



**Asia-Pacific
Economic Cooperation**

APEC Study Center Consortium Conference 2011

Key Findings and Policy Recommendations:
Green Growth, Trade Integration and Regulatory
Convergence



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Introduction

The annual pan-APEC Study Centers Consortium (ASCC) conference convened on September 22-23, 2011, in San Francisco, California, in the context of the Senior Officials Meeting (SOM) III. The ASCC 2011 conference brought together scholars from 19 of the 21 APEC member economies as well as scholars from Colombia and Brazil.

Of the approximately 75 scholars who attended the conference, 29 presented papers on three core themes of APEC's agenda for 2011: green growth, regulatory convergence, and trade and regional economic integration (the conference agenda is presented at the end of this introduction). Eight panels discussed the papers, after which an open discussion followed. At a final session, as co-chairs we offered a "sense of the meeting" (not claiming a full consensus with every point) with regard to the three themes, which was accepted by the participants. We then presented our conclusions and policy recommendations to the SOM III as a formal agenda item. This exchange between ASCC and APEC senior officials fulfills a goal of the study centers: to provide a bridge between the academic community and government officials and to have some of the region's best policy research enrich the APEC agenda.

At ASCC 2011, scholars had an opportunity to hear from Ambassador Muhamad Noor, Executive Director of the APEC Secretariat, Senior Official Kurt Tong of the United States, and Senior Official Roberto Zapata of Mexico. We want to again thank them for addressing the ASCC meeting and engaging in lively discussions with participants. We would also like to thank USAID and the US State Department for its generous financial support, without which the ASCC2011 would not have been possible.

In the rest of this section, we summarize the major findings and recommendations of the ASCC2011 conference and introduce nine of the essays presented at the conference.

SUMMARY OF ASCC 2011 FINDINGS AND RECOMMENDATIONS

APEC Institutional Strengthening

ASCC members were pleased at the recent institutional strengthening of APEC, including the multi-year appointment of an Executive Director and creation of the Policy Support Unit (PSU), which is already doing admirable work. The members recommended that the PSU be made permanent and given a firm financial underpinning. The ASCC also called for close collaboration between APEC Study Centers and the PSU. PSU director Denis Hew addressed the ASCC and welcomed the ASCC's expression of interest in collaboration.

The ASCC 2011 agenda concentrated on three key pillars of APEC 2011, with a focus on practical measures and “getting stuff done.”

Pillar 1: Trade and Regional Economic Integration

The ASCC expressed support for the fact that many free trade agreements (FTAs) are now deeper and trans-regional (e.g., ASEAN+, and Asia – Latin America). Under some circumstances they can be building blocks of region-wide and global freer trade and liberalization, if they continue to be negotiated to high standards. Some participants expressed concern that the transparency of FTA drafts and of completed agreements was sometimes insufficient, and might create distrust and suspicion. Thus, it would be helpful if APEC made Individual Action Plans (IAPs) and peer reviews more effective regarding FTAs and sought convergence among FTAs toward high standards. To do this, participants suggested that APEC assess FTAs (drafts and completed agreements) for consistency with APEC model measure standards and that the ASCC could play a role in assessing IAPs and FTAs together with other groups.

Pillar 2: Green Growth

The ASCC supports green growth as an APEC pillar. Participants suggested that ECOTECH should put more resources into green growth initiatives and that nondiscriminatory and transparent government procurement should be employed to advance green growth goals. ASCC also suggested that APEC provide support for research and development in science and technology, especially among small and medium-sized enterprises in developing economies. It called for collaboration between APEC and other forums in pursuing green growth, and recommended that members share “best practice” case studies. The APEC Study Centers can assist by preparing independent, credible case studies. With respect to green growth, participants argued that green protectionism that has no scientific basis must be avoided.

Pillar 3: Regulatory Convergence

The participants found that while various international rankings are useful in affording pro-reform officials political and technical clout, rankings need to be disaggregated with care. In particular, ASCC argued that there is a role for independent analysts to assess and clarify methodologies. Moreover, success in regulatory reform and convergence toward high international standards depends on (1) leadership from the top, (2) internal coordination among ministries, and (3) strong external coordination.

With respect to other issues, to promote a success in 2012, APEC should support the WTO membership of the Russian Federation during 2011.

THE ESSAYS

This volume contains nine of the most outstanding papers presented at the ASCC 2011 conference. The essays highlight some of the key points of discussion within the conference’s three primary areas of focus: green growth, regulatory efficiency, and regional economic integration. First, we include two papers related to green growth. I-Chun Hsiao and Jerry I-H Hsiao argue that APEC has been ineffective at fostering sustainable development because of poor coordination among APEC economies and lack of political will. The authors advocate a new approach that balances APEC’s traditional emphasis on trade liberalization with new

attention to environmental protection and social equity. And they recommend policies designed to encourage green growth in APEC. In a second paper, Yumiko Okamoto examines the changing patterns of innovation in the Asia-Pacific region, noting that “there is much less evidence of new innovation capacity in the Asian-Pacific region than is sometimes claimed,” that increases in innovation are limited to a small number of countries, and that the gap between these “fast learners” and the rest of the region is growing.

We turn next to regulatory efficiency, featuring two papers on Chinese Taipei’s achievements in this area. Yi-Hung Chiou presents a case study of Chinese Taipei’s progress in terms of the ease of doing business, and argues that Chinese Taipei’s rapid improvements in this area can be attributed to three factors: strong, high-level political support for regulatory reform; a well-organized internal coordinating body (the Council for Economic Planning and Development); and close cooperation with and learning from the best practices of other APEC economies. The second paper likewise points to the important role of APEC as a platform for disseminating best practices to member economies. Ko-Hsin Yang and her coauthors describe a new set of indicators developed to assess Chinese Taipei’s progress in developing rule of law, transparency, and other components of good governance, and argue that these indicators could be put to good use by other APEC economies as well.

The remaining five papers address trade and economic integration. Sri Adiningsih and her coauthors argue that since financial market instability can trigger financial crises, it is vital to work toward greater financial integration of APEC economies as a means of ensuring financial market stability. The paper’s recommendations include financial market reforms; an improved regulatory framework to enable supervision of short-term capital flows; deposit insurance for investors; and an early warning system in the region. Artyom Lukin describes the development of multilateral ties in East Asia as a “game on two chessboards.” He argues that APEC may be a good forum for integrating Russia and the United States into a region that is increasingly dominated by China, and points to the simultaneous development of two distinct tiers of multilateral integration in the region: security cooperation within a “Northeast Asian concert” involving the countries involved in the Six-Party Talks, and economic integration driven by trilateral cooperation between China, Japan, and Korea.

Ipppei Yamazawa describes changes in the Individual Action Plan (IAP) peer review process, and explains how IAPs have enabled progress toward the Bogor Goals. He further argues that APEC must play an “incubator role,” facilitating progress on binding regional trade agreements while itself remaining nonbinding and voluntary. Cai Penghong argues that lack of transparency and the exclusion of certain countries, including China, from the Trans-Pacific Partnership (TPP) are problematic, and emphasizes the importance of including China in regional integration efforts. Finally, Robert Scollay traces the differing avenues toward regional economic integration in the Asia-Pacific. He analytically examines prospects for deeper ASEAN integration, the ASEAN plus 3 effort to create an East Asian Free Trade Agreement, and the Comprehensive Economic Partnership for East Asia (CEPEA) initiative of the ASEAN plus 6 group. He links these efforts to the TPP and APEC efforts to move toward a Free Trade Area of the Asia Pacific.

ASCC Conference Agenda, September 22-23, 2011

THURSDAY, SEPTEMBER 22, 2011	
9:00-9:15	<p>WELCOME AND OPENING REMARKS</p> <p>Prof. Vinod K. Aggarwal, Berkeley APEC Study Center, UC Berkeley, USA Prof. Richard E. Feinberg, APEC Study Center, UC San Diego, USA Co-Chairs, U.S. APEC Study Centers Consortium</p>
9:15-9:45	<p>KEYNOTE ADDRESS</p> <p>Ambassador Muhamad Noor Yacob, APEC Executive Director</p>
9:45-11:15	<p>PANEL 1: SUSTAINABLE GROWTH IN EAST AND SOUTHEAST ASIA</p> <p>Chair: Mignonne Chan, Chinese Taipei APEC Study Center</p> <p>Green Growth: New Impetus for Economic Growth in the Asia-Pacific—A Chinese Perspective Li Wentao, APEC Study Center of Nankai University, China</p> <p>Directions for Sustainable Development—Public-Private Partnerships for Infrastructure Investment Dennis L. McNamara, Georgetown University, USA</p> <p>A New Geography of Innovation? Opportunities and Challenges Facing the Asia-Pacific Region Yumiko Okamoto, Doshisha University, Japan</p> <p>Discussant: Omkar Shrestha, Visiting Senior Research Fellow, Institute of Southeast Asian Studies (ISEAS), Singapore</p>
11:15-11:30	Coffee Break
11:30-1:00	<p>PANEL 2: MULTILATERAL INSTITUTIONS AND SUSTAINABLE GROWTH</p> <p>Chair: Wu Zhenglong, China National Committee for Pacific Economic Cooperation</p> <p>An Analysis of APEC's Green Growth Strategy in the Context of the United Nations Conference on Sustainable Development I-Chun Hsiao, United Nations Foundation, USA Jerry I-H Hsiao, Taylor's University, Malaysia</p> <p>Strengthening the Economy-Ecology Alignment: Incorporating Social Aspects for APEC Green Growth Wayne Chen, Chinese Taipei APEC Study Center, Chinese Taipei</p> <p>Growth Strategies in a Greener World Kaoru Nabeshima, Institute of Developing Economies, JETRO, Japan</p>
1:00-2:30	<p>LUNCH AND KEYNOTE ADDRESS</p> <p>David Frigstad, CEO, Frost and Sullivan, USA</p>
2:30-4:00	<p>PANEL 3: REGULATORY EFFICIENCY</p> <p>Chair: Richard Feinberg, APEC Study Center, UC San Diego, USA</p> <p>Racing to the Top: Chinese Taipei's Achievements on the Ease of Doing Business Yi-Hung Chiou, Chinese Taipei APEC Study Center, Chinese Taipei</p> <p>Liberalization of Trade in Services by APEC Economies: Toward Achieving a Seamless Region-wide Linkage Hikari Ishido, Chiba University, Japan</p> <p>The Design of Chinese Taipei Governance Indicators and their implications for Effective Regulatory Policy Ko-Hsin Yang, Georgetown University, USA</p>

	<p>Yu Chieh Lin, University of Michigan, USA Ri Sharng Chiang, National Taiwan University, Chinese Taipei Yung Tai Hung, National Taiwan University, Chinese Taipei Chun Ming Chen, Shih Hsin University, Chinese Taipei</p> <p>Discussant: Kui-Wai Li, City University of Hong Kong</p>
4:00-4:20	Coffee Break
4:20-6:00	<p>PANEL 4: ECONOMIC INTEGRATION IN ASIA AND LATIN AMERICA</p> <p>Chair: Artyom Lukin, Far Eastern Federal University, Russia</p> <p>Comparative Analysis of Integration Processes in Asia and Latin America (1990-2010) Fernando Alfonso Rivas Mira, University of Colima, Mexico Juan González García, University of Colima, Mexico José Ernesto Rangel Delgado, University of Colima, Mexico</p> <p>China's FTAs with Latin American Economies and their implications for APEC Yu Chai, Chinese Academy of Social Sciences, China</p> <p>Brazil and the Asia-Pacific Region Neantro Saavedra-Rivano, University of Brasilia, Brazil</p> <p>Discussant: Barbara Stallings, Brown University, USA</p>
7:00-9:00	<p>KEYNOTE ADDRESS</p> <p>SOM Amb. Kurt Tong, U.S. Ambassador to APEC Evening Dinner (Generously sponsored by the National Center for APEC)</p>
FRIDAY, SEPTEMBER 23, 2011, LOCATION TBD	
9:00-9:30	<p>KEYNOTE ADDRESS</p> <p>Ambassador Jorge Heine, Chile</p>
9:30-11:15	<p>PANEL 5: APEC AND THE TRANS-PACIFIC PARTNERSHIP</p> <p>Chair: Manfred Wilhelmy, Institute of International Studies, University of Chile</p> <p>The Future of APEC and Strategic Scenarios Cai Penghong, Shanghai Academy of Social Sciences, China</p> <p>Pathway to an Asia-Pacific Economic Community: ASEAN +3, +6, or TPP? Sangkyom Kim, Korea Institute for International Economic Policy, Korea</p> <p>Russia and the Emerging Institutional Order in the Asia-Pacific Artyom Lukin, Far Eastern Federal University, Russia</p> <p>Discussant: Richard Feinberg, UC San Diego, USA</p>
11:15-11:30	Coffee Break
11:30-1:00	<p>PANEL 6: TRADE AND ECONOMIC INTEGRATION</p> <p>Chair: Yang Zerui, China National Committee for Pacific Economic Cooperation</p> <p>Production Networks in the Asia-Pacific Region: Facts and Policy Implications Daisuke Hiratsuka, Institute of Developing Economies, JETRO, Japan</p> <p>Strengthening Regional Economic Integration and Expanding Trade Jeremy Firster, Shih Chien University, Chinese Taipei</p>

	<p>Tony Sowang Kuo, Shih Chien University, Chinese Taipei</p> <p>The Importance of Intra-industrial Trade between ASEAN-7 and the AIP: A Mechanism to Strengthen Economic Integration and Expand Trade Across the Pacific</p> <p>Adriana Roldán, Universidad EAFIT, Colombia</p> <p>Camilo Pérez, Universidad EAFIT, Colombia</p> <p>Discussant: Erlinda Medalla, Philippine Institute for Development Studies</p>
1:00 –2:00	<p>LUNCH AND KEYNOTE ADDRESS</p> <p>Mignonne Chan, Chinese Taipei APEC Study Center, Chinese Taipei</p>
2:00-3:30	<p>PANEL 7: REGIONAL TRADE INSTITUTIONS</p> <p>Chair: Jean Luc Le Bideau, Vice-Chair, France (Pacific Territories) National Committee for Pacific Economic Cooperation</p> <p>More Than A “Talk Shop”—APEC and the FTAAP: The Role of APEC in the Governance of Regional Economic Integration within the Asia-Pacific Region</p> <p>Paul J. Davidson, Carleton University, Canada</p> <p>Multilateralizing Regionalism: New Evidence and Arguments for APEC's Agenda</p> <p>Andrey N. Spartak, All-Russian Academy of Foreign Trade, Russia</p> <p>Pavel Kadochnikov, All-Russian Academy of Foreign Trade, Russia</p> <p>Evolution of the Asia-Pacific Regional Trade Architecture: Stocktake and Future Outlook</p> <p>Robert Scollay, University of Auckland, New Zealand</p> <p>Discussant: Dennis McNamara, Georgetown University, USA</p>
3:30-4:00	Coffee Break
4:00-5:30	<p>PANEL 8: ISSUES IN APEC INTEGRATION</p> <p>Chair: Vinod Aggarwal, University of California at Berkeley</p> <p>Strengthening Financial Market Stability in APEC Economies</p> <p>Sri Adiningsih, Universitas Gadjah Mada, Indonesia</p> <p>Muyanja Ssenyonga, Universitas Gadjah Mada, Indonesia</p> <p>A.Ika Rahutami, Universitas Gadjah Mada, Indonesia</p> <p>Laksmi Yustika Devi, Universitas Gadjah Mada, Indonesia</p> <p>Rosa Kristiadi, Universitas Gadjah Mada, Indonesia</p> <p>How Does APEC Continue its TILF Process Toward the Final Bogor Goals?</p> <p>Ippei Yamazawa, Hitotsubashi University, Japan</p> <p>Managing the Threat to Trade and Competition in APEC Economies of the Misuse of Sustainability Standards</p> <p>Alan Oxley, Royal Melbourne Institute of Technology, Australia</p> <p>Discussant: Chai Yu, Chinese Academy of Social Sciences, China</p>
5:30-6:30	<p>DISCUSSION OF ASCC FINDINGS AND RECOMMENDATIONS</p> <p>Prof. Vinod K. Aggarwal, Berkeley APEC Study Center, UC Berkeley, USA</p> <p>Prof. Richard E. Feinberg, APEC Study Center, UC San Diego, USA</p> <p>Co-Chairs, U.S. APEC Study Centers Consortium</p> <p>Response by SOM Ambassador Roberto Zapata from Mexico</p>
6:30	Conference ends

1. APEC's Green Growth Strategy and the United Nations Conference on Sustainable Development

INTRODUCTION

On 4th-6th June 2012, the United Nations will be observing the fortieth anniversary of the 1972 UN Conference on the Human Environment, the twentieth anniversary of the 1992 UN Conference on Environment and Development (also known as the Rio Earth Summit), and the tenth anniversary of the 2002 World Summit on Sustainable Development (WSSD) when it hosts the United Nations Conference on Sustainable Development (UNCSD) in Rio de Janeiro. The Asian Pacific Economic Cooperation (APEC),¹ on the other hand, will be entering its nineteenth year since sustainable development first appeared on its agenda in 1993. This subject received a recent boost when the United States assumed the chair of APEC and listed sustainable growth as one of three key goals. The 2011 APEC Summit is set to revisit the Yokohama Vision, which has identified sustainable growth as one of five growth strategies for the APEC member economies going forward.

As the world embarks on the road to Rio+20, now is a timely moment to analyze APEC's green growth strategy in the context of the UNCSD. There are two motivations for this research. One, sustainable development has arguably made limited progress over the past 20 years, despite global enthusiasm immediately following the 1992 Rio Earth Summit. Hence, it is practical to assess what worked and what didn't, so as to maximize the chances of success for APEC's green growth strategy. Two, the problems addressed by sustainable development are global in scale. Thus, not only can global developments serve to inform and assist APEC in its regional work, achieving the objectives will also require clear and integrated policies at the global, regional, and national levels.

¹Asian Pacific Economic Cooperation (APEC) was established in 1989 for the goal of regional economic cooperation and development. APEC's 21 member economies account for 45% of the world population, 55% of global economics, 60% of global energy demand, 50% of trade value, two of the world largest economic entities (United States and Japan), two BRIC countries (China and Russia), and three of five members of the UN Security Council (China, Russia and United States). APEC thus, in many senses, represents half of the world.

This paper is divided into three sections. The first two are loosely based on the two themes of the UNCSO: (1) a green economy in the context of sustainable development and poverty eradication and (2) the institutional framework for sustainable development. The first section introduces the concepts of sustainable development, green economy/growth, and APEC's activities to achieve these objectives. The second examines the progress of sustainable development both in the APEC and global contexts. The final section provides recommendations for the problems raised in section two, with an emphasis on institutional reform for APEC and non-institutional reform for the APEC member economies.

1. GREEN ECONOMY AND GREEN GROWTH

Sustainable Development—The Prelude

The concept of sustainable development² emerged from academic seminar rooms about two decades ago out of a recognition that the three pillars of sustainable development: economic development, environmental protection, and social equity should not be treated independently of each other. This is because addressing any of the pillars in isolation without considering their interactive effects can give rise to unanticipated consequences, and the weakening of any one pillar can lead to problems in the others. For example, it is now widely understood that environmental degradation undermines the achievement of developmental goals and contributes to a growing gap between the rich and the poor.³ Sustainable development thus provides a framework which makes the case that boosting the economy, protecting natural resources, and ensuring social equity are not conflicting but interwoven and complementary goals (Dernbach 2002). With the world facing multiple existing and emerging challenges (e.g. climate change, food security, the economic crisis, etc.), sustainable development remains as, if not more, relevant than ever.

A Brief Introduction to Green Economy and Green Growth

Due to the multifaceted and somewhat nebulous agenda of sustainable development, the concepts of green economy and green growth has been introduced as an operational strategy of economic system change where investments in ecological resources and services acts as a driver of economic development.⁴ Hence, green economy/growth is regarded as a subset – not a replacement – of sustainable development. Furthermore, green economy/growth is meant to dispel the prevalent myth that there is an inescapable trade-off between environmental sustainability and economic progress, and provide an alternative paradigm that offers the

² The most common definition of sustainable development, “Development that meets the needs of current generations without compromising the ability of future generations to meet their own needs.” was popularized in the landmark publication *Our Common Future* (known as the Brundtland Report) in 1987.

³ The poorest of the poor often depend heavily on natural resource use and the maintenance of biological diversity. Environmental degradation therefore disproportionately affects and undermines the livelihoods of the rural poor.

⁴ A green economy is generally defined as an economy where economic prosperity and ecological sustainability can be achieved simultaneously. Green growth is generally defined as the process of greening the conventional economic system and a strategy to arrive at green economy. While some argue that a precise definition is not necessary, others argue that imprecision can be a source of dispute as, for example, when trading partners have different understanding of what constitutes a “green” production or production method.

promise of growth while protecting the earth's ecosystems. This is important because while economic development has brought prosperity to much of the world in the past twenty years⁵, it has also led to problems such as environmental degradation and resource depletion. But despite the advantages green economy/growth may bring, there is concern that the social equity pillar of sustainable development is being ignored in this paradigm. After all, while economic progress often fosters social progress, the link is not automatic. As a result, how challenges such as poverty eradication, ensuring gender equity, or achieving universal primary education can be addressed in the context of green economy/growth is an area of emphasis for the 2012 United Nations Conference on Sustainable Development.

The discussion above highlights the complexity involved in transitioning to a pathway of green economy/growth. As the term implies, a green economy will require many changes to the framework of national economies, such as adjustments to the structure of capital and labor supply. To illustrate, some of the existing capital for energy production may become obsolete or redundant when nations transit into a low-carbon economy. Not only will this bring about additional costs compared to a business-as-usual scenario, jobs may also be lost as the sector is reorganized. Even in the favorable case where a green economy would result in net job creation at the national level, questions remain as to how the new jobs will compare in terms of skill and remuneration with those lost through structural change, and what can be done to retrain displaced workers quickly (United Nations 2011b). Given the differences between each country's natural, human capital and relative level of development, the ability to move towards a pathway of green economy/growth will vary considerably between nations. Accordingly APEC, in conjunction with other international organizations such as the United Nations and the European Union, have central roles to play in designing the policy framework and enabling conditions to ease the transition toward this pathway.

APEC's Activities to Achieve Green Growth

APEC has initiated a broad range of activities in order to achieve its green growth strategy. For example, the Fukui Declaration on Low Carbon Paths to Energy Security has highlighted the importance of energy security (e.g. strengthening the ability to respond to oil supply disruptions), energy efficiency (e.g. reducing energy intensity by at least 25% between 2005 and 2030, promoting the Peer Review on Energy Efficiency⁶), and clean energy supply (e.g. accelerating renewable energy, carbon capture and storage, and smart grid deployment, etc.). Furthermore, APEC is also aiming to lower the trade barrier for Environmental Goods and Services (EGS). This is important because the trading system between countries can have significant influences on green economic activity. For example, systems that focuses on 'green' can enable, rather than obstruct, products that use less energy and produce less greenhouse gases to be used more widely among member economies (APEC 2010). If designed properly, they can also minimize the non-tariff barriers (e.g. harmonizing different testing procedures, certification processes, standards) that can cause delays and increase the

⁵According to World Bank data, world GDP grew from \$24.5 trillion in 1992 to \$58.3 trillion in 2009, an increase of 137%. World CO₂ emissions from the burning of fossil fuels and the manufacture of cement grew from 22.4 gigatons in 1992 to 30.6 gigatons in 2007, an increase of about 37%.

⁶ The PREE is particularly important because it would be difficult to improve on something for which one does not know the baseline. Hence, APEC should, in collaboration with other multilateral institutions such as the International Energy Agency, the World Bank, and United Nations, conduct comprehensive and credible assessments of economic, environmental, and social indicators for the purpose of informing the measures recommended in this paper.

cost to do business. Moreover, APEC is looking to improve cooperation not only between the different subsidiary bodies of APEC, but also with other international organizations such as the UN, OECD, and the Major Economies Forum. Finally, APEC is working on sustainable forest management and rehabilitation, where the goal is to increase forest cover by at least 20 million hectares of all types of forests by 2020. All of these activities are put into practice in APEC's Low Carbon Model Town (Tianjin, China being the first test case) which integrates all of the components for a low carbon economy into a livable, workable, and comfortable city. These and other activities, such as eliminating fossil fuel subsidies, promoting private investment in green industries, and promoting green jobs training, are all areas APEC will focus on to achieve its green growth strategy (APEC 2011).

2. PROGRESS OF SUSTAINABLE DEVELOPMENT IN APEC AND THE GLOBAL CONTEXTS

Given the relative novelty of green growth, it is too early to predict whether this paradigm would be slower growth, faster growth, or merely growth of a different kind. And since there is no established or predefined blueprint for policy makers to follow, the shift to a green growth strategy will be a process of learning by doing. Changing the growth paradigm from “develop now, clean up later” to one that seeks to capture the synergies between environmental protection and economic development will therefore be challenging for both developed and developing countries alike. To maximize APEC's chances of success in transitioning to a green growth pathway, it may be useful to look back at the twenty-year history of sustainable development globally to see if any lessons can be learned. After all, green growth is an integral part of sustainable development, thus many of the issues will be broadly applicable both globally and regionally. Having an understanding of what worked and what didn't will therefore allow APEC's leaders to avoid repeating the mistakes that have hindered its implementation.

The Gloomy Picture of Sustainable Development

Over the past 20 years the world has witnessed numerous conferences on sustainable development both at the global and regional levels. With over 500 conventions and instruments established since 1992 and with more than 100 countries reporting that they are currently implementing a national sustainable development strategy (United Nations 2011), it may seem as if the world is implementing the sustainable development agenda fully and effectively. Unfortunately, implementation has been hindered by a diffuse and fragmented framework, overlapping and duplicating activities, and ad hoc and inconsistent execution (United Nations, 2010b).⁷ Furthermore, the high-level meetings have not produced concrete action items but instead have resulted in broad and sweeping declarations that offer something for everyone but do not demand any change of perspective. Moreover, problems are often discussed as remediable through homogeneous global solutions even though it is clear that no

⁷ Various options to promote better integration of the three pillars and coordinate existing work programs are being discussed leading up to Rio+20. One option is to reform the Commission for Sustainable Development (CSD) and strengthen its mandate. This is important because the CSD currently has no power to require action from decisions made at international meetings, it does not report to the United Nations General Assembly, and has insufficient financial resources to operate effectively. Another suggestion is to establish a completely new institution such as the ‘Sustainable Development Council’, using the establishment of the Human Rights Council as a precedent. A third option is to strengthen the UN Environmental Programme (UNEP), or to establish a specialized agency such as a World Environmental Organization (WEO).

single, homogeneous model mandated by an international authority is suitable for every community on the earth. This is troublesome because what is most needed, most appropriate, or workable depends heavily on the context, as the needs of different areas of the world are as diverse as their geographical and cultural surroundings. In short, sustainable development has practical relevance only if it can accommodate local preferences and capabilities.

The gloomy picture of sustainable development is not news, as various commentaries have drawn attention to this problem for more than a decade. To illustrate, a report prepared in 1997 ahead of the Rio+5 Forum to review global compliance with pledges made at the 1992 Rio Earth Summit stated while some “remarkable progress” has been made at the local level, “far too few countries, companies, institutions, communities and citizens have made the choices and changes needed to advance” the goals of environmental health, economic prosperity, social equity and general well-being (Son 1997). Ahead of the WSSD (also known as Rio+10) in 2002 it was pointed out that, “...almost 10 years after Rio, the sustainable development agenda has failed to be implemented...The nexus between environment and development that was affirmed in Rio has been weakened, if not broken, in policy and political terms” (Kibel 2002). More recently, one commentator has observed that the pace, scale and depth of progress towards sustainable development has been inadequate; the root causes of unsustainability remain firmly in place even if some symptoms have been tackled; and most people do not yet ‘feel the burn’ to act, whether in government, business or as individuals (Bass, 2007). Even though there is no globally accepted metric to measure the success and/or failure of sustainable development, increasing environmental degradation and persistent poverty gives empirical evidence that the sustainable development agenda has not been adequately realized.

Reasons for Limited Progress

While progress at the international level has languished, achieving the goals of sustainable development has also remained elusive among the APEC member economies. To illustrate, per capita emissions has increased across the APEC region despite steady improvement in environmental production efficiency. Furthermore, current patterns of production and resource consumption are placing heavy stresses on many ecosystems and on critical life-support systems (APEC Policy Support Unit 2010). It is beyond the scope and intention of this article to review all of the reasons why sustainable development has been unable to fundamentally alter the way societies manage their economic, social, and environmental affairs.⁸ Nevertheless, some of the more important reasons are examined below:

Lack of a Strong and Coherent Framework for Implementation

The international census on sustainable development envisaged integrated decision-making at the national and local levels. At the global level, the Commission for Sustainable Development (CSD) was created to monitor, follow-up, and ensure that the agreements reached at the Rio Earth Summit are implemented at the local, national, regional, and international levels. At the regional level, regional commissions have organized ministerial conferences and implementation meetings. At the national level, a number of institutional formats have emerged, including national sustainable development councils, national sustainable development strategies, incorporation of sustainable development goals in other

⁸ See generally Victor (2006), Carroll (2009), and Drexhage and Murphy (2010).

processes or institutions, etc. At the local level, Agenda 21⁹ processes have been developed by urban municipalities and other localized institutions. Perhaps inevitably, this variegated process has compromised the global implementation of the sustainable development agenda (United Nations 2010b).

APEC, on the other hand, is not a rule-making institution and thus it is not empowered to issue or enforce directives over its members. In other words, member economies abide by the rules voluntarily and no enforcement mechanisms are in place to compel compliance. This ‘soft law’ approach is favorable in one sense because it prevents developed member economies from imposing ‘one-size-fits-all’ practices onto developing member economies. It also allows the culturally, socially, politically, and economically diverse group of APEC member economies at different stages of development to pursue recommendations at their own pace and as needed. But while this approach has helped to cultivate a ‘culture of cooperation’, the lack of a formal institutional structure to implement, monitor, and enforce commitments have weakened APEC’s ability to carry out the sustainable development agenda.

Moreover, APEC has a system where the chair rotates among member economies on an annual basis. Not only does the arrangement generate unrealistic expectations for each Leaders’ and Ministerial meeting to produce ‘action plans’ or political deliverables, it also leads to a disruption of institutional continuity (Avila 2000). This has, perhaps inevitably, resulted in disjointed efforts to achieve the goals outlined in the joint declarations, making them little more than statements of intent.

Lack of Legally Binding Targets and Timetables

Setting specific targets and timetables is particularly important because the issues of sustainable development will take decades to address (National Research Council 1999). This long timeframe can easily dissuade decision makers from feeling compelled to take any action, especially when the outcomes are beyond the retirement date, political term of office, and the immediate problems they confront on a daily or weekly basis. Furthermore, targets and timetables can, if properly established, provide a specific and measureable way of moving the sustainable development agenda from rhetoric toward reality.¹⁰ Moreover, achieving discrete, short-term goals will help governments learn how to address specific problems and gain the confidence and experience for further implementation.

Without legally-binding targets and timetables, the goals outlined in Agenda 21 and other high-level summits have become little more than aspirational goals. For example, the Johannesburg Plan of Implementation, which set out new commitments and priorities for action on sustainable development, agreed to “substantially increase the global share of renewable energy sources with the objective of increasing its contribution to total energy supply.” Yet, neither a date nor a percentage share was specified. Furthermore, countries agreed to maintain or restore fish stocks “on an urgent basis and where possible not later than 2015”, but a specific deadline was also not stipulated.

⁹ Agenda 21 was the major outcome of the Rio Earth Summit. It “is a comprehensive plan of action to be taken globally, nationally and locally by organizations of the United Nations System, Governments, and Major Groups in every area in which human impacts on the environment.”

¹⁰ While targets and timetables are important, they are not enough by themselves. They must be complemented by legal commitments and resources to achieve them.

Nevertheless, it is important to note that while international targets and timetables can put pressure on national governments to adopt the same or similar objectives, nations may be unwilling to be bound by them under international law. This is a major concern for APEC because one of APEC's key characteristics is that it allows countries to take on commitments as needed and at their own pace. Hence, member economies can conceivably delay action towards green growth as long as they wish without consequence. This makes the agreements negotiated at international conferences and assented to by national governments seem unimportant, especially when they are not ratified and adopted at the national and local levels.

Sustainable Development Remains Fundamentally an Environmental Issue¹¹

Sustainable development was intended to encompass multiple dimensions. However, the CSD and many national councils on sustainable development have historically been dominated by staff from the environmental ministries. As a result, parties devote most attention to the environmental protection pillar while discussions on economic development and social equity are marginalized. This is problematic because the narrow scope of discussions necessarily limits the impact of both the CSD and the national councils on sustainable development. Furthermore, since ministers of the environment usually have fewer resources, influence, and control over policy tools than ministers of industry, economy, or trade, the sustainable development agenda ends up having little impact in mainstream decision making.

This shortcoming is not really applicable to APEC because APEC's primary mission is to support sustainable economic growth and prosperity in the Asia-Pacific region. Hence, instead of having sustainable development be treated fundamentally as an environmental issue, APEC's chief concern is that environmental and resource concerns are rarely the primary focus of the working groups where the sustainable development agenda are to be carried out (the Energy, Fisheries, and Marine Resources Conservation Working Groups are notable exceptions). Starting a trend where economic and development ministries are present to participate in the decision making process is an area where APEC can play a leadership role to enhance the global efforts for achieving sustainable development.

Competing Agendas between Developed and Developing Countries

Competing agendas from developed and developing countries underlines the difficulties in pursuing an integrated strategy for sustainable development. For example, developing countries have feared that the developed world's concern about the environment (e.g. climate change, biodiversity loss, deforestation, and declines of the world marine fisheries) would overshadow their interest in development (e.g. liberalization, debt relief, poverty reduction, and increase in foreign developmental assistance). This fear became reality at the Rio Earth Summit, where three instruments on global environmental governance: the UN Framework Convention on Climate Change (UNFCCC), the Convention on Biological Diversity, and the non-legally binding Statement of Forest Principles were established. However, comparable treaties or commitments on economic and social development did not materialize.

¹¹ There has been a trend over the past 40 years to place greater emphasis on development and social issues and less on simply protecting the environment. To illustrate, the United Nations Millennium Declaration adopted by the UN General Assembly in 2000 undoubtedly played a major role in shifting negotiations at the 2002 WSSD away from environmental protection and towards social and development.

Although the developing (especially sub-Saharan Africa) countries-focused United Nations Conference to Combat Desertification (UNCCD) was adopted in 1994 (stemming from a direct recommendation of Agenda 21) and came into effect in 1996, this distrust has not subsided up to this day.¹² Leading up to Rio+20, some developing countries are worried that the concept of green economy/growth is a form of green protectionism which will lead to stricter conditions and rules on development aid and international trade. Hence, serious questions are being asked about whether green economy will add value or be detrimental to the multilateral framework of sustainable development. If greening the economy were to lead to trade restrictions through unilaterally imposed standards or border-price adjustments, most of the impact would likely fall on developing countries. With small and medium enterprises lacking the capacity to comply with stricter requirements, this could lead to market loss, reduced national export capacity, reduced growth, etc. (United Nations 2011).

One example of competing interests between developed and developing countries in APEC is the ongoing debate over phasing out inefficient fossil fuel subsidies. Subsidy reform is widely recognized as an important policy tool to combat the adverse effects of climate change and is under serious consideration by international organizations such as G20 and the OECD, composed of exclusively developed countries. However, developing nations, such as China, have argued vigorously that the subsidy reform should be focused not only on reducing subsidies, but also on social impacts and the welfare of vulnerable groups. Otherwise, this policy option may undermine the overall quality of living by neglecting its negative effects on society.¹³

3. RECOMMENDATIONS TO ENHANCE IMPLEMENTATION OF GREEN GROWTH IN APEC

Section 2 highlights several reasons why the sustainable development agenda has not been fully achieved. This section seeks to address these challenges and presents a range of policy options to reinvigorate and enhance the implementation of green growth in the APEC region. Since APEC member economies are generally keen to limit bureaucracy and constrain formal institutional development, or “governance without government” (Larsky and Hunter 1997), the challenge is to improve coordination without instituting too many bureaucratic processes into APEC’s Secretariat and institutional framework. Two categories of recommendations are proposed: institutional reform for APEC and non-institutional reform for the APEC member economies.

¹² A manifestation of this distrust is evident from the contentious and ongoing UNFCCC negotiations, which pit the interests and responsibilities of the developed nations against those of the developing nations.

¹³ Developed countries are also considering the effects phasing out fossil fuel subsidies may have on their poorer households. For example, a current OECD report states, “the distributional effects of subsidy reform and environmental fiscal reform need to be examined carefully. Low income households can be vulnerable to these reforms as the percentage of their expenditure of water and energy is much higher compared to rich households; although the extent to which costs are born by the rich or the poor differs at country and regional levels” (OECD 2011).

Institutional Reforms¹⁴

Laws can give the concept of green growth legitimacy but implementation will require solid governance structures and a proper appropriation of resources. This paper recommends three areas where APEC should focus on strengthening/establishing to enhance its institutional capacity without turning it into a more Western-style contract-based legal institution. The three areas are: strengthening the Economic and Technical Cooperation (ECOTECH) workplan, establishing a monitoring, reporting, and verification (MRV) system, and establishing a centralized dispute settle mechanism.

Strengthen ECOTECH

There is no way to avoid providing additional aid (financial assistance, technology transfer, skills training, etc.) to developing countries if the goals of green growth are to be met.¹⁵ This is crucial, as a shortfall in financial assistance after the Rio Earth Summit was identified as a major reason why implementation of the sustainable development agenda has experienced less-than-expected progress (Dernbach 2002).¹⁶

With a diverse membership, APEC offers the opportunity to create a broad and cooperative framework for regional cooperation and developmental assistance.¹⁷ APEC is equipped with ECOTECH for the purpose of promoting economic and social development of its member economies to reduce inequalities among its members. However, the activities of ECOTECH have not been given enough attention as Trade and Investment Liberalization and Facilitation (TILF). Currently, ECOTECH reports to the Senior Officers while TILF reports directly to the APEC Ministerial Meetings. In order to promote green growth, it is necessary to elevate ECOTECH to have a similar status as TILF in APEC's hierarchy and equal access to Ministers and Leaders (Szzvedra-Rivano 2007). Furthermore, it is necessary to allow ECOTECH to have the capacity and authority to launch and fund projects. Member economies should realize that not having an equal footing and collaboration between the two will seriously undermine the overall effectiveness of APEC (APEC SOM 2010).

¹⁴ In 2004, APEC Leaders endorsed a work program called the Leaders' Agenda to Implement Structural Reform (LAISR). Overseen by the Economic Committee, LAISR seeks to achieve economic growth and support APEC's goal of trade and investment liberalization through with initiatives in five key areas: regulatory reform, competition policy, corporate governance, public sector governance and strengthening economic and legal infrastructures. In the 2010 Leaders' Meeting in Yokohama, APEC Leaders endorsed the APEC New Strategy for Structural Reform (ANSSR). Going forward to 2015, ANSSR will further stress the importance of structural reform to promote more open, well functioning, transparent, and competitive markets, etc.

¹⁵ Technology transfer from developed to developing countries is crucial to achieving equity in a green economy. This is because an environmentally-focused growth paradigm will necessarily promote technologies that are mastered mostly by developed countries. This may result in a loss of competitiveness of developing countries in key "green industries, further increasing the technological gap.

¹⁶ While assistance from developed to developing member economies is important, cooperation and aid between developing countries cannot be ignored. Many developing economy experiences and successes in achieving a green economy can provide valuable ideas and means for other developing economies to address similar concerns. Besides, cooperation between developed economies may be able to increase the flow of information, expertise, and technology at a reduced cost.

¹⁷ It is true that national governance in many countries need to be made more effective, both to reduce the need for aid and to increase the likelihood that aid will be used effectively. Hence, improving assistance in the form of enhancing governance must be the priority in a number of developing countries.

Establish a Monitoring, Reporting, and Verification System

Targets and timetables are most useful when they are effectively monitored and reported to see whether or not they are meeting their commitment. Hence, a mechanism should be established within APEC to overlook the implementation process, coordinate the task of various working groups and committees, and monitor the member economies to see whether they are meeting their commitments. Having a tracking and reporting system would reward the leaders and, at a minimum, oblige the laggards to explain why they are behind. It might also put pressure on all member economies to find ways to assist those falling behind get back on track (Dernbach 2002). As a side benefit, the MRV process will give greater clarity on how policies set by APEC and statements made by Leaders are being translated into practical programs. Most importantly, it guarantees the continuation of action plans will continue within APEC member economies despite the changes in APEC's chair each year.

Establish a Centralized Dispute Settlement System

A centralized dispute settlement system would be useful as an arbitration system to avoid the legal hurdles and expenses that might or might not be borne by the developing countries. Currently, all APEC member economies have dispute mediation systems in place but their fragmented nature has led to some challenges (APEC Policy Support Unit 2010).¹⁸ For example, it is difficult to determine which system prevails when a member economy's adherence to a multilateral environmental agreement is seen as a violation of trade obligations.¹⁹ Furthermore, member economies may end up forum shopping for systems that are most beneficial for their respective positions, leading to more complexities. Thus, establishing a centralized dispute settlement system where all APEC member economies can work out their differences is a critical component towards achieving the goals of green growth.

Non-Institutional Reforms

Strong Political Commitment for Green Growth

Strong political commitment is crucial because the best institutions, arrangements, and mechanisms will not work to their maximum effect if political commitment is weak or nonexistent. After all, weak implementation of sustainable development may not just be an institutional problem but the result of weak political commitment as well. Thus, renewing and strengthening the political commitment for green economy and sustainable development has been highlighted as a key goal in the preparatory process towards Rio+20.²⁰ Among other

¹⁸ Dispute settlement systems used by APEC member economies include New York Convention, the WTO dispute settlement Understanding, the UNCITRAL Model Law on International Commercial Arbitration, or the International Convention on the Settlement of Investment Disputes. APEC economies could also use dispute settlement systems included in their bilateral RTA/FTA or Bilateral Investment Treaties.

¹⁹ For example, Korea's new vehicles fuel efficiency rule of 17 km/liter was regarded as trade barrier for the American automobile industry, which follows the standard of 14.6 km/liter. This has led to a dispute between the two countries.

²⁰ Commitments should ensure that the green economy does not lead to green protectionism. To ease the doubts of developing countries, it is necessary to emphasize that the principle of common but differentiated responsibilities should remain as the standard to be followed. Hence, countries will retain the flexibility to set their own path towards sustainable development and to take on green economy agenda in accordance with their national interests. Furthermore, since it is relatively difficult to ascertain environmental protection measures against green protectionism, it is questionable whether the

things, the level of a country's political commitment is measured through legislation and policy at the national and regional levels. Factors such as budgetary allocation, development of institutions, and stakeholder participation are strong indicators of political commitment translated into action (United Nations 2011a).

Strong Policies and Regulations for Green Growth

Strong policies are required to prioritize government investment and spending in areas that stimulate green growth, while limiting them in areas that deplete natural capital. For example, governments can stimulate markets by using government procurement practices that create high-volume and long-term demand for green goods and services.²¹ Doing so will stimulate the private sector to make investments and innovate in green goods and services, promoting sustainable consumption. Furthermore, since government investments in infrastructure can lock in patterns of private investment that remain for many years (e.g. different ways of developing road or rail networks will lead to transportation patterns and industry location that will either be environmentally beneficial or harmful), strong “green” policies are crucial to ensure sustainability going forward. Poorly managed government spending, on the other hand, can be both environmentally harmful and economically costly. For example, artificially lowering the price of goods through subsidization not only reduces the profitability of green investments, but can also encourage waste and overuse of finite resources. Moreover, subsidization can also make unsustainable fuels and activities artificially cheap or low risk, thus biasing the market against investment in green and more sustainable alternatives (UNEP 2011).

In addition to policies, strong regulations can also spur renewable energy generation, energy efficiency deployment, and other green activities. For example, creating minimum technical standards²² (e.g. requirements on products and/or processes and production methods) and labeling programs can help ‘push’ and ‘pull’ the market towards greener goods and services. Moreover, a green tax²³ or a tradable permit system can be deployed to “internalize” the negative externality cost into the price of a dirty good or service.²⁴ While green taxes are usually thought of being applicable only to developed countries, developing APEC member economies such as China, Malaysia, Philippine, and Thailand have successfully used some level of environmental taxation since the 1970s and 1980s (Bluffstone 2003). Conversely, an

existing APEC institutional arrangements have the capacity to adjudicate these distinctions. Hence, it is important not only to make green growth a transparent goal, but APEC's collaboration with other multilateral agencies must be enhanced in order to use their expertise for decision making.

²¹ Public procurement accounts for an average of 23% of GDP around the globe. The number approaches 50% for some countries like Brazil and India. In the OECD, the average is closer to 15%.

²² Poorly designed standards can either be met anyway without any additional effort or act as a non-tariff barrier for SMEs in developing countries who can't meet those standards. Hence, standards must be designed to achieve environmental protection while safeguarding market access.

²³ The revenue raised from green taxes can be recycled back into other parts of the economy, keeping the overall tax burden unchanged. This will be crucial in making these taxes more politically acceptable.

²⁴ Taxes fix a price for pollution and then allow the market to determine the level of pollution. Tradable permits, on the other hand, first establish an overall level of pollution and then let the market determine the price.

APEC regional cap-and-trade system similar to that of the European Union's Emissions Trading Scheme may be instituted instead of a taxation system. Regardless of which system (or a combination thereof) is implemented, strong regulations are crucial to promoting more innovation and investment towards green growth.

Strengthening Multi-Stakeholder Engagement

Existing literature has noted an apparent disconnect between the bodies making the decisions and the bodies responsible for implementing the sustainable development agenda, leading the latter to feel weak ownership of those decisions. Hence, integrating staff at the working group level into the policy design process will be useful in making sure that all of the various stakeholders are on the same page. More generally, there should be greater coordination between top-down policies with bottom-up initiatives, between different levels of government, and across sectoral institutions (United Nations 2011b).

The vast, complex, and elusive goals of sustainable development described in the preceding sections may have created the false impression that this is something beyond one's individual capacity to influence and change. This, however, cannot be further away from the truth as the goals of achieving environmental protection, economic growth, and social equity cannot be achieved through passive reliance on public policies and government actions. Fact is, having the active engagement of civil society is a valuable means of implementation at local level, especially but not only where local authorities' capacities and resources are limited. Hence, incentives should be designed to not only send the message that ordinary citizens²⁵ are part of the solution, but to also make them "feel the burn" to act towards green growth (Carroll 2009).²⁶ One thing APEC member economies can do is to draw on the expertise of NGOs according to Article 27(9) of Agenda 21.²⁷ For example, greater NGO engagement in the dispute settlement systems can lead to an increase in the amount and quality of information available to the panel—possibly leading to more informed, higher quality, and fewer erroneous decisions (Charnovitz 1996).

CONCLUSION

The transition to green growth/economy is a new paradigm that focuses on greening the economic system through a system change. Instead of achieving economic growth at the expense of environmental degradation and vice versa, green growth/economy illustrates how economic development and environmental sustainability can reinforce each other to create a

²⁵ "Non-traditional" stakeholders of sustainable development must be engaged to ensure a successful implementation of the sustainable agenda. For example, given that approximately 70% of the world's population is projected to live in cities in 2050, urban planners, architects, and home builders need to be part of the discussion in order to design and construct more sustainable living environments.

