KONRAD ADENAUER STIFTUNG

PANORAMA

Trade and Economic Connectivity in the Age of Uncertainty

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Trade and Economic Connectivity in the Age of Uncertainty

Panorama: Insights into Asian and European Affairs is a series of occasional papers published by the Konrad-Adenauer-Stiftung's "Regional Programme Political Dialogue Asia/Singapore".

Editors: Christian Echle, Megha Sarmah

Publisher:
Konrad-Adenauer-Stiftung Ltd
Arc 380
380 Jln Besar
#11-01
Singapore 209000
Registration Number: 201228783N
Tel: (65) 6603-6160
Tel: (65) 6227-8343
Email: Politics.Singapore@kas.de
Website: www.kas.de/singapore

Manuscript offers, review copies, exchange journals, and requests for subscription are to be sent to the editors. The responsibility for facts and opinions in this publication rests exclusively with the authors and their interpretations do not necessarily reflect the views or the policy of Konrad-Adenauer-Stiftung.

Cover design by Flava Design LLP

Design, Layout and Typeset:
Select Books Pte Ltd
65A, Jalan Tenteram
#02-06, St Michael's Industrial Estate
Singapore 328958
Website: www.selectbooks.com.sg

ISSN: 0119-5204

PANORAMA

INSIGHTS INTO ASIAN AND EUROPEAN AFFAIRS

Trade and Economic Connectivity in the Age of Uncertainty

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CONTENTS

Preface

Trade has always been a cornerstone of connectivity between nations around the world. However, the world order which was established after the second world war, based on the ideals of multilateralism, the rule of law, market economy and free trade, is undergoing massive shifts and facing a multitude of challenges.

Since early 2018, rising trade tensions have become a major cause of geopolitical volatility. With the US imposing three rounds of tariffs on more than $250bn worth of Chinese goods, we witnessed China retaliating by imposing tariffs ranging from 5% to 25% on $110bn of US products. The escalating US-China tension over the last few years has not only contributed to market uncertainty but has also led many to question if multilateralism is slowly giving way to preferential trade deals, leading perhaps ultimately to the decline of multilateralism.

While it has been repeatedly pointed out that the US runs a large deficit with China and it is quite well known that China has over the years flouted many global rules of trade and exchange rate management, an attempt to rectify this by raising tariffs on Chinese goods is not the best way forward. Furthermore, the US attempt to isolate China is virtually impossible as the Chinese government's Belt and Road Initiative now involves around 126 countries and 29 international organisations.

While the temporary truce between the US and China in the recent G20 meeting has given cause for optimism, just days after the truce, Europe became the new target of US trade policies. The US proposal of new tariffs on EU goods worth $4bn covering 89 products could be seen as an intensification of the trade fight with the EU over aircraft subsidies. The US has been locked in a dispute with the European Union for years over two of the largest airplane manufacturers. As the escalation of trade tensions comes just after the truce with China, there is a growing sense that the danger of departure from multilateralism still looms ahead.

This departure from the multilateral trade system would have pernicious long-term effects and would lead to the creation of a complex web of trade barriers erected, which will affect global economic growth and prosperity. Without US support for open market principles, and the divergent interests of economies and trading blocs, countries are facing a major choice between openness and isolation, between the belief in win-win cooperations or a zero-sum game. The need for global economic and trade cooperation has never been greater.

It is important that nations strengthen their ties and uphold multilateralism and the rules-based free trade system. Europe and Asia as "natural partners" have a common interest in preserving a rules-based, cooperative and international system where multilateral organisations are the natural fora for achieving common objectives.

In this issue of *Panorama*, we focus on the economic and trade connectivity between Asia and Europe. Our authors not only look at the US-China trade war but also provide an overview of Asia-Europe relations in the age of rising uncertainty, including the development and implications of the Asia-Europe connectivity strategy and the Belt and Road Initiative. The impact of regional blocs on trade relations between Asia and Europe is also elucidated. Aside from the various multilateral and bilateral trade deals, the articles also look at other issues such as currency swap and bilateral agreements which help to forge a common bond between Asia and Europe.

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Asia-Europe Economic and Trade Connectivity in the Age of Rising Protectionism

Michael G. Plummer

1. INTRODUCTION

The international trading system is facing its biggest challenges since the 1930s. In part this is due to a new global landscape in which the distribution of power has broadened to include a diversity of economies at different levels of economic development and featuring a variety of policy regimes. It was far easier to produce accords under the auspices of the General Agreement on Tariffs and Trade (GATT), under which multilateral commercial governance fell from its creation in 1947 until it was superseded by the World Trade Organisation (WTO) in 1994, when only a few dominant, like-minded, developed countries led multilateral cooperation. Today, those same countries are joined by emerging and developing economies characterised by different economic interests and approaches, making negotiations far more complicated. In fact, the many required reforms associated with the "democratisation" of global governance have challenged all multilateral institutions, including the World Bank and the International Monetary Fund (IMF).

The need to give greater weight to emerging and developing economies is obvious but how to do this is far less so. Moreover, the sword is two-edged: emerging and developing economies are also finding it difficult to take on leadership responsibilities in this new context, especially when they profited to some extent from advantages as less-developed economies. For example, if China has become the second largest economy in the world, the world's largest exporter, a leader in several key high-tech areas, a major exporter of foreign direct investment (FDI), and a supplier of infrastructure even in developed economies, should it still be able to benefit from special preferences reserved for developing countries?

These secular challenges are being exacerbated by policy trends in leading economies, in particular the United States, which has led global trade governance from the beginning. The "America First" doctrine of the Trump administration is ostensibly predicated on the fundamental arguments of *mercantilism,* namely, that trade is a zero-sum game in terms of its welfare effects and, hence, an optimal policy is to ensure that exports exceed imports. At his inauguration, President Trump laid out his vision: "We must protect our borders from the ravages of other countries making our products, stealing our companies and destroying our jobs. Protection will lead to great prosperity and strength." This constitutes a major break with previous US trade strategies. While some observers had hoped that, over time, harsh rhetoric would yield to pragmatism, no such change has been in evidence, e.g., the Trump Administration has withdrawn from the Trans-Pacific Partnership (TPP) trade agreement, applied controversial tariffs on steel and aluminum imports based on "national security" considerations, threatened to pull out of the WTO, and initiated a full-blown trade war with China, the first major conflict in the global trading system since the 1930s.

As outward-oriented, trade-dependent regions, the economies of Asia and Europe have large stakes in an open and vibrant international trading system. Given this new inward-focused approach of the United States, can they step in to provide the necessary leadership to support international commerce in the 21st century?

Thus far, signs have been positive. For example, the two regions have responded to this challenge by embracing regional approaches to trade cooperation: Europe has been building regional links for over sixty years and has a great deal of experience in forging practical approaches to removing commercial impediments at the border as well as behind it. Regional cooperation is less advanced in Asia; even though the Association of Southeast Asian Nations (ASEAN) began cooperation over 50 years ago, its accomplishments have been more modest, despite the fact that it is still the most advanced organisation of regional cooperation in the developing world. In addition, Asia has been very active in forging "mega-regional" trade agreements, which could have an important bearing on regional and global trade and investment flows, as well as rule-making, in the coming decades. Further, the European Union (EU) has been active in forging closer links via bilateral arrangement with key players in the Asia-Pacific region.

In this short paper, we consider some of the associated leadership challenges facing Asia and Europe in charting a path forward. It begins in Section II with an overview of mega-regionalism in the Asia-Pacific region and its potential effects. Section III considers implications for Europe, followed in Section IV by a review of Asia-Europe approaches to removing impediments to trade and boosting connectivity. Section V gives some concluding remarks.

2. MEGA-REGIONAL TRADE COOPERATION IN THE ASIA-PACIFIC

To begin, it is worth noting that a large majority of preferential trading arrangements concluded or initiated by Asian economies are bilateral free-trade areas (FTAs), which tend to be easier to negotiate than, say, larger memberships. Moreover, a majority of these FTAs are with economies outside of Asia. Thus, when Asian governments consider bilateral accords, they think globally, rather than just regionally. These priorities reflect the driving forces behind regionalism in Asia, which tend to be economic rather than political, though of course political and diplomatic dimensions continue to be important to various degrees. Indeed, this might distinguish Asia from bilateral and regional accords elsewhere, which tend to be politically dominated. For example, early integration initiatives in Europe, beginning with the Coal and Steel Community and the European Economic Community, had strong political backing (integrating France and Germany after World War II, Cold War priorities), even though the economics were not obvious at the time. Even monetary union in the EU was made possible due to political reasons, that is, post-Cold War incentives and, in particular, facilitating the political integration of East and West Germany. In fact, the need to support economic integration in Asia is even helping to overcome some of the most difficult obstacles to cooperation in the region; a decade ago few if anyone could have foreseen that China, South Korea and Japan would be able to improve relations sufficiently to sit down and negotiate an FTA. Yet, that is exactly what was agreed to at their May 2012 Summit; a China-South Korea-Japan FTA has not been concluded but negotiations continue.

Mega-regional trade agreements are defined as multi-country, comprehensive cooperative agreements designed to address cutting-edge border and non-border barriers with significant implications for regional and international trade. In the Asia-Pacific region, this has involved bringing together an ambitious trade and investment liberalisation agenda in the context of many partners at all levels of economic development. This ambition and diversity explain why the emerging mega-regionalism agreements have taken so long to put into place.

The TPP in particular was designed as a modern trade agreement with the aim of setting a “gold standard” for regional cooperation. The TPP and its successor, the Comprehensive and Progressive Agreement on Trans-Pacific Partnership (CPTPP), include cutting-edge chapters on the digital economy, state-owned enterprises engaged in trade, trade in services, intellectual property rights (IPR) protection, non-tariff barriers, and protection of labour and environmental standards, while at the same time cutting virtually all tariffs to zero (except in a few notable sectors, such as agriculture). Given the diversity of the region, negotiations were complicated and challenging; TPP negotiations started in February 2008 and an agreement was signed eight years later in February 2016. But it succeeded in creating an ambitious, 21st-century template that brought together pro-trade economies that were rich and poor, policy regimes in which the state was more and less active, varying degrees of openness to the global marketplace with trade/GDP ratios ranging from 30 percent to 400 percent, and featuring an impressive menu of rules that could serve as global templates.

In essence, the main purpose of mega-regionals apart from liberalisation of barriers at the border is to find ways to create and harmonise new international benchmark standards for modern trade that has eluded cooperation under the WTO, which is made up of 164 heterogeneous economies. Hence, the region is forging new standards that could eventually serve as global templates, or at least global "best practices" benchmarks. Addressing such issues is necessary to facilitating real economic connectivity.

In part, the new architecture of mega-regional trade agreements is shaped by the emergence of international corporate networks in Asia that integrate dispersed production, engineering, product development and research across geographic borders.[1] While global production networks date back to the late 1970s, they have become far more prominent in the 21st century, and a more recent development is the rapid expansion of global innovation networks, driven by the relentless slicing and dicing of engineering, product development, and research. These processes have become prominent in Asia but also involve many US and European multinational corporations.

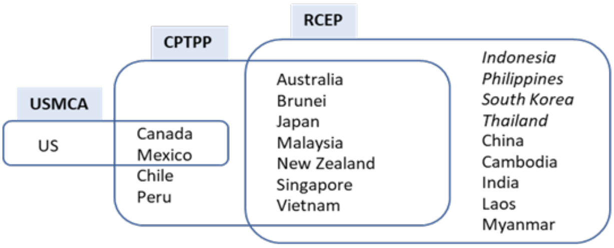
Despite the withdrawal of the United States from the 12-nation Trans-Pacific Partnership agreement in January 2017, the remaining eleven TPP countries[2] have moved forward anyway and the resulting CPTPP went into effect on 30 December 2018, with the expectation that all members will have ratified the agreement by the end of 2019. The CPTPP is remarkably similar to the TPP; it has suspended 22 measures – mostly dealing with the protection of intellectual property – but otherwise remains the same in terms of content. At least five other Asian economies (Indonesia, Korea, the Philippines, Thailand and Taiwan) have expressed interest in joining the CPTPP, and China is currently studying the possibility of member-

1 Ernst and Plummer (2018).

2 These include Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, New Zealand, Peru, the Philippines, Singapore, and Vietnam.

ship.[3] Even the UK has expressed an interest in joining post-Brexit. Moreover, negotiations to create a Regional Comprehensive Economic Partnership (RCEP) arrangement, launched in November 2012 and composed of 16 Asian economies,[4] received a boost from the US TPP exit. It has completed 25 rounds of negotiations as of February 2019, held seven ministerial meetings as of March 2019, and two Heads of State Summit as of November 2018, underscoring strong commitment at the highest levels. It has the goal of completing the agreement this year. In short, while the United States has always been a key player in and advocate of Asia-Pacific economic integration, the region is clearly intent on moving forward without it.

Figure 1. Asia-Pacific Regional Groups



Regional groups discussed in the text, charts and tables:

USMCA	United States-Mexico-Canada Agreement
CPTPP	Comprehensive and Progressive Trans-Pacific Partnership
RCEP	Regional Comprehensive Economic Partnership
CPTPP16	CPTPP + RCEP economies shown in italics + Taiwan

Source: Petri, Peter A., and Michael G. Plummer, 2019. China Should Join the New Transpacific Partnership, Policy Brief 19-1, Peterson Institute for International Economics, January.

The motivations for deeper economic integration in the Asia-Pacific are many, but the economic rationale is obviously critical. For example, in Petri and Plummer (2019) we estimate that the CPTPP will generate global gains of approximately $157 billion to member-countries per year by 2030 relative to the baseline. The preponderance of the gains flow from trade creation and there is very little trade diversion, testifying to the open nature of the agreement. These net gains constitute 1 percent of regional income, slightly less than the 1.1 percent estimated from the TPP12. The income gains are led by trade, which are estimated to rise by 6.2 percent. Should the CPTPP expand – and it likely will, based on statements from leaders – the gains

[3] See Petri and Plummer (2019).

[4] RCEP members include 16 Asian economies: Australia, Brunei, Cambodia, China, India, Indonesia, Japan, Korea, Laos, Malaysia, Myanmar, New Zealand, the Philippines, Singapore, Thailand and Vietnam.

could be far greater. For example, including Indonesia, Korea, the Philippines, Thailand and Taiwan in the CPTPP, income gains from the "CPTPP16" more than double. The accession of China to the CPTPP would lead to particularly large positive effects: income would rise by $632 billion (1.5 percent of member-country income) and $1,225 billion (2.4 percent of member-country income) if it were to join the CPTPP or CPTPP16, respectively. The gains from an expanded CPTPP are far larger than those estimated in the case of RCEP ($260 billion for member-countries), due to the fact that the RCEP template is less ambitious than the CPTPP and most economies already have free-trade areas (FTAs) in place.

Importantly, these mega-regional agreements demonstrate that Asia-Pacific economies are committed to taking a leadership role in bolstering global markets. This was never a given. In fact, when the United States pulled out of the TPP, many scholars believed that the agreement was dead. Prime Minister of Abe of Japan said that the CPTPP without the United States was "meaningless". Vietnam, which was slated to gain the most from the TPP due to greater access to the US market, was hesitant to continue in the CPTPP since it would have to adopt many difficult reforms for far less immediate return. Some saw the RCEP as a Chinese reaction to the TPP and, with the United States out of it, predicted that the RCEP, too, would be put on hold. Still, the region opted to move forward with both mega-regionals; the contents of the CPTPP are already influencing other regional agreements and it is likely that plurilaterals at the WTO may well use the CPTPP as a benchmark.[5]

3. CLOSER ASIA-EUROPE CONNECTIVITY

European economic cooperation has traditionally been a model for economic cooperation in Asia, though always adapted to the regional context. For example, from the beginning ASEAN leaders looked to Europe for inspiration in searching ideas for regional cooperation – for example, the organisational structure of ASEAN was based on the European Commission – but always filtered to take account of regional exigencies. In particular, the willingness of member-states to pool sovereignty was always far less prominent in ASEAN than in Europe, limiting the degree to which regional cooperation can take place (even in Europe this sovereignty issue is coming back to haunt the region, as evidenced by Brexit). Still, when ASEAN sought deeper integration at the turn of the century, it looked to Europe for ideas: the ASEAN Economic Community (AEC), which was declared to be in effect as of

[5] For example, the newly-constituted NAFTA, now to be called the US-Mexico-Canada Agreement (USMCA), borrow some from the CPTPP.

December 2015, resembles the idea of the European Economic Community; the "four freedoms" of the 1986 Single Market Program in Europe (i.e., free flow of goods, services, capital and labour) were watered down in the AEC to be free flow of goods, services, skilled labour, and long-term capital (FDI). In sum, the European project has helped mould regional aspirations.

The direct implications of Asia-Pacific mega-regionalism for Europe are not large and, in fact, tend to be positive, due in part to the non-discriminatory elements of the agreement (e.g., improving trade facilitation is an important goal of both the CPTPP and RCEP and associated reductions in trade costs will apply to both member and non-members). For example, Petri and Plummer (2019) show that Europe should gain (marginally) in all mega-regional scenarios due to positive spillover effects of regional cooperation. Still, to the extent that new global rules are being created in the context of the CPTPP, the EU is at a disadvantage.

A major study by the Centre for European Policy Studies (CEPS) and the World Trade Institute (WTI) considers the potential of an EU-China FTA (CEPS and WTI 2018), taking a similar approach adopted by the Peterson Institute of International Economics that looks at the potential of a China-US FTA from aggregate and sectoral levels (Bergsten, et al., 2014). The idea of an EU-China FTA was first made by China's President Xi Jin Ping in the spring of 2014. The CEPS and WTI (2018) study underscores a long list of reasons for the agreement, from economic potential to geopolitical motivations. For example, it estimates that a modest FTA between the EU and China would lead to an increase in income of 1.16 percent and 0.43 percent for China and Europe, respectively, but 1.87 percent and 0.76 percent under a more ambitious scenario. Of course, the political obstacles to creating an EU-China FTA are high, as they are for a China-US FTA, despite the large attendant gains.

Moreover, while the United States seems to be reducing its ambitions for cooperation with the region, Europe is being pro-active: it has already concluded bilateral agreements with Canada, Chile, Colombia, Japan, Korea, Mexico, Peru and Singapore, and has negotiations underway with India, New Zealand, the Philippines, Thailand and Vietnam.

Further, it could gain considerably due to the China-led Belt and Road Initiative, which envisions a massive string of infrastructure investments to connect China to Europe and territories along the way. The March 2019 (non-binding) Italy-China Memorandum of Understanding on Italy's participation in the Belt and Road Initiative – the first G-7 country to have one – is indicative of a strong desire to improve the connectivity between Asia and Europe (though admittedly controversial). The new Asia Infrastructure Investment Bank (AIIB), of which many European countries are members (and the United States is not), will provide financing of Belt and

Road Initiative infrastructure projects as well as other initiatives. Finally, it could be that the EU will want to consider expanding relationships with the fledgling mega-regional agreements in the Asia-Pacific.

Of course, the United States may decide to join the CPTPP in the future, which existing members would welcome, as indicated by their suspending 22 measures from the TPP rather than excluding them entirely. Indeed, the United States is still committed to a possible Free-trade Area of the Asia-Pacific (FTAAP), which could include all Asia-Pacific Economic Cooperation (APEC) economies (and possibly others), and the CPTPP has an accession clause similar to the TPP. But US re-engagement with Asia-Pacific mega-regionals seems off the table under the current administration. In the meantime, the economic and policy costs of US disengagement will be high.

4. CONCLUDING REMARKS

For the past half century, trade has made substantial contributions to development in many economies, making a vibrant trading system a global priority. Yet world trade growth is now decelerating, while the complex challenges of today's trading environment and divergences across WTO members have stymied progress on further liberalisation at the WTO. In this vacuum, new experiments in regional economic cooperation have emerged, including a dramatic rise in regional trading arrangements since 2000.

Against this background, ambitious, new mega-regional trading agreements are now emerging as a possible answer to the global stalemate, with the Asia-Pacific region serving as their main incubator. The economics of these mega-regionals are strong; the CPTPP and RCEP are both expected to yield significant gains, and the possible enlargement of the CPTPP to include other East Asian economies, including China, promises even greater gains. Given the outward-oriented nature of these agreements, Europe will likely gain (at the margin) from Asia-Pacific regionalism, given the positive spillover effects associated with the non-discriminatory nature of deep integration (estimates of the effects of the European Single Market Program on non-partners were positive as well).

Still, to the extent that the CPTPP is forging new global standards and best practices in regional trading agreements, Europe will lose out from not being part of the process. Moreover, the potential economic benefits of deeper economic integration between Europe and Asia should be large. Europe has been active in concluding bilateral FTAs with the region and does well to explore new ones, including with China. The Belt and Road Initiative offers great potential in reducing trade costs. In the medium term, Europe would do well to consider a close cooperative agreement with the CPTPP, perhaps even a formal integration scheme.But most importantly, the new inward-looking approach to trade being adopted by the main protagonist of global economic integration in the post-war period, United States, risks leaving the global system without leadership. This would come at high costs given the nature of globalisation in the 21st century, with developing economies standing to lose the most. There is plenty of potential for economies in Asia and Europe to step up to the plate and cooperate in guiding future global cooperation from the bottom up. Forming cross-regional accords that are open and comprehensive would be a good place to start.

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The EU-Asia Connectivity Strategy and Its Impact on Asia-Europe Relations

Bart Gaens

INTRODUCTION

The EU is gradually adapting to a more uncertain world marked by increasing geopolitical as well as geo-economic competition. Global power relations are in a state of flux, and in Asia an increasingly assertive and self-confident China poses a challenge to US hegemony. The transatlantic relationship is weakening, and question marks are being placed on the future of multilateralism, the liberal world order and the rules-based global system. At least as importantly, China is launching vast connectivity and infrastructure development projects throughout Eurasia, sometimes interpreted as a geostrategic attempt to re-establish a Sinocentric regional order. The Belt and Road Initiative (BRI) in particular, focussing on infrastructure development and investments in over 80 countries, including some within Europe, has been causing concern at regional as well as global levels. At the most recent BRI summit in April 2019 Chinese President Xi Jinping announced that China had signed new deals amounting to 64 billion USD, underscoring Beijing's continuing cheque book diplomacy.[1]

It is clear that these ongoing dynamics potentially have important ramifications for Europe's own prosperity, in terms of trade and economy but also security. Overall however, the EU has been slow to react, in particular in formulating a response to connectivity challenges. In September 2018 the EU published its first coordinated attempt to formulate the European vision on connectivity and infrastructure development, in the form of a European connectivity strategy for Asia, officially entitled a Joint Communication on "Connecting Europe and Asia – building blocks for an EU strategy". This article explores the potential impact of this strategy on Asia-Europe relations.

1 *Financial Times*, 29 April 2019.

THE EU'S CONNECTIVITY STRATEGY FOR ASIA

An EU strategy paper to form the basis for cooperation in the field of connectivity with and in Asian countries was long overdue. For a protracted period of time the EU stuck to a reactive wait-and-see approach. This was quite obvious in multilateral fora such as the Asia-Europe Meeting (ASEM), in which the EU and its member states as well as two other European countries interact with 21 Asian states. ASEM can be seen as an excellent "real-time observatory" for global power transformations. ASEM has shifted, for example, from a forum focussing on a region-to-region structure, to one placing more emphasis on bilateral relations (both state-to-state and EU-Asian state). The higher prominence of bilateral relations reflects the development of a more multipolar world, or even the crisis of globalisation and resurgence of nationalism and populism, as marked by Brexit, the election of Donald Trump as US president, and the failure of large-scale trade deals such as the Trans-Pacific Partnership (TPP). In other words, ASEM serves as a signpost of the "changing interlinkages of bilateral, regional and transregional relations that the EU has around the globe".[2]

Even though ASEM is a forum for informal dialogue, the focussed initiatives launched by individual members in a particular field offer valuable insights into global transformations. China, for example, has been driving forward the ASEM connectivity agenda since 2014, not in the least to find synergies with its own BRI, conceived as "One Belt One Road" (OBOR) in 2013. According to the ASEM Connectivity Inventory, seven out of twelve events organised by China in the period 2014-2018 related to connectivity.[3] Beijing sponsored the ASEM Industry Dialogue on Connectivity, held in Chongqing in 2015, floating ambitious ideas on improved Eurasian land bridges, transport corridors, sea routes and rail links, while at the same time promoting people-to-people exchanges, policy coordination, and trade and capital flows. China furthermore organised initiatives such as a Media Dialogue on connectivity in 2016 and a High-Level Forum on digital connectivity in 2017. It has also aimed to promote institutional connectivity through multiple events in the fields of food safety, sustainable development, small and medium-sized enter-

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[2] Francis Baert, Tiziana Scaramagli, and Fredrik Söderbaum, "Introduction: Intersecting Interregionalism," in Francis Baert, Tiziana Scaramagli, and Fredrik Söderbaum (eds.), *Intersecting Interregionalism. Regions, Global Governance and the EU*. Dordrecht: Springer (2014): 9.

[3] Okano-Heijmans, Maaike and Prakash, Anita. ASEM Connectivity Inventory. Clingendael and ERIA, June 2018, p. 20. https://cdn.aseminfoboard.org/documents/S02_ASEM-connectivity-study_FINAL-VERSION-11.10.2018.pdf.

prises (SMEs), and human rights, and people-to-people connectivity in the field of university-business partnerships, for example.

China's brisk activity in the field was met with a strongly ambivalent and reactive European stance based on a wait-and-see policy. The EU often seemed unable to choose between competing or cooperating with China in third countries. On the one hand, the EU was strongly aware of the importance of a connected Asia for European prosperity[4], not in the least because trade between both regions amounts to 1.5 trillion euro. Furthermore there was the potential to connect the Trans-European Transport networks (labelled TEN-T) to networks in Asia. On the other hand however, the EU was aware of the challenges posed by China's connectivity project. First of all, China is investing strongly in integration towards the West, but a comparable flow from West to East is generally absent. Furthermore, China-funded projects most often are tied with Chinese companies, and are much more to the benefit of China than of the local countries. Frequently lacking a transparent bidding process, they are generally less open to local or international companies. Importantly, China typically provides loans to countries rather than investments, which can have a profound impact on national debt, as in the case of Montenegro. It can even result in a debt trap and loss of sovereign control, as was the case in Sri Lanka's Hambantota Port project. In addition, concerns have risen about standards, environmental considerations and social requirements, including labour rights or human rights, often lacking in China-sponsored projects.

The Chinese presence in Europe, including growing political influence, is certainly a key challenge. Chinese Foreign Direct Investments (FDI) in Europe amounted to 37 billion euro in 2016 and 29 billion in 2017.[5] China's FDI are still mainly concentrated in Western Europe, in particular in the UK, Germany and France. However, an increasing share is going to Central and Eastern Europe. The Czech Republic, Hungary and Greece are often-quoted examples of countries where China's influence is said to be visible, causing intra-European divisions and blocking EU-level criticism of China. Additionally, the 16+1 framework[6], a platform driven by China to promote cooperation between Beijing and 16 Central and Eastern European countries, is often seen as a tool for driving a wedge between the European Union and

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4 "Shared vision, common action: A stronger Europe" - A Global Strategy for the European Union's Foreign and Security Policy, June 2016, p. 37. http://eeas.europa.eu/archives/docs/top_stories/pdf/eugs_review_web.pdf.

5 Hanemann, Thilo; Huotari, Mikko and Kratz, Agatha. Chinese FDI in Europe: 2018 trends and impact of screening policies. Rhodium Group and Mercator Institute for China Studies, March 2019, p. 9.

6 Or 17+1, after Greece expressed its willingness to join the forum.

its neighbourhood, and even within the EU itself. 14 out of 28 EU member states have now signed bilateral endorsements of the BRI. The Union seems divided between those member states that advocate a tougher stance against a "systemic rival", and those that support closer cooperation.[7] A further concern is that China's investments can undermine EU rules, especially in sensitive industries such as steel and nuclear energy, posing a challenge in regard to transparency and technological and legislative standards.

The European Union's Global Strategy (EUGS) endorsed in June 2016, can be seen as the starting point for a new European Asia strategy in terms of connectivity. The EU realised it is in its own interests to tap into Asian economies by deepening economic diplomacy and by striving for cooperative regional orders. ASEM, together with the EU-China Connectivity platform and the EU-ASEAN framework, is referred to as a key tool to pursue a coherent approach to China's connectivity drives westwards. The EU-Asia security guidelines of 28 May 2018 further emphasised that connectivity and security go hand in hand.[8] The EU's connectivity strategy, published on 19 September 2018, then, denoted Europe's ambitions to step up the EU's engagement with Asia as for connectivity.

The strategy emphasises that connectivity has to be economically, fiscally, environmentally and socially sustainable, comprehensive across sectors and financial frameworks, and based on international rules and an open and transparent investment environment. As noted elsewhere, the implementation, and eventual success, of the strategy depends on the increased funding deriving from the EU's investment framework for external action, as well as on the extent to which additional financial resources can be raised from the private sector and national, international and multilateral financial institutions.[9] Even so, the document clearly puts forward a European model for connectivity and a blueprint for building up international support for the values and principles it promotes, allowing Europe to help shape the rules of the global marketplace. As such it offers an alternative to the BRI, while also forming the basis for cooperation with third countries, including with China in Europe's immediate neighbourhood.

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7 *Financial Times*, 26 April 2019.

8 Council of the European Union. Enhanced security cooperation in and with Asia – Council Conclusions (28 May 2018).

9 Gaens, Bart. "Europe's connectivity strategy and the challenge of China: Rivalry, reciprocity, or both?" *FIIA Comment 22*, December 2018.

BUILDING ON FOUNDATIONS IN PLACE

Some of the groundwork for cooperation in connectivity is already in place. First and foremost there is the definition of connectivity. Connectivity is a very comprehensive and vague concept. Whereas for some it means essentially the same as globalisation but without the negative connotation of that term, for others it is the same as regional integration. For yet others, primarily as a result of the highly-promoted BRI, it is synonymous to Eurasian land bridges and maritime transport corridors. The EU's definition of connectivity is rooted in work conducted in the context of the Asia-Europe Meeting. A so-called ASEM Pathfinder Group on Connectivity (APGC) held its first meeting in Brussels in June 2017. The APGC, basically a Working Group consisting of Senior Officials, concluded that the definition of connectivity should cover all 3 ASEM pillars (security, economy, social/culture), and should include both hard connectivity (infrastructure projects) and soft connectivity (people-to-people or digital connectivity), and all links: land, sea, air, cyber, and educational connections, as well as customs cooperation and trade facilitation. The Pathfinder Group meeting proposed four clusters in which ASEM could work in strengthening Asia-Europe connectivity, namely transport connectivity, customs and trade facilitation, investment financing and quality infrastructure, and digital connectivity including e-commerce. Second, connectivity has to be in line with international standards and based on full transparency. Third, sustainability needs to be a quality benchmark, and there should be a link with the implementation of the Sustainable Development Goals (SDGs). Fourth, work on connectivity should build on existing forms of regional cooperation, while avoiding duplication. Fifth, connectivity should function as a means to foster deeper economic and people-to-people links.[10] The 13th ASEM Foreign Ministers' Meeting in Nay Pyi Taw in November 2017 followed this comprehensive definition, including the importance of market principles and agreed international rules, norms and standards, and the link with sustainable development for achieving the 2030 Agenda. This definition thus formed the basis for the 2018 Strategy paper.

