

Impacts and Implications of ASEAN Enlargement on Trade*

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Introduction

The Bangkok Declaration of 1995 stated that “ASEAN shall work toward the speedy realization of an ASEAN comprising all Southeast Asian countries as it enters the 21st Century.” The enlargement of ASEAN to cover the entire Southeast Asian region is a priority and the ultimate objective of ASEAN regional cooperation. Subsequently, in July 1997, ASEAN accepted Lao PDR and Myanmar as full members of ASEAN.¹ Due to internal political conflict, Cambodia was only granted observer status in 1997, although it is expected that Cambodia will be integrated in the near future. The new members joined the Common Effective Preferential Tariff (CEPT) scheme with a different timeframe; Vietnam started reducing tariff rates in January 1996, and will reach the target in 2006, while Lao PDR and Myanmar will complete tariff reductions by 2008, eight years after the old members.

ASEAN is not a homogeneous group; there are considerable differences among members with regard to size, historical background, and level of industrialization and development (Ariff 1995). Inclusion of the new members increases the differences. These countries are in the process of institutional adjustment toward market-orientation and standard capitalist business practices. Their experiences in the international economic forum are still limited. Although enlargement of ASEAN will create trade and economic activities, new members might have difficulty adjusting and might delay the onset of free flowing resources within ASEAN.

To enhance ASEAN cooperation, it is important to evaluate the positive impacts of incorporating the new members and identify the obstacles to future cooperation. The paper will explore the economic structure of trade patterns, and comparative advantages of ASEAN members toward understanding how trade will affect the ASEAN enlargement and the potential for future progress on cooperation.

In this paper, the term “ASEAN-6” includes the old members: Brunei, Indonesia, the Philippines, Malaysia, Thailand, and Singapore. “ASEAN-5” is the same group, excluding Brunei. The term “new members” refers to Vietnam, Lao PDR, Myanmar, and Cambodia. Cambodia attained observer status and is expected to be a member soon. The term “ASEAN-10” is loosely used to include the present members and Cambodia.

COMPARISON OF ECONOMIC DEVELOPMENT: ENLARGEMENT INCREASES DISPARITY

The economies of the new ASEAN members are much smaller in comparison with the older members, although Vietnam and Myanmar have larger GDPs than Brunei, which is the smallest economy in the ASEAN-6. In 1994, Vietnam’s GDP, the largest of the new members, was \$15,570 million, while the GDP of the Philippines, the smallest of ASEAN-5, was \$64,162 million ([Table 1](#)). Lao PDR’s GDP was only \$1,534 million in 1994. The coefficient of variation of GDP rises from 0.70 for the ASEAN-6 to 1.11 in the case of the ASEAN-10.

Table 1 also shows the difference in per capita income. Lao PDR’s per capita GDP was \$320 in 1994, which was only one-fourth of per capita GDP of Indonesia and one-seventh of Singapore’s. The ASEAN-6 have some disparities in income per capita; the coefficient of variation of GDP per capita of the ASEAN-6 members is 1.19. The variation is significantly reduced if Singapore is excluded. However, for the ASEAN-10 the coefficient of variation rises to 1.67.

The GDP growth rates of the ASEAN members were quite high compared to other developing countries. The average growth rate of GDP of Malaysia was 8.4 percent per annum over 1990-94. The growth rates were 8.3 percent, 8.2 percent, and 7.6 percent for Singapore, Thailand and Indonesia respectively during the same period. Only Brunei and the Philippines had disappointing growth rates of less than 2 percent per annum. The growth rates of the new members were satisfactory although they were not as high as those of some older members. GDP growth was 8 percent per annum for Vietnam, 6.2 percent per annum for Lao PDR and 5.7 percent per annum for Myanmar.

While the economies of these new members are small, their populations are not negligible. Myanmar and Vietnam have about the same population as Thailand and the Philippines. The population of the ASEAN-10 is 38 percent larger compared to the ASEAN-6, amounting to 481.6 million persons.

Considering the structure of production, agriculture dominates in the new member countries. The share of agriculture in GDP was as high as 63 percent for Myanmar, 47 percent for Cambodia, and 51 percent in the case of Lao PDR. Agriculture accounts for only 28 percent of GDP in Vietnam, a level still higher than in the old member countries. The shares of agriculture in Singapore and Brunei are negligible. The Philippines' agriculture sector constitutes 22 percent of GDP, the highest in the ASEAN-6, followed by Indonesia at 17 percent.

