
An ASEAN+6 Economic Partnership: Significance and Tasks

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[Main Points]

- An economic partnership of the members of the Association of Southeast Asian Nations plus Australia, China, India, Japan, New Zealand, and South Korea, which is known as the ASEAN+6 group, would accelerate economic growth in East Asian countries, promote cooperation in energy, foods, and other fields vital to economic activities, and in other ways greatly benefit Japan and the region's other countries. By adding Australia, India, and New Zealand to the ASEAN+3 group (ASEAN plus China, Japan, and South Korea), the ASEAN+6 framework produces a group with a number of significant merits, including a larger market scale and increased resource supply capacity.
- The key to the formation of an ASEAN+6 economic partnership may be the moves made by India, which has a very large population and tremendous growth potential. India has been pursuing economic reform since 1991, but compared with the countries of East Asia, it still has many domestic regulations and external barriers, which constrain the freedom of economic activity. India also has numerous problems in infrastructure and other areas vital to economic development. Within the ASEAN+6 framework, not just governments but also actors on the private-sector level need to extend cooperation in human resource development, infrastructure, and other areas.
- Japan, which strongly endorses an ASEAN+6 economic partnership, needs to play a leadership role to bring about the partnership's realization, making contributions in a variety of forms including personnel and funding. On the external front, Japan should ask that Australia, India, and New Zealand be invited to join the meetings taking place in the ASEAN+3 framework, and it should also newly organize ASEAN+6 meetings. On the domestic front, Japan must promote the opening and reform of its agricultural sector so that it can promote an ASEAN+6 free trade agreement.

Introduction

The regional framework known as the ASEAN Plus Six, which consists of the 10 members of the Association of Southeast Asian Nations plus Australia, China, India, Japan, New Zealand, and South Korea, took concrete shape at the first East Asia Summit in December 2005. Before that, the grouping called the ASEAN Plus Three (ASEAN plus China, Japan, and South Korea) had been promoting regional cooperation to deal with such issues as the Asian currency crisis, which broke out in 1997. Specifically, the group staged summit meetings of leaders and organized a variety of other ministerial meetings and sectoral conferences as venues to promote energetic activities. Talk of holding an East Asia summit moved to the fore in this context, and at the urging of Japan, which received backing from such ASEAN members as Indonesia and Singapore, the event was organized as an ASEAN+6 summit rather than an ASEAN+3 affair.

Japan has subsequently been working constructively to promote the enlarged group as an economic cooperation framework. In concrete terms, it put forward the concept of an East Asian version of the Organization for Economic Cooperation and Development (OECD)—the Economic Research Institute for ASEAN and East Asia (ERIA)—and it has earnestly promoted intellectual support including policy proposals aimed at the realization of sustainable economic development in East Asia. In addition, in 2007 Japan established a research group to stimulate discussion on the formation of a Comprehensive Economic Partnership in East Asia (CEPEA), which would have the ASEAN+6 countries as members.

While the ASEAN+3 is engaged in a variety of activities, the ASEAN+6 is just now moving into action. In light of this situation, this report examines the significance and merits of adding Australia, India, and New Zealand to the framework for regional cooperation in East Asia, making it an ASEAN+6 grouping. The report pinpoints tasks relevant to broad-based cooperation and integration in Asia and gives consideration to how they should be handled. Below, in the first section of this introductory chapter to the report, I review the evolution of economic relations in East Asia in recent years, with a focus on trade and investment in the ASEAN+3. My aim is to facilitate understanding of the features of the ASEAN+6 group, which is the main theme of the report. The second section introduces the analyses contained in the respective chapters of the report, and the third section advances proposals to the Japanese government.

1 East Asia's Shift from Market-Led to Institution-Led Regional Integration

1.1 Regional integration led by the market

Until the countries of East Asia were hit by the crisis of 1997, a number of them were

undergoing the dazzling economic growth known as “the East Asian miracle.” With their high growth rates, these nations successfully attracted vast quantities of foreign capital. The crisis arose on account of the inefficient use of this capital due to, among other factors, the fragility of domestic financial markets. Breaking out first in Thailand, the crisis spread contagiously into many other East Asian countries. The region’s economies recovered rapidly, however, with help from the introduction of appropriate measures to remedy weaknesses in financial markets and other causes of the crisis. Export growth driven by a global upturn also assisted the recovery.

Brisk direct investment and trade played key roles in both the high-tempo growth before the crisis and the swift recovery from it. An inward flow of direct investment promotes capital investment, production, and employment in the recipient country, and working through technology transfer, it lifts the country’s technological level, which also plays a key role in economic development. Direct investment works in such ways to accelerate growth in recipient countries. The inflow of such investment into East Asia caused a major expansion of trade, which made high-tempo growth possible.

