

The 'new East Asian regionalism': A political domino effect

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ABSTRACT

10 The proliferation of regional economic agreements involving East Asian economies in the years since the financial crises is usually explained in the political economy literature by reference to economic factors. These agree-
15 ments have been viewed either as a response to the costs of increasing interdependence and/or to the demand by domestic exporters to level the playing field when their rivals benefit from preferential trade agreements. A detailed examination of economic data finds no support, however, for
20 the argument that intra-regional economic interdependence in East Asia has increased significantly since the financial crises. Case studies suggest that business has not played a major role in either promoting or oppos-
ing the agreements – not surprisingly in that the agreements are unlikely to have a major economic impact, and are not being widely used. Rather than there being an 'economic domino' effect at work, the new East Asian regionalism is best understood as being driven by a 'political domino' effect.

KEYWORDS

Regionalism; trade; East Asia; ASEAN; China; Japan; free trade agreements.

25 The regional architecture of East Asia has been transformed in the years since the Asian financial crises of 1997–98. As late as 2000, the region had only one effective preferential trade agreement (PTA) in operation (the ASEAN Free Trade Agreement); by the start of 2009 governments had concluded 45 PTAs and a similar number were under negotiation. From
30 being a laggard in regional trade agreements, East Asia has become the most active site globally for their negotiation (see Aggarwal and Urata, 2006). Two pan-East Asian cooperative arrangements have come into existence – the ASEAN Plus Three grouping, and the East Asia Summit (EAS).

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In addition, governments in the region have engaged in unprecedented collaboration on monetary matters including the creation of a set of bilateral currency swap arrangements (the Chiang Mai Initiative – CMI) and the promotion of domestic and regional bond markets through the Asian Bond Market Initiative and the Asian Bond Fund. 35

Q1 For the purposes of this article, East Asia is defined as the countries participating in the East Asia summit. I follow the recent literature in economics in applying the concept of ‘regionalism’ to all preferential trade arrangements that East Asian countries have negotiated, a set of economic policies ‘that represents a clear break from East Asia’s strong history of multilateralism’ (Harvie, Kimura and Lee, 2005: 3). This article focuses on the new inter-governmental collaboration on trade that East Asian countries have engaged in since the financial crises of 1997–98 and reviews its implications for theorizing about regional integration. I do not address the impact that the proliferation of bilateral/minilateral agreements may have on collaboration organized at the level of the East Asian geographical region (for a cogent analysis see Dent, 2006a). Rather, I focus on the question of what has driven the new enthusiasm of East Asian states for formal inter-governmental collaboration. In doing so, I challenge the principal arguments of a number of contributions that focus primarily on economic explanations of the new regionalism. To assert that economic factors have played no role in the new collaboration would be naïve. The weight of evidence suggests, however, that economic factors in many instances have been less important in the new regionalism than states’ use of economic instruments to pursue political objectives. 40 45 50 55

If economic factors were predominant in states’ decisions to enter into inter-governmental collaboration one would expect to find: (a) that regionalism has been a response to an increase in interdependence and its associated policy challenges, as has been argued by a substantial body of functionalist literature; (b) that inter-governmental collaboration will have concentrated on those relationships that offered the greatest potential economic benefit; (c) that a transmission mechanism existed through which the costs of increased interdependence were translated into policy outputs. Rather than domestic economic actors being the primary driving force behind the new East Asian regionalism, my argument is that it has been a state led process, in which non-state actors were often marginalized. And, in those instances where pro-liberalization non-state actors have played a role in lobbying for the conclusion of a preferential trade agreement, their influence has often been offset by protectionist interests. The dominance of political concerns – manifested both in diplomatic/strategic reasons for choice of PTA partners, and in agreements that have little impact on economic welfare – in turn shapes their impact on domestic interests, and reduces the likelihood that these agreements will pave the way for broader liberalization. 60 65 70 75

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**HAS INCREASED ECONOMIC INTERDEPENDENCE
DRIVEN THE NEW EAST ASIAN REGIONALISM?**

Arguments that increased economic interdependence has driven regionalism have a long pedigree. They rest on various strands of theoretical literature from economics, including those pertaining to the securing of property rights and to the actions required to overcome transactions costs. Functionalist explanations for why governments demand and supply regional institutions continue to enjoy popularity (e.g. Mattli, 1999).

The relevance of functionalist accounts of regionalism for East Asia has long been questioned, however. There the puzzle was to explain the absence of formal inter-governmental collaboration despite the substantial increase in economic interactions among states. East Asia had experienced regionalization without regionalism. Haggard (1997: 45–6) provided one of the most sophisticated accounts: greater economic interdependence in the region, he suggested, simply had not created the collaboration and coordination problems that would have led to a demand for regional institutions (see also Kahler, 1995: 107; Solingen, 2008: 288–9).

Many analysts pointed to the 'market-led' character of Asian integration. Such accounts, e.g. Drysdale (1988), provided a persuasive explanation for the traditional North–South trade (exchange of manufactures for raw materials) that characterized the region through the 1970s. They were far less satisfactory in accounting for the development of a more complex division of labor in the region from the 1980s onwards when exchange increasingly took the form of intra-industry trade, the consequence of a 'fragmentation' of the production process. Government actions actually played a crucial role in fostering this new division of labor.

- First, unilateral action by governments in creating free trade zones and duty drawback arrangements were important in the early incorporation of Korea, Taiwan and then the economies of Southeast Asia into the new division of labor (Warr, 1989). This selective liberalization was followed by a more general unilateral liberalization across Southeast Asia in the second half of the 1980s and the 1990s.
- Second, the coordinated action on exchange rates by the G7 countries following the 1985 Plaza Accord effected a dramatic shift in relative costs of production across the region, encouraging the extension of Northeast Asian production networks into Southeast Asia (Bernard and Ravenhill, 1995; Funabashi, 1989).
- Third, the negotiation of the Information Technology Agreement within the World Trade Organization (WTO) at the Singapore ministerial meeting in 1996 played an important role in freeing trade in the most significant category of Asian exports.

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- Fourth, the further extension and re-orientation of production networks was facilitated by the actions that governments – notably in China and Vietnam – undertook in preparation for their entry into the WTO. 120

Economic integration in Asia has been driven by market forces. But national governments played a decisive role in creating the environment in which businesses could successfully construct transnational supply chains. 125 What was distinctive about the East Asian experience was that these actions occurred at the national and global levels whereas the contribution of *regional* institutions, including ASEAN (Ravenhill, 2008a), to this facilitating environment was negligible.

Many commentators have suggested, however, that the financial crises of 1997–98 marked a critical juncture in regional collaboration in East Asia. 130 The East Asian regional architecture, writes T.J. Pempel (2008: 164), ‘today is more complex, more institutionalized, and more Asian than it was when the crisis struck’. For some authors, this new regionalism has been driven by the imperative of responding to the challenges of increased interdependence, a process that MacIntyre and Naughton (2004: 98) suggest 135 ‘increasingly requires a more structured and binding framework for policy coordination’. Similarly, Kawai and Wignaraja (2009: 5) in concluding that deepening market-driven integration has been ‘first and foremost’ among the factors driving East Asian PTAs, assert that ‘market-driven economic integration has begun to require further liberalization of trade 140 and FDI [foreign direct investment], as well as harmonization of policies, rules, and standards governing trade and FDI’. Munakata (2006b: 29) concludes that in contemporary East Asia ‘the intensity of economic interaction contributes substance and depth and thereby a basis for institutionalized inter-governmental cooperation, including preferential trade 145 agreements’.

