Economic Integration and Infrastructure in Asia: Presentation and Discussion at the 2010 Global Development Network Conference in Prague

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Abstract

The importance of infrastructure in economic development is self evident. It is especially important for deepening economic integration which may generate positive outcomes. The Asian economies are on the way to economic integration, but further development necessitates the development of infrastructure. Asian countries should have a common goal and framework for integration as well as mechanism of financing and capacity development to carry out programmes for the development of infrastructure. The effective implementation of infrastructure development programmes may create regional demand and lessen dependence on the external market, which is one of the characteristic to make the regional economy vulnerable the shocks.

1. Global Development Conference 2010 and the session on Economic Integration in Asia

The Global Development Conference 2010 was held in Prague, Czech Republic from the 15th to the 18th of January 2010. The Global Development Conference was organized by the Global Development Network (GDN), which was established in 1999 as a network of researchers, policy makers and aid practitioners. The mission of the GDN is to bridge research and policy to enhance the effectiveness of development assistance, through global research projects, human resource development programmes and various network activities such as seminars, workshops and conferences. This year's conference, which commemorates the 10th anniversary of the GDN, was titled "Global and Regional Integration: Quo Vadis" to discuss various aspects of economic and, to a lesser extent, political integration under the environment of the global downturn. Among the plenary

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and parallel sessions, the session titled "Economic Integration in Asia, Trade, Infrastructure and Finance" was organized by the GDN-Japan and the East Asian Development Network, which are members of the regional networks of the GDN. The session chaired by me was to discuss economic integration in an Asian context with three speakers and one discussant. Professor Shujiro Urata, Waseda University presented a paper titled "Direction of Regional Trade Cooperation". Dr. Chalongphob Sussangkarn, Distinguished Fellow of the Thailand Development Research Institute, presented a paper titled "Economic Crises and East Asian Financial Cooperation" and I myself presented a further paper. We also invited Dr. Mohamed Ariff, Executive Director of the Malaysian Institute of Economic Research as a discussant.

The following sections introduce my paper on economic integration and the significance of the development of infrastructure in an Asian context.

2. The role of infrastructure in economic development and poverty reduction.

It is of no doubt that both physical and institutional infrastructure are a prerequisite for economic development. The infrastructure facilities which provide good regional connectivity may enhance economic activities in the relevant area and eventually promote economic development. The World Bank (2004) estimates that a 1% increase in infrastructure stock is associated with a 1% increase in GDP. Investment in infrastructure may help promote efficient use of regional resources, combining products and market and providing people access to various opportunities.

To make physical infrastructure well functioning, the legal and administrative frameworks and capacity to manage them, which are called case institutional infrastructure, must be developed. In the case of road transport, for example, it is necessary to establish a system of cost recovery to compensate both construction and maintenance expenses. This requires coordination among the stakeholders. In regions where many countries, some of them landlocked, share borders, the construction of a cross-border road network is key to regional development by integrating the market. However, it would not automatically mean that the conditions for the development of cross-border trade are satisfied only by the construction of physical facilities; a system of smooth processing of immigration and custom clearances at the border must also be established and operated in a transparent manner. Under the environment of globalization, therefore, the development of an infrastructure is not only a national agenda but also a regional and global agenda, where international cooperation is strongly required.

3. Infrastructure and inclusive development

There are two ways in which development of infrastructure may help poverty reduction. One channel is, as noted above, through economic growth which is (1) a direct result of enhanced efficiency in transport and consequent market-based income generation and, (2) a macro-economic multiplier effect of the construction work itself. Another channel is through improved access to various social services, particularly in education and health.

While investment in infrastructure is largely regarded as having a positive impact on poverty reduction, we should not overlook the negative side of it. Economic growth induced by investment may have a sometimes negative effect for the poor in the relevant area. The outcome of economic growth is not always even among the regions which are combined together into a market by the infrastructure. Some region may expand production capacities rapidly, while others not, to create a large disparity of income among the regions. Some regions may be forced to sell primary commodities at lower prices due to unfavourable trade terms with the other regions. This is often associated with uneven distribution of political entitlement. Some of infrastructure facilities are designed for the benefit of big businesses, without paying enough attentions to the local people affected by the construction. There are a lot of projects in both developing and developed countries where implementation is disputed at a political level and sometimes intercepted by opposition groups. If we cannot successfully manage to achieve the goal of inclusive development, economic growth and subsequent poverty alleviation may be hampered or deadlocked.