The multinational companies that advanced into East Asia using direct investment as a medium constructed regional production and distribution networks. Flows of parts and intermediate goods grew larger between home offices and overseas subsidiaries and also among overseas subsidiaries. The work within the regional production networks culminated in the assembly of final products, most of which were exported to the advanced countries of North America and Europe, as well as to Japan. In the background of the construction of regional production networks lies a fragmentation strategy based on the multinational corporation’s separation of production processes to optimize siting. When the items being produced have numerous components, as in the case of machine-made products, a company can effectively make use of a fragmentation strategy, which splits apart the production processes so that each component will be produced in the country or region where it can be manufactured most efficiently.

The formation of regional production and distribution networks in East Asia led to a rise in each country’s dependence on trade with other East Asian countries, thereby boosting regional economic integration. The degree of intraregional dependence in East Asian trade has risen. When the region is defined as the 10 ASEAN members along with China, Hong Kong, Japan, South Korea, and Taiwan, interdependence climbed from 43% in 1990 to 53% in 2006. Over the same period, interdependence rose only from 38% to 44% in the area of the North American Free Trade Agreement (NAFTA), while it lessened slightly from 67% to 66% in the 25 members of the European Union. In this light, we may appreciate that economic integration has progressed quite rapidly in East Asia.

Policies to liberalize trade and direct investment have made a major contribution to this regional integration in East Asia, which has been mediated by trade and investment. This liberalization has facilitated smooth functioning of the market mechanism, leading to the formation of production and distribution networks and progress in regional integration. With the economic integration in East Asia proceeding in this fashion, it has been termed a market-led type of regional integration. Though in this way trade and investment policies have been substantially liberalized, they have ample room for further liberalization. Indeed, further liberalization is indispensable for sustaining and promoting economic growth. Countries also have other tasks to tackle, including improvement of infrastructure, in order to attract investment.

1.2 The shift to institution-led regional integration

Moves to establish free trade agreements (FTAs) became active around the world in the early 1990s, but East Asia did not initially show much interest. In fact, until Japan and Singapore concluded an FTA in November 2002, the only major FTA in the region was the ASEAN Free Trade Area (AFTA). The original six members of ASEAN (Brunei, Indonesia, Malaysia, the Philippines, Singapore, and Thailand) established AFTA in 1993, and the other four members (Cambodia, Laos, Myanmar, and Vietnam) joined the area in the second half of the 1990s, making it a free trade area of 10 countries. ASEAN is also working on FTAs with countries outside of Southeast Asia. There has been much talk in recent years about the FTA between ASEAN and China; ASEAN also has an FTA with South Korea that has gone into effect, and it has reached a final understanding in its talks with Japan. In addition, it is working on an agreement with India. Many ASEAN members, meanwhile, are separately concluding their own FTAs.

Compared with Southeast Asia, where ASEAN is active, there was initially little enthusiasm for FTAs in Northeast Asia, where China, Japan, and South Korea are situated. In recent years, however, the situation has changed. Japan's policy until the late 1990s was to pursue trade liberalization mainly within the multilateral framework overseen by the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO). In those days the government was not in favor of FTAs. Its interest gradually grew stronger, however, in a situation where WTO negotiations were making little progress and FTAs were quickly spreading in many of the world's regions. Japan's first FTA, which is an economic partnership agreement (EPA) with Singapore, went into force in November 2002. Following that, Japan put into effect an EPA with Mexico in April 2005, an EPA with Malaysia in July 2006, an FTA with Chile in September 2007, and an FTA with Thailand in November 2007. At the present time (November 25, 2007), Japan has also signed FTAs with the Philippines and Indonesia, reached a final understanding with ASEAN, and entered into negotiations with such

prospective partners as Australia, India, and Vietnam.

China and South Korea are also actively promoting FTAs. After joining the WTO in 2001 and securing access to the world's markets, China worked out an FTA with ASEAN, which went into effect in July 2005, as a stepping stone to a comprehensive economic partnership. Beijing is strongly advocating this partnership so as to realize not just free trade but also cooperation in economic development. It is actively promoting FTAs at present with the aim of securing export markets and resource supplies, and it also hopes to strengthen friendly relations. Among the FTAs South Korea is promoting, the one that has attracted the most attention is its agreement with the United States, which was signed in June 2007. South Korea had been expected to have trouble with the need for liberalization in agriculture and other areas, but in the end, while excluding rice from the agreement, it was able to promote liberalization for other farm products. Being eager to assure and improve access to the world's big markets, it is currently negotiating an FTA with the EU.

Free trade pacts embracing the East Asian countries are also being examined. China and South Korea are in favor of an agreement covering the ASEAN+3 group, while Japan is promoting the aforementioned CEPEA, which would reach the ASEAN+6 group more broadly. The two concepts are not necessarily mutually incompatible, but since each has different prospective members and supporters, they are not being promoted in partnership.

