**Forum:** Advisory Panel On The Question of South-East Asia (APQSEA)

**Issue:** Strengthening regional economic growth among the ASEAN states in order to withstand the volatility of the global economy

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**Introduction**

The Asian Financial Crisis in 1997/1998 and the Sub Prime Mortgage Crisis that rocked the global economy in 2007 roused some vital and pertinent fears about the likelihood of such disruptions in the global economic equilibrium repeating in the future. Decreased global consumption of goods and services, coupled with debt-ridden governments in the Balkans and North America resulted in decreased aggregate demand, giving rise to recessionary quarters and sustained increase in food prices over time. The west bore the brunt of this phenomenon, with effects including but not limited to, repeated quarters of negative economic growth, cyclical & structural unemployment, and stagflation.

Many developing countries, including the ASEAN\(^1\) nations, however, until recently, fared well amidst this global economic disequilibrium, presenting robust economic growth in a time of economic austerity. Yet, in 2010, at the ASEAN summit meeting, Secretary General, Dr Surin Putsiwan expressed concern at the reduction in annual economic growth of the ASEAN region, down from 6.7% in 2009 to 6.2% in 2011. While this reduction may seem marginal, its significance has been felt in the farthest corners of South East Asia, with structural unemployment at a 4 year high in Vietnam and an increase in inflation witnessed in Laos from 4.875% in 2008 to 7.5% in 2011. Critics have argued that while the cause of diminished economic performance within the ASEAN states can be attributed to the global economic slowdown, with decreased demand from the west for raw materials abetting this situation, the ASEAN should strive to formulate appropriate economic and trade policies in an attempt to gain place as a more influential production base in the competitive global market. Dr Putsiwan recently argued for the cooperation for ASEAN member nations in a bid to implement strategic methods of regional integration, producing the end result of a more self sustained regional economy, less vulnerable to global economic mood swings. The solution is not as simple as it seems, as many variables have to be considered, such as political popularity, regional acceptance, economic costs as well as environmental ramifications.

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\(^1\) Experts should be aware of the distinction between ASEAN and Asian. The two terms may not be used interchangeably
Definition of Key Terms

Economic Growth

An increase in the value of the Real GDP of an economy over a set period of time, Analogously, economic growth could also be defined as the increase in the real value of goods and services produced in an economy.

GDP

Final value of the total goods and services produced in an economy, in a given fiscal year, regardless of who owns the factors of production which lead to the production of the particular good or service. It can also be expressed in a componential form: C + I + G + (X-M) wherein, C refers to consumption, I refers to investment, G refers to government spending and X-M refers to net exports (Exports- Imports_)

ASEAN

Association of South-East Nations, is a geo-political and economic group of sovereign nations situated in Southeast Asia with common aims of accelerated economic growth, social progress, cultural development between nations and protection of peace and stability, among others. ASEAN covers a land area of 4.46 million km², which is 3% of the total land area of Earth, and has a population of approximately 600 million people, which is 8.8% of the world’s population. In 2011, its combined nominal GDP had grown to more than US$ 2 trillion.

Regional Integration

It is a process wherein states enter into a regional agreement in order to enhance regional cooperation through regional institutions and rules. The objectives of the agreement could range from economic to political to environmental, although it has typically taken the form of a political economy initiative where commercial interests have been the focus for achieving broader socio-political and security objectives, as defined by national governments. Regional integration has been organized either via supranational institutional structures or through intergovernmental decision-making, or a combination of both. Examples include ASEAM, SAARC, NAFTA.

Global Economic Volatility

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2 Elie Tragakes, Economics for the IB Diploma, 2011
5 An Introduction To Trade: World Trade Organization Press 2009
6 Investorpedia, Economics Definitions, 2010
It refers to global swings from booms to recessions and vice versa. Fluctuation in prices of goods and services are a component of global economic volatility. For example, Oil, a highly price volatile good, reached an 5 year low during 2008-2009 (insufficient demand), after wherein due to market based corrections in the global economy, the price of oil increased. Economic volatility also foster business insecurity and negative economic sentiments, thereby engendering decreased aggregate consumption and investment.

**Capital Flight**

It occurs when money or assets rapidly flow out of a country due to an event of economic consequence. Such events could be political instability, increase in taxes or government defaulting on its debt, among others.