In a similar context, public involvement in the process is indispensable. During the first half of the 1990s, developing countries received huge private investments in the infrastructure sector, dwarfing the money provided through bilateral Official Development Assistance and multilateral financing programmes. Although private investments, coupled with deregulation, have their advantage in introducing market-based investment decisions and management, their limitation is apparently that there are slim chances that public objectives are given highest priority. The inflow of money during the 1990s was quite volatile. The Asian financial crisis in 1997 swept away the expectation that private investments might replace the public financing. In addition, private investments were concentrated in rather limited sectors and countries. Table 1 shows cumulative private investment commitments from 1990 to 2002. About half of the commitments are for Latin America and the Caribbean followed by the East Asian and Pacific region which accounts for a quarter. If we look at sectorwise allocation, 44% was received by the telecommunication sector and 28% by electric

Table 1

	Cumulative Private Investment Commitments from 1990 to 2002									
	(2002-US$ Billion)									
Region	Telecom	Electricity	Natural Gas	Airports	Railways	Seaports	Toll-roads	Water and Sanitation	Total	Percentage
East Asia and Pacific	58.2	68.3	6.8	2.8	10.3	11.2	26.8	17	201.4	24.9%
Europe and Central Asia	68.1	21.1	11.3	1.5	0.3	1.8	2.8	3.5	110.4	13.6%
Latin America and Carribean	182.9	100.4	19.5	7.5	18.3	6.9	40.6	21.3	397.4	49.1%
M East and North Africa	10.6	8.4	3.9	0.9	0.2	1.2		1.3	26.5	3.3%
South Asia	19.7	22.6	0.2	0.2		2.1	0.8	0.2	45.8	5.7%
Sub-Sahara Africa	18.5	5	1.3	0.4	0.3	0.4	2	0.2	28.1	3.5%
Total	358	225.8	43	13.3	29.4	23.6	73	43.5	809.6	100.0%
Percentage	44.2%	27.9%	5.3%	1.6%	3.6%	2.9%	9.0%	5.4%	100.0%	
Source JBIC 2008										

power. Private investments, as a whole far from well balanced, may widen the disparity among regions, countries and sectors. This is why interventions from a public point of view are necessary. Governments and international organizations have significant roles to play.

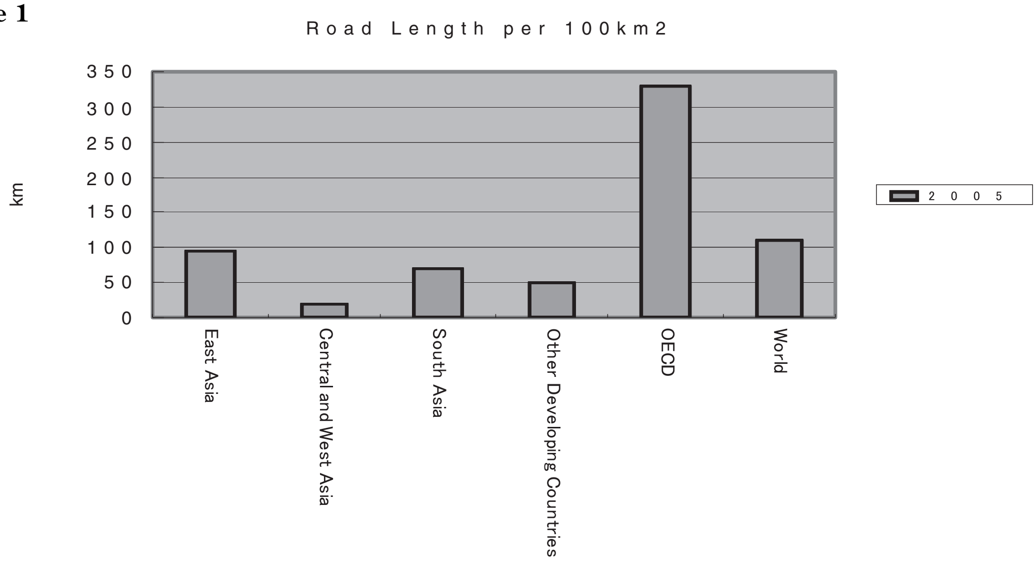
4. Infrastructure and economic integration in an Asian context

