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The Asian Way of Regional Integration: Are There Lessons from Europe?

Rolf J. Langhammer

- East Asian regional integration has widened in two directions: from the Southeast Asia-based ASEAN context to "ASEAN+3," which includes China, Japan, and South Korea, and from real sector integration (trade liberalization and factor movements) to monetary integration. The driving factors behind these new developments have been the stalemate situation in the multilateral trade negotiations (the Doha Round) and efforts to avoid a new financial crisis. Thus, regional integration in East Asia has been driven by external events rather than by an internal political process like in the European integration process.
- East Asian integration relies on a large number of bilateral "criss-crossing" free trade agreements (FTAs) that are seemingly too cumbersome to be used by the private sector. There is no true integration hub in East Asia, but rather many spokes. Anecdotal evidence speaks of a noodle bowl syndrome that causes traders in the region to forgo applying for preferential treatment while nevertheless expanding intra-regional trade. In short, market-driven regionalization dominates institutionalized regionalization.
- Extreme heterogeneity in almost each and every aspect (size, income level, economic structure, tariff levels), as well as the Asian preference for informality and unsettled political disputes on past and present issues, is a major stumbling block for regional integration EU style: a constructivist stages approach based on the rule of law. Surrendering sovereignty to supranational institutions is unacceptable in East Asia, which leaves pooling national sovereignty as the only alternative.
- Monetary cooperation at an early stage has been pursued since the so-called Chiang Mai Initiative of 1999 with bilateral standby agreements, informal discussions on rationalizing foreign exchange reserves, and the promotion of regional bond markets. But such endeavors have not yet had to cope with the "bad weather conditions" of financial turbulences. Making a reasonable forecast on the quality of monetary cooperation in deterring financial attacks against single countries like those that happened in 1997 is difficult both because of the lack of institutionalized trade areas, currency areas, and capital flow areas and because of the lack of an undisputed regional anchor currency.
- Trying to influence East Asian integration by pointing to EU experiences would probably not be very fruitful given the fact that East Asia, if it continues to follow the ASEAN+3 concept, will become as inward-oriented as the EU with its widening and deepening process. Yet, even under such disperse styles of integration in Europe and East Asia, globalization and the ever-rising importance of cross-border externalities like environment, management of common resources, terrorism, and military threats will induce East Asia to consider using most European ways of making integration and cooperation effective, such as by defining the rationales, setting targets, monitoring implementation, multilateralizing bilateral arrangements, and, finally, involving the private sector. And it is this last way that is most likely to convince East Asia to take the lessons provided by EU integration seriously.

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1 The Issue

For many years, East Asia[1] had been a champion of multilateralism. Countries maintained non-preferential most-favored-nation treatment MFN-based relations to countries outside the region, and inside East Asia, regional integration schemes never reached the magnitude and depth of comparable non-OECD regions such as Latin America. Comparing the two leading subregional schemes outside the OECD region, Mercosur and ASEAN, Mercosur's *acquis communautaire* (institutionalized achievements) is more advanced than that of ASEAN (if one can compare an incomplete customs union with an incomplete free trade area).

However, since the turn of the decade, the region has accounted for the largest number of incremental regional integration agreements (RIAs) in the world, that is, agreements notified to the WTO since the year 2000.

All these agreements are bilateral, with no supranational institution responsible for concluding negotiations with third parties, which means that the ten ASEAN countries alone could conclude up to 45 different bilateral arrangements if each ASEAN country negotiated different product lists and different conditions of conceding preferences with each other ASEAN country (Baldwin 2006a; Dieter 2006). Adding China, the Republic of Korea, and Japan to the group, the number of potential bilateral agreements could jump to 78. This has raised concerns about the effectiveness of such "noodle bowl" type RIAs (see Figure 1, taken from Baldwin 2006a).

In assessing this, one has to take account of five characteristics of the East Asian RIAs.

First, they are all "shallow." This means that they neither include common policies such as common trade policies in a customs union nor policy harmonization (economic union) or the free mobility of factors of production (common market). For the time being, they are confined to the lowest level of integration, free trade areas (FTAs).

[1] East Asia excludes the South Asian countries such as India, Bangladesh, Sri Lanka, and Pakistan. This exclusion is increasingly being questioned. For the debate on an Asian community including India, see Lim (2006).

Second, they are all either still being negotiated or implemented. So, they are still incomplete even at the FTA level. This is important because the dynamics of East Asian economic growth and structural change can lead to a continued revision of initial targets, means, procedures, and timetables. Shooting at a moving target is a characteristic description of East Asian regional integration.

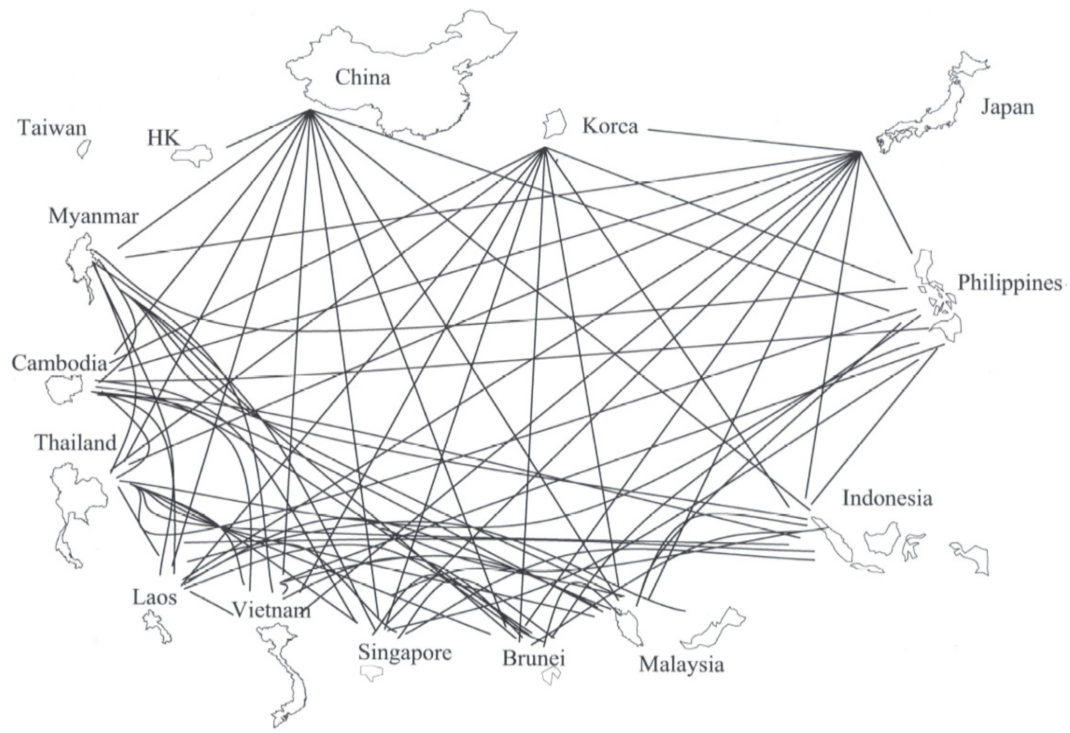
Third, achievements reached in the past, such as the ongoing implementation of ASEAN's common effective preferential tariff scheme (CEPT), are discounted with respect to their effective use. The very low one-digit utilization rates reported in the 1990s for the ASEAN CEPT have not been revised upwards since then (JETRO 2003). Obviously, companies avoid the red tape involved in applying for preferences and thus are prepared to pay the applied MFN tariff, which in many East Asian countries is known to be significantly lower than the WTO bound rate (overhang). So is there much ado about nothing?

