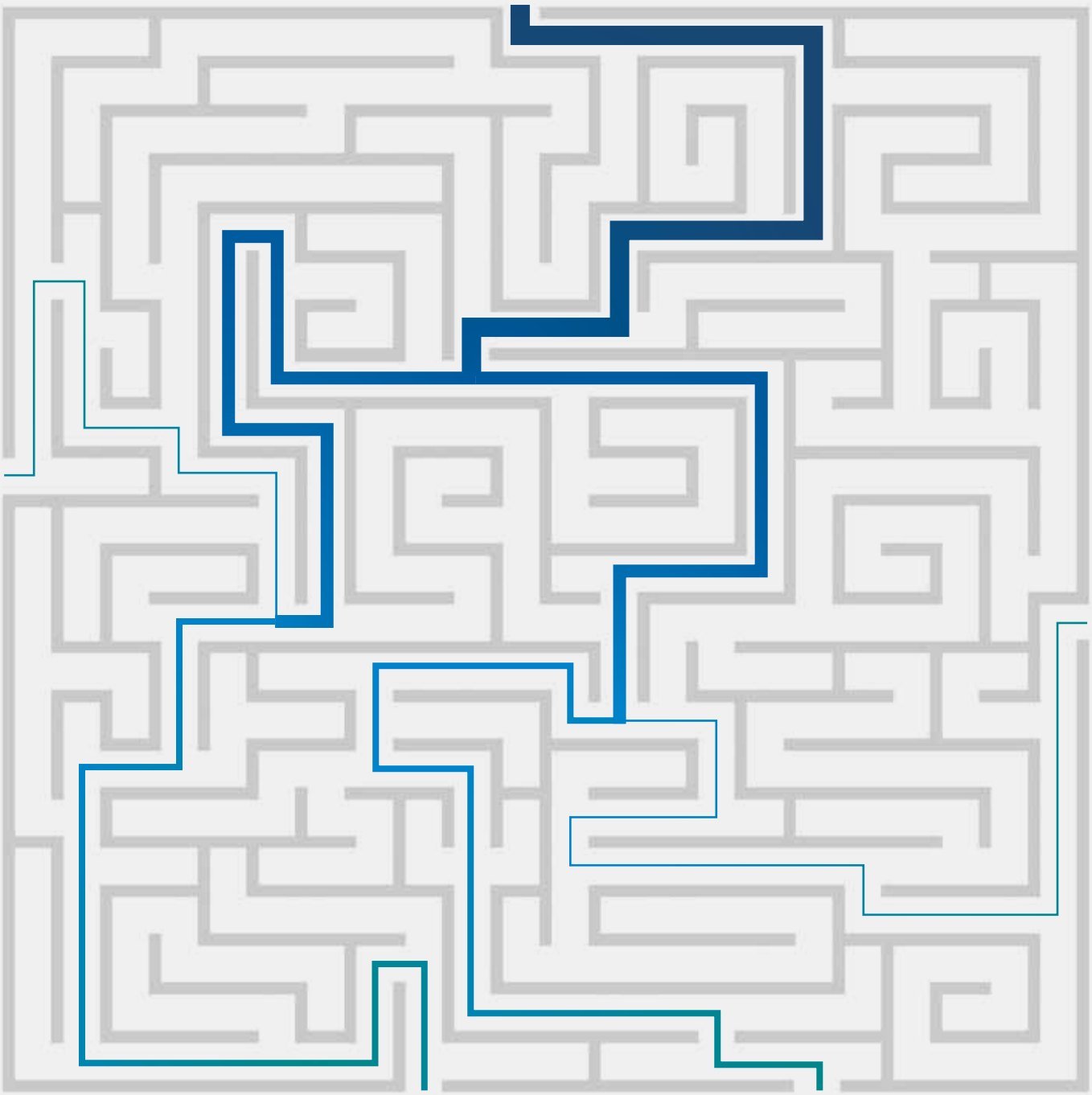
Pacific Economic Cooperation Council

STATE OF THE REGION

2014 – 2015



ABOUT THE PACIFIC ECONOMIC COOPERATION COUNCIL

The Pacific Economic Cooperation Council (PECC) is a non-profit, policy-oriented, regional organization dedicated to the promotion of a stable and prosperous Asia-Pacific. Founded in 1980, PECC brings together thought-leaders from business, government, civil society and academic institutions in a non-official capacity. Together, PECC members anticipate problems and challenges facing the region and through objective and rigorous analysis, formulate practical solutions. The Council serves as an independent forum to discuss cooperation and policy coordination to promote economic growth and development in the Asia-Pacific. PECC is one of the three official observers of the APEC process.

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The State of the Region report is a product of a taskforce established by the governing body of PECC. While efforts are made to ensure that the views of the PECC members are taken into account, the opinions and the facts contained in this report are the sole responsibility of the authors and editorial committee and do not necessarily reflect those of the member committees of PECC, nor their individual members.

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MESSAGE FROM THE CO-CHAIRS OF PECC

On behalf of the Pacific Economic Cooperation Council's twenty-six member committees, we are pleased to present our ninth annual report on the *State of the Region*.

When we changed the product from the *Pacific Economic Outlook to the State of the Region* our objective was to try to provide a unique report on the Asia-Pacific – to capture general trends defining the development of the region and to highlight the challenges facing us.

The challenge of today is growth. As highlighted in Chapter 1 of the report, the recovery from the Global Financial Crisis continues, albeit at a far from robust pace, with economic growth at around two percentage points off from the immediate pre-crisis period. Furthermore, growth remains supported by extraordinary stimulus measures that cannot continue into the foreseeable future. We focus this year on some of the potential 'engines of growth' for the region over the medium to longer term.

One of these is middle-class consumption in the region's emerging economies. Since the foundation of APEC in 1989, average incomes in the region have tripled from around US$5,000 to more than US$15,000. More and more people in the region have gone from living at barely subsistence levels to being able to live more like their counterparts in more advanced economies. As the report points out, consumers in the region's emerging economies still spend around a third of their income on food compared to just a tenth in advanced economies. As incomes rise, that proportion will lessen allowing consumers more discretionary expenditure.

If one of the characteristics of this so-called 'new normal' is lower consumption growth in advanced economies then the firms that used to export to those markets will need to find new customers – or go bust. These new customers might well be the very people producing the products that used to be only within the reach of those in rich economies or indeed the rich in emerging ones.

However, this is but one potential growth engine; there are others. Last year's report focused on the need for infrastructure. This remains an area where bottlenecks exist and emerging economies are well-behind. As we argued in last year's report, investment in infrastructure is not only needed but timely given the need to boost aggregate demand.

Another potential engine of growth is innovation. Over the past couple of decades, advanced economy growth in the region has benefitted much more from investment in ICT and in skills than emerging economies.

One of the major features of the *State of the Region* report is our annual survey of regional opinion-leaders. The results this year are instructive. Once again a slowdown in China is the top risk to growth but strikingly the lack of political leadership was the second highest risk. This finding is perhaps best taken in conjunction with other findings: the third highest risk to growth was the failure to implement structural reforms. The top priority for APEC Leaders was progress on a Free Trade Area of the Asia-Pacific (FTAAP); and the second most important factor for Asia-Pacific growth was further trade and investment liberalization.

Taken as a group of findings they perhaps reflect an underlying sense that while we know that structural reforms are needed, and that trade liberalization is important to the future of growth, the political will to achieve them could be a problem. Overcoming entrenched interests resistant to change is not a new problem; it has always been there. But in today's political environment characterized by wrong-headed economic nationalism and short-termism exacerbated by political cycles, leadership is much harder to come by at the domestic level, let alone the international.

One initiative where leadership is required is the FTAAP. Chapter 2 goes into some detail on how the current trade initiatives like the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP) could form the basis of an eventual FTAAP. As the central narrative here is growth, the point we emphasize is that its achievement could add around 2.3 percent to global GDP in 2025. This is one initiative that could significantly contribute to the G20's objective to increase global growth. This is not to suggest that it will be easy to achieve. Neither the TPP nor the RCEP are foregone conclusions, and even if negotiations are concluded, there is no guarantee that the domestic political support will be there to see them through difficult ratification processes.

Another issue that has been on our radar for some time is the changes taking place in regional and global energy markets. Our 2011 report focused on the potential for transpacific energy trade. This year's survey results showed some sharp differences in views among sub-regions. While only 4 percent of respondents from North America picked energy security as a top 5 risk to growth for their economies 30 percent of Southeast Asians rated it as a top 5 risk.

On the occasion of APEC's 25th anniversary we are pleased to note that 61 percent of respondents to our survey thought that the organization is as important or more important today compared to 1989 when it was created. This marks a significant improvement over previous years. In particular, respondents from Southeast Asia have gone from being rather ambivalent towards the APEC process to being much more supportive. One reason may well be the focus that has been put on addressing supply side constraints – a major concern for Southeast Asia and other emerging economies. As last year's survey showed, while Southeast Asians remained supportive of the idea of freer trade, they also believed that the benefits they received from it were limited due to supply side constraints like lack of infrastructure and skills.

In this regard we believe that APEC needs to keep a balance to its agenda as it has done since its formation. The emphasis on free trade and now behind the border reforms are critical – they will help to ensure the most efficient allocation of resources, but this must come with significant initiatives to ensure that all economies are ready to benefit from the process.

The region and the world have changed much since APEC was founded. As a progenitor and forerunner of APEC we have had a privileged role of being able to actively contribute to this evolution. As much as APEC needs to be an institution that brings this region together, it must also find a way to ensure that the region remains outward looking and play its role in guiding the development of the world economy.

There are many people we would like to thank for their contributions to this report: the editorial committee and the report's coordinator, Eduardo Pedrosa, Peter Petri & Ali Abdul Raheem, Chen Bo, CNCPEC, JANCPEC and USAPC, the staff at the PECC International Secretariat, especially Jessica Yom, Betty Ip and Lee Ho Ching. We would also like to express our appreciation to all of our member committees as well as all those who have taken the time to share their views and perspectives on the region with us through the survey.

Jusuf Wanandi
Co-Chair

Don Campbell
Co-Chair

EXPLANATION OF TERMS USED IN THE REPORT

ABAC	APEC Business Advisory Council
ADB	Asian Development Bank
ADBI	Asian Development Bank Institute
Advanced economies	Economies with a GDP per capita of more than US$12,746 (In this publication, 'advanced economies' refers only to those economies in the region, namely: Australia, Brunei Darussalam, Canada, Chile, Hong Kong (China), Japan, Korea, New Zealand, Russia, Singapore, Chinese Taipei, and the United States.)
AEC	ASEAN Economic Community
AFTA	ASEAN Free Trade Area
AP	Asia-Pacific
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
ASEAN-5	Indonesia, Malaysia, Philippines, Thailand, and Vietnam
ASEAN-6	Brunei Darussalam, Indonesia, Malaysia, Philippines, Thailand, and Vietnam
ASEAN+3	ASEAN plus China, Japan, and Korea
ASEAN+6	ASEAN plus China, Japan, Korea, India, Australia, and New Zealand
BRICS	Brazil, Russia, India, China, and South Africa
CJK	China, Japan, and Korea
CLMV	Cambodia, Laos, Myanmar, and Vietnam
CPI	Consumer Price Index
DDA	Doha Development Agenda
EAS	East Asia Summit
Emerging economies	Economies with a GDP per capita less than US$12,746 (In this publication, 'emerging economies' refers only to those in the region, namely: Cambodia, Myanmar, China, Colombia, Ecuador, India, Indonesia, Laos, Malaysia, Mexico, Mongolia, Papua New Guinea, Peru, Philippines, Thailand, and Vietnam.)

EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
FTAAP	Free Trade Area of the Asia-Pacific
G20	Group of Twenty (Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, United Kingdom, United States, and the European Union)
GCF	Gross Capital Formation
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GNI	Gross National Income
IADB	Inter-American Development Bank
ICT	Information and Communications Technology
IMF	International Monetary Fund
NAFTA	North American Free Trade Agreement
NEA	Northeast Asia
NGO	Non-Government Organization
NA	North America
OCE	Oceania
OECD	Organisation for Economic Co-operation and Development
PA	Pacific Alliance
PECC	Pacific Economic Cooperation Council
PPP	Public-Private Partnership
QE	Quantitative Easing
QQE	Qualitative and Quantitative Easing
RCEP	Regional Comprehensive Economic Partnership
ROO	Rules of Origin
R&D	Research and Development
SA	South America
SEA	Southeast Asia
SME	Small and Medium Enterprises
SMME	Small, Medium, and Micro Enterprises
TPA	Trade Promotion Authority
TPP	Trans-Pacific Partnership
TTIP	Transatlantic Trade and Investment Partnership
US	United States
WEO	World Economic Outlook
WTO	World Trade Organization

EXECUTIVE SUMMARY

The Asia-Pacific region is forecast to grow at around 3.8 percent over the next two years before moderating to around 3.5 percent in 2018-2019. While far from the heady rates of above 5 percent growth during the pre-Global Economic Crisis period it represents a steady if unremarkable recovery from the depths of dark days of the 2008-2009.

The challenge ahead is whether the region can do better. While growth has become more balanced in the region, it has also become slower. Moreover, some of the growth remains supported by extraordinary stimulus that cannot be sustained over the medium term.

Regional economies will need to identify alternative growth engines if they are to achieve the objective of sustainable high quality growth. Two areas hold promise in this regard –innovation and middle class consumption. Providing an environment that facilitates their growth should be a priority.

According to PECC's annual survey of opinion-leaders from the policy community, the top five issues that APEC Leaders should discuss are:

1. Progress towards a Free Trade Area of the Asia-Pacific (FTAAP)
2. Innovative development, economic reform and growth
3. The APEC Growth Strategy
4. Reducing the income inequality in the region
5. Attaining the Bogor Goals of free and open trade and investment

Of concern should be the fact that opinion-leaders selected a lack of political leadership as the second highest risk to growth. It stands as a stark observation if not a rebuke to politicians at a time when leadership is badly needed. The third highest risk, possible failure to implement structural reforms, also suggests considerable anxiety about the political ability of leaders to address an important domestic and regional agenda.

Out of a list of 10 possible drivers of growth, technological innovation was ranked as the most important followed by policy reform and then exports to emerging markets.

In 2010 APEC member economies adopted a new growth strategy; however, tangible results from the strategy are difficult to see. The adoption of clear targets focused on innovation – especially skills development will help to focus efforts in this area.

While respondents did not rank trade liberalization as a top factor for growth in their individual economies, it was the second most important factor for growth in the region as a whole. Indeed, progress on the FTAAP was ranked as the most important issue for APEC Leaders to discuss in Beijing.

As the region and the world struggle with slower growth, the estimated economic benefits of Asia-Pacific wide integration are large at 2.3 percent of world GDP in 2025 or US$2.4 trillion. But even the current negotiations on the Trans-Pacific Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP) would generate substantial gains.

Potential gains increase sharply with the scale of integration—for example, expanding the TPP with 12 members to an FTAAP with 17 members

would triple global benefits from $223.4 billion to $1,908.0 billion in 2025. The benefits would grow further to $2,358.5 billion if Hong Kong (China), Chinese Taipei, Papua New Guinea, and most importantly, Russia were added based on APEC membership, and still larger benefits could be achieved if India, Cambodia, Laos, and Myanmar were added to form FTAAP-25.

While the RCEP and the TPP are critical—and arguably indispensable—steps toward FTAAP, they will not guarantee its realization. They will promote economic integration among members, but neither will offer comprehensive regional coverage or, at first, broadly acceptable rules. At worst, they could establish conflicting standards that are difficult to reconcile and would make the "noodle bowl" of overlapping trade agreements more intractable. A clear vision of FTAAP will minimize the possibility of adverse outcomes. Hence the time is right for analyzing how an FTAAP might be structured and how the current regional negotiations could become, as economists hope, stepping stones rather than stumbling blocks on the path toward it.

Opinion-leaders showed no clear-cut preference for either route – the TPP or the RCEP - and prefer the more agreeable but nebulous concept of building on various agreements including the TPP, RCEP and the Pacific Alliance.

An umbrella agreement will be needed if neither RCEP nor TPP can attract FTAAP-wide membership. This agreement will then have to be separate from RCEP and the TPP, although it should be shaped by their provisions. Since the two smaller agreements will differ, FTAAP will need to formulate positions on issues that are absent from at least one of the agreements as well as harmonize provisions that are included in both.

Under the FTAAP umbrella, members could converge to higher standards. Precedents for an evolutionary approach to standards are offered by ASEAN's upgrading of the ASEAN Free Trade Area and some ASEAN-plus-one partnerships. NAFTA is itself an umbrella agreement built around the Canada-US free trade agreement and has been upgraded over time. The TPP is also envisioned to be a "living agreement" to be adjusted in the future.

RCEP and the TPP provide way-stations for experimenting with and adjusting to deeper integration. This is important for the large trade flows that connect the United States, China and Japan with each other and other partners. Asian and trans-Pacific regional negotiations are moving forward, despite business cycles, elections, geopolitics, and political controversy.

Deeper economic integration in the Asia-Pacific is likely to produce large economic gains and could help minimize dangerous geopolitical tensions. Yet agreements that foster integration will be very difficult. Lengthy and complex negotiations are required and much opposition is bound to emerge from special interests throughout the region. Asia-Pacific integration will depend on exceptional, collaborative leadership, not least from the region's largest economies.

The economic integration of the Asia-Pacific region has rebounded since the Global Financial Crisis according to PECC's index of regional economic integration. The index measures the degree of integration taking place in the Asia-Pacific region based on intra-regional flows of: goods; investment; and tourists and five measures of convergence: GDP per capita; share of non-agriculture to GDP; the urban resident ratio; life expectancy; and share of education expenditure. While the region has become more integrated through increased flows of goods, people and capital, the index shows that there is a long way to go in terms of closing development gaps. Integration is not an end in itself but a means to ensuring that all citizens can achieve their potential.

CHAPTER 1

PROSPECTS FOR GROWTH IN THE ASIA-PACIFIC REGION*

The Asia-Pacific region is forecast to grow at around 3.8 percent over the next two years before moderating to around 3.5 percent in 2018 – 2019. While far from the heady rates of above 5 percent growth during the pre-Global Economic Crisis period it represents a steady if unremarkable recovery from the depths of dark days of the 2008 – 2009.

* Contributed by Eduardo Pedrosa

The challenge ahead is whether the region can do better and reach the growth rates it had during the pre-Global Financial Crisis (GFC) period. While growth has become more balanced in the region, it has also become slower. Moreover, some of the growth remains supported by extraordinary stimulus that cannot be sustained over the medium term.

FUTURE DRIVERS OF GROWTH

Regional economies will need to identify alternative growth engines if they are to achieve the objective of sustainable high quality growth. In addition to the challenge of weak demand from traditional markets, many of the region's emerging economies have reached middle-income status and as such can no longer rely on their low labor cost advantage to drive growth. The APEC Growth Strategy set out in 2010 provides a framework for high quality growth but implementation is lacking.

Over the past two decades, economic growth for the emerging economies of the region has been overly reliant on one factor of production – investment in non-ICT capital which accounted for, on average 61 percent of GDP growth (compared to 40 percent for the region's advanced economies). These numbers are only slightly distorted by the weight of China among the region's emerging economies and the huge amount of investment that took place after the crisis.

Advanced economy growth, on the other hand, has benefitted much more from investment in ICT, 33 percent (compared to 12 percent for emerging economies). Advanced economies in the region also had a much bigger contribution to growth from the composition of their labor force, i.e. skills (14 compared to 3 percent).

The region's growth could also receive a boost from increased middle-class consumption. On average, food still accounts for around 31 percent of consumption in the region's emerging economies, compared to 12 percent in advanced economies. Another category with a significant differential is expenditure on healthcare. Expenditure on miscellaneous goods and services such as hairdressing salons and personal grooming; appliances and products for personal care; jewelry and watches, and insurance accounts for around 14 percent of consumption expenditure in high income economies while it is just 8 percent in the region's emerging economies.

It is likely that the emerging middle class in the Asia-Pacific will become the most important source of global demand in the intermediate future. Much of this demand will be for products and services that are currently produced in these economies but for export to end-consumers in advanced economies. This consumption could play the same role that exports to advanced economies have played in the previous stage of development in the region's emerging economies.[1]

However, middle class consumption in emerging Asia-Pacific economies – whether it is of education, healthcare or consumer goods faces particular and almost unique challenges as well as opportunities. The region is home to the most populated economies in the world. If all APEC economies were to have same number of cars as their counterparts in OECD economies an additional 910 million cars would be on the road and if all APEC citizens spent the same on healthcare as OECD there would be an additional US$7.5 trillion spent on healthcare. The resource implications are enormous.

[1] See: *'Can Asia Grow Fast on its Own? The Economics of the Dynamic Middle'*, Peter A. Petri, September 15, 2012, Joseph Fisher Lecture, University of Adelaide, 2012

Overcoming both of these challenges will require changes in both business models as well as the production process – especially if this is to include the consumers at the bottom of the pyramid. The conclusion from this is that there is potential for emerging economies of the region to continue to grow at high rates through investing more in ICT services and the skills of their people – in other words improving the environment for innovation.

CHANGING BALANCE BETWEEN EMERGING AND ADVANCED ECONOMIES?

While the flat recovery is at first glance unexciting what is remarkable is where the growth is coming from – while much attention is paid to emerging markets, BRICS and other notable acronyms, advanced economies in the region look to have regained their footing and now contribute almost as much to regional growth as middle income economies.

Prior to the 2008-2009 crisis, the region's emerging economies were contributing up to 60 percent of regional growth with the exception of the heady days of the dot com bubble. Over the next few years at least, the expectation is that emerging economies of the region will account for closer to 54 percent of regional growth.

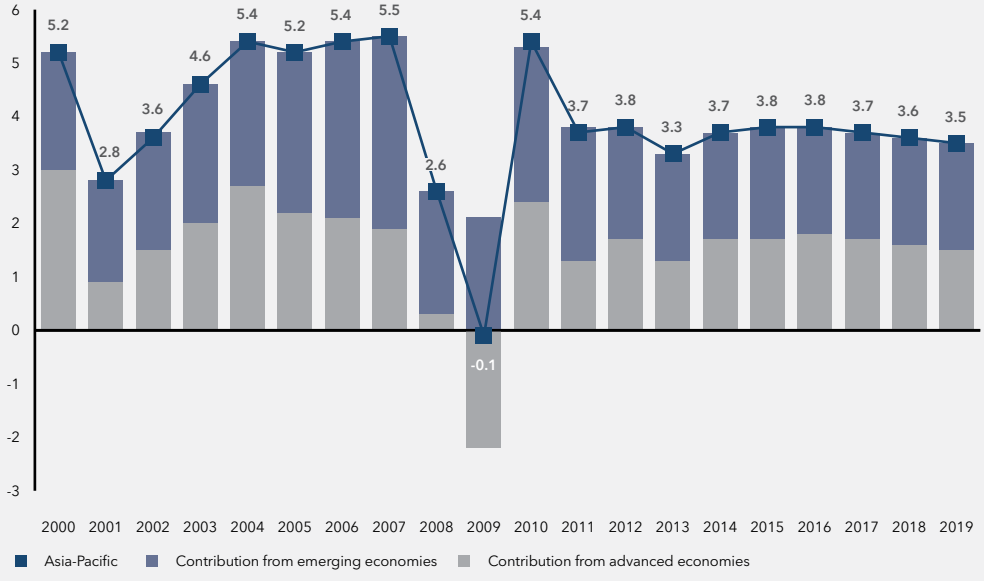
Two big resource economies are forecast to show the biggest swings in growth between 2014 and 2015 – Papua New Guinea and Mongolia. Papua New Guinea is forecast to grow at 21.6 percent in 2015 compared to 6.0 percent in 2014, and Mongolia at 7.7 percent down from 13.0 percent. For Papua New Guinea the expectation is that growth will come from a surge in consumption as well as an improvement in net exports. For Mongolia, the slowdown will come from decreased investment – after several years of very high gross capital formation as well as a 3.3 percentage point decrease in net exports.

Growth in most regional economies is expected to improve over the next year by as much as 1 percentage point; exceptions to this general trend are: Colombia, Malaysia, New Zealand, China, Japan, Ecuador, and Brunei Darussalam.

Among the region's three largest economies, China's growth is expected to slow moderately from 7.5 to 7.3 percent, Japan is expected to also slow from 1.4 to 1.0 percent while the US is expected to improve from 2.8 to 3.0 percent.

The three largest economies of the region account for 69 percent of total output in the Asia-Pacific so whatever happens in each is likely to have a large impact on their neighbors. Estimates vary on the impact of changes in growth in the region's economies. In the case of China, the IMF estimates that a 1 percent slowdown may lower GDP growth in the median Asian economy by about 0.3 percentage points after a year, compared with 0.15 for non-Asian economies. The correlation is even higher for the ASEAN-5 economies. In the case of the US, IMF research also suggests that the magnitude of second order policy responses have an impact on the direction of the correlation; for example, a positive growth shock for the US that came with tighter monetary policy would be beneficial. However, if the 1 percent growth shock came with an increase in 100 basis point increase to long-term government bonds it would generate a moderate slowdown in most Asian economies. For example, in the case of ASEAN-5 it would shave 0.85 percentage points off growth, in China 0.79, Japan 0.86, and Korea the most at 0.98.

Figure 1.1: Asia-Pacific GDP growth



Source: IMF WEO Database April 2014. For definition of emerging and advanced economies see Explanation of Terms Used in the Report

UNITED STATES

While the relative weight of the US economy in the region has declined over the past quarter of a century, it still accounts for 37 percent of the region's total output. Growth in the US economy is expected to improve over the next 12 months, from 2.8 to 3.0 percent. In terms of rebalancing, the US economy continues to be driven largely by consumption which has been adding roughly 1.6 percentage points to US GDP in recent years, some 0.5 percentage off the highs in the run up to the crisis. What has changed of some significance is that government expenditure has been reducing total output as a result of the fiscal austerity measures put in place to try to get the US budget under control. Also of importance is that net exports are now much less of a drag on the economy than they used to be (see Box 1: The US Economy).

Box 1: The US Economy

The performance of and outlook for the US economy look more solid than it has at any time since the beginning of the Global Financial Crisis in 2008, but there are continued weak spots and doubts about the underlying strength of the expansion. GNP growth for calendar year 2014 will likely be about 2 percent, a rate that may only slightly rise in 2015. If measured against the APEC Leaders goal of balanced, sustainable, and inclusive growth, despite the improved performance of the American economy, many challenges remain.

On the positive side of the ledger, recent labor force growth has been more robust than at any time in the past five years. The total size of the labor force has finally exceeded pre-2008 crisis levels and unemployment has dropped from nearly 10 percent in 2009 to below 6.5 percent. This has stimulated some growth in consumer spending and business investment, although both groups remain cautious. Despite reduced unemployment, inflation appears to be in check, with core inflation well below the Federal Reserve's 2 percent target and little inflationary expectations. The substantial growth of U.S. energy production has reduced American dependence on vulnerability on external petroleum supplies and contained growth of the trade deficit. While oil prices are affected by international market supply insecurities, domestic gas prices in the United States have plummeted to the benefit of consumers and the international competitiveness of domestic downstream industries. At the same time, the negative forces affecting the economic performance – notably the weak housing residential sector and the fiscal drag as a result of reduced Federal and local government expenditure – have abated.

Given this positive picture, the Federal Reserve is expected to continue to terminate its already tapered asset purchasing program as scheduled. However, because of the still cloudy outlook and lack of inflationary pressures, the Fed may be reluctant to proactively increase interest rates, particularly if overseas growth remains weaker than expected and the dollar is strong. While some believe that growing business confidence will cause the economy to pick up steam by 2016 and that the Federal should shift its attention to potential inflation issues, others believe the economy is still performing below potential, that growth is likely to remain below historical recovery rates and even that current, slow 4-year expansion could end prematurely. Several factors will determine the future.

Labor and Productivity: Despite robust job growth in 2014, labor participation rate continues to decline and the quality of the new jobs is debated. Structural changes in the labor market including the aging of the labor forces and the continued shift toward service sector jobs complicate assessment of what the highest sustainable employment level might be, a goal of U.S. monetary policy. The Federal Open Market Committee finds that despite improvement in market conditions, "underutilization of labor resources still remains significant." Moreover, labor productivity is growing only slowly in the absence of any major new technological driver.

Housing: The performance of the housing sector remains below historical expectations, despite apparent pent-up demand. While there have been a general rise in sales of existing units and new housing starts despite variable monthly figures, this sector has not fully recovered. A spike in mortgage interest rates in 2013, continued tightness of credit, and college loan indebtedness of many younger families may account for this and dampen future prospects.

Exports: With wage rates rising abroad relative to domestic rates, the U.S. had hoped for a large boost in exports over time, particularly in the manufacturing sector. But while total exports are at an all-time high, they have been rising only slowly (and far below President Obama's 2010 five-year, export-doubling goal). There has hardly been any rise at all for manufactured goods since 2011. Increased domestic petroleum production has been the major factor in holding the growth

of U.S. trade deficit in check, not rising exports. Crude oil and petroleum products imports have decreased from about 5 billion barrels yearly in 2005-07 to 3.6 billion barrels in 2013. Weak economic performance in Europe is one factor in slow U.S. export growth, but Asian markets are also disappointing. In the case of Korea, for example, U.S. exports declined despite the conclusion of a free trade agreement, increasing the future political difficulties in selling such agreements. Without more rapid export growth and with improved domestic economic performance, the U.S. trade balance, now running at about $60 billion a month, will probably rise moderately.

Fiscal policy: It has been estimated the reductions in government expenditure shaved as much as 1.5 percent from GNP growth in 2013. The figures for 2014 and 2015 will be much lower with only a moderate fiscal drag. The Federal budget deficit has declined dramatically, but with Federal pension and health care costs rising and differing fundamental views about the role of government in the economy, the two political parties remain deadlocked on many budget issues. There is little to no expectation of an expansionary fiscal policy.

Widening Income Gap: President Obama argues that the widening gap is a more significant economic change than the Federal budget deficit. Data suggests that the richest tenth of Americans own close to half its wealth, a figure that has been rising for a half century. How to provide a greater measure of equality of opportunity in an era in which there are reduced returns to labor, as opposed to capital, a more skewed return of benefits to labor, and strong resistance to government programs that redistribute income remains a fundamental dilemma.

CHINA

China's growth is forecast to slow moderately from 7.5 to 7.3 percent, largely as a result of a forecasted decline in gross capital formation – much in line with the plan to wean the economy off its reliance on stimulus in recent years. In terms of rebalancing the economy, it is clear that net exports have declined in importance to the economy. However, it remains to be seen whether this is a result of a decline in demand from external markets or a real change in the structure of the economy. Over the longer term much work needs to be done to increase consumption in China which accounts for just 37 percent of aggregate demand and has been decreasing in importance as a result of the massive increase in investment in response to the crisis.

Over the medium term the forecast suggests that the consumption share of GDP will increase by about 0.3 percentage points a year over the next 5 years with the converse happening to investment.

Box 2: China's Economy for 2014: Steady and Sound Growth with Reform and Innovation
Contributed by CNCPEC

Overall stability to date

In the first half of the year, the Chinese economy registered 7.4 percent growth. The CPI rise was kept at 2.3 percent. Despite economic slowdown, between January and August, the surveyed unemployment rate was kept at around 5 percent in 31 big and medium-sized cities. More than 9.7 million urban jobs were created, which is over one hundred thousand more than the same period last year. This suggests that the economy is running within the reasonable range.

The structure of the economy is further improved; in terms of economic drivers, consumption contributed 54.4 percent and investment in fixed assets contributed 48.5 percent, while trade contributed – 2.9 percent.

In the first half of the year, the tertiary industry increased by 8 percent, accounting for 46.6 percent of GDP, which is 0.7 percent and 0.6 percent respectively over the secondary industry. The tertiary industry continued to outperform the secondary industry in terms of growth rate and share of GDP, and is a leading sector of the economy.

The reform taken thus far has greatly contributed to the achievements. The reform of the administrative review and approval system has lowered the threshold for starting businesses and removed restrictions on them. Between January and August, the amount of newly registered market entities was more than eight million, and from March to August, the number of newly registered businesses grew by 61 percent over the previous year. The reforms to investment financing, taxation and logistics systems spurred the service sector and other emerging industries. In the first half of the year, new businesses and new business models such as logistics, express delivery and e-commerce all developed fast. This plays an important role in spurring employment.

The government has successfully refrained from using extensive financial and monetary stimulus measures to maintain the targeted economic growth rate. Instead, favorable policies and liquidity were directed to specific sectors with precision to stimulate vitality while maintaining market stability.

Outlook for the year

The economy is still faced with downward pressure and many international economic institutions have lowered their outlook of China's economic growth. Some economic institutions call for extensive stimulus policy. However, the government remains level-headed against these fluctuations, taking them as inevitable and expectable given the volatility of the global economy and the high-base of the relevant figures of the same period of last year.

The actual economic growth rate is forecast to be within the proper range; that is, slightly higher or lower than the 7.5 percent target. The government will go on with the range-based policy package and will not succumb to the fluctuations of specific economic indicators and make a policy overhaul. The tolerance to the fluctuations is based on the confidence of the resilience of China's economy, the potential and ample space for growth and a full range of tools of macro-control at disposal, and a judgment that the fluctuations are small ripples.

The favorable conditions for the optimistic outlook include the generally stable employment and prices, the ever bettered economic structure, the fairly robust growth of consumption, the good development of the tertiary industry, increasing external demand with the recovery of the major economies including the United States, Europe and Japan. Even the industrial indicators such as Purchasing Managers' Index (PMI), Producer Price Index (PPI) and industrial electricity consumption will give better performance in the coming months. Real estate will be in the best season of the year. Investment in railway and urbanization is well in position.

According to an outlook of the National Reform and Development Commission, the third quarter will see a growth of 7.3-7.4 percent, followed by a 7.5 percent of growth in the fourth quarter. This will make the annual goal of economic growth achievable.

However, well-targeted policies are in need. More support in taxation and finance should be directed to the small, medium and micro-enterprises, in addition to the continued efforts to create a favorable environment for the small, medium, and micro enterprises (SMMEs). The balance of monetary and credit supply and demand should be maintained to secure adequate liquidity. The momentum of reform, innovation and structural readjustment should be retained.

Innovation and strong reform instead of strong stimulus

China is now in a 'new normal' state with a shift from high economic growth to medium-high growth, a painstaking task to readjust the economic structure, and an imperative to digest the side-effects of the stimulus package employed to fight the 2008-2009 global financial crisis.

In this stage, the government has no option but to coordinate the efforts to stabilize growth, promote reform, readjust the structure, improve people's livelihoods and prevent risks.

The innovative approach of targeted macro-control on the basis of range-based macro-control, structural reform and readjustments, reforms in key areas of systemic importance has proved effective and will be carried on in the foreseeable period of time. Innovation and promotion of institutional innovation as well as innovation in science and technology is the "golden key" to tackle the deep-seated problems. It is commonly accepted that the traditional track of investment-driven growth and reliance on real estate should be avoided.

The government will continue streamlining administration and delegating powers, and clearly define the borders of the government and market. In this way, the vitality of the market will be further released with a level playing ground set for the market players. In order to boost the service sector, the pilot programs to transform business tax to value added tax will be expanded. In-depth reforms will be practiced in fiscal and financial areas to upgrade the budgetary management system and develop a multi-tiered capital market. State-owned enterprises will be reformed and mixed ownership economy will be promoted. Supply of public goods will be increased to generate effective demand. More fiscal and financial resources will be channeled to the real economy, and emerging industries and businesses, specially favoring rural areas, agriculture and farmers, micro-businesses, and the service sector.

JAPAN

Economic growth in Japan is set to slow down from 1.4 to 1.0 percent over the next year and then to 0.7 percent in 2016. In 2015, this is expected due to a slowdown in consumption growth and investment. While consumption is expected to bounce back in 2016, the forecast is for net exports to be a greater drag on the economy reducing growth by 0.25 percentage points. Beyond the next two years, the concern for Japan is in the external sector with exports unable to grow as fast as imports.

Box 3: Japan: The Progress of Abenomics
Contributed by JANCPEC

Japanese Prime Minister Shinzo Abe`s economic reform strategy, popularly known as "*Abenomics*," was set in motion after his re-election in December 2012. *Abenomics'* "three arrows" consist of aggressive monetary easing with an inflation target of 2 percent, flexible fiscal policy and a growth strategy, all aimed at pulling Japan`s economy out of prolonged deflation and stagnation and achieving sustainable economic growth. The first two arrows have been boldly fired with positive consequences for Japan`s economy so far, with the third arrow launched in June 2013 and a revised growth strategy announced in June 2014.

The effects of the QQE and stimulus package

The first arrow, "qualitative and quantitative easing (QQE)" as a means to achieve an inflation target of 2 percent, was launched in April 2013 by the Bank of Japan (BOJ) under the bank`s governor, Haruhiko Kuroda. The BOJ intends to nearly double its balance sheet by purchasing Japanese Government Bonds of all maturities as well as other types of funds and equity over a period of about two years. Even prior to its actual implementation, the QQE remarkably altered investors' expectations of the markets, resulting in a depreciation of the yen and a sharp increase in stock prices. Between November 2012 and April 2014, the yen depreciated by about 25 percent against the US dollar and stock prices rose by about 50 percent. A lower yen is favorable for Japanese exporting companies, in particular those in the manufacturing industry, and higher stock prices created a wealth effect that boosted private consumption.