There are variations in the Asian economies. East Asian countries have achieved rapid growth led by exports since the mid1960s. South Asian countries shifted their economic policies in the mid1990s toward a more export orientation. The economic development in India and China is remarkable. It is obvious that East Asian countries are more advanced than South Asian countries.

East Asian Countries are generally characterized by higher growth of intra-regional export, the emerging presence of China in export and import market, increase of high value-added goods in export, development of value chains or production networks and progress of trade interdependence (Fujita, et al., 2005). These developments are attributable to the investments in infrastructure in the region, which were financed, in earlier stages, by predominantly official sources including Yen Loan from Japan. Thailand has developed its automobile industry to become one of the production centres of the world. The Yen Loan provided to the industrial estates and infrastructure projects located in the east of the capital city of Bangkok helped the formation of an industrial base in Thailand including automobiles.

The end of the Cold War opened various opportunities in the war-devastated Indo-China Peninsula. Among the programmes and projects, the "Greater Mekong Sub-region (GMS)" is one of the most important initiatives. It started in 1992 on a full scale, although the idea itself can be traced back to the early 1990s when an unstable political environment prevented the programme being initiated. The GMS is promoted by South East Asian countries with the Asian Development Bank as a lead financier. The countries include Cambodia, Lao PDR, Thailand, Vietnam, and China represent-

Figure 1



ed by Guangxi and Yunnan Provinces. Investments consists of transport (US$13.3billion), energy (US$6.0billion), telecommunication (US$356million), and trade facilitation (US$453million). Japan has provided substantial amounts of Yen Loan to projects such as the second Mekong Bridge project which connects Lao PDR and Thailand over the Mekong River.

The GMS is now in an advanced stage of connecting the entire Indo-China Peninsula by east-west and north-south axes. The inauguration of the road transport network reduced the trip from Hanoi to Bangkok from the previous fortnight to several days, which may further facilitate the development of a production network within the region. However, the challenge for Asia is that intra and inter regional infrastructure networks are yet to be developed and transport capacities and power supplies are seriously constrained. For example, Figure 1 indicates road length per 100 square kilometres. The road length of East Asia is still slightly lower than the world average, while those of South and Central Asia are far behind.

According to a survey carried out by JBIC in 2007 on the perception of investors in Japan, more than 35% answered that transport facilities and power supplies are not sufficient in India, and approximately 30% answered insufficient that they are in Vietnam. The GMS is an exceptional case and a large part of Asia is yet to be covered by effective international initiatives that meet the requirements of the current globalized economy. This is one of the most serious challenges for the further economic integration of Asian economies.

Table 2 shows intraregional trade flows in 2007 expressed as a percentage of total trade volume in Asia. In case of North East Asia (NEA), trade within NEA accounts for 18.4% of total Asian

Table 2 Intraregional Trade Flows in Asia (2007); percentage of export of Asia's total trade

	North East Asia	South East Asia	South Asia	Central Asia	Outside
North East Asia	**18.4**	4.21	0.56	0.13	**16.67**
South East Asia	**5.21**	3.62	0.25	0	4.85
South Asia	1.12	0.51	0.23	0	2.65
Central Asia	0.27	0	0	0.04	0.62
Outside	**29.26**	**7.65**	2.59	0.8	

Source: ADB/ADBI(2009)

trade volume while 29.26% of that is from NEA to outside Asia, of which the majority is supposed to be toward North America. In the case of South East Asia (SEA), despite GMS related programmes, only 3.62% is within SEA and double that is to outside Asia. Intraregional trade between Central Asia and the rest of Asia is almost 0 percent.