The reference in all these pieces is to regionalism more narrowly defined than in the introduction to this article – that is, to inter-governmental collaboration exclusively among East Asian economies. Accordingly, I look 150 first at whether the central premise of these arguments is correct: has interdependence among East Asian economies increased in recent years?

Q2 With the emotive responses that the financial crisis and Western responses to it generated, arguments about the increasing integration of East Asia assumed a symbolic importance: commentators seemed to take 155 pride in suggesting that intra-regional trade in East Asia as a share of total trade had already surpassed the equivalent figure for NAFTA, and was approaching that for the European Union (see, for instance, Asian Development Bank, 2008; Kawai and Wignaraja, 2007: 2).

But has economic interdependence really increased in the years since the financial crisis? It all depends on how the ‘region’ and ‘interdependence’ 160 are measured. If the region is defined as ASEAN Plus Three, that is, the

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10 member states of ASEAN plus China, Japan, and Korea, then the share of intra-regional trade in the 10 economies' total trade rose only from 37.6% in 1995 to 38.3% in 2006 (an increase so small that one might regard it as being within a statistical margin of error, and a final total figure that is substantially below the equivalent for NAFTA) (data from Kawai and Wignaraja, 2008: Table 1).¹ To be sure, production networks and their associated trade within East Asia have been radically re-orientated in the years since the financial crisis. China's rapid economic growth has seen it emerge as a major (frequently the single most important) export market for other East Asian economies (Ravenhill, 2006). But, at the same time, China's own export dependence on East Asian markets has declined dramatically – down from 53% in 1996 to 36% in 2007 (if Hong Kong is excluded, the East Asian share was only 20.7% – author's calculations from IMF *Directions of Trade* data). The consequence is that the dependence of East Asia as a whole on markets outside of the East Asian geographical region changed little over the decade.

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Moreover, as has long been recognized, conclusions regarding the 'bias' that economies have towards trading with one another that are based merely on the portion of trade with specific partners can be misleading if they are not adjusted for the changing share of the economies concerned in overall world trade (Frankel, 1991; Lincoln, 2004). Asian economies in the last two decades have grown far more rapidly than the world average, with a consequent increase in their overall shares in global GDP and trade. To avoid such distortions, the trade intensity index adjusts raw shares in trade for the changing share of the region in global commerce. When this adjustment is made (see Figure 1), one finds that the intra-regional trade intensity of Asia declines consistently from 1955 through to 1995, at which point it stabilizes. In contrast, the equivalent indices for the European Union and North America trend upward throughout the period.

The significance of markets within the East Asian geographical region for East Asian economies' exports is also over-stated in the unadjusted market share figures because of substantial double-counting arising from the trade in components across the region. Whereas under one half of East Asian exports in 2006 were shipped directly to European and North American markets, fully two-thirds of the value of total exports ultimately ended up in these markets once the parts and components content of exports was taken into account (Asian Development Bank, 2009: p.71; see also Athukorala, 2009). Substantial double-counting also arises because of Hong Kong and Singapore's role as entrepôts (both economies have ratios of exports to GDP in excess of 200 per cent).

Can the hypothesis that increased interdependence among East Asian economies has been responsible for a growth in inter-governmental collaboration among these economies be 'salvaged'? One could argue that the

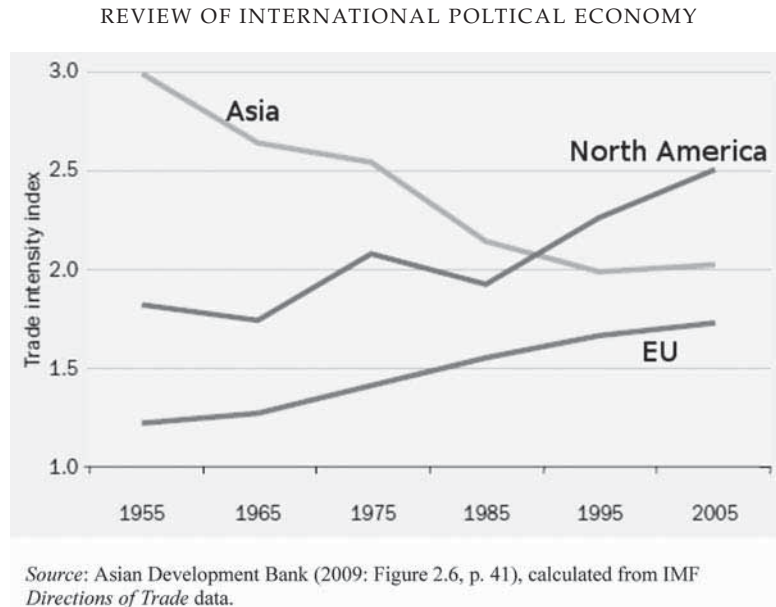


Figure 1 Intra-regional trade intensity indices.

end of the decline in East Asia's intra-regional trade index in the mid-1990s was sufficient to prompt a new interest in inter-governmental collaboration – but this is hardly persuasive. Alternatively, one might suggest that a time lag occurred between when the raw shares of East Asian exports going to other East Asian economies increased (the key period was the decade after 1985 during which the figure for ASEAN Plus Three jumped from 30.2 per cent to 37.6 per cent (Kawai and Wignaraja, 2008: Table 1) and when governments became interested in negotiating new instruments for cooperation. Possibly. The increase in intra-East Asian trade was almost certainly necessary – if not sufficient – for the subsequent increase in inter-governmental collaboration to be launched. And commentators have frequently argued that the financial crises of 1997–98, through creating a new sense of shared identity and/or interests, generated a new enthusiasm for regionalism. But the key question here is whether one can identify any additional costs arising from the increased trade integration that inter-governmental action might conceivably have effectively addressed. This is far from easy to do.

As noted above, production networks across East Asia had flourished because of the unilateral actions that governments had taken to support them by removing barriers to trade – for instance, by introducing duty free zones and duty drawback schemes that enabled companies to import components duty-free provided they were used in assembly for export

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(see, for instance, McKendrick, Doner and Haggard, 2000). In addition, all
 230 of the major East Asian economies signed on to the WTO's Information
 Technology Agreement (1996), which provided for the removal of tariffs on
 most electronics products, by far the largest single category in East Asian
 trade (the only EAS members that have not signed the ITA are Brunei,
 Burma, Cambodia, and Laos – Hong Kong and Taiwan are also signatories).
 235 More generally, tariffs have become of decreasing importance in trade
 involving East Asian economies – by 2005 only three East Asian economies
 (Cambodia, Malaysia, and Vietnam – no information was available for
 Burma) had average applied most-favored nation tariffs on manufactures
 that exceeded 10 per cent (Asian Development Bank, 2009: Table 3.3 pp.
 240 82–3).

Against this, a critic could contend that the objective of recent PTAs has
 been to go beyond dealing with tariffs to address 'WTO Plus' issues such
 as competition policy, intellectual property rights, investment, etc. But, as
 argued later in this article, only a handful of the agreements negotiated
 245 among East Asian countries tackle these issues (although, to be sure, some,
 particularly those relating to investment, have been high on the Japanese
 government's agenda).

