

THE POSSIBILITY OF REGIONAL ECONOMIC INTEGRATION IN SOUTHEAST ASIA

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I

The long-heralded state of Malaysia was inaugurated on September 16, 1963, with the proclamation by Prime Minister Tengku Abdul Rahman of the Federation of Malaya. The inauguration of Malaysia was aimed at organizing a sub-regional economic confederation in an area embracing the Federation of Malaya, Singapore, North Borneo, and Sarawak. It has long been argued that Malaysia would face many complex problems—political, social, and especially racial. If the new merged state develops steadily and achieves its envisaged economic objectives, then the new experiment could lead to the creation of a stable but small economic sphere, with as its centre the Malayan peninsula. In a series of negotiations conducted in Tokyo and Manila from June to July 1963 between the Federation of Malaya, the Philippines and Indonesia, the concept of "Maphilindo"¹ was made public.

This development gave rise to hopes that co-operative relations might develop among the three countries with Malaysia as its centre.

In connection with the problem of regional economic integration in Southeast Asia, it may be recalled that the idea of establishing an Organization for Asian Economic Co-operation (OAEC) was discussed by Asian countries prior to the 18th General Conference of the Economic Commission for Asia and the Far East (ECAFE) held in Tokyo in March 1962. This idea, which envisaged the establishment of a loose organization embracing all Asian countries affiliated with the ECAFE, was shelved at the Tokyo congress on the ground that the project was premature. It clearly proved the difficulty of establishing a joint organization embracing all countries in the region.

But the concept of the OAEC is not completely forgotten. An

¹ On August 5, 1963, the concept of Maphilindo was proclaimed in the Manila Declaration signed by the heads of the three nations concerned. Instead of a tightly binding organization for co-operation, it envisaged a conciliation organ based on the principle of *musjawarah* (mutual consultation).

increasing number of countries will come to realize the need of having such an organization. The possibility that such an organization may be formed at some future date should not be ruled out.

From a more realistic and short-range standpoint, however, there seems to be more hope for the formation of a sub-regional organization among a relatively small number of neighbouring countries with common interests. The formation of Malaysia, therefore, can be considered a pioneering experiment in organizing a group according to this pattern. If the birth of Malaysia had led to the inauguration of "Maphilindo," it would have raised hopes for the emergence of a stabilizing influence in the heart of Southeast Asia which would eventually form the nucleus of an O.A.E.C. But Indonesia raised strong objections to the proclamation of Malaysia, while the Philippines reserved her attitude. Diplomatic and economic relations between these countries and newly-born Malaysia were disrupted and the idea of Maphilindo crumbled overnight. In the wake of this development, new factors of unrest presented themselves in this region.

Why is it then that co-operation and solidarity fail to develop among Southeast Asian countries? One of the fundamental reasons is the fact that in these countries, which attained independent nationhood only a decade or so ago, rash nationalism and sometimes radical chauvinism are prone to develop into narrow-minded national egoism. This trend manifests itself either in a violent opposition to any interference, direct or indirect, by advanced nations as in the case of Indonesian President Sukarno's charge of "neo-colonialism" against Malaysia or in the lack of mutual trust among neighbouring countries.

The problem, however, is not such that it can be fully explained by emotional factors alone.

II

With these recent developments in mind, let us first consider the fundamental factors that are hampering the formation of a far-flung common organization in Southeast Asia.

In a previous study¹ the following conclusion was reached: in this area, natural (geographical), political, and economic conditions are not sufficiently ripe for such a goal.

1. *Natural or Geographical Conditions*—So-called economic integration at the present stage of world history is characterized by the reten-

¹ Noboru Yamamoto, "Problems of Regional Economic Co-operation and 'Common Market' in Asia," *Asian Affairs*, Vol. II, No. 3, Sept., 1957, pp. 233-244.

tion of regionalism. Economic integration as it is understood today means primarily the strengthening, among geographically adjacent countries, of mutual co-operative relations for the sake of promoting common economic interests. It follows that the closer the nations are geographically, the stronger is their mutual cohesion. Good examples are found in the European Economic Community, the Council of Mutual Economic Aid (COMECON), and the Central American Common Market. Judging from the formula used and the extent of cohesion, these regional groups can be called "common markets."