The second arrow is flexible fiscal policy. The Japanese government approved a 13.1 trillion yen stimulus package in January 2013, and an additional 5.5 trillion yen was approved in December 2013. The budgets for these stimulus packages were earmarked to assist recovery in areas hit by the 2011 earthquake/tsunami and build disaster-resilient infrastructure, to enhance business competitiveness by promoting private investment and small-and-medium enterprises, and to support local economies, including the agricultural and fishery industries, and increase the labor participation rates for women and youth. The government set targets to facilitate executing these stimulus budgets as planned, and about 70 percent of the FY2013 budgets had been executed as of the end of June 2014.

In 2013, Japan saw encouraging figures in numerous macroeconomic indicators. The real GDP growth rate was 2.3 percent, indicating that overall economic performance improved notably from the previous year. The main drivers of growth were private consumption, capital investment, government expenditure and exports. The high growth rate cannot be solely attributed to domestic policies, however, and credit is due also to the steady recovery of the world economy that has improved the overall economic situation. Nevertheless, one can observe that the QQE and fiscal policy smoothly and rightly facilitated the process of achieving Japan`s high growth rate.

As the economy was stimulated, the employment situation also improved favorably. The latest unemployment rate is 3.7 percent (June 2014), returning to the level prior to the GFC. Set against this backdrop, it has become apparent recently that the labor shortage associated with a shrinking working-age population is becoming acute in various industries, especially the construction and service sectors. This is leading to an uptrend in workers' wages, concurrent with a degree of pressure from Prime Minister Abe's call for salary increases. This year`s spring labor offensive achieved a wage increase of 2.2 percent, and workers will benefit from bigger bonuses as well. In spite of the nominal wage increase, however, the rise in the Consumer Price Index (CPI) and the impact of the consumption tax hike mean the growth of real wages was actually negative. Continuous wage increases thus still remain a critical challenge.

As the BOJ targets an inflation rate of 2 percent, there are signs that the prolonged deflationary trend in the CPI has been broken. The CPI rose by an average of around 1.5 percent during the first half of this year, excluding the effect of the consumption tax rise. While this was largely driven by higher energy and commodity prices associated with the weaker yen, there has also been a slight natural uptrend in other commodity prices.

This stronger domestic economic growth is reflected in Japan's outward foreign direct investment (FDI). The level of net FDI has been rebounding since 2011, and in 2013 it returned to its pre-GFC level. Since Abenomics was instituted, the most striking growth has been driven by investment by financial institutions expanding their business abroad. Japanese FDI into Asia, the US and the EU has steadily increased; FDI into ASEAN has seen particularly remarkable growth.

The QQE and fiscal policy are functioning well to date, though there are downsides to these short-term-oriented policies. The QQE aims to boost inflation, but given that Japan`s gross public debt is already over 200 percent of the GDP, there is a potentially higher risk of exacerbating long-term economic problems with high inflation. The interest rate for Japan 10-year Government Bonds is currently stable at around 0.5 percent, but this is a generic rate resulting from BOJ intervention. Therefore, the fundamental challenge for the first and second arrows is striking a balance on fiscal soundness. To pave the way for fiscal consolidation, Japan increased its consumption tax rate from 5 to 8 percent in April 2014 and plans to raise it to 10 percent in 2015. The Japanese government's long-term target is to achieve a primary balance surplus by 2020. Likewise, continuous efforts towards fiscal consolidation are necessary.

The third arrow: Structural reform policy
To complement the first and second arrows, the third arrow – structural reform – is a medium – and long-run economic strategy to achieve sustainable economic growth. The revised growth strategy announced in June 2014 is focused on four areas: boosting private investment, encouraging the labor participation of women, youth and the elderly, creating new markets and promoting global economic integration.

Among these targets, boosting private investment, including inward FDI, is of critical importance. One of the highlighted policies designed to promote investment is cutting corporate taxes from the current 35 percent or so to below 30 percent in the next few years in emulation of Germany and the UK, while broadening the tax base to maintain corporate tax revenue. The government has also established National Strategic Special Zones where business-friendly regulatory arrangements apply. Domestically, it is promoting corporate governance reforms such as requiring companies to include external directors on their management boards and introducing a Japanese version of the "Stewardship Code" for institutional investors. In addition, the Government Pension Investment Fund, with $1.2 trillion in assets, will be switching some of its funds into the JPX-Nikkei 400 and J-REIT.

Another key issue is increasing labor participation to counterbalance the decline in the working-age population. Prime Minister Abe has devised a policy he labels "womenomics" to encourage more women to participate in labor markets. It aims to increase the participation rate of females aged 25-44 from 68 percent in 2012 to 73 percent in 2020, and requests that companies appoint women at leadership positions. As enabling factors, "womenomics" policies seek regulatory reform and greater support for building child-care facilities. The government has also introduced a new policy to attract foreign workers.

In addition to these domestic-oriented policies, integration with global markets, in particular those in the fastest-growing Asian economies, is imperative. In this regard, Japan is involved in several ongoing negotiations for such important free trade agreements (FTAs) as the Trans-Pacific Partnership (TPP), the Regional Comprehensive Economic Partnership (RCEP) and the EU-Japan Free Trade Agreement. With the WTO Doha Round negotiations at an impasse, these mega-regional trade negotiations, once concluded, will prove of great significance in promoting international trade and investment. In addition, TPP aims for a high level of liberalization covering 21 areas – investment, service trade, intellectual property and competition policy to name a few – and reduced behind-the-border barriers. It will work in conjunction with the third arrow of Abenomics to expedite the process of Japan's domestic structural reform and liberalization.

INDIA

India, although not a member of PECC or APEC, is part of the East Asia Summit grouping and a key player in the ongoing negotiations in the RCEP trade agreement. As shown by the results in PECC's annual survey, there is a strong view that India should, at some time, become part of APEC. Over the next 12 months, India's growth is expected to improve by a full percentage point, from 5.4 to 6.4 percent growth. The improvement will be balanced across consumption, investment as well as net exports, with government expenditure's contribution remaining much the same as it was in 2014. The election of a new government which has been courted by both Beijing and Tokyo augurs well for the engagement of India in the region.

Box 4: India: Middle Class Strikes Back

Contributed by: Amitendu Palit[2]

Within seven years of its launch in 2007, *Flipkart*, now India's largest e-commerce market platform, sells more than 15 million products cutting across various categories of consumer requirements including books and lifestyle items. Its last round of fundraising fetched US$1 billion in what was one of the largest fund mobilizations done globally by e-commerce companies[3]. With around 22 million registered users and 5 million shipments per month, *Flipkart* is poised to achieve amazing scales in online retailing and e-commerce.

The *Flipkart* story is an example of how business start-ups in India can experience rapid growth in a short time through innovative supply responses to large consumer demand. India's fast expanding middle class in terms of people earning between US$10 and US$100 per day is estimated to be at around 200 million by 2020 and almost half a billion by 2030[4]. Rising personal disposable incomes would continue to positively influence propensities to consume. Catering to the diverse needs of the hungry middle class would require smart and innovative supply responses, such as those introduced by *Flipkart* by integrating product delivery and shipments with advancements in Internet use and mobile technology. With the country expected to have half a billion Internet users by 2020, and the current telecom subscriber base close to a billion, the growth of the middle class and its online consumption habits can make India's e-commerce one of the largest global industries.

The size and strength of India's market has been well known, particularly since the 'BRICS' was coined at the beginning of the century, and India widely tipped to become the biggest success among the emerging markets after China. India responded well to expectations by recording annual average GDP growth of 8.5 percent for most of the last decade, accompanied by corresponding growth of 35.5 percent in investments. Since then, however, investment growth has declined, pulling down GDP growth, too. Nonetheless, with a 5.6 percent growth rate in GDP in 2013, India still grew higher than the Asia-Pacific average (3.5 percent) and was on par with Southeast Asia (5.5 percent).

More than the growth deceleration, the 'India story' was hit badly by the inability of the authorities to implement necessary structural reforms in various sectors. This resulted in the rather inglorious 'policy paralysis' coming to characterize the previous government in India. Symptoms of weakness in external and domestic macroeconomic fundamentals visible through widening of the current account and fiscal gaps led to cynical reactions from credit rating agencies and jerky pullouts by short-term institutional investors. Careful management over the last one and a half years has restored macroeconomic health and investor confidence. Consumer spending has also picked up and the upcoming *Deepavali* (Festival of Lights) is expected to shine brighter as the capital market scales new highs.

Details are often missed for large economies like India that hide surprises in layers. Copious discussions on India's problems in allowing majority foreign equity in multi-brand domestic retail trade, particularly the incumbent BJP (Bharatiya Janata Party) government's aversion, has overlooked the open invite to foreign investors in wholesale trading and B2B (business-to-business) e-commerce. Given the chunks of the domestic market that can be tapped through these functions, it is hardly surprising that *Amazon* has picked India as its first non-US market for launching an online portal for wholesale trade. By integrating wholesale trading through online B2B functions, *Amazon* is following in the footsteps of *Walmart* and *Metro* that are already into wholesale trading in India[5]. It is also taking on existing e-commerce retail platforms and pre-empting future entries of larger players like *Alibaba* in a market that is back on the upward trajectory of a new growth crest driven by an expanding middle class.

[2] Amitendu Palit is Senior Research Fellow and Programme Lead (Trade and Economics) in the Institute of South Asian Studies in the National University of Singapore. Usual disclaimers apply.

[3] 'Flipkart Raises USD One Billion in Fresh Capital; One of the Largest Funding Rounds in E-commerce Globally', 29 July, 2014, Bangalore; http://www.flipkart.com/s/press

[4] 'China and India: tomorrow's middle classes', Ernst & Young; http://www.ey.com/GL/en/Issues/Driving-growth/Middle-class-growth-in-emerging-markets---China-and-India-tomorrow-s-middle-classes

[5] 'Amazon plans portal for wholesale merchants in India, first country outside the US', The Economic Times, 12 September 2014; http://economictimes.indiatimes.com/industry/services/retail/amazon-plans-portal-for-wholesale-merchants-in-india-first-country-outside-the-us/articleshow/42296996.cms

The new government in India seems keen on encouraging consumption by using technology in an enabling fashion. The ambitious financial inclusion program *Jan Dhan Yojana* is aiming to bring 75 million poor households under the formal banking system by issuing new bank accounts backed by life insurance and accident insurance covers. The scheme would expedite direct cash transfer of subsidies in the long run through identification of beneficiaries by their unique identification, or *Aadhar*, numbers. Putting money directly in the hands of people by eliminating intermediaries is the cleanest and surest way of abetting consumption in an inclusive manner. Aggregate consumption demand in India should significantly augment from these enabling measures that would positively influence spending at the lower income segments.

Indeed, if ongoing efforts to change labor laws by introducing greater flexibilities in hiring and firing practices succeed, then new jobs in manufacturing and labor-intensive services should increase rapidly. The job creation would act as a fresh multiplier for the middle class by adding new members at the bottom end. Consumption demand would increase, as would the demand for innovative 'budget' products.

Regional producers have already spotted the opportunity. The Chinese '*Apple*'-equivalent, *Xiaomi* is planning to open a new R&D facility in Bangalore for designing hand phones incorporating features specific to the Indian market. And why would it not if 40,000 of its *Redmi 1S* phones priced at around US$100 are booked on the *Flipkart* in 4 seconds?[6]

Innovative products and business practices planted in the fascinating dynamics of an expanding middle-income class can clearly take the Indian market to where other markets have hardly gone.

[6] Amitendu Palit, 'The Chinese Apple', The Financial Express, 9 September 2014; http://m.financialexpress.com/news/columns-the-chinese-apple--canvassing-china/1287070

SOUTHEAST ASIA

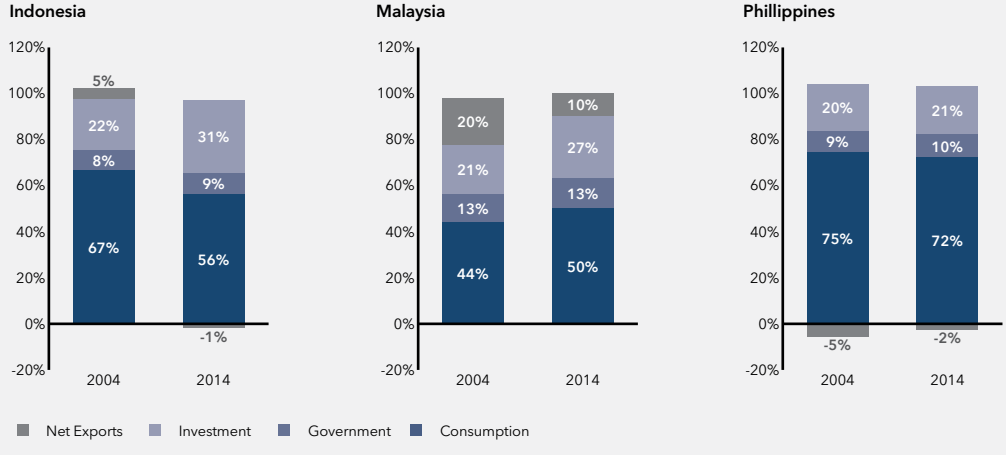
Growth for Southeast Asia as represented by the ASEAN-10 economies is set to accelerate over the next 2-3 years from 4.9 percent in 2014 to 5.2 percent in 2015. ASEAN is home to some of the most open economies in the world, with trade accounting for over 100 percent of GDP in Malaysia and Singapore, making them vulnerable to downturns in the global economy. Nonetheless, they have shown remarkable resilience in their ability to bounce back quickly from exogenous shocks.

Over the past ten years, the balance of aggregate demand has seen significant shifts, some in response to the changes wrought by changes in the external environment, others due to the increasing levels of development in the region.

In the case of Indonesia, there has been a significant shift in the balance of aggregate demand; in 2004 investment expenditure accounted for 22 percent of aggregate demand, in 2014 it is estimated to account for 31 percent. Some of this is a return to the status quo ex ante; investment in Indonesia had dropped sharply after the Asian Financial Crisis and indeed, levels are still below what are needed to remove some of the bottlenecks in the economy now apparent.

In the case of Malaysia, net exports have dropped from 20 percent of aggregate demand to 10 percent, with domestic demand, i.e. consumption and investment taking up the slack. The composition of demand in the Philippines has changed the least among the three examples shown here; net exports are less of a drag on

Figure 1.2: Balance of aggregate demand in selected ASEAN economies



Source: IMF WEO Database 2014

the economy rising from negative 5 percent to negative 2 percent while consumption's share of demand dropped from 75 percent to 72 percent. The forecast for GDP growth in Thailand in 2015 is 3.8 percent, a significant improvement over this year at 2.5 percent where political instability and natural disasters have not helped it deal with relatively weak external demand.

Next year, 2015, will be a critical year for the ASEAN integration experiment with the deadline for the completion of its Economic Community looming at the end of the year. However, challenges lie ahead if it is to maintain its dynamism over the medium to long term.

Box 5: ASEAN Economy Post-2015: Issues, Challenges, Policies
Contributed by: Giovanni Capannelli, Asian Development Bank Institute, Tokyo

By the end of 2015, ASEAN will be launching the ASEAN Economic Community (AEC), which is expected to enhance its members' GDP growth through productivity and efficiency gains generated by domestic structural reforms and economic integration. A proper combination of domestic reforms and initiatives for closer integration that complement and reinforce one another are indeed needed to promote the region's equitable and inclusive development, strengthen macroeconomic stability, enhance competitiveness and innovation, as well as protect the environment and manage natural resources.

A recent study by the Asian Development Bank Institute (ADBI) entitled, "ASEAN 2030—Toward a Borderless Economic Community" identified the region's long-term economic aspirations and challenges, offering a wide range of recommendations to policymakers. The findings suggest that ASEAN can enter a high-growth scenario, during the two decades from 2010 to 2030, tripling average real per capita income while raising quality of life to average levels enjoyed today by members of the Organization for Economic Cooperation and Development (OECD). Average incomes are expected to grow faster in the less developed ASEAN economies of Cambodia, Laos, Myanmar, and Vietnam (CLMV) than in the more advanced ASEAN-6, contributing to a narrowing of intraregional development gaps. But if ASEAN members fail to introduce the appropriate policy mix combining structural reforms with initiatives for closer economic integration, they may enter a low-growth path that would lead to an average GDP expansion of no more than 3 percent per year, as economies fall into the middle income trap and are unable to manage emerging issues such as natural disasters, climate change, territorial disputes, and internal political tensions.

ASEAN economies remain considerably diverse, marked by huge development gaps across and within members. Yet, they are exposed to common risks and challenges in facing rapid transformations in the global environment and they increasingly realize the importance of shaping common economic growth strategies as they feel competitive pressures arising from China, India, and other emerging economies in Asia as well as other parts of the world. And while it is unlikely that by 2015 the AEC will be fully in place (even the EU common market is still quite incomplete), the study suggests that ASEAN's long-term growth strategy should be to deepen the AEC into a truly borderless economic community by further lowering tariff and especially non-tariff barriers, creating more effective systems for resource pooling, and introducing innovative structures to manage labor and capital markets—as they become progressively liberalized. Overall, closer integration requires stronger intraregional policy coordination mechanisms. ASEAN needs to introduce proper schemes for mutual recognition of standards and regulatory harmonization to enable shifting responsibilities from national agencies to regional bodies while strengthening functional institutions.

The study also highlights the need for reforming some of ASEAN governance principles to keep pace with the expanding economic agenda and enhance institutional efficiency. This relates in particular to increasing flexibility in decision-making and financial contributions, and introducing proper feedback mechanisms and sanctions against non-compliance of members' commitments. Human and financial resources for the ASEAN Secretariat must also increase considerably as their current level is largely inadequate to accomplish an institutional mandate, which has been expanding over the last decade, especially since the introduction of the ASEAN Charter in 2007.

Enhancing macroeconomic and financial stability
One important lesson from past financial crises is that policy frameworks overly designed for rapid growth can destabilize financial markets, damaging economic development. Prudent and coherent macroeconomic policies are instrumental in balancing the need to both sustain economic expansion and ensure overall economic and financial stability. And while national

measures are always the first line of defense, the macroeconomic framework increases its regional dimension as national economic barriers are brought down over time, heightening the risk of contagion. Thus policy cooperation and coordination assume central importance in formulating strategies aimed at preventing economic and financial crises.

To increase resilience to macroeconomic shocks, financial stability should be a clear policy objective, with national authorities conducting economic and financial supervision using proper macroprudential tools and ensuring banking soundness through periodical monitoring and stress-tests. Policies should ensure flexibility in adjusting to shocks, while developing strong external positions as self-insurance against financial crises and carefully monitor short-term capital flows to manage risks and volatilities. Regionally, authorities should establish an ASEAN Financial Stability Dialogue (including finance ministries, central banks, financial supervisors, and market regulators) and introduce a flexible mechanism to maintain stable exchange rates between regional currencies in times of stability, while providing flexibility in times of stress. ASEAN members should also develop 'regional guidelines on effective capital control measures' to assist authorities on deciding whether or not—in case of excessive short-term capital flows—capital controls are needed as an additional, temporary and well-targeted macroeconomic tool to help maintain economic and financial stability.

Supporting equitable growth

Coupled with social and demographic transformations, inequality is one of the most difficult challenges ASEAN faces. While development policies have largely reduced poverty and improved living standards, many people continue to live on less than US$2 a day and over recent decades Gini coefficients have generally worsened throughout the region. Improving economic convergence within and across members is a key ASEAN development challenge.

National policies are needed to draw in the marginalized, offering equal opportunities to all. Macro-level programs are important to narrow income gaps across the region, improving social cohesion and welfare. They must be accompanied by inclusive policies, introducing schemes that support SMEs, increase financial inclusion, and enhance governance and regulations to improve education and healthcare. A distinct set of policies is also needed to avoid falling into the middle-income trap, including measures aimed at promoting knowledge-led growth, R&D investment, and reducing business costs. ASEAN's region-wide strategy to support equitable and inclusive growth is based on the Initiative for ASEAN Integration and the ASEAN Framework for Equitable Economic Development—which include support from the ASEAN-6 to CLMV countries. In addition to implementing these strategies it is important to establish an ASEAN Convergence Fund, which aims to mitigate the negative impact of regional economic integration initiatives on specific groups of people and sectors, while fostering growth in lagging regions. In particular, such fund could be created by enlarging the existing ASEAN Development Fund, entrusting qualified professionals for its administration.

Promoting competitiveness and innovation

The rise of the China, India and other emerging economies are increasingly pushing ASEAN to enhance its competitiveness especially with regard to the way production and distribution systems are being organized. And while ever more efficient logistics systems are needed to improve production efficiency, economic progress requires eliminating trade and investment barriers as well as increasing the free movement of production factors such as labor, capital, and information.

ASEAN economies show pronounced diversity in global competitive rankings depending on the presence and quality of institutions, economic and social infrastructure, macroeconomic policy, the business climate, corporate strategies, and production networks. Although many economies remain product and process imitators, in the next decades through proper investment in R&D and innovation most of them should be able to reach technological frontiers and build competitiveness in a number of non-industrial sectors, from high-yielding crops in tropical agriculture, to tourism, telecommunications, and finance, to name a few.

Policies that promote competitiveness and innovation focus on better social infrastructure, political institutions, and the environment for doing business. R&D investment is critical for technological advancement and innovation. It is also important to introduce common ASEAN product and governance standards to create a single market for the region. To complement national efforts, ASEAN should create its own brand—a "Made-in-ASEAN" product label. To this regard, establishing a regional agency for the certification and standardization of "Made-in-ASEAN" products will have a multiplier effect not only on industrial development, but also in terms of strengthening

the ASEAN identity of firms and individuals. Among other agencies, the ADBI study suggests establishing an 'ASEAN Competitiveness Institute' to formulate a regional innovation strategy and construct a framework for a regional R&D policy based on accelerating technological diffusion and absorption in areas with large spillovers and exploiting science-R&D-innovation synergies in biotechnology and nanotechnology.

Protecting the environment and managing natural resources
Although natural resources are abundant across Southeast Asia, they are depleting rapidly as they are increasingly used for industrial production and to meet consumption needs—and when transformed into energy, most natural resources unavoidably aggravate environmental pollution. As ASEAN becomes an integrated production base by implementing the AEC, the lack of a unified regulatory regime for environmental protection may cause firms to gravitate to countries with weak environmental regimes, worsening overall environmental standards. The key challenges related to promoting sustainable development relate to balancing rapid growth while ensuring environmental stewardship; managing energy supply and demand; and handling urbanization and the expansion of the middle class. Following a 2010 ASEAN Blueprint that adopted ten priority areas for environmental protection, the Ministerial Meeting on the Environment introduced several agreements to lower carbon emissions, reduce greenhouse gases, manage water resources, and lower transboundary haze pollution.

While ASEAN resolutions are non-binding nationally, countries should proactively introduce long-term development plans that reflect decisions taken regionally and agree on an overall approach for mainstreaming "green growth" in national strategies. In particular, they should promote "green" products adopting common standards across the region and provide new impetus for joint-development of niche sectors. Overall, national policies should be focused on controlling pollution and solid waste, improving energy efficiency, providing safe water, and managing urbanization. Meanwhile, as ASEAN implements the AEC and becomes an integrated production area, policymakers should encourage policies that tax environmental "public bads" and eliminate harmful subsidies that encourage inefficient use of natural resources. They should also establish a region-wide regulatory regime protecting the environment, including the introduction of strict product and governance standards.

PACIFIC SOUTH AMERICA

As Southeast Asia completes a stage of its integration experiment, a new one is under way on the other side of the Pacific that will bring together economies on South America's Pacific coast closer together and moreover to bring them closer to the dynamism of their Asia-Pacific through the Pacific Alliance. Mexico and Chile are forecast to show the best improvement in growth over the next 12 months, accelerating by 0.4 percentage points.

OCEANIA

The three economies of Oceania covered in this report show diverging fortunes. As discussed above, Papua New Guinea is expected to be the fastest growing economy in the region at close to 22 percent growth, mostly as a result of a sharp improvement in the external sector as well as continued robust consumption growth. For Australia, growth is expected to be at roughly the same pace as in 2014. However, the headline number masks some changes in the contribution to growth, a positive swing of 0.2 percentage points is expected in investment to make up for a decreased contribution from the external sector.

For New Zealand, growth is expected to slow by 0.2 percentage points, largely due to a decreasing contribution from investment to overall demand.

NORTHEAST ASIA

As a group, Northeast Asia is dominated by the massive economies of China and Japan, which combined, account for 80 percent of the sub-region's economic weight. Over the next 12 months, Chinese Taipei is expected to improve its growth almost a 1 percentage point, while Korea and Hong Kong (China) will grow at roughly the same rate. How the current Occupy Central movement impacts growth in Hong Kong (China) will depend largely on how it lasts and the business community becomes concerned and begins to postpone investments.

THE EXTERNAL SECTOR

Trade growth in the region is forecast to remain relatively weak over the coming years. Export growth is forecast to be at an average of 6 percent a year between 2014 and 2019 compared to the 10.8 percent growth between 2003 and 2007.

As with the GDP story, there are also changes in where the growth is coming from. Prior to the GFC, the share of export growth between emerging and advanced economies was roughly 60-40 percent in favor of emerging economies; over the next 5 years the balance is reversed with advanced economies contributing roughly 55 percent a year to the region's total export growth.

On the import side, prior to the crisis, emerging economies accounted for, on average, 52 percent of the region's import growth. Looking ahead over the next five years, the expectation is that they will account for around 42 percent of the region's import growth.

Another point that has been continuously made is the changing composition of growth. With consumer demand relatively weak in traditional markets such as the US and the EU, the expectation is that either domestic demand will have to take up the slack or new markets will need to be found.

CURRENT ACCOUNT BALANCE

The transpacific current account balance, for long a concern, remains muted. Towards the end of the forecast period however, the imbalance is beginning to reach the same levels in US dollar terms. In terms of percent of GDP, the imbalance remains manageable: the US current account deficit is at 2.8 percent of GDP, while China's surplus is at 3 percent of GDP.

In reference to Figure 1.6, presenting the data by sub-region masks over substantial differences in current accounts, especially over this long time period. The imbalance in terms of percentage of GDP reached its zenith in 2006. Within Southeast

Figure 1.3: Asia-Pacific trade growth

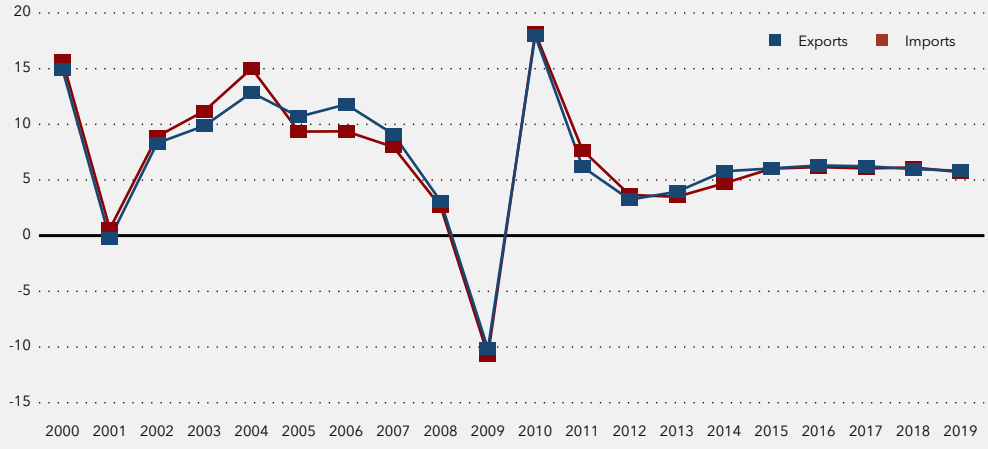


Figure 1.4: Export growth

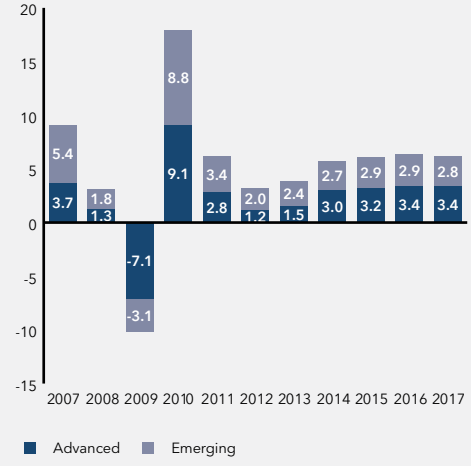


Figure 1.5: Import growth

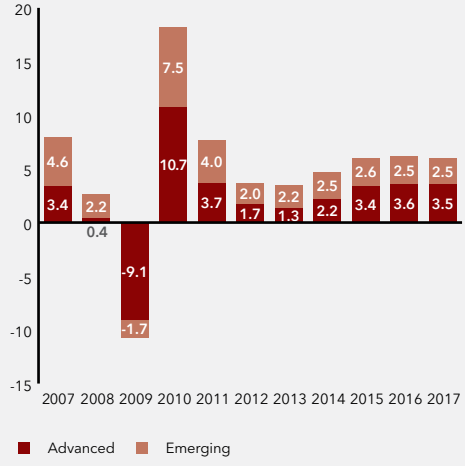


Figure 1.3 to 1.5: Source: IMF WEO Database April 2014

Figure 1.6: Transpacific current account balance

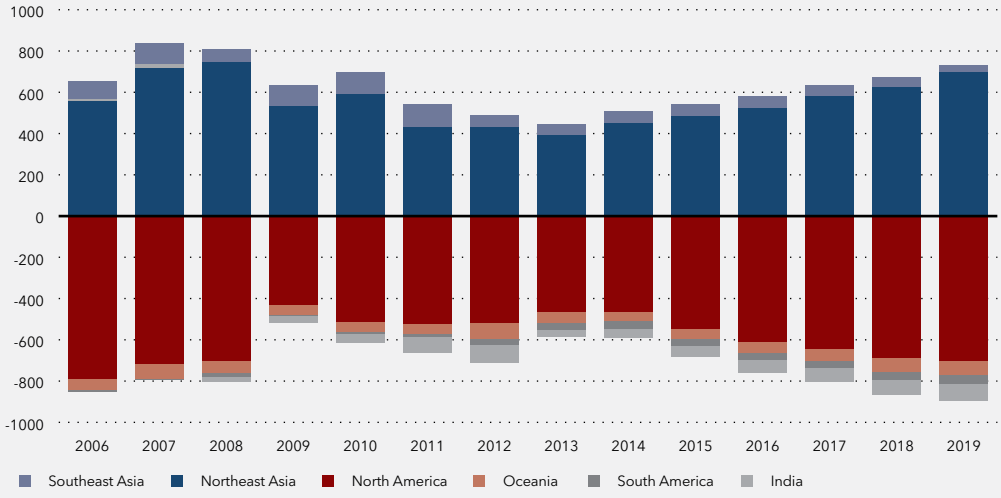


Figure 1.7: Asia-Pacific vs. Global Growth

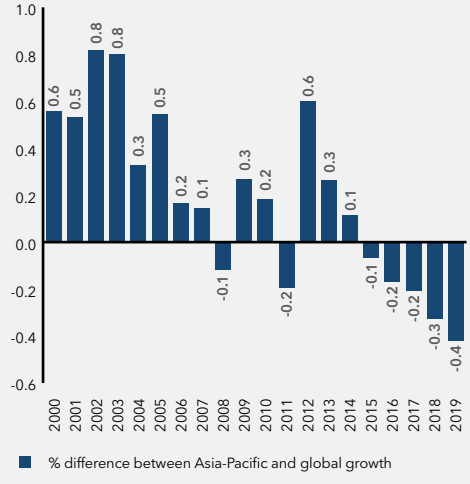


Figure 1.8: Emerging and advanced economy growth in the Asia-Pacific

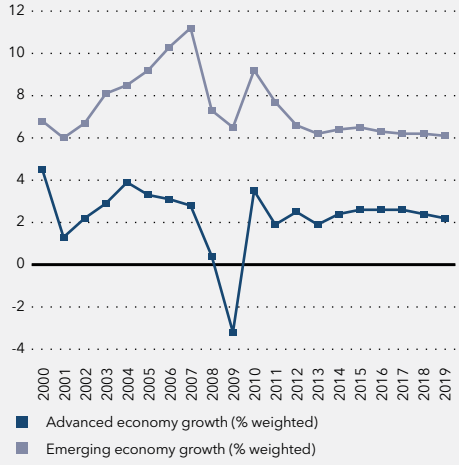


Figure 1.6 to 1.8: Source: IMF WEO Database April 2014

Asia, Indonesia has since moved from running a current account surplus to a deficit accounting for the sub-region's significantly reduced contribution to the surplus side.

In looking at the imbalance issue through a transpacific lens, it misses one of the central changes that has taken place in the world economy. Germany has moved from running a current account deficit in 2001 to running the largest surplus of any major economy in the world, almost US$100 billion higher than China's in 2013, and in percentage terms, at 7.5 of GDP, close to those run by China in the run up to the GFC.

THE FUTURE OF GROWTH IN THE ASIA-PACIFIC

As the global economy enters into a 'new normal' of slower growth, there are questions on whether the Asia-Pacific can continue its role as the anchor of global growth. For the first decade of the 21st century the Asia-Pacific grew at around 0.4 percentage points higher than the world economy. However, for the second decade, the forecast for the region is either at par or below global growth. Of concern is that the differential is on an increasing trend, calling into question the future of the region as the anchor for global growth.

The slowdown in regional growth should not come as a surprise. Over the past 25 years, many regional economies have graduated from being low income to middle income economies and a few are now in the high income bracket. However, the risk for those middle income economies is that they enter into the so-called middle income trap and are unable to graduate to the high income level.

For the period 2000-2009, the emerging economies of the region grew at an average rate of around 8.1 percent while the advanced economies grew at around 2.1 percent a year.

For 2010-2019, the forecast is for emerging economies to grow at 6.8 percent and advanced economies at 1.9 percent. While growth for both groups is slower, the reduction in growth for emerging economies of 1.3 percentage points is far more significant.

BALANCED GROWTH

In addition to the need to boost growth, a lot of emphasis is being placed on the composition of growth, i.e. to make it higher quality and more balanced. In 2009, a PECC taskforce used a simple simulation to estimate the magnitude of changes to the pattern of aggregate demand to avoid the excess imbalances in the region. The basic assumption was that growth in the pre-GFC was imbalanced, driven by excessive consumption in the US facilitated by cheap credit. The PECC work attempted a simple simulation exercise to see if the growth rates prior to the crisis could be maintained by redistributing where growth came from, among different regional economies. The basic underlying assumption was to keep the US current account deficit at 3 percent of GDP rather than the 6 percent that it reached in 2006. A few key points emerged from the study: a number of surplus economies in East Asia could sustain their growth rates in the face of declining external demand by increasing either consumption or investment, while the US needed to decrease the percentage share of private consumption and increase exports.

Any assessment at this current juncture needs to come with some caveats. The first is that stimulus policies adopted in response to the crisis remain in play. The second is that these are snapshots of two specific points in time – that should represent the general structure of the region's economies but there may be reasons why 2007 and 2014 are not necessarily representative. The third is that the GDP includes significant statistical discrepancies, in some instances larger than the actual components of GDP – namely, consumption, investment, government expenditure and net exports.

Moreover, while the balance of aggregate demand has changed, this has brought with it some additional challenges that policy makers need to confront. Some of these structural problems are most severe in the region's two largest economies – China and the United States.

The core thesis of the rebalancing was whether the region – or indeed the world – could maintain the kind of growth rates from the pre-crisis period at a time when demand in advanced economies was likely to be low as consumers rebuilt their balance sheets. The suggested answer was yes, but there needed to be a much stronger emphasis on domestic demand in the region's emerging economies.

China has been successful in maintaining impressive rates and indeed has been managing gradual change in the composition of aggregate demand. However, it has seen significant investment growth that has been holding up domestic demand rather than an accelerated consumption. In the case of the United States, consumption has maintained, if not increased, its significance in the economy while both government expenditure and investment have declined in importance. The positive news is that net exports are now less of a drag on the economy.

Of concern is the slow progress being made in the region's third largest economy – Japan, where consumption remains relatively weak. While Japan's' trade surplus has indeed decreased, this has mostly been due to the shutdown of its nuclear reactors which has precipitated a need to import more energy.