A variety of reasons lie behind the rise of interest in FTAs among East Asian countries. One is that agreements of this sort are rapidly proliferating around the world. The accumulated number of FTAs reported to GATT between 1948 and 1990 was 27, but it swelled to 62 over the five years from 1990 to 1995, the year of the WTO's establishment. Thereafter the trend gained further momentum, with the number of FTAs rising to 104 in 2000 and 194 as of October 2, 2007. A second reason is the Asian crisis. The East Asian countries that were engulfed by the crisis found that they were unable to secure the level of assistance they hoped for from countries outside of the region, and this demonstrated the importance of regional cooperation to prevent the occurrence of another such crisis. While the cooperation projects underway in East Asia are of various types, it has come to be appreciated that FTAs can serve effectively to expand trade and investment.

Promotion of domestic reform may be cited as a third reason for the rise of interest in FTAs. While the response to the Asian crisis is also involved here, East Asian countries have succeeded in realizing fast economic growth by pursuing a course of liberalization and domestic reform. Recognizing the need for further liberalization and reform to push development to yet higher levels, they have selected the option of the

free trade agreement as a means to achieve this end. A fourth reason is the relations of rivalry that exist within the East Asian region. Particularly in the case of China and Japan, which have been competing over leadership in the region, FTAs are seen as a tool for strengthening relations with countries in Southeast Asia and elsewhere.

2 Significance of and Tasks for an ASEAN+6 Economic Partnership: Chapter Summaries

2.1 Economic effects of an ASEAN+6 FTA

Liberalization of trade and investment is moving forward rapidly in the countries of the ASEAN+6 group. This has facilitated high economic growth in the countries of East Asia by encouraging foreign companies to make direct investments and construct intraregional production and distribution networks, which has led to trade expansion. Despite these steps taken in the direction of liberalization, however, many countries still have high trade and investment barriers. China, India, and Vietnam, for instance, continue to apply high tariff rates on average. The first chapter of this report presents a simulation using a general equilibrium model of the economic effects in a case where the ASEAN+6 members conclude an FTA and remove tariffs on trade with each other. The free trade agreement that is being considered for the region covers more than trade liberalization. It is to be a comprehensive pact also involving investment liberalization, unification and mutual recognition of each country's product standards, trade facilitation including measures to streamline customs procedures, investment facilitation including measures to shorten investment screening procedures, and economic cooperation. For this reason, the simulation was premised on not just trade liberalization, but also trade and investment facilitation and economic cooperation.

The results of the simulation indicate that an ASEAN+6 FTA would boost gross domestic product by 2.11% in the group's member countries. Within the group, the increase in GDP would be particularly large among the ASEAN members. In the region at present, separate FTAs that join one outside member to ASEAN are being concluded, such as the ASEAN plus China and ASEAN plus South Korea agreements. Consideration is also being given to an agreement covering all of East Asia, such as an ASEAN+3 FTA. For comparison with the ASEAN+6 FTA scenario, results for a set of six ASEAN+1 FTAs and for an ASEAN+3 FTA were also simulated. The results confirm that an ASEAN+6 FTA would lead to the most economic benefits for the ASEAN+6 countries. Since there is considerable resistance to trade liberalization in the agricultural sector, another simulation excluding agriculture was also performed. The finding was that from the standpoint of overall economies, benefits are maximized when an FTA is applied to all sectors, agriculture included. However, it was also found that

depending on the industry, trade liberalization might come at the cost of reductions in production and employment. It is to be desired for this reason that governments, in order to minimize the adjustments costs of lost jobs, implement temporary measures to supplement income and improve skills.

2.2 The ASEAN+6 group's growing economy

In order to analyze the significance of and tasks for an economic partnership adding Australia, India, and New Zealand to the ASEAN+3, we need to have a good grasp of the ASEAN+6 economy. The second chapter examines the realities of this economy. With growth moving forward at full speed in China, India, and elsewhere, the ASEAN+6 economy is gaining importance in the world economy. Measured using dollar-denominated GDP statistics, this economy grew by 1.3 times over the 10 years from 1995 to 2005. (When the sluggish Japanese economy is excluded, the economy grew 2.1 times larger.) When we recall that the Asian currency crisis of 1997 dealt a severe blow to many East Asian countries, the expansion appears even more remarkable. Because of Japan's stagnation and its large presence in the ASEAN+6 economy, the group's share of world GDP contracted from 26.9% to 22.6%. But when Japan is excluded, we find that the world GDP share of ASEAN and the other five countries increased from 9% to 12.4%.

Earlier I noted that dependence on intraregional trade has risen in the ASEAN+3 group. When Australia, India, and New Zealand are added to the picture, discrepancies grow larger. Australia and New Zealand have a relatively high level of reliance on intraregional trade in the vicinity of 55%, but India's is at a low level under 30%. In commodity trade with ASEAN+3 countries, there are large shares of energy exports from Australia, raw material exports from India, and farm product exports from New Zealand. On the import side, all three countries have large shares of machinery. In their trade with each other, the ASEAN+3 countries have large shares of manufactured products and parts in both exports and imports, and machinery has been incorporated into intraregional production networks, but at this stage Australia, India, and New Zealand have not been drawn into these networks. An analysis of the composition of exports and imports in commodity trade shows that Australia and New Zealand have a complementary relationship with the ASEAN+3, but in India's case such a relationship is not clearly evident.