Second, in addition to a definition, other groundwork has been laid in ASEM. ASEM has connectivity as one of its core tasks, bringing together and connecting the people from the two regions and 51 countries, including political leaders, but also businesspeople, academics, civil society representatives and non-governmental organisations (NGOs), parliaments, labour fora, and youth. As of 2014 and the 10th

[10] ASEM Pathfinder Group on Connectivity. *Chair Summary*. 21 June 2017. https://eeas.europa.eu/sites/eeas/files/chair_summary_apgc_21_june_2017-final.pdf.

ASEM summit in Milan, ASEM has started emphasising connectivity as a core objective and even as a guiding concept that should drive all ASEM initiatives, making the forum the “institutional home of connectivity”.[11] Also, before 2014, connectivity had already been addressed in ASEM. For example, the Trans-Eurasia Information Network (TEIN), launched at the ASEM3 summit in Seoul in 2000, has successfully enhanced interconnectivity between European and Asian research and education networks, and is currently in its fourth phase. TEIN4 provides a large-scale research and education data-communications network for the Asia-Pacific region. It connects Asian researchers to each other and with their counterparts in Europe via direct links to Europe’s GÉANT network[12], providing the Asia-Pacific countries with a gateway for global research collaboration. It currently connects twenty-three countries in the Asian and South Asia region. The TEIN project has been co-funded under the EU Development Cooperation Instrument since 2004. The EU contribution has been about 21 million euro under TEIN2 and TEIN3. TEIN gives researchers better internet access, at increased speed and capacity, and it enables exchanging big amounts of data and makes international research collaboration possible. TEIN4’s applications include supporting disaster-warning systems, e-learning, and tele-medicine (e.g., conducting surgeries with the remote consultation of experts in other countries).

A third foundational basis is a set of data, which can point to further possible areas of focus for cooperation. The ASEM Sustainable Connectivity Portal, in place since October 2018, is an online tool to measure physical, economic/financial, political, people-to-people and institutional connectivity between Asia and Europe, as well as to provide data on social, economic/financial and environmental sustainability. The Portal is accompanied by complementary publications, including a survey of ASEM connectivity activities since 2014,[13] and a study indicating areas for further cooperation.[14]

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[11] Asselborn, Jean. “Connectivity as the key feature of ASEM’s third decade”. Asia Europe Foundation, 28 March 2016. http://www.asef.org/press/corporate/news-3798-connectivity-as-the-key-feature-of-asems-third-decade.

[12] A pan-European data network for the research and education community.

[13] Okano-Heijmans, Maaike and Prakash, Anita. ASEM Connectivity Inventory. Clingendael and ERIA, June 2018.

[14] Becker, William et al. *Exploring ASEM Sustainable Connectivity – What brings Asia and Europe together?* Joint Research Center (JRC), September 2018. http://publications.jrc.ec.europa.eu/repository/bitstream/JRC112998/asem-report_online.pdf.

COOPERATING WITH OTHERS

Building on this groundwork, the EU-Asia Connectivity Strategy sets out the conditions for Europe to cooperate with other countries, including China, bilaterally and in multilateral fora, and to find synergies, not least in the EU's immediate neighbourhood. The document can be seen as a blueprint for building up international support for the values and principles it promotes, allowing Europe to help shape the rules of the global marketplace. To a certain extent an impact may be visible already, at least at the level of rhetoric. China committed to more sustainable and transparent financing and to "supporting open, clean and green development and rejecting protectionism".[15] The document therefore defines the EU's interests and principles as a basis for flexible and trust-based cooperation with China, including in the EU's immediate neighbourhood.

Furthermore, emphasising sustainable, comprehensive and rules-based connectivity, the strategy offers scope for cooperation with like-minded Asian countries such as Japan and ASEAN. Japan launched its "Partnership for Quality Infrastructure: Investment for Asia's Future" in 2015. Furthermore, in 2017, Japan and India proposed their jointly envisioned "Asia-Africa Growth Corridor" (AAGC), focussing on connectivity and "quality infrastructure", including large-scale strategic projects conducted together with the Asian Development Bank (ADB) and the private sector. The values and norms behind the AAGC dovetail with the EU's own norms as for connectivity, opening up vistas for cooperation, especially in regions such as Africa where China is increasingly present and where the EU and Japan can provide an alternative model based on quality infrastructure and sustainability. This is especially salient in the light of the gradual convergence between EU and Japanese development aid practices, for example. The EU now increasingly emphasises the need to shift from aid dependence to self-reliance, as well as strongly supports private sector involvement in development and an emphasis on economic infrastructure rather than social/administrative infrastructure, similar to Japan's traditional aid philosophy.[16] This offers opportunities for cooperation in promoting sustainable connectivity in order to tackle the SDGs. The recently concluded EU-Japan Economic Partnership Agreement (EPA), signed in tandem with a Strategic Partnership Agreement (SPA), offers a solid base in this respect.

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[15] *Financial Times*, 28 April 2019.

[16] Cf. Gaens, Bart. "Comparing Japan and the European Union: The Development Cooperation Policies of Two Civilian Powers", in Asplund, Andre and Söderberg, Marie (eds.), *Japanese Development Cooperation. The making of an aid architecture pivoting to Asia*. London: Routledge, 2017.

As for ASEAN, the bloc is projected to become the fourth largest economy in the world by 2050. The EU has already concluded free trade agreements (FTAs) with Singapore (2012) and Vietnam (2015), and is continuing negotiations with the Philippines, Malaysia, Thailand and Indonesia. In March 2018 the EU and ASEAN agreed to revive their efforts, abandoned in 2009, to integrate these bilateral FTAs into a more comprehensive region-to-region FTA. The evolving US engagement in the region, including its withdrawal from the TPP, offers opportunities for the EU to intensify commercial links and further promote free trade with Asian partners. Connectivity is one particularly promising area for cooperation, with an EU-ASEAN Comprehensive Air Transport Agreement currently being negotiated.

UTILISING ASEM

ASEM can provide a further venue to promote European and Asian connectivity. Continuing ongoing work, the forum can serve as a level playing field in order to share experiences, best practices and expertise, build a common agenda, and set further objectives. Furthermore, it can contribute to the creation of partnerships at the bilateral, minilateral, region-to-region, or multilateral levels. Importantly, ASEM brings together multiple stakeholder groups including government officials, the private sector and civil society. Utilising this set-up to the full, ASEM could establish a dedicated "Connectivity Forum", bringing together the private sector, media and civil society organisations to discuss infrastructure-related issues with an impact on sustainable development, security and climate change.[17] ASEM's role in promoting "hard connectivity", in the form of transport connections or infrastructure projects, will remain limited. However, the forum can do a lot to promote dialogue on procedures, standards, and transparency as a basis for further cooperation at other levels. Soft connectivity is also an area where results can be achieved, building on success stories such as ASEM's cultural, social, and educational exchanges. Especially education as a field of cooperation is given added importance because of its crucial impact on sustainable development. The recent EU-Asia Connectivity Strategy is important here as it helps to set objectives and determine the added value of dialogue. It can also steer the EU in launching new initiatives based on European priorities. The EU strategy importantly looks beyond investment in in-

[17] As proposed by Werly, Richard (2015). "ASEM initiatives and challenges - Surfing the Asia-Europe waves", in Bart Gaens (ed.), *The Future of the Asia-Europe Meeting (ASEM): Looking Ahead into ASEM's Third Decade*. Brussels: European External Action Service (2015), p. 91.

frastructure, pointing the way to niche markets in which the EU has a comparative advantage, such as green technology or educational mobility.

As a possible next step, the plan on areas for cooperation on connectivity, as drawn up by the ASEM Pathfinder Group on Connectivity, points out useful future directions in order to achieve tangible results.[18] The "Tangible Areas of Cooperation in the Field of Connectivity" (TACCs) focus on (1) best practices and international standards in connectivity policies; (2) quality infrastructure and sustainable connectivity; (3) trade and investment connectivity including customs clearance facilitation and transport connectivity; (4) future connectivity and digital economy including e-commerce; (5) people-to-people mobility including educational exchanges, sustainable tourism and the empowerment of women; and (6) security challenges linked to connectivity. Combined with the "the European way" outlined in the Europe-Asia Connectivity Strategy, dialogue and cooperation in these fields can help the EU establish partnerships in and with Asian countries. These could help the EU become a norm provider in the field of sustainable connectivity, as well as promote European priorities.

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[18] ASEM Pathfinder Group on Connectivity. "APGC Plan for Areas of Focus and Related Actions on Connectivity". Brussels, 19 October 2018. https://cdn.aseminfoboard.org/documents/APGC-Plan-for-Area-of-Focus-and-Related-Actions-on-Connectivity.pdf.

US-China Strategic Economic Competition: Impact on EU-China Relations

Alicia Garcia Herrero

1. INTRODUCTION

As the European Union was recovering from the deepest economic crisis since the Euro was created, a number of new challenges popped up. First and foremost, Brexit since June 2016 and a growing number of anti-European and/or populist governments with the most recent – and probably most relevant case – being Italy. Beyond those internal problems, another external shock hit the EU in 2018, namely, the trade war between the US and China. The US-led trade protectionism against China affected the European Union in several ways. First and foremost, it puts multilateralism in trade relations at risk and, in particular, the good functioning of the World Trade Organisation (WTO) (Jean, Martin, and Sapir, 2018). Second, it opened the door to additional trade protectionism which could possibly impact the EU as it sits on the largest trade surplus in the world. Third, trade measures taken by the US against China as well as China's retaliation have indirect consequences on Europe. These can be positive for some sectors and European exporters have gained a comparative advantage against US exporters in China markets for the US goods on which import tariffs have been imposed and that Europe can produce (Wolff, 2018). Conversely, European exporters have an advantage in the US market compared to Chinese exports for those sectors targeted by the US with tariffs. However, this positive scenario gets blurred when one thinks of the complexities of the global value chain which can lead to increases in European costs of production due to third countries' import tariffs as long as they lie within Europe's production chain (Chiacchio, 2018). This is, no doubt, the case of China.

Given the above complexities, it is important to analyse in detail what has happened so far in the US-China trade war and beyond trade as this article will hold the view that trade is just one of the facets of a much more structural economic confrontation between China and the US. Second, we move to analyse the EU's potential gains on the basis that the trade measures taken by the US and China on each other can help us to focus on Europe's potential gains, at least at a sectoral level. Finally, there will be a review of Europe's strategic options in a world that tends to be increasingly divided into two blocs (China and the US).

The paper is divided into 5 sections. The first section is to introduce the background of the US-China trade war. The second section is to provide a review of US-China trade protectionism and the impact of the trade war on China and the US. The third section is to show a sectoral analysis of trade measures taken by China and the US. The fourth section illustrates EU's first-best strategy regarding the US-China trade war. The fifth section discusses how the EU should behave in the US-China trade war.

2. THE CURRENT STATUS OF THE US-LED TRADE WAR

The trade negotiation between China and the US is a key factor influencing market sentiment. First of all, it is important to realise that the trade war has evolved into a more complex reality, namely the strategic competition between the two largest economies in the world. Within that context, US expectations regarding China seem to be gearing towards two fronts: increasing Chinese imports from the US (not necessarily a market measure) and improving market access for US companies in China. For the latter, a better legal framework for protecting intellectual property rights and discouraging forced technology transfers is the key. More generally, a foreign investment law reform is an inevitable way for China to improve the market environment for foreign firms.

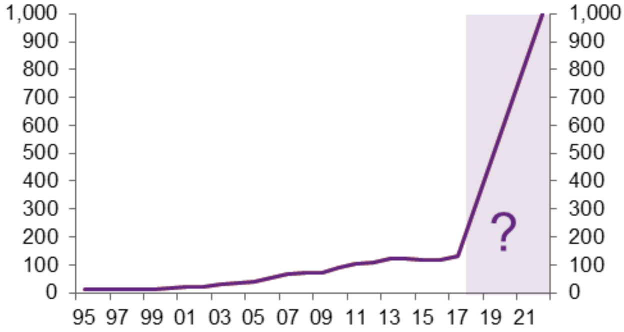
Under pressure exerted by the US, China is moving on these fronts. While achieving such measures could be beneficial, especially for the US, it is not necessarily the best outcome in all dimensions. In particular, targeted imports will create trade diversion for China, thereby reducing China's imports from the US' main competitors, Europe and Japan. Also, forcing better market access will not be sufficient to solve China's key economic characteristic, i.e., state capitalism.

As such, the true target of the US seems to be not only turning China into a market economy, but rather pushing it into a stream of imports from the US and forcing it to offer better market access to foreign companies. However, even such agreements cannot be fully achieved in a single meeting because of the complex reality. The most likely outcome of this round of negotiation is to reach consensus on some specific measures. That said, the "partial" deal should still be perceived positively by market participants because it allows both parties to freeze additional import tariffs which had been announced earlier.

Down the road, China's increasing wages and its quest to bypass the middle-income trap leave no option for China but to continue to move up the technology ladder. The movement will only increase the US' containment forces, especially as far as technology is concerned. The announcement of possible progress is at most a "partial" deal, which could be well received in the market but is only a temporary solution which masks the structural competition between the two economies.

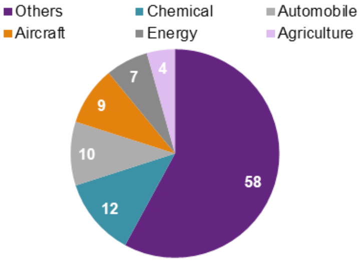
All in all, for the ongoing negotiation, China needs to accommodate the requests to calm the US, but it cannot give up its strategy of moving up the technology ladder to escape the middle-income trap.

Chart 1
US Export to China (USD bn)



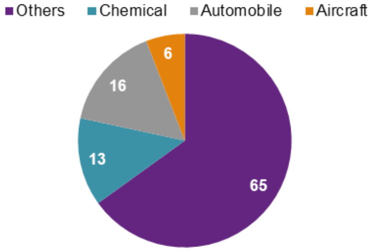
Source: Natixis, UNCTAD

Chart 2
China's import from US
Breakdown by sector (%)



Source: Natixis, UNCTAD, UNCOMTRADE

Chart 3
China's import from EU
Breakdown by sector (%)



Source: Natixis, UNCTAD, UNCOMTRADE

3. AN ACCOUNT OF US-CHINA TRADE PROTECTIONISM

From seemingly untargeted measures announced in early February 2018 for solar panels and washing machines, the US has moved to increasingly targeted action against China. The most obvious case in point was the announcement of 25% additional import duties to be applied to USD 50 billion equivalents of imported goods from China on the basis of China's infringement of intellectual property rights (Garcia Herrero, 2018a). More importantly, about two thirds of those import tariffs have been applied since 6 July. The US' speedy introduction of the announced import tariffs, without allowing for much time to negotiate a deal between China and the US, shows the US resolve to move away from the status quo in terms of the functioning of the global trading system, at least as far as China is concerned. On that basis, China had no choice but to retaliate with equivalent import tariffs on US goods.

Since then, the list of Chinese imports that the US is aiming at increasing tariffs on has expanded to an additional USD 200 billion. Thanks to a three-month truce reached recently at the side-lines of the G-20 summit, the additional USD 200 billion goods from China will not be confronted with a 25% import tariffs yet but it looks increasingly clear that this is just a truce to buy time for both sides and that the confrontation is escalating. The recent arrest of Huawei's CFO because of a potential breach of sanctions against Iran is the proof of the pudding of how far the US is ready to go in weaponizing its current hegemonic position as rule setter.

Going back to the trade war, China's ability to retaliate on trade is obviously more limited as it does not import enough goods from the US to match the announced additional USD 200 billion in import tariffs from the US, which explains why China's second batch of retaliatory measures have been more moderate, at least in size (USD 60 billion). Also the latter have been put on hold thanks to the recently agreed three-month truce.

The market reaction so far seems to have been more negative for China than the US, at least as far as the stock market is concerned, which has lost more than 20% in value year to date. Furthermore, the RMB has depreciated quite substantially since the beginning of the trade war until recently, helped by the recently announced truce between the US and China. One may wonder whether the market is overreacting to the potential consequences of such a trade war on China or, perhaps, underestimating the impact on the US. So far, European markets seem to have remained relatively more insulated from the US-China trade war except when the US pointed towards protectionist measures against Europe directly, as was the case when the tariffs on EU steel and aluminium were raised in spring 2018 and threats over increasing import tariffs on autos and auto parts were made in early summer 2018. Moving on to the potential economic impact of the trade war, there have been attempts to estimate the direct impact of tariffs on trade and, thereby, on growth. For example, the International Monetary Fund (IMF) in its latest World Economic Outlook has estimated that the Chinese economy would grow 1.6% point less in 2019 and the US economy would grow 0.9% point less in 2019 if the trade war were to be maintained in 2019. Also, the Euro area's growth rate would be shelved by 0.4% in that scenario. The World Bank, in contrast, has a much more benign scenario in its latest global economic prospects, as it has estimated that the Chinese economy will only grow 0.2% point less in 2019 and the US economy will grow 0.2% point less in 2019. In the same vein, estimates of price and income elasticities of Chinese exports into the US by Garcia Herrero (2018b) point to a relatively limited value of China's total exports affected by tariffs. Even if the USD 200 billion Chinese goods were to be confronted by full 25% tariffs, the overall impact on Chinese trade would be limited to only 3% of China's exports and only 1.3% of the US' exports.

Overall, the reason for this relatively limited economic impact, especially when compared with the very negative market reaction, especially for China, is that such exercises only take into account the direct effects of tariffs on trade and not indirect effects on investment through a worsening of market sentiment, among many other channels. The impact on expectations and, thereby, future investment, is probably behind the market fear, especially in China but also in the US and, to a lesser extent, Europe.

The issue is that the market may be realising that the risk is not only protectionism but much more than that as the US' ultimate goal is to try to contain China. In fact, investors both in China and abroad are starting to worry that their investments may possibly be completely blocked by the US or indirectly affected by the worsened relationship between China and the US (Garcia Herrero and Xu, 2018). Moreover, the multilateral trade order maintained by the US is likely to be massively transformed. If that happens, the world will have to return to a much less free system for goods and services flow. It is due to these increasing uncertainties that market investors' sentiments have become more and more negative.

One way to go about analysing the potential impact of the ongoing trade war might be to look in more detail at the measures taken so far and analyse their rationale so as to draw conclusions about their potential consequences down the road.

4. A DEEPER ANALYSIS OF THE TRADE MEASURES TAKEN BY THE US AND CHINA

The analysis of the sectoral composition of the goods targeted by the US administration would support the view regarding relevant structural changes to happen in the global economy due to the trade war. The first round of the US tariffs (USD 50 billion) was aimed at China's high-end exports, with a view to containing China's technological advance, with 7% on very high technology products and 55% on high technology products (Garcia Herrero, 2018c). Some of the products included in the US tariffs list have not been exported to the US yet, such as aircraft and aerospace or arms and ammunition, so the US' true intention of the tariffs is not to reduce the trade deficit with China, but to contain China's move up the technology ladder. By including products that do not contribute at all to the US' bilateral deficit with China, one could argue that the US is revealing its preferences, at least indirectly, which are to contain China in what it wants to become, namely a technological power that competes with the US in high-end products.

Very interestingly, China appears to have realised quite quickly the US intention as it has rapidly modified its own retaliation list from a more balanced one which included high-end imports from the US (including aircraft and aerospace) to one more focused on low-end products, such as agriculture (especially soy) and energy. Such a strategy makes sense as imposing tariffs on high-end products which China does not yet produce or cannot be sourced from anywhere else would only hurt China. This is because it would only increase the price of products needed for China to achieve its ultimate objective, namely, to move up the value chain ladder.

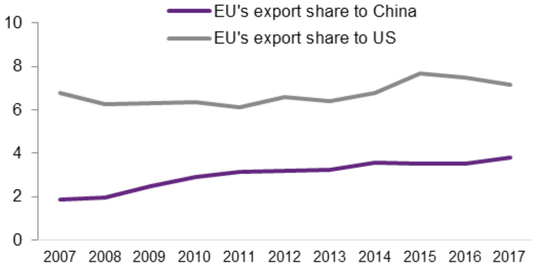
Moving on to the second set of import duties announced by the US, namely that of USD 200 billion to be imposed by 30 August, the products composition seems to be very different. In fact, low-end products dominate but, interestingly, very few of them are final – especially consumer – products (with only 22% of the total) but rather are intermediate products. One could interpret this second wave of import tariffs as a way to re-shore the production of intermediate goods back to the US (or at least to a third country which is not China) and reduce China's role in the global value chain. This interpretation of the second round of tariffs could have tangible implications for third countries which are now part of the value chain and have better economic relations with the US (even a free trade agreement which insulates them from increases in US import tariffs across the board). This is the case with Vietnam as well as Mexico (if NAFTA is finally renewed). But the US has silently removed some key products which would be expensive to substitute in terms of increase in prices for the final consumer (such as white goods for which China has become the largest supplier by far).

For this second round of tariffs, China's retaliation is much smaller, only USD 60 billion, due to the limitation of the total volume of China imports from the US. Yet, it is already a large bulk of the total retaliation list China can further extend. In this round of retaliation, all low, medium and high technology stuff are included, which shows a determined stance by the Chinese authorities that they will not retreat from the US threat. Also, more high-technology products were included as China's imports from the US are limited.

5. WHAT IS THE IMPACT ON EUROPE?

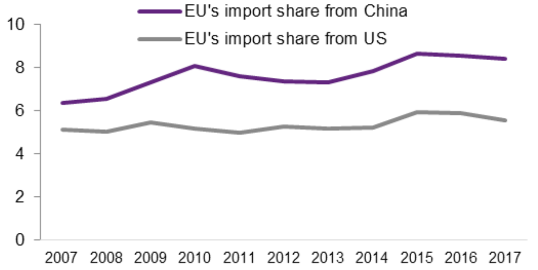
Potential European gains or losses arising from the US-led trade war on China will very much depend on whether Europe remains neutral on the US-China trade war instead of following the US' lead by imposing import tariffs on China. If the EU is forced to pick the US side and imposes its own import tariffs on China, China will probably also retaliate against EU companies. It should also be noted, though, that the potential gains to be made are bigger in the US (beyond the already larger export revenues), largely due to more tariffs imposed from the US side. In other words, beyond Europe's historical alliance with the US, which will keep the EU closer to the US than they would ever be with China, the EU also fears losing the US market even more than that of China as its export share to the US is larger than China (Chart 4) while China remains more relevant for EU imports (Chart 5). The fact that Europe, an overall net exporter, continues to maintain a bilateral trade deficit with China does not help (Chart 6). Obviously, a neutral stance as regards China is the best of all situations, with some clear winners among European export sectors, but the US clearly comes first in the EU's interests even if you only focus on trade gains.

Chart 4
EU's export share to China and US, 2007-2017, %



Source: UNCTAD

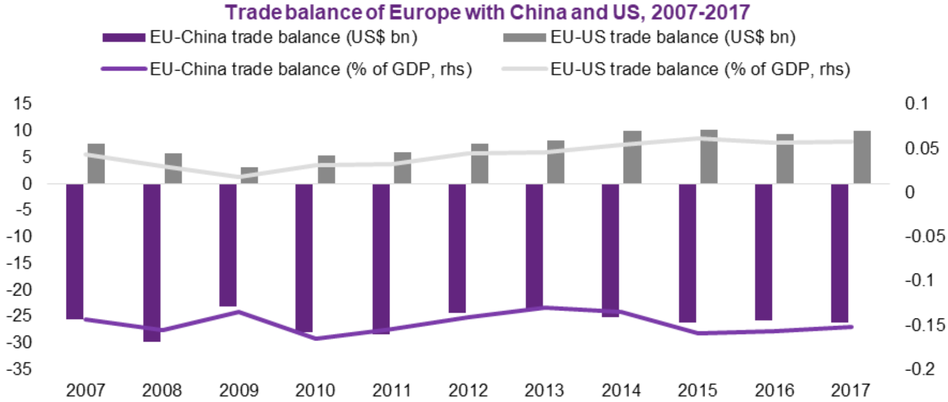
Chart 5
EU's import share from China and US, 2007-2017, %



Source: UNCTAD

All in all, our analysis shows US-China trade frictions are here to stay in so far as they are a response to a fight for hegemony in the global economy. The US wants to contain China's future – which basically implies direct competition with Chinese products in third markets. In that regard, Europe, being export oriented and with a similar economic structure, can benefit by substituting some of their exports to China. This, however, requires that there be no retaliation from the US towards Europe. Otherwise, it will be extremely difficult for the EU to keep a neutral stance on the trade war.

Chart 6
Trade balance of Europe with China and US, 2007-2017

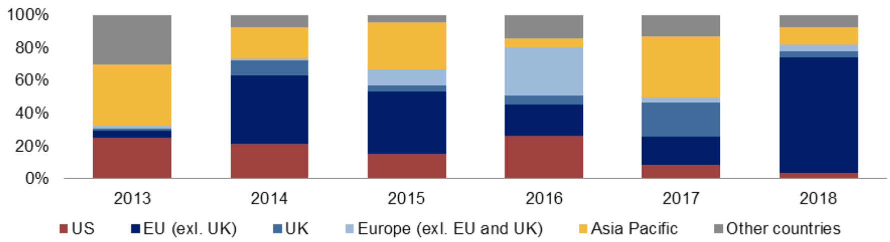


Source: UNCTAD

Beyond trade an increasingly important consequence of the US strategic competition with China is that the latter is turning to Europe to acquire relevant companies to move up the technology ladder. More specifically, in 2011, China's outward foreign direct investment (FDI) (including that from Hong Kong) accounted for only 1 percent of EU total inward FDI, whereas China took 3.5 percent of the EU's outward

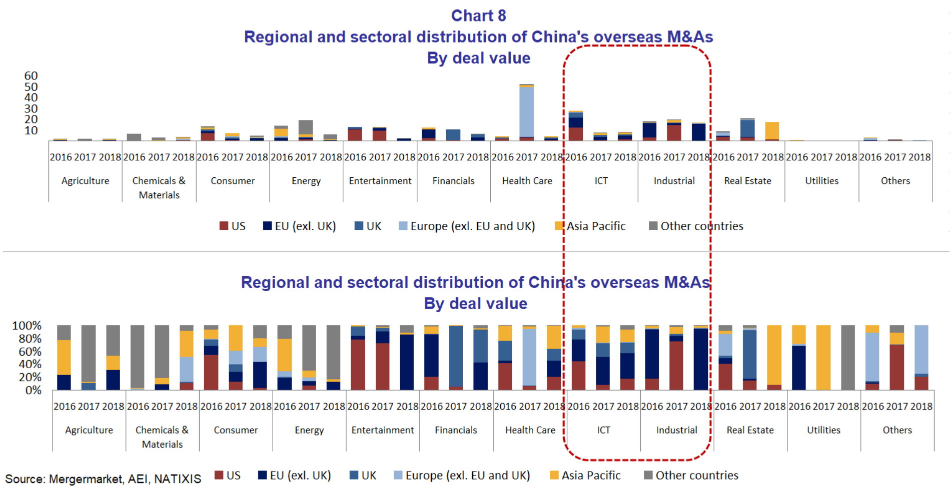
FDI. Given the size of the Chinese economy in the world already in 2011, this can be considered relatively modest. The situation today is very different. Chart 7 shows that Europe, especially the EU-27, has become, by far, the most attractive destination for China's overseas acquisitions, accounting for 70% of the total in terms of deal value, particularly in the industrial and information and communications technology (ICT) sectors where China has been eager to cooperate to climb up the technology ladder (Chart 8). Because the US has closed its door to China on the basis of "national security concerns", the EU is now the only place that is easier for China to access in buying foreign companies.

Chart 7
Destination of the overseas completed M&A
The percentage by deal value



Source: Mergermarket, AEI, NATIXIS

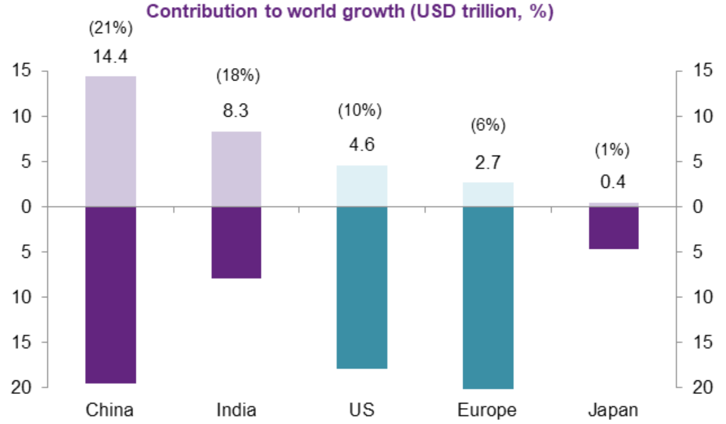
Chart 8



6. OPTIONS FOR EUROPE IN LIGHT OF INCREASING ECONOMIC COMPETITION BETWEEN CHINA AND THE US

What the US-China trade war has brought about is not only short-term trade tensions, but more importantly, a systematic shift in the trade order which has supported the world's development for the past century. Undoubtedly, the US and China will be the most influential bloc in the 21st century, and their conflict is doomed to be long lasting. While the two countries may find some temporary solution to the current tariffs dispute, their conflicts are intrinsically embedded in the competitive stance, which could only be exacerbated in the future. This is all the more natural when we realise that China's economy is already as large as that of the US (at least in purchasing power terms and soon in USD terms) but, most importantly, will contribute more than three times that of the US to the global economy in the next 10 years (Chart 9). In other words, although the US is a more important market for Europe today, this will soon no longer be the case, based on the positive growth differential between the US and China, which continues to be very large.

Chart 9
Contribution to world growth (USD trillion, %)



Source: Natixis

The global influence of the US-China cold war will be persistent. At this turning point, as the world's only figure that can balance the power between the US and China, the EU has to decide how to respond to the trade war. There are several options under current discussion.

Safeguard multilateralism?

The EU has long called for economic multilateralism and is pushing for the reform of the WTO to adapt to China's sheer size without it having become a market economy. In fact, one could argue that one of the key areas of contention from the US side is indeed China's different economic model while still being part of a free trade world. The European response to this reality is to keep, if not enhance, multilateralism, by reforming existing institutions, especially the WTO, so as to impose market practices on all members in order to protect fair trade (Demertzis, 2018).[1] This really means that the WTO will need to address the issue of the large role of state-owned enterprises (SOEs) in the production of goods and services and the pervasive role of subsidies in production. This would bring the WTO close to the US concerns over China's unfair practices in international trade.

While the EU may easily find common ground on the key issues with the US (only if the current US administration were to engage in such a reform, which is not the case now), it could be hard to achieve the requested reforms in China. In fact, the role of SOEs is considered key in China's model of socialism with Chinese characteristics and, thus, they are impossible to dismantle in the foreseeable future. The Chinese will argue that the role of SOEs remains moderate[2] and, thus, should not be an issue for WTO reform. The Chinese have also borrowed the concept of competitive neutrality from the Organisation for Economic Co-operation and Development (OECD) and have argued that they are increasingly close to applying competitive neutrality among companies operating in China. Garcia and Xu (2017) hold a very different view on the role of SOEs in the Chinese economy both because of their more pervasive influence but, more importantly, because of their very different nature compared to other SOEs in the world. In fact, the key reason for their unequal footing with the rest of companies operating in China, including private Chinese companies, is their preferential access to market in many sectors as well as their special connection with China's long-standing ruling party, namely the Communist Party.