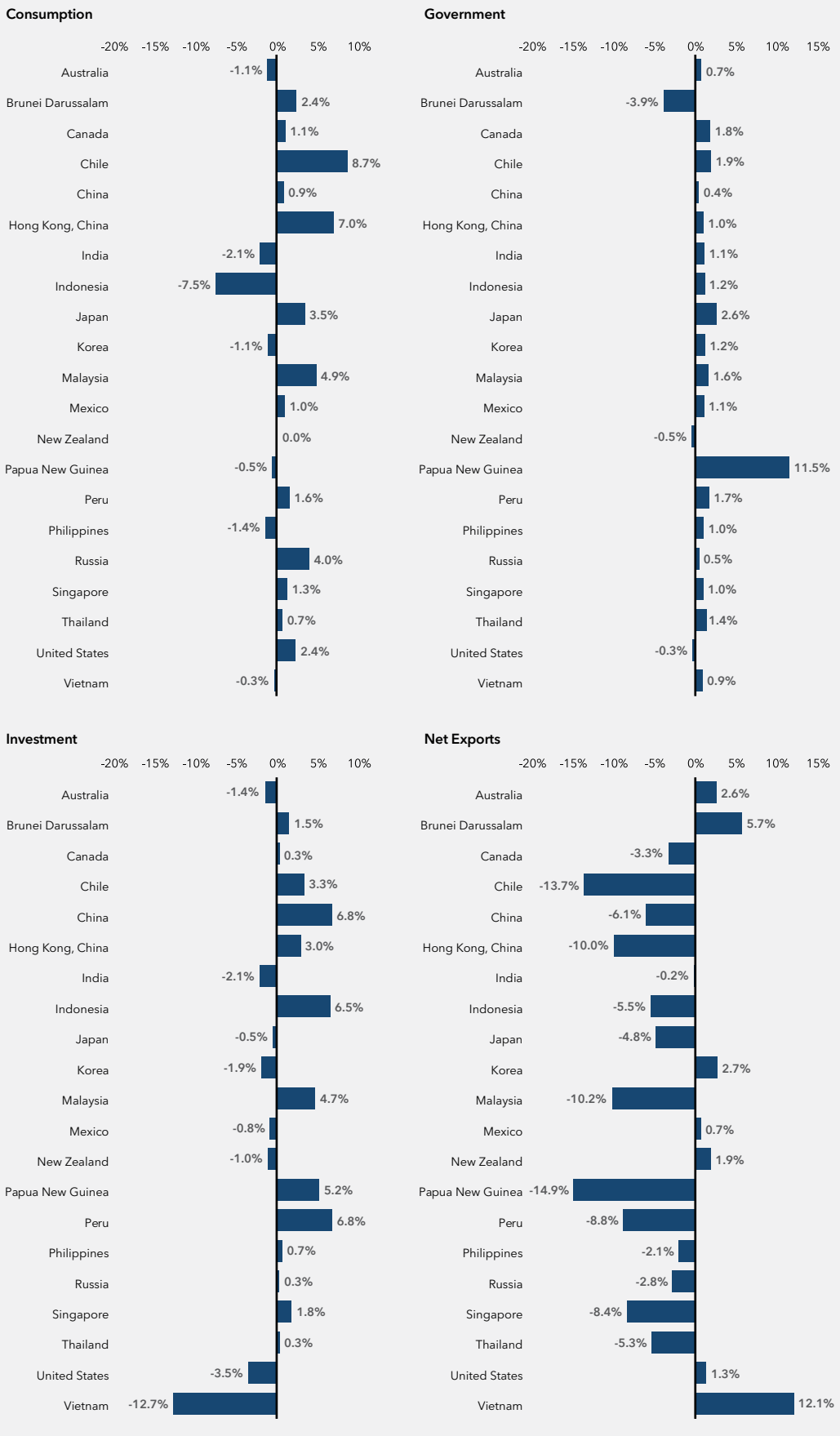
However, the region's two largest economies, China and the United States, are still facing a number of challenges that make an assessment at this stage early. As part of the stimulus measures in response to the crisis, investment in China has risen from the already high baseline in 2007 of around 39 percent to 46 percent of GDP. Without this stimulus it is probable that growth would have been much slower in recent years, the challenge now is weaning the economy off this reliance on investment and finding alternative engines of growth. Conversely, investment as a percentage of US GDP has come down and aggregate demand has been supported by rising consumption and improvements to net exports.

Figure 1.9 shows the estimated changes to the composition of aggregate demand in a number of Asia-Pacific economies between 2007 and 2014. The most obvious change that has taken place over the past seven years is the reduction in the importance of net exports to most economies. This should be welcomed given the rebalancing thesis outlined above. However, it is not at all clear whether this represents a structural shift in economies or simply a reaction to the lack of demand for exports from key markets.

CONSUMPTION

One of the key questions being asked is the extent to which growth for the region's middle income economies is shifting from being export and investment-driven towards domestic demand – especially consumption. The forecast for 2014-2019 shows a considerable increase in the annual growth of private consumption. Consumption in the Asia-Pacific is forecast to growth by approximately 5.9 percent a year over the next few years or an increase in US dollar terms, around US$1.4 trillion in 2015 and US$1.6 trillion in 2016. Over the medium-term, consumption in the region is forecast to increase from 2014 to 2019 by a total of US$6.8 trillion.

Figure 1.9: Estimated changes to share of GDP 2014 (percentage points change from 2007 baseline)



Source: IMF WEO Database April 2014

While much of the growth in consumption expenditure will continue to come from the region's more advanced economies – the United States alone accounts for around 43 percent of total Asia-Pacific consumption – over the next 5 years, the region's emerging economies are forecast to account for an increasing percentage of consumption. In 2013, they accounted for 28 percent of total consumption expenditure; by 2019, emerging markets are expected to account for 32 percent.

As seen in Figure 1.10, at the moment, food and drinks account for around 31 percent of consumption expenditure in the region's emerging economies, compared to 12 percent in higher income economies. This is likely to change as more consumers in emerging economies become middle class.

Another category with significant differential is expenditure on healthcare. On average, consumers in emerging economies spend around 6 percent of their income on health, while those in higher income economies around 11 percent. As incomes increase in emerging economies and a smaller proportion is spent on food, consumers are likely to spend more on health similar to consumers in higher income economies.

The last category of expenditure where these is a marked difference in expenditure is miscellaneous goods and services. This includes what are considered luxury or nonessential items such as hairdressing salons and personal grooming; appliances and products for personal care; jewelry and watches, and insurance. On average, 14 percent of consumer expenditure in higher income economies is spent on this category compared to just 8 percent in middle income economies.

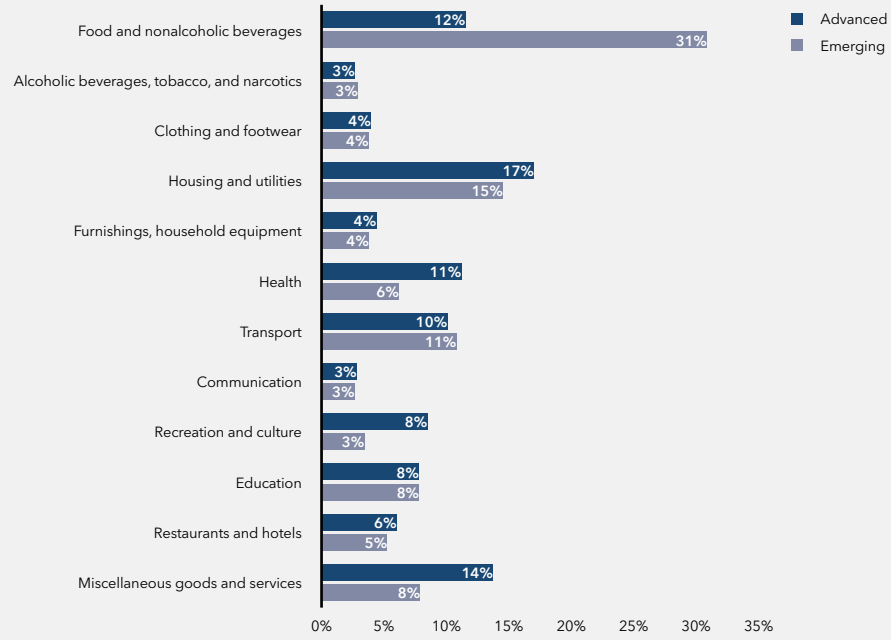
PECC's survey results in Chapter 3 show that the region's policy community thinks that consumers in emerging markets are likely to spend more on electronics, cars, household appliances – and other items associated with becoming a middle class consumer compared to their counterparts from more advanced economies. This opens significant opportunities for the corporate sector to switch from a focus on advanced economies to demand from an emerging middle class in the region.

INVESTMENT

While advanced economies are driving consumption growth in the region, the opposite is true in terms of investment/gross capital formation. Investment in the region is set to increase by US$833 and US$916 billion in 2015 and 2016 respectively. Of this, emerging economies will account for approximately 55 percent.

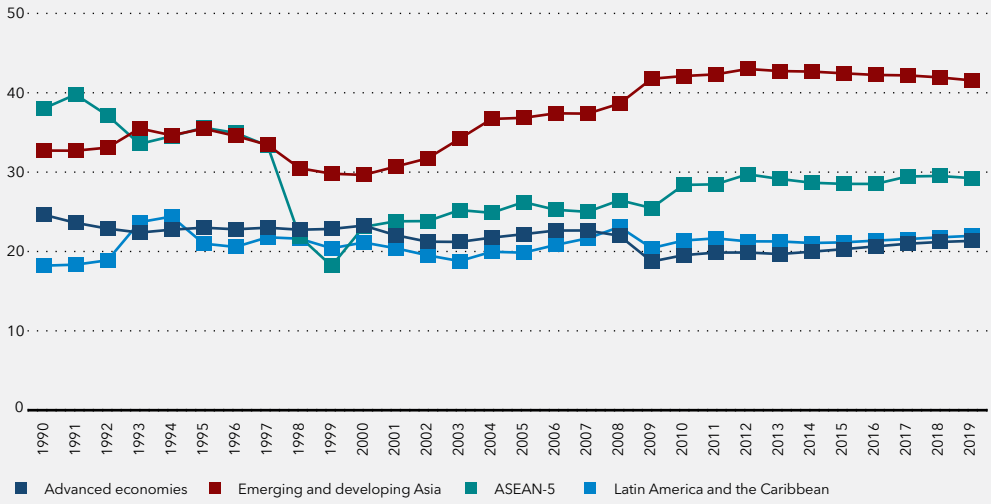
Much has been made of the need for increased investment in infrastructure both globally as well as for the region. Over the past 25 years, the investment as a percentage of GDP has been volatile. For the ASEAN-5 members, investment as a percentage of GDP was around 35 percent a year in the run up to the 1997-98 crisis, roughly the same as emerging and developing Asia. After 1997-98, the level of investment dropped significantly to around 25 percent of GDP, and even though it has been on an upward trend it remained well below the whole of developing

Figure 1.10: Average household expenditure in Asia-Pacific economies



Source: World Bank 2011 International Comparison Program

Figure 1.11 Investment as a percentage of GDP[7]



Source: IMF WEO Database April 2014

[7] Groupings used here follow IMF definitions, not used elsewhere in this report

Asia. The numbers for developing Asia are skewed by the large amount of investment in China where investment accounts for above 45 percent of GDP.

Investment in Latin America and the Caribbean is at a similar level to those of advanced economies at an average of only 20 percent of GDP, indicating an area where policy initiatives could help to increase investment and boost growth.

The prescription for increasing growth above current baseline forecasts will depend on the individual circumstances in each economy. While increased middle-class consumption in emerging Asia-Pacific economies holds much potential there are some challenges ahead peculiar to the region which is home to the most populated economies in the world.

If all APEC economies were to have same number of cars as their counterparts in OECD economies an additional 910 million cars would be on the road (in perspective, car sales per year in APEC region are about 35 million). If all APEC citizens were to fly at the same rate as OECD members there would be an additional 2.2 billion people flying a year and if all APEC citizens spent the same on healthcare as OECD there would be an additional US$7.5 trillion spent on healthcare. The resource implications are enormous.

Another challenge arises from the internet age in which consumers have the ability to know and desire the same things that their counterparts have in other economies – even if their income levels are significantly smaller.

Overcoming both of these challenges will require changes in both business models as well as the production process if the region is to meet the growing expectations of its population.

INNOVATION AND GROWTH

New Actions Needed for the Growth Strategy

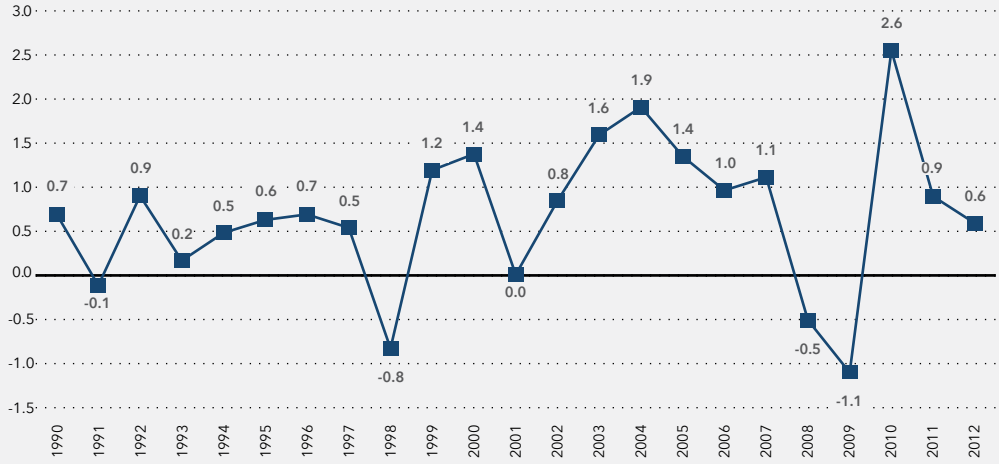
As highlighted in the previous section, regional growth is expected to moderate over the coming years and likely to be significantly lower than the levels achieved by the region in the lead up to the GFC. This 'new normal' has put significant weight on the need to take actions to support stronger regional and global growth.

The G20 has set a target of increasing baseline economic growth by 2 percentage points by 2018 as part of its commitment to addressing this concern. This is not for growth for growth's sake, but to generate the jobs needed and ensure a sustained rise in living standards and achieve a more balanced global economy. While G20 members account for 85 percent of global economic output, half of them are also members of APEC, most of which are among the fastest growing economies in the world.

While the G20 set out its agenda for stronger, more sustainable and balanced growth in the context of fiscal sustainability, APEC members set out their own strategy for balanced, inclusive, sustainable, innovative and secure growth. As shown by the results of both the 2013 and 2014 PECC survey, opinion-leaders are less than impressed with the actions taken thus far to implement the growth strategy.

The approach taken by the G20, to set a specific growth target followed by the individual action plans of economy, echoes that of APEC in respect to the Bogor Goals. While the details of the G20 plans are not yet known they will focus on four key areas:

Figure 1.12: Contribution of total factor productivity to Asia-Pacific growth (weighted by GDP US$)



*Source: The Conference Board **Total Economy Database™**, January 2014 and IMF WEO Database April 2014*

*Data from the **Total Economy Database™** is reproduced with permission from The Conference Board, Inc. © The Conference Board, Inc. 2014.*

- Reducing barriers to trade;
- Increasing competition;
- Creating more employment opportunities; and
- Improving infrastructure through increased investment.

Need to Boost Productivity

Over the past quarter of a century, the Asia-Pacific has posted impressive growth rates. However, there are a number of bottlenecks to growth that need to be addressed. One of the concerns that the region faces is the potential decline in total factor productivity (TFP). China, as the chair of APEC for 2014, has put emphasis on the challenge of the 'middle income trap' that many emerging economies in the region are facing. Figure 1.12 shows the contribution of TFP to GDP growth for the Asia-Pacific. During the boom years of 2000-2007 the average contribution of TFP was around 1.1 percent, while from 2011 to 2012, it has dropped to 0.6 percent.

Some important messages arise from a look at the contribution of factors of production to growth in the region:

- On average capital investment has contributed the most to growth of emerging markets – 20 percent more than to growth in advanced economies.
- On average labor composition has contributed much less to the growth of emerging markets than to advanced economies – almost 10 percent less.
- Investment in ICT has contributed much more to advanced economy growth than for emerging markets – 33 percent compared to 12 percent.

Over the past couple of decades, investment in ICT has contributed 0.6 percentage points to advanced economy growth and 0.7 to emerging economy. However, in terms of percentage contribution, ICT investment for emerging economies accounted for on average 12 percent of growth compared to 33 percent for advanced economies.

Moreover, economic growth for the emerging economies of the region has been overly reliant on one factor of production – investment in non-ICT capital – which contributed on average 3.4 percentage points to their growth or 60 percent. These numbers are only slightly distorted by the weight of China among the region's emerging economies and the huge amount of investment that took place after the crisis. However, discounting that extraordinary period, investment in non-ICT capital contributed on average 2.9 percentage points to the Asia-Pacific emerging economy growth during the 1990s.

In terms of the contribution to growth from labor – whether in quantity or composition, the contribution to emerging market growth has been much less volatile than it has been for the advanced economies of the region. As one would expect, labor quantity contributed significantly more to growth in emerging economies around 0.8 percentage points to GDP growth compared to 0.3 for advanced economies. However, the contribution from labor force composition was significantly higher for advanced economies 0.3 percentage points compared to 0.16 for emerging economies.

Improving Productivity

Indeed, the Conference Board's 2014 Productivity Brief[8] warns that the growth rate of TFP is less than zero for the global economy. Their analysis suggests that this has been caused by slowing demand in recent years, which caused a drop in productive use of resources that is possibly related to a combination of market rigidities and stagnating innovation.

[8] https://www.conference-board.org/pdf_free/economics/TED3.pdf

Figure 1.13: Asia-Pacific GDP growth (weighted average)

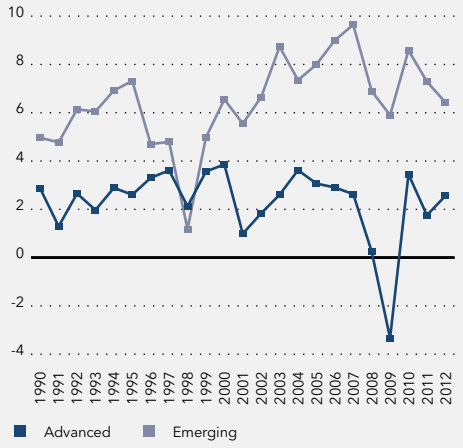
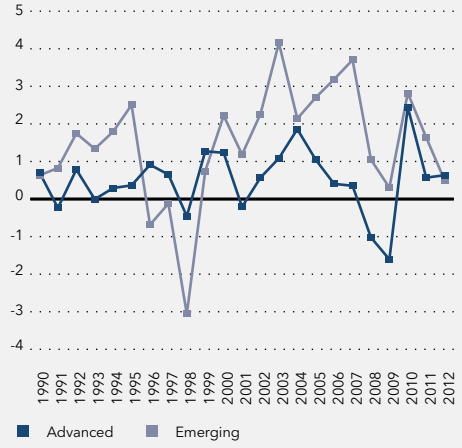


Figure 1.14: Contribution of TFP to Asia-Pacific GDP growth (weighted average)



Source: The Conference Board Total Economy Database™, January 2014 and IMF WEO Database April 2014[9]

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Figure 1.15: Contribution of ICT capital to Asia-Pacific GDP growth (weighted average)

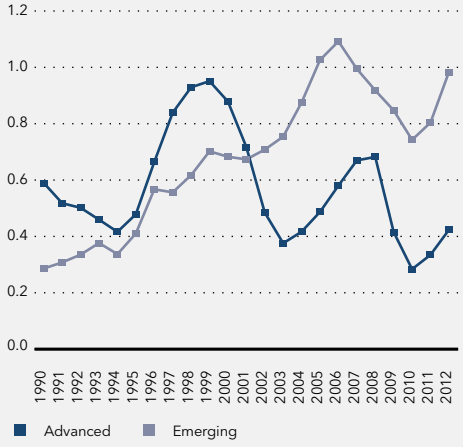


Figure 1.16: Contribution of Non-ICT capital to Asia-Pacific GDP growth (weighted average)

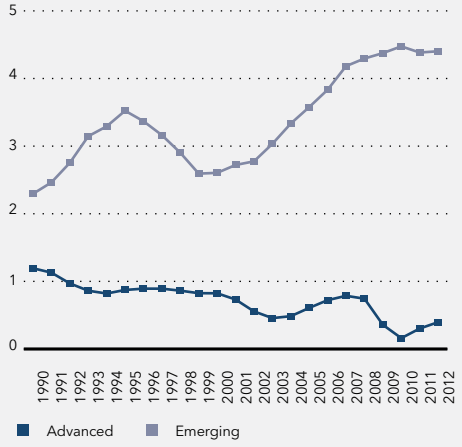


Figure 1.17: Contribution of labor quantity to Asia-Pacific GDP growth (weighted average)

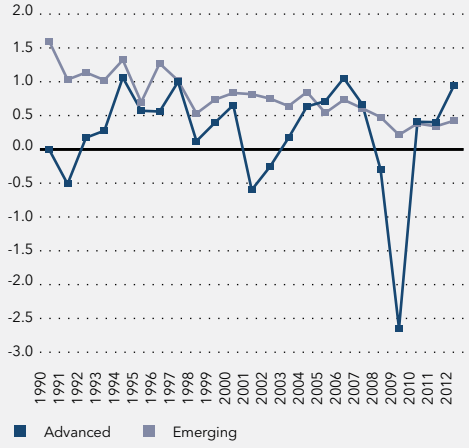
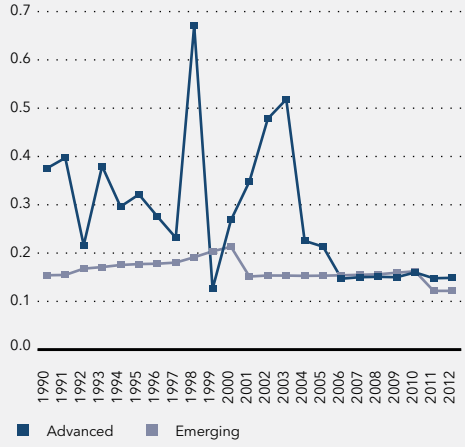


Figure 1.18: Contribution of labor composition to Asia-Pacific GDP growth (weighted average)



[9] Growth models look at the contribution of the different factors of production to growth, ie labor, capital and total factor productivity (TFP). The Conference Board's Total Economy Database further disaggregates the contribution from labor into two parts: the contribution of labor quantity (hours work) and the contribution the composition of labor (different skills levels. It also divides capital into ICT (IT hardware, telecommunication equipment, and software) and non-ICT (non-residential construction, transport equipment, and machinery). TFP is average output produced by a combination of the other inputs. For more details see: https://www.conference-board.org/data/economydatabase/

The data available does not cover all Asia-Pacific economies included in the rest of the report, and covers only: Australia; Cambodia; Canada; Chile; China; Colombia; Ecuador; Hong Kong (China); India; Indonesia; Japan; Korea; Malaysia; Mexico; New Zealand; Peru; Philippines; Russia; Singapore; Chinese Taipei; Thailand; United States; and Vietnam. Aggregates are weighted by gross domestic product in US$ at current prices.

The Innovation Challenge

Innovation is one of the five dimensions of the growth strategy that APEC Leaders adopted in response to the crisis. Progress on the strategy is due to be reviewed in 2015. As defined in the 2010 APEC Leaders' Declaration, the task was to *'create an economic environment that promotes innovation and emerging economic sectors.'* APEC Leaders put an emphasis on the enabling environment for innovation rather than any specific output that might arise from it.

The Global Innovation Index, which is a collaborative effort among Cornell University, INSEAD, and the World Intellectual Property Organization (WIPO) as co-publishers, and their Knowledge Partners, attempts to measure innovation for almost all economies. The Global Innovation Index has two sub-indices– the Innovation Input Sub-Index and the Innovation Output Sub-Index–each built around a number of pillars. The Innovation Input Sub-Index which is composed of 5 pillars provides a useful measure of the economic environment, and these are:

(1) institutions;
(2) human capital and research;
(3) infrastructure;
(4) market sophistication; and
(5) business sophistication.

As shown in Figure 1.19, there is considerable variability among the economies' rankings in terms of the environment they provide to foster greater innovation. While the region includes some of the best environments in the world for

Figure 1.19: Asia-Pacific economies ranking on global innovation index's input-sub-index

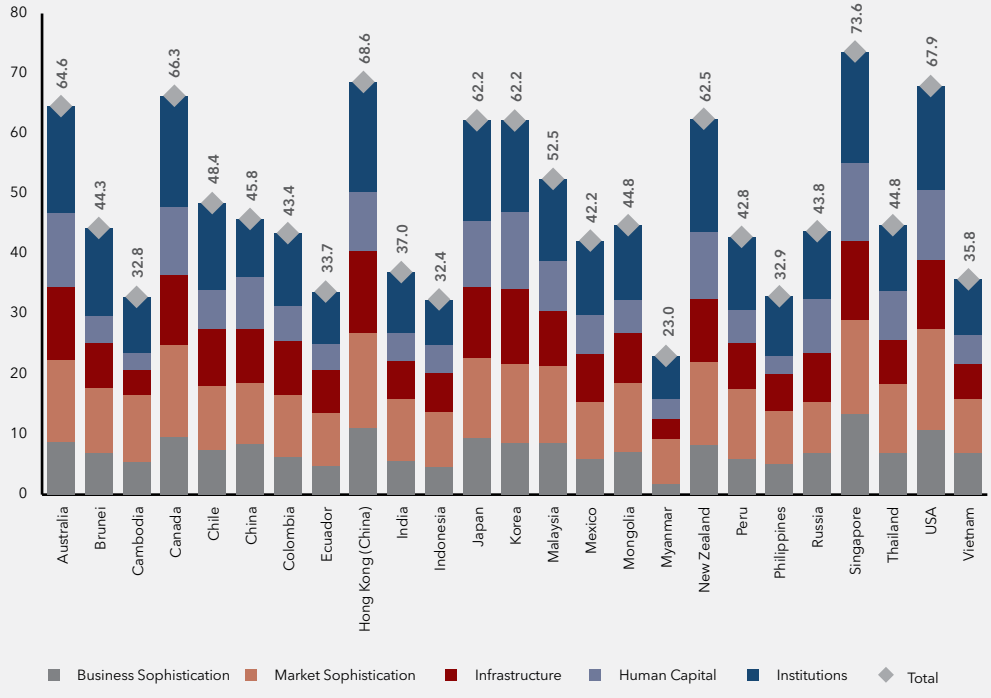


Figure 1.20: Gross domestic expenditure on R&D (% of GDP)

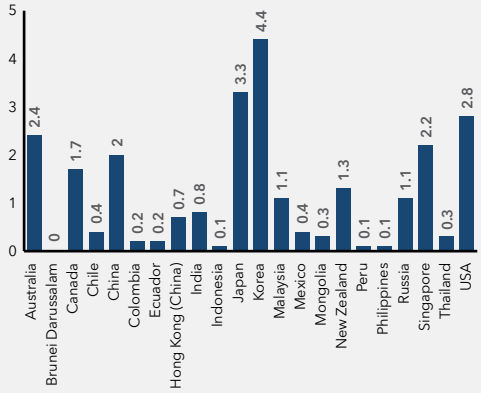


Figure 1.21: Graduates in science and engineering (%)

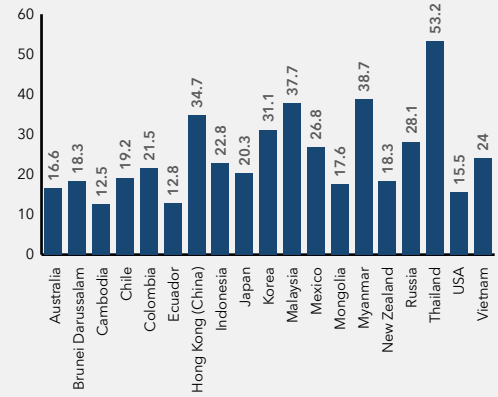


Figure 1.19 to 1.21
Source: Global Innovation Index (2014)

innovation, it also includes economies where much more could be done.

The pillars on which more could be done are business sophistication and human capital on which the region has the lowest average score compared to other pillars.

Human Capital

The human capital pillar captures 12 indicators including: education; tertiary education; and research and development (R&D). Looking at just two indicators – gross domestic expenditure on R&D; and the percentage of graduates in science in engineering – there is much that regional cooperation could offer in terms of improving the environment for innovation. For example, while the average gross expenditure on R&D in the region is about 1.2 percent, some spend significantly above this, like Korea at 4.4 percent. In terms of the percentage of graduates in science and engineering, the average for the region is around 24 percent but some economies like Thailand and Hong Kong (China) are significantly above the average. Through processes like APEC, regional economies could share experiences on how and why they chose the policies that have led to these differences as well as the ultimate results they have had.

Business Sophistication

Another metric of innovation is the extent to which the business and academic sectors collaborate on research. The data here comes

Figure 1.22: University/industry collaboration

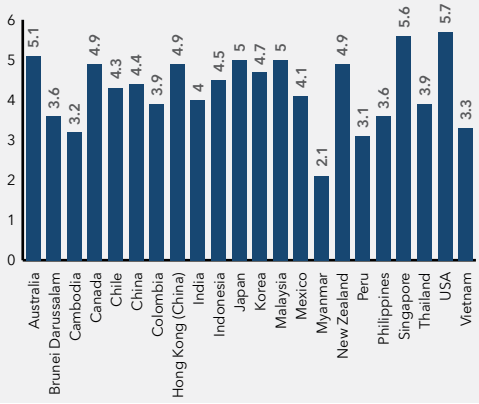


Figure 1.23: Firms offering formal training (% of firms surveyed)

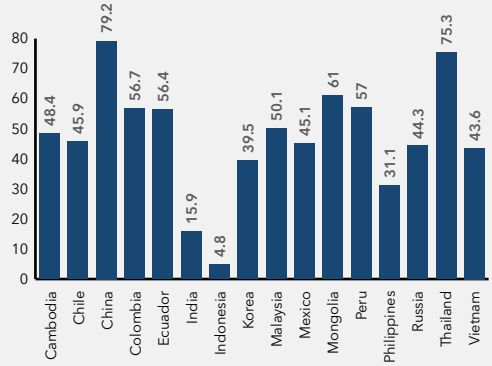


Figure 1.24: Asia-Pacific economies innovation input sub-index score (0-100)

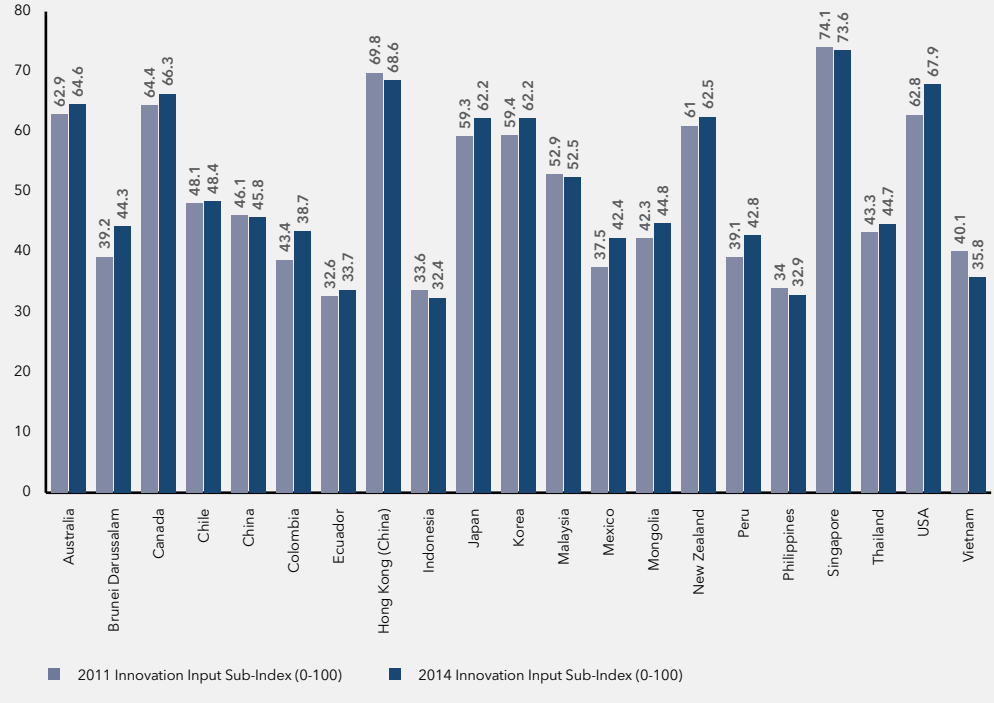


Figure 1.22 to 1.24
Source: Global Innovation Index (2014)

from the World Economic Forum's Executive Opinion Survey which asked: *"To what extent do business and universities collaborate on research and development in your country?"* The score is obtained from '1 = Do not collaborate at all' to '7 = Collaborate extensively.' While the regional average is high at 4.1, there is significant room for improvement. This would be an area where APEC's classic approach to regional cooperation of experience sharing would be valuable and give focus to its new Policy Partnership on Science, Technology and Innovation.

The idea of continuous education and vocational training has become a central topic for policy-makers. The lack or shortage of talent available was ranked as the tenth highest risk to growth in the region in this year's *State of the Region* survey and in 2013, affordable education to provide workers with the skills required to compete in a global marketplace was rated as the most important issue for which APEC Leaders should set an aspirational target. As shown in Figure 1.23, some economies like China and Thailand have placed strong emphasis on firms offering training to employees while many other economies are well behind.

Using the Global Innovation Index's ranking of economies, between 2011 and 2014, fourteen out of the 21 Asia-Pacific economies covered by the index improved their score for the innovation input sub-index. It should be noted that the index pulls together data from multiple sources, not all of which are available on an annual basis. However, the index does provide a useful basis on which to begin a discussion on both how the region has done in terms of improving the environment for innovation as well as what kind of policy initiatives might be adopted in the future.

THE FUTURE OF GROWTH IN THE ASIA-PACIFIC

Although the economic outlook remains relatively positive and there are reasons to be optimistic about the future of growth in the region, much needs to be done if the Asia-Pacific is to continue on the path it has set out over the past few decades. The region includes not only the world's three largest economies but also many of the world's fastest growing economies.

A quarter of a century ago, in recognition of the growing interdependence of this region, the APEC forum was founded. Five years later the region's leaders set out a course of actions to *'enhance the prospects of an accelerated, balanced and equitable economic growth not only in the Asia-Pacific region, but throughout the world as well,'* in the Bogor Declaration. Over the past 25 years much there has been much progress but as outlined in this chapter there significant challenges ahead. The composition of growth is changing; middle class consumption would not only be a driver of growth but more importantly, meets the aspirations of people for a better life. A renewed focus on opening up and economic integration that has been behind much of the past two decades of growth is needed – as will be discussed in the next chapter.

CHAPTER 2

CAN RCEP AND THE TPP BE PATHWAYS TO FTAAP?*

The vision of free trade in the Asia Pacific has remarkable staying power. Nearly fifty years after it was first proposed[1], it is gaining traction due to the emergence of the Regional Comprehensive Economic Partnership (RCEP) and Trans-Pacific Partnership (TPP) initiatives and the continuing stalemate in global trade negotiations.

As host of the Asia Pacific Economic Cooperation (APEC) forum in 2014, China has made the Free Trade Area of the Asia Pacific (FTAAP) a priority. A wide regional agreement could generate large benefits and help to overcome stubborn challenges to economic integration in the region and the world.

RCEP and the TPP are critical—and arguably indispensable—steps toward FTAAP, but will not guarantee its realization. They will promote economic integration among members, but will not offer comprehensive regional coverage or, at first, broadly acceptable rules. Since neither negotiation includes both China and the United States, much of the economic and political benefits of regional economic integration would be still unrealized. At worst, the two agreements could establish conflicting standards that are difficult to reconcile and would make the "noodle bowl" of overlapping trade agreements more intractable. Intensified discussions of FTAAP could help to turn the current negotiations, into stepping stones rather than stumbling blocks on the path toward it.

Some paths to FTAAP—indeed the simplest paths —would involve the conclusion of RCEP and TPP and the enlargement of one or the other to cover the region. But another would be to create a new "umbrella agreement" to complement RCEP and the TPP. We examine these pathways, estimate benefits on them, and show that the largest gains would result from those that consolidate RCEP and TPP under high standards. We consider one pathway in depth—an FTAAP umbrella agreement that would set relatively high standards, encourage liberalization across the Asia-Pacific, and offer alternative levels of rules to diverse economies.

The obstacles to such positive outcomes and the time required to achieve them cannot be underestimated. The building blocks of the regional system, RCEP and the TPP, face strong political opposition[2] in many economies despite their overall benefits. Efforts to integrate these agreements will be still more difficult and will require a favorable geopolitical environment. Yet the opportunities are also great.

APEC AND FTAAP

APEC's historic goal is region-wide economic integration. As one of its principal architects, Prime Minister Bob Hawke of Australia, put it, APEC's job is to *"investigate the scope for further dismantling of barriers to trade within the region"* (Hawke, 1989). The Bogor Declaration of 1994 made this vision concrete by committing to *"free and open trade and investment in the Asia-Pacific no later than the year 2020"* (APEC, 1994). Related initiatives by APEC and its member economies are summarized in Figure 2.1. APEC members have made significant progress toward the Bogor Goals, reducing average applied tariffs from 16.9 percent in 1989 to 5.8 percent in 2010 (APEC Policy Support Unit, 2012), but the 2010 target of full liberalization by developed members was not met, and it is widely expected that the 2020 target for developing members will be also missed.

The high bar of the Bogor Declaration nevertheless continues to attract region-wide support. What would be the best way to make progress toward it—global, regional, or unilateral liberalization? The global route seems blocked, and unilateral policies are sometimes moving in a reverse direction. In 2004, the APEC Business Advisory Council (ABAC) proposed a "Free Trade Area of the Asia Pacific (FTAAP) to consolidate and accelerate progress toward achievement of

* Contributed by Peter A. Petri and Ali Abdul-Raheem. The authors are grateful to Wendy Dobson, Charles Morrison, Eduardo Pedrosa and Jeffrey Schott for comments on an earlier draft.

1 Regional free trade was formally proposed at a 1967 conference organized by Professor Kiyoshi Kojima of Hitotsubashi University. The conference led to the creation of the Pacific Trade and Development Forum (PAFTAD) in 1968 and, indirectly, the Pacific Economic Cooperation Council (PECC) in 1980. These set the stage for the Asia Pacific Economic Cooperation (APEC) initiative in 1989 (Patrick, 1996).

2 A recent global survey shows wide skepticism about the employment effects of trade agreements in the United States and many other advanced economies (Pew Research Center, 2014). These views may change once governments enter the debate; lacking concrete results so far, most have not yet launched a vigorous case for new trade agreements.