²⁶ Knowledge is the preamble to useful action. Hence, investment in public education of the importance of sustainable development may be required before ordinary citizens feel the urge to act. In this process, governments should make it a priority to promote and invest in the education of women and girls. This is important because even though women have a central role to play in environmental, economic, and social life, they are often excluded from formal education opportunities offered to boys and men.

²⁷ Agenda 21, art. 27(9), U.N. DOC. A/CONF.151/26 (1993) states that, all intergovernmental organizations and forums should, in consultation with non-governmental organizations, take measures to: ...enhance existing or, where they do not exist, establish, mechanisms and procedures, within each agency to draw on the expertise and views of non-governmental organizations in policy and program design, implementation and evaluation...

win-win situation. But given that there is no pre-defined blueprint available for policymakers to achieve these dual goals, it is vital that APEC look back at the past 20 years of sustainable development to see if any lessons can be learned.

As an organization for regional cooperation, APEC is well-suited for this task. However, APEC, like many other international organizations, has not been particularly effectively in transition to a pathway of sustainable development. These issues could be summarized by: a lack of political commitment, coordination, integration and collaboration – leading to fragmented and overlapping efforts. Nevertheless, APEC does not have to turn itself into a more Western-style contract-based legal institution to achieve green growth. The Asian model of cooperation and consensus building has its merits especially in an organization where the majority of its members are developing economies. Going forward, APEC should balance its priority in trade liberalization with the three pillars of sustainable development: environmental protection, social equity, and economic growth. A more harmonious focus on both trade and development will bring APEC member economies closer toward the green growth/economy agenda for the eventual aim of sustainable development without the shadow of green protectionism.

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2. A New Geography of Innovation? Opportunities and Challenges Facing the Asia-Pacific Region

INTRODUCTION

Traditionally, Asia-Pacific Economic Cooperation (APEC) has focused on promoting trade and investment liberalization, regarding them as two important drivers of growth. Through individual and collective efforts made toward achieving the Bogor Goals, the Asia-Pacific nations eliminated many barriers to trade and investment. Efforts like these and the resulting increased trade and investment flows have made the region a driving force and engine of growth in the world economy for the past two decades.

Liberalization of both trade and investment remain important. It is increasingly evident, however, that they alone will not sustain economic growth nor improve the welfare of people in the region. Therefore, at the 18th APEC Economic Leaders' Meeting in Yokohama in 2010, APEC leaders set forth the APEC Growth Strategy as the organization's first substantial effort to provide a comprehensive long-term framework for promoting sustainable growth and social good in the region.¹ The importance of adopting policies that foster an environment enabling innovative growth was recognized when it was included as one of the five pillars of the Growth Strategy.²

Research on the role of innovation in economic and social change has proliferated in recent years (Fagerberg 2005, 1). Research on innovation and innovation policies in the Asia-Pacific region is considered particularly timely because of global shifts in innovation capacity to the Asia-Pacific region, which have often been pointed out. For instance, Leadbeater and Wilsdon (2007) argue that the European Union should prepare itself for a world wherein ideas and technologies arise not only from the United States or within the EU itself, but also from regions such as Asia, since the innovation capacity of Asian countries is developing rapidly.

¹See APEC (2010a) for details.

²See APEC (2010b) for details.

Despite the rising innovation capacity of many Asian countries, however, three concerns are evident. First, there seems to be a rising divergence in terms of the innovation capacity among the Asia-Pacific countries (Gill and Kharas 2007). The world does not seem to be flat.

Second, there seems to be much less evidence of new innovation capacity in emerging Asian economies such as those of China and India than is often claimed. Ely and Scoones (2009) concludes that the global redistribution of innovation, while undoubtedly under way, has a long way to go before innovation capabilities worldwide are comparable to those established in the Western world.

Moreover, unlike in the EU, the degree to which Asia-Pacific researchers and firms are engaged in research collaboration and cooperation seems to be small (Sakata 2011). This is a matter of concern with regard to the region's global competitiveness, because worldwide, the spread of inter-organizational or inter-firm networking is widely observed nowadays, especially among high-technology companies.

The purpose of this paper is, therefore, twofold. The first goal is to examine the validity of these rising concerns. The second is to investigate what kind of role APEC can play in removing barriers and narrowing the growing innovation gap in the Asia-Pacific region. This paper hopes to identify the barriers to further regional integration and cooperation within the region and contribute to the creation of robust and sustainable regional growth.

THE GLOBAL REDISTRIBUTION OF INNOVATION

Trends in Global Redistribution of Research and Development

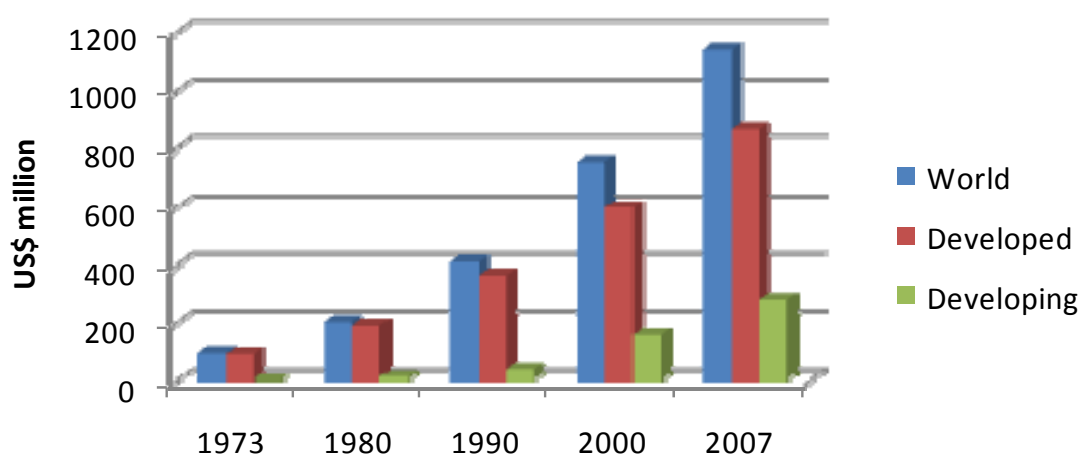
An important development has been the emergence of new indicators of innovation inputs and outputs, including economy-wide measures that have some degree of international comparability (Smith 2005, 148). By far the longest-standing measure of innovation input is expenditure on R&D.

There has been a continuing increase in global expenditure on R&D activities since the 1970s (Arond and Bell 2010, 16). As Figure 2-1 shows, there was a more than tenfold increase in global R&D outlay between 1973 and 2007, from about US\$100 billion to a little over 1.1 trillion. What is notable globally during this period is that the overall share of developing countries in total world R&D activity increased substantially—rising eightfold, from about 2.8 percent to around 24 percent (Arond and Bell 2009, 18).

There are, however, substantial differences between regions and countries within the group of developing countries. Table 2-1 provides a highly condensed overview of trends in global R&D expenditure in terms of shares of the global total and R&D intensity by region/country.³ The changing regional shares of global R&D are clear. Above all, it is notable that the Asian share increased from 1.8 percent in 1993 to 18.9 percent in 2007 (Table 2-1). In fact, the Asian region accounted for about 80 percent of the total increase in developing countries' R&D between 1973 and 2007.

³Expenditure on R&D as percentage of Gross Domestic Product (GDP).

Figure 2-1. Global Distribution of R&D Expenditure, 1973–2007



SOURCE: Based on data from Arond and Bell (2010, 19).

Table 2-1. Global Distribution of R&D Expenditure (GERD), 1973–2007

	1973 (%)		1980 (%)		1990(%)		1999/00(%)		2007 (%)	
	Share	GERD/ GDP	Share	GERD/ GDP	Share	GERD/ GDP	Share	GERD/ GDP	Share	GERD/ GDP
Developed Countries	97.2	2.4	93.4	2.3	89.8	2.3	79.0	2.3	75.9	2.3
North America	33.7	2.3	31.0	2.2	38.2	2.6	37.2	2.7	34.7	2.6
Japan	7.9	NA	10.2	NA	16.3	3.1	13.0	2.9	13.0	3.4
Other Developed Countries	55.6	NA	52.2	NA	35.3	NA	28.8	NA	28.2	NA
Developing Countries	2.8	0.4	6.6	0.4	10.2	0.7	21.0	0.9	24.1	1.0
Asia	1.8	0.4	4.0	NA	6.2	0.8	17.4	1.1	18.9	1.2
China	NA	NA	NA	NA	3.0	0.8	6.7	1.0	9.2	1.5
India	NA	NA	NA	NA	0.6	0.8	2.6	0.7	2.2	0.8
Korea	NA	NA	NA	NA	1.8	1.8	2.3	2.3	3.7	3.5
Chinese Taipei	NA	NA	NA	NA	NA	NA	1.1	2.0	1.5	2.6
Singapore	NA	NA	NA	NA	NA	NA	0.3	1.9	0.5	2.6
Hong Kong, China	NA	NA	NA	NA	NA	NA	NA	NA	0.2	0.8
Other Asian Countries	NA	NA	NA	NA	NA	NA	NA	NA	1.6	NA
Latin America and Caribbean	0.8	0.3	1.7	0.5	2.8	0.5	2.8	0.6	2.9	0.6
Other Developing Countries	0.2	NA	0.9	NA	1.2	NA	0.8	NA	2.3	NA

SOURCE: Based on Annex 1 of Arond and Bell (2010).

Trends in Global Distribution of the Production of Science and Engineering Articles and Patents

Two other indicators of innovation activities, namely, (1) number of patent applications, grants and citations, and (2) number of scientific publications and citations, are often used in innovation studies (Smith 2005, 152). Table 2-2 provides ranks in science and engineering article output and patents granted by the United States Patent and Trademark Office (USPTO) in 1995 and 2007. In 1995, Japan was the only country in Asia ranked among the global top 10 in both scientific publications and patents granted by the USPTO. By 2007, other Asian

countries, including China, Chinese Taipei, and Korea, ranked among the global top 10 in either scientific publications, patents granted by the USPTO, or both. India and Singapore started to follow suit during the same period.

While the US, Europe, and Japan still dominate the global innovation landscape, new Asian players such as China, India, Korea, Chinese Taipei, and Singapore are seen as increasingly important (Leadbeater and Wilsdon 2007). The innovation capacity of the Asia-Pacific region seems to be developing rapidly.

Table 2-2. Ranks in Science and Engineering Article Output and Patents Granted by US Patent and Trademark Office, by Selected Countries

Country	S&E Article Output		Country	Patents Granted	
	1995	2007		1995	2008
US	1	1	US	1	1
China	14	2	Japan	2	2
Japan	2	3	Germany	3	3
UK	3	4	Korea	8	4
Germany	4	5	Chinese Taipei	7	5
France	5	6	Canada	6	6
Canada	6	7	France	4	7
Italy	8	8	UK	5	8
Spain	11	9	China	19	9
Korea	22	10	Italy	9	10
India	12	11	Netherlands	12	11
Australia	9	12	Australia	13	12
Netherlands	10	13	Israel	15	13
Russia	7	14	Switzerland	10	14
Chinese Taipei	18	15	Sweden	11	15
Brazil	23	16	Finland	16	16
Sweden	13	17	India	30	17
Switzerland	15	18	Belgium	14	18
Turkey	34	19	Austria	17	19
Poland	19	20	Singapore	44	20

SOURCE: National Science Board (2010).

INNOVATION IN THE ASIA-PACIFIC REGION: CONVERGENCE OR DIVERGENCE?

A Rising Concern in the Asia-Pacific region

Freeman and Hagedoorn (1995) had already identified in the 1990s global patterns of convergence and divergence of technological development similar to those today. The redistribution of R&D seems to be to a very large extent restricted to developed economies. Except for a few Asian emerging economies, there is a clear divergence with respect to technological capabilities between developing and developed countries (Freeman and Hagedoorn 1995, 54-55).

Gill and Kharas (2007) found similar patterns in divergence and convergence of technological development within East Asia. They found that R&D intensity, defined as expenditure on R&D as percentage of GDP, was twice as high in economies such as China, Korea, and Chinese Taipei as would be proportional to the global average by per-capita income. On the other hand, R&D intensity in Southeast Asian economies such as Indonesia, the Philippines, and Thailand consistently undershot the estimated average relationship over a long period (Gill and Kharas 2007, 148).

If this finding is also true in the Asia-Pacific Region as a whole, this is a matter of great concern for APEC, because Fagerberg and Verspagen (2002) found that since the 1990s it has become scientifically and technologically more demanding to catch up economically. This implies that the differences in the degree of R&D efforts made across countries may cause technological and economic divergence in the Asia-Pacific region in the future.

Innovation-Input Measures: R&D Intensity and Research Personnel

Both convergence and divergence of innovation capacities are observable in the Asia-Pacific region. Table 2-3 shows R&D intensity, defined as expenditure on R&D as a percentage of GDP and research personnel per thousand workers, by country in the region in 1997/98 and 2007/08. Not only advanced economies such as those of Australia, Canada, New Zealand, Japan, and the United States but also Asian Newly Industrialized Economies (NIEs) such as Korea, Chinese Taipei, Singapore, and China have shown steady increases in R&D activities from the perspectives of both expenditure and personnel (Table 2-3). During the 1997/98–2007/08 period, several Asian NIEs reached almost the technological level of advanced Asia-Pacific economies. In certain areas, they have even advanced technological frontiers (Gill and Kharas 2007, 160).

On the other hand, Asia-Pacific countries such as Indonesia, the Philippines, Thailand, Peru, and Mexico are lagging behind in R&D efforts. Not only is R&D intensity low, but it has not changed much since the late 1990s.

Innovation-Output Measure: Scientific Publications

Both convergence and divergence of science and technology development in the Asia-Pacific region are also found in innovation-output measures such as number of scientific publications. Figure 2-2 shows trends in the coefficient of variation⁴ of science and engineering (S&E) articles on a per-capita basis for Asia-Pacific countries during the 1997–2007 period.

As seen in the figure, the coefficient of variation of S&E articles tends to become smaller during the early part of this period, indicating the existence of a strong force of convergence at the initial stage—immediately after the 1997 Asian Financial Crisis. This trend, however, reversed itself in 2003, implying the existence also of a force of divergence in innovation activities in the region.

⁴Coefficient of variation is the standard deviation divided by the average of sample data.

Table 2-3. R&D Intensity and Personnel

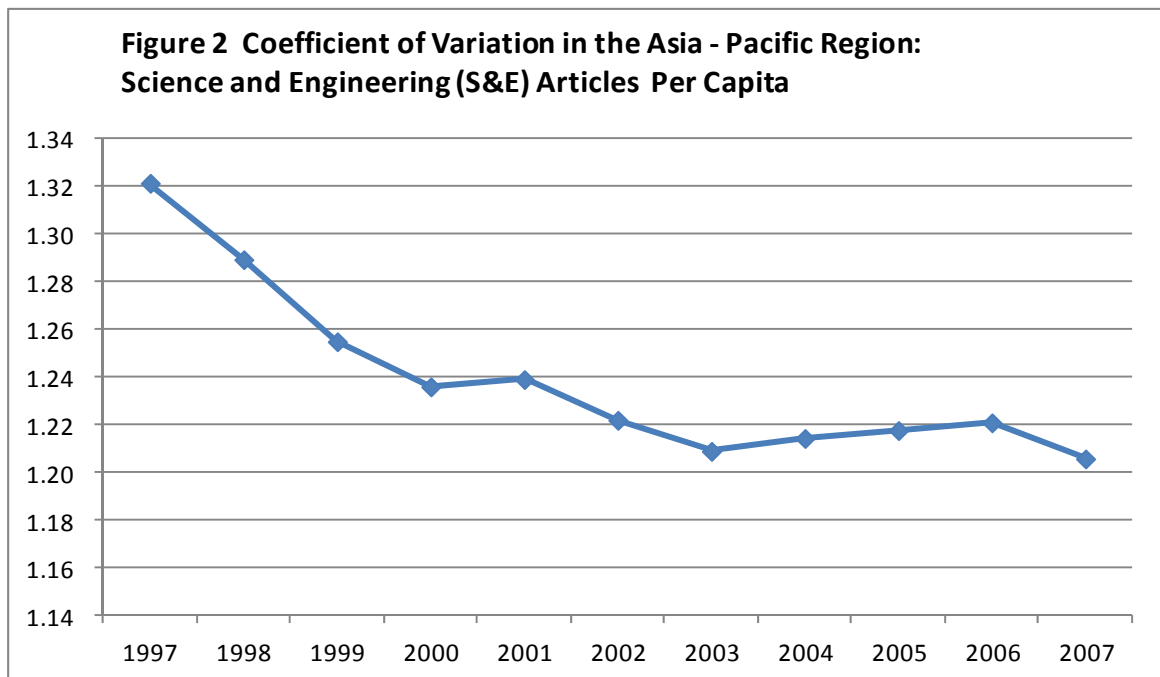
Country	Expenditure on R&D as Percentage of GDP		Researchers per Thousand Workers	
	1997/98	2007/08	1997/98	2007/08
Australia	1.51	2.35	6.7	8.2
Brunei Darussalam	NA	0.02	NA	0.6
Canada	1.71	1.88	6.1	7.8
Chile	0.50	0.68	1.0	2.0
China	0.65	1.43	0.8	1.9
Hong Kong, China	0.43	0.75	2.1	5.1
India	0.70	0.76	0.3	0.4
Indonesia	0.07	0.08	0.5	0.2
Japan	2.94	3.44	9.4	10.1
Malaysia	0.40	0.63	0.4	0.9
Mexico	0.36	0.37	0.5	0.8
New Zealand	1.08	1.17	4.4	8.1
Papua New Guinea	NA	NA	NA	NA
Peru	0.09	0.15	NA	NA
Philippines	0.15	0.11	0.2	0.2
Republic of Korea	2.41	3.29	4.5	9.5
Russian Federation	1.00	1.08	7.1	6.1
Singapore	1.64	2.49	5.5	11.3
Thailand	0.10	0.21	0.1	0.6
United States	2.58	2.71	8.0	8.8
Viet Nam	0.19	NA	0.2	NA

Notes: Brunei Darussalam: average of figures for 2002, 2003, and 2004. Indonesia: figures for 2000 and 2009, respectively. Vietnam: figures for 2002.

SOURCE: <http://stats.ulis.unesco.org/>, last accessed on August 11, 2011.

Figure 2-3 also supports the argument for the existence of both convergence and divergence forces in science and technology development in the region. The figure shows the simple relationship between annual average growth rates in number of S&E articles per capita between 1997 and 2007, and the 1997 level of S&E articles per capita in the Asia-Pacific Region. There is no significantly positive or negative relationship between the two variables, statistically. This implies the existence of both convergence and divergence in science and technology development in the region in the years covered.

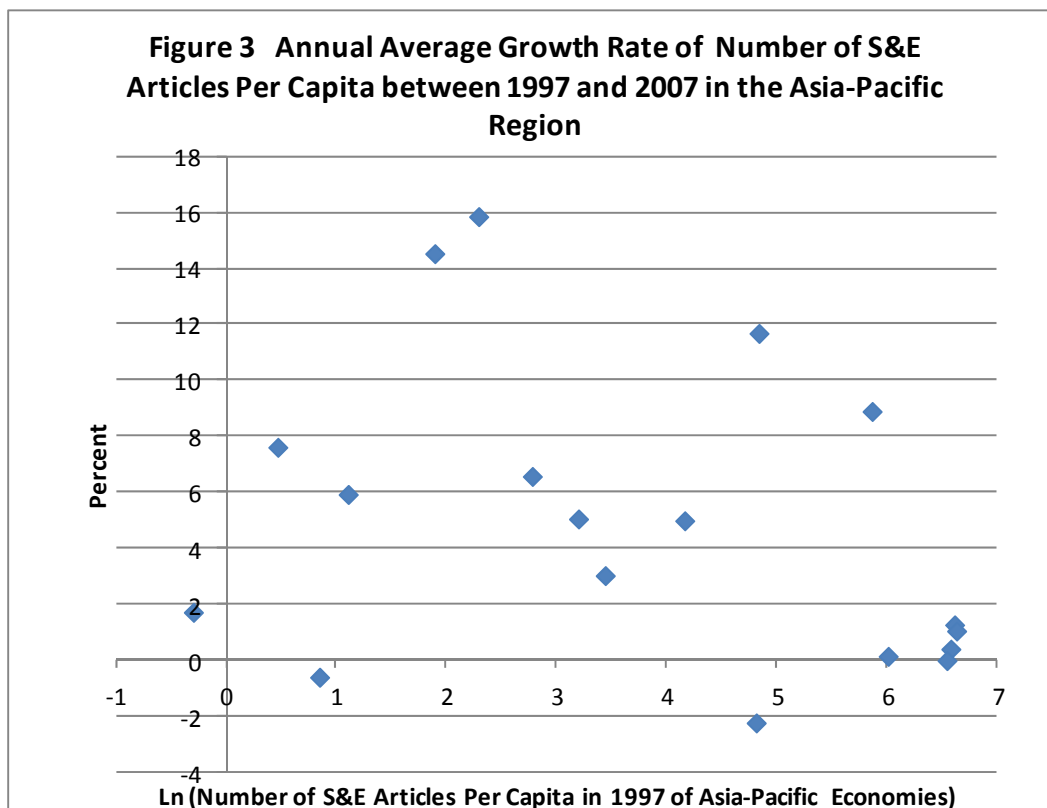
Figure 2-2. Coefficient of Variation in the Asia-Pacific Region: Science and Engineering Articles per Capita, 1997-2007



Note: Three APEC members (Hong Kong, China; Chinese Taipei, and Papua New Guinea) are not included.

SOURCE: Based on data from National Science Board (2010) and World Development Indicators Online.

Figure 2-3. Annual Average Growth Rate of Number of Science and Engineering Articles Per Capita in the Asia-Pacific Region, 1997-2007



Note: See Figure 2-2

SOURCE: See Figure 2-2.

LACK OF LOCAL EMBEDDEDNESS OF INNOVATION IN THE ASIA-PACIFIC REGION

Importance of Local Scientific and Technological Capabilities

Ely and Scoones (2009) argue that global redistribution in innovation, while undoubtedly under way, has a long way to go before innovation capabilities in new centers are comparable to those in established centers, because there is much less evidence of new innovation capacity in emerging economies than is sometimes claimed. They caution us to keep in mind the lack of embeddedness of innovation in emerging economies in particular.

In contrast to neoclassical economists, scholars at Science and Technology Policy Research (SPRU), University of Sussex, as early as the 1970s, rejected the idea that the existing international division of labor in science was adequate for sustainable development and took the view instead that developing countries must have their own scientific and technological capabilities (Ely and Bell 2009, 5). More recently, Sachs (2003) joined them by arguing that the challenges of economic development are not going to be addressed properly until issues of science, technology, and innovation are integrated into the economic-development strategies of low-income countries (Sachs 2003, 131).

The importance of local innovation capabilities in the context of development has received increasing emphasis because the ability to use transferred technology as the basis of further innovations—which is crucial to maintaining competitive efficiency at rising income levels—depends entirely on local scientific and technological capabilities (Ely and Bell 2009, 13).

Local Embeddedness of Innovation in the Asia-Pacific region

Ely and Scoones (2009) found that the participation of Chinese firms in global value chains has delivered growth but that only in a very few cases (such as that of Lenovo) have they become lead firms, which accrue the major proportion of value added through control of key intellectual property or brands: Chinese manufacturing is still largely focused on outsourcing for multinationals (Ely and Scoones 2009, 14).

While the successes of the outsourcing model cannot be denied in India either, the same observation can be made: India's exports of its own software and licensing of its own intellectual property amounted to just US\$450 million in 2008, a very small proportion of total export revenues (Ely and Scoones 2009, 18).

Okamoto (2009) found weak local innovation capacities in Singapore as well. Foreign companies accounted for more than 65 percent of private R&D expenditure in Singapore in 2006. Multinationals dominate not only production but also innovation. Moreover, Okamoto also found Singapore's innovation system to be weak in the linkage between private and public basic research and local business and market applications.

With intellectual property rights often secured by multinational companies based in developed economies, there are relatively few options for local start-ups and other businesses to move up the value chain unless they strengthen their local innovation capacities. Trade and investment liberalization alone will not make the Asia-Pacific region a vibrant center of knowledge production and innovation activities.

GLOBALIZATION OF INNOVATION SYSTEMS IN THE ASIA-PACIFIC REGION

A Distinct Shift Toward a New Mode of Knowledge Production

Gibbons et al. (1994) discovered fundamental changes in the ways in which scientific, social, and cultural knowledge are produced. They found knowledge production increasingly to be a socially distributed process. Moreover, its locus is becoming global.⁵

Globalization of science and technology is also found by Niosi and Bellon (1996). Delocalization of R&D laboratories, soaring numbers of international technological alliances, intense cross-border technology transfer, and overseas scientific and technological collaboration and cooperation are said to be some of its major manifestations in the global economy. Where does the Asia-Pacific region stand in this regard?

Figure 2-4 compares annual average growth rates of total number of S&E articles with those of number of S&E articles coauthored internationally, for selected countries.⁶ Growth rates of internationally coauthored S&E articles higher than those of total number of S&E articles are evident in almost all of the countries, including the Asia-Pacific economies. An increasing number of international authors and studies contend that scientific and technological knowledge in the region is becoming increasingly global.

A Contrast Between the EU and the Asia-Pacific Region

In developing indicators of international collaboration between countries and across regions, researchers have developed statistical techniques that account for the unequal size of countries' S&E article output and coauthorship patterns (National Science Board 2010, 5-37). One of the simplest is the index of international collaboration, defined as the ratio of country A's rate of collaboration with country B divided by country B's rate of total international authorship. Indexes above 1 represent rates of coauthorship that are higher than expected, and indexes below 1 indicate rates of coauthorship that are lower than expected. This is similar to the concept of the index of trade intensity between countries and across regions.

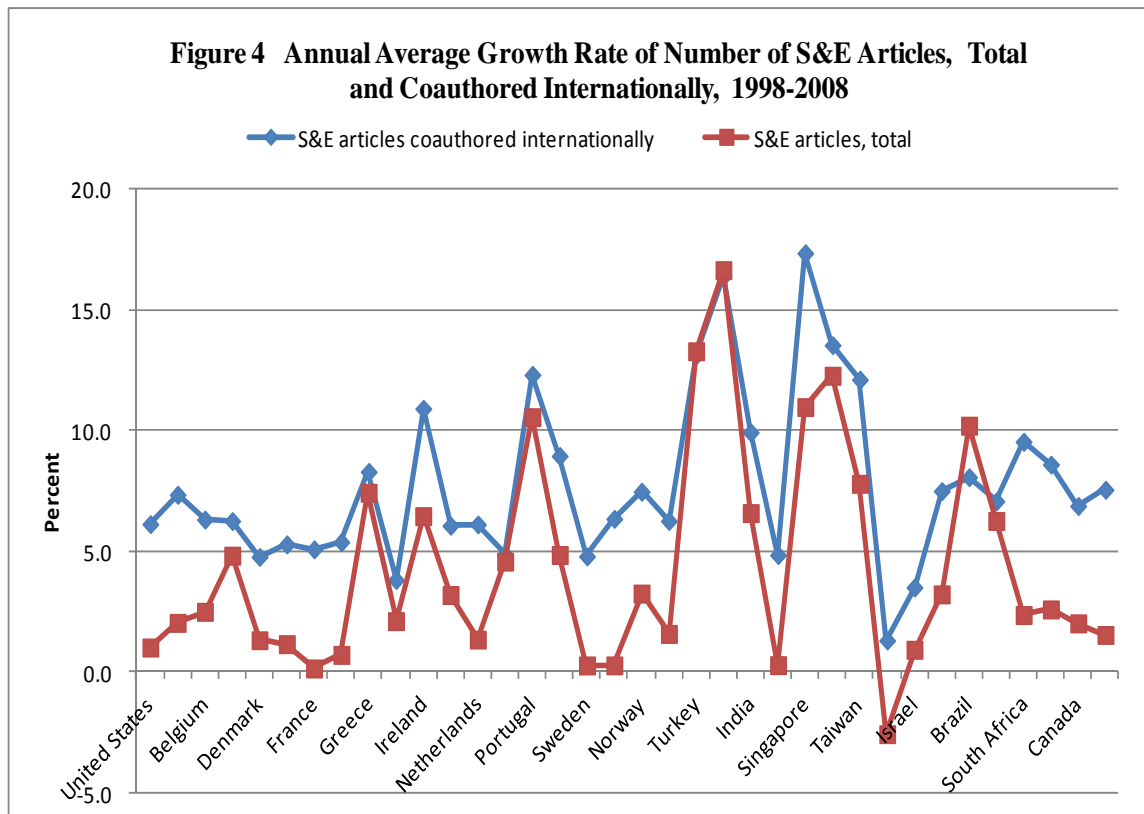
Tables 2-4 and 2-5 show changes in indexes of international collaboration for selected pairs of countries in the EU and Asia-Pacific. Changes are shown, rather than the indexes per se, because the indexes are influenced by a variety of other factors, such as geographical distance, history, culture, language, etc.

The EU distinguishes itself from the Asia-Pacific region in that while between 1998 and 2008 indexes of international collaboration increased within the EU, indicating growing integration across the EU in terms of S&E article publication, the indexes of international collaboration for the selected pairs of Asia-Pacific countries in fact decreased during this period.

⁵Senker (2006) offers several theoretical explanations of why knowledge production is becoming global, especially in the fields of life sciences and biotechnology.

⁶Figure 2-4 shows only countries that account for more than 1 percent of internationally coauthored articles in 1998.

Figure 2-4. Annual Average Growth Rate of Number of Scientific and Engineering Articles, Total Annual and Coauthored Internationally, 1998-2008



Note: Annual average growth rate of total number of S&E articles published is between 1997 and 2007.

SOURCE: Based on data from National Science Board (2010).

Sakata (2011) argues that this is a matter of concern in the Asia-Pacific region because regional collaboration is increasingly necessary to solve a variety of problems and cope with new challenges facing the region, such as environmental, health, and energy issues. Asia-Pacific countries must also respond to the growing innovation capabilities within the region, because otherwise those increasing capabilities, although still growing, remain largely untapped.

ROLE OF APEC IN ENHANCING INNOVATION IN THE ASIA-PACIFIC REGION

APEC is considered to play at least two important roles in enhancing innovation in the region. First is the narrowing of the gap in innovation capabilities among APEC member countries and supporting improvement in the local scientific and technological capabilities of member countries. In developed economies, innovation-driven growth is nothing new, because the economic growth of these countries has been driven by productivity growth backed by innovation, both radical and incremental. What is new is that the importance of innovation for development is increasing with time, highlighting the urgency of the matter for policy makers both in individual countries and in the regional community (Fagerberg and Verspagen 2002).

What is unique about APEC is the inclusion from the beginning of economic and technical cooperation (ECOTECH) as one of three pillars of its major activities. APEC needs to strengthen ECOTECH activities, including programs to enhance scientific and technological

capabilities of member economies. Human-resource development in the fields of science and technology is currently very much in demand in the region.

APEC also needs to play a role in enhancing science and technology cooperation, especially in areas in which member countries have a common interest, such as environment, energy, or healthcare. The important question is how we can achieve a situation in which APEC plays this role.

While institutions are important for the formation and functioning of particular innovation systems, “they may also, by their very nature, impede internationalization of innovation systems” (Carlsson 2006, 63). For instance, Foray (1995) analyzed the persistence of country-specific requirements in national intellectual property rights. He also showed that “the path-dependent nature of any institutional arrangement is an obstacle to the international standardization of the national systems of intellectual property rights” (Foray 1995, 126).

The adoption of a single, regional innovation regime in the Asia-Pacific region appears to be a good idea at a glance, but might in fact be counter-productive, because it would require a reduction in the diversity of the innovation systems themselves. In fact, it is this kind of diversity that is a key feature of the process of scientific and technological change (Carlsson 2006, 63).

As an alternative, the Asia-Pacific region could follow the EU approach. Beginning in the late 1990s, the EU sought to encourage cooperation in science and technology among member states as part of its effort to create a “European Research Area” (Wagner 2008, 7). Participants in a series of framework programs for research and technological development identified thematic priorities while making funding conditional on collaboration involving two or more EU countries. As a result, scientific collaboration grew rapidly in Europe (Wagner 2008, 7).

CONCLUSION

The locations of R&D activity globally have dramatically shifted since the 1970s. New players in the Asia-Pacific region, such as China, India, Korea, Chinese Taipei, and Singapore, are seen as increasingly important in the global shift. The purpose of this paper was twofold. One was to examine carefully to what extent these new moves within the world of science and technology signified a shift in innovation. The second was to consider the roles of APEC in enhancing innovation capabilities and processes in the region.

The author found that there is much less evidence of new innovation capacity in the Asia-Pacific region than is sometimes claimed. Most data indicate large increases in inputs into R&D activities in the Asia-Pacific region, but these inputs tend to concentrate in a small number of countries. Countries such as China, Chinese Taipei, Korea, and Singapore have succeeded in catching up with the advanced Asia-Pacific countries in many fields of science and technology. Some countries are even expanding technological frontiers in fields such as electronics. But the gap between these Asian “fast learners” and the rest of the developing countries in the region is widening. Thus, forces of both convergence and divergence of innovation capabilities are prevalent in the region.

Local embeddedness of innovation is even harder to find among newly emerging countries, except Korea and Chinese Taipei. Local participation in innovation activities is crucial to sustain growth in the long run.

Finally, in contrast to the EU, Asia-Pacific countries were not able to intensify regional research and technological cooperation between 1998 and 2008. Indexes of international collaboration for selected pairs of Asia-Pacific countries did not increase during this period.

Trade and investment liberalization remain important in the development and growth processes in APEC economies, but simple market solutions have been found insufficient. APEC needs to play an active role in creating innovation-led, vibrant economic growth.

Table 2-4. Changes in Indexes of International Collaboration for Selected Pairs of Countries in the EU between 1998 and 2008

	Austria	Belgium	Czech Republic	Denmark	Finland	France	Germany	Greece	Hungary	Ireland	Italy	Netherlands	Poland	Portugal	Spain	Sweden	UK	Overall Intra-EU
Austria		0.42	(0.38)	(0.21)	0.22	0.22	0.22	(0.57)	0.93	0.16	0.37	0.13	0.69	(0.09)	0.15	0.55	0.09	2.90
Belgium	0.42		0.19	0.22	(0.15)	0.14	0.23	0.04	0.72	0.42	0.35	0.18	0.30	(0.33)	0.18	0.07	0.24	3.22
Czech Republic	(0.38)	0.19		0.10	0.44	0.33	0.19	0.10	1.79	1.77	0.27	0.06	1.33	(0.30)	0.08	0.50	0.21	6.68
Denmark	(0.21)	0.22	0.10		0.79	0.10	0.12	(1.04)	0.58	0.48	0.07	0.16	0.44	(0.86)	(0.16)	0.50	0.09	1.38
Finland	0.22	(0.15)	0.44	0.79		0.15	0.28	0.04	(0.15)	1.26	0.31	0.14	0.38	(0.20)	(0.06)	0.59	0.48	4.52
France	0.22	0.14	0.33	0.10	0.15		0.17	(0.12)	0.16	0.25	0.22	0.23	0.15	(0.29)	(0.13)	0.22	0.14	1.94
Germany	0.22	0.23	0.19	0.12	0.28	0.17		(0.04)	0.11	0.27	0.20	0.34	0.19	0.09	0.19	0.28	0.18	3.02
Greece	(0.57)	0.04	0.10	(1.04)	0.04	(0.12)	(0.04)		0.95	0.69	0.04	0.13	0.65	(1.66)	0.14	0.30	(0.13)	(0.48)
Hungary	0.93	0.72	1.79	0.58	(0.15)	0.16	0.11	0.95		0.52	0.26	0.13	1.24	0.23	0.22	0.79	0.05	8.53
Ireland	0.16	0.42	1.77	0.48	1.26	0.25	0.27	0.69	0.52		(0.05)	0.51	0.38	(0.78)	0.10	0.68	(0.07)	6.59
Italy	0.37	0.35	0.27	0.07	0.31	0.22	0.20	0.04	0.26	(0.05)		0.09	0.32	(0.13)	0.25	0.28	0.18	3.03
Netherlands	0.13	0.18	0.06	0.16	0.14	0.23	0.34	0.13	0.13	0.51	0.09		0.13	(0.49)	0.12	0.26	0.22	2.34
Poland	0.69	0.30	1.33	0.44	0.38	0.15	0.19	0.65	1.24	0.38	0.32	0.13		0.28	0.29	0.14	0.15	7.06
Portugal	(0.09)	(0.33)	(0.30)	(0.86)	(0.20)	(0.29)	0.09	(1.66)	0.23	(0.78)	(0.13)	(0.49)	0.28		0.35	(0.24)	(0.52)	(4.94)
Spain	0.15	0.18	0.08	(0.16)	(0.06)	(0.13)	0.19	0.14	0.22	0.10	0.25	0.12	0.29	0.35		0.19	0.02	1.93
Sweden	0.55	0.07	0.50	0.50	0.59	0.22	0.28	0.30	0.79	0.68	0.28	0.26	0.14	(0.24)	0.19		0.26	5.37
UK	0.09	0.24	0.21	0.09	0.48	0.14	0.18	(0.13)	0.05	(0.07)	0.18	0.22	0.15	(0.52)	0.02	0.26		1.59

Note: Figures in parentheses are negative.

SOURCE: Based on data from National Science Board (2010).

Table 2-5. Changes in Indexes of International Collaboration for Selected Pairs of Asia-Pacific Countries between 1998 and 2008

	Australia	Canada	China	Japan	South Korea	Mexico	New Zealand	Russia	Singapore	Chinese Taipei	United States	Overall Intra-APEC
Australia		(0.02)	0.09	(0.09)	0.07	0.15	(0.48)	0.07	(0.23)	(0.03)	(0.02)	(0.49)
Canada	(0.02)		0.07	(0.04)	0.12	0.37	(0.08)	0.20	0.07	0.02	(0.03)	0.68
China	0.09	0.07		(0.15)	(0.55)	0.20	(0.18)	0.10	(2.18)	(0.90)	0.15	(3.35)
Japan	(0.09)	(0.04)	(0.15)		(0.09)	0.08	(0.04)	0.26	(0.15)	0.36	(0.14)	0.00
Korea	0.07	0.12	(0.55)	(0.09)		(0.01)	0.12	0.08	0.55	(0.66)	(0.15)	(0.52)
Mexico	0.15	0.37	0.20	0.08	(0.01)		0.44	0.27	0.18	0.17	0.02	1.87
New Zealand	(0.48)	(0.08)	(0.18)	(0.04)	0.12	0.44		0.02	(0.08)	(0.06)	0.01	(0.33)
Russia	0.07	0.20	0.10	0.26	0.08	0.27	0.02		0.10	0.60	0.07	1.77
Singapore	(0.23)	0.07	(2.18)	(0.15)	0.55	0.18	(0.08)	0.10		(2.08)	0.05	(3.77)
Chinese Taipei	(0.03)	0.02	(0.90)	0.36	(0.66)	0.17	(0.06)	0.60	(2.08)		(0.21)	(2.79)
United States	(0.02)	(0.03)	0.15	(0.14)	(0.15)	0.02	0.01	0.07	0.05	(0.21)		(0.25)

Note: Figures in parentheses are negative.

Source: Based on data from National Science Board (2010).

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3. Racing to the Top: Chinese Taipei's Achievements on the Ease of Doing Business

Abstract

Striking a balance between protecting the welfare of nationals and catching up with world standards in regulations has presented each economy with a dilemma. Before APEC launched the Ease of Doing Business Initiative in 2009, Chinese Taipei was reviewing and improving relevant regulations. It hopes to further improve its business environment by removing unnecessary regulatory restrictions on business activities.

The effort of climbing up the ladder has had significant results: Chinese Taipei's overall ranking on the World Bank's *Doing Business* report jumped from 61 in 2008 to 33 in 2010. The goal of this paper is to present Chinese Taipei as exemplifying how external pressure—stemming either from regional economic arrangements, like APEC, or the assessment of international organizations, like the World Bank—compels governments to initiate regulatory reforms and shapes the policy orientation of the public sector.

This paper argues that it is critical for an export-oriented economy, like Chinese Taipei, to catch up to international standards in order to remain competitive in the global economy. This paper contends that Chinese Taipei's achievements in improving its business environment are attributable to three factors: political support from the top, an effective internal coordination mechanism, and close cooperation with external players.

INTRODUCTION

In the era of an increasingly globalized world, each economy not only has to enhance its competitiveness to take on different challenges from various fronts beyond the borders, but also needs to have a keen awareness of world standards of good governance in order to keep up with competitors. Nevertheless, undertaking any reform related to institutional change or regulatory adjustment is likely to be difficult, since reform affects the status quo and requires enough domestic political support to overcome possible bureaucratic hindrances and obstinacy.

However, it is interesting to note that assessments of economies by international organizations (including nongovernmental organizations) can be a driving force in compelling governments

to initiate reforms. In this respect, Chinese Taipei's achievements on the World Bank's Doing Business (DB) project provide an interesting case since it illustrates how much the government values its performance in the eye of the World Bank's Doing Business report, so as to take active steps to improve its ranking by making regulatory reforms and adjustments.

As the fact revealed, in the Doing Business 2009 report issued by the World Bank in September 2008, Chinese Taipei was ranked 61st in the indicator of ease of doing business, among 181 economies (World Bank 2008). This unsatisfactory performance invoked attention from the Chinese Taipei government, which decided to take actions to address this issue by conducting a series of regulatory reforms. Before long, in the Doing Business 2011 report issued by the World Bank in September 2010, Chinese Taipei had made a significant progress and its ranking was improved to 33rd in the overall indicator of ease of doing business among 183 economies (World Bank 2010).

Another factor which should not be ignored is the influence of the Asia-Pacific Economic Cooperation (APEC) on Chinese Taipei's regulatory reforms. Being a long-term dedicated APEC member for two decades, Chinese Taipei has been adjusting its domestic regulations in order to support APEC's initiatives to facilitate and liberalize trade and investment. In addition, APEC's Ease of Doing Business (EoDB) Action Plan, launched by APEC leaders in 2009 to improve APEC members' regulatory performance measured by Doing Business by 25% by 2015,¹ gave Chinese Taipei more momentum to devote substantive political capital in regulatory reforms.

The purpose of this paper is to illustrate how external factors, such as the World Bank's Doing Business project or APEC's EoDB Action Plan, can generate either a positive influence or significant pressure for regulatory reform. Furthermore, this paper argues that in addition to possible peer pressure from APEC and the concerns of a national reputation at stake on the Doing Business' evaluation, another factor is that export-oriented economies are likely to pay more attention to their status in the global economy. Therefore, they are more willing to catch up with the world standards and to race to the top in order to enhance their competitiveness in the world economy.

This paper is organized as follows: The next section illustrates the connections between the World Bank's Doing Business project and Chinese Taipei's regulatory reforms. The second section focuses on Chinese Taipei's recent regulatory reforms. The third section compares the performance of Chinese Taipei on Doing Business indicators with the performance of neighboring APEC economies. The concluding section summarizes the findings, limitations, and directions for the future research.

WORLD BANK'S *DOING BUSINESS* PROJECT AND CHINESE TAIPEI'S REACTIONS

In order to provide objective measures of business regulations and their enforcement across nations, the World Bank launched a multiple-year research project, *Doing Business*, in 2002 to look at domestic small and medium-size companies and to measure the regulations applying to them. *Doing Business* has issued an annual report since 2003, providing

¹ APEC Economic Committee website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013553>

quantitative data and ranking assessments of economies to compare business regulation environments across economies and over time.

By collecting and analyzing relevant regulations affecting business environments in most economies, *Doing Business* ranks each economy on the basis of nine areas of regulation:

1. Starting a Business
2. Dealing with Construction Permits
3. Registering Property
4. Getting Credit
5. Protecting Investors
6. Paying Taxes
7. Trading across Borders
8. Enforcing Contracts
9. Closing a Business.

Currently, *Doing Business* also enlarges its focus to the regulations on employing workers and getting electricity (World Bank 2010).

Chinese Taipei has been evaluated by the Doing Business project since its first annual report of 2003. During the 2003-2004 period, it did not rank economies based on their overall performance, but only provided quantitative data on specific items, such as number of procedures and time required for starting a business (World Bank 2003, 2004). Until 2005, in the *Doing Business 2006* report, it started ranking each economy's comprehensive performance on the basis of its major categories among 155 economies around the world (World Bank 2005).

In the first report, Chinese Taipei was ranked 35th out of 155 economies on the overall indicator of ease of doing business, which was far behind some neighboring APEC economies like Singapore (2), Hong Kong, China (7), Japan (10), Thailand (20) and Korea (27), but better than China (91), Viet Nam (99), the Philippines (113) and Indonesia (115) (World Bank 2005). Notably, this report also revealed the fact that the business environment in Chinese Taipei was the worst compared with other Asian Tigers.²

Despite this disappointing performance which should have been viewed as an early warning, Chinese Taipei seemed not to take sufficient action to respond it. During the 2006-2007 period, the ranking of Chinese Taipei in the category of ease of doing business continued to drop for two consecutive years. It was ranked 47th in 2006 and 50th in 2007. With regard to the indicator of starting a business, Chinese Taipei was ranked 94th in 2006 and further fell into 103rd in 2007 (World Bank 2006, 2007). These frustrating performances appeared not to invoke sufficient attention from the former administration, due to different policy priorities and upcoming presidential election in 2008.³ As a consequence, the final wake-up call came from the *Doing Business 2009* report, issued in September 2008 in the aftermath of Chinese Taipei's presidential election and another shift of political power to the current administration.

² The Four Asian Tigers are Korea, Hong Kong, China; Singapore, and Chinese Taipei.

³ According to some officials, the former administration considered that improvement in the World Bank's ranking could not help enlarge the international space for Chinese Taipei.

In *Doing Business 2009*, Chinese Taipei was ranked 61st out of 181 economies on the overall indicator of ease of doing business. On starting a business, it ranked 119th, the worst among the four Asian Tigers and lagging behind Viet Nam (108) (World Bank 2008). Table 3-1 compares the Asian Tigers on the ease of doing business indicator from 2005 to 2008.

Table 3-1. Asian Tigers' Performance on the Ease of Doing Business Indicator

Issued Year	Chinese Taipei	Rep. of Korea	Hong Kong, China	Singapore	Surveyed Economies
DB 2006	35	27	7	2	155
DB 2007	47	23	5	1	175
DB 2008	50	30	4	1	178
DB 2009	61	23	4	1	181

SOURCE: World Bank, *Doing Business 2005, 2006, 2007 and 2008*.

As Table 3-1 shows, Chinese Taipei's ranking fell for three consecutive years, while the rankings of Hong Kong, China and Singapore were climbing and Korea's stayed in the top 30.

