ASEAN trade in focus

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In 1992, the Association of Southeast Asian Nations (ASEAN) embarked on an ambitious endeavor to establish the ASEAN Free Trade Area (AFTA) in pursuit of functional and dynamic economic integration. The idea was to meld the disparate economies and political peculiarities of ASEAN member countries into a single, regional economic unit, akin to the European Communities (EC). This environment will allow goods and services to freely move about and encourage member countries to efficiently exploit gains from specialization. However, over a decade hence, much potential still remains untapped with several business issues still up for practical resolution. The upcoming 12th ASEAN Summit in Cebu would give businesses the chance to monitor the most recent developments on this and make their concerns known.

One major aim of AFTA is to transform ASEAN into a single market, investment destination, and production base where international businesses can set-up regional operations. The AFTA framework was envisioned as a catalyst that would instill harmony, stability, and transparency affording global companies a conducive environment to invest not only in a single country, but across the entire region. Through the reduction of trade barriers, companies are given the opportunity to more strategically and efficiently plot out their regional cross-border supply chains, drawing from the comparative advantages of each country.

As a first step towards regional economic integration, ASEAN agreed to implement a substantial tariff reduction scheme called the Common Effective Preferential Tariff (CEPT). Developments on this front have been dramatic, with 98% of all products traded within ASEAN now enjoying CEPT rates in the range of 0-5%. In first decade of its implementation, the average CEPT rate for the first 6 members of ASEAN (Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand) dropped from 12.76% to a low of 1.61%. For the Philippines, the average CEPT rate has already been reduced to 3.77% as of 2003.

Tangible effects of the AFTA in the Philippines can already be perceived. It is no longer uncommon to find consumer and industrial products from soaps and detergents, to cars and heavy equipment bearing the distinct markings of our ASEAN neighbors. You may have come across a car component labeled in Thai and Bahasa Malaysia, or a shampoo bottle with ingredients translated in Bahasa Indonesia all produced by a single company under a single brand. It is fascinating to note that the parts and ingredients of these products were obtained from different countries within the region. These were processed in varying degrees (accumulating value-added) in different ASEAN countries, before finally being retailed off to the end user. Interestingly, apart from the tangible products, the design and idea behind these products and their components were most probably conceptualized in one ASEAN country and implemented in another.

Economists of different orientations have long been at loggerheads in responding to the debate on whether the economic and policy adjustments to accommodate AFTA (or any FTA for that matter) has or would indeed be beneficial. Questions have been raised on whether such would lead not only to positive marks in our economic indicators, but also in net welfare gains for the common Filipino. Debates continue in search of a clear and convincing answer to this, but it is undeniable that efficiency gains from specialization and economies of scale are increasingly being exploited through the AFTA. Companies no longer have to establish duplicate facilities in different ASEAN countries to produce the same product. They can instead capitalize on the comparative advantage and resource endowments of each country by setting up specialized production facilities in different strategic locations. Efficiency gains in specialized production can generate broader economic activity in the host countries leading to wider employment and higher levels of income. Consumers, on the other hand, benefit from the lower prices brought about by reduced tariff and other transaction costs. Other unquantifiable benefits, such as closer diplomatic relations and the positive recognition of the region as a solid economic unit and viable investment area, lend a very helpful hand in promoting the Philippines to international businesses.

After all is said and done in touting the benefits of economic integration, however, it remains fair and valid to comment that, frankly, ASEAN has not been up to the mark as far as the promotion of trade and investments (a cornerstone of economic integration) is concerned. Positive manifestations as to the efficacy of the region in luring international business to agglomerate and establish regional operations may be tangibly observed. However, the benefits that have so far been reaped are still but a far cry from the true economic potential that ASEAN and its resources have to offer.

A prominent indication of ASEAN's apparent lack of success in economic integration is its wanting performance in promoting intra-

ASEAN trade. As present figures stand, trade amongst ASEAN member countries account for a little over 20% of total ASEAN trade. In so far as investments go, intra-ASEAN investments barely exceed 10% of total investments in ASEAN in cumulative terms since the past 5 years. Note that these results came out notwithstanding a substantial reduction in intra-ASEAN tariffs. There is no dearth of explanation for this less than satisfactory outcome but some of the more common will be discussed below. Notably, business has one of the largest roles to play in addressing each of these.

Given the fact that not much headway has been made in the expansion of international trade and investments in spite of substantial tariff reductions in the region leads one to be deduce that the root of the problem lay more on non-tariff barriers. ASEAN economic officials have come to recognize this issue and have opened more functional debates on how the region should iron out the finer details of economic integration beyond the initial step of tariff reduction. The new issue areas now being deliberated include among others: trade facilitation, rules of origin, and a complementation between trade and investment policies.

Trade facilitation, which deals with the speedy clearance of goods from Customs jurisdiction, is becoming a growing concern among businesses in ASEAN. A number of importing companies in the region apparently have developed an impression that the costs they save from the reduced tariff rates are merely offset by the administrative costs of managing through tedious customs bureaucracies. To assuage this, an initiative called the ASEAN Single Window has already been set in motion, for which pilot tests were conducted in the Philippines. This program is intended to introduce common documents and to set-up a common information sharing network among Customs administrations in ASEAN that will allow the easy transmission of official trade information (importers, trade profiles, statistics, pricing, tariff classifications, certificates of origin etc.) to reduce time costs whilst managing the risks of technical smuggling.

The Rules of Origin is the system by which a product is deemed as originating from an ASEAN country and thus granted preferential tariff treatment. On a general note, the main method of determining this is based on a minimum percentage (40%) of the product’s freight-on-board (FOB) value. However, strict criteria apply as to which particular cost components can be treated as counting within that minimum percentage. A number of certain cost items which are incurred in ASEAN are still omitted in the calculations which preclude some goods from being allowed preferential access to ASEAN markets. These rules, however, are constantly being reviewed to ensure that they are neither too lenient enough to be vulnerable to transshipment leaks nor too strict so as to mitigate intra-ASEAN preferential trade altogether.

It was discussed in an ASEAN Report that trade and investment polices in ASEAN have to be harmonized for the region to fully optimize the benefits of the CEPT. Notably, trade policies have already significantly lowered tariffs within ASEAN. Investment policies, on the other hand, are already granting comprehensive incentives to prospective investors. Then again, trade and investments within and among ASEAN members have remained relatively low. Observers pin down the reason for this to a seeming disconnect in the way trade and investment policies are conceived and formulated. Trade policy, they say, seems to have limited itself to liberalization, while investment incentives in ASEAN seem bent on attracting similar and competing (rather than complementary) operations in the region. Commentators aver that trade policies, apart from just focusing on the reduction of tariffs, will also have to serve as a vehicle for the promotion of complementary investment activities. Investment policies in ASEAN, on the other hand, should be envisioned within the framework of objectives for which AFTA was created, which is to promote cooperation over competition among ASEAN members. Investments in Research and Development (R&D), where ASEAN is known to be lacking, is strongly recommended.

The 12th ASEAN Summit will be held in Cebu in January to be attended by political and economic leaders in each of the 10 ASEAN member countries. This will provide policymakers and business in the region (and especially in the Philippines) the opportunity to deliberate on how the aforementioned concerns should be addressed to set ASEAN in the proper course.