That said, the EU will also find the US difficult to cooperate with in the reform of the WTO. Since his arrival to power, Trump has pushed "America first" policies and certainly not policies in support of multilateralism. In fact, the tariffs measures taken by the US based on "security" reasons while bypassing the WTO's multilateral

1 For more details as to how Europe can defend multilateralism in the world and what the options are for Europe, please see, Jean, S., Martin, P., and Sapir, A. (2018) and Wolff G. (2018).

2 According to China's National Bureau of Statistics, in 2015, SOEs accounted for 38.8 percent of total assets for industrial enterprises above scale.

settlement mechanisms is a clear sign that the US may overthrow the multilateral value based on its own interests. As such, while the US seems to share more of the market and democratic values with the EU, it does not seem ready to fully conform to the EU's proposal for a WTO reform so as to preserve multilateralism.

Under such circumstances, it does not seem very credible for the EU to continue to push the agenda of multilateralism without the support of the US and China. On the other hand, though, it looks extremely dangerous for the EU not to do so as it is no longer a superpower, nor does it intend to be one. All in all, while continuing to make efforts to preserve multilateralism, Europe may need to explore other responses to the current standoff between China and the US, aware of the increasingly slim chance that multilateralism becomes the driving force again.

Enhancing Europe's Reliance on the Transatlantic Alliance?

Another potential option for Europe is to maintain the status quo while reinforcing it on the basis of an increasing economic confrontation between the US and China. In other words, the EU may also choose to lean completely on the US. The question is whether it is wise to do so in the current environment with clear changes in the US attitude towards multilateralism. This is all the more disappointing in so far as it was the US which had pushed for such a system, as a way to create a safe environment for its allies and eventually to enable it to engage the rest of the world after the collapse of the Soviet Union.

The current US administration has made it very clear that multilateralism and open trade is something of the past. The gunfire that the US has triggered is not only against China but against many other countries, including the EU. Just in 2018, the US has already threatened tariffs on steel, aluminium, and cars on the EU. It also criticised the EU for its large trade surplus against the US. Also, the US has criticised the EU for not fulfilling its economic responsibility on military spending as members of the North Atlantic Treaty Organisation (NATO). As such, the EU alliance with the US will be more costly for the EU than it has ever been as the US is not happy with the current distribution of costs and benefits of the Transatlantic Alliance.

More importantly, because the US has chosen a non-market bilateral way to deal with China as well as other issues, the EU's complete support for the US will mean that it has to give up on its rule-based approach to problem solving and, thereby, its principles. This is obviously very costly for the EU as its own internal market is based on a strong rule-based system as well as for the world since the EU is the bastion of multilateralism. The case of the reform of the World Trade

Organisation is a clear case in point since the EU is really holding on to it and would probably not manage to do so if pushed towards a relation of clear dependence on the US.

There is another practical reason which restricts the EU from leaning on the US completely. The EU is not a single country but a group of 28 (soon probably 27) countries which have different views about the US and also about China. In fact, while it may be easier for Western Europe to unite against China, Eastern Europe, but also Greece and Portugal, and recently perhaps even Italy, may express opposing views as to a strategic alliance with the US which requires leaving China aside. In fact, the recent effort of the EU to establish an EU-level investment screening system resembling the US' famous Committee on Foreign Investment in the United States (CFIUS) has been vetted to such an extent by some EU members that its final version is really very limited in scope and hardly a threat for China. China has also created a platform with Eastern European and Balkan countries, the so-called 16+1, since all of these countries are part of China's Belt and Road Initiative (BRI). Many of these countries expect to ease their financial concerns through investment from China as well as to reduce their dependence on Brussels. This, in itself, poses problems for the EU and might actually push it even closer to the US, notwithstanding the costs.

Strengthening Cooperation with China

Strengthening cooperation with China is also a practical – albeit unlikely – choice for the EU in so far as its current strategic ally, the US, is moving away from multilateralism, thereby harming EU interests. In fact, not only is China's economy of a similar size to the US already today but its contribution to global growth will be much bigger in the future, as previously shown. This means that opportunities in the medium term should be bigger in China but under a very important hypothesis: market access.

This is why most of the discussion as to whether Europe should rebalance its economic partnership towards China, at least partially, boils down to improving European companies' market access in China. Within that context, the EU had started negotiating a bilateral investment agreement (BIT) with China at a time when the economic relations still had a positive perception from the European side but things have changed quite dramatically since then. In fact, the 12th round of BIT negotiations has been without an agreement. The key stumbling block is indeed market access for European companies in China and reciprocity, which is of course related to the perceived lack of market access.

Beyond market access, EU authorities are concerned about potential discrimination against EU investors operating in China, including explicit or implicit preferential subsidies for certain enterprises. Such discrimination may also be a factor for Chinese companies operating in Europe. While market access is a more general issue, potential discrimination by means of implicit or explicit subsidies has linkages to the role played by Chinese SOEs. This is not only true for the Chinese economy, but also for Chinese investments in Europe because a good part of it (most of it until very recently) originates from SOEs.

In China, SOEs have a much wider scope as they originate from the planned economy era when they dominated all sectors (either SOEs or collectively owned companies). Most Chinese SOEs, even now, are not established on the basis of correcting market failure, but more to carry out government objectives. Chinese SOEs are bigger, more pervasive, and more dominant than their EU counterparts, and, more importantly, exist in nearly every key sector in Chinese society. Against this backdrop, the Chinese government has created a special favourable environment for the SOEs. This actually triggered the concerns over their unfair competition in the international market and is one of the key barriers confronting China's building of an economic alliance with the EU. The hope for an EU-China BIT is that it should foster investments on both sides, but the reality is that, at this current juncture, Chinese investment into the EU is ballooning while EU investment into China is slowing down and is already smaller than that of China's investment into the EU.

All in all, given the increasingly difficult relations with the US, a certain degree of rebalancing towards China should be explored by the EU. However, the key stumbling block will continue to be China's state capitalism and the lack of market access for foreign companies. For the specific case of state-owned enterprises, preferential market access in China, rather than ownership of SOEs, should be the key consideration for European policy makers when evaluating the undue advantage enjoyed by Chinese corporates. This is because private companies with ties to the Chinese government might also benefit from preferential market access. The recent case of Huawei shows how much the Chinese leadership may support key private companies, especially if they belong to strategic sectors.

More generally, the highest priority issue that an EU-China BIT should pursue is market liberalisation, so that any market access granted through the BIT puts European companies on an equal footing to their Chinese competitors (even with SOEs). This obviously requires, at least, reciprocity (García Herrero and Xu, 2017). In fact, market liberalisation is important not only for foreign companies but also for Chinese private companies so that gains are also shared with China.

While engaging with China in its liberalisation and opening up, the EU cannot remain fully open to China's acquisitions of technology and the competition of Chinese state-supported companies in the single market. Europe has just announced a stricter framework for the screening of foreign investment (mainly directed at Chinese companies). Still, three key instruments might be used, with some reinterpretation of the EU Treaty, namely competition, dispute resolution and state aid policy. The first one does not require explanation nor does state aid policy, with the caveat that it cannot yet be applied to non-Member States. As for dispute resolution, identifying unfair behaviour by a firm can be easier after a firm reveals its status by operating in the EU market. An appropriate dispute settlement mechanism can protect both European and Chinese corporates. Among the different options, an investor-state dispute settlement system (ISDS) seems to be favoured internationally, but would need to be revised so that governments (either China or EU governments) do not fall prey to corporates suing them without clear justification. Furthermore, in the Chinese case, the very close links between corporates and the Chinese government (especially when operating abroad) could make the ISDS a double-edged sword for the EU, because in certain cases China could, for its own purposes, support its enterprises in suing EU companies. In addition, the implementation of the ISDS might be difficult in China where experience with investor-state arbitration is rather limited and there is very low probability that the Chinese government will enforce foreign court decisions. A revision of the ISDS is thus warranted so as to balance the interests of the parties in the BIT negotiation.

As such, we can see that Chinese internal reform is the key for the EU to pursue a better alliance relationship with China. The priority issue that EU and China need to pursue is market liberalisation, so that any market access granted through the BIT puts European companies on an equal footing to their Chinese competitors (even with SOEs). This obviously requires, at least, reciprocity. Yet, there is still a long way to go in this direction.

7. CONCLUSIONS

This paper reviews the impact of the US-led trade war against China and its immediate consequences, not only for China and the US, but especially for the European Union. The first thing to note is that although protectionism can never be growth enhancing, and certainly not for a net exporter like the EU, there are still gains to be made by European companies from the ongoing US-China trade confrontation in so far as they may be able to substitute US exporters into China or, less so based on our findings in this article, Chinese exporters into the US. Unfortunately, the current truce agreed between the US and Chinese governments at the sidelines of the G-20 meeting might reduce such opportunities for EU exporters and might even create trade diversion, again from European products and in favour of American products.

The fact that the EU feels increasingly squeezed between the US and China in their strategic competition should push us to ponder our options in the current global set-up. So far the EU's option seems to have been to support multilateralism at any cost. Unfortunately, the latter is increasingly less likely as the US has no intention to revert to the model which it once helped create. On that basis, and given Europe's reluctance to play a leading role without the US, the push for a return to multilateralism seems more an option of the past than an option of the future, let alone the present. The second most obvious option for the EU would be to increase its dependence on the US or, in other words, to push its strategic alliance further. However, we should realise that this comes at a cost, more specifically two concerns which were not present before. The first is the increasing unreliability of the US as an ally and its insistence on a seemingly different distribution of costs and benefits with its allies (more costs for the EU, such as military expenses, but fewer benefits on the trade side). The second caveat concerning a further reliance on the US is the need to align against China on issues of interest to the US. Although such issues are not too different from the complaints raised by the EU with respect to China (market access, reciprocity, excessive role of the state in the economy and a stronger defence of intellectual property rights), the reality is that the US interest will come first in this battle. In other words, the EU could lose its potential preferential access to China because of a stronger alliance with the US. Finally, the third option, namely rebalancing toward China, at least partially, cannot be an option for Europe in the current circumstances because of very limited access to the Chinese market. However, if China were really to further open up its economy to foreign competition (i.e., offer full market access), this option could become much more favourable. Based on past experiences since China entered the WTO, this option seems highly unlikely but worth pursuing. In that context, China's willingness to open up its markets to foreign competition clearly requires market access and reciprocity. While China makes up its mind on whether the above is a real option, the EU has no choice but to protect its strategic sectors from China's acquisitions and to safeguard the single market from unfair competition from Chinese SOEs.

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Economics and Trade Impact of the Silk Road Economic Belt Initiative

Kaewkamol Pitakdumrongkit

The Belt and Road Initiative (BRI) is a project proposed by China to foster and enhance connectivity between Asia, Europe, and Africa. Chinese President Xi Jinping proposed the Silk Road Economic Belt during his visit to Kazakhstan in September 2013 and unveiled the Maritime Silk Road during his speech at the Parliament in Indonesia in October 2013. Since its official launch, BRI has increasingly been promoted by Beijing. For example, in December 2013 the BRI was discussed at the Central Economic Work Conference, a gathering of top Chinese leaders.[1] In November 2014, President Xi announced that China would establish the Silk Road Fund with a capital of US$40 billion as a financing mechanism for BRI.[2] The document "Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road", published in March 2015, elaborated on the details of this scheme. In December 2015, the Asian Infrastructure Development Bank (AIIB) was created to additionally finance connectivity projects.[3] Beijing, in May 2017, convened leaders from more than 30 nations to the Belt Road Forum. At this meeting, several countries and international organisations signed agreements with the former to advance the BRI concept.[4] The 19th National Congress of China's Communist

[1] http://www.china.org.cn/opinion/2013-12/25/content_30996971.htm, accessed 16 January 2019.

[2] Chan, Minnie, 2014. "China to create US$40 billion Silk Road Fund to upgrade Asia links", *South China Morning Post*, 9 November.

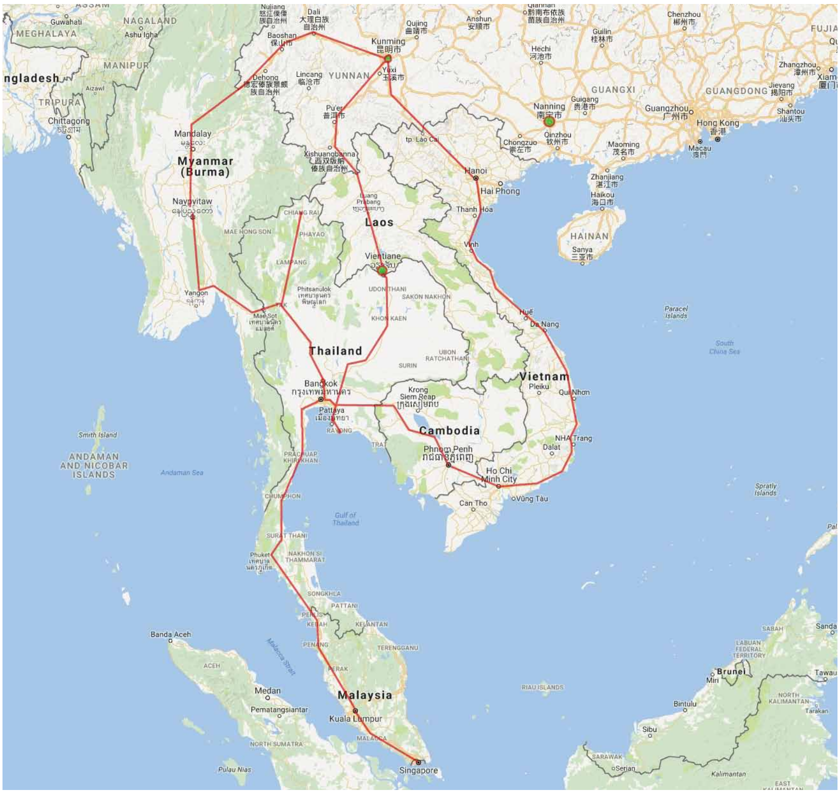
[3] Low, Aaron, 2015. "Looking back: Key events that impacted markets and global economy in 2015", *The Strait Times*, 22 December.

[4] Tiezzi, Shannon, 2017. "What Did China Accomplish at the Belt and Road Forum?", *The Diplomat*, 16 May.

Party, in October 2017, incorporated BRI into the Constitution to further solidify Beijing's commitment in pursuing this initiative.[5]

The BRI has two components: the 21st Century Maritime Silk Road, and the Silk Road Economic Belt. The former is a sea-based initiative striving to connect the South China Sea, Indian Ocean, Mediterranean Sea, and Suez Canal. On the other hand, the latter is a land-based programme aimed at linking the Chinese economy to the Asian, Middle Eastern, and European ones. The Silk Road Economic Belt envisages six economic corridors: (1) China-Indochina Peninsula; (2) Bangladesh-China-India-Myanmar; (3) China-Pakistan; (4) New Eurasian Land Bridge; (5) China-Central Asia-West Asia; and (6) China-Mongolia-Russia (Figure 1).

Figure 1: Map of CICPEC.



Source: Luft, Gal, 2016. "China's One Belt One Road Initiative: An American Response to the New Silk Road", Institute for the Analysis of Global Security, Washington D.C., United States of America.

[5] *The Straits Times*, 2017. "19th Party Congress: Belt and Road in CCP charter shows China's desire to take global leadership role", 24 October.

This paper examines the effects of BRI on Southeast Asian countries and global economic relations. It aims to answer the following puzzles: (1) What are the key trends of BRI?; (2) How has BRI affected China's trade and investment patterns, its diplomatic reach, and its soft power in the Southeast Asian region?; (3) What are the economic implications of BRI for global economic relations?; and (4) Why is BRI still perceived as a debt trap by the regional states? To shed light on these questions, I chose to analyse the China-Indochina Peninsula Economic Corridor (CICPEC) under the Silk Road Economic Belt because it is aimed at linking eight major economic and transportation hubs in China and Southeast Asia, Nanning (the capital of China's Guangxi province), Vientiane (Laos' capital), Phnom Penh (Cambodia's capital) Bangkok (Thailand's capital), Ho Chi Minh City (Vietnam's capital), Hanoi (a Vietnamese city), Kuala Lumpur (Malaysia's capital), and Singapore. Consequently, this arrangement has greater potential to impact Southeast Asia than the other Belt initiatives.

1. KEY TRENDS

CICPEC consists of several projects to boost connectivity between China and Southeast Asia. Regarding land transport, CICPEC seeks to link Chinese cities (especially Kunming and Nanning) to those in Southeast Asia by major land routes. First, the Central Route starts in Kunming, then goes to Vientiane, and down to Bangkok, Kuala Lumpur, and Singapore. Second, the Eastern Route connects Kunming to Hanoi via the Mengzi-Hekou Railway, which started its operation in December 2014.[6] From Hanoi, the route will lead to Ho Chi Minh City. Finally, the Western Route links Kunming to Yangon using the Dali-Ruili Railway.[7]

It would be a mistake to think that CICPEC consists of only the routes above. On the contrary, there are other land courses under this framework designed to reach certain key regional commercial and logistics hubs. The 250-kilometer Bangkok-Nakhon Ratchasima railway is a case in point. Once built, it will connect Bangkok to Nakhon Ratchasima (Thailand's commercial hub in its northeastern region); subsequently it will be extended to Nong Khai (a Thailand-Laos border town) and eventually to Laos. Other plans are geared towards developing land links to reach economic centres in Guangzhou and Hong Kong. In addition, CICPEC encompasses

[6] Ge, Jieru, 2014. "Mengzi-Hekou Railway to start operation in December", *China Daily*, 3 November.

[7] *Business Times*, 2018. "A Primer on China's Belt and Road Initiative Plans in Southeast Asia", 2 April.

projects to develop seaports, economic zones, industrial parks, and tourist destinations in Southeast Asia. For instance, the Melaka Gateway Project in Malaysia encompasses a cruise passenger terminal, a commercial city, and a maritime industrial park.[8] The combined population under the CICPEC framework is estimated to be about 50 million.[9]

As far as progress is concerned, the projects along the Central Route are the most advanced. For example, the Kunming-Vientiane railway is under construction and expected to be completed by 2021. The first part of the Bangkok-Nakhon Ratchasima rail line in Thailand was built in December 2017 and the whole railway is slated to be finished as early as 2022.[10] Regarding the Melaka Gateway Project launched in 2014, the authorities announced that 60% of the work had been done and that they expected it to be completed in 2025.[11] Moreover, China signed MOUs with some ASEAN nations to jointly develop economic cooperation zones. One example is the Mohan-Boten Economic Cooperation Zone, the first cross-national economic zone Beijing set up in the Southeast Asian region. In 2015, Beijing and Vientiane inked the Joint General Scheme to Develop the Mohan-Boten Economic Cooperation Zone, seeking to create such a zone at the borders of China's Yunnan province and Laos' Luang Namtha province.[12] In addition, the Malaysia-China Kuantan Industrial Park (MCKIP) in Pahang, modelled after its sister park China-Malaysia Qinzhou Industrial Park (CMQIP) in Guangxi province, was established in 2013.

8 Aisyah, Fara, 2018. "Cloudy future for RM40b Melaka Gateway", *The Malaysian Reserve*, 12 September.

9 Derudder, Ben, Liu, Xingjian, and Charles Kunaka, 2018. "Connectivity Along Overland Corridors of the Belt and Road Initiative", MTI Global Practice Discussion Paper No. 6, World Bank, Washington, D.C., United States of America.

10 *Bangkok Post*, 2017. "Thai-Sino rail contract bids to kick off by year end", *Bangkok Post*, 16 August.

11 Murali, R.S.N., 2018. "State gives the green light to Melaka Gateway project", *The Star*, 22 September.

12 http://english.mofcom.gov.cn/article/newsrelease/significantnews/201509/20150901109922.shtml, accessed on 15 January 2019.

2. HOW HAS THE BRI AFFECTED CHINA'S TRADE AND INVESTMENT PATTERNS, ITS DIPLOMATIC REACH, AND ITS SOFT POWER?

2.1. Effects on trade and investment

CICPEC is likely to bring about two-way economic gains as it can boost Beijing's trade and investment ties with ASEAN economies. For example, CICPEC has set up some cross-border economic zones such as the Friendship Pass in Pingxiang (a city in Guangxi Province bordering Vietnam). Such areas enabled Chinese entrepreneurs to employ Southeast Asians to work in their production processes to cut costs.[13] CICPEC can also help Chinese companies lessen the impact of trade clashes between China and the US on Beijing's economy. Even though both powers agreed to a 90-day truce in December 2018, during which they would attempt to resolve their conflicts regarding technology transfer and intellectual property,[14] the talk might not completely end the tensions and the trade war might continue. The Asian Development Bank (ADB) estimated that a full-blown Sino-US trade war would shrink Beijing's GDP by 1 percent within a few years.[15] In such a scenario, CICPEC offers an alternative for the state to deepen its trade and investment ties in Southeast Asia and thus ameliorate the effects of Washington's tariffs and other protectionist measures on its economy.

Likewise, CICPEC is likely to yield positive effects on ASEAN stakeholders in several aspects, namely, connectivity, trade, investment, and employment. First, as BRI, including CICPEC, seeks to build upon the existing regional economic integration frameworks such as Master Plan for ASEAN Connectivity 2025 (MPAC 2025), it has great potential to complement ASEAN's connectivity programmes. MPAC 2025 is purposed "to achieve a seamlessly and comprehensively connected and integrated ASEAN that will promote competitiveness, inclusiveness, and a greater sense of Community."[16] The scheme focuses on five strategic areas: (1) sustainable infrastructure; (2) digital innovation; (3) seamless logistics; (4) regulatory excellence; and (5) people mobility. Going forward, there could be more collaboration

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13 Zhang Li, and Shi Ruipeng, 2018. "Guangxi city bordering Vietnam enjoys booming foreign trade volume", *China Daily*, 6 December.

14 Breuninger, Kevin and Javier E. David, 2018. "US will hold off on raising China tariffs to 25% as Trump and Xi agree to a 90-day trade truce", CNBC, 3 December.

15 https://www.adb.org/sites/default/files/publication/471496/ewp-566-impact-trade-conflict-asia.pdf, accessed on 19 January 2019.

16 ASEAN Secretariat, 2016. "Master Plan on ASEAN Connectivity 2025", Jakarta, Indonesia, August, p. 9.

between China and Southeast Asian nations on these aspects. Also, CICPEC can help fill ASEAN's financing gap. According to the ADB, Southeast Asia will require US$2.8-3.1 trillion from 2016 to 2030 for infrastructure building. In other words, the region will need US$184-210 billion annually. However, the ASEAN Infrastructure Fund can only supply about $485 million. Such a financing deficit partly accounted for the slow progress of certain transnational connectivity projects, namely, the Trans-ASEAN Gas Pipeline and ASEAN Power Grid.[17]

Because CICPEC seeks to boost Sino-Southeast Asia connectivity, it can hence improve both sides' capacity to better receive foreign direct investment (FDI), galvanising transnational production networks and trade. The analysis by the ASEAN+3 Macroeconomic Research Office demonstrated that Chinese FDI in ASEAN and ASEAN FDI in China will rise to about US$500 billion and US$200 billion respectively by 2035. On the trade front, it was forecast that by 2035 China will account for 22 percent of ASEAN's total trade, while the latter is expected to account for 16 percent of Beijing's total trade.[18] Given that China-ASEAN trade and investments are projected to soar, CICPEC could further enhance these trends.

A close look at individual Southeast Asian economies reveals that CICPEC is beneficial to the former. For instance, the infrastructure projects can give Laos access to the sea, ultimately transforming it from a land-locked to a land-linked country. To elaborate, the Sino-Laos railway network could be expanded to connect to Thailand's Nong Khai province and Map Ta Phut seaport. This rail line has also been found to better link Laos' northern region to the electricity grids.[19] Also, CICPEC has provided jobs to the Vietnamese. As of October 2018, around 121,000 Vietnamese were working in the Friendship Pass, a China-Vietnam border economic zone.[20]

In Malaysia, MCKIP has attracted FDI from Beijing as several Chinese firms such as Alliance Steel and Huawei Technologies established their production plants in the

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[17] http://www.aseanenergy.org/blog/status-and-challenges-towards-regional-energy-connectivity/, accessed on 18 January 2019; Pitakdumrongkit, Kaewkamol, 2018. "Southeast Asia and China's Maritime Silk Road", presented at the CNA-RSIS Conference on East-Asia Maritime Issues, Copthorne King's Hotel, Singapore, 7 March.

[18] Poonpatpibul, Chaipat, Li, Wenlong, Foo, Suan Yong, Xinyi, Simon Liu, Tang, Xinke, and Tanyasorn Ekapirak, 2018. "China's Reform and Opening-Up: Experiences, Prospects, and Implications for ASEAN", Working Paper, WP/18-03, ASEAN+3 Macroeconomic Research Office (AMRO), October.

[19] Business Times, 2018. "A Primer on China's Belt and Road Initiative Plans in Southeast Asia", 2 April.

[20] Zhang Li and Shi Ruipeng, 2018. "Guangxi city bordering Vietnam enjoys booming foreign trade volume", *China Daily*, 6 December.

manufacturing and services sectors.[21] According to one Malaysian authority, this industrial park has created about 19,000 jobs and will further attract US$7.3 billion in investments.[22] The Melaka Gateway Project could generate additional Chinese investment, spurring Malaysia's employment rate and growth. Seeing the potential benefits of participating in CICPEC, Bangkok is planning to link it to the country's Eastern Economic Corridor, a special economic zone for high-tech industries such as smart electronics, robotics, and aviation with the potential to draw in $50 billion in investment to Thailand's economy.[23]

2.2. Impact on China's diplomatic reach

Beyond economic gains, BRI projects such as CICPEC can enable China to expand its diplomatic clout by using economic means to strengthen political ties with some regional stakeholders. The latter were sometimes found to accommodate Beijing's requests and shift their policy behaviour in its favour, affecting the regional dynamics. ASEAN's failure to coin a joint communiqué at the 45th ASEAN Foreign Ministers' Meeting in July 2012 was a case in point. While disagreements among Southeast Asian governments over what to be included in the statement regarding the South China Sea matters contributed to the debacle, one cannot deny that China's ties with Cambodia was another factor causing this incident.

Furthermore, Beijing's rejection of the July 2016 Tribunal Ruling concerning the South China Sea and continued construction of military installations on artificial islands have deteriorated the trust in China by the regional states and heightened the latter's fear that the former's use of economic diplomacy would negatively affect the regional order. Illustratively, Chinese facilities built under BRI in their countries could someday be converted to military outposts, altering Asian security dynamics. As one source posits, "Large ports in Pakistan, Sri Lanka and Malaysia – three countries along a major oil and commerce route from the Mideast and Africa – could someday double as naval logistics hubs."[24] As a result, BRI programmes,

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[21] Rahimi Yunus, 2018. "How will China-linked projects be impacted?", The Malaysian Reserve, 15 May.

[22] Aziz, Mohamad Azim Fitri Abd, 2018. "Opposition creates hate sentiment against BN with MCKIP", *The New Strait Times*, 30 April.

[23] Pongsudhirak, Thitinan, 2018. "China's Belt & Road impact on Thailand", *Bangkok Post*, 28 September; https://www.prnewswire.com/news-releases/thailand-targets-to-connect-belt-and-road-initiative-and-eec-to-boost-investment-opportunities-in-asean-300702545.html, accessed on 18 January 2019.

[24] Watkins, Derek, Lai, K.K. Rebecca, and Keith Bradsher, 2018. "The World, Built by China", *The New York Times*, 18 November.

including CICPEC, possess "the potential to erode the current security architecture in the region, allowing China to use its economic leverage to accumulate inordinate geopolitical power in its immediate neighbourhood".[25]

Such a trust problem was unveiled by the 2019 survey of regional experts and stakeholders by the Institute of Southeast Asian Studies (ISEAS). 51.5% of the respondents had either little or no confidence that Beijing would "do the right thing" in contributing to global peace, security, prosperity, and governance. 45.4% of them thought that China would become a revisionist state with an objective of turning Southeast Asia into its sphere of influence. When asked about the effects of BRI on their countries, almost half of these individuals believed that the arrangement would push ASEAN member states to get "closer into China's orbit…The fear of being drawn into China's orbit is widely shared across seven ASEAN member states: Singapore (60.2%), Vietnam (58.7%), Brunei (52.3%), Malaysia (51.8%), Thailand (51.3%), Indonesia (44.4%) and the Philippines (38.7%)."[26] To conclude, the economic benefits of BRI notwithstanding, this trust deficit may end up thwarting China's efforts to augment its diplomatic clout and domination in the region.

2.3. Effects on China's soft power

While greater attention has been paid to the infrastructure, one should not ignore the fact that BRI also seeks to boost people-to-people ties so as to bolster Beijing's soft power in the world. Soft power is defined as the "the ability to get what you want through attraction rather than through coercion."[27] Via BRI, China has been promoting its positive image through several means, such as Confucius Institutes offering courses on Chinese languages and cultures, educational exchange programmes and scholarships, cultural ambassadors, and development of English-language news outlets such as CCTV and China Daily newspaper.

However, such efforts have yielded little success. This is largely due to a mismatch between the image Beijing is trying to promote and what it is actually doing. For example, Confucius Institutes were chastised when they were found to be curbing academic freedom at host institutions regarding certain issues, namely, Taiwan,

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[25] Luft, Gal, 2017. "Silk Road 2.0: US Strategy toward China's Belt and Road Initiative", Strategy Paper No. 11, Atlantic Council, Washington D.C., United States of America, October, p. 29.

[26] Tang Siew Mun, Moe Thuzar, Hoang Thi Ha, Termsak Chalermpalanupap, and Pham Thi Phuong Thao, 2019. "Survey Report State of Southeast Asia: 2019" in ASEAN Focus, Issue 1/2019, Institute of Southeast Asian Studies, Singapore, January, p. 11.

[27] Nye, Joseph, 2004. "Soft power and American foreign policy", *Political Science Quarterly* 119: 255-270, p. 256.

Tibet, and Tiananmen Square.[28] The nation's crackdown on non-governmental organisations, media control and censorship, and rising assertiveness in the South China Sea have thwarted its efforts to enhance its persona in the international community.[29]

Moreover, Beijing's reputation has been suffering from the way it does business overseas. For example, its corporations were viewed as key players contributing to food safety and environmental degradation problems in other states, making the latter reluctant to adopt a Chinese model of development.[30] Other censures include a lack of transparency and little private sector participation as the majority of the infrastructure projects were awarded to state-owned enterprises (SOEs).[31] In short, 95 percent of BRI programmes have been implemented by the Chinese government and SOEs.[32] In addition, these entities tended to possess "a different view when it comes to labour and environmental strictures. To staff overseas projects, Chinese companies have flown in their own workers by the thousands, drawing complaints that they are doing little to create local jobs...[Also,] Beijing continues to export polluting technologies like coal-fired power plants, even as such projects have become unpopular in China."[33] In sum, the Chinese way of doing business seems to beget little buy-ins from the regional stakeholders and undermines Beijing's effort to strengthen its soft power in the region.