An alternative argument might be that data on intra-regional trade are
 too blunt an instrument to capture a new 'deeper' interdependence that
 250 has arisen among East Asian economies. Inconveniently for such argu-
 ments, however, other data point to a similar lack of increase in economic
 interdependence within East Asia. Data for Japan, the largest source within
 East Asia of foreign direct investment, show that whereas this geographical
 region accounted on average for 40 per cent of the country's outward
 255 FDI in the three years before the financial crisis, the average for the years
 2005–2007 was less than 29 per cent (author's calculations from data in
 JETRO, 2008). More broadly, ASEAN Plus Three countries accounted for
 less than one third of total ASEAN FDI inflows over the years 1995–2006;
 the percentage actually fell during the years after 2002. In Northeast Asia,
 260 the share of intra-regional FDI was much smaller (Hew *et al.*, 2007). And
 intra-regional portfolio asset holding as a share of total assets held by East
 Asian states is smaller still – in 2006, under 8 per cent of the total, in con-
 trast to 37 per cent derived from the United States (Kim and Lee, 2008:
 Table 5). A similar lack of interdependence is evident in the exchange rate
 265 field. Ogawa and Yoshimi (2008) demonstrate that East Asian currencies,
 rather than moving in alignment with a notional Asian Monetary Unit (a
 weighted basket of regional currencies) have increasingly deviated from
 this unit in terms of real exchange rates.

Moreover, if concern over the increasing transaction costs from grow-
 270 ing interdependence within East Asia was the principal driving force be-
 hind the new enthusiasm for PTAs then the expectation would be that
 these agreements would be negotiated with countries' major East Asian

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trading partners. To date, this has not happened, particularly for the larger economies of Northeast Asia. China's rapid economic growth has catapulted it to the position of top export market for several East Asian economies – including Japan, Korea and Taiwan. Yet the Japanese government has completely eschewed a PTA with China (rejecting a Chinese proposal in 2002). Similarly, the Korean government has resisted Chinese overtures: negotiations (that Beijing rather than Seoul has repeatedly proposed) have not begun. Of the three Northeast Asian economic powers, only Taiwan has (recently), with the warming of relations with the mainland that followed the election of Ma Ying-jeou as President, expressed interest in negotiating an agreement with China (this did not occur until February 2009). ASEAN did negotiate an agreement with China – but the initiative for this agreement, which took ASEAN leaders by surprise, came from China (for whom ASEAN constitutes a tiny market, with observers attributing the initiative to political motives – see Jiang paper in this special section). Meanwhile, neither of the Pan-East Asian groupings has gone beyond conducting feasibility studies of 'region'-wide trade agreements, further development being blocked by governments concerned in particular about the impact on domestic interests of liberalized economic relations with China.

Most of the PTAs that East Asian governments have concluded or are currently negotiating are with states outside the East Asian geographical region. Of the 108 agreements completed, under negotiation or proposed at the start of 2009, 86 were with countries outside the region (Asian Development Bank, 2009: p. 87). While this orientation is inconvenient for arguments that increasing economic interaction among East Asian economies has driven the new interest in inter-governmental collaboration, it is potentially entirely consistent with a more general argument that PTAs are negotiated in response to the policy challenges posed by increasing interdependence (and would be consistent with the argument above that intra-regional trade as a share of East Asian economies' total trade has not increased significantly). But the concentration of negotiations on relatively minor trading partners casts doubt on such arguments. Japan has negotiated PTAs only with ASEAN collectively, the larger ASEAN economies individually, and with Mexico – countries that collectively account for only 14 per cent of Japan's exports (see the article by Solis in this special section). China has a larger number of PTAs than does Japan – but excluding that with Hong Kong, a treaty that China regards as a 'domestic' economic agreement, its PTA partners account for only 9 per cent of its total exports (Ravenhill and Jiang, 2009). For Korea, the share of total exports covered by PTAs is 13 per cent (the share is doubled if the agreement with the US, not ratified by either party at the time of writing, is included). The extreme case is Taiwan, whose participation in PTAs has been limited by Beijing's frequently expressed hostility to countries entering agreements

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with Taipei (despite Taiwan's membership in the WTO): the country's four PTAs collectively cover less than one quarter of one per cent of its total exports (author's calculations from IMF *Direction of Trade* data, except for Taiwan, from Bureau of Foreign Trade, Government of Taiwan, <http://cus93.trade.gov.tw/bftweb/english/FSCE/FSC0011E.ASP>).

In short, conventional indicators of trade and financial interdependence provide no support for arguments that increasing economic integration has driven the new East Asian regionalism. Such skepticism is reinforced by the absence of empirical evidence for a transmission belt through which any concerns over the costs of increasing interdependence have been translated into effective demands for governments to engage in regional collaboration.

THE SOURCES OF TRADE POLICY IN EAST ASIA

In recent years, many IPE theorists have borrowed heavily from economics in their efforts to explain the growth of regionalism. The starting assumption in the literature on the political economy of trade policy is that governments are rational actors whose primary concern is to maximize their utility, which in this instance means re-election to office. Exporting interests will lobby the government for improved access to foreign markets. But why would governments that respond to their pressures, and exporters themselves, choose a regional (preferential) approach to trade liberalization rather than a non-discriminatory global agreement, which all economic modeling suggests would bring larger aggregate economic gains?

For governments, the political advantage of PTAs is that they can exploit the lax discipline of the WTO's rules on regional trade agreements to exclude sensitive domestic sectors from the liberalization process, which, consequently, poses fewer political risks for them (Grossman and Helpman, 1995). For firms, the literature predicts that exporting interests are more likely to lobby for regional rather than global liberalization when they are competitive within the proposed regional market but not at the global level. A variant of this argument suggests that a regional trade agreement will be particularly attractive to companies that either currently or could depend on a regional market to realize economies of scale (Chase, 2005; Milner, 1997). Although attractive as a theoretical proposition, little empirical support has been offered for arguments based on scale economies. In many industrial sectors, the introduction of numerically-controlled machine tools has facilitated more flexible manufacturing, making shorter production runs more viable. Similarly, economies of scope have substituted for economies of scale. In any event, the relatively small additional markets provided by the current PTAs involving East Asian economies render such arguments implausible as an explanation for the new East Asian regionalism.

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An intuitively more persuasive explanation views the support that exporting interests give to PTAs as being driven primarily by defensive concerns. For Baldwin (1993), the new enthusiasm of exporting interests for regionalism in the 1990s was triggered by 'idiosyncratic' developments – NAFTA, and the EU's move to a Single Internal Market. A 'domino effect' of proliferating PTAs was created as exporting interests in countries excluded from the new regional arrangements pressured their governments to negotiate their own agreements to level the playing field with their rivals within the PTAs.

Regionalism is indeed the product of purposive action by state elites. But where does the initiative for trade policy originate? Most of the writing on the political economy of trade policy has been developed in the context of the US political system where the legislature, especially in a context of weak party discipline, enjoys a more central role in trade policy-making than its counterparts in other industrialized economies. And the central assumption of arguably the most influential political economy model of regional trade agreements (Grossman and Helpman, 1995) is that trade policy is driven by government calculations of its likely impact on campaign contributions. Despite the US-centric character of the premises, the expectation is that the propositions are of universal applicability: economic and political rationality knows no geographical bounds.