After encountering a crisis in 1991, India embarked on an economic reform program including trade liberalization, and it substantially lowered tariff rates. But its rates are still far higher than those of the other ASEAN+6 countries, particularly Australia and New Zealand, with which it is compared in this report. Obviously it has

considerable room for trade liberalization. It appears that Australia, India, and New Zealand could all realize greater economic growth by strengthening their ties with the ASEAN+3. On the side of the 13 countries of the ASEAN+3, moving closer to these three countries would help them to secure mineral resource supplies and expand sales in the Indian consumer market. A constant market share (CMS) analysis of export expansion factors shows that for the ASEAN+3, the widening of export markets to the ASEAN+6 would increase the components of market composition. That is, the composition of the export market would tend to move in a direction promoting exports. For the ASEAN+3, then, an ASEAN+6 economic partnership would presumably be desirable.

2.3 Trade and investment barriers in India and Australia

Collaboration in a variety of areas is conceivable in an economic partnership covering the ASEAN+6 group. The centerpiece of the partnership would be a free trade agreement. Chapter 3 gives consideration to trade and investment policies in India and Australia from the viewpoint of the significance of and tasks for an ASEAN+6 FTA.

For many years India followed a protectionist course, but ever since the reforms of 1991, it has been liberalizing trade and direct investment, and the tempo of trade liberalization was accelerated in 2000. The country still has complex tariff and nontariff barriers, however, giving it ample room for further liberalization. Even as trade has been liberalized, moreover, there has been a sudden increase in the imposition of antidumping duties, which have become a substitute for tariffs as a tool of protectionist policy. Australia, meanwhile, has low tariff barriers; with the exception of some industrial goods, it does not apply high tariff rates. Like India, however, Australia frequently imposes antidumping duties, and it has a quarantine system that acts as a nontariff barrier to food imports.

On the investment front, India is taking a phased approach to expanding the areas in which investments can be made, but it remains a market in which the activities of foreign companies are constrained, with limits on the capital shares of domestic companies they can acquire and the expansion of operations they can undertake after moving into the country. Australia is liberalizing its policy toward foreign capital, but it requires prior approval when investments exceed a certain size. One of the tasks for it to address is a regulatory setup that leaves room for discretionary decisions on granting approval when business ventures do not conflict with national interests.

India and Australia have entered into some free trade agreements with individual East Asian countries, but the scope of the trade liberalization differs considerably between them. Whereas Australia's FTAs provide for wide-ranging

liberalization, India's provide for liberalization only for specified products. A study of the effects of their respective FTAs with Thailand confirms that trade has greatly expanded among products that have been exempted from tariffs in the two agreements.

If an ASEAN+6 FTA comes into being, the region's countries will gain improved access to the huge and much-discussed Indian consumer market, and Indian participation in East Asia's production networks will be accelerated. Australia, meanwhile, is a major supplier of primary products to the Asian region, and intraregional trade would be stimulated by the application of the cumulative provision of the rules of origin and other arrangements to these products. If the FTA were a comprehensive agreement including investment liberalization, relations of the foregoing sorts with both India and Australia would be further strengthened.

2.4 Commodity trade and East Asian production networks

Earlier I commented on the existence of East Asia's production networks. In the context of rapid growth, foreign-owned corporations have led the way in network construction. Chapter 4 contains a detailed analysis of the status quo and future possibilities in the relationship between India and the East Asian production networks.

East Asia's share of India's trade is growing larger, but the share is still quite small compared with the shares in the countries of East Asia. These countries are engaged in brisk intraindustry trade (horizontal trade) with each other centered on trade of manufactured products. In the trade between India and East Asia, by contrast, interindustry trade (vertical trade) assumes a more prominent position, with India exporting primary products and East Asian countries exporting machinery. Trade of parts plays a prominent role in the trade within East Asia, but it accounts for only a small share of the trade with India. In short, this is because India has not been incorporated into the East Asian production networks. On the Indian side, there are several overlapping reasons for this, including (1) the long distance from East Asia, (2) the delay in moves to attract foreign direct investment, (3) the history of an import-substitution policy, and (4) the delay in upgrading infrastructure. It should be noted, though, that in some industries India is now becoming involved in production networks, as shown by the large expansion in the trade of computer and automobile parts between India and East Asia.

In the strategies they pursue toward India, many Japanese companies make use of bases they have set up in Southeast Asia. From the viewpoint of foreign companies, setting up operations in India is an attractive proposition not just because of the anticipated market expansion but also because of the rising technological level and other environmental improvements on the supply side. In fact, moving into India can provide

an opportunity for rethinking regional and global strategy. From India's perspective, various tasks need to be tackled in order to engage in East Asian and global networks, which generally are centered on foreign companies. For instance, tariff and nontariff barriers need to be lowered or dismantled; an environment congenial to foreign capital needs to be prepared; and physical infrastructure needs to be improved. If India makes use of an FTA framework in its pursuit of trade and investment liberalization and facilitation, it can realize great benefits. And if Japan, in addition to working on the formation of an FTA, cooperates in the improvement of Indian infrastructure, making use of official development assistance (ODA), there will be favorable effects for both countries' economies and their diplomatic relations.