As mentioned earlier, the ASEAN-6 are not homogenous in the structure of their economies. Incorporating the new members widens the differences in social and economic characteristics further.

ASEAN TRADE PATTERNS

Importance of Intra-ASEAN Trade

Trade statistics in [Table 2](#) show that intra-ASEAN trade is greatest among the ASEAN-6 rather than with new members, although trade with the new members rose from 1990 to 1995. Trade among the ASEAN-6 represented 93 percent of exports and 97.7 percent of imports in 1995. The corresponding shares were 98.3 and 97.5 respectively in 1990. The new members depend on trade with the older members rather than within their group. The ASEAN-6 are important to the new members for their markets and as suppliers. Thailand's share of exports and imports to the new members are high, though not much higher than those of Indonesia and Singapore.

However, intra-ASEAN trade is not yet large. Intra-ASEAN exports as a percentage of total exports were 23.6 percent in 1995. The share was as low as 6 percent in the case of Indonesia and as high as 30 percent in the case of Singapore in the same year. The dependence on imports from within ASEAN has been low with the exception of Brunei. This means that the ASEAN-6 depend on imports of machinery and materials for production from industrial countries outside ASEAN, although intra-ASEAN imports have been rising.

The new members depend more on the ASEAN market, compared to the old members. The share of exports to ASEAN was 64 percent in the case of Cambodia, and 54 percent, 25.7 percent, and 13.8 percent for Lao PDR, Myanmar and Vietnam respectively. Cambodia and Lao PDR have stronger trade relations with ASEAN than Myanmar and Vietnam. The share of ASEAN imports were higher than exports at 75.4 percent, 70.3 percent, 46.7 percent and 27.4 percent in the case of Cambodia, Lao PDR, Myanmar and Vietnam respectively.

Trading Partners of the New Members

Within ASEAN in 1995, Singapore was the biggest market for Myanmar, followed by Malaysia and Thailand. Myanmar exports to the USA and Japan were greater than to Malaysia and Thailand. With respect to imports, Singapore and Malaysia were two major suppliers to Myanmar with an import value of \$701 million from Singapore and \$225 from Malaysia, which was greater than imports from Japan and even much larger than from Thailand.

In the case of Vietnam, Singapore and Malaysia were the principal ASEAN markets, though less important than Japan. However, with regard to imports, Singapore was the major supplier for Vietnam, while Japan was second.

The picture is quite different for trading patterns of Cambodia and Lao PDR. These two countries relied more on ASEAN markets, especially Thailand, which was the major market for Cambodia and second to Vietnam for Lao PDR. Thailand was the major supplier of imports for Lao PDR but second to Singapore in Cambodia. However, the trade statistics do not include informal cross border trade which is significant between Thailand and the new members and among the new members themselves.

COMPARATIVE ADVANTAGE ANALYSIS

To examine comparative advantage of ASEAN members, revealed comparative advantage (RCA) indexes were calculated, at the two-digit standard international trade classification (SITC) level. RCA refers to the share of an export product in total exports of a country divided by the product's share in total world exports. A value of greater than one indicates that a country has revealed comparative advantage in that particular product, and vice versa. An increasing RCA value indicates that the country is gaining advantage in that product relative to the world market.

[Table 3](#) presents RCA indexes of ASEAN members for export products with an RCA value of greater than one for 1994 or 1995, depending on data availability.

Brunei exports are very concentrated, with a strong advantage in natural gas and petroleum products, and to a lesser extent, photographic apparatuses and miscellaneous manufacturing products. In 1995, products that showed comparative advantage for Cambodia were crude rubber, cork and wood, textiles and garments, crude animal and vegetable materials, and fish. Comparative advantage declined in coffee, hide skin, and minerals.

Lao PDR was competitive in cork and wood products, and in recent years, garments. She also showed export advantage in other natural resources such as coffee, animal hides and crude animal and vegetable materials.

Myanmar's and Vietnam's competitiveness were more diversified than those of Cambodia and Lao PDR. Myanmar exports for which the RCA was greater than one in 1995 were cork and wood, vegetable and fruit, fish, oil seeds, sugar, crude rubber, cereals, feeding stuff for animals, animal hides, oil seed, minerals and garments. In the same year, products that showed comparative advantage for Vietnam were resource-based products like coffee, fish, cereals, oil seeds, crude rubber, minerals, crude animal and vegetable materials, coal and petroleum products; and labor-intensive products such as garments, travel goods, furniture, and footwear.

