Singapore, and lead author of a recent report based on interviews with senior executives of more than 400 companies with operations in south-east Asia.

As a single economic unit, Asean would have a lot going for it. For a decade, the region has achieved average annual economic growth of 6-7 per cent. Its favourable demographics, with a much larger proportion of young people than China, suggest that rapid growth is sustainable for many years as the workforce grows and consumer spending increases.

A few international companies are blazing the trail, many with one eye on the local market and the other on its potential as a hedge against problems in China. [BASF](#), the German chemicals group, has plants in Singapore and Thailand, and is planning a presence in Malaysia through a €1bn speciality chemicals venture with state-owned Petronas. South Korea's [Hyundai](#) is considering a plant in the Philippines if economic integration ends regional tariffs on cars, as planned. [Piaggio](#), the Italian scooter group, has established itself in Vietnam and is exporting across the region.

Relations with China: Disputes grow more frequent and more fraught

Largely divided between British, French, Dutch and Spanish colonialists, south-east Asia was rarely thought of as a region until the second world war, when a command was created under that name by UK prime minister Winston Churchill and US president Franklin Roosevelt for Lord Mountbatten, the allied commander.

The concept reappeared in 1967, when the Association of South East Asian Nations was created by Indonesia, Thailand, Malaysia, Singapore and the Philippines in an attempt to end cross-border disputes and facilitate a degree of collective security against China, then starting to look outwards again after two decades of recovery from civil war.

Almost half a century on, with Vietnam, Brunei, Laos, Cambodia and Burma now also in the club, the issues remain the same. The stakes, however, are higher as the region seeks to reconcile fear of Chinese domination with the economic opportunities offered by its giant neighbour's booming economy.

The big security problem is the

Some local companies are beginning to think more regionally, too. [AirAsia](#), the Malaysian budget carrier, markets itself as Asean's airline and wants to operate between all its major population centres. [PTT Chemical](#), Thailand's largest petrochemicals group, has a joint venture plant in Malaysia making speciality chemicals. CIMB, the Malaysian bank, has adopted an official "Think Asean" strategy. [Axiata](#), the Malaysian telecoms group, has established operations in multiple Asean markets, as has [Singapore Telecommunications](#).

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Yet there is widespread, if discreet, scepticism in the region's business and financial community about whether the economic community will happen, and how effectively it will be implemented. In a fairly common exchange, a senior international banker rolls his eyes when asked about its prospects. "I wouldn't hold my breath," he says. "Does Asean ever get anything done on time?"

Michael Porter, a Harvard Business School professor, says he doubts that Asean has sufficient weight and influence to push member states into implementing its bold vision. "Collective action, especially among a group of disparate countries, only occurs if there is strong political will and sufficient institutional capacity to make change happen," he says.

An academic team at the National University of Singapore came to the same conclusion in a recent report, pointing out that 20 per cent of the regulatory and legislative preparations intended to have been delivered by 2009 had not been implemented by the end of 2010, mainly because of

South China Sea, which borders many of the Asean countries but is claimed almost in its entirety by Beijing. There are also competing claims to island groups within the sea, such as the Paracels and Spratlys.

Disputes are frequent, and becoming more fraught as Beijing's assertiveness grows. A Chinese coastguard vessel recently cut deepwater cables on an oil exploration survey ship 120 miles off Vietnam, and harassed another off the Philippine coast.

Maritime security will be a central issue in talks between Asean and Beijing in Bali, but the prospects for a lasting deal are poor because of China's insistence on negotiating separately with each member state rather than with the group as a whole. The two sides agreed in July on a set of loose guidelines for taking talks forward, which allow members to negotiate collectively so long as they do not consult in advance – even though China knows they are bound to do so by the Asean treaty.

The agreement was not pointless – it served to lower tensions. But it takes the two sides no nearer to their declared aim: a code of conduct on maritime activity. Even if such a deal could be reached, the grouping knows it could not enforce it without US help.

