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Session: Can the Asia-Pacific Region Adjust?

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What can APEC do?

Purpose: Information

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What can APEC do to assist the asia-pacific region to adjust?

Gordon de Brouwer and Luke Yeaman¹

Presented by Luke Yeaman

The overarching theme for this conference is 'Driving Growth – APEC's Destiny'. Today, I would like to talk about a '*next generation*' of reform within the Asia-Pacific; one that I believe can make the single biggest contribution to driving growth in the region, and which the APEC forum is well-placed to embrace.

A key to driving sustainable growth is open and well-functioning markets, with clear price signals, open trade and investment, market transparency, good governance, and effective competition among firms.

In moving towards this goal of free and open markets, the '*first generation*' of reforms has taken place at the border of each economy; tariff rates have fallen and regional trade has increased. APEC's trade and investment liberalisation and facilitation (TILF) mission, which remains at the core of APEC's identity, has been very successful and has benefited the entire region.

There is still work to be done in relation to trade liberalisation (although recent progress has been relatively limited) but there is another set of pressing issues which also needs to be addressed.

Many of the remaining impediments to open trade and investment are not at the border. They are structural in nature and occur behind the border. They arise because domestic economic policies are too restrictive, fail to provide the right incentives, and limit the emergence of appropriate markets.

To keep driving growth, we need to build on the '*first generation*' of reform by addressing these behind-the-border impediments through domestic structural reform. This is the '*next generation*' reform I referred to earlier and there is a growing sense that this broader focus on economic structural issues should be at the core of APEC's mission and identity.²

Structural reform can have significant domestic economic benefits. Restrictive regulations and weaknesses in competition policy, governance arrangements and legal systems can hamper domestic business activity by increasing costs and uncertainty. Reforms that allow domestic markets to operate more efficiently can contribute significantly to economic growth and stability.

The empirical evidence shows that economies that pursue comprehensive structural reform generally experience rises in productivity and living standards, and are more resilient to economic shocks.

- An example of this is Australia's strong economic performance and resilience following a period of significant structural reform beginning in the 1980s.

But structural reform also has the potential to greatly enhance regional economic integration. Improvements in the operation of domestic markets encourage greater trade and investment flows by providing increased opportunities and certainty to foreign firms. In this way,

¹ The authors would like to thank Trudie Wykes for her assistance in preparing this presentation.

² As an example, see the paper by one of East Asia's pre-eminent strategic thinkers, Hadi Soesastro, 'Microeconomic Policy Reform: Strategy for Regional Cooperation', *EABER Working Paper No. 12*, <http://www.eaber.org/intranet/publish/Public/Publications.php>

domestic structural reform assists economies to realise the full benefits of trade and investment liberalisation.

These sizeable benefits are increasingly being recognised across the region.

However, the challenges of developing and implementing structural reform are many and varied.

These reforms are inherently domestic in nature. Their design needs to take account of the unique economic and social environment and objectives of each economy; there is no one size fits all option.

Once an economy has identified its priorities for reform, it often faces significant resistance from vested interests, both within the government and the bureaucracy, and from private agents. Overcoming this resistance is made more difficult by the typical distribution of costs and benefits associated with reform; the 'winners' from reform are often dispersed and poorly informed while the 'losers' are likely to be concentrated and well-informed.

Furthermore, the technical capacity (or 'know-how') to implement chosen reforms is lacking in many economies. Unlike a reduction in trade barriers, which may require a small legislative amendment, implementing structural reform can be highly complex and may, for example, require the creation of a new government entity.

Institutions, both domestic and international, can play a major role in overcoming these challenges.

Domestic institutions can be particularly useful in building support for structural reform. By reviewing potential policy options in an objective, rigorous and transparent way, institutions can provide expert technical advice, expose vested interests, and inform and unite the prospective 'winners' from reform.

- The Australian Productivity Commission and the Japanese Council for Economic and Fiscal Policy are examples of policy institutions explicitly undertaking this role in the Asia Pacific region.

International forums, such as APEC, also have a major role to play in supporting structural reform.

They can facilitate peer exchange, which can help policy makers identify and develop reform priorities and options that best suit their individual economy circumstances. Peer exchange can help identify common lessons from other economies' reform experience and can also identify why a specific policy has worked well under one set of conditions, but has not worked well under different circumstances.