From the RCA analysis, it is apparent that new members had comparative advantage in resource-based industries and some labor-intensive industries, especially garments. For the old members, the advantage was in manufactured products. Singapore had the advantage in high-technology products such as computers, telecommunications equipment, electrical machinery, and photographic equipment. Malaysia showed competitiveness in manufacturing products like computers, electrical machinery, furniture, telecommunications equipment, and in some resource-based products like crude rubber, wood, vegetable fat and petroleum.

Thailand, the Philippines and Indonesia had similar patterns of export competitiveness. They were competitive in agricultural, resource-based and labor-intensive products. In addition, Indonesia was competitive in petroleum products.

Thus, the ASEAN countries do not exert one clear pattern of comparative advantage. The implications of these variations in comparative advantage on the enlargement of the ASEAN free trade area are explored below.

IMPACTS AND IMPLICATIONS OF ASEAN ENLARGEMENT

This section discusses the potential impact of the new members on ASEAN. The implications of expansion of ASEAN and the ASEAN Free Trade Area (AFTA) can be viewed in two directions. On one hand, it will increase economic activity within ASEAN. On the other hand, it may undermine the implementation of AFTA. Both issues will be investigated below.

Trade Creation

Increasing market size and resource endowment diversification

ASEAN enlargement will raise the population from 355.2 million, for the ASEAN-6, to 468.9 million for the ASEAN-10. This increased market size will increase intra-ASEAN trade. Average income in each new member country is still low but GDP growth rates are satisfactory, therefore the prospect of trade creation taking advantage of market size is quite good.

Another factor that will stimulate intra-ASEAN trade is resource diversification. The structure of the economies of the ASEAN-6 is quite similar and the scope of exchange is limited. The new members are different from the ASEAN-6 in regard to factor endowments and patterns of production. These new members are rich in natural resources, with low-wage labor forces, while the old members have higher-skilled labor and more capital. Classical trade theory suggests that trade between two countries stems from the differences in comparative advantage, which are determined by factor endowments. For example, countries with abundant natural resources will export resource-intensive products and countries that are relatively capital abundant will export capital-intensive goods. Economic integration has stronger trade creation effects when resource endowments are more diversified among members because the pattern of production is complementary among them. In the previous section, the analysis shows that new members have comparative advantages in agriculture and raw materials; while old members have comparative advantages in manufactured goods. Therefore, integration widens the scope of exchange and increases intra-ASEAN trade.

While the expansion will raise the volume of intra-ASEAN trade, the volume of new member trade is small. Therefore, intra-ASEAN trade will not rise significantly. The trade data in 1995 (Table 2) show that the new members have stronger trade linkages with ASEAN than the old ones, however, the share of intra-ASEAN exports in total exports rose from 23.6 percent for the ASEAN-6 to only 25 percent in the case of the ASEAN-10, and the corresponding share of intra-ASEAN trade (exports and imports) increases from 20 percent to 21 percent. One can see that, even with the enlargement, trade with non-member countries is still important for ASEAN.

Tariff reductions

AFTA, which entails the elimination of tariff and non-tariff barriers, was launched in 1993, and the main mechanism of AFTA is the CEPT scheme. At the beginning of the AFTA agreement, the timetable for tariff reduction was 15 years; it was shortened to 10 years in the Fifth Meeting of the AFTA Council in 1994. The meeting also admitted unprocessed agricultural products into the CEPT scheme. Under the present scheme, fast-track tariff reductions will be completed by the year 2000 and normal-track tariff reductions will be finished in 2003. AFTA allows sensitive items to be excluded from these two tracks. Products in the Temporary Exclusion List have been transferred to the Inclusion List in five equal installments annually since 1 January 1996 so they have more time to adjust to tariff reduction. There is also a permanent exclusion list for sensitive products (ASEAN Secretariat 1995).

According to the agreement, the old members will reduce tariff rates to 0-5 percent by 2003. New members have a different timetable. Vietnam will lower tariff rates to 0-5 percent by year 2006 and Lao PDR and Myanmar by 2008.

Vietnam placed 857 tariff lines on the inclusion list, the smallest number compared to the ASEAN-6. The temporary exclusion list includes 1,189 tariff lines, the second largest next to Indonesia. The products in the temporary exclusion list will be phased in beginning 1 January 1999. Vietnam included products with tariff rates less than 5 percent on the inclusion list and most of the products in Myanmar's and Lao PDR's inclusion lists have tariff rates under 5 percent. Therefore, tariff reduction with respect to the inclusion list will not be a problem for the new members. However, a large number of products are on the exclusion lists (2,818 tariff lines for Lao PDR and 2,722 tariff lines in the case of Myanmar) and some products have very high tariff rates, so the next step will be more difficult.

