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EU – ASEAN FTA: regional cooperation for global competitiveness

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Abstract. *The recent interest shown by the European Union towards the countries in South-east Asia, as well as the initiatives for setting up free trade areas in the region, come to confirm the uneasiness that portrays the situation at home, as well as the efforts that it set out to make in order to maintain its competitiveness on a global scale. Particularly, the attention that the EU has given to bi-regional cooperation, initiating talks for a free trade area with ASEAN, rather than with its member countries, strengthens the belief that the EU is currently seeking to consolidate its position in South-east Asia and to counter the increasing influence of China and Japan.*

Key words*: European Union, regional cooperation, competitiveness, free trade area*

JEL classification: *F13, F15*

Introduction

For the first time in decades, the EU is facing a strategic challenge in its external policies, both in trade relations and on the strategic level. The rises of Russia and China as international actors – with India close behind – and the increasing difficulties upsetting the national economies are creating a serious threat to the EU's ambition to become the most competitive economy in the world, capable of making its voice heard on the international arena.

This situation demanded a far-reaching rethink of the approach the Union takes to its external relations. If the EU is to remain a serious global actor, it will have to find ways to reconcile the imperative of internal economic revival with the need to establish new "bridgeheads" in the "hot" regions of Latin America and South-East Asia.

An test of the Union's ability to meet the challenges of the shifting international order is taking the form of the EU's relationship with the countries in Southeast Asia, a region which has recently emerged as an important focus for the EU for various reasons and with which it opened a series of negotiations for establishing several agreements, either bilateral, or multilateral.

These new and ambitious agreements proposed by the EU, focused mainly on investment and services, come in the context of the disappointment caused by the recent evolution of the Doha round of negotiations. The European Union has openly declared the objective of these agreements, in its strategy *Global Europe – Competing with the World*, defining them as "new competitiveness-driven FTAs [...] aiming at the highest possible degree of trade liberalization including far-reaching liberalization of services and investment".[1] However, this task in not easily achievable, considering the differences between the EU and its partners, not only in terms of economic development, but also politically, socially and culturally. Thus, although negotiations are under way, their outcome, if any, is still to be identified.

[1] European Commission, October 2006

In this context, the question is not WHETHER a free trade area between the EU and the ASEAN (The Association of Southeast Asian Nations), one of the most important actors in the region and a significant trade partner to EU, but WHEN this will take place.

EU – ASEAN current relations

The European Union's (EU) policy towards Southeast Asia is largely premised on strengthening its economic presence and securing market access and investment opportunities for its corporations in an expanding Asian market. Securing economic dominance in Asia is perceived as central to maintaining the EU's leading role in the global market place.

In its 1994 '**Towards a New Asia Strategy'** policy, the EU argued for a greater Asian priority and presence. The EU suggested that "the Union needs as a matter of urgency to strengthen its economic presence in Asia in order to maintain its leading role in the world economy. The establishment of a strong, coordinated presence in the different regions of Asia will allow Europe at the beginning of the 21st century to ensure that its interests are taken fully into account there"[2]. However, its approach was based on developing bilateral relations with the Asian countries like Japan, China, Korea and India.

Only in the past few years, with the launching of the ASEM process in 1996, has the EU sought to deal with Asia as a region. There is increasing recognition of the fact that EU and Asia have to deepen their region-to-region dialogue, not least to balance the respective dialogues between the EU and the US and Asia and the US.

The EU TREATI scheme is an example of this trend, which comes to complement ASEAN's own integration plans. This initiative is aimed at increasing the degree of harmonization between ASEAN member states and at bringing a progressive liberalization of regional trade, which is to culminate in the formation of an ASEAN Economic Community by 2015.

Also, the EU offers financial support for ASEAN's regional integration. There is a certain level of self-interest here: the EU favors trade agreements with regional blocs, as this allows EU corporate industry access to larger, integrated markets at a single stroke.

Common interests of EU and ASEAN

The EU shares many common features and interests with South East Asia. Both are seeking to deepen regional cooperation and integration between highly diverse Member States through the EU and ASEAN respectively. Countries from both regions cherish the respect for their cultural, religious and linguistic identity. Both regions are committed to a multi-polar world based on strong multilateral international institutions.

1. On the *political* side, the triangle formed by the US, EU and Asia is increasingly important in world affairs. Strengthening the EU-Asia side of that triangle would also strengthen the prospects for global governance based on multilateral institutions to which both Asia and the EU are strongly committed.