Figure 2.1: Timeline of regional initiatives by APEC economies

1994	• APEC leaders adopt Bogor Goals calling for free trade and investment by 2010 for developed economies and 2020 for developing economies
1996	• APEC economies submit collective and individual action plans on Bogor Goals
1997	• ASEAN, China, Japan and Korea form ASEAN+3 group • APEC leaders endorse "Early Voluntary Sectoral Liberalization" (EVSL)
1999	• Negotiations on EVSL collapse and the project is passed to the WTO
2002	• Chile, New Zealand and Singapore, with Brunei as observer, meet on the sidelines of APEC to launch FTA negotiations
2004	• ASEAN+3 economic ministers commission feasibility study of the East Asia FTA (EAFTA) • APEC Business Advisory Council (ABAC) recommends feasibility study of the Free Trade Area of the Asia Pacific (FTAAP)
2005	• ASEAN convenes the East Asia Summit (EAS) comprising the ASEAN+3 economies plus Australia, New Zealand and India • The Trans-Pacific Strategic Economic Partnership (TPSEP) agreement is signed by Brunei, Chile, New Zealand and Singapore • APEC Leaders endorse the "Busan Roadmap," which includes drafting model chapters for high-quality, transparent and consistent regional FTAs
2006	• ABAC and the Pacific Economic Cooperation Council jointly study the feasibility of FTAAP • APEC leaders pledge further study of FTAAP
2007	• Japan proposes a Comprehensive Economic Partnership of East Asia (CEPEA) • APEC Leaders endorse a comprehensive report on regional integration • APEC Leaders agree on trade and investment facilitation action plans
2008	• Australia, Peru, the United States and Vietnam enter negotiations with P-4 on the Trans-Pacific Partnership (TPP) • APEC publishes "Convergences and Divergences of APEC RTAs/FTAs"
2010	• APEC identifies the EAFTA, CEPEA and TPP as pathways toward FTAAP
2011	• China, Japan and Korea complete study of trilateral FTA • China and Japan agree to advance the EAFTA and CEPEA in parallel • ASEAN proposes new negotiation, eventually named the Regional Comprehensive Economic Partnership (RECEP)
2012	• RCEP negotiations are launched • CJK-FTA negotiations are launched

Source: Compiled by the authors.

APEC's Bogor goals" (Scollay, 2004). In 2006, US President George W. Bush noted that the idea *"deserves serious consideration"* (Bush, 2006) and the Leaders' Summit of 2006 *"instructed Officials to undertake further studies on ways and means to promote regional economic integration, including a Free Trade Area of the Asia-Pacific"* (APEC, 2006). The resulting study concluded that *"APEC should target a high quality and comprehensive FTAAP agreement"* (APEC, 2009).

The Leaders' Summit in Yokohama in 2010 provided further detail, noting that FTAAP *"should be comprehensive, high quality and incorporate and address 'next generation' trade and investment issues"* (APEC, 2010). The Leaders also identified regional and trans-regional liberalization initiatives—including the TPP, the ASEAN+3 and the ASEAN+6 processes—as potential pathways to FTAAP. ABAC recently suggested adding the new Pacific Alliance, comprising four Latin American economies, as a further pathway (ABAC, 2014).

APEC support is essential for FTAAP, but the forum will not be the venue for hammering out an agreement. Since 1998, when the "Early Voluntary Sectoral Liberalization" initiative failed, APEC has focused on non-binding, voluntary projects, including reducing trade costs and acting as an incubator for initiatives by subgroups of members. APEC discussions helped to clarify the details of the Information Technology Agreement (ITA) in 1996 and the proposed Environmental Goods Agreement, and APEC served as a "midwife" to the four-country TPSEP trade agreement. Through its network and analytical initiatives, APEC can also promote region-wide agreements. It has already produced model templates for FTAs (under the 2005 Busan Roadmap) and reviewed the convergences and divergences of regional trade agreements in 2008 (APEC, 2008).

China is showing interest in the FTAAP in the run-up to the Leaders' Meeting in Beijing in 2014[3]. In April 2014, Premier Li Keqiang called for a feasibility study (Li, 2014) In Qingdao, APEC Ministers Responsible for Trade (2014) endorsed drafting a *"roadmap for APEC's Contribution to the Realization of an FTAAP"* and other measures. A prominent Chinese expert has suggested conducting the feasibility study over 2015-16, beginning negotiations in 2017 and concluding

[3] Bergsten (2007) argued that China's "support, on top of that of the United States, Japan, and the other APEC members … would clinch the launch of serious negotiations" on FTAAP. Morrison and Pedrosa (2007) noted that China, Japan or the United States (or perhaps all three) would have to be champions of FTAAP to make it viable. The three economies are still not jointly committed to FTAAP in 2014, perhaps because of geopolitical strains, or because the United States and Japan see the TPP as a difficult enough priority.

them by 2020, the target year of the Bogor Declaration (Y. Zhang, 2014a). The concreteness of these proposals is noteworthy, although the timeline itself is probably too optimistic. As Tang & Wang (2014) note, discussions about the future of FTAAP still need to resolve fundamental questions about *"scope, standards, leadership and membership."*

The successful conclusion of the RCEP and TPP negotiations would help to advance FTAAP in the longer run. These agreements would develop FTA templates acceptable to key subsets of APEC members and serve as test beds for new trade rules and adjustments to them. In some countries, they may help to accelerate urgent domestic reforms that would also make future integration more likely. Regional attention would be focused on the results and interactions of the new FTAs, ideally promoting consolidation. For economies that are not members of both tracks, like China, *"there might be practical ways … to integrate the TPP pathway with the RCEP pathway in the future"* (J. Zhang, 2014). None of this can be expected to happen quickly or smoothly, but launching an FTAAP study in 2014, as China proposed, would be a timely starting point for related work.

THE PATHWAY STRATEGY

As APEC Leaders noted in 2010, FTAAP is likely to require a pathway—that is, initiatives that prepare the ground for regional agreements by connecting groups of members. Both Asian and Trans-Pacific negotiations aspire to become such pathways by developing 21st century trade rules, albeit their approaches differ. Before examining this progress, we briefly review economic theories of pathways—that is, the *dynamics* of regional integration. These theories offer insights and benchmarks for evaluating the processes underway.

What are pathways?

Much work on trade liberalization focuses on single outcomes, such as the effects of specific free trade areas. The benchmark for such analysis is free trade and much early work—including the classic study by Viner (1950)—examines how closely an agreement approximates that standard. Recent work[4], however, recognizes that economies seldom establish a free trade regime at once but rather negotiate a series of agreements toward it. Europe's path to a customs union started with six members in the Treaty of Paris in 1951 but now includes 28 countries. Dynamic effects are important. Economic integration combines a series of unilateral actions, bilateral and regional liberalization, the enlargement of existing free trade areas, as well as global negotiations. In the post-World War II period these strategies resulted in extensive, world-wide reductions in trade and investment barriers.

In an influential paper, Krugman (1991a) showed that the enlargement of trade blocs could lead to very poor outcomes—a world with three giant blocs that erect high barriers against each other. In his model, economies formed blocs in order to increase their market power and improve their terms of trade against other blocs. The end result was an equilibrium with three giant blocs that imposed high barriers and, among alternative configurations of blocs, *minimized* world welfare. However, another paper by Krugman (1991b), published almost simultaneously, showed an opposite effect. In that paper, economies that formed blocs already traded extensively with each other. The bloc then created more internal trade, rather than exploiting market power against outsiders. This pathway led to positive global effects. Frankel, Stein, & Wei (1995) later showed that several actual regional groupings tend to be "natural trading blocs." The Asia-Pacific easily meets the requirements of such a bloc.

Studies that focus on the political economy of trading blocs generally produce more positive results. These emphasize not total gains, but benefits to political actors within economies. Baldwin's (1993) domino theory of regionalism argues that as a bloc grows, potential partner economies benefit more from joining and offer deals good enough to tilt the political calculus within blocs toward enlargement. Blocs that gain critical mass—for example, the European free trade area—thus attract steadily growing membership. Another mechanism presented in McCulloch & Petri (1997) argue that the political constituencies within blocs change as they grow. As a result of a free trade area, efficient firms become more plentiful and inefficient firms disappear. Thus, blocs can become increasingly open to new members. Petri (2008) shows that once a region is saturated by bilateral and plurilateral agreements, the calculus of liberalization favors their consolidation. With many agreements in place, preference erosion reduces the value of each bilateral agreement, while rising administrative costs argue for merging them.

The TPP pathway

Since 1998, APEC has encouraged groups of economies to experiment with "pathfinder" initiatives that may include binding commitments. One such initiative (though officially not labeled a pathfinder) was the high quality Trans-Pacific Strategic Economic Partnership (TPSEP, now called P-4) agreement among Brunei, Chile, New Zealand and Singapore, launched on the sidelines of the 2002 APEC Leaders' Summit and concluded in 2005. The United States announced its intention to enter negotiations with the group in 2008, and Australia, Peru and Vietnam also joined in that year. Negotiations began in March 2010 and four economies have been added since: Malaysia in

[4] This literature is summarized in the survey by Baldwin & Freund (2011).

2010, Canada and Mexico in 2012, and Japan in 2013. Korea, the Philippines, Chinese Taipei and Thailand have also expressed interest, and China and Indonesia have indicated that they are following the negotiations closely.

The emerging content of the TPP reflects the diverse economic structures and governance of its members, and their high level of interdependence. Major trade agreements already exist among many of them. Negotiators are thus seeking a "21st century agreement" that will be comprehensive, high quality, and beneficial to both developing and industrialized members. The official objectives of the TPP are summarized in Figure 2.2 and compared with those of RCEP.

As the table suggests, TPP participants are grappling with highly controversial issues such as intellectual property, services, investment, government procurement, labor and environmental standards. The negotiations have not yet resolved disagreements on some of these.

In the fall of 2014, with 19 rounds of negotiations completed, TPP negotiators have arrived at possible solutions to many problems–which they call "landing zones"–even as conclusions await decisions from high levels of government. An important source of uncertainty is US politics; the Congress has not granted trade promotion authority (TPA) to the President, and "fast track" procedures[5] may be necessary to conclude the

Figure 2.2: Comparison of TPP and RCEP objectives

	Transpacific Partnership	Regional Comprehensive Economic Partnership
Market access for goods	• Elimination of tariff barriers with significant WTO+ commitments • Elimination of non-tariff barriers • Negotiated market access and trade facilitation for textiles and apparel	• Progressive elimination of tariff and non-tariff barriers on substantially all trade in goods • Comprehensive and high level of tariff liberalization
Trade facilitation	• Predictable, transparent and expeditious customs procedures • Strong and common rules of origin • Build on WTO commitments on sanitary and phytosanitary measures (SPS) and technical barriers to trade (TBT) • Facilitate regional value chains	• Facilitate trade and investment, enhance transparency in trade and investment • Facilitate regional and global value chains
Services	• Fair, open and transparent markets for services across borders, while preserving right to regulate • Open trade and investment in financial services, e-commerce and telecommunications • Negotiate on a negative list basis • Transparency and efficiency in temporary entry	• Substantially eliminate restrictions and discriminatory measures on trade in services • Build on commitments made by RCEP members under WTO and ASEAN+1 FTAs • Negotiate on all sectors and modes of supply
Investment	• Liberal access for investment and legal protection for investors • Expeditious, fair and transparent investor-state dispute settlement	• Liberal, facilitative, competitive investment regime • Negotiate on promotion, protection, facilitation and liberalization
Competition	• Promote competitive business environment, protect consumers, ensure level playing field • Establishment and maintenance of competition laws and authorities, fairness, transparency, consumer protection, private rights	• Promote competition, economic efficiency, consumer welfare, curtailing anti-competitive practices • Recognize differences in capacity in RCEP on competition policy
Intellectual property	• Ensure effective and balanced intellectual property rights • Reinforce and extend WTO TRIPS • Cover trademarks, geographical indications, copyrights, patents, trade secrets, data exclusivity • Cover intellectual property enforcement, genetic resources and traditional knowledge	• Reduce intellectual property related barriers to trade and investment • Promote cooperation in utilization, protection and enforcement of intellectual property rights

[5] Fast-track procedures such as TPA commit Congress to a yes-or-no vote on a trade agreement, eliminating decisions on individual provisions that could unravel compromises. Of course, TPA would be useful throughout a negotiation. However, some political observers argue that, when Congress is sharply divided, a fast-track bill cannot be expected until an FTA is nearly complete and its advantages can be more persuasively argued (Cooper 2014).

Dispute resolution	• Clear and effective rules for resolving disputes	• Effective, efficient and transparent process for consultation and dispute resolution
Cooperation	• Focus on needs of developing member economies in implementing high-standard provisions • Establish institutional mechanism for cooperation and capacity building	• Build on cooperation agreements between ASEAN and dialogue partners • Focus on development gaps in RCEP and maximize the mutual benefits
Accession	–	• ASEAN FTA partners may join negotiations as agreed by negotiating members • Accession clause to enable other ASEAN FTA partners to join RCEP later
Environment	• Address trade and environment challenges • Discuss marine fisheries, conservation, biodiversity, invasive species, climate change, environmental goods and services	–
Government procurement	• Ensure fair, transparent, non-discriminatory government procurement • Comparable coverage by all economies; transitional arrangements for developing economies	–
Labor	• Address labor rights protection and ensure cooperation, coordination and dialogue	–

Sources: United States Trade Representative (2011) for TPP and ASEAN (2012) for RCEP.

negotiations. Nevertheless, some believe that an agreement in principle can be reached either before or not long after the US congressional elections in November 2014.

If concluded on this schedule, the TPP will have first-mover advantage among the pathways toward FTAAP (Schott, 2014). Supporters believe that a successful agreement will then lead to the inexorable enlargement of TPP membership until essentially all FTAAP economies are admitted. Building on an existing, complete agreement would be the fastest way to move forward, and some exceptions could be still granted to accommodate the sensitivities of new entrants. But this scenario could prove too optimistic: some TPP provisions may not be acceptable to key potential entrants like China because they represent standards that are either too high or too closely tied to the preferences of the original TPP members. Negotiations between potential new members and incumbent TPP members, which include economies whose preferences may be eroded by the admission of new members, will also present hurdles. Connecting the TPP with other FTAAP economies may therefore require substantial additional agreements.

The RCEP pathway

RCEP is partly the result of sustained efforts by the Association of Southeast Asian Nations (ASEAN) to promote regional economic integration. An ASEAN Free Trade Area (AFTA) was concluded in 1992, followed by a deeper and wider effort, the ASEAN Economic Community, launched in 2007. ASEAN also helped to develop the Chiang Mai Initiative in 1997, a multilateral currency swap agreement among ASEAN, China, Japan and Korea. In 2002, ASEAN and China initiated a framework agreement for an FTA, which was later followed by similar agreements with the other "plus six" partners, Australia, India, Japan, Korea and New Zealand.

Due to political tensions in Northeast Asia, wider regional cooperation emerged slowly. In 2005 a feasibility study was undertaken on an East Asia FTA (EAFTA) consisting of ASEAN plus China, Japan and Korea. Also in 2005, ASEAN convened the first East Asia Summit (EAS), consisting of the ASEAN+6. In 2007, Japan proposed a new FTA project based on the EAS, to be called the Comprehensive Economic Partnership of East Asia (CEPEA). For several years, EAFTA and CEPEA represented competing visions of regional integration, backed by China and Japan, respectively. At the 2011 ASEAN Summit in Bali, China and Japan finally agreed to allow both tracks to proceed, and in 2012 ASEAN developed an approach that came to be formalized as RCEP.

RCEP is based on the ASEAN+6 economies and its "Guiding Principles and Objectives" call for "a modern, comprehensive, high-quality

and mutually beneficial economic partnership agreement… [to] cover trade in goods, trade in services, investment, economic and technical cooperation, intellectual property, competition, dispute settlement" (ASEAN 2012). The Principles stress flexibility and the agreement is expected to include "special and differential treatment" for developing members (Urata, 2014). As Figure 2.2 suggests, the agreement will be confined mainly to market access and connectivity issues (reflecting the region's focus on production chains) rather than "behind-the-border" rules targeted by the TPP.

Negotiations were launched in late 2012 with 2015 as the target date for agreement. Little is known about details. Observers expect RCEP to emerge in phases and a 2015 outcome may include only market access issues (Urata, 2014). As Figure 2.2 suggests, RCEP does not intend to negotiate provisions on labor, environment and government procurement, and its provisions in other areas may adopt intermediate standards. It is not known whether members will apply common market access schedules to all partners, as some economists hope. Some question to what extent RCEP will be able to improve existing ASEAN FTAs (which have been concluded with all RCEP members) or whether it can result in a meaningful agreement among China, India, Japan and Korea. Observers expect RCEP to be "guided by the 'ASEAN way' where objectives and commitments are driven by a consensus process," to be accommodative (Das, 2013), and to produce only modest reductions in tariff barriers (Urata, 2014).

While RCEP's directions remain uncertain, the negotiations may not reach the level of ambition that liberal supporters hope and advanced economies expect in a regional agreement. Also, some observers see RCEP not so much as a step toward common rules, but as a "counterbalance to the new rule-making process championed by the developed economies" (Yi, 2014; Y. Zhang, 2014b). If so, it would become still harder to gain support from developed economies. On this pathway too, new agreements will need to be developed to achieve region-wide integration.

HOW THE PATHWAYS MIGHT WORK

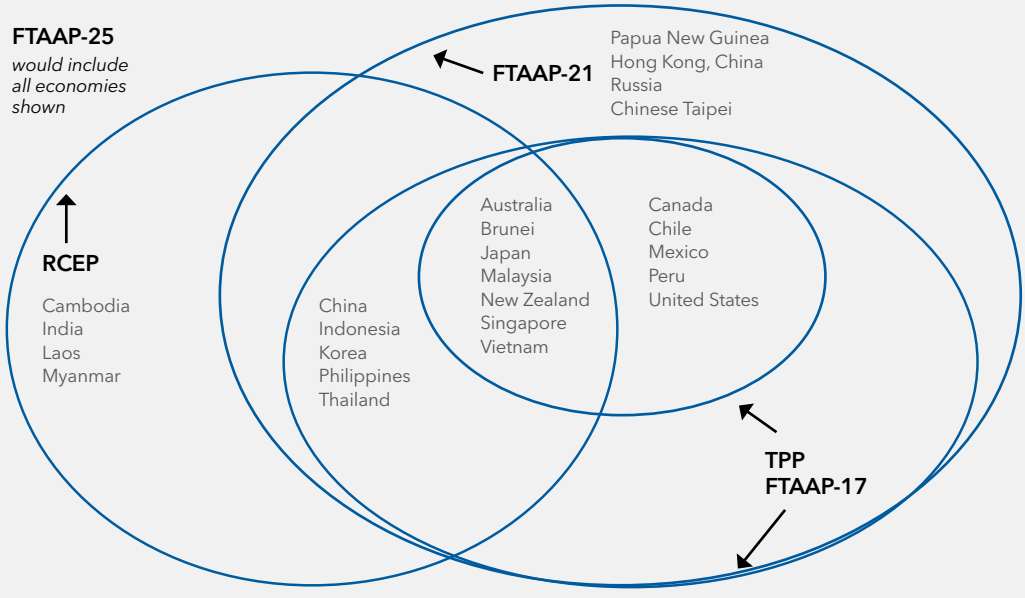
The simplest path to FTAAP, as already noted, would be to approach region-wide coverage by expanding, say, the TPP to 17 economies, including China (Petri, Plummer, & Zhai, 2014b; See Figure 2.3). Such enlargement could yield positive benefits for incumbent TPP members as well as new entrants, and some high-level attention is already directed toward it[6]. But it may turn out that neither RCEP nor TPP provisions are acceptable, at least at first, to all economies outside their negotiating groups. In that case FTAAP would require building a new, umbrella agreement around RCEP and the TPP. A "hybrid" approach proposed by Schott (2014) has some similar features. This section examines the logic of the umbrella path, ranging from membership to the harmonization of specific provisions.

Membership

The economic structure of the Asia-Pacific has changed dramatically since APEC was launched in 1989. APEC membership, which has been updated modestly, no longer coincides with the region's major trading relationships. An early, difficult choice therefore concerns the definition of an FTAAP negotiating group. RCEP membership

[6] These possibilities were explicitly noted, for example, by Wang Shouwen, Assistant Commerce Minister, and Lin Yifu, Vice Chairman of the All-China Federation of Industry and Commerce, speaking at the Boao Forum on April 9, 2014 (See http://www.businesstimes.com.sg/breaking-news/asia/china-says-watching-trans-pacific-trade-pact-great-interest-20140409 and http://www.aastocks.com/en/stocks/analysis/china-hot-topic-content.aspx?id=200000331986&type=18&catg=3, respectively).

Figure 2.3: Membership of possible Asia-Pacific trade agreements



Source: Authors.

is based on ASEAN's FTA partners, while the TPP represents self-selected APEC economies. If FTAAP were to be based only on participants of RCEP and the TPP, it would have to go beyond APEC membership and also include Cambodia, India, Laos and Myanmar, while excluding Hong Kong (China), Chinese Taipei, Russia, and Papua New Guinea. Further, as Scollay (2014) notes, additional non-APEC members may eventually join RCEP and the TPP.

Since an FTAAP negotiation would be independent from APEC, there is no strict requirement to link the memberships of the two groups. Three possibilities for defining FTAAP membership are illustrated in Figure 2.3. Decisions on the membership of FTAAP will have to strike a balance between inclusiveness and limiting the negotiations to the economies most committed to reaching an agreement. First, since the FTAAP concept arose in APEC, an obvious possibility is to define membership in terms of APEC's 21 members. A second, a more inclusive option is to *expand* the group to 25 members, by including economies in RCEP and TPP that are not members of APEC (perhaps by admitting them into APEC). A third intriguing option is to *limit* the initial negotiations to the 17 economies that (a) are APEC members, and (b) are participating in the RCEP and/or TPP agreements. This group has demonstrated the greatest commitment to regional trade and has accumulated the most experience with regional and sub-regional institutions.

Decisions on the eight economies that fall outside the 17-member configuration but within the 25-member group will be especially difficult. To be sure, political circumstances are likely to change by the time an FTAAP negotiation begins. If political trends favor regional integration, they will also make the resolution of membership issues less contentious than it would be today. Moreover, additional members—from within or outside APEC, including additional economies from the Pacific Alliance—could be added after an agreement is completed. Intermediate solutions would involve forming a relatively small negotiating group, along with a commitment to timely, favorable accession procedures for other Asia-Pacific economies.

The logic of an umbrella agreement

An umbrella agreement would be separate from RCEP and the TPP, although it should be shaped by their provisions. Since the two smaller agreements will differ, FTAAP will have to take positions on some issues that are absent from at least one of the agreements as well as harmonize provisions that are included in both.

Economies that have negotiated less ambitious rules previously (say in RCEP) will need to adopt more demanding ones in FTAAP. And others that have accepted more ambitious rules (say, in the TPP) may have to dial back those ambitions. The benefits of FTAAP—including its provisions for broader market access—will have to be large enough to satisfy both of these groups. Of course, members may continue to observe higher standards with partners in existing agreements such as the TPP, and in turn offer larger concessions to them. And some economies may not be ready to move beyond agreements that require more limited commitments, such as RCEP. The result would be a multi-tiered system, with RCEP, FTAAP or TPP representing successively higher standards—much as economies today build on their WTO commitments in FTAs with "WTO-plus" obligations.

Under the FTAAP umbrella, members might be expected to converge to higher standards. This could happen as economies join the TPP (so more and more trade under the umbrella agreement would be governed also by TPP standards) or by upgrading FTAAP, construed as a living agreement. Precedents for an evolutionary approach to standards are offered by ASEAN's upgrading of the ASEAN Free Trade Area and some ASEAN-plus-one partnerships. NAFTA is itself an umbrella agreement built around the Canada-US free trade agreement and has been upgraded over time, for example, in its rules of origin. The TPP is also envisioned to be a "living agreement" to be adjusted in the future. That said, the political process in the United States makes such adjustments in trade agreements difficult.

Bilateral provisions

A large subset of issues within FTAAP could be resolved in bilateral negotiations among members not already connected by an FTA. To make such a strategy possible, the FTAAP would absorb existing market access commitments among economies that already have agreements. New bilateral negotiations would be limited to economies that do not already have an agreement (either directly or through RCEP or TPP). This is how the TPP avoided multilateral negotiations on market access and the renegotiation of existing agreements. The remaining bilateral deals will be still difficult—as demonstrated by the Japan-US negotiation in the TPP—and China-US negotiations are likely to be especially challenging. Finding bilateral solutions to important issues is hardly a perfect solution—it leads to discrimination even within an FTA—but it can make negotiations more manageable.

Cooperation between China and the United States will be critical on bilateral as well as plurilateral provisions, so prior China-US agreements on relevant issues would greatly improve prospects for a region-wide agreement[7]. Some trends are encouraging. Direct discussions between the two

[7] An analysis of steps toward China-US free trade is provided by Bergsten, Hufbauer, & Miner (2014) and, in that volume, by Petri, Plummer, & Zhai (2014a).

economies are already underway on investment issues, and on services, government procurement and other issues in the WTO context. Also, FTAs concluded by the two economies with third partners can promote common approaches to international rules. China either has or is negotiating FTAs with 9 of the 12 TPP members. Only Canada, Mexico and the United States are not on this list at this time. Significantly, a China-Korea FTA is said to be near completion, and this agreement will presumably mirror some features of the high quality agreement that Korea recently concluded with the United States.

Harmonized provisions

Issues not negotiated bilaterally will require text that spans the difference between RCEP and the TPP. One would expect that most differences may be resolved with intermediate positions. The minimum years of protection for an intellectual property asset, for example, could be set higher than in RCEP (which may just stick with TRIPS standards) and lower than in the TPP. The "Guiding Principles and Objectives for Negotiating the RCEP" have so far only identified the WTO General Agreement on Trade in Services (GATS) and the ASEAN FTAs as guidelines for service sector liberalization. As Anuradha (2013) explains, these are modest benchmarks: many economies in fact are already pursuing a more ambitious agenda in various forums, such as the "ASEAN Framework Agreement for Services" (AFAS) adopted by the ASEAN Economic Community.

Fukunaga & Isono (2013) calculate a "Hoekman Index" to measure the extent to which ASEAN's new agreements exceed GATS standards. They generally find ASEAN's FTAs to have made substantial progress beyond GATS, and further note that service liberalization under AFAS (package 7) surpassed commitments in all FTAs, in part because the latter included opt-out clauses.

Still, intermediate positions will be hard to agree in the service sectors. The TPP approaches services on a negative-list basis, opening all sectors except those explicitly excluded, while RCEP is likely to adopt a positive list. Intermediate text will thus have to determine the negotiating modality as well as the level of sectoral commitments.

Conflicting provisions

Two other kinds of compromises will be also complicated to negotiate. First, RCEP and TPP may have conflicting provisions—for example, different dispute settlement rules. A common position would then require some members to abandon some prior commitments. Such direct conflicts, however, are unlikely. The WTO rules serve as the basis of both RCEP and the TPP, and 7 economies are members of both agreements. They will likely avoid contradictory provisions in the two agreements. Second, some issues may be missing in the RCEP agreement, while being considered critical in the TPP. As Figure 2.2 shows, these include government procurement, state-owned enterprises, labor, environment and others. These provisions are often based on international conventions and standards which member economies are asked to accept. Thus reasonable, WTO-plus intermediate positions will usually exist. Still, some economies often oppose entering certain areas of negotiations altogether. Defining the scope of the agenda broadly while treating issues flexibly will be important in getting the negotiations launched.

Rules of origin (ROO)

Rules of origin are designed to control "trade deflection." They require goods exported under regional preferences to originate within an FTA zone, rather than merely pass into it through the borders of the member economy with low external barriers. Strict ROO minimize deflection but also make it harder for firms to utilize the benefits of FTAs. ROO are especially important in the Asia-Pacific because they affect the operation of manufacturing supply chains.

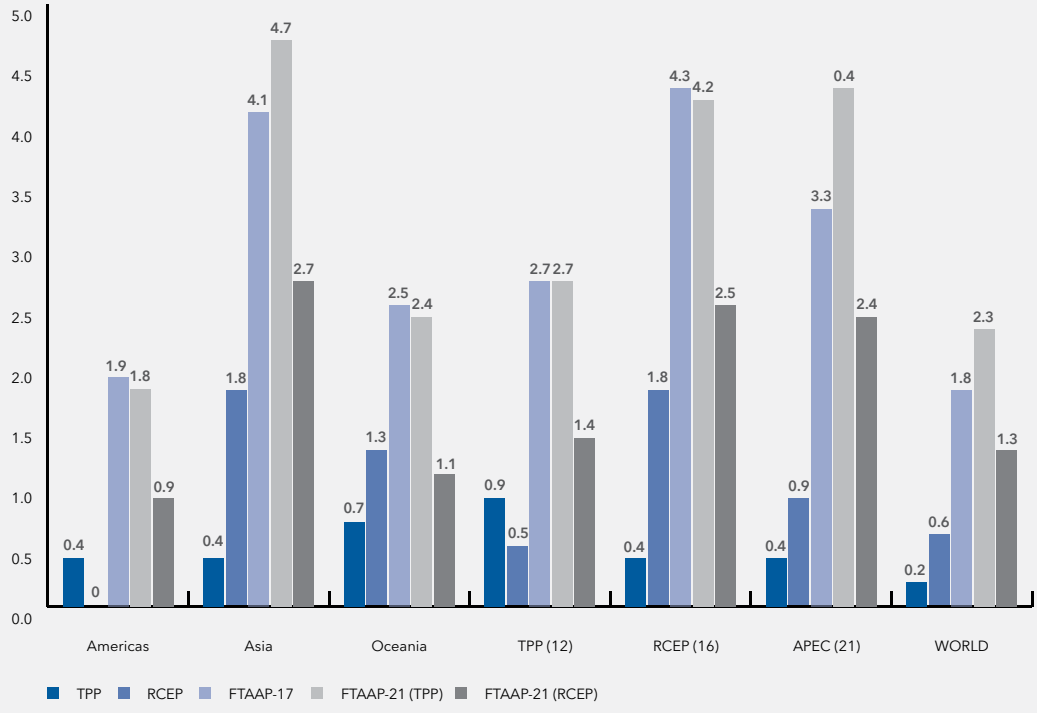
Economics strongly favors ROO that are simple, common to all members, and permit cumulation—that is, the practice of counting intermediate inputs produced anywhere in the FTA zone as "originating" and thus eligible for FTA preferences (Plummer, 2007). However, reconciling ROO across the region's agreements will be difficult[8]. An APEC (2012) study of existing regional FTAs demonstrated a preference for product-specific ROO over general rules, with details varying widely. A major obstacle to harmonization, for example, is the "yarn forward" rule in textiles and garments that the United States typically includes in trade agreements and is likely to require in the TPP (Schott, Kotschwar, & Muir, 2013).

Still, the ROO negotiations may be surprisingly manageable in FTAAP. The threat of trade deflection is modest in large agreements, since in this case most production will rely on regional intermediate inputs. Even industry-specific rules, such as yarn-forward, would exert minimal constraints in a setting that includes entire production chains. Moreover, Estevadeordal, Blyde, Harris, & Volpe (2013) show that complex ROO tend to be streamlined over time in a large zone. NAFTA initially applied product-specific rules that were highly restrictive of third-party content, but over the last 20 years progressively eased them in four rounds of amendments. Similarly, FTAAP could lead to improvements in the region's ROO regime.

In sum, RCEP and the TPP represent foundations for an FTAAP. They provide way-stations for experimenting with and adjusting to deeper integration. This is important for the large trade flows that connect the United States, China and Japan with each other and other partners. To be an effective way-station, FTAAP needs to

[8] ROO could theoretically differ among RCEP, TPP and FTAAP, separately activating the market-access concessions in each agreement. However, such differences would have complicated consequences. For example, if the FTAAP ROO are less restrictive than the TPP ROO, then the effect of market access commitments made by economies in the TPP would change. In that case, TPP market access provisions might also have to be renegotiated.

Figure 2.4: Income gains from alternative agreements (% of GDP)



Source: Petri, Plummer, & Zhai (2012); see asiapacifictrade.org and Figure 2.5 below

be ambitious enough to move beyond RCEP toward the TPP. Yet it also has to provide flexibility to attract broad membership. Much effort and ingenuity will be needed to achieve this balance.

THE BENEFITS

We conclude with estimates—inevitably uncertain—of gains from FTAAP pathways. These are based on an advanced, computable general equilibrium (CGE) model[9] to simulate the 12-member TPP, the 16-member RCEP, and two variants of FTAAP, one with 17 economies (FTAAP-17, based on APEC members that also participate in RCEP or TPP) and another with all 21 APEC economies (FTAAP-21). The benefits of FTAAP are assessed for two levels of standards, those expected to be included in the TPP, and those expected in RCEP.

The estimates rely on new data on the provisions of trade agreements in order to make the trade policy simulations realistic. Detailed information on issues covered in nearly 50 regional trade agreements has been used to assign "scores" to the quality of these agreements in 24 dimensions. Future agreements are assumed to use templates comparable to those used in the past by similar economies. For example, the TPP's template is based on that of the Korea-US free trade agreement, and RCEP's template on those included in recent agreements by ASEAN. The templates differ significantly on issues such as government procurement, intellectual property rights, investment, and competition, as well as the depth of liberalization of tariff and non-tariff barriers.

The results summarized in Figure 2.4 (based on the detailed results reported in Figure 2.5) suggest several key conclusions. Most importantly, the benefits of Asia-Pacific integration are estimated to be large; for strong, comprehensive agreements income gains could reach 2.3 percent of world GDP in 2025 or US$2.4 trillion. But even the current negotiations on the TPP and RCEP would generate substantial gains. RCEP shows the larger benefits of the two (0.6 percent compared to 0.2 percent of GDP), due largely to the effects of trade liberalization among China, India, Japan, and Korea.

There are, to be sure, significant differences in how the agreements would affect Asia-Pacific economies. The TPP favors economies that do not yet have an FTA with the United States, such as Japan and Vietnam. At the same time, the TPP generates trade diversion losses for China, Europe and Asian economies not included in the agreement. RCEP favors China, India, Japan and Korea because it assumes—perhaps too optimistically—major trade liberalization among these economies as part of RCEP. ASEAN economies would gain only modestly in RCEP, since FTAs already cover ASEAN's relations with all RCEP partners. The significant contribution of an FTAAP would be an agreement between China and the United States, which would sharply increase overall gains.

Significantly, as the theoretical analysis of modern trade agreements suggests, much of the benefits

[9] The details of the model cannot be included here, but they are fully described in Petri, Plummer, & Zhai (2012) and on the website asiapacifictrade.org.

of integration accrue to economies with the highest initial barriers—this is why the gains of Asian economies are generally higher than those of other groups. In addition, a vast majority of benefits in all of the agreements would reflect trade-creation and productivity increases within them, rather than trade diversion from outsiders. Even for the TPP, the smallest group among those examined, total trade diversion losses affecting China and some other economies would represent only 22 percent of the benefits of gainers, with the remaining 78 percent reflecting trade creation. For the larger FTAAP-21, the ratio of diversion losses to total gains would fall to 6 percent.

Finally, the benefits from alternative agreements confirm well-established expectations given their size and quality. Potential gains increase sharply with the scale of integration—for example, expanding the TPP with 12 members to an FTAAP with 17 members would increase global benefits from $223.4 billion to $1,908.0 billion in 2025. The benefits would grow further to $2,358.5 billion if Hong Kong (China), Chinese Taipei, Papua New Guinea and most importantly Russia were added under the APEC membership-based FTAAP-21. Still larger benefits could be achieved if India, Cambodia, Laos and Myanmar were added to form an FTAAP-25 (these results are not shown in Figure 2.4). Similarly, gains increase with the quality of the agreement, or specifically the ambition of its template. The benefits of the 21-member FTAAP, for example, would be $2,358.5 billion with the more rigorous TPP-style template with APEC membership compared to $1,315.1 billion with an RCEP-style template, some 79 percent higher. The benefits would extend to all economies, even to Asian economies which might have been expected to gain more from their "own" template incorporated into RCEP.

CONCLUSIONS

Asian and trans-Pacific regional negotiations are moving forward, despite business cycles, elections, geopolitics, and political controversy. Pathways toward the FTAAP are also garnering new interest. Estimates suggest that they could generate large economic benefits. The gains will depend on the size of the ultimate agreement and the quality of the templates used. There is tension between these objectives—a rigorous template, as in the TPP, yields greater gains, but also impedes participation. However, there are ways to balance these extremes, through a multi-tiered process that eventually includes an FTAAP.

While the case for FTAAP is compelling, achieving an agreement on this scale is at best a challenging, long-term prospect. Detailed policy recommendations are premature and would go beyond the scope of this paper in any event. Nevertheless, the following broad issues merit attention:

- APEC has long recognized the value of region-wide free trade. Progress on the RCEP and TPP negotiations would make FTAAP more likely and the analysis of pathways to achieve it more timely.

- RCEP and the TPP would provide essential way-stations for economies on the path to region-wide integration. These agreements are likely to differ on many difficult issues. Still, they are unlikely to include contradictory provisions, and region-wide membership would make it easier to address ROO, an unusually contentious issue in trade negotiations.

- FTAAP promises huge benefits, on the order of $2 trillion annually. The benefits would be widely shared in the region. Their scale would depend on the breadth of the membership and the quality of the agreement negotiated.

- The prospects for integration depend most importantly on cooperation between the region's two largest economies, China and the United States. This could involve early milestones such as a bilateral investment treaty and joint support for plurilateral initiatives in the WTO. China-US agreements—like Japan-US agreements in the TPP—would dramatically improve the prospects for FTAAP.

Deeper economic integration in the Asia-Pacific would produce large economic gains and could help to defuse dangerous geopolitical tensions. To be sure, agreements that foster integration will be very difficult to achieve. Lengthy and complex negotiations may be required and much opposition is bound to emerge from special interests throughout the region. Asia-Pacific integration will depend on farsighted, collaborative leadership, not least from the region's largest economies.