This worst-ever record in September 2008 had caught attention by the Chinese Taipei government. In response to this report, the Cabinet-level Council for Economic Planning and Development (CEPD) immediately formed a task force to carry out an in-depth study on the report by calling for an inter-ministerial collaboration.⁴

One month after the issue of the *Doing Business 2009* in October 2008, the CEPD completed its initial reform suggestions and allowed them to be studied and discussed among relevant Cabinet agencies before being submitted to a meeting jointly chaired by ministers without portfolio for final policy decision. It was noteworthy that in May 2008 the CEPD even undertook a self-assessment and simulation ranking, based on the World Bank's criteria and data, to examine the strengths and weaknesses of its business environment and to study possibilities for its improvement. Eventually, the CEPD was able to set mid-term and long-term improvement plans based on the preceding procedures.⁵

From September 2008 to August 2009, improvement plans were deliberated at regular intervals for discussion and conferral at meetings of a deregulation committee chaired jointly by ministers without portfolio, as a means of sweeping all obstacles impeding the relevant agencies from proceeding with reforms, and to serve as the basis for regular monitoring of progress. Noticeably, in July 2009, the CEPD was assigned by the Executive Yuan (the Cabinet) to establish the "Task Force for Improving the Performances in International Rankings," focusing on drafting improvement plans, taking policy measures, and monitoring actual implementation for advancing Chinese Taipei's rankings in various international assessments.⁶ The Minister of CEPD was appointed to chair this task force and vice ministers

⁴ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013553>

⁵ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013536>

⁶ CEPD website: <http://www.cepd.gov.tw/m1.aspx?key=empty&SNo=0015455>

from other departments were all included. This task force holds a meeting per three months.⁷ Relevant international ranking agencies, such as the *IMD World Competitiveness Yearbook*, the Heritage Foundation's *Index of Economic Freedom*, the Business Environment Risk Intelligence's (BERI) *Overall Investment Environment*, the World Bank's *Doing Business*, etc., were included within the coverage of 20 international ranking agencies, which were closely monitored by this task force.⁸

After an inter-ministerial discussion, two areas were targeted for business environment reforms in 2009: (1) starting a business and (2) paying taxes. The following section details how Chinese Taipei took actions to achieve its goals.

Starting a Business in the 2009 Reform

Regarding Starting a Business, the main objectives of the 2009 reforms were to eliminate the minimum capital requirement and to abolish the profit-seeking enterprise uniform certification system. With the majority in the parliament, on April 29, 2009, the current administration easily passed the amendments of the Company Act to delete the provisions in Articles 100 and 156, which authorized the Ministry of Economic Affairs to issue an executive order setting a minimum capital requirement for starting a business. As a consequence of this change, Chinese Taipei formally became an economy without any minimum capital requirement for starting a business. Furthermore, on April 12, 2009, the Executive Yuan announced the abolishment of the profit-seeking enterprise uniform certification system, with the effect that starting a business in Chinese Taipei would thereafter require only application for incorporation and would no longer require registration as profit-seeking enterprise.⁹

Paying Taxes in the 2009 Reform

For Paying Taxes, the 2009 reforms focused on enhancing and promoting the process for online filing and payment of value added tax (VAT).

Bridging the Gap between the DB Report and Reality

In addition to taking steps in improving the business environment, Chinese Taipei also seeks to bridge the gap between the World Bank's survey results and the reality in Chinese Taipei. Thus, the CEPD had assigned all relevant agencies to draft talking points and to provide related official regulations for the World Bank and its local observers, hoping to offer accurate and updated information for this research project.¹⁰ In fact, the CEPD had based on the World Bank's eight indicators in the *Doing Business 2009* report to assign agencies concerned and ask them to set the goals for improvement.¹¹

As a result of aforementioned efforts, the overall ranking of Chinese Taipei in the *Doing Business 2010* report was moved to 46th among 183 economies. In the indicator of Starting a

⁷ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0012857>

⁸ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0014453>

⁹ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013731>

¹⁰ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013553>

¹¹ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0013553>

Business, Chinese Taipei's ranking had jumped from 119th in 2008 to 29th in 2009. The number of procedures and the days of time needed for starting a business were reduced from eight to six procedures and from 42 to 23 days, respectively. The item of paid-in minimum capital was eliminated to zero.

In terms of Dealing with Construction Permits, the number of procedures and time required were shortened from 119 to 29 procedures and from eight to six days. As a result, Chinese Taipei's ranking in this indicator improved from 61st to 46th. In the Paying Taxes indicator, Chinese Taipei's ranking was advanced from 102nd to 92nd with the payments (number per year) simplified from 23 to 17 and the time needed from 340 to 281 hours (World Bank 2008, 2009).

Overall, these remarkable achievements suggest that Chinese Taipei had effectively carried out relevant reforms to work in line with the World Bank's standards. Moreover, the World Bank recognized these efforts as reflected in improved rankings for many indicators.

DEEPENING AND BROADENING THE DEPTH AND SCOPE OF REFORMS

After achieving significant progress in the *Doing Business 2010* report issued in September 2009, the CEPD initiated another round of reforms to facilitate a business-friendly environment by the following two directions. The first was to raise the supervisory level of the reforms. The second was to enlarge the scope of the reforms.

First, in October 2009, the CEPD presented to the Vice Premier a report on "Reform Strategies for Modernizing the Law and Institutions of the Business Environment." This report obtained strong political support from the government and the supervisory level of the business environment reforms was raised from direction by joint meeting of ministers without portfolio to direction by the Vice Premier.

In addition, the CEPD also drafted the "Assessment Operating Points for the Executive Yuan and Its Related Agencies to Promote the Business Environment Reform" for relevant agencies to implement reforms. The Assessment Operating Points was approved by the Executive Yuan in April 2010, which prescribed that Chinese Taipei should be ranked within 35th in 2010 and 20th in 2011. Again, the CEPD was assigned to take charge of the progress in this regard, in order to provide relevant information to the World Bank and to report to the Vice Premier.¹²

Second, the scope of advancing the business environment was expanded to fit the five indicators of the World Bank. To a large extent, the enlarged scope of regulatory reform was due to the APEC EoDB Initiative in 2009, since this initiative had identified the same five key indicators in the World Bank's *Doing business* project. These five indicators include starting a business, dealing with construction permits, registering property, protecting investors, and paying taxes. The major reforms associated with these indicators are summarized in Table 3-2.

¹² CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0014978>

Table 3-2. Chinese Taipei's 2009/10 Reforms on *Doing Business*' Five Indicators

Indicator (Ranking in DB2010)	Reform Items
Starting a Business (29)	<ol style="list-style-type: none"> 1. Reduce the administrative processing time for company registration. 2. Shorten time for arranging national health insurance coverage for employee of a newly established entity. 3. Speed up the work rules review process. 4. Amend the Company Act to reduce the time needed for starting a company.
Dealing with Construction Permits (46)	<p>The Taipei City Government</p> <ol style="list-style-type: none"> 1. Established a single window to process applications for construction permits. 2. Prescribed that applications for review and approval of plans for construction related under a certain size need not to be submitted. 3. Simplified application documentation.
Registering Property (30)	<ol style="list-style-type: none"> 1. Complete the Local Tax Online Filing Portal, an e-system for filing and payment of local taxes. 2. Amend the Deed Tax Act.
Protecting Investors (73)	<ol style="list-style-type: none"> 1. Amend the Company Act regarding the provision on the board of directors. 2. Amend the Security and Exchange Act to give minority shareholders the right to request that the competent authority inspect a company's documents and accounts.
Paying Taxes (92)	<ol style="list-style-type: none"> 1. Simplify online filing and payment for profit-seeking enterprise income tax. 2. Amend the Income Tax Act to replace the previously applicable corporate income tax dual rates of 15% and 25% with a flat rate of 20%. 3. Reduce the corporate tax rate from 20% to 17%.

SOURCE: Council for Economic Planning and Development, 2010.

Nothing can highlight the importance of the *Doing Business* project to Chinese Taipei's regulatory reforms more than the following paragraph from the CEPD's *Report on Taiwan's 2010 Ease of Doing Business Reforms*:

We recognize the significance of the World Bank's *Doing Business* report in promoting reforms by economies worldwide in the areas highlighted, and we view this report as an important source of reference for our active efforts in these last years to modernize and internationally align the law and institutions of Taiwan's business environment. (CEPD 2010, 10)

To sum up, Chinese Taipei has regarded the World Bank's *Doing Business* report as an important reference and guideline to direct and formulate its regulatory reforms for a better business environment. The case of Chinese Taipei illustrates that an economy is willing to take steps domestically and to abide by policy prescriptions from the outside actor (the World Bank), in order to make significant regulatory reforms in its business environment. In other words, one can argue that Chinese Taipei is gradually adjusting its domestic regulatory regime to accommodate the international standards/principles set by the World Bank for facilitating a better business environment and strengthening its global competitiveness.

CONTINUING TO STRENGTHEN REFORMS ON BUSINESS ENVIRONMENT

Chinese Taipei's 2009/10 reforms have accomplished positive outcomes. In the *Doing Business 2011* report issued by the World Bank in November 2010, Chinese Taipei was ranked 33rd in the indicator of ease of doing business among 183 economies, advancing 13 places from 46th in 2009. This ranking was also satisfied with the goal set in the Assessment

Operating Points, which required Chinese Taipei to improve its the ranking within 35th in 2010.

As shown in Table 3-3, in terms of the indicator of Starting a Business, the ranking of Chinese Taipei was also improved from 29th in 2009 to 24th in 2010. In the Trading across Borders, its ranking was advanced from 33rd in 2009 to 17th in 2010, which was the most significant achievement among all indicators. Within this indicator, for example, Chinese Taipei had cut down the cost to export (per container) from US\$720 in 2009 to US\$645 in 2010. Similarly, the cost to import (per container) was also reduced from US\$732 in 2009 to US\$700 in 2010. In the indicator of Dealing with Construction Permits, Chinese Taipei's ranking was improved from 46th to 33rd, which was the second best improved item. Specifically, Chinese Taipei had simplified the number of procedures from 29 to 24 and also reduced the cost for applying a construction permit from 23% to 15% of income per capita (World Bank 2009, 2010). On the other hand, there are some areas, such as registering property, protecting investors and enforcing contracts, in which Chinese Taipei was not performed well in the World Bank's ranking. In the CEPD's report, it attributed these underperformed categories to the delay of legislation process, certain regulatory reforms unrecognized by the World Bank, and conflicting jurisdiction of different branches (i.e., enforcing contracts).¹³

Overall, this significant progress demonstrates that Chinese Taipei's efforts to enhance its business environment have resulted in remarkable achievements recognized by the World Bank.

Table 3-3. Chinese Taipei's Ranking Changes in the DB2010 and DB2011

DB Report Year	Ease of Doing Business	Starting a Business	Dealing with Construction Permits	Registering Property	Getting Credit	Protecting Investors	Paying Taxes	Trading Across Borders	Enforcing Contracts	Closing a Business
DB 2010	46	29	46	30	4	73	92	33	90	11
DB 2011	33	24	33	32	4	74	87	17	90	10
Diff.	13	5	13	-2	0	-1	5	16	0	1

SOURCE: World Bank (2009, 2010).

Nevertheless, compared with neighboring East Asian economies, Chinese Taipei's 33rd place in the ease of doing business was not impressive and still lagged behind most East Asian economies. Take the *Doing Business 2011* report as an example, among four Asian Tigers, in terms of overall business environment, Singapore was ranked No. 1, Hong Kong, China No. 2 and Korea No. 16, while Chinese Taipei remains the last place. Needless to say, Chinese Taipei's ranking was far behind the ranking of other neighboring developed economies, such as New Zealand (3), Australia (10), and Japan (18). What is more disappointing is that Chinese Taipei's performance was not even close to some neighboring developing economies, like Thailand (19) and Malaysia (21).

¹³ CEPD website: <http://www.cepd.gov.tw/m1.aspx?sNo=0014979>

Table 3-4 shows the performance comparison between Chinese Taipei and some neighboring East Asian economies in the *Doing Business 2011* report. Except for some indicators, such as starting a business, registering property, trading across borders and getting electricity, in which Chinese Taipei received better rankings in the top 40, Chinese Taipei's performances in other indicators were not even in the top 50. Hence, there remains room for Chinese Taipei's further improvement.

Table 3-4. Comparison of Rankings of East Asian Economies in *Doing Business 2011*

Doing Business 2011 Issued in 2010		Singapore	Hong Kong, China	Korea	Japan	Malaysia	Chinese Taipei	China
Ease of Doing Business		1	2	16	18	21	33	79
1	Starting a Business	4	6	60	98	113	24	151
2	Dealing with Construction Permits	2	1	22	44	108	95	181
3	Employing Workers	—	—	—	—	—	—	—
4	Registering Property	15	56	74	59	60	32	38
5	Getting Credit	6	2	15	15	1	72	65
6	Protecting Investors	2	3	74	16	4	74	93
7	Paying Taxes	4	3	49	112	23	87	114
8	Trading Across Borders	1	2	8	24	37	17	50
9	Enforcing Contracts	13	2	5	19	59	90	15
10	Getting Electricity	2	15	13	1	55	10	68

SOURCE: World Bank, *Doing Business 2011*.

In order to continue improving its business environment, Chinese Taipei has initiated reforms by closely orchestrating interdepartmental collaboration, establishing effective division of tasks and holding regular conferral among the relevant cabinet agencies to ensure that all government's efforts can achieve the reform objectives and deliver some concrete results.

Given that in the "Assessment Operating Points," it had set a goal for Chinese Taipei to improve its ranking within 20th in 2011, the CEPD held the first interdepartmental meeting to discuss the reform strategy for the 2010 business environment in August 2010 and the second meeting in December 2010. These meetings decided to take the following steps in main four categories as shown in Table 3-5.

Table 3-5. Chinese Taipei's 2009/10 Reforms on *Doing Business*

Indicator (Ranking in DB 2011)	Description
Starting a Business (24)	An interdepartmental collaboration was carried out to set up a website at which all administrative applications related to starting a business could be made and processed together online. The one-stop website was launched by the Ministry of Economic Affairs on May 30, 2011, making the whole process of starting a company easier and more convenient for the public.
Dealing with Construction Permits (33)	An interdepartmental collaboration was carried out to streamline construction permit application procedures, and particularly to expand and enhance single-window services for

Indicator (Ranking in DB 2011)	Description
	construction permit applications. On March 2011, the Taipei City Government officially set up the One-Stop Center for Warehouse Building Permits, to provide a fast and convenient integrated service to the public.
Getting Credit (72)	With a view to building a workable legal framework for accommodating new concepts of using movable property as collateral, the Executive Yuan has instructed the competent agency to broadly solicit view from academic, industrial, and government spheres on revision of the Personal Property Secured Transactions Act and related regulations.
Protecting Investors (74)	The government has drawn up amendments to various provisions of the Company Act and the Securities and Exchange Act aimed at strengthening corporate governance, enhancing minority shareholder protection, and underpinning the sound development of Chinese Taipei's capital markets.

SOURCE: Council for Economic Planning and Development (2011).

Noticeably, in the area of Starting a Business, Chinese Taipei had made a remarkable progress and its ranking moves to 24th in 2010. For racing to the top, since the second half of 2010, the Chinese Taipei government has been working arduously to advance greater reforms by constructing a company startup procedure online, as listed in Table 3-5. It is worth noting that the One-Stop Website (<http://onestop.nat.gov.tw>) for Online Application to Start a Business formally began to operate on May 30, 2011. The relevant procedures, including checking a new company's name, approving the name, registering the company, obtaining labor and national health insurance coverage, filing work rules, etc., are all included on the one website (CEPD 2011). It makes the whole process of starting a business much easier and more efficient.

On the other hand, regarding Dealing with Construction Permits, it is also noteworthy that Chinese Taipei has launched inter-ministerial efforts to simplify the application procedures for construction permits, usage permits, and related fire-safety and sanitary requirement. As indicated in Table 5, the Ministry of the Interior and Taipei City Government set up the One-Stop Center for Warehouse Building Permits. This newly regulatory innovation was drew reference from the similar reforms undertaken in Hong Kong, China and other places, which shortens the number of procedures to merely 5, and takes a total of 56 working days to complete the process (CEPD 2011).

In these two reforms, it is not difficult to find that Chinese Taipei is eager to play the catching-up game by fully utilizing its strength in information technology with regard to the One-Stop Website for Starting a Business and by adopting a successful model from other economies in terms of building a the One-Stop Center for Construction Permits. In fact, the preceding two reforms show that Chinese Taipei has actively utilized APEC as a useful platform to learn the best practices from other economies, which is articulated in the following section.

In sum, Chinese Taipei has strived to climb up the ladder by following the World Bank's criteria in the *Doing Business* project. Although there is room for further improvement, as long as Chinese Taipei overcomes other obstacles step by step, it is expected that Chinese Taipei's ranking in the *Doing Business* can move forward in the foreseeable future.

IMPACT OF THE APEC EODB ACTION PLAN

In addition to the World Bank's *Doing Business* report that pushes Chinese Taipei to initiate relevant reforms, the external pressure from APEC that initiated the "Ease of Doing Business

(EoDB) Action Plan” in 2009 also plays a pivotal role in compelling Chinese Taipei to expedite its pace of reforms.

The origin of the EoDB was proposed by the APEC Economic Committee (EC) in 2009 for continuing existing regulatory reforms in APEC economies. Specifically, the EC identified five priority areas from the World Bank's *Doing Business* indicators, as mentioned before. It is not surprising that Chinese Taipei has targeted at these five areas as the major focus of 2009/2010 reforms in line with APEC's initiative.

Furthermore, the EoDB Action Plan was launched by APEC Leaders in 2009. They set an APEC-wide ambitious goal of improving APEC's collective ranking by 25 percent in the aforementioned five areas by 2015. This plan intended to make the APEC business environment 25 percent cheaper (cost), faster (time) and easier (procedures) to do business. APEC Leaders also made an interim target of a 5 percent improvement by 2011 through a program of capacity building and implementation of improvements to the regulatory environment affecting business. In addition, this plan indicated six champion economies, including the United States, New Zealand, Japan, Korea, Hong Kong, China and Singapore, to take a lead in terms of capacity building in five areas. Each champion economy was assigned to lead in different areas. In the Phase I, awareness-building workshops have been held on each of the priority areas by champion economies.¹⁴

Although not being included in champion economies, Chinese Taipei has also held an “APEC Seminar on the First Steps of Successful Reform in Doing Business” in October 2010 in Taipei, which revealed Chinese Taipei's ambition to take an active role on this issue. Table 3-6 lists the links between champion economies and its focus area, as well as relevant seminars and workshops held by APEC economies.

Table 3-6. EoDB Action Plan's Policy Priorities, Champion Economies and Related Seminars

Relevant Seminars and Workshops	Champion Economies	Five Priority Areas
“Reducing Start-up and Establishment Time of Businesses” in Hiroshima, Japan.	U.S. & New Zealand	Starting a Business
“Getting Credit for Small and Medium Enterprises” in Sendai, Japan.	Japan	Getting Credit
“Enforcing Contracts” in Seoul, Korea.	Korea	Enforcing Contracts
“Trading Across Borders” in Sendai, Japan	Singapore & Hong Kong, China	Trading Across Borders
“Reforming the Regulatory System for Construction Permits” in Singapore	Singapore	Dealing with Permits
“APEC Seminar on the First Steps of Successful Reform in Doing Business” in Taipei, Chinese Taipei.	Chinese Taipei (not champion economy)	N/A

In this seminar, Chinese Taipei invited 22 experts from 14 APEC economies and 80-plus participants from Chinese Taipei's public sector, business community, and academia. The

¹⁴ APEC Economic Committee website: <http://www.apec.org/Groups/Economic-Committee.aspx>

seminar was designed to promote the improvement of the domestic business environment in line with the APEC EoDB Action Plan. During the seminar, CEPD Minister Christina Liu pointed out that in the age of globalization, the only way that an economy can become a successful partner in international economic integration is to build a more friendly business environment. Since Chinese Taipei has close relationships with other APEC economies, in the future it will strive to strengthen connections with Asia-Pacific supply chains and deepen regional cooperation on the basis of an improved business environment and its existing industrial strength.¹⁵

In addition, Liu also mentioned that over the past years, the CEPD has already carries out the revision of 600 laws and regulations. However, more efforts are needed to improve Chinese Taipei's position in the World Bank survey. She specifically indicated that in terms of construction license application procedures, Chinese Taipei could learn from international practices by integrating the procedures of different agencies and creating an easier process for companies applying for construction permits. Furthermore, through sharing the best practice from one of invited economies, Liu emphasized that in the reform of Starting a Business, Chinese Taipei could learn relevant procedures from New Zealand's experience, which encourages private individuals to form a company by providing online company registration.¹⁶

As a matter of fact, the above two reflections from Minister Liu during the seminar were later transformed into policy practices in Chinese Taipei's 2009/2010 reforms, as noted before. These cases show that Chinese Taipei did not hold a seminar merely for more spotlights, but it was genuinely and vigorously committed itself to reforms by absorbing the best practices and relevant experiences from other economies.

COMPARISON WITH NEIGHBORING APEC ECONOMIES

Undeniably, Chinese Taipei's economic success in the past is largely grounded on its robust, flexible, and responsive small and medium-size enterprises (SMEs) as well as its export-oriented economy, both of which are closely linked with the global supply chains. The future prosperity for Chinese Taipei will continue to rely on a more open and integrated global economy. Hence, how to enhance its global competitiveness and facilitate a business-friendly environment conducive to SMEs' development becomes a crucial task for the Chinese Taipei government.

As noted earlier, the declining ranking in the *Doing Business* in 2008 was a wake-up call for Chinese Taipei. In fact, many international ranking agencies showed similar results during that period. For instance, the IMD's *World Competitiveness Yearbook* indicated that Chinese Taipei's ranking was dropped from 11th in 2005 to 17th in 2006, 18th in 2007, improved to 13th in 2008, and declined again to 23rd in 2009. Additionally, in the World Economic Forum's *Global Competitiveness Report*, Chinese Taipei's ranking was also fallen from 13th in 2006, to 14th in 2007, and 17th in 2008. In other words, various dropping rankings of Chinese Taipei from different international ranking agencies suggest that Chinese Taipei's overall competitiveness is gradually declining in the global competition. These negative signs were closely mirrored with the weakening position of Chinese Taipei in the world trade in the past

¹⁵ CEPD website: <http://www.cepd.gov.tw/encontent/m1.aspx?sNo=0014471>

¹⁶ CEPD website: <http://www.cepd.gov.tw/encontent/m1.aspx?sNo=0014471>

years, suggesting that Chinese Taipei has to take these negative indications seriously and need to deal with these issues for the sake of its economy. Table 3-7 shows Chinese Taipei's trading position and other important rankings of its economic environment over the past few years.

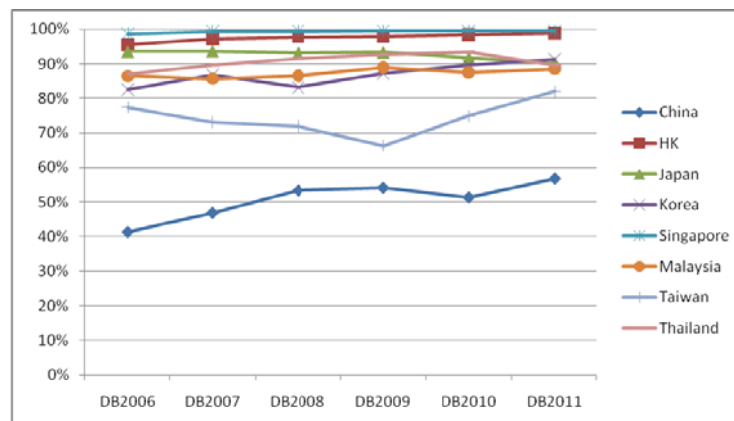
Table 3-7. Chinese Taipei's Trading Position and Relevant International Rankings

Year	Merchandise Trade	Global Exports	Global Imports	IMD World Competitiveness	WEF Global Competitiveness	Ease of Doing Business	Heritage Foundation Economic Freedom
2005	16	16	16	11	8	35	19
2006	17	16	16	17	13	47	29
2007	17	16	17	18	14	50	25
2008	17	18	18	13	17	61	25
2009	18	17	18	23	12	46	35
2010	18	16	17	8	13	33	27

SOURCE: Various sources from the WTO, IMD, WEF, and Heritage Foundation.

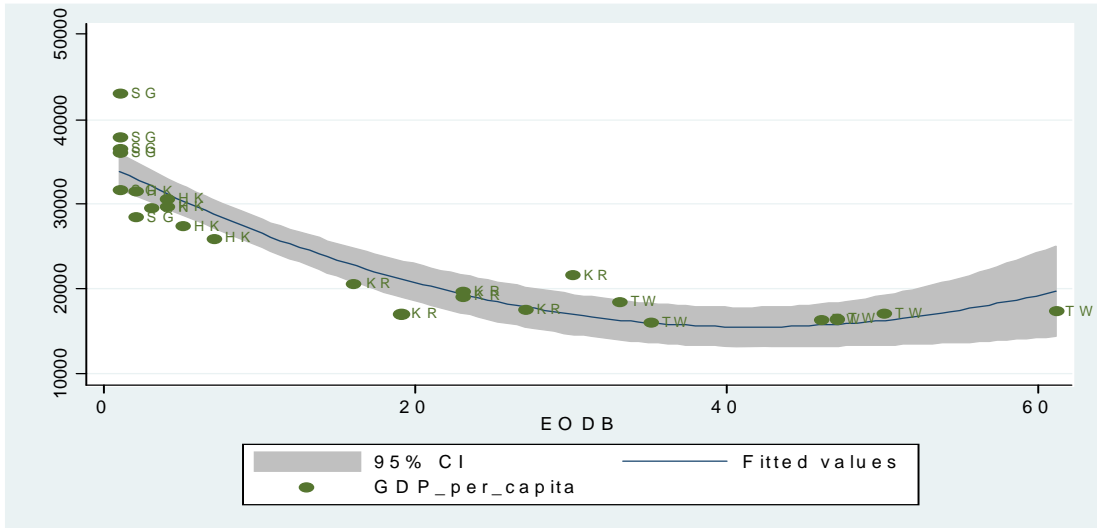
In comparison with other Asian Tigers and neighboring economies, Chinese Taipei's performance in terms of the World Bank's ease of doing business indicator has not been outstanding during the past five years. As shown in Figure 3-1, Singapore, Hong Kong, China and Japan have been in the top 10% in terms of ease of doing business among all surveyed economies for years. The economies in the second-tier include Thailand, Korea and Malaysia, which are among the top 20% of all surveyed economies. Noticeably, Chinese Taipei's ranking has swung between the top 40% and 20% in the past five years. Although many progresses have been made, Chinese Taipei in 2010 (in DB 2011 report) still remains a 10% gap from catching up with Korea, and it is far behind Singapore and Hong Kong, China.

Figure 3-1. East Asian Economies' Performances in Ease of Doing Business, 2005-2010



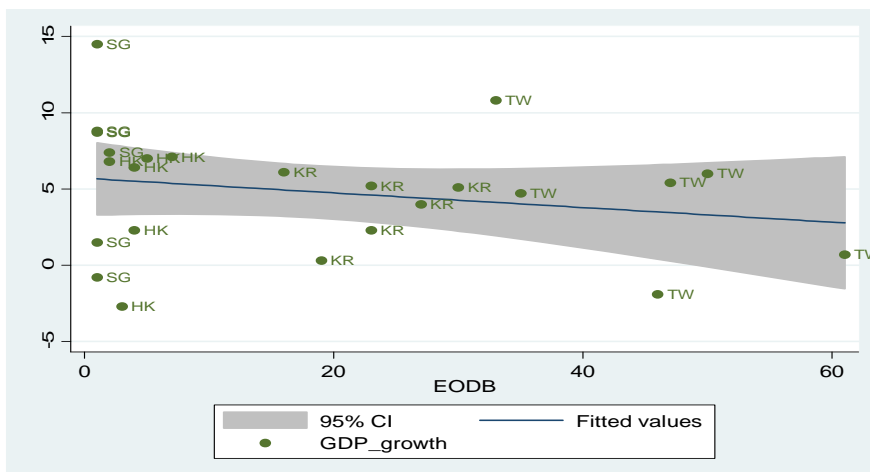
Take Asian Tigers for further analysis, first, I plot the EoDB ranking (i.e., ease of doing business ranking) against each economy's per capita GDP to see whether a better business environment has any connection with the productivity of each citizen in the economy. As shown in Figure 3-2, not surprisingly, an economy with a better ranking in the EoDB has a higher GDP per capita. Singapore and Hong Kong, China perform much better than Korea and Chinese Taipei in both GDP per capita and the EoDB ranking.

Figure 3-2. Pattern of EoDB Ranking and GDP Per Capita among Asian Tigers, 2005-2010



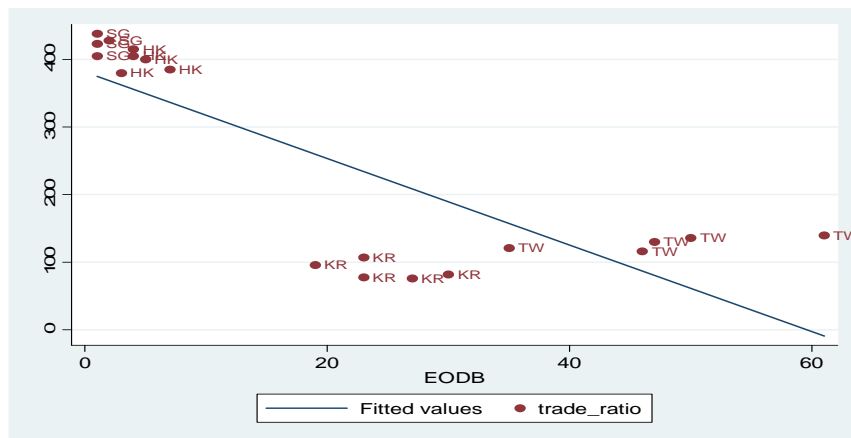
Similarly, it is reasonable to expect that a better business environment will be more likely to stimulate economy growth. When examining the pattern between the EoDB ranking and Asian Tigers' GDP growth in the past five year, as illustrated in Figure 3-3, I find that a weak positive association between a better EoDB ranking and a rising GDP growth, implying that facilitating a business-friendly environment may only slightly promote economic growth among Asian Tigers.

Figure 3-3. Pattern between EoDB and Economic Growth among Asian Tigers, 2005-2010



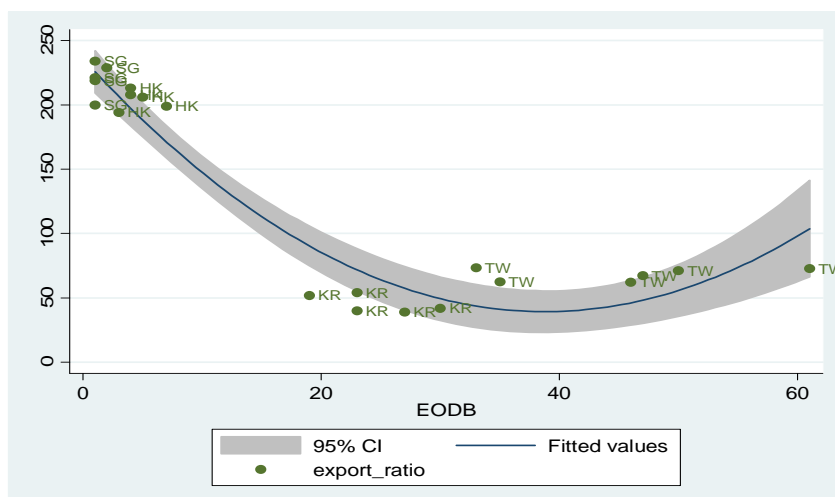
On the other hand, since external trade is vital to all Asian Tigers, it is also crucial to examine whether there is any linkage between the EoDB ranking and trade performance. First, it is interesting to know whether an economy dependent on trade is more likely to have a better business environment. The pattern in Figure 3-4 shows that an economy with a higher trade ratio of its GDP is likely to have a very high score in the EoDB indicator. Nevertheless, due to limited cases and skewness caused by two city-state economies (Hong Kong, China and Singapore), more data and further statistical analyses are needed to build a more credible connection between the two.

Figure 3-4. Pattern of EoDB Ranking and Trade Ratio of GDP among Asian Tigers, 2005-2010



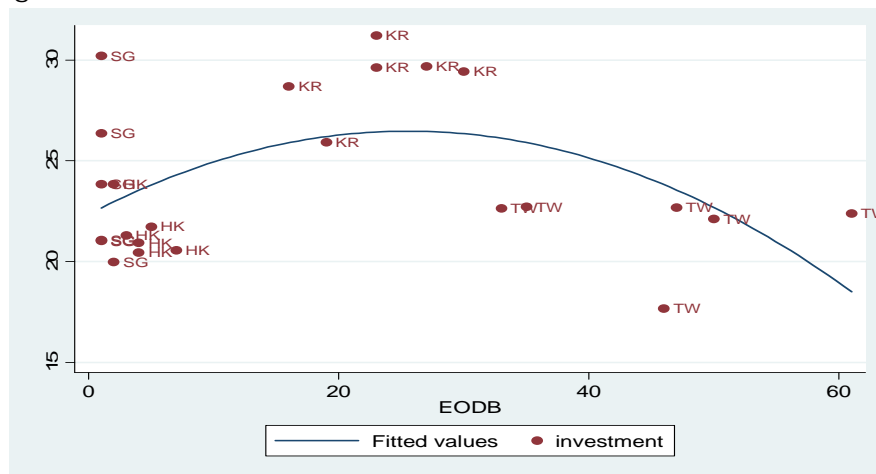
In addition to the significance of trade, which may affect an economy's will to improve its business environment, for Asian Tigers, whether a more efficient business environment is connected with a higher export ratio of GDP is also critical. By plotting Asian Tigers' export ratio of GDP against the EoDB rankings, Figure 3-5 displays a U-curve pattern between the two. It is not difficult to find that two economies (Singapore and Hong Kong, China) with the highest EoDB rankings are also extremely dependent on export. By contrast, Korea and Chinese Taipei have relatively lower export dependence and also possess lower rankings in the EoDB indicator.

Figure 3-5. Pattern of EoDB Ranking and Export Ratio of GDP among Asian Tigers, 2005-2010



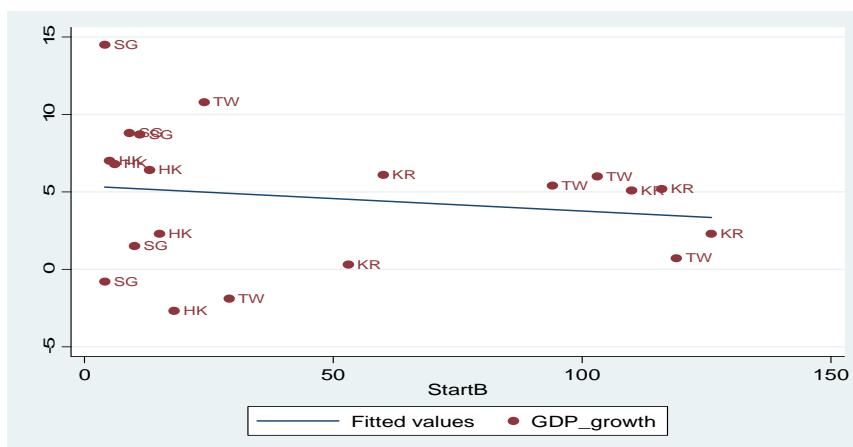
Furthermore, economic literature points out that a better business environment generally induces more investment. Therefore, one may assume that an economy with a better performance in the EoDB may have a higher investment ratio in its GDP. As the pattern displayed in Figure 3-6, an inverse-U curve indicates that an economy, like Korea within the top 30 in the EoDB, has a higher investment ratio of GDP. It is noteworthy that Hong Kong, China with a very high ranking in the EoDB does not have a high investment ratio of its GDP. Similarly, Chinese Taipei's investment ratio of GDP is not particularly followed with a higher EoDB ranking, either. Hence, more cases are needed for a further investigation.

Figure 3-6. Pattern of EoDB Ranking and Investment Ratio of GDP among Asian Tigers, 2005-2010



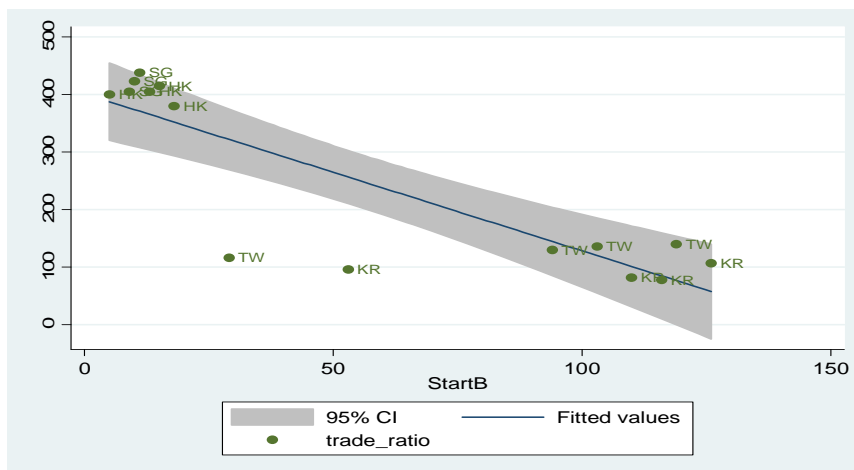
Another variable that deserves attention is the indicator of Starting a Business (SB), since most Asian Tigers have a significant proportion of SMEs as a backbone of economy. Hence, whether the business environment is easy to start a business is crucial for SMEs' development. The following section examines the patterns between this indicator and other economic phenomena. First, much alike the pattern between the EoDB and economic growth, Figure 3-7 shows that the relationship between the SB and GDP growth among Asian Tigers appears to be slightly positive associated. It means that an environment conducive to starting a business is more likely to have a higher GDP growth.

Figure 3-7. Pattern of SB Ranking GDP Growth among Asian Tigers, 2005-2010



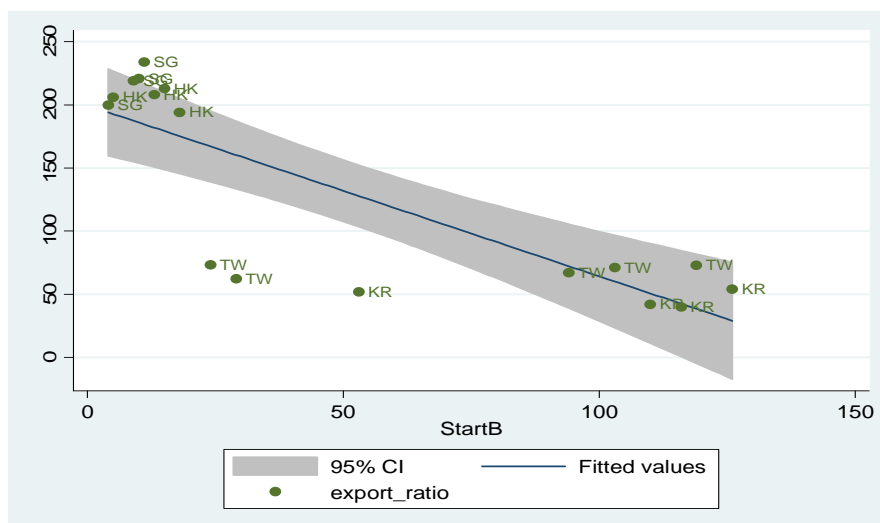
In terms of the association between the SB and trade ratio of GDP, as shown in Figure 3-8, the pattern is very similar to the one between the EoDB and trade ratio of GDP, since both are strongly positive correlated. This result indeed suggests that an economy with a favorable environment to start a business is likely to be the one which economy highly depends on trade. Nevertheless, since Singapore and Hong Kong, China are two city-state economies, which extremely rely upon foreign trade, this factor may skew the pattern. Hence, more data are needed to build a more credible connection.

Figure 3-8. Pattern of SB Ranking and Trade Ratio of GDP among Asian Tigers, 2005-2010



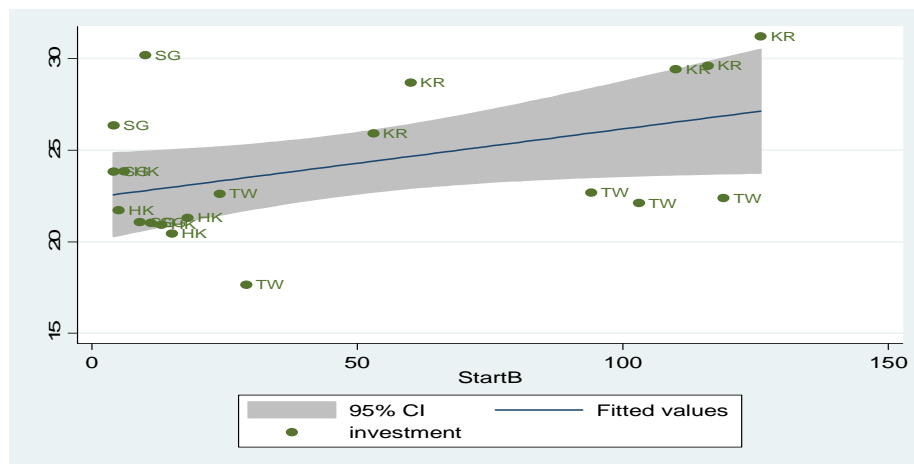
With regard to the linkage between the SB and export ratio of GDP, Figure 9 illustrates a positive association between the two, suggesting that an environment favorable to start a business is prone to be have a higher export ratio of GDP. The pattern in Figure 3-9 is slightly different from the one in Figure 3-5 with a U-curve shape. Similarly, the caution applies to any further interpretation, due to limited cases here.

Figure 3-9. Pattern of SB Ranking and Export Ratio of GDP among Asian Tigers, 2005-2010



Finally, it is crucial to explore the question of whether an environment easily to start a business can bring more investment. Notably, the previous pattern between the EoDB and investment ratio of GDP does not provide a clearly positive association between the two. Interestingly, Figure 3-10 shows a negative pattern between the SB and investment ratio of GDP, implying that a better performance in the SB may not be necessarily associated with more investment in the economy. This result is somewhat unexpected and partly can be attributed to the limited cases used here.

Figure 3-10. Pattern of SB Ranking and Investment Ratio of GDP among Asian Tigers, 2005-2010



In short, within the limited cases of Asian Tigers, it is not difficult to find that in general, a more business-friendly environment is more likely to be associated with a higher GDP per capita, better economic growth, more trade, and heavily export-oriented economy. More importantly, these patterns commonly reveal that Chinese Taipei, in various aspects, has been lagged behind other three Tigers. Although it is not the very latest phenomenon, it is imperative for Chinese Taipei to play a catch-up strategy to strengthen its global competitiveness by improving its business environment. As a consequence, the World Bank's *Doing Business* project can continue to provide a legitimate reason and a very useful reference for Chinese Taipei to launch regulatory reforms to improve its business environment.

CONCLUSION

In the increasingly economic globalized world, the boundary between economies has been gradually penetrated by various implicit and explicit forces. Facing a more intense global competition, each economy has been forced to take active measures to enhance its strengths and improve its weaknesses. Against this backdrop, Chinese Taipei has initiated substantive regulatory reform to facilitate a more business-friendly environment in order to stimulate better economic growth and maintain its global competitiveness. Particularly, Chinese Taipei has followed the *Doing Business*' criteria from the World Bank to improve its business environment and has achieved significant progress.

Although many factors can contribute to Chinese Taipei's accomplishment in this regard, this paper finds that three elements are significant to this improvement, including a strong

political support, an effective internal coordination mechanism, and close cooperation with external actors.

First, for any reform in the public sector, a strong political support from the top is the key to success. In this regard, Chinese Taipei's regulatory reforms obtain full political support from the highest-ranking officials, since the current administration has viewed economic growth as the most important priority in its platform before it won the presidential election in 2008. Of course, Chinese Taipei's deteriorating economic situation in recent years also forces the government to pay more attention to international rankings about Chinese Taipei's business environment, since these rankings may affect business climate, foreign investment, and also people's support to the government. As a result, the worst-ever ranking of Chinese Taipei in 2008 from the World Bank became a significant warning to the new government. To respond, the government, therefore, organized a task force and later upgraded the level of this task force to the cabinet, in order to effectively coordinate different departments to improve Chinese Taipei's international ranking. In other words, a fully political support ensures that Chinese Taipei's reforms can overcome bureaucratic obstacles and achieve real progress.

Second, a well-organized internal coordination mechanism to design improvement plans and monitor progress in each department also plays a critical role in Chinese Taipei's achievements. In this regard, the CEPD can take most credits from being successfully coordinating different departments, setting mutually acceptable goals, and closely watching the improvements made by each department. This internal coordinating mechanism has some important features to its success. First, it includes vice ministers from each department, implying that any decision or goal made in this mechanism can be actually implemented. Second, encountering conflicting interests from different departments, the Minister of CEPD or the Vice Premier can be the one who has the final say and makes a decision. Third, this mechanism requires its members to meet regularly, so it can closely monitor any progress and detect any issue during the implementation of reforms.

Finally, one factor that cannot be ignored is close cooperation with other external players. In this regard, it is important for Chinese Taipei to use APEC as an efficient platform to absorb valuable experiences and the best practices from other economies. As noted above, Chinese Taipei has learned important practices from New Zealand and other economies in terms of how to improve its business environment. Hence, on the issue of regulatory cooperation, APEC's emphasis on capacity-building through sharing best practice and exchanging experiences is extremely beneficial to Chinese Taipei. Furthermore, in order to improve its ranking in the *Doing Business* report, Chinese Taipei has to meticulously examine its performance in the report. And it also has to correct and report any flawed information to the World Bank. This way of exchange strengthens information flows and communications between Chinese Taipei and the outside ranking agency, which not only shortens the information gap between Chinese Taipei and international organizations, but also positively enhances Chinese Taipei's capacity to initiate regulatory reforms.

In sum, Chinese Taipei's successful experience on regulatory reforms in terms of improving its business environment is closely linked with its previously disappointing ranking in the World Bank's assessment as well as APEC's collective initiative on facilitating business environment in the region. The significant implications of this case include few points. First, the orientation of domestic regulatory reforms in Chinese Taipei has been significantly influenced by the standards and criteria set by the World Bank, suggesting that, to some

extent, Chinese Taipei's regulatory regime has gradually converged into the international standards. Second, Chinese Taipei's case also suggests a possible approach for APEC to make important progress, in which each economy can undertake regulatory reforms based on its own pace to achieve the common principles accepted by APEC members and be evaluated and monitored by the third party, such as the World Bank. Finally, although Chinese Taipei has made progress in the past years, it remains the last place among Asian Tigers and even lagged behind many East Asian economies. Hence, Chinese Taipei has to make more efforts in line with APEC's relevant initiatives to further move toward a more business-friendly environment.