Fourth, RIAs in East Asia are embedded in strong market-driven regionalization and economic growth. The costs of bridging distances have greatly declined thanks to new networks of surface, air, and sea transport links within the region. Intra-area trade has risen strongly, for instance, due to the famous "flying geese" patterns of Japanese multinationals, which again lower transaction costs if trade is party-related. This raises the question whether the strong growth of intraregional trade in East Asia is due to regionalism (institution building on a preferential base) or to regionalization as transaction costs have declined faster within the region than in trade with the rest of the world.

Fifth, the strong bilateral focus in East Asian integration is mirrored by bilateral approaches from abroad, basically by the United States and its "competitive regionalism," followed very likely soon by the EU after the disappointing suspension of the Doha Round.

Based on these observations, this paper will first try to conceptualize the possible approaches to RIAs if relationships are asymmetric, either due to the existence of hegemons or due to uneven intensities of initial economic interdependencies between the partner countries (Section 2).

Figure 1:
The Asian "Noodle Bowl"



Source: Baldwin 2006a.

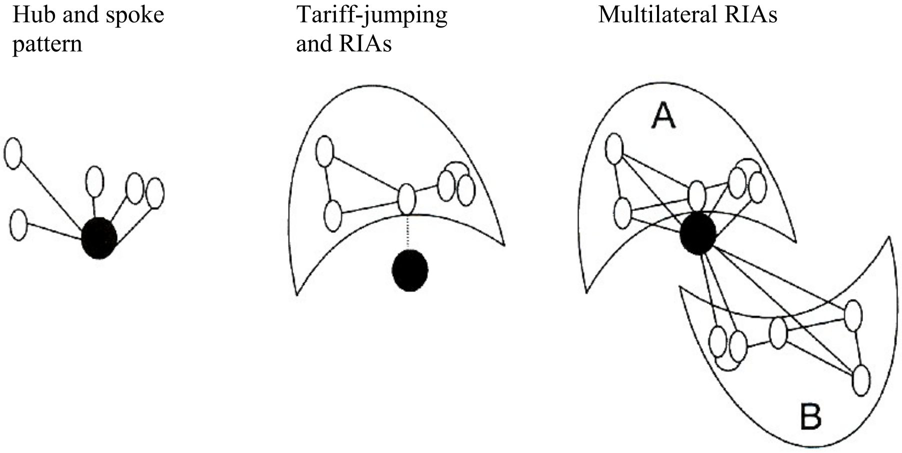
The paper will then discuss in more detail constraints inherent in East Asian RIAs and how these constraints are responsible for the current noodle bowl syndromes and asymmetries (Section 3). Section 4 will turn to the topical debate in East Asia on the sequencing of real sector integration (trade) and monetary integration. This has particular relevance for explaining the efforts that East Asian countries have been making to avoid a second Asian financial crisis and to build a regional "insurance scheme" against speculative attacks of financial markets against individual countries (Belaisch and Zanello 2006). Section 5 will associate lessons from sections 3 and 4 with the vast body of EU integration experience with stalemate situations, crises, and policy sequencing. Section 6 will conclude.

2 Some Conceptual Underpinnings: From "Noodle Bowls" via "Hubs and Spokes" to "Multilateral RIAs"

The Asian Noodle Bowl concept has been adopted by Baldwin (2006a) from Jagdish Bhagwati et al's famous Spaghetti Bowl picture.[2] The latter highlights the EU as a hub that maintains preferential relations at different levels (free trade areas, customs unions, associations agreements, nonreciprocal agreements) with spokes (European, African, Caribbean, and Pacific countries). These are sometimes linked to each other, but not always, by bilateral free trade agreements, in a few cases by customs unions like Switzerland and Liechtenstein. Hub and spoke (H&S) relations (see Figure 2) are characterized by bilateral contracts between a hub and several spokes. Such

[2] See Bhagwati (1995), Snape (1996), and Bhagwati et al. (1998).

Figure 2:
Patterns of Regional Integration Agreements



Source: Altomonte (2003).

relations are asymmetrical, as they give the hub a privileged stance over the spokes.

Agreements between spokes are eventually transformed into an RIA and thus contribute to eroding asymmetries. In Figure 2, this second stage in the transformation of RTAs is called tariff-jumping and RIAs. The background to this is that the hub can circumvent tariff hurdles imposed by individual spokes (tariff jumping) against third countries unless rules of origin fix conditions of eligibility of the hub's exports to a partner country via another partner country. This is why rules of origin are the most important (and most heatedly debated) policy instrument in tariff-jumping schemes with a hub, for instance, in EU negotiations with Mercosur or in transforming the H&S relations in Central and Eastern Europe into this second stage when the Central European Free Trade Area among the spokes was founded. This second stage as depicted in the figure may characteristically be incomplete on the spokes' side in the sense that not all the spokes share the same relations with each other as with the hub. As it is often the hub that is the driving force in pushing from the first to the second stage, it is also the hub that can provide the incentives for this transformation by setting the rules for defining the "origin of goods." These rules take into account the hub's content (export from the hub to the spokes followed by value-added processing in different spokes and re-export to the hub) by including the hub's value added in the cumulative value-added content of the hub plus spokes. The third stage in Figure 2 multilateralizes the RIAs by eroding the asymmetries between many spokes and forming various complete RIAs (A and B) with the hub. The enlargement of the EU, an EU agreement with a Mediterranean FTA, or the pending U.S.-Latin American Free Trade Agreement of the Americas are examples of this stage.

It is important to note that these three stages were not the model pursued by the European Economic Community (EEC) in the 1950s, since Germany at that time would have not been accepted as a hub, but only as an (important) partner among equals. Yet, the three stages are typical today for any RIA initiated by either the United States or the European Union in their relationships with third countries. They are increasingly important the more economic relations are ruled by asymmetries such as market size differences, growth differentials, differences in income levels, and differences in the capability of the partners to produce goods and services that impact upon third countries without obliging these countries to pay for them (collective international goods).

These conceptual underpinnings may provide criteria that can explain why East Asian integration developed the way it did and what would have to be changed if dead-end roads are to be avoided and if regionalism is to complement multilateralization rather than substitute for it. As will be shown below, the driving economic forces behind the past development of regional integration in general and East Asian integration in particular have been heterogeneity and asymmetry. Heterogeneity in terms of size, economic distance, and trade policy differences may hinder leading countries in the region from being accepted as hubs and in particular may give rise to fears that the net benefits from integration may be distributed unequally. Such distributional concerns can dominate allocative targets and prevent "shallow" integration such as bilateral free trade agreements from deepening towards agreements with common policies and factor mobility. East Asian integration will be shown to suffer from such deficiencies.

Apart from providing pure economic determinants of goods and factor trade, the role of hubs includes a political economy aspect. Hubs produce cross-border collective goods such as monetary or political stability, they determine the relationship both between spokes and between Asian and the non-Asian partners (the European Union, the United States), and they are relevant for the attractiveness of regional versus multilateral institutions.