[2] Towards a New Asia Strategy Commission of the European Communities COM(94) 314 final, Brussels, 13.07.94

At the same time the EU and Asia must recognize the shortcomings of the multilateral system and seek to promote "effective multilateralism." This means more serious reflection on how to strengthen the UN, the WTO institutions; and also how to tackle the new security threats caused by "failed states."[3] This requires a frank debate on when to use force to resolve international problems. Southeast Asian nations and Europe also share the same security concerns with regard to terrorism, drugs and illegal immigration. The EU's "soft power" and its ability to promote peace and security through development aid, economic assistance and non-military security cooperation is increasingly welcome among the ASEAN members.

2. For ASEAN, a key priority remains how it should deal with the *development* gap between its richer and poorer members following the enlargement with Vietnam, Cambodia, Laos and Burma/Myanmar in the nineties. Average per capita income in South East Asia is 1,217 euro: ranging from 215 euro in Cambodia to 3,900 euro in Malaysia and 23,500 euro in Singapore. The enormous disparity between the poorest and the richest ASEAN members places a direct restraint on economic and social integration. In this context, financial aid from the European Union is more than welcome while taking on the European model of integration is an opportunity not to be missed. So far, the EU is the only economic organization in the world to have social solidarity and economic convergence as priority objective

3. The two regions also enjoy very strong *commercial* links. On trade, relations with the EU have increased ten fold since the early 1990s. The EU is now ASEAN's third largest trading partner, accounting for 12.5% of ASEAN trade. Significantly, the EU is ASEAN's second largest export market after the US. Also on investment, ASEAN remains a preferred destination for EU companies, in spite of the slight decrease in favor of China.

Table 1. ASEAN major trading partners (left) and export destinations (right)

	Partners	Mio euro	%
	World	968 484	100.0
1	USA	125 062	12.9
2	Japan	121 395	12.5
3	EU	117 004	12.1
4	China	96 803	10.0
5	Singapore	82 741	8.5
6	Malaysia	67 636	7.0
7	Korea	42 145	4.4
8	Hong Kong	42 040	4.3
9	Indonesia	39 621	4.1
10	Thailand	37 188	3.8

	Partners	Mio euro	%
	World	519 332	100.0
1	USA	78 367	15.1
2	EU	69 478	13.4
3	Japan	58 372	11.2
4	China	48 773	9.4
5	Singapore	35 968	6.9
6	Malaysia	34 331	6.6
7	Hong Kong	32 181	6.2
8	Indonesia	24 123	4.6
9	Korea	20 611	4.0
10	Thailand	18 516	3.6

Source: DG trade, 2006

ASEAN countries are again displaying impressive growth figures and are set to become one of the most dynamic growth engines for the world economy. With its growing export-led economies and a fast developing domestic market of 530 million

[3] Failed state is a term intended to mean a weak state in which the central government has little practical control over much of its territory. The US think-tank, the *Fund for Peace*, publishes an annual index called the 'Failed States Index'. (Noam Chomsky, *Failed States*, 2006)

people, ASEAN is a region of global economic importance that the EU cannot afford to neglect, especially at a moment when the trade balance is in favor of ASEAN. Surely, the establishment of a free trade area would significantly benefit the Europeans, as seen in *Figure 1*. Due to the quality requirements, property rights and other regulations on which the EU has the upper hand, there are enough reasons to believe that once the FTA is established, the trade balance will change.

Figure 1. EU-25 merchandise trade with the ASEAN

Source: Eurostat, 2006

Also, the prospect of using the euro more in financial markets and for trade has enormous potential. However, there should be noted that there are marked regional variations within this overall booming relationship, between the more and less developed countries in Southeast Asia. For example, if referring to investments, the EU FDI flows Singapore attracts more FDI than all the other ASEAN countries taken together and was the 4th largest destination for EU direct investment in 2003, after Russia and ahead of China.

4. Cooperation on *environment*, especially on the Kyoto protocol, has been good but there are many other problem areas to be tackled together, such as sustainable natural resource management (e.g. forestry), the management of urban development, and energy security. European experience and technology is advanced in this area and could be of interest to Asian partners.

5. Migration is an increasingly sensitive issue and Asia is the source of potentially significant migratory flows to Europe. The EU and Asian countries have started a dialogue on this common challenge in the context of ASEM and are beginning to develop common approaches.

