

The Next Stage of ASEAN Integration: Liberalization of the Services Trade

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ASEAN needs to sustain its dynamism

- Has 10 member countries with total population about 500 million people
- Founding member, known as ASEAN-6: Brunei, Indonesia, Malaysia, Philippines, Thailand and Singapore
- New members: Cambodia, Lao PDR, Myanmar and Viet Nam
- ASEAN is a region that had attracted large FDI and home to a regional production network established by multinational companies (MNCs)
- ASEAN also plays an important role in East Asian regional integration e.g. ASEAN+3 and ASEAN+6 initiatives
- ASEAN Vision 2020 – transforming the region into a stable, prosperous and highly competitive region with equitable economic development and reduced poverty and socio-economic disparities
 - **economic integration** (formation of a single market and production base) is a critical element of this Vision



ASEAN Economic Integration

- In 1976 ASEAN introduced a system of preferential tariffs to encourage regional trade in goods but it was not effective
- ASEAN also introduced regional industrial projects, with regional governments as investors. This initiative was also not successful
- Regional economic integration began with the formation of the **ASEAN Free Trade Agreement (AFTA)** in 1993
- Other regional economic integration initiatives:
 - **ASEAN Framework Agreement on Services (AFAS)** – liberalization of services trade
 - The Framework Agreement on ASEAN Investment Area (AIA) – free flow of investments



Progress of AFTA (1)

- Lowering tariffs through the Common Effective Preferential Tariff (CEPT) scheme
- In 2007, ASEAN-6 (Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand) and Viet Nam have reduced import duties on all products to 0-5%
- Exceptions - Products in Sensitive and Highly Sensitive Lists have a longer period for tariff reduction
- ASEAN-6 will eliminate duties on all products by 2010



Progress of AFTA (2)

- Lao PDR and Myanmar are expected to reduce tariff rates by 2008, Cambodia is given until 2010
- Cambodia, Lao PDR, Myanmar and Viet Nam are required to eliminate duties by 2015, with some flexibilities for some sensitive products by 2018
- Elimination of non-tariff trade barriers such as import quotas and import licenses
- Simplification of the rules of origin for imports
- Improving trade facilitation e.g. custom procedures
- Harmonizing product classification nomenclature



Was AFTA successful in creating a single market in ASEAN?

- Significant progress has been made in lowering import duties and removing trade barriers
- Intra-regional trade has increased but this can be partly due to the MNCs production network
- Some industrial restructuring has taken place e.g. the emergence of Thailand as the regional automotive centre
- But, the regional economies are still not fully integrated, e.g. no free flow of capital and economic integration limited to only a few countries
- The development gap between ASEAN-6 and the newer members is still wide



Intra-Regional Trade Share, 1995-2006 (%)

Region	1995	2000	2001	2002	2003	2004	2005	2006
ASEAN (10)	21.1	22.7	22.2	22.7	24.4	24.4	24.9	25.7

AFAS: liberalization of the services sector

- AFAS liberalization launched in 1995 is modeled after the WTO General Agreement on Trade in Services (GATS)
- Offers for services sectors for liberalization are made on a non-reciprocal basis
- AFAS has entered into its 6th Package of Liberalization commitments
- Faster liberalization for 11 priority sectors
- Signed one Mutual Recognition Arrangement on nursing

Malaysia: AFAS commitments (6th Package)

No	Sector	No. sub-sectors committed
1	Air transport	3
2	Maritime transport	8
3	Tourism	12
4	Business services	33
5	Construction services	7
6	Financial and insurance services	4
7	Telecommunication services	23
8	Distribution services	1
9	Education services	7
10	Healthcare services	3
11	Recreational services	2
12	Environmental services	1
13	Other services	1
	Total	105

Evaluation of Malaysian Commitments

- The sectors offered for liberalization are very much in line with Malaysia's services sector strategy and strength.
- Greater offer of liberalization in business services, telecommunication, tourism, maritime transport, construction and education services
- Liberalization of services involved exports and imports of services, establishment of foreign services companies and movement of workers
- Degree of liberalization of services trade
 - Significant liberalization is made on exports and imports of services
 - But there are still limitations on foreign equity on services companies
 - There are also limitations on movement of workers