3. WHAT ARE THE ECONOMIC IMPLICATIONS OF BRI FOR GLOBAL ECONOMIC RELATIONS?

Some observers may contend that it is too soon to determine the effects of BRI on global economic relations given that it has only been launched for five years. Yet, evidence concerning Southeast Asian states' recent responses to this scheme can help us grasp such impacts. At the time of this writing, BRI, including CICPEC, is facing push-backs in the region. In short, Southeast Asian governments are

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28 https://www.dw.com/en/why-is-the-us-targeting-chinas-confucius-institute/a-43403188; https://www.nas.org/images/documents/confucius_institutes/NAS_confuciusInstitutes.pdf.

29 "China is spending billions to make the world love it", *The Economist*, 23 March; Lim, Kheng Swe, 2014. "China-ASEAN Relations: Hamstrung Soft Power in South China Sea?", RSIS Commentary No. 174, S. Rajaratnam School of International Studies, Singapore, 3 September.

30 https://www.cfr.org/backgrounder/chinas-big-bet-soft-power.

31 Moss, Daniel, 2018. "Indonesia's Jokowi counts on populism", *The Myanmar Times*, 8 May.

32 Greer, Tanner, 2018. "One Belt, One Road, One Big Mistake", *Foreign Policy*, 6 December.

33 Watkins, Derek, Lai, K.K. Rebecca, and Keith Bradsher, 2018. "The World, Built by China", *The New York Times*, 18 November.

increasingly reluctant to allow the projects to make headway in their countries. For example, in August 2018, Malaysia halted the US$22 billion East Coast Rail Link (ECRL) and a gas pipeline project in Sabah province, citing the prohibitive costs and Putrajaya's fiscal constraints.[34] Although the country's Prime Minister, Mahathir Mohamad, in January 2019 posited that his country could proceed with the ECRL if its construction cost was reduced, at the time of this writing the deal is still under negotiation.[35] Likewise, Myanmar, in August 2018, decided to scale down Beijing's stake in its Kyaukpyu deep seaport from US$7.3 to US$1.3 billion, constituting a 82 percent drop from the initial plan. This move was driven by the fact that Naypyidaw did not want its economy to be too reliant on China.[36] Additionally, Thailand delayed talks on the Sino-Thai rail line to acquire better contract terms. At the time of this writing, the Ministry of Finance is still pondering whether to borrow from the Export-Import Bank of China or from alternative financial institutions such as the World Bank and the ADB. A Thai cabinet member stressed that Bangkok could tap multiple sources to fund the construction.[37]

In conclusion, the evidence above indicates that BRI is not progressing as well and as fast as Beijing desires. For the initiative to have more significant implications for global economic relations in the future, Beijing must effectively address the issues causing concerns among the regional states, including transparency, business conduct, and Beijing's behaviour in the South China Sea. Failure to do so could lead to additional push-backs, diminishing the effects of BRI on a global scale.

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[34] Reuters, 2018. "Malaysia's Mahathir cancels China-backed rail, pipeline projects", 21 August.

[35] Strait Times, 2019. "Malaysia may resume East Coast Rail Link project, but on smaller scale: Mahathir", 2 January.

[36] Kapoor Kanupriya, and Aye Min Thant, 2018. "Exclusive: Myanmar scales back Chinese-backed port project due to debt fears - official", *Reuters*, 2 August.

[37] Theparat, Chatrudee, 2019. "Thai-Chinese high-speed rail opened up to foreign finance", *Bangkok Post*, 9 January.

4. WHY IS IT STILL PERCEIVED AS A DEBT TRAP?

Southeast Asian stakeholders are increasingly worried about Beijing's ability via BRI projects to create a debt trap problem in developing Asia. Such a perception was revealed in the 2019 ISEAS survey, which found that 70% of the ASEAN respondents agreed with the statement that their governments should be cautious when striking BRI deals with Beijing so as to avoid being trapped in an unsustainable debt situation.[38]

This angst about BRI intensified as ASEAN policymakers watched how the situations in Sri Lanka and Laos unfolded. Illustratively, in its efforts to avoid defaulting on its loans, the Sri Lanka government, in late 2017, granted a 99-year lease of the country's Hambantota Port (a project financed by Chinese loans) to Beijing. As a result, a Chinese SOE named Merchants Port Holdings is operating the facility.[39] Regarding the Kunming-Vientiane Railway, criticism centred upon the agreement details that enabled China to gain an upper hand over Laos in the long run.[40] In other words, the fact that this project costs the latter about US$6.7 billion, which is about half of the country's 2016 GDP of US$13.7 billion. This raised questions about Vientiane's ability to repay. Moreover, the contract grants Beijing the power to acquire Laos' land up to 50 meters on each side of the track, triggering concerns over sovereignty compromises when participating in China-led BRI projects.[41]

To sum up, in the eyes of ASEAN leaders, these cases demonstrated that BRI participants might not only become indebted nations, but also lose sovereign control over their territories. Sri Lanka's debt burden forced its government to give up control of its own seaport for 99 years while the land concession in Laos indicated Beijing's ability to dictate certain BRI terms in its favour. Therefore, Southeast Asian stakeholders still view such schemes as creating a potential debt trap.

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[38] Tang Siew Mun, Moe Thuzar, Hoang Thi Ha, Termsak Chalermpalanupap, and Pham Thi Phuong Thao, 2019. "Survey Report State of Southeast Asia: 2019", in ASEAN Focus, Issue 1/2019, Institute of Southeast Asian Studies, Singapore, January, p. 11.

[39] https://www.marinelink.com/news/china-merchant-port-holdings-pays-usd-mln-438870, accessed on 19 January 2019.

[40] Hutt, David, 2018. "Laos on a fast track to a China debt trap", *The Asia Times*, 28 March.

[41] Janviroj, Pana, 2017. "Laos; from land locked to land linked", *The Nation*, 12 September.

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Hang Together! The Case for Unity in EU Trade Negotiations with China

Frederick Kliem

After 15 years of negotiations (including GATT), the People's Republic of China (PRC) joined the World Trade Organization (WTO), an intergovernmental organisation overseeing regulation of international trade between member nations. Following successful negotiations between China and the WTO working party for China's accession, the eventual agreement[1] included commitments to be undertaken by China to provide non-discriminatory treatment to all WTO members: all foreign individuals and enterprises must be accorded equal treatment to enterprises in China with respect to the right to trade. China will eliminate dual pricing practices as well as differences in treatment accorded to goods produced for sale in China in comparison to those produced for export. Price controls will not be used for purposes of affording protection to domestic industries or services providers. The new member's commitments are to apply equally to all WTO members under normal non-discrimination rules. However, the EU leaves no doubt as to its opinion that there has been a frustrating lack of progress in giving the market a more decisive role in key areas of the economy and that EU enterprises face new and ever tougher restrictions in China, which go against market opening and the principles of equal treatment and a level playing field.[2]

In late March this year (2019), on a working trip to Europe, PRC President Xi Jinping visited, inter alia, French President Emmanuel Macron in Paris. Whenever possible, Beijing prefers bi- over multilateral avenues and avoids third party participation, making the most of China's relative weight advantage vis-à-vis its international partners. This behaviour has been criticised often in Asia, where Beijing

[1] World Trade Organization (11 December 2001), "Accessions: China", https://www.wto.org/english/thewto_e/acc_e/a1_chine_e.htm.

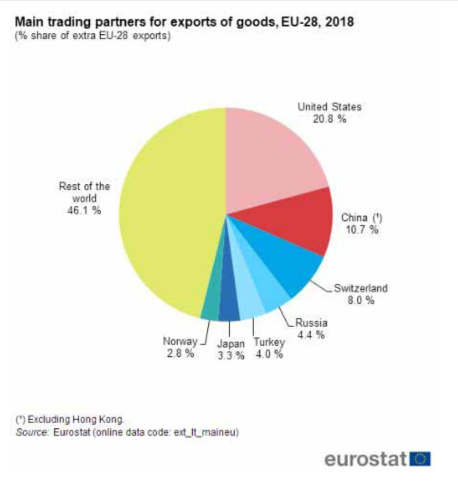
[2] E.g., EU Commission (2016), "Elements for a new EU strategy on China", http://eeas.europa.eu/archives/docs/china/docs/joint_communication_to_the_european_parliament_and_the_council_-_elements_for_a_new_eu_strategy_on_china.pdf.

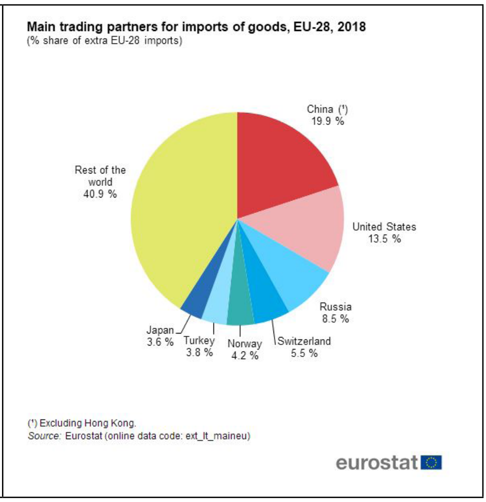
allegedly divides the Association of Southeast Asian Nations (ASEAN) by engaging the ten members of the organisation individually rather than as a united bloc. In Paris, however, two further invitees upset Xi's preference when Emmanuel Macron brought along his two strongest European allies: German Chancellor Angela Merkel and Jean-Claude Juncker, Chief of the European Commission. Whether or not Xi was disturbed by this remains speculation, of course, but what is evident is that this configuration is indicative of what Macron and other European leaders are working towards in their relations with China: a more coordinated European approach towards an awkward, but inevitable trading partner. EU leaders want to put multilateralism back on the menu and get tough on China, allegedly not complying with its commitments. Macron's effort also underscored division as the key weakness in the EU's external engagement process and symbolised the search for much-needed European unity at a time when Beijing is out to expand its global influence via its ambitious Belt and Road Initiative (BRI). In Europe, most EU nations, including Germany and France, willingly jump on the Chinese bandwagon at the expense of a united EU response.

While China poses significant challenges to international trade, competition and systemic differences do not equate to conflict. Cooperation between China and Europe and a healthy, market-driven competition on eye level is necessary. For this to be possible, though, Europe must "hang together". This article is about an unequal trade relationship that ought not to be unequal at all.

China and Europe need each other

The Chinese economic miracle is real. It began in the late 1970s under Deng Xiaoping, who led the People's Republic of China onto a path of successful economic reforms. Some four decades on, China has become the second largest economy in the world, growing dynamically year on year, and is the single most important cause and driver of global geopolitical and economic change. In spite of all the (often exaggerated) suspicion of, and problems with, China, the Chinese growth trajectory is a positive force for both domestic and global development. Not only have the last two decades of enormous growth propelled hundreds of millions of Chinese out of poverty and rapidly improved the socio-economic situation of the Chinese society at large, China's sustained growth has also benefited its European partners immensely, especially the strong export nations, Germany, France, Italy, Great Britain and the Netherlands. The European Union is one of the largest trading blocs in the world, its leading economies are significant exporting nations, and its financial centres are major hubs of capital exchange. As such, the PRC remains an important partner, and, to say that much upfront, neither the European Union nor any of its members can have any interest in a conflictual relationship with Beijing, least of all a Chinese containment strategy.





The Chinese market absorbs enormous exports and foreign direct investments (FDI) from Europe on the one hand, and feeds European markets with comparatively cheap consumer goods on the other. Both exchanges are particularly beneficial to the lower-middle income groups in Europe.

EU-China: Trade in goods

Trade in goods 2015-2017, € billions

Year	EU imports	EU exports	Balance
2015	351.0	170.4	-180.7
2016	345.1	169.7	-175.3
2017	374.8	198.2	-176.6

EU-China: Trade in services

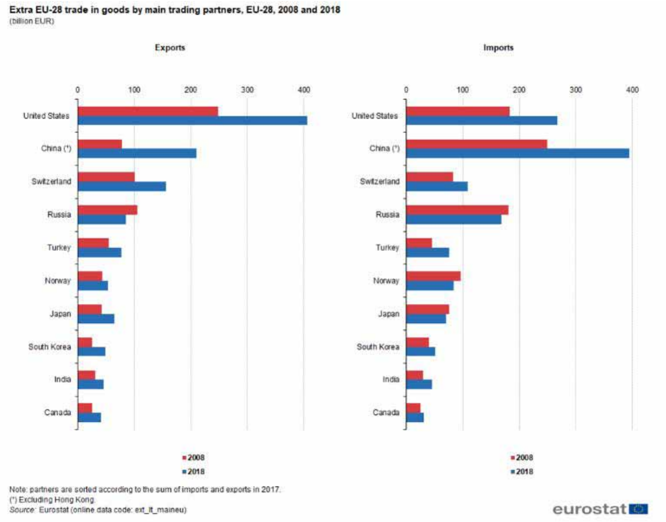
Trade in services 2014-2016, € billions

Year	EU imports	EU exports	Balance
2014	23.1	30.3	7.2
2015	28.7	38.3	9.7
2016	29.6	38.3	8.8

EU-China: Foreign direct investment

Foreign direct investment 2016, € billions

Year	Inward stocks	Outward stocks	Balance
2016	45.1	177.7	132.6



Between 2008 and 2018, the EU exports of goods recorded the highest growth rate for exports to China, which almost trebled over this ten-year period. China is the EU's second-biggest trading partner behind the US and the EU is China's biggest trading partner. China is the EU's biggest source of imports and its second-biggest export market. Europe's main imports from China are industrial and consumer goods, machinery and equipment, and footwear and clothing, while the EU exports mostly machinery and equipment, motor vehicles, aircraft, and chemicals.[3] Particularly Germany, Europe's leading economy and by far the largest net contributor to the EU budget, benefits from China's positive development trajectory. European companies have had an extensive role in facilitating Chinese development over the past decades. There have been significant transfers of technology and know-how, necessary for much of China's infrastructure and other development and Europe has been instrumental in creating a skilled Chinese domestic labour market. Mutual investment is significant and the European consumer benefited from comparatively cheap Chinese manufacturing, whilst the European labour market benefited from an increasingly strong Chinese consumer base. China is an important production base, consumer market, import source as well as one of the largest research and development (R&D) hubs in the world. The EU and China have the potential for mutually beneficial trade relations, spurring each other's further development.

[3] European Union, DG Trade (March 2019), "European Union Trade with China", https://webgate.ec.europa.eu/isdb_results/factsheets/country/details_china_en.pdf.

China remains an awkward partner

Having said this, the alluring Chinese market and inevitable and desirable cooperation should not obscure the fact that China is not an easy partner and there is an urgent need to recalibrate relations – not an easy ask from a major trading partner in an interdependent global economy. Slowly, the realisation has sunk in in Europe that China has been a living falsification of the largely western belief in a path-dependency that leads from decades of growth, socio-economic progress and the development of a significant middle-class to inevitable democratisation and market liberalisation. Despite, or rather because of, stunningly rapid Chinese growth and development, the Communist Party of China (CPC) has stayed in power and solidified its control over the economy, polity, and society. China has not moved towards more market orientation, liberalism, and democracy, but has instead realised its very own model of political and economic governance. The Chinese model combines characteristics of a market-driven economy with substantial state intervention policies and centralised control and oversight. There are some market economy elements, driven by economic liberal supply and demand and price competition dynamics, mostly in the domestic market. However, especially when it comes to global trade, China remains a tightly centrally controlled economy. Through significant state intervention, tightly controlled resource allocation, and the dominance of state-owned enterprises (SOE), market distortion characterises the domestic market as well as much of China's international trade and investment and favours Chinese enterprises. Moreover, in addition to those operational disadvantages, there are also structural disadvantages European enterprises suffer from. While Chinese companies enjoy relatively unrestricted market access in the EU, this is not the case for European competitors in a highly protected Chinese investment environment. Many EU economies are increasingly frustrated that their businesses more often than not are excluded from realising or investing in infrastructure projects in China, while the domestic EU markets are open to PRC bidders in most public tenders. This applies to general market access as well as public tender contracts and FDI in specific sectors. According to the European Commission, financial services are a sector in which the lack of reciprocal market access is particularly severe. While Chinese fintech companies, banks and insurers are expanding their presence in the EU, their European counterparts are denied access to the Chinese market.

There is also a clear trend in China away from the private sector towards state control and management of the market. Lardy has for example pointed to a decline in private investment in favour of state investment, facilitated by easy access to credit and diversion of resources towards Chinese SOEs, and evidently away from the private sector.[4] In Europe, this has clear implications for economic security. A study by the German Bertelsmann Stiftung found that between 2014 and 2017, 64% of Chinese investments above a 10% stake in German companies were in sectors prioritised by the "Made in China 2025" campaign,[5] a central initiative to make China a leader of the fourth industrial revolution. Foreign acquisitions are an evident tool to acquire know-how and to realise "Made in China 2025". Simplified, China is buying up European, and global, companies to acquire the technology and know-how gained elsewhere to rapidly further its own development and leapfrog the rest of the world.

A systemic rival as a most favoured partner

In Davos recently, Xi Jinping had juxtaposed himself to US President Trump and declared his interest in free trade and stand against protectionism.[6] In practice, however, European leaders had to conclude that the Chinese President seems to define free trade and multilateralism differently from them. The EU Commission recently named the PRC a "systemic rival and competitor".[7] With this, China is not only a structurally difficult market itself, but also offers an alternative growth model to third parties, and thus, is in direct systemic competition with the European Union. Xi presents China increasingly as a global player, willing and able to shape the geopolitical and economic agenda. The Belt and Road Initiative makes China a most favoured partner in many countries around the world and maximises Beijing's global influence. Since its inception in 2013, the BRI has become a defining feature of the global economy and provided oftentimes much needed infrastructure investment not only for Asian countries, but also across the globe. BRI critics argue that it is a Chinese effort to take aim at the post-WWII international order conceived and enforced by the United States, and that the BRI attempts to trap countries in unsustainable debt, perpetuating unequal relationships. While this so-

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4 Lardy, N. (2017), "State Resurgence in China", in Adam/Jiming (eds.), *U.S.-China Cooperation in a Changing Global Economy*, PIIE Briefing, 17-1 June.

5 Jungbluth, C. (2018), "Kauft China systematisch Schlüsseltechnologien auf? Chinesische Firmenbeteiligungen", in Deutschland im Kontext von, "Made in China 2025", Bertelsmann Stiftung, Gütersloh, p. 22.

6 *Reuters*, "In Davos, Xi makes case for Chinese leadership role", 17 January 2017, https://www.reuters.com/article/us-davos-meeting-china/in-davos-xi-makes-case-for-chinese-leadership-role-idUSKBN15118V.

7 European Commission (2019), "Contribution to the European Council. EU-China – A strategic outlook", 12 March 2019.

called “debt-trap” argument is exaggerated, it is true that China increases its status and importance via specifically targeted FDI. New Chinese financing institutions, such as the Asian Infrastructure Investment Bank (AIIB), a Chinese development bank headquartered in Beijing and investing in infrastructure and other productive sectors in Asia, increasingly shape the international order and provide significant resources to developing countries. They are also a covert attempt by China to become a norm-entrepreneur itself, setting standards and practices according to its own preferences.

For the EU, this is both promising and worrying at the same time. While China’s interest in international trade and its increasing investment in often less developed countries are generally positive, Chinese-style institutions and trade regimes do not satisfy European standards and aspirations at all. Moreover, Beijing knows how to use its thus-increased leverage economically and politically. Especially, since it does not stop outside of Europe’s borders. Just like in Asia, in Europe, too, the enormous appeal of the Chinese market and Chinese investment monies has the potential to divide friends and partners and drive up competition. Other competitors have made advances towards individual European countries, exposing divisions among EU members; Russia for example. However, unlike with other competitors before, the EU can this time around not rely on its ace card of superior economic strength and investment power; China’s pockets are deep. So it happened that in 2012, the Chinese Ministry of Foreign Affairs inaugurated the Cooperation between China and Central and Eastern European Countries (16+1, soon to be named 17+1 with Greece having joined the grouping) initiative to promote investment relations between China and 17 countries of Central, Southern, and Eastern Europe, most of them EU members. 17+1 serves to further the Chinese Belt and Road Initiative beyond Asia and 14 EU members have signed bilateral agreements with China, officially becoming members of the BRI. While the EU is still a far cry away from having anything resembling a coherent policy on China, Beijing is carefully targeting “softer” countries in Europe, expanding its influence and its bargaining power.

This is far from only being an issue with smaller European economies though, as just before the cited Paris meeting, Xi had been to Italy, where the government of the fourth largest European economy dealt a further blow to European coherence on China. The government in Rome had just signed up to the BRI, leaving those European leaders and officials scratching their heads, wary of this increasing Chinese influence in the EU. At a time when Europe was just about to get its act together on China (see below), the Italian newspaper *La Stampa* reported that Xi received the most lavish of receptions in Rome and was courted with all state honours.[8] Italy's Premier, Giuseppe Conte, then became the first and only G-7 leader to officially sign up to the BRI. Previously, Athens had ceded a 51% controlling stake in its key port of Piraeus to China's SOE COSCO, which also controls container ports in Spain. And many European economies from Germany to Portugal are in some way connected to the BRI. Even the cited Paris meeting was somewhat ambivalent and Macron's strong words and gestures would have been that much more credible had Paris not used the opportunity of Xi's visit to sign business and investment deals for French companies with China totalling EUR40bn.

This is significant, since Rome and other governments lend ever more credence to the BRI project itself and implicitly legitimise the Chinese macro-economic vision that underpins the controversial Belt and Road Initiative. Something that has not gone unnoticed in the White House, where the National Security Council reacted with concern and warned Rome not to give this "legitimacy to China's infrastructure vanity project".[9] At the same time, there is a risk of a future over-dependency on Chinese capital and the Chinese market. The ASEAN lesson should be valuable to Europe. Chinese investment is transforming smaller Southeast Asian countries significantly both in economic and social terms. Countries such as Cambodia and Laos are dependent on China to an extent that has them being accused of becoming Chinese proxies within ASEAN, where member states decide on the basis of unanimity and a veto by one country can hold up moving forward on issues, such as a coherent China approach. Of course, most ASEAN countries are significantly smaller and less diversified economies, hard to compare to the likes of Italy, or even to some the poorer of EU countries. Nonetheless, the ASEAN example should be studied more seriously in Europe.

Europe's getting tough(er)

The risk of increasing over-dependence on Chinese capital and market is exacerbated by the unclear future of trade ties with the traditional ally, the USA. Standing up to China may well please Washington – in fact, this is something Washington demands. However, the Europeans cannot do so assured that the Americans will have their back in terms of trade. On the contrary, Germany especially is worried

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8 *La Stampa*, "Italy endorses China's Belt and Road plan under wary gaze of Western allies", 23 March 2019, https://www.lastampa.it/2019/03/23/esteri/italy-endorses-chinas-belt-and-road-plan-under-wary-gaze-of-western-allies-BTzx2SyRBAntxrzKZFNAGN/pagina.html.

9 *Reuters*, "China's Xi looks to strengthen Italian ties, evokes ancient trade routes", 22 March 2019, https://www.reuters.com/article/us-italy-china-president/china-italy-looking-to-strengthen-trade-infrastructure-ties-xi-idUSKCN1R318U.

about the spectre of a looming trade war with the US, or at least a skirmish, once US President Trump gets serious on tariffs on European key exports such as automobiles – this scenario is only one nightly tweet away.

For this reason and the fact that the EU usually struggles to produce coherent strong policy communiqués, not to mention strategy papers – often due to dissents among its ranks – it is somewhat surprisingly unusual that the EU presented the above-mentioned strategy paper on China, just weeks before Xi's visit to Europe. This time, the EU could agree on a new China strategy paper, calling the strategic partner a de facto competitor and systemic rival.[10] This is a radical change in rhetoric and strong language from Brussels. Brussels makes it abundantly clear that it no longer regards China as a developing country, but as a key technological power and competitor instead. The EU agrees to unite behind demands for clear policies and action from Beijing to ensure equal market access and fair regulations, transparency, and greater Chinese responsibility for upholding the rules-based international order. In sum, the Commission demands a more responsible China and an interaction based on reciprocity.

The EU strategy paper was a solid first step to kick-start a process of reversing the unequal access of Chinese companies in the European market, while China is failing to reciprocate. But the litmus test is if Brussels bureaucrats and EU leaders manage to translate "talk into walk", tougher rhetoric into more concrete, biting policies based on that reciprocity they demand. For this to happen and to have any effect, member states need to be behind this; Europe needs an effective common response, which begins with a diplomatic show of force. The unusual format in Paris was, therefore, a further laudable step. Hidden in diplomatic niceties was an obvious attempt by major EU leaders to get two European messages across: The European market is not a free for all and we will stand united if we must. Or as Macron bluntly put it later in Brussels after a joint meeting of European leaders: "The time of European naiveté ended. […] For many years we had an uncoordinated approach and China took advantage of our divisions."[11] Macron, Merkel and Juncker have diagnosed that the unfair advantage rests with Asia and the Europeans are more determined than ever to level the playing field.

In concrete terms, this means that the European Commission, together with the External Action Service, the EU's diplomatic service, aim to tighten the rules for Chinese FDI in Europe, especially mergers and acquisitions in sensitive and security-relevant areas. Earlier in the year, the EU member states had passed new

[10] EU Commission (2019), cited above.

[11] *FT Weekend,* "Naivety on China is over, says Macron", p. 2, 23/24 March, 2019.

EU regulation to screen foreign takeovers in strategic sectors in response to concerns that foreign firms – many of them Chinese – were buying up key technologies. German Chancellor Angela Merkel said that Europeans had to make sure that there is no unilateral protectionism, but reciprocity instead in world trade. "Germany is a country that is in favour of open trade, but we also want to guard our interests. That is why, together with France, we will put forward ever more proposals to that effect."[12]

European Union leaders and China then met on 9 April 2019 in Brussels for their annual EU-China Summit, usually an outcome-deprived affair, and achieved a further milestone on the reciprocity journey. Although not quite the "breakthrough" European Council President Donald Tusk called it,[13] the summit produced a joint statement. In fact, the Europeans put on a show of unity and strength, even threatening to leave the summit without any communiqué at all. The tough approach worked, with China making last-minute concessions to secure a meaningful declaration.[14] Leaders agreed to include a commitment "to build their economic relationship on openness, non-discrimination, and fair competition, ensuring a level playing field and transparency". The two sides also committed "to achieve in the course of 2019 the decisive progress required, notably with regard to the liberalisation commitments" as well as "broader and non-discriminatory market access". Chinese negotiators reaffirmed support for the rules-based trading system and included a reference to "forced transfers of technology", a staggeringly unique implicit acknowledgement by China of this transfer even being an issue.

Such Chinese pledges are no major change in Beijing's economic policy. During the press conference following the summit, Premier Li Keqiang reiterated the standard Chinese position that its opening is an ongoing process.[15] And yet, even minor results are significant, for they demonstrate how the EU can successfully pressure China, negotiate on eye level, and achieve results, if its leaders act in unison and refrain from the aggressive and destructive attitude displayed by the

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12 Angela Merkel, "Regierungserklärung der Kanzlerin zum Europäischen Rat", https://www.bundeskanzlerin.de/bkin-de/mediathek/videos/regierungserklaerung-zum-europaeischen-rat-1592474!mediathek?query=.

13 *Deutsche Welle*, "EU announces 'breakthrough' on trade with China", https://www.dw.com/en/eu-announces-breakthrough-on-trade-with-china/a-48269078.

14 Delegation of the EU to China, "Joint statement of the 21st EU-China summit", https://eeas.europa.eu/delegations/china_en/60836/Joint%20statement%20of%20the%2021st%20EU-China%20summit.

15 *South China Morning Post*, "As China-EU summit ends, Premier Li Keqiang vows reforms: 'When we say it, we have got to do it'", 10 April 2019, https://www.scmp.com/news/china/article/3005462/china-eu-summit-ends-premier-li-keqiang-vows-reforms-when-we-say-it-we.

Trump administration. With this communiqué, Europe begins to walk the talk of its earlier strategy paper and begins to implement the much-needed shift in the EU's approach towards China. The summit can – at least to some extent – be interpreted as a small victory for the EU, as China implicitly agreed to open up its economy, allow foreign investors and limit state subsidies for industries. It was certainly a further logical step in the right direction, building upon the strategy paper and efforts to present the EU as a coherent actor.

CONCLUSION AND RECOMMENDATIONS

Without a doubt, the EU and China, two of the largest markets in the world, need each other and trade between them is desirable. All of the above is not at all to discourage trade with China and there is nothing wrong with having good trading relationships with China per se, nor with signing up to the BRI. Increased trade volume and mutual FDI, even in critical infrastructure, is something to work towards and can be beneficial to both sides. However, this must be done according to WTO-agreed rules or possible future free trade agreements (FTAs), and must be completely transparent and reciprocal. If the major European trading nations and the EU as a whole want to have some credibility, they must stand up to Beijing's disregard of established trade practices and Europeans must address some of the major issues that still undermine a sound relationship. In particular, Europeans take issue with what they see as unfair trade practices on China's part, making this relationship essentially unequal. The EU's budget commissioner, Günther Oettinger, made a valuable proposal: Oettinger argued that the EU should have the right to deny Chinese-funded infrastructure deals in any EU member state if they do not serve the common EU interest. An EU Commission veto on Chinese infrastructure projects, in other words. Adding to this, companies from countries that do not allow for full EU bidding, first and foremost China, should reciprocally be banned from EU's own public tenders. This reciprocity must also apply to protectionist regulations on mergers and acquisitions with locals in such countries.

The EU should also work towards its key industries becoming more competitive. To this end, the EU needs a long-term strategy on how to maintain a leading position in technological R&D, and sustainable hard infrastructure and digital infrastructure development. Second, the EU needs competitive firms. Internal European mergers should be seen in this light first and foremost, not from a domestic cartel perspective only. The external environment, i.e., competition with mega conglomerates from China and the US, should be regarded as equally important to domestic market implications when weighing up intra-European mergers. Regretfully, EU anti-trust regulators recently rejected a rail industry merger deal between Alstom and Siemens' rail unit, on the basis of concerns over a lack of competition, leading to higher prices for consumers. However, the building of European champions, better equipped to compete globally, should be particularly encouraged. More than 15 years beyond China's accession into the WTO, it has become clear that China's SOEs are not going to disappear anytime soon and if Europeans want to compete, they must cooperate internally and draw on the full strength of its combined market.

Lastly, a competitive Europe, on par with China, needs European unity. Countries signing up to the BRI pose extraordinary frustrations and challenges to those Europeans who seek to sustain an open and equal trade and investment environment. But the fault also lies with the major European economies as well as with the United States. Instead of threatening and being frustrated with countries like Italy, Brussels (and Washington) should respect different positions across European capitals and discuss non-BRI alternatives in a constructive manner. Instead of prioritising national preferences, especially vis-à-vis China, the European common market should take priority and bilateral relations should be embedded in the European context. Macron's Paris meeting was laudable in this regard – despite the bilateral deals with China. Germany has also a lot to do in this regard, facing pressure from its domestic industry to cosy up to China. As critical of the EU as some in Europe may be, especially when it comes to trade and market regulations, the EU must hang together. What has happened in some ASEAN countries are warning signals, and even if these countries are not easily comparable to most EU economies, the case of smaller ASEAN countries should be studied well in Brussels and warnings should be communicated to EU capitals. If individual EU countries undermine a common EU approach in order to reap some benefits, they may soon find themselves overly dependent on China. It was a rare show of unity and resolve on the EU side, buoyed by the recent legislation on foreign investment and public procurement, that allowed the EU-China Summit to produce something it usually does not: deliverables in European priority areas. This resolve and a coherent China strategy in times of geopolitical and economic uncertainty, within Europe and vis-à-vis the USA and China, must become the norm guiding the EU's trade policy towards China.