3 East Asian Constraints in Regional Integration Agreements

3.1 Heterogeneity and Asymmetry in Economic Size, Income and Trade Structure

One of the reasons why RIAs in recent years have increasingly become an attractive alternative to multilateral trading arrangements and to the WTO with its 150 member states is the lower heterogeneity of RIA partners. Lower heterogeneity helps to identify common interests, accelerates decision-making, and lowers the cost of enforcement, implementation, and compliance. This is not a new insight. The success of the EEC in implementing its FTA and customs union stages between 1958 and 1968 has been widely attributed to the relatively high economic and political homogeneity of its six founding countries.

Yet, the term "homogeneity" hides more than it discloses. One has to assess what homogeneity means and how it possibly impacts upon regional integration in East Asia. One aspect of homogeneity is the economic size of economies measured in GDP or population. Sharply unequal size can make trade policy negotiations difficult if the larger partner sees the opening of its market to the smaller party as a "concession" in a mercantilist sense with no relevant reciprocity gain, as the smaller market is not attractive as an export market for the larger partner. As the MFN principle holds for the relations between the partners of an RIA, there is the risk that two equally large partners would dominate the negotiations to maximize the value of their concessions in exchange for concessions by their partners. They would leave smaller partners aside, thus tilting the level playing field. This so-called "principle supplier" syndrome is known from multilateral negotiations and threatens to burden RIAs too.

In East Asia, unequal size is unrivaled relative to the rest of the world. This is the case even if we disregard China and the two small and low-income Indochinese economies of Lao PDR and Cambodia. The 2004 PPP gross national income ratio between Japan (the largest country, next to China) and Singapore (the smallest country) was 33:1. Including China, the ratio to Singapore was 66. For the EU-15 less Luxembourg (EU-14) it was 17:1 (Germany v. Ireland).

Second, even more important indicators of heterogeneity are the level of income and factor endowment differentials. On the basis of the Heckscher–Ohlin trade theory and the Vinerian customs union theory, one can derive that in a South-South integration scheme, it is the country with the lowest level of income and highest proportion of unskilled labor endowment that bears the cost of trade diversion (Venables 2003). In an RIA, it imports from more expensive partner countries what it used to import from the formerly cheaper rest of the world. South-South RIA experiences are rich in terms of these trade flows (Uganda and Tanzania bearing costs of trade diversion versus Kenya being the winner; Bolivia and Paraguay versus Brazil, Honduras versus Costa Rica, Mali and Burkina Faso versus Senegal and Ivory Coast). The richer country usually benefits from its more advanced and diversified production structure and thus penetrates into the neighboring less diversified markets after forming the RIA. In 2004, per capita PPP income levels reveal ratios between Japan (the richest) and Cambodia (the poorest) of 106:1, and even if we exclude Japan and the two low-income Indochinese countries, the ratio does not fall below 45 (Singapore v. Vietnam). For comparison, for the EU-14, the ratio is 2.8 (Denmark v. Portugal[3]). Given these numbers, it is very likely that income differentials reflect differentials in resource endowment and thus trigger trade diversion effects to the detriment of countries like Lao PDR and Cambodia in the ASEAN context but potentially also to the detriment of Malaysia, the Philippines, and Thailand, should they open their markets to China by means of a complete FTA between China and ASEAN. Even if one can assume ASEAN countries to benefit substantially from gaining access to the buoyant Chinese market, experiences with the sequencing of changes in export and import flows after integration suggest that the more advanced country will be faster in expanding its exports than the less advanced partner country. Politically, such lags can become stumbling blocks for the sustainability of a medium-term integration agenda if less advanced countries see a causality between deteriorating bilateral trade balances with the more advanced partner countries and the formation of FTAs.

A third element of heterogeneity is differences in the sectoral composition of production and trade. Whether this heterogeneity, however, impedes regional integration, is not straightforwardly evident, since heterogeneity (homogeneity) as a stumbling block (stepping stone) also depends on income levels. Countries may be homogenous in their structure of production at a very low level of income but then try to protect their production facilities against the competition of the neighboring countries. At that level, there is little intraindustry specialization that could help contain protectionist tendencies. Homogeneity of production structures at a high level of income usually includes a high level of intraindustry trade with rising economies of scale, differentiated consumer preferences, and often cross-border party-related trade within a multinational company. High heterogeneity can mean interindustry specialization with one-way trade and strong protectionist tendencies. How relevant are these issues for East Asia?

Table 1 presents calculations of so-called trade similarity or overlap indices showing how much trade of a country is "matched" by similar trade of another country. Thus, sectoral patterns of exports of East Asian countries to the world are compared in the ten most important 3-digit SITC categories. While accounting for the core of exports of these countries, they do not cover the entire export pattern.[4] The index ranges between 100 (totally identical trade structure) and 0 (totally dissimilar trade structure). The comparison for bilateral pairs of nine East Asian countries (the five founding member countries of ASEAN plus Vietnam, China, Japan, and the Republic of Korea) for 1991–1992 and 2001–2002 show rising similarity over time, especially both between the two high-income countries Japan and Korea and between the low-income countries (Indonesia, Vietnam). This reflects converging trends in the export pattern of East Asian countries in labor-intensive as well as human-capital-intensive industries caused (among other explanatory factors) by rising vertical integration of cross-border value-added chains in the so-called "Asian factory." On average, China's export structure has become more similar to that of most Asian countries. Yet, the overlap level for the ten categories is still relatively low. Levels of similarity are much higher within ASEAN than outside ASEAN, especially if Singapore is involved. This can be explained by the importance of the electronics industry and its vertical processing

[3] Since the Eastern enlargement (excluding Bulgaria and Romania), this ratio has risen to 7 (Denmark v. Latvia) but is still significantly lower than in East Asia.

[4] Doing the same exercise for the EU countries leads to much lower indices than in East Asia due to the much larger degree of sectoral diversification in Europe.

Table 1:
Indices of Similarity[a] of the Export Supply[b] between Selected Asian Countries

	1991–1992								
	China	Indonesia	Japan	Korea	Malaysia	Philippines	Singapore	Thailand	Vietnam
China	0.0	11.3	15.5	3.5	5.0	22.6	9.8	7.0	0.0
Indonesia		0.0	10.8	8.3	10.4	12.3	6.3	7.1	7.2
Japan			0.0	19.5	18.1	13.5	5.6	12.7	12.4
Korea				0.0	11.6	0.0	2.0	16.1	20.4
Malaysia					0.0	9.3	7.1	12.7	8.3
Philippines						0.0	11.8	0.0	0.0
Singapore							0.0	4.4	2.9
Thailand								0.0	16.1
Vietnam									0.0
	2001–2002								
	China	Indonesia	Japan	Korea	Malaysia	Philippines	Singapore	Thailand	Vietnam
China	0.0	4.7	13.5	16.9	17.5	18.4	17.9	11.6	8.4
Indonesia		0.0	2.4	2.4	12.8	2.4	2.4	2.4	14.3
Japan			0.0	24.6	18.9	20.9	24.6	21.8	2.6
Korea				0.0	25.3	22.0	28.0	19.4	2.6
Malaysia					0.0	41.5	42.7	24.4	6.0
Philippines						0.0	49.0	23.0	3.9
Singapore							0.0	26.8	2.6
Thailand								0.0	7.5
Vietnam									0.0

[a]Finger–Kreinin trade similarity index. The index of export similarity is defined by the formula $S(ab,c) = \sum_i \mathit{Minimum}\left[Xi(ac), Xi(bc)\right] \times 100$, which measures the similarity of the export patterns of countries *a* and *b* to market *c*. $Xi(ac)$ is the share of commodity *i* in *a*'s exports to *c*. If the commodity distribution of *a*'s and *b*'s exports are identical ($Xi(ac) = Xi(bc)$ for each *i*), the index will take on a value of 100. If *a*'s and *b*'s export patterns are totally dissimilar (for each $Xi(ac) > 0, Xi(bc) = 0$, and vice versa) the index will take on a value of 0. — [b]Based on the ten most important SITC three-digit export categories.

