

Services Trade on the Road to the ASEAN Economic Community

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The Member States of the Association of South East Asian Nations (ASEAN) have set themselves the ambitious aim of establishing a region-wide economic community by 2015. In striving to achieve this objective, there are strong reasons, both internal to ASEAN's internal integration process and linked to the region's deepening ties with a dense layer of external economic partners, to believe that service sector reforms, and trade (and investment) in services more particularly, will occupy a place of choice in the region's policy priorities.

The region's rapid economic advance and the steady rise in living standards achieved in recent decades have been anchored in a growth model assigning to external demand and insertion in global (regional) value chains, particularly in manufacturing, dominant roles. Such progress could not have been possible without marked improvements in the efficiency with which the region's underlying services infrastructure has sustained productivity growth in downstream industries. Such efficiency gains, however, have primarily resulted more from unilateral policy benevolence than from concerted collective action initiatives. The ASEAN Economic Community (AEC) Blueprint spells out a comprehensive set of treaty-based objectives through which Members States aim to work together in freeing up trade and investment in services under the ASEAN Framework Agreement on Services (AFAS) and the ASEAN Comprehensive Investment Agreement (ACIA).

The road to the AEC confronts ASEAN Member States (AMS) with the numerous (and simultaneous) challenges that other successful middle income emerging nations are also contending with in a world of heightened production fragmentation. These include the need to move up value chains and escape the "middle income trap" through continued improvements in product and process innovation and sustained gains in labor productivity. It also entails coping with the demographic transition that significant improvements in living conditions tend to usher in while also addressing the derived demand for enhanced social safety nets. It also implies responding to increasingly assertive middle class demands for the improved delivery of a range of services with public good characteristics, such as health, education, transportation, press and internet freedoms.

Moving forward, ASEAN Member States have little choice but to rebalance what for most of them will be continued high dependence on external markets with more endogenous sources of (consumption-based) growth. Such rebalancing of essence

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entails a shift, already well underway in a majority of (but not all) Member States, towards a more service-centric development model.

In responding to the above challenges, ASEAN Member States face the additional task of devising policy paths flexible enough to accommodate and reconcile steep gaps in income levels and implementation capacities across the regional grouping. The region's long-standing practice of promoting deeper integration in a progressive manner and on the basis of variable geometry approaches should continue to serve it well. Such flexibility will prove especially important given that service sector reforms and trade raise complex issues of regulatory convergence and approximation for which the strengthening of regulatory institutions and enforcement capacities are critical ingredients.

As ASEAN Member States enter the home stretch leading to the realization of their agreed 2015 EAC objectives in the services field, two distinct challenges will likely need to move up the regional policy agenda.

A first challenge concerns the need for ASEAN Member States to update their collective rule-book under AFAS. This should be done in a manner analogous to the major facelift performed in the investment field a few years ago through the adoption of ACIA.

ASEAN Member States cannot arguably meet the deep integration targets they have set for themselves in services trade without revisiting the incomplete and outdated set of rules governing services trade among them. An exercise aimed at embedding a number of best practices in services regulation, many of them practiced already by ASEAN as a whole and by individual Member States under various preferential agreements entered into with key trading partners since AFAS was devised in 1994, is overdue and could anchor the region's deep integration process with a modern and comprehensive set of disciplines rooted in the economic realities of IT-driven trade in tasks.

A second pressing challenge is to raise the bar higher on the services liberalization front. Despite the genuine progress achieved in the various market opening packages pursued (but not always fully implemented) under AFAS to date, the region continues to maintain a high overall level of restrictiveness in services trade and investment (see Figures 1 and 2 below) that not only contradicts the stated aims of realizing an economic community but also acts as a potentially punitive tax on region-wide economic efficiency. The fact that ASEAN Member States wish to cap *intra-ASEAN* foreign equity limitations at 70% in the context of a *completed* EAC (rather than 100%) sums up such policy ambivalence, a stance paradoxically taken with regard to the most important mode of supplying services.

