

APEC at 20 and the Rise of China

26-27 February 2010

Summary Report

A regional conference on “APEC at 20 and the Rise of China” was held in Hong Kong on 26-27 February 2010, co-organized by the Hong Kong APEC Study Centre at Lingnan University, the East Asian Institute at National University of Singapore, the Asia-Pacific Economic Association and the Department of Economics at Hong Kong Baptist University. The conference brought together around thirty local and regional experts from academia, business and policy, to discuss the achievements and the future of APEC, and the evolving Asia-Pacific regional economic integration and cooperation, particularly with the rise of China. The conference consisted of a series of sessions with individual lead authors presenting their findings and views, followed by general discussion by the audience. The papers presented in the conference raised timely issues and generated lively exchanges of ideas. Some of the issues examined and findings presented included:

I. *Opening Address: Ms Maria Kwan Sik-ning, Director-General of Trade and Industry*

Ms Kwan delivered the conference’s Opening Address. In her presentation she covered the background and the development of APEC over time, with particular attention to the current situation and hopes under the Japanese chairmanship of APEC in 2010. She highlighted Hong Kong’s participation in various APEC initiatives.

II. *APEC at 20 and the Rise of China: an Overview and Assessment (i)*

1. *APEC at 20: Looking back and looking forward: John Ravenhill (Australian National University)*

Prof. Ravenhill offered a comprehensive evaluation of the performance of APEC and the problems that it faced in the past two decades. APEC has maintained an ongoing drive for trade liberalization through voluntary trade liberalization among member economies and has begun to address behind-the-border issues. However, the failure of Early Voluntary Sectoral Liberalization

and the failure to respond to the Asian Financial Crisis could sound a loss of credibility of APEC. He suggests that APEC should continue to promote free trade in Asia Pacific. Although China, as a regional superpower, supports APEC, it focuses on technical cooperation rather than on liberalization agenda.

III. Monetary and Financial Cooperation

Several Asian currency crises and the recent global financial crisis have indicated the importance of closer regional financial cooperation. Given the risks from the unpredictability of capital flows and volatile exchange rates, Kawai champions for the creation of an Asian Monetary Fund taking advantage of the Asian Financial Stability Dialogue and Asian Currency Unit to promote exchange rate coordination and macroeconomic and financial system stability.

3. *The future of the Renminbi and its implications for the Hong Kong Dollar: He Dong (Hong Kong Monetary Authority)*

HE Dong suggests that the convertibility of the *Renminbi* (RMB) is best seen as being subject to differences in degree, much like variations in a spectrum. It is possible for the authorities to reap the benefits of a wider use of the RMB outside Mainland China through offshore markets without removing all restrictions on access to domestic financial markets by non-residents. From Hong Kong's point of view, He Dong thinks that an international role of the RMB provides vital opportunities for developing Hong Kong's financial market and strengthening its role as an international financial centre. The expansion of RMB banking in Hong Kong will not undermine the status of the Hong Kong dollar. Moreover, there is no inherent conflict or logical inconsistency between the Hong Kong dollar peg to the US dollar and Hong Kong's role as a RMB offshore centre.

4. *Reform of RMB exchange rate regime: a trade-off solution: Zhang Bin (Chinese Academy of Social Sciences)*

Zhang evaluates the benefits and shortcomings of four different reform schemes on RMB exchange regime and concludes with what he calls "a trade-off solution": a one-time appreciation of the RMB exchange rate against the US dollar by 10% and then allowing annual fluctuation of $\pm 3\%$, based on pegging to a basket of currencies. The benefits of such a solution include

reducing pressure from international community and safeguarding the free trade system, being good for reallocating domestic resources between tradable and non-tradable sectors to reduce the related imbalances and helping to bring down the inflation expectations as well as actual inflation.