Source: UNCTAD (1994), Handbook of International Trade and Development Statistics; UNCTAD (2004), Handbook of Statistics; own calculations.

stages that are common to Singapore, Malaysia, and the Philippines. It is in the ASEAN region where the "Asian factory" phenomenon is most widely spread. Based on these findings, there is still little ground for the concerns of East Asian economies competing with Chinese exports in standardized manufactures that they would have to suffer from terms of trade losses due to expansion of these Chinese exports. South Asian countries, such as Bangladesh and India, that have their export strongholds in textiles and clothing seem to have been affected more than East Asian countries by increasing overlaps with the Chinese exports.

In the short run, price effects of regional integration could contribute to strengthening specialization structures, thus promoting more dissimilarity in intraregional trade, while in the medium run, income effects could trigger a trend towards more intraindustry trade.

3.2 Trade Barrier Discrepancies

Trade policy harmonization and the removal of intraregional barriers to trade is at the heart of RIAs. The ASEAN Free Trade Area with its CEPT scheme is advanced but, as mentioned earlier, is not used very much probably because of the small amount of tariff savings it offers compared to the amount of red tape it imposes on countries wishing to comply with its rules of origin and other regulations. Table 2 tries to portray the tariff profile of East Asian countries in order to find out whether it is meaningful to apply for preference margins. What matters in this context is the applied tariff not the WTO-bound tariff. The difference engenders the binding overhang or "the water in the tariff" problem, which was and still is one of the basic issues of contention in the NAMA (nonagricultural market access) negotiations of the Doha Round. The large dis-

Table 2:
Tariff Profiles of East Asian Countries by Products, 2005

	Indonesia		Malaysia		Philippines		Singapore		Thailand	
	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty
Agriculture										
Sugar	9.5	58.3	2.8	X	15.2	44.7	0.0	10.0	26.6	48.9
Grains	2.6	68.4	0.0	10.8	15.7	36.7	0.0	10.0	X	35.7
Oil seeds	3.8	39.9	1.7	6.0	5.6	36.6	0.0	10.0	21.1	X
Beverages, spirits	67.9	98.1	X	X	8.5	44.8	0.0	X	57.1	X
Dairy products	5.0	74.0	3.6	X	3.9	26.4	0.0	7.0	23.9	34.0
Manufacturing										
Wood, pulp, paper, furniture	5.2	39.4	12.5	18.7	7.2	24.2	0.0	3.0	14.7	X
Textiles	10.5	28.7	13.2	19.5	10.8	28.0	0.0	10.0	22.0	X
Leather, rubber, footwear, travel goods	7.7	39.8	15.1	21.5	6.7	32.7	0.0	10.0	21.6	29.9
Metals	7.3	38.4	8.8	19.7	4.6	25.7	0.0	5.4	11.7	23.9
Chemicals, phographic supplies	5.4	38.1	3.8	11.9	3.8	19.6	0.0	5.1	6.7	29.4
Transport equipment	12.2	38.9	19.6	14.2	8.8	19.1	0.0	6.0	27.7	48.3
Nonelectric machinery	2.2	34.9	3.7	9.1	2.3	19.0	0.0	6.3	8.4	20.2
Electric machinery	6.0	30.3	8.1	13.8	3.7	18.1	0.0	5.4	12.8	18.2
Mineral products, precious stones, metals	5.1	39.6	9.9	15.3	4.9	23.0	0.0	7.9	10.7	25.4
Manufactured articles not specified	7.5	35.7	6.2	9.9	4.9	24.9	0.0	3.1	12.8	24.9
Fish, fish products	4.9	40.0	6.4	7.8	8.0	31.0	0.0	10.0	10.1	8.8
Petroleum	2.1	40.0	X	5.0	2.9	...	0.0	...	15.1	...

Notes: … denotes Data not available. X denotes simple averages not calculated because more than 40 percent of HS 6-digit subheadings contain at least one non-ad valorem duty.

Table 2 continued

	Average ASEAN 5		Laos		Cambodia		Vietnam		Average ASEAN 8	
	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty
Agriculture										
Sugar	10.8	40.5	12.7	–	12.3	27.8	17.7	–	12.1	38.4
Grains	4.6	32.3	5.0	–	11.9	18.6	14.7	–	7.1	30.4
Oil seeds	6.4	23.1	11.8	–	9.5	22.8	13.4	–	8.4	23.1
Beverages, spirits	33.4	71.5	31.7	–	42.3	43.7	70.0	–	39.6	64.5
Dairy products	7.3	35.4	8.3	–	30.8	36.5	X	–	10.8	35.5
Manufacturing										
Wood, pulp, paper, furniture	7.9	21.3	13.4	–	16.9	24.8	17.2	–	10.9	21.9
Textiles	11.3	21.6	9.2	–	19.8	12.2	35.6	–	15.1	20.0
Leather, rubber, footwear, travel goods	10.2	26.8	10.8	–	24.1	28.3	19.0	–	13.1	27.0
Metals	6.5	22.6	6.0	–	11.5	19.8	8.3	–	7.3	22.2
Chemicals, phographic supplies	3.9	20.8	6.8	–	10.1	9.3	5.1	–	5.2	19.2
Transport equipment	13.7	25.3	13.7	–	19.4	24.3	22.2	–	15.5	25.2
Nonelectric machinery	3.3	17.9	6.0	–	14.5	15.3	5.4	–	5.3	17.5
Electric machinery	6.1	17.2	6.6	–	24.7	26.6	12.8	–	9.3	18.5
Mineral products, precious stones, metals	6.1	22.2	5.6	–	15.9	21.6	13.9	–	8.3	22.1
Manufactured articles not specified	6.3	19.7	10.4	–	17.2	24.9	15.2	–	9.3	20.4
Fish, fish products	5.9	19.5	16.6	–	19.3	23.5	31.3	–	12.1	20.1
Petroleum	5.0	22.5	7.3	–	15.1	22.7	17.5	–	8.6	22.6