2.5 Trade in services: A pattern of diversity

One of the prominent trends in recent years in the world economy and international economic relations is for trade in services to grow larger. In the background are such factors as deregulation and liberalization of the service sector and expansion of service economy activities. Because service trade is assuming greater importance in many of the ASEAN+6 countries, chapter 5 examines the realities of this trade within the group and the tasks for its expansion.

Travel and transport services command a prominent place in the service trade of many East Asian countries, but a feature of the Indian trade is the extremely large share of computer and information services. Exports of information technology services can be broadly broken into three categories: (1) software services; (2) IT-enabled services (ITES, a type of business process outsourcing featuring such services as call centers and medical record processing); and (3) R&D services, such as for product development. At present the first category of software services is the largest, but the second category of IT-enabled services is quickly growing. On account of the language barrier and other factors, Indian companies have traditionally engaged in business transactions mainly with Western companies, but recently, taking advantage of swelling demand, they are doing more business with Japan, China, and other East Asian countries. It is possible for India's firms to join in the East Asian production networks by using computer and information services to develop deeper ties with this region. Another recent trend not limited to India is for trade in medical services to expand. This trade is occurring not just because medical costs are low in some countries but also because efforts have been invested in fostering skilled and experienced doctors.

Travel services occupy a major position in the service exports of Australia. Many educational services are included in this category, and the Australian government has been energetically promoting them. One of the features of these exports is the key

role played by offshore campuses of Australian schools, which enable students to in effect study at an Australian university without leaving their home country. East Asian students account for a large share of the international students in Australian schools, and many of them are enrolled in programs of the offshore type.

A number of steps can be taken to expand service trade. Tax treaties can be concluded to eliminate discriminatory tax measures; qualifications for special occupations (such as technicians, doctors, accountants, engineers, and architects) can be mutually certified, harmonized, and unified; and credits in the educational field can be mutually recognized. It is to be desired that all such measures be implemented under an ASEAN+6 FTA.

2.6 Possibilities for energy cooperation

Oil and other energy prices have recently been rising. A phenomenon of excessive global liquidity is one of the factors in the background, in addition to the rapidly rising demand for energy to support high-paced economic growth in China, India, and elsewhere. Economic growth cannot be achieved without stable supplies of energy. Based on this understanding, chapter 6 presents an examination of the energy situation and tasks in the ASEAN+6.

Australia, India, and New Zealand differ in their energy portfolios, but basically all three are countries with a rich endowment of energy resources other than oil. Australia in particular stands out as one of the few energy exporters among the members of the OECD. India and New Zealand are both net energy importers, and have energy self-sufficiency ratios of 78.0% and 72.2%, respectively.

Adding Australia, India, and New Zealand to the framework of East Asian cooperation would be significant in a number of respects. It would enhance the region's bargaining power vis-à-vis the Middle East, Russia, and other energy producers by expanding the scale of the energy market; it would lift the self-sufficiency ratio (and the intraregional dependence level) for coal and natural gas; it would stimulate reform in energy markets; and it would expand the cooperation options for responding to emergencies, conserving energy, and implementing environmental measures (making use of, for instance, the Asia-Pacific Partnership on Clean Development and Climate [APP] and the International Energy Agency [IEA]). As for tasks, meanwhile, mention can be made of the growing likelihood that the demand for energy will expand, that reliance on oil imports (and the Middle East) will rise, that environmental loads will grow heavier, and that China and India will step up their energy diplomacy and energy acquisition rivalry.

Because of the rise and volatility of oil prices and the increasing gravity of environmental problems, all countries are keenly eager to suppress energy consumption, and are instituting measures toward that end. The programs each is pursuing play an important role in their efforts to strengthen energy security and improve the environment. If one country's measures to promote its energy strategy become overly exclusive, however, tensions and conflicts with other countries may arise, and that could become a factor damaging the country's energy security.

Energy cooperation in East Asia has been gathering momentum recently. This cooperation is going forward through such mediums as East Asia summits, the APP, the Asia-Pacific Economic Cooperation forum (APEC), a five-nation energy ministerial meeting between China, India, Japan, South Korea, and the United States, and the Japan-Indonesia FTA. Active participation by Australia, India, and New Zealand in such regional cooperation would make a contribution to the sharing of information, promotion of stockpiling, and cooperation to use energy efficiently.

2.7 Prospects for stable food supplies

As a result of abnormal weather thought to be caused by global warming, frequent floods and droughts are destabilizing food production. And as a result of industrialization and urbanization accompanying economic development, the area of farmland in developing nations is shrinking. At the same time, population growth is causing global demand for food to increase. Under the circumstances, apprehensions have arisen over the stability of food supplies. Chapter 7 contains an analysis of the agricultural and food circumstances of the ASEAN+6 group, and it gives consideration to policies to realize stable food supplies.