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Countering Global Protectionism: The CPTPP and Mega-FTAs

Kazushi Shimizu

1. INTRODUCTION

Protectionism and trade friction are expanding throughout the world. Mr. Donald Trump was inaugurated as United States (US) president in January 2017, and the United States withdrew from the Trans-Pacific Partnership (TPP) soon after. The US has increased the trade friction with China and other countries, and protectionism is rapidly increasing in the world. The spread of protectionism and trade friction has a major negative impact on the world economy. The evolving East Asian economy will be hit hard.

In view of the expansion of protectionism, Japan proposed the 11-nation Trans-Pacific Partnership free trade agreement (TPP11) in May 2017. The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) was agreed on at the Ministerial Meeting in November 2017, signed by 11 countries on 8 March 2018, and finally entered into force on 30 December 2018. Also, the Japan-EU Economic Partnership Agreement (EPA) came into force on 1 February 2019. The East Asia Regional Comprehensive Economic Partnership (RCEP), which is a mega-free trade agreement (Mega-FTA) in East Asia, is aiming to conclude negotiations in the fall of 2019.

With the current rise of protectionism and trade friction in the world economy, the development of the CPTPP is important. The original TPP promoted ASEAN and East Asian economic integration. Similarly, the CPTPP will promote ASEAN and East Asian economic integration. In addition, three Mega-FTAs: the CPTPP, the Japan-EU EPA and the RCEP will have the potential to gradually reverse the current trend of increasing protectionism and trade friction practices.

The Association of Southeast Asian Nations (ASEAN) was founded in 1967 and East Asian economic integration began some time after. I have analysed ASEAN and East Asian economic integration within the structural changes of the world economy, on a specific and long-term basis. This paper will consider the significance of CTPPP and Mega-FTAs against the trend of protectionism, including looking back on the original TPP's impact on East Asian economic integration.

2. EAST ASIAN ECONOMIC INTEGRATION AND THE TPP'S IMPACT

In view of the structural changes since the global financial crisis starting from 2008, the TPP has accelerated East Asian economic integration. Furthermore, this economic integration has progressed through interaction. The TPP and East Asian economic integration were a great impetus to promote a freer trade system in the world economy. This section will review this process.[1]

In East Asia, ASEAN has led economic integration. ASEAN was established in 1967, and has promoted regional economic integration since 1976, aiming to realise the ASEAN Free Trade Area (AFTA) from 1992, and aiming to realise the ASEAN Economic Community (AEC) from 2003. At the end of December 2015, ASEAN finally established the AEC, and ASEAN has set its sights on a new AEC goal ("AEC 2025"). Also, in East Asia, multi-layered cooperation has been developed, centring on ASEAN. Regional economic cooperation initiatives such as ASEAN+3 and ASEAN+6 have been developed in response to the 1997 Asian economic crisis. In addition, five ASEAN+1 FTAs have been established around ASEAN.

The structural changes after the world financial crisis forced East Asia to make a major transformation. Given the structural changes in the world economy, the US joined the TPP with the aim of expanding its exports to East Asia, the world's growth centre. The TPP was originally P4, comprising Brunei, Chile, New Zealand and Singapore, coming into effect in 2006. But the United States, Australia, Peru, and Vietnam joined the grouping and the TPP became very significant in the world economy. The TPP negotiations began in eight countries in March 2010, and Malaysia also joined in October.

While the TPP was establishing itself, Japan and China made a joint proposal in August 2011, and agreed to advance an FTA for the entire East Asian region, which had not progressed much until then. Under these circumstances, ASEAN proposed, in November 2011, the RCEP, an FTA for East Asia as a whole, because ASEAN wanted to maintain its centrality in East Asian regional cooperation.

1 Refer to Shimizu (2016a, 2016b).

The first RCEP negotiation meeting took place in May 2013. Japan officially participated in the TPP negotiations in July 2013. The TPP was agreed upon in October 2015 and signed in February 2016.

The TPP supported negotiations on the Japan-China-Korea FTA and the Japan-EU EPA. Furthermore, the progress of the RCEP negotiations also boosted the TPP and other FTA negotiations.

3. PRESIDENT TRUMP'S INAUGURATION AND PROTECTIONISM

3.1. President Trump's Inauguration and the US Withdrawal from the TPP

Mr. Trump was elected in the US presidential election on 8 November 2016, and took office as President of the United States on 20 January 2017. He has changed the trading landscape significantly. On 23 January 2017, President Trump signed an executive order withdrawing the US from the TPP. President Trump has also reversed the US trade policy that has driven the world's free trade system, aiming to renegotiate the North American Free Trade Agreement (NAFTA) and the United States-Korea Free Trade Agreement (US-ROK FTA) and to negotiate bilateral FTAs instead of multilateral FTAs.

The US withdrawal from the TPP also greatly affected the economic integration of ASEAN and East Asia. It became almost impossible for the TPP to accelerate economic integration in East Asia.[2]

3.2. The Trade Friction between the US and China

The US's actions on protectionism and trade friction have further damaged the world economy. Along with the US's withdraw from the TPP, President Trump renegotiated the NAFTA and the US-ROK FTA and caused trade friction by imposing high tariffs on imports from countries around the world.

In particular, trade friction with China from 2018 onwards has had a major negative impact on the world economy. On 23 March 2018, the US imposed additional tariffs of 25% and 10% on steel and aluminum, respectively, based on Section 232 of the Trade Expansion Act of 1962. In opposition to this measure, China imposed additional tariffs on fruits and pork from the US on 2 April.[3]

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[2] Refer to Shimizu (2017).

[3] Refer to Maie (2018) about trade friction between the US and China.

Furthermore, as measures against China were implemented, the US imposed an additional 25% tariffs on imports of US$34 billion from China on 6 July, under Article 301 of the Trade Act of 1974. On the other hand, China imposed 25% tariffs on imports of $34 billion from the US as a retaliatory measure. Next, the second round: on 23 August 2018, the US put additional 25% tariffs on imports of $16 billion from China. In response to this measure, China imposed an additional 25% tariffs on imports of $16 billion from the US. In the third round, on 24 September 2018, the US put an additional 10% tariffs on imports of $200 billion from China. On the other hand, China imposed an additional 5-10% tariffs on $60 billion of imports from the United States. As a result of these measures, the United States is applying high tariffs to about 50% of the imports from China while China is applying high tariffs to about 70% of the imports from the US.

The expansion of protectionism and US-China trade friction are having a major negative impact on the world economy. It will not only hurt the economies of the US and China, but also the countries and companies providing parts and intermediate goods to the United States and China. East Asia, especially, is experiencing a great negative impact, because in East Asia parts and intermediate goods are mutually traded in a huge production network and East Asia is developing rapidly through this production network.

Furthermore, the slowing growth of the US and China economies, the world's two largest economies, will have a major negative impact on the world economy. And the slowing of world economic growth will have a major negative impact on the world economy as a whole.

The increased protectionism and the US-China trade conflict have also affected the Asia-Pacific Economic Cooperation (APEC) and G20 forums. For example, at the APEC Summit in November 2018, it was not possible to adopt the Summit Declaration for the first time since the start of the Summit in 1993 due to the conflict over trade policy between the US and China.

4. THE CPTPP IN GLOBAL PROTECTIONISM: FROM THE TPP TO THE CPTPP

4.1. Japan's Proposal and the Entry into Force of the CPTPP

The withdrawal of the US from the TPP and the expansion of protectionism led Japan to propose the TPP11. The TPP11 negotiations were launched in May 2017, and the CPTPP was agreed on at the Ministerial Meeting in November 2017. The CPTPP was signed by 11 countries on 8 March. Some of the tough conditions each country had contracted with the US in the TPP were suspended. Six countries completed their domestic procedures in November and the CPTPP finally entered into force on 30 December.[4]

The CPTPP comprises 11 countries: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam. The CPTPP will be a Mega-FTA with a population of 500 million people, about 13% of world GDP, and 15% of total trade.

4.2. The Contents of the CPTPP: Inheritance of the Original TPP

The CPTPP inherits the contents of the original TPP. The original TPP was characterised as having a high level of trade liberalisation and included new rules in services trade, investment, e-commerce, government procurement, state-owned enterprises, intellectual property, labour and environment.[5] In the CPTPP, market access such as tariff elimination and services trade liberalisation remain as in the original TPP, and most of the original TPP's rules remain except for 22 suspended items.

The CPTPP consists of the following seven articles: "Preamble," "Article 1: Incorporation of the Trans-Pacific Partnership Agreement," "Article 2: Suspension of the Application of Certain Provisions," "Article 3: Entry into Force," "Article 4: Withdrawal," "Article 5: Accession," "Article 6: Review of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership," and "Article 7: Authentic Texts," followed by "Annex."[6]

The CPTPP itself is a short agreement consisting of seven articles, but "Article 1" incorporates the original TPP agreement with 30 chapters. Although "Article 2" provides for the suspension of the application of specific provisions, the suspended provisions finally account to 22 in total. Half of them are related to intellectual property, and there are two items for government procurement and two items for state-owned enterprises.

The requirement for entry into force of the CPTPP became easier than the original TPP. "Article 3: Entry into Force," prescribes: "this agreement shall enter

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4 Refer to Shimizu (2016a), Umada, Urata and Kimura (2016) and some papers in "East Asian Economic Integration" (Introduction: Shimizu, K., Papers: Hirawaka, H., Ishikawa, K., Yukawa, K. and Oba, M.) in *Asian Studies*, Vol. 64 No. 4, December 2018.

5 "Text of Trans-Pacific Partnership," http://www.tpp.mfat.govt.nz/text.

6 "Comprehensive and Progressive Agreement for Trans-Pacific Partnership," https://www.mfat.govt.nz/assets/CPTPP/CPTPP-Text-English.pdf.

into force 60 days after the date on which at least six or at least 50 per cent of the number of signatories to this agreement, whichever is smaller, have notified the depositary in writing of the completion of their applicable legal procedures.”[7]

4.3. The Effects of the CPTPP

The impact of the entry into force of the CPTPP is significant, although CPTPP became smaller compared to the original TPP. The CPTPP will promote trade liberalisation and rule-making in the Asia-Pacific region. And it will be a template for future Mega-FTAs. Finally, the CPTPP will boost AEC deepening and RCEP negotiations. The original TPP strongly promoted AEC, the RCEP and the Japan-EU EPA. The CPTPP will boost them again.

With the entry into force of the CPTPP, new members will be welcomed. The expansion of the CPTPP with new members will further increase its impact. Currently, Thailand, Indonesia, the Philippines, Korea, Taiwan, Colombia, the United Kingdom, etc. have announced their participation and interest in it. In January 2019, the first Commission meeting of the CPTPP was held in Japan, and the procedures of “accession” were discussed.

The entry into force of the CPTPP within 2018, earlier than the initial forecast of 2019, will enhance the impact of the CPTPP, due to the acceleration of trade liberalisation. In the CPTPP, tariff reductions began on 30 December 2018, the day the agreement entered into force. On 1 January 2019, only 2 days later, the second year’s tariff reductions were implemented.

5. THREE MEGA-FTAS COUNTERING GLOBAL PROTECTIONISM: THE CPTPP, THE JAPAN-EU EPA AND THE RCEP

Through the boost the CPTPP provided, the Japan-EU EPA came into force on 1 February 2019. The RCEP, which is a Mega-FTA in East Asia, is aiming to conclude negotiations in the fall of 2019. These three Mega-FTAs: the CPTPP, the Japan-EU EPA and the RCEP, will have the potential to gradually reverse the current trend of increasing protectionism and trade frictions.

The Japan-EU EPA entered into force on 1 February 2019, promoted by the CPTPP negotiations. In addition to the CPTPP, which is a Mega-FTA across the Asia-Pacific, a Mega-FTA across Japan and Europe has also taken effect. The CPTPP and the Japan-EU EPA will have a positive effect on each other.

[7] Ibid.

The Japan-EU EPA will be a Mega-FTA with a population of 640 million, about 28% of world GDP and 37% of world trade. The Japan-EU EPA has a high trade liberalisation level and a high level of rules by developed countries, under the 23 chapters of the agreement. It will be a comprehensive Mega-FTA, including trade in goods, trade in services, investment liberalisation, e-commerce, capital movement, government procurement, state-owned enterprises and intellectual property.[8]

Despite the expansion of protectionism, the RCEP negotiations have also been advanced. The RCEP is a Mega-FTA in East Asia, which is the world growth centre, and aims to conclude negotiations this fall. The RCEP will have a significant positive impact on East Asia and the world economy.[9]

The RCEP comprises 16 countries: the 10 ASEAN countries and Australia, China, India, Japan, Korea and New Zealand. The RCEP will be a Mega-FTA with a population of 3.4 billion, which is about half of the world's population, about 32% of world GDP and about 29% of world trade. The RCEP has three pillars, "market access", "rules" and "cooperation", and the negotiation field covers 18 broad areas, including trade in goods, trade in services, investment, intellectual property, e-commerce, government procurement.[10]

Although the RCEP negotiations aimed to arrive at a substantial agreement by 2018, it could not be concluded as planned. This was due to the gaps between some countries about trade liberalisation and various rules. It was also due to an Indian factor. India had great concerns about further trade liberalisation before the general election in spring 2019, because India had a trade deficit with China.

The RCEP aims to completely conclude negotiations this fall after the election in India. The "Joint Leaders' Statement on the RCEP Negotiations" stated: "We have advanced to the final stage of negotiations. We are determined to conclude a modern, comprehensive, high quality, and mutually beneficial RCEP in 2019."[11]

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8 "Agreement between the European Union and Japan for an Economic Partnership," https://www.mofa.go.jp/files/000382106.pdf.

9 Refer to Shimizu (2018a, 2018b) about the RCEP.

10 "Joint Leaders' Statement on the Negotiations for the Regional Comprehensive Economic Partnership (RCEP) (as at November 2017)," https://www.mofa.go.jp/mofaj/files/000307671.pdf.

11 "Joint Leaders' Statement on the Regional Comprehensive Economic Partnership (RCEP) Negotiations (as at November 2018)," https://www.mofa.go.jp/mofaj/files/000419160.pdf.

6. CONCLUSION: THREE MEGA-FTAS COUNTERING GLOBAL PROTECTIONISM AND JAPAN'S ROLE

Despite the expansion of protectionism, the CPTPP finally entered into force. Also, the Japan-EU EPA came into force. The RCEP is aiming to conclude negotiations in the fall of 2019. The original TPP promoted AEC, the RCEP and the Japan-EU EPA. The CPTPP will again boost them. Furthermore, these three Mega-FTAs will interact and have a synergistic effect.

In addition, the increase in the number of member countries, for example, in the CPTPP, will have further synergetic effects. Although the current world economy is in a very difficult situation, the three Mega-FTAs will gradually reverse the current trend of increasing protectionism and trade frictions.

Japan, the world's third largest economy, plays a large role in countering global protectionism in the current tough conditions of the world economy. Japan is promoting three Mega-FTAs and countering global protectionism. Japan must go ahead with these three Mega-FTAs. Japan must cooperate with ASEAN so as to work towards the successful conclusion of the RCEP negotiations.

Next, Japan must continue to persuade the US to return to the TPP, explaining the benefits of the TPP and Mega-FTAs. The CPTPP has a good mechanism to release the 22 suspended items when the United States returns.

Finally, Japan must manage the G20 to counter global protectionism. Japan is the chair of G20 in 2019 and will hold the G20 Summit in Osaka in June. Japan must play a major role in countering global protectionism.

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RCEP Negotiations for the Reshaping of the Liberal Economic Order

Mie Oba

Over 18 chapters, the Regional Comprehensive Economic Partnership (RCEP) focuses on setting rules to foster further economic liberalisation among the Association of Southeast Asian Nations (ASEAN) member countries and six other countries, namely, China, the Republic of Korea (ROK), Japan, Australia, New Zealand, and India. If the RCEP is concluded, a US$25.4-trillion market will emerge. The total population of the RCEP member countries is 3,552 million, which is about half of the total population of the world.[1]

Although the expected potential of the RCEP has been discussed, the negotiation has taken a great deal of time. The sixteen countries involved formally announced in November 2012 that they had decided to start the negotiation, and held the first official round in May 2013. Since then, six years have passed and the member countries have still not reached an agreement. Last year, they said that they would conclude the negotiation in 2018; however, they had to give up on this deadline, and instead, they have now announced that they will do it in 2019.

This chapter will outline the characteristics, potential, problems, and prospects of the RCEP. First, it will identify the specific characteristics of the RCEP, while showing that the RCEP is more than just a trade deal and, rather, holds significant importance in the context of the changing regional and global order in this current uncertain era. Second, it will provide an overview of the current status of the RCEP negotiation. In spite of the rising expectations for the RCEP after the United States (US) withdrawal from the Trans-Pacific Partnership (TPP), the RCEP negotiation has been advancing extremely slowly because of numerous conflicts of interest among the member countries. Finally, it will describe the potential and problems of the RCEP. Specifically, it will highlight how the RCEP negotiation will affect the region,

[1] The values of the total GDP and population are obtained from the Data Bank of the World Bank, https://databank.worldbank.org/data/home.aspx.

especially considering the current uncertain situation of the liberal economic order. In addition, the chapter will try to outline the tentative prospects of the RCEP. As mentioned later in this chapter, we must consider how the escalation of the Sino-American confrontation as well as domestic politics in key countries like India and Thailand will impact the RCEP negotiation.

1. THE IMPORTANT CHARACTERISTICS OF THE RCEP

As mentioned above, the size of the total GDP and population of the RCEP member countries is extremely large. Therefore, the RCEP market has a lot of potential for providing opportunities for further development of the private sectors of member countries. Size, however, is not the only reason for the immense potential of the RCEP negotiation.

First, the RCEP involves both China and India, which are leading players among the emerging global powers. China's economic development has slowed down, as the GDP growth rate reached 6.6% in 2018, down by 0.2% as compared to the previous year.[2] However, the size and potential of the Chinese economy is still significant, and its power is partially converted into political leverage, especially in neighbouring areas. According to the Global Economic Prospects (GEP) report released in early 2019, India is also expected to develop its economy, even though it experienced the slowest GDP growth rate among the previous five quarters in the third quarter of 2018.[3] The inclusion of these top-two emerging powers is an important advantage for the RCEP as a trade deal.

Second, the RCEP is a trial to attempt region-wide economic integration, as opposed to the bundle of bilateral economic ties between ASEAN and the six countries, each of which already has either a bilateral free trade agreement (FTA) or an economic partnership agreement (EPA) with ASEAN. In other words, the RCEP negotiation is focusing on setting common rules on economic activities based on the existing six FTAs/EPAs. To converge diverse FTAs/EPAs into one economic agreement, however, is extremely challenging.

Third, the RCEP is an opportunity to try an ASEAN-centred economic integration scheme. From ASEAN's point of view, the RCEP is an important step to maintaining ASEAN centrality amidst the changing regional circumstances in East Asia.

[2] "China's GDP growth slows to 28-year low in 2018", *Nikkei Asian Review*, 21 January 2019, https://asia.nikkei.com/Economy/China-s-GDP-growth-slows-to-28-year-low-in-2018, accessed 1 February 2019.

[3] The World Bank, "Global Economic Prospects: Darkening Skies", January 2019.

However, the negotiation process has been significantly complicated by various claims from the six external countries. Japan, one of the external powers relative to ASEAN, demonstrated its ability to assume a leading role in promoting the RCEP negotiation, especially after the US withdrawal from the TPP. However, the ASEAN countries' initiative will determine the trajectory of the negotiation process, while the other countries respect the leading role of ASEAN.

Finally, the RCEP is increasing its importance as a scheme to retain and foster the liberal economic order in Asia and the rest of the world. The international liberal order, based on the belief that a free and open economy is ideal for economic development, has determined the basic mindset of political elites in East Asia and the Asia-Pacific after the end of the Cold War, which revealed the prominence of the capitalist market economy model and the defeat of the socialist model for economic development. During the post-Cold War period, the political elites of the Western powers, especially the United States, intentionally established the capitalist market economy model as a global standard, thus leading the political elites of East Asia and the Asia-Pacific to base their behaviours and mindsets on the liberal economic order.

Now, the liberal economic order is facing many serious challenges, such as the growing protectionism of the United States under the Trump administration, the expanding influence of the state capitalism model due to the economic success of China, and the escalation of the Sino-American economic war. The US withdrawal from the TPP in January 2017 greatly impacted the political elites in East Asia and the Asia-Pacific. Subsequently, the Comprehensive and Progressive TPP agreement (CPTPP) was signed and came into effect in 2018. However, many people are still worried about how effective the TPP will be without the huge US market. Due to these factors, the importance of the RCEP as a way to foster the liberal economic order has, ironically, been further taken notice of.

2. THE DIFFICULTIES OF FINALISING THE RCEP NEGOTIATION

The RCEP negotiation is not finalised yet, even though the member countries have announced their desire to do so several times in the past. Especially in 2018, after the US withdrawal from the TPP, expectation for the completion of the RCEP negotiation had grown, and member countries announced that it would be done within the year. Singapore, the chair country of ASEAN in 2018, had significant interest in fostering economic liberalisation among ASEAN countries, and eagerly pushed the negotiation. The priorities of the chair country generally determines the activities of ASEAN in that year; therefore, Singapore's determination to finalise the negotiation increased the confidence that it would be completed by the date that they announced.

Japan also demonstrated its eagerness to finalise the RCEP negotiation. Japan used to prioritise the TPP over the RCEP negotiation because the former was a more challenging scheme for economic liberalisation and had strong political implications for US-Japan collaboration to dilute China's leverage in East Asia and the Asia-Pacific. After the US withdrawal from the TPP, the prospect of countering China decreased significantly, and, as a result, the political elites of Japan became seriously concerned about the demise of the liberal economic order because of the rise of protectionism, as symbolised in Trump's trade and economic policies. From Japan's perspective, the RCEP is an important tool in stopping the trend of strengthening protectionism and sustaining the free and open economy, as well as in pressuring the United States to come back to its "normal track" as a promoter and patron of the liberal economic order. In early July 2018, Prime Minister Shinzo Abe emphasised in his speech at the 5th RCEP Intersessional Ministerial Meeting that free trade was the key to economic development of the RCEP regions, and insisted: "The question is whether we, the Asian region, can unite as one and keep on raising the flag of free trade while concern on protectionism has been increasing worldwide. The RCEP negotiations are drawing attention from the rest of the world more than before. Let us act in solidarity to create a free, fair and rule-based market in this region."[4]

Japan and Singapore held this intersessional ministerial meeting as co-chairs and succeeded in accentuating the common goal of the member countries to "work together and see through the RCEP negotiations toward conclusion."[5] After this meeting, RCEP member countries concluded two additional chapters at the 23rd round of the negotiation: "Customs Procedures and Trade Facilitation" and "Government Procurement".[6] The pairing of two additional chapters with the existing two that had been already finalised ("Economic and Technical Cooperation" and

[4] Speech by Prime Minister Shinzo Abe at the Fifth Regional Comprehensive Economic Partnership Intersessional Ministerial Meeting in Tokyo, Japan, 1 July 2018.

[5] The Fifth Regional Comprehensive Economic Partnership Intersessional Ministerial Meetings, Tokyo, Japan, 1 July 2018, paragraph 2, http://asean.org/storage/2018/07/5ISSL-MM-Joint-Media-Statement-FINAL-1July2018.pdf, accessed 3 July 2018.

[6] The sixth RCEP Ministerial Meeting, Joint Media Statement, Singapore, 30-31 August 2018, https://asean.org/wp-content/uploads/2018/08/RCEP-MM-6-JMS_FINAL.pdf, accessed 3 September 2018.

"Small and Medium Enterprises") resulted in the finalisation of four chapters, which in turn accelerated the RCEP negotiation.

However, the RCEP negotiation was not completed in 2018 and was postponed to the following year. The RCEP leaders said in a joint statement after the RCEP leaders' meeting in November 2018: "[We] are determined to conclude a modern, comprehensive, high quality and mutually beneficial RCEP in 2019."[7] In addition to the four completed chapters, three chapters were finalised during the leaders' meeting. However, member countries could not agree on the rest of the ten chapters. Instead, the leaders stated that they would conclude "a modern, comprehensive, high quality, and mutually beneficial RCEP" in 2019.[8]

Entering 2019, the negotiation is continuing. The 25th round was held in Bali in February 2019. According to a report, the member countries progressed the negotiation on market access and text-based negotiation, and agreed on a working plan to help guide the negotiation to be completely finalised in 2019.[9] This "progress" was emphasised in the Joint Media Statement in the 7th Intersessional Ministerial Meeting of the RCEP, which was held in Siem Reap in March 2019.[10] This statement also provided assurance that the member countries wished to conclude the RCEP within the year.[11]

The negotiation of the RCEP, despite the rising expectations that it has provoked, will not be easy to complete; the interests of the member countries remain at odds. The chapter about market access is the most difficult area to conclude because the interests of member countries clash – especially regarding India's reluctant attitude about the liberalisation of trade of goods, specifically tariffs reduction. India's industrial policy prioritises the protection of its own manufacturing industry from imports by using tariffs barriers. For example, the liberalisation rate of goods of trade set by the ASEAN-India FTA (AIFTA) is the lowest at 76.5%,

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[7] The RCEP negotiations, Joint Leaders' Statement, 14 November 2018, paragraph 5.

[8] Ibid.

[9] Department of Foreign Affairs and Trade, RCEP negotiation, Twenty-fifth round of negotiation, https://dfat.gov.au/trade/agreements/negotiations/rcep/news/Pages/twenty-fifth-round-of-negotiations-19-28-february-2019-bali-indonesia.aspx.

[10] The 7th RCEP Intersessional Ministerial Meeting, Joint Media Statement, Siem Reap, Cambodia, 2 March 2019, paragraph 2, https://dfat.gov.au/trade/agreements/negotiations/rcep/news/Documents/joint-media-statement-seventh-rcep-intersessional-ministerial-meeting.pdf, accessed 9 March 2019.

[11] Ibid., paragraph 3.

while those of the other ASEAN+1 FTAs are above 90%.[12] In addition, the people in India's industrial sector are seriously concerned about the huge flooding of China's cheaper manufacturing goods into the Indian market, concerns which the Indian government should address.[13]

India also has a strong role in the negotiation on intellectual property rights. For example, Japan and South Korea proposed that RCEP members should take on obligations that go beyond the World Trade Organisation's (WTO's) agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), especially in terms of the rules on patents, including the extension of the duration of the patent term by as much as 20 years. This rule is affecting India's competence in the generic medicines market. Furthermore, the acceptance of such an extension of the patent conflicts with India's opposition to TRIPS-Plus proposals.[14]

What to prioritise among the rapid conclusion of negotiation regarding the level of liberalisation and the quality of the finalised RCEP is also a critical issue. The ASEAN countries tend to rush into conclusions, accepting some extent of compromise regarding the level of liberalisation and the quality. One of the important political implications contained in the RCEP is its characteristic as an ASEAN-centred scheme, so the conclusion of the RCEP, from the viewpoint of the ASEAN countries, is evidence of ASEAN centrality in the current changing international circumstances. If the conclusion is further postponed, the momentum for finalising the RCEP might decrease. However, the level of liberalisation and the quality of the finalised RCEP will determine the trajectory of economic integration in East Asia; therefore, the level of liberalisation and quality should be deliberately and prudently considered. How to balance the speed and quality is one of the most difficult challenges that the RCEP member countries are facing.

12 Ishikawa, Koichi, "Higashi-ajia no FTA: Genjo to Kadai (FTAs in East Asia: the present and problems)", Japan Institute of International Affairs (JIIA), *The present and future of regional integration*, March 2014, p. 66.

13 "What is stopping India from joining RCEP trade deal?", *The Economic Tim*es, 6 January 2019, https://economictimes.indiatimes.com/news/economy/foreign-trade/what-is-stopping-india-from-joining-rcep-trade-deal/articleshow/67399881.cms, accessed 3 February 2019.

14 "Investment protection proposals under RCEP threaten India's Pharma industry", 15 March 2019, https://www.bilaterals.org/?investment-protection-proposals&lang=en, accessed 20 March 2019.

3. THE PROSPECTS OF THE RCEP

The prospects of the RCEP negotiation are still unclear. One of the critical concerns is the influence of the decoupling policy by the United States, which comes from the escalation of the Sino-American confrontation. The essence of this confrontation is the competition between the existing hegemonic power and an emerging power, as well as power over superiority of high-technology, which is a core part of hegemonic power. Some people in the policy-making circle in the United States have started calling the escalation of the Sino-American confrontation "the new Cold War."[15] In Washington D.C., the bi-partisan anti-China coalition, which is uniting because of a fear of China's emergence, has pushed US policy regarding China toward economic disengagement by means of setting barriers for Chinese entry into the US market.

Furthermore, the Trump administration has started to prevent other countries from engaging with China. The United-States-Mexico-Canada Agreement (USMCA), which replaced the North American Free Trade Area (NAFTA), was signed in November 2018. The USMCA contains a "non-market clause," which allows any party of the USMCA to review a trade agreement between the other parties of the USMCA and non-market economies before signing, and to withdraw from the USMCA if they choose the agreement with non-market economies.[16] No provision of the USMCA names China, but the "non-market clause" clearly aims to prevent Canada and Mexico from signing a trade agreement with China.

Now, the Trump administration aims to conclude or review bilateral trade agreements with economic partners in the Asia-Pacific such as Japan. The "non-market clause" in the USMCA implies the possibility that the US government would ask its counterparts to accept the same provision. If this happens, Japan and other trading partners of the United States would not be able to sign the RCEP as it includes China.

In addition to the possible negative pressure from the outside, the RCEP negotiation is facing serious obstacles from the inside. The most serious concern is the effect of the general election in India in 2019. As mentioned above, India was originally a reluctant player in fostering liberalisation because of strong pressure from the private sector in the country. India is also a democratic and pluralistic country, which means that political leaders must consider the strong voices of domestic

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15 "The new era of US-China decoupling", *Financial Times*, 20 December 2018, https://www.ft.com/content/019b1856-03c0-11e9-99df-6183d3002ee1, accessed 25 December 2018.

16 Agreement between the United States of America, the United Mexican States, and Canada Text, Article 32.10, https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/agreement-between, accessed 25 December 2018.

interest groups. Such considerations must occur during the election, and, due to this, the Indian government could not further compromise on market access this year. Thailand, the chair country of ASEAN in 2019, has just held a general election in March 2019 for the first time since the military junta came into power through a coup d'état in 2014. However, the political situation regarding the outcome of the election in Thailand is unclear. Thailand may be unable to take the initiative to promote the RCEP negotiation as the ASEAN chair in 2019 because of the unstable situation in its domestic politics. Such domestic political situations in key member countries will prevent the RCEP negotiation from being finalised.

