

POLICY BRIEF**STRENGTHENING ASEAN INSTITUTIONS FOR AEC 2015
AND BEYOND**

January 2015

Executive Summary

As ASEAN gears up for ASEAN Community 2015, questions have been raised whether this is achievable and what it will mean for ASEAN citizens and corporations. Deeper policy questions also arise as to how ASEAN works and whether its institutions can further support the process. Integration and ongoing economic liberalisation also surface questions of risk from contagion and negative spill-over effects between member states' economies.

This brief will identify the institutional issues that arise and discuss what ASEAN can and should do, looking not just to end 2015, but toward deeper integration in the future. Key suggestions include:

- Engage different stakeholders beyond governments to gather views on the quality of governance of ASEAN institutions. A formal scorecard on governance of ASEAN institutions can be developed;
- Develop centres of excellence on public policy and specialised areas of governance in different ASEAN countries;
- Commission project teams on identified key issues that cut across existing political-security, economic and socio-cultural pillars as a first step to enhance policy coherence across the different areas;
- Strengthen risk surveillance and financial stability monitoring. Steps should be

taken to enhance the research capacity of the ASEAN+3 Macroeconomic Research Office (AMRO) and its synergy with ASEAN Integration Monitoring Office (AIMO), so as to minimize systemic risk and contagion as ASEAN integrates its diverse member-states' economies; and

- Take steps to incrementally enhance policy coordination and foster cross-sectoral cooperation. A recommended method is for greater frequency of cross-pillar officials training to encourage an ASEAN-wide perspective across the Community pillars. This is to help officials beyond country or pillar defined specialisations.

1. INTRODUCTION: INTEGRATION AND INSTITUTIONS

December 31, 2015 is the deadline for the Association of Southeast Asian Nations (ASEAN) to establish its ASEAN Economic Community (AEC). While we expect some measures to be delayed, the AEC that will result is not only a milestone for integration, but also a foundation for further cooperation and integration in the years beyond 2015.

However, there remain doubts whether ASEAN can fully implement the AEC and, indeed, move further ahead in the next years. More integration and ongoing economic

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liberalisation among ASEAN members can increase the risk of contagion and negative spill-over effects from one economy to another. The pace and depth of reform and liberalisation vary considerably among different ASEAN countries, and this continues to complicate the integration process. Consolidation cannot intensify without the support of strong and robust institutions within the countries and at the regional level.

There is a growing recognition that regional institutions need to be more effective and efficient. Already a High-Level Task Force (HLTF) on “Strengthening the ASEAN Secretariat and Reviewing the ASEAN Organs” has been established.¹ A region-wide exercise is currently in progress to strengthen ASEAN’s institutional capacity as well as to ensure that the ASEAN Secretariat is equipped with adequate financial resources and competent manpower².

Can ASEAN institutional quality keep pace with the region’s continued liberalisation and integration? Is it possible for ASEAN institutions to effectively guide the integration process and respond to new trends and challenges?

Maintaining the impetus for stronger and more efficient institutions is critical if ASEAN is to meet the increasing competition from other developing regions.

ASEAN’s economic integration agenda is ambitious and considerable. As ASEAN countries grow closer to one another economically, the impetus for strong and more efficient ASEAN institutions will only increase. The region must at least bridge wide development gaps, create growth synergies, and raise overall and national competitiveness. Moreover, the region also

seeks to integrate with the global supply chain and economy through mega regional structures such as the Trans-Pacific Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP). Ultimately, Southeast Asia must be ready to take the long-term perspective to capitalize on ongoing discussions for a wider free trade area for Asia-Pacific. These efforts are necessary for ASEAN to remain open to the wider region and global economy.

Some 80 percent of the AEC targets for 2013 were reported to have been achieved, according to the recent 46th ASEAN Economic Ministers Meeting³. The unsaid is that the remaining 20 percent are probably the most difficult to accomplish. Even more significantly is the fact that some of the reported progress has yet to be validated with actual on-the-ground implementation. Harmonisation of standards in trade, financial sector and competition laws too remain challenging to member states.

According to a Midterm Review⁴, the gaps that remain are mostly due to poor coordination and weak ASEAN institutions and processes. The study recommended the review of ASEAN’s institutional design as a priority before the establishment of the AEC next year.

This may seem ambitious. But while the AEC has progressed, much more needs to be done. Maintaining the impetus for stronger and more efficient institutions is critical if ASEAN is to meet the increasing competition from other developing regions.

As at 2012⁵, ASEAN’s share in the world’s investment flows stood at 8 percent. The grouping may have overtaken China and India in terms of investment inflows. But competition from the Asian giants remains.

Other regions, including Latin America and Africa are also drawing investment interest⁶.

A lot of effort is needed if ASEAN is to enhance its competitiveness. Consider the infrastructure. It is estimated that ASEAN will need to spend US\$7 trillion to develop infrastructure, housing and urban spaces between now and 2020⁷. Against this background, regional and international observers have called for “more ASEAN institutionalisation”, and “more ASEAN institutions”.

This issue is acknowledged within the ASEAN community and regarded as priority during the ASEAN Summit in November 2014. State leaders adopted a joint declaration on “Strengthening the ASEAN Secretariat and Reviewing the ASEAN Organs”, with the following six key measures:

1. Enhance the capacity of ASEAN to seize opportunities and address challenges;
2. Maintain ASEAN outward-looking organisation, and enhance its external relations;
3. Strengthen the capacity and coordination among ASEAN Organs;
4. Ensure that the ASEAN Secretariat is provided with adequate financial resources and competent manpower;
5. Task ASEAN Coordinating Council and the ASEAN Community Councils to implement the recommendations by the HLTF in a timely fashion; and
6. Task the Secretary-General of ASEAN to report annually on the progress of the implementation.

Within the broad mandate (listed above), this policy brief has tried to identify and prioritise some key issues within ASEAN institutions and made recommendations for change. The purpose would be for ASEAN institutions to:

1. Improve the quality of governance to boost efficiency and effectiveness;
2. Enhance coordination and policy coherence; and
3. Deepen regional financial integration, yet limiting risk.

2. KEY AREAS TO ADDRESS

2.1 Quality Governance

Policies decided but without implementation mean little, and one key to achieve results is by the quality of governance. How effective is ASEAN? At present, there is no agreed means to measure and evaluate this. A World Bank study however does exemplify a significant improvement in governance and regulatory quality among ASEAN economies, with marked improvement after the 1997 Asian currency crisis. Yet the study also identifies key areas that need improvement. One example is the indicator for the “Rule of Law”, a critical legal pillar with political, economic and social dimensions.⁸

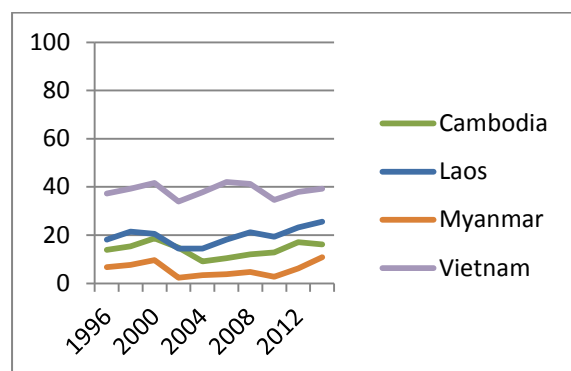
ASEAN needs a deeper, better quality of governance to be effective, not only at the high levels of political leadership.

For the period 1996 to 2013, Cambodia, Laos, Myanmar and Vietnam were ranked with low governance percentile scores⁹ (refer to [Table 1](#)). The “Rule of Law” was also found to be lacking in other ASEAN economies, including Thailand and Philippines (refer to [Table 2](#)). The comparison is telling not just amongst ASEAN members but relative to other countries and regions.

ASEAN will also need to take concrete steps to meet the growing demands for better governance. An ongoing United Nations global survey – “MY World 2015”¹⁰ ranked governance institutions among the top

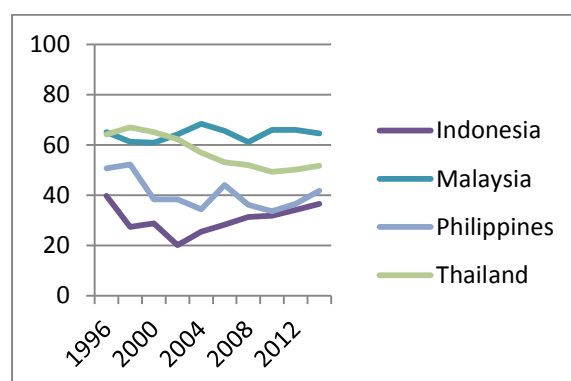
priority issues for post-2015, with emphasis for greater openness, accountability and transparency.

Table 1: Governance Indicators – Rule of Law (CLMV Countries)



World Bank Governance Report (1996-2013)

Table 2: Governance Indicators – Rule of Law (IND, MH, PH, THA)



World Bank Governance Report (1996-2013)

For greater effectiveness, ASEAN needs its policies to reach a deeper level of member states' governments, transcending only the highest levels of political leadership. Much depends on translating policies to reach the operational levels of bureaucracy, to impact all levels and segments of society – including corporations and civic group of citizens. Consulting and finding ways to include more stakeholders in ASEAN would be a key towards more effective governance.

2.2 Policy Coordination

As ASEAN plays a role in the wider region and global community, the concept of ASEAN centrality (a subject of other policy papers by the SIIA) is key. If it is to take up that role, the idea of ASEAN centrality must not only be about managing external and larger powers. It must also be a way for ASEAN to develop frameworks -- like the ASEAN-plus-one processes, the Asia-Pacific Economic Cooperation (APEC) and the East Asia Summit (EAS)¹¹ -- so that these institutions guide and strengthen ASEAN at the core.

To deal with the issue at its core require coordination between the different sectors to promote development that is sustainable – both for good economics and the environment, moving away from “silo” mentality.

Governing ASEAN better must also take into account the rules and norms in the international community and wider Asian region. It also means trying to ensure a consistency of policy between what happens within ASEAN, in ASEAN-led institutions for the wider region, and in ASEAN's participation in the global community (e.g. G20 summits).

Policy coherence within ASEAN is challenged as it pushes for regional integration in 2015, especially with the ASEAN Economic Community (AEC). The AEC is to be one of three pillars of ASEAN Community – the other two being political-security, and socio-cultural. Besides these, there is also the Coordinating Council as well as interactions arising from the ASEAN leadership summits. But as emphasis unevenly focused on the AEC's progress, there is some danger that it is seen in isolation.

To the contrary, as the region's economic integration deepens and also broadens, the

cross-sectoral linkages are becoming important within the system of ASEAN institutions and processes and require increased coordination and coherence among the ten sovereign nations on issues and policies.

For example, when the AEC moves towards an integrated manufacturing base and includes the authorised movement of those with skills and talents, the incidental consequence of greater instances of undocumented workers and of the trafficking in people must be dealt with, in a coherent manner. Another example is the haze issue that impacts many ASEAN countries, and is caused mainly by fires on plantations and forests in Indonesia. This may seem to be an environmental problem but it derives its roots and driving factors from economic activity, trade and investment.

To deal with the issue at its core must therefore require coordination between the different pillars and sectors to promote development that is sustainable – both for good economics and the environment. The pillars must not act in “silo”. As these two examples show, coordination and policy coherence needs to be improved.

2.3 Increasing Financial Integration, Limiting Risk

Going forward, a critical aspect of ASEAN economic integration is for the consolidation of the region’s financial sectors – to achieve a semi-integrated financial market by 2020. Financial integration in the region has been uneven. To date, gaps in regulatory frameworks and capacity continue to persist. The divergences in regulation range from accounting standards and disclosure requirements to discrepancies in anti-money laundering and consumer protection laws.

The 1997 Asian currency crisis continues to serve a strong and enduring reminder to governments in our region that they simply cannot rely on the support from others for solutions.

For example, in terms of capacity, many domestic banks and financial institutions in ASEAN are small and face challenges in scale and capabilities. This is not only in comparison with global banks but also reflects a spectrum of size and scale of banking institutions between ASEAN member states.

These gaps in regulations and differences in capacity can create problems for the region as a whole. Unless they are managed adequately, the increase in potential systemic risks and contagion would accompany greater regional integration process as ASEAN moves towards closer financial cooperation.

ASEAN economies are integrating their financial sectors and service offerings, which involve harmonising rules and processes, albeit at a slow pace. Singapore, Malaysia and Thailand, for instance, have linked up their individual stock exchanges, and established a Collective Investment Scheme (CIS) to allow investor access to cross-border financial services and products. The utilisation of the scheme remains to be assessed, since CIS was only introduced on 25 August 2014.¹²

As these steps are being taken, added layers of governance and regulations will be needed. It is important to note that cross-border investment portfolios are often subjected to risks related to domestic currencies and interest rates. Unless these are monitored at a regional level, the region could be at risk if a financial untoward occurs in one country.

We draw example from the European Union (EU) crisis as it illustrated how contagion spread from one to another of the sovereign states, notwithstanding considerable differences in economic structures of each member. Effects of crisis had since resulted changes in the EU's functioning, namely with the institutional reform measures established at the Lisbon Treaty¹³, to restore public confidence in EU institutions and their governance. Closer to home, another lesson is the Asian currency crisis.

Although almost two decades have passed, the 1997 Asian currency crisis continues to serve a strong and enduring reminder to governments in our region that they simply cannot rely on the support from others for solutions¹⁴. The region needs its own institutions¹⁵. For ASEAN, as one of the most economically exposed trading regions in Asia, the group is especially susceptible to global fluctuations and shocks.

Extra-ASEAN trade accounts for more than 75.8 percent of total net trade activity. In terms of foreign direct investments (FDI), extra-ASEAN FDI contributes roughly 83.7 percent of total inflows into ASEAN-6 economies (refer to [Table 3](#)). As such, without its own robust policy tools and actions, shifts in capital flow can make ASEAN economies very vulnerable. Specifically, inflows may result in asset price bubbles while outflows could trigger a currency collapse.

3. RECOMMENDATIONS: KEY DIRECTIONS AND POSSIBLE NEXT STEPS

3.1 Quality Governance: Engage Stakeholders and Develop a Scorecard

Presently, ASEAN recognises the need for governance to be effective and to bring in stakeholders from different segments of

Table 3: Intra & Extra ASEAN Trade and Investments (Share of Total Net, %)

Net Trade (Imports and Exports)	
Intra-ASEAN	24.2
Extra-ASEAN	75.8
Foreign Direct Investment	
Intra-ASEAN (ASEAN-6)	16.3
Extra-ASEAN (ASEAN-6)	83.7
Intra-ASEAN (CLMV bloc)	27.0
Extra-ASEAN (CLMV bloc)	69.8

ASEAN statistics updated as Dec 2013

society – including corporations and civic groups of citizens. There are existing platforms to seek corporation opinions and interactions with civic groups and non-governmental organizations. These however can be in danger of becoming merely annual showcase meetings.

ASEAN needs to build up organisational learning, governance and overall organisational sustainability.

To be more effective, ASEAN should consider more systemic ways to integrate various levels of stakeholders. Credible and consistent engagement mechanisms need to be developed, and there are many possibilities to achieve this.

A first step forward would be to develop a scorecard system on the quality of governance of ASEAN institutions. Such a scorecard would provide a systematic way to assess and evaluate the performance of the region's institutions. If stakeholder feedback and best practices for governance can be

gathered and shared publicly, this would strengthen the process.

To further improve, ASEAN would need to build up their organisational learning, governance and overall organisational sustainability. In different countries, there are already centres of excellence to distill and share best practices – for example, in the academia and the private sector – to complement the work of governments. These need to be connected and also ramped up.

Centres of excellence on public policy (and other specialized areas of governance) could provide a framework to help ASEAN improve its understanding and practices. The opportunities for creation of knowledge, innovation and exchange of perspectives are all essential for improving the quality of governance and effective policy implementation.

3.2 Policy Coordination: Cross-Pillar Teams and Training Together

There are calls for better ASEAN coordination and policy coherence as the AEC and larger ASEAN Community progress. The ASEAN Charter provides a Coordinating Council of Ministers, working to support the Community overall as well as the Summit among ASEAN leaders.

ASEAN should help the officials of the different countries interact and share their perspectives and understandings.

Existing efforts are however quite limited and often centered on inter-governmental committees and meetings. The ASEAN Secretariat, while named as the principal facilitator for ASEAN and the AEC, is limited in capability by the lack of funding and manpower, as well as by ASEAN member

states' aversion to grow the power of a supranational institution.

A recent suggestion was raised by Malaysian Prime Minister Najib Razak, in April 2014, to institutionalise a “fourth pillar” in the ASEAN to address cross-cutting issues. He argued that one of the priorities of the new pillar would aid the “creation of strong, robust and efficient ASEAN institutions”¹⁶. Particularly, as ASEAN makes progress towards the establishment of the AEC next year, the region would need to “strengthen coordination and coherence”, and “promote efficiencies”. In this context, a fourth pillar was proposed with the purpose to deal with cross sectoral issues, such as transboundary haze, climate change and to impose and execute economic sanctions, which may cut across the existing three pillars.

The suggestion at present is short on details and execution. It also remains to be seen, almost one year on, how it would be received through the region and at the Secretariat. Starting a “fourth pillar” promises attention to issues that cut across the pillars. However, it also runs a high risk of resulting in a proliferation of bureaucracy and additional costs on ASEAN manpower and resources.

More incremental steps may be preferred and this policy brief have made several recommendations. They would, by nature, go a step beyond the current High Level Task Force's efforts to streamline internal processes and structures, and minimise task duplication.

First, we suggest that ASEAN commission project teams on identified key areas that cut across existing pillars. Such teams would be tasked to deepen the understanding and policy development of cross-sectoral issues to deal with the identified problems. This could help germinate the habit of officers to work

across the pillars in order to better deal with cross-cutting issues.

Building on this, ASEAN should help the officials of the different countries interact and share their perspectives and experiences. A possible activity to facilitate this would be greater frequency of training programs for officials from different countries and sectors to engender an ASEAN-wide perspective and across the Community pillars, rather than adopting a view specific to one country and one specialisation.

These efforts may serve in themselves to improve policy coherence, especially if they are synchronized on the calendar with the Coordinating Council of Ministers. It is possible that, as the idea of a “fourth pillar” gains traction, these activities would serve as preparatory steps towards the formation.

3.3 Financial Supervision: Synergise AIMO and AMRO

ASEAN has recognised the risks of financial flows since the 1997-98 crisis and steps have been taken. The process began with the first ASEAN surveillance process in 1999 and, over time, this has resulted in the formation of the ASEAN+3 Macroeconomic Research Office (AMRO). Another similar body focusing on economics – the ASEAN Integration Monitoring Office (AIMO) – was created to support research on AEC.

AMRO must also enlarge its research focus to study and monitor other regional cooperation initiatives.

Despite efforts to draw a clear division of research mandates between AIMO and AMRO, the former overlaps with the latter in its portfolio of regional economic surveillance and development¹⁷. It is therefore recommended that the AIMO should

concentrate primarily on monitoring ASEAN economic integration and leave regional financial surveillance to AMRO, given its mandate to support the multilateralised Chiang Mai Initiative¹⁸.

Yet, the research mandates between AIMO and AMRO should also not be watertight separation because ASEAN economic integration cannot be assessed in isolation. The integration process needs to be evaluated in the regional and global context and ASEAN economies need to be apprised of the implications of global trends and developments.

In this context, AIMO and AMRO should instead work towards creating synergies between the two institutions’ research mandates. For instance, AMRO could provide regular updates on the macroeconomic and financial situation in the region to AIMO, and the opposite for AIMO to AMRO. The two institutions could also develop greater research value through synergistic collaborations. These synergies can be achieved through: (i) coordinating funding strategies on parallel projects that complement each other; and/or (ii) undertaking successive projects that build on each other. Such collaborations can help address the demand for expanded capacity that is required of both institutions.

Furthermore, AMRO needs to strengthen its research capacities to support its surveillance mandate. This is especially as the ASEAN+3 economies have become deeply interconnected as massive volumes of goods, services and capital are traded across the borders.

To be truly effective, the AMRO must adopt a multi-dimensional coverage, encompassing surveillance on a bilateral, multilateral and macroeconomic basis¹⁹. The financial sectors

in the region were also identified as a priority area for surveillance.

However, AMRO still conducts surveillance on a country-by-country basis, and this may inadequately recognise the interconnectedness of the region²⁰.

AMRO must also enlarge its research focus to study and monitor other regional cooperation initiatives. One example is the upcoming Asian Infrastructure Investment Bank (AIIB). Since the initiative was first announced by Chinese President Xi Jinping in October 2013, a total of 21 countries have signed up for the AIIB network, including all ten ASEAN members. AIIB would offer the region an additional source to finance infrastructure projects.

However, its governance arrangements remain to be seen, and new and evolving practices for governance will be needed in the future. Additionally, given that the proposed bank may exercise bond issuances to raise capital, some financial risks are to be expected, as payments on debt obligations may default. Therefore, the AIIB will likely require an organisation like the AMRO to provide risk surveillance and research. If AMRO is able to boost its capacity significantly, it could be well-positioned to serve this future need.

4. CONCLUSION: STRENGTHENING ASEAN INSTITUTIONS INCREMENTALLY

While the mantra of ASEAN has been for a limited Secretariat, there is greater recognition today that the group's regional body and its institutions need to be strengthened, in line with the ASEAN Community and especially the AEC.

There have been calls for sweeping and large scale changes, setting new directions and

arguing that these necessitate a Secretariat that would be built on a much larger scale. They do not always specify in what directions and how ASEAN should expand.

This policy brief has taken a different approach and put forward various different ideas. We have identified key directions on which ASEAN should move as it enters a new phase in 2015 and beyond.

The policy brief also suggests incremental steps that can be taken to start something new – rather than a “Big Bang”. This is in recognition that not all ASEAN members may share the same perspective about the benefits of strong institutions for the region, or the attendant costs.

Moreover, rather than looking at ASEAN generally, this policy brief has focused on the AEC and the institutions that need to be grown to support economic integration both now and into the future.

To move ASEAN ahead and to grow its institutions, a necessary next step is to prove that better institutions will benefit all countries in the group. This is not only a “once and for all” debate but one that must be revisited as the first steps are taken. Institutions need to be incrementally improved and those increments proven to deliver effectively and efficiently.

Only then can the political will be found, and sustained, for ASEAN and its institutions to move forward.

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About this policy brief

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