Figure 1. Services Trade Restrictiveness Index (STRI)*: Regional Comparison

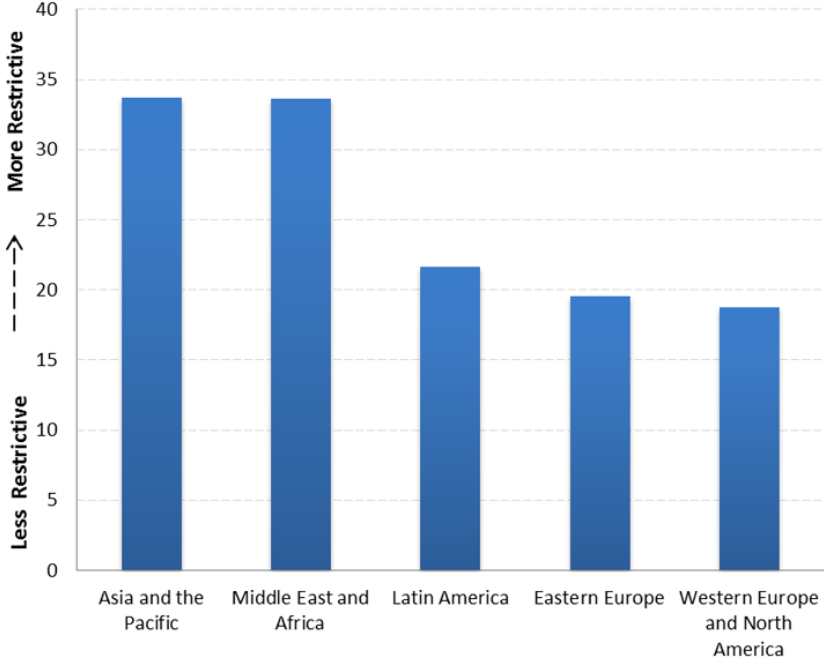
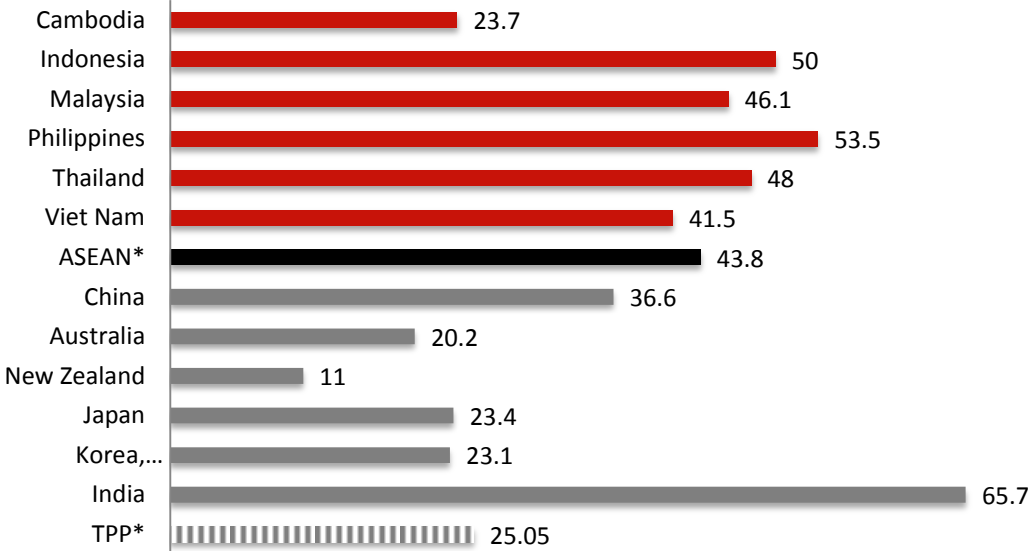


Figure 2. Overall Services Trade Restrictiveness Indices: ASEAN* and Major Partners



*Index figures range from 0 (fully closed market) to 100 (fully open market). Data for ASEAN and TPP excludes Singapore.

Source: World Bank, Services Trade Restrictiveness Index database, available at www.worldbank.org

Meanwhile, care will need to be taken in ensuring that the multiplicity of external liberalization initiatives pursued by ASEAN collectively (e.g. RCEP) and by individual Member States (e.g. TPP, EU-Malaysia) in the services field do not afford third countries better access to ASEAN markets than that enjoyed by ASEAN Member States under AFAS. In revising AFAS, Member States may wish to include an MFN clause targeted at avoiding such a risk and at spreading regionally agreed liberalization benefits with greater automaticity.

A final observation concerns the adequacy of the institutional architecture that ASEAN Member States have decided to assign to the realization of a region-wide economic community in a field where obstacles to market integration stem from domestic regulatory conduct.

ASEAN's institutional architecture is a (deliberate) far cry from the supranational forms of pooled regulatory governance and policed liberalization practiced in the European Union in pursuit of a single market for services. The latter construct has rested on the constant interaction between the various "freedoms" embedded in the Treaty of Rome, the adoption of a series of horizontal and sector-specific liberalizing Directives initiated by the European Commission, as well as on the arbitral decisions taken by the European Court of Justice and by EU-wide competition authorities in striking down national measures deemed inconsistent with the Single Market's stated aims.

In pursuing deeper market integration in services markets within ASEAN, the AEC Blueprint affirms the collective desire of AMS to limit their services toolkit to only the first of the EU's market opening arsenal. The lessons from the (still far from complete) six decade-old process of services liberalization in Europe suggest that ASEAN Member States will need to brace themselves for occasional bumps along the road to an integrated services market so long as they fail to align in a coherent manner the policy instruments and enforcement means to effect meaningful market opening. A tangible illustration of the latter point can be seen from the lack of traction generated to date under the seven (otherwise welcome) mutual recognition agreements negotiated by ASEAN Member States in selected professional categories in the absence of an implemented complementary agreement on the movement of natural persons, without which the potential gains from recognition agreements simply cannot be harnessed.

This latter point underlines the need to look at the AEC as a long-term journey in services liberalization, with 2015 as an important, if far from final, step along a path likely to be characterized for some time by significant learning by doing externalities and confidence building as the ASEAN Economic Community progressively takes shape in an environment of marked diversity of incomes, capacities and collective preferences.