Yet, institutional configurations matter. The extensive literature on East Asian political economy suggests that the logic of political action may be different in that part of the world. In particular, researchers have asserted that the state has been both a relatively autonomous actor and the lead player in formulating economic policies – whether of a 'developmental' type as in Northeast Asia (Amsden, 1989; Deyo, 1987; Johnson, 1982; Wade, 1990; Woo-Cumings, 1999) or those that facilitate rent-seeking patrimonialism as in many Southeast Asian countries (Mackie, 1988; MacIntyre 1991). This literature argues that the state enjoys substantial autonomy from domestic interests in formulating foreign economic policies: implicit is the idea that models of economic policy-making that depend on predictions of the behavior of the median voter are unlikely to have much purchase in East Asia's authoritarian and quasi-democratic polities.

In Singapore, government-linked corporations dominate the local economy, providing an opportunity, Lee (2006) notes, for the state to impose its trade policy priorities with little domestic resistance. In Taiwan, Hseuh (2006: 170) asserts, a different logic of state action applies: because of the relative political weakness of sectoral interests and the government's pre-occupation with the Cross-Straits relationship, 'the Taiwanese government's trade policy is often made in response not to domestic economic interests, but rather to the international political economic environment of threat under which Taiwan is forced to operate' (see also Dent, 2005). In Thailand, where the administration of former Prime Minister Thaksin

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Shinawatra embarked on an active policy of simultaneously negotiating multiple PTAs with partners as diverse as Croatia and Peru, Nagai (2003: 279) states bluntly that 'the private sector does not play an important role in forming FTA policy'. Similarly, Chirathivat and Mallikamas (2004) noted that under Thaksin, 'academia, policy-makers and even the business sector have difficulties monitoring the longer term development and progress of this FTA strategy'; some of Thailand's PTAs, Hoadley (2008: 111) contends, 'seemed impulsive, the result of tourism by Thai leaders, for which the preparatory staff work had not been done'.

And in Southeast Asia in particular, the configuration of economic actors may be very different from that in Western industrialized economies, with consequences for both policy preferences and the policy-making process itself. In Malaysia and in Singapore, for instance, subsidiaries of multinational corporations are responsible for more than 80 per cent of the value of domestic exports. The regional production networks they operate often import components from a number of countries for local assembly for ultimate export to markets outside East Asia. Their interests in trade agreements *within* the region, therefore, may lie less in securing tariff reductions in other countries' markets than in ensuring low *domestic* barriers to the components they wish to import.

The one example that is often cited in support of arguments that domestic business interests were a primary driving force in the new regionalism is the PTA between Japan and Mexico. In the negotiation of this agreement, a domino effect is said to have occurred with Japanese business interests, led by *Keidanren*, the peak organization of large Japanese business firms, scrambling to level a playing field that had been tilted against them by the implementation of NAFTA (particularly by the changes it required in Mexico's treatment of maquiladora industries) and by the negotiation of a PTA between Mexico and the European Union (Solis, 2003). Manger (2005) uses the Mexican case to argue that Japanese business interests were the driving force behind the government's PTAs, and that trade policy-makers were motivated primarily by their need to cater to their core constituents, that is, manufacturing firms. In short, in Manger's (2005: 806) words, lobbying by firms was 'crucial in motivating Japanese policymakers to pursue FTA'.

The evidence is more equivocal than acknowledged by such arguments, however. *Keidanren* did publish strong statements in support of the government's concluding a PTA with Mexico *after* negotiations were under way. But several dimensions of the case are inconvenient for those who see the negotiations for a PTA as being driven primarily by Japanese business interests that were responding to their disadvantaged position in an important export market. First, the initiative for the PTA came not from Japan but from Mexico, initially an informal proposal from the Mexican Secretary of Commerce and Industrial Development, Herminie Blanco

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Mendoza, to the Chairman of the Japan External Trade Organization, Noboru Hatakeyama, on a visit to Tokyo in June 1998. It was only after the Mexican president repeated the invitation, at the 22nd Japan-Mexico Businessmen's Joint Committee, hosted by *Keidanren* in Tokyo in January 1999, that *Keidanren* established a working group to examine the possible effects of a PTA between Japan and Mexico (Ogita, 2003: 220–2). Second, the initial response of the Japanese government was not to pursue a PTA but to offer the counter-proposal of a bilateral investment treaty. The proposed bilateral investment treaty would have given Japanese firms most-favored-investor status (something the Mexican government subsequently refused to concede except in the context of a PTA) but would not have addressed market access concerns. Third, a JETRO survey conducted among Japanese subsidiaries in Mexico in the second half of 1999, after the initiative had been launched, Ogita (2003: 244) reports, found no company stating that it required a PTA to sustain its Mexican operations. Fourth, even though the public position adopted by *Keidanren* favored a PTA, the business sector in Japan was by no means unified on the issue.

The *Keidanren* position was driven primarily by electronics companies (its committee that researched the Japan–Mexico PTA was chaired by an official of Matsushita Electronics). But automobile companies were split on the proposal: those that already had established assembly operations in Mexico (and enjoyed duty-free imports under an export-offset arrangement) were concerned that a PTA would lead to greater competition from other Japanese assemblers that would now be able to ship duty-free from their home base (Sekizawa, 2008). Moreover, even the initial enthusiasm of the electronics industry for the proposed PTA was tempered when the Mexican government, in July 2001, announced a new Sectoral Promotion Program (PROSEC) under which manufacturers, regardless of nationality, could petition the government for relief on 16,000 tariff lines in 22 industrial sectors – including electronics. To circumvent the problems that NAFTA Article 3 had created for the *maquiladoras*, the tariff reductions under PROSEC on imported components were not made conditional on the export of the final product. By the time the PTA with Mexico was implemented, Japanese electronics companies no longer needed it. Not surprisingly, therefore, Ando's (2007) study of the initial impact of the Japan–Mexico agreement on bilateral trade found that it had a negligible effect on Japanese exports of electrical machinery because exports from this sector already enjoyed duty-free access to the Mexican market either under MFN rates or through the PROSEC arrangements.

Japan's Ministry of Economy and Industry had been re-considering its approach to trade policy even before the invitation from the Mexican government to negotiate a PTA. Elements within the ministry had been disappointed at the Japanese government's failure to back the proposal from Malaysia's Prime Minister Mahathir Mohamed for an East Asian Economic

