



# "European and Asian Integration: Achievements and Challenges"

**Opening Remarks by  
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## **I. Introduction**

Distinguished guests, ladies and gentlemen:

I am honored to be here today to open this important conference on European and Asian Integration: Achievements and Challenges, jointly organized by the European Commission and the Asian Development Bank.

Asia's export-orientation continues to be the foundation of our economic success, giving rise to an obvious and quite natural gravitation toward regionalism. In fact, we expect economic cooperation and integration to be a key pillar of Asia's future development strategy as we move deeper into the 21st century.

China and India's increased openness, their vast domestic markets and rapidly expanding productive capacity will continue as major drivers of the region's growth. Coupled with cooperative efforts of ASEAN, the expanded ASEAN+3 and the relatively new East Asian Summit process, we have seen intraregional trade and cross-border investment expand rapidly. In the decade since the Asian financial crisis, there has been greater cooperation in linking financial systems and calls from several quarters for regional exchange rate stability. These palpable moves toward integration have placed regionalism-and regional initiatives-high on the list of national priorities and, in some cases, mainstreamed in national agendas.

Market-led regional economic integration in Asia has deepened as production networks have grown. And it will continue to do so as Asian governments increasingly nurture the trend. Before I set the stage for today's discussions on financial stability, macroeconomic interdependence and Asian regionalism in general, let me briefly touch upon the evolving relationship between our two regions, Asia's economic prognosis, and the risks we see in the immediate months ahead.

## **II. Europe and Asia: Growing Ever Closer**

Although our discussions will be primarily about the process of integration within our respective regions, in many ways Europe and Asia are also closer today than ever before. And it is not simply due to reduced structural distances caused by high-speed infrastructure, financial mobility and globalization. There is a very strong, and growing, cultural element as well.

As our societies meld in tandem with our products and services, contact between cultures expands. Tourism has increased dramatically over the past decade. Twenty million Europeans visited Asia in 2005, 70% more than in 1995. And two million more Asians visited Europe in 2005 than a decade earlier, a 42% increase. While more Europeans

practice martial arts, Asian football has become world class. The arts, both classical and popular, whether from Cannes or Bollywood, cross our regions' borders more fluidly. And of course, food is the great equalizer: as Chinese restaurants spread out across Europe, it is not unusual to find Asians savoring European dishes. Even the European "Spaghetti Bowl" of free trade agreements has been seamlessly translated into an Asian "Noodle Bowl" of FTAs.

As Asia continues to diversify its export markets, our economic contact intensifies. Total trade between Asia and Europe nearly doubled between 2000 and 2006-to almost \$1 trillion, with Asian exports to Europe growing at nearly the same pace as European exports to Asia. Asian portfolio investments to Europe grew 90% from 2001 to 2006. And European assets invested in Asia more than tripled over the same period-both to more than \$1 trillion. Given the current global climate, it is unlikely these trends will change.

Our two regions have much to share. We both follow an incremental step-by-step, pragmatic approach to integration. And while Asia lacks the grand-plan for regionalism as you have in Europe, the European Commission and ADB can effectively work together and use our distinctive expertise to add value to economic cooperation and regional integration more generally.

That's why we were so pleased to note the great interest shown by several European scholars in preparing our study on the emergence of Asian regionalism. The book-to be launched at the ADB Annual Meeting in Madrid in early May-includes several important contributions from European colleagues. Our study team welcomed the excellent comments it received when it visited here last September. Today we will discuss some of the results of that study, in particular on financial market integration and macroeconomic interdependence in the context of the current global economic situation.

### **III. Economic Outlook and Risks**

Naturally, Asia will be affected by the projected slowdown in global growth. Yet it appears that our region's economic expansion in 2008 will remain robust, perhaps a percentage point or less below the 2007 growth of around 8.5%. In fact, many economists are hoping that the US slowdown will help China ensure its economy avoids overheating. So far, Asian exports remain robust, primarily due to intraregional trade and continued demand, especially from emerging economies worldwide. Domestic demand within our region is also on the upswing.

In terms of risks, the big worry around the region is that inflation, mostly from high food and energy costs, but also from continued capital flows, will limit policy options for monetary authorities. Global financial volatility is always a significant concern, although the region had limited and apparently quite controllable exposure thus far to the US subprime crisis.

There has been a lot of talk about decoupling lately. To us, that is neither here nor there. In past US recessions, the drop in economic growth in Asia largely mimicked that in the US. We would expect that to continue to a certain extent. But with Asia's internal dynamic changing, the effect should be lessened.

Although we still believe the US can avoid an all-out recession, we will be watching very carefully for any indication that the slowdown accelerates to a sharper-than-expected recession in the United States or leads to a significant slowdown of the global economy. In any case, it is clear that the Asia and Pacific region needs to assess policy options and continue needed reforms to further enhance our region's financial stability and bolster macroeconomic interdependence.