Agricultural and food issues change considerably when you shift the framework in which they are viewed from the ASEAN+3 to the ASEAN+6, which adds Australia as a major exporter of agricultural products, New Zealand with its decisive comparative advantages in dairy products, and the broad territory of India, which is engaged in various kinds of agriculture. Agricultural trade reflects each country's balance of agricultural production and consumption, and Australia, New Zealand, and India are all net exporters. India's excess of exports is to some extent a result of failed agricultural policies, and the country's capacity to export is likely to decline as domestic consumption expands under the impetus of population growth and rising income levels. Australia and New Zealand, however, should continue to be exporters of farm products. Japan and South Korea are now and will continue to be net importers. China's exports and imports are at present more or less in balance, but the likelihood is that the nation will become a net importer as a result of industrialization and economic growth, which

will boost demand for food. The ASEAN+6 in this way has a mixture of farm-product exporting and importing countries, and yet the level of intraregional dependence in this category of trade remains low. This suggests that agricultural trade is likely to expand within the region and that the level of dependence will move up.

The first chapter confirmed that an ASEAN+6 FTA would have economic merits for each of the group's countries, which would realize gains in GDP and economic welfare. The construction of this agreement and the liberalization of agricultural trade would cause intraregional trade to expand and intraregional food self-sufficiency to rise. This would facilitate stable supplies of food. The realization of an FTA is being made difficult, however, by agricultural and food production protectionism in importing countries. Agricultural liberalization is indispensable in order to realize the economic merits of an ASEAN+6 FTA and gain greater stability in food supplies.

The key to the promotion of this liberalization will be for Japan, which is the group's largest importer, to liberalize its imports and open up its market. In its FTA negotiations thus far, Japan has applied a strategy of excluding agricultural products from liberalization, but that is not a course that will lead to a free trade agreement for the ASEAN+6 group. Japan should instead use a variety of measures to pursue liberalization. In place of excluding agricultural products from agreements, it could establish periods for the reduction of their tariffs differing from the periods applied to other products, and instead of promising to cut tariffs to zero by a certain date, it could propose that a new round of talks begin once tariffs have been cut to some specified level. Structural reform of agriculture must be implemented at the same time the market is opened to imports. If this sort of mixed policy is pursued, Japanese agriculture will be able to make the most of its technological prowess. The road will open to an industrial agriculture that is friendly to the environment, and the farm sector can be shifted from a protected position to an aggressive one.

2.8 Business opportunities in the vast Indian market

A vast market is forming in India, which has a huge, still-growing population and an economy that is expected to develop steadily. Chapter 8 presents an analysis of India's future market and discusses the tasks involved in realizing the market's potential, with a focus on how cooperation in the ASEAN+6 framework can address the tasks.

When we view the scale of the Indian market by income group, we find that consumers with substantial purchasing power, or people in the middle and high income groups, have a 7%–8% share of the population at present. The situation in China is much the same. What this means is that if we measure only people in income tiers with

purchasing power equivalent to consumers in the developed countries, which is the group the companies of these countries are interested in, China has about 100 million people, India about 70 million. The expansion of the ASEAN+3 to the ASEAN+6 would thus provide the group with a new Indian market about 70% of the size of the large Chinese market. When we forecast trends in income groups using projections for population size and economic growth rates, we find that in 2030 India's middle and high income groups will have population shares of 45.8% and 6.3%, respectively, giving the country a truly gigantic market. Economic growth is forecast to continue at a very fast pace, and it will turn latent demand into real demand for automobiles, household appliances, mobile phones, and other such products, causing the market to grow much larger.

The Indian market does not have generally high value-added levels and does not readily lend itself to the pursuit of selection and concentration by the developed nation's companies. It is a very hard market to handle for many Japanese companies, which are striving to expand supplies of high-value-added goods and services. Even so, if Japanese firms continue to adhere to a passive posture toward business operations in India on the grounds that only low value added can be realized at present, they will lose the chance to benefit from the enormous demand the market will be generating. With the markets in Japan and other industrial nations approaching maturity, it is hard to think of any other market to concentrate on if the Indian market, with its great potential, is rejected at the selection stage. In the world to come, there is likely to be an increase in markets of the Indian type, which while having low prices offer possibilities for quantitative expansion. A key managerial issue for firms in Japan and elsewhere in East Asia will be securing a larger share in markets of this type.

In order to encourage active Indian involvement in the ASEAN-6 group, it will be important for the group's members to cooperate in finding solutions to India's infrastructure inadequacies, educational needs, and other such structural issues. Group members other than India will reap benefits from these efforts to actualize the latent demand in the vast Indian market, enhance the sustainability of the Indian economy's development, and boost the market's expansion.