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Group; the financial crisis and subsequent unhelpful response from Western governments and existing regional institutions alike reinforced the case for strengthening regional cooperation and opened a window for policy change (Munakata, 2006b provides the most detailed discussion; see also
 495 Krauss, 2003; Ogita, 2003). The policy appeared to be driven more by geopolitical concerns and a desire to enhance the effectiveness of Japan's economic diplomacy both within East Asia and globally rather than by efforts to level the playing field for Japanese business. Japanese companies did not face significant economic competition in Southeast Asia where there
 500 were no PTAs that provided any substantial advantage to competitors, and where they were able to take advantage of various duty draw-back arrangements to import components duty-free for products destined for export to third country markets. Hence, the first PTA that Japan negotiated was with Singapore, essentially a free port, where Japanese exporters
 505 faced tariffs on only four product lines: the agreement provided minimal gains for Japanese economic interests. The Japanese government reportedly sought support from the business community for the agreement but failed to gain an enthusiastic response (Ogita, 2003: 244). A subsequent decision to negotiate with ASEAN as a whole was prompted by China's
 510 proposal of a PTA to ASEAN (which itself followed quickly after Singapore's initiation of negotiations for PTAs with the United States and Australia) – again primarily a reflection of defensive diplomatic-strategic concerns rather than economic issues or lobbying by the business community (Munakata, 2006b: 117, 121).
 515 I have given detailed consideration to the Japan–Mexico negotiations because this is the case that commentators rely on in making a case for business primacy in driving PTAs in the region. No commentator would be so naïve as to suggest that governments in their foreign economic policy-making pay no attention to the interests of domestic firms. But little
 520 evidence can be drawn from the Mexican negotiations to support the argument that lobbying by business interests was 'crucial' for the switch in Japanese government policy away from multilateralism towards the negotiation of PTAs. Rather, the change in policy was largely government-driven, an attempt to stimulate East Asian cooperation in the wake of
 525 the financial crisis, and to ensure Japan's centrality within the emerging regional architecture (cf. Sekizawa, 2009: 'a popular argument is that industry pressured the government to pursue FTAs, but my own research suggests that this is an exaggeration, with industry actually putting very little pressure on government to hit the FTA trail'). A similar government-led process is evident across the region. Interviews I conducted in Korea,
 530 for instance, indicated that the government determined the choice of partners with which to negotiate FTAs: government officials reported that many businesses were either ill-informed about and/or indifferent to the government's strategy.

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Even if one were to concede a role for business lobbies in driving the PTAs, this lobbying evidently was offset to a considerable extent by the Japanese government's concern for other domestic economic interests that opposed the domestic liberalization that they feared would accompany PTAs (see Solis article in this special section). The East Asian experience does provide strong support for one political economy argument: that in negotiating PTAs governments have been pre-occupied with balancing, on the one hand, the potential economic gains from liberalization (and possible increased political support from exporting interests) with, on the other, the potential loss of support from domestic interests hurt by liberalization. Given the autonomy from societal interests that many Asian states are said to enjoy, governments might be anticipated to be able to resist domestic pressures in their design of PTAs. But protectionist interests have frequently triumphed. Again, institutional design has been important – as noted in the Solis and Jiang contributions to this special section. Protectionist interests have often been aided by electoral systems that over-represent the countryside. In its choice of partners for PTAs the Japanese government appeared to be motivated as much by a concern to minimize domestic economic adjustment costs as to maximize gains in foreign markets, hence the choice of relatively minor economic partners, and the exclusion of most agricultural products that competed with domestic production (see, for example, Mulgan, 2008; Solis, 2003, Solis in this special section).

More generally, the significance of political factors in shaping the agreements is seen in their often superficial content, which in turn has implications for the 'domino' effects such agreements create.

A POLITICAL DOMINO EFFECT?

Richard Baldwin's (1993) influential 'domino theory' of regionalism rests on the argument that PTAs will proliferate once exporting interests that are disadvantaged by an agreement signed by the government of the country in which their principal competitors are located demand that their own government level the playing field by negotiating an equivalent agreement. Baldwin has extended the argument to suggest that the proliferation of PTAs will ultimately provide a platform for trade liberalization on a broader geographical scale: PTAs generate their own non-tariff-barriers in the form of incompatible rules of origin that will lead businesses that operate increasingly globalized production networks to demand a multilateralization of regional arrangements (Baldwin, 2006). A straightforward explanation for the proliferation of trade agreements involving East Asian governments follows from the domino theory: it simply reflects a rational response on the part of business groups to their being disadvantaged by preferential arrangements afforded their competitors.

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But has a domino effect been in operation in East Asia in the years since the financial crises? Arguments in the previous section questioned assumptions about the centrality of business in trade policy-making in most East Asian economies. In this section, the focus is on how business interests are being affected by the proliferation of PTAs.

Preferential trade agreements by definition are discriminatory in character, and therefore in breach of the most fundamental principle of the WTO, its most-favored nation (MFN) clause. Regional trade arrangements were legitimized first under Article XXIV of the original General Agreement on Tariffs and Trade (GATT) and subsequently (for arrangements solely involving less developed economies) under the 1979 Enabling Clause, and for services under Article V of the General Agreement on Trade in Services (GATS). WTO members have failed to agree on operationalizing the requirements of Article XXIV that PTAs should cover 'substantially all trade' among their signatories – with the consequence that PTAs have largely escaped effective scrutiny by the international community. The Enabling Clause, meanwhile, does not require even the loose disciplines of Article XXIV, providing only (in its third paragraph) that preferential arrangements involving less developed economies should not 'raise barriers to or create undue difficulties for the trade of any other contracting parties' and shall not constitute an impediment to the reduction or elimination of tariffs and other barriers on a most-favored-nation basis.

As noted above, it is the capacity to take advantage of the lax discipline of WTO requirements on PTAs that is one basis of their political attractiveness for governments (for further discussion see Ravenhill, 2003). For business, the appeal of PTAs is two-fold. They can provide a 'positional good' if they afford an advantage that is not available to competitors. Second, PTAs may be regarded as essential for removing disadvantages generated by the PTAs enjoyed by competitors. In the first instance, we would expect to see business lobbying to preserve any advantage that PTAs have created. In the second, lobbying would be prompted by desires to level the playing field. For PTAs to have such effects, their content must create significant advantage or disadvantage for business groups. For several reasons, skepticism that current PTAs involving East Asian economies have had such effects is warranted.

The first points to the limited coverage of many of the agreements, particularly those exclusively among the region's developing economies. Taking advantage of the lack of specificity of the Enabling Clause requirements, the agreements entered into by ASEAN, China, and India are vague in their provisions, frequently failing to clearly specify the products that will be included and the specific tariff rates that will apply (ASEAN's definition of 'free' trade is tariffs that fall in the range from 0 to 5 per cent). Moreover, agreements involving these countries typically have lengthy timetables for implementation. India is particularly notorious for seeking to carve

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out substantial sectors of its economy from its PTAs. In its agreement with Singapore, for instance, only 4.3 per cent of products were granted duty-free access when the agreement was initially implemented, while 56 per cent of the total was completely excluded from the agreement (Institute of South Asian Studies, 2006: 24–5). 625

Few of the agreements involving the region's less developed economies are 'WTO Plus' in scope: they fail to address issues of 'deeper integration' such as intellectual property rights, investment and competition policies, government procurement, the environment and labor standards. On services, the region's developing economies have seldom gone beyond a restatement of their existing commitments under GATS. But in their lack of ambition they are not unique. Although the agreements involving industrialized economies (Japan, Australia, New Zealand) do attempt to extend coverage of trade in services, and in some instances include provisions on government procurement, competition policy, the environment and labor standards, the measures are typically shallow, for instance, commitments not to use lax environmental standards to attract investment. And their references to intellectual property rights are typically no more than re-statements of the governments' commitments under existing international agreements. Even on services, industrialized countries have failed to extract substantial concessions from the region's developing economies (Ravenhill, 2008b). Some of the more advanced economies have also taken advantage of the lax disciplines of the WTO to carve out sensitive sectors – most notably, of course, agriculture, but also key service industries – from their liberalization schedules. 630 635 640 645

Do East Asian PTAs significantly disadvantage non-participants?