Now, a multi-layered structure in terms of regional economic integration is emerging in the Asia-Pacific: the ASEAN Economic Community (AEC) was established in 2015; the CPTPP took effect in December 2018; and the RCEP is under negotiation. In addition, the United States is trying to push bilateral FTAs with its trading partners in the region. Given the current unclear global and regional circumstances, the overlapping of various trade agreements is a reflection of the competition over the vision of the appropriate international and regional order. While trials like the RCEP negotiation and the CPTPP encourage the liberal economic order based on a free and open market economy, the political, economic, and social systems of countries in East Asia and the Asia-Pacific are diverse, and protectionism is strengthening its influence on the world.

On the other hand, some have started to question whether the liberal economic order itself is desirable for every stakeholder. For example, some citizens' organisations protested the 25th round of the RCEP negotiation because they insisted that the RCEP "will worsen widespread poverty, injustice, and inequality through its numerous chapters that mainly cater to the needs of transnational corporations."[17] Not only the RCEP negotiation but also other trade agreements might have to address such concerns from grassroots movements in order to achieve a genuine, fair, and prosperous regional order in the region.

[17] "Women protest RCEP negotiations in Bali, Indonesia", AFTINET, 26 February 2019, http://aftinet.org.au/cms/node/1694, accessed 1 March 2019.

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ASEAN and E-Commerce: Lessons from the Singapore Chairmanship

Tham Siew Yean

INTRODUCTION

Google and Temasek's 2017 highlights on Southeast Asia's e-economy indicates the huge potential for e-commerce development in the region.[1] For example, the region as a whole has the third largest number of internet users in the world, totalling 330 million monthly active users as at the end of 2017. The internet economy for the region has grown from 1.3 percent of the region's Gross Domestic Product (GDP) in 2015 to 2 percent in 2017 and it is projected to reach 6 percent by 2025. It is relatively easier for the region to embrace new technology as the region's overall population is relatively young. An estimated 3.6 hours is spent on mobile internet every day in the region as compared to the 2 hours a day for the United States (US) and 1.8 hours a day for the United Kingdom (UK). More importantly, the people in the region also devote more time for shopping online every month. This is estimated at 140 minutes every month, or twice as much time expended by the Americans on shopping online.

Despite the potential, the region faces a fragmented e-commerce landscape that is considerably divided in terms of the stage of e-commerce development in each country. Numerous challenges abound, ranging from the legal and physical infrastructures needed to facilitate e-commerce to payment systems, security issues, logistics, including transportation challenges, especially in archipelagic parts of the region, to customs and cross-border administration. Thus, the Association of Southeast Asian Nations (ASEAN) has an important role to play here to foster greater cooperation in e-commerce that can contribute towards realising the region's

[1] See full report at http://storage.googleapis.com/201712/e-conomy-sea-spotlight-2017-unprecedented-growth-southeast-asia-50-billion-internet-economy/APAC-Google-Temasek-2017-spotlight.pdf, accessed 6 January 2019.

potential in e-commerce as well as using e-commerce to deepen the region's integration process.

This article seeks to provide a review of the evolution of e-commerce cooperation in ASEAN. Singapore's chairmanship in 2018 is highlighted in terms of the goals and achievements in e-commerce cooperation as well as important lessons from its chairmanship. In particular, how Singapore utilised the opportunities conferred from the rotational chairmanship to push further cooperation is summarised in the conclusion.

E-COMMERCE COOPERATION IN ASEAN

1997-2017

E-commerce cooperation in ASEAN has a long history as the seeds for cooperation can be traced back to the ASEAN Vision 2020 Plan that was launched in 1997. In the Plan, member countries were urged to accelerate the development of science and technology, including information technology (IT), by establishing a regional IT network.[2] Subsequently, an e-ASEAN initiative was introduced in 1999, leading to the launch of an e-ASEAN Framework Agreement in November 2000. The creation of an e-commerce friendly environment was one of the main elements in this agreement, which also has a specific focus on the adoption of e-commerce regulatory and legislative frameworks. Task forces and technical working groups were established to meet the e-ASEAN agreement goals, with Singapore being assigned as the shepherd for the task force on e-commerce, assisted by Malaysia and Brunei Darussalam. The primary mandates of the task force were to oversee e-commerce legislation on electronic transactions and electronic signatures as well as consumer protection in terms of online alternative dispute resolution as well as privacy and personal data protection.[3]

Accordingly, the task force developed an e-commerce reference framework in 2001, based on the existing e-commerce laws of ASEAN Member States (AMS), and in consultation with the legal experts from member states. At that time, five AMS,

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[2] Quimbo, R.N.S. (n.d.). "The E-ASEAN Legal Framework and Its Challenges". Retrieved from https://pdfs.semanticscholar.org/cd95/b15151d4fa37d206476ec222956fa5da056d.pdf, accessed 14 December 2018.

[3] Pichet Durongkaveroj (2002). "An Overview of e-ASEAN Initiative". Power-point presentation at ITU Workshop on Creating Trust in Critical Network Infrastructures 20-22 May 2002, Seoul. https://www.itu.int/osg/spu/ni/security/workshop/presentations/cni.24.pdf, accessed 14 December 2018.

namely Brunei Darussalam, the Philippines, Malaysia, Singapore and Thailand, already had e-commerce related laws which were included in the framework. The framework served to provide the general principles for e-commerce laws as well as the minimum provisions in these laws for the AMS. In this way, member countries without e-commerce laws at that point in time, namely Cambodia, Laos PDR, Myanmar and Vietnam, could use the reference framework to develop their own e-commerce laws. Concurrently, the framework was also meant to facilitate cross-border e-commerce and the cross-recognition/cross-certification of digital certificates/digital signatures.

The focus on e-commerce cooperation in ASEAN was continued in the ASEAN Economic Community (AEC) 2015 Blueprint as it is listed as one of the elements in the development of a competitive economic region, which is one of the four pillars in the Blueprint. The other three pillars are: (a) a single market and production base, (b) a region of equitable economic development, and (c) a region fully integrated into the global economy. E-commerce together with competition policy and intellectual property rights are meant to improve a country's business environment, thereby enhancing the competitiveness of ASEAN as a region.

The goal for e-commerce in the 2015 Blueprint is to lay the policy and legal infrastructure for e-commerce and to enable online trade in goods within ASEAN, through the implementation of the e-ASEAN Framework Agreement.[4] The priority actions for e-commerce, as shown in Table 1, continued to emphasise on the enactment of e-commerce laws, aiming for a harmonised legal infrastructure for ASEAN since the laws that were already enacted in the five AMS differed from each other in terms of electronic legislation; electronic signatures; licensing of certification authorities; and the liability of service providers.[5] However, capacity building was also explicitly recognised as needed for the region.

[4] Irawan, B. (2017). "AEC Blueprint Analysis: An Analysis of the ASEAN Cooperation in E-commerce". *CIMB ASEAN Research Institute (CARI)*, Vol. 1, Paper 19, 14 March.

[5] Quimbo, R.N.S. (n.d.). "The E-ASEAN Legal Framework and Its Challenges". Op. cit., p. 88.

Table 1. Strategic Schedule for ASEAN Economic Community 2015: Priority Actions for E-commerce.

2008-09	2010-2011	2014-2015
Member countries to enact their e-commerce laws	Update and/or amend relevant legislations in line with regional best practices and regulations in e-commerce activities	A harmonised legal infrastructure for e-commerce fully in place in ASEAN
Implement harmonised guidelines and principles for electronic contracting and online dispute resolution services	Adopt the best practices/ guidelines on other cyber-law issues (i.e., data privacy, consumer protection, intellectual propriety rights, internet service provider liability, etc.) to support the regional e-commerce activities	
Adopt regional framework and strategy for the mutual recognition of digital signatures	Advancing cross-border electronic transactions, through pilot implementation of mutual recognition of foreign digital signatures	
Continued capacity building and information sharing for Member Countries on e-commerce legal infrastructure activities		

Note: There were no actions lines given for 2012-13.

Source: ASEAN Secretariat.[6]

Since the designated monitoring tool, the AEC scorecard, is essentially each AMS's self-assessment of their respective compliance to the AEC Blueprint goals based primarily on ratification rather than outcomes or impact, it cannot indicate the actual progress made towards the goals for e-commerce as stated in Table 1. An alternative assessment on the state of legislation of e-commerce laws in ASEAN indicates that this is very much work-in-progress. Furthermore, according to the assessment made, there was also little sharing of best practices in cyber-security nor was the aspired harmonisation of legislative frameworks achieved.

[6] ASEAN Secretariat (n.d.). *Strategic Schedule for ASEAN Economic Community*. Retrieved from https://www.asean.org/storage/images/archive/21161.pdf, accessed 11 December 2018.

Table 2. Status of e-commerce laws in ASEAN.

Countries	Electronic transactions	Privacy	Cyber crime	Consumer protection	Content regulation	Domain names
Indonesia	Yes	Draft or partial	Yes	Draft or partial	Yes	Yes
Malaysia	Yes	Yes	Yes	Yes	Yes	Yes
Philippines	Yes	Yes	Yes	Yes	No	Yes
Singapore	Yes	Yes	Yes	Yes	Yes	Yes
Thailand	Yes	Draft or partial	Yes	Yes	Draft or partial	Draft or partial
Vietnam	Yes	Draft or partial	Yes	Yes	Yes	Yes

Source: ATKearney and CIMB Research Institute (CARI), n.d.[7]

Focussing on the regulatory framework is, however, insufficient as creating a trade-friendly e-commerce ecosystem requires other complementary initiatives in terms of Information, Communication and Technology (ICT) development, logistics as well as coordination in customs procedures, tax rates and invoicing standards.[8] ASEAN's efforts to address these related pertinent issues are found in the other AEC 2015 initiatives. The ASEAN ICT Masterplan 2015 (AIM 2015), for example, addressed the need for supportive infrastructure development as well as to bridge the digital divide, while the Roadmap for the Integration of Logistics (RILS) aimed at the creation of an integrated ASEAN logistics environment. Trade facilitation in the ASEAN Trade in Goods Agreement (ATIGA) covered customs as well as non-customs issues. Effectively, this implies that the multi-dimensional nature of e-commerce is addressed through numerous existing ASEAN agreements, rather than housed under one agreement. But, even though the actual work programmes of these different initiatives were rather narrow in scope, not all were achieved by 2015.

Thus, when the AEC 2015 was launched as a milestone in the evolution of the AEC, the Blueprint goals which were not achieved were included in the AEC 2025 plans. Consequently, e-commerce is also included in the AEC2025 Plan to continue the efforts made in e-commerce cooperation due to its potential to support eco-

[7] ATKearney and CIMB Research Institute (CARI) (n.d.). "Lifting the Barriers to E-Commerce in ASEAN". Retrieved from https://www.atkearney.co.uk/documents/10192/5540871/Lifting+the+Barriers+to+E-Commerce+in+ASEAN.pdf, accessed 20 December 2018.

[8] Mik, Eliza (2017). "Legal and Regulatory Challenges to Facilitating E-Commerce in the ASEAN". Retrieved from https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3100578, accessed 20 December 2018.

nomic integration in ASEAN.[9] In the AEC2025 Plan, developing an ASEAN Agreement on e-commerce that can facilitate cross-border e-commerce transactions in the region is an important goal. Efforts to broaden the scope of cooperation within the ambit of e-commerce law and legislation can be seen from the areas for co-operation that are in the Plan, such as: (i) harmonisation of consumer rights and protection laws; (ii) harmonisation of legal frameworks for online dispute resolution mechanisms; (iii) development of inter-operable, mutually recognised, secure, reliable and user friendly e-identification and authorisation (electronic signature) schemes; and (iv) the development of a coherent and comprehensive framework for personal data protection. As in the case of other ASEAN agreements, the stated goals in the Plan need an action and/or work plan to work out the concrete actions that will be undertaken to attain the aspired areas of cooperation.

When the Philippines assumed the ASEAN chairmanship in 2017, its focus for the AEC was on inclusive, innovation-led growth.[10] E-commerce was included as one of the 11 priority deliverables and it was subsequently announced at the 49th ASEAN Economic Ministers' Meeting that an ASEAN Coordinating Committee on Electronic Commerce (ACCEC) had been established to promote, coordinate and enhance the efforts made by various ASEAN sectoral bodies to promote the growth of e-commerce in ASEAN.[11] The Ministers also adopted the ASEAN Work Programme on Electronic Commerce (AWPEC) 2017-2025. The AWPEC focusses on cross-border e-commerce and brought together the multi-sectoral needs of e-commerce. Specifically, the work programme covers ten areas of cooperation, namely: (i) infrastructure; (ii) education and technology competency; (iii) consumer protection; (iv) modernising the legal framework; (v) security of electronic transactions; (vi) payment systems; (vii) trade facilitation; (viii) competition; (ix) logistics; and (x) e-commerce framework. The Work Programme specifies the initiatives for each of these ten areas, the output to be delivered as well as the implementing

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9 ASEAN Secretariat (2015). *ASEAN 2025: Forging Ahead Together*. Retrieved from https://www.asean.org/wp-content/uploads/images/2015/November/KL-Declaration/ASEAN%202025%20Forging%20Ahead%20Together%20final.pdf, accessed 20 December 2018.

10 Undersecretary Enrique A. Manalo's Keynote Address at the Foreign Service Institute's *Mangrove Forum on International Relations* on *"The Philippines Chairmanship of ASEAN"*, 24 January 2017, Mindanao Ballroom, Sofitel Philippine Plaza, Pasay City in Foreign Service Institute Insights, Vol. IV, No.1, 2017. Retrieved from http://www.fsi.gov.ph/the-philippines-chairmanship-of-asean-in-2017/, accessed 4 January 2019.

11 Retrieved from https://cil.nus.edu.sg/wp-content/uploads/formidable/14/2017-49th-AEM-Joint-Media-Statement.pdf, accessed 4 January 2019.

bodies.[12] The tenth dimension in the AWPEC 2017-2025 refers back to the need to develop an e-commerce Framework, which includes a review of the elements of an ASEAN e-commerce framework and the development of an agreement in 2018. Getting an ASEAN agreement on e-commerce signed is listed as the sole output in this dimension.

2018: E-commerce developments under Singapore's chairmanship

When Singapore took over the chairmanship in 2018, it was close to two decades since the e-ASEAN Framework Agreement was launched in November 2000. Based on the theme of a resilient and innovative ASEAN,[13] five key thrusts were chosen as the deliverables for furthering the development of the AEC. These are promoting innovation and e-commerce; improving trade facilitation; deepening services and investment integration; cultivating a conducive regulatory environment; and forging ahead on ASEAN's external relations.[14] Given that the digital economy contributed seven percent of ASEAN's Gross Domestic Product (GDP), and has the potential to grow further, digitalisation became a flagship deliverable under Singapore's chairmanship.[15] Therefore, Singapore prioritised getting an ASEAN Agreement on Electronic Commerce signed by the end of its chairmanship. The agreement will serve to streamline rules governing e-commerce so as to lower the operating barriers to entry and enable business to better navigate the regulations in the region. Another priority is the ASEAN Digital Integration Framework, which will identify the key focus areas for ASEAN in the immediate future. The two priorities are clearly in line with the theme on an innovative ASEAN and using innovation to create regional resilience.

Importantly, Singapore did not just use its chairmanship to shape the agenda for ASEAN to forge ahead in terms of e-commerce cooperation. It has also successfully delivered on the two stated priorities. The ASEAN Economic Ministers signed

[12] For further details, see https://asean.org/asean-economic-community/sectoral-bodies-under-the-purview-of-aem/e-commerce/, accessed 4 January 2019.

[13] See ASEAN 2018 page in https://www.mfa.gov.sg/content/mfa/overseasmission/asean.html, accessed 4 January 2019.

[14] See "Updates on the ASEAN Economic Community", in *ASEAN Integration Brief*, No. 03, June 2018. Retrieved from https://asean.org/storage/2018/02/AEIB_3rd-Issue_v3-Ready-Print-Single-Page.pdf, accessed 4 January 2019.

[15] Chan Chun Sing, 2018. "A Resilient and Future-Ready ASEAN", in *ASEAN Integration Brief*, No. 4, November 2018. Retrieved from https://asean.org/storage/2018/11/AEIB_4th-Issue_r1.pdf, accessed 4 January 2019.

the ASEAN Agreement on e-Commerce on 12 November 2018, on the side-lines of the 33rd ASEAN Summit and Related Meetings. Furthermore, the ASEAN Digital Integration Framework (DIF) was also endorsed to monitor the progress of ASEAN's digital integration.

The E-commerce Agreement itself builds on past efforts that are pertinent to the issue. Specifically, Article 5 in the e-ASEAN Framework Agreement (2000) which refers to the facilitation of the growth of electronic commerce and the electronic commerce chapter of the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA, 2009) are used as the foundations for the agreement.[16] At the same time, modern elements such as cross-border transfer of information by electronic means, location of computing facilities and cybersecurity are incorporated into the agreement. The three stated objectives of the agreement are to: (i) facilitate cross-border e-commerce transactions; (ii) contribute towards creating an environment of trust and confidence in the use of e-commerce; and (iii) deepen cooperation among AMS to further develop and intensify the use of e-commerce to drive economic growth and social development in the region. Eight dimensions are covered in the agreement, namely, domestic regulatory framework; transparency; cooperation; facilitating electronic transactions and trading; cross-border data and information flows and location of computing facilities; logistics; consumer protection and privacy; and technology neutrality. Given the fast changing nature of e-commerce, a review clause is also included in the agreement to amend it based on the evolution of this type of trade over time.

CONCLUSION: KEY LESSONS FROM SINGAPORE'S CHAIRMANSHIP

The chairmanship of ASEAN is rotated annually based on the alphabetical order of the AMS. An important component of the chairmanship is the prerogative to propose the priorities for ASEAN's agenda for the year of its chairmanship. Of course, given the ASEAN way, this prerogative needs to be exercised with the agreement of other member states. For 2018, Singapore has successfully utilised its chairmanship to set an agenda that will drive ASEAN cooperation forward. Specifically, for e-commerce, it chose to focus on one of the stated goals of the AWPEC, and which is crucial for moving ahead in the region's e-commerce cooperation. Indeed, being

[16] Factsheet, 2018. "Promoting innovation and e-commerce through the ASEAN Agreement on Electronic-Commerce", Retrieved from https://www.gov.sg/~/sgpcmedia/media_releases/mti/press_release/P-20181112-1/attachment/Annex%20A%20Factsheet%20on%20ASEAN%20Agreement%20on%20e-Commerce.pdf, accessed 5 January 2019.

able to choose strategically an important and relevant agenda for the times is a hallmark of Singapore's past chairmanship as well, such as the establishment of the ASEAN Free Trade Area (AFTA), during the 4th ASEAN Summit in Singapore in 1992, and the conclusion of the ASEAN Charter at the 13th ASEAN Summit in 2007 in Singapore.[17]

Having set the agenda, Singapore has to manage the difficult task of building consensus to be able to meet its deliverables.[18] As noted by Ambassador Ong Keng Yong at the start of Singapore's chairmanship, getting other member states to buy into the agenda can be quite an onerous task due to the different levels of economic development in the region.[19] Considerable diplomatic acumen is needed to build the needed consensus in order to conclude the agenda successfully.

Thus, key lessons from Singapore's chairmanship are the adroit use of leadership and diplomacy to set an agenda that is appropriate for the times and equally importantly, to be able to bring the agenda to a successful conclusion. Clearly then the chairmanship role in ASEAN is far from ceremonial and has been put to good use by Singapore to further cooperation within ASEAN. Given that there are many more desired outcomes in e-commerce in the AWPEC until 2025, the momentum that was set in 2018 by Singapore should be continued to bring all these to fruition.

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17 Termsak Chalermpalanupap (2018). "Singapore as the ASEAN Chair: Responsibilities and Legacies". *ASEAN Focus*, Issue 4/2018, page 15.

18 Tang Siew Mun (2015). "The ASEAN Chairmanship: Duties, Obligations and Challenges", *ASEAN Focus*, Issue 2/2015, page 4.

19 Albert Wai (2017). "Looking ahead to 2018: ASEAN's Chairmanship poses a stern test for Singapore." Retrieved from https://www.todayonline.com/world/looking-ahead-2018-asean-chairmanship-poses-stern-test-singapore, accessed 5 January 2019.

EU-Singapore Free Trade Agreement

Deborah Elms

AT THE OUTSET

In the beginning, the European Union (EU) intended to start negotiations on a bloc-to-bloc trade agreement with the 10 member nations of the Association of Southeast Asian Nations (ASEAN). Such an arrangement would hook together two large and diverse regional actors – the then-27 members of the EU with the 10 members of ASEAN (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam). The importance of ASEAN to European markets was large and rising, making the prospects for deeper integration in 2007 look quite promising.

However, while ASEAN may appear to operate as an integrated bloc, it does not negotiate as one. Instead, the 10 members negotiate trade separately, making a potential trade agreement with the EU a long and protracted affair. The EU therefore decided to switch tacks, building up to an integrated deal by starting with a series of bilateral arrangements with ASEAN member states.

Singapore was the most promising initial candidate. Not only was it the member most familiar with negotiating trade agreements, but the bulk of European trade was routed into or through Singapore.

Figure 1: EU-Singapore Trade Figures.[1]

Keeping consistency across ASEAN-member FTAs could make it easier to combine six agreements into one (with Singapore, Malaysia, Thailand, Philippines, Indonesia and Vietnam). Cambodia, Laos and Myanmar were not invited to join in bilateral negotiations with the EU, but these countries already received preferential access to Europe through "Everything But Arms" trading schemes.[2] Hence, by the end of the process, the Europeans could combine enough "building block" agreements to finally wrap up a region-to-region deal.

Negotiations commenced with Singapore in 2010. The basic framework was finished by 2012, with a few minor issues remaining. As discussed in greater detail below, sticking points included geographical indications, financial services, and investment rules. The deal (except for investment) was finished by October 2014. In May 2015, both sides announced the conclusion of the agreement, when the final legal scrubbing was completed for the investment chapter.[3]

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[1] *European Union-Singapore Trade and Investment Agreements Booklet*, EU Commission and Singapore MTI, 2019, http://trade.ec.europa.eu/doclib/docs/2019/february/tradoc_157684.pdf.

[2] The last ASEAN member, Brunei, was simply not an important enough bilateral partner to warrant separate negotiations. It would have to wait until the regional agreement was ready and be folded in at that time.

[3] See Singapore's Ministry of Trade and Industry Press Release at http://www.mti.gov.sg/NewsRoom/SiteAssets/Pages/Singapore-and-the-European-Union-Initial-the-Investment-Protection-Chapter-/Press%20release%20on%20EUSFTA%20IPC%20Initialling.pdf, accessed on 15 July 2015.

EXPLORING THE EUSFTA IN DETAIL[4]

So, what happened in the EU-Singapore FTA (EUSFTA)? In brief, the bilateral agreement represents a relatively high quality outcome. This result was easier to obtain than in many negotiations, given the quite open nature of the Singapore market. For example, Singapore's applied tariff rate for all goods (except for six tariff lines for some alcohol products and cigarettes) is zero. This always makes it easier to craft a trade agreement, since Singapore has fewer built-in sensitivities in goods that must be accommodated.

The final trade agreement covers most goods, including a few new provisions on electronics and a consultation process for agricultural trade regulations. Several important sectors have specific coverage under the agreement. Services trade was also opened and liberalised with a clear eye towards crafting an ASEAN-wide deal on services for the future.

The agreement also included provisions on government procurement, new rules on intellectual property rights including a greatly expanded set of covered geographical indications, a chapter on competition, development objectives, and labour standards. Each of these elements is covered in more detail below.

Trade in Goods

Given Singapore's duty-free applied access to goods, the EUSFTA binds Singapore tariffs at 0 for European goods imports. The bulk of the negotiations focused on tariff reductions for the European side. Basically, the EU agreed to reduce its own tariffs to match the levels found in the 2011 EU-Korea free trade agreement (EUKTA) within five years of entry into force. This included dropping tariffs to 0 on entry into force for approximately 75% of tariff lines. Most of the remaining lines were also scheduled to go to 0 across a time period of 3-5 years, with reductions taking place in annual instalments.

A goods agreement cannot be evaluated on the basis of tariff line reductions alone, however. Trade between parties is often concentrated, so the bulk of actual trade between members in an FTA might take place in a handful of tariff lines alone. If these lines are not included in the final agreement, a headline figure of even 95% tariff reductions may not translate into meaningful economic outcomes on the ground. However, EU-Singapore trade is relatively widely dispersed making it more

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[4] This section borrows heavily from the chapter by Elms in AnnMarie Elijah, Donald Kenyon, Karen Hussey, and Pierre Van Der Eng (eds), *Australia, the European Union and the New Trade Agenda*, ANU Press, 2017.

likely that tariff cuts would affect tradeable sectors like machinery, chemicals and pharmaceuticals.

Tariffs also interact with rules of origin (ROOs). ROOs are necessary to ensure that only firms from member countries are eligible to receive the benefits (particularly lower tariff rates) built into the agreement. If any company could take advantage of the deal, it would undermine the specific benefits for members. Hence, every FTA comes with rules of origin to ensure that products claiming preferences are either wholly "from" members (i.e., grown, produced, mined or extracted from the member without any additional content added from any other member state) or are substantially transformed from their original materials or components into a new type of product within the geographic spaces covered by the FTA.

It is possible to create an agreement with 0 tariffs across the board, but make the requirements for receiving duty-free treatment so onerous that almost no firms are able to take advantage of the lower tariff rates. Or, conversely, it is possible to have tariffs drop by less, but make it so easy for firms to use the agreement that nearly all companies participate in the agreement.[5]

The EUSFTA contains mostly product-specific ROOs. The agreement includes some co-equal rules (which allow firms to use one *or* the other of two calculation methods to prove sufficient content). The agreement is effectively a bilateral agreement between the EU (counting EU members as if they were one) and Singapore. Hence, the agreement does not allow content from across ASEAN to count towards content. This can be a problem for Singapore, since the country has very few indigenous items to add to a product's content. Singapore's major exports to the EU include oil and oil-related products, manufactured goods (especially electronics), and pharmaceuticals. With raw materials, parts and components usually coming from overseas, it is not always possible to reach high levels of locally added content, absent the ability to add up, or cumulate, content from elsewhere. Nevertheless, as the EU moves towards incorporating all the bilateral trade agreements into one

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[5] Companies never get the benefits of an FTA automatically – each requires firms to certify that they are using an FTA. The method of certification varies, but often FTAs require a certificate of origin to be obtained from a local chamber of commerce or another designated body before customs officers at the border will grant lower tariffs. Without a certificate of origin (or self-certification in some newer generation agreements), products cannot qualify for the preferential rate and are instead charged the most-favoured-nation (MFN) rate. The MFN tariff rate is the tariff charged to all World Trade Organisation (WTO) members automatically without requiring any certification of origin. Since more than 160 countries are WTO members, practically speaking, nearly all firms can use MFN rates for their goods shipments. For many firms, unless the preferential benefits of an FTA are substantial, companies often opt to avoid the hassle required in using the provisions of an FTA and ship goods under MFN tariffs.

region-wide ASEAN agreement, it is likely that ASEAN cumulation rules will be built in the future, making it easier for Singaporean firms to use the final ASEAN-wide agreement.

The EU did not pledge to reach duty free status in all products. The EUSFTA left some items that will not be subject to tariff elimination including some fish products (tilapia, catfish, salmon in vegetable oil, bonito, and surimi); as well as chemically pure fructose; and sweetcorn and maize.

Specific customs duties will remain for some vegetable and fruit products imported into Europe including: vegetables (fresh or chilled tomatoes, cucumbers, globe artichokes, and courgettes); citrus (including fresh sweet oranges, clementines, monreales and satsumas, mandarins and wilkings, tangerines, and lemons); and fruits (including table grapes, apricots, sour cherries, nectarines, and plums).[6]

Other Goods Provisions

The agreement included an additional chapter on what are called Technical Barriers to Trade (TBT). These are largely regulatory and standards-based rules that govern specific types of goods. The EUSFTA sets up a rudimentary structure to strengthen cooperation in regulatory areas in the future, as well as better procedures for exchanging information and streamlining regulations between the parties.

One exception to the largely generic nature of the TBT rules can be found in an annex on electronics. Singapore has an unusually complex system of testing in this sector. The agreement contains promises to use conformity assessments and international standards bodies as much as possible.

Another chapter covers rules for food and food safety. The Sanitary and Phytosanitary (SPS) chapter codified that both sides can have import requirements for food and food stuffs. Imports can be stopped and checked for compliance with relevant SPS rules, under a set of procedures that were tightened and clarified with specific timelines for inspections. The agreement sets out a variety of committees and consultations to take place around SPS issues in the future.

Finally, the agreement also sets out four sector-specific provisions. For autos, Singapore agreed to recognise EU standards and testing regimes for cars and car parts. The agreement also has language on green rebates for more environmentally friendly autos. A second section covers electronics, where Singapore agreed to gradually replace third-party testing of products (particularly to accept supplier's

[6] For the specific exceptions, please see the market access schedules of the EU found in Annex 2A Appendix at: http://trade.ec.europa.eu/doclib/press/index.cfm?id=961, accessed 21 February 2019.

declarations of conformity that are widely used inside the EU). A third sectoral element of the EUSFTA looked at pharmaceuticals where the primary pledge calls for greater transparency in pricing structures. Finally, the agreement has a section on green technology. Both sides pledged to allow renewable energy equipment to move between the EU and Singapore with national treatment (foreign products granted the same treatment as locally produced comparable items) and no additional conformity tests.

Trade in Services

While the agreement covers trade in goods, the primary offensive objective of the European Union was to improve access to Singapore's services markets. Services could include financial services, insurance, banking, brokerage, accounting, design, architecture, legal, management, food and beverage, travel and tourism and so forth. For most developed economies, services can represent the bulk of economic activity. Even in manufactured goods, the services content of goods in cross-border supply chains can be 40-70 percent. Hence, greater access and better protections of these key sectors were important objectives for both sides.

The European Union claimed to have given Singapore levels of access comparable to the EU-Korea FTA[7] in telecommunications, financial services, computer, transport, environmental services and some business services. The sections of the agreement covering postal services, the EU argued, went beyond what Korea got.

Both parties agreed that the governments may not use licensing requirements as a mechanism to obstruct entry into services markets. While licensing is not a particularly serious barrier to entry in either the EU or Singapore, this remains a favoured mechanism in many ASEAN countries to restrict foreign firm competition. Hence, the inclusion of clauses on licensing for services in the EUSFTA is primarily a marker for future ASEAN and ASEAN-wide agreements.

To ensure that both parties maintain the very best access to each other's services markets going forward and to capture whatever gains come from future negotiations with other partners, the parties agreed to include a most-favoured-nation ratchet clause into the agreement. This means that the EU automatically receives new, matching benefits if Singapore ever negotiates an improved services agreement in any other format and vice-versa for Singaporean firms entering the EU.

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[7] The text of EUKFTA can be found at https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=OJ:L:2011:127:TOC, accessed 21 February 2019.

The services chapter does not cover all services. Carved out of the deal are: audio-visual services; national maritime cabotage; air transport; and mining, manufacturing and processing of nuclear materials. The Europeans were not terribly successful in getting new market access to Singapore's financial services sector.[8]

The EUSFTA opens up competition in postal services. These are services that are often considered sensitive by many governments with extensive restrictions or non-existent options for entry into the market.