**Background Information**

The advent of integrated networking and communication processes has engendered “economic globalization” a phenomenon that has led to enhanced connectivity and international integration amongst nations worldwide. As economies become more integrated with each other, they indirectly become co-dependent on each other. Gradually, the physical distance between the East and the West is being diminished and the idea of a singular global economy becoming more apparent. Yet, one should not disregard the negative economic consequences of economic globalization; the economic stagnation of the West, primarily in the United States and Europe, starting from 2007, slowly drizzled its way to the East, adversely influencing the regional economic growth of the ASEAN. Decreased economic growth had for some years not been a primary concern of the ASEAN, as the economic performance of its member nations was prodigious, relative to that of other nations in Asia, Europe and North America. Yet, as the ASEAN become more economically integrated with the West and the rest of the world, economic fluctuations in the latter affected the former, and as Dr Surin Putsiwan acknowledged, (Refer back to Introduction) regional economic growth decelerated within the ASEAN. The following is a list of explanations, not exhaustive however, which appropriate the economic liaison between the ASEAN and the global economy: (includes Africa, Europe & N&S America)

1. **Reduced demand for major export goods**

   As the West and concurrently a large proportion of the global economy entered a recession, these economies reduced their demand for raw materials and food such as rice, garments, gypsum among others in order to save money during such times of economic uncertainty.

   ASEAN member nations, primarily rely on semi-manufactured and primary goods such as the

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7: The Development of Freedom, Amartya Sen, Republished in 2012
ones mentioned previously for income on exports, experienced a reduction in income from this reduced demand. As exports decreased, the (X-M) component of GDP reduced thus consequentially leading to a reduction in GDP growth or economic growth.

2. Rice Price Fluctuations

Rice is a major export for ASEAN nations. However the reliance on rice as a major export varies across the ASEAN spectrum, with Myanmar, Laos, Vietnam, Cambodia and Thailand deriving a significant proportion of export revenues from rice, forming an average of 15.3% of all exports. Singapore, Indonesia & Malaysia, on the contrary, derive very little export revenue from rice, contributing to less than 2% of exports. Regardless, repeated fluctuation in rice prices incurs menu costs as well as adjustment costs in the private and public sector. This contributes to an overall decreased profit in rice exporting firms, also disincentivizing to continue production, thus reducing overall export and hence reducing economic growth. Volatility of rice prices also contributes to food insecurity and dissuades investment in the secondary sector of the country.

3. Negative global business confidence

As the global economy lies in disarray, investors tend to save money or invest in low risk sectors, where returns are guaranteed. The ASEAN has only recently started to gain prominence as an investment hotspot, and is not globally considered to be a safe investment zone, a misconception generated by lack of investment in the previous years by the West. Investors may also consider the option of saving in a period of economic difficulty, rather than investing at all, as interest rates would be increased during recession (monetary policy tool used to combat inflationary pressure and recession) and the cost of borrowing would not suffice the return of the investment.

4. Capital flight from ASEAN states

The aftermath of the 1997/1998 Asian financial crisis was marked by capital flight from the ASEAN nations, Capital flight occurred in a number of ways: MNC’s operating in the ASEAN nations, closed their operations following the Asian Financial Crisis, as business confidence plummeted and profitability was unsatisfactory. Secondly, domestic investors also moved their investments outside of the ASEAN region to tax havens and more secure economies such as Luxembourg, Liechtenstein. According to World Bank statistics, approximately 56 billion USD of capital flight and resource reallocation was experienced by Indonesia, Thailand, Vietnam and Singapore between 1997-2002.

Major Countries and Organizations Involved

ASEAN
The issue essentially deals with the responsiveness of the ASEAN in order to mitigate the effects of global economic volatility on the economic performance of its member nations. Hence each and every member of the ASEAN is equally pertinent in this matter, as in the end only cooperation between all members would ease the process of drafting appropriate economic policies in order to combat this issue. The list of all permanent ASEAN members as of June 2013 is: Indonesia, The Philippines, Malaysia, Singapore, Vietnam, Thailand, Myanmar, Laos, Cambodia and Brunei Darussalam.

