

A Realistic Vision of Asian Economic Integration:

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Key Developments in Asian Economic Integration

- 2000 Chiangmai Initiative to pool forex reserves via web of bilateral swap agreements (BSAs)
- 2001 China proposes ASEAN+China FTA
- 2002 Japan proposes Asian Bond Market Initiative
- 2005 ASEAN+3 summit to East Asia Summit
- 2006 ADB proposes Asian Currency Unit
- Oct 2008 to establish \$80b emergency fund for ASEAN+3 by June 2009

Forms of Integration

	<u>EU</u>	<u>NAFTA</u>	<u>Proposed Asian Integration</u>
Free trade	yes	yes	yes
Free capital movement	yes	yes	yes
Free labor movement	yes	limited	very limited
Common currency	yes	no	in (far?) future; exchange rate coordination now
Political union	yes	no	no

**Could there be a common
currency in Asian economic
integration (without political
integration)?**

**The answer depends partly on
how the future looks like.**

NAFTA GDP: US dominates now and in future

<u>2005\$</u>	<u>USA</u>	<u>Canada</u>	<u>Mexico</u>
<u>trillion</u>			
2005	12.5	1.2	0.7
2025	19.6	1.8	2.4
2050	37.7	3.0	7.8

- Survival of individual currencies
- If neighbors are VERY small (e.g. Panama), then dollar bloc

EU GDP: Fairly equal size

<u>2005\$</u>	<u>France</u>	<u>Germany</u>	<u>UK</u>
<u>trillion</u>			
2005	2.3	3.1	2.3
2025	3.2	3.9	3.3
2050	4.9	5.4	5.1

- Strong spillover effects. Cooperative equilibrium is win-win over Cournot eqm. Common currency as coordinating mechanism.
- Political union to prevent any more French-German wars.

Asia GDP: Japan now, China in future

<u>2005\$</u>	<u>China</u>	<u>Korea</u>	<u>Japan</u>
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trillion

2005	1.9	0.8	5.3
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2025	11.7	2.6	6.7
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2050	48.6	3.7	8.0
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- Yen bloc now and Yuan bloc in future?
- If NAFTA outcome, then present push for Asian Currency Unit will be wasted effort.

**What sort of defense
against financial
contagion in absence of
common currency?**

No to New Bretton Woods at G20 Meeting, 15-11-08 & Position on IMF Reform

- Increase resource base: Yes but conditional on performance improvement
- Increase in jurisdiction: BIS exists; problem is not regulatory fragmentation but regulatory over-reach
- Restructure ownership: Yes but low chance
- Improved technical performance will still disappoint Asia: infeasible to have enough expertise for optimum timely response for every case. Executive Directors are instructed by ignorant national agencies

Better first line of defence for Asia is an Asian Financial Facility

- Lots of forex reserves in Asia, option of self-insurance thru pooling reserves
- Pooling to fight financial contagion not to finance balance of payments adjustment from economic mismanagement, i.e. to reduce costs of bad luck not costs of bad policies
- South Korea in last month, no draw on \$80b facility
- replace IMF clause with surveillance mechanism to pre-qualify members for emergency loans (otherwise facility would not reach meaningful size)
- Part of the AFF funds to be used on infrastructure projects in the poorest members

Realistic regional economic cooperation

- AFF to evolve according to progress Asian needs. World Bank co-exist with regional development banks, so why not an IMF and regional monetary funds?
- Cooperation to promote a regional financial center that matches London and NY
- Existence of 3 ASEAN+1 FTAs but no ASEAN+3 FTA reveals political concerns
- ASEAN+6: bigger is better not only in economics but also in politics? APEC level?