Features of an EU-ASEAN FTA

From the perspective of the European Union, the two regions should establish a "deeper" FTA, constituting a reduction of tariffs and elimination of non-tariff barriers and technical barriers to trade. If possible, the EU will expand the FTA to include investment. Also, it should involve harmonization of trade rules and regulations and WTO-plus principles, regulatory market access restrictions and intellectual property. The ASEAN governments do not want government procurement on the negotiation table, contrary to the EU's demands. The EUs "deeper" FTA roadmap is already in place in the context of

the Trans-Regional EU-ASEAN Trade Initiative (TREATI), which is a precursor to the establishment of a free trade agreement (FTA).

ASEAN nations are expected to make such fundamental changes to their economy in exchange for European market access. Furthermore, these changes are perceived as fundamental requirements to entice investments and limited FDI flow to the region. Also, it is argued that these changes are an absolute requirement to ensure foreign investors that their investments are indeed safe, certain and predictable. Basic concerns include Standards and Quality Control; Intellectual Property Rights and the negotiation of Mutual Recognition Agreements on standards, testing and certification.

Concretely, the scope of the ASEAN-EU FTA should *inter-alia* include the following:

• The progressive and reciprocal liberalization of trade in goods and services, which goes beyond the level of existing commitments in the WTO within an agreed time frame;

• The liberalization and facilitation of investment and creation of an open and nondiscriminatory environment;

• The elimination of barriers to trade and the creation of clear, stable and transparent rules for exporters, importers and investors. This includes provisions which aim at the facilitation of trade and as well as provisions on standards, technical regulations, conformity assessment procedures, and sanitary and phytosanitary measures;

• Setting up a pragmatic approach for addressing government procurement by enhancing transparency, as well as possible improvements in market access opportunities on a pluri-lateral basis;

• The adequate and effective protection and enforcement of intellectual property rights;

• The establishment of an effective mechanism for co-operation in the field of competition.

Opportunities for EU and ASEAN

Internationally, ASEAN continues to compete with MERCOSUR on the agricultural market. Should an EU-MERCOSUR FTA be established, the ASEAN would be the only large agricultural region in the world facing EU tariffs in this sector. Thus, ASEAN would lose in the absence of an EU-ASEAN FTA. The same is true for the EU: if ASEAN concludes an FTA with all other industrialized countries, the EU would be the only industrialized region facing tariffs on the ASEAN market. Therefore, an FTA between the ASEAN and the EU would not only mean more liberalized trade, but also *less discrimination* between significant trade partners.

The importance of concluding an FTA is magnified by the fact that the EU and other industrialized countries compete to provide the same kind of goods and services, and within the same quality range. Thailand and the Philippines are large agricultural exporters. Hence for them, an agreement with the EU becomes crucial if the EU were to conclude an agreement with Mercosur.

Moreover, the Japanese government has recently floated the idea of an East Asia Free Trade Agreement. This involves ASEAN member countries including Japan, Korea and China, New Zealand, Australia and India. The Agreement will be the biggest FTA in

the world involving as much as two billion people, providing a reason more for the EU to hurry the negotiations with the ASEAN.

Various studies[4] commissioned to evaluate the impact of an EU-ASEAN FTA suggested that in 2020 the gains accruing to ASEAN members will be about 2 % of GDP. However, the gains for individual member countries would be different with modest gains for the Less Development Countries, namely Cambodia, Vietnam, Laos and Burma. Gains accruing to the EU will be positive. The bulk of the gains to ASEAN will come from the liberalization in services. An ambitious ASEAN-FTA would lead to a sizeable welfare gains including an increase in production and employment.

Also, several opinions state that an ASEAN-EU FTA serves ASEAN and EU strategically. The EU could consolidate its commercial presence of EU transnational corporations in a dynamic and expanding ASEAN. Also, the EU would be able to ensure a more stable and predictable environment for the protection of intellectual property rights and other regulatory requirements. ASEAN's strategic advantage would be to secure market access and commercial presence in Europe. An FTA with the EU could increase FDI attractiveness for ASEAN, a prerequisite to compete with China.

EU-ASEAN FTA-related risks

What is obvious in the ASEAN-EU FTA schema is that the ASEAN that needs to reform its economy if it wants to do business with Europe. European investments would find ASEAN attractive *only* if ASEAN meets European expectations. In fact, the roadmap towards an FTA dictates that ASEAN governments, not withstanding the different stages of growth, commit themselves to embracing a development strategy that is going to place them and their companies in direct competition with powerful European TNCs.