As President Benigno Aquino of the Philippines said after the last incident, there is little his country can do against China with a second-rate navy and an air force that does not include a single fighter jet. "If we were to engage in a boxing match, there's 15 of them for every one of us," he told the Financial Times.

obstruction by individual countries.

More fundamentally, the study challenged the idea that the region has been a strong economic performer, noting that GDP per person has risen at an average rate of only 2.3 per cent a year in the past decade, just above the global average. That suggests that much of the growth has been the result of population increases rather than productivity improvements.

Donald Emmerson, director of the Southeast Asia Forum at Stanford University, says some of Asean's difficulties flow from a combination of its fragmentation and its positioning between India and China, which has left it with no sense of a "primordial identity", unlike its two giant neighbours. "South-east Asia was invented from the outside in and the topside down," Mr Emmerson says. "It is an artificial identity. In a sense, you had the label before you had the reality. And it is a reality that is in many ways still coming about."

That reality includes massive disparities. In terms of wealth, Singapore produces GDP per capita at close to US levels, while Burma, Cambodia and Laos remain among the world's poorest countries. A few members are democracies; most are not. Singapore is building an international business in arbitration, but corruption and official interference with judicial independence are widespread elsewhere. The Asian Corporate Governance Association's latest report says Indonesia's securities laws fail to prevent either insider trading or market manipulation. "The attorney general's office is considered to be one of the most corrupt institutions in Indonesia, while judges can almost always be had for a price," it says.

These cultural, legal and governance differences have contributed to the development of the so-called Asean way – a system of progress by consensus. That means holding hundreds of meetings a year between officials and ministers of member states, who must agree unanimously before anything can be done. The intention is to avoid any impression of interference in each country's affairs. But it also means there is no mechanism for rallying laggards or resolving disputes about implementation.

The result is that agreements tend to deliver less than they promise, or to provoke destabilising disputes once they have taken effect and their impact becomes clear. For example, the four poorest countries have not yet fully applied Asean's trade

agreement, fearing they will not be able to compete with more prosperous neighbours. Many others insisted on lists of excluded “sensitive” products that run to hundreds of pages. Farcically, the group’s charter on democracy and human rights contains no enforcement mechanisms, and was thus signed enthusiastically by Burma’s military junta, Vietnam’s Communists and Brunei’s absolute monarchy.

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Resistance to change is widespread. A final deal on tariff reductions for trade in goods between member states was held up by an unrelated row over rice trading between Thailand and the Philippines, and there were angry protests in several countries over a trade deal with China. “Our state is in the hands of the Chinese and Koreans,” the head of an Indonesian private equity firm told the Financial Times after a deal was agreed with China. Non-tariff barriers are widespread. AirAsia recently dropped plans for a joint venture in Vietnam in the face of government interference aimed at protecting its state-owned flag airline from unwelcome competition.

Yet Asean has defied repeated predictions that it would collapse or fade away. Indeed, there has been real progress. Internal trade may not be completely free but 99 per cent of physical goods do move without tariffs between the bigger countries. Capital markets remain separated by borders and currencies but limited cross-border stock trading is imminent, though only larger members will be involved. There is no freedom of the skies, but limited competition among airlines between national capitals and some other big cities has helped produce a thrusting budget carrier sector in which AirAsia competes with rivals such as Cebu Pacific in the Philippines and Tiger Airways in Singapore.

Tai Hui of Standard Chartered Bank in Singapore says there are plenty of opportunities for the disparate grouping to integrate, with Singapore acting as a service hub, Thailand and Malaysia as advanced manufacturing centres and Indonesia and Vietnam as bases for low-cost production, and all sides making use of the region’s commodities and natural resources.

In Bali, Asean has a chance to show it can bring about further change by making clear that economic integration will happen, and on time.

But Mr Hui remains to be convinced its leaders will pull it off this time. “Asean as an entity is probably far too diverse to bring about such a shift.”

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