Table 2 continued

	China		Japan		Korea		Average ASEAN +3	
	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty	Average applied duty	Average bound duty
Agriculture								
Sugar	27.4	27.4	X	X	19.0	24.6	13.8	35.6
Grains	30.5	27.1	1.0	1.5	186.3	249.8	23.3	47.4
Oil seeds	13.3	11.6	2.2	2.0	13.7	22.2	8.5	19.7
Beverages, spirits	23.3	21.4	13.7	15.6	31.4	37.4	34.9	49.6
Dairy products	13.8	12.2	28.0	X	67.5	69.8	16.9	36.8
Manufacturing								
Wood, pulp, paper, furniture	5.7	5.0	0.9	0.9	2.4	2.8	8.8	16.2
Textiles	12.9	11.5	6.7	6.7	10.1	19.4	13.6	17.8
Leather, rubber, footwear, travel goods	13.7	13.7	6.4	6.6	7.9	12.2	12.0	22.6
Metals	7.0	7.1	1.0	1.0	4.3	7.0	6.5	17.5
Chemicals, phographic supplies	6.8	6.7	2.5	2.0	5.8	5.8	5.1	15.3
Transport equipment	13.1	11.5	0.0	0.0	5.4	8.2	13.2	20.1
Nonelectric machinery	8.5	8.4	0.0	0.0	6.0	9.5	5.0	14.4
Electric machinery	9.0	8.8	0.2	0.2	6.0	9.0	8.1	15.1
Mineral products, precious stones, metals	9.6	9.7	0.8	0.8	5.7	8.8	7.4	17.9
Manufactured articles not specified	12.3	12.3	1.1	1.0	6.4	10.0	8.4	17.0
Fish, fish products	11.5	11.0	5.7	5.0	16.1	15.0	11.4	17.4
Petroleum	5.1	3.3	X	3.5	5.1	12.3	7.6	16.5

Source: World Trade Report (2005); own calculations.

crepancy between applied and bound rates indicates that even high cuts in bound tariffs are ineffective if the final tariff is still above the applied rate.[5] Various findings emerge. First, the binding overhang is significant, especially in the ASEAN countries, less so in the Big Three. Second, intercountry differences in applied tariffs are particularly large in agricultural products. This is the case as regards intra-ASEAN relations as well as regards relations between the Big Three, and between these countries and the ASEAN group. RIAs usually handle this problem by keeping agricultural products out of the negotiations and by establishing special regulations for these "sensitive products." Third, with relevant export items such electrical and nonelectrical machinery, applied tariffs are often at the one-digit tariff level. Here, the incentives to apply for preferences and to bear the costs of red tape are relatively small. Fourth, the three Indochinese economies impose higher tariffs on average and thus will apply for infant-industry protection. Fifth, an average ASEAN+3 applied tariff in manufacturing ranges between 5 and 14 percent and should not pose an insurmountable barrier to negotiations (unlike negotiations in the agricultural sector). However, this excludes nontariff barriers such as technical standards.

3.3 Preferences for National Sovereignty

FTAs are common today, but with declining MFN tariffs, their effectiveness will erode as much as the preference margins do. Shallow integration no longer makes a difference. It is true that the "new age" generation of FTAs in East Asia between the advanced countries like Japan and Singapore includes new features like e-trade provisions, customs automatization, and collaboration in media, broadcasting, tourism, education, training, and other public and private services (Hertel et al. 2001).[6] These all help to reduce delivery and transaction costs. Yet, there is one overriding issue that sets the upper limit to the prospects of regional and bilateral agreements in Asia. This is national sovereignty and strong resistance so far against transferring competences to a common institution that takes responsibility as regards "common policies." Neither is the ASEAN Secretariat such an institution nor do bilateral agreements have such provisions. One can even argue that the preference for bilateralism over regionalism in East Asia mirrors the failure of deep integration with common policies and policy harmonization. This has implications for agreements concluded by ASEAN with third parties. As concerns the substance of agreements, such as detailed tariff preference schedules (Baldwin 2006a), these are basically bilateral agreements of ASEAN countries put together under a common umbrella framework. Yet, the ASEAN Secretariat has no mandate to negotiate trade policies on behalf of its member countries as the EU Commission does.

The reasons for the failure of common policies in the East Asian region are probably rooted in historical legacies (or heritage) of colonialism, intraregional imperialism, a still unfinished agenda to correctly describe and acknowledge the atrocities during wartime, a lack of full political and societal reconciliation, the still ongoing nation-building process in some of the countries, and, finally, a missing public debate and common understanding of the future role of the East Asian region in global politics and economic affairs. It is the latter that is of primary interest to economists. Departing from the assumption that East Asia is defined geographically but not as a cultural, political, or economic entity, the pressure to cooperate within the region comes basically from outside challenges and is subject to ad hoc decisions. To cite a few of these challenges, the Asian financial crisis of 1997 was a wake-up call to negotiate genuine Asian early warning systems and stand-by agreements and to develop regional bond markets. Other challenges that spawned regional or subregional measures include natural disaster relief, ecological precautions (for instance, in river commissions) and

5 In some cases, applied tariffs are higher than bound tariffs. This is due to the fact that the tariff figures in Table 2 are unweighted averages constructed from six-digit HS individual products (tariff lines).

6 This is also stressed by Dee (2006) with respect to service trade, but she also argues that East Asian FTAs remain second best, as they continue to discriminate against nonmembers.

common measures against maritime piratry and terrorism. But as in trade policy, these cooperative measures are still shallow and often only of subregional relevance. Mostly, they are not binding and thus noncompliance is not subject to litigation, court decisions, and sanctions.

3.4 Potential Hegemons, Yes, but Internationally Relevant Collective Goods, No

Hegemons can be important catalysts of regional integration. Due to their political and economic leverage and their self-interest in completing integration, they shoulder more costs than they should if seen from a purely national cost-benefit analysis point of view and they provide more goods and services to their partner countries than these have to pay for. Their visible balance of payments may be in deficit but this may just indicate that partner countries are prepared to be a lender for hegemons in exchange for the invisible part of their balance of payments that is in surplus.[7] The empirical postwar history of hegemons and their collective goods focuses basically on the U.S. postwar role in the multilateral trading system and in the old Bretton Woods system, which collapsed in the early 1970s (Fratianni and Pattison 1982; Keohane 1982; Krasner 1982; Yarbrough and Yarbrough 1985). Examples of collective international goods were the U.S. pressure for the MFN principle in trade (at that time), the role of the dollar as an international currency, and the role of the United States as a military superpower. The theory of international organizations applies to regional integration as a special form of international coordination if it allows for the implementation of the exclusion principle to restrict concessions to members of a club. Apart from predicting that returns of net benefits of membership in a regional scheme will decrease when membership rises by numbers, the theory also predicts that to agree on common issues absorbs more costs when membership rises. Net benefits can even become negative. Appeasing or even excluding a marginal member with a negative net benefit for the integration scheme and compensating this member for its forgone benefits can be a prime task for a hegemon. Such compensation usually takes the form of financial flows, as these flows can much more easily serve to publicly demonstrate a government's role in an integration scheme.

Who in East Asia is in principle prepared to act as a widely accepted hegemon? In terms of a donor, Japan has maintained a leading role in the Asian Development Bank for many years, but it has never been politically accepted as a hegemon, nor has it produced collective international goods at a level that other countries would miss. Its market is still not as open and dynamic as that of the United States or as that of China in recent years. Its currency is a regional but not an international currency and even domestic traders still hesitate to use the Japanese currency as an invoice currency. Its banking system has gone through a number of serious adjustment problems and for more than a decade its economic growth was stalled.