Liberalisation According to Services Modes

- Mode 1 (cross-border transmitted services e.g. electronically transmitted architectural design): liberalised because technically it is difficult to restrict trade
- Mode 2 (consumption abroad e.g. tourism): liberalised because wants to encourage consumption of services in home country
- Mode 3 (commercial presence e.g. foreign banks) : does not bound liberalisation commitments and restrictions are in the form of limitations on foreign equity
- Mode 4 (movement of workers): does not bound liberalisation commitments and the liberalised movement of workers is limited to skilled workers only

Assessment of AFAS – Study by Thanh and Bartlett (2006)

- Services sectors offered by ASEAN countries in AFAS are more than the offerings made under GATS (overall 50% more by 4th package)
 - But for some countries, the AFAS liberalization was only marginally better than their GATS commitments
- Improvement are made in transparency and predictability but inferior to that of GATS
- Although has achieved wider bound liberalization than GATS and has removed some trade restrictions, there still significant differences in level of liberalization among member countries.
- Limited regulatory convergence and harmonization among member countries
- The depth of liberalization (as represented by bound commitments) is also poor

Importance of services in ASEAN

- With the rise of China and India, ASEAN needs to accelerate its economic integration and be a truly single market and production base.
- As it is, ASEAN no longer received the bulk of FDI inflow into East Asia
- Increase in intra-regional trade and effectiveness as a production base not only depend on liberalization of trade in goods (AFTA) but also in services (AFAS)
- Thus, the next stage of ASEAN integration must focus on **services liberalization (AFAS) because it is behind the progress made in liberalization of trade in goods (AFTA)**

Services is important because.....

- To increase economic competitiveness by securing efficient services that will give high quality and lower cost
- To support goods trade –
 - Singapore, Thailand, Malaysia made the largest offer for services liberalization
- To facilitate regional production network so inputs can move efficiently between the various production locations, establishment of support industries and availability of skilled workers
- To boost the sources of regional growth – tourism, education, healthcare services

ASEAN Economic Blueprint

- At the Bali Summit in 2003, ASEAN Leaders agreed to establish the ASEAN Community by 2020
 - Has three components: ASEAN Economic Community, ASEAN Security Community and ASEAN Socio-Cultural Community
- **ASEAN Economic Community (AEC)** to be a reality by 2015
- ASEAN Economic Blueprint is the roadmap for AEC by identifying its characteristics and elements with clear timelines
- AEC will established ASEAN as a single market and production base by
 - New mechanism and measures for implementing its existing economic initiatives
 - Accelerating regional integration in priority sectors
 - Facilitating movement of business persons, skilled labour and talent
 - Strengthening institutional mechanisms
 - Address the development divide and accelerate the integration of Cambodia, Lao PDR, Myanmar and Viet Nam

Services Component of the ASEAN Economic Blueprint (1)

Overall strategy - removal of restrictions to ASEAN services suppliers in providing services and in establishing companies across national borders within the region

- More liberalization of services trade
 - Remove all restrictions in priority sectors by 2010
 - Remove substantially restrictions for all other sectors by 2015
- Set the rounds of negotiations – every two years
- Target minimum numbers of new sub-sectors to be offered in each round of negotiation

Services Component of the ASEAN Economic Blueprint (2)

- Deepen the liberalization commitments made, e.g. ASEAN equity holding be liberalized from 51% in 2008 to 70% by 2015
- Compile inventory of barriers by 2008
- Liberalization flexibility through **ASEAN Minus X formula**
- Complete Mutual Recognition Arrangements (recognition of professional qualification) currently under negotiation
- Set parameters of liberalizing movement of services skilled workers

Challenges in liberalization of services

- Timeline of AEC targets is too short
- Even when liberalization were committed, in reality there are many barriers in the form of domestic regulations, e.g:
 - Licenses and permits, technical requirements, burdensome administrative processes to start a business, control on price of services offered, and qualification requirements
- Difficulty in reaching consensus at the domestic level – matching objectives in the Agreement with the reality of domestic reforms
- The negotiation non-reciprocal basis may result in the minimum liberalization because countries could not bargain on their offers

Conclusion



- Services liberalization is crucial for AEC, but
- Difficult to negotiate and implement
- Resistance from domestic services suppliers because of they may not benefit due to lack of capacity
 - Fear of influx of foreign services suppliers
- Difficult to measures if liberalization will produce the desired increase in services trade or it is because of natural growth