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APPENDIX. CHINESE TAIPEI'S PERFORMANCE ON EASE OF DOING BUSINESS INDICATORS, 2004-2011

(Figures in brackets are the latest revised data from the World Bank)

Issued Year	Report Year	Ease of Doing Business Rank	Starting a Business					Dealing with Construction Permits			
			Rank	Procedures (number)	Time (days)	Cost (% of income per capita) (Cost US\$)	Paid-in Min. Capital (% of income per capita)	Rank	Procedures (number)	Time (days)	Cost (% of income per capita)
2003	DB2004			8	48	6.3 [6.1]	224.7 [217.4]			8	48
2004	DB2005			8	48	6.3	224.7			8	48
2005	DB2006	35		8	48	5 [6]	216.3	35		8	48
2006	DB2007	47	94	8	48	4.6	200	47	94	8	48
2007	DB2008	50	103	8	48	4.1	178.4	50	103	8	48
2008	DB2009	61	119	8	42	4.1	177.4	61	119	8	42
2009	DB2010	34 [46]	28 [29]	6	23	3.9	0	34 [46]	28 [29]	6	23
2010	DB2011	33	24	6	15	4.1	0	33	24	6	15

Issued Year	Report Year	Registering Property				Getting Credit				
		Rank	Procedures (number)	Time (days)	Cost (% of property value)	Rank	Strength of legal rights index (0-10)	Depth of credit information index (0-6)	Public registry coverage (% of adults)	Private bureau coverage (% of adults)
2003	DB2004									
2004	DB2005		3	5 [7]	6.2 [7.0]		3	5	0 [33.4]	33.4 [.]
2005	DB2006		3	5	6.2		3 [4]	5	0	57.1
2006	DB2007	24	3	5	6.2	48	3 [4]	5	0	59.5
2007	DB2008	24	3	5	6.2	48	3 [4]	5	0	67.1
2008	DB2009	26	3	5	6.2	68	4	5	0	62.7
2009	DB2010	30	3	5	6.2	69 [71]	4	5	0	63.2
2010	DB2011	32	3	5	6.2	72	4	5	0	90.4

Issued Year	Report Year	Protecting Investors					Paying Taxes						
		Rank	Extent of disclosure index (0-10)	Extent of director liability index (0-10)	Ease of shareholder suits index (0-10)	Strength of investor protection index (0-10)	Rank	Payments (no. per year)	Time (hours per year)	Profit tax (%)	Labor tax and contributions (%)	Other taxes (%)	Total tax rate (% profit)
2003	DB2004												
2004	DB2005		[6]										
2005	DB2006		7 [8]	4	5 [4]	5.3		22 [15]	340 [296]				34.9 [23.6]
2006	DB2007	60	7 [8]	4	5 [4]	5.3	78	23 [15]	340 [1104]				38.2 [35.8]
2007	DB2008	64	7	4	5	5.3	91	23	340				42.3 [40.6]
2008	DB2009	70	7	4	5	5.3	100	23	340				42.1 [40.4]
2009	DB2010	73	7	4	5	5.3	96 [92]	17 [18]	281				42.1 [40.4]
2010	DB2011	74	7	4	5	5.3	87	17	269	21	16.7	4.2	41.9

Survey Year	Report Year	Trading Across Borders							Enforcing Contracts				Closing a Business			
		Rank	Exports			Imports			Rank	Procedures (no.)	Time (days)	Cost (% of claim) [Cost US\$]	Rank	Recovery rate (cents on dollar)	Time (years)	Cost (% of estate)
			Docs (no.)	Time (days)	Cost (US\$ per container)	Docs (no.)	Time (days)	Cost (US\$ per container)								
2003	DB2004								37	47 [15]	510 [210]	17.7 [68]		81	1.9 [0.8]	4
2004	DB2005									47 [22]	510 [210]	17.7 [7.7]		81 [89.6]	1.9 [0.8]	4
2005	DB2006		5 [8]	12 [14]	747	6 [8]	12 [14]	747		47 [28]	510 [210]	17.7 [7.7]		80.2 [89.4]	1.9 [1]	4 [4]
2006	DB2007	42	5 [8]	12 [14]	747	6 [8]	12 [14]	747	62	47 [28]	510	17.7 [16.6]	4	80.3 [89.5]	1.9 [0.8]	4
2007	DB2008	29	5 [7]	12 [13]	747	6 [7]	12	747	92	47	510	17.7 [17.4]	13	80.2	1.9	4
2008	DB2009	30	5 [7]	12 [13]	757	6 [7]	12	769	88	47	510	17.7	11	80.9	1.9	4
2009	DB2010	15 [33]	5 [7]	12 [13]	720	6 [7]	12	732	90	47	510	17.7	11	80.9	1.9	4
2010	DB2011	17	5	12	645	6	12	700	90	47	510	17.7	10	82.2	1.9	4

4. Design of Chinese Taipei Governance Indicators and Implications for Effective Regulatory Policy¹

Abstract

This paper seeks to examine the effectiveness of regulatory policy among Asia-Pacific economies via the newly established set of governance indicators designed to measure governance quality under the Asian style government, and aims to bridge the gap between abstract guidelines and concrete outcomes of policies.

Effective regulatory policies lie in the midst of good governance, where sound enforcement and implementation of public affairs is made possible. For over a decade, many organizations like the World Bank have combined opinion surveys with official statistics to create various indicators of the governance of member economies. These indicators, however, capture only a few specific issues or were created from a western perspective, without benefit of insights about cultural sensitivity or the shared contexts of Asia-Pacific economies.

Therefore, this study constructs a set of governance indicators, initiated in 2008 for Chinese Taipei, and follows good governance guidelines defined by the Asia-Pacific Economic Cooperation (APEC). The indicators reflect seven dimensions of governance: rule of law, government efficiency, responsiveness, transparency, control of corruption, accountability, and public participation. This study adapts sources of both subjective (opinion surveys) and objective data (government statistics), from various regional economies and international organization databases along with a panel of experts from the government, private sector, academia, and the civil society. These experts will assess governance quality on annual bases. The unified governance scores are obtained from yearly assessments, and comparisons of multi-year estimates are conducted.

¹ Launched in 2008, this is a four-year study by Taiwan Public Governance Research Center (RDEC-TPG-097-005, RDEC-TPG-098-007, RDEC-TPG-099-006) funded by the Research, Development and Evaluation Commission of the Executive Yuan, Chinese Taipei and commissioned to National Taiwan University, Department of Political Science.

This study shares best practices from the governance indicators established by Chinese Taipei, and the operating experience of Asia-Pacific economies. It will provide government and the private sector guidance on facilitating governance and effective regulatory policy.

1. INTRODUCTION

Good public sector governance is the cornerstone of national competitiveness and the quality of democracy, and has a great influence on citizen trust towards the government and satisfaction to policies. Good public sector governance is being able to respond to the global demand in enhancing public sector efficiency, effectiveness and responsiveness; and bears the capability of structuring an appropriate mechanism that responds to the social, economic, cultural and political relationships that exist in this complex world.²

The 2008 Asia Pacific Economic Cooperation (APEC) Workshop on Government Performance and Result Management held in Chinese Taipei emphasized that public sector governance and regulatory reform, competition policy, corporate governance and strengthening economic and legal infrastructure are the keys to overcome structural impediment to economic growth in the Asia Pacific region. Indeed, good policy making sets the foundation for economic and legal framework. And with good public sector governance, policies are better implemented, and thus lead to a better economic future.

The United Nations Economic and Social Commission for Asia and the Pacific on the other hand, listed 8 major characteristics of good governance. It is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law. It assures that corruption is minimized, the views of minorities are taken into account and that the voices of the most vulnerable in society are heard in decision-making. It is also responsive to the present and future needs of society.

This is similar to public sector governance. Among the various definitions of public sector governance, APEC suggested that the most comprehensive one is that by the United States Institute of Internal Auditors: “Public sector governance encompasses the policies and procedures used to direct an organization’s activities to provide reasonable assurance that objectives are met and that operations are carried out in an ethical and accountable manner. In the public sector, governance relates to the means by which goals are established and accomplished. It also includes activities that ensure a government’s credibility, establish equitable provision of services, and assure appropriate behavior of government officials—reducing the risk of public corruption.”³ Thus, public sector governance indicates a status of completeness regarding systems and procedures, and emphasizes on the compliance of regulations by system and procedures.

To achieve good public sector governance, regulatory quality is a crucial element as sound and effective policies leads to economic development. Member economies of APEC and the Organization for Economic and Development (OECD) have recognized that regulatory reform is a central element in the promotion of open and competitive markets, and a key

² TPGRC. 2010 Taiwan Public Governance Indicators. The Executive Yuan.

³ APEC. 2011. APEC Outcomes & Outlook 2010-2011. Asia Pacific Economic Cooperation.

driver of economic efficiency and consumer welfare.⁴ APEC and OECD developed a checklist to assess regulatory reform. This checklist is comprised of four sections including 40 specific open questions in total⁵. However, open-end questionnaires often are more difficult to analyze, and can only reach out to very specific people in the public sector.

Therefore, this paper seeks to create a more comprehensive version of indicators to measure and assess governance – The Chinese Taipei Governance Indicators (CTGI). These indicators would need to incorporate the broader concept of public sector governance and be able to gather opinion from people in very different sectors. Section 2 of this paper introduces different governance indicators by various organizations that this paper referenced to construct CTGI. Section 3 lays out the methodology used in CTGI, section 4 shows the result of CTGI, and section 5 concludes the paper.

2. ESTABLISHING GOVERNANCE INDICATORS

Chinese Taipei government has dedicated to establish a set of comprehensive public governance indicators in 7 dimensions: rule of law, government efficiency, responsiveness, transparency, control of corruption, accountability, and public participation. These indicators can be used to assess the nature of politics, to evaluate the implementation of regulatory policies, and to provide the recommendations of regulatory policy revisions since 2008.

Numerous international or regional organizations and public sectors have collaboratively or individually developed the framework or operational indicators to assess the public governance performance. However, many of these only focus on a certain part of the public governance performance. For instance, Freedom House⁶ specifies on measuring the degree of freedom of a country which is defined by level of democracy; also, it measuring freedom of the press, an important aspect to regulatory policy as media now serve as public guardian to government deeds. Transparency International, measured corruption since 1993, and published its annual report on corruption, with a specific topic each year. Different public sectors have also tried to measure government performance. The most common approach is public opinion surveys. For instance, the Research, Development and Evaluation Commission of Chinese Taipei Executive Yuan publishes Public Satisfactory Poll regularly on government

⁴ OECD. 2008. “APEC–OECD Cooperative Initiative on Regulatory Reform.” Organization for Economic Co-operation and Development.

⁵ According to the 2008 “APEC–OECD Cooperative Initiative on Regulatory Reform,” the first is a horizontal questionnaire on regulatory reform across levels of government that invites reflection on the degree of integration of regulatory, competition and market openness policies across levels of government, and on the accountability and transparency mechanisms needed to ensure their success. The second is regulatory policies which are designed to maximize the efficiency, transparency and accountability of regulations based on an integrated rule-making approach and the application of regulatory tools and institutions. The third is competition policies which promote economic growth and efficiency by eliminating or minimizing the distorting impact of laws, regulations and administrative policies, practices and procedures on competition; and by preventing and deterring private anti-competitive practices through effective enforcement of competition laws. The fourth is market openness policies which aim to ensure that a country can reap the benefits of globalization and international competition by eliminating or minimizing the distorting effects of border as well as behind-the-border regulations and practices.

⁶ Freedom House releases the annual “freedom in the world” rating of global political rights and civil liberties each year. More can be found at: <http://www.freedomhouse.org/template.cfm?page=594>.

efficiency.⁷ It also contracted out individual projects to the Taiwan Public Governance Research Center⁸ to understand a certain aspect of governance, such as disaster management, financial transparency, operation of policy planning agencies, etc. However, these projects alone cannot show a comprehensive view of public sector governance.

Some organizations did try to capture the different aspects of governance. For instances, the Asia-Pacific Economic Organization (APEC) talked about good governance as the key to good public sector governance. It suggested that governments should hold accountability and be transparent, manage the performance of public sector agencies, monitor political and bureaucratic structures, develop good policy and institutions, be responsive to stakeholders, and ensure rule of law and public sector ethics and probity. The Organization for Economic Cooperation and Development (OECD) also developed some criteria of good governance under “Public Governance and Management.”⁹ In addition, the United Nations (UN) Program in the Division for Public Administration and Development Management and the World Bank (WB) Public Sector and Governance Organization both have governance related projects concerning public sector performance. Nonetheless, these criteria are not operational.

The Worldwide Governance Indicators (WGI) developed by the World Bank Institute is by far the most comprehensive and operational set of governance indicators. WGI looks at accountability, public participation, rule of law, regulatory quality, government efficiency, corruption and political stability; and integrates opinion survey data with government statistics¹⁰. The World Competitiveness Index (WCI) from the Institute of Management and Development (IMD) in Switzerland also has a set of operational indicators featuring business efficiency, government efficiency, economic performance and infrastructure.¹¹ Nevertheless, the indicators developed did not account for the fact that the political environment and the nature of policy making are different among Asian nations. Therefore, those sets of indicators may not fully apply to Chinese Taipei, or other Asia Pacific nations. Table 4-1 summarizes indicators by different organizations that CTGI referenced.

⁷ Each year, Research, Development and Evaluation Commission of the Executive Yuan, Chinese Taipei and local governments conduct Public Satisfactory Survey on different topics relating government policies and policy implementations, such as transportation, public construction, education, etc.

⁸ Taiwan Public Governance Research Center established in 2008, and is to provide timely research support on issues of public governance, in accordance with the goals of the Research, Development and Evaluation Commission. More information can be found here: <http://www.tpgrc.org.tw/en/>.

⁹ These criteria include budgeting and public expenditures, e-governance, fighting corruption in the public sector, public finance, and regulatory policy. For the specifics of each criterion, please refer to the OECD public management website at: http://www.oecd.org/topic/0,3373,en_2649_37405_1_1_1_1_37405,00.html.

¹⁰ For data source and analysis result, please refer to the WGI official website at: <http://info.worldbank.org/governance/wgi/index.asp>.

¹¹ A full description of indicators and analysis results are on the WCI website at: <http://www.imd.org/research/publications/wci/index.cfm>.

Table 4-1 Governance Indicators by Organization

CTGI	OECD	UN Program in DPADM	APEC	WGI	IMD
Rule of Law	N/A	N/A	Jurisdiction effectiveness	Rule of law	Economic Performance/ Business Efficiency
Government Efficiency	System governance; budget; employment; public finance	Governance system and organization power division	Performance management; politics and bureaucratic	government effectiveness/ regulatory quality	Government Efficiency/ Infrastructure
Responsiveness	N/A	N/A	responsiveness	N/A	Government Efficiency
Transparency	E-governance	Transparency and accountability mechanism	Transparency	corruption	Government Efficiency
Accountability	N/A	Transparency and accountability mechanism	Accountability mechanism	accountability	Government Efficiency/ Business Efficiency
Control of Corruption	Ethics and corruption of the public sector	N/A	Morality guidelines of the public sector	corruption and political stability	Government Efficiency
Public Participation	N/A	N/A	N/A	Public participation and political civil rights	N/A

Hence, following the good governance framework set by APEC, the Chinese Taipei Governance Indicators (CTGI) were proposed and built based on the comprehensive overview of operational indicators from multiple international and regional organizations. The comprehensive CTGI framework covers seven main dimensions of the public governance performance, which are Rule of Law, Government Efficiency, Responsiveness, Transparency, Control of Corruption, Accountability, and Public Participation. Each main dimension has at least two sub-dimensions and they have been defined as below:

- **Rule of Law** - this dimension focuses on the rigor and efficiency of the Chinese Taipei judicial and legislative systems, and whether the government has provided a stable environment for investment to Chinese Taipei's international competitiveness. Three sub-dimensions cover the development of the rule of law in Chinese Taipei:
 - Legislative regulation - how protective laws and regulations are;
 - The judicial system - assess whether law implementation is fair and just;
 - Police administration - efficiency regarding maintaining social order.
- **Government Efficiency** - analyses government's ability to implement policies and its consistency regarding the direction of policy making. It is analyzed in two sub-dimensions:
 - Individual policies – measuring public satisfaction of individual policy efficiencies;

- Comprehensive policy making – assessing the efficiency of the total outcome of policy making and implementation.
- **Responsiveness** - refers to how far government policies satisfy public demands. The purpose of this dimension is to look at whether individual policies respond to public needs, and whether policy-making generally is able to take account of different public demands. Two sub-dimensions are:
 - Active responsiveness - how responsive public sectors are, to acknowledge public needs, and make relevant policies;
 - Passive responsiveness - how responsive public sectors are to public demands.
- **Transparency** - denotes the availability to the public of clear, accurate and low-cost information on government policies and their implementation. This dimension examines the level of information on government policies, elections and finances released by the Chinese Taipei. Three sub-dimensions are:
 - Information transparency - accessibility of government information;
 - Political transparency - whether public officials are transparent about their income, use of political donations, and other financial status;
 - Financial transparency – assess legitimacy of budgetary status according to OECD’s “Best Practices for Budget Transparency.”
- **Control of Corruption** - corruption refers to any behavior leading to illegitimate personal gain for any individual or group within the executive, legislative or judicial branches in the course of their duties or political activities. This indicator looks at the situation within the government, as well as examining the state of political ethics underpinning it. The two dimensions are:
 - Corruption Perception - reviews abuse of political power for personal gain in four government sectors: executive, legislative, judicial and others;
 - Ethics- measures the strength of ethical standards and anti-corruption measures.
- **Accountability** - looks at the strength of external supervision of the government’s use of data and exercise of political power, including forms of accountability, the relationship between the executive and legislative branches and the personal integrity of public servants. Five dimensions are:
 - Auditing – assess government finance as a whole;
 - Budget control – how well the government is in controlling deficits;
 - Government procurement – review the procedures of procurement;
 - Code of Conduct – assess the behavior of government employees;
 - Representative accountability – assess whether representatives and legislators have fulfilled their duties.
- **Public Participation** - reviews the current level of public participation in government and social affairs in Chinese Taipei, including the political party system, the role of interest groups in policy implementation, and freedom of the media and political expression. Two dimensions are:

- Political participation – includes direct participation, like voting, or indirect participation, like expressing point of views to local representatives;
- Freedom of Press and Speech – degree of freedom of mass media and freedom of public to express their ideas.

3. METHODOLOGY

CTGI is divided into objective (statistical) data and subjective (opinion) data, and then integrated into a single score. This is a common method used in governance indicators, such as WGI¹² and IMD.¹³ Research at the World Bank¹⁴ pointed out that the advantage of an aggregated governance indicator is that it can provide more precise measures of government effectiveness than individual indicators, such as the Corruption Perception Index (CPI) or country freedom rating. Also, it is easier to make cross-country comparison by taking the advantage of both the aggregated and individual indicators to test the difference in governance among countries. Therefore, the CTGI is developed based on the current methodology set by international organizations, but created the database only with Chinese Taipei data for the indicator to be applicable to Asian politics.

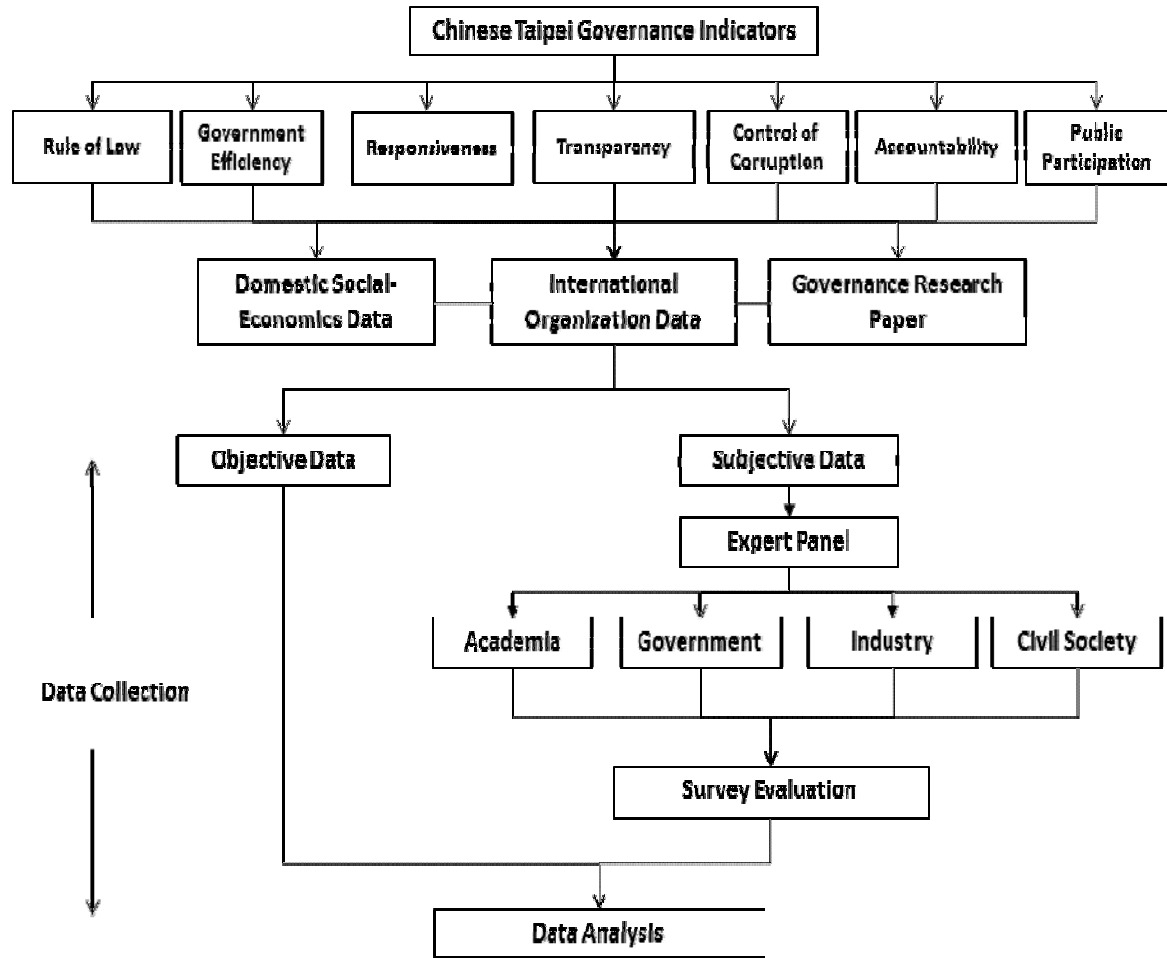
CTGI objective data is taken from statistical data of domestic political-economic statistics and international organizations. The subjective data is collected from surveys evaluated by a panel of experts. The survey questions used to interview experts are designed by CTGI team, with reference to domestic and international research reports and complemented by specially designed questions. Figure 4-1 summarizes the research method of this study.

¹² Kaufmann, Daniel, Kraay, Aart & Massimo Mastruzzi. 2010. *The Worldwide Governance Indicators: Methodology and Analytical Issues*. World Bank Policy Research Working Paper No. 5430. The World Bank.

¹³ Rosselet-McCauley, Suzanne. 2011. *Methodology and Principles of Analysis*. World Competitiveness Yearbook. IMD.

¹⁴ Kaufmann, Daniel, Kraay, Aart & Zoido-Lobaton, Pablo. 1999. *Aggregating governance indicators*. *Policy Research Working Paper*. The World Bank.

Figure 4-1. Research Methodology



Subjective Data

Subject data is obtained by a survey created by the CTGI team. The survey referenced international and domestic governance research projects and surveys, including the WB Worldwide Governance Indicators, the Global Competiveness Yearbook by the World Economic Forum, Taiwan Social Change Survey (TSCS) by the Academia Sinica, and Taiwan's Election and Democratization Study (TEDS). The first wave of CTGI was conducted in 2008, which consisted of 116 items, with 16-20 items in each dimension. CTGI also used principle component method to analyze the relationship of questions within each items and among all dimensions, and adjust the questions wordings or the classifications of items accordingly. Thus in 2009, the survey had 14 revised items, and in 2010, the survey was revised again to 127 items. In 2011, CTGI is continuing to use the same 2010 version survey for evaluation. Table 4-2 indicates sources of the seven dimensions in CTGI.

Table 4-2. Sources of Subjective Data

Dimension	Sub-dimension	Source
Rule of Law	Legislative Regulation	WB Worldwide Governance Indicators
	Judicial System	
	Police Administration	
Government Efficiency	Individual Policies	Revised from TEDS 2003
	Comprehensive Policy Making	Revised from IMD government efficiency
Responsiveness	Active Responsiveness	Revised from TSCS no.5-2
	Passive Responsiveness	Revised from TEDS 2003, 2004
Transparency	Information Transparency	Data extracted from government transparency study by the Executive Yuan
	Political Transparency	
	Financial Transparency	IMD
Control of Corruption	Corruption Perception	Ministry of Justice Survey 2007
	Ethics	Papers from Transparency International, Taiwanese National Integrity System
Accountability	Auditing	OECD Budget Governance and Management guidelines
	Budget Control	
	Government Procurement	
	Code of Conduct	
	Representative Accountability	Revised from OECD
Public Participation	Political Participation	TSCS
	Freedom of Press and Speech	

Expert Panel

The survey is designed for an Expert Panel consisted of Chinese Taipei experts from the academia, government, industry to evaluate the seven dimensions of governance. The Expert Panel was launched in 2008. Panel experts in that year helped CTGI in accessing the applicability of the survey, and provided suggestions for improving the data collection of the survey. Thus, the survey result of 2008 is only for revision reference. The composition of the Panel is described as below:

- For academia, CTGI recruited board members from the “Taiwan Association for School of Public Administration and Affairs (TASPAA)” and editors from “Taiwan Social Science Citation Index (TSSCI),” and scholars from university in the field of political science, sociology, economics, law and management;
- For government, CTGI asked government employees in the Research and Development department from both the local and central government agencies;
- For industry, CTGI referenced the top 100 companies listed in the Common Wealth Magazine which categorize these companies into manufacturing, financial and service industry.

In 2010, CTGI added another field of experts –civil society to fully accomplish the idea of governance. Civil society is made up of nongovernmental organizations (NGOs) and the mass media. CTGI researched NGOs that are not sponsored by the Chinese Taipei government, and that has the most “hit” in google.com to ensure the representativeness of that particular NGO. Table 4-3 summarizes the composition of the Expert Panel.

Table 4-3. Composition of the Expert Panel

Field of Expert	Sub-field of Expert	Number of Experts							
		2008		2009		2010		2011	
Academia	TASPAA & TSSCI	19	111	15	97	15	105	21	119
	Political Science	18		19		22		21	
	Sociology	20		10		15		17	
	Economics	18		23		26		26	
	Law	16		12		9		11	
	Management	20		18		18		23	
Government	Central R&D	22	39	24	42	37	62	37	59
	Local R&D	17		18		25		22	
Industry		29	29	37	37	35	35	39	39
Civil Society	NGOs	N/A		N/A		23	28	22	34
	Media					5		12	
Total		179		176		230		251	

Objective Data

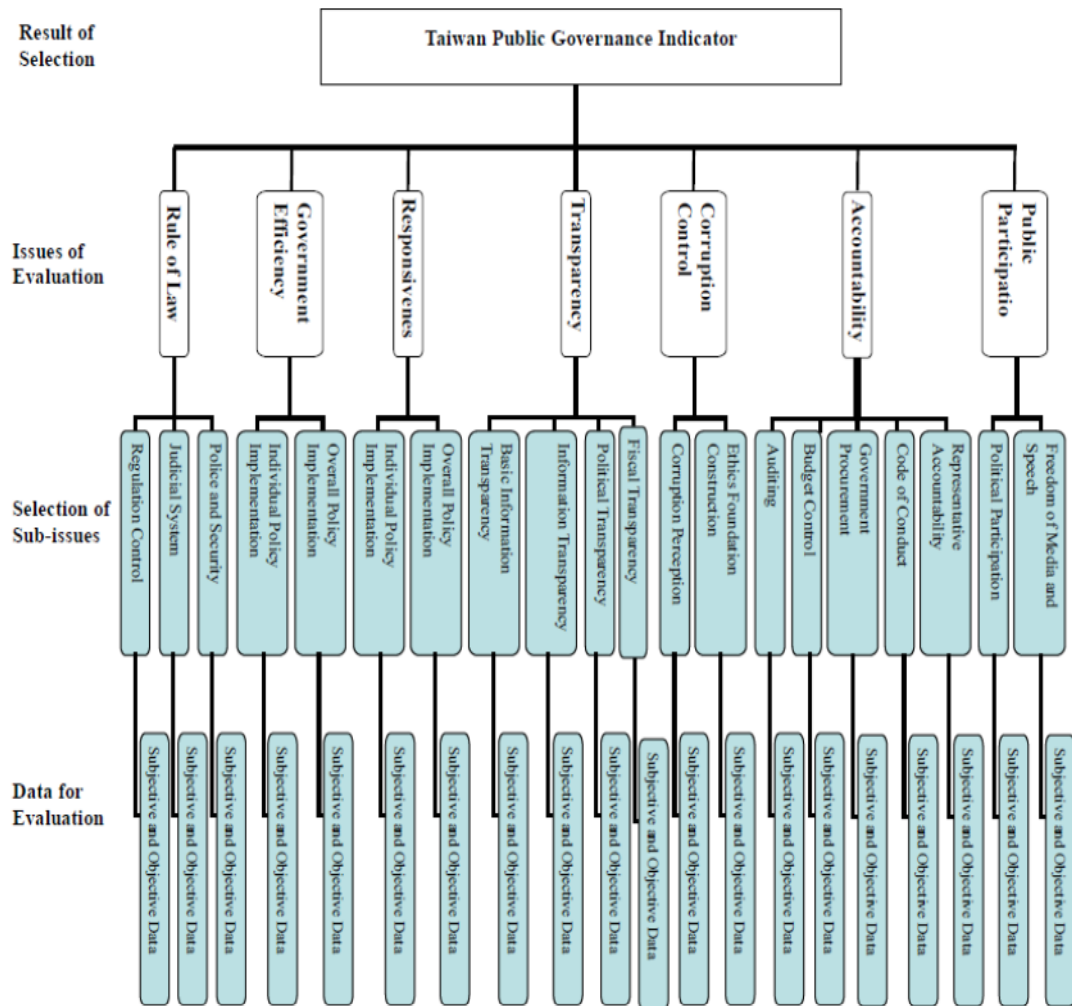
Objective data is collected from domestic sources and international databases. The CTGI dataset is mainly governmental statistics. Ministry of Economic participates with IMD each year providing statistics on economics, trade, GDP, etc. Also, CTGI reviewed governmental statistics from different ministries, and selected appropriate data that represents corresponding sub-dimensions. For instance, statistics from our own judicial system, law system, control system, police system, annual audit bulletin of the Ministry of Audit, the Public Construction Commission, and the National Communications Commission. As for international sources, data for “transparency” is from the OECD budgetary database. Public Participation data references media freedom from Reporters without Borders, IMD, WGI, Transparency International (TI) and the Freedom House. Table 4-4 summarizes sources of each dimension of the objective data.

Table 4-4. Sources of Objective Data

Dimension	Sub-dimension	Source
Rule of Law	Legislative Regulation	IMD efficiency data
	Judicial System	Taiwanese Judicial & Regulatory Statistic
	Police Administration	Police Department Statistic
Government Efficiency	Individual Policies	IMD Efficiency Data
	Comprehensive Policy Making	
Responsiveness	Active Responsiveness	IMD Efficiency Data
	Passive Responsiveness	
Transparency	Information Transparency	OECD budgetary dataset & “The Freedom of Government Information Law”
	Political Transparency	
	Financial Transparency	Control Yuan Statistics
Control of Corruption	Corruption Perception	Ministry of Justice Statistics
	Ethics	Examination Yuan Statistics

Dimension	Sub-dimension	Source
Accountability	Auditing	Ministry of Audit Annual Statistical Report
	Budget Control	IMD Efficiency Data
	Government Procurement	Public Construction Council statistics
	Code of Conduct	Judicial Yuan Statistics
	Representative Accountability	Examination Yuan Statistics
Public Participation	Political Participation	General Budgeting, Accounting, and Statistic Data
	Freedom of Press and Speech	Judicial Yuan statistics & National Communications Council Statistics

Figure 4-2. Hierarchies and Networks of CTGI



Weight Distribution

In order to transfer and combine subjective and objective data into a concrete score, the each field of experts and dimensions need to be assigned a weight. CTGI uses Analytical Hierarchy Process (AHP) to determine the weight of different fields of the expert panel, and Analytic Network Process (ANP) to calculate the weight of different dimensions. AHP and ANP use paired-comparison to analyze the relative importance of the factors that are being analyzed. In CTGI’s case, this method is to find out the weights for each dimensions/sub-dimensions, and each field of experts. The difference between AHP and ANP is that in a hierarchy, each item needs to be independent from one another, but in a network, this is not required. In the CTGI

case, experts should be independent when making their decisions. However, the seven dimensions of governance are inter-dependent; for instance, good control of corruption is beneficial to rule of law. Figure 4-2 shows the hierarchy of the dimensions and sub-dimensions of the indicators, and Tables 4-5 and 4-6 are the weights obtained.

Table 4-5. CTGI Weights for Expert Panel

Field of Expert	Weight	Sub-field of Expert	Weight
Academia	0.284	TASPAA & TSSCI	0.241
		Political Science	0.262
		Sociology	0.145
		Economics	0.156
		Law	0.134
		Management	0.062
Government	0.189	Central R&D	0.77
		Local R&D	0.23
Industry	0.197		
Civil Society	0.331	NGOs	0.425
		Media	0.575
Total	1		

Table 4-6. CTGI Weights for the Seven Dimensions

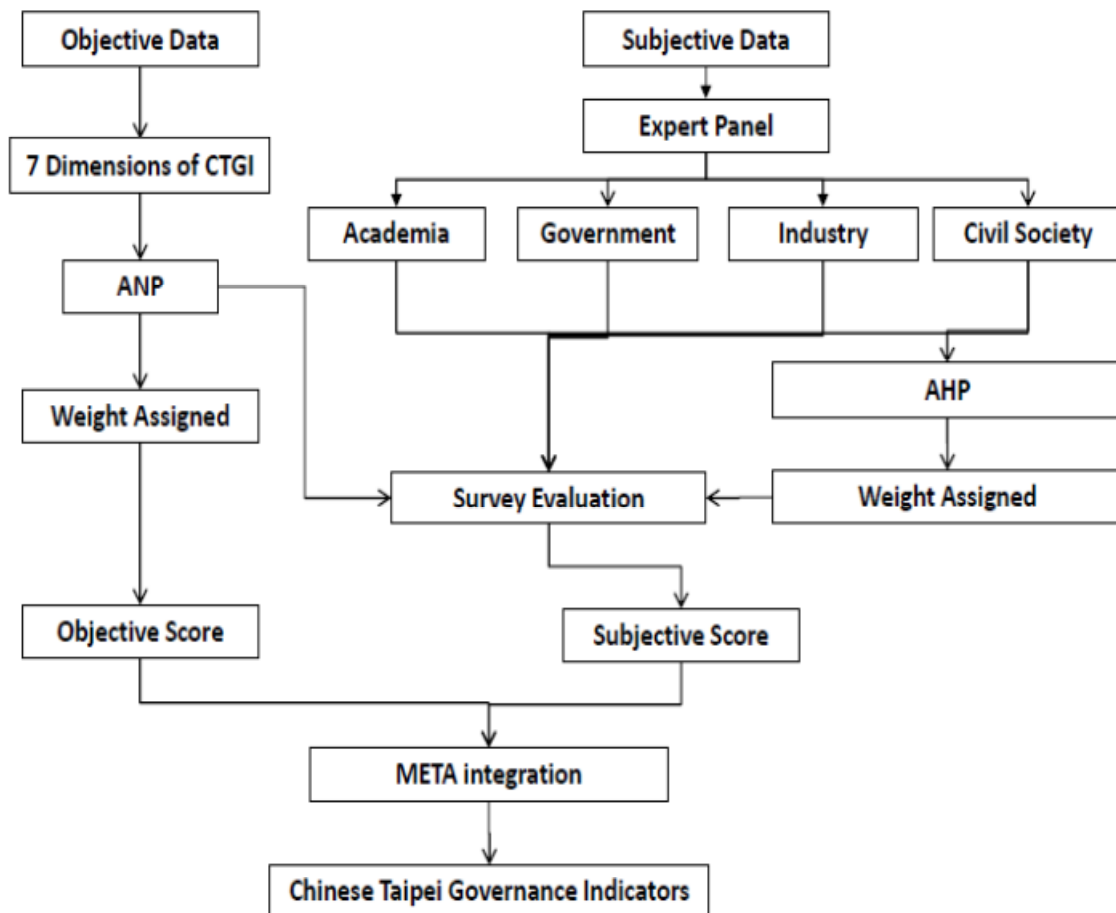
Dimension	Weight	Sub-Dimension	Weight
Rule of Law	0.154	Law & Regulation	0.377
		Judicial System	0.47
		Crime & Order	0.153
Government Efficiency	0.124	Individual Policies	0.35
		Comprehensive Policy Making	0.65
Responsiveness	0.139	Active Responsiveness	0.579
		Passive Responsiveness	0.421
Transparency	0.148	Basics	0.144
		Information Transparency	0.42
		Political Transparency	0.25
		Financial Transparency	0.186
Control of Corruption	0.15	Corruption Perception	0.494
		Ethics	0.506
Accountability	0.15	Auditing	0.16
		Budget Control	0.163
		Government Procurement	0.181
		Code of Conduct	0.169
		Representative Accountability	0.327
Public Participation	0.136	Political Participation	0.417
		Freedom of Press and Speech	0.583
Total	1		

Data Transformation and Combination

Subjective data and objective data first undergo Z score standardization, and then calculated separately by different weights, then combined together to form a single score for CTGI.

Figure 4-3 shows the how the score for each indicator is formed.

Figure 4-3. CTGI Data Transformation



Subjective Data

Each item in the survey is originally rated on a 0-10 scale for consistency and calculated as below:

- For each survey item, the average score for each field and sub-field of experts is calculated first as the raw score.
- The raw score is then multiplied by the assigned weight accordingly (see table 4) and this weighted average score represents each item under different expert fields.
- The weighted score obtained from above then is multiply by the different dimension weight (see Table 4-5).
- The sum for weighted scores from all dimensions and sub-dimensions is final the subjective data result for CTGI.

Objective Data

Objective data comes in different units, and therefore needs to be statistically standardized before further data transformation.

- Baseline score is calculated by the average of the latest 5 year data. For instance, baseline score for 2011 would be the average for 2006 – 2011.
- Standardized score for each item is calculated as: (current year data – the latest 5 year average) / (s.d. of the latest 5 year data)
- Majority of the standardized score falls between -3 and 3, and would transform into 0 to 10 accordingly, to be consistent with subjective data. Any value which is larger (smaller) than 3 (-3) is treated as 3 (-3) and then transformed.
- The transformed score for each item has the same weight within their sub-dimensions; therefore, the average of the total items under each sub-dimension is the “raw score.”
- The raw score is multiplied by the assigned weight of each sub-dimension, and then multiplied by the assigned weight of each dimension.
- The sum for weighted scores from all dimensions is the objective data result for CTGI.

Data Combination

To assign combine both subjective and objective data, CTGI referenced data transformation methods of IMD and WGI and learned what are appropriate weights of these two types of data. WGI argues that subjective data should have heavier weight than objective, while IMD assigned 1/3 to subjective and 2/3 to objective data. CTGI put a lot of effort in establishing the Expert Panel, and selecting experts, designing the survey. These experts are valuable to the construction of CTGI, therefore, CTGI agrees with WGI’s point of view, and assigns 2/3 to subject data and 1/3 to objective data. The final score of CTGI is therefore the sum of the total weighted score of subjective and objective data with their designated weights.

4. DATA ANALYSIS

The Expert Panel is a major accomplishment in CTGI. Subjective data analysis shows that though governance performance is improving each year, there are significant differences of opinion among experts. Government experts are much more optimistic about governance situation in Chinese Taipei, while the civil society is more critical about it. Integrally, accountability and government efficiency are two worst performed CTGI dimensions before 2011, while rule of law has a significantly higher score. This suggested that there are sufficient regulations and laws, but there are issues within policy implementation that government officials must pay attention to. However, the objective score of government efficiency dimension improved significantly in 2011, which is most likely due to Chinese Taipei’s good economic performance in international trade and business. However, the subjective score of government efficiency, whether taken the civil society into account of not, did not show such improvement. Nevertheless, considering that subjective score weights 2/3 of the total score, the total score of government efficiency still improved.

Also, if looking at objective scores, generally they are all higher than subjective data. And it is worth noting that though government efficiency and accountability got lowest subjective scores, they have relatively high objective scores. This suggests that authorities should re-examine government data bases, and consider modifying. Tables 4-7 and 4-8 summarize objective score and subjective score of each CTGI dimension with and without the Civil Society experts.

Table 4-7. Data Analysis Result with Civil Society

Dimension	2010			2011		
	Subjective	Objective	Total	Subjective	Objective	Total
Rule of Law	5.42	5.46	5.44	5.29	4.99	5.19
Government Efficiency	5.74	4.61	5.36	5.63	5.80	5.68
Responsiveness	6.10	6.23	6.14	6.23	5.96	6.14
Transparency	5.87	5.59	5.78	5.93	5.54	5.80
Control of Corruption	5.79	5.77	5.78	5.69	5.45	5.61
Accountability	6.17	4.30	5.56	6.07	4.66	5.60
Public Participation	6.29	5.10	5.90	6.26	5.61	6.05
Total	5.91	5.31	5.71	5.87	5.42	5.72

Table 4-8. Data Analysis Result without Civil Society

Dimension	2009			2010			2011		
	Sub	Obj	Total	Sub	Obj	Total	Sub	Obj	Total
Rule of Law	5.32	5.71	5.45	5.56	5.46	5.53	5.50	4.99	5.33
Government Efficiency	5.94	4.85	5.58	6.01	4.61	5.54	5.82	5.80	5.81
Responsiveness	6.34	5.79	6.16	6.39	6.23	6.34	6.29	5.96	6.18
Transparency	5.89	4.89	5.56	6.00	5.59	5.86	6.02	5.54	5.86
Control of Corruption	5.79	5.24	5.61	6.10	5.77	5.99	5.95	5.45	5.78
Accountability	6.11	4.80	5.67	6.45	4.30	5.73	6.28	4.66	5.74
Public Participation	6.38	4.49	5.75	6.46	5.10	6.01	6.49	5.61	6.20
Total	5.96	5.13	5.68	6.14	5.31	5.86	6.05	5.42	5.84

Differences of Opinion on Expert Panel

When the Panel was first launched, there were variances among expert opinion. Therefore, different weights were assigned to the experts.

In 2008, the first year of CTGI, and “civil society” has yet added to the panel, the lowest score was rated by the Academia throughout the seven dimensions. But Government rated the scores generally higher. Industry is somewhere in between. From the coefficient of variation, Industry shows the smallest degree of variation, meaning experts in this field have less variance in the evaluation of the seven governance dimensions. On the other hand, Academia has the highest degree of variation in all seven dimensions. Also, Analysis of Variation (ANOVA) shows that experts have very different opinions about CTGI. Therefore, weights were assigned to the Expert Panel to illustrate the differences with AHP (see the methodology section) starting the second year of CTGI.

As Table 4-4 shows, Civil Society experts have the highest weight in CTGI, Academia the second, and Government has the lowest. The AHP result corresponds with the common belief that the people should have a louder voice in public governance. However, after weights were assigned, analysis still showed that Academia gave the lower score, and Government the highest. And Civil Society gave lower scores to almost all of the dimensions in CTGI.

Subjective Data Analysis

Rule of Law

Members from the economic field of academia and nongovernmental organizations granted lower scores to this dimension. This also indicates that they have less confidence in the economy in comparison with governmental agencies. Also, Panel members from each sub-field gave relatively lower scores to the Judicial System sub-dimension.

Government Efficiency

In terms of Individual Policies, experts from all four fields gave higher scores to “national health”, “personal and property safety”, and “cross-straits relations.” Moreover, government and industries gave scores higher than 6.00 for “tax reform.” However, Comprehensive Policy Making received lower scores, with members of civil society giving scores averaging below 5.00.

Responsiveness

“Government” gave the highest scores for this dimension, followed by members from industry, both gave scores higher than 5.00. In contrast, members from the academia and civil society gave relatively lower scores. This strongly shows the differences between the government and the public. However, “industry” does agree that government is being responsive to their needs, and this is a positive sign for business development.

Transparency

All experts, especially academic experts in law, gave relatively lower scores to “Political Transparency”, and lowest to “conduct for the handling of 2009 election expenses”, “degree of execution of campaign budget-related regulations”, and “degree of transparency when legislative institutions are discussing an act.” Members of civil society yet gave very high scores to the “necessity of change” for “law of governmental information publicity.” All in all, it shows that nongovernmental organizations and media place hopes on the criterion of governmental information publicity.

Control of Corruption

It is worth noting that central government gave higher scores to this dimension than local government, and is more confident than both academia and the civil society. However, the public is directly influenced by public sector corruption, and public perception on control of corruption should be taken into account seriously.

Accountability

Civil society gave lower scores than experts from other fields, and the score for some items was even lower than 5.00. In general, government had a relatively optimistic attitude towards the accountability of our country in 2009. This is evident from the higher scores given by the government in comparison with other fields. Supervisors from TASPAA and editors from TSSCI public administrative and political journal gave comparatively lower scores than the heads of faculties of law and administration. By the same token, nongovernmental organizations also showed similar evaluation.

Public Participation

Government experts gave relatively higher scores, and experts from other fields all gave lower scores. The media in the civil society gave even lower scores. This shows that the influence of the media is not likely being affected even if it receives its budget from the government.

Differences between Objective Data and Subjective Data

Tables 4-7 and 4-8 show the analysis results of CTGI. Note that in 2008, the pilot year of CTGI, data is analyzed differently and is therefore not included in the CTGI multi-year comparison. Also, Civil Society experts were added to the Expert Panel in 2010, therefore, CTGI used different weights and calculated scores with and without Civil Society experts for comparison purposes.

Generally speaking, subjective scores are higher than objective scores (see Table 4-7 and 4-8). This suggests that there is a gap between our panel assessors and Chinese Taipei's statistical data. Either experts are more positive about CTGI, or Chinese Taipei needs to rethink and improve the social-economic data system.

CTGI Yearly Improvement

Figures 4-4 through 4-7 show the yearly trend of CTGI. Without the civil society, CTGI analysis suggested that government performance improves each year. However, if civil society is taken into account, CTGI does not show yearly improvement. When considering only Academia, Industry and Government experts in the Expert Panel, total scores improved by 3% from 2009 to 2010, but a slight decrease of 0.3% from 2010 to 2011. However, from individual dimensions, objective data all improved; though there are variances among subjective data, but majority improved. Nevertheless, when consider all four fields of experts, the total CTGI score went from 5.71 in 2010 to 5.72 in 2011, indicating that there was almost no improvement in government performance when considering the opinions of the civil society.