The proliferation of PTAs within the region has created regular work for economic modelers. Most of the negotiations for PTAs have been preceded by the creation of 'study groups', which in turn have commissioned (either from private consultancies, think tanks or academic economists) economic modeling exercises to gauge the potential welfare gains from the proposed agreements. These exercises, because they involve *ex ante* estimation of the impact of the PTA, typically apply a computable general equilibrium (CGE) model. Although a core component of the contemporary economist's toolkit, CGE models have a number of significant limitations, especially when applied in the context of PTAs. 650 655

The results generated by CGE models are dictated by the parameters chosen, which inevitably rest on a number of simplifying assumptions on how economies work and on how they will be affected by a PTA. As noted by the lead economists of a major World Bank project on regional trade 660

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arrangements, in CGE modeling 'critical relationships are often specified with no empirical justification; many crucial variables cannot be measured satisfactorily; the level of sectoral detail is often rather low ... and the specification of the behavioral relationships is usually very simple' (Schiff and Winters, 2003: 49). Even economists sympathetic to CGE modeling acknowledge that the record of assumptions regarding the substitution elasticities governing trade flows, critical to the modeling of trade agreements, is 'checkered at best' (Hertel *et al.*, 2004).

The most important assumption that CGE models make regarding PTAs is that they will be 'clean', that is, they will involve a complete removal of tariff barriers, and that potentially restrictive non-tariff barriers such as the rules of origin that are an inevitable component of free trade agreements will generate no significant distortions. As already noted, however, the lax disciplines imposed by the WTO on PTAs has meant that such assumptions are not reflected in the agreements negotiated by East Asian governments. Other problematic common assumptions found in CGE models, and utilized in the most comprehensive modeling of East Asian PTAs published to date (Scollay and Gilbert, 2001), are that industrial sectors are under perfect competition (no returns to scale, etc.), that national and foreign goods are imperfect substitutes for one another (the 'Armington assumption', which discounts the possibility, for instance, that a Honda produced in Thailand will be identical to the same model manufactured in Japan), and that no factor mobility occurs across national borders. Further unrealistic assumptions are introduced in the various 'closure rules' that the models use, e.g. employment is constant, and the wage endogenous (for further discussion see Kimura, 2006; Taylor and Amim, 2007).

Even with the assumption of a comprehensive liberalization of trade between parties, CGE models predict very low aggregate welfare gains from PTAs – typically less than 0.1 per cent of GDP for an industrialized economy with low tariffs (Kimura, 2006: 65). Although the assumption of clean implementation of PTAs may lead CGE modelers to over-estimate their benefits, many economists believe that the static nature of the models fails to capture some of the potentially important effects of PTAs, e.g. stimulation of foreign investment. Consequently, the distinguished Japanese trade economist, Fukio Kimura (2006: 65) notes, 'researchers face strong temptations to enlarge the estimated effects by introducing model settings that include accumulation, technological progress, and FDI'. He cautions that such extensions are entirely 'ad hoc'. It would not be unreasonable to assume that such temptations are strengthened by the desire to provide government patrons with the results that they want to see. The outcome can be a modeling process based on assumptions far divorced from reality.

An egregious example occurred in the context of the negotiation of a PTA between Australia and the United States. A consulting firm's original modeling of the agreement assumed a clean implementation of a

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comprehensive agreement. The anticipated welfare gains to Australia were driven primarily by increased exports of sugar and dairy products, which were estimated to contribute 60 per cent of the total increase in Australian exports projected for the PTA (Centre for International Economics, 2001). 710 When an agreement was reached that excluded sugar and severely limited the potential for expansion of Australian exports of dairy products, the Australian government commissioned a second report from the same consulting firm. This second study attempted to measure the potential dynamic effects of the agreement, suggesting that investment liberalization 715 and 'dynamic productivity improvement' resulting from the agreement would contribute a welfare gain four times the magnitude of that derived from trade liberalization, and that the total welfare gain would be more than double that estimated in the original study (Centre for International Economics, 2004). Few economists found the assumptions underlying the 720 new model to be plausible.

Economic modeling of PTAs, then, gives little confidence that these arrangements will result in any substantial welfare gains for participating states. *A priori* reasoning supports a skeptical conclusion about their aggregate economic impact. Two factors of importance here have already 725 been noted. The first is the capacity of governments to exclude politically-sensitive sectors, that is, the ones that are most likely to have the highest levels of protection. The second is the trend in East Asia for negotiations to be conducted with countries that are relatively minor trading partners. To these must be added several others. 730

- Overall tariff levels are low, even for many less developed economies so that a PTA may provide a partner with limited preferential advantages. Moreover, given the extended time period afforded countries to phase in reduced tariffs under PTAs, situations may arise where the preferential tariff is actually *higher* than the MFN tariff. In his study of Japan's PTA 735 with Mexico, Ando (2007: 7–8) found that in January 2007 about one half (close to 10,000) of Mexico's MFN tariff lines on manufacturing and mining commodities were *lower* than those that Japanese exporters enjoyed through the provisions of the PTA.
- Various mechanisms (duty-drawback arrangements, export-free zones, 740 and sectoral trade arrangements – especially the Information Technology Agreement) already provide duty-free access for components to many economies in the region.
- In a world of floating exchange rates, any advantage provided by a PTA may be more than offset by currency realignments. 745
- Restrictive rules of origin together with other limitations on liberalization, such as tariff rate quotas, seasonal limitations, etc. may constitute significant non-tariff barriers that limit the benefits from an agreement.

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750 **Does business take advantage of current PTAs?**

CGE modeling of the welfare effects of PTAs assumes not only that the agreements will have comprehensive coverage and be cleanly implemented but also that traders will take advantage of their provisions – which, in reality, is another problematic assumption. The incomplete coverage of trade afforded by PTAs creates uncertainty for business. Rules of origin generate costs that firms must incur if they are to gain access to the preferential tariffs. The cost of complying with rules of origin is estimated to vary from four to eight per cent of the overall value of a consignment (Esteveordal, Harris and Suominen, 2007), which may not be substantially less than the advantage afforded by a preferential tariff.

Estimating the extent to which traders take advantage of PTAs is complicated by the failure of most Asian customs offices to collect or publish specific information on the value of trade that takes advantage of preferential tariffs. Only two countries regularly publish this information: Malaysia and Thailand. In 2007, the percentage of Thai exports to other ASEAN countries that took advantage of the ASEAN Free Trade Area (AFTA) amounted to 30.9 per cent (as reported by Hiratsuka *et al.*, 2008: 415 citing an unreferenced JETRO study) (up from the 21 per cent in 2005 reported by an earlier study (Prasert, 2007: 123)). The equivalent figure for Malaysia was 19.1 per cent. For the Philippines, a study of customs documentation suggested that in 2005 only 14 per cent of exports to other ASEAN countries took advantage of AFTA preferences (Avila and Manzano, 2007: 109). These figures are higher than the notorious estimate that less than 5 per cent of intra-ASEAN trade was conducted under the preferential rules established by AFTA (McKinsey and Company, 2003); the overall ASEAN usage of preferences is dragged down, however, by the lower income economies. Cambodia issued only 23 certificates of origin for AFTA in 2005, for trade with a total value of under one half of a million dollars (Kakada and Hach, 2007: 70). A study of the issuance of ASEAN's Form D by the Foreign Trade Department of the Ministry of Commerce in Laos indicates that only 0.1 per cent of that country's trade with other ASEAN economies, by far the major trading partners of Laos, make use of AFTA preferences (Phetmany and Rio, 2007: 105). Anas (2007: 91) estimates that less than 4 per cent of Indonesia's exports to other ASEAN economies makes use of AFTA's provisions; for Vietnam, the figure was under 8 per cent (Van, 2007).