In contrast to these groups, member nations of the European Free Trade Association (EFTA) and the Latin American Free Trade Association (LAFTA), both of which take the form of "free trade areas," are less adjacent geographically and, accordingly, the extent of their cohesion is weaker.¹

Supposing that the Southeast Asian region consists of an area stretching from Afghanistan in the West to Japan and the Republic of Korea in the East, it is no exaggeration to say that it is well-nigh impossible to have a strongly knit common organization embracing such a vast region. Moreover, this area comprises not only landlocked and oceanic countries but a number of island nations. Furthermore, these countries lack at present sufficient facilities for mutual transportation and communications. Leaving aside possible developments in the distant future, it is not possible for the moment to envision an organization covering the whole area because of the prevailing natural and geographical conditions.

2. *Political Conditions*—The fact that many of the newly risen countries in Southeast Asia have been beset ever since their founding by political unrest, both domestic and external, raises a certain pessimism with regard to planning a common organization.

Until their independence, these nations found a common objective in national freedom; but once independence was attained, the domestic political front crumbled in many cases due to internal strifes over the administrative policies of the new regimes. Domestic conflicts entailed ideological confrontations and desintegration of political parties, causing civil war and disputes just at the initial stage of newly-won statehood when domestic political unity and stability were of primary necessity. Political leaders who grasped the reins of power were often preoccupied

¹ The differentiation of formulas and stages of economic integration discussed here is based on Bela Balassa, *The Theory of Economic Integration*, Homewood, Illinois, R.D. Irwin, 1961, p. 2.

with expanding their egotistic influences or indulged in corruption, deepening the public's distrust of their leadership. Such a state of affairs often triggered *coups d'état* by young military officers, further delaying domestic political stability.

The already bad situation was aggravated by struggles and conflicts of interests among international influences. Because many of the countries in this area used to be colonies or semi-colonies the ex-colonial powers still maintain persistent political and economic interests even after the independence of their former colonial possessions. In particular, the postwar conflict between the so-called East and West has exerted serious effects. It divided Southeast Asia, while a neutralist force emerged, making the international political environment all the more complicated.

The East-West race for aid to developing nations, while helping the recipient countries' economic development, has also abetted political and military conflicts. The *coup d'état* in South Viet-Nam in November 1963 is a typical example. Such external subversive political factors combined with domestic causes of friction have either aggravated or prolonged the political instability in this region.

So long as these external and internal political factors remain, it is only natural that there exists no positive enthusiasm to promote co-operative relations and much less than a willingness for economic integration.

3. *Economic Conditions*—Subjected to colonial rule for many years, Southeast Asian countries still retain colonial backwardness in their economic conditions. They have long been assigned the role of agricultural producers—the tail-end of the vertical scheme of international division of labour—in their relationship with their colonial master countries or the industrially advanced nations. As a result, the economies are monocultural, producing only a small number of primary products—in many cases only two or three kinds of special goods. Thus, economic modernization based on industrialization was suppressed on the whole.

It is natural, therefore, that these countries should aim at economic independence after gaining political freedom. In many cases, however, they have tended to become overzealous in achieving economic independence, with each country undertaking its own economic development projects without due consideration to the need of establishing effective complementary relations with neighbouring nations.

During the initial stage of their independence, these countries,

carried away by surging nationalistic sentiments, turned their back to almost all foreign aid. This attitude is understandable as a natural reaction to the economic exploitation they suffered in the past at the hands of the colonial powers and other industrialized nations. It soon dawned on them, however, that this attitude amounted to reckless adventurism where the basic prerequisites of economic development—capital, technical know-how and construction materials are lacking: They also realized that population, hitherto considered the only abundant resource in their possession, was becoming a drawback because of the postwar rapid decline of the death-rate and sharp increase in the birth-rate. Abundant manpower *per se* does not necessarily constitute a useful labour force necessary for economic modernization; it takes a considerable period of time and technological training to convert manpower into a useful labour force.