Figure 4-4. CTGI Trend-Subjective Data with Civil Society

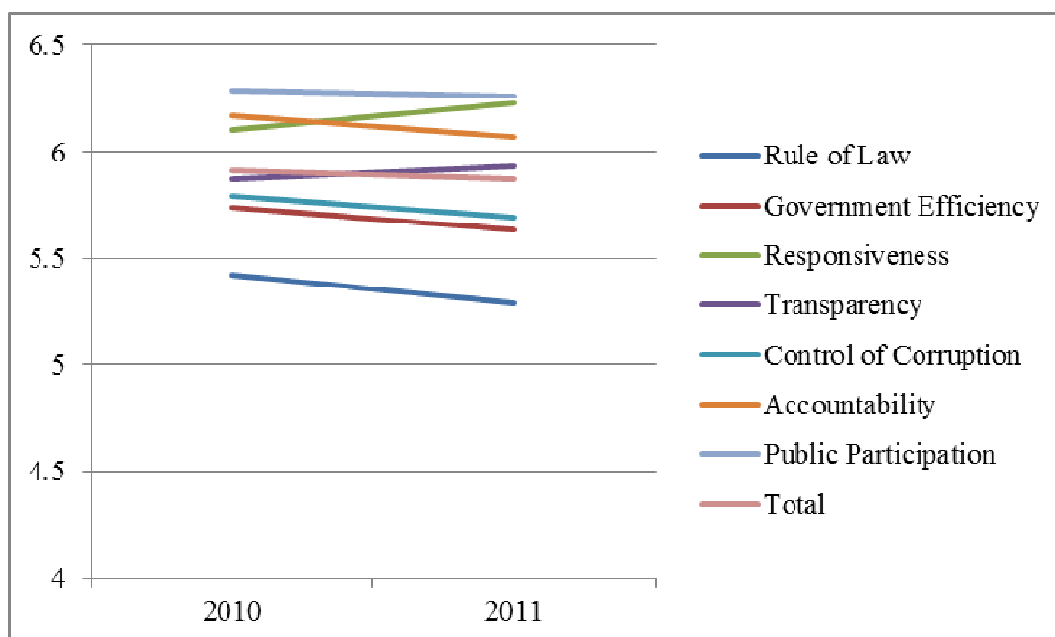


Figure 4-5. CTGI Trend-Subjective Data without Civil Society

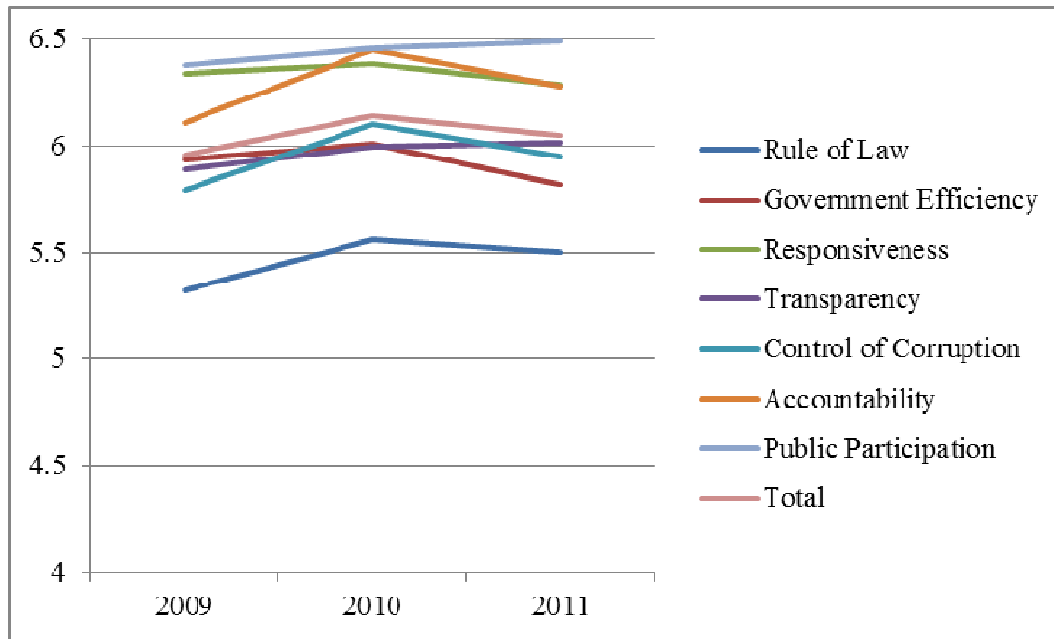


Figure 4-6. CTGI Trend-Objective Data

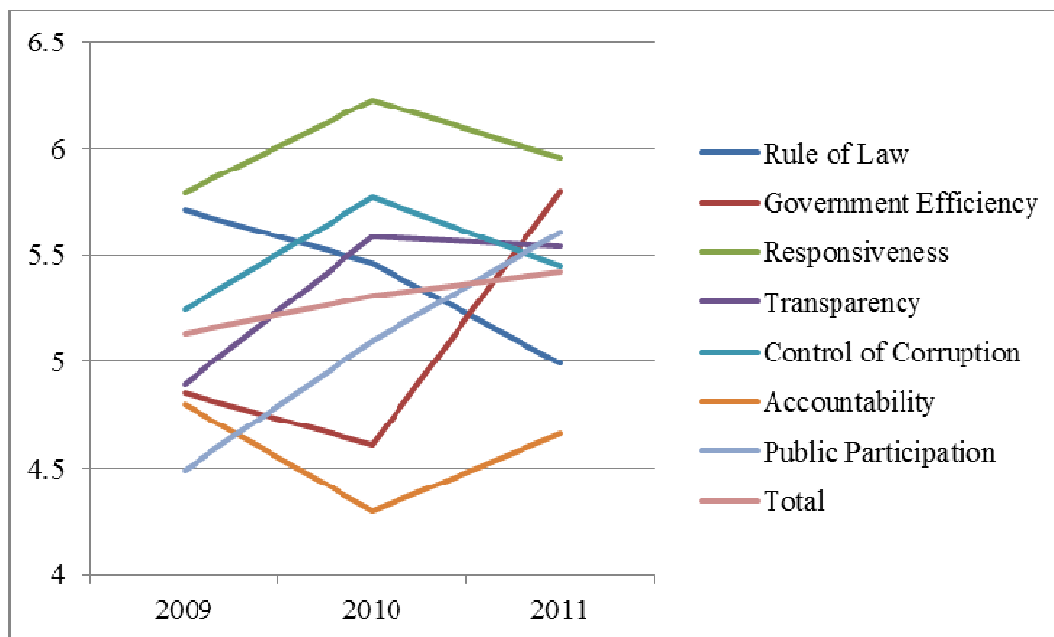
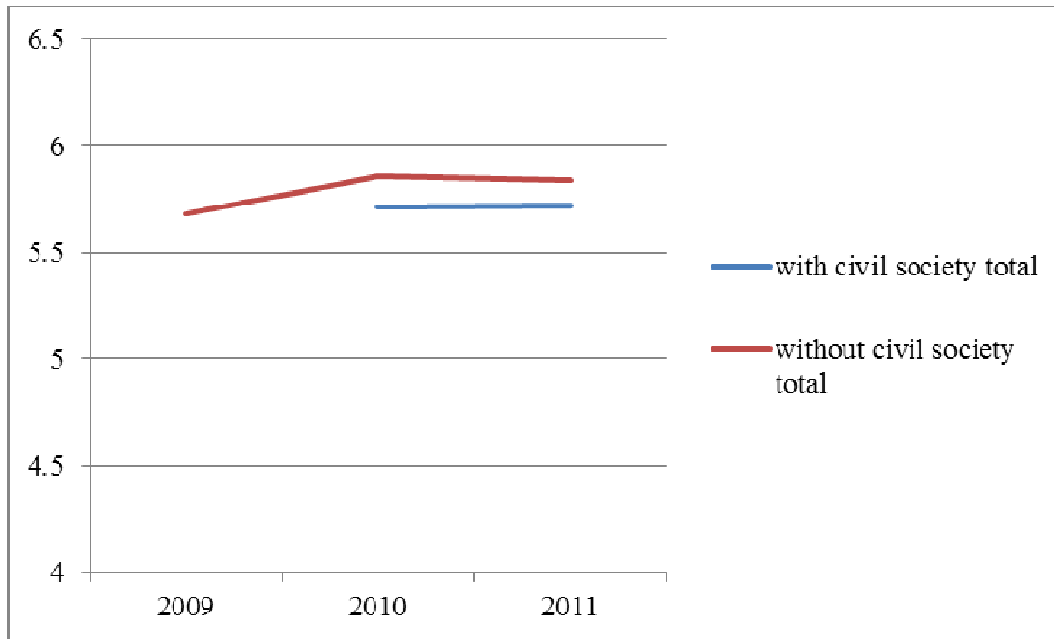


Figure 4-7. CTGI Trend–Total Score



5. CONCLUSION

The CTGI framework was established in 2008 and the CTGI score is generated annually in late August and released at the end of the year. CTGI referenced WGI for its research methods and indicator framework, and applies exclusively Chinese Taipei data to see differences in analysis. According to the current analyses in 2008-2011, this study highlights significant differences in scores of governance performance among panels, where government officials tend to give high scores and civil society low scores. This discrepancy reflects not just differences between government policies and public perception but also in the understanding of the stream between policymaking and policy implementation. Thus, to be successful, a policy must be implemented efficiently and effectively, and most important, the public need to be aware of it and agree with what the government has done. Otherwise, enforcement agencies don't make appropriate implementations or don't correct implementation and the reform fails due to lack of public support.

The most challenging task for CTGI is to systematically measure public opinion of governance and, at the same time, assist the government in understanding the status of public governance development. Another key challenge is to secure regulatory quality and ensure that the CTGI measurement system can be integrated into the management system properly. Performance measurement is not an end in itself but a means to support better decision-making based on previous performance in order to improve performance and/or accountability and ultimately lead to better outcomes for society that can be communicated to stakeholders. As a powerful decision-making tool, performance measurement can either provide objective justification for organizational and management decisions or else inform management as to the changes required, thereby clarifying and hastening the decision-making process (OECD 2011).

Currently, the CTGI framework and the subjective-objective data combined methodology are in place to enable long-term follow up on the government's overall performance in public governance. The CTGI Expert Panel consists exclusively of domestic experts, and this is very important to ensure that cultural sensitivities and local contexts are taken into account.

However, CTGI has shared its experience and findings with international organizations to avoid blind spots and better detect issues in government policy implementation and seek improvements.

A prime feature of 21st century public governance is improving civil society through joint efforts of the public and private sectors that make public governance more efficient and effective. In the past few decades, government services around the world have shifted from providing comprehensive services with public resources and institutions to new thinking that stresses holistic governance and public-private partnership. Therefore, in the short-term, CTGI hopes to establish this assessment framework, and systematically tracks public attitudes for timely policy amendments. In the long-term, CTGI hopes to monitor and improve government performance in Chinese Taipei, and in this endeavor the in-depth opinion research by the Expert Panel will prove valuable. CTGI has set up a new and practical public governance indicator system to reliably reflect performance measurement in public governance not only for Chinese Taipei but also for developed and developing countries in the Asia Pacific region. We ask for the cooperative efforts of each country, their APEC study centers, and relevant authorities in their government to improve the future of Asia.

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5. Contributing to Financial Market Stability in APEC Economies

INTRODUCTION

High financial instability tends to trigger financial crises that often culminate in economic crises. When a financial crisis occurs, an economy suffers not only great financial loss but also struggles to recover from the crisis. When the Asian Financial Crisis struck, several economies, including APEC members, began reforming their banking sectors and financial markets and deregulating their financial systems, opening services to foreign institutions and liberalizing capital accounts. When the recent global financial crisis struck and spread over the world, many APEC economies experienced a sudden reversal of capital flow that put substantial pressure on their currencies and stock markets. As capital flow was disrupted, cross border trade activity was also disrupted significantly. This experience was a stark reminder to most APEC economies of the vital importance of regional collaboration, particularly in strengthening financial markets, whose strength is a necessary condition of economic stability and resilience. In addition, it is also crucial for APEC economies to promote regional financial integration in order to reduce their vulnerability to financial contagion. Greater financial integration in APEC economies is more likely to help create more stable financial markets and rebalance the global economy, thus benefitting the region and the world.

This paper is a summary of an ongoing study.¹ Research for the study is expected to identify options and strategies for removing investment rules that hamper investors' participation in financial markets, strengthening regulatory frameworks, and implementing more effectively the enforcement processes necessary for better corporate governance and transparency in financial markets. To shed light on APEC financial markets in general, research focuses on four sample economies: the United States, Australia, Mexico, and Indonesia. These economies represent developing and developed economies in APEC. The United States was chosen because it has one of the most deregulated and liberalized financial markets in APEC. Australia was chosen because it has a resilient capital market and financial system. Mexico was chosen for its proximity to the United States and because it is a developing economy in

¹ The study is by Sri Adiningsih, Muyanja Ssenyonga, A.Ika Rahutami, Laksmi Yustika Devi, and Rosa Kristiadi of the Asia Pacific Study Center of Universitas Gadjah Mada, Yogyakarta, Indonesia.

America. Indonesia was chosen because the devastating Asian economic crisis of 1997—which crumpled Indonesia’s financial market and banking industry—has taught it some lessons. Indonesia is one of the economies in APEC that suffered least from the global crisis of 2008.

Data gathered from these economies were used as sample indicators in determining the extent of financial market stability and integration in the region. Primary data consisted of firsthand information on financial market stability, expert and practitioner opinion on the determinants, degree of financial market stability, and impact on economic activities in each economy, and best practices in financial markets.

Research was conducted over an eight-month period commencing in April 2010 and culminating in a workshop in Yogyakarta on May 22-23, 2011 to disseminate findings and draft recommendations for the Senior Finance Officials Meeting (SFOM).

Theories of Financial Market Stability

Financial markets are mechanisms that allow people to sell and buy financial securities and other fungible items of value for low transaction costs. These functions are to facilitate the raising of capital, transfer and sharing of risk, liquidity, efficiency by bridging surplus spending units (savers) to deficit spending units (individuals, companies, governments) who need more funds in excess of their incomes, thereby reducing transaction cost. Besides, the other functions are to collect information and analysis which market participants use in valuing financial instruments, price determination of financial instruments, and facilitate international trade (Besley and Brigham 2009).

Financial markets consist of stock markets and bond markets, which provide financing by issuing shares or common stock and bonds respectively, and enable the subsequent trading thereof; money markets, which provide short-term debt financing and investment; derivatives markets, which provide instruments for the management of financial risk; futures markets, which provide standardized forward contracts for trading products at some future date; insurance markets, which facilitate the redistribution of various risks; and foreign exchange markets, which facilitate the trading of foreign exchange.

Financial markets present a crucial task for economic well being. Therefore, financial markets stability is a necessity for macroeconomic stability and economic growth. Financial stability means that financial system has capability to allocate funds efficiently and absorb shocks as they arise, and securely settle payments and securities transactions (Weber 2008). Similarly, Schinasi (2004) defines financial stability as a financial system’s ability to facilitate and enhance economic performance, manage risks and absorb shocks.

Financial system instability can be triggered by turmoil and many other causes. In some cases, instability results from microeconomic and institutional failings (BIS and IMF 1997). High moral hazard as investors lacked incentives to act prudently in supervising managers, leading the latter to execute policies that are not commensurate with sound financial practices. Weak legal framework fostered supervisory forbearance, and ended up creating investor uncertainty.

In order to maintain financial stability, there are several key elements underpin a robust financial system which is characterized by an institutional setting and financial infrastructure

that complies with prudential principles of sound risk based capital. The key elements, among others include: sound, comprehensive regulatory and supervisory regime; sound, complementary fiscal, monetary, and prudential policies; sound risk management programs; openness, transparency and legal certainty; strengthening risk management programs.

Objectives

The research project aims at

- Explaining the current situation of macroeconomic and financial markets in the four APEC economies chosen.
- Determining the conditions that encourage financial market stability in the four economies.
- Determining factors that support market integration across APEC.
- Formulating policy recommendations to overcome obstacles to financial market stability and integration within the APEC region.

Significance and Policy Relevance of the Research

The research findings are going to have a strong relevance to promote market stability in the four APEC economies chosen and integration among APEC economies. The expectation of the research output is to acquire a better understanding of financial market stability and the need of financial integration.

Outputs of the Research

Based on the analyses, outputs of this project are

- Finding the degree of financial integration among APEC economies and factors which support the financial stability;
- Recommendation of best practices in maintaining financial market stability;
- A workshop to form recommendation draft to SFOM by discussing project results and accommodating inputs from all related stakeholders.

ECONOMIC AND FINANCIAL MARKET STABILITY IN APEC ECONOMIES

Economic Cooperation Among APEC Member Economies

Economic cooperation in APEC region is becoming more important. Even though economic crises come and go, the intensity of flows of goods, services, and capital in APEC region is increasing. These flows are predicted to increase considering that the global crisis has been overcome.

APEC member economies are very diverse in population size, levels of economic development, and GDP. The combined GDP of the APEC member economies was more than US\$ 30 trillion in 2010, approximately 56 percent of total world's income.

The combined merchandise exports of APEC members reached US\$7.06 trillion in 2008, which accounted for more than 43 percent of world exports. Generally, APEC members'

major industrial products and natural resources are also their main exports. Since APEC economies are three times more likely to export to other member economies and two times more when compared to trade with non-member economies, it is evident that exports of some APEC economies are also imports of other APEC members (APEC 2009).

In brief, APEC members trade more with each other than with other non-APEC trading partners. APEC members are three times more likely to export to another economy than to a non-member economy and two times more likely to import from another member economy than from a non-member (APEC 2009). The larger intra-regional share of export and import within APEC demonstrates the high level of dependency among APEC economies.

Financial Openness and Integration in APEC Economies

The development of financial market in APEC economies is diverse. The United States has a deep and broad financial market while Viet Nam and Brunei have narrow and shallow markets. The different levels of market development do not hinder financial market openness and integration in the area.

To determine the financial market openness in APEC economies, this research analyzed data on foreign direct investment (FDI) and external debt of the economies. The results show that Hong Kong, China and Singapore have the highest FDI index (FDI/GDP) among APEC economies. Their index exceeds 100 percent, reflecting their highly dependence on FDI in developing their economies. Among ASEAN, Indonesia has the lowest FDI index, which less than 15 percent, followed by Philippines. Besides, both economies are faring poorly in business competitiveness as shown by the low position of 155 and 156 respectively in the starting business ranking during 2010 among 183 economies surveyed (World Bank 2011). On average, ASEAN countries have debt index of 30 percent, excluding Brunei and Singapore.

Similarly, Japan has also the lowest FDI index, followed by PRC. Japan tends to invest abroad whereas PRC's growth is increasingly driven by the use of its own resources rather than FDI. However, Japan has a higher debt index than PRC's. Other East Asia economies, ROK and Chinese Taipei, have less than 15 percent FDI index and more than 20 percent debt index. The 2008 global financial, in general, have raised external debt of East Asia economies.

Furthermore, the level of openness can be shown by FDI and external debt indexes. Hong Kong, China and Singapore are the most open economies in APEC region as shown by their highest indexes. Conversely, Brunei has zero debt, illustrates that it is not an open financial market. In general, most APEC economies are shown to be open economies. Nonetheless, the results on the two indexes on their own, cannot lead to the conclusion that that developing economies are more open than developed ones.

Instead of being more open economies, the interdependence among APEC economies has also increased, reflecting from high growth in trade among them. However, regarding portfolio investment, APEC economies prefer to trade with non-APEC economies. According to the IMF's Coordinated Portfolio Investment Survey, the US dominates intra-APEC investments, as shown by its share accounted for 40.45 and 42.96 percent in 2001 and 2009, respectively. Next is Japan with its share of 34.18 and 26.27 percent in 2001 and 2009 respectively. In terms of share, APEC economies contributed 38 and 39 percent to the world's portfolio

investments assets in 2001 and 2009 respectively. In term of growth, extra APEC portfolio investment assets were higher than the intra ones, recorded for US\$ 6,889 billion and US\$ 4,408 in 2009 respectively. Securities issued by the US were the largest source and destination for securities investment in the APEC region. Securities issued in Japan and Canada was in the second position and third position, respectively. It should also be noted that intra APEC portfolio investment liabilities experienced higher growth than those issued by non APEC economies, meaning that APEC financial market has become increasingly interconnected.

Since APEC region has more integrated, the financial market integration in the study is proxied by using stock market composite index (SMCI). The results show that a dominant economy's SMCI influence SMCI of one economy. APEC financial markets stability is highly depended on the stability of dominant economies' financial markets, such as the US and Japan. Hence, each of APEC member's financial market stability needs to be preserved in order to maintain the region stability. The study analyzed four chosen APEC economies in term of their macroeconomic and financial market condition, their financial market dependency to other markets in the region, and their efforts in maintaining financial market stability. A regression of SMCI for those economies is also employed to deliver a comprehensive study on the economies' The results show that each economy' SMCI is also significantly influenced by other economy's SMCI which are Japanese SMCI and the US SMCI.

ANALYSIS OF FOUR APEC ECONOMIES

In this section we describe the financial stability of our four selected APEC economies: Indonesia, Mexico, the United States, and Australia.

Indonesia's Financial Stability

The Indonesian government has adopted several measures to offset the impact of the global financial crisis:

- Monetary Policy
 - Bank Indonesia (BI) progressively increased its benchmark rates beginning in May 2008 until it reached 9.5 percent in November 2008. Afterward, the BI rate was lowered gradually from 8.75 percent at the beginning of semester I 2009 to 7 percent at the end of semester II 2009. Since August 2009, BI has maintained the interest at 6.5 percent.
 - BI has conducted policy to intervene foreign exchange markets as it is authorized to maintain exchange rate stability.
- Liquidity Support:
 - In order to provide more liquidity to the banking sector, BI agreed to reduce the minimum limit of bank reserve requirement at the central bank from 9.08 percent to 7.5 percent on October 14, 2008.
 - BI requires state-owned enterprises to place their funds in domestic banks to increase liquidity in the banking system.
 - BI has free banks of mark to market obligations on their bond holding.

- Deposit Guarantees: Increased the amount of deposits guaranteed from Rp 100 million to RP 2 billion.
- Fiscal Stimulus: in coping with the global financial crisis, the government provided total stimulus packages for about IDR 71.3 trillion in 2009.
- Structural Policy to support real sector: the government has developed financing facilities such as infrastructure guarantee fund and infrastructure fund.
- Financial Regulation:
 - In 2008, BAPEPAM-LK issued a new regulation regarding share buyback during the crisis. The regulation was expected to minimize composite stock price index downturn at stock exchange as the impact of the global financial crisis that influenced capital markets worldwide.
 - In December 2008, Ministry of Finance (MoF) issued a regulation (Nr 238/2008) making listed companies eligible for a 5 percent cut income tax to help them reduce their costs (certain conditions applied e.g. at least 4 percent of their shares are owned by the public).
 - BAPEPAM-LK has issued relevant regulations regarding securities credit rating in June 2009 in order to improve management and monitoring activities toward credit rating companies.

Generally, Indonesia showed better preparedness in responding to another global financial crisis than it did in the Asian financial crisis in 1997/1998. At the time, Indonesia had a macro prudential supervision that was handled by Financial Stability System Bureau (FSSB) in BI. FSSB has developed early warning system (EWS), known as financial stability index to detect vulnerability in banking sectors. Thus, when a global financial crisis spread worldwide, the Indonesian government will be able to respond quickly as the financial stability index per-November 2008 recorded at 2.43, which was above the indicative maximum of 2.0 (Bank Indonesia, 2009). Besides, MoF has also developed EWS that monitors several key performance indicators, such as Indonesia Composite Index, the IDR exchange rate, GDP economic growth, net selling of shares and bonds within the Indonesia Stock Exchange, and exports and imports values.

Regarding to foster financial stability, the financial authorities (MoF, BI, and IDIC) signed a coordination agreement and agree to share information on financial sector conditions that can cause instability. They also agreed to establish a crisis management protocol. Therefore, the drafting law on financial safety net is necessary to be accelerated. Besides, in order to reform the financial sector, Indonesia has planned to set up financial service authority (OJK).

Additionally, in the efforts to strengthen its financial stability, Indonesia has joined various international organizations such as the BIS, G20, EMEAP, WFE, AOSEF, and IOSCO. The purpose is to respond to the various international issues in monetary and banking sectors and to promote the strengthening international financial system.

Mexico's Financial Stability

The global financial crisis has also affected Mexican economy. In 2008, the economy slowed down in response to the gradual deterioration of external demand (Banco de Mexico 2008). This condition affected the levels of activity in tradable goods sectors and labor market indicators. Inflation also increased during the first half of 2008 that was caused by an increase

in production cost structures. An increase in the international prices of commodities also affected the supply structures in Mexico. Pressures of demand were identified during 2008.

In dealing with the crisis, the Mexican government has implemented several policies, namely (Banco de Mexico 2008; Moreno-Brid 2009):

Fiscal Policies

Mexican government applied sound budgetary discipline, raising tax rates, also increased public spending on infrastructure. In 2008, Government established the National Infrastructure Fund, Standing out Program to Promote Growth and Employment (PICE). In 2009, the government has implemented economic stimulus program and established Protecting families' economy and employment through National Agreement.

Monetary Policy and Other Measures

Since January 21, 2008, Banco de Mexico has adopted an operating interest rate target (overnight interbank rate); whereas it adopted an explicit inflation targeting regime beforehand. Other measures implemented are

- Supplying US dollar liquidity to the foreign exchange market through the Foreign Exchange market
- Providing liquidity in domestic currency for commercial banks
- Modifying the programs for government securities issuing in favor of short-term financial instruments
- Implementing a program to repurchase IPAB bonds.

Banking and Stock Market Policies

Regarding banking policies, Mexico has an early warning system that serves as a trigger for banks to add more capital or otherwise come under more regulation (under 10 percent CAR). Besides, banks are given incentives to increase their equity capital through a number of ways, which reduced the potential for firm stress. Additionally, foreign banks in Mexico are allowed to operate as subsidiaries and not as bank branches which reduce the impact of parent company policy on their performance and enhance the authority of Mexican regulators and supervisors over their activities.

In stock market, government implements good information disclosure. Financial information disclosure is strong and measures are underway to encourage delisted banks to list their stocks on the highly liquid Mexican stock exchange so that they can increase their information disclosure.

With regard to the degree of financial stability in Mexico, a lot of confidence was shown in the fact that although Mexico experienced a contraction close to seven percent of GDP in 2009, Mexico did not experience a financial crisis. The decline in GDP was caused by a reduction in exports to US, a major trading partner. However, the drop in GDP did not go as far sparking off a financial crisis. Financial system in Mexico has been stable and was not significantly affected by the 2008 international financial crisis.

Mexican financial system is still mainly bank-based but has over time diversified and now other financial institutions are making significant contributions to financial intermediation.

United States' Financial Stability

Financial Reforms

The causes of the 2008 financial crisis in the United States have been linked to various factors, such as the US\$8 trillion highly leveraged shadow banking system made possible by too much deregulation (Geithner 2010). Equally important were weak capital requirements made possible by a light regulatory regime compounded by weak capital requirements for financial institutions outside commercial banks.

Measures suggested to prevent recurrence of the 2008 financial crisis (Financial reform blueprint Treasury department and later adopted in the Dodd-Frank Act, 2010).

- Short term goals include improving regulatory coordination and oversight achieved by establishing a new federal commission for mortgage origination.
- Intermediate term goals encompass reducing duplication in U.S. financial regulatory structure, and modernization of the existing regulatory system.
- Long term recommendations entail development of a long term objectives-based regulatory model that will comprise a market stability regulator, a prudential regulator, and a business conduct regulator that would focus on consumer protection.

Highlights include:

- Ensure uniform supervision of all providers thereby reducing regulation costs and efforts (Pellerin et al. 2009).
- Robust, comprehensive supervision of financial firms that pose a risk to financial system under clear regulatory accountability.
- Better disclosure and transparency. This is proposed to be achieved through improvements in accounting standards, by among others forging international accounting convergence
- Taking regulatory action to deal with uncertainty in the repo market and money fund industries.
- Increase transparency and oversight to OTC derivatives markets through bringing them to central clearing arrangements, ensuring full transparency; reduce degree of financial contagion arising from perceived counterparty exposure.
- Standards to be put in place on disclosure and accountability for executive compensation, compensation committees to be equipped with tools and independence to bargain harder on executive pay.
- Resolution regime that winds down failing financial institutions (establishing a bankruptcy-like regime for large financial institutions to manage themselves into failure.

However, compromises resulted into the Dodd-Frank Act, 2010, which among other things is expected to strengthen if all the components of the Act are implemented. The Act deals with the main source of financial instability that culminated into 2008 financial crisis such as envisages a regime of high capital requirements for banks and financial institutions, strengthening of regulations, supervision and oversight over all financial institutions, and financial transactions including derivatives which prior to the crisis used to be undertaken under OTC framework, strengthening supervision and oversight over large financial

institutions that have systemic importance hence have high likelihood of sparking off systemic risk in case they face liquidity and insolvency problems.

Other important components of the Dodd-Frank Act 2010 lauded for strengthening long term financial stability include efforts to deal with too big to fail financial institutions by requiring them to have higher capital requirements, calls for the formation of council of federal regulators to be responsible for monitoring for signs of financial instability in the financial system under the financial stability oversight council. Banks are obliged to spin off proprietary trading units thereby reducing the potential danger that risk that emanates from such activities can impact on overall risk of the banks. This is an attempt to reduce counterparty risk, which was an important factor that caused underestimation of risk banks and financial institutions faced due to undisclosed contingent assets and liabilities entered into through proprietary trading activities.

The Act also calls for higher capital requirements for any financial institution that takes excessive risk investments, envisages the establishment of the systemic oversight body, which will coordinate and monitor the economy for signs of vulnerability, and the proposed formation of the consumer protection bureau, which will ensure that consumers of all financial services and products are protected from fraud and other malpractices perpetrated by practitioners in the financial services sector. The establishment of the consumer protection bureau within the federal reserve system, which is to be charged with the task of protection consumers of financial products from fraud, equips the government with the legal framework under which orderly liquidation troubled financial institutions is made.

The Dodd-Frank Act is a comprehensive act that takes into account key G20 guidelines as well as is a bold attempt to deal with the root causes of the bubble in sub sector of the U.S. housing market that eventually bust sparking off the worst recession U.S. had faced since the great depression. Nonetheless, unless the balance of power in the congress remains as it is for some time to come, considering the long term period in which the key components of the package will be implemented, there is likelihood that some of the fundamental measures will face watering down or outright repeal thereby reducing its impact on overall long term financial stability in future.

Australia's Financial Stability

In general, the global financial crisis did not cause a major shock in Australia's economy, only gave a little shake to its financial market. There was no financial institutions' bail out as performed by many other countries. However, several fund managers failed during the crisis. Australia could go through the crisis smoothly because of its solid fundamental financial market supported by good coordination among regulators. Additionally, Australia has had conservative financial market with small derivative market. The domination of domestic investors (60 percent of total investors) has also supported Australia's financial stability. The Australian Stock Exchange (ASX) relies on its domestic investors, particularly from superannuation.

Australia's major reformation on financial market started in which the major regulators divided into two, namely APRA and ASIC. Afterwards, the financial system and those regulators considered well performed in maintaining Australia's financial stability.

Australia does not have any macro prudential regulation as it is considered not necessary. However, there is so called the Council of Financial Regulators whose mandate is to contribute to the efficiency and effectiveness of the regulation and the stability of the financial system. Additionally, other efforts performed by the regulators to deal with financial crisis are:

- APRA, ASIC, and RBA have their own financial stability reports.
- APRA conducts a kind of stress testing. It also has a risk assessment, which implicitly has been used to categorize banks' condition (systemic or not).
- External auditors in institutions under ASIC supervision are obliged to be carried out once a year.

In dealing with the global financial crisis, the Australian government has taken several policies, namely (IMF, 2009 and results of Australia visit):

- Monetary Policy
 - The Reserve Bank of Australia (RBA) has cut cash rate target by cumulative 425 basis points to 3 percent since September 2008.
- Liquidity Support
 - The list of securities used as collateral in repo operations was extended. Furthermore, the RBA extended the maturity of repos to one year.
 - An amount of US\$30 billion swap line with the US Federal Reserve Bank was established in September 2008, initially through January 2009 and later extended to October 2009.
 - An amount of up to AUD \$8 billion of residential mortgage-backed securities would be purchased by the government.
- Funding Guarantees
- Total deposit balances up to AUD \$1 million per customer held in eligible authorized deposit taking institution. Deposits over AUD \$1 million can also be guaranteed for the same fees as applied for wholesale funding. The scheme was put into action in October 2008.
- Eligible authorized deposit taking institutions can secure guarantees for their existing or a new wholesale funding for a fee ranging from 70 to 150 basis points depending on the credit rating of the institution.
- Financial Regulation/ Supervision
 - The authorities enhanced supervision of credit rating agencies and research houses.
 - Short selling of financial and nonfinancial stock is banned.
 - The RBA is working with industry representatives to improve disclosure of securities lending activity.
- Fiscal Stimulus Package
 - Economic Security Strategy amounted AUD \$10.4 billion was announced on October 14, 2008 to strengthen the national economy and support Australian households.

- On December 2008, the government introduced Nation Building Program. The AUD \$4.7 billion program aimed at improving the performance of land transport infrastructure.
- On February 2009, the government introduced \$42 billion Nation Building and Jobs Plan to support jobs and to invest in future long-term economic growth. Moreover, the government also introduced a stimulus package for young Australians amounted AUD \$1.5 billion in the form of skills jobs package.
- The government announced a fiscal stimulus package by giving up to AUD \$900 bonus payment for tax payer on 6 April 2009.
- The government invested AUD \$22 billion in the nation's infrastructure on May 2009.

According to regulators and financial market participants, sources of Australia's financial market instability are

- High housing prices forcing banks to lend less for housing,
- Banks' fund sources being dominated by offshore borrowing, and
- An exchange rate strongly influenced by commodity prices.

The key factors to avoid the instability are:

- Transparency, means that the regulators have to deliver clear messages to the market
- Application of international accounting standard
- Investing education for investors as part of consumer protection.

As a part of global financial markets, Australia has contributed to the efforts to greater financial stability by joining numbers of international fora which are formed to promote the strengthening of the international financial system.

RESEARCH FINDINGS

Financial markets in the Asia-Pacific region have registered rapid development and become increasingly integrated in recent decades. Despite the high variation among APEC economies, in general, higher level of economic development and better public welfare have induced broader and deeper financial markets in the region. The US has the most advanced, broadest, and deepest financial market; whereas Indonesia and Mexico are still simple. Nonetheless, the rapid development of financial markets in the APEC region in recent decades has increased sources of volatility. There is no better indicator of that than a series of financial crisis and banking crises, which have affected APEC economies in the past two decades. The Asian economic crisis of 1997-1998, the Tequila crisis in Mexico in early 1990s, and the Sub Prime Mortgage crisis in the U.S. in 2008 which led to the global financial crisis are some examples of increasing level of financial markets volatility in the region. Hence, maintaining financial stability in the APEC region has become a crucial issue. This study constitutes an effort to contribute to financial market stability in the APEC region, using the United States, Australia, Indonesia, and Mexico as case studies.

Differences in the characteristics of financial markets in the four sample economies, explain varying impact of the recent global financial crisis across economies. Similarly, policies implemented to deal with the crisis also varied as the sources of financial market vulnerability differ in each economy. Additionally, factors supporting financial market stability also varied.

To that end, policies necessary to ensure financial market stability also varied across the economies.

Impact of the Global Financial Crisis

The impact global financial crisis on APEC economies varied, depending on level of openness and degree of financial market development. The US, as the centre of the global crisis, was hit hard and its economic growth reached bottom in 2009. At that time, financial institutions with huge investments in securities suffered huge losses, which led to write downs and write offs of their assets. Many banks and other financial institutions used much of their capital to make the massive write-offs, which undermined their liquidity and solvency, and led to the closure of many banks (147). The government's injection of capital into troubled financial institutions and nonfinancial institutions worsened the budget deficit (estimated to have reached US\$1.3 trillion in 2010). The weaker economy put pressure on the dollar (depreciation vis a vis other hard currencies) and caused a noticeable reduction in portfolio and FDI (at least during the peak of the crisis).

On the other hand, Australia was better prepared to deal with the crisis as a result of financial market reform in 1990s and supported by its strong domestic investor institutions. Hence, when the 2008 global financial crisis occur, Australia was not hit hard. Even so, Australia still experienced economic slowdown, depreciation in Australian dollar, increased unemployment, exports and imports declined but not as severe as other advanced economies. Besides, government bond yields, bank asset quality, equity prices and general insurer's profit also dropped. Additionally, the spreads and volatility in Australian financial market increased, and several fund managers in Australia failed.

Meanwhile, Indonesia and Mexico have similar characteristics. They had faced financial crisis in the 1990s, which obliged them to restructure their financial markets, including the banking industry. Their financial markets are dominated by the banking sector, implying that restructuring of the banking industry laid a strong foundation for financial markets stability. Hence, though the global financial crisis affected capital markets of both economies, the banking industry has remained robust and resilient. Similar to other economies, Indonesia economic dropped slightly during the global financial crisis but still posted positive economic growth, recorded at 4.5% in 2009. Besides, foreign ownership of SBIs, stock exchange index, export and import also declined. Conversely, Mexican economy suffered from the global financial crisis largely because of its high economic dependence on the US. During the crisis, Mexican economic growth, exports and imports dropped significantly. However, Mexico was able to rise quickly and posted economic growth rate of 7.6 percent in the second quarter of 2010 and relatively low unemployment rate of just 5.7 percent in July 2010.

The impact of the global financial crisis varied among APEC economies, there is little doubt that it impacted, albeit to varying degree, the four economies which were used as sample in this research. In general, some common features of the impact of the global financial crisis on the four sample economies were identified. These include among others

- Slower economic growth that reached its bottom in 2009
- An upsurge in unemployment , which meant an increase in dependency, lower taxation revenues (except for Indonesia)
- Depreciation in of the local currency

- A decrease in capital market composite index
- Decline in exports and imports
- An increase in interest spread and volatility in the financial market
- Bank asset quality declined.

Policies Implemented to Deal with the Global Financial Crisis

All economies implemented policies to overcome the global financial crisis. Those policies reflected the severity of impact of the crisis on the economy overall, its financial markets, and the condition of its financial market. In general, however, the four economies studied implemented policies for

- Fiscal stimulus programs
- Monetary easing
- Increasing or introducing the deposit insurance guarantee (except for Mexico)
- Strengthening financial markets
- Providing liquidity support for troubled financial institutions.

The U.S. has launched many policies to stabilize its financial markets and restore its economy. The economic stimulus program entailed the injection of capital into key troubled financial and nonfinancial institutions. The Federal Reserve launched expansionary monetary policies by reducing interest rates. Congress has also enacted Dodd-Frank Act in 2010 which is aimed at reforming and overhauling the financial market by strengthening supervisions of banks and nonbank financial institutions, establishing financial stability council, consumer protection agency, and widen the coverage of supervision and regulation to all players in money and capital markets. The fact reveals that an economy as big and as strong as the U.S. was eventually forced to reform its financial markets.

Similarly, Australia also reduced the cash target rate, and gave liquidity support and funding guarantees to the banking sector. At the same time the monetary authority also enhanced supervision of credit rating agencies and research house, banned short selling in financial and non-financial institutions, improved disclosure of securities lending activities, conducted stress testing, and performed fiscal stimulus package.

Likewise, Indonesia through its central bank reduced its interest rate and provided liquidity support by decreasing the reserve requirement ratio, obliged State Owned Enterprises to deposit their funds in domestic banks, and freed the banks from the requirement to mark to market obligations on their bond holdings. The Indonesia government also implemented a fiscal stimulus policy and increased the amount of the deposit insurance up to Rp2 billion. In the capital markets, the authority simplified the share buyback during the crisis, implemented the regulation that reduced income tax by 5 percent for listed companies, and improved good corporate governance.

Equally, Mexico also implemented several policies that were aimed to strengthen financial market stability. The government has developed EWS, giving incentives to banks to increase their capital equity, and giving liquidity support in domestic currency to commercial banks. Besides, the government implemented a regulation that aimed at increasing good information disclosure in Mexican stock market. The government also launched fiscal stimulus through many policies such as tax incentives, temporary pensions for the unemployed and increasing public spending on infrastructure.

Sources of Financial Market Vulnerability

Although all economies have implemented policies to overcome the global financial crisis, each still faces risks. The source of financial market vulnerability differs among the four chosen APEC economies. The sources of financial market vulnerabilities in the US are indebted household sector that needs more deleveraging, large budget deficit and high government debt, and large current account deficit, which is continues to elude solution. Similarly, Australian financial markets face serious potential financial market volatility unless sources of vulnerability are addressed, such as source of funds for banks that is highly dominated by offshore funds, high household debt, and high housing prices.

Meanwhile, Indonesia and Mexico face even greater sources of vulnerability. Indonesia, which has become a destination for large short-term capital inflows, faces financial market vulnerability because such inflows could destabilize the financial market if huge capital outflow occurs. In addition, that the financial market is narrow and shallow makes it even more susceptible to shocks. The same applies for Mexico's financial market, which still faces some vulnerability. Sources of Mexico's financial vulnerability, among other things, are attributable to high concentration of share issuers (only three listed companies contribute to 30 percent of market capitalization), counterparty risks, and hidden derivative transactions in financial institutions.

Factors Supporting Financial Market Stability

In general, US financial markets have suffered the most from the global crisis. Conversely, Australia, Indonesia, and Mexico were not as affected and their financial markets remained relatively stable for several reasons:

- Successful financial reforms that had set a strong foundation for a resilient financial market that withstood shocks.
- Good coordination among regulators.
- Simple and conservative financial markets.
- High commodity prices.

A major reform on financial market in the 1990s, good coordination among regulators and the dominance of domestic investors in Australia's financial market (accounted for 60 percent of total investors) are major factors supporting market stability.

Similar to Australia, Mexico also supported by several factors in maintaining its financial market stability, namely reforming its financial markets in the wake of the financial crisis in 1990s, the low leverage ratio of Mexican firms, low national debt and deficit (low sovereign risk), and long term nature of the largest percentage of Mexican national debt. Besides, regulatory framework in financial market is on good terms with other regulators such as Central bank, Ministry of Finance, CNBV. The existence of consumer protection agency also induces confidence in investment in securities. Additionally, banks in Mexico have strong capital foundation. Meanwhile, factors supporting Indonesia financial markets stability are the simple financial markets, good coordination among national authorities, and financial market reform as a result of Asian financial crisis 1997/1998. In addition, Indonesia's financial market is still dominated by healthy and strong banking sector.

Moreover, the quick recovery of the US financial markets from the crisis was largely due to the percentage of its huge international reserves, for example, keeping the US an important

destination for both portfolio and FDI. Besides, advanced financial markets were able to deal with fluctuation of capital flows, while the large competitive, innovative, liberalized and diversified economy and US dollar as an international reserve currency also contributed significantly.

Policies That Should be Implemented to Ensure Financial Market Stability

In general, financial stability requires strong regulatory authorities and regulations in financial markets that follow developments in those markets. Nonetheless, each economy is unique, which means that policies to ensure financial stability may vary and differ from one to the other.

Australia was able to maintain its financial markets stability during the global financial crisis. However, the economy should implement policies to reduce potential sources of vulnerability in its financial markets, such as introducing an unweighted leverage ratio as a supplement to the Basel II risk-based framework to ensure financial stability. The same applies to APRA, which will implement prudential standards and a prudential practice guide on sound compensation practices to strengthen the links between compensation and risk management in the prudentially regulated sector and will update the capital standards for general insurers and life insurers.

Meanwhile, the US, which suffered a severe impact from the financial crisis, enacted the Dodd-Frank Act, 2010. The Act will strengthen supervision of banks and nonbank financial institutions, establish a financial stability council (this has been established), and establish a central clearance agency for OTC financial instruments. The Act also envisages intensified supervision and regulation of all players in money and capital markets, and the establishment of a consumer protection agency. In addition, it calls for higher capital requirements for banks and other financial institutions that have systemic influence on the financial sector and economy, requires financial institutions to spin off proprietary trading activities to reduce potential sources of counterparty risk. The Act also calls for closer coordination with G20 members to ensure fair and equitable all inclusive balanced growth, financial sector regulation and supervision, and prevention of financial fraud and money laundering practices, increased regularity of financial sector assessment programs tailored towards identifying potential sources of financial instability for quicker and timely handling.

Moreover, Mexico has also had strong regulatory and supervisory framework that ensured its financial stability. Such regulations include regulation of foreign banks in Mexico which obliges them to incorporate in Mexico rather than serve as mere subsidiaries or branches. Such a policy enhances the control supervisory and regulatory authorities in Mexico have over their activities. This also reduced potential repercussions from problems that emanate from mother financial institutions to impact their own subsidiaries in Mexico. There is need for Mexico to put in place prudent regulations on lending practices especially to affiliates, as well as regulations on foreign currency operations net exposures to reduce vulnerability. The importance of banks in Mexico means that strong provisioning in banking industry is needed, which should contribute significantly toward strengthening the financial market.

Similar to the other economies, Indonesia also needs to strengthen its financial market. Hence, the draft laws on the financial safety net and the establishment of financial authority need to be accelerated urgently as it will strengthen the resilience of Indonesian economy to

withstand shocks in the financial markets. Additionally, there is need for enhancing safety and protection of investors as it will encourage them to participate actively in the capital market and foster the emergence of a strong domestic investor, which lead to strengthen financial markets stability.

POLICY IMPLICATIONS

The research findings indicate that maintaining the financial markets stability in an increasingly complex and integrated APEC region is becoming more difficult but more important. Some important findings of this study are as follows:

- Financial market reforms that can develop healthy, strong, and efficient financial markets can be fortifications against shocks. The reforms are not only required by small or developing economies, but also by advanced or developed economies.
- It is evident from some APEC economies' experiences that it is getting more difficult for financial market regulators to follow the development of new instruments and new institutions of the market as the market is becoming more complex. Therefore, there is need for better management of the development of the market to ensure that regulators have the necessary capacity to supervise them.
- Regulatory framework needs to follow market developments. Even if necessary, it should be anticipated for market developments so that financial institutions or financial instruments developed in the market can be regulated and supervised properly. Especially in developed economies where financial engineering plays important role in the development of new instrument or new financial institution, the financial market regulators do not only need to keep following the development, but also directing it. In this way, all the instruments and financial institutions can be well managed despite their rapid development. For the developing economies, it should be easier to design and develop a financial market regulatory framework because instruments and financial institutions developed in the market are generally still simple and they follow market developments in developed economies.
- Short-term capital flows should be supervised properly to minimize the volatility of financial markets. This recommendation should be implemented particularly in a small opened economy that only has small foreign exchange reserves compared with its short term capital inflows.
- Financial markets volatility can be reduced by enhancing investor protection or deposit insurance.
- An institution that acts as a macro prudential supervision is necessary in the market. This is required in both developed and developing economies.
- Applying international standards for best practices will help strengthen the financial market of an economy, for example follows the Basel Principle for central banks and follows the IOSCO principle for capital market regulatory body. This is appropriate either for developed or developing economies.
- An agreement or cooperation in maintaining financial market stability across economies is needed to minimize the volatility of the region's financial markets, particularly in the framework of Financial Stability Board formed by G-20. This is particularly important because generally the financial market in APEC region is integrated.

- An early warning system in the region in each economy's financial market is important in maintaining financial market stability. This is appropriate either for developed or developing economies.
- Prudent fiscal policies and strong international reserve can reduce the potential of financial market volatility. This is appropriate for both developed and developing economies.
- Financial markets are becoming more integrated and financial stability is becoming more important in APEC, so APEC needs to talk more about financial market stability.

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6. Russia and the Emerging Institutional Order in the Asia-Pacific

NORTHEAST ASIA AT THE CENTER?

The Asia-Pacific has always been an imagined region in many ways. It is essentially an ideational construct engineered by the epistemic community of business people, scholars, and politicians who have been promoting the Asia-Pacific identity from the 1960s onwards. This is not to deny its realness, though. The Asia-Pacific region does exist, defined not only by verbal discourses, but also by very material economic, social and political links connecting the countries of the Pacific basin, although the density of those links is distributed very unevenly across the region.