Similarly low utilization rates have been reported for other preferential arrangements involving Asian countries. Thai customs data indicate that only 11 per cent of Thai exports took advantage of the China-ASEAN FTA (CAFTA) in 2007 (Hiratsuka *et al.*, 2008: 415). Case studies based on the issue of the appropriate rules of origin documentation suggest even lower rates of utilization in other countries. Anas (2007: 91) estimated that only

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2 per cent of Indonesian exports were using the preferential provisions of this agreement. For Cambodia, only 6 certificates of origin were issued in 2005 for exports to China, for a total value of under \$100,000 (Kakada and Hach, 2007: 70). Chinese exporters similarly failed to make use of the agreement: in 2005, the value of trade covered by Form E, required for certification of rules of origin compliance under CAFTA, amounted to less than one third of one per cent of China's exports to ASEAN (Zeui, 2007: 81). 795

The relatively recent (and phased implementation) of the CAFTA (implementation began in 2005 and will not be complete until 2010 (2015 for Cambodia, Laos and Myanmar)) may have contributed to the low utilization of its preferential arrangements. But the continuing low take-up of preferences in ASEAN's own free trade agreement suggests that there are broader factors at work in the Asian region. Even if one attempted a more relevant but more complex calculation, that is, the percentage of trade in products with non-zero MFN tariffs that takes advantage of the preferential arrangements, it is clear that the figure would still be small. The utilization of AFTA preferences is exceptionally low by international standards (and contrasts with, for example, over 60 per cent of the total value of Mexican and Chilean exports to the US taking advantage of preferential arrangements, and similar figures being reported for many European agreements). 800 805 810

In the absence of customs data for most of the countries in the region, estimates of the utilization of PTAs have depended on surveys of firms. Such studies have numerous problems, not least issues relating to the representativeness of the sample of firms that take the trouble to respond to the surveys. And no inferences can be drawn from the percentage of firms that report that they utilize PTAs to the actual percentage of trade that takes advantage of these agreements. The data suggest a 'glass half full, glass half empty' situation. On the one hand, the percentage of firms that report that they have used PTAs has increased over the years. Nonetheless the percentage doing so remains relatively low both in absolute terms and relative to the take-up of such agreements in other parts of the world. Kawai and Wignaraja (2009: 11) report that 22 per cent of 609 firms from Japan, Singapore, Korea, Thailand, and the Philippines make use of FTAs; an almost identical figure (23 per cent) is reported for 607 Japanese affiliates in ASEAN, India and Oceania by (Hiratsuka *et al.*, 2008: 415). Takahashi and Urata (2009), from a survey of 1,688 Japanese companies, report utilization rates of Japan's FTAs ranging from 12.2 per cent for the Malaysian agreement to 23.7 per cent for the Chile agreement to 32.9 per cent for that with Mexico. Chia Siow Yue (2008) reports substantially lower utilization rates for companies based in Singapore – only seven of 75 companies surveyed had made use of AFTA. Fifty-two of the sample of 75 firms reported that they had not utilized and had no intention of utilizing *any* of Singapore's large number of PTAs. 815 820 825 830 835

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Of particular interest in the survey reports are the grounds companies provide for not taking advantage of PTAs. These provide strong support for the *a priori* reasoning earlier in this article about the likely effects of the agreements. Reasons commonly cited included negligible preferential margins (with specific reference sometimes given to concessions enjoyed through the ITA, export-processing zones and/or the removal of tariffs by investment incentives), and the costs (and delays) incurred by attempting to obtain relevant documentation required by the agreements. Hiratsuka *et al.* (2008: 415) calculated that the average tariff value at which Japanese firms would make use of PTAs was 5.3 per cent, a figure consistent with calculations of the cost of compliance with rules of origin cited above. For the China–ASEAN FTA, Prasert (2007: 123) reports that the average preferential margin for Thai exports was only 1.03 per cent, a strong factor in the very low usage of the scheme. Well under 10 per cent of the Japanese firms surveyed by Takahashi and Urata (2009: Table 3) reported that the FTAs had led to an increase in their exports.

Ex post evaluations of the impact of PTAs in East Asia are likely to be particularly prone to error given the relatively brief period that many of the agreements have been in force, the extended timetables for their complete implementation, and the intervention of other variables. Changes in exchange rates are often the most important of the latter; these can easily offset any advantages afforded by a preferential tariff. Other unanticipated developments may have significant consequences on bilateral trade for reasons that have little or nothing to do with a preferential trade agreement. For instance, the substantial increase in Mexican exports of beef to Japan after the implementation of the Japan–Mexico agreement (the commodity where Mexican exports experienced the largest post-PTA increase) was caused not by the preferences created by the agreement (which allowed for a duty-free quota of only 10 metric tons for the first two years) but by the BSE outbreak in the US, which led to Japan banning imports from this source (Ando, 2007: 9). Moreover, examinations of aggregate trade data can be misleading because changes in bilateral trade may be driven by products where the MFN tariff was zero or where, for other reasons such as previous duty drawback arrangements, the PTA did not create any preferential advantage.

Detailed studies of trade in products where agreements have created preferences will be required before definitive judgments are reached on the impact of PTAs on welfare. But preliminary indications support intuitive *a priori* reasoning about the likely limited potential of the agreements. Consider, for instance, the much-vaunted 'Early Harvest' provisions of the China–ASEAN Free Trade Agreement: these covered trade of a total value of less than \$1 million (Munakata, 2006b: 118). PTAs with Singapore,

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given its zero tariffs on all except a handful of merchandise products, will only generate benefits of any significance in services trade – and while these may be of import to individual financial services firms or law firms, they will not have a noticeable impact on aggregate bilateral trade. Similarly, agreements on merchandise trade with Japan, especially given the pattern of excluding the heavily protected agricultural sector from any major concessions, are unlikely to generate major welfare gains: following the implementation of its Uruguay Round commitments, more than half of Japan's tariff lines were bound at zero: its average tariff on manufactures was 3.5 per cent.

All the evidence that points to the probable limited economic impact of existing PTAs has significant implications for the likelihood that they will generate an economic domino effect. If businesses are not adversely affected by the negotiation of PTAs that favor their rivals, then they are not likely to lobby their governments to negotiate similar arrangements. Similarly, if PTAs do not create significant benefits for domestic businesses, they would not be expected to lobby governments to maintain the 'positional goods' that PTAs are expected to create – as Baldwin (2006: 1469) acknowledges, there is little evidence in the real world that governments have been unwilling to extend the benefits of PTAs to third parties, suggesting that business either has not lobbied to prevent the erosion of preferential margins that the proliferation of agreements would generate or that any such lobbying has been ineffective. To the extent that business interests in East Asia have lobbied against any proliferation of PTAs, the pressure has come overwhelmingly from protectionist interests concerned that their position will be further eroded by additional PTAs. The evidence we have to date, however, suggests substantial indifference on the part of business interests to the proliferation of PTAs.