During the period that followed the initial post-independence stage, it seems that these points came to be understood gradually. These nations began to open the doors to capital and technical aid from foreign countries, and tried to promote co-operative relations among themselves. Without exception, Southeast Asian countries have demonstrated enthusiasm for technical training and diffusion of compulsory education. The trend would seem to vindicate the theory that in all developing countries, social development must be pushed along with, or even ahead of, economic development. If these preconditions develop, although slowly, the economic development of Southeast Asian countries ought to progress gradually and preparations could be made for mutual co-operation in carrying out development programmes more effectively.

On the other hand, it cannot be denied that the colonial frame of mind which has seeped deeply into the national character will not be rectified overnight. This tendency has given rise to a mad scramble for foreign aid or, sometimes, to jealousy over the faster pace of development in neighbouring countries.

Mention should be made of a more fundamental underlying problem, the difference of social and cultural conditions among the countries under review, but the conditions described above show sufficiently the difficulty of establishing a common organization embracing the region.

III

What, then, is the possibility for sub-regional cohesion instead of over-all integration?

In the former case, obstacles resulting from natural, geographical

conditions may be dismissed, but political and economic difficulties persist. Accordingly, mutual concessions must be sought by minimizing as much as possible the effects of these disparities.

As an example of such sub-regional cohesion, one can cite, besides Malaysia, the Southeast Asia Treaty Organization (SEATO)¹ and the Association of South Asia (ASA). These two organizations are manifestly political and partially military forms of cohesion. SEATO in particular lives up to expectation, and has thus bred a new conflicting relationship with the so-called neutralist bloc.

ASA's declared aim calls for friendly consultation, co-operation and mutual assistance among its three original members—Thailand, the Federation of Malaya, and the Philippines—in the economic, social, cultural, scientific, and administrative fields. The very extensiveness of its aim, however, tends to obscure the real, practical objective which the organization seeks to attain. Moreover, one cannot deny the fact that, in the background of ASA's establishment, lie political purposes such as strengthening the anti-Communist front and the construction of anti-Communist bases.

In comparison with these two organizations, newly-born Malaysia is more expressly aimed at strengthening economic cohesion and, accordingly, promises a better chance of success in the future. However, here too, political and military motives cannot be overlooked when account is taken of the strong British support and assistance given in the process of Malaysia's formation. In this regard, Singapore's military value cannot be underestimated. Be that as it may, the formation of Malaysia has paved the way for a sub-regional economic integration based on a compromise between the community of Malaya and that of Chinese settlers in general, and on the tie-up between Malaya's natural resources and the capital of Chinese settlers in Singapore. Mention should be made of the fact that a common currency is already in circulation in Malaya, Singapore, and the three small states in North Borneo (although Brunei is still withholding membership in this group).

These facts, however, do not necessarily guarantee the successful development of Malaysia in the years ahead. For one thing, the Mahilindo idea has collapsed, and for another, President Sukarno still refuses to recognize the new federation. Indonesia's opposition may very well prove to be the fuse for a new dispute in this area. If

¹ SEATO members include, besides the three Asian countries of Pakistan, the Philippines, and Thailand, such "outsiders" as Australia, New Zealand, the United States, Britain, and France. This membership reflects the organization's real objectives.

Malaysia develops smoothly, it could induce similar experiments in other areas of Southeast Asia. For example, if Britain would give strong backing, India, Pakistan, Burma, and Ceylon may possibly come to form a group in the future. If the Indo-Pakistani strife persists, a co-operative relationship might be established among the other countries without Pakistan.