The vast and amorphous Asia-Pacific is superimposed onto other entities that can be regarded as either its “subregions” or regions in their own right. Those areas are more compact, easily definable, and arguably more “real” than the Asia-Pacific, since they have stronger geographical and historical roots. For all the advances of globalization, which shrinks distances and facilitates communication, territoriality remains a crucial factor in international politics (Buzan and Wæver 2003). It is also true in the case of “the Pacific hemisphere,” of which East Asia claims to be the central constituent part. Yet East Asia, although it is much less hazy and much more territorial than the Asia-Pacific concept, is no monolith and has its own subdivisions.

The most salient division is that between Northeast Asia and Southeast Asia. Which of the two takes the pride of place? Official Asia-Pacific/East Asian discourses refer to Southeast Asia, collectively represented by ASEAN, as “the fulcrum” and “the driving force” of region-wide multilateral cooperation and integration (Clinton 2010a; ASEAN Regional Forum 2011; ASEAN Plus Three Summit 2009). In a similar vein, many academics highlight the prominence of ASEAN, resulting, in their view, from the Association’s capacity to be a collective leader and institute norms governing region-wide politics (Bogaturov 1997; Acharya 2003).

Unlike Southeast Asia, whose geographical area almost perfectly corresponds to the 10-country ASEAN membership, the concept of Northeast Asia is less clearly defined. It is unanimously recognized that Northeast Asia includes China (the mainland and Chinese Taipei), Japan, and Korea (both the South and the North). Beyond that it becomes less uncontroversial. What about Russia and the United States? Can they be regarded as Northeast

Asian actors?¹ I believe that they can, although their status in Northeast Asia should be designated as *peripheral* as opposed to the *central* position of China, Japan and Korea, the three nations forming the core of the region in terms of geography, as well as by virtue of their longstanding historical and cultural affinity.²

Russia is, of course, territorially present in Northeast Asia and has been a major player in the region's international system ever since the late 19th century. The case of the United States is less obvious. It does not have direct geographic presence in Northeast Asia, but is extremely close to the region, thanks to territories such as Alaska, Aleutian Islands, and Guam. This, among other things, considerably raises U.S. exposure to threats and challenges originating in Northeast Asia.³ Therefore, U.S. behavior in Northeast Asia is driven not only by the logic of a global superpower, but also by its concerns as a local "resident power."

Having thus delineated the membership of Northeast Asia, what is its standing in the wider regional picture, especially vis-à-vis Southeast Asia? As noted earlier, official international discourse gives clear priority to ASEAN as "the driver" of regional processes. However, this may result not so much from ASEAN's inherent strengths as from the big powers' unwillingness to change the status-quo under which Southeast Asian countries lead only for as long as major Northeast Asian powers let them do so. This is why Southeast Asia's current centrality in the Asia-Pacific is, in a sense, a leadership "by default." Its heretofore substantial role is even described as increasingly a thing of the past, "an embedded Cold War artifact" (Calder 2010, p. 5). For all the ASEAN's diplomatic skills and achievements, it lacks material power to be the real center of gravity as opposed to Northeast Asia. The latter (even excluding Russia and the United States) generates over 80 percent of East Asia's GDP. It is significant that the Northeast Asian trio supplies the lion's share of the foreign exchange reserve pool under the ASEAN Plus Three's Chiang Mai Initiative Multilateralization scheme—of 120 billion US dollars China, Japan and Korea are collectively contributing 96 billion, while ASEAN's share is only 24 billion.

Northeast Asia's military potential dwarfs Southeast Asia capabilities. Suffice it to say that four out seven Northeast Asia players (the United States, Russia, China, North Korea) have nuclear weapons, while the other three (Japan, Korea, Chinese Taipei) are all able to go nuclear very promptly if they make a political decision. Their formidable military capabilities, along with smoldering conflicts such as the Chinese Taipei and Korea issues, make Northeast Asia one of the most explosive regions in the global international system. If a war breaks out there, it will shake the entire world. It is telling that when the Thai-Cambodian border dispute

¹ Apart from Russia and the United States, there is, of course, Mongolia which may or may not be seen as a Northeast Asia country. My view is that Mongolia does belong to the region in question, but is still too weak politically and economically to be a significant factor. That is why Mongolia is omitted here from further analysis.

² Russia's and the U.S.'s peripheral position in Northeast Asia also results from the two nations' transcontinental nature. Unlike most countries, they are directly "resident" not in one, but two or more regions. Northeast Asia is just one of the regions where Russia and the United States have vital interests.

³ For instance, it is believed that Guam is already within range of North Korean missiles ["North Korea is fully fledged nuclear power, experts agree", 2009]. During the Second World War, the Japanese briefly occupied part of the Aleutian Islands, underlining the U.S. vulnerability to neighboring Northeast Asian powers.

erupted in 2010 that was just one of many international headlines⁴. By contrast, when Republic of Korea and North Korea went at loggerheads in the same year, it sent shock waves across the globe. There is little doubt that strategic stability in East Asia and the broader Asia-Pacific region is mainly a function of the relationships among the Northeast Asian powers.⁵

It is economic, political, and strategic weight of Northeast Asia, along with its conflict-generating potential, that makes it the real center of gravity in the Asia-Pacific, and indeed places it among the most crucial world's regions, on a par with Europe and the Middle East. Developments in Northeast Asia will increasingly shape international order in the Asia-Pacific and beyond.

EMERGING INSTITUTIONAL ARCHITECTURE IN NORTHEAST ASIA AND BEYOND: A GAME ON TWO CHESSBOARDS

Despite an array of powerful factors fuelling rivalry and conflict in Northeast Asia, the region has been witnessing developments that could lead it to much more cohesion. One obvious trend is the emergence of multilateral institutional architecture.⁶ Until recently, Northeast Asia lacked multilateral arrangements of its own. The U.S.-dominated San Francisco system of “hub and spokes” had long acted as some sort of institutional surrogate, but it is now being gradually dismantled (Aggarwal, Min Gyo Koo 2008).

Although Northeast Asia is still lagging behind many other regions in building multilateral institutions, noticeable progress has been made in the recent years. There is a trend towards a two-tiered structure of multilateralism in the region. The first level is represented by the Six-Party talks on the North Korean nuclear issue, which were initiated in 2003, involving China, North Korea and Republic of Korea, Russia, Japan, and the United States. The nuclear problem has not yet been resolved, but the Six-Party process may lead to a Northeast Asian regional organization to manage political and strategic security (Aggarwal, Min Gyo Koo 2008, p.8). In February 2007, the participants of the Six-Party talks agreed to set up five working groups, one of which was tasked to study ways to achieve “Northeast Asia peace and security mechanism.” Despite periodic walkouts by North Korea, the Six-Party talks have already become a de facto permanent consultative mechanism in Northeast Asia, albeit with a mandate still confined to issues related to the Korean Peninsula.

The second layer of Northeast Asian multilateralism is embodied in the trilateral cooperation of the “core” regional states – Japan, China, and the Republic of Korea. Their informal trilateral summits have been regularly held since 1999, but until recently they took place on the sidelines of ASEAN plus Three meetings. December 2008 saw a watershed event, when the first Northeast Asian summit was held on its own, attended by Japan's prime minister, China's chairman and the Republic of Korea's president. The leaders signed an action plan

⁴ This is another indication that ASEAN has a long way to go to reach solidarity and security community, without which it can hardly claim to be “in the driver's seat” of the Asia-Pacific multilateralism.

⁵ Some authors go even as far as to suggest that as few as three major powers of Northeast Asia – China, Japan, and the United States –determine the strategic landscape in the broader Asia-Pacific [International relations theory and the Asia-Pacific, 2003].

⁶ Here I use the term “multilateral” as designating a kind of inter-state cooperation involving more than two sides.

for promoting trilateral cooperation and agreed to hold such meetings annually. So far, four summits of the trio have taken place.

At their third meeting in May 2010, the three leaders adopted a blueprint for future economic cooperation, environmental protection, and expansion of personnel and cultural exchanges. They also agreed to establish a permanent secretariat in Republic of Korea starting from 2011 (Japan-China-ROK Trilateral Summit 2010). The sides are negotiating a trilateral investment agreement and studying a trilateral FTA. It is expected that the study will be concluded within 2011 and formal negotiations will begin in 2012 (Japan-China-Republic of Korea Summit Declaration 2011; “Wen presents proposal for economic cooperation with Japan, S. Korea” 2011).

More than 50 trilateral consultative mechanisms, including 17 ministerial meetings, are now in full operation and over 100 trilateral cooperation projects in the economic and social fields, people-to-people exchanges, green growth, and disaster management are promoted (“China, Japan, S. Korea agree to further strengthen trilateral cooperation”, 2010). Apart from official meetings, nongovernmental forums are also held among the three countries, with participation by academia, business, NGOs, and mass-media.

To be sure, institutionalization of this trilateral interaction is still in its nascent stages. It is too early to speak of a new economic bloc born in Northeast Asia. However, the trend is clear. Necessary economic prerequisites are in place. China, Japan, and Republic of Korea have become crucial trade partners for one another. Their trilateral trade accounts for 17 percent of the global trade volume and 90 percent of East Asian trade (“A milestone & new starting point for China, Japan, ROK,” 2009). Another driving force is big business, especially in Japan and Republic of Korea, which has a stake in economic integration and pushes for further development of trilateral cooperation.

For a trilateral economic grouping to come into being, it is critical that China and Japan come to agreement. The two biggest economies in Northeast Asia have to resolve their differences, particularly on the issue of regional leadership. There are essentially only two options. They could decide on joint management of the integration arrangement in Northeast Asia, as well as East Asia at large. Or else Japan might accept China’s economic leadership. The latter seems increasingly more likely, especially with China overtaking Japan as the second biggest economy in the world in 2010.

So far, it has been China that acted as the principal promoter of Northeast Asian integration. In 2002, Chinese Premier Zhu Rongzi proposed a plan for the trilateral free trade area. Japan was unwilling to support this plan at that time, fearing that it could strengthen China’s positions in the region. However, after the Democratic Party of Japan came to power in 2009, Tokyo reversed its stance on the issue. Prime Minister Yukio Hatoyama emphasized the importance of East Asian integration, calling for an East Asian Community, with China, Japan and Republic of Korea as its collective core. It appears that Hatoyama’s regional initiatives were not only his personal preferences, but also reflected interests of powerful sectors in Japan’s political and economic elites. Therefore, despite his resignation in June 2010, the idea of East Asian economic community, based on a China-Japan-Republic of Korea partnership, is likely to stay relevant for Japan, even if it means ever closer ties to China (Funabashi 2011).

It is not clear yet how these two tiers of an evolving Northeast Asia's institutional architecture will interact and relate to each other. The question is whether it would be possible for a more broad-based six-party grouping and "the Asian⁷ only" bloc to act in concert. What if competition arises between them? For instance, what are going to be the implications if China, Republic of Korea, and Japan would go beyond the largely economic and cultural agenda they currently pursue, advancing into political and security issues as well?⁸ Would the United States and Russia feel marginalized if the trilateral partnership among Beijing, Seoul, and Tokyo intensifies, with Washington and Moscow being kept on the sidelines?

One can put the question even more bluntly: What is the likelihood that the emerging China-Japan-Republic of Korea triangle would grow into a political alliance, with Beijing calling the shots? Economic reasons seem to be already in place. Japan and Republic of Korea are increasingly drawn into the Chinese economic orbit. China has become the biggest trade partner for both Japan and the Republic of Korea. Their relations are characterized by asymmetric interdependence, with Japan and Republic of Korea depending on China more than China depends on them. The recent global crisis has deepened this trend. China now accounts for 20 percent of Japan's total exports and imports, while just 13 percent of China's trade is with Japan. China's share of Republic of Korea's trade currently stands at 20.5 percent, while China's trade with Republic of Korea is only 7 percent of its total volume (Yul Sohn 2010).

Meanwhile, America's economic presence in the region has significantly decreased, although it is still quite noticeable. The United States remains a key export market for Northeast Asian countries and a major source of vital technologies. Washington is seeking to promote its own neoliberal version of regional integration, which, although thus far with little success, attempts to challenge China-centered economic regionalism in East Asia. America's strategy is, in particular, based on the recently launched Trans-Pacific Partnership, as well as bilateral FTAs, the most substantial one to date being Republic of Korea-US FTA.

However, even if the United States were ultimately to lose the competition in *economic* regionalism to China, this would not automatically entail the advent of Sino-centric *political* institutions in the region. Economic integration does not necessarily lead to stronger political (intergovernmental or supranational) arrangements. Indeed, when integration makes great progress in the economic area, member-states may deliberately constrain it in other, especially political, spheres, so as not to put their national sovereignty at risk. Even the European Union's experience testifies to such a hedging strategy (Busygina, Filippov 2010).

East Asian countries, including Japan and both North Korea and Republic of Korea, are well aware of the risks inherent in their high economic dependence on China. Therefore, they are seeking to offset such risks by maintaining political and strategic ties to the actors capable of balancing a rising China, especially the United States. Both Tokyo and Seoul have no

⁷ "Asian" here designates countries that belong to Asia both geographically and culturally.

⁸ So far, the security agenda has been peripheral to the CJK process. Yet at the fourth summit in May 2011 it was decided to hold "Trilateral Policy Dialogue on Asian Affairs" within senior foreign officials' annual consultation "in order to promote comprehensive, objective and in-depth understanding of each other's Asian policies and contribute to peace and stability in the region" [Japan-China-Korea Summit Declaration, 2011]. It remains to be seen whether this mechanism will evolve into something substantial.

intention of abandoning their alliances with Washington. Indeed, they are even strengthening their strategic cooperation with America in some areas, as well as enhancing political collaboration between themselves (Ryo Sahashi 2011). There are reasons to believe that even North Korea is wary of growing China's might and might be interested in the United States acting as a balancing force (see, for example, Lankov 2010; Feffer 2010).

Russia, although its regional clout is much less than America's, can be seen as another independent player, performing a balancing function. That is probably why in 2003 Pyongyang insisted on Moscow having a seat at the Six-Party talks (Sevastyanov 2008, p. 252). In other words, the Six-Party process, and a prospective institutionalized mechanism with full American and Russian membership, might be viewed as a vehicle to maintain balance of power and prevent Chinese dominance in Northeast Asia.

The economic triangle of Beijing, Tokyo, and Seoul could be transformed into a Chinese-led political bloc only if full-fledged China's hegemony arrives, similar to what happened following the Second World War, when the United States used its predominance to build and manage a "Western" institutional architecture. Economic leadership alone is not enough for actual hegemony. Two other requirements are military-strategic primacy and the recognition of hegemony as legitimate from lesser states (Alagappa 2003, pp. 53-4). It is clear that China does not meet these requirements as yet. Its military capabilities are still no match for America's. And in terms of moral and political legitimacy, neither Republic of Korea nor Japan appear ready to recognize Chinese primacy. To be sure, one cannot rule out the emergence of Beijing's hegemony in the future. However, at present it seems unlikely.

In a nutshell, Northeast Asia is going to witness the evolution of a dual institutional architecture in the foreseeable future. On the one hand, economic integration linking China, Japan, and Republic of Korea will deepen and expand, which is likely to result in their economic community. On the other hand, this economic process will be paralleled by the development of political multilateralism originating from the Six-Party talks, with the active involvement of the United States and Russia. Thus "the balance of institutions" is likely to emerge, whereby China's influence will be pre-eminent in regional economic cooperation, but significantly diluted within the political multilateral arrangement—a kind of Northeast Asian concert of powers.

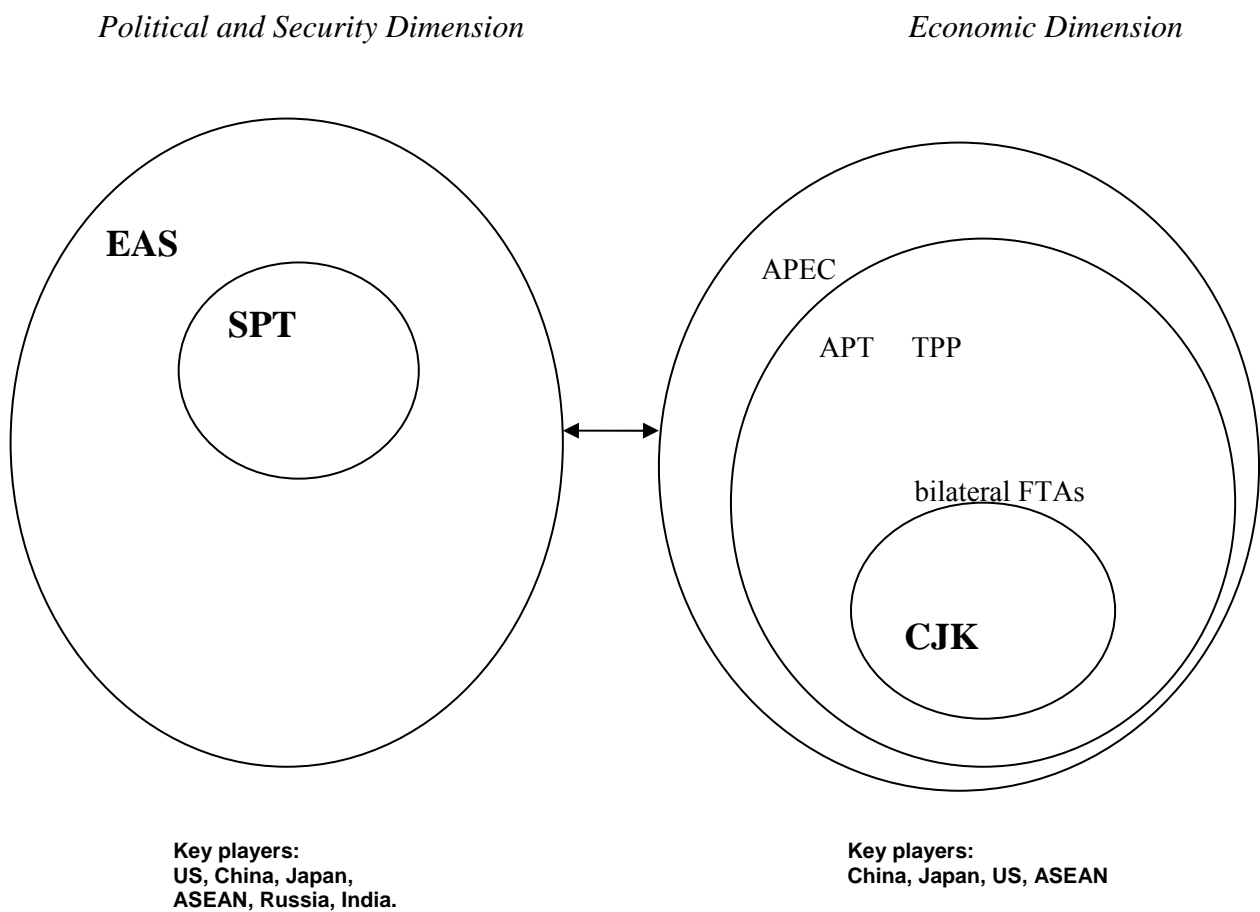
Northeast Asia's evolving institutional architecture reproduces what has already been going on in the wider East Asia, where China-centered, exclusively Asian and economically focused ASEAN Plus Three coexists with the ASEAN Regional Forum, ASEAN Defense Ministers' Meetings Plus Eight and the East Asia Summit that are characterized by more inclusive membership and security agenda.

Northeast Asia not just replicates this—it may well be becoming the most crucial part of Asia-Pacific's institutional order. Indeed, it is hard to imagine that Asia-Pacific/East Asian multilateral institution building will succeed unless Northeast Asian countries form a viable system of collective cooperation and dialogue. Thus, a likely future scenario can be drawn up in which the Six-Party-based "Northeast Asian concert"⁹ would act as the primary core for

⁹ Concert can be defined as joint management of international affairs by great powers on the basis of certain common goals, values, and interests. The concert type of international order combines elements of power balancing and elements of collective security (Alagappa 2003, p. 55).

the Asia-Pacific security and political cooperation, while in a region-wide context it is supplemented by ARF, ADMM+8 and EAS.¹⁰ In a similar manner, the prospective China-Japan-Republic of Korea FTA would function as a center for the region-wide economic integration, enveloped by a multitude of bilateral, minilateral and multilateral arrangements in the Asia-Pacific (see Figure 6-1). Evolving balance of institutions in the form of the dual regional architecture is part of soft power balancing in the Asia-Pacific, whose primary aim is to hedge against strategic uncertainties associated with the rise of China.

Figure 6-1. Emerging Balance of Institutions in the Asia-Pacific: Political Concert of Asian and non-Asian Powers vis-a-vis China-dominated Economic Integration



What role, if any, could APEC play in this institution-building scenario? Is it facing the unenviable prospect of being an odd man out in the emergent regional order? When APEC was born in 1989, it had no “peer competitors” in the Asia-Pacific, except ASEAN. Nowadays there is an alphabet soup of multilateral bodies in the region, and APEC is just one piece in this puzzle. APEC was, from the very beginning, supposed to be largely about trade liberalization, but on this front it showed lackluster performance and is now overshadowed by

¹⁰ So far EAS has been primarily concerned with economic, environmental, and social issues. However, following the addition of Russia and the United States, the forum’s members expressed interest in giving more attention to strategic and security issues (Lavrov 2011).

proliferating bilateral and minilateral FTAs. There used to be talk of APEC taking on certain political-security dimensions as the most inclusive top leaders' gathering in the Asia-Pacific. Yet, with the creation of East Asia Summit, and with the United States and Russia formally joining EAS in 2011, APEC is going to lose this important status-related advantage. In fact, EAS could be seen as more representative compared to APEC, since it counts India, a crucial Asian power, in its membership.

Nevertheless, APEC may have at least two strong points. The first lies in its genesis as an institution standing for the imagined and ideational "Asia-Pacific" versus more concrete, narrow, and territorial versions of regional cooperation. Globalization was the huge fad of the 1990s. As its glamour faded in the 2000s, so did APEC's, because the forum has always been seen as the champion of globalization in the Asia-Pacific. With pendulum swinging now in favor of more territorial forms of integration, APEC could help prevent this swing going too far towards closed regionalisms. APEC's liberal and globalization-friendly discourse, although an intangible asset, still matters a lot.

APEC's other strength is related to its accomplishments in specific areas of functional economic cooperation and business facilitation, such as APEC businesspeople mobility scheme. If APEC continues making such "niche contributions" it will remain relevant and in demand even in the face of other competing institutions in the Asia-Pacific.

RUSSIA AND THE ASIA-PACIFIC COOPERATION

Despite a Pacific coastline of 16,700 miles, Russia is a latecomer to Asia-Pacific regionalism. Due to the Cold War, the Soviet Union was shut out of regional cooperation, having instead to rely on bilateral ties with a few allies such as Viet Nam and Mongolia. Following the end of the bipolar confrontation in the early 1990s, Russia strove to integrate itself into Asia-Pacific bodies. It quickly joined the region's premier nongovernmental forums, Pacific Economic Cooperation Council and Pacific Basin Economic Council, in 1992 and 1994, respectively. Yet acquiring APEC membership proved much more difficult. For one thing, in the 1990s Russia's share of Asia-Pacific total exports stood at a meager 0.4 percent. This did not quite square with one of APEC's membership requirements that an applicant country should have substantial economic ties to the Asia-Pacific. Another hurdle to Russia's membership was the apprehensions of some among the smaller and middle-sized APEC economies that the addition of another big country would weaken their positions and raise the risks of the great power domination within the forum.

However, at the 1997 Vancouver summit Russia's APEC application was finally approved, along with Peru's and Viet Nam's. Moscow's bid was supported by the United States, China and Japan, thus deciding the matter. Not everyone was happy, though. For example, the former Australian Prime Minister Paul Keating made the following remark:

Russia's membership was supported by the United States in part, I believe, to atone for another bad decision - to expand NATO to the borders of the old Soviet Union. This sent a signal to Russia that it wasn't wanted as part of the European system. Instead it was offered APEC membership as a consolation prize in the "Asia Pacific" (Keating 1998).

In Russia itself, the admission to APEC was met with enthusiasm and as a confirmation of the country's status as an Asia-Pacific power. In 1996, Russia also became a dialogue partner of ASEAN and a member of the ASEAN Regional Forum.

Despite joining APEC and ARF, Russia, due to domestic turmoil, ceased to be a major factor in the Asia-Pacific during the 1990s. However, during Putin's and Medvedev's presidential tenures, Russia managed to substantially improve its internal situation, enabling Moscow to embark on more proactive foreign policies in the 2000s. The Asia-Pacific region became and still remains one of the top priorities of Moscow's external strategy. On the political and diplomatic front, Russia resuscitated contacts with Pyongyang, while keeping good relations with Seoul. Most important, Moscow established a "strategic partnership" with China, both in bilateral and multilateral (the Shanghai Cooperation Organization) formats. In addition, the Russian government launched a massive program of state-funded investments in the social and economic development of its Far Eastern areas. The objective is not only to upgrade the economy and infrastructure but also to reinforce Russia's geopolitical position in the Pacific. Russia's more vigorous policy is generally seen in the region as a positive factor. According to such assessments, "Russia's pragmatic neomercantilism... would do no harm to countries of the region or to the rising Asian regionalism. Properly utilized and implemented, it might actually help facilitate bilateral and multilateral cooperation in Northeast Asia" (Tachwan Kim 2008, p. 209).

One sign of Russia's return to the Asia-Pacific is its involvement in key security forums. In 2003, Russia became a co-sponsor of the Six-Party talks. In 2005, it sought membership in the East Asia Summit at its inaugural meeting in Kuala Lumpur, where President Vladimir Putin attended as a special guest. At that moment, the bid failed to gain consensus approval of the 10+6 forum. Yet, in 2010 Russia secured an invitation to join the EAS, along with the United States. In 2010 Russia also joined the ASEAN Defense Ministers Meeting process (ADMM+8). Thus Russia now holds membership of all the Asia-Pacific multilateral security-political bodies: SPT, ARF, ADMM+8, and EAS.

Russia views its involvement in the Asia-Pacific security forums as a kind of guarantee that its voice will be heard and heeded. Russia's preferred model for the Asia-Pacific political order is a multi-polar concert system, where Moscow a major player, along with Beijing, Washington, Tokyo, New Delhi, and perhaps Seoul and Jakarta. The Kremlin emphasizes the role of the Six-Party talks as not only the diplomatic vehicle for North Korea denuclearization, but also as the mechanism for "the creation of reliable political and legal guarantees of security in Northeast Asia" (Russian Ministry of Foreign Affairs 2011). Moscow's strong commitment to the Six-Party talks is not surprising, given that Russia wields substantial geopolitical leverage in Northeast Asia, while in other regions of the Asia-Pacific its influence is much more limited. At the same time, Russia wants to see the East Asia Summit as an umbrella political grouping in the Asia-Pacific which could "integrate regional security agenda in order to promote strategic dialogue" (Lavrov 2010).

While Russia has secured for itself full representation in the Asia-Pacific political institutions, in the economic arena its presence can be characterized as very modest at best. Russia accounts for roughly one percent of the region's trade. APEC remains the only regional economic grouping in which Russia participates. Even with APEC, Russia's involvement has mainly been limited to attending gatherings at a high political level such as Leaders' summits and ministerial meetings. Russia has kept a low-profile or been altogether absent in most of the forum's practical activities and projects. For instance, it was the last member-economy to join the APEC Business Travel Card initiative in 2010 (as a transitional member). Yet Russia has been lately stepping up its involvement in APEC. One reason is, of course, the hosting of APEC-2012 in Vladivostok, which means that Russia has to act as the forum's formal leader.

Apart from that, it seems that Russia, as part of its broader shift in priorities towards the Asia-Pacific, is actually getting more interested in APEC. This might give hope that Russia's enhanced involvement in APEC will outlast the Vladivostok events and continue beyond 2012.

Russia remains one of the very few economies in the Asia-Pacific that have no free trade agreements in the region. Moscow clearly sees the danger of its increasing economic marginalization in the Asia-Pacific and seems determined to change this, even though Russia has not yet been admitted to the World Trade Organization (as of this writing in October 2011). The necessity of concluding FTAs with the Asia-Pacific countries was emphasized by President Dmitriy Medvedev during his visit to the Russian Eastern city of Khabarovsk in July 2010 (Medvedev 2010). In 2010, Russia launched formal FTA negotiations with New Zealand.¹¹ FTAs with Viet Nam and Singapore are also being studied.

Integration with the Asia-Pacific is among Russia's three most important regional integration projects. Moscow's paramount goal is to secure economic reintegration of the post-Soviet space, which should come in the form of the Russian-led Eurasian Union proposed by Vladimir Putin in October 2011¹². The number two priority is integration with the European Union, which accounts for the bulk of Russia's foreign trade. In fact, according to Putin, the Eurasian Union should become part of "Greater Europe." At the same time, Moscow has an ambitious goal of turning the Eurasian Union into a link between Europe and the Asia-Pacific (Putin 2011).¹³

Russia's institutional integration into the highly competitive Asia-Pacific markets will only make sense if it can identify and exploit niche areas where its economy has comparative advantages. Russia's most visible advantage is, of course, its rich natural resources, especially hydrocarbons. Russia has been making great efforts to become a major supplier of oil and natural gas to the Asia-Pacific. The Eastern Siberia-Pacific Ocean came online in 2010, bringing to the regional markets crude from inside Siberia, and more energy-related projects are now underway.

Even more ambitious projects are under discussion to drastically expand Russia's economic links with the Asia-Pacific. In particular, there is an idea, proposed by an influential think tank in Moscow, of turning Russia's eastern territories, with their abundance of water, energy, arable land and timber, into a major producer of energy-consuming basic products, like grain, meat and paper, for voracious Asian markets. Foreign investment and technologies, mostly to be provided by the Asia-Pacific countries, are to play a crucial role in realizing this grand project (Karaganov 2011).

Russia also seeks to play a major role in innovative and intellectual sectors of the Asia-Pacific economy. One of the biggest recent efforts in this direction was the creation of Far Eastern

¹¹ Russia-New Zealand trade is minimal, a meager US\$230 million in 2010 [Russian Federal Customs Agency, 2011]. Yet it is hoped that an FTA with the advanced economy of New Zealand will be path-breaking and help Russia enter the FTA game in the Asia-Pacific.

¹² The prospective Eurasian Union is expected to build on the Customs Union of Russia, Kazakhstan and Belarus, which took effect in July 2011.

¹³ Although it is never explicitly stated by the Russian government, expanded engagement with the Asia-Pacific could also serve as a fallback option, should integration with the European Union fail to meet Moscow's expectations.

Federal University in Vladivostok in 2011, which consolidated several smaller higher education institutions into what the Russian government wants to become a world-class research university targeting Asia-Pacific education markets. Moscow has allocated hefty sums for the development of the university. Its state-of-the-art campus, now under construction, will serve as the venue for APEC Leaders' meeting and is expected to be inaugurated by them in September 2012.

It appears that Russia's preferred model of economic integration into the Asia-Pacific has similarities to Canada's and Australia's in that it seeks to combine large-scale exports of natural resources with the strong emphasis on innovative sectors such as high-tech science and higher education. It remains to be seen, of course, whether Russia will be as successful as Canada and Australia in pursuing this path.

The success of Russia's efforts at regional integration significantly depends on whether it has support of the established Asia-Pacific powers. China is Russia's main "strategic partner" in the region. In 2010 it overtook Germany to become Russia's biggest trading partner. However, it is doubtful that China will make it a priority to help Russia become the full-fledged member of the Asia-Pacific system of economic cooperation. China is quite content with having Russia as a reliable supplier of raw materials and is interested in keeping this resource base to itself rather than facilitating Russia's links to other Asia-Pacific markets.

Another major Asia-Pacific economy, Japan, although presumably interested in weaning Russia away from growing dependence on China, is unlikely to do much to assist Russia's regional aspirations. This is, of course, mainly because of the ill-fated dispute over South Kuriles/Northern Territories still poisoning relations between Moscow and Tokyo.¹⁴

This leaves another Asia-Pacific power, the United States. Can it possibly be a partner for Russia seeking to expand its ties to the region? There is a good chance that it can. It is remarkable that of all the areas, where Moscow's and Washington's geopolitical concerns overlap, it is the Asia-Pacific where their interests are least conflicting and most compatible. Whereas in Eastern Europe, the Caucasus, and Central Asia, Russia and America are competitors rather than partners, they do not have irreconcilable disagreements in the Pacific. Although Moscow's influence in Northeast Asia has grown somewhat in recent years, it is still too weak to be perceived by Washington as an actual, or even potential, challenge. Russia's central geopolitical interest in the region is to retain effective control over its Pacific territories, not to expand at the expense of others. This is well understood in Washington. It is also important that both Russia and the United States want to hedge against serious geopolitical uncertainties stemming from China's rise.

Of note, in this regard, is a recent report on the prospects for Russia-U.S. ties prepared by a group of prominent Russian experts (Karaganov, Suslov, et. al. 2011). They point out that under the Obama Administration Russian-U.S. relations have markedly improved, opening up opportunities for setting a new bilateral agenda. The report emphasizes that Russia and the United States do not pose a danger to each other. They have to be concerned not with one another, but with other threats and challenges. Both Russia and the United States experience the diminution of their relative power in the face of "the global diffusion of power" and the

¹⁴ For instance, Japan has been blocking Russia's bid to join the Asian Development Bank ever since Moscow made an application in 1997.

rise of new ambitious players in Asia, especially China. This makes it necessary that Russia and the United States become close friends, even to the point of “selective military-political alliance in order to counter a wide range of new threats and challenges” (Karaganov, Suslov, et. al. 2011, p. 4). As the authors of the report indicate, the biggest regional challenge in global politics lies in the uncertainty of China’s future behavior (Karaganov, Suslov, et. al. 2011, p. 10). Strategic alignment with the United States would allow Russia to feel more confident vis-à-vis China. America’s friendship and support will avert the possibility of Russia becoming China’s periphery and its client state, a development that could greatly strengthen Beijing’s geopolitical might, to the detriment of U.S. national interests (Karaganov, Suslov, et. al. 2011, pp. 16, 19).

Although Russia and the United States have somewhat different approaches to North Korea, with Moscow favoring a softer line on Pyongyang and Washington taking a tougher stance, they have been working together in the Six-Party process. And their collaboration can move beyond just denuclearizing North Korea, perhaps towards some concerted steps on building a kind of regional architecture that would be acceptable to Moscow and Washington. Both Russia and the United States face the risk of being marginalized if the Northeast Asian integration evolves towards an exclusive Asian club of Beijing, Tokyo and Seoul. If China-Japan-Republic of Korea partnership becomes the principal regional institution in Northeast Asia, it will hardly be a desirable outcome for Russia and the United States. Instead, they are both interested in the development of a more inclusive version of Northeast Asian multilateralism originating from the Six-Party talks, possibly excluding Pyongyang, if it continues to show intransigence. This shared concern might spur Moscow and Washington to enhance their cooperation.

Russia has long been pushing for multilateralism in Northeast Asia. In 2007, as part of the Six-Party process, Moscow became the chair of the working group on Northeast Asia peace and security mechanism. The United States has historically been less enthusiastic about Northeast Asian multilateralism, relying on its bilateral alliances in the region. Yet, there are signs that Washington might reassess its stand. The hub-and-spoke system was only possible under America’s undisputed hegemony. Now that the era of the U.S. political dominance appears to be nearing its end, the best option for America could be multilateral diplomacy, a concert-like order within which Washington might hope to be a *primus inter pares*. Influential American experts now talk about the need to create “a formal five-party mechanism for Northeast Asia”, adding the United States and Russia to the existing trilateral grouping of China, Japan and Republic of Korea (Feigenbaum and Manning 2009, p.22). Russia and Washington also have similar expectations for the East Asia Summit, wanting it to become the Asia-Pacific’s main venue for discussing political and security issues (Lavrov 2010; Clinton 2010b).

Being non-Asian powers culturally and historically, Russia and the United States are naturally interested in preserving the trans-Pacific dimension of the Asia-Pacific institution building. It is telling that Russian political and intellectual elite are increasingly talking of Russia as “the Euro-Pacific power” as opposed to the “Euro-Asian” concept (Nikonov, Toloraya et al. 2010). This implies that Russia wants to avoid exclusive focus on the continental Asia, meaning China in the first place.

APEC, as the leading trans-Pacific institution, could become a good venue for promoting Russia’s and America’s common interests in the Asia-Pacific. So far, Russia-U.S.

collaboration in APEC has been largely non-existent. In fact, the two sides have missed the chance to take advantage of their successive APEC chairmanships, in 2011 and 2012 respectively, when they could have had more coordination and launched some joint initiatives. Yet, there are still plenty of opportunities for Russia-U.S. cooperation, both within APEC and other APEC-related multilateral arrangements. As one option, Russia might consider joining the U.S.-led Trans-Pacific Partnership initiative, especially given the fact that it is already negotiating an FTA with New Zealand and studying FTAs with Viet Nam and Singapore (all the three economies are the TPP participants). This no doubt would be quite a bold move, particularly in the light of Russia's still continuing WTO-accession saga. It is clear that Russia will hardly be able to join the TPP very soon, since Moscow's neomercantilist policies are not consistent with the TPP claiming to be "a high-quality FTA." Yet, as the long-term prospect, Russia's membership in the TPP should not be ruled out, especially as Russian economy will likely gradually move away from neomercantilism and evolve towards more openness. If Moscow at some point decided to ask for the TPP entry and Washington responded positively, it might usher in a new era for Russia's relations with the Asia-Pacific, as well as with the United States.

CONCLUSION

The Asia-Pacific is in many ways an imagined region superimposed onto more territorial and historically rooted regions. Northeast Asia, with its huge strategic and economic potential, seems to be the most important of these. Developments in Northeast Asia will increasingly shape international order in the Asia-Pacific and beyond. Despite the presence of powerful factors fuelling rivalry and conflict in Northeast Asia, the region has lately been witnessing more cohesion and multilateral cooperation.

Northeast Asia seems to be moving towards a dual institutional architecture. On one hand, economic integration linking "the core states," China, Japan, and Republic of Korea, is deepening and expanding, which is likely to result in an economic community. On the other hand, this economic process is paralleled by the development of political multilateralism originating from the Six-Party talks, with the active involvement of the United States and Russia. "The balance of institutions" is likely to emerge, whereby China's influence will be pre-eminent in regional economic cooperation, but significantly diluted within the political multilateral arrangement, a kind of Northeast Asian concert of powers.

Northeast Asia's evolving institutional architecture reproduces what has already been going on in the wider East Asia, where the China-centered, exclusively Asian and economically focused APT coexists with the ARF, ADMM+8 and EAS that have more inclusive membership and security oriented agenda.

A likely future scenario can be drawn up in which the Six-Party-based "Northeast Asian concert" would act as the primary core for the Asia-Pacific security and political cooperation, while in a region-wide context it is supplemented by ARF, ADMM+8 and EAS. In a similar manner, the prospective China-Japan-Republic of Korea FTA would function as a center for the region-wide economic integration, enveloped by a multitude of bilateral, minilateral and multilateral arrangements in the Asia-Pacific. On one hand, the dual regional architecture reflects the underlying reality of China's increasing economic weight, while, on the other, it appears to be part of soft power balancing in the Asia-Pacific, whose primary aim is to hedge against strategic uncertainties associated with the rise of China.

In this emerging institutional order, APEC could stay relevant as standing for more open and globalised “Asia-Pacific” versus more closed and purely territorial versions of regionalism. APEC’s other strength has to do with its achievements in specific areas of functional economic cooperation and business facilitation.

Russia’s efforts to engage with the Asia-Pacific is one element in its three-pronged strategy of regional integration, the other two dimensions being the Russian-led reintegration of the post-Soviet space and closer cooperation with the European Union. Russia has stepped up its involvement in Asia-Pacific affairs and seeks to be a major player in the regional institution-building. Russia has secured full representation in the Asia-Pacific political institutions, but in the economic arena its presence is still minimal. To successfully integrate into the Asia-Pacific, Russia needs support from the established regional powers. The United States might play such a helping role, as the Asia-Pacific seems to be a region where Moscow’s and Washington’s interests are least conflicting and most compatible. Being non-Asian powers culturally and historically, both Russia and the United States face the risk of being marginalized if the Northeast Asian/East Asian integration evolves towards an exclusive Asian club. Russia and the United States are naturally interested in preserving the trans-Pacific dimension of the Asia-Pacific institution building. APEC, as the leading trans-Pacific institution, could become a good venue for promoting Russia’s and America’s common interests in the Asia-Pacific. Joining the Trans-Pacific Partnership, as the long-term prospect, could be a way for Russia to expand its ties to the Asia-Pacific, as well as strengthen its relationship with the United States.

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7. New IAP Peer Review Process toward FTAAP

APEC HAS RENEWED ITS LIBERALIZATION PROCESS

President Barack Obama will host the APEC Leaders' meeting in Honolulu in November, highlighting this year's APEC activities under the U.S. initiative. His priority is, of course, to complete the negotiation of the Trans-Pacific Partnership among nine APEC economies and report to other APEC leaders that the TPP will guide APEC to be graded up eventually to FTAAP, FTA of the Asia-Pacific area.

In September last year, in preparation for APEC Yokohama, Prime Minister Naoto Kan proposed that Japan join the TPP negotiations so that Japan would take an initiative in forming a free trade regime in Asia Pacific. But he met strong resistance from the domestic farm lobby and failed to make it a highlight of Yokohama APEC. His predecessor, Yukio Hatoyama, expressed his wish to form an East Asian Community (EAC) at APEC Singapore in November 2009 but quit without any progress toward it. TPP and ASEAN-plus FTAs (in line with EAC) have been highlighted as rival proposals for regional economic integration (REI) in Asia Pacific by media at the time of successive APEC meetings. But neither TPP nor ASEAN-plus FTAs are conducted in APEC, the sole intergovernmental network for Asia-Pacific cooperation. APEC has had liberalization and facilitation as core activities for the past 15 years. The media, however, has not paid much attention to these activities, leaving the general public as well as young scholars unaware of them.

As a matter of fact, it was in 1993, at the first leaders' meeting in Seattle, that APEC announced its goal of achieving "free and open trade in the region." This was followed by the ambitious Bogor Declaration and its implementation plan, the Osaka Action Agenda, in successive years. Last year, 2010, was the mid-term target of the Bogor Goals and senior officials conducted a thorough assessment of 13 economies' progress toward the goals. APEC Leaders acknowledged the SOM report and committed to continue the process toward its final goal of 2020. A new liberalization program was adopted by SOM at Montana last May. These facts are all on the website of the APEC secretariat but have not attracted much attention by outside people. It is the role and task of us ASCC experts to monitor closely these moves by government officials in charge of APEC activities and give advice. My report aims to

encourage the ASCC participants, especially young scholars, to get interested in APEC's proper activities as well as TPP and ASEAN plus FTAs.¹

The title of this presentation, 'toward FTAAP' may be better revised as 'toward 2020', since FTAAP is the Leaders' future vision of APEC after APEC achieves the Bogor Goals. Leaders indicated TPP and ASEAN-plus FTAs as plural paths to arrive eventually at FTAAP and gives APEC an incubator role in this direction. But I would like to stick to this title in order to urge you to look to the APEC's own liberalization program as a supporting route to FTAAP.

APEC 'ACHIEVES FREE TRADE BY 2020'

In 1989, APEC started as a series of meetings by foreign and trade ministers from twelve economies on economic cooperation matters in the Asia Pacific region. The United States was among the founding members along with Japan and Australia.

Trade and investment liberalization and facilitation (TILF) has become one of APEC's major tasks since the first Economic Leaders Meeting in Seattle in 1993, where leaders jointly declared that they would 'achieve free and open trade in Asia and Pacific'. In 1994 President Suhart of Indonesia hosted the second Leaders meeting in Bogor and delivered the ambitious Bogor Declaration, "...to complete the achievement of our goal of free and open trade and investment in the Asia-Pacific no later than the year 2020,with the industrialized economies achieving the goal of free and open trade and investment no later than the year 2010 and developing economies no later than the year 2020" (APEC Leaders' Declaration 1994). In 1995, Japan hosted the Osaka APEC and adopted the Osaka Action Agenda (OAA) which provided concrete measures that could be taken to achieve the Bogor Goals. The Manila APEC in 1996 adopted the Manila Action Plan for APEC, MAPA) and their implementation started in 1997.

The annual APEC gathering of prime ministers and presidents of major economies with bold declarations attracted the media's attention. Expectations for APEC became heightened and participating economies increased up to 21 in 1998, covering all major economies surrounding the Pacific Ocean.

APEC has pursued its liberalization and facilitation measures toward the Bogor Goal within the IAP/CAP framework. Its concrete design, the Osaka Action Agenda (OAA), had a comprehensive coverage of 14 areas of trade and investment liberalization and facilitation, and described measures to be implemented for each area. Facilitation measures aimed to reduce the cost of doing business by enhancing the transparency and certainty of rules, legislation and standards and harmonizing them between participating economies, which are equally important to liberalization in order to enhance trade and investment in the region.

The IAP formula reflected APEC's unique modality of implementing liberalization and facilitation, that of "concerted unilateral liberalization." Under this scheme, individual economies unilaterally announced their own liberalization and facilitation programs and implemented them in accordance with their domestic rules. However, individual economies closely watched each other's liberalization program and implementation and were obliged to submit liberalization programs as broad-ranging as their neighbors' and were encouraged to

¹ For this purpose the author is publishing a book, *APEC: New Agenda for its Third Decade*, (Yamazawa 2011).

implement in line with their commitments. SOM has conducted a peer review process of individual IAPs at its special sessions since 2002. APEC relied on peer pressure to urge all economies to join the liberalization efforts.

Individual economy governments have continued to revise their IAPs every year. The reporting has been made more elaborate and transparency improved in response to a common format. The number of liberalization measures increased as their Uruguay Round (UR) commitments were implemented. Voluntary liberalization was also added either in the form of accelerated implementation of the UR agreement or reduction of applied tariffs from their UR rates in several economies. The CAP was especially effective in introducing new legislations of facilitation consistent with the APEC system prescribed in the OAA. By and large, the IAP process encouraged individual economy governments to implement liberalization and facilitation measures toward the Bogor Goals. One short-coming accompanying such implementation was its 'positive list formula' in which the IAP reported only the impediments to be liberalized but not those still remaining. Thus the IAPs increased the volume but did not provide a comprehensive list of existing impediments.

A PARADIGM SHIFT TOWARD EAST ASIAN COMMUNITY

However, APEC encountered a big setback during the Asian financial crisis when several ASEAN members and Republic of Korea were severely hit, with their currencies depreciated substantially, and some suffered from negative growth. The EVSL (Early Voluntary Sector Liberalization), a breakthrough attempt of liberalization in the "easy sectors" also failed. As such, the IAPs implemented since 1997 brought about much less liberalization than had been expected. Although it included the liberalization committed in the Uruguay Round agreement, its unilateral liberalization beyond the URA to be applied to other APEC members and nonmembers alike has been limited in terms of its coverage and depth, and further liberalization in sensitive sectors tended to be suspended.²

On the other hand, APEC itself has shifted to a more realistic line for the past decade. Its gravity has shifted from liberalization to trade facilitation, capacity building, and structural reforms. The business environment has also changed in the Asia Pacific under an environment of accelerated globalization and prevailing regionalism of bilateral and sub-regional preferential trading arrangements. The Busan Roadmap was announced to include these realistic measures in 2005.