Peer exchange is most effective when undertaken in an environment of trust, respect and open communication, with an emphasis on mutual gain and shared learning. In the Asia-Pacific, attempts to exert pressure, or impose policies, on an economy through binding resolutions are not well-suited to addressing reforms that are domestic in nature.

International institutions can also facilitate capacity building initiatives to assist economies in the design and implementation phases of structural reform.

This is the new role APEC can adopt and embrace: to promote and facilitate structural reform through peer exchange and capacity building.

APEC is already well suited to carry out this role. It is an important part of the regional economic and financial architecture and has already played a key role in the '*first generation*' of reforms; it has a track record of success. APEC is not a negotiating forum. There is no cut and thrust confrontation. It is voluntary and non-binding in nature. This is a real strength in tackling sensitive domestic economic reform issues.

With its diverse membership, APEC possesses a wealth of experience in implementing structural reform under a range of different conditions. This diversity is sometimes seen as a weakness but, in this context at least, diversity is actually a real strength.

APEC already has the infrastructure in place to address structural reform issues, giving it a head start on other international forums. In 2004, APEC Economic Leaders emphasised the importance of structural reform through the *Leaders' Agenda to Implement Structural Reform (LAISR)*. LAISR identifies five priority work areas – regulatory reform, strengthening economic and legal infrastructure, competition policy, corporate governance, and public sector management.

The Economic Committee (EC) was given the task of promoting and coordinating the structural reform agenda. The EC is already adapting to better deal with these issues. Its focus has shifted away from economic research and into policy advice, an ambitious forward work programme is being constructed, and the membership increasingly represents domestic agencies with direct responsibility for structural reform.

APEC also has a good track-record in identifying and delivering technical capacity building that is tailored to each economies own priorities and needs.

Conclusion

As policy advisers, the task ahead is to keep our approach fresh and responsive to the challenges the Asia Pacific region currently faces; moving towards our long-term goals and finding more effective ways to drive growth.

These challenges now focus on issues behind-the-border that inhibit business between our economies and are entrenched in domestic policy making processes. The '*next generation*' of reforms that promote regional economic integration and drive economic growth will revolve around these behind-the-border barriers to doing business.

APEC is an ideal institution for addressing these issues and this role should be at the core of APEC's identity and destiny.



What can APEC do to assist the Asia-Pacific region to adjust?

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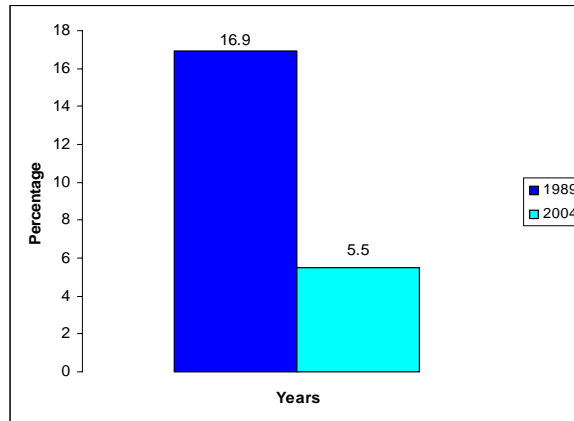


Driving Growth

- A key to sustainable growth is open and well-functioning markets
- '*First Generation*' reform took place at the border
 - Trade and investment liberalisation and facilitation (TILF)

APEC Tariff Rate Reduction

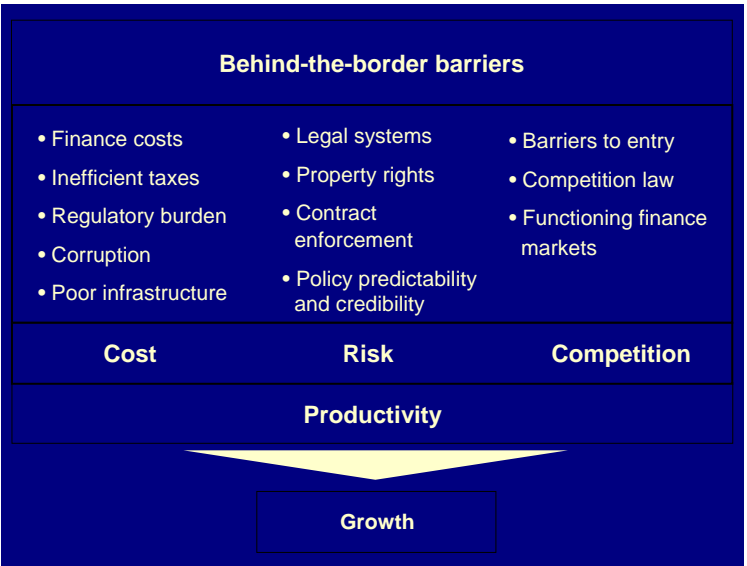
(Average applied tariffs of APEC economies)