### **IV. Financial Stability in Asia**

One lesson of the Asian financial crisis was that, with the natural integration that globalization brings to markets, greater regional cooperation is mandatory. It is necessary to prevent crisis, promote financial reform, enhance monetary and exchange rate stability, build new institutions, and improve physical, capital, and human interconnectivity. The crisis, if anything was a trigger for Asian regionalism.

While there have been widespread reforms over the past decade, Asia remains much more integrated in trade than in finance. It is much less integrated overall than Europe, especially in finance. However, Asian leaders have made regional financial integration a priority-in part as a safeguard against the vagaries of global markets, but also as a platform for regional development. Major initiatives since the crisis include the ASEAN's surveillance process, the Chiang Mai Initiative and the [Asian Bond Market Initiative \(ABMI\)](#)-both launched by ASEAN+3-and the Asian Bond Fund initiative promoted by the Executives' Meetings of East Asia-Pacific Central Banks, or EMEAP. Still, regional financial integration remains at an early stage. In many ways, Asia is more financially integrated with the global economy than with itself.

Where do we see regional financial cooperation moving in the medium term? There are four concrete directions. The first is continued strengthening of local currency bond markets-as an alternative to dominant bank financing, a means of translating savings into productive investment for both institutional and small investors, and a way of financing infrastructure through innovative, market-sensitive instruments.

Second is greater harmonization of financial systems in response to private sector demands for trade finance and cross-border intraregional investment.

Third is to establish a minimum set of standards, or best practices, that all recognize and strive to follow.

And fourth, to help foster the first three, the creation of a top-level financial stability dialogue, forum, or roundtable to bolster financial stability through enhanced cooperation between finance ministries, central banks, and market regulators in the region. This can also become an important high-level venue to guide macroeconomic cooperation, to build on existing ASEAN+3 Economic Review and Policy Dialogues.

## **V. Macroeconomic Interdependence**

Asia needs to manage its growing exposure to external shocks-both to reduce the economic volatility and risk they generate, and to create an environment for deepening regional linkages.

With globalization, macroeconomic variables-such as growth, inflation, exchange rates-are affected by exogenous shocks, whether driven by price, demand, or contagion from financial crisis. This underscores the need to coordinate monetary, fiscal, and exchange-rate policies, along with foreign exchange reserve management.

For example, over the past 5 years, a sharp buildup in foreign exchange reserves in East and Southeast Asia, and more recently in India, provided a buffer against external shocks. Now, however, these reserves are considered by many as excessive. Costs of holding large reserves are significant not only in terms of increasingly difficult price stabilization and monetary policy operations, but also in terms of foregone investment. Better returns on reserves could help finance needed infrastructure, supply essential public goods, or retire public debt. The region's policy makers are increasingly interested in ways to better use these international reserves. Also, multilateralization of the Chiang Mai Initiative is already underway, and we await the ASEAN+3 Finance Ministers Meeting-on the sidelines of the ADB annual meeting this May in Madrid-to see if any agreement will be announced.

In general, Asia's open regionalism and the various surveillance and dialogue processes allow effective communication on monetary policies between economies, particularly within ASEAN+3. Because the continuous depreciation of the US dollar could destabilize Asian economies, there is a need for closer dialogue and cooperation in the area of monetary and exchange rate policies. One of the presentations this afternoon will discuss a possible means of effecting this.

## **VI. Asia's Approach to Regionalism**

All in all, a feasible, workable approach for Asian integration is evolving—one that is market-friendly, multi-track, and multi-speed, and allows for a healthy dose of pragmatism among a collegial group of economies.

There are several advantages to cooperating in limited areas first, and then gradually deepen and widen the scope of cooperation. First, any group of countries, economies, subregions, or territories can integrate according to their particular levels of development and the specific opportunities that regionalism offers them. Second, as such partnerships strengthen, smaller units are more likely to merge into larger ones, leading to wider and deeper partnerships across an ever-growing swathe of Asia. Third, and extremely important, this approach has the potential to ensure that Asia's economic integration remains market-friendly, as its integrating framework remains responsive to private sector needs.

Subregional cooperation is the building block of Asia's regional integration, given our diversity and size. Cooperation at the subregional level is only logical as a way to move forward. Whether in the middle income ASEAN countries, South Asia, Central Asia or the Pacific, different subregions will inevitably have different scope and speed for regional cooperation. As they develop, bridges naturally form across subregional boundaries, leading eventually to wider and more comprehensive cooperation and integration.

Asia remains "institution"-light compared to the EU structure—even if ASEAN's new Charter has begun the transition to a more rules-based system. But even here, the institutional framework toward integration will develop from the bottom up, in a gradual fashion, to bring about an inclusive, equitable, and prosperous integrated Asia.

## **VII. Conclusion**

In closing, Asia has learned much from the European experience. With Europe and Asia growing ever closer, I am confident we will continue to do so, working together as our regions deal with the global economic challenges of the day. I look forward to today's discussions as one way of furthering the process of building effective regionalism across Asia.

Thank you.

**Story from ADB:**

<http://www.adb.org/Documents/Speeches/2008/ms2008011.asp>