While APEC suffered a set-back at the Asian currency crisis, East Asian regional cooperation has enhanced since 1997-1998. Most evident is the Chiang Mai Initiative (CMI), a package of currency and financial measures preventing the recurrence of the currency crisis, which includes currency swap agreement at the emergency and Asian Bond market. CMI was agreed on by ten ASEAN members and China, Japan and Republic of Korea, so-called ASEAN plus Three (APT) group at the Asian currency crisis.

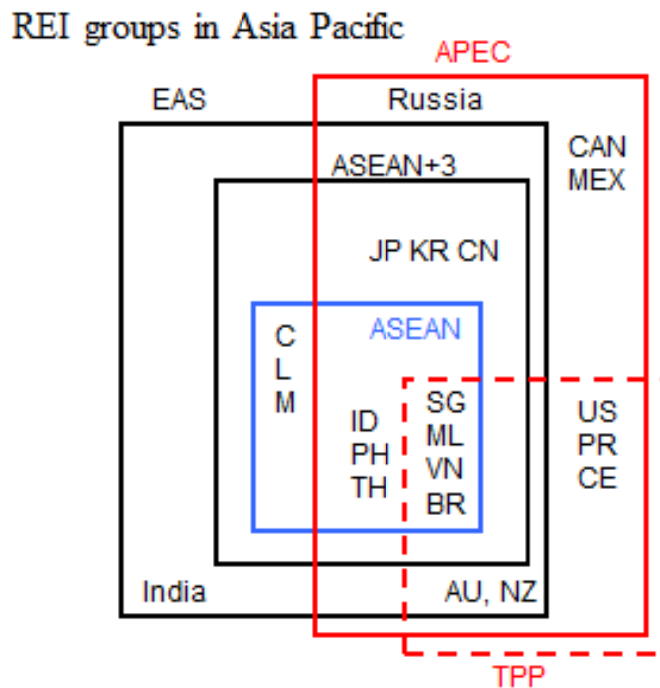
On the other hand, institutional integration has proceeded in this region. Bilateral FTAs have been concluded both within the region and with outside partners; Japan-Singapore, Singapore-Australia, Thailand-India, Thailand-Australia, Singapore-ROK, Japan-Malaysia,

² The author summarized the IAPs/CAPs of 18 APEC economies in 1997 as 'Uruguay Round plus alpha' (Yamazawa 1998) reprinted in Yamazawa and Urata (1999).

Japan-Thailand, Japan-Philippines, and Japan-Indonesia. Furthermore, China, Japan, and ROK have concluded FTAs/EPAs with ASEAN as a whole, so-called ASEAN plus 1 type. However, APT has attracted attention as a core institution in the region. Its joint statement was announced at the APT Summit meeting in 2001 and the East Asian Community idea was proposed by the East Asian Vision Group (EAVG) set under the APT Summit. (EAVG 2001).

ASEAN has taken an initiative in the East Asian cooperation. While started with five countries (Indonesia, Malaysia, Philippines, Thailand, and Singapore) in 1967, it had made a few achievements in political and diplomatic negotiation with outside partners but not much in economic areas. In 1992 ASEAN started to implement a large-scale tariff reduction, AFTA, toward an effective regional integration. It has taken an initiative of the APT implementing the Chiang Mai Initiative and formed a co-centric circle of cooperation, such as ASEAN + 1 and ASEAN +3, around ASEAN as a core and on the driver's seat (Figure 7-1).

Figure 7-1. REI Groups in Asia Pacific



Here ASEAN has taken advantage of its unique formula of ASEAN Post Ministerial Conference (ASEAN PMC). While ASEAN organized its economic and trade ministers meeting every year, it has started since the late 1980s to invite counterpart ministers of such partner countries as Japan, China, ROK, and Australia and to negotiate as a group with individual partners, that is ASEAN + 1 type formula. ASEAN extended this formula to summit meetings so that it could easily organized ASEAN +3 Summit and ASEAN + 1 Summits taking advantage of the presence of leaders of partner countries. This is a big success of ASEAN diplomacy. China, Japan, and ROK have all accepted this ASEAN initiative.

While hosting ASEAN Summit in 2005, Malaysia organized the first East Asia Summit (EAS) by inviting three more countries, Australia, New Zealand and India, and discussed

broader regional cooperation on such issues as anti-terrorism, recovery from natural disaster, preventing pandemic, environmental protection, and energy cooperation. APEC is referred to as an outer circle organization for cooperation but is not assigned a major role for East Asian cooperation.

Although sitting in the driver's seat of APT and EAS, ASEAN perceives well the fact that ASEAN is its weakest member and has moved to strengthen its economy. At the ASEAN Summit in December 2007 it adopted the ASEAN Charter and all ten leaders signed it. The charter has institutionalized ASEAN as an international organization and announced its plan to build Economic Community, Political and Security Community, and Social and Cultural Community by 2015. The Blue Print for Economic Community details concrete measures to be implemented every other year toward 2015. It reflects an increased momentum among advanced ASEAN members toward further institutionalization but there are some concerns that the blue print will not be implemented on schedule. Nevertheless, individual members completed their ratification and the charter went into effect at the ASEAN Summit in Bangkok in March 2009.

LIBERALIZATION REVIVED: TPP TOWARD FTAAP

The liberalization move has revived among advanced economies. In 2006, the APEC Business Advisory Council (ABAC) proposed an FTA covering the whole of APEC economies (ABAC 2006). It aimed to promote the integration and conglomeration of all FTAs mushrooming in the APEC region for the past decade and thus creating a greater single market and achieving the maximum scale economy. In spite of prudent attitude by Asian side, it was adopted as a long-term agenda of APEC in 2007 (APEC/LM 2007).

On the other hand, the Trans-Pacific Partnership (TPP) has emerged as a binding FTA among a selected economy group of APEC. TPP was originally formed by Brunei, Chile, New Zealand, and Singapore in 2006. It aims to “establish a Trans-Pacific Strategic Economic Partnership (TPSEP) among the parties, based on common interest and deepening of the relationship in all areas of application.” It has taken a “WTO plus” approach, covering not only commodity and services trade but also such facilitation areas as rules of origin, customs procedures, trade remedies, technical barriers to trade, competition policy, intellectual property, government procurement, and dispute settlement. (TPP 2006).

The evolution of TPP originated in the late 1990s, when some APEC economies were disappointed by the stalled move for liberalization within APEC. The like-minded economies of Australia, New Zealand, the United States, Singapore, and Chile started the P5 talks on the occasion of APEC meetings in order to find a path toward further liberalization.³ While the US and Australia came out, the remaining P3 conducted four round negotiations in 2002-2005 and announced their agreement on TPSEP agreement at the APEC/MRT in 2005. Brunei joined at the last minute to form the P4 (Elms 2010). In late 2008 the United States expressed interest in participating in TPP and started a negotiation for the expansion together with Australia, Peru and Viet Nam in March 2010. The United States wishes to conclude it by the time of APEC 2011 in Honolulu.

³ Please refer to my forthcoming book (Yamazawa 2011), Chapter 2 and 6 for further detail .

How do other Asian economies respond to the TPP negotiation? Prime Minister Kan proposed that Japan join the TPP as a symbol of the “third country opening,” as Japan’s economy and society have matured and it has become inward-looking. Japan should join the TPP in order to arrest this process and promote advancement overseas. Japanese firms cannot survive global competition with only a domestic market characterized by an aging population, few children, and weakened dynamism. They have to move out to growing markets in Asia. It is imperative to produce a seamless business environment in which both Japanese and other Asian firms can do free and stable business. This leads to the East Asian Community idea. Although it is supported by the business community it has provoked a strong objection by farmers. Partly because of his weak political leadership and partly because East Japan was hit by Great Earthquake and Tsunami on March 11th, Japan’s participation in the TPP negotiation has receded for the moment. On the other hand, ROK has taken an open trade stance and concluded FTAs with the United States and European Union. She will be able to join TPP in near future.

There still remain cautious attitudes against the TPP in Asia. Other ASEAN members, Indonesia, Philippines and Thailand, do not express interest in TPP negotiations. On the other hand, they have achieved the AFTA liberalization and are tackling the 2015 target for the ASEAN Economic Community. China achieved the liberalization required for its accession to WTO in 2001, and this has paved the way for the globalization of Chinese economy and firms for the past decade. However, there still remain in her economic regime various forms of government regulations and the Chinese government is cautious about hasty deregulation. China is afraid of conceding to the NAFTA modality such as labor standards and human rights in the TPP negotiation. Furthermore, China stands against the United States in security. It feels excluded from the TPP and prefers the liberalization in East Asia along ASEAN + 3.

To conclude, the TPP negotiation has a trade-off of the high level FTA and greater scale merit of including China and other ASEAN. If it continues with the NAFTA modality under the US initiative, it will be a trans-Pacific but divide Asia. Of course, the U.S. contends that she never excludes China but expects that China will achieve further liberalization in future and join the TPP (Petri 2010 and USTR 2011). We wish the current promoters of TPP will have a clever mind of balancing the trade-off. In this regard Japan should join the TPP negotiation at an early stage and guide it in that direction.

MID-TERM ASSESSMENT AT APEC 2010 YOKOHAMA

Throughout last year APEC senior officials undertook a detailed examination of individual economies’ achievement in individual TILF areas, including own assessment by the 13 volunteered economies and the assessment report by Policy Support Unit (APEC/PSU 2010), in addition to the three rounds of IAP peer reviews for the past decade and Mid-Term Stocktakes in 2005, and produced a SOM report (APEC/SOM 2010) at SOM1 to 3.

APEC SOM reported the assessment of the Mid-term Bogor Goals achievement to Leaders’ Meeting in 2010. It included five industrialized economies designated to achieve the free and open trade by 2010 plus eight economies which volunteered to be assessed this time, namely Chile, Hong Kong, China; Republic of Korea, Malaysia, Mexico, Peru, Singapore, and Chinese Taipei. They were not assessed individually but as a group of five plus eight economies. Leaders summarized the achievement of the 13 economies as follows (APEC/LM 2010b):

- The overall growth in commodity trade for all APEC economies increased by 7.1% annually for 1994-2009, services by 7.0%, and inflow and outflow of FDI by 13.0% and 12.7% respectively.
- The 13 economies reduced their simple average tariffs from 8.2% to 5.4% for 1994-2009, far lower than the world average of 10.4%, as well as further tariff reduction within their FTA framework.
- They opened their services markets through unilateral reform of domestic policy and maintained liberalized investment regime.
- They have also taken significant steps on trade facilitation to streamline customs procedures and align standards and conformance procedures. Under the Trade Facilitation Action Plan (TFAP) they have reduced transaction costs in the region by 5% for 2002-2006 and are achieving an additional 5% under the second TFAP by this year.

Leaders also noted that impediments remain in sensitive sectors (APEC/LM 2010b), such as

- Higher tariffs in agricultural products and textile and clothing;
- Restrictions in financial, telecommunications, transportation, and audiovisual services, and the movement of people least liberalized;
- Sectoral investment restrictions in the form of prohibitions or capital ceiling and continuing general screening systems;
- Nontariff measures;
- Standards and conformance, customs procedures, intellectual property rights, and government procurement; and
- Behind-the-border issues that can be resolved through structural reform.

Leaders concluded as follows:

It is a fair statement to say that the 2010 economies have some way to go to achieve free and open trade in the region. APEC challenges in pursuing free and open trade and investment continues. APEC will continue to review economies' progress towards the Bogor Goals of free and open trade and investment. We recognized that all APEC economies must maintain their individual and collective commitment to further liberalize and facilitate trade and investment by reducing or eliminating tariffs, restrictions on trade in services, and restrictions on investment, and promoting improvement in other areas, including non-tariff measures and behind-the-border issues.

APEC has achieved much since its inception, evolving to become the pre-eminent economic forum in the Asia-Pacific, the world's most dynamic and open region. Looking back over the past 15 years, the progress made by APEC in pursuit of the goal of free and open trade and investment has reinforced the fact that full achievement of the Bogor Goals for all economies should continue to provide direction for APEC's work of trade and investment liberalization and facilitation (APEC/LM 2010b)

This is a fair assessment of APEC's achievement, considering the severe constraints that the WTO/DDA negotiation has stumbled on recently and that the Bogor process has been implemented under the modality of nonbinding liberalization. APEC's TILF process will continue for all APEC economies, including the 13 economies summarized as above.

NEW IAP PEER REVIEW PROCESS

Leaders committed in Yokohama to continue the TILF process toward the final Bogor Goals in 2020. SOM2 last May in Montana adopted “the new IAP peer review Process” for all 21 members to remove remaining barriers toward 2020.

- The new IAP should cover all 14 areas of the Osaka Action Agenda plus those added afterwards (transparency, RTAs/FTAs, and other voluntary reporting areas). 2010 economies (13 were assessed in 2010) might give emphasis to those areas where shortcomings were highlighted by Leaders, cited above.
- Economies should describe, in brief points only, significant new developments under each chapter heading.
- Economies would report in 2012, 2014, 2016, and 2018. The final assessment would be in 2020.
- Policy Support Unit support SOM in this new IAP peer review process. It will prepare a one to two page report with key highlights on members’ main achievements and remaining areas for improvements in the year of review. PSU reports will be discussed at SOMs and finally made public.

These respond to often heard criticism of the previous IAP peer review process. If implemented faithfully, the new IAP process will be much stronger. For APEC 2010 Yokohama, the author conducted an independent quantitative assessment of all 21 economies’ progress toward the Bogor Goals in eight areas of the Osaka Action Agenda.⁴ I found that 13 economies differed greatly in their achievement and 8 achieved much less with regard to the Bogor Goals. They may be treated differently according to their extent of liberalization and facilitation. The six sensitive areas suggested by Leaders above are consistent with my findings. The concise and pinpointing ways of addressing achievements will be closer to “negative list formula” that I suggested earlier.⁵

Lastly, I would like to stress the importance of “individual assessment” and “make it public outside APEC rather than peer review within SOM.” While the final report of the mid-term assessment tells us only the group assessment of the 13 volunteered economies, individual senior officials, both the 13 economies and the rest of APEC economies, have understood well how far they have progressed toward the Bogor Goals and how much remains to be done. It is no use keeping the “no name, no shame” modality, but make them known to outside APEC officials, such as ABAC and ASCC experts. APEC may keep its modality of non-binding nature and voluntarism but should open its review process to outside critics.⁶

ALTERNATIVE PROCESSES TOWARD FTAAP

For the past few years FTAAP has been “translated from an aspiration to a more concrete vision.” It is mainly because of strengthened US initiative in the TPP negotiation but partly

⁴ Yamazawa, Ippei, *A Quantitative Assessment of APEC’s Achievement towards the Bogor Goals*, presented at a seminar ‘APEC Japan 2010 Symposium’ organized by Japanese senior officials in Tokyo, December 2009.

⁵ Please refer for further detail Yamazawa (2011) chapters 2 and 4.

⁶ Only a few attempt have been conducted outside APEC official procedure to monitor and evaluate the APEC’s TILF process, including Feinberg and Zhao (2001) and Yamazawa (1998 and 2009).

because of the DDA negotiation has got halted for the past years so that the Plan B is still relevant. Last year APEC Leaders declared

FTAAP should do more than achieve liberalization in its narrow sense; it should be comprehensive, high quality and incorporate and address next generation trade and investment issues.

It should be pursued as a comprehensive FTA by developing and building on ongoing regional undertakings such as ASEAN+3, ASEAN+6, and TPP. To this end APEC will make an important meaningful contribution as an incubator of a FTAAP by providing leadership and intellectual input into the process. (Pathway to FTAAP, APEC/LM 2010c)

We ASCC members should monitor the progress of individual paths and advise so that they merge toward FTAAP. Otherwise, TPP and ASEAN plus will proceed separately so that two blocs will be formed dividing Asia and making “free trade in Asia Pacific” a mere dream. If APEC merely implements its new IAP process just as its predecessor in the past, it will not be an incubator of FTAAP. Let me overview their progress and clarify their major tasks.

ASEAN+3 and +6 have been examined together by a task force of member governments’ officials, following the suggestions of ASEAN+3 Summit and East Asian Summit. It was reported that China submitted a concept paper on East Asia FTA (EAFTA), while Japan submitted a concept paper on Comprehensive Economic Partnership for East Asia (CEPEA). The media make fun of their rivalry reflecting different perspectives on regional cooperation framework, which tends to impede their smooth conversion in future. However, as is apparently urged by the TPP negotiations, China and Japan made a compromise proposal at the last ASEAN +6 Economic Ministers’ meeting in Indonesia in August. They proposed ‘ASEAN + α ’, not specifying either +3 or +6 and set up three task forces on commodity trade, services trade, and investment in order to discuss the extent of tariff reduction and exception areas in detail. The task forces are to report to EAS in December so as to start negotiation in 2012.⁷ However, if the negotiation goes along their existing FTAs between ASEAN and plus 3, it is likely to remain at a lower level than TPP.

On the other hand, the TPP negotiation has tended to be constrained by domestic interests of individual participating economies. The United States, while taking initiative, faces difficulty in appeasing various interest groups at the congress. They are likely to reach only a broad agreement by Honolulu APEC in November and to extend its detailed negotiation until 2013, beyond the Presidential election in 2012. However, I am concerned with the possible conflict between TPP and ASEAN plus, that is, the fact that TPP excludes China, while ASEAN plus exclude the United States, which will cause difficulty in merging them in future. TPP with only current nine economy participation cannot achieve a sufficient scale merit. In order to invite ASEAN plus members, they need to introduce a flexibility clause, while keeping its high level FTA in principle.

Here I would like to stress that APEC can play a positive role in merging TPP and ASEAN plus. The new IAP Peer Review conducted currently by APEC SOM has a comprehensive coverage, including WTO plus areas and is close to the TPP’s high standard, except for its non-binding modality. APEC, with its two decade experience in ECOTECH and capacity building, helps developing economies to implement various facilitation programs, thus

⁷ *Nippon Keizai Shinbun*, August 7th, 2011 and *Asahi Shinbun*, August 14, 2011

inviting them to join high level FTAs. Above all APEC is their least common multiple, that is, includes all members of the Asia Pacific. TPP and ASEAN plus pull the Asia Pacific from above, while APEC pushes it up from behind.

Postscript

A senior Chinese participant supported my proposal but inquired about its feasibility. I appreciated his support and responded “it should be feasible. Otherwise APEC will be marginalized and end in a talk shop.” Let me add here how APEC can play its coordinator role. It will be achieved by the elaborate follow-up of the new IAP peer review process by Secretariat’s Policy Support Unit (PSU) and SOM’s continuous effort to connect the new IAP process with TPP and ASEAN plus negotiations.

As regards the follow-up of the new IAP process, PSU has the important job of organizing this process for effective liberalization and facilitation programs. It should not merely summarize individual IAPs but help them publicize commitments and achievements. A mapping exercise can be attempted to clarify the differences among the three. If necessary, ASC experts are willing to provide assistance. This will encourage SOM to get concerned about reducing differences of the three so that their possible convergence will be seen toward 2020. I expect the final assessment of the new IAP process dated in 2020 will announce the converging stage toward FTAAP.

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8. The Future of APEC and the Strategic Scenarios

Abstract

The paper focuses on APEC regional integration with emphasis on Trans-Pacific Partnership (TPP) towards FTAAP and the APEC vision (Asia Pacific Community). While the American dominance remains in Asia Pacific, China with its rapid growth has increasingly influenced regional institution building. The author argues that APEC must attach its importance to China's role in APEC regional integration. A Trans-Pacific agreement or FTAAP could be a genuine end for free trade Bogor Goal although an Asia Pacific Community is a longer term aim. As a platform or a bridge to FTAAP, the TPP could be an appropriate method to promote integration in the region. Taking a secret negotiating approach and deliberately excluding some APEC members is not in the spirit of the new century.¹

INTRODUCTION

The last 22 years have seen APEC go up and down on its track towards Bogor Goals. Generally, it seems successful in maintaining peace through summit diplomacy but some still despair for the future. Disappointing sentiments notwithstanding, APEC has done some valuable things. The vision of APEC community remains. It was initiated by the United States in 1993 and is now emphasized as an economically integrated community.² The U.S. has its capability to lead the process toward the community but China should have considered contributing more. This year marks the 20th anniversary that China joins APEC. When APEC started, China was not among the founders and most Chinese did not have personal phone—now nearly all Chinese people have cell phones. When China joined APEC, “outward processing trade” was just transferring to China from APEC members, now, 20 years later, China is supplying huge shares of intermediate inputs into producing sectors of its fellow APEC members.

APEC is now trying to build a trans-Pacific free trade agreement as a step to an economically-integrated APEC community. China, like many APEC member economies, has signed 10 FTAs and been negotiating others but in the early 1990s no FTA could be imagined. Diversity does not stall the APEC members to catch up with the integration pace through FTAs/PTAs

¹ This paper is a part of research in progress and the opinions expressed here are the author's only.

² Declaration of the 18th APEC Economic Leaders' Meeting: "The Yokohama Vision: Bogor and Beyond," Yokohama, Japan, November 13-14, 2010.

and even Viet Nam is pursuing a member of TPP. China should have considered joining in the negotiation.

The proliferation of FTAs/RTAs around APEC region has resulted not only from the global trend of regionalism but also from domestic policies, interest groups and the unilateralist way for trade and investment liberalization but the unilateralist way has been unacceptable by some members of APEC. Although the development gap could have some impacts on undeveloped economies, it is not an impediment to regional integration but new era needs new rules to regulate integration for the community of common interest. APEC needs new thinking to go forward. This presentation, therefore, tries to weave new developments and facts of the recently triggered process of APEC regional integration, particularly the Trans-Pacific Partnership (TPP) towards FTAAP into an argument that APEC in the 21st century and its regionalism should be a different concept than the thinking suggested in the 1990s'. Open regionalism is no longer a possibility to point to the way of designing FTAAP for the regional integration – specifically, its economic community. The process through TPP to FTAAP must be a process transparent. In nature, FTAAP is a free trade area that is to be a high standard FTA. As an FTA, its building process follows the steps of forming an official FTA. The secret negotiating approach and deliberately excluding some APEC members do not represent the new spirit of the new century. APEC survival depends on the new thinking about regionalism which is driven by a new approach for a binding regime towards FTAAP. This is not only a challenge but also an opportunity to APEC and its member economies including China.

This paper is in five parts. The next section provides a brief assessment of APEC development with emphasis on the complexity of current trade architecture. Then a new theme is touched on the China's access to APEC, the evolution of China's regionalism and its implications on Asia. The subsequent section discusses FTAAP and TPP. The final section considers China's choices, APEC's future and development scenarios for the economically integrated community, and presents some concluding remarks.

ASSESSMENT OF APEC DEVELOPMENT

The past 22 years have seen a dramatic transformation in the Asia Pacific region, a transformation never imagined when APEC was initiated at the end of 1980s. Since its establishment, APEC—and the whole of the Asia Pacific—has become a fast growing part of the global economy. Now the region with China and other Asian countries booming has been acknowledged as a driver of global economic recovery and will continue to be a driving force in years to come.

APEC's important achievement is the reduction in average applied tariffs from 15.4 percent in 1988 to 6.95 percent in 2008. Some APEC developing economies have drastic reductions, for instance, those of China have been reduced from 40.3% to 9.8% in 2010, Indonesia from 20.3% to 7.72%, the Philippines from 27.9% to 6.23%, Thailand from 40.8% to 11.83%. Since 1996, APEC trade regimes have been improved and become more transparent with tariff and customs information available online in most APEC economies. Intra-APEC trade in goods and services more than tripled between 1989 and 2003, and account for an increasing proportion of APEC economies' GDP from 13.8 percent in 1989 to 18.5 percent in 2003. (APEC Senior Officials Report 2005) Chinese diplomats regard APEC as the highest economic cooperation forum with the most comprehensive mechanisms in the Asia-Pacific region. China, as a member of the Asia-Pacific community, attaches importance to and

actively participates in APEC cooperation in various fields. The Chinese presidents have attended all the APEC informal leaders' meetings since the inception of APEC Summit. (He 2009)

The Bogor Goals set by APEC economy members in 1994 is significant with a common goal of free and open trade and investment in the Asia-Pacific region but its weakness is lack of concrete standard and specific requirements³. The Busan Roadmap designs a future picture and a way forward for the Bogor Goals but unsuccessful in defining the exact standards to reach the goal. The Ha Noi Action Plan did not become a successful one, either. But, there were 13 economies that passed the review in 2010⁴. It seems a significant achievement of the Bogor Goals but critics regard it as a game that developed economies played.

APEC region has experienced two financial crises, the 1997 financial crisis and the 2008 international financial crisis. The first one affected the process of liberalization because the developed economies were reluctant to give a hand, particularly the American reluctance to have a resolve. That was a frustration for APEC developing economies. The second one emerged from the US in 2008 and has had the adverse effects on APEC developing as well developed economies. The region has been slowly recovering from the crisis but pessimist sentiments have not been away. Luckily, some prognostication that the ever severe financial crisis could cause a war has not come true.

APEC observes special interest in FTAs/RTAs and the most influential proposals like the 'Asia Pacific Community', the 'East Asia Community' and 'Trans-Pacific Partnership' emerged and some ebbed away. No one can deny the argument that greater regional cooperation is consistent with integration theory but some APEC members are awaiting and seeing how to define an overall strategic coherence and an all-inclusive regionalism. While in the early 1990s there were only three FTAs in APEC (i.e., NAFTA, ASEAN and ANFTA), APEC EPG suggested in 1994 to unite those three FTAs into APEC. The suggestion actually echoed with the Bill Clinton's initiative to establish Asia Pacific Community (APC). The U.S. intended to institutionalize APEC to be a legally binding mechanism. Bogor Goals directed an unclear destination and thus APEC's trade agenda has floundered and the liberalization has almost lost an exact way to a free trade area. APEC governments have pursued bilateral and sub-regional FTAs. APEC has not yet been a trade institution mainly because of the fact that ASEAN has had its policy, which persisted in a coherent group that has one voice in APEC but refused to be under APEC, China at that time had some hesitation in joining a legal-binding regional institution and finally the conflict between the legalism the U.S. advocated and the Asian way led to trade liberalization.

Now in the second decade of the new century, Asia seems to have a new orientation to the American led Asia Pacific regionalism. The 1997 Asian crisis legacy to work together to sustain growth and stability by establishing FTAs/RTAs has been slowly eroded. The American "Back to Asia" has political economy impacts on Asia and the East Asian unity to addressing common challenges is meeting new challenge of leading issue about who will lead the regionalism, ASEAN or the U.S. Besides, China has completely abandoned old-fashioned thinking on the regionalism and been active in negotiating FTAs with APEC fellow

³ Andrew Elek: "The mid-term review of APEC's Bogor Goals," APEC Economies Newsletters, vol.9, No.5, 2005.

⁴ "The Yokohama Vision - Bogor and Beyond", Yokohama, Japan, 13-14 November 2010.

economies and those beyond APEC. It seems all the region has been prepared to accept a principled trade institution but the U.S. tries to go out to dominate rule-setting in APEC trading mechanism. The secret negotiation for a trans-Pacific free trade agreement does not help APEC to be a welcome trade system and possibly is an effort to marginalize China and others. The simplicity in the early 1990s just tried to include and adopt China has been gone. Things have been deliberately made complex now.

CHINA'S ACCESS TO APEC AND ITS REGIONALIST POLICY

China's APEC access is a milestone for China but also for the region. APEC is the first regional organization China ever participated in and China's access improved China's economic relations with APEC members and spurred China's connection with developing pace of regional economy. China's rapid growth and rise to be a second economy is closely connected with China's access to APEC and WTO.

Last twenty years saw China its rapid growth at an average annual rate of more than 9%. In 2010, China's GDP reached RMB39798.3billion (about US\$6.1228 trillion)⁵ and China becomes the second economy in the world. This has been in pace with its APEC and WTO accession as well as China's uneven path transiting from the rigid economic structures under a centralized system to a market economy with Chinese socialist characteristics.⁶ Besides, China and Asian countries "uphold the Asian spirit of standing on its own feet, being bold in opening new ground, being open and inclusive and sharing weal and woe."⁷

APEC members as well as others have been acting on China through foreign investment. China assimilated FDI from US\$ 0.916 billion in 1983 up to US\$105.7b in 2010.⁸ Those figures and resources have shown that China benefits from its opening policy and the rapid growth is closely connected with regional cooperation due to over 60% of external resources have been invested by East Asia and APEC member economies. This, in fact, has been the reality promoting Chinese economic cooperation and integration in East Asia and expansion to Asia Pacific region. Some steps observe the policy shift so that China seeks regionalism.

First, China access to APEC in 1991 was a primary trial to establish regional cooperation with a governmental-based regional organization and it was also a political byproduct for China breaking a sanction by Western countries because of the Incident occurred on 4 June 1989. This trial was significant to China because of strategic reform transiting from internal to external orientation, that is, the almost fulfilled domestic adjustment in the 1980s and then beginning with the 1990s the domestic reform turned opening to the outside. China was just seeking outward-oriented strategy not only for a specific region but also other regions and wanted it to be assisting to its reform. APEC with its not inward-oriented nature seems a just

⁵ National Bureau of Statistics of China: Yearly Dada 2010, <http://www.stats.gov.cn/english/statisticaldata/yearlydata/>.

⁶ The undergoing transition has been first from a backward agricultural society to an industrial society, second from a socialist planning economy to a market economy and third from a non-WTO country to a WTO country. What is impressive is that the transition did not cause some grave consequences as in the former Soviet Union, which disintegrated.

⁷ Xinhua (New China News Agency): A White Paper on China's Peaceful Development, Information Office of the State Council, Beijing, September 6, 2011.

⁸ The figure is collected from the website at <http://www.mofcom.gov.cn/aarticle/tongjiziliao/v/201101/20110107370784.html>.

response to China's seeking regional arrangement without a strict limitation. China really had a very good opportunity to rehearse how to seek benefits from basic regional cooperation with tariff reductions, non-tariff reductions, increasing transparency of non-tariff barriers, opening service market and etc. APEC is an arena important for China to participate in subsequent bilateral and multilateral cooperation.

Second, China's accession of the Bangkok Agreement (BA) in 2001 heralded a new step of China shifting forward to a protectionist bilateral FTA policy. As a preferential tariff agreement under the Economic and Social Commission for Asia and the Pacific of United Nations, BA is a longest existed PTA institution in Asia but mainly serves as a platform for the exchange of tariff concessions on goods among developing countries and this sort of a government-organized institution is comfortable for China because no serious conflicts exist between China and most BA members. Harish Iyer has pointed out that China entered the Bangkok Agreement with an offer of 739 items for general concession and an additional 18 items for special concession to least developed member countries (Iyer 25). This has a breakthrough and historical significance for the accession is a first event in China's tariff history. According to BA, China's offer is given a return with a preferential tariff rate and this is a first time China obtains a preferential tariff rate through tariff reduction talks. China's accession satisfied some special interest groups inside China who has been advocates supporting to strengthen China's relations with its traditional friends in the third world. Harish Iyer presented his comments that China's entry into the Agreement has brought with it several interesting possibilities and could have profound implications for trade in the region.

Third, China initiated an ASEAN-China Free Trade Area. China put forward a proposal to establish an FTA with ASEAN in order to allay ASEAN's concerns over China's growing competitive threat for foreign investments after its WTO accession. With that initiative, China proposed tariff reductions on 600 agricultural items for ASEAN countries and soon both sides decided to prepare for signing a Framework of Agreement on Comprehensive Economic Cooperation (CEC) including an FTA at the Phnom Penh ASEAN-China Summit and completed the signature at Vientiane Summit by the end of 2004. The procedure of tariff reduction officially kicked off from July 2005 and over 7,000 items have been on the list, starting a formal process for FTA between China and ASEAN. The more important is that both sides also signed an Agreement on Dispute Settlement mechanism of the Framework Agreement on CEC, which will be followed by an agreement on services. The FTA was officially launched in 2010 and the first year the bilateral trade almost reached US\$300b. The mechanism seems very straightforward and functional but this is an initial step for China to pursue a new regionalism-oriented policy.

Fourth, Chinese pursuit of economic regionalism has been parallel with improving political relationship. The relationship between China and most ASEAN members has been since the early 1950s experiencing some stages through rival against each other in the time of the Cold War, engagement, resuming diplomatic relations and gradually getting together for a vision of East Asia Community. The improvement of relations has generated an appropriate climate preserving East Asia integration process. China and ASEAN separately and jointly made every effort to push the movement smoothly forward. The interactive actions had been conducted in the 1980s including former China's Foreign Minister Wu Xueqian's visit to Indonesia with a low profile in 1985 and the 1989 Tokyo meeting between former Chinese Foreign Minister Qian Qichen and former President Suharto that heralded the resumption of the diplomatic relations between China and Indonesia. Singapore initiated a proposal in 1990

that China be accepted as an APEC member, which was regarded by China as a breakthrough to the June Fourth sanction. Soon China's foreign minister was invited to attend ASEAN ministerial conference in 1991 and China supported the ASEAN-initiated ASEAN Regional Forum and accepted the concept of security interdependence declared in the statement of that conference, indicating that China's diplomatic thinking was in transition. China tried to play some role beginning with 1996 ASEAN Regional Forum (ARF) annual conference when China put forward a new security concept, whose core thinking is to solve regional disputes and maintain peace through methods such as dialogue, consultation and negotiation, which are also requested for by ASEAN. China was not only to support ARF but to build confidence with ASEAN for a stable and peaceful East Asia. In 1997, China fully supported ASEAN's suggestion to set up a new mechanism "ASEAN Plus Three" and accepted ASEAN as a leading role to play in East Asia integration process. China has no longer looked at ASEAN as a part of western rival force. Therefore, stable peripheral regions, particularly in the region bordering with small and middle countries in Southeast Asia, will be clearly contributive to China's internal economic development program.

There are features of China's way towards regional integration process. First, the international background in the 1990s is unique and different from the previous time. China envisioned there is a possibility of neither a global sized war nor an all out military attack on China to happen between the post cold war period and the year of 2030. Although China upholds a multi-polar world, China does not want to challenge the United States as a dominant superpower and recognizes the fact that the United States can maintain its status over a long term (Jiang 1996). China's regionalism policy has thus been considered to take up in a new international situation, in which no direct confrontation between China and the current superpower the US. The new situation has been regarded as a good opportunity for China to utilize as a rare time in its history. Second, China has chosen a gradual approach to enter into regional cooperation. The gradual approach avoided a therapy shock way but fitting to China's reality. The gradualism way can be best explained with Deng Xiaoping's remark "groping for stones to cross the river." The approach was not only been used in the 1980s the first stage China drove the momentum of economic reform but also the second since the early 1990s China has been using to expand the reform from internal to external, suggesting bilateral FTA with neighboring countries and even those across the Pacific Ocean. The approach can be very pragmatic to secure and keep China's economic development process uninterrupted. China's FTA policy, therefore, has been quite flexible without strict preconditions to ASEAN but benefits, particularly to sub-regional ASEAN members. China needs to design and give a clear policy to clear away any suspicion, particularly at this time the East Asian integration has been drawn to a dilemma whether East Asia Summit or ASEAN Plus Three (APT) is more effective for the regional integration process to East Asia Community. Third, China's regional policy has been governmental- controlled but is effective. With a new policy going abroad in the end of the 1990s, Chinese government began to encourage state-owned companies to go beyond border and invest in Southeast Asia and other regions.

With access to APEC, China participated in APEC programs and played a role in maintaining regional stability. Economically, China's contribution to APEC's trade liberalization is the tariff reduction from the average rate 35% in 1995 down to 9.8% in 2010.⁹ China as an

⁹ China's National Media Office: China's Peaceful Development White Paper, Beijing, September 6, 2011.

important APEC economy member carried out a positive policy to diminish the negative effects of the international financial crisis and obtaining an extraordinary achievement in 2010 with its GDP reaching around US\$4.9 trillion and 9.1% growth. The booming China is affecting the regional trade architecture and Asia is facing change in its political and economic structure. China has never been hesitated to take part in a regional or a global organization and China plays a constructive and contributive role to international institutions including APEC.¹⁰ A rising China has been driving the APEC region to be the center of gravity of global economic and strategic weight. China wants to work together with the APEC members to create a future the region wants to have. The new realist theory argues that the emerging power(s) have difficulty in peacefully joining the current regional as well as global order. The liberalist advocates, however, have emphasized that economic interdependence would generate win-win results. This means regional states will pursue their national development policies through free market and multilateral trade system instead of trade protectionism, mutual confrontation and arms race. Historical facts reveal that the rise of the US at the end of the 19th century and early 20th century, the Japanese rise in the 1960s prove the peaceful rise feasible. China's contributions to APEC since its becoming membership have been the primary evidence that China is in a peaceful development. If the American policy "back to Asia" is predicated on liberalism, open and inclusive to China, China's peaceful development and rise can be more assured. Obama believes if both China and US can cooperate to meet challenges the win-win results can be realized (Obama's Speech at Tokyo, Nov 13, 2009. To be dynamic again, APEC needs China's active participation.

FTAAP AND TPP

The FTAAP idea was proposed by APEC's Business Advisory Council in 2004 but Robert Schollay's presentation to Phuket ASCC in 2003 lay the foundation of its theory and policy analysis.¹¹ The ABAC proposal was then regarded as the only means by which APEC could achieve Bogor goals adopted in 1994 with the target "free and open trade and investment in the region." The U.S. supported it and initiated the American version of the FTAAP at Ha Noi Summit in 2006. The FTAAP remained on the agenda of APEC Summit meetings in Sydney (2007), Lima (2008) and Singapore (2009). Although an analytical study by officials generated some positive suggestions, challenges do exist in creating the FTAAP (2008 ALEM Lima Declaration). For instance, the FTAAP should be a legally binding mechanism but APEC's approach is that of a voluntary, consensus-based decision making system. One observed that there is a set of 15 completed chapters for Regional Trade Agreements (RTAs) and FTAs that will promote high-quality RTAs/FTAs and greater consistency and coherence among these agreements in the region (Bosan and Ha Noi Declarations). But now the Obama Administration prefers to participate first in the Trans-Pacific Partnership (TPP) Agreement and next step is the FTAAP. The TPP agreement negotiations have gone through eight rounds and the ninth is scheduled for October 2011. U.S. participation is an important strategic action, which indicates a strategic adjustment of US trade policy on regional cooperation and signals its new trade negotiation fashion from the previous bilateral approach.

Like others, China pays close attention to the Trans-Pacific Partnership (TPP). Although former United States Trade Representative (USTR) Susan Schwab had an announcement that

¹⁰ Ibid.

¹¹ Robert Schollay: Proliferation of RTAs and the Future of Asia Pacific Economic Integration, ASCC meeting in Phuket, May 26—28, 2003.

the United States was beginning negotiations to enter into the Trans Pacific Strategic Economic Partnership Agreement almost two years ago (Vaughn 2008), President Obama's announcement in Tokyo on November 13, 2009 that the United States would engage with the Trans-Pacific Partnership in a new effort toward regional economic cooperation in the Asia-Pacific Region had a special and significant implication. There are some special reasons for the American engagement with an already running regional trade arrangement TPP.

First, the Obama Administration has a pragmatic intention to seek American interest. At this moment that the international financial crisis has still haunted but not yet totally passed away, Obama Administration believed it the best option to take some concrete action using TPP to increase jobs at home, eliminate domestic complaints through dramatically increasing American exports to the Asia-Pacific.¹² It is understandable that national interest lies at the core of a country's strategy governing the state's foreign policy. President Obama stresses the US national interests while dealing its relations with China. (Obama Speech in Tokyo on November 13, 2009) China has seemingly learnt from the American capitalist way and emphasized national interests as the "highest principle" governing country to country relationships. The assumption seems to be that, once countries start to deal with each other based on their own national interests, the bilateral relations will be shining, regional and global peace will be realized. But this seems to remind us of the other assumption of political realism that power defines the interest and therefore the conflict is unavoidable. The inference may be conducted that where starting point overemphasizes its own interest the motivation will often be questioned and mutual trusts will be discounted. Balancing mutual interests needs to be considered for starting TPP negotiating agreement by what is regretful is lack of transparency.

Second, the United States wants to create a high quality FTA as an example to substitute Asian model, which has been regarded as a lower standard (Cutler 2009). By crafting a FTA standard, the US wants to set an example for the region to follow the American-created model in the process of regional integration. This may reflect US fears that the 30 some FTAs in APEC and the nearly 70 FTAs being negotiated will generate a spaghetti bowl of low level trade groupings that could harm U.S. trade interests. A primary factor to be supported by a mix of the American bipartisanship, various interest groups and federal government is of a comprehensive agenda in TPP including service trade, intellectual property, labor standard, digital data from movement through internet, state owned enterprises (SOEs) and others. These elements have not all been included in those completed bilateral FTA agreements the US signed with other partners. As a matter of fact, not all those bilateral FTA agreements have significant trade effect but sometimes the U.S. side tends to politically consider, and even to have security consideration. A high quality agreement would be welcome but should not be politicized.

Third, the US fears the building Asian trading bloc would exclude and at least marginize the U.S. Since the middle of the 1990s, RTAs/FTAs have been organized in East Asia and some have increasing influences over regional integration, in particular, ASEAN Plus Three (APT), East Asia Summit (EAS), ASEAN Plus Ones and also some other plans such as East Asia Free Trade Area and East Asia Community. Obama Administration and American commerce circles have been watching what East Asian are doing. They are worrying about trade and

¹² Kirk, Ron. Remarks by Ambassador Ron Kirk at 7th Annual U.S.-Asia Pacific Council Washington Conference, Washington, DC, May 6, 2010.

investment transfer effects that will affect their opportunities doing business in Asia. While first advocating FTAAP and now TPP, Dr. Bergsten has worries over a line down the middle of the Pacific. His position is that the American participation of TPP would engage the United States fully with the Asians and reducing the risk to the United States, both in economic and foreign policy terms, of an exclusive Asian bloc (Bergsten 2009).

Fourth, the United States wants to deter China and tries to continue playing a leadership role. China's rise triggers a debate on regional leadership issue along with the transformational power. China's drastic growth becomes a spur of neighboring diplomacy and the launch of China-ASEAN free trade area in 2010 pulls close relations of both sides. The US as a dominant role fears the dominance to be a history and believes TPP would be a better selection to prevent China from being a leader in East Asia.

Fifth, the United States wants to use TPP as a springboard to push FTAAP into reality and maintains its leadership in the process of regional integration in Asia Pacific. The American approach to FTAAP through TPP may be a good approach but 15 chapters for RTAs/FTAs still have their positive connotations for creating high quality FTA for Free Trade Area of the Asia-Pacific as a long-term prospect.

In a word, the United States' participation in the TPP is a significant event. This is mainly because the United States is an important trade partner for East Asia as well as a military power with an important role in regional geopolitics. Now there are already four members (Singapore, New Zealand, Brunei, Chile) while another five are ready for participation (Australia, Malaysia, Peru, the United States, Viet Nm). The nine countries have wrapped up the eighth round negotiation and it seems there were some opinions in disparity but the participants have been active. A broader membership has been encouraged but only Japan at this moment seems expected to join in the near future.

CONCLUSION: APEC'S FUTURE AND DEVELOPMENT SCENARIOS

APEC has done some valuable things for regional trade but for the last decade has been at a near standstill. Many times some countries tried to trigger a new passion to push APEC forward but have little advance. With the U.S. enthusiastic in pushing TPP and FTAAP, APEC may have a new horizon.

There may be three options for the future of APEC should the region not have a TPP and FTAAP. The first is a network of bilateral and multilateral FTAs. This network could also be called a comprehensive but overlapping FTAs. The second is to have a major or leading FTA group and this one plays a role as a hub, which would gradually abstract others into a final large group. The third is based on Bogor Goals to seek a big step toward trade liberalization. All these choices could not be good because it does not want to make a complete reform over APEC forum, a non-binding forum. The thinking in the 1990s to set up APEC should change to meet the new age's requirement. TPP may be a good scenario but its secret approach seems hard to understand. APEC and the regional prosperity based on healthy trade system cannot be maintained without China. China's development is inseparable from its friendly cooperation with the outside world, in particular, the APEC and fellow member economies.

With its access to APEC in 1991 and to WTO in 2001, China has been adjusting itself to regional and global environments and forging its integration policy. The guiding principles

for the adjustment are to accelerate the opening of its economy to the outside world to introduce foreign technology and know-how, develop foreign trade, and promote "sound economic development."¹³ China aims to further strengthen the multilateral trading system and at the same time China has been intensifying its pursuit of bilateral/regional free-trade agreements with some of its trading partners, which can complement the multilateral system. China intends to maintain a stable relationship with its peripheral countries and to be an accountable builder contributive to regional institutions. This is logical because that an FTA can provide an institutional guarantor to the development of bilateral/regional trade, maintenance of economic relations and benefit businesses and consumers in the participating countries and economies, by helping expand trade, achieve market diversification, reduce consumer prices, and lower producer costs; and drive economic growth and create new job opportunities. It appears that all countries and economies that have concluded bilateral/regional FTAs recognize China as a market economy. China has therefore taken pragmatic steps to establish bilateral/regional FTAs/RTAs with some trading partners. It is therefore that mechanism is necessary for the APEC trade liberalization. Open regionalism is hard to further push.

China has had a very supportive policy to East Asia integration through ASEAN Plus One, Plus Three and East Asia Summit. Vice President Xi Jinping appreciated Japanese proposal on East Asia Community¹⁴. Unfortunately, former Prime Minister Hatoyama stepped down but that does not mean that Japan will completely depend on the U.S., particularly at the time the U.S. has to deal with its own economic issues. East Asia cooperation should be based on Ten plus three (ASEAN 10 members plus Japan, Republic of Korea and China). It seems at this moment that China is not very active to respond to FTAAP and TPP initiated by the US. China dislikes using cold war mentality to organize a regional trade group. China prefers to participate in some fields like trade, financial projects or currency cooperation to construct a stable peripheral region, seek open markets that will fairly treat China's goods and welcome Chinese investment. Functional and pragmatic cooperation is in the first priority of China's external cooperation but China is cautious about some plans that would be inclined to or related to security reassurance, collective security, anti-terrorist war, climate change and other non-economic issues.

It is obvious that China and US relations have been attached to a very important weight in East Asia and Asia Pacific regional cooperation. Obama administration has admitted China's position is significant in the regional and global economy. The bilateral relations, however, have some challenges, which mainly resulted from the new administration's diplomacy back to Asia, which has some decisive role affecting China's decision toward American FTA initiatives. China must have been cautious to some sensitive issues, particularly those possible policies which may be against China or will harm China's national interests. Generally or roughly at this moment, an argument is that either FTAAP or TPP is to point at China.

China supports ASEAN to play a leading role in the process of East Asia or Asia Pacific integration. This policy is regarded as fundamental policy that has been consistent with China's standing in with developing countries. China enhances the cooperation with ASEAN

¹³ Trade Policy Review Body: WTO's Trade Policy Review, WT/TPR/S/199, 16 April 2008, p 24.

