

UBS Investment Research

Asian Economic Comment

ASEAN Linkages: Friends like these

■ Competing for influence in ASEAN

We argued in *ASEAN: Friends with benefits* (21 November 2011) that the US and China were competing for influence in ASEAN. This, we suggested, implied potential beneficial access to the domestic markets of the world's two largest economies and aid or investment flows from the same. However, we also thought that there would be political strings attached. These ideas continue to be borne out with news flow on the US backed Trans-Pacific Partnership, the widely suspected influence of China over Cambodia at a July ASEAN foreign ministers' meeting and a subsequent Chinese aid package to Cambodia.

■ With friends like these...

While we believe the US and China are competing for influence in ASEAN, the two regional powers have limited interest in a united ASEAN speaking and acting as a unit. Commentary out of last week's APEC summit in Vladivostok make it clear that the US is not going out of its way to gather ASEAN as a unit into the Trans-Pacific Partnership – a trade deal that promises access to US markets and seems very likely to exclude China. So far, in ASEAN, only Singapore, Malaysia, Vietnam and Brunei are members. Likewise, China has gone to great lengths to avoid engaging ASEAN as a unit over its claims within the South China Sea. Commentators in SE Asia have been quick to link a Chinese loan and aid package to Cambodia with suppression of the usual post meeting statement, including comments on the South China Sea dispute, after July's ASEAN foreign ministers' meeting chaired by Cambodia. According to Reuters, the package was worth over USD 500m or 4% of Cambodian GDP. In short, the US and China are more friendly to individual ASEAN member states than to ASEAN as a group.

■ The case for ASEAN Linkages

This is completely understandable. Part of the rationale for ASEAN is that the region taken together has a greater economic and geographical footprint and hence more bargaining power than an individual nation state. For this reason, the US and China often wish to deal at the member state level in SE Asia. Meanwhile, ASEAN member states have an incentive to appeal to the group as a whole when engaging the US and China. It was partly to avoid economic domination by a rising China that encouraged ASEAN member states to step up engagement with each other and break down barriers to trade and investment. However, ASEAN is not a unitary state and it is clearly possible for the US or China to split the group if they try hard enough – the current TPP membership and the failure to produce a common statement on the South China Sea at the ASEAN foreign ministers meeting in July are merely examples of this.

■ Investment implications

Far from implying that ASEAN member states should or will give up on closer links, these pressures serve to underline the above rationale for integration. This notion is reflected in the hurried diplomacy by Indonesia post the ASEAN meeting in July and the comments by Singapore's Prime Minister in Beijing last week. Prime Minister Lee reiterated the case for 'ASEAN Centrality', the idea that ASEAN is "the partner around which all the other major countries gather, and talk with one another". In line with our ASEAN Linkages theme, we look for public and private integration efforts between ASEAN member states to continue. We also expect the US and China to court ASEAN states with offers of market access, aid and investment. That should be good news for ASEAN companies with the balance sheet and inclination to expand beyond their home markets. However, this will, over time, come at the cost of unwelcome political pressures, in our view.

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www.ubs.com/economics

Edward Teather

Economist

edward.teather@ubs.com

+65-6495 5965

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