Of course, the EU admits the existing asymmetries and declares itself ready to negotiate. However, it requires the ASEAN states to reach a common ground level from which negotiations will start. This kind of FTA certainly favors European TNCs with in-built advantages and are global market leaders in a variety of sectors by protecting their advantage.

The need to adapt product design, re-organize production systems, and satisfy multiple testing and certification procedures can entail a significant cost (or technical trade barrier) for suppliers, and this will only affect ASEAN producers, since they are required to catch up with Europe.

If we take into consideration the other agreements initiated by the EU with its commercial partners, like Mexico, setting up a free trade area with ASEAN could mean the deepening of the commercial deficit in EU favor.

When the EU-Mexico Free Trade Agreement (FTA) came into force in 2000, the then EU trade commissioner Pascal Lamy touted its significance for the future of Europe's trade strategy. It has since served as a model for further Investment Promotion and Protection Agreements (IPPAs) between the EU and Latin American countries and regions. Seven years on, though, the impact of the EU-Mexico FTA is clear. Instead of

[4] It should be noted that these studies are not independent, but ordered by the European Commission, so their conclusions should be regarded with circumspection.

the promised economic and social benefits, the treaty has left the Mexican state unable to implement policies to promote local small and medium size companies. Mexico's finance sector is now at the mercy of EU capital, while across various economic sectors the FTA has worked to the benefit of European transnational corporations and to the detriment of Mexican industries. The Mexican example is bound to repeat for the ASEAN members, as the partners are significantly different in their development levels.

In the case of the EU-Mexico FTA, which took effect in 2000, the European Commission delegation in Mexico had predicted that Mexican exports to the EU would increase from US$4.8 billion in 1999 to $30 billion by 2005. According to official data, in the first two years of the agreement, Mexican exports to the EU actually was in fact negative. Subsequently, Mexican exports did increase but only to $10 billion in 2006, far below the $30 billion predicted by the EU for 2005.

Moreover, Mexican imports from the EU grew rapidly, reaching $27 billion in 2006. The result was a steadily growing trade deficit, from $9.4 billion in 2000 to $14.2 billion in 2004 and $16.9 billion in 2006. Thus, that between 2000 and 2006, Mexico's trade deficit with the EU increased by 79.6 percent.

An FTA with the EU would force the 10 ASEAN members to adjust their investment regulations to meet the standards of the EU countries, which he said was inappropriate in the context of the ASEAN members, which had vastly different levels of development.

Moreover, although foreign investment might rise, this won't necessarily mean a higher employment level, or better wages, as investors count on the comparative advantage of cheap labour force and on the poor worker social protection.

A striking feature of the proposed EU-ASEAN FTA is that it is not – as has been normal EU practice to date – embedded in an association agreement, containing provisions on political, economic and development cooperation along with a focus on social cohesion, democratic principles and human rights. The fact that the EU already maintains or is negotiating partial agreements on political and economic cooperation with individual ASEAN countries, and the urgency with which the Commission would like to conclude the negotiations (by 2009), has evidently sparked a feeling that a cumbersome negotiating of an umbrella agreement could be dispensed with, and separate FTA negotiations launched immediately.

The EU's willingness to sideline social and developmental issues in the interest of a swift conclusion of the trade negotiations may be interpreted as a reflection of the importance it attaches to the opportunities offered by the ASEAN market. Such an approach is fully in line with the policy shift indicated in the 'Global Europe' document, but certainly not in the ASEAN countries' interest.

Conclusion

The EU-ASEAN FTA talks must be seen against the backdrop of EU concerns that its economic interests in South-East Asia will be sidelined as the US, China and Japan are negotiating a widening web of bilateral agreements in the region. Therefore, it is of vital importance to the EU's objectives to consolidate its position as a global player to gain a foothold in this crucial emerging region.

With ASEAN emerging as the world's largest exporter by 2050, the EU has singled out the region as one of its priority targets. ASEAN is a key market for the EU, as expectations are that the world's economic centre of gravity will increasingly shift to the Asia-Pacific region.

In a global environment increasingly populated by region-to-region agreements, neither the EU, nor the ASEAN can afford to stand aside. The establishment of a free trade area would undoubtedly bring economic benefits and promote the European model of integration among the ASEAN countries, while it would also allow Asian producers an easier access on the European market.

However, taking into consideration past EU agreements, there are some concerns, including the failure to mention asymmetry in the negotiating mandate, the EU's demands for WTO-plus commitments from developing countries like ASEAN in total disregard of any development dimension to trade, the real possibility of bringing damage to Asian producers.

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