Figure 2.5: Income gains from alternative agreements (2025 estimates)

Alternative	GDP Baseline	TPP	RCEP	FTAAP-17	FTAAP-21	FTAAP-21	TPP	RCEP	FTAAP-17	FTAAP-21	FTAAP-21
Template		TPP	RCEP	TPP	TPP	RCEP	TPP	RCEP	TPP	TPP	RCEP
		Billions of US dollars, 2007 prices					Percentage changes				
Americas	**24,867**	**101.7**	**2.5**	**468.0**	**452.3**	**228.5**	**0.4**	**0.0**	**1.9**	**1.8**	**0.9**
Canada	1,978	8.7	-0.1	33.2	31.4	14.3	0.4	0.0	1.7	1.6	0.7
Chile	292	2.5	0.0	7.8	8.6	2.2	0.9	0.0	2.7	3.0	0.7
Mexico	2,004	9.9	2.8	91.1	76.3	43.0	0.5	0.1	4.5	3.8	2.1
Peru	320	3.9	0.0	8.4	7.7	2.5	1.2	0.0	2.6	2.4	0.8
United States	20,273	76.6	-0.1	327.6	328.2	166.6	0.4	0.0	1.6	1.6	0.8
Asia	**34,901**	**125.2**	**627.0**	**1442.1**	**1653.4**	**947.2**	**0.4**	**1.8**	**4.1**	**4.7**	**2.7**
Brunei	20	0.2	1.2	1.7	1.4	0.6	0.9	5.8	8.4	7.1	3.2
China	17,249	-34.8	249.7	808.6	837.1	520.6	-0.2	1.4	4.7	4.9	3.0
Hong Kong	406	-0.5	46.8	-1.9	118.8	51.6	-0.1	11.5	-0.5	29.3	12.7
India	5,233	-2.7	91.3	-29.3	-37.1	-20.6	-0.1	1.7	-0.6	-0.7	-0.4
Indonesia	1,549	-2.2	17.7	82.0	60.3	26.1	-0.1	1.1	5.3	3.9	1.7
Japan	5,338	104.6	95.8	237.3	233.1	154.2	2.0	1.8	4.4	4.4	2.9
Korea	2,117	-2.8	82.0	136.3	132.7	97.7	-0.1	3.9	6.4	6.3	4.6
Malaysia	431	24.2	14.2	45.4	44.7	16.5	5.6	3.3	10.5	10.4	3.8
Philippines	322	-0.8	7.6	30.6	22.5	11.2	-0.2	2.3	9.5	7.0	3.5
Singapore	415	7.9	2.4	27.1	26.5	-0.7	1.9	0.6	6.5	6.4	-0.2
Chinese Taipei	840	-1.0	-16.1	-31.5	83.8	30.5	-0.1	-1.9	-3.8	10.0	3.6
Thailand	558	-2.4	15.5	64.9	43.7	19.2	-0.4	2.8	11.6	7.8	3.4
Vietnam	340	35.7	17.3	71.9	81.1	37.9	10.5	5.1	21.2	23.9	11.2
Other ASEAN	83	-0.4	1.6	-1.1	4.6	2.4	-0.4	1.9	-1.3	5.5	2.9
Oceania	**1,634**	**10.7**	**21.7**	**41.3**	**39.4**	**17.4**	**0.7**	**1.3**	**2.5**	**2.4**	**1.1**
Australia	1,433	6.6	19.8	34.1	32.5	15.3	0.5	1.4	2.4	2.3	1.1
New Zealand	201	4.1	1.9	7.2	6.9	2.0	2.0	0.9	3.6	3.4	1.0
Others	**41,820**	**-14.1**	**-6.8**	**-43.4**	**213.4**	**122.0**	**0.0**	**0.0**	**-0.1**	**0.5**	**0.3**
Europe	22,714	-3.7	5.1	0.9	-40.9	-23.9	0.0	0.0	0.0	-0.2	-0.1
Russia	2,865	-1.4	-5.3	-8.8	339.5	199.3	0.0	-0.2	-0.3	11.9	7.0
ROW	16,241	-9.0	-6.6	-35.5	-85.2	-53.4	-0.1	0.0	-0.2	-0.5	-0.3
WORLD	**103,223**	**223.4**	**644.4**	**1908.0**	**2358.5**	**1315.1**	**0.2**	**0.6**	**1.8**	**2.3**	**1.3**
Memorandum											
TPP (12)	33,045	285.0	155.1	892.8	878.6	454.5	0.9	0.5	2.7	2.7	1.4
RCEP (16)	35,290	137.4	617.9	1516.8	1490.2	882.4	0.4	1.8	4.3	4.2	2.5
APEC (21)	58,951	239.2	553.0	1973.0	2517.1	1410.7	0.4	0.9	3.3	4.3	2.4

Source: Results from model described in Petri et al. (2012).
Notes: FTAAP is simulated using 17 and 21 member groups as described in the text. The templates indicated represent those projected for TPP and RCEP agreements.

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CHAPTER 3

PERCEPTIONS OF GROWTH AND INTEGRATION IN THE ASIA-PACIFIC*

When the region's Leaders meet in Beijing on the occasion of the 25th anniversary of the Asia Pacific Economic Cooperation (APEC) forum, they will be confronting a plethora of issues.

* Contributed by Eduardo Pedrosa

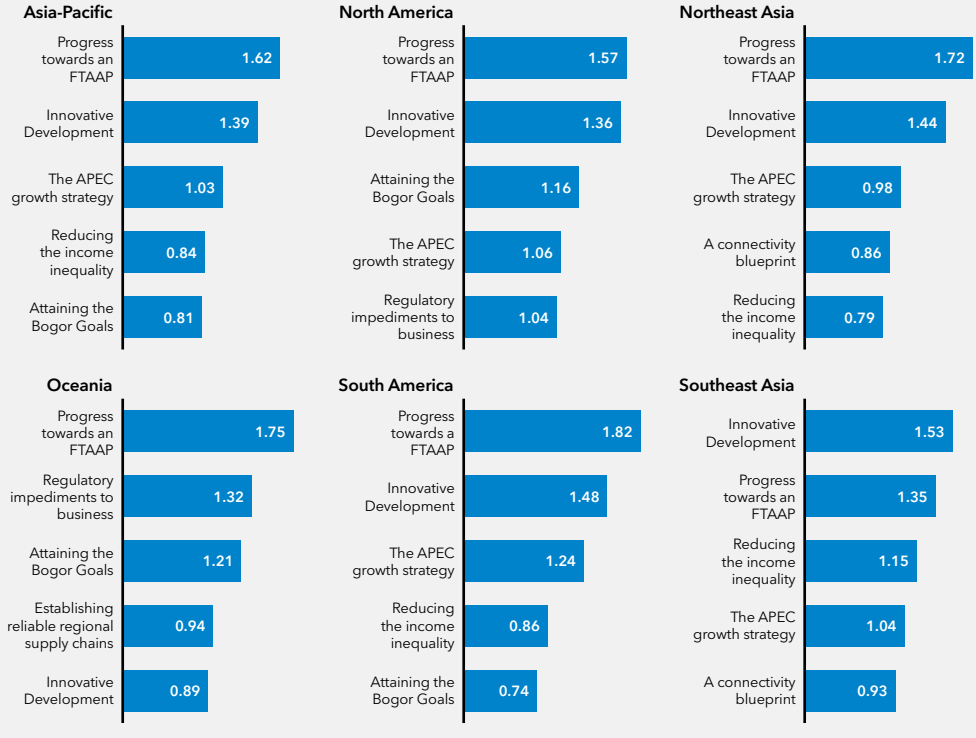
According to a survey of opinion-leaders from the policy community conducted by the Pacific Economic Cooperation Council (PECC), the top five issues are:

1. Progress towards a Free Trade Area of the Asia-Pacific (FTAAP)
2. Innovative development, economic reform and growth
3. The APEC Growth Strategy
4. Reducing the income inequality in the region
5. Attaining the Bogor Goals of free and open trade and investment

The first two correspond to the themes that China has set as priorities for this year as the chair of APEC. While the top five priorities are linked and overlap, they each demonstrate pressing concerns. The FTAAP and the Bogor Goals can be seen as aspirations to address remaining barriers to trade and investment and the future rules of a rapidly integrating region at a time the WTO continues to be mired in controversy over 20th century issues.

Innovative development, economic reform and growth, income inequality and the APEC Growth Strategy all reflect an awareness of the importance of new strategies to respond to the so-called 'new normal' of characterized by slower growth, income inequality and slow job creation – especially in major advanced economies.

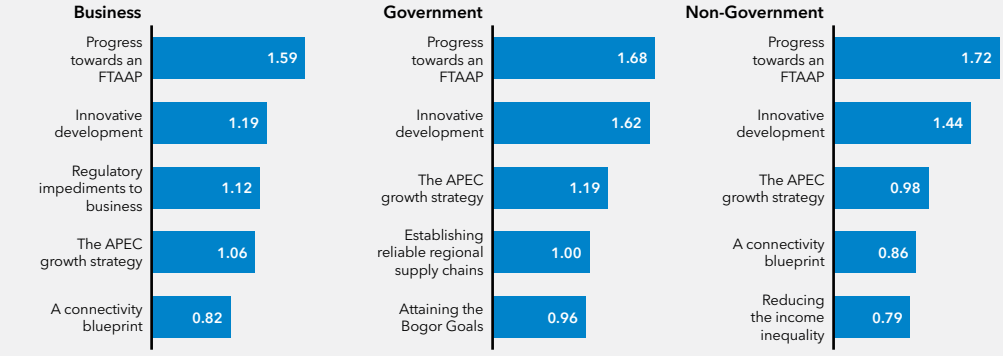
Figure 3.1: Top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing (by sub-region)



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: What do you think should be the top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing?

Figure 3.2: Top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing (by sector)



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: What do you think should be the top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing?

For a region characterized by great diversity, there was a remarkable degree of convergence on what the top issues should be. Only Southeast Asians did not select progress towards an FTAAP as the top priority which came in second after 'innovative development'. Respondents from Oceania were the only ones to select 'establishing reliable supply chains' as a top 5 priority. Opinion-leaders from Oceania and North America thought 'regulatory impediments to business' was an important agenda but did not include 'reducing income inequality' as a top 5 concern as did the Asians and South Americans.

The Connectivity blueprint, which follows from framework adopted by Leaders last year in Bali, was another issue where there were differences in emphasis: 28 percent of respondents from Southeast Asia selected it as a top 5 priority but only 18 percent of those from Oceania.

The same level of convergence on priorities is seen among the various stakeholder groups surveyed by PECC, the only differences being higher emphases among business leaders on regulatory impediments, income inequality among the non-government community, and supply chains as well as attaining Bogor Goals from government officials. Interestingly, establishing reliable regional supply chains did not feature as a high priority at all for business leaders with only 15 percent of them selecting it as a top 5 priority compared to 35 percent of government officials who did.

WHITHER THE WTO?

While APEC has been a staunch supporter of the WTO through the years, its stakeholder community is clearly losing patience. It is not just because all sub-regions and stakeholders-whether from government, business or non-government - chose what was originally proposed as a Plan B to the Doha Round as the top priority but because a decreasing portion of them think the WTO Doha Round is even worth discussing. Only 13 percent of business respondents thought the WTO Doha Round should be on the APEC Leaders' agenda. There were also clear differences among sub-regions on this issue with a relatively high 23 percent of respondents from South America selecting it as a priority and only 9 percent of those from North America.

FUTURE OF GROWTH A KEY ISSUE

The list of priorities includes many issues that overlap or are variations on a theme that could easily be subsumed into a broader category. For example, the attainment of the Bogor Goals and progress towards an FTAAP could have been listed as 'regional economic integration.' Similarly, innovative development, economic reform and growth could have been subsumed under the APEC Growth Strategy. Were the priorities grouped this way, the Growth Strategy would have topped the list.

As APEC is set to review progress on the Growth Strategy next year, this points to an urgent need for a coherent approach to how regional economies adopt to the new normal. This might provide an opportunity for APEC to consider how it might respond to the G20's target of increasing baseline economic growth by 2 percentage points by 2018 as part of its commitment to addressing this concern. The approach taken by the G20 has been to set a specific growth target as well as actions that each individual economy will take echoes that of APEC with respect to the Bogor Goals. While the details of the G20 plans are not yet known they will focus on 4 key areas:

- Reducing barriers to trade
- Increasing competition
- Creating more employment opportunities
- Improving infrastructure through increased investment

These are all issues where APEC has set out specific work programs and might be able to widen and deepen commitments to the global agenda.

ECONOMIC OUTLOOK

The regional policy community has become increasingly optimistic over the prospects for growth of the world economy over the next 12 months with just under a third of respondents expecting stronger growth and less than a sixth believing there will be slower growth, the lowest percentage in five year.

Respondents were most optimistic about the growth prospects in the United States and Southeast Asia. They were most pessimistic on the prospects of growth for Russia with 67 percent expecting slower growth over the next 12 months, not surprising given the imposition of sanctions. Opinions suggest slower growth for China with 34 percent expecting a slowdown, which compares very favorably against last year's result when 62 percent correctly expected slower growth for the host of this year's APEC meetings.

RISKS TO GROWTH

A slowdown in the Chinese economy was once again the top risk to growth amongst regional opinion-leaders – in terms of both the number of respondents who selected it as a top 5 risk as well as its impact.

However, the regional breakdown shows some large differences in views. Respondents from resource rich economies in Oceania by far were the most concerned with73 percent of respondents citing a slowdown in China as a top 5 risk to growth for their economy. Respondents from Southeast Asia were considerably less concerned than their counterparts with just 30 percent citing a slowdown in China as a top 5 risk to growth.

Respondents were asked to select the top 5 risks to growth for their economy over the next 2-3 years using a scale of 1 to 5 with 1 showing the least serious risk and 5 the most serious risk. The data gathered by this survey can be shown in a number of different ways. For example, by showing – the risks most frequently selected and the weighted score of each individual risk. For the most part, there is a strong correlation between the two. However, in a number of cases, while a risk might be frequently selected, - suggesting a higher probability of the event happening, the weighted score could be lower if respondents considered its impact to be less serious.

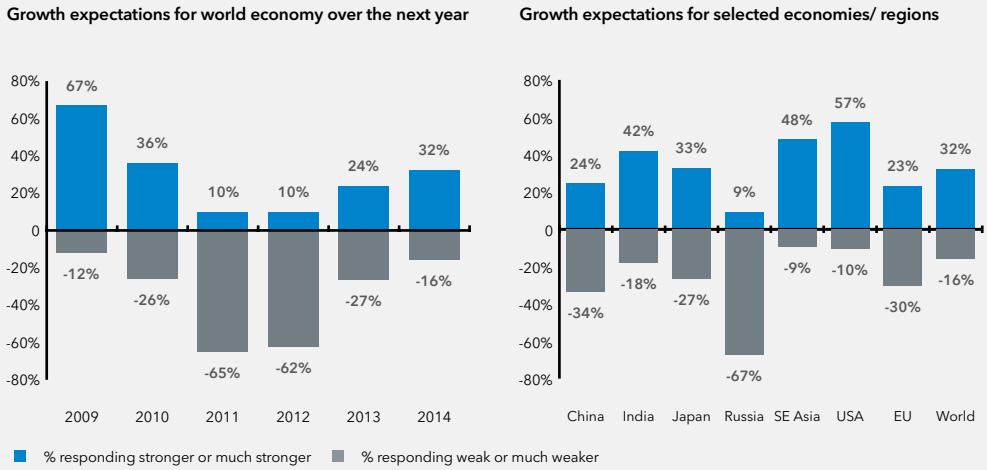
The top 5 risks in terms of the percentage of respondents who selected them were:

- A slowdown in the Chinese economy
- Lack of political leadership
- Failure to implement structural reforms
- Fiscal crises in major economies
- Shortage of available talent/skills

The top 4 in terms of their seriousness were the same, except for shortage of talent. While almost the same number of respondents picked a slowdown in the US economy and a shortage of talent/skills as a top 5 risk to growth (27.4 percent), a slowdown in the US economy was considered more serious scoring 0.85 compared to the shortage of talent which score 0.76.

Figure 3.4 plots the frequency with which respondents selected the risk on the horizontal axis and the severity of the risk on the vertical. Among the top 3 risks there is a strong correlation between the possible severity and the frequency with which opinion-leaders selected the issue. However, while energy security and a sharp fall in asset prices were selected as risks with the same frequency, energy security scored significantly higher in terms of its seriousness. Similarly, the shortage of available talent was cited as frequently as a slowdown in the US economy, but the latter was considered to be a much more serious risk to growth.

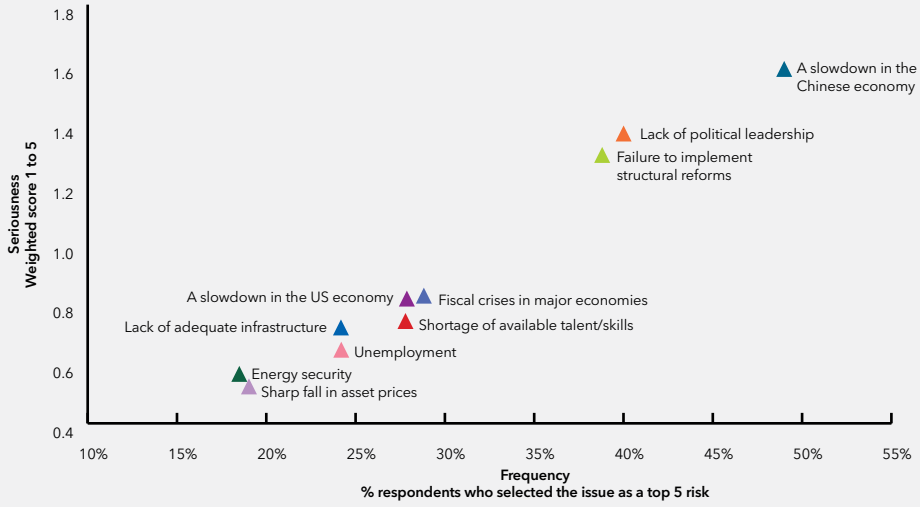
Figure 3.3: Expectations for economic growth over the next 12 months compared to the last year for the following economies/ regions



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: What are your expectations for economic growth over the next 12 months compared to the last year for the following economies/regions?

Figure 3.4: Top 10 risks to growth



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please select the top five risks to growth for your economy over the next 2-3 years.

While unemployment and the lack of adequate infrastructure were both selected as a top 5 risk by the same proportion of respondents, unemployment was considered to be a slightly less serious.

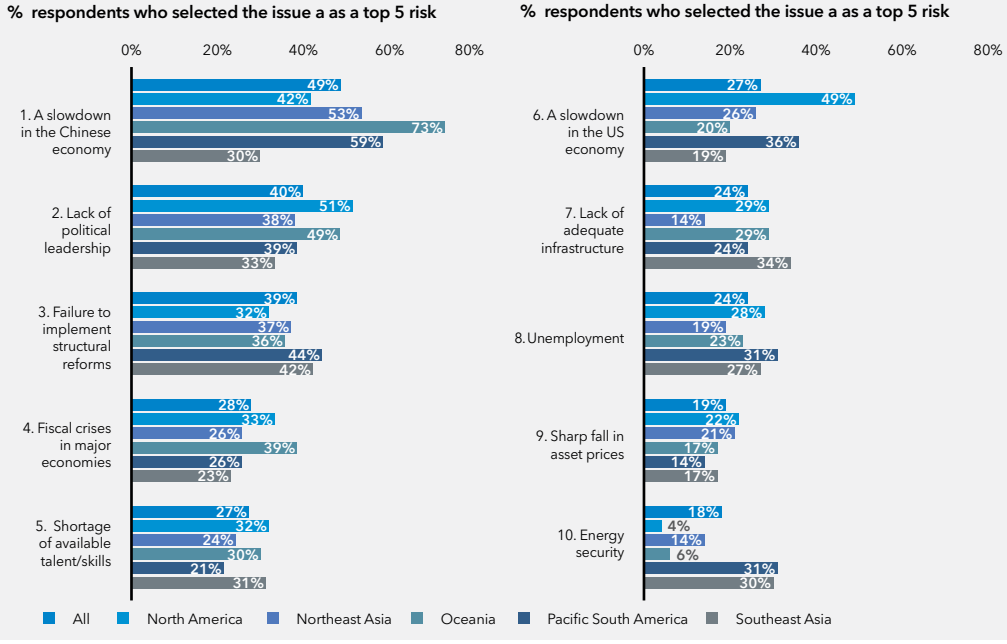
LACK OF POLITICAL LEADERSHIP – A SHARED CONCERN

Of concern should be the fact that opinion-leaders selected a lack of political leadership as the second highest risk to growth. This was selected a high risk by all sub-regions. It stands as a stark observation if not a rebuke to politicians at a time when leadership is badly needed. Moreover, 46 percent of business respondents selected the lack of political leadership compared to just 30 percent of those from the government.

The third highest risk, possible failure to implement structural reforms, also suggests considerable anxiety about the political ability of leaders to address an important regional agenda. As many economies of the region have run out of fiscal space to maneuver and monetary policy is already considered unconventional, getting growth on a higher trajectory will require structural reforms that come with significant adjustment costs in vulnerable sectors.

There were also considerable differences in perceptions of risk among sub-regions. For example, 34 percent of respondents from Southeast Asia selected lack of adequate infrastructure as a top 5 risk to growth compared to just 14 percent of those from Northeast Asia.

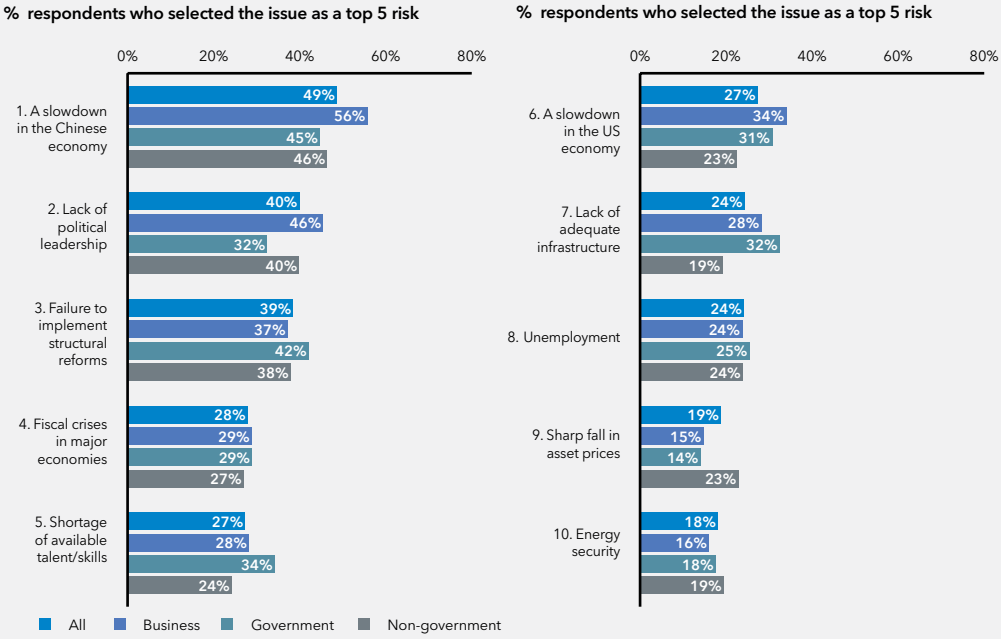
Figure 3.5: Top 10 risks to growth (by sub-region)



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please select the top five risks to growth for your economy over the next 2-3 years.

Figure 3.6: Top 10 risks to growth (by sector)



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please select the top five risks to growth for your economy over the next 2-3 years.

For once, the shortage of available talent, which has been rising up the list of risks in recent years, was seen as a higher risk by respondents from government than business which has usually been the case.

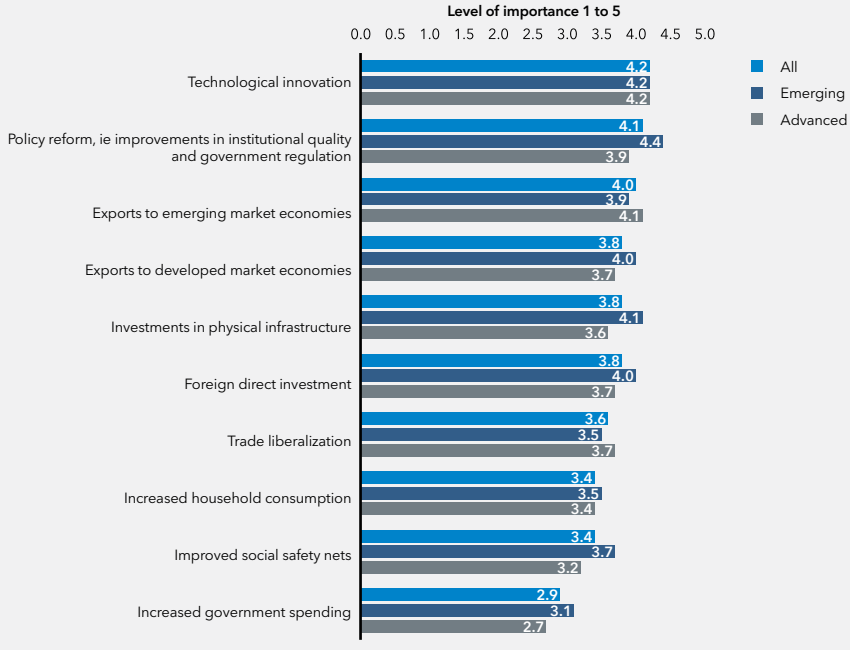
FUTURE GROWTH AND CONSUMPTION IN THE ASIA-PACIFIC

There is a clear need for the region to focus efforts on technological innovation as part of the strategy to overcome the middle income trap. Out of a list of 10 possible drivers of growth, technological innovation was ranked as the most important followed by policy reform and then exports to emerging markets.

As has been widely discussed, the global economy is entering into a 'new normal' characterized by slower growth as well as significant changes in the balance of aggregate demand.

The challenge for the policy community is to increase total factor productivity – including

Figure 3.7: Drivers of growth over the next 5-10 years



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

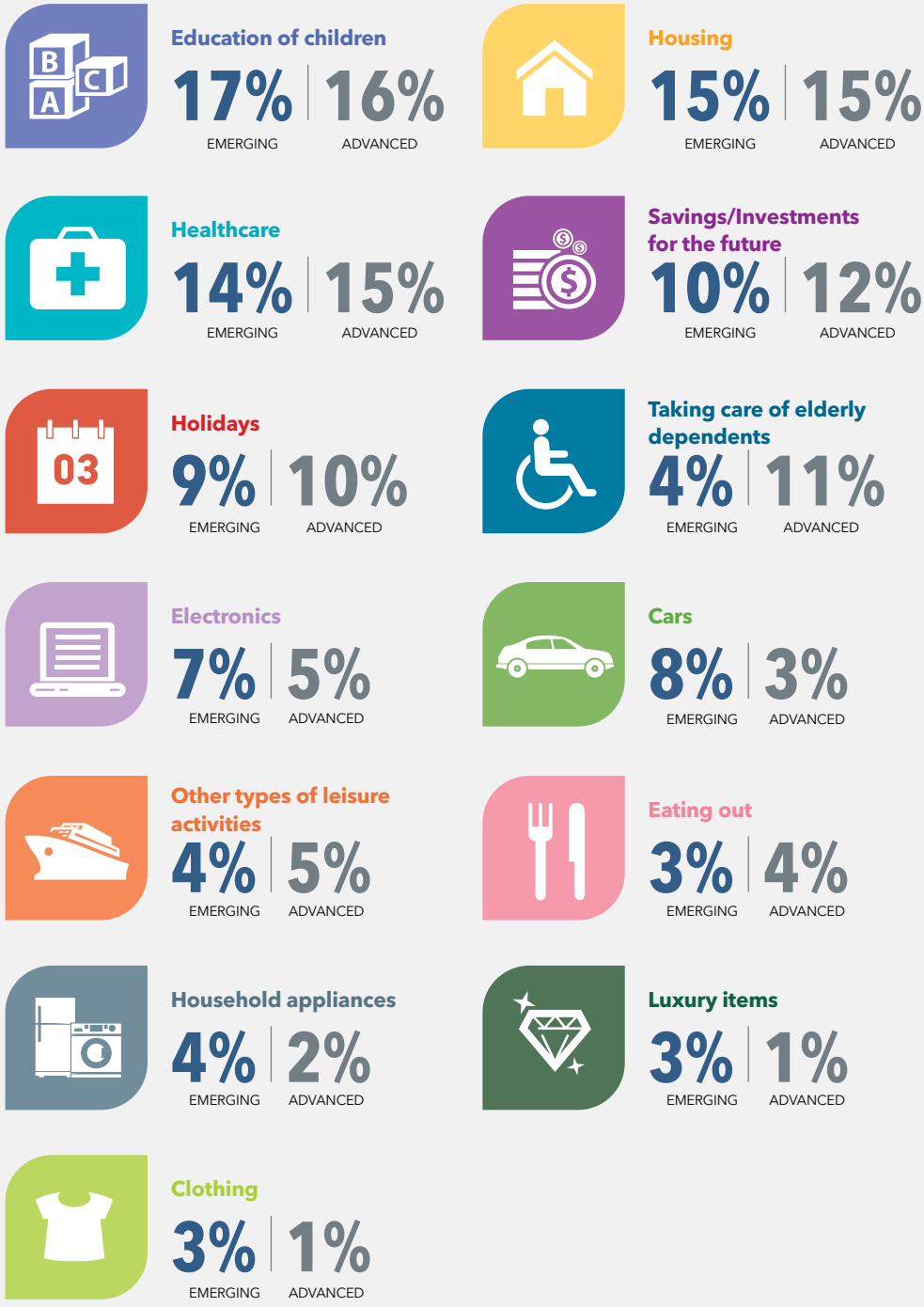
Question: Please rank each of the following in order of how important you think they will be to the future growth of your economy over the next 5-10 years. Use a scale of 1-5, select: '1' if you think the issue not at all important; '2' of little importance; '3' moderately important; '4' important, '5' very important or 'don't know' if you are not sure.

innovation as well as institutional quality. Without these improvements, economies of the region risk slower growth. Respondents from middle-income economies placed a much higher emphasis on policy reforms to improve both institutional quality and government regulation than their counterparts from high-income economies.

Interestingly, while respondents from emerging economies tended to see equal importance in exports to other emerging markets as well as developed markets, respondents from developed economies put much more emphasis on emerging market exports than to other developed markets.

Trade liberalization is not regarded as an especially significant growth driver. This may seem at odds with the emphasis placed on the FTAAP as a leaders' priority, and may reflect the respondents' belief about what the APEC process can best achieve.

Figure 3.8: Consumer expenditure in the Asia-Pacific



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please select the top 5 categories in which you think consumers in your economy are likely to spend an increasing share of their income on.

THE FUTURE CONSUMERS

There is some speculation that the emerging economies of the region are on the cusp of a consumer boom. The previous decades of growth have brought average incomes in many economies beyond a threshold level – moving from expenditure on day-to-day living to having more discretionary income. Figure 3.8 shows the percentage of respondents who selected each category as an area where they expected consumers in their economy to spend an increasing proportion of their income.

Interestingly there was substantial convergence between respondents from both advanced and emerging economies on the top categories for future expenditure by consumers in their economies – education, housing, and healthcare. Where there were some differences were in categories that might be related to the emergence of new middle class consumers – for example, those from emerging economies were expected to spend more on electronics, cars, luxury items and clothing.

One striking finding is the expectation among opinion-leaders from higher income economies that consumers would be spending more on taking care of elderly dependents. While in general, societies in advanced economies are older and the labor supply for taking care of the elderly more limited, the ageing phenomenon is not limited to high-income economies. This is not an issue of importance only to advanced economies as many emerging economies are yet to put in place the kinds of pension schemes available in high-income economies.

Questions on consumer trends are more typically found in marketing surveys. However, the purpose of including this question in this year's survey was to relate the changing consumption basket to the broader question of the future of economic growth. Not surprisingly, big ticket items such as housing, education and healthcare dominated the list.

As discussed in Chapter One, the expectation is that consumption will take up an increasingly high portion of aggregate demand in emerging market economies as incomes pass threshold levels allowing more discretionary expenditure. The survey results show an expectation among the policy community that emerging markets are likely to increasingly be a source of demand for key consumer goods like cars, electronics and household appliances.

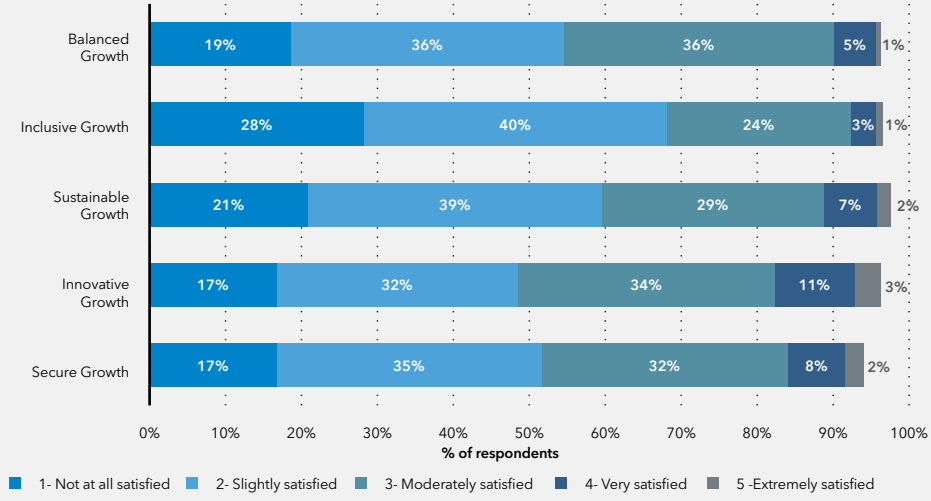
Although it is clear that there is a strong expectation that education, healthcare, housing, and savings for retirement are likely to continue to dominate a typical household's expenditure basket. It also points to a need for more sophisticated financial sector in emerging markets to meet this growing demand.

APEC GROWTH STRATEGY

In 2010, APEC Leaders agreed that the quality of growth of the region needed to be improved so it will be more balanced, inclusive, sustainable, innovative, and secure. Strikingly, satisfaction with efforts made on each dimension of APEC's Growth Strategy remains low.

Respondents were asked to rank efforts made under each dimension from a score of 1 to 5 with 1 being not at all satisfied and 5 very satisfied. Across the board grades given were around 2 – equivalent to slightly satisfied. Respondents were most satisfied with actions taken to make growth more innovative with 48 percent expressing extreme to moderate satisfaction. Since the adoption of the growth strategy APEC leaders' declarations have focused on innovation adopting 2 frameworks for promoting innovation in 2011 and 2012.

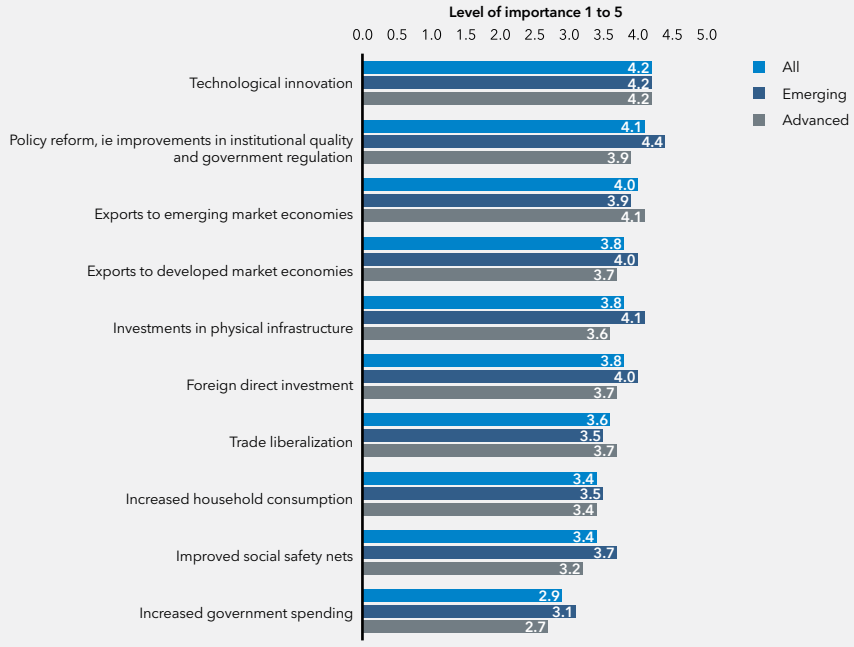
Figure 3.9: Satisfaction with efforts to improve the quality of growth in the region



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: In 2010, APEC leaders agreed that the quality of growth of the region needed to be improved so it will be more balanced, inclusive, sustainable, innovative, and secure. How satisfied are you with efforts so far on each dimension? Use a scale of 1-5, select: '1' if you are not at all satisfied; '2' if slightly satisfied; '3' if moderately satisfied; '4' if very satisfied; '5' if extremely satisfied; or 'don't know' if you are not sure or are not aware of actions taken to promote the APEC growth strategy.

Figure 3.10: Future drivers of growth



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please rank each of the following in order of how important you think they will be to the future growth of your economy over the next 5-10 years. Use a scale of 1-5, select: '1' if you think the issue not at all important; '2' of little importance; '3' moderately important; '4' important, '5' very important or 'don't know' if you are not sure.

Similarly in 2012, APEC economies made a breakthrough promoting sustainable growth by agreeing on a list environmental goods on which tariffs would be reduced to 5 percent or less.