China's position, while strongly improving, has not yet proven to be sufficiently consolidated to master adjustment shocks and help trickling down effects for neighboring countries to materialize. It causes terms of trade deteriorations for countries with similar production structures because its massive export expansion puts world market prices in specific manufactured goods under pressure. Net importers of Chinese products among the more advanced countries in the region, however, benefit from such expansion. China's financial system is still untransparent as concerns the true exposure of domestic banks to potentially nonperforming loans of state-owned companies. Other risks for a sustained 9–10 percent economic growth rate (such as bottlenecks in the environment, human capital, and institution building) linger around the corner. Yet, the main problem with China playing the role of economic hegemon is that it is potentially exposed to a balance-of-payments-driven consolidation crisis in the United States. While it is acknowledged that the transfer mechanism from a U.S. crisis to a Chinese crisis is no longer as linear as it used to be when China rigidly fixed the exchange rate to the dollar, it will remain intact un-

[7] In the debate on the U.S. current account deficit, this is referred to as the "dark matter view."

til still more exchange rate flexibility is allowed. This is not to say that China should follow this course, but the longer cross-Pacific exchange rate flexibility is constrained, the more it becomes evident that the true hegemon with positive and negative externalities for East Asia is located outside the region.[8] It is still the United States. Other possible candidates in East Asia are either too small, though economically potent (Singapore), or too fragile and poor (Indonesia).

3.5 Lack of Enforcement Capacities of Regional Institutions

Deepening regional integration towards common policies and common institutions is one of the main pillars of RIAs that strive for reputation and credibility (Langhammer 2004).[9] After the 1997 Asian financial crisis, East Asian integration had the chance to catch up in terms of institutional progress. Yet, even at the subregional level of ASEAN, with its long tradition and long list of institutional bodies such as the regular heads of state meetings, the post-ministerial meetings, and the ASEAN dialogue partner system, progress has stalled. In a *Financial Times* article (September 2, 2004) by Yasheng Huang and Bernard Yeung, ASEAN's institutions were rated "still in poor shape."

Given the large number of subregional and—increasingly—also regional committees and working parties (ASEAN plus Three), it does not seem to be the lack of regional institutions per se but the lack of enforcement capacities of these institutions that prevents progress. Enforcement competences are firmly anchored at the national level in East Asia.[10] This is not only the result of the lack of common policies. It is also a consequence of lowly perceived interdependencies between the countries. River institutions like that of the Mekong are the closest to interdependencies seen as an issue to be solved regionally or subregionally.

The most straightforward approach to complement technocratic advisory committees by decision-taking institutions could be to empower a group of outstanding "elder statesmen," one from each country, to set up a master plan for supranational institution building based on an understanding of which challenges of regional relevance East Asia will have to master in the years ahead. Simultaneously, subregional cooperation schemes with narrowly defined tasks, such as river cooperation schemes, or coastal surveillance cooperation schemes, should be encouraged to deepen their programs.

However, there is the argument that there is no need to institutionalize regionalism if the economic dynamism in the region itself promotes regionalization driven by a decline in all transaction costs (transport, tariffs, nontariff barriers, and costs of uncertainty). So why should East Asia do what comes naturally? The argument is specially relevant for East Asia, where informal ties through kinship, families, clans, etc., often substitute for formal institutions and thus develop and advance differently from the Western tradition. Furthermore, given the inertia and delays in the process of institution building especially in developing supranational institutions, it is feared that this process would not keep pace with the economic dynamics of the private sector. Yet, in the trade policies that are at the core of RIAs, it is less the gap between public policy inertia and private sector dynamics that matters. It is the issue whether economies of scale could be realized if a single supranational institution, instead of diverse and numerous national public policies (suffering from inertia just as much as supranational institutions do), took responsibility. In East Asia as much as in other regions, rules for trading beyond borders are ideal candidates for such gains in economies of scale. This is witnessed by the superiority of multilateral MFN-based rules over both national and regional rules of trading, with the latter clearly being the second-best alternative.

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[8] See Kaplan (2006) for a recent debate from a political economy angle on the issue whether the Chinese exchange rate is undervalued.

[9] Langhammer (2004) discusses this issue for the most difficult integration efforts between China, Japan, and the Republic of Korea.

[10] Pooling national sovereignty rather than surrendering national sovereignty is the political jargon used in ASEAN circles.

4 Heterodox Sequencing: Can East Asia Promote Monetary Integration First?

The successful launch of a common currency among 12 member countries of the EU has raised much attention in East Asia, where for many years integration concentrated only on liberalizing trade and capital movements between one another. Especially since the Asian crisis of 1997, East Asian governments have started to analyze whether entry into monetary cooperation based on standby agreements or exchange-rate coordination could protect their currencies against speculative attacks from financial markets. Furthermore, regional or bilateral standby agreements have been concluded and implemented as a first step towards creating a regional firewall against such attacks (e.g., the Chiang Mai Initiative, see below). Early experiences in the EU, such as the implicit signal ostensibly sent by the German Bundesbank to defend the French franc/ Deutsche mark exchange rate against attacks against the franc in the early 1990s, are thought to provide support for similar endeavors in East Asia even though it is well known that the state of real sector integration there is rudimentary compared to Europe.

Therefore, the debate centers around the question whether one needs a sufficiently high level of real sector integration to make an entry into monetary cooperation credible and sustainable or whether an early entry into monetary cooperation can even engender further real sector integration and thus even create conditions for what is called an optimum currency area in the literature. Technically, the question focuses on the so-called exogeneity or endogeneity of an optimum currency area (OCA).

The ruling view on sequencing regional trade integration and monetary cooperation has recently been labeled Mundell-I by McKinnon (2004). Mundell argues in his earlier works that in a situation where

- economic structures of potential partner countries are diverse,
- labor markets are segmented, and
- expectations are stationary,

exogenous shocks to countries are asymmetric, as they affect one country only. Therefore, a flexible exchange rate is needed to adjust to such shocks. OCA conditions are not given and they cannot be created by an early entry into monetary cooperation through fixing exchange rates. In more popular terms, this view has also been called the coronation theory because after deep real sector integration brought about by liberalizing trade and factor movements, the economic structures of countries would converge, shocks would become symmetric, and countries would enter into monetary cooperation culminating in the creation of a single currency, which would be the coronation of this long-term process.

In recent years, a competing theory (Mundell-II) also stimulated by Mundell has arisen saying that, expectations are not stationary. Therefore, a common currency across countries could mitigate asymmetric shocks by allowing better reserve pooling and portfolio diversification. In simple terms, a common currency would force trading partners to share the adjustment costs of an adverse shock. Under flexible exchange rates, costs of adjustment would have to be borne entirely by the country hit by a shock and that would have also negative implications for real sector integration. It could even put achievements in real sector integration attained in the past at risk. In popular terms, this view has been labeled vehicle theory because monetary cooperation would be instrumental to promoting real sector integration or preventing real sector integration from disintegration. Proponents of this view often point to what happened in Italy when it became evident that the country would be among the first-round members of EMU. Interest rates on lira-denominated bonds declined to the level of the other qualifiers, and that "free lunch" helped Italy to stimulate growth and to be prepared for further deepening of real sector integration.