Both sides agreed that telecommunications has a vital role to play in business today. They agreed to respect the confidentiality of information and to require firms to provide services on non-discriminatory terms, conditions or rates. The agreement also outlined competitive safeguards for major suppliers of telecoms services. While the agreement does not break new ground on e-commerce, it does pledge cooperation between both sides. Both sides agreed to avoid imposing unnecessary restrictions or regulations on e-commerce activities. The agreement recognises the importance of the free flow of information and commits both sides to uphold international standards of data protection.

Other New Areas of Coverage

Meat: One issue of concern for Europe was Singapore's complex system of approval for meat imports. Under the EUSFTA, Singapore agreed to remove a requirement that meat products should be individually inspected and approved by the Agri-Food and Veterinary Authority (AVA) in Singapore. Going forward, Singapore agreed to set up an auditing system and allow inspections only when triggered by the auditing system.

Government procurement: Both Singapore and the European Union are signatories to the Government Procurement Agreement (GPA) at the World Trade Organisation (WTO). Since both parties are included in the GPA, the EUSFTA extended the coverage areas under which tenders are to be accepted. The EU agreed to include EU central government entities, public works concessions like railways, and some additional utilities. In addition, the EU dropped the threshold levels for bidding by Singaporean firms.

8 The goal was to get comparable coverage to what the Americans received in their bilateral FTA with Singapore. But the EU was not successful in meeting this object. See Singapore's specific commitments on financial services in Annex 8B-2: http://trade.ec.europa.eu/doclib/docs/2013/september/tradoc_151750.pdf, accessed 21 February 2019.

Geographical Indications (GIs)

Although the EUSFTA includes other elements in the intellectual property rights chapter, nearly all the focus was on geographical indications (GIs). This issue nearly derailed the entire negotiations and largely held up the conclusion of the agreement for nearly two years.

The basic problem is that the EU is the world's most staunch supporter of GIs, while Singapore has been generally hostile to the idea. To complicate matters further, Singapore was simultaneously negotiating an FTA with the United States and other parties in the Trans-Pacific Partnership (TPP). The TPP specifically did not include GIs and TPP members were extremely uncomfortable with reconciling the two agreements at the end.[9]

A GI is a specific type of product protection. Put simply, a GI suggests that products are unique largely due to specific conditions, reputations and traditions surrounding their creation. These products cannot be recreated elsewhere and should not be allowed to bear similar names. To allow similar names is to confuse consumers who are not receiving benefits from all the specific aspects of a good.

The EU has pushed for the inclusion of GIs in FTAs and has expanded the list of products beyond wines and spirits (many of which now have protections at the global level under the WTO) to items like cheeses and meats.[10] Once a product receives GI protections, no other similar product can use the same product terms even if the label makes the origin explicit. The EU tries to stop firms from producing products made "like" or "in the style of" or using a "method."

Singapore had no list of GI protections and no products that it wanted included on a list. After heated negotiations, Singapore developed a list of 196 products to be granted GI protections in the marketplace. Recognition was therefore not automatic, but subject to negotiation and approval from the regulatory authorises in Singapore. The Singapore list is particularly heavy on compound names (not just

[9] The resolution of this issue in the aftermath of Singapore's commitments in the EUSFTA for the TPP has been to allow GIs for "compound names." In general, such product designations require two names. Thus, "feta" cheese is considered generic (and not protected). But "Wisconsin cheddar" might qualify. See the CPTPP texts, Chapter 18, Section E at: https://www.mfat.govt.nz/assets/Trans-Pacific-Partnership/Text/18.-Intellectual-Property-Chapter.pdf, accessed 21 February 2019.

[10] In the EU-Korea FTA, the GIs annex runs to 22 pages and includes a wide range of products including a host of different types of mushrooms. The EU's internal register of these products includes more than 1000 food items and 3000 different types of alcohol. The US, by contrast, prefers to give products protection under trademarks, if the products meet the necessary criteria for trademark protection.

parmesan cheese, but Parmesan-Reggiano cheese or not just ham but Parma Ham) and items already protected with trademarks. In general, the stance of the Singaporean government was to add products to the list only after determining whether such product names were viewed in Singapore as a "generic" name. If so, products could not be granted GI protection.

Singapore added another wrinkle to the negotiations by insisting in a side letter that the entire agreement would not go into force until the GI procedures were sorted out and the list of protected GIs was confirmed by the Singapore Parliament. The bill was passed in April 2014.[11]

Competition Chapter

The agreement includes a chapter on competition policy. Both Singapore and the EU already have in place laws that are designed to prevent the growth and spread of monopolies. Hence, the chapter starts at a deeper level and commits both parties to enforcing their own respective laws on competition. The chapter also urges both sides to address the horizontal and vertical agreements between undertakings that might distort competition.

The chapter does, however, explicitly allow for public undertakings with special or exclusive rights and the maintenance of state monopolies. Finally, the chapter includes provisions that clarify procedures around subsidies. The agreement allows for subsidies for things like: serious disturbances to the economy; the coal industry; social character; natural disasters; economic development for abnormally low income areas; certain economic activities like research and development (R&D), environment and supporting small and medium sized (SMEs) enterprises; culture; and regional interest projects.

Trade and Sustainable Development

All European agreements include a chapter on trade and sustainable development, including the EUSFTA and the EUKFTA. The primary purpose in these two agreements is to include binding commitments on domestic levels of environmental and labour protections consistent with core international standards and agreements.

The deal has provisions for corporate social responsibility (CSR) activities, as well as conservation efforts. Fish and logging are specifically highlighted in the texts.

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[11] The legal text of the legislation can be found at https://sso.agc.gov.sg/Act/GIA2014/Uncommenced/20171124?DocDate=20140523, accessed 21 February 2019.

This chapter includes information about the procedures for stakeholder engagement and consultation with civil society. Finally, the chapter comes with its own dispute mechanism.

Labour Standards in EUSFTA

The agreement gives each party the right to establish their own levels of labour protection. Both sides also have the right to adopt or modify relevant laws or policies on labour. Finally, both sides committed to upholding the 1998 International Labour Organisation (ILO) Declaration. Under this provision, parties agreed to the freedom of association, and effective recognition of the right to collective bargaining; elimination of all forms of forced or compulsory labour; effective abolition of child labour; and elimination of discrimination in respect of employment and occupation.

THE INVESTMENT AGREEMENT

The original EUSFTA included a chapter on investment. However, internal changes in the EU over the prolonged course of negotiations meant that investment was eventually detached from the EUSFTA and put into a separate agreement, now called the EU-Singapore Investment Agreement.[12] There is insufficient space to detail the specifics of this element of the negotiations except to note that the investment provisions should be viewed in parallel with the EUSFTA.

THE RATIFICATION JOURNEY

Issues over investment derailed ratification of the EUSFTA for years. To simplify significantly, while the EU Commission originally negotiated investment as part of the FTA, by the time of conclusion, member states insisted that a decision on competence should be determined by the European Court of Justice (ECJ). The ECJ decision took a very long time and the final determination split the EUSFTA into two elements – the trade components and a separate investment agreement.

The EU Parliament gave approval to both elements in February 2019, paving the way for final procedures to be completed. The last hurdle prior to entry into force for the EUSFTA has been that Singapore needed to register GIs. This final step

[12] The complete text can be found at: http://trade.ec.europa.eu/doclib/press/index.cfm?id=961, accessed 21 February 2019.

over GIs replicated the delay in the original negotiations which kept the talks from concluding for over a year.

However, once the latest issue with GIs is resolved, the EUSFTA will come into force and companies will – at very long last – be able to start using the provisions of the agreement first mooted more than a decade previously. At that point, the EU will finally be able to move ahead as well with the original plan to use the deal as the first building block to a regional agreement in the future.

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Trade and Economic Connectivity in an Age of Uncertainty: South Asia and Indo-Pacific

Amitendu Palit

The world of global commerce has been experiencing multiple disruptions in recent years. Soon after national economies began settling down to a new period of global growth following the financial crisis of 2008, fresh disruptions affected the adjustment. A lot of the disruptions began from the assumption of office by Donald Trump as the president of the United States (US). However, there were also other sources of disruption, including from the ambitious connectivity project – the Belt and Road Initiative (BRI) – proposed by China. Continental connectivity has become the new domain for competition on strategic influence as is evident from the articulation of the Indo-Pacific by the United States. Given that the overall tussle for global economic supremacy between the US and China has little possibility of receding in the foreseeable future, countries have to reconcile to the prospects of connectivity and trade being heavily influenced by geopolitics. This paper is an attempt to locate these prospects in a South Asian regional perspective of the Indo-Pacific. The paper traces the genesis of the idea of the Indo-Pacific and discusses how modern infrastructure connectivity projects, particularly in the Indo-Pacific, are becoming hubs of geostrategic competition. Arguing the possibility of new connectivity enlarging existing economic gaps, the paper discusses the implications of various US pronouncements on the Indo-Pacific and how the US-China battle for influence might employ connectivity for shaping trade on geopolitical lines. There is little that South Asia can do in terms of a response except the realising of the inevitability of trade and connectivity being influenced by the security and strategic interests of major powers.

THE IDEA OF INDO-PACIFIC

Though the phrase *Indo-Pacific* has gained wide traction in global security and strategic discourses since President Trump's articulation of it at the Asia-Pacific

Economic Cooperation (APEC) Summit in Vietnam in November 2017,[1] its salience was iterated in Asia much earlier. In his address to both Houses of the Indian Parliament on 22 August 2007, the Japanese Prime Minister Shinzo Abe had mentioned: "The Pacific and the Indian Oceans are now bringing about a dynamic coupling as seas of freedom and of prosperity. A 'broader Asia' that broke away geographical boundaries is now beginning to take on a distinct form."[2] Apart from the allusion to major geostrategic shifts imminent in the global order that were discernible from the speech, the fact that it was delivered in India was also equally significant; ostensibly in terms of the importance that India and the South Asian region would have in the shaping of the Indo-Pacific.

Prime Minister Abe's speech highlighted several critical points. The first of these was the emergence of the Asian continent as a distinct geo-economic and political variable with as much importance as the US and Europe. Furthermore, within Asia, there was clear recognition of the strategic hub settling in the arc encompassing the Indian and Pacific Oceans. From the point of view of extra-Asian actors, like the US and Europe, it entailed a wider focus on the continent. It must be noted that till almost the end of the last decade, the greater attention of the US and Europe on Asia was concentrated primarily on the Middle East and West Asia regions. From 2009 onward, under President Barrack Obama, US policy attention shifted significantly towards the Asia-Pacific through what is described as the US "pivot to Asia"[3]. Among other factors, the US policy shift would have been influenced by the rise of China, as well as that of India, leading to significant changes in the geo-economic and political character of Asia and greatly enhancing the strategic importance of the Indian and Pacific Oceans.

Prime Minister Abe's speech was also visionary as it was delivered about a year before the outbreak of the global financial crisis in 2008. The damage suffered by financial institutions on both sides of the Atlantic made it evident that non-Atlantic economies would need to play a much bigger role in the recovery and sustenance

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1 "Remarks by President Trump at APEC CEO Summit | Da Nang, Vietnam", Foreign Policy, 10 November 2017, The White House, https://www.whitehouse.gov/briefings-statements/remarks-president-trump-apec-ceo-summit-da-nang-vietnam/, accessed on 20 March 2019.

2 "Confluence of the Two Seas", Speech by H.E. Excellency Mr Shinzo Abe, Prime Minister of Japan at the Parliament of the Republic of India, 22 August 2007, Ministry of Foreign Affairs, Government of Japan, https://www.mofa.go.jp/region/asia-paci/pmv0708/speech-2.html, accessed on 20 March 2019.

3 Michael J Green, 2016; "The Legacy of Obama's 'Pivot' to Asia", Foreign Policy, 3 September, https://foreignpolicy.com/2016/09/03/the-legacy-of-obamas-pivot-to-asia/, accessed on 20 March 2019.

of global economic growth. This included not just China, Korea, Japan and the industrial and emerging economies of Southeast Asia (i.e., Singapore, Malaysia, Indonesia and Vietnam), but also India and South Asia, thereby drawing into sharp focus the geo-economic vitality of the Pacific and Indian Oceans. A deeper reflection on Prime Minister Abe's speech and his articulation of the concept of Indo-Pacific cannot avoid identifying the rising engagement between East and Southeast Asia, the Middle East, Africa, and the hitherto under-recognised, but nonetheless critical role of the Indian Ocean. The construct for future cross-continental trade and connectivity frameworks could be visualised in a framework assuming the combined growth of both through the congruence of the Pacific and Indian Oceans.

Since Prime Minister Abe's speech, the concept of Indo-Pacific has gained considerable traction, particularly after its expanded US iteration as the "Free and Open Indo-Pacific (FOIP)", culminating in the pronouncement of the Asia Reassurance Initiative Act (ARIA) of 2018. Signed into law on 31 December 2018, ARIA marks the US strategy to "increase U.S. security, economic interests, and values in the Indo-Pacific region"[4]. Separately, various earlier American pronouncements on the subject[5] leave little doubt about the salience of the Indo-Pacific as a multicontinental and cross-ocean entity poised to alter the geo-economic and geopolitical architectures engulfing the Pacific and Indian Oceans. The development has great significance for India and the South Asia region in terms of its impacts on trade and economic connectivity.

CONNECTIVITY: CHARACTER AND COMPETITION

The notion of connectivity, as visualised through cross-country infrastructure projects, has undergone fundamental changes. Nowhere are these changes more visible than in the Indo-Pacific region in the form of large-scale ambitious projects linking territories, markets and communities across the continent. The Pacific and the Indian Oceans have been at the core of regional connectivity schemes from well before the FOIP was pronounced. The most notable project has been the China-led

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[4] S 2736, Bill Announcement, The White House, 31 December 2018, https://www.whitehouse.gov/briefings-statements/bill-announcement-12/, accessed on 20 March 2019.

[5] 1. "Remarks by President Trump at APEC CEO Summit | Da Nang, Vietnam", Foreign Policy, 10 November 10 2017, The White House, https://www.whitehouse.gov/briefings-statements/remarks-president-trump-apec-ceo-summit-da-nang-vietnam/; 2. "President Donald Trump's Administration in Advancing a Free and Open Indo Pacific", Economy & Jobs, 30 July 2018, The White House, https://www.whitehouse.gov/briefings-statements/president-donald-j-trumps-administration-advancing-free-open-indo-pacific/, both accessed on 20 March 2019.

Belt and Road Initiative (BRI). The Asia-Africa Growth Corridor (AAGC)[6] proposed by Japan and India is also a mega-connectivity project aiming to link Asia and Africa through the Pacific and Indian Oceans. Indeed, AAGC actually aspires to realise a "free and open Indo-Pacific" through "growth and interconnectedness between and within Asia and Africa".[7] Given the respective geographies they encompass, South Asian countries are integral to both the BRI and the AAGC.

Infrastructure projects like the BRI and the AAGC, as well as those that could come up in the Indo-Pacific in the future through sub-regional or multi-country efforts, are certain to be multi-modal and exhaustive in scale and scope. Apart from comprising land corridors through cross-country road and rail links, the projects would be linking discrete geographies through sea and the cyberspace. These characteristics make the connectivity projects complex to comprehend. However, there's little doubt about their far-reaching impacts, which are not just economic but also geo-political. The scale and scope of the BRI and AAGC can hardly avoid geostrategic implications, notwithstanding their substantial economic spillovers through creation of new infrastructure assets and additional economic activities around the generation of these assets.

China's commanding role in funding BRI projects enables it to cultivate strategic influence in host nations through control over major resources and services (e.g., roads, ports, telecoms and cyber networks) that are critical from internal security and external geopolitical perspectives. The ripples created by the BRI in South Asia are therefore understandable given the concerns arising for India through Chinese funding of infrastructure in neighbouring Sri Lanka, Maldives and Pakistan. Such a geo-strategically sensitive and significant project like the BRI is quite likely to generate counter-responses from other major regional actors like India and Japan. The AAGC, notwithstanding its emphasis on sustainable development and physical infrastructure, can hardly be overlooked in its geopolitical significance. This might mark the beginning of a period of strategic rivalry across the Indo-Pacific around infrastructure connectivity. The stage for such a prolonged connectivity competition appears set with the US pronouncement of the FOIP, which is for all practical purposes a counter to the BRI.

[6] "Asia-Africa Growth Corridor: A Vision Document", African Development Bank Meeting, Ahmedabad, India, 22-26 May 2017, http://www.eria.org/Asia-Africa-Growth-Corridor-Document.pdf, accessed on 20 March 2019.

[7] Ibid., p. 14.

WIDENING ECONOMIC GAPS

Heterogeneity is perhaps the most noticeable economic aspect of the Indo-Pacific. From an economic perspective, the region represents a collection of heavily contrasting economic geographies, where some of the world's largest and most populous economies co-exist with some of the poorest. More specifically, the Indo-Pacific is a region with some of the world's most prosperous high-income economies (e.g., Australia, Japan, Korea, New Zealand and the US) co-existing with large and populous middle-income economies (e.g., China, India, Indonesia, Iran and Malaysia); and high-income small economies (e.g., Singapore, Mauritius, Maldives, Seychelles) residing with low-income economies (e.g., Cambodia, Kenya, Lao, Myanmar, Nepal). These structural economic heterogeneities reflect a region saddled with a variety of economies in different stages of economic development and countries with varying degrees of economic capabilities and quality of institutions. These variations are further evident from the differences among regions within the Indo-Pacific in terms of their integrations with the global economy and their current infrastructure capacities, particularly those influencing their abilities to trade.

East and Southeast Asia have much higher shares of intra-regional trade than South Asia, Middle East and Africa, underscoring the strength and capability of their institutions and practices in participating in trade through regional and global production networks. The difference in capacities is easily visible from the national logistics performance indices (LPI). Logistics include a host of institutional functions ranging from operational efficiencies of ports and speed of customs clearances to domestic transport linkages between ports on coasts and their hinterlands. Quality of logistics determines the abilities of economies to exploit infrastructure facilities effectively for entrenching participation of producers in global production networks. The more economically advanced and relatively higher-income economies in the Indo-Pacific, such as Japan, the US, Singapore, New Zealand, Australia, Korea, Taiwan and China, have better logistics capacities than the rest. While India ranks 47 in overall LPI, large South Asian economies like Bangladesh, Nepal and Pakistan rank beyond 100 with Bhutan and Afghanistan being among the lowest.[8] A similar difference in capacities is noticed in the space of digital communication with more high-income developed economies like Australia, Canada, New Zealand, Japan, Singapore and the US leading the rest of the Indo-Pacific in access of local popula-

[8] Logistics Performance Index (LPI) 2018, https://lpi.worldbank.org/, accessed on 20 March 2019.

tions to the internet and internet infrastructure, including speed of accessing data and broadband services. A vast number of countries from Africa, Middle East, South and Southeast Asia and the Pacific continue to suffer from low broadband speeds[9], impinging their abilities to take part in fast-paced cross-border digital transactions, particularly financial transactions.

The marked difference in infrastructure capacities and the overall ability to trade and engage in global commerce – as visible between several South Asian countries and many of the economically developed high-income economies of the region – is also noted between the latter and economies from several other sub-regions, such as Africa and Middle East, as well. This points to a situation where economies with more capacities and higher systemic and institutional efficiencies will be better placed to exploit new infrastructure – a situation that might just further widen current economic gaps within the region.

US PRONOUNCEMENTS AND INDO-PACIFIC

As mentioned earlier, various US pronouncements on the FOIP make it amply clear that connectivity and infrastructure-building in the Indo-Pacific is not just in American strategic and security interests, but also an effort to strengthen existing American alliances and create new partnerships for neutralising the Chinese influence in the region. Some key elements of the US pronouncements, such as the US interest in entering into bilateral free trade agreements (FTAs) with any Indo-Pacific country, the initial commitment of $113.5 million to digital connectivity,[10] cybersecurity and sustainable infrastructure in the region, and the introduction of the BUILD (Better Utilization of Investments Leading to Development) Act of 2018 for establishing the US International Development Finance Corporation (USDFC),[11] leave little doubt over connectivity, infrastructure, development finance, trade and investments getting embroiled in a critical game of strategic leverage across the Indian and Pacific Oceans.

For India, which is visualised as an important stakeholder in the Indo-Pacific by the US, as well as other South Asian countries located around and on the Indian Ocean – Bangladesh, Maldives and Sri Lanka – growth of FOIP as a primarily

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[9] https://www.cable.co.uk/broadband/speed/worldwide-speed-league/, accessed on 21 March 2019.

[10] As in 4 earlier.

[11] “The BUILD Act”, OPIC, https://www.opic.gov/build-act/overview, accessed on 21 March 2019.

security-oriented framework has serious implications. India would be hesitant to commit to a regional initiative that is limited in inclusivity and focused on economic development more for optics.[12] Notwithstanding its differences with China on various issues and its stated reservations on the BRI, India has insisted on the Indo-Pacific being "free, open and inclusive".[13] The insistence underscores its hesitation to be seen as a part of a regional order that is primarily a counter to China. Indeed, committing to such an order focusing on the geopolitical and security interests of the US might mean endorsing the precise legitimacy limitations that affect the BRI: the "strategic price" that countries might have to pay in terms of geopolitical commitment in exchange for development assistance and infrastructure funding. Countries like Bangladesh and Sri Lanka have already enthusiastically endorsed the BRI and are relying on Chinese funds for lasting infrastructure developments. For these South Asian countries, the FOIP poses a serious challenge of choice given that an enthusiastic approach to the former might be considered inimical by the Chinese. The FOIP might be able to avoid the problems of choice and legitimacy for many of the relatively smaller countries if it takes care to promote multi-country involvement, as opposed to a prominent US-centrality. The latter might invite for it the same legitimacy issues that an excessive China-centric focus has for the BRI.[14]

CONNECTIVITY AND TRADE WAR

The forceful US articulation of the Indo-Pacific comes at a time when the US-China trade hostilities are at an unprecedented high. The back and forth tariffs imposed by the US and China on a large number of items traded by each other began with the US decision to impose unilateral tariffs on steel and aluminium imports into the US in March 2018. The unilateral action was the first pointer to the emergence of a trend likely to influence global trade significantly in the days to come: viewing trade through the broad prism of national security. The US tariffs were imposed

[12] Palit, Amitendu and Sano, Shutaro, 2018, "The Free and Open Indo-Pacific Strategy and Concerns for India and Japan", Asia Pacific Bulletin, East West Center, No. 442, 10 October 2018, https://www.eastwestcenter.org/system/tdf/private/apb442_0.pdf?file=1&type=node&id=36846, accessed on 22 March 2019.

[13] "Indo-Pacific must be free, open and an inclusive region: Sushma Swaraj", The Economic Times, 19 July 2018, https://economictimes.indiatimes.com/news/defence/indo-pacific-must-be-free-open-and-and-inclusive-region-sushma-swaraj/articleshow/65060360.cms, accessed on 22 March 2019.

[14] Palit, Amitendu, 2018, "Indo-Pacific Connectivity: Lessons from China's Belt and Road", Griffith Asia Institute, 28 February 2018, https://blogs.griffith.edu.au/asiainsights/indo-pacific-connectivity-lessons-from-chinas-belt-and-road/, accessed on 22 March 2019.

under Section 232 of the US Trade Expansion Act of 1962 and were justified on the grounds of national security. More American tariffs on China came under Section 301 of the Trade Act of 1974 on the grounds of specific harm caused to US business interests in China by unfair domestic trade practices. It is notable though that investigations under Section 232 are continuing on automobiles and auto parts for examining whether these imports impinge on US national security.

The US and China are engaged in intensive discussions for settling their trade acrimony. But there is no doubt that even if there is a temporary truce, the US-China battle for economic supremacy and the resultant geostrategic influence is going to continue. The battle might result in trade getting increasingly fashioned by geopolitics. This might happen through other countries being forced to make choices between the US and China and getting impacted in their trade relations accordingly. The Indo-Pacific is particularly vulnerable in this regard.

Countries aligning with the US in Indo-Pacific connectivity projects, for example, might obtain more favourable conditions for market access through bilateral deals with the US given the current US proclivity to look at all trade relations exclusively and bilaterally. The same countries, on the other hand, might find themselves encountering greater difficulties in trading with China given their strategic alignment with the US. The reverse scenario is equally possible for countries aligning with China on the BRI.

While South Asian countries reflect on these possibilities, they are also aware that geopolitical fashioning of trade would also be conditioned by connectivity. New infrastructure corridors and cross-border linkages would command a strategic price, which might include a new orientation of trade based on geopolitical loyalty. This would mark a complete shift away from market-based comparative advantages in production that has traditionally fashioned trade, particularly since the establishment of the World Trade Organisation (WTO). Unilateral trade actions – as witnessed in the ongoing US-China hostilities – are leading to a steady erosion in the significance of the multilateral rules-based trade order run by the WTO. Such a consequence might alter the global trade order fundamentally, leading to a trade landscape where politics determines partners for trade, as it was before World War I.[15]

[15] Eichengreen, Barry, Mehl, Arnaud and Chitu, Livia, 2019, "Mars or Mercury redux: the geopolitics of bilateral trade agreements", European Central Bank, Working Paper Series, 2246, February, https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2246~1a43a0b375.en.pdf?144e06dd62f499eed4bf05559a304006, accessed on 22 March 2019.

CONCLUDING THOUGHTS

Trade and connectivity are being increasingly repositioned by the world's major powers in a manner that is suitable for their security and strategic interests. The tendency creates several challenges for South Asian countries as discussed in the paper in the context of the Indo-Pacific. As of now, there appears to be little that the region can do in terms of response, except for being alert and attentive to a pattern of regional development that is largely unprecedented. Improvements in internal and domestic institutional capacities, though, might always prepare the region for better responses to challenges economically.

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Currency Swap Arrangements and Its Role in Stabilising Financial Markets

Xu Mingqi

1. BASIC FUNCTION OF CENTRAL BANK CURRENCY SWAPS

Central bank currency swaps is not a new phenomenon. It first emerged under the Bretton Woods System on 28 February 1962 when the US Federal Reserve (FED) singed a currency swap agreement with the Central Bank of France, which came into effect on 1 March 1962. At that time, the US government faced great pressure to maintain the fixed exchange rate of the US dollar to gold and was obliged to convert at a fixed rate of 35 dollar per ounce with gold for the dollar to the other central banks. The swap agreement was in the form of mutual credit to each other's account. The Central Bank of France credited 500 million francs into the Federal Reserve account while the Federal Reserve credited USD 50 million into the Central Bank of France account. This enabled the Federal Reserve to use French francs to intervene in the market to maintain US dollar market stability. The Federal Reserve signed more swap agreements with other western countries' central banks subsequently, amounting to USD 0.9 billion in 1963, so as to acquire liquidity to intervene in the market. However, the stability was only short-lived and US dollar crises frequently broke out, which ultimately led to the US government ceasing the dollar convertibility with gold in August 1971.

Currency swaps once again attracted international attention in the wake of the turbulence caused by the global international financial crisis triggered by the US sub-prime mortgage crisis. In December 2007, the Federal Reserve signed currency swap agreements of USD 20 billion and USD 4 billion separately with the European Central Bank and the Switzerland National Bank; later, more swap agreements were signed and the amount was increased. By 29 October 2008, 14 central banks had signed currency swap agreements with the Federal Reserve individually and the total amount was up to USD 850 billion, which was four times the IMF's gross assets. After the international financial crisis broke out, many central banks needed the US dollar liquidity to intervene in the market and the Federal Reserve became the main supplier of USD liquidity to other countries. Paradoxically, currency swaps first emerged as a means to help the US FED to have liquidity to intervene in the market and to maintain the dollar exchange rate under the Bretton Woods System; while this time, after the global financial crisis erupted, the US FED became the only reliable source to provide additional liquidity. This was because after the US ceased its obligation to maintain the dollar's fixed rate and full convertibility to gold, the US FED became free to create US dollar liquidity at its own discretion. Currency swaps is no longer quite demanded by the US FED but rather by other central banks. Under the current international monetary system, only the other central banks need external sources to provide additional USD liquidity if they need to intervene in the market to prevent their own currency's sharp depreciation. They need the swap arrangement to have additional USD and this is why most central bank currency swaps were bilateral swaps between the US FED and other western countries' central banks during the global financial crisis.

The reason behind this is obvious. The US dollar is the key international currency and most central banks hold US dollar assets as their main reserve. Most commercial banks and non-bank financial institutions that are doing business internationally do the same. The US financial crisis hit the US financial market severely and the market price of all forms of US financial assets dropped dramatically. This created huge risk exposures not only for the US financial firms but also for international banks worldwide. If their assets' value cannot cover their debts, financial institutions' stock prices will drop. For the central banks, the reserve value's decrease may lead to currency depreciation. If a central bank wants to stabilise the market by intervention, it needs more US dollar liquidity or credit. Unlike the US FED, the other central banks could not create US dollars by themselves. In most cases, only the US Federal Reserve can act as the lender of last resort other than the IMF. That is why after the global financial crisis was triggered by the sub-prime mortgage crisis in the US in 2007-2008, it later hit others even more severely and many central banks needed additional US dollar liquidity much more badly. Hence, central bank swap agreements enabled the US FED to provide standby credit to other central banks in case they needed additional US dollar liquidity to stabilise the financial markets. However, central bank currency swaps also manifested the problem of the current international monetary system being heavily dependent on the US dollar.

On 31 October 2013, when the old type of swap agreements between the US FED and Bank of Canada, Bank of England, European Central Bank, Bank of Japan and Switzerland National Bank expired, the six central banks declared the renewal of their swap agreements with no term and quota limits. This created a new kind of swaps and the function of central bank currency swaps evolved to a new sphere. Some regarded this as the prototype of a new international monetary system (Li Yang, 2013).[1] To me, this is a move led by the US to consolidate the current US dollar-dominant international monetary system and to prevent other currencies from emerging to become more competitive relative to the US dollar. It is clear that while this new swap arrangement will enhance the stability of the US dollar-centred international financial market, it degraded the multilateral international safety net based on the IMF, limited the capability of developing countries to access the contingent liquidity as only six western central banks are included, and may create a new kind of moral hazard in relations to these developed countries' central banks pursuing monetary policy targets. There are reasons to believe that the US FED-led six central banks currency swap arrangements with no term and no quota limits has a negative impact on the reform of the international monetary system and the IMF itself. Scholars appealed for wider cooperation of global central banks by currency swaps other than US FED currency swaps (Shen, 2017).[2]

2. DEVELOPMENT OF REGIONAL CURRENCY SWAP AGREEMENTS

When developing countries build their regional economic cooperation framework, currency swaps also becomes one of the choices for bilateral or regional financial safety net building. The pioneer agreement was signed by the five ASEAN members, Indonesia, Malaysia, the Philippines, Singapore and Thailand, in 1977. After the eruption of the Southeast Asian financial crisis, this swap agreement was extended to all members of ASEAN as well as China, Japan and Korea. It developed into the so-called 10+3 "Chiang Mai Initiative (CMI)". However, most of the bilateral swap agreements under CMI are still based on the US dollar as the key currency and the swap-out currency is the US dollar. Only the agreements between China and Japan, Korea and the Philippines were in national currencies. This also showed the dominant position of the US dollar in East Asia. CMI was multilateralised and converted from a network of bilateral agreements between countries into one

[1] Li Yang, 2014. "Actively Respond to Six Central Bank Currency Swap Upgrading", http://bank.cnfol.com/pinglunfenxi/20140120/16800192.shtml, accessed 10 February 2019.