Of concern is that the lowest grades were given to efforts to make growth inclusive. As income inequality is considered a top risk to growth, APEC will need to do more work in this area in the future. Also worth noting that respondents from government tended to give slightly higher marks than counterparts from business and the non-government sectors.

DRIVERS OF FUTURE GROWTH FOR INDIVIDUAL ECONOMIES

Looking further ahead over the next 5-10 years, respondents were asked to rank how important different factors would be to the future growth of their economies. By far technological innovation was ranked as the most important followed by policy reforms and then exports to emerging markets.

There were significant differences in responses from those from emerging economies and those from advanced economies. Those from emerging economies placed a much higher emphasis on institutional quality and governance – i.e. the types of issues covered by the World Bank's Ease of Doing Indicators while those from high income economies looked to exports to emerging markets at the second most important driver of future growth.

Increased government spending is not expected to play that significant a role in future growth in either emerging or advanced economies. Respondents in both placed this at the bottom of the list of factors.

The results once again highlight the importance of infrastructure to the future of growth in the region's emerging markets. Those in emerging markets placed investments in physical infrastructure as the third most important driver of growth for their economies after policy reforms and innovation.

FUTURE GROWTH IN THE ASIA-PACIFIC

Figure 3.11 shows the results of the survey for the question on factors affecting growth prospects in the Asia-Pacific as a whole. The results reflect the growing importance of the Chinese economy to the rest of the region, for most of whom, China is their largest trading partner. That the importance of the success of structural reforms in China is seen as the top factor influencing the future of growth in the Asia-Pacific echoes the finding that the top risk to growth is a slowdown in China.

TRADE LIBERALIZATION IN THE ASIA-PACIFIC

While respondents did not rank trade liberalization as a top factor for growth in their individual economies, it was the second most important factor for growth in the region as a whole. That is not to say that trade liberalization was considered unimportant; 57 percent of respondents did select it as being important or very important for their economies future growth, but a much more significant 69 percent thought further liberalization was important to very important for the growth of the region as a whole.

Figure 3.11: Critical factors for the future of Asia-Pacific growth

Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: How important do you think the following are for growth prospects in the Asia-Pacific region as a whole over the next 5-10 years? Use a scale of 1-5, select: '1' if you think the issue not at all important; '2' of little importance; '3' moderately important; '4' important, '5' very important or 'don't know' if you are not sure.

THE RULE OF LAW

Improvements to the rule of law also ranked highly echoing the finding from the question on factors influencing growth in individual economies on the importance of policy reform and institutional quality.

WORKFORCE TRAINING AND MOBILITY

Workforce training and mobility was seen a key factor for the future growth of the region, again, echoing the list of perceived risks to growth – where the shortage of available skills and talent was a top risk. This was a much more important factor for respondents from Southeast Asia who scored it at 4.1 – as important as the success of structural reforms in China.

THE FUTURE OF ASIA-PACIFIC REGIONAL COOPERATION

As APEC celebrates its 25th anniversary there are increasing questions about its future role. Its traditional agenda of trade liberalization is taken up by the various mega-regionals in the region and there are now other architectures that bridge the Pacific Basin.

The question of India joining APEC has been at the background for a number of years. As with the results from previous years there was strong agreement that India should be a member of APEC. However, when all respondents were asked for priorities for APEC leaders, the issue of membership ranked extremely low: 19th out of 27 issues.

Figure 3.12

Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please indicate your agreement or disagreement with the following statements - India should be a member of APEC.

Figure 3.12: Whither India in the Asia-Pacific

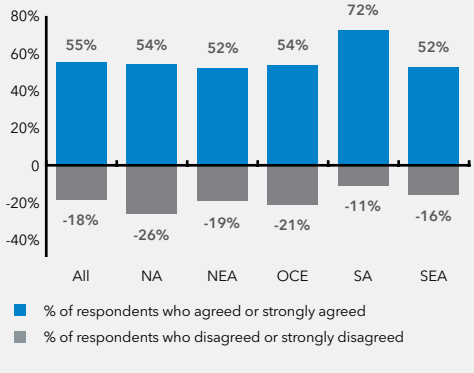


Figure 3.13

Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: What do you think should be the top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing –The Expansion of APEC Membership"

Figure 3.13: APEC membership as a top 5 priority

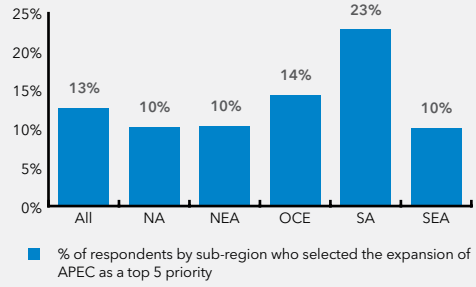
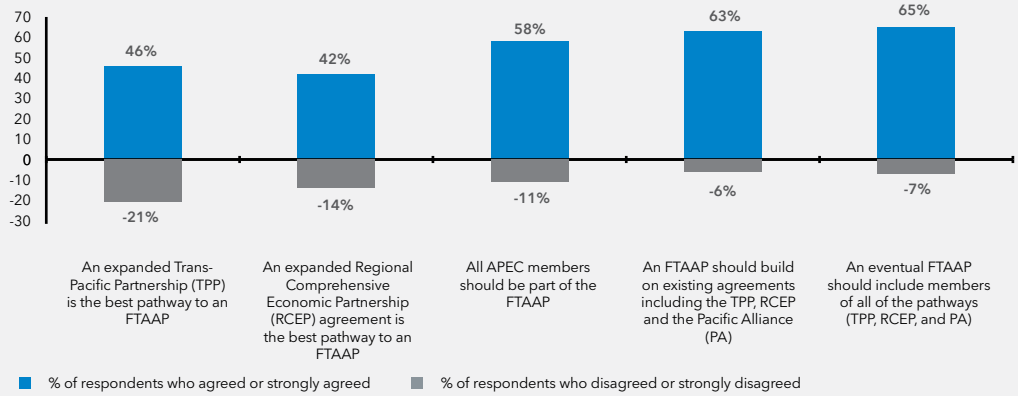


Figure 3.14: Views on the Free Trade Area of the Asia-Pacific (FTAAP)



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please indicate your agreement or disagreement with the following statements:

TOWARDS AN FTAAP

Although an FTAAP has principally been a concept espoused by APEC and related institutions, especially the APEC Business Advisory Council (ABAC), there is little clarity on what the FTAAP is and who would be part of it. The 2010 APEC Leaders' declaration stated: *'An FTAAP should be pursued as a comprehensive free trade agreement by developing and building on ongoing regional undertakings, such as ASEAN+3, ASEAN+6, and the Trans-Pacific Partnership, among others.'*

Opinion-leaders showed no clear-cut preference for either route – the Trans-Pacific Partnership (TPP) or the Regional Comprehensive Economic Partnership (RCEP) - and prefer the more agreeable but nebulous concept of building on other agreements including the TPP, RCEP and the Pacific Alliance. Chapter 2 of this report suggests some details on how this concept might work. It suggests that the RCEP and TPP negotiations may, if successfully concluded, provide way-stations toward the FTAAP – through new, regionally acceptable rules and also facilitate experimentation with and adjustment to deeper integration. However, by themselves, neither is likely to lead directly to an FTAAP and additional agreements are needed to achieve rules that encompass the Asia-Pacific region. The chapter examines an FTAAP umbrella agreement built around RCEP and the TPP, it argues that such an agreement could set relatively high standards, encourage liberalization across the region, and lead to a system of tiered rules for economies at different stages of development.

On the question of membership of the eventual FTAAP, generally there was agreement that all APEC members should be part of the FTAAP but there was even stronger support for the proposition that it should include members of all of the pathways. This raises the question of APEC membership for India, Cambodia, Laos, and Myanmar who are part of the ongoing RCEP negotiations, and Colombia which is part of the Pacific Alliance – if APEC is to play a significant role in guiding the development of an FTAAP.

HOW LIKELY ARE ANY OF THE REGIONAL TRADE DEALS TO REACH A CONCLUSION?

Opinion-leaders were skeptical about any of the proposed trade deals in the region reaching a conclusion within the next three years. They were most optimistic about the ASEAN Economic Community (AEC) with 43 percent thinking it was likely to reach a conclusion and 20 percent not likely. The AEC has a self-imposed deadline for completion by the end of 2015.

Some 35 percent of respondents expected the TPP to reach a conclusion within the next three years, with 27 percent thinking it unlikely. The TPP has already missed a deadline at the end of 2013 but continues an intense series of negotiations. Furthermore, even if negotiations are concluded, in the case of the United States, the deal would need Congressional approval, a big hurdle given the lack of Trade Promotion Authority.

AMBIVALENCE REIGNS

In general, opinion-leaders were ambivalent about the likelihood of a conclusion within the next three years of many of the trade deals currently being pursued.

Just 27 percent of respondents thought it likely that a conclusion would be reached for the Regional Comprehensive Economic Partnership, involving the 10 members of ASEAN Plus economies with which it has existing trade agreements, namely, China, India, Japan, Korea, and Australia & Zealand with a deadline of 2015 for completion. The numbers were reversed for the Trans-Atlantic Trade and Investment Partnership (TTIP) involving the US and the EU with 27 percent thinking a conclusion unlikely and 24 percent likely.

Figure 3.15: Likelihood of RTAs reaching a conclusion within next 3 years

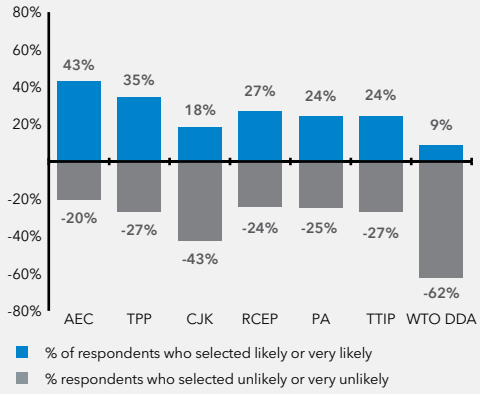
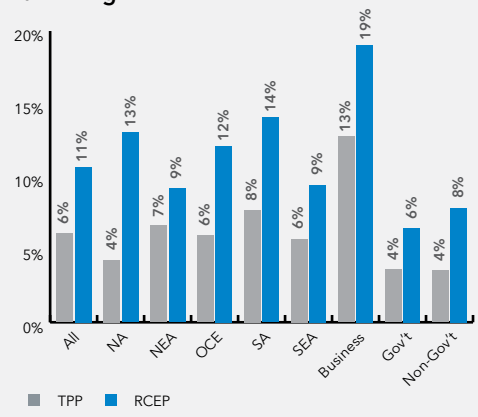


Figure 3.16: Undecided, uninformed, or unwilling



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: What do you think is the likelihood of success in concluding the following proposed agreements over the next 3 years? Use a scale of 1-5, select '1' if you think it is not at all likely if the negotiations will be completed within the next 3 years; '2' if not likely; '3' if neither unlikely nor likely; '4' if likely, '5' if very likely or 'don't know' if you are not sure.

Respondents were equally ambivalent about the Pacific Alliance involving Chile, Colombia, Mexico and Peru with 25 percent thinking a conclusion unlikely and 24 percent likely.

Respondents were most skeptical about the possible conclusion of the CJK involving China, Japan and Korea; 43 percent thought it an unlikely possibility and 18 percent likely.

While not a regional deal, WTO Doha Round remains something Ministers and Leaders continue to pay lip service to but opinion-leaders in this survey have all but given up on it with only 9 percent thinking a conclusion in the next three years likely.

NEED FOR OUTREACH

These survey results are not gauging public opinion but those of the informed policy community but even amongst this group there was a proportion of respondents who selected 'don't know' when asked if the agreements would be completed within the next three years – especially the business community. This could mean either that they don't know enough about the agreement to make a judgment or simply don't know about the agreement at all. It could also mean that they know a lot about the agreements, but feel unable to judge their political dynamics. No matter what the case, this casts a shadow over these mega-regional deals which are supposed to facilitate trade across the region.

While the TPP has received substantial media coverage and has completed at least 18 rounds of negotiations (more if counting some the other 'mini-rounds') as well as numerous ministers' and chief negotiators' meetings, a remarkable 13 percent of respondents selected 'don't know.' With the RCEP, a much newer concept with a deadline of 2015, 19 percent selected 'don't know.' Respondents were most unfamiliar or unwilling to make a judgment on the Pacific Alliance with 27 percent selecting 'don't know.' The lack of familiarity with the PA bodes ill for those members who would like to see it considered as a potential pathway towards an FTAAP.

PRIORITY ISSUES FOR REGIONAL TRADE AGREEMENTS

Respondents were asked to rate 17 issues in terms of their need to be addressed in Asia-Pacific trade agreements. The list of 17 issues broadly corresponds with the typical chapters in trade agreements such as the TPP and RCEP.

There was a remarkable degree of convergence between respondents from the business and government sectors in terms of priorities, at least among those who work on Asia-Pacific issues. The issues where the gap between government and business were highest were:

1. Movement of persons
2. Agricultural market access
3. Cooperation, capacity building
4. E-commerce
5. Consistent product standards

Business respondents rated the 'movement of persons' and 'e-commerce' higher than government, while government respondents rated 'agricultural market access,' 'cooperation and capacity building,' and surprisingly, 'consistent product standards higher' than their business counterparts.

One of the challenges for Asia-Pacific integration is the diversity in levels of development; even though there was some convergence on priorities, there were some significant and interesting differences. The areas with the highest divergence between emerging and advanced economies were:

Figure 3.17: Priority issues for regional trade deals

Government vs. Business Views

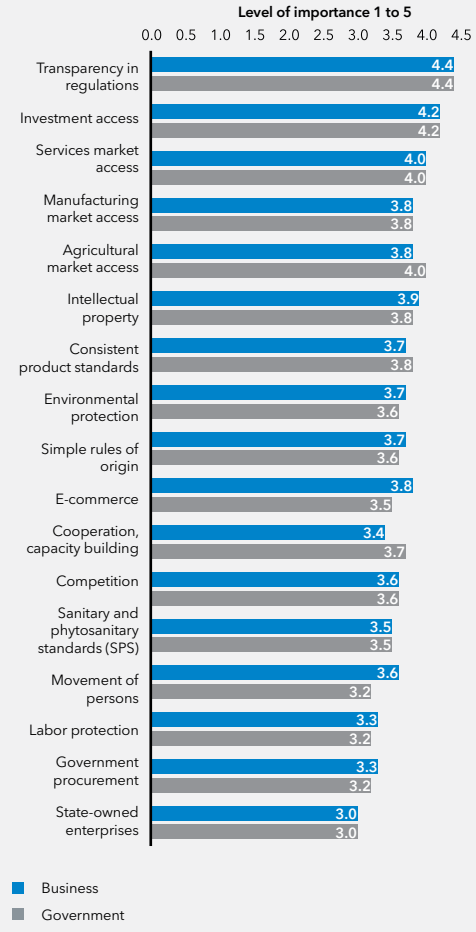
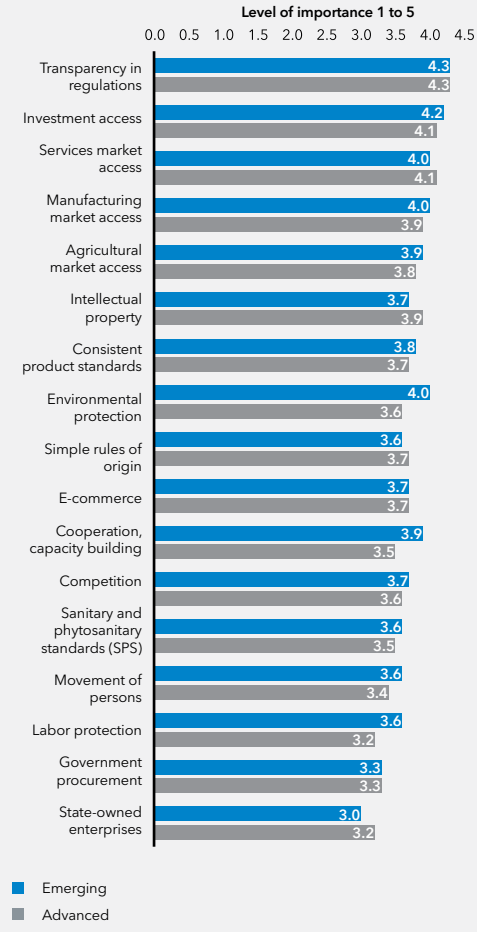


Figure 3.18: Priority Issues for regional trade deals

Emerging vs. Advanced Economy Views



Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please rate each of the following in terms of the need for them to be addressed in Asia-Pacific free trade agreements? Please use a scale of 1-5, with 1 representing lowest priority and 5 highest priority.

1. Environmental protection
2. Cooperation, capacity building
3. Labor protection
4. Movement of persons
5. State-owned enterprises

These differences were not intuitive; for example, respondents from emerging economies rated environmental and labor protections higher than their counterparts from advanced economies. Not surprisingly, 'cooperation and capacity building' were a higher priority for those from emerging economies as was movement of persons, while 'state-owned enterprises' was a higher priority for advanced economies.

THE FUTURE OF APEC

On the occasion of APEC's 25th anniversary, there are questions being asked about the future role of what has been the region's pre-eminent regional institution, and until the creation of the East Asia Summit, the only forum where the leaders of the region's major economies would meet on an annual basis.

When PECC started the survey in 2007, views on APEC were at best ambivalent. Some 48 percent of respondents had positive view of APEC and 47 percent negative. Over time the negative sentiments towards APEC have been decreasing but so had positive sentiments, until this year when APEC had a strong positive approval of 61 percent and only 17 percent negative.

SOUTHEAST ASIANS MORE POSITIVE ON APEC

Part of the reason for this shift, is the increased positive sentiments towards APEC from Southeast Asian respondents. In PECC's 2013 survey, only 26 percent of opinion-leaders from Southeast Asia expressed positive views towards APEC with 25 percent having a negative view compared to this year with 54 percent having positive views and only 16 percent negative. Indonesia's hosting of APEC in 2013 could be a reason for this shift, especially due to the strong emphasis in last year's agenda on infrastructure and supply side constraints which are clearly issues of great concern to the region's emerging economies, especially those in Southeast Asia.

Figure 3.19

Source: PECC Survey of Asia-Pacific Opinion-Leaders, 2014

Question: Please indicate your agreement or disagreement with the following statement: APEC is as important or more important today compared to 1989 when it was created

Figure 3.20

Source: PECC Survey of Asia-Pacific Opinion-Leaders 2006-2014

Question: APEC is as important today as it was in 1989 (2007, 2008, 2010, 2014); How effective do you think each of the following institutions has been in achieving its objectives? (2011, 2013)

Figure 3.19: APEC is as important or more important today compared to 1989 when it was created

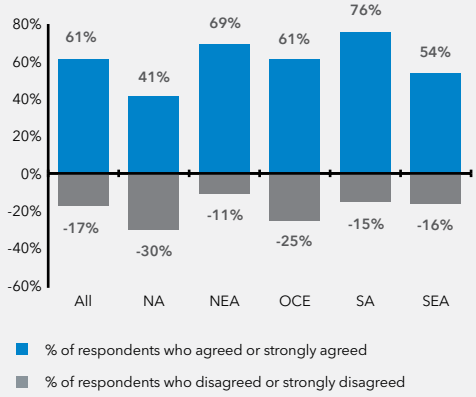
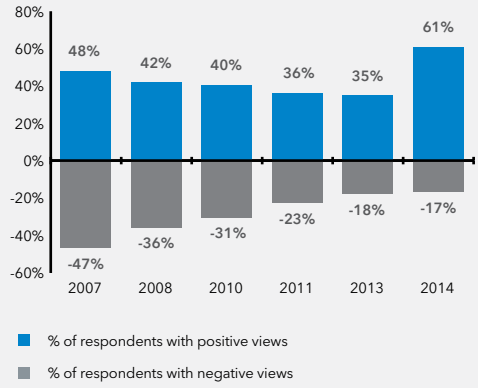


Figure 3.20: Views on APEC over time



NORTH AMERICAN AMBIVALENCE

Of concern perhaps is the ambivalence among opinion-leaders from North America towards APEC; 41 percent of respondents had positive views and 30 percent negative. While still a net positive, it is far from a ringing endorsement, but it is an improvement from 2013 when only 30 percent of respondents from North America had a positive view of APEC and 22 percent negative.

APEC'S IMPORTANCE FOR SOUTH AMERICA

Respondents from South America remain by far the most positive towards APEC with 76 percent having positive view and 15 percent negative. While many members of APEC now have alternative architectures for broad engagement with the Asia-Pacific, APEC remains the only one for Pacific Rim South American economies to engage with their counterparts in the rest of the region.

APEC: NEW CHALLENGES AND AGENDA AHEAD FOR ASIA-PACIFIC COOPERATION

The findings of this survey indicate the broad range of challenges facing the Asia-Pacific. It is clear that the regional policy community remains extremely concerned about the implementation (more lack thereof) of the reforms needed to keep growth momentum high. This is evidenced by the types of risks to growth identified such as the failure to implement structural reforms as well the factors identified as being critical to future growth prospects – policy reform, i.e. improvements in institutional quality and regulation.

While APEC has addressed many of these issues through its work on structural reform and the Growth Strategy, opinion-leaders are not satisfied with the actions taken thus far. Next year's assessment of the strategy provides an opportunity to review what has been done and to consider next steps. By then it will be clear what commitments G20 members will have made, and how APEC members might respond.

In the 20 years since the Bogor Goals were set, the number of regional trade agreements has proliferated and APEC has yet to fully come to terms with what this means for its mission and its modalities. Clearly the concerted unilateralism that characterized its earlier phase has been replaced by competitive liberalization. In setting the Bogor Goals, APEC Leaders also emphasized their *'strong opposition to the creation of an inward-looking trading bloc that would divert from the pursuit of global free trade.'* The challenge APEC faces is in ensuring that the current spate of mega-regionals are not exclusive, but building blocks for regional and global free trade.

CHAPTER 4

ANNUAL REPORT OF THE COMPOSITE INDEX OF ECONOMIC INTEGRATION IN THE ASIA-PACIFIC REGION: 1990~2011*+

The economic integration of the Asia-Pacific region has rebounded since last year's update to the index. This rebound follows declines in the index during the Global Economic Crisis.

The index measures the degree of integration taking place in the Asia-Pacific region based on intra-regional flows of: goods; investment; and tourists and five measures of convergence: GDP per capita; share of non-agriculture to GDP; the urban resident ratio; life expectancy; and share of education expenditure in GNI.

The index was developed in 2008 as a tool to measure the degree of integration taking place in the Asia-Pacific. Regional economic integration has become a core objective of the Asia Pacific Economic Cooperation (APEC) forum. The process of economic integration is commonly defined as the freer movement of goods, services, labor, and capital across borders.

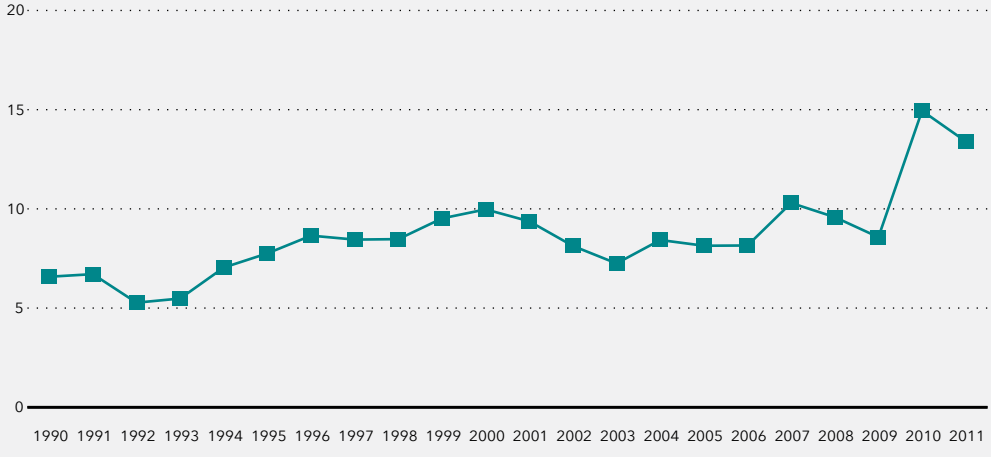
The degree of economic integration can be analyzed at bilateral, regional, and global levels. Even though the Asia-Pacific region is not covered by a single trading agreement, there is much anecdotal evidence to suggest that it is becoming more integrated. As defined by APEC membership, the region consists of not only developed economies such as the US, Japan, Canada, and Australia, but also emerging markets such as the ASEAN economies. It is well known that parts of the region are already highly integrated through production networks that facilitate trade of intermediate and finished goods across borders. Since 1998, many economies in the region have negotiated bilateral and sub-regional free trade agreements with partners in the region as well as outside the region. From 2004, APEC leaders began formally discussing a Free Trade Area of the Asia Pacific (FTAAP) and in 2010 agreed to take concrete steps towards its realization. If and when successful, FTAAP would constitute the largest regional trading bloc in the world.

An important feature of the index is that it excludes trade and investment flows among geographically contiguous sub-regional trading partners, namely NAFTA, the ASEAN Free Trade Area, and Australia-New Zealand Closer Economic Relations. It also excludes flows between China, Hong Kong (China), and Chinese Taipei. This is to

* Contributed by Bo Chen Shanghai University of Finance and Economics, and Asia Pacific Foundation of Canada. 100 Wudong Rd., Yangpu District, Shanghai, China, 200433. Email: chen.bo@mail.shufe.edu.cn

+ For approach details, data sources and treatment, please refer to Bo Chen and Yuen Pau Woo (2010), "Measuring Economic Integration in the Asia-Pacific Region: A Principal Components Approach", *Asian Economic Papers*, Vol.9(2), pp 121-143.

Figure 4.1: Composite index of regional economic integration



control for the effect that sub-regional flows may have on the index, whereby a very high degree of integration among, for example, NAFTA economies could result in a falsely high measure of integration with the Asia-Pacific region as a whole.

Furthermore, since the trade, investment, and tourism measures are calculated relative to global transactions, the index will rise for a given economy only if that economy's share of trade/investment is growing relative to total trade and investment.

The weights given to each dimension are determined using principal component analysis.[1]

[1] See Bo Chen and Yuen Pau Woo (2010), "Measuring Economic Integration in the Asia-Pacific Region: A Principal Components Approach," Asian Economic Papers, Vol.9 (2), pp. 121-143.

WEIGHTS USED

Composite Index

Category	Weight
Convergence	18.90%
Trade	18.73%
FDI	32.58%
Tourism	29.79%

Convergence Sub-Index

Category	Weight
GDP per capita	11.24%
Non-agriculture share of GDP	10.47%
Urban ratio	12.72%
Life expectancy	15.57%
Education expenditure share of GNI	50.00%

The convergence measures are premised on the notion that integration will lead to greater uniformity among the economies. Accordingly, more trade and investment among regional partners may not translate into a higher score on the integration index if at the same time the partners are diverging in terms of income, education, life expectancy, urbanization, and economic structure.

Caution should be exercised in the interpretation of these findings. The measures chosen for inclusion in the composite index are imperfect indicators of "convergence" and trade/investment integration. The rankings in turn should not be read normatively as "league tables" in the sense that a higher ranking is superior to a lower ranking. Indeed, a low ranking may simply indicate that an economy is more oriented globally than regionally, as is likely the case for China and the United States.

Nevertheless, the change in index value for a given economy over time can be read as a measure of its changing economic orientation. The index value for the region as a whole can also be seen as a measure of closer economic ties among Asia-Pacific economies and as one indicator of APEC's success.

The 2014 update to the index is based on data from 2011. Missing data were approximated using standard interpolation and extrapolation techniques.

Figure 4.2: Comparison of 2010 and 2011 indices

Index	Convergence Index		Composite Index		
Economy	2010	2011	2010	2011	Ranking*
Australia	-0.43	-143.60	55.14	50.05	7 (7)
Canada	15.80	-19.87	22.86	21.30	11 (12)
Chile	46.85	51.03	23.64	23.79	10 (11)
China	-49.92	-52.54	3.58	3.58	17 (16)
Hong Kong, China	-51.86	-19.89	433.35	450.42	2 (2)
Indonesia	-145.69	-84.45	1.93	3.68	16 (17)
Japan	6.91	-33.56	24.76	13.22	12 (10)
Malaysia	49.73	28.59	68.39	62.49	3 (3)
Mexico	38.31	27.65	7.52	6.46	15 (15)
New Zealand	8.05	-24.74	57.9	53.35	5 (6)
Philippines	-78.00	-91.60	10.18	9.01	14 (13)
Korea	65.27	74.50	67.81	42.48	8 (4)
Singapore	-90.11	-67.18	464.09	490.79	1 (1)
Chinese Taipei	-5.94	46.39	67.28	57.58	4 (5)
Thailand	-1.21	-18.27	42.4	51.96	6 (8)
United States	-12.17	-9.03	10.09	10.56	13 (14)
Vietnam	-74.46	-88.67	25.53	28.81	9 (9)
Asia-Pacific Region	**-7.59**	**-14.90**	**14.94**	**13.40**	**--**

* Rankings shown in parentheses indicate those from previous year (2010)

Source: Authors' calculations and Chen and Woo (2010).

The index has reached its highest level over the twenty year period. After a sharp increase in 2010, the index declined again in 2011. It mainly results from weakening tourists (due to intra-regional political and military tensions) and declining convergence. The 2011 update to indices by economy shows how the overall integration process was suspended in 2011; as a result, 9 out of the 17 included Asia-Pacific economies decreased their levels of integration with the rest of the Asia-Pacific region.

Noticeably, Singapore and Hong Kong (China) are still the most integrated economies with the Asia-Pacific markets; their levels of integration increased respectively from 464 to 491 and from 433 to 450, compared to the previous update. As trading hubs in the region, Hong Kong (China) and Singapore have benefited the most from economic recovery in trade, investment, and tourism.

The two largest economies in this region, namely the United States and China, are still near or at the bottom in the ranking. It nevertheless indicates that they may be more integrated with other regional or sub-regional markets.

ASIA-PACIFIC TRADE FLOWS

Figure 4.3 shows the share of Asia-Pacific intra-regional imports and exports to regional GDP. After various economic stimulus plans, regional economies showed some recovery in terms of intra-regional trade flows. Over the twenty-year period, intra-regional flows of exports and imports (over GDP) have increased from 11 percent to 13.4 percent. It should be re-emphasized here that this index discounts flows among sub-regions: the economies of Southeast Asia, North America and those among China, Chinese Taipei and Hong Kong, China.

The share of Asia-Pacific intra-regional merchandise trade recovered from the big hit in 2009 to pre-crisis levels of above 14 percent. However, it is still noted that China, Philippines, Malaysia, and Singapore showed slight decrease in the Asia-Pacific share of their total trade.

Figure 4.3: Intra-regional trade flows

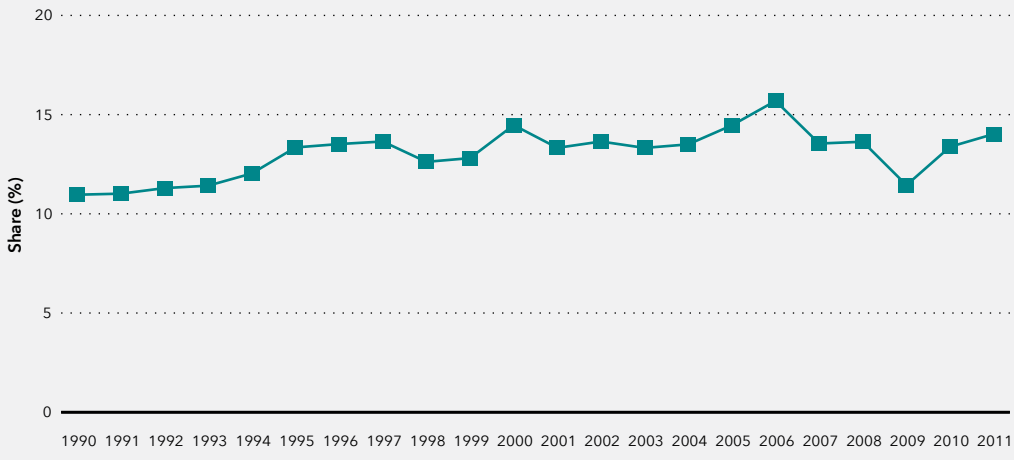


Figure 4.4: Intra-regional flows of foreign direct investment

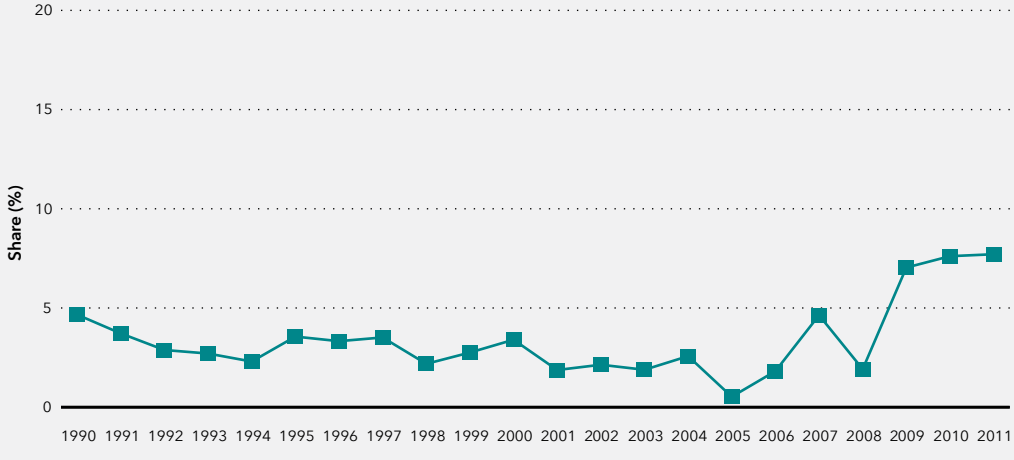


Figure 4.5: Intra-regional tourist inflows (% of total)

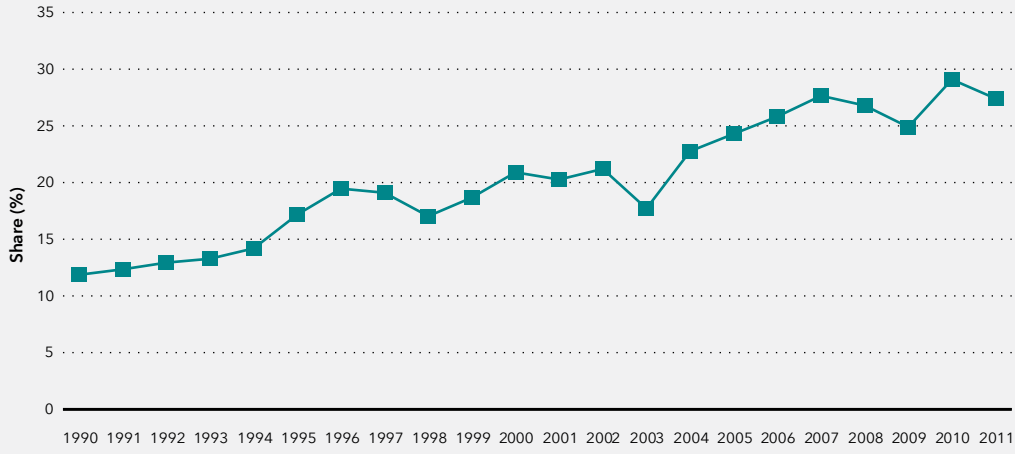
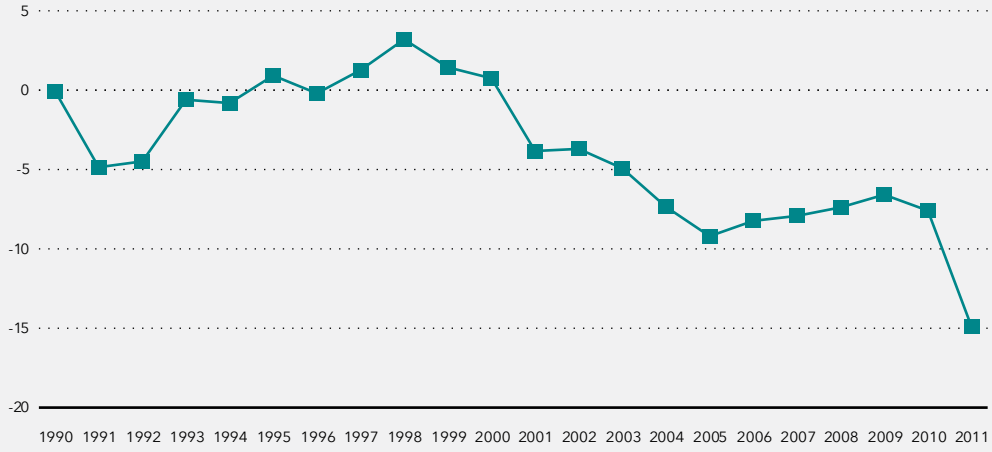


Figure 4.6: Convergence index



FOREIGN DIRECT INVESTMENT

Compared to flows of goods, intra-regional flows of investment show a much more erratic pattern. After the large decrease in FDI flows in 2008, they grew by over 200 percent year on year between 2008 and 2009, another 29 percent from 2009 to 2010, and more than 11 percent from 2010 to 2011. The biggest increases were for Japan, Singapore, and Australia, which contributed more than 75 percent of increment in the intra-regional FDI flows.

TOURISM FLOWS

Figure 4.5 shows that the recovery of the intra-regional tourism was not stable: according to the statistics, Figure 4.5 indicates that the intra-regional tourist share (to every one thousand citizens in hosting economy of the sample) stops its rebound in 2010 but the overall level is still slightly higher than previous years.