The question is whether East Asian could profit from at least some of these European experiences.

It is obvious that Asia defined as Southeast and Northeast Asia is far from fulfilling OCA conditions. Even though one could argue that neither the United States nor the European Union meet these conditions, there is no doubt that the conditions in Asia are far less fulfilled than in any other area. As discussed in the previous chapter, economic structures are diverse between commodity-producing countries and non-commodity-producing countries. Income levels differ greatly between advanced countries and the Indochinese countries. Institutions such as the common external trade policy of a customs union do not exist, capital markets are segmented, and labor cannot move freely across the borders of individual countries. But what matters more is that currency blocs, trading blocs, and capital blocs do not overlap. In Asian countries (except for Japan), external debt is basically dollarized and not denominated in one of the regional currencies. This is in essence the "original sin" problem. The development of regional bond markets is still in its infancy. The countries have preferred to use different sorts of pegs to the dollar. Trade is rarely invoiced in regional currencies. Even the yen does not play a major role as an invoicing currency in Japanese trade. Trade with the United States and Europe has been greater than with neighboring Asian countries, though with the emergence of China in international trade this could now change, at least with respect to incremental trade. Capital transactions, as well as the reserve currencies and anchor currencies, rely basically on nonregional currencies. No currency in the region qualifies to serve as an international currency (see Section 3 above on the role of hegemons).

Some weaknesses of an institutionalized regionalism have already been discussed with respect to the not-yet-completed ASEAN FTA but can be extended to the open regionalism model of the Asia-Pacific Economic Cooperation (APEC). APEC, which includes countries of the Western Pacific Rim, is not based on a formal agreement. It reflects the very limited possibilities to bring about regional coherence in this area by hoping that peer-driven competition between the neighboring countries will bring the region towards free trade by the year 2020 at the latest. Ways to achieve this are left to the discretion of the individual countries.

In recent years, in spite of their low level of institutionalized relations, Asian countries have tried to establish some instruments of monetary cooperation. The Chiang Mai Initiative of "ASEAN plus Three" introduced bilateral explicit standby agreements. Yet, unless these agreements can convince financial markets that in cases of emergency financial support would be unlimited, they are unlikely to impress markets. Implicit bailout signals have not yet been sent. And, given the low state of real sector integration and political will, promises would probably face the so-called Groucho Marx problem: one should never become a member of a club that accepts you as a member; or bluntly, joining a club with a bad reputation can, or definitely will, damage the reputation of the joining member.

Yet, small technical steps are possible, one being propagated by Williamson (1999) and others claiming that the countries could jointly peg to a common basket of currencies instead of only to the dollar. The countries could also agree on common weights of currencies in their joint basket. The problem with this approach is twofold. First, countries are not symmetrically linked to the same nonregional trading partners. The Philippines, for instance, are much more oriented in trade towards the United States than is Thailand, which is more oriented towards Europe. Strong fluctuations between the euro and the dollar could drive a wedge into a common basket peg, making common weights unsustainable. The second problem is that countries are known to manipulate their exchange rates for different reasons. For example, Singapore has often manipulated its exchange rate in an upward direction in the past in order to decouple the country from international inflation or it has used its exchange rate policy to put pressure upon the domestic industries to upgrade and relocate labor-intensive manufacturing abroad. Commodity-producing countries like Indonesia could suffer from "Dutch disease" problems or real appreciation and thus could be tempted to manipulate exchange rates toward depreciation in order to lower the burden for exports of noncommodity sectors. Such asymmetries could make a common basket peg very difficult to sustain.[11]

Clear proposals come from Mundell (2003) to either introduce a parallel currency in the region, supported by reserves of an "Asian Monetary Fund" to compete against the national currencies, or to convince the Japanese government to irreversibly fix the exchange rate between the yen and the dollar. The latter step would in fact be the first credible internal anchor of further monetary integration. It is very likely that other countries would join this peg and also fix their national currencies to the yen/dollar peg. Yet, it would place a heavy burden of adjustment pressure on the Japanese economy (and especially its labor market) and on countries linked to the Japanese market, since an autonomous national monetary policy would then no longer be possible and the prices of the relatively immobile factor "labor" would have to substitute for a buffer against the transmission of international shocks. Given the differences in the economic structures in the US and the Japanese economy with the Japanese economy being more manufacturing-oriented against the US economy being much more service-oriented, especially the not yet fully recovered Japanese financial system (banking and insurance) would have to master the adjustment burden. Japanese trade would also be exposed to the volatilities of the dollar/euro exchange rate. In view of the strong exposure of Japanese industry in the European market, any appreciation of the dollar against the euro would immediately impede the competitiveness of the Japanese manufacturing export supply in Europe.

Outside the real sector, there is the so-called "original sin" problem of emerging markets in Asia, where a regional bond market does not yet exist. Unless there is genuine demand for intraregional trading in bonds denominated in the national currencies, it seems very difficult to establish such a market that then would become also attractive to institutional investors outside the region.

Summarizing the issue of sequencing trade integration versus monetary integration, it seems that East Asia will not be able to promote the process of monetary integration without succeeding in regional integration and starting dialogues on coordinating macroeconomic conditions. Political commitments are of utmost importance. Any attempt to accelerate monetary integration that lacks such commitments may induce macroeconomic instability and endanger the stability of real exchange rates (Langhammer and Schweickert 2006b:73).

Lessons from EU monetary integration (Langhammer and Schweickert 2006a) suggest that the effects of monetary integration on promoting intraregional trade are stronger if trade barriers are lower, i.e., the more integrated the partner countries are. This does not necessarily imply that a monetary union has to be preceded by institutionalized regionalism if de facto regionalization of trade is strong. This is especially the case in East Asia, where the motivation for monetary integration since 1997 has primarily been ruled by nonregional issues, such as reducing foreign exchange reserves, avoiding currency crises, and establishing a regional capital market (Click and Plummer 2005; Kwack 2005). Yet, agreeing on common policies, such as on trade policies in a customs union, would very likely facilitate any attempt toward monetary integration, since such agreement would demonstrate political commitment in favor of deep integration.

5 Gradualism, Cooling-Down Periods, and Multilateralization of Preferences: Where Europe Can Offer Valuable Experiences

What could East Asia learn from EU integration?

At first glance, very little overlap between the two regions' experiences in regional integration seems to exist, basically because of the much larger heterogeneity of Asian countries and their domestic institutions, the lack of a joint common tradition of stateness (with bad as well as good political historical legacies) and the obvious reluctance of policy-makers to develop a regional

[11] See also Langhammer (2005).

political and economic master plan for East Asia and its role in global political and economic affairs. Unlike in Europe, with its French-German partnership, history has hindered East Asia in developing a single economic and political gravity center with strong interests of its own in regional integration and positive spread effects to partner countries.

For the time being, East Asia will still derive its motivation for regional integration primarily from two objectives: to find export markets in neighboring countries on a mutual basis and second, to avoid further financial crises with massive negative repercussions for the entire region.