5. *Towards an effective (more or less) monetary union in Asia: Ho Lok-sang (Lingnan University)*

Noting that true monetary union in Asia is unachievable and even possibly undesirable, Ho proposes a “more or less effective” “mimic” monetary union which is based on pegging with a common anchor. He argues that a GDP-weighted basket of “normalized exchange rates” of key currencies would provide much flexibility and pegging a currency to it will stabilize effective exchange rates. Pegging with a common anchor would lead to stable inter-regional exchange rates and thus de facto “near” monetary union. Under his proposal, the GDP weights are adjusted every year using data two years ago. It is expected that this will foster inter-regional trade and investment, and at the same time greater resilience against external shocks. He proposes that consistency with economic fundamentals is paramount, which implies that changes for a currency’s peg to the common benchmark basket may be necessary from time to time. Provided that the initial peg is at an appropriate level he expects such changes to be infrequent.

IV. APEC at 20 and the Rise of China: an Overview and Assessment (ii)

6. *Trade gains and public goods: further thoughts: Murray Kemp (University of New South Wales)*

Kemp discusses the relationship between trade gains and local public goods. Suppose all public goods are local and all (local) public goods are provided by benevolent but parochial governments strategically, free trade is potentially beneficial to all participating countries. Kemp also shows that under some related sufficient conditions, a similar result would obtain even when some of the public goods are non-local. In order to achieve Pareto improvement, however, he points out that suitable transfers would be necessary.

7. *Continuing agenda for APEC, regional institutional architecture in the context of an emerging Asia: Tan Khee Giap (East Asian Institute)*

Tan suggests an eight-element continuing agenda for APEC and reviews the evolution of regional institutional architecture in Asia Pacific. The continuing agenda for APEC includes implications of massive fiscal stimulus, growth of the export-oriented East Asian economies, fine-tuning trade over-dependence, fiscal imbalances between East Asian economies and the U.S., the role of the greenback as a major reserve currency, sustainable development and creating a comprehensive social safety net for East Asia.

Given the robust emergence of China since the late 1990s, China's core economic political interests would no doubt reflect and shape the future evolution of the regional institutional architecture, hinting at the possibilities of ASEAN 10+3 and the newly proposed 3G Group.

8. *China: a new engine of the regional economy: Huang Yiping (Peking University)*

Huang thinks that China's current international influences tend to be overstated, given that China is not an independent growth driver and China's current account surpluses are dominated by processing trade. Asymmetric market liberalization in China is responsible for both the successes (optimism) and risks (pessimism) during the reform period. Effective rebalancing requires liberalization of the factor markets and elimination of cost distortions. Huang also thinks that G-2 (US and China) may become a reality eventually. However, maintaining good relation with Japan is critical for its regional role.

V. The Politics of Asian Regionalism

9. *European and Asian regionalism: comparative connections: Brian Bridges (Lingnan University)*

Bridges examines the record and challenges of regionalism in the Asian Pacific region through a comparison with the experiences of regionalism in Europe. A certain amount of skepticism and suspicion as well as complementary interest has been evident in both cases. While the states of both region share certain ideals such as a belief in the efficacy of regional organizations in bringing about prosperity and stability, there are significant differences in timing and format, types of leadership and initiative, focus and agendas, and fundamental kinds of regionalism.

10. *Is there a question of relations between East Asian and trans-Pacific institutions? Evolving regional architecture features: Pang Zhongying (Renmin University of China)*

Pang discusses the transformation of APEC since its beginning, with special attention to both APEC's variants and counterparts in East Asia and its current and potential alternatives. He emphasizes the relationship between Asian/East Asian and Asia-Pacific (trans-Pacific) institutions and addresses the roles of big players (particularly the U.S., Japan, and China) in such regional institutions. Pang concludes that pursuing the formation of an East Asia community is a necessary and legitimate choice with clearly far-reaching significance. However, the future of multi-institutions in Asia and the Pacific is still uncertain because the U.S. may attempt to resume its regional multilateral domination.