From 2007 to 2009 the number of intra-regional tourist flows had been decreasing. However, in 2010, intra-regional tourist flows rebounded to close to 30 percent, the highest level recorded in our index. In 2011, the intra-regional tourist number dropped again but still remained significantly high.

Compared to 2010, the market with the biggest intra-regional tourist decline was Korea, followed by Japan, and the Philippines, which reported around 40 percent decline.

CONVERGENCE INDEX

The sub-index of convergence shows that economies in the region have continued their trend towards divergence. GDP per capita levels in the region had been converging somewhat during the crisis years. However, in 2010, divergence in incomes began once again and continued into 2011. It should be noted here that GDP per capita accounts for just 15 percent of the weight of this sub-index while education expenditure accounts for 50 percent of the weight. Shifts towards convergence in education, even minor ones would more than outweigh much larger shifts in income.

Figure 4.7: Deviation of GDP per capita

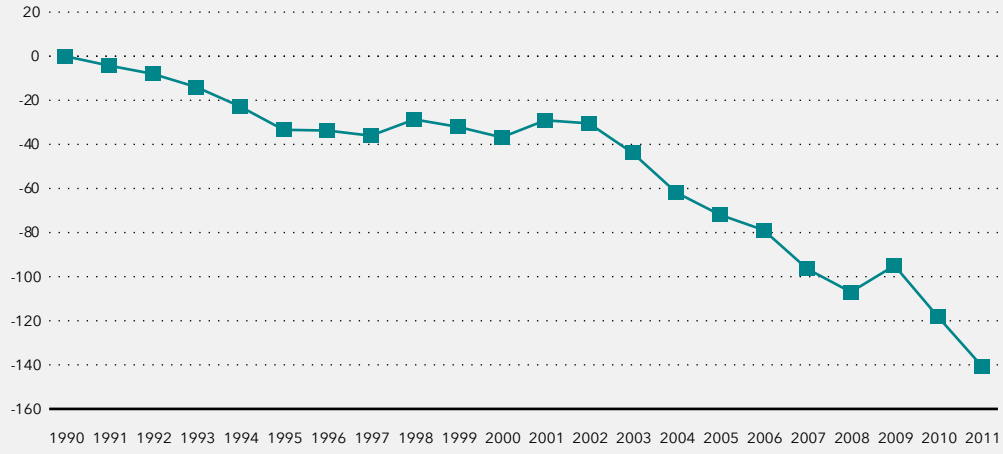
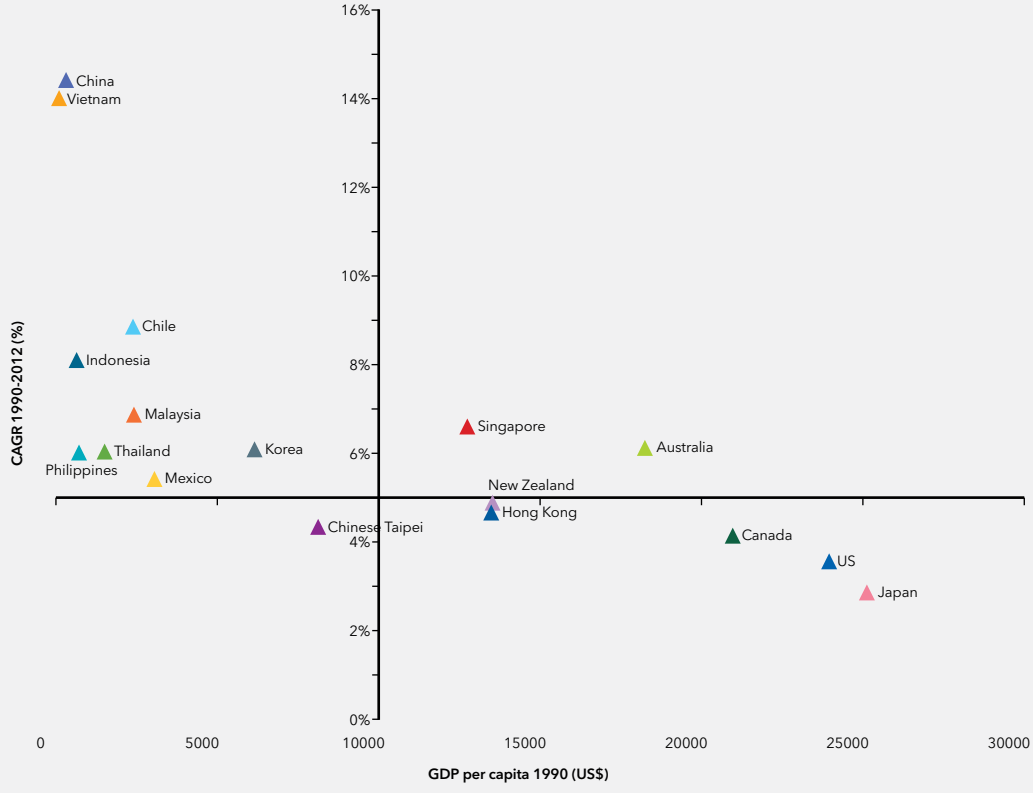


Figure 4.8: GDP per capita growth



DIVERGING INCOMES

Figure 4.7 shows that the convergence indicator of real GDP per capita continued to decrease from 2009 into 2011 which reveals that the gap in real income among sample economies has resumed its diverging trend. This finding suggests that the richer economies (i.e. the US and Japan), which suffered from the recent global economic crisis more than the poorer ones (i.e. the Southeast Asian economies minus Singapore), have been recovering.

Over the whole index period, the divergence in incomes has been driven by differences in growth rates. In 1990, the average GDP per capita in the region was just below US$10,000; by 2011, it had increased to above US$25,000 or a growth rate of around 5 percent. However, income levels in some economies have grown at a much higher rate than the average in the region while others under the average.

Figure 4.8 plots compound annual growth of GDP per capita over the past 22 years against starting values in 1990. For a convergence in income to happen, lower-income economies need to grow at a substantially higher rate than those of higher income. While some economies such as China

and Vietnam have posted very high growth rates in GDP per capita, others are only growing at rates similar to their richer counterparts. This explains the divergence seen in Figure 4.7.

The pace of urbanization in the region has been steady throughout the period as represented by the percentage of population living in urban areas. In 1990, the urban resident ratio was 65 percent with a standard deviation of 22. By 2011, the urban resident ratio had increased to 73 percent with a standard deviation of 18, meaning that all economies are becoming increasingly urbanized at a similar rate. As seen in Figure 4.9, this has been a very linear trend with few interruptions to the process unlike the share of non-agriculture in GDP which has been much more volatile, and diverging since 2009.

As shown in Figure 4.9, the indicator of urban resident share is still steadily converging over time thanks to the ambitious urbanization process in developing economies such as China and Southeast Asia. Regardless of the last two years

Figure 4.9: Deviation indicator: urban resident ratio

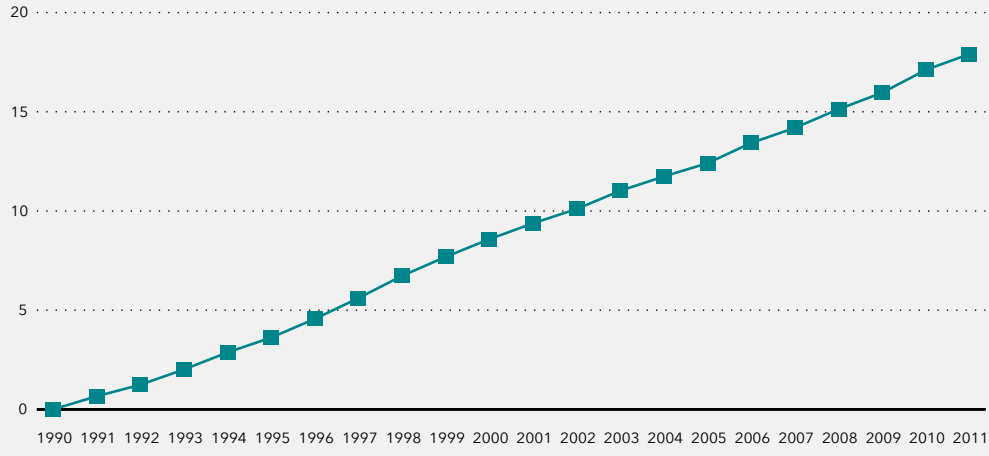


Figure 4.10: Deviation indicator : share of non-agriculture in GDP

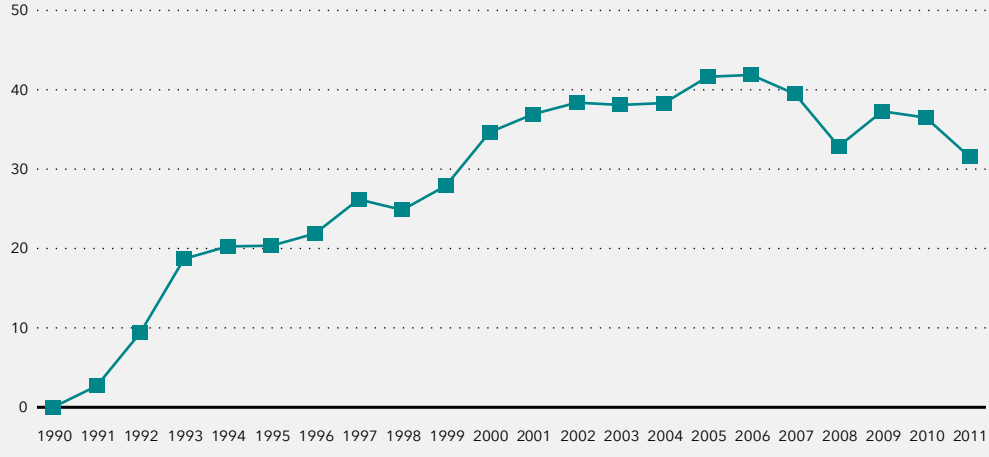


Figure 4.11: Deviation indicator: expenditure on education as a proportion of GNI

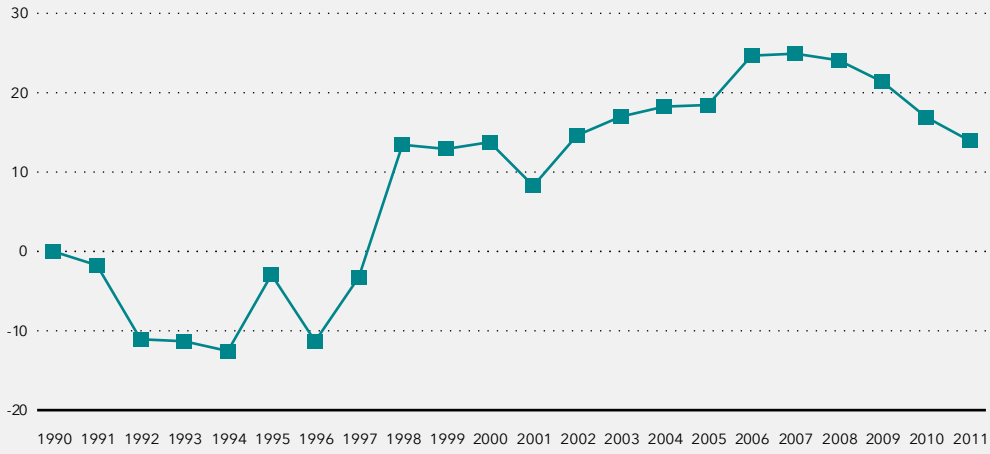
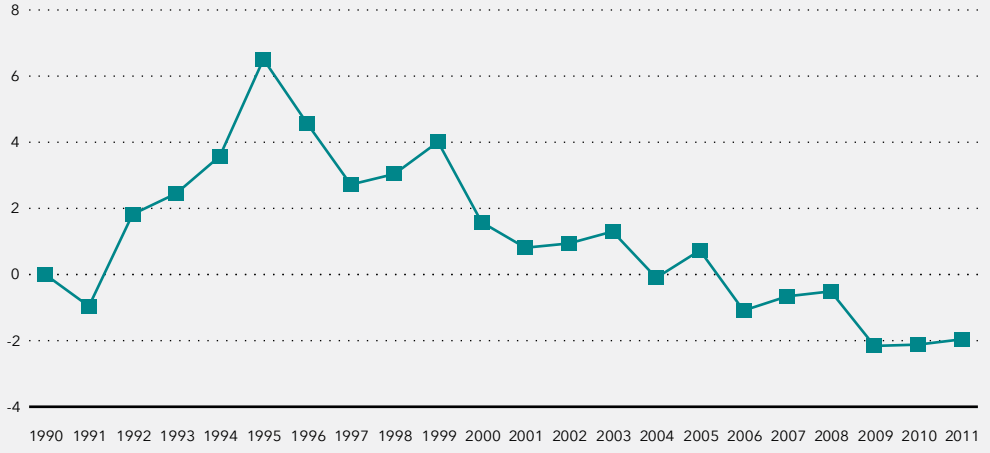


Figure 4.12: Deviation indicator: life expectancy



of divergence, the share of non-agriculture in GDP increased both on average and its convergence: in 1990 the average share of non-agriculture in GDP was 89 percent with a standard deviation of 8.2; over the next 21 years, the share of non-agriculture has steadily increased in the region and now accounts for 94 percent of total output with a standard deviation of 5.6.

While the proportion of expenditure on education in the region has significantly risen over the past 22 years, Figure 4.11 shows that its level of convergence has declined since 2008. In 1990, the average expenditure on education as a percentage of gross national income was 3.6 percent; the latest data shows that average expenditure was around 4.2 percent of GDP.

In 1990, the average life expectancy in the region was 72.4 years; by 2011, it had increased by 5 years to 77.9, with a standard deviation of 3.6. As seen in Figure 4.12, between 1991 and 1995, life expectancies had been converging. However, the level of convergence began to decrease thereafter. The latest update to the index shows that the level of convergence in life expectancy in the region is even below the level in 1990. This means life expectancy is increasing faster in some economies than others.

When APEC Leaders set out the Bogor Goals in 1994, they set out a vision through which the region would not only maintain high growth rates but also narrow development gaps. While the region has done well in integrating and overall incomes have increased at a dramatic pace, the index shows that there is a long way to go in terms of closing development gaps. Integration is not an end in itself but a means to ensuring that all citizens can achieve their potential.

ANNEX A

FOR CHAPTER 1: PROSPECTS FOR GROWTH IN THE ASIA-PACIFIC REGION

Table 1: GDP growth (%)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	3.6	2.4	2.6	2.7	2.9	3.0	3.0	3.0
Brunei Darussalam	0.9	-1.2	5.4	3.0	3.7	5.5	5.6	3.5
Cambodia	7.3	7.0	7.2	7.3	7.3	7.5	7.5	7.5
Canada	1.7	2.0	2.3	2.4	2.4	2.2	2.1	2.0
Chile	5.5	4.2	3.6	4.1	4.2	4.5	4.5	4.5
China	7.7	7.7	7.5	7.3	7.0	6.8	6.6	6.5
Colombia	4.2	4.3	4.5	4.5	4.5	4.5	4.5	4.5
Ecuador	5.1	4.2	4.2	3.5	3.5	3.5	3.5	3.5
Hong Kong, China	1.6	2.9	3.7	3.8	3.9	3.9	4.0	4.0
India	4.7	4.4	5.4	6.4	6.5	6.7	6.7	6.8
Indonesia	6.3	5.8	5.4	5.8	6.0	6.0	6.0	6.0
Japan	1.4	1.5	1.4	1.0	0.7	1.0	1.0	1.1
Korea	2.0	2.8	3.7	3.8	3.8	3.8	3.8	3.8
Laos	7.9	8.2	7.5	7.8	8.0	7.7	7.5	7.5
Malaysia	5.6	4.7	5.2	5.0	5.0	5.0	5.0	5.0
Mexico	3.9	1.1	3.0	3.5	3.8	3.8	3.8	3.8
Mongolia	12.4	11.7	12.9	7.7	5.7	9.0	6.7	8.8
Myanmar	7.3	7.5	7.8	7.8	7.8	7.8	7.8	7.7
New Zealand	2.6	2.4	3.3	3.0	2.6	2.5	2.5	2.5
Papua New Guinea	8.1	4.6	6.0	21.6	3.3	3.4	3.4	3.7
Peru	6.3	5.0	5.5	5.8	5.8	5.8	5.8	5.8
Philippines	6.8	7.2	6.5	6.5	6.2	6.0	6.0	6.0
Russia	3.4	1.3	1.3	2.3	2.5	2.5	2.5	2.5
Singapore	1.9	4.1	3.6	3.6	3.6	3.6	3.7	3.8
Chinese Taipei	1.5	2.1	3.1	3.9	4.2	4.4	4.5	4.5
Thailand	6.5	2.9	2.5	3.8	4.8	4.7	4.5	4.5
United States	2.8	1.9	2.8	3.0	3.0	2.9	2.6	2.2
Vietnam	5.2	5.4	5.6	5.7	5.8	5.9	6.0	6.0

	2012	2013	2014	2015	2016	2017	2018	2019
Asia-Pacific	3.8	3.3	3.7	3.8	3.8	3.7	3.6	3.5
of which advanced economies	1.7	1.3	1.7	1.7	1.8	1.7	1.6	1.5
of which emerging economies	2.1	2.0	2.0	2.1	2.0	2.0	2.0	2.0

Table 2: Inflation, average consumer prices (%)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	1.8	2.5	2.3	2.4	2.5	2.5	2.5	2.5
Brunei Darussalam	0.1	0.4	0.5	0.5	0.5	0.6	0.6	0.6
Cambodia	2.9	3.0	3.8	3.2	3.0	3.0	3.0	3.0
Canada	1.5	1.0	1.5	1.9	2.0	2.0	2.0	2.0
Chile	3.0	1.8	3.5	2.9	3.0	3.0	3.0	3.0
China	2.7	2.6	3.0	3.0	3.0	3.0	3.0	3.0
Colombia	3.2	2.0	1.9	2.9	3.0	3.0	3.0	3.0
Ecuador	5.1	2.7	2.8	2.6	2.5	2.5	2.5	2.5
Hong Kong, China	4.1	4.3	4.0	3.8	3.5	3.5	3.5	3.5
India	10.2	9.5	8.0	7.5	6.9	6.3	6.2	6.1
Indonesia	4.0	6.4	6.3	5.5	5.4	5.5	5.3	5.0
Japan	0.0	0.4	2.8	1.7	1.8	2.0	2.0	2.0
Korea	2.2	1.3	1.8	3.0	3.0	3.0	3.0	3.0
Laos	4.3	6.4	7.5	7.5	7.6	6.0	5.7	5.7
Malaysia	1.7	2.1	3.3	3.9	3.0	2.7	2.7	2.7
Mexico	4.1	3.8	4.0	3.5	3.0	3.0	3.0	3.0
Mongolia	15.0	9.6	12.0	11.0	7.9	7.3	6.9	6.5
Myanmar	2.8	5.8	6.6	6.9	6.5	6.1	5.3	4.7
New Zealand	1.1	1.1	2.2	2.2	2.1	2.0	2.0	2.0
Papua New Guinea	2.2	3.8	6.0	5.0	5.0	5.0	5.0	5.0
Peru	3.7	2.8	2.5	2.1	2.0	2.0	2.0	2.0
Philippines	3.2	2.9	4.4	3.6	3.5	3.5	3.5	3.5
Russia	5.1	6.8	5.8	5.3	5.2	5.0	5.0	5.0
Singapore	4.6	2.4	2.3	2.6	2.4	2.5	2.4	2.4
Chinese Taipei	1.9	0.8	1.4	2.0	2.0	2.0	2.0	2.0
Thailand	3.0	2.2	2.3	2.1	2.1	2.0	2.0	2.0
United States	2.1	1.5	1.4	1.6	1.8	2.0	2.0	2.0
Vietnam	9.1	6.6	6.3	6.2	6.1	5.8	5.4	5.2
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
Asia-Pacific	2.6	2.4	2.7	2.6	2.7	2.7	2.7	2.7
of which advanced economies	1.2	1.1	1.4	1.3	1.4	1.5	1.5	1.5
of which emerging economies	1.3	1.3	1.3	1.2	1.2	1.2	1.1	1.1

Table 3: Current account balance (US$ billions)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	-64.0	-44.2	-37.6	-41.2	-42.0	-42.8	-51.6	-57.9
Brunei Darussalam	7.9	6.3	6.6	6.3	6.2	6.4	7.1	7.3
Cambodia	-1.2	-1.3	-1.4	-1.4	-1.3	-1.3	-1.3	-1.5
Canada	-62.3	-58.9	-46.7	-45.9	-47.3	-49.4	-49.1	-45.8
Chile	-9.1	-9.5	-8.6	-8.0	-7.9	-8.2	-8.8	-9.2
China	193.1	188.7	224.3	265.5	308.1	346.2	390.1	444.3
Colombia	-11.8	-12.7	-12.9	-13.1	-12.8	-13.4	-14.3	-15.0
Ecuador	-0.3	-1.4	-2.4	-3.3	-4.3	-5.6	-6.8	-8.0
Hong Kong, China	7.3	8.6	9.8	12.3	13.4	15.4	17.7	20.5
India	-88.2	-37.2	-47.5	-53.8	-60.7	-66.9	-74.2	-81.7
Indonesia	-24.4	-28.5	-25.8	-24.6	-26.7	-28.8	-30.5	-32.3
Japan	60.4	34.3	57.2	65.0	65.5	73.5	75.5	84.8
Korea	48.1	70.7	57.3	48.4	50.1	55.5	56.7	56.7
Laos	-2.6	-2.9	-3.0	-2.8	-2.6	-2.5	-2.9	-3.2
Malaysia	18.6	11.8	13.9	15.1	17.0	18.4	19.4	19.6
Mexico	-14.8	-22.3	-24.0	-27.4	-29.0	-28.6	-29.2	-27.1
Mongolia	-3.4	-3.2	-2.7	-2.6	-3.1	-2.8	-2.8	-3.0
Myanmar	-2.4	-2.8	-3.2	-3.4	-3.7	-4.1	-4.7	-5.2
New Zealand	-7.0	-7.7	-9.6	-11.0	-12.4	-13.6	-14.7	-15.3
Papua New Guinea	-7.7	-4.5	-0.7	2.6	1.9	1.9	1.7	1.3
Peru	-6.8	-10.2	-10.4	-10.3	-10.2	-10.6	-11.0	-11.1
Philippines	7.2	9.4	9.3	8.7	7.6	6.3	4.5	2.6
Russia	72.0	33.0	44.9	34.4	29.8	30.1	24.5	24.7
Singapore	49.4	54.4	53.7	54.2	54.6	55.2	56.1	56.7
Chinese Taipei	50.7	57.4	59.0	58.4	58.4	60.1	62.9	66.9
Thailand	-1.5	-2.8	0.8	1.2	0.7	1.3	1.3	2.6
United States	-440.4	-379.3	-391.1	-472.0	-532.7	-566.5	-609.7	-627.1
Vietnam	9.1	11.3	8.2	7.1	5.4	4.2	-2.4	-8.7
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
North America	-517.5	-460.6	-461.8	-545.3	-609.0	-644.5	-688.0	-699.9
Northeast Asia	428.3	389.5	449.7	481.4	522.2	577.8	624.6	695.0
Oceania	-78.7	-56.4	-47.8	-49.6	-52.5	-54.5	-64.5	-71.8
South America	-28.0	-33.7	-34.3	-34.6	-35.2	-37.8	-40.8	-43.3
Southeast Asia	60.0	55.0	59.1	60.5	57.0	55.0	46.6	38.0
India	-88.2	-37.2	-47.5	-53.8	-60.7	-66.9	-74.2	-81.7

Table 4: Current account balance (% of GDP)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	-4.1	-2.9	-2.6	-2.8	-2.7	-2.7	-3.1	-3.3
Brunei Darussalam	46.9	39.0	39.3	37.9	36.3	37.1	38.7	38.8
Cambodia	-8.7	-8.6	-8.4	-7.4	-6.6	-6.0	-5.5	-5.8
Canada	-3.4	-3.2	-2.6	-2.5	-2.4	-2.4	-2.3	-2.2
Chile	-3.4	-3.4	-3.3	-2.8	-2.6	-2.5	-2.5	-2.5
China	2.3	2.1	2.2	2.4	2.6	2.7	2.8	3.0
Colombia	-3.2	-3.3	-3.3	-3.2	-2.9	-2.9	-2.9	-2.8
Ecuador	-0.3	-1.5	-2.4	-3.1	-3.8	-4.7	-5.4	-6.0
Hong Kong, China	2.8	3.1	3.3	3.9	4.0	4.3	4.6	5.0
India	-4.7	-2.0	-2.4	-2.5	-2.6	-2.6	-2.6	-2.6
Indonesia	-2.8	-3.3	-3.0	-2.7	-2.7	-2.7	-2.6	-2.6
Japan	1.0	0.7	1.2	1.3	1.3	1.4	1.4	1.5
Korea	4.3	5.8	4.4	3.5	3.4	3.4	3.3	3.0
Laos	-28.4	-29.5	-27.3	-23.7	-19.4	-17.0	-17.0	-17.0
Malaysia	6.1	3.8	4.0	4.0	4.1	4.1	3.9	3.7
Mexico	-1.2	-1.8	-1.9	-2.0	-2.0	-1.9	-1.8	-1.6
Mongolia	-32.6	-27.9	-22.1	-19.7	-22.2	-18.0	-16.2	-15.9
Myanmar	-4.4	-4.9	-5.3	-5.2	-5.3	-5.3	-5.4	-5.4
New Zealand	-4.1	-4.2	-4.9	-5.4	-5.8	-6.1	-6.3	-6.3
Papua New Guinea	-51.0	-27.9	-3.7	11.0	7.9	7.4	6.6	4.6
Peru	-3.4	-4.9	-4.8	-4.4	-4.0	-3.9	-3.7	-3.5
Philippines	2.9	3.5	3.2	2.6	2.0	1.5	1.0	0.5
Russia	3.6	1.6	2.1	1.6	1.4	1.3	1.0	1.0
Singapore	17.4	18.4	17.7	17.1	16.5	16.0	15.5	15.0
Chinese Taipei	10.7	11.7	11.7	10.9	10.3	9.9	9.7	9.6
Thailand	-0.4	-0.7	0.2	0.3	0.2	0.3	0.3	0.5
United States	-2.7	-2.3	-2.2	-2.6	-2.8	-2.8	-2.9	-2.8
Vietnam	5.8	6.6	4.3	3.5	2.5	1.8	-1.0	-3.3
	2012	2013	2014	2015	2016	2017	2018	2019
North America	-2.7	-2.3	-2.2	-2.5	-2.7	-2.7	-2.8	-2.7
Northeast Asia	2.4	2.1	2.4	2.4	2.4	2.5	2.5	2.7
Oceania	-4.5	-3.3	-2.9	-2.9	-3.0	-3.0	-3.4	-3.6
South America	-3.0	-3.5	-3.5	-3.4	-3.2	-3.2	-3.2	-3.2
Southeast Asia	2.6	2.3	2.4	2.3	2.0	1.8	1.4	1.1
India	-4.7	-2.0	-2.4	-2.5	-2.6	-2.6	-2.6	-2.6

Table 5: Export growth (%)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	6.9	7.3	7.2	6.2	5.2	3.1	3.1	3.3
Brunei Darussalam	-2.6	2.7	7.5	6.3	9.1	3.6	9.9	4.0
Cambodia	28.3	16.4	13.8	14.1	12.3	12.3	11.9	10.1
Canada	2.1	2.2	3.8	5.5	5.3	5.1	4.8	4.5
Chile	2.1	3.5	3.2	2.7	3.6	4.0	4.1	4.1
China	5.7	8.6	6.8	7.0	6.9	6.8	6.6	6.5
Colombia	4.5	1.8	4.4	6.7	6.5	4.7	3.8	6.1
Ecuador	2.2	7.6	-0.2	6.1	4.9	3.2	3.9	3.2
Hong Kong, China	1.8	6.7	8.4	8.4	8.4	8.4	8.4	8.4
India	2.2	5.8	7.7	8.2	8.2	8.2	8.2	8.2
Indonesia	-1.0	2.2	2.4	6.8	11.6	9.0	9.5	8.3
Japan	-4.2	-2.0	2.8	3.2	3.5	3.7	3.5	3.1
Korea	5.6	4.8	7.1	8.5	10.7	10.6	9.6	9.7
Laos	8.6	7.7	6.4	7.6	13.9	10.0	5.7	5.7
Malaysia	-4.0	-3.3	4.3	4.2	4.3	4.3	4.1	3.5
Mexico	9.0	2.8	6.0	7.3	8.4	8.6	7.6	7.6
Mongolia	-8.2	-2.4	30.4	11.0	-4.1	16.7	1.6	12.4
Myanmar	1.0	16.3	23.3	12.2	12.1	13.4	16.1	15.4
New Zealand	4.1	0.7	3.2	3.9	3.9	3.3	2.8	2.5
Papua New Guinea	-9.2	6.8	15.8	30.6	-1.1	-0.4	-0.4	0.3
Peru	2.7	-1.8	7.8	7.9	7.9	7.1	6.8	6.8
Philippines	10.7	0.6	7.5	7.7	6.6	6.3	6.1	6.3
Russia	3.3	1.0	1.8	3.6	3.5	3.8	3.9	3.8
Singapore	-0.1	2.9	5.8	6.1	6.4	6.5	6.3	6.2
Chinese Taipei	-1.1	3.3	3.9	5.4	5.7	5.7	5.9	6.0
Thailand	2.5	0.2	6.7	5.1	5.2	5.2	5.5	5.2
United States	3.8	2.4	5.8	4.6	5.0	5.3	5.0	4.6
Vietnam	21.3	11.8	18.3	13.6	11.2	10.5	8.0	7.9
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**
Asia-Pacific	3.2	4.0	5.8	6.0	6.3	6.2	6.0	5.8
of which advanced economies	1.2	1.5	3.0	3.2	3.4	3.4	3.3	3.2
of which emerging economies	2.0	2.4	2.7	2.9	2.9	2.8	2.7	2.7

Table 6: Import growth (%)

	2012	2013	2014	2015	2016	2017	2018	2019
Australia	6.7	-3.4	-2.4	1.8	2.3	2.4	2.5	2.2
Brunei Darussalam	21.4	-5.2	5.4	5.1	3.7	5.5	5.6	3.5
Cambodia	8.1	12.1	9.7	12.7	11.6	11.4	9.4	10.8
Canada	3.3	1.7	3.5	4.3	4.4	4.3	4.3	4.1
Chile	7.0	1.0	2.9	4.3	4.5	4.5	4.5	4.5
China	5.1	10.6	7.1	6.6	6.2	6.0	6.0	6.0
Colombia	10.7	1.0	4.0	6.2	4.8	4.8	4.4	4.5
Ecuador	1.9	8.5	4.5	5.8	6.3	5.8	5.8	5.1
Hong Kong, China	3.0	7.6	8.0	8.1	8.1	8.1	8.1	8.1
India	2.1	-4.5	8.6	8.6	8.6	9.0	8.6	8.6
Indonesia	11.3	-0.4	1.1	4.9	8.9	7.5	7.5	7.4
Japan	3.0	0.7	0.5	4.3	4.3	3.9	5.3	3.9
Korea	0.5	4.3	5.9	7.9	11.3	11.6	10.8	10.9
Laos	32.5	-1.7	-2.1	2.0	3.9	5.3	8.3	8.3
Malaysia	0.3	-2.1	1.5	1.9	2.5	3.1	3.2	3.8
Mexico	4.6	3.0	6.0	7.7	8.0	7.8	8.0	7.8
Mongolia	2.8	-5.8	11.5	6.2	5.0	6.6	1.8	9.7
Myanmar	20.4	12.4	17.0	12.9	11.6	12.2	20.0	0.0
New Zealand	3.6	7.6	6.5	3.9	3.7	2.7	2.7	2.3
Papua New Guinea	19.5	-35.4	-3.3	10.2	0.6	1.0	1.0	8.4
Peru	9.5	5.5	6.0	6.2	6.4	6.5	6.5	6.5
Philippines	6.6	3.8	10.0	11.3	11.1	10.1	9.8	9.7
Russia	9.0	2.6	1.5	4.7	4.6	4.6	5.2	3.8
Singapore	2.5	1.9	6.2	6.5	7.0	7.1	7.0	6.9
Chinese Taipei	-2.9	4.1	3.6	4.2	4.4	4.6	4.9	5.1
Thailand	7.1	1.7	2.6	6.6	4.6	4.7	4.8	4.5
United States	2.1	1.2	3.6	5.6	5.5	5.2	5.2	4.3
Vietnam	9.8	15.3	18.1	12.1	10.9	10.2	9.8	9.0
	2012	2013	2014	2015	2016	2017	2018	2019
Asia-Pacific	3.7	3.5	4.7	6.0	6.2	6.0	6.1	5.7
of which advanced economies	1.7	1.3	2.2	3.4	3.6	3.5	3.7	3.3
of which emerging economies	2.0	2.2	2.5	2.6	2.5	2.5	2.5	2.4

Table 7: GDP and inflation weights (%)

	Asia-Pacific Weight	Advanced Economies	Emerging Economies
Australia	3.5	5.1	
Brunei Darussalam	0.0	0.1	
Cambodia	0.0		0.1
Canada	4.1	6.1	
Chile	0.6	0.9	
China	18.8		58.9
Colombia	0.8		2.6
Ecuador	0.2		0.6
Hong Kong, China	0.6	0.9	
India	4.3		13.4
Indonesia	2.0		6.2
Japan	12.8	18.8	
Korea	2.6	3.9	
Laos	0.0		0.1
Malaysia	0.7		2.2
Mexico	2.8		8.6
Mongolia	0.0		0.1
Myanmar	0.1		0.4
New Zealand	0.4	0.6	
Papua New Guinea	0.0		0.1
Peru	0.4		1.4
Philippines	0.6		1.8
Russia	4.6	6.7	
Singapore	0.6	1.0	
Chinese Taipei	1.1	1.6	
Thailand	0.8		2.6
United States	37.0	54.5	
Vietnam	0.4		1.1

Table 8: Export and import weights (%)

	Export Weight	Import Weight
Australia	2.8	2.6
Brunei Darussalam	0.1	0.0
Cambodia	0.1	0.1
Canada	5.0	4.8
Chile	0.9	0.8
China	22.5	18.9
Colombia	0.6	0.6
Ecuador	0.3	0.3
Hong Kong, China	5.4	5.8
India	3.3	4.9
Indonesia	2.1	1.9
Japan	8.5	8.8
Korea	6.1	5.3
Laos	0.0	0.0
Malaysia	2.5	2.0
Mexico	4.0	3.9
Mongolia	0.0	0.1
Myanmar	0.1	0.1
New Zealand	0.4	0.4
Papua New Guinea	0.1	0.0
Peru	0.5	0.4
Philippines	0.6	0.7
Russia	5.7	3.4
Singapore	4.5	3.8
Chinese Taipei	3.3	2.8
Thailand	2.5	2.5
United States	16.8	23.8
Vietnam	1.3	1.2

ANNEX B

FOR CHAPTER 3: PERCEPTIONS OF GROWTH AND INTEGRATION IN THE ASIA-PACIFIC

The results of this survey are based on an online or paper questionnaire conducted from 31 July to 5 September 2014. A total of 602 opinion-leaders from 25 Asia-Pacific economies, including all 21 APEC members responded to the survey.

The survey is disseminated through PECC member committees who are asked to identify panelists based on their knowledge of the Asia-Pacific region.

As this is a multi-stakeholder survey, the Council's member committees are asked to identify stakeholders – from business, government and the non-government sectors. This year 27 percent of respondents were from the business sector, 20 percent from the government, and 53 percent from non-government (including analyst, civil society and the media).

This is not a survey of public opinion but rather, a survey of those whose views influence policy-making, especially at the regional level. As some of the questions tend to be technical, they require a relatively deep knowledge of developments at regional level. This is by no means a reflection of the general views of a population within any sub-region or even economy. However, we do believe that those surveyed include those who are responsible for influencing and often making decisions on various aspects of their economy's positions within different regional groups.

The profiles of respondents are:

- **Government**
  Panelists should be either decision-makers or senior advisors to decision-makers. As a guide, the government respondents in previous years included a number of former and current Ministers, Deputy and Vice-Ministers, Central Bank Governors and their advisors for Asia-Pacific issues, current APEC Senior Officials, and a number of former APEC Senior Officials.

- **Business**
  Panelists should be from companies who have operations in a number of Asia-Pacific economies or conduct business with a number of partners from the region. This might include each economy's current ABAC members as well as past ABAC members. In last year's survey, these included CEOs, vice presidents for Asia-Pacific operations, and directors of chambers of commerce.

- **Non-government: Research Community/Civil Society/Media**
  Panelists should be well-versed in Asia-Pacific affairs, being the type of people governments, businesses, and the media would tap into to provide input on issues related to Asia-Pacific cooperation. These included presidents of institutes concerned with Asia-Pacific issues, heads of departments, senior professors, and correspondents covering international affairs.