WTO

The WTO has been instrumental in abetting the development of the trade policies of the ASEAN, since its inception. The ASEAN has also always had a vocal position at the WTO, when discussing tariffs and duty free quotas on behalf of all South East Asian nations and many developing countries. As of 2013, the WTO has made many recommendations to the ASEAN in order to combat this issue and is viewed by the ASEAN as a key partner in drafting trade & economic policies for the latter.

USA, UK other MEDC’s

These economies are the ones that have most strongly experienced economic volatility in the past decade. They also house a major proportion of the MNC’s and investors that invested in the ASEAN economies prior to 1997 and post 2002. It is imperative that these economies amend their current economic policies as to prevent any future economic upsets that may or may not affect the ASEAN and other nations in the future.

Timeline of Events

<table>
<thead>
<tr>
<th>Date</th>
<th>Description Of Event</th>
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<tr>
<td>1961</td>
<td>Formation of ASEAN</td>
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<tr>
<td>1982</td>
<td>Formation of ASEAN Free Trade Area (AFTA)</td>
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<td>1997/1998</td>
<td>Period of Asian Financial Crisis</td>
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<td>1997-2002</td>
<td>Period marked capital flight from ASEAN economies; worth up to 56 billion USD</td>
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<tr>
<td>2007 onwards</td>
<td>Period marked by global Financial crisis</td>
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<td>2010</td>
<td>Recognition of reduced economic performance by ASEAN Secretary General at ASEAN summit</td>
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Relevant UN Treaties and Events

- (A/RES/39/29)- Recognizing the need for Global Economic reforms in the wake of the recent financial crisis

Previous Attempts to solve the Issue

Considering the fact that the issue at hand is relatively recent, no direct solutions have been proposed by any of the stakeholders. Yet, the ASEAN has expressed concern over this issue and aims to deal with it effectively in the near future, as mentioned by Dr Surin Putsiwan in 2010 at the ASEAN Global Summit in Danang.

Possible Solutions

Taking into account the differences in the political and market structure of every nation in the ASEAN and the uncertainty of global economic volatility, it would be imprudent to state an optimum solution exists, agreeable to all. Yet, equitable solutions do exist, rendering maximum possible benefit to every nation. Prospective solution are given as follows:

Solutions

1. Strengthening and greater implementation of the ASEAN Free Trade Agreement-

The ASEAN Free Trade Agreement was signed in 1982 in a bid to support local manufacturing within the ASEAN states. As a part of the AFTA, the Common Effective Preferential Tarriff (CEPT) scheme was initiated, as a means to promote self-sustainable regional economic growth in the ASEAN. The CEPT scheme essentially dictates minimal or zero tariff on import of selected goods within the ASEAN, and a relatively higher tariff on goods imported from outside on the ASEAN. The CEPT hence effectively aims to make the ASEAN self reliant in the long run, devoid of major dependence on imports from the west, an economically sensitive area whose unpredictable economic fluctuations (with regards to demand, capital flight etc.) have a deleterious effect on the ASEAN nations. While the CEPT is established theoretically and should be adopted by all the ASEAN states, each member nation has implemented the CEPT on their own accord, and to a varying degree. During the boom of 2005/2006, the ASEAN economies experienced unprecedented growth and they took this as a incentive to lax the CEPT. However a reduction of economic growth witnessed from 2009-2011, should serve as a tale of caution to the ASEAN and member nations should aim to proactively implement the policy

2. Diversification of export and import markets
Many of the ASEAN states export and import a significant proportion of their goods from a country or a small group of countries. This leads to a high concentration ratio of exports and imports, thus making the states dangerously dependent on the few countries for trade. ASEAN members such as Indonesia, Brunei and Thailand export and import more than 40% of their goods from Europe and North America. This may be undesirable in the long run, as these trading partners (Europe and North America) experience economic volatility, a phenomenon that may cause them to decrease their demand during a recession and hence decrease export income for the ASEAN. An appropriate solution would be diversifying and spreading out the export and import markets, i.e. exporting and importing from a greater variety of markets. This would help spread the risk in case of a global economic meltdown and provide the ASEAN cheaper goods.

Bibliography

6. ^ People's Agenda for Alternative Regionalisms. "About PAAR. What is the Initiative People’s Agenda for Alternative Regionalisms?