Regional tariff reductions will increase trade among members based on comparative advantages. However, to get the most from tariff reduction, ASEAN member should commit to their schedule and speedup the timeframe for reduction. In addition, since new members' major exports are unprocessed agricultural products, crude materials and labor-intensive goods, the ASEAN-6 should lower tariffs on major exports from new members which are still high. For example, products with tariff rates greater than 20 percent are live animals, food, furniture, footwear, vegetable and fruit (Vu Tuan Anh and Bui Tat Thang 1997). For agricultural products, 20 percent of tariff lines are on the temporary exclusion list and 12 percent are on the sensitive list for which the timetable for tariff reduction can be longer than 2003 and the rates may be greater than 5 percent. Furthermore, some major agriculture products are on the sensitive list (ASEAN Secretariat 1995). Therefore, the scope of tariff reduction for agricultural products should be expanded to provide market access for new members.

Enhancing Investment and Tourism

While the enlargement increases market size with respect to population and diversification of resources which create trade, the principal objective of AFTA is not intra-regional trade, rather, the objective is to make ASEAN an attractive investment area. The new members present new opportunities for investment and tourism with a larger market, diversification of natural resources, labor abundance, low cost of living, and numerous tourist attractions. Investment in these countries will induce trade through imports of materials and machinery and exports finished products. Infrastructure development, which requires large investments, and is needed in the new member countries, also creates demand for imports of raw materials. For example, investment in construction in Lao PDR increases exports of cement and petroleum from Thailand. Tourism creates trade in services and demand for local souvenirs that can be developed into exports.

Stimulating the Process of Liberalization and Internationalization of New Members

All new members have restructured their economies from socialism to capitalism. AFTA forces the new members to adjust trade practices to international standards. AFTA makes tariffs uniform in term of rates and classifications. Non-tariff barriers have to be reduced and conformed to international regulations. The AFTA agreement also includes cooperation on a customs area which includes activities such as the formulation of a uniform ASEAN tariff list, building a green corridor for commodities participating in CEPT, and coordination of customs forms and procedures.

Joining ASEAN is a first step toward participating in other international forums. Vietnam and Lao PDR have stated clearly that they want to join Asia-Pacific Economic Cooperation (APEC) and the World Trade Organization (WTO) (AFTA Monitor, July 1997). ASEAN cooperation assists these countries in making institutional adjustments for other international forums. The enlargement also helps ASEAN in trade negotiations as ASEAN always tries to negotiate as a group since representing a larger number of countries and a larger population strengthens the position of any individual ASEAN country.

The reduction of tariffs will encourage competition from imports. New members will have to make adjustments in production according to comparative advantage with less protection. The external forces of freer trade will make the economy more efficient and make exports more competitive, reinforcing the need to deregulate domestic production.

Possible Issues Undermining AFTA Progress

The benefits of ASEAN enlargement were discussed above. It is possible that the inclusion of the new members will slow progress under AFTA. The possibility is discussed below.

Concerns over tariff revenues and the current account deficit

New member countries are concerned that tariff reductions will decrease tariff revenue. The countries in Indochina still rely on tariff revenue. In Lao PDR, the percentage of tariff revenue in total government revenue was 20.1 percent in 1995. The corresponding shares were 28.3 percent in Vietnam and 54.1 percent in Cambodia (Suzuki 1997). Due to this concern, policymakers may delay tariff reductions, which will undermine regional trade creation. The current account deficits in these countries make some people worry that tariff reduction will stimulate imports and worsen the trade deficit. Recently, Vietnam increased tariff rates on cars, motorcycles and consumer goods to slow down imports and improve the trade deficit.

The concern can be countered if one realizes that tariff reduction can increase government revenue. The government can collect more tax from increasing economic activities including increased tariff revenue stemming from an increased volume of imports, and from other forms of tax, such as increased amounts of sales and consumption tax, or income tax. A study by Vietnam's Ministry of Finance indicates that if import values remain the same, the CEPT agreement will lower import-export tariff revenue by 9.4 percent in 2006 from 1995 levels. However, if imports grow at the current level of 20 percent per annum, the tariff revenue in 2006 will increase despite the reduction.