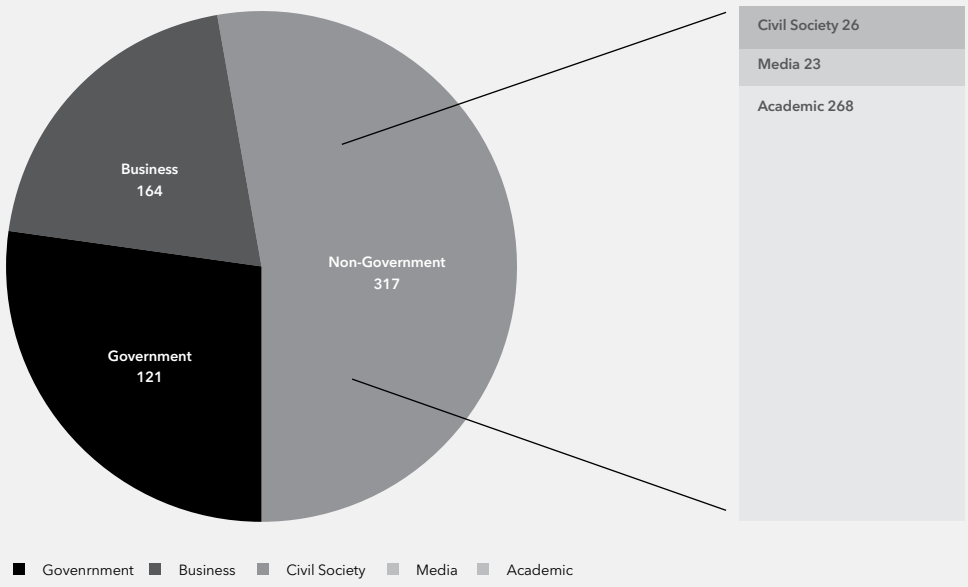
  In addition to our member committees, we would like to express our appreciation towards UN ESCAP and the Consumer Unity and Trust Society (CUTS International) from whom we have also received assistance to reach out to more respondents beyond our membership for participation in the survey.

Respondent Breakdown
We do not disaggregate results for each economy but rather by sub-regions – Northeast Asia, North

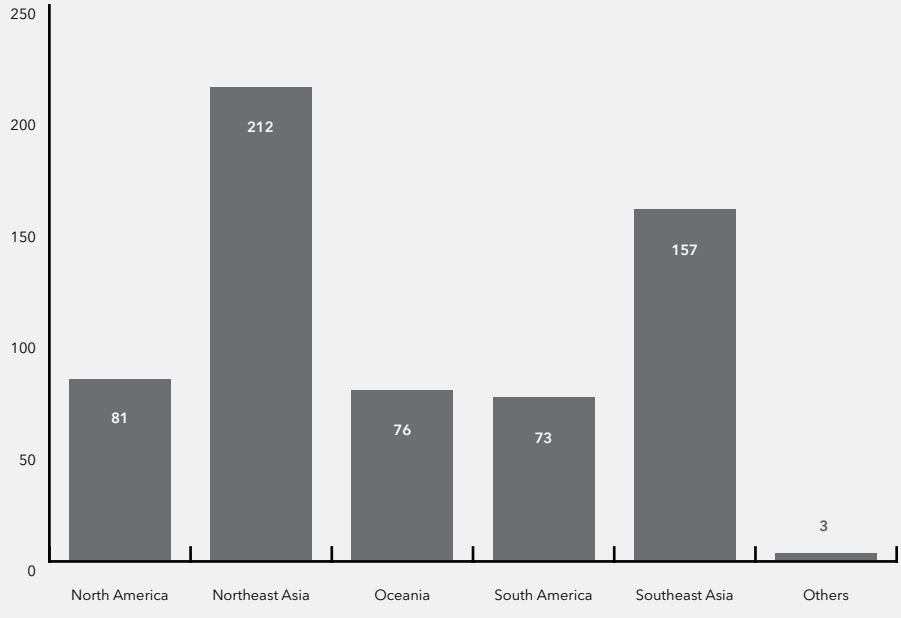
America, Oceania, Pacific South America, and Southeast Asia.

- North America: Canada, Mexico, and the United States
- Northeast Asia: China, Hong Kong (China), Japan, Korea, Mongolia, Russia, and Chinese Taipei
- Oceania: Australia, New Zealand, and Papua New Guinea
- Pacific South America: Chile, Colombia, Ecuador, and Peru
- Southeast Asia: Brunei Darussalam, India, Indonesia, Malaysia, Philippines, Singapore, Thailand, and Vietnam

Number of respondents by sector



Number of respondents by sector



ECONOMIC OUTLOOK AND RISKS TO GROWTH

1. What are your expectations for economic growth over the next 12 months compared to the last year for the following economies/regions? *Please select/tick the appropriate box.*

	Much weaker	Somewhat weaker	About the same	Somewhat stronger	Much stronger	Don't know/ No response
China	2.2%	31.4%	41.1%	20.6%	3.8%	0.8%
India	1.3%	16.8%	37.2%	38.1%	3.9%	2.7%
Japan	3.3%	23.4%	39.6%	30.8%	1.8%	1.0%
Russia	18.9%	48.2%	20.9%	8.0%	1.2%	2.7%
Southeast Asia	0.5%	9.0%	40.7%	41.2%	6.9%	1.7%
The United States of America	1.2%	9.2%	31.8%	52.0%	5.2%	0.7%
The European Union	2.8%	27.2%	44.7%	21.4%	1.8%	2.0%
The world economy	0.8%	14.7%	50.9%	31.3%	1.0%	1.2%

2. Please select the top five risks to growth for your economy over the next 2-3 years.
Please select ONLY five (5) risks, using a scale of 1-5, please write 1 for the least serious risk and, 2 for the next most important risk and so on.

	1 - Least serious	2	3	4	5 - Most serious	Weighted Score
A slowdown in the Chinese economy	6.0%	6.6%	12.3%	11.2%	12.6%	1.6
Lack of political leadership	5.3%	6.2%	5.3%	7.8%	15.3%	1.4
Failure to implement structural reforms	4.4%	5.2%	7.5%	10.1%	11.4%	1.3
Fiscal crises in major economies	5.0%	5.7%	5.7%	6.0%	5.5%	0.9
A slowdown in the US economy	4.1%	5.3%	7.3%	5.0%	5.7%	0.8
Shortage of available talent/skills	6.0%	7.1%	5.2%	4.8%	4.3%	0.8
Lack of adequate infrastructure	4.4%	5.2%	4.6%	5.0%	5.2%	0.7
Unemployment	5.5%	4.6%	5.9%	4.8%	3.4%	0.7
Energy security	1.4%	4.6%	3.2%	4.8%	4.1%	0.6
Sharp fall in asset prices	4.4%	3.0%	4.4%	4.6%	2.3%	0.5
Banking/financial sector crisis	3.9%	4.1%	3.0%	3.9%	3.2%	0.5
Political tensions or military incidents in the South China Sea	4.6%	2.7%	2.8%	3.2%	3.2%	0.5
Increasing corruption	4.3%	3.2%	3.7%	3.6%	1.8%	0.4
Protectionism	4.8%	3.4%	3.2%	2.8%	2.1%	0.4
Deterioration in US-China relations	3.0%	4.3%	2.5%	3.0%	2.1%	0.4
Inflation	4.6%	4.8%	2.3%	2.0%	2.5%	0.4
Natural disasters	4.8%	1.8%	2.8%	2.7%	2.0%	0.4
A health pandemic	2.1%	3.0%	2.0%	1.2%	2.3%	0.3
Terrorist acts including cyber attacks	2.1%	4.4%	2.8%	0.5%	1.8%	0.3
Unfavorable currency realignments	2.3%	2.3%	2.3%	2.1%	0.9%	0.3
New global regulations	2.5%	1.4%	2.0%	2.5%	1.1%	0.3
Air pollution	1.6%	1.6%	1.2%	2.0%	1.6%	0.2
Water security	2.7%	2.1%	1.6%	2.0%	0.9%	0.2
Economic sanctions	2.5%	1.8%	0.9%	1.8%	1.2%	0.2
Food security	2.8%	2.0%	2.3%	0.9%	0.7%	0.2
Political tensions or military incidents related to North Korea	1.8%	1.4%	1.2%	0.5%	1.2%	0.2
A slowdown in the Japanese economy	1.4%	1.2%	1.2%	0.5%	0.9%	0.1
Deflation	1.4%	1.1%	0.7%	0.7%	0.9%	0.1

FUTURE GROWTH AND CONSUMPTION IN THE ASIA-PACIFIC

3. In 2010 APEC leaders agreed that the quality of growth of the region needed to be improved so it will be more balanced, inclusive, sustainable, innovative, and secure. How satisfied are you with efforts so far on each dimension? *Use a scale of 1-5, select: '1' if you are not at all satisfied; '2' if slightly satisfied; '3' if moderately satisfied; '4' if very satisfied; '5' if extremely satisfied; or 'don't know' if you are not sure or are not aware of actions taken to promote the APEC Growth Strategy.*

	1 - Not at all satisfied	2 - Slightly satisfied	3 - Moderately satisfied	4 - Very satisfied	5 -Extremely satisfied	Don't know
Balanced Growth (i.e. through macroeconomic policies and structural reforms that will gradually unwind imbalances and raise potential output)	18.6%	35.9%	35.6%	5.5%	0.7%	3.6%
Inclusive Growth (i.e. ensure that all our citizens have the opportunity to participate in, contribute to, and benefit from global economic growth)	28.2%	39.9%	24.2%	3.3%	0.9%	3.5%
Sustainable Growth (i.e. growth compatible with global efforts for protection of the environment and transition to green economies)	20.8%	38.8%	29.1%	7.1%	1.8%	2.4%
Innovative Growth (i.e. create an economic environment that promotes innovation and emerging economic sectors)	16.7%	31.8%	33.8%	10.5%	3.5%	3.6%
Secure Growth (i.e. protect the region's citizens' economic and physical well-being and to provide the secure environment necessary for economic activity)	16.7%	34.9%	32.4%	7.6%	2.4%	6.0%

4. Please rank each of the following in order of how important you think they will be to the future growth of your economy over the next 5-10 years. *Use a scale of 1-5, select: '1' if you think the issue is not at all important; '2' of little importance; '3' moderately important; '4' important, '5' very important or 'don't know' if you are not sure.*

	1- Not at all important	2	3	4	5 – Very important	Don't know	Weighted Score
Technological innovation	0.6%	3.6%	11.4%	27.7%	53.6%	3.2%	4.2
Policy reform, i.e. improvements in institutional quality and government regulation	1.3%	6.3%	16.0%	27.1%	47.8%	1.5%	4.1
Exports to emerging market economies	0.6%	4.0%	19.2%	36.6%	38.3%	1.3%	4.0
Exports to developed market economies	0.4%	7.3%	27.1%	35.0%	29.2%	1.1%	3.8
Investments in physical infrastructure	1.7%	9.1%	23.5%	26.4%	37.2%	2.2%	3.8
Foreign direct investment	1.5%	7.7%	24.0%	37.8%	27.9%	1.1%	3.8
Trade liberalization	2.8%	10.6%	28.3%	35.7%	21.7%	0.9%	3.6
Increased household consumption	3.0%	16.9%	29.3%	28.8%	20.3%	1.7%	3.4
Improved social safety nets	4.6%	15.6%	27.7%	29.0%	20.8%	2.2%	3.4
Increased government spending	9.9%	25.2%	36.8%	16.1%	10.8%	1.1%	2.9

5. Please select the top 5 categories in which you think consumers in your economy are likely to spend an increasing share of their income on *(select only 5)*

Category	Total
Education of children	16.2%
Housing	14.8%
Healthcare	14.5%
Savings/Investments for the future	10.7%
Holidays	9.5%
Taking care of elderly dependents	8.5%
Electronics	6.0%
Cars	5.3%
Other types of leisure activities	4.4%
Eating out	3.5%
Household appliances	2.9%
Luxury items	1.9%
Clothing	1.8%

6. How important do you think the following are for growth prospects in the Asia-Pacific region as a whole over the next 5-10 years? *Use a scale of 1-5, select: '1' if you think the issue not at all important; '2' of little importance; '3' moderately important; '4' important, '5' very important or 'don't know' if you are not sure.*

	1 - Not at all important	2	3	4	5 – Very important	Don't know	Weighted Score
The success of structural reforms in China and more demand-led growth	1.3%	1.8%	10.0%	31.2%	55.2%	0.6%	4.4
Further liberalization of trade and investment in the Asia-Pacific as a whole	0.9%	5.8%	23.6%	40.1%	29.2%	0.4%	3.9
Improvements to the rule of law	1.1%	5.7%	24.0%	33.9%	33.9%	1.3%	3.9
Qualitative improvements to workforce training and mobility	0.9%	5.5%	23.0%	39.8%	29.6%	1.1%	3.9
Structural changes and a higher growth path in the US	1.1%	5.1%	25.0%	41.4%	26.5%	0.9%	3.8
The development of new products and services	2.1%	13.1%	32.7%	32.9%	17.8%	1.5%	3.5
The success of Abenomics and the restoration of growth in Japan	1.7%	12.0%	31.7%	36.4%	15.8%	2.4%	3.5
The ASEAN integration process	2.4%	15.0%	32.9%	29.5%	18.3%	1.9%	3.4
Significantly higher growth in South Asia	1.7%	13.0%	37.2%	37.5%	10.0%	0.6%	3.4
New energy sources from North America and the Arctic	1.9%	19.5%	35.9%	28.1%	11.6%	3.1%	3.2

REGIONAL COOPERATION AND INTEGRATION

7. Please indicate your agreement or disagreement with the following statements:

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree	Don't know
APEC is as important or more important today compared to 1989 when it was created	3.0%	14.2%	19.0%	43.0%	18.5%	2.4%
India should be a member of APEC	4.1%	14.3%	22.6%	40.0%	15.0%	4.1%
An expanded Trans-Pacific Partnership (TPP) is the best pathway to a Free Trade Area of the Asia-Pacific (FTAAP)	5.0%	15.7%	27.1%	30.1%	15.5%	6.6%
An expanded Regional Comprehensive Economic Partnership (RCEP) agreement is the best pathway to an FTAAP	2.8%	11.1%	34.0%	33.8%	8.3%	10.0%
All APEC members should be part of the FTAAP	1.3%	9.6%	23.8%	35.8%	22.3%	7.3%
An FTAAP should build on existing agreements including the TPP, RCEP and the Pacific Alliance (PA)	1.7%	4.3%	22.5%	40.9%	22.5%	8.2%
An eventual Free Trade Area of the Asia-Pacific should include members of all of the pathways (TPP, RCEP and PA)	1.3%	5.4%	21.7%	41.6%	23.6%	6.5%

8. What do you think is the likelihood of success in concluding the following proposed agreements over the next 3 years?
Use a scale of 1-5, select '1' if you think it is not at all likely if the negotiations will be completed within the next 3 years; '2' if not likely; '3' if neither unlikely nor likely; '4' if likely, '5' if very likely or 'don't know' if you are not sure.

	1 - Not at all likely	2	3	4	5 - Very likely	Don't know
ASEAN Economic Community (AEC)	4.8%	15.6%	28.1%	28.1%	15.0%	8.3%
Trans-Pacific Partnership (TPP)	4.4%	22.8%	32.0%	22.4%	12.2%	6.1%
China-Japan-Korea (CJK) FTA negotiation	11.3%	31.5%	28.3%	13.1%	5.2%	10.6%
Regional Comprehensive Economic Partnership (RCEP)	3.6%	20.7%	37.9%	22.2%	4.9%	10.7%
The Pacific Alliance (PA)	4.5%	20.3%	24.2%	14.6%	9.6%	26.8%
The Transatlantic Trade and Investment Partnership (TTIP)	3.2%	23.8%	28.7%	18.8%	5.4%	20.1%
WTO Doha Round	29.4%	33.0%	19.6%	7.6%	1.5%	8.9%

9. Please rate each of the following in terms of the need for them to be addressed in Asia-Pacific free trade agreements?

	1 - Lowest priority	2	3	4	5- Highest priority	Weighted Score
Transparency in regulations	0.2%	1.7%	11.3%	36.4%	49.6%	4.3
Investment access	0.4%	1.1%	15.6%	43.7%	38.4%	4.2
Services market access	0.9%	2.3%	17.0%	43.8%	34.9%	4.1
Manufacturing market access	0.6%	2.3%	19.5%	46.3%	29.1%	3.9
Agricultural market access	2.1%	6.2%	21.8%	35.2%	32.6%	3.8
Intellectual property	1.9%	6.4%	23.1%	38.0%	29.3%	3.8
Consistent product standards	0.6%	6.0%	24.5%	40.3%	26.0%	3.8
Environmental protection	2.1%	9.7%	20.8%	34.5%	30.9%	3.8
Simple rules of origin	0.6%	5.5%	23.8%	35.4%	29.1%	3.7
E-commerce	1.1%	7.3%	29.1%	35.8%	24.5%	3.7
Cooperation, capacity building	1.3%	8.4%	28.0%	35.6%	23.9%	3.6
Competition	0.9%	8.3%	28.5%	39.3%	20.1%	3.6
Sanitary and Phytosanitary Standards (SPS)	0.8%	6.9%	26.8%	34.9%	24.5%	3.6
Movement of persons	1.7%	12.7%	32.3%	30.2%	19.9%	3.4
Labor protection	3.6%	14.4%	33.0%	30.7%	16.1%	3.4
Government procurement	2.3%	12.1%	40.4%	29.4%	13.3%	3.3
State-owned enterprises	6.5%	21.3%	33.1%	24.5%	12.3%	3.1

10. What do you think should be the top 5 priorities for APEC Leaders to address at their upcoming meeting in Beijing?
Please select ONLY five (5) issues, using a scale of 1-5, please write 1 for the issue you think is most important, 2 for the next most important issue and so on.

	1 - Most important	2	3	4	5 - Least important	Weighted Score
Progress towards a Free Trade Area of the Asia-Pacific	16.6%	9.5%	7.3%	6.4%	6.2%	1.6
Innovative Development, Economic Reform and Growth	12.0%	9.3%	7.3%	6.5%	6.7%	1.4
The APEC growth strategy	10.8%	5.4%	3.7%	6.0%	3.7%	1.0
Reducing the income inequality in the region	5.0%	6.4%	6.5%	4.5%	5.0%	0.8
Attaining the Bogor Goals of free and open trade and investment	8.0%	5.0%	3.4%	3.9%	3.2%	0.8
Regulatory impediments to business	4.7%	4.5%	7.3%	6.5%	5.0%	0.8
A connectivity blueprint for the region	5.4%	6.0%	4.7%	4.1%	5.0%	0.8
Establishing reliable regional supply chains	2.8%	5.4%	5.2%	5.2%	4.9%	0.7
Corruption	4.3%	3.6%	3.7%	4.3%	4.5%	0.6
The reform of regional institutional architecture	3.9%	3.4%	3.6%	4.1%	4.1%	0.6
Financial sector regulatory reform	2.4%	3.6%	4.7%	4.5%	4.7%	0.5
The WTO Doha Round	4.1%	3.2%	3.2%	2.6%	2.6%	0.5
Food security	3.2%	3.4%	3.0%	3.9%	4.5%	0.5
Energy security	1.1%	3.6%	4.1%	4.7%	3.0%	0.4
The ending of quantitative easing and its impact on the region	2.8%	3.0%	3.6%	2.6%	1.9%	0.4
The impact of continued monetary easing and hot money flows on the regional economy	1.7%	2.6%	3.7%	4.5%	2.8%	0.4
Intellectual property rights	1.3%	2.6%	3.9%	3.4%	3.2%	0.4
Increasing the effectiveness of development assistance	1.7%	2.4%	3.0%	2.1%	4.5%	0.4
Expansion of APEC membership	1.3%	2.2%	1.7%	2.8%	4.5%	0.3
Labor mobility	0.9%	2.1%	2.2%	3.2%	3.6%	0.3
A plurilateral agreement on services	0.4%	2.6%	2.8%	2.4%	3.6%	0.3
Cyber-security	0.9%	2.2%	2.4%	2.8%	2.4%	0.3
Unemployment	1.5%	1.9%	2.1%	2.1%	2.2%	0.3
Terrorism	1.3%	1.7%	1.3%	2.4%	2.8%	0.2
Exchange rate adjustments	1.1%	1.7%	1.9%	1.5%	1.5%	0.2
Inflation	0.2%	1.9%	2.1%	1.3%	1.3%	0.2
Emergency preparedness	0.4%	0.9%	1.7%	1.7%	2.6%	0.2

MEMBER COMMITTEES

PECC Co-Chairs
Mr. Jusuf WANANDI and Ambassador Donald CAMPBELL

Contacts:
c/o Ms. Rosita RAMDANI
Secretary, INCPEC
Tel: +62 (21) 5365 4601
Fax: +62 (21) 5365 4607
Email: rosita@csis.or.id

c/o Ms. Eva BUSZA
Vice-President of Research, Asia Pacific Foundation of Canada
Email: eva.busza@asiapacific.ca

Ms. Trang NGUYEN
Email: trang.nguyen@asiapacific.ca

AUSTRALIA
Australian Pacific Economic Cooperation Committee (AUSPECC)

Chair:
Mr. Ian BUCHANAN
Senior Executive Adviser
PwC Strategy& (ANZSEA) Pty Ltd

Secretariat:
Mr. Sung LEE
Director, Publishing and Partnerships
Crawford School of Public Policy
The Australian National University

Address:
Australian Pacific Economic Cooperation Committee
Crawford School of Public Policy
The Australian National University
Canberra ACT 0200 Australia
Tel +61-2-6125 9568
Fax +61-2-6125 5448
Email: sung.lee@anu.edu.au

Committee Homepage:
http://auspecc.anu.edu.au

BRUNEI DARUSSALAM
Brunei Darussalam National Committee for Pacific Economic Cooperation (BDCPEC)

Chair:
Dato' LIM Jock Hoi
Permanent Secretary
Ministry of Foreign Affairs & Trade

Secretariat:
Ms. LEE Kok Ting
Second Secretary
Department of Economic Cooperation
Ministry of Foreign Affairs & Trade
Email: kokting.lee@mfa.gov.bn

Address:
Brunei Darussalam National Committee for Pacific Economic Cooperation
c/o Ministry of Foreign Affairs & Trade
Jalan Subok
Bandar Seri Begawan
BD 2710, Brunei Darussalam
Tel: +673 2383374
Email: bdcpecc@mfa.gov.bn

CANADA
Canadian National Committee for Pacific Economic Cooperation (CANCPEC)

Chair:
Ambassador Donald CAMPBELL
Distinguished Fellow
Asia Pacific Foundation of Canada
and Senior Strategy Advisor
Davis LLP

Secretariat:
Ms. Eva BUSZA
Vice-President of Research,
Asia Pacific Foundation of Canada
Email: eva.busza@asiapacific.ca

Ms. Trang NGUYEN
Email: trang.nguyen@asiapacific.ca

Address:
Canadian National Committee for Pacific Economic Cooperation
c/o Asia Pacific Foundation of Canada
Suite 220, 890 West Pender Street

Vancouver, B.C
Canada , V6C 1J9
Tel: +1 (604) 6845986
Fax: +1 (604) 6811370

Committee Homepage:
http://www.asiapacific.ca/about-us/affiliations/pecc

CHILE
Chilean National Committee for Pacific Economic Cooperation (CHILPEC)

Chair:
Dr. Manfred WILHELMY
Executive Director, Chile Pacific Foundation

Address:
Chilean National Committee for Pacific Economic Cooperation
c/o Chile Pacific Foundation
Av. Los Leones 382
Of. 701
Providencia, Santiago
Chile
Tel: +56 (2) 3343200
Fax: +56 (2) 3343201
Email: info@funpacifico.cl

Committee Homepage:
http://www.funpacifico.cl/english/index.html

CHINA
China National Committee for Pacific Economic Cooperation (CNCPEC)

Chair:
Amb. TANG Guoqiang

Secretariat:
Mr. AN Zhongli
Secretary General, CNCPEC

Address:
China National Committee for Pacific Economic Cooperation
c/o China Institute of International Studies
3 Toutiao Taijichang
Beijing, China 100005
Tel: +86 (10) 85119648
Fax: +86 (10) 85119647/65235135
Email: cncpec@pecc-china.org

COLOMBIA
Colombia National Committee for Pacific Economic Cooperation (COLPECC)

Chair:
Mrs. Maria Angela HOLGUIN
Minister of Foreign Affairs

Standing Committee Member:
Dr. Fidel DUQUE
Director General, COLPECC

Address:
Colombia National Committee for Pacific Economic Cooperation
Ministry of Foregin Affairs
c/o Asia, Africa & Oceania Bureau
Palacio de San Carlos
Calle 10 No 5-51
Bogota, Colombia
Tel: +57 (1) 381 4000 ext. 1509
Fax: +57 (1) 381 4077 ext. 1532
Email: aocolpecc@cancilleria.gov.co

ECUADOR
Ecuadorian Committee for the Pacific Economic Cooperation Council (ECUPEC)

Chair:
Mr. Mauricio DÁVALOS-GUEVARA
President, ECUPEC

Secretariat:
Amb. Paulina GARCÍA-DONOSO
Executive Director, ECUPEC

Address:
Ecuadorian Committee for the Pacific Economic Cooperation Council
c/o Ministry of Foreign Affairs,
Trade and Integration
10 de Agosto NS 21-255 y Jeronimo
Carrion Edificio Solis, 4to. Piso
Quito, Ecuador
Tel: +593 (2) 2500 654
Fax: +593 (2) 2508937
Email: ecupec@mmrree.gob.ec

HONG KONG, CHINA
Hong Kong Committee for Pacific Economic Cooperation (HKCPEC)

Chair:
Prof. Stephen CHEUNG
President and Chair Professor of Public Policy
Hong Kong Institute of Education

Secretariat:
Ms. Vega WONG
Secretary General, HKCPEC

Address:
Hong Kong Committee for Pacific Economic Cooperation
Trade and Industry Department
17/F, Trade and Industry Department Tower
700 Nathan Road
Kowloon, Hong Kong
Tel: +852 23985305
Fax: +852 27877799
Email: hkcpec@tid.gov.hk

Committee Homepage:
http://www.hkcpec.org

INDONESIA
Indonesian National Committee for Pacific Economic Cooperation (INCPEC)

Chair:
Dr. Djisman SIMANDJUNTAK
Chairman of the Executive Board of Prasetiya Mulya Foundation
Chairman of the Board of Directors of Center for Strategic and International
Studies Foundation, Jakarta

Secretariat:
Ms. Ira SETIATI
Email: ira.setiati@csis.or.id

Address:
Indonesian National Committee for
Pacific Economic Cooperation
c/o Centre for Strategic and
International Studies (CSIS)
Jl. Tanah Abang III No. 23-27,
2nd Floor
Jakarta 10160 Indonesia
Tel: +62 (21) 3865 532-5
Fax: +62 (21) 3847 517
Email: rosita@csis.or.id

Committee Homepage:
http://www.csis.or.id

JAPAN
Japan National Committee for Pacific Economic Cooperation (JANCPEC)

Chair:
Ambassador Yoshiji NOGAMI
President
Japan Institute of International Affairs (JIIA)

Secretariat:
Mr. Toshiro IIJIMA
Executive Director, JANCPEC

Address:
Japan National Committee for Pacific
Economic Cooperation
c/o Japan Institute of International Affairs
3rd Floor Toranomon Mitsui Building
3-8-1 Kasumigaseki, Chiyodaku
Tokyo 100-0013 Japan
Tel: +81 (3) 35037261
Fax: +81 (3) 35037292
Email: peccjp3503@jiia.or.jp

Committee Homepage:
www2.jiia.or.jp/en/pecc

KOREA
Korea National Committee for Pacific Economic Cooperation (KOPEC)

Chair:
Dr. Il Houng LEE
President
Korea Institute for International Economic Policy
(KIEP)

Secretariat:
Dr. Chul CHUNG
Vice Chair, KOPEC

Address:
Korea National Committee for
Pacific Economic Cooperation
c/o Korea Institute for International
Economic Policy (KIEP)
137-747, 246 Yangjaedaero, Seocho-gu
Seoul, Korea
Tel: +82 (2) 34601240
Fax: +82 (2) 34601244
Email: kopec@kiep.go.kr

MALAYSIA
Malaysia National Committee for Pacific Economic Cooperation (MANCPEC)

Chair:
Tan Sri RASTAM Mohd Isa
Chief Executive
ISIS Malaysia

Secretariat:
Mr. Steve WONG
Deputy Chief Executive
ISIS Malaysia
Email: steve@isis.org.my
cc: Ms. Norazzah
Email: azza@isis.org.my

Address:
Malaysia National Committee for
Pacific Economic Cooperation
c/o Institute of Strategic and
International Studies (ISIS)
No. 1 Pesiaran Sultan Salahuddin
PO Box 12424
50778 Kuala Lumpur, Malaysia
Tel: +60 (3) 26939366 / 26939439
Fax: +60 (3) 26939430 / 26938485

Committee Homepage:
http://www.isis.org.my

MEXICO
Mexico National Committee for Pacific Economic Cooperation (MXCPEC)

Chair:
Dr. Jose Antonio MEADE Kuribrena
Secretary of Foreign Affairs

Standing Committee Member:
Minister Alejandro MADRIGAL Becerra
Director General for Asia-Pacific
Mexican Secretariat of Foreign Affairs

Secretariat:
Ms. Monica OCHOA Palomera
Email: mochoap@sre.gob.mx

Address:
Mexico National Committee for Pacific Economic Cooperation
c/o Ministry of Foreign Affairs
Plaza Juárez No. 20, Floor 20
Col. Centro, Deleg. Cuauhtémoc, C.P. 06010
Mexico City, Mexico
Tel: +52 (55) 3686-5946/3686-5387
Fax: +52 (55) 3686-5947

MONGOLIA

Mongolian National Committee on Pacific Economic Cooperation (MONPECC)

Chair:
Mr. Khalzkhuu NARANKHUU
Member of the State Great Hural (Parliament) of Mongolia

Secretariat:
Mr. Jargalsaikhan DAMBADARJAA
Secretary General, MONPECC

Address:
Mongolian National Committee on Pacific Economic Cooperation
c/o Ministry of Foreign Affairs
Suite 307, DCS Building
Peace Avenue 7B
Ulaanbaatar-48, 14210 Mongolia
Tel/Fax: +976 (11) 262394
Email: djargal@yahoo.com

NEW ZEALAND

New Zealand Committee of the Pacific Economic Cooperation Council (NZPECC)

Chair:
Mr. Denis MCNAMARA
Consultant, Lowndes
Email: mcnamara@lowndeslaw.com

Secretariat:
Ms. Christine CONNON
Email: cconnon@chamber.co.nz

Ms. Liz BELL
Email: liz.bell@nzpecc.org.nz

Address:
New Zealand Committee of the Pacific Economic Cooperation Council
c/o Auckland Chamber of Commerce
Level 3, 100 Mayoral Drive
PO Box 47, Auckland, New Zealand
Tel: +64 (9) 302 9932
Fax: +64 (9) 309 0081

Committee Homepage:
http://nzpecc.org.nz

PERU

Peruvian National Committee for Pacific Economic Cooperation (PERUPEC)

Chair:
Ambassador Armando Raul PATINO Alvistur
Director of APEC and Specialized Fora
Ministry of Foreign Affairs

Secretariat:
Ms. Krizia Karen HERRERA Celi
Email: kherrera@rree.gob.pe

Address:
Peruvian National Committee for Pacific Economic Cooperation
4th Floor
Ministry of Foreign Affairs
Jr Lampa 545, 4th Floor
Lima 1, Peru
Tel: +511 204 3050
Fax: +511 204 3032

THE PHILIPPINES

Philippine Pacific Economic Cooperation Committee (PPECC)

Chair:
Ambassador Antonio I. BASILIO
President
Philippine Foundation for Global Concerns, Inc

Secretariat:
Ms. Evelyn Q. MANALOTO
Executive Director, PPECC

Address:
Philippine Pacific Economic Cooperation Committee
c/o Philippine Foundation for Global Concerns, Inc.
32/F Zuellig Building Makati Avenue
corner Paseo de Roxas
Makati City 1226, Philippines
Tel: +63 (2) 843 6536
Fax: +63 (2) 845 4832
Email: ppecc@pfgc.ph

SINGAPORE

Singapore National Committee for Pacific Economic Cooperation (SINCPEC)

Chair:
Dr. TAN Khee Giap
Associate Professor of Public Policy

National University of Singapore
Email: spptkg@nus.edu.sg

Secretariat:
Ms. YAP Xin Yi
Email: sppyxy@nus.edu.sg

Address:
Singapore National Committee for Pacific Economic Cooperation
c/o Lee Kuan Yew School of Public Policy
National University of Singapore
469A Bukit Timah Road
Level 2 Tower Block
Singapore 259770
Tel: +65 6516 5025
Fax: +65 6467 8714

Committee Homepage:
http://sincpec.sg

PACIFIC ISLANDS FORUM (PIF)

Chair:
Mr. Tuiloma Neroni SLADE
Secretary General
Pacific Islands Forum Secretariat

Address:
Private Mail Bag
Suva, Fiji
Tel: +679 3312600
Fax: +679 322 0230
Email: sg@forumsec.org.fj
Cc: info@forumsec.org.fj

CHINESE TAIPEI
Chinese Taipei Pacific Economic Cooperation Committee (CTPECC)

Chair:
Dr. David S. HONG
President
Taiwan Institute of Economic Research (TIER)
Email: d7319@tier.org.tw

Secretariat:
Dr. Darson CHIU
Director General, CTPECC
Email: d11224@tier.org.tw

Address:
Chinese Taipei Pacific Economic Cooperation Committee
c/o Taiwan Institute of Economic Research (TIER)
7F, 16-8, Dehuei Street
Taipei, Taiwan 10461
Tel: +886 (2) 25865000
Fax: +886 (2) 25956553 / 25946563

Committee Homepage:
http://www.ctpecc.org.tw

THAILAND
Thailand National Committee for Pacific Economic Cooperation (TNCPEC)

Chair:
Dr. Narongchai AKRASANEE
Minister of Energy

Secretariat:
Ms. Vimon KIDCHOB
Executive Director, TNCPEC

Address:
Ms. Vipada Tuchinda
The International Institute for Asia Pacific Studies (INSAPS)
Bangkok University
Rama 4 Rd, Klong Toey
Bangkok 10110 Thailand
Tel: +66 (2) 350 3599 ext 1845
Email: vipada.t@bu.ac.th

UNITED STATES
United States Asia Pacific Council (USAPC)

Chair:
Ambassador Stapleton ROY
Director, Kissinger Institute on China and the United States
Woodrow Wilson International Center for Scholars

Standing Committee Member:
Dr. Charles E. MORRISON
President
East West Center

Secretariat:
Dr. Mark BORTHWICK
Executive Director, USAPC
Email: borthwim@eastwestcenter.org

Address:
United States Asia Pacific Council
6th Floor
1819 L Street, N.W.
Washington, D.C. 20036 USA
Tel: +1 (202) 2933995
Fax: +1 (202) 2931402

Committee Homepage:
http://www.eastwestcenter.org/ewc-in-washington/us-asia-pacific-council

VIETNAM
Vietnam National Committee for Pacific Economic Cooperation (VNCPEC)

Chair:
Mr. Vu Tien LOC
Chairman
Vietnam Chamber of Commerce
and Industry (VCCI)

Secretariat:
Mr. Nguyen Van HAI
Deputy Director
International Relations Department
Ministry of Foreign Affairs

Address:
Vietnam National Committee for
Pacific Economic Cooperation
c/o Vietnam Chamber of Commerce
and Industry (VCCI)
9 Dao Duy Anh Street, Hanoi
Tel: +84 (4) 35742022 Ext. 241
Fax: +84 (4) 35742020/35742030
Email: hainv@vcci.com.vn

ASSOCIATE MEMBER

FRANCE (PACIFIC TERRITORIES)
France Pacific Territories National Committee for Pacific Economic Cooperation (FPTPEC)

Chair:
Mr. Michel ROCARD
Former Prime Minister, France

Secretariat:
Prof. Jean Luc LE BIDEAU
Vice-Chair, FPTPEC
Tel. +33 (6) 85082141
Email : lebideaujeanluc@aol.com

Ambassador Jacques LE BLANC
Secretary General, FPTPEC
Tel: +33 (1) 53692495
Fax: +33 (1) 53692276
Email: jacques.leblanc@outre-mer.gouv.fr

Ambassador Christian LECHERVY
Permanent Secretary for Pacific Affairs
Ministry of Foreign Affairs
Tel: +33 (1) 53692929
Fax: +33 (1) 53692276
Email: christian.lechervy@diplomatie.gouv.fr

Chair, Polynesia:
Mr. Eric POMMIER
Email: ecpommier@gmail.com

Chair, New Caledonia:
Mr. Dominique CHU VAN
Email: dchuvan@gmail.com

Address :
Comité France (Territoires du Pacifique)
pour le PECC
c/o Ministère de l'Outre Mer
Secrétariat Permanent pour le Pacifique
27, Rue Oudinot
75007 Paris, France
Tel: +33 (1) 53692495
Fax: +33 (1) 53692276

INSTITUTIONAL MEMBERS

PACIFIC TRADE AND DEVELOPMENT CONFERENCE (PAFTAD)

Chair:
Prof. Wendy DOBSON

Address:
Pacific Trade and Development Conference
International Secretariat
c/o East Asian Bureau of Economic Research
Crawford Building
Lennox Crossing
Building #132
The Australian National University
Canberra ACT 0200, Australia
Tel: +61 (2) 6125 0552
Fax: +61 (2) 6125 5570
Email: paftad.sec@anu.edu.au

Committee Homepage:
http://paftad.org

Pacific Basin Economic Council (PBEC)

Chair:
Mr. Wilfred WONG Ying Wai
Email: wilfredwong@hcg.com.hk

Address:
Pacific Basin Economic Council
Room 1809, Harbour Centre
25 Harbour Road, Wanchai Hong Kong
Tel: +852 2815 6550
Fax: +852 2545 0499
Email: info@pbec.org

Committee Homepage:
http://www.pbec.org

29 Heng Mui Keng Terrace
Singapore 119620
www.pecc.org