2.9 Prospects and tasks for the Indian economy

Over the past 25 years the Indian economy has steadily grown at annual average rates of 5%–6%, and this pace of growth accelerated after the economic reform of 1991. Although the country had great growth potential, including a wealth of human resources and considerable industrialization experience, it also had rigid systems of permits and licenses, which blocked the tapping of this potential. The reform program has taken the

form of deregulation and trade liberalization, which has enabled the market mechanism to function and business activities to become brisk. Initially economic growth was led by the service sector, especially IT services, but recently some new developments have provided growth with additional vigor. These developments are the activation of the industrial sector, the expansion of saving and investment, and the advance of globalization.

Many people are inclined to take a rosy view of the Indian economy's future in light of the presence of growth-inducing factors, such as a beneficial demographic profile and a large pool of talented human resources, but there are numerous issues that need to be resolved for the realization of high-level growth that can generate jobs and reduce poverty. Among the particularly critical tasks are full-fledged deregulation and improvement of governance, especially at the level of regional governments. It is true that systems of industrial permits and licenses have largely been removed, but sugar, oil refining, fertilizers, pharmaceuticals, and others fields are still subject to economic controls. Reform of the labor market has also not made much progress. With respect to the issue of governance, there are serious problems of corruption in government, and efficient management is also being frustrated by government control over sectors that play a vital role in economic development, including agriculture, education, health, sanitation, and infrastructure. Inadequacy of infrastructure is presenting severe bottlenecks in such areas as roads, railroads, airports, and electricity.

Subsequent to the economic reform of 1991, India embarked on an outward-oriented course of economic development in order to take advantage of the opportunities presented by the ongoing process of globalization, and calls have also been made for a "Look East" policy to reap benefits from relations with the fast-growing East Asian region. In response, East Asian countries have stepped up trade with and direct investment in India. Within the region, China and South Korea in particular have rapidly developed trade and investment relationships. The response by Japan was slow, but recently it has finally begun to appreciate the importance of India as a country with a vast market as well as merits as a production base, and Japanese companies are showing signs of making a full-scale advance into the country, particularly in the industries of automobiles and electronic machinery.

India has shown considerable interest in the concept of an ASEAN+6 FTA and is actively seeking to get involved in it. For Japan and the other countries of East Asia, the merits of a free trade agreement encompassing India would include the potential of its large market and the abundance of its highly talented human resources. For the conclusion of an FTA and other regional agreements, there needs to be a deepening of mutual understanding, which can be assisted by personal exchanges through a variety of channels. It will be important to eliminate the psychological distance separating India

from East Asia.

2.10 Political and economic tasks for an ASEAN-6 economic partnership

Cooperation within the ASEAN+3 group in a variety of fields began to make progress in 1997, on the occasion of the Asian currency crisis. It was in this context that construction began on an ASEAN+6 framework, with Japan taking the initiative. In concrete terms, the construction led in 2005 to the East Asia summit and in 2007 to moves to realize the CEPEA and ERIA concepts. The analysis in chapter 10 uses the vantage point of international relations for a study of the background to the establishment of the ASEAN+6 framework and the tasks involved in the framework's promotion.

The conceptualization of the ASEAN+6 framework was the product of interrelations among international factors, especially factors within the East Asian region, and domestic Japanese factors. Among the international factors were four structural changes on the regional level that have become conspicuous since the turn of the century. These are (1) strengthening interest in regional integration, (2) the rise of China on the economic and diplomatic fronts, (3) involvement in East Asia on the part of Australia, India, and New Zealand, and (4) the development of East Asian regional organizations.

Among the domestic Japanese factors, one is the emergence of apprehension concerning the growing strength of China's involvement in East Asia. This concern was aroused in part by China's proposal in November 2000 for a free trade agreement between it and ASEAN. Two actors that play a key role in the shaping of Japan's foreign strategy are the Ministry of Foreign Affairs (MOFA) and the Ministry of Economy, Trade, and Industry (METI), and while they hold opposing views on quite a few matters, they were in agreement on the view that the best strategy to pursue in East Asia is not an ASEAN+3 approach, which China favors, but an approach centered on the ASEAN+6 group. MOFA, viewing the situation from a perspective of politics and diplomacy, and METI, viewing it from an economic perspective, share the recognition that what is best for Japan is not a Chinese-led ASEAN+3 arrangement, and that an ASEAN+6 orientation is of importance.

The ASEAN+3 and ASEAN+6 approaches are now being pursued in parallel, but whereas there are some 50 meetings that have been organized for the ASEAN+3, including summit meetings, basically only a summit exists for the ASEAN+6. It is conceivable that the ASEAN+3 could be merged into the ASEAN+6, but that would not be likely to proceed without a hitch. For regionalism to function usefully in a framework like the ASEAN+3 or the ASEAN+6, the officials in charge of trade,

industry, finance, and other affairs need to form networks with their counterparts in the region's countries, making use of a variety of related meetings and working groups, and they also need to construct mechanisms on multiple levels for an intimate exchange of information. If the governments of East Asia establish more networks for exchange among their respective ministries and agencies, both at home and with their counterparts abroad, a sense of solidarity will be born among the region's officials within the complex setting of political and economic maneuvering by Japan and China, and this will facilitate the promotion of policy interests shared by all the participating countries. In a region such as East Asia, where differences of opinion and clashes of interests over the promotion of regional cooperation are still prominent, it is particularly desirable that such arrangements be fully developed.