[2] Shen, Andrew, 2017. "World's Central Banks Need to Cooperate to Deal With Crises", Caixin, 25 July 2017, https://www.caixinglobal.com/2017-07-25/101121856.html, accessed 10 February 2019.

single agreement, the Chiang Mai Initiative Multilateralisation (CMIM), in 2010. A surveillance unit, the ASEAN+3 Macroeconomic Research Office (AMRO), was created. This Common Reserve Pool was expanded to USD 240 billion in 2012 from the original USD 120 billion.

After the global financial crisis, not only did the US FED-centred central bank swaps further developed, other bilateral and regional central bank currency swaps also arose. The US dollar's value experienced huge volatility, resulting in heavy stress to many central banks in their efforts to maintain the stable value of their foreign exchange reserve and the cost of holding USD reserve continually rising. In order to manage the reserve currency exchange rate risk, the trend of diversifying the reserve currencies appeared to gain new impetus. With the development of the multilateralisation of the international reserve currency, some major developing countries' currencies also became the assets willingly held by other countries' central banks. Against such a background, national currency swap agreements emerged. For example, on 25 June 2012, the Switzerland and Poland central banks signed a swap agreement of Swiss Franc and PLN; on 4 December 2012, India and Japan signed a national currency swap agreement of amount equivalent to USD 15 billion; this was renewed twice on 19 December 2013 and 29 October 2018 and the amount was expanded to USD 50 billion and again to USD 75 billion. Japan also signed bilateral swap agreements with Indonesia, the Philippines and Singapore and extended the amounts in 2013 when the US FED was thought to be tapering the monetary supply. Reserve Bank of Australia and Bank of Korea signed a local currency swap agreement of amount A$ 10/KRW 9 trillion in 2014 and renewed it in February 2017. Bank of Australia also signed a currency swap agreement with the Indonesian central bank of amount A $10 billion/IDR 100 trillion in December 2015 and this was renewed in August 2018. Korea and Indonesia signed a local currency swap agreement of amount KRW 10.7 trillion (9.2 billion US dollars) or 115 trillion rupiah in 2014 in addition to the CMIM and it was renewed in 2017. In Europe, most currency swaps are based on the Euro. For example, the ECB provides a swap line to Hungary; and the Swedish central bank provided the Euro standby credit to Latvia, Estonia, and Iceland with swap agreements.[3] According to di Mauro and

[3] Council on Foreign Relations. "The Spread of Central Bank Currency Swaps Since Financial Crisis", https://www.cfr.org/interactives/central-bank-currency-swaps-since-financial-crisis#!/central-bank-currency-swaps-since-financial-crisis, accessed 10 February 2019.

Zettelmeyer (2017), there are about 160 bilateral central bank currency swaps at present and they form an important part of the global financial safety net.[4]

China actively launched bilateral currency swap agreements against the background of RMB internationalisation. The first national currency swap agreement of China's central bank, People's Bank of China (PBOC), was signed with Korea in December 2008 and the amount was worth RMB 180 billion/WON 38 trillion. Since then, PBOC has signed bilateral currency swap agreements with 38 central banks respectively and the total amount has reached RMB 3.57 trillion. The latest one was signed with Bank of Japan, of amount RMB 200 billion, on 26 October 2018. Most of these swap agreements were for three-year terms and were renewed after maturity. A few of them were not renewed after maturing owing to some reasons. As at the end of 2018, there are still 31 swap agreements in effect and the existing total amount is RMB 3.2 trillion.

There are different views on the spread of central bank currency swaps. Mainstream economists in the US have a positive attitude toward central bank currency swaps and believe it would be better to build a global network of central bank swaps with three levels to form an international lender of last resort (Truman, 2013).[5] According to Ricardo Reis and Saleem Bahaj (2018), central bank swap agreements enhance the cooperation of central banks in providing liquidity, lower the cost of borrowing and promote cross-border capital flow.[6] However, some argue that central bank currency swaps could create moral hazards and insolvent countries should not normally have access to crisis lending unless they pass prequalification tests associated with access to the IMF's "flexible credit line" (FCL) and there is assurance that structural adjustments should follow.[7] Developing countries' economists believed that central bank currency swaps could be coordinated with the IMF function of lender of last resort and that the IMF can play the role of

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[4] di Mauro, Weder Beatrice and Zettelmeyer, Jeromin. "The New Global Financial Safety Net: Struggling for Coherent Governance in a Multipolar System", 30 January 2017. CIGI Essays in International Finance, Volume 4, January 2017. Available at SSRN: https://ssrn.com/abstract=2946452, accessed 10 February 2019.

[5] Truman, Edwin M., 2013. "Enhancing the Global Safety Network Through Central Bank Cooperation", *Vox,* 13 September 2013.

[6] Reis, Ricardo and Saleem Bahaj, 2018. "This is the role of central bank swap lines in the global Economy", World Economic Forum, 28 September 2018, https://www.weforum.org/agenda/2018/09/central-bank-swap-lines/, accessed 14 February 2019.

[7] See di Mauro and Zettelmeyer, above-mentioned paper in note 4.

a clearing house of swaps network (Yeyati and Cordella, 2010).[8] I think that bilateral and regional central bank swap lines are only the second-best choice and that the best approach is to enhance the IMF role of lender of last resort and to have a global governance rule and principles in place. However, it will be quite difficult to enhance the IMF role of lender of last resort and to increase the IMF quota as the US is not supportive of these two proposals. Regional and bilateral central bank swaps become the second-best choice instead of enhancing a global comprehensive safety net based on the IMF.

3. RMB INTERNATIONALISATION AND THE PURPOSE OF PBOC CURRENCY SWAP AGREEMENTS

Many believe that PBOC actively participates in bilateral national currency swaps so as to promote RMB internationalisation. I do not question this view and believe that China is in favour of the trend of international currency multilateralisation and RMB internationalisation is a part of this trend. For this reason, some swap agreements that PBOC signed, especially those with developing countries that lack US dollar reserves, stated that the swap agreement was to promote bilateral trade and investment. It was regarded as helping to promote RMB denomination in trade and investment across the two countries. Empirical studies by some scholars also showed that high trade and investment interdependence between China and specific partner countries tend to correlate with the presence of currency swap agreements with PBOC (Liao and McDowell, 2015).[9] This is beyond the traditional purpose of short-term liquidity provision for market stabilisation. However, most PBOC currency swap agreements still emphasised market stability as the priority purpose. Hence, RMB internationalisation is not the only driving force of PBOC currency swaps. To help to create an additional safety net for financial stability is a higher priority than promoting RBM internationalisation. RMB internationalisation itself is not simply to enable it to become an international reserve currency, as many believe, but rather to reduce the exchange rate risk for Chinese companies doing international business. Managing the financial market risk is a more urgent

8 Yeyati, Eduardo Levy and Tito Cordella, 2010. "Global safety nets: The IMF as a swap clearing house", Vox CEPR Policy Portal, 18 April 2010, https://voxeu.org/article/global-safety-nets-imf-swap-clearing-house, accessed 14 February 2019.

9 Liao, Steven and Daniel McDowell, 2015. "Redback Rising: China's Bilateral Swap Agreements and Renminbi Internationalization", *International Studies Quarterly*, Volume 59, Issue 3, 1 September 2015, pp. 401-422.

need for China and most other developing countries. Currency swap agreements are thought to be effective means for this purpose.

Although most of these bilateral swap quotas have not been drawn and executed, their symbolic value and function in stabilising financial markets are still important. Swap agreements could be regarded as the additional reserves of central banks and may discourage market speculation in cases of distress. On special occasions or under special conditions, increasing the swap amount could enhance the central bank's credibility so as to calm down market turbulence. For instance, in August 2018, when Argentina experienced financial market distress, the Argentine central bank asked PBOC to increase the existing bilateral swap quota from RMB 70 billion to RMB 130 billion. The agreement was reached on 2 December 2018 and helped Argentina to calm down market expectations.

As mentioned above, in some PBOC currency swaps with other central banks, there are clauses to allow the credit line to be used for trade and investment purpose. On 27 January 2013, Bank of Korea executed a currency swap agreement with PBOC and drew RMB 620 million to make a loan to Korea Exchange Bank. The latter then provided RMB loans to Korea companies for trade settlement. On 30 May 2014, People's Bank of China obtained KRW 400 million from the Bank of Korea and then loaned it to Bank of Communications to support the cross-border settlement between Korean Won and RMB in Seoul. Another case was when the Belarus central bank executed RMB 1 billion under swap agreement to provide RMB credit to their commercial banks and Belarus commercial banks then using the fund to support Belarus companies to import Chinese products. This sort of using of the central bank swaps is beyond the crisis-lending purpose that central bank currency swaps were supposed to fulfil. If swaps line becomes an export credit, it could lead to some problems, not only in disturbing PBOC's monetary policy operation but also in creating a new kind of moral hazard in using the credit line. Once the currency swap becomes loans for trade and investment purpose, the time period of loans and the risk assessment will be quite different from that of short-term liquidity provision for market intervention and crisis-relief purpose. The interest rate charged on currency swaps is usually the central banks' policy rate and lower than the commercial lending rate. This creates an incentive to use the currency swap line. If all the swaps are converted to this kind of usage, the potential risks need to be seriously considered. Until now, PBOC currency swaps have mainly focused on the financial safety net purpose and have not been largely deployed to promote trade and investment denominated by RMB. Even in promoting the Belt and Road (B&R) initiative, trade and investment project finances are mainly provided by China Development Bank and the Export and Import Bank of China. They are specialised in these kinds of finance and the relevant risk assessment. So, in practice, this kind of risk is controllable and only needs to be reviewed with case-by-case studies.

Some developing countries' economists tend to emphasise PBOC currency swap agreements together with China's intention of RMB internationalisation and have exaggerated the RMB competition with the US dollar hegemony. They quite often mention the creation of the Asian Infrastructure Investment Bank (AIIB) and RMB offshore market development and put them together with the PBOC currency swaps to sum up the trend that the RMB is going to be a competitor to the US dollar (Shen, 2014; Awan, 2018).[10] I think these comments show their wish to reform the current international monetary system and the role that RMB currency swaps could play in such a reform. But I believe that PBOC currency swaps and the promotion of RMB internationalisation are not aimed at competing with the role of the US dollar. PBOC currency swaps is only playing a supplementary role to the six western countries' central banks currency swaps that are not extended to developing countries. China benefits from the stability of the international monetary system and hopes to make a contribution to regional and global financial market stability. China's initiative to create the AIIB and to actively support the BRICS New Development Bank are aimed at providing additional development finance besides those of the World Bank and the Asian Development Bank but not at undermining existing institutions and systems. China believes that there are positive roles for emerging market economies to play in global economic governance, especially in the realm of international finance. If possible, China will enhance the bilateral swap line and also participate in the six developed countries' currency swap network.

4. HOW TO ENHANCE THE ROLE OF STABILISING FINANCIAL MARKETS BY CENTRAL BANKS CURRENCY SWAPS?

The quick development of bilateral central bank currency swaps provided a supplementary safety net parallel to the multilateral framework based on the IMF, but also created potential problems. The coordination between the IMF and bilateral swap lines is mentioned frequently by many scholars. In theory, bilateral swaps should be more flexible in usage prior to IMF financial help. In reality, when there is a need for crisis-relief finance, the IMF still plays a more important role. In a few

[10] Shen, Andrew, 2014. "Central Bank Currency Swaps Key to International Monetary System", *East Asian Forum,* 1 April 2014. Awan, Zamir Ahmed, 2018. "Currency swap good for Developing Countries", Center for China and Globalization, http://www.sohu.com/a/277918997_828358, accessed 14 February 2019.

cases, currency swaps provided timely liquidity help, enough to relieve market stress. Hence, some scholars suggested that the IMF and G20 should play a coordination role and provide global level governance on central bank currency swaps (Rhee et al., 2013; Destais, 2014).[11] How to enhance the role of the IMF and G20 in this regard? I think it would be difficult to make the IMF the clearing house of bilateral central bank currency swaps as some have proposed. The US FED-led six central banks swaps and other central banks' swaps all have their special purposes and the IMF is not capable of providing the function of a wider range of clearing and settlement. What is possible is to take a first step to entrust the IMF to get all central bank swaps' information and to make the IMF a watcher and supervisor of all central bank currency swaps. Similar to the obligation on WTO members to report their Free Trade Arrangements (FTAs), all members of the IMF should report their central bank currency swaps to the IMF. At present, most bilateral and regional swap agreements are not transparent and the terms and conditions for the swap agreements are not quite clear to others. Obligations under a swap agreement are not subject to any international organisation's supervision and governance. So the IMF and G20 could establish some basic guidelines to enhance the transparency and based on this, the IMF could consider providing coordinating finance when a swap is activated under financial distress conditions. With this kind of coordination, crisis-relief financing will be more effective.

Central bank swaps is going to become like the FTAs of recent years. It has spread widely as a means for bilateral or regional economic cooperation. In some cases, swap agreements also serve as instruments for geopolitical or geo-economic purposes. Like FTAs, swap agreements overlapping is inevitable. Central bank swaps are multifold in some regions. For example, the CMIM is a comprehensive swap agreement of ASEAN+3 countries while many ASEAN members also signed bilateral swap agreements with China, Korea and Japan respectively. Theoretically, the more swap agreements one country has, the more financial safety it can potentially gain. However, as many bilateral swaps are conditional, overlapping swap agreements are not necessarily of the same quality and ease to execute. In order to enhance the role of central bank swap agreements, I think swaps can be divided into two categories. One is related to promoting trade and investment and the other for crisis relief. The first one could be used more flexibly and could be embodied in FTA agreements. The second one is strictly to be used for financial market stability

[11] Rhee, Changhyong, Lea Sumulong, Shahin Vallee, 2013. "Global and Regional Safety Network: Lessons from Europe and Asia", *Bruegel Working Paper* 2013/06，November 2013; Destais, Christopher, 2014. "Central Bank Currency Swap and International Monetary System", *CEPII Policy Brief*, No. 2014-15, September 2014.

and should be coordinated with the IMF for collaborative fund arrangements. The main international currencies countries' central banks should consider extending their swap network to more emerging market central banks and to create a safety net with a wider range.

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Assessing the Benefits and Costs of Mega Infrastructure Initiatives in Asia

Ganeshan Wignaraja

INTRODUCTION

Much of the academic and policy debate on Asia's infrastructure development has focused on China's Belt and Road Initiative (BRI), which aims to improve regional connectivity and cooperation on a trans-continental scale (see Jinping, 2017; Hillman, 2018; Prasad, 2018). But several large-scale BRI infrastructure projects have come under greater scrutiny recently, as Asian economies reassess their benefits (Saara, 2019). Yet the BRI is only one of many competing initiatives started by major economies that are seeking to exploit new infrastructure investment opportunities in Asia (Shepard, 2017). The impact of these initiatives on Asian economies is not well understood, due to, among various reasons, their recent origin, the lack of available data and gaps in national infrastructure capacity.

This article attempts to assess the benefits and costs of mega infrastructure initiatives in Asia. It examines four related issues: (1) the role of infrastructure investment in Asia's development and the infrastructure investment gap, (2) the spread of mega infrastructure initiatives across Asia, (3) emerging risks to Asia from such initiatives, and (4) national strategies to mitigate risks.

WHY INFRASTRUCTURE INVESTMENT MATTERS

One of the key lessons from Asia's economic miracle story is that investing in national infrastructure (transportation, power, water, and telecommunications systems) facilitates trade, people movement and growth. Famous examples of trade-related infrastructure projects are available from newly industrialising economies (NIEs) in East Asia. South Korea invested US$10 billion to build the Busan Port, which today handles about three-quarters of the country's container traffic. Singapore invested around US$6 billion to construct Changi Airport, which has become one of Southeast Asia's busiest transport hubs, annually moving over 60 million people and over 2 million tonnes of air freight. These investments have helped both economies to experience rapid structural transformation and growth over several decades. Per capita incomes have risen rapidly and enabled Korea and Singapore to become high-income economies.

More recently, Asia has invested in regional infrastructure which has traditionally linked neighbouring countries for trade-led development. This has roots in the economic literature on geography and trade pioneered by Krugman (1991) and others. It highlights the notion that distance matters for trade and that trade costs between neighbours can be reduced by building roads, railways, power transmission lines and other means for regional connectivity. The Kunming-Singapore railway, often labelled the Pan-Asian Railway Network, which links China, Singapore and other Southeast Asian countries, is an important example. This builds upon a fragmented railway network that originated in British and French colonial times. Another is the Central Asia Road Links Programme of the World Bank, which aims to improve road connectivity between Tajikistan, Kyrgyz Republic and Uzbekistan.

There is little doubt that such cross-border projects have contributed to Asia's rapid economic development, by stimulating flows of goods, services, investment, and people across the borders of neighbouring countries. By improving connectivity, they have also fostered regional peace and cooperation among the region's small and large countries alike. Safeguards and public policies have been pursued to reduce negative effects from such projects, including displaced people, environmental degradation, and crime.

Recent research has examined the plethora of infrastructure challenges globally and in Asia. The enormous infrastructure investment gap – the different between investment needs and current investment levels – has been identified as one of the most pressing issues (Peel and Mitchell, 2017). McKinsey Global Institute (2016) found that the world invests US$2.5 trillion a year in infrastructure while US$3.3 trillion is required annually from 2016 until 2030 to support projected growth. A particularly glaring infrastructure investment gap exists in Asia. The Asian Development Bank (ADB) (2017) found that Asia annually invests US$881 billion a year in infrastructure while US$1.7 trillion a year is needed until 2030 to maintain regional growth and respond to climate change. The region's infrastructure investment gap is thus US$819 billion per year until 2030.

THE SPREAD OF MEGA INFRASTRUCTURE INITIATIVES

Asia's large investment gap has also led to several competing mega infrastructure initiatives led by major economies in Asia (China, Japan, ASEAN, Korea and India) and elsewhere (the EU and the US). Being much more ambitious and complex than arguably simpler two-country infrastructure projects, these large initiatives will likely have significant implications for Asian economies and businesses within them. The motives for mega infrastructure initiatives range from narrowly promoting the commercial interests of state-owned enterprises (SOEs) and multinational enterprises of major economies to providing broader philanthropic support to develop poorer Asian countries. Other motives include export of surplus capital and manpower, defence-related interests, strategic competition between major powers, and global domination of critical Asian sea-lanes and land corridors.

Table 1 provides an overview of five mega infrastructure initiatives criss-crossing Asia on which some data was available from different sources. Some observations should be noted.

First, these are all relatively recent. The first movers in 2013 were China's ambitious Belt and Road Initiative (BRI) and the much smaller ASEAN Infrastructure Fund (AIF). These were followed in 2015 by Japan's significant Partnership for Quality Infrastructure (PQI) and in 2016 its Enhanced Partnership for Quality Infrastructure (EPQI). In 2017 the US-led Free and Open Indo-Pacific Strategy (FOIP) was launched and in 2018 the EU Strategy for Connecting Europe and Asia.

Second, these five mega infrastructure initiatives collectively make only a modest contribution to financing Asia's enormous infrastructure needs. A conservative estimate (assuming a BRI lower bound estimate of US$340 billion) of the combined value of the five initiatives in Table 1 gives a figure of about US$754 billion over a 5-7 years time horizon. This works out to between US$108 to US$151 billion annually. Assuming that the financing in mega infrastructure initiatives is additional money and only spent in Asia, the region's infrastructure investment gap only reduces to between US$668 to US$711 billion annually until 2030.[1] Financing Asia's unmet infrastructure needs thus remains a significant development challenge for regional economies.

[1] The annual value of the five mega infrastructure initiatives (US$108 billion to US$151 billion) was added to the annual regional infrastructure spending figure of US$881 billion from ADB (2017) and subtracted from the estimated regional needs of US$1.7 trillion.

Table 1: An Overview of Selected Mega Infrastructure Initiatives in Asia.

Launch Date and Major Economy	Name	Size (US$)	Focus Sectors and Key Actors
2013 September, China	Belt and Road (BRI) Initiative	$340 billion – $1 trillion (1)	Port, transport and energy infrastructure across Asia, Africa and Europe. China's state-owned enterprises (SOEs), China Development Bank (CDB), Export-Import Bank of China (EIBC), a Silk Road Fund, and the Asian Infrastructure Investment Bank (AIIB).
2013 December, ASEAN	ASEAN Infrastructure Fund (AIF)	$4 billion 2013-2020 (2)	Projects listed under the ASEAN Master Plan for Connectivity (like power and water) exclusively for Southeast Asian economies. Multinational corporations (MNCs) from ASEAN and elsewhere and co-financing by the AIF, ASEAN economies, the ADB and the World Bank.
2015 May, Japan 2016 May, Japan	Partnership for Quality Infrastructure (PQI) Enhanced Partnership for Quality Infrastructure (EPQI)	$110 billion 2016-2020 $200 billion 2017-2021 (2)	Port, transport and energy infrastructure projects across the world. Japan's MNCs, Asian Development Bank, Japan International Corporation Agency (JICA) and Japan Bank for International Corporation (JIBC).
2017 November, US	Free and Open Indo-Pacific (FOIP) Strategy	$70 billion (1)	Energy infrastructure (LNG plants), digital connectivity and cybersecurity, safe storage/transport of nuclear materials across Indo-Pacific region. US MNCs, International Development Finance Corporation (IDFC), Millennium Challenge Corporation (MCC) and the World Bank.
2018 October, EU	EU Strategy on Connecting Europe and Asia	$140 billion (Euro 123 billion) 2021-2027 (3)	Transport, energy and digital infrastructure to link Europe with Asia. European MNCs, European Union, European Investment Bank (EIB), and the European Bank for Reconstruction and Development (EBRD).

Notes: (1) Estimate. (2) Official Pledge. (3) Proposed.

Sources: Hillman (2018); Izumi (2017); http://europa.eu/rapid/press-release_MEMO-18-5804_en.htm; https://www.state.gov/secretary/remarks/2018/07/284722.htm; http://icr.unwto.org/fr/content/asean-infrastructure-fund-aif-asian-development-bank.

Third, China and Japan's mega infrastructure initiatives are more ambitious geographically and in size than those of the US and EU. In fact, China's initiative is larger in terms of US$ than those of the US and EU combined while Japan's is about the same size. Meanwhile, ASEAN's initiative is much smaller than that of either the US or EU.

Fourth, financial commitments and scope, although not yet determined, are likely to be relatively small for three other mega infrastructure initiatives that are known to exist – Russia's Trans-Eurasian Belt Development of 2015; the Asia-Africa Growth Corridor of 2017 led by India and Japan; and South Korea's Northern and Southern Policy of 2017 (Shephard, 2017).

As Asia's mega infrastructure initiatives are still in the initial phase of development, detailed information about them and the project pipelines within them are generally lacking. For instance, neither China's BRI nor Japan's PQI post online a complete list of projects and the terms granted to recipient economies in Asia. Likewise, official information is absent about plans for Korea's Northern and Southern Policy or Russia's Trans-Eurasian Belt Development. That said, some initiatives seem better designed than others; with deep project management, high-quality engineering solutions, strong buy-in from recipients, sizable financial commitments and support from multilateral development banks (MDBs) with high standards. As good management, engineering, and donor practices spread, laggard initiatives may well emulate their predecessors; a coherent and transparent architecture of mega-regional infrastructure initiatives might one day emerge in Asia.

EMERGING RISKS

Aside from an information deficit, multiple and overlapping mega infrastructure initiatives in Asia also risk creating a "noodle bowl" phenomenon. The "noodle bowl" effect, which is more typically associated with free trade agreements (FTAs) in Asia, refers to a situation in which a growing number of overlapping arrangements generate increasingly complex rules and standards which give rise to significant transaction costs for economies and business (Kawai and Wignaraja, 2011). A similar analogy can be applied to the more recent spread of mega infrastructure initiatives (Wignaraja, 2015). These initiatives share the goal of financing infrastructure in Asia and largely focus on similar sectors. However, they differ significantly in their vision, scale and terms of financing, implementation strategies, procurement approaches and the actors involved.

The risk of an entangled "noodle bowl" of mega infrastructure initiatives in Asia may be exacerbated by three factors.

First, scarce finance may be packaged in a complex way that could make the "noodle bowl" effect more pronounced. As mentioned above, Asia has a large infrastructure investment gap. Recipients and donors want to stretch these limited funds in clusters of projects and individual projects through innovative financial means; such as procurement rules favouring single sourcing by SOEs and MNCs from the donor economy, co-financing mega projects with MDBs, state guarantees to incentivise private investors, fully-fledged public private partnerships (PPPs), and re-packing of various financing instruments. Governments often need to finance increased spending for mega infrastructure projects in cash-strapped national budgets through international bond issues. Indeed, a bewildering array of partnerships, instruments and financial terms will likely make managing the financing of infrastructure projects more difficult to fathom by recipients and to coordinate among the various actors. The more complex the project and the larger the number of bidders, the more difficulties for recipients.

The potential "noodle bowl" problem is illustrated by a high-speed rail (HSR) project in Indonesia, Southeast Asia's largest economy. Indonesia wished to build a 150km HSR link from Jakarta to the country's fourth largest city, Bandung, and attracted the interest of Chinese and Japanese consortiums during tendering (see Prasad, 2018). This was a new technology to the country, which lacked the capability. The Japanese side undertook careful feasibility studies over five years and thought the deal was clinched in 2015. However, a Chinese bid undercut Japan's offer and altered the project specifications. Unlike the Japanese offer, the Chinese one did not need a full sovereign guarantee from Indonesia. A bidding race followed with each consortium offering more financing and reducing the implementation timeline. Construction began in 2016 after the Chinese side won the contest but stalled due to mounting project costs and financing problems. It is expected to be completed in 2021 at a escalating cost from the initial figure of about US$6 billion. The next rail project – to upgrade the railway line between Jakarta and Surabaya – was awarded to Japan, which signalled that Indonesia wanted to maintain a competitive environment for rail tenders. However, it meant that Indonesia now had two vastly different HSR rail systems, which could strain its limited technical and operating capacity. If future HSR projects are awarded to consortiums from other major economies, the "noodle bowl" problem could be exacerbated for Indonesia.

Second, intense selling by some bidders from major economies under mega infrastructure initiatives can lead to "white elephant" projects which poses economic risks to participating economies. Lucrative project contracts coupled with a lack of transparency in tendering procedures provide incentives for rent-seeking activity in recipients. A recipient's infrastructure landscape could become littered with large infrastructure projects which are over-budget, loss-making and low-return generating. The consequences are debt sustainability, governance, and transparency issues in participating countries. Asian economies, with weaker financial capacity and governance standards, may be more susceptible than richer countries to these risks, and may find that their implementation capacity is overstretched.

The problem of white elephant projects is illustrated by the Sinamale bridge project[2] in the Maldives, a strategically located group of dispersed atolls in the Indian Ocean. The Maldives wanted to build its first inter-island sea bridge, 2.1km long, between the airport and the wider metropolitan island of Hulumale and the capital city, Male (Saara, 2019). An Indian and a Chinese company bid for the project, which the latter won. The bridge opened in 2018. The original project cost of US$210 million – which allegedly over-ran to US$300 million – was financed by a part grant and part commercial loan from China under the BRI initiative during the administration of former President Yameen Abdul Gayoom. Cost-recovery was limited due to nominal toll fees for vehicles. The project is also clouded by allegations of corruption and debt trap diplomacy (Macan-Markar, 2019). The incoming administration of President Ibrahim Mohamed Solih alleges that the Maldives paid for a four-lane vehicular bridge but only got two lanes. An investigation is planned into BRI projects in the Maldives.

Third, mega infrastructure initiatives will likely create winners and losers. Winners arise when initiatives (i) reinforce comparative advantage reflected in trade and foreign direct investment (FDI) patterns in Asia, to avoid the risk of "building ports and airports to nowhere"; (ii) are backed by open regionalism initiatives and domestic structural reforms; (iii) incorporate adequate safeguards (e.g., for the environment and resettlement) in formulating projects; and (iv) coordinate among themselves in key areas such as planning, project formulation, procurement practices, financing, and implementation.

Losers from initiatives are hard to predict, as the devil is in the detail for specific projects. Landlocked countries like Nepal, or island states like the Maldives or Fiji, that are somewhat excluded from mega infrastructure initiatives may be marginalised. The same might apply to distant provinces within large Asian economies like Indonesia or Bangladesh. Some transport routes – either land or maritime transport, for instance – and some workers, such as port workers, may also fail to benefit from efficiency-seeking PPPs.

Ironically, the quest to maximise the benefits of mega infrastructure measures could contribute to the "noodle bowl". Asian economies should collectively adopt offsetting measures in order to avoid this outcome and mitigate the negative effects of such initiatives. Creating Asian variants of the EU's regional development funds would address regional development imbalance; these funds are best established under the framework of sub-regional cooperation bodies like ASEAN, Bay of

[2] Also referred to as the China-Maldives Friendship Bridge.

Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) or Indian Ocean Rim Association(IORA).

NATIONAL STRATEGY

As more mega infrastructure initiatives are established, the likelihood of Asian "noodle bowl" risks increases as well as the transactions costs for economies and business. Several actions are needed to mitigate these risks and costs in Asian economies.

First, Asian economies need to do their homework to efficiently utilise the package of finance and expertise from mega infrastructure initiatives to raise national economic development. This means the following measures:

- developing a medium-term national infrastructure master plan which carefully assesses needs, priorities and projects;
- ensuring that the projects in the national budget originate from the master plan;
- investing infrastructure management and financing capacity in ministries of finance particularly for international procurement practices for infrastructure projects and the capability to evaluate the financial costs and benefits of alternative bids;
- formulating enforceable anti-corruption laws with credible penalties to deter offenders; and
- implementing prudent macroeconomic policies which emphasise careful debt management, build-up of foreign exchange reserves and efficient tax revenue administration.

Second, in view of the long gestation period of infrastructure projects and the potential risk of white elephant projects under mega infrastructure initiatives, holding a national dialogue on infrastructure development can help to reduce economic risks. The draft national infrastructure master plan should be the basis for such a dialogue, which should be attended by all political parties, ministries of finance and central bank officials, academics, businesses, civil society and the media. Successful Asian economies have managed the difficult exercise of forging a national consensus on infrastructure development in a transparent manner.

Third, embedding the financing requirements for infrastructure projects in economic reform programmes – either home-grown or under the preview of the IMF and the World Bank – is a necessary task for implementing a stable and predictable macroeconomic policy.

Fourth, major economies behind mega infrastructure initiatives should be more transparent about releasing project-level data (including agreements with governments, financial terms and feasibility studies), provide training for national counterparts and adhere to strict anti-corruption standards.

CONCLUSION

Major economies in Asia and elsewhere deserve praise for attempting to solve Asia's large infrastructure investment problem with mega infrastructure initiatives and various project pipelines. However, the proliferation of such initiatives may give rise to an Asian "noodle bowl", which could raise transactions costs for regional economies. It is important for Asian economies to develop coherent national strategies to reap the benefits while minimising the costs of mega infrastructure initiatives. Major economies should be supportive of these efforts through data, training and anti-corruption measures. Clearly, more thought and time are needed to ensure that these mega infrastructure initiatives support Asia's transition to successful middle-income and high-income status in the future.

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