¹⁴ Chines Vice President Xi Jinping Met with Japanese Prime Minister Yukio Hatoyama, in People's Daily, Dec. 15,2009, P.1.

in commodity, service, investment and economic technology and also China tries to supply aids and establish aid projects with ASEAN countries. All these efforts enhance the foundation of China-ASEAN cooperation. It is clear China would also seek developing countries to support China on the issues such as FTAAP and TPP. Meanwhile there are some challenges and difficulties in competition over scarce resources—such as oil and gas, water and food, and very sensitive issue over territory, particularly over maritime regions between China and other developing nations. Some ASEAN members seem to be worrisome about China rise and hope external force like the United States to come on in to balance China.

With the analysis above, the presentation would like to end with these policy suggestions:

First, the U.S. should have negotiated or at least consulted with China on the TPP issue. When she first visited Beijing as Secretary of State, Hillary Rodham Clinton used a Chinese saying “those who are in the same boat have to row in the same direction” to describe the unique relationship between U.S. and China. Recently, she unexpectedly places China among emerging partners¹⁵, raising China to a new level of American Asia Pacific strategy. We understand if those who are in the same boat are rowing in the same direction should have common goal. For the survival goal we should have effective cooperation at least in the field of economy at this critical juncture. It seems that American action to update TPP is to exclude China. China is more developed than some who are now among the negotiation table. It is time for the U.S. to translate its positive words into effective cooperation. TPP has been accepted as a pathfinder like ASEAN+3, ASEAN+6 and others toward FTAAP. APEC members on the track to FTAAP should be informed what happened and the U.S. should have consulted with China on the TPP issue.

Second, keeping positive posture to the US’ proposal would come up to Chinese interests. PM Wen Jiabao remarked that China would not only positively participate in and maintain international cooperation mechanism but also wants to play a constructive role for building international institution. China must have changed its seemingly reluctant manner for some new initiatives. Positive participation and consultation with some new initiatives should be beneficial to China’s national interests.

Third, regarding to FTAAP and TPP issues, China should start to invest in research. The U.S. must have had some wrong judgment on the TPP membership and therefore any limitation or discrimination will not benefit TPP members. China wants to be constructive, participative and contributive to regional and global organizations, and if China joins in the relevant negotiations, China can also be in a very early stage to submit its ideas to complement current negotiators’ suggestions.

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¹⁵ Hillary Clinton, America’s Pacific Century, in *Foreign Policy*, November 2011.

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9. Evolution of the Asia-Pacific Trade Architecture: Stocktake and Future Outlook

One of the key sets of questions underlying Asia-Pacific economic cooperation over the last decade has been over the nature and form of the regional trade architecture that would emerge from the Asia-Pacific “noodle bowl” of bilateral and plurilateral FTAs, and how that architecture would accommodate the separate impulses of East Asian and trans-Pacific economic integration.

Calls for East Asian economic integration took centre-stage in the wake of the East Asian economic crisis of 1997/98, and were quickly reflected in the proposal for an East Asian Free Trade Area (EAFTA) based on the ASEAN Plus Three group. The subsequent development of the so-called “ASEAN Plus One” FTAs provided a feasible way forward in the absence of a politically viable basis for integration among the major Northeast Asian economies, and entrenched the idea of East Asian economic integration as an ASEAN-centred process. Japan’s proposal for a Comprehensive Economic Partnership for East Asia (CEPEA), based on an ASEAN Plus Six group of countries that made up the East Asian Summit (EAS) at the time, provided an alternative configuration for a region-wide trade bloc. Since then the EAFTA and CEPEA initiatives have moved forward in parallel, but no agreement has been reached to commence formal negotiations in either case.

The trans-Pacific approach to regional economic integration, which appeared to have been eclipsed by the East Asian developments, was revived by the ABAC (APEC Business Advisory Council) proposal for a Free Trade Area of the Asia Pacific (FTAAP), which after some initial hesitation was strongly endorsed by the United States at the APEC Economic Leaders Meeting in Hanoi in 2006. At that time, the apparent clash between the East Asian vision embodied in the EAFTA and CEPEA proposals and the trans-Pacific vision reflected in the FTAAP was resolved in APEC by a compromise whereby APEC formally adopted a Regional Economic Integration (REI) agenda in which the FTAAP was recognized as a “long-term” prospect. The absence of a credible vehicle for the trans-Pacific approach to regional trade liberalization was remedied in 2008 by the emergence of the Trans Pacific Partnership (TPP) initiative, which formally involved converting a somewhat obscure trade agreement (the Trans Pacific Strategic Economic Partnership or TPSEP) among four small APEC member economies into a potentially much more significant region-wide trade agreement involving also the United States and Australia as well as Peru, Viet Nam and later Malaysia. The commencement of formal TPP negotiations in early 2010, and the openly

declared ambition to draw in further APEC members as participants, focused attention squarely on the TPP as a potential building block for the FTAAP and confronted other APEC members with the need to define their position toward this new development.

The 2010 APEC Economic Leaders Meeting appeared to mark an important step toward resolving the question of how these separate East Asian and trans-Pacific initiatives would be reconciled in promoting the evolution of the trade architecture of the Asia-Pacific region. In the leaders' 2010 statement the status of the FTAAP is elevated from that of a "long term prospect" to that of "a major instrument to further APEC's Regional Economic Integration (REI) agenda." The FTAAP is to be "translated from an aspirational to a more concrete vision." The leaders further declare that the FTAAP is to "be pursued as a comprehensive free trade agreement by developing and building on ongoing regional undertakings, such as ASEAN+3, ASEAN+6, and the Trans-Pacific Partnership, among others."

The leaders have thus unambiguously endorsed the FTAAP as the end-point to be reached in the evolution of the Asia-Pacific regional trade architecture. At the same time they have given equal endorsement to the EAFTA, CEPEA and TPP initiatives as the building blocks from which the FTAAP may be developed. In doing so they have clearly posed a challenge to the promoters of these three initiatives. If the TPP is to play the leading role in the genesis of the FTAAP it will have to attract additional participation from leading East Asian APEC members in both Northeast and Southeast Asia. In order for EAFTA or CEPEA to play that role ways will have to be found firstly to overcome the obstacles which have so far prevented those two initiatives from proceeding to the stage of formal negotiations, and ultimately to widen participation to include the rest of the APEC membership.

At the time of the 2010 APEC leaders' meeting it was arguably possible to put forward a reasonably clear assessment of the state of play in each of the three initiatives, the challenges that they each faced, and the factors that would be important in determining whether and to what extent those challenges would be overcome. Since then economic and political developments at the regional and global levels have changed somewhat the outlook for each initiative.

The paper will now proceed as follows. First a brief assessment will be presented of the state of play and outlook for each of the three initiatives as they appeared at the time of the 2010 APEC leaders' meeting. This will be followed by a discussion of developments in these initiatives in 2011, as well as implications for these initiatives of developments in other arenas.

ISSUES IN THE EVOLUTION OF EAST ASIA'S TRADE ARCHITECTURE

The ASEAN Plus Three (APT) group, formed in the aftermath of the East Asian economic crisis and comprising the ten members of ASEAN plus China, Japan and Korea, remains one of two groupings whose agenda focuses on region-wide economic integration in East Asia. Understandably, in view of its origins in the East Asian response to the crisis, the APT agenda has focused strongly on monetary integration. The main products of this focus have been the Chiang Mai Initiative (CMI) and its subsequent multilateralisation, and the rather less well defined Asian Bond Market Initiative (ABMI). There has also been ongoing discussion in think tank on the possibility of creating an "East Asian currency unit" as a unit of account in East Asian economic transactions, and possibly also some form of exchange rate

coordination. Trade was also included in the APT agenda at an early stage, via the proposal for an East Asian Free Trade Area (EAFTA). Studies on this proposal by both an East Asian “Vision” Group and successive study groups have resulted in recommendations that EAFTA should have a central role in East Asian economic integration, and working groups have been formed to prepare the way for eventual negotiations. Conceptually, the establishment of EAFTA could be viewed as broadening the integration achieved within ASEAN through the ASEAN Free Trade Agreement (AFTA, later known as the ASEAN Trade in Goods Agreement, or ATIGA), to incorporate the three major Northeast Asian economies, China, Japan and Korea. It was obvious from the beginning that establishment of a viable basis for economic integration among these three Northeast Asian economies would be among the most difficult challenges to be faced in achieving this transition, given the longstanding political and economic sensitivities and antagonisms in relation between them.

In moves that could be interpreted partly as ways of sidestepping the issue of economic integration between themselves, and partly as expressions of the rivalry between them, the three major Northeast Asian economies, China, Japan and Korea, each focused in the early years of the twenty-first century on establishment of their individual “ASEAN Plus One” FTAs with the ASEAN group. The successive establishment of the ASEAN-China FTA (ACFTA), ASEAN-Korea FTA (AKFTA) and ASEAN-Japan FTA (AJFTA) was accompanied by entrenchment of the understanding that ASEAN should play the central and leading role in East Asian economic integration. For ASEAN this understanding took on something of the character of a fundamental non-negotiable principle, while for the three Northeast Asian economies it was a convenient mechanism that allowed them to avoid resolving leadership issues among themselves.

Concerns over the potential dominance of the APT group by China, especially on the part of Japan, were one of the motivations behind the decision to establish an East Asian Summit (EAS) with expanded membership. Japan is known to have favoured inclusion of the United States as a foundation member of the EAS, but in the end the East Asian economies looked south and west for the expanded membership of the EAS, by including Australia, New Zealand and India in an EAS group that has also been known as “ASEAN Plus Six”. ASEAN subsequently moved to conclude “ASEAN Plus” FTAs with the additional three members of the “ASEAN Plus Six” group, leading to establishment of the ASEAN Australia New Zealand FTA (AANZFTA) and the ASEAN-India FTA. The “ASEAN Plus Six” group has thus emerged as an alternative to the APT group as the vehicle for region-wide economic integration in East Asia. It has been generally understood that Japan prefers the “ASEAN Plus Six” group for this role while China prefers APT.

The economic agenda of the ASEAN Plus Six group centres on the concept of a Comprehensive Economic Partnership for East Asia (CEPEA), strongly promoted by Japan and supported by a substantial Japanese financial commitment to a CEPEA-related research programme implemented through the Economic Research Institute for ASEAN and East Asia (ERIA), located alongside the ASEAN Secretariat in Jakarta. The CEPEA concept includes an FTA among the ASEAN Plus Six members. Where the APT focuses on monetary integration as a key complement to regional trade and investment liberalisation, CEPEA places more emphasis on development of regional infrastructure and supply chain connectivity. ERIA’s research agenda also includes a strong emphasis on supporting the realization of the ASEAN Economic Community (AEC).

For some time the work programmes associated with the EAFTA and the CEPEA FTAs proceeded separately and in parallel, each with their own working groups, which not surprisingly had overlapping agendas. In 2009 a decision was taken to merge the working groups for the two initiatives. ASEAN was given the responsibility of bringing about this merger of working groups. Progress on the merger has been slow.

Two issues stand out in assessing the prospects of moving forward to establish either the EAFTA or the CEPEA. These are, first, the establishment of a feasible way forward to achieving economic integration in Northeast Asia, and second, the role of ASEAN as leader of the process.

The three major economies of Northeast Asia account for around 90% of East Asian GDP, and the trade flows between them are the largest and most important in East Asia. The lack of economic integration arrangements among these three economies thus stands out as a major gap in the matrix of East Asian bilateral trade flows covered by preferential trade agreements. Moving from the current array of “ASEAN Plus” FTAs to a single EAFTA or CEPEA FTA necessarily requires that this gap be filled, either as part of the process of establishing the EAFTA or CEPEA, or by the establishment of a Northeast Asian FTA as a prelude to the conclusion of either of the East Asian region-wide agreements.

In fact the issue of Northeast Asian integration has never been an entirely neglected facet of the East Asian regional integration process. Japan and Korea announced in 1998 that they would explore the possibility of an FTA between themselves, and FTA negotiations subsequently commenced, although they were later suspended, reportedly over reluctance by Japan to open its agricultural market to Korean exports. It is known that more recently a “track two” study has been completed of a possible China-Japan-Korea (CJK) FTA, and that studies have been undertaken in both China and Korea on a possible China-Korea FTA.

The obstacles, either to a CJK FTA or to agreeing terms for trade liberalisation between China Japan and Korea in the context of EAFTA or CEPEA, remain formidable. The political sensitivities in relationships between the three countries are well known. In each country the perceived competitive threat to domestic industries represents a further serious political economy difficulty. Japan and Korea, for example, are concerned about the impact on their agricultural sectors, while China and Korea are concerned about the impact on some of their manufacturing industries, for example the motor vehicle and chemical industries in China.

A recent development that injects a new potential dynamic into the Northeast Asian equation is the conclusion in 2010 of an Economic Cooperation Framework Agreement (ECFA) between China and Chinese Taipei, which is perceived in some quarters in Korea in particular as a significant competitive threat because of direct competition between Korea and Chinese Taipei in the Chinese market. Reports from Korea towards the end of 2010 indicated that Korea may be leaning toward moving immediately to negotiate an FTA with China, rather than wait for a CJK accommodation. Such a move by Korea would not be welcome to Japan, which would then find itself under pressure to counter this development by moving forward more quickly than it might wish on economic integration with China in particular but also with Korea. The conclusion of the ECFA thus appeared to have the potential to have a catalytic effect on economic integration in Northeast Asia, and consequently on the overall process of East Asian economic integration.

Another regional significance of the ECFA is that it may open the way for greater participation by both Chinese Taipei and Hong Kong, China in the process of East Asian regional economic integration. China has hitherto been strongly opposed to FTAs between Chinese Taipei and other Asia-Pacific economies, but it has reportedly signaled that following the conclusion of the ECFA it will no longer oppose such FTAs, provided the formula followed in the WTO, where Chinese Taipei participates as a separate customs territory, is also observed in each FTA, and provided that Chinese Taipei's partner in each case already has a bilateral FTA with China. Relying on this signal, Singapore is reported to have moved immediately to revive an earlier aborted proposal for an FTA between itself and Chinese Taipei.

Opening participation in East Asian regional economic integration processes to Chinese Taipei and Hong Kong, China would be a significant development. Both Chinese Taipei and Hong Kong, China are major players in East Asian trade, and their exclusion to date from both the EAFTA and CEPEA processes has represented a substantial limitation on the scope of the economic integration that the region has been able to contemplate.

Increasing recognition of the centrality of progress toward economic integration in Northeast Asia for the overall process of East Asian integration has perhaps inevitably been accompanied by an increasing tendency to question both the capacity and appropriateness of ASEAN in the role of leader of the East Asian process. Acceptance of ASEAN leadership and "ASEAN centrality" has hitherto suited the purposes of both ASEAN and the Northeast Asian economies. As and when concrete steps begin to be taken to break the impasse in Northeast Asia the centre of gravity of the East Asian integration process is however likely to shift to Northeast Asia and there would be a natural tendency for leadership of the process to shift with it. ASEAN may find it difficult adjust to this shift. There have been questions however, not least within ASEAN itself, over whether ASEAN has sufficient internal cohesiveness to form a united view on how to move East Asian integration forward, especially when the principal issues being addressed concern integration in Northeast Asia. The incentive for ASEAN to move from the current array of "ASEAN Plus" FTAs to an EAFTA or CEPEA FTA may also be questionable, since the move may involve some erosion not only of ASEAN's leadership status but also of its preferential access to the markets of its APT or EAS partners.

ASEAN members have recognized that achieving greater progress in integration among themselves is both important to the credibility of ASEAN's role as leaders in the East Asian integration process, and also necessary for their own successful adjustment to a possible East Asia-wide trade agreement. This recognition provided an important element in the motivation for the decision by ASEAN members to commit themselves to establishment of the ASEAN Economic Community (AEC), essentially an ASEAN single market, by 2020. The target date for achieving the AEC was later brought forward to 2015. It may be rational for ASEAN to prioritise establishment of its own ASEAN Economic Community over EAFTA or CEPEA, but this may not be helpful in moving the East Asian integration process forward in the short term.

Another background issue that has taken centre stage is how East Asia should manage the implications of integration for its relationship with the United States—a crucial export market, a major source of foreign direct investment, and a key player in regional security. The United States, for example, cannot be expected to welcome being discriminated against by an

emerging economic bloc. One solution often suggested in East Asian circles is the adoption of a sequential approach, whereby EAFTA is launched first, to be followed by a move to CEPEA once EAFTA is operating successfully, with establishment of an Asia-Pacific-wide FTA as the final step (the Free Trade Area of the Asia Pacific or FTAAP, discussed in the next section of this paper). It may not be realistic, however, to expect that the United States will readily accept a sequencing that would require it to suffer discrimination for several years while East Asian integration is being established, before finally being invited to join the process itself.

EVOLUTION OF THE TPP AND ITS ROLE IN ASIA-PACIFIC ECONOMIC INTEGRATION

As noted above, the TPP process developed out of an FTA between four small Asia Pacific economies, the Trans Pacific Strategic Economic Partnership (TPSEP) or “P4” agreement between Singapore, Chile, New Zealand and Brunei.¹ This relatively obscure agreement was transformed into a potentially major element in the development of the Asia-Pacific regional trade architecture by the United States’ announcement in September 2008 that it would negotiate to join the TPSEP. In November 2008, Australia and Perú announced that they too would join negotiations to forge an expanded agreement, which from that time has been known simply as the Trans-Pacific Partnership or TPP. After a delay following the 2008 U.S. presidential election, in late 2009 President Barack Obama confirmed that the United States would “engage” in shaping the expanded agreement. At that time the TPP was the first significant trade initiative to which the Obama Administration had committed. In March 2010, TPP negotiations formally commenced among the United States, Australia, Peru and the four founding members of the TPSEP—Singapore, New Zealand, Chile and Brunei—with Viet Nam participating as an observer. A quick pace in the negotiations was set from the beginning, with four negotiating sessions held in 2010. At the third session Malaysia announced that it would join the negotiations as a full participant.

Of the 36 bilateral relationships or dyads among the existing 9 TPP participants, only 11 are not already covered by an FTA relationship, and the latter are generally of only minor trade importance to at least one and sometimes both of the countries involved. Figure 9-1 summarises the extent to which bilateral trade between TPP participants is already covered by FTAs. Malaysia, New Zealand, Viet Nam, and Brunei are the participants for whom the TPP as now configured offers the most significant “prizes” in the form of new FTA relationships with the United States, but these four economies account for only a tiny share of U.S. trade. In fact the 7 economies that joined the United States in the opening TPP negotiations at the beginning of 2010 account for only 4% of U.S. trade. Thus, in establishing a limited number of new bilateral FTA relationships, the TPP does not signify a dramatic increase in the overall coverage by FTAs of trade between the current participants, although it may of course also extend the trade coverage of some FTAs and is intended to add new dimensions to some if not all of them. In particular, trade potential with TPP members clearly does not explain the level of commitment of the United States to the TPP.

¹ For background on the genesis of the P4 and its evolution, see Scollay (2010).

Figure 9-1. Coverage of Existing FTAs of Bilateral Trade Between TPP Participants

	USA	Australia	Singapore	Chile	Peru	NZ	Viet Nam	Brunei	Malaysia
USA		<i>Bilateral</i>	<i>Bilateral</i>	<i>Bilateral</i>	<i>Bilateral</i>				
Australia	<i>Bilateral</i>		<i>Bilateral</i> <i>AANZFTA</i>	<i>Bilateral</i>		<i>Bilateral</i>	<i>AANZFTA</i>	<i>AANZFTA</i>	<i>AANZFTA</i>
Singapore	<i>Bilateral</i>	<i>Bilateral</i> <i>AANZFTA</i>		<i>TPSEP</i>	<i>Bilateral</i>	<i>Bilateral</i> <i>TPSEP</i> <i>AANZFTA</i>	<i>AFTA</i>	<i>AFTA</i>	<i>AFTA</i>
Chile	<i>Bilateral</i>	<i>Bilateral</i>	<i>TPSEP</i>		<i>Bilateral</i>	<i>TPSEP</i>		<i>TPSEP</i>	
Peru	<i>Bilateral</i>		<i>Bilateral</i>	<i>Bilateral</i>					
NZ		<i>Bilateral</i>	<i>Bilateral</i> <i>TPSEP</i> <i>AANZFTA</i>	<i>TPSEP</i>			<i>AANZFTA</i>	<i>TPSEP</i> <i>AANZFTA</i>	<i>AANZFTA</i>
Viet Nam		<i>AANZFTA</i>	<i>AFTA</i>			<i>AANZFTA</i>		<i>AFTA</i>	<i>AFTA</i>
Brunei		<i>AANZFTA</i>	<i>AFTA</i>	<i>TPSEP</i>		<i>AANZFTA</i>	<i>AFTA</i>		<i>AFTA</i>
Malaysia		<i>AANZFTA</i>	<i>AFTA</i>			<i>AANZFTA</i>	<i>AFTA</i>	<i>AFTA</i>	

The significance of the TPP arises from its potential as a stepping stone to the FTAAP. It is the inclusion of the additional participants that may be attracted into the TPP in future, especially major economies in Northeast Asia, which offers the greatest economic benefit to the United States and several other current participants. Strategically, as Barfield and Levy (2009) explain, the TPP is intended by the United States as the vehicle for maintaining the trans-Pacific link as an integral element of the Asia-Pacific regional trade architecture, an objective shared by the other participants. In effect, the TPP is today's expression of the original APEC rationale of ensuring that there is no "line drawn down the middle of the Pacific."

The TPP is formally open to additional participants. The current participants have established ground rules that new participants are expected to accept. It is common ground among existing participants that the TPP should be a "high quality" "twenty-first century" agreement, and this is interpreted among other things to mean that no issues should be excluded from the negotiations, even if agreement cannot ultimately be reached on all details, including product coverage of the market access provisions. Potential new participants are permitted to attend negotiations as observers for a maximum of three negotiations, after which they are expected to become full participants in order to continue attending.

The TPP negotiation, like any trade negotiation, inevitably involves issues that are sensitive to a greater or lesser degree for one or more participants. Likely examples include market access for sugar, dairy products, beef and textiles and clothing for the United States; pharmaceutical purchasing systems for Australia and New Zealand; government purchasing for Malaysia; and intellectual property protection issues for most participants. By the standards of other FTA negotiations the challenges posed by the individual sensitive issues in the TPP do not appear severe, given the extent to which issues have already been resolved in previous bilateral FTAs, and given also what seems to be a broad consensus among participants that product and issue coverage in the TPP should be as comprehensive as possible, and that there should be no *a priori* exclusion of any issue. The principal source of difficulty is likely to be the

relatively small economic gains anticipated for most participants from the TPP if its membership remains as it is, which implies correspondingly small incentives for the participants to reach agreement on sensitive issues, unless they factor in the potential larger gains from the uncertain prospect of future expansion of the TPP membership.

A key architectural issue that has also had to be faced in the TPP negotiations is whether the TPP should replace the existing bilateral agreements among the participants, or complement them and if so on what basis. This issue of course arises in any initiative that seeks to create a large plurilateral agreement among countries that are already connected by bilateral agreements. It had to be addressed in the negotiations for the Free Trade Area of the Americas (FTAA) and it will also have to be addressed in any future EAFTA or CEPEA negotiations. It was one of the main issues addressed in the initial rounds of TPP negotiations. The extent to which the original “P4” agreement and the participants’ other existing agreements, both with each other and with other partners, would be used as sources for text of the TPP, has also been an issue to be gradually resolved in the course of the negotiations.

The emergence of the TPP also helped to bring the issues surrounding the future of East Asia’s relationship with the United States sharply into focus. By throwing its weight behind the TPP the United States gave a clear signal of its determination to maintain and deepen its economic engagement with East Asia. Petri (2010) has highlighted the economic imperative underlying this stance, deriving from the need for a sharp increase in U.S. exports to re-balance the U.S. economy and restore sustainability in its external position, with East Asia projected to account for by far the largest share (41%) of that increase in exports over the next five years. The strength of this imperative, and the lack of clear alternative routes toward the objective perhaps accounts for the extent of resources devoted by USTR to a domestic outreach programme – described by Elms 2010 as “unprecedented” – to build support for the TPP.

At the same time the experience of the global financial crisis served to underline for East Asian economies the extent of their ongoing economic interdependence with the United States (and with Europe), contradicting suggestions that the rapid expansion of intra-East Asian indicated that East Asia has been successfully “decoupling” itself from the United States and Europe. Re-assessment of East Asia’s economic relationship with the United States was in turn linked to broader questions of the future role of the United States in East Asia, which had come into sharper focus in regional debates sparked by the proposals in 2008 and 2009 of Australia’s then Prime Minister Rudd for an Asia-Pacific Community and by Japan’s then Prime Minister Hatoyama for an East Asian Community, with sharply divergent views being expressed even within the normally cohesive Singapore policy establishment (Tay 2010; Koh 2010).

Concern that the United States remain engaged in East Asia—arising from renewed recognition of the importance of economic relationships and the anxiety of several East Asian governments about keeping the U.S. regional security presence strong—began to gain ground relative to the desire to build a regional economic identity independent of U.S. influence. Support began to grow—not least in Japan following the replacement of Mr. Hatoyama by Mr. Naoto Kan as Prime Minister—for the view that the apparent desire of the United States to re-engage with East Asia should be encouraged. An important upshot was the announcement in late 2010 by ASEAN Foreign Ministers of a decision to invite the United States (along with Russia) to join the East Asian Summit. It remains to be seen whether this

development will have any influence on the evolution of the ASEAN-Plus trade arrangements. In the meantime the deposing of Mr. Rudd and Mr. Hatoyama from their respective prime ministerships has been accompanied by an ebbing of the attention paid to the Asia Pacific Community and East Asian Community concepts.

There is little doubt that the success or failure of the TPP will ultimately be judged according to whether in practice it has a catalytic effect on progress toward establishment of the FTAAP. Progressive attraction of new participants is essential if the TPP is to successfully play this role. The importance of potential future participants implies that there is an interesting strategic game surrounding the TPP negotiations.

On the one hand, existing participants have an incentive to consider the interests of potential additional participants. This derives from the peculiarity in the TPP case that the expected economic benefits of a new trade agreement among the current TPP participants are relatively small, and the larger economic and strategic benefits that are expected to make the exercise worthwhile depend on the future attraction into the TPP of significant new members, especially from East Asia.

This issue is relevant to TPP design choices. In particular it is well known that the United States has a “template” that it seeks to apply to all its FTAs, as it has done in its four bilateral FTAs with current TPP participants, with only limited “customisation” to the sensitivities and circumstances of each partner. Furthermore, the template tends to become more demanding over time as it incorporates additional features that the United States secures in each new FTA, as has occurred with the KORUS FTA. On the one hand, there are signs that United States may resist major deviations from its template for the TPP. On the other hand, elements of the U.S. template are unpalatable to other TPP participants and, more important, basing the TPP rigidly on the template could make the TPP less attractive to additional participants in East Asia, thus reducing expected economic and strategic benefit for current participants. The intellectual property component of the U.S. template may be a sticking point for some potential new entrants from East Asia.

The negotiators thus face the challenging task of crafting an agreement that fulfills desires for a “high quality” agreement and satisfies the fundamental interests of current participants to an acceptable degree—in particular U.S. preferences to an extent sufficient to secure political acceptance in the United States—while avoiding features likely to impede expansion of membership.

Potential new members must also make choices. While the TPP is likely to be formally open to accession at any time, as was the case with the original “P4” agreement, the ability of acceding members to negotiate revision of the terms and conditions of the agreement will likely be limited. Their ability to influence the design of the agreement will be greatest if they participate in the current negotiations, which would allow them to exploit the bargaining power that derives from the incremental economic gains that would flow from their inclusion in the TPP. On the other hand, meeting the conditions required for participation in the TPP negotiations will often face them with the need to make decisions that are unpalatable in the domestic political context. This consideration appears to have deterred Canada from seeking early participation in the TPP negotiations and led to a polarizing debate in Japan.

During the latter part of 2010 a groundswell of opinion in favour of Japanese participation in the TPP began to develop within the Japanese business sector and large parts of the Japanese

policy establishment, reacting to the economic and political implications of the TPP as well as developments elsewhere such as the reaction in Northeast Asia to the conclusion of the ECFA between China and Chinese Taipei. In early October 2010 Japan's Prime Minister made a statement indicating that the Japanese government was seriously considering participation in the TPP, with a possible announcement to this effect to be made at the APEC Economic Leaders' Meeting in Yokohama. This sparked a furious response from agricultural interests in Japan, who mounted a fierce campaign against Japanese participation. In the event Japan's Prime Minister Kan announced a compromise outcome at the APEC Leaders' Meeting, whereby Japan would make its decision on participation in the TPP in mid-2011, and would work during the intervening period on policy measures to assist adjustment in its agricultural sector.

Japan's decision is important both for Japan and for the TPP's role as a stepping stone to an eventual FTAAP. In order for the TPP to fulfill this role it is clearly important that it should attract participation by the major Northeast Asian economies. Japan would be the first of these three economies to come on board, and its decision to join might also add decisive weight to Korea's incentives to participate. Elsewhere in East Asia the Philippines government under newly elected President Benigno Aquino had made statements indicating a serious interest in joining the TPP. This would leave Indonesia and Thailand as the two remaining ASEAN members of APEC yet to indicate a stance toward the TPP.

Looking further ahead the issue of Chinese participation looms as the ultimate challenge for realizing the strategic potential of the TPP as a step in the process towards an FTAAP. Since Chinese participation in the FTAAP is indispensable, there is a strong case for Chinese participation in the TPP if the latter is intended to form the basis of the eventual FTAAP. On the other hand both the United States and China will have reservations over early Chinese participation in the TPP. It is clear that Chinese participation would greatly complicate the task of the U.S. Administration in securing passage of the TPP through the U.S. Congress. From China's perspective the fact that it already has FTA relationships with seven of the nine TPP participants and is in negotiations for an FTA with an eighth (Australia) serves to underscore the obvious point that any decision about its TPP participation is essentially a decision about its trade and economic relations with the United States. China is likely to be wary of anticipated efforts by the United States to secure concessions that China has so far been resisting in bilateral and multilateral forums. At the same time there are risks in deferring Chinese participation. China will understandably wish to have a role in shaping any FTAAP in which it is to participate, and may well be inclined to resist proposals that a TPP in whose negotiations it has played no part should be accepted as the basis for design of the FTAAP. It is clear that China is watching TPP developments closely, and influential figures in China are known to have suggested that China should seriously consider participating in the TPP.

Korea is also known to be maintaining a close watch on the TPP. From one perspective the conclusion of the Korea-EU FTA and the prospective ratification of the KORUS FTA mean that Korea feels little pressure for early participation in the TPP. Decisions by Japan and China to participate in the TPP on the other hand would likely change the calculus of Korea's interest, and tip the balance in favour of Korean participation as well.

The difficulties in achieving economic integration in Northeast Asia will also be relevant here. As in the case of EAFTA and CEPEA, simultaneous participation of the three major

Northeast Asian economies in the TPP or subsequently in an FTAAP will imply a need for a viable basis to be found for economic integration among themselves.

DEVELOPMENTS IN 2011: PROGRESS AND EMERGING UNCERTAINTIES

By unambiguously endorsing the FTAAP as the eventual goal of regional economic integration in the Asia-Pacific, and by giving equal endorsement to EAFTA, CEPEA and TPP as avenues toward the achievement of that goal, the APEC leaders in their 2010 statement appeared to encourage the pursuit of each of these three initiatives, with the relative influence of each on the ultimate shape of the FTAAP likely to be dependent on the extent of progress made in each case. The competitive dynamic thus established has become an obvious factor influencing the evolution of the East Asian initiatives in particular during 2011. The outlook for the three initiatives has also been influenced by new developments elsewhere.

One such development that may have far-reaching repercussions has been the spectacular failure of economic leadership in the political systems of the European Union and the United States over issues relating to government deficits and debt, and accompanied in the latter's case by a perception that economic decision-making is now paralysed by political gridlock, with impacts on international relationships now carrying even less weight than previously in the deliberations of the US Congress on economic matters. This development will have strengthened already widespread perceptions that the passage of a TPP agreement through the US Congress is likely to be a very difficult and lengthy exercise with uncertain prospects of success. With the US President lacking Trade Promotion Authority, and having no prospect of securing it, there are likely to be also heightened concerns over the extent to which Congress is likely to insist on modifying any agreement that is reached. At the same time some informed observers in the United States continue to insist that the TPP will in fact be able to successfully pass the Congress.

These developments in the United States may in turn have a number of consequences for prospects of widening participation in the TPP. Some APEC economies that have been hesitating over possible TPP participation may be encouraged to think that nothing will be lost by holding back. New doubts are likely to be raised over the reliability of the United States as an economic partner, leading to increased emphasis on the risks rather than the benefits of economic interdependence with the United States. Despite continued emphasis by leading figures in the U.S. Administration on U.S. commitment to re-engagement with East Asia, perceptions that the United States has become less committed to its economic re-engagement with East Asia may grow at a time when there is a noticeable increase in East Asian suspicions that U.S. pursuit of the TPP is motivated more by the aim of dividing Asia rather than of promoting trans-Pacific economic integration (Cai 2011; Yamazawa 2011). To the extent that all this results in diminished enthusiasm in East Asia for economic engagement with the United States, widening participation in the TPP may become increasingly problematic.

The renewed economic disturbances in the United States and Europe during 2011 have also further underlined the stark reality that weak economic growth is the best that can be expected in both of these advanced economies in the immediate future, and that in the meantime the centre of global dynamism has shifted, perhaps irreversibly, to the emerging economies and to the East Asian emerging economies in particular, with China as the undisputed focal point of

this dynamism. These considerations are likely to concentrate the attention of East Asian policymakers on the arguments in favour of prioritizing East Asian integration.

The entry of the United States into the East Asian Summit group may also lead to some adjustments in perceptions in both the United States and East Asia of the importance of the TPP as an instrument of U.S. re-engagement with East Asia, especially among those who emphasise the security rather than the economic dimension of the need for that re-engagement. While the U.S. presence in the East Asian security architecture continues to be seen as essential by many East Asian governments as well as the United States itself, the admission of the United States to the East Asian Summit provides an alternative avenue for pursuing these interests without any necessary requirement to pursue economic engagement at the same time. Utilisation of the East Asian Summit as the forum for addressing security issues in East Asia is likely to be congenial to both the East Asia and the United States, in East Asia's case because it ensures that such dialogue takes place within an East Asian institution, and in the case of the United States case because it offers the opportunity for dialogue with India, which is not available for example through APEC. Some East Asian governments may also be inclined to promote the East Asian Summit as an alternative to the TPP as a vehicle for U.S. economic re-engagement with East Asia.

A fourth relevant development has been the dramatic collapse in early 2011 of any expectation that the WTO's Doha Round can be successfully concluded in the near future. This appears to have caused a decisive shift among opinion leaders towards the FTAAP as the most hopeful avenue for region-wide trade liberalization. In the survey of Asia Pacific opinion leaders reported in PECC's latest State of the Region report (PECC 2011), the FTAAP is ranked as the most important issue to be considered by APEC leaders at their Hawaii meeting, while the WTO Doha Round has slipped to third place. PECC reported that business respondents in particular "appear to have given up on the WTO Doha round, ranking it 12th out of a list of 23 issues, and instead placing top priority on what is seen by many as 'Plan B' – the FTAAP." This prioritization of the FTAAP is likely in turn to be reflected in increased focus on the three routes to its achievement endorsed by APEC leaders in 2010.

Meanwhile the pace of the TPP negotiations has been maintained or even increased in 2011. Eight TPP negotiating sessions have now been held, with one further round of negotiations, in Lima, remaining to be held before the APEC Economic Leaders' Meeting to be hosted by the United States in Hawaii in November 2011. As has been evident from early on in the negotiations there is no possibility that the final agreement will be concluded by November. Efforts are focused on reaching the point where an agreed outline of the agreement can be announced at the APEC meeting.

The TPP negotiations involve a considerable widening of scope beyond the range of issues covered in the original "P4" agreement (Lim 2011). Investment, financial services, electronic commerce, and telecommunications are issues being negotiated in the TPP that were not included in the "P4" agreement. TPP negotiators are also addressing a range of "horizontal" issues with the declared ambition that the TPP treatment of these issues should extend well beyond anything found in existing agreements. These issues include supply chain connectivity, competitive business development, small and medium enterprises (SMEs), and development. Transparency issues are also understood to be heavily emphasized in the TPP negotiations. There are other issues where the level of commitment being sought extends far beyond that found in the "P4" agreement. These include intellectual property, environment,

and labour. The latter two issues will be covered in the TPP in chapters in the main agreement, rather than the Environmental Cooperation Agreement and MOU on Labour that were attached to the “P4.”

Negotiating groups have been established to address a wide range of issues, including industrial goods, agriculture, textiles, sanitary and phytosanitary standards, services, investment, financial services, intellectual property, regulatory coherence, the environment, competitiveness, supply chain development, and small- and medium-sized enterprises, among others.

Approaches to the development of the TPP text have evolved gradually. Preliminary discussions between the original “P4” parties and the United States focused on the extent to which use could be made of the original “P4” text, which is still used as a reference point to some extent for chapters which are common to both “P4” and TPP. Subsequently participants have submitted a range of draft text proposals for many of the proposed chapters of the agreement, based on both on the texts of their own FTAs and their ambitions for improvement. The United States can be assumed to have put forward proposals based on its well-known “template” for chapters on issues such as environment, labour, intellectual property. Negotiations aimed at reaching consensus around agreed text are proceeding on a chapter-by-chapter basis, and the end result will almost inevitably be a hybrid of the various proposals put forward. Progress is being made in discussions to develop TPP rules of origin. It appears that the negotiators expect to ultimately reach agreement on a common text for all chapters of the TPP.

Indications are that so far the parties are adhering to the principle of being open to negotiation on all issues. No participant has yet taken an issue “off the table”, and the participants are maintaining the stance of requiring prospective new participants to accept that all issues must be “on the table” for negotiation.

The structure of market access commitments that will emerge from the negotiations is unclear at this stage. The United States has stated that it does not intend to re-open market access arrangements with its bilateral partners although it is having informal discussions with them on market access issues. It appears that other participants are likely to negotiate bilaterally with the United States. At the same time most other participants are understood to have made plurilateral market access offers on goods applicable to partners other than the United States. It remains to be seen how far it will be possible to consolidate the bilateral commitments into a common schedule of commitments. It may be that in the end the schedules of market access on goods will be a mixture of common and bilateral elements, as is the case in agreements such as the ASEAN-Australia-New Zealand FTA (AANZFTA) and the US-DR-CAFTA agreement. Acceptance of a mixture of common and bilateral commitments would ease the way for some exclusions, and the U.S. position of not re-opening existing bilateral market access arrangements would also appear to be inconsistent with a “no exclusions” approach, since exclusions exist in at least some of those bilateral agreements. Agreement that TPP services market access offers will be made on a negative list basis also applies acceptance of some exclusions. The parties are a long way from declaring final positions, and it remains to be seen what the outcome will be in practice. There is still scope to explore alternatives to exclusions from goods commitments, such as longer time periods for phasing out tariffs, special safeguards, transitional tariff rate quotas, and other mechanisms to facilitate adjustment.

There has been no further increase in the number of participating economies. Japan's decision on TPP participation remains pending. In the opening weeks of 2011, the issue of Japanese participation in the TPP became one of the most hotly debated topics in Japanese politics, as supporters of greater Japanese integration with the regional and global economies clashed head-on with defenders of the status quo, especially from the traditional agricultural interests. The picture was complicated by the weakness of Prime Minister Kan's DPJ government, and the prospect that its possible imminent collapse would preclude a decision to proceed with TPP participation. In March 2011 the debate was overtaken by the devastating Great East Japan Earthquake and tsunami that hit Japan, and the subsequent crisis at the Fukushima nuclear power plant. Faced with the enormous task of recovering from these disasters the Japanese government understandably announced that the decision on TPP participation would be deferred. The subsequent replacement of Mr. Kan by Mr. Noda as Prime Minister of Japan means that some re-assessment of Japan's position on the TPP is bound to occur and this will take time. The APEC Economic Leaders meeting in November looms as the next likely forum for Japan's announcement of its decision on the TPP. The deferral of Japan's decision on participation may also be encouraging other economies to adopt a 'wait and see' attitude.

The issue of Chinese participation in the TPP continues to revolve around the China-United States economic relationship and remains something of a dilemma. While it is clear that TPP developments continue to be closely watched in China, there are also signs of increasing signs of frustration in the commentaries of leading Chinese academics who cite the lack of access for potential participants like China to information on progress in the TPP negotiations as support for their contention that China is effectively being excluded from the TPP, and seem increasingly inclined to label the TPP as part of a U.S. strategy to "contain" China. (Cai 2011) In contrast to its attitude toward Japanese participation the United States has shown no sign of encouraging China's participation, which does nothing to dispel perceptions that the United States has a tacit preference for deferring the issue of China's participation until after the TPP negotiations have been concluded. At the same time representatives of some other TPP participants have made public statements strongly opposing any use of the TPP as a strategic weapon against China, and there is little doubt that other participants continue to regard China's participation as essential to fulfillment of the TPP's intended role as a stepping stone towards the FTAAP, and remain anxious to communicate this message to China. It is however an unfortunate reality that the entry of China into the negotiations as a full participant would greatly complicate the politics of the TPP in the United States. Furthermore, the rhetoric likely to be manifested on the campaign trail during the U.S. presidential election year is also not likely to be conducive to constructive approaches to the issue of Chinese participation in the TPP.

Indeed, when the U.S. presidential election year is factored in along with the scheduled change in China's top leadership also in 2012, and the ongoing weakness of political leadership in Japan, it is easy to imagine that relatively little progress may be made during 2012 on widening participation in the TPP, leaving substantive progress in 2013 as a best-case scenario. The likely intensification of "toxic politics" during the U.S. presidential election year could also slow the progress of the TPP negotiations in moving from an agreed outline to a completed agreement.

One question that might be considered by APEC is the extent of disclosure of details of the TPP negotiations to other APEC members. While TPP participants are regularly reporting progress in the negotiations to APEC senior officials (Lim 2011), it is clear that China and

perhaps other potential participants among APEC members believe that there should be fuller disclosure, perhaps even to the point of releasing draft texts, for the benefit of APEC non-participants (Cai 2011). This belief derives from the extent to which the TPP is embedded in the APEC agenda as a springboard for the FTAAP, and the clear intention that the TPP should be open to accession by other APEC members, resulting in the peculiar feature of the TPP negotiations that all APEC economies can be argued to have an interest in the negotiations, whether or not they are participating at present.

In the meantime there have been interesting developments in relation to the East Asian economic integration initiatives that can be interpreted at least in part as a response to the competitive dynamic in regional economic integration established by the APEC leader's declaration on the subject in November 2011. In something of a surprise move China and Japan recently came together to make a proposal to ASEAN for commencement in 2012 of negotiations for a region-wide "ASEAN Plus" trade agreement, leaving open the issue of whether the "plus" should involve three, six or some other number of partners. China and Japan apparently asked ASEAN for a response to this proposal in time for the East Asian Summit and APEC leaders' meetings in November. At the recent ASEAN Plus Six meeting in Manado, Indonesia, ASEAN noted the proposal from China and Japan, but countered with their own proposal to develop a "template" drawn from the provisions of the existing "ASEAN Plus" agreements, and to invite participation in a region-wide agreement based on this "template" by any countries willing to accept the "template", again with no presumption as to the eventual number or identity of partners. This concept has been described as "ASEAN Plus Plus" or "ASEAN Plus n". It remains to be seen whether the template will be based on the lowest common denominator among the current "ASEAN Plus" agreements, the ASEAN-India FTA, or on the most ambitious of these agreements, perhaps the AANZFTA. The outcome of this development will be an interesting test of ASEAN's capacity to provide ongoing leadership in the East Asian economic integration processes, and also of its willingness to move away from its preferred "ASEAN Plus One" configurations to actively support the consolidation of most if not all of the "ASEAN Plus One" agreements into a single "ASEAN Plus" agreement. In particular it remains to be seen whether ASEAN will be able to propose a template that will be acceptable to the three major Northeast Asian economies as the basis for a region-wide agreement that will include integration among themselves within its scope.

There are also unconfirmed reports that a decision in principle has been made to commence negotiations for a CJK (China-Japan-Korea) FTA in 2012, and that China and Korea have separately decided to commence negotiations in 2012 for a bilateral China-Korea FTA.

Simultaneous negotiation of a CJK FTA, a China-Korea FTA and a region-wide "ASEAN Plus" FTA will be a formidable challenge for the governments involved. If these foreshadowed negotiations do in fact materialize however, the pressure within the "competitive dynamics" of Asia-Pacific regional economic integration may swing across to the TPP. If this happens it will occur at a time when the signs are that progress in the TPP, both toward conclusion of an agreement among the existing participants and toward expanding participation in the TPP, may slow down at least temporarily. With these possibilities in play, 2012 promises to be an interesting year in the evolution of the Asia-Pacific regional trade architecture.

POTENTIAL ROLE FOR APEC

The APEC leaders' 2010 declaration reaffirmed the position of the FTAAP as the ultimate objective of APEC's Regional Economic Integration agenda. By giving equal endorsement to EAFTA, CEPEA and the TPP as potential routes to the FTAAP they arguably also created the basis for a link between these three initiatives and the Regional Economic Integration agenda. If the FTAAP is the objective to which all APEC members have agreed to aim, it would be reasonable for the APEC members to expect that the understandings on regional economic integration that have been developed within APEC should be reflected in the design of the agreements being negotiated in the initiatives that have been designated as potential routes to the FTAAP.

One such set of understandings is the APEC model measures for FTA chapters, which were developed through a consensus-building process within APEC over several years. These model measures can provide a benchmark against which the chapters developed within the TPP and eventually also EAFTA or CEPEA or one of the proposed "ASEAN Plus-Plus" initiatives could be assessed. While the level of ambition for some chapters of these initiatives might well exceed that reflected in the model measures, some reassurance could be derived from confirmation that the model measures are being used as benchmarks, and that the chapters being negotiated will be consistent with the approach found in the model measures.

APEC has also pursued work programmes over many years that equip it to provide technical input into some of the challenging issues being negotiated in the TPP and that may prospectively also be subjects for negotiation in EAFTA and CEPEA, including issues where the TPP participants have expressed intentions to develop particularly ambitious provisions, such as supply chain connectivity and SMEs. APEC's work programmes on regulatory issues and ABAC's work on the seamless business environment are other examples that have the potential to provide valuable technical input into negotiations on the same issues in the TPP, EAFTA or CEPEA.

One question that might be considered by APEC is the extent of disclosure of details of the TPP negotiations to other APEC members. While TPP participants are regularly reporting progress in the negotiations to APEC senior officials (Lim 2011), it is clear that China and perhaps other potential participants among APEC members believe that there should be fuller disclosure, perhaps even to the point of releasing draft texts, for the benefit of APEC non-participants as well presumably as other interested parties (Cai 2011). This belief derives from the extent to which the TPP is embedded in the APEC agenda as a springboard for the FTAAP, and the clear intention that the TPP should be open to accession by other APEC members, resulting in the peculiar feature of the TPP negotiations that all APEC economies can be argued to have an interest in the negotiations, whether or not they are participating at present. To the extent that this argument derives validity from the status of the TPP as a potential springboard to the FTAAP, it should apply equally to disclosure of information from EAFTA and CEPEA negotiations once those are under way, since those initiatives have been accorded the same status in relation to the FTAAP by the APEC leaders.

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