Assuming political motivation in East Asia is not yet sufficiently strong to give sustainable impulses to economic integration, the European lessons that would be most useful to East Asia would be those relating to the following.

a) Economic rationale

In the early period of EU integration, including the stage of the Single Market Program, the rationale of integration was that of unifying diverse national markets. More recently, however, globalization pressure and the fear of Eurosclerosis in its various facets (aging, decline in innovation, and R&D spending) have shifted the rationale of integration to the issue of "Europe's role in the World Economy." It is the external dimension that is gaining in importance. The Lisbon strategy of promoting Europe as the world's leading knowledge-based region, Europe's concern about its competitiveness in the Triad with Asia and the Americas, and, finally, the role that Europe could play in G-8 issues, like making its own contribution to reducing global macroeconomic imbalances, are today important engines of economic integration. Deepening and widening the EU market is increasingly seen as an instrumental variable to improve Europe's position in global competition for mobile resources rather than as a target in itself.

This largely parallels feelings that came up in Asian political circles after the financial crisis of 1997. For the first time, East Asia as a region and not an individual country felt stigmatized, since the crisis swept over Asian countries only. How the EU tried to separate itself from the Eurosclerosis stigma by balancing domestic policy tasks and Europe-wide initiatives conducted by the EU Commission is something from which East Asia could draw lessons with respect to avoiding a new crisis. This includes the setting of milestones, and the conducting of reviews, progress reports, and peer reviews.

b) Targets

Many policy issues today spread over borders and cannot be dealt with satisfactorily at the national level by national measures only. The list of issues gets longer as the cross-border effects of national events and developments, such as environmental precautions, terrorism, consumer protection, or infrastructural planning and financing, start mushrooming. In recent years, EU policy-makers have tacitly begun to coordinate policies even if these efforts were not legally based on a clear EU mandate such as in common policies. It is evident that East Asian countries will increasingly become victims of negative cross-border effects of national policies unless these policies are subject to at least a minimum of supranational coordination. Furthermore, many events, by definition, spread over borders and/or cannot be blocked at national borders because they are invisible, particularly as regards environmental, health, and security issues. The scope for joint measures ranges from early warning systems to damage control and rehabilitation.

c) Implementation

From the very beginning of its history, the EU has set priorities and milestones in implementing program in order to remain credible when stressing the so-called "costs of non-Europe," that is, the gains forgone if integration programs were not implemented. Examples of such milestones can be found in all periods of EU history, from the implementation of the free trade area and customs union in five substages (1958–1968) via the Single Market Program (1985–1992) to the Lisbon Strategy 2010. Timetables were negotiated and became subject to midterm reviews, revisions, and post-date monitoring. While the shortcomings of a purely legal or institutional fulfillment of commitments cannot be neglected, publishing data on the distance of achievements from the target created both pressure for compliance among the member states and some sort of competition for good results. This is something where any East Asian RIA could improve its international standing significantly, or could lose it if milestones were not kept without there being sanctions. Noncompliance without costs would stigmatize East Asian RIAs as paper tigers and would never impact on financial markets' assessments. Ideally, commitments on implementation should be based on fundamental rules, such as they should be self-binding and provide accountability, predictability, protection against time inconsistencies and "short-term passions," and "suicide" prevention (with ex ante fixed cooling-down periods), to be ensured by a constitution (Elster 1994). This is a state that even the EU has not yet achieved, as the failure of the Constitutional Treaty to find acceptance in France and the Netherlands has witnessed. Yet, at lower levels, the European Court can monitor and set sanctions for noncompliance.

Any sort of sanctions for noncompliance in East Asian RIAs (provided commitments are binding) would be helpful just because this is their major lacuna.

d) Multilateralization of bilateral arrangements

East Asian RIAs are essentially bilateral and differ from each other. Due to the fact that they are all still at the FTA level and that member countries maintain different levels of import duties against third countries, rules of origin (ROO) matter a lot. They matter especially in sectors with a large offshore assembly potential, such as the automobile sector, which is also sensitive in partner countries, like the EU. There are a number of EU-based companies that produce cars in East Asia using CKD (completely knocked down) plants. EU countries' governments try hard in negotiations to avoid disadvantages for these plants that result from the bilateral FTAs of East Asian countries with Japan, which is the most important car exporter in the region. To minimize the trade costs arising from the protectionist enforcement of ROO, bilateral ROO could be integrated into an umbrella agreement with so-called cumulative and diagonal ROO (the latter comprising nonmember countries of an FTA, such as in the EU Generalized System of Preferences with cumulative ROO for ASEAN member countries).[12] Baldwin (2006b) recommends the EU procedure of multilateralizing ROO (the so-called Pan-European Cumulation System, PECS) as a second-best alternative for East Asian countries that do not want to abandon bilateral or subregional RIAs in favor of MFN-based multilateral agreements.

e) Supranational company laws

East Asian regional integration and cooperation has always been accompanied (perhaps also influenced) by private sector initiatives. Each public scheme has a companion organization on the private sector side consisting of senior business leaders such as the Pacific Basin Economic Council (PBEC) for APEC or the ASEAN-CCI (ASEAN Chambers of Commerce and Industry) at the ASEAN level, for instance.

The EU offers an even more far-reaching alternative for the private sector: the European Company Law used recently by the German insurance company Allianz. Submitting companies to a supranational company law signals both the scope of business of a multinational company and its legal anchoring in its major region of business activity. It may be widely premature for East Asia to think of an East Asian company law. However, the private sector could establish working parties to propose elements and procedures needed to initiate a process of harmonizing national company laws in the region.

Similar endeavors could be started with respect to national tax laws, again departing from the (difficult) process of indirect tax harmonization in the EU.

[12] For a description of various EU different rules of origin, see http://www.ecdpm.org/Web_ECDPM/Web/Content/Navigation.nsf/index2?readform& http://www.ecdpm.org/Web_ECDPM/Web/Content/Content.nsf/0/F58ABF0BDF233FEAC12570DC0049AC9F? Open Document.

6 Concluding Remarks

Extending East Asian of regional integration attempts from the subregional to the region-wide level has widely increased the heterogeneity of potential member states. "True" regional integration has not become easier than for the Southeast Asian early starters in ASEAN.

This explains the "noodle bowl" syndrome of sophisticated and untransparent rules that, however, seem to be ignored by the private sector by just not applying for preferences. Costs of "non-use" seem low but this should not give rise to complacency on the part of East Asia. Benign neglect of preferences or even explicit "non-use" is a strong signal for international financial markets that a minimum level of institutionalized regionalism including the political will to surrender national sovereignty has not yet been reached. This is critical, as the major impulse toward RIAs in East Asia still seems to be coming from external pressure, primarily from the financial sector.

As a second-best alternative to multilateralism, which is unlikely to be successful after the disappointing suspension of the Doha Round in mid-2006, the current state of RIAs in East Asia could be improved. Even if European institutionalized regionalism rooted in the Western tradition of stateness will never be taken as a blueprint for East Asia's integration, some general lessons from Europe can be considered. This paper has discussed a few and—given the very divergent stages of integration in Europe and East Asia—has concentrated on more general rules and procedures rather than on detailed sector specifics. The more these rules are accepted, the more sector specifics, will appear on the agenda (but not vice versa).

Finally, while Europe also offers lessons for disappointments and delays, especially in recent years, one of the most encouraging experiences is that EU regional integration has been an irreversible process. This is something that in East Asia, where gradualism and patience is widely recognized will be seen as a genuine European asset.

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