

Executive Summary of the Report of the Track Two Study Group on Comprehensive Economic Partnership in East Asia (CEPEA)

1. Economic Integration in East Asia

1. Over the past decades, trade and investment linkages in the region of ASEAN, Australia, China, India, Japan, Korea and New Zealand (hereinafter referred to as 'East Asia') have intensified, and the resulting business networks in turn have contributed to the remarkable economic growth of the region. Active intra-regional trade in the region, the ratio of which is higher than that of NAFTA, has been led by trading of intermediate goods, and the final products assembled from those intermediate goods are exported throughout the world. The formation of production networks has become an important engine for regional economic growth.
2. Along with *de facto* integration, *de jure* integration has evolved in East Asia. ASEAN countries are covered by the ASEAN Free Trade Area (AFTA). The non-ASEAN countries in East Asia have been concluding FTA/EPAs with both individual ASEAN members and other non-ASEAN countries. Further efforts taken by East Asian countries toward regional economic integration have resulted in the progress of 'ASEAN+1' FTA/EPAs, of which Leaders of East Asia encouraged expeditious conclusions at the third East Asia Summit (EAS) in November 2007. ASEAN has also adopted the ASEAN Economic Community (AEC) Blueprint, with the goal of turning ASEAN into a single market and production base, a highly competitive economic region, a region of equitable economic development, and a region fully integrated into the global economy.
3. However, there still exist wide social and economic gaps and barriers to business and trade in the region. Furthermore, East Asia needs to respond to structural changes in the global economy, particularly the new realities in the food, energy and financial markets and the associated slowdown and threat of a new wave of protectionism.

2. Objectives and Scope of CEPEA

4. Reflecting the current situation of economic integration in East Asia, in the Chairman's Statement of the second EAS in January 2007, the Leaders welcomed ASEAN's efforts towards further integration and community building, and reaffirmed their resolve to work closely together in narrowing development gaps in the region. The Leaders also reiterated their support for ASEAN's role as the driving force for economic integration in this region and agreed to launch a Track Two study on Comprehensive Economic Partnership in East Asia (CEPEA) among EAS participants to deepen integration.

5. Based on the above statement, we set the following objectives of CEPEA: it must contribute to deepening economic integration in the region, and at the same time it must help narrow development gaps in the region. Along with these two objectives, sustainable development, which will enable the region to enjoy the benefits of development in the years to come, should be the third objective.
6. CEPEA has three key features. Firstly, ASEAN should be the driving force of economic integration. Secondly, CEPEA should build on the *de facto* integration of the region that has so far been led by the business sector for the economic and social benefit of all the people of the region. Finally, open regionalism also should be taken into account, as development of the region under CEPEA should contribute to global liberalization, be beneficial to the region outside East Asia, and not hinder the development of the world economy.
7. To achieve the above objectives of CEPEA, we recognize the scope of CEPEA as: economic cooperation, facilitation of trade and investment, and liberalization of trade and investment. Lacking any of the three pillars would seriously impede achievement of the three objectives.

3. Economic Impact of CEPEA

8. The more comprehensive an FTA, the greater the benefits arising out of it. Simulation analysis of the economic impact of CEPEA confirms that East Asian countries will benefit from CEPEA. Assuming that measures on cooperation, facilitation and liberalization are implemented under CEPEA, the GDP increase of East Asian countries will be 2.11 percent, whereas the figure will be 1.30 percent in the case that only facilitation and liberalization are implemented under CEPEA. The gains of East Asian countries are largest in the case of CEPEA compared to other alternatives in the region.