At any rate, economic integration even on a sub-regional scale seems only a remote possibility in Southeast Asia, when we think of its prevailing unsettled situation as exemplified by the open strife between Communist and Nationalist China, continuing border dispute between Communist China and India, the aggravating disturbances in Laos and Viet-Nam, as well as the East-West confrontation looming over all these areas.

Under such circumstances, attention is naturally drawn to the idea of establishing an Organization for Asian Economic Co-operation as an agency to facilitate mutual consultation among Southeast Asian countries in order to adjust their economic development projects. The envisaged organ would be a loose affiliation—something like an adjunct to the ECAFE—and serve as a forum where Southeast Asian countries may discuss problems of common concern while maintaining their respective independent positions.

IV

The possibilities of regional economic integration in Southeast Asia must, however, be studied.

Generally speaking, the following four points are essential to the materialization of a satisfactory regional integration:

- (1) Interrelationship with political integration,
- (2) Realization of the "economies of scale,"
- (3) Agreed specialization,
- (4) Free interchange of capital and labour.

These conditions apply both to industrially advanced nations and developing countries. But one must remember that in developing countries, materialization of these four conditions is more difficult, because the problem should be considered from the viewpoint of political economy rather than that of pure economics.

(1) If a perfect economic integration is to be attained, it is necessary for member nations to entrust a part of their political and economic sovereignty to a supra-national central organ. In other words, integration becomes complete if and when economic integration is accompanied

by, or merged with political integration. Under the powerful control of a central supreme organ, member nations are to maintain partially restricted political and economic independence.

(2) Such a regional economic integration must guarantee "economies of scale," that is, the benefit of large-scale production, stable and expansive markets, increased employment, and higher productivity. It is not necessary, therefore, to integrate a large number of countries spreading over a wide area. The best possible form of integration is a union agreed upon by countries meeting these requirements within a scope that promises the materialization of the expected benefits.

(3) The countries thus integrated must pursue productive activities in accordance with an agreed specialization programme as decided by the central supreme organ. Under the regional economic integration setup, economic barriers are removed as a matter of principle and, therefore, it is desirable that member nations agree on their respective share of industrial activities as if they were having part in the industrial programme of one single country.

(4) In order to make the regional economic integration more dynamic, not only the free movement of goods among member nations but also a free flow of capital and labour are desirable. In this sense, a "common market" designed to promote such a free interchange is more desirable than a "free trade area" aimed at increasing the volume of trade within the area.

Even among industrially advanced countries, it is not easy to find the aforementioned four conditions. For example, the European Economic Community has developed beyond expectations precisely because it has so far placed emphasis on its function as a customs union. The EEC is likely to encounter many difficulties in the future when it proceeds towards the goals of a "common market" with intra-regional free movement of productive factors, and then to an "economic union" aimed at adjusting common economic and social policies. It will take a long time and much effort before this organization reaches the stage of complete economic integration, namely, proceeds one step towards political integration.

In the case of developing countries, the four preconditions might be harder to achieve. As regards political integration, the emerging nations which attained political independence only recently will need a long time for deliberations and consultations before being persuaded to accept the status of limited independence under the control of a supra-national central organ. With regard to the "economies of scale" too,

the goal will be reached only after these countries have more fully become aware of the weaknesses affecting their respective economic development programmes and realized the need for mutual co-operation. The same can be said of the aim of "agreed specialization." In this respect, the matter must be considered with more emphasis on the industries and enterprises to be fostered in the future than on those already in existence. Since the problem must be studied with due consideration for the respective countries' economic development programmes or, in other words, as a comprehensive economic development plan embracing the whole area, considerable difficulty is expected in the adjustment of their individual programmes. The free interchange of capital and labour is not an exclusively intra-regional problem but presupposes the invitation of capital, specialists, and skilled labourers from outside the region. Accordingly, much judicious consideration must be given to the problem of inducing and accepting such outside help.

