

Asean-China Trade Relations :15 Years of Development and Prospects",The Gioi Publishers,2008 **Recent Development of China-ASEAN Trade and Economic Relations:**

**From Regional Perspective**

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Abstract: The development of China-ASEAN trade and economic relations within the recent 15 years has of great significance not only for both sides but also for the whole East-Asia region. This paper intends to discuss the latter that is regional implications of 15 years' development of China-ASEAN trade and economic relations and provide some further consideration for both sides' trade and economic relations.

## **I. Introduction**

The past 15 years is an important historical period of the development of China-ASEAN trade and economic relations. It has been an obvious fact in the East-Asian region. Both sides have developed from the loose trade and economic relations into close one, as shown in China-ASEAN Free Trade Agreement (CAFTA). Regarding both sides as developing economies, the development of their trade and economic relations is of significance not only for themselves but also for the regional economic growth and integration.

Different from the EU and North America, East-Asian region is undeveloped with lower Per Capita GDP and much more population than the above two and of social diversity. To some extent, such weak economic developmental stage does not support the process of economic integration within the region. As a matter of the fact, although a lot of efforts about regional integration have been made by East-Asian members, it seems that few results come out, especially at the multilateral institutional level. The past 15 years' development of both sides' trade and economic relations, especially the establishment of CAFTA provides both developing China and developing ASEAN with opportunities of trade and economic growth, opportunities of perfecting market infrastructures and institutions each other, and opportunities of enhancing welfare level to the people of the both sides, which will contribute directly to the regional institutional architecture. Therefore, different from the development of other bilateral or multilateral trade and economic relations in the East-Asian region, the recent development of China-ASEAN economic relations is of special importance to the regional economic growth and integration.

Changes in both sides' trade and economic relations have been noted and discussed from the viewpoint of both sides in many occasions and papers. However, there is little discussion on

implications of both sides' developments in trade and economic relations from the regional viewpoint. This paper will focus on the regional implications of both sides' developments of trade and economic relations. Firstly, the paper will provide the historical retrospect on both sides' trade and economic relations and then will discuss their regional implications in detail. Lastly, the paper will provide some further considerations for both sides' development of trade and economic relations.

## **II. Development of China-ASEAN Trade and Economic Relations**

### **1. Three major phases of China-ASEAN Trade and Economic Relations**

China-ASEAN trade and economic relations have basically experienced three stages, accompanying with the improvement in the political and diplomatic relations between the two: The first stage is the period from 1967 to 1990. During this stage, the relations between two has experienced from mutual suspect to mutual understanding and trust in spite of close neighbors. After the initial ASEAN members established diplomatic relations with China and China formally recognized ASEAN as a regional organization in the 1970s, China and ASEAN began to strengthen mutual understanding gradually through bilateral activities, especially in the late 1970s and early 1980s when China greatly altered its foreign policy. By 1991, China had established or resumed diplomatic relations with all ASEAN members, preparing for their future dialogue and cooperation.

The second stage is the period from 1991 to 2001 when political and economic relations between China and ASEAN developed very quickly. In the political area, the both sides began a series of high-level official dialogue. Meantime, bilateral trade and investment got a new driving force and grew rapidly. In 1997, the both sides issued a joint declaration on building a good-neighborly partnership oriented to the 21<sup>st</sup> century. By 2001, the both sides have developed into to a full dialogue partnership from the initial general relations in the early 1990s.

The third stage from 2002 to the present represented a new stage of a strategic partnership between the two. In 2002, the both sides signed the Framework Agreement on China-ASEAN Comprehensive Cooperation, launching the process of forming the China-ASEAN Free Trade Area by 2010. In 2003, China joined the Treaty of Amity and Cooperation in Southeast Asia, becoming the first non-ASEAN signatory to the treaty. In 2004, all ASEAN members unanimously recognized China's full market economy status and signed the Agreement on Trade in Goods of the Framework Agreement on Comprehensive Economic Cooperation with China. In July 2005, the 'early harvest trade in goods' programme came into effect. In 2007, both sides signed the Agreement on Trade in Services. By now, China and ASEAN have forged a kind of relations of close economic partners.

## 2. Changes in Trade and Economic relations for Both Sides

### (1) Trade in goods

According to China's statistical data, China's trade with ASEAN has increased rapidly over the period 1990 to 2007. Though from a low baseline of 7 billion US\$ in 1990, the trade volume exceeded 100 billion U.S. \$ as a mark in 2004, and amounted to 202.6 billion US\$ in 2007 as a new record and three years in advance to reach the goal of 200 billion US\$ when the planned year is 2010. The growth rate of China's trade with ASEAN is an average 21.9% per year over the same period, more than the 18.8 percentage of China's overall trade.

As indicated in Figure 1, the share of China's trade with ASEAN in China overall trade rose from 6.0% in 1990 to 9.3% in 2007 while that of ASEAN's trade with China in ASEAN overall trade from 2.4% in 1990 to 9.8% in 2006. The rapid rise in trade flows between China and ASEAN over the past few years led to that the both sides become one of the largest partners each other.

Figure 1 Share of trade between ASEAN and China in Total Trade of China and ASEAN Respectively

Source: UN comtrade.

### (2) Trade in services.

China's trade in service with ASEAN is an important area of economic and trade cooperation. In recent years, China's trade in services with ASEAN have developed rapidly (See table 1), especially in the fields of investment in service sectors, project contracting, labor cooperation, and others and ASEAN has become China's important destination of export in services. At the same time, ASEAN has invested a lot in China in the fields of maritime transport, air transport, financial services, and construction services, and has become an important resource of imports in China's service. At present, the ten ASEAN members have become the tour destination of Chinese citizens after Lao became the last one in 2005. Personnel exchanges between the two sides have reached over 600 million in 2006 and China has become one of the top five sources traveling to ASEAN. In the areas of education, transportation, energy, culture, medical care, and other service areas, the cooperation between two is also increasing and of great prospects for development.

Table 1 Turnover of Economic Cooperation with ASEAN

	Turnover with ASEAN(US\$ billion)				ASEAN's share in China (%)			
	Total	Contracted Projects	Labour Cooperation	Design Consultation	Total	Contracted Projects	Labour Cooperation	Design Consultation
1998	2.31	1.84	0.47	0.00	19.6	19.9	19.7	2.4
1999	1.79	1.18	0.59	0.00	15.9	13.8	22.7	0.0
2000	1.92	1.25	0.67	0.01	17.0	14.9	23.7	4.2

2001	2.10	1.27	0.80	0.02	17.3	14.3	25.1	37.8
2002	2.31	1.64	0.66	0.01	16.1	14.6	21.4	13.9
2003	2.30	1.76	0.53	0.01	13.3	12.7	15.9	11.0
2004	2.79	2.23	0.54	0.02	13.1	12.8	14.3	16.8
2005	3.35	2.86	0.47	0.02	12.5	13.2	9.8	7.5
2006	4.40	3.88	0.50	0.03	12.3	12.9	9.2	9.2

Source: China's Statistical Yearbook (1999-2007).

### (3) Mutual Investment.

Mutual investment between China and ASEAN has got the rapid growth since the both sides improved their economic and diplomatic relations in the 1990s and now they have formed a two-way pattern of direct investment. In 2006, ASEAN investment in China and China investment in ASEAN amounted to 3.4 billion US\$ and 2.5 billion US\$ respectively (See table 2). ASEAN members have become one of the main sources of foreign direct flows to China, among them, Singapore, Malaysia, Thailand become an important source of foreign investment flow to China. Since the 1990s, China has begun to invest in ASEAN. With China's economic strength increasing, China's government encourages Chinese firms to "going out" and China investment in ASEAN also increased rapidly, especially in recent years. By the end of 2006, China's accumulated direct investment in ASEAN has reached 11.8 billion U.S. dollars. At present, the two sides are constantly improving the investment environment in order to attract substantial foreign investment and promote rapid economic development. It can be believable that in spite of the growth of mutual investment lagging behind that of trade, there is great potential for development between the two.

Table 2 Actual Mutual FDI Between China and ASEAN (US\$ Billion)

	ASEAN's FDI in China	Share of ASEAN's FDI in Total China(%)	China's FDI in ASEAN	Share of China's FDI in ASEAN(%)
1993	0.99	3.6		
1994	1.89	5.6		
1995	2.59	6.9		
1996	3.21	7.7		
1997	3.39	7.5		
1998	4.18	9.2		
1999	3.31	8.2		
2000	2.85	7.0		
2001	3	6.4		

2002	3.26	6.2		
2003	2.93	5.5		
2004	3.04	5.0	1.5	4.3
2005	3.11	5.1	0.6	1.5
2006	3.35	5.3	2.5	4.9

Sources: China's Statistical Yearbook (1994-2007) and World Investment report (2007).

### 3. Turning Point: Establishment of China-ASEAN Free Trade Agreement

The establishment of CAFTA has marked an important milestone in the development of China-ASEAN trade and economic relations. Just as shown the data, it sped up both sides' growth of mutual trade and investment and brought benefits to them.

As the first FTA between developing members among the East-Asian region which would create one of the world's largest trading blocs, the background of the establishment of CAFTA is that both sides have similarities based on the GDP per capita and the technological level to a great extent within the region. This encourages them to implement a policy of relatively full and mutual market openness to each other and not to be worried to hurt each other largely. The important principles for CAFTA are mutual benefit, compromise, and consolidation and the coverage of liberalization through FTA is comprehensive, including goods, service and also investments. The direct results from CAFTA are as follows. It firstly provided both sides with an internal and integrated market. FTA itself means unifying the separate markets into a single one among members who sign the FTA agreement after tariffs and NTBs are reduced and abolished. The integration of market would help the participants to make a new division of labor and resources allocation to produce a new driving force of economic growth. As a matter of fact, recent years has seen the faster growth of trade and investment between two than before. Secondly CAFTA would decrease the transaction cost between China and ASEAN. Both the high tariff rate and NTBs themselves are a kind of transaction cost. Their reduction and abolishment would bring direct benefits to the producers and consumers from the two sides. For this reason, trade, investment and other economic activities are more active than before the establishment of CAFTA. The third or additional benefit from CAFTA is to help the two resist the external risks such as the financial crisis. The establishment of FTA signs the high-level economic integration based on the good political relations. This kind of economic integration reduces the dependence of the participants on the external market and naturally increases their resistance to the external risks. Since the financial crisis in 1997, ASEAN, China and other East-Asian economies are trying to find an effective way to increase their abilities to be faced with the occurrence of the crisis again such as building up the reserve fund.

Table 3 The process of CAFTA

Year	Major Events
1997	the first ASEAN + China summit held
2000	CAFTA proposed
2002	the Framework Agreement on China-ASEAN Comprehensive Cooperation signed
2004	the agreement on trade in goods and dispute settlement mechanism signed
2007	the agreement on trade of services signed

### III. Implications of China-ASEAN Trade and Economic Relations for East-Asian Region

The development of China-ASEAN trade and economic relations has its big implications for the whole region. Basically speaking, it alters the economic pattern in the region, enlarges the regional internal market, and develops the construction of the regional institution, which helps to expand the regional economic scale and improve the regional integration.

#### (1) Enlargement of Regional Trade

As shown in Figure 2, the regional trade volume among East-Asia members has enlarged rapidly since the early 21<sup>st</sup> century, amounting to 2959.8 billion US\$ (according to incomplete statistics) in 2006, doubling that in 2000. The major contribution of the enlargement of trade volume is made from China, ASEAN and newly developing industrial markets. Among them, both China and ASEAN contributed a lot while Japan has made little contribution over the period. The increased share of contribution of China and ASEAN is attributed to enlargement of trade between China and ASEAN. Entering into the 21<sup>st</sup> century, the share of trade volume between China and ASEAN in the total regional trade increased fast to over 40%, surpassing that of Japan and other East-Asia members (See figure 3).

It may be said that 15 years' development of both China and ASEAN's trade has enhanced East Asia's growing regional trade interdependency and become a powerful force for integrating the East Asian economies.

Figure 2 Trade Scale in East-Asia Region (US\$ Billion)

Source: comtrade.

Figure 3 Share in total Trade within East-Asian region(%)

Source: comtrade.

#### (2) Growth of Regional Market

In recent years, enlargement of trade between both sides promotes the rapid growth of GDP, which leads to the expansion of intra-regional market. The absolute volume of GDP in the East-Asia region got to over 11000 billion US\$ in 2006 from 7000 billion US\$ in the early 21<sup>st</sup> century. Just like the change in the members' contribution to trade, the contribution of the growth of GDP

is made mainly from China, newly developing industrial markets and ASEAN while Japan contributes little (See figure 4).

In this context above, the structure of regional economic strength has been altered in terms of members. There is little change in the share of GDP of newly developing industrial markets in the whole region over the period of 1990-2007, holding about 15% of the regional GDP. The big change happens in the contrast of GDP between Japan and combination of China and ASEAN. In 1990, Japan accounted for 70.9% of the whole GDP while both China and ASEAN for 16.4%. By the end of 2007, Japan accounted for 42.1% while both China and ASEAN for 41.6%, close to that of Japan after 15 years (See figure 5).

The Change in regional share of members' GDP indicates the increase of the economic strength of both China and ASEAN in the whole region and therefore they have the abilities to affect the region's patterns of production, trade and investment, and resource flows. On the one hand, the rapid increase in regional GDP means the expansion of intra-regional market which would produce the big benefits to the participants including intra- and extra-regional producers and consumers. On the other hand, East-Asian regional integration could be pushed and finally realized by the developing members since their economic strength is equal to now or even would be more than that of the developed members in the near future in terms of GDP. In other words, CAFTA would be the base of regional integration.

Figure 4 GDP in East-Asia Region (US\$ Billion)

Note: East Asia refers to "10+3" +Hong kong + Taiwan.

Singapore is excluded from ASEAN.

Newly Developing industrial markets: Korea, Taiwan, Singapore and Hongkong.

Source: IMF.

Figure 5 Changes in Share of GDP in the East-Asian Region (%)

Source: IMF.

### (3) Construction of Regional Institution

After the CAFTA initiative was born, it would be doomed to produce the far-reaching effects. The most obvious effect is that it propels the institutional process of the regional cooperation, especially between developed and developing members such as the establishment of ASEAN-Japan FTA. In addition, China-Korea-Japan tripartite cooperation is also promoted to accelerate the realization of greater East Asian economic integration through the ASEAN+3 process.

In the past, East-Asian regional integration has been lagged behind other regions for a long time. Except for the political will, the disparity in the stage of economic development is another major reason. In particular, East-Asian developing members in the region have a relatively low Per Capita GDP and imperfect market institution, slowing the regional integration process. The CAFTA initiative would facilitate East Asian integration and cooperation, as an early effort to push

EAFTA and comprehensive cooperation since FTA itself is a kind of effective means to improve Per capita GDP and market mechanism in both sides. At the same time, CAFTA is just one core part between the two. They have also listed up the other areas for broad cooperation such as agriculture, information and communications technology, human to improve the environment for economic growth comprehensively and completely in the context of CAFTA.

In return, the East-Asian regional cooperation beyond ACFTA has more benefits to both China-ASEAN than just CAFTA. Firstly East-Asian integration would provide the greater internal market for the economic development of both China and ASEAN; secondly it would decrease the transaction cost for trade development, and thirdly it would decrease intra-regional dependence on the external market and resist the extra-regional risk. Benefits from East Asian integration is much larger than any “10+1”, which has been shown in results of some CGE models. Therefore, the future of China-ASEAN trade relations will go beyond CAFTA.

Of course, there still are some basic limitations existed in trade and economic relations between China and ASEAN, which could lead to delaying integration among East-Asian region. At present, the division of labor between both China and ASEAN and other regional members is vertical due to the weak technological strength in both sides. This causes a kind of non-full and asymmetric market openness between East-Asian developing and developed members since the East-Asian regional cooperation demands the horizontal division of labor between the two and other regional members. Therefore it is essential for the two to improve the technological level in the future and improve the regional division of labor.

In short, the development of both China and ASEAN's trade and economic relations is the most important driving force for changes in regional economic strength, and CAFTA initiative is the first step for economic integration process in the East Asian region as a whole. As long as China and ASEAN would sustains their dynamic growth and smooth development of trade relations, East-Asian regional integration will be in real process.

#### **IV. Some further Considerations on Deepening China-ASEAN Trade and Economic Relations**

During the past 15 years, both China and ASEAN have forged solid, comprehensive and mutually beneficial ties in terms of economic and political relations. In the the next 15 years or more they still are faced with a common need to improve their economic strength since both China and ASEAN are developing countries. In order to improve their status in the region, it is necessary for them to consider the following suggestions.

Firstly both China and ASEAN should make their efforts to increase their technological strength on their own and positively strengthen the technological cooperation with developed members. At present, both China and ASEAN are not each other's major markets, which indicates that their trade and economic nature is fundamentally competitive rather than complementary. Both sides



are mainly oriented toward developed economies such as U.S.A. and Japan as their major export markets. Improvement in their technological abilities will be favorable for altering similarities in China and ASEAN's trade structures and exploring a lot of potentials for complementarities among themselves to promote trade expansion. Besides their own efforts, they should accelerate the technological cooperation with developed countries since both sides mainly sources their capital and technology from developed economies such as U.S.A. and Japan.

Secondly both should make their efforts to improve further their own investment environment to promote mutual investment. Compared with other members' FDI flows, mutual FDI flows between the two has been weak. In fact, FDI, especially intra-regional FDI can operate as a powerful integrating force in East Asia, especially since a great deal of regional FDI is trade related in nature. Both China and ASEAN could take use of FDI to tie the two economic relations in the future instead of or supplement for the role of trade in both sides' economic relations. Thus mutual FDI is treated not just as an additional source of capital supply but, more important, as a means of technology transfer and export market development.

Thirdly both sides should make their efforts to enlarge and deepen the bilateral cooperation areas such as human resource development, financial cooperation and policy coordination related to technological development. Beyond merchandise trade, many of China's service activities, on account of their socialist legacies, are known to be more backward than those in ASEAN although China may generally have a strong comparative advantage in manufacturing. Both China and ASEAN may make broad and deep cooperation to promote trade in services based on both sides' complementary nature in the service industries.

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