Transaction costs of joining ASEAN

Since these former-socialist countries are less developed and have lower incomes, joining ASEAN is burdensome. ASEAN members contribute \$1 million to a contribution fund and \$0.6 million for annual membership fees. In addition, there are traveling expenses, correspondence expenses and other operating costs for meetings, which were held more than 270 times in 1995. Training in English, international law, and economics are required to prepare personnel to participate in meetings and other activities. The transaction costs will obstruct participation of new members and make it harder to reach consensus among ASEAN countries, so assistance is needed to alleviate the costs for these countries.

Resistance from domestic producers

Trade liberalizations always resisted by domestic producers who want protection. Even in old member countries, producers lobby the government to put industries on the exclusion list and delay tariff reduction. The problem in new members is more serious because domestic producers include public enterprises. Public enterprises are still important with respect to production in these countries. The share of public enterprise production in GDP was 40.2 percent, 22.2 percent, and 15 percent in Vietnam, Lao PDR, and Myanmar respectively. Public enterprises are usually managed by people close to the government so they can influence government decisions. The process of liberalization depends on the political will to overcome the resistance from people who benefit from protection.

More difficult to liberalize trade in services and investment

ASEAN's Vision 2020 advocates regional cooperation via creation of the ASEAN Investment Area (AIA) by 2010 and the integrated ASEAN Economic Region by 2020, with zero tariffs and free flows of capital and services. To achieve the goal of Vision 2020, the liberalization of investment and trade in services is necessary. ASEAN set up the Coordinating Committee on Services to negotiate trade in services. The negotiation employed the WTO's General

Agreement on Trade in Services (GATS) framework. Members will present a Schedule of Commitments listing sectors and activities for which market access and national treatment will be provided to other members according to mode of supply. Any limitations will be indicated in the Schedule of Commitments. The ASEAN framework will be “GATS-plus,” i.e., the scope and coverage of the commitments must be an improvement over GATS commitments. The members, excluding Lao PDR and Myanmar, are currently negotiating their schedules of commitment. The scope is still limited because under GATS, there are many constraints on market access and national treatment and the coverage includes only tourism, telecommunications, finance, maritime transport, air transport, construction and professional services, with an emphasis on the first three sectors.

The negotiations on trade in services and investment are more difficult than trade issues. The CEPT scheme on tariff reductions are well established and under implementation, while the frameworks on trade in services and investment are in the beginning stages, not only in ASEAN but under other international forums. Furthermore, trade in services usually requires the establishment of a foreign business and the movement of natural persons, so it requires adjustments with regard to law, accounting systems, government regulations, tax systems, visa procedures, among others, to standard under which foreign firms can operate. Institutions under socialist systems are very different from market-oriented systems, so it takes time for countries to adjust to international practices. After a decade of reforming, Vietnam has just recently promulgated commercial law and bankruptcy law. Attitudes toward foreign investors are also important. There is still some thought that foreign investment hurts the economy since it exploits natural resources and cheap labor and undermines the development of national industries. Public enterprises usually do not want any competition either from foreigners or locals, so they always discourage foreign investment and advocate protectionism. All of these factors make it hard to establish a free flow of investment and people.

CONCLUSION

With ASEAN enlargement, new members will complement old ones in trade and investment and enhance intra-ASEAN trade. However, the volume of trade of new members is still small. Thus the share of intra-ASEAN trade in total trade will not increase significantly. This means economic activities with non-members are still important for ASEAN.

Joining ASEAN will serve as a stepping stone for Indochina participation in other regional and multilateral forums. It is easier to adjust trade and investment policies to close neighboring countries with a common history of social, political and economic relations. Including new members also strengthens ASEAN in multilateral negotiations and as an attractive investment area.

Since extra-ASEAN trade is important, unilateral liberalization is a key strategy for economic development. AFTA must be viewed as an instrument to increase ASEAN member competitiveness in international markets and induce foreign investment. Therefore, most-favored-nation (m.f.n.) tariff reductions will benefit members more than preferential tariff reductions in ASEAN. To achieve the goals of ASEAN’s Vision 2020, CEPT is not adequate. Further liberalization in trade in services and investment is critical, and ASEAN lags behind other regional groupings in these two areas. Enlargement may cause some difficulties in negotiations due to different levels of development and different institutions.

Delay in market deregulation and institutional adjustment in the new member countries will undermine the process of ASEAN cooperation. Therefore it is crucial for the new members to commit to AFTA and economic liberalization. For these countries, privatization and deregulation are the key strategies for success. The old members must help them pursue economic restructuring and help by assisting with the adjustment costs.

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