With the above as background knowledge, let us now consider to what extent the above conditions can be met in Southeast Asia, and thus determine the possibility of economic integration in this region.

V

(1) As discussed above, it is quite improbable that a political integration will materialize in the vast region of Southeast Asia. If at all possible, such a union would be limited to a political alignment among several neighbouring countries in a limited area. It may thus be possible for several political integrations to materialize.

Even a limited political union will not be easy to attain because neighbouring countries also differ in their political systems and the degree of political development. As pointed out earlier, international relations among neighbouring countries in Asia have not necessarily been cordial due to political uncertainties, both domestic and external, and because of the apparently excessive nationalism prevailing in many countries. Except for some large countries, these facts have acted to delay the progress of economic development—especially in small countries.

It is both desirable and necessary for small countries to seek political and economic independence as members of a regional group in view of past failures and the world-wide trend towards regional economic integration. In particular, Japan, a primary industrial nation in this region, must take this course if she is to insure her future development.

It should be emphasized that, although it remains possible for economic co-operation among several countries to progress towards economic integration and then to a political union, in the case of developing countries, a bold step towards political integration may lead to economic integration.

(2) The problem of "economies of scale" also deserves judicious consideration by small Southeast Asian countries which are still in the developing stage. It is evident that, if these small nations aim only at their own domestic markets in planning industrial construction, they will immediately face serious difficulties. It is also conceivable that if several neighbouring countries make the same efforts, the result would be unnecessary competition and disadvantages for all. If these countries work in harmonious co-operation and plan economic development on an appropriate scale, they will be able to profit a great deal both in marketing and industrial efficiency.

(3) The problem just mentioned naturally leads to the question of agreed specialization. It is desirable that, in working out economic development programmes, several neighbouring countries adjust and co-ordinate their plans on the basis of full mutual consultation and understanding, and specialize in those industrial endeavours most suitable to their respective topographical conditions. This process calls for mutual consent and agreement. The ideal formula would be to go about this task under the control of a supra-national supreme organ. In this connection, we should recall Prof. Myrdal's argument:

"It should be clear that the underdeveloped countries would need much more than do the developed regions, neighbourhood co-operation, agreed specialization in their industrialization and, indeed, 'free trade areas' for themselves behind common protective walls in order to have real success with their development programmes."¹

In connection with the points (2) and (3), the view expressed in the *Economic Survey of Asia and the Far East, 1959*, deserves close attention :

"Quite apart from the co-existence of under-utilized capacity within the region and imports from outside of products identical or similar to those produced in the region, there is likely to be considerable scope for co-operation in import substitution between the countries of the region. It would be interesting to make a systematic investigation of the type of commodities which at present are being imported, and the

¹ G. Myrdal, "Problems of Economic Integration," *Commerce*, Vol. XCIV, No. 2400, Bombay, 9th March, 1957, p. 486.

extent to which these could be replaced by production in the region within the cost differentials (between regionally produced and imported goods) which may be permitted if account is taken of the real cost of foreign exchange. It is certain that these differences in cost would be kept within narrower bounds, especially for the smaller countries, if some specialization could be agreed upon within the region, enabling it to benefit as much as possible from the economies of scale in manufacturing and from the differences in national endowment for primary production."¹

(4) In regard to free exchange of capital and labour in the Southeast Asian region, establishment of a joint development fund or the free movement of technicians and workers within the region could be expected to a certain extent. The primary concern of developing countries is, however, the induction of external aid. Most countries welcome foreign technical aid but, as referred to earlier, show a very cautious attitude towards the induction of foreign capital during the initial stage of development. In many cases, it has proved impossible for countries lacking domestic capital to carry out effective economic development without the supply of foreign capital. As a result, policies have been changed recently by the enactment of various laws governing foreign capital. In this connection, the foreign aid race between East and West places Southeast Asian countries in an advantageous position. These countries, for many years under colonial rule, should take full advantage of the privileged position which has become theirs for the first time. But they may not be contented with this new status.