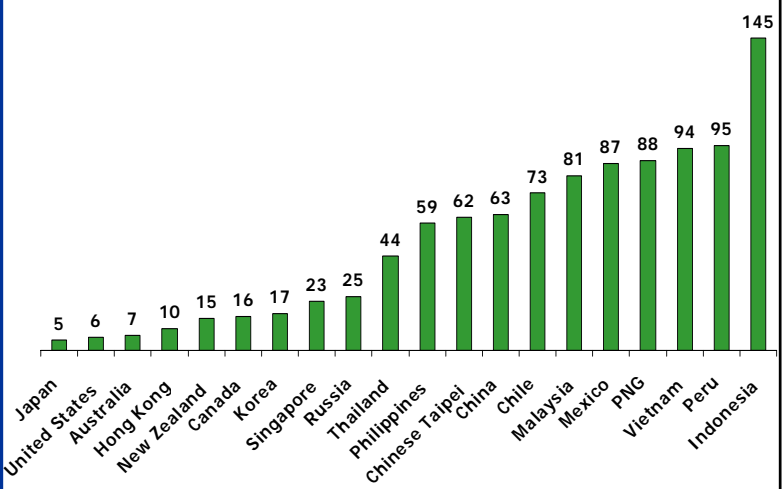
'Next Generation' Reform

- Behind-the-border structural reform is the '*next generation*' of reform
 - Domestic benefits
 - Improved productivity, economic growth, macroeconomic stability and resilience
 - Regional benefits
 - Removes impediments to cross-border trade and investment

'Next Generation' Reform

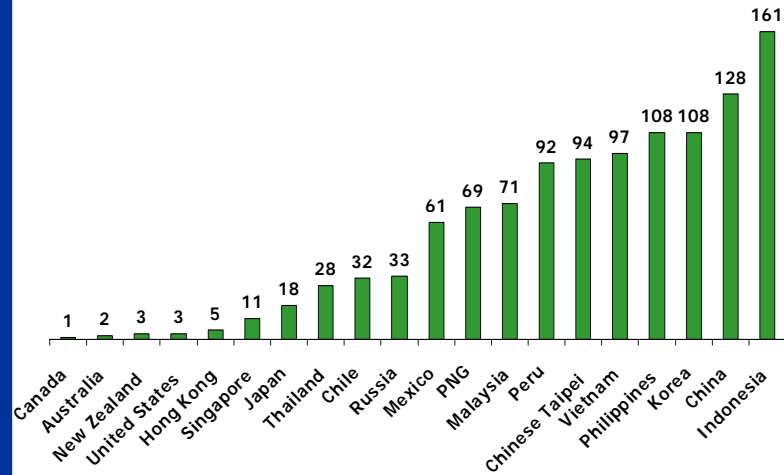


Enforcing Contracts



Source: Doing Business database

Starting a Business



Source: Doing Business database

Reform Challenges

- There is no 'one-size-fits-all' option
- Significant resistance from vested interests
 - Political, bureaucratic, private
- Many economies lack the technical capacity to implement reform

Role for Institutions

- Domestic institutions can help build support for reform
 - Expose vested interest and unite and inform ‘winners’ from reform
- International institutions can facilitate peer exchange and capacity building
 - Emphasis on mutual gain, shared learning
 - Peer *pressure* is rarely successful

Why APEC?

- Consensus and non-binding decision making, well-suited to domestic issues
- A diverse membership with a broad range of reform experience
- The infrastructure already exists to address reform issues
 - LAISR, Economic Committee
- A strong record of capacity building



Australian Government
The Treasury

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