These illustrate that (1) Asian economies are heavily dependent on the export market, which makes them vulnerable to shocks coming externally like the recent financial crisis, and (2) they have not yet exploited the opportunity expected from intraregional trade, especially trade with resource-rich Central Asian countries.

5. Significance of development of infrastructure in Asia

The Lehman shock in September 2008 and subsequent crises have shaken Asian economies. The current crisis has a more serious impact on the real sector than the previous one in the late 1990s. Asia's economies are suffering from the decline of export to the US and other major markets outside Asia. The first lesson is that the Asian economies should reduce their dependency on the US and other markets outside Asia by increasing regional demand. Investment in infrastructure, which is still not enough, may help increase demand as well as foster regional economic integration.

However, the planning and implementation of the infrastructure projects and programmes have real risks. Among these, the political risk of investments being captured by those who have political influence or vested interests must not be overlooked. If we fail to control this, investment may become the source of fiscal drain. Therefore, the capacity to manage investment is of crucial importance.

On the other hand, investment decisions should be made under the full ownership of the country, according to national priority. It is particularly important for those countries where external financing is still required due to insufficient domestic savings. Public Private Partnership (PPP) should be promoted. To have good PPP, fair and transparent rules and regulations are required. The proper sharing of cost, risk and benefit must be in place. Policy makers of each country must take the particular condition of the country into account to make the process inclusive, especially for the poor. In this regard also, capacities must be developed. In short, the capacities to manage infrastructure may be almost synonymous with those of good governance.

6. Lessons from the EU

Although the EU's experience is often referred to as a success story of economic integration, it is hardly replicable in other regions as a model since the historical background, political conditions and level of economic development of the rest of the world is different from those of the EU. The points which might be regarded as refernce points are: (1) the formation of common goals and the establishment of an institutional framework helped the integration of the EU; (2) multilateral programmes to assess the needs of infrastructure and coordination of planning, such as the Trans-European Transport Network (TEN-T) and Transport Infrastructure Needs Assessment (TINA) also played important roles; (3) the mechanism to finance projects, such as EU funding and European Investment Bank (EIB) loans were indispensable.

Taking lessons from the EU, the Asian regions have to first establish the common goal of integration and a framework where the countries concerned would be locked in. Then the mechanism for cooperation and coordination of capacity development and financing must exist.

7. Discussion at the Global Development Conference, in place of a conclusion.

As mentioned earlier, the session had three speakers.

Professor Urata pointed out that the economic integration in Asia, led mostly by foreign direct investment, is rapidly deepening in accordance with the expansion of bilateral Free Trade Agreements (FTAs). The effects of FTAs being still limited to South East Asia, it is necessary to extend them to South Asia and the rest of Asia. Dr. Chalongphob argued that institutional arrangements, especially in the area of finance, is important. He suggested that, although the Chiangmai Initiative, which is the nexus of bilateral agreements, was a big step forward for regional cooperation, a multilateral framework for financial cooperation may be more effective in providing finance to the economies in the region, and as a shock absorber in the case of the crisis we are facing. As Dr. Chalongphob pointed out, it may be an opportune time to examine again the possibility of an "Asian Monetary Fund", which was proposed by Japan but failed to obtain support from the US and China. The new proposal must reflect the reality that China and India have already become global powers. Among the arguments raised from the floor, it is worthwhile noting that the development of infrastructure has been often associated with rent seeking activities, a less transparent bidding process and involuntary resettlement of people. Transparent procedures of planning and implementation, public accountability, proper financial management of financial budgets, which comprise major elements of good governance must develop simultaneously.

In conclusion, there are still huge potentials for the further progress of economic integration in Asia. To realize them, (1) open trade regimes, (2) financial mechanisms to provide funds as well as to counter shocks, (3) good infrastructure and (4) institutional frameworks for coordination and cooperation must be put in place. In addition, it is necessary to develop the human capacity to implement the above. Among these tasks, effective development of infrastructure projects or programmes may create regional demand and lessen dependence on the external markets, one of the characteristics that makes regional economies vulnerable the shocks.

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