If the domino effect has not caused business to lobby for PTAs, and the overall welfare effects of such agreements appears likely to be minimal, are there other economic effects that might have stimulated government interests in negotiating such agreements? Some observers (extrapolating from the early experience of NAFTA), believe PTAs may stimulate a substantial boost to investment flows. The preliminary evidence available for some of the region's earlier PTAs, however, shows no positive correlation between the signature of an agreement and subsequent investment flows (on the Singapore experience see Low, 2008).

How, then, does one explain East Asian governments' enthusiasm for PTAs? Some of it undoubtedly is based on the opportunity they afford to pursue trade policies that maximize domestic political advantage (or minimize domestic political costs). But much of the explanation lies not in economics but in governments' political-strategic considerations. The explosion of PTAs in the region has been driven by a 'political domino effect', with governments' primary concern being their potential exclusion from

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925 a new dimension of regional economic diplomacy. Choi and Lee (2005: 15)
 note, for instance, that the Korean government expressed increasing alarm
 in the early years of the new millennium at being isolated as the only WTO
 member besides Mongolia that had not entered into a PTA. With the econ-
 930 omy in disarray in the immediate post-financial crisis period, Korea had
 experienced difficulties in finding potential partners willing to negotiate
 with it (Park and Koo, 2007).

Once the PTA bandwagon started rolling, competitive regionalism be-
 came the name of the game. As Munakata (2006a: 133) argues, competing
 conceptions of the region rather than a desire to reduce transaction costs
 935 have been the principal driving force. Of particular significance here has
 been the rivalry between China and Japan for leadership in East Asia.
 China's offer of a PTA to ASEAN was a diplomatic masterstroke. It was
 designed to assuage ASEAN fears (reinforced by contemporaneous econo-
 metric studies) that low-income Southeast Asian economies would be the
 940 principal losers from China's accession to the WTO (Ravenhill, 2006). But
 it also served to place Tokyo on the defensive because of the domes-
 tic problems Japan faced in negotiating comprehensive agreements with
 ASEAN economies that were significant exporters of agricultural products.
 Moreover, its status as a 'framework' agreement not only was in keeping
 945 with ASEAN's own preference for a lack of specificity in trade liberal-
 ization but was also likely to impose few domestic costs on the Chinese
 economy.

With governments unhappy at the prospect of missing out on new diplo-
 matic opportunities, they clamored to enter agreements. Recipients of re-
 950 quests for negotiations faced a dilemma: a negative response would have
 been regarded as undiplomatic in a region where 'face' is of great im-
 portance. Governments frequently found themselves under pressure to
 sign on to negotiations with relatively minor partners (or with partners in
 whose capacity or commitment to implement effective arrangements they
 955 had little confidence – for an earlier discussion of such problems in US
 negotiations with Japan, see Cowhey, 1993).

The proliferation of PTAs has been driven more by a political domino
 than an economic domino effect. A survey of elite opinion in eight Asia-
 Pacific countries (Dent 2006b: Chapter Two) provides support for this
 960 conclusion: 'strengthening *diplomatic* relations with key trade partners'
 (emphasis added) was the reason most frequently cited for the negotiation
 of PTAs. The failure of the vast majority of businesses to take advantage
 of current PTAs also casts doubt on Richard Baldwin's argument that the
 proliferation of PTAs will generate a business-led momentum towards
 965 multilateralization of the agreements. Faced with potential benefits that
 are minor compared with the costs of compliance with any agreement,
 most businesses have simply displayed indifference towards the whole
 panoply of preferential trading arrangements.

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CONCLUSION

Despite the hype, there is little evidence to date that significant region-wide inter-governmental collaboration is emerging in East Asia. Two factors are important here. First, the vast majority of inter-governmental collaboration is bilateral in character (and, in the trade field, more often undertaken with countries outside of East Asia than within it). Although a large number of projects have been launched under the ASEAN Plus Three umbrella, these are typically initiated and financed by one of the Plus Three countries with little or no input from the others. The outcome is a series of 'bilateral' ASEAN Plus One projects – 'Chinese', 'Japanese' and 'Korean' – rather than 'East Asian' schemes.² At times the rivalry between China and Japan has led the two governments to propose rival projects to address the same issues, e.g. for Mekong regional cooperation (Yoshimatsu, 2008). In the field of financial cooperation, the Chiang Mai Initiative has until recently existed in the form of a series of bilateral swap agreements (Henning, 2009; Amyx, 2008; Grimes, 2006).

Second, East Asian regional projects have seldom aspired to more than information exchange and to establishing a dialogue. They involve little cooperation as the term is normally understood in international relations, that is, the adjustment of actor behavior to meet 'the actual or anticipated preferences of others, through a process of policy coordination' (Keohane, 1984: 51). East Asian governments have eschewed measures that would constrain their policy-making autonomy. One referee for this journal suggested that to apply such 'Western' criteria in assessing East Asian regionalism was inappropriate. This strikes me as the sort of argument that the late Susan Strange would have described as 'woolly'. The point here is not to praise one form of regional cooperation and to criticize others: rather, it is to understand why East Asian governments have chosen a particular institutional design for regional engagement, and what the consequences of this choice are. Institutional design matters (Aggarwal and Choi in this issue, Aggarwal, 1998; Koremenos, Lipson and Snidal, 2004; Acharya and Johnston, 2007). By choosing shallow arrangements, East Asian governments have limited the effects – both positive and negative – this cooperation will have on domestic interests and on economic welfare more generally, and, consequently, on the political dynamics they will set in train.³

The shallowness of current East Asian regionalism reflects the primacy of political motivations in driving inter-governmental agreements on trade and finance. This article has suggested that little support can be found for arguments that the new East Asian economic regionalism has been a response to the transaction costs of increased economic interdependence or that it has been driven primarily by business interests seeking either to enlarge the 'domestic' market or to level the playing field in response to trade

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1015 agreements that other countries have negotiated. Early evidence supports
a priori expectations that the overall economic impact of the agreements
 East Asian governments have entered into to date is slight. The failure
 of business to make use of preferential trade provisions indicates that in
 the first 12 years of the new East Asian regionalism, the supply of such
 arrangements has exceeded the demand for them. The political domino
 effect to date has been more powerful than any economic domino effects.

1020 Such a conclusion does not rule out the possibility that domino effects in
 the economic realm may become more important in the future. A scenario
 where Korea succeeds in negotiating, ratifying and implementing PTAs
 with the United States and the EU will put pressure on the Japanese gov-
 ernment to follow suit. Japanese business interests have already expressed
 concern at the discrimination they will face if these agreements come into
 1025 effect, and have argued for the negotiation of PTAs with Europe and the
 United States (Nippon Keidanren, 2009a, 2009b). But because of the sig-
 nificance of these trading relationships, such a domino effect will have as
 much an impact on the global trading system as on regional collaboration
 in East Asia.

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NOTES

- 1035 1 For the broader EAS grouping, the figures were, respectively, 40.8% and 42.6%.
 2 Interviews November 2007 – March 2008 with various East Asian govern-
 ment officials and the ASEAN Secretariat. For a comprehensive list of APT
 and ASEAN Plus One projects see ASEAN Secretariat (2008).
 3 The decision by ASEAN Plus Three Finance Ministers in May 2009 to multi-
 1040 lateralize the Chiang Mai Initiative, that is, to convert the bilateral swap ar-
 rangements into a self-managed reserve pooling arrangement, will require the
 development of surveillance mechanisms if it is to be fully implemented that
 will involve unprecedented monitoring of national government policies by an
 Asian regional institution.

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