Advanced countries outside the Southeast Asian region are expanding assistance to developing nations through the agency of international joint aid schemes such as the second World Bank and the Development Assistance Committee. Developing nations in Southeast Asia should set up a joint agency for receiving aid and a formula for the apportionment of foreign capital aid. For, if a weak developing nation receives a vast amount of capital assistance from a powerful country, it is liable to become economically subservient to the "benefactor," and faces the danger of re-colonization. On the other hand, it is desirable to expand and encourage, through a systematic formula, the supply of technical aid free of such dangers and the interchange of technical experts and skilled workers.

This common organization should ultimately develop into an Economic Development Community. If such a community develops further

¹ U.N., *Economic Survey of Asia and the Far East, 1959*, p. 102.

into a supreme central organ for the regional group, we can expect that it will be able to carry out still more extensive and dynamic activities.

VI

The fact of it remains, however, that it will take a long time before Southeast Asian countries can meet the four preconditions listed above.

During long periods, these countries have maintained close political and economic ties with the advanced nations of the West, and after attaining independence, in postwar years, they have tended to overstress their respective independent positions. It is only natural, therefore, that they cannot establish close co-operative relations among themselves on short order. At the present time, Southeast Asia is not united either geographically, politically, or economically.

In order to push the project of economic integration among Southeast Asian countries, it is essential to increase the opportunities of consultations and to devise a systematic and gradual implementation. Much is expected of intensified activities of such an agency as the ECAFE, which is the best organization for promoting conciliation and understanding. If it fails, then we should reconsider the proposed Organization for Asian Economic Co-operation. The envisaged setup, often called an "umbrella formula," calls for the establishment of a loose affiliation covering the entire area. Even this modest aim is hard to realize through the efforts of Southeast Asian countries alone, and herein lies the problem.

As mentioned above, the OAEC plan was shelved at the 18th general meeting of ECAFE. Three reasons may be cited. The first is that, in view of the generally stagnant economic situation of the world, Southeast Asian nations reportedly hesitated to establish it by themselves because they are still heavily dependent on the export of primary products to advanced Western nations and are also receiving from them a great deal of economic and technical aid. The second reason is that, despite the insistence of the three-man preliminary committee comprising representatives of India, Thailand, and Japan, the nations concerned proved to lack sufficient solidarity and mutual trust. The third cause was an implicit opposition by some advanced countries.

In the future, therefore, it would be wise to obtain full understanding of existing international organizations before promoting such a scheme, whether all-embracing or sub-regional. Seen from this standpoint, one opportunity may be to make use of the General Assembly

of the United Nations where the voice of developing countries has lately been enhanced. Another good forum will be the U.N.-sponsored World Trade Development Conference scheduled for March 1964. It is also necessary to study the matter from various angles and over a long period of time at the U.N. Economic and Social Council and at the ECAFE, its sub-organ. It seems essential to win the support of international public opinion.

Notwithstanding the great difficulties, Southeast Asian nations must make their own efforts in the light of the world-wide trend towards regionalization. In this connection, the plan for a step-by-step integration in Southeast Asia, discussed at the ECAFE's first Conference of Asian Economic Planners held in New Delhi in September-October, 1961 must be taken into consideration. This formula calls for a gradual progress from economic co-operation to economic co-ordination and eventually to economic integration. At present, Southeast Asian countries are still in the first stage of this process. They should aim at the second stage where the countries concerned are "to adjust the contradictions and duplication in their respective economic development programmes, avoid the waste of materials and seek economic development from a broader regional standpoint."¹

Repeatedly in the foregoing discussion the point has been made that it is necessary to study what can be accomplished in a sub-regional form if an over-all organization is difficult to establish on short order. The establishment of an Economic Development Community deserves consideration even within such a limited scope.

¹ "Economic Development and Planning in Asia and the Far East," Conference of Asian Economic Planners—First Session, Japan, *ECAFE Bulletin No. 26*, Preface.