When we focus on economic affairs, we can see that it is important to realize market integration by means of free trade agreements, but for the creation of the ASEAN+6 FTA Japan is promoting, other FTAs must also be established. Those under negotiation with Australia and India need to be completed, and an FTA with China should also be concluded. Furthermore, for the purpose of reducing or averting a backlash from the United States, which has strong influence in Asia, against the moves to build an ASEAN+6 framework, it will also be desirable to encourage the conclusion of bilateral FTAs between the United States and the East Asian countries. From this perspective, it will probably be wise for Japan to consider the possibility of an FTA with the United States.

3 Proposals: Tasks for Japan for the Promotion of an ASEAN+6 Economic Partnership

The establishment of an economic partnership within the ASEAN+6 framework centered on a free trade agreement would not merely boost GDP and enhance economic welfare in Japan and the other ASEAN+6 countries, but it would also have other merits including greater stability in energy and food supplies. The scale of these merits would be larger than those arising from an economic partnership within the ASEAN+3 framework. This is because the ASEAN+6 framework includes India, a country whose growing population and developing economy hold the promise of offering a supply of capable labor and a vast market, and it also encompasses Australia and New Zealand, major supplies of food and energy.

In this way there is much that could be expected from an economic partnership for the ASEAN+6 group. At present, however, all that has happened toward its realization is that East Asia summits got off to a start in 2005, the idea of ERIA—the Economic Research Institute for ASEAN and East Asia, an East Asian version of the OECD—was put forward in 2007, and work began on creating CEPEA, the

Comprehensive Economic Partnership in East Asia, also in 2007. Naturally it behooves Japan, as the country taking the initiative in the realization of the ASEAN+6 economic partnership concept, to cooperate in the creation of an FTA, doing whatever it needs to do in the fields of energy and foods, as discussed in this report. And in areas not directly addressed in the report, such as the environment and education, Japan should not just constructively promote discussion but also extend concrete cooperation, such as by supplying personnel. In specific terms Japan, working with the other ASEAN+6 countries, should allocate personnel and funds for full-fledged implementation of the ERIA and CEPEA concepts, and Japan and the countries backing it should urgently request the inclusion of Australia, India, and New Zealand in the meetings and projects underway within the ASEAN+3 framework. In addition, the establishment and efficient operation of a secretariat function will be vital for effectively promoting an economic partnership within the ASEAN+6.

Even though an ASEAN+6 FTA would be the centerpiece of the economic partnership and Japan ought to be taking the lead in bringing it into being, Japan is not playing a leadership role on account of strong opposition within the domestic agricultural sector, where people fear that trade liberalization would be likely to harm them. In fact, in bilateral FTAs with Southeast Asian countries, Japan has avoided opening up the farm sector by offering instead to provide cooperation in the agricultural field. Such a strategy is workable in the case of Southeast Asia, because there Japan is dealing with developing nations, but it will not pass muster in the FTA talks now underway with Australia, a developed nation. Liberalizing the farm sector cannot be sidestepped.

The debate on agricultural liberalization tends to dwell excessively on the damage that may be incurred, but if appropriate measures were worked out, this damage could be limited. More than that, a bright future for Japanese agriculture will come into view by promoting structural reform in tandem with liberalization. One way to minimize the damage from opening up the farm sector would be to move ahead first with liberalization in areas that are relatively competitive and to work later on areas that are not. In point of fact, many FTAs provide for different tempos of liberalization depending on the sector. In this case, however, it will still be necessary to set up a schedule for liberalization and to institute measures in keeping with this schedule. For workers who are forced into unemployment, support needs to be extended in the form of temporary income compensation and re-education and re-training programs, which will help jobless workers improve their skills for securing productive jobs.

Agricultural liberalization has to be coupled with structural reform of the sector. Inefficiency in the agricultural sector is the cause of the protective farm policy. Protective policies are put into place to meet the demands for them, which employ the

argument that protection is required on account of the sector's inefficiency. But buffered by these policies, the sector only becomes increasingly inefficient, and even stronger protection becomes necessary. In order to get liberalization going, the ability of agriculture to compete has to be strengthened. Structural reform paves the way for this by, for example, enabling the use of farmland in productive ways and improving managerial efficiency.

Japan can make a major contribution to rosy prospects for itself and its neighbors in East Asia by moving forward on liberalization and structural reform in the agricultural sector, taking the initiative in the creation of an ASEAN+6 FTA, and extending cooperation in the energy and food fields. Because an economic partnership including a free trade agreement will entail temporary sacrifices along the road to a brighter future, its realization will depend on strong leadership by farsighted government leaders and the support of the people.

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