11. *APEC in the context of US-China relations: Zhang Baohui (Lingnan University)*

Zhang starts from the realist international relations theory which emphasizes the importance of hegemonic power in the creation of multilateral cooperation and multilateral institutions, and argues changes in balance power among great powers have impacts on multilateral cooperation. The rise of China and the relative decline of the United States can profoundly affect the future of APEC. The expected power trajectories of China and the United States do not bode well for APEC. However, specific prospects for APEC could be affected by developments along two dimensions: US-China mutual strategic accommodation and China-Japan strategic reconciliation.

VI. Trade Matters: Policies and Directions

12. *Prospects for FTAAP and implications for East Asia: Inkyo Cheong (Inha University)*

Cheong discusses that the Free Trade Area of the Asia-Pacific (FTAAP) may result from new momentum for saving APEC, economic gains from the FTAAP, the United States' involvement in Asian regionalism, and APEC bureaucracy. He also analyzes the feasibility of FTAAP and its implications for East Asia. Cheong concludes that the progress of East Asian economic integration needs to be expedited, for it will bring huge benefits for the region.

13. *Global free trade: regionalism as a building block or a stumbling block?* Juyoung Cheong (University of Queensland) and Kar-yiu Wong (University of Washington)

Global free trade can be achieved through either multilateralism (i.e., the World Trade Organization path) or regionalism (i.e., the Free Trade Agreement path). The authors argue that if both paths are feasible, global free trade (GFT) can be reached no matter which path countries take. However, GFT cannot be achieved on a voluntary basis if both paths are not feasible. If the WTO path is not feasible but the FTA path is, the latter can lead to GFT. This is the building block case. Alternatively, if the WTO path is feasible but the FTA path is not, and if some countries prefer regional integration, GFT will not be achieved. This is the stumbling block case.

14. *The role of China in Asia-Pacific trade framework in the context of APEC:* Emile Kok-kheng Yeoh and Im-soo Yoo (University of Malaya)

Yeoh and Yoo argue that China needs to resolve its domestic problems, enhance social and economic development, and maintain and develop sound economic cooperation with countries in the region to strengthen itself as a major power in the region and the world trade market.

15. *Building APEC as an effective vehicle for facilitating international business: at the border, behind the border and across the border:* Jane Drake-Brockman (Trade and Environment Solutions Pty Ltd)

Drake-Brockman recalls the Asia-Pacific region's fundamental economic interest in retaining a global outward-looking trade and investment stance, while building steadily towards a single business market, against a backdrop of regional political debate about the desirability, the feasibility or the likelihood of an APEC-wide Free Trade Agreement (FTA). Her analysis supports an APEC agenda focused on regulatory inefficiencies and other behind-the-border barriers to doing international business, especially in promoting the regional services economy. Additionally, the paper suggests that an APEC FTA would be important in addressing this fundamental agenda.

VII. Trade and Investment

16. *Foreign direct investment in a closer linked Asia: Hsiang-Chih Hwang (Lingnan University)*

Hwang analyzes the trend and economic determinants of bilateral foreign direct investment (FDI) flows of fifteen host countries in East and South-east Asia from 1990 to 2005. Based on a gravity model with variables reflect both market access and comparative advantage incentives, the estimation results suggest that multinational companies from the region and the outer world have dissimilar incentives to engage in FDI in the region. The increased regional trade is associated with a 0.85 percent increase in regional FDI in the study period. The estimation results imply the importance of using a multilateral decision-making framework rather than a two-country model to analyze FDI flows in East and South-east Asia.

17. *The role of China-ASEAN Free Trade Area in economic integration in the context of APEC: Sarah Y. Tong (East Asian Institute)*

Tong regards the China-ASEAN Free Trade Area (CAFTA) as a new attempt in economic cooperation and a stimulus and an example for intra-ASEAN integration and other regional and sub-regional arrangements in Asia. APEC's transition from cooperation to integration faces great challenges in the absence of strong leadership, growing complexity due to multi-layer regional trade agreements and weak internal integration. However, ASEAN could play an instrumental role as a coordination and consensus building while China could serve as a constructive force in the pursuit of the long-term economic integration objective for APEC.