4. Elements of CEPEA

4.1 Economic Cooperation

9. Economic cooperation is essential for narrowing development gaps among East Asian countries, and building a basis for further development in each country. Economic cooperation will also help solve regional issues, such as environmental problems, and thus lead to the sustainable development of the region. Moreover, economic cooperation will also enhance intra-regional production and trade, and thus contribute to economic integration.
10. The East Asian Leaders have emphasized the importance of ‘working closely together in narrowing development gaps in our region’ while endorsing the Track Two Study Group on CEPEA. One of the indicators to measure the progress of CEPEA would be its ability to reduce the development gaps in the region.
11. Cooperation measures have a broad range of scope, ranging from human resource

development and transfer of technology to improvement of infrastructure. Among the fields for economic cooperation, improvement of infrastructures is of great importance as it enhances the connectivity of countries and provides a basis for further integration. At the same time, cooperation on 'soft' infrastructure, such as human resource development, is also significant for the region.

4.2 Facilitation of Trade and Investment

12. Facilitation of trade and investment is another important aspect of CEPEA. A stable business environment governed by transparent, predictable, streamlined, and harmonized market rules is also necessary for economic development. Transparent and predictable market rules will be incentives for investors to promote their investments in East Asian countries including least developed ones. Streamlined market rules will reduce the costs of transactions. The costs of enterprises complying with a variety of rules in each country will be alleviated by harmonized market rules.
13. There are a wide range of provisions that can be considered as falling under facilitation. More specifically, there is scope for cooperation in:
 - improvement of customs performance,
 - overall improvement of logistics right along the supply chain,
 - investment protection,
 - government procurement,
 - harmonization of rules of origin (ROO),
 - the development of mutual recognition agreements, and
 - intellectual property rights.
14. The AEC Blueprint identifies facilitation of trade as key to the development of AEC. ASEAN's efforts in facilitation could provide the basis for considering facilitation programs under CEPEA. Moreover, the non-ASEAN countries in East Asia could play a useful role in capacity development, along with ASEAN countries. This approach of extending ASEAN's arrangements to a wider region including six countries would be entirely consistent with the view of EAS Leaders that ASEAN should be at the center of efforts to create CEPEA.

4.3 Liberalization of Trade and Investment

15. East Asian countries' trade and economic relations both within and outside the region have been deepening. These closer relationships have been fostered to a large degree by the open and liberal attitudes of governments in East Asia and the trade and investment liberalization they have undertaken over the past two decades. The growing importance of the trade and economic relationships has in turn stimulated new efforts toward greater liberalization, both within existing arrangements, such as ASEAN, and through new trade and investment liberalizing agreements in the region.
16. The integration of East Asia is based on the progress of regional production networks. Strengthening the competitiveness of economies through a broad range of liberalization of trade in goods and services, investment and other areas will bring further economic

development and integration to the region. With the elimination of barriers in these fields, it would be possible for business to formulate genuinely efficient industrial networks expanding across the region.

17. Balance should be kept between ambition and the possibility of actual implementation of commitments for liberalization. It is also important to incorporate special and differential treatment (S&D) to enable the less developed countries to participate in the regional economic integration according to their capacities.
18. A regional liberalizing arrangement through CEPEA is clearly feasible and undoubtedly would produce positive economic benefits considerably greater than a collection of individual agreements and the ASEAN+1 model.

4.4 Environment and Energy

19. CEPEA can also be an appropriate framework to solve issues which require a combination of measures on cooperation, facilitation and liberalization. Among these types of issues are the environment, energy, and information and communication technology (ICT).
20. Issues such as global warming, the increasing energy demand, and various water-related problems, have been increasing in East Asia. These issues threaten not only the potential for economic growth, but finally the sustainability of economic development, especially in the developing economies.
21. Full use of advanced and appropriate technology is necessary to increase energy efficiency. Considering that most of the countries in East Asia are developing economies, mobilization of financial support and cooperation in capacity building are important.
22. CEPEA can serve as a valuable framework in designing and implementing environment and energy cooperation in East Asia. Actions under CEPEA may take the dual approach of individual and collective action plans.

4.5 Information and Communication Technology

23. East Asian countries also need to pay close attention to ICT issues in attaining the objectives of CEPEA. These issues can be solved through combining the measures under all three pillars of cooperation, facilitation and liberalization.
24. ICT, with its effect of enhancing business linkages and collaborations, can be effective in facilitating and expanding trade and investment cross-flows among East Asian countries. However, the state of ICT readiness varies among East Asian countries. Adequate attention and support should be given to collaboration and cooperation programs, addressing areas such as:
 - capacity building through infrastructure development and human resource development,
 - harmonization of policies, laws and mutual recognition in e-commerce,
 - trade facilitation (e.g., establishment of the East Asia Single Window on the ASEAN

- Single Window initiative), and
- e-logistics.

25. In East Asia, many regional initiatives on ICT have taken and will take place, and e-commerce provisions are starting to be introduced into FTA/EPAs. The main challenge is not what to do with ICT, but how to integrate multiple and diverse initiatives into a coherent and effective whole. Redundancy in the actions already taken or to be taken in fora such as ASEAN and APEC should be avoided.

5. Structure and Roadmap for CEPEA

5.1 Structure of CEPEA

5.1.1 Basic Framework

26. CEPEA is an integrated framework composed of measures for the three pillars, namely, cooperation, facilitation and liberalization. All three pillars complementarily serve to achieve CEPEA's objectives of deepening economic integration, narrowing development gaps, and realizing sustainable development. None of cooperation, facilitation nor liberalization can be left out in pursuing the three objectives. However, this does not mean that each measure must proceed simultaneously. There should be flexibility in the speed and timing of implementation in consideration of the development status of the countries.

5.1.2 Role of ASEAN

27. The role of ASEAN should be stressed in the formation of CEPEA. ASEAN has played a key role as the driving force of economic integration in East Asia for years, and is expected to take up a more important position in realizing further integration. Enhancement of ASEAN's successful integration is an essential step towards any possible advance of East Asia's integration. From this viewpoint, the function of the ASEAN Secretariat should be stressed and enhanced. The active role of the ASEAN Secretariat is essential in forming a consensus among ASEAN member countries regarding the direction of economic integration in East Asia.

5.1.3 Role of Private Sector

28. The role of the private sector is also important in formulating and implementing measures under CEPEA. The business sector, whose views are recommended to be incorporated in the work process of the Track Two Study at the third EAS, will be both the primary beneficiary of many of CEPEA's measures and the major player in their implementation. The business leaders the Study Group has met stressed that their activities extend across borders and continue to expand widely in the region. They also reiterated that further integration could be realized by eliminating a series of obstacles to cross-border business activities. Listening to and incorporating the voice of the private sector in the forthcoming processes will make

CEPEA truly valuable for the private sector, and such business activities will contribute to attaining CEPEA's objectives.

5.1.4 Open Regionalism

29. As mentioned previously, CEPEA should be built upon the principle of open regionalism. East Asia's development under CEPEA should contribute to global liberalization, be also beneficial outside the region, and not hinder the development of the world economy. In this regard, East Asian countries should remain committed to the multilateral trading system and keep an open attitude toward other regional fora such as APEC.

5.2 Roadmap for CEPEA

30. The roadmaps for the three pillars should consist of the concrete goals under the three pillars, assessment of the present situation, benchmarks to evaluate progress, mechanisms for implementation, and a concrete timeframe.

5.2.1 Roadmap for Economic Cooperation

31. The scope for economic cooperation is enormously wide and its goals are sometimes difficult to define. Each country should enhance and accelerate the existing cooperation programs in the region. Moreover, member countries should immediately start cooperation measures which they are prepared to implement. In considering appropriate measures, it is necessary to review the existing measures, examine their effects, and identify what additional value CEPEA can bring to the region.
32. Furthermore, cooperation initiatives and programs have to be designed in a way that enhances the benefits of facilitation and liberalization initiatives. Cooperation measures such as capacity building should be addressed appropriately under CEPEA to enhance capacity for facilitation and liberalization measures. They can also help to narrow the development gaps and build capacities and capabilities for implementation of liberalization measures through an FTA under CEPEA.

(1) Setting Work Plans for Collective and Individual Actions

33. Action-oriented economic cooperation agenda should be adopted with work plans for collective and individual actions. Under the work plans for individual actions, each country should identify and declare the country's roles in the achievement of the collective actions. The work plans will help to clarify the objectives and functions of each cooperation initiative in the overall objectives of CEPEA, and to avoid any unnecessary overlap with other initiatives.

(2) Establishing Frameworks for Dialogue

34. There are several ministerial- and senior official-level dialogue frameworks in East Asia which have contributed to economic cooperation through information exchange and policy coordination. A dialogue framework will play an essential role in agreeing on and implementing collective action plans, and in avoiding duplication and maximizing the synergy

of cooperation programs in the region. Enhancing dialogue frameworks under EAS is essential in accelerating economic cooperation under CEPEA. The establishment of the EAS Energy Ministers' Meeting and the EAS Environment Ministers' Meeting provides good examples.

(3) Utilizing Existing Institutions Related to Regional Integration

35. Existing institutions that act to promote regional economic cooperation as part of their activities, such as the ASEAN Secretariat, ERIA, ADB and the World Bank, could play key roles in identifying current bottlenecks, possible solutions and desirable goals, all of which are prior conditions of implementing cooperation measures. These institutions also could help at the review and evaluation stage after the cooperation programs have been implemented.

(4) Creating New Institutions Related to Regional Integration

36. Creating a new institution is also an option, although we must be aware that an 'institution first' approach might not be suitable in East Asia, a region led by *de facto* integration. Unnecessary overlaps with existing institutions should be avoided. Suggestions were made in the course of our study that, in the long run, an OECD-type organization may be helpful in activities such as policy coordination and sharing of policy experiences. It was also noted that ERIA, as an independent research institution, may help to foster such development. Another option would be the establishment of a 'cooperation office' under the ASEAN Secretariat. Other options include structural funds for bringing about regional development and a regional financial mechanism to assist the region in intermediating between rising foreign exchange reserves and growing infrastructure deficits.

5.2.2 Roadmap for Facilitation of Trade and Investment

37. The roadmap for facilitation of trade and investment will share many characteristics with those of economic cooperation. Work plans will be necessary as the basis for facilitation. Other necessary processes include information exchange and policy coordination based on a dialogue framework, and contributions from regional institutions. There are various facilitation measures already existing in the region, such as the AEC Blueprint and initiatives in APEC. Overlap among initiatives should be avoided, and the fruits of the other existing initiatives should be incorporated into measures under CEPEA as necessary. As part of early harvest, facilitation may start in certain areas, regardless of the progress in the FTA component of CEPEA.

5.2.3 Roadmap for Liberalization of Trade and Investment

38. Elimination and reduction of tariffs and non-tariff barriers, elimination and relaxation of regulations in services, and ensuring national treatment and most-favored-nation treatment in investment are examples of specific targets for liberalization.

(1) Voluntary Liberalization

39. Voluntary lowering of barriers and regulatory reform should be encouraged. Although voluntary liberalization is an individual measure, information exchange and monitoring could be an effective way to promote such voluntary efforts.

(2) Negotiating an FTA under CEPEA

40. Some of the measures on liberalization can be implemented only through an FTA/EPA and investment treaties. There are concerns that a flood of FTAs in the region leads to the so-called ‘spaghetti bowl’ phenomenon and creates a complicated trade environment for business. Analysis of the economic impact indicates that a region-wide FTA, under which the cumulative ROO becomes available, brings larger benefit than an FTA with a smaller grouping. One question that arises is the relationship between an FTA under CEPEA and existing FTAs in the region. Presumably, if the level of liberalization through a CEPEA-wide FTA is higher than that of existing FTAs in the region, the ‘spaghetti bowl’ phenomenon might be practically dissolved. An FTA under CEPEA will also make bilateral FTAs less relevant. Needless to say, an FTA under CEPEA must be fully consistent with WTO rules.
41. The timing for initiating FTA negotiations needs special attention, as there are several other initiatives such as ASEAN+1 FTAs, EAFTA and a Free Trade Area of the Asia Pacific (FTAAP). In this regard, the progress of ASEAN+1 FTAs and *de facto* economic integration, have to be taken into account. Five ASEAN+1 FTAs covering East Asia are just being implemented, concluded or negotiated in the region, and considerable progress on *de facto* integration has been achieved in East Asia. Once the five ASEAN+1 FTAs are concluded, one possible option for relevant governments will be to consider consolidating the five FTAs. For example, a track one study could start or the track two study could be continued focusing on more detailed issues.

5.2.4 Issues to be Tackled by Combining the Three Pillars

42. Regional issues such as environment, energy, and ICT can be resolved by combining the measures on cooperation, facilitation and liberalization mentioned above. Therefore, the steps toward solving these regional issues will be a mixture of the approaches analyzed previously. In working on the various regional issues, it would be necessary to conduct deeper analysis on the actual measures to be included in the package of cooperation, facilitation and liberalization.
43. There are fields such as energy and environment for which regional frameworks have been established and actions have begun. Measures should be taken immediately in these fields, using fora such as the EAS Energy Ministers’ Meeting and the EAS Environment Ministers’ Meeting as necessary.

5.2.5 Integrated Roadmap for CEPEA

44. Roadmaps for each of the three pillars of cooperation, facilitation and liberalization are not independent of each other. CEPEA’s objectives of economic integration, narrowing development gaps and sustainable development will surely be achieved if the three roadmaps are implemented coherently to maximize the synergy among the three pillars. In other words, the three roadmaps will form one integrated roadmap for CEPEA.
45. For instance, an increase in foreign direct investment through liberalization of investment will help bridge technology gaps among the countries, as foreign-affiliated companies will

promote the transfer of technology to the less developed countries. Trade will be facilitated by cooperation, such as capacity building for customs authorities. If 'hard' and 'soft' economic infrastructures are improved through cooperation in logistics, more companies acting in the region, including SMEs, will enjoy the fruits of trade liberalization.

FINAL VERSION

5.3 Recommendations

46. The Track Two Study Group on CEPEA recommends to the Leaders of East Asia Summit through their economic ministers that:

- (a) **The objectives of CEPEA be affirmed to be deepening economic integration, narrowing development gaps and achieving sustainable development, and the structure of CEPEA be affirmed to be composed of the three pillars of economic cooperation, facilitation of trade and investment, and liberalization of trade and investment;**
- (b) **Discussions be commenced among East Asian governments on cooperation and facilitation measures under CEPEA.** This Study Group believes that it is best to commence discussions on work plans for collective actions in areas such as environment, energy, logistics, and facilitation issues covered by the AEC Blueprint. Institutions such as the ASEAN Secretariat, ERIA and ADB should assume an important role in this process;
- (c) **Necessary decisions be made regarding an FTA under CEPEA: whether to commence a governmental process immediately, provide a clear timeline for future negotiations, or continue a further detailed study as a track two process;**

If the decision is to continue further the track two study, possible agenda items include:

- Detailed study of recently concluded FTAs in the region focusing on the progress of ASEAN+1 FTAs, and areas such as establishing an effective S&D rule.
 - Appropriate measures of facilitation and liberalization that can contribute the most to narrowing the development gaps.
 - Identifying cooperation initiatives and programs that can help to narrow the development gaps and build capacities and capabilities for implementation of liberalization measures through an FTA under CEPEA.
- (d) **A mechanism be developed for enhancing the opportunity for regional business leaders to contribute to the CEPEA realization process.**