

Regionalism, Asian style

Its uniqueness in a global context is being substantially market-driven

BY STEPHAN RICHTER
& JOHN WEST

Despite its current problems, the EU is often considered to be the gold standard for countries working together for peace and prosperity. While there are many types of regionalism in the world — North America has NAFTA, South America has Mercosur, Australia and New Zealand have Closer Economic Relations — Asia is seen as a latecomer.

This is actually the time for a perfect role reversal: Today's Europe needs to embrace Asia's original private-sector orientation, while Asia now needs Europe's starting point of using trade to overcome difficult history.

What is unique about Asian regionalism in a global context is that it has been substantially market-driven. This move started in 1985, following the Plaza Agreement to revalue the yen, when many Japanese companies began offshoring labour-intensive manufacturing activities to lower-cost destinations, such as the Asean countries of Southeast Asia and China.

Soon after, Hong Kong, Korea, Singapore and Taiwan followed suit in offshoring production. The region's value chains for electronics, automobiles, clothing and footwear and other products were thus gradually established.

In the first phase, the final products of these value chains were primarily sold to US, European and Japanese markets. However, ever since the 2008 Lehman shock and the subsequent financial crisis, there has been an acceleration of regional integration. China, in particular, became a more active



Filepic of a farmer working in a paddy field under the power lines near Nam Theun 2 dam in Khammouane province, Laos. Filepic of the skyline of Singapore's central business district. Asia is diverse in terms of level of development from rich Singapore to very poor Laos, but it has not stopped Asian nations from working together towards peace and prosperity. **Photo by Reuters**

trading and investment partner of all Asian countries.

With the rising purchasing power of Asia's middle class, Asia's value chains are now increasingly servicing Asian consumers. Today, some 40% of East Asian trade takes place within the region, compared with 30% two decades ago.

In Europe, the percentage of trade that is conducted within the region already amounts to 69%. The goal for East Asia should be to move dynamically into the same percentage range.

Given the current level, that would require at least a 50% increase in the share of regional trade. That seems entirely feasible, given the growth and population dynamics of the wider region. Consider also that this by no means implies any "decoupling" from other global markets, or specifically the US market.

It just foreshadows a trading world where Asia completes the

process from initially being an outsourcing destination for multinational corporations to becoming the key growth driver of the global economy. Such a broadening of Asian nations' trade portfolio would be a win-win situation for Asia.

The European example shows that such an intensification of trade within the region also has important spillover effects into fields other than trade. Doing business with each other ultimately is the best instrument with which to build what most of Asia seems to strive for — better neighbourly relations. Trade ultimately is the best confidence-building measure.

Compared to the model Europe pursued, Asia has had the distinct advantage that it did not put the cart before the horse. Its regionalism has been market-led — and thus started out with emphasising the right path for creating the basis for shared prosperity in the region. Unlike in

Europe, Asian governments have arguably followed, rather than led, this process.

That does not mean, however, that governments don't have an important role to play. One concrete example where they can achieve something transformative is discussions of a possible FTA between China, Japan and Korea that have been underway for some time.

Another example concerns relations between South Korea and Vietnam. The two nations, very much on opposite ends militarily during the Vietnam War, are now slated to sign a bilateral free trade agreement by year's end.

That kind of forward-looking pragmatism should be an inspiration to other nations across Asia. A particularly crucial economic dimension where this should play out, given the size of both economies, is in the trade relationship between Japan and South Korea, two coun-

tries that have continued to see their difficult pasts haunt their future. Will South Korea follow Vietnam in putting progress first?

The history-healing aspect aside, the cross-cultural understanding that trade connections foster are also pivotal for Asia's future.

Asia is undoubtedly more diverse than Europe — whether in terms of level of development (from rich Singapore to very poor Laos), politics (from democracy to dictatorship and everything between), economics (free markets to state capitalism and more), or religion (Buddhism, Hinduism, Islam, Christianity, Shintoism and more). In fact, diversity is the very definition of Asia.

But this diversity has not stopped Asian countries from working together for prosperity and peace. And over time, market-led regionalism has proven its value and is now progressively becoming more institutionalised.

The evidence to date suggests that Asia's experience in regionalism has been very successful. Almost seven decades ago, in the midst of the Cold War, no one could have imagined Asian countries working together as they are doing today.

Asia's regionalism is most certainly a work-in-progress, but it is progressing step-by-step. And while it showed the European Union the importance of basing regionalism on the private sector as a driving force, Asia can now take a decisive step forward by emulating Europe's past focus on governments working with each other to overcome the spectres of the past.

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Stock markets set to take off as Europe, Asia abandon austerity

BY ANATOLE KALETSKY

THE Great Divergence is a term coined by economic historians to explain the sudden acceleration of growth and technology in Europe from the 16th century onward, while other civilisations such as China, India, Japan and Persia remained in their pre-modern state. This phrase has recently acquired a very different meaning, however, more relevant to global economic and financial conditions today.

Early last year, the International Monetary Fund published in its World Economic Outlook an article analysing "The Great Divergence of Policies" around the globe since the 2008 crisis. The article pointed out that "exceptionally accommodative" monetary policies designed to stimulate recovery were being counteracted by "unusually contractionary fiscal policies" in every

advanced economy, first in the eurozone and Britain, later in the US and Japan. More recently, financial markets have become obsessed with another "great divergence." Allianz Global Investors, parent company of Pimco, the world's biggest bond fund, described it like this in "Navigating the Great Divergence": "With the Fed(eral Reserve) pondering rate hikes and the ECB (European Central Bank) launching new stimulus...investors are faced with divergent influences from [monetary policy]. Investor concerns are diverging on both sides of the Atlantic."

Why should businesses and investors care about this lexicography? Because by the time an economic trend has become an analytical cliché, it is usually over — and sometimes a counter-trend has already begun.

The Great Divergence — both

between fiscal and monetary policy and between the US and other countries — is a case in point. The important trends today, especially after October policy changes in Japan and Europe, are not divergence but convergence.

This Great Convergence of macroeconomic policies between the US and the rest of the world will drive financial markets and dominate business conditions in the year ahead. It is not yet reflected, however, in asset prices or market trends. Investors continue to obsess about the tiny gap that may or may not open up between US and European policies sometime next year, when the Fed starts gently raising interest rates.

Far more important than a likely difference next year of a quarter or half a percentage point between short-term interest rates on both sides of the Atlantic, though, is the

convergence of economic philosophies and objectives for the first time since the 2008 economic crisis. In the past two months, Japan, Europe and China all moved toward further aggressive monetary stimulus and reversed previous commitments to fiscal austerity.

Though it is true that these global policy shifts coincided with the end of the Fed's quantitative-easing programme, this accident of timing does not imply that the US is diverging from Europe and Asia. What is really happening is that Europe and Asia are finally — and reluctantly — following Washington's road map out of the Great Recession.

In the eurozone, Britain and China, hawkish central bankers have been silenced and monetary policy has been reset for full-scale stimulus — most recently by the ECB, which has belatedly accepted the principle of US-style quantita-

tive easing. In Japan, where money-printing presses were already running at full throttle, they have speeded up even more.

The budgetary consolidation planned in Japan and the eurozone has been abandoned — discretely in Italy, France and Britain, where the government will confirm a massive budget slippage this Wednesday, or spectacularly in Japan, where Prime Minister Shinzo Abe has called a snap general election to confirm his political victory over the austerity-minded ministry of finance bureaucrats who were insisting on another tax hike next year.

The upshot is that every advanced economy is now following broadly the same macroeconomic policies as the US: maximal monetary stimulus combined with fiscal neutrality and the suspension of counterproductive budget rules.

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