Conference Programme

Friday, 26 February 2010

8:30 – 9:00 **Registration**

9:00 – 9:15 **Welcoming Remarks**
Prof. CHAN Yuk-Shee (Lingnan University President)

9:15 – 9:30 **Opening Address : APEC at 20 and the Rise of China**
Ms. Maria KWAN (Director-General of Trade and Industry, HK SAR Government)

**Session 1: APEC at 20 and the Rise of China:
an Overview and Assessment (i)**
Chair: Jesús SEADE

9:30 – 10:15 *APEC at 20: Looking Back and Looking Forward (Keynote)*
John RAVENHILL (Australian National University)

10:15 – 10:30 Tea Break

Session 2: Monetary and Financial Cooperation
Chair: John WONG

10:30 – 11:15 *Monetary and Financial Cooperation in East Asia (Keynote)*
Masahiro KAWAI (Asian Development Bank Institute)

11:15 – 11:45 *The Future of the Renminbi and its Implications for the Hong Kong Dollar*
HE Dong (Hong Kong Monetary Authority)

11:45 – 12:15 *Reform of RMB Exchange Rate Regime: A Trade-off Solution*
ZHANG Bin (Chinese Academy of Social Sciences)

12:15 – 12:45 *Towards an Effective (More or Less) Monetary Union in Asia*
Lok Sang HO (Lingnan University)

12:45 – 2:00 Lunch

**Session 3: APEC at 20 and the Rise of China:
an Overview and Assessment (ii)**
Chair: Juyoung CHEONG

2:00 – 2:45 *Trade Gains and Public Goods: Further Thoughts (Keynote)*
Murray KEMP (University of New South Wales)

2:45 – 3:15 *Regional Institutional Architecture and the Rise of China*
TAN Khee Giap (East Asian Institute)

3:15 – 3:45 *China: A New Engine of the Regional Economy*
Yiping HUANG (Peking University)

3:45 – 4:00 Tea Break

Session 4: The Politics of Asian Regionalism

Chair: Jane DRAKE-BROCKMAN

4:00 – 4:30 *European and Asian Regionalism: Comparative Connections*
Brian BRIDGES (Lingnan University)

4:30 – 5:00 *APEC and Other Regional Arrangements: The Emergence of New
Regional Order in Asia and the Pacific*
PANG Zhongying (Renmin University of China)

5:00 – 5:30 *APEC in the Context of U.S.-China Relations*
ZHANG Baohui (Lingnan University)

5:30 – 6:15 **Session 5: Roundtable Discussion: APEC, Doha and FTAs**
Chair: Lok Sang HO

6:15 – 8:00 Dinner

Saturday, 27 February 2010

Session 6: Trade Matters: Policies and Directions

Chair: Jesús SEADE

9:00 – 9:30 *Feasibility of APEC FTA and Implications for East Asia*
Inkyo CHEONG (Inha University)

9:30 – 10:00 *Global Free Trade: Regionalism as a Building Block or a Stumbling Block?*
Kar-yiu WONG (HK Baptist University and APEA) and Juyoung CHEONG
(University of Queensland)

10:00 – 10:30 *The Role of China in Asia-Pacific Trade Framework in the Context of APEC*
Emile Kok-Kheng YEOH and Im-Soo YOO (University of Malaya)

10:30 – 11:00 *Building APEC as an Effective Vehicle for Facilitating International
Business; at the Border, behind the Border and across the Border*
Jane DRAKE-BROCKMAN (Trade and Environment Solutions Pty Ltd)

11:00 – 11:15 Tea Break

Session 7: Trade and Investment

Chair: Brian BRIDGES

11:15 – 11:45 *FDI in a Closer Linked Asia*
Hsiang-Chih HWANG (Lingnan University)

11:45 – 12:15 *Road Investment and Inventory Reduction: Evidence on Causality and
Externality from China*
Zhigang LI (University of Hong Kong)

12:15 – 12:45 *The Role of CAFTA in Economic Integration in the Context of APEC*
Sarah Y. TONG (East Asian Institute)

12:45 – 1:00 **Concluding Remarks:** *John